

NICHOLAS C. DREHER, ESQ. 1299-0  
THEODORE D.C. YOUNG, ESQ. 5735-0  
CADES SCHUTTE LLC  
1000 Bishop Street  
Honolulu, Hawaii 96813  
Telephone: (808) 521-9200  
Facsimile: (808) 521-9210  
ndreher@cades.com  
tyoung@cades.com

LISA G. BECKERMAN, ESQ.  
AKIN GUMP STRAUSS HAUER & FELD LLP  
590 Madison Avenue  
New York, New York 10022  
Telephone: (212) 872-1000  
Facsimile: (212) 872-1002  
lbeckerman@akingump.com

DAVID P. SIMONDS, ESQ.  
California State Bar No. 214499  
AKIN GUMP STRAUSS HAUER & FELD LLP  
2029 Century Park East, Suite 2400  
Los Angeles, California 90067  
Telephone: (310) 229-1000  
Facsimile: (310) 229-1001  
dsimonds@akingump.com

Proposed Counsel for Debtor  
and Debtor in Possession

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)

**MOTION FOR ENTRY OF ORDER  
AUTHORIZING THE DEBTOR TO  
ASSUME JET FUEL SALE AND  
PURCHASE AGREEMENT PURSUANT**

**TO SECTION 365 OF THE  
BANKRUPTCY CODE; PROPOSED  
ORDER**

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, files this Motion for Entry of Order Authorizing Debtor to Assume Jet Fuel Sale And Purchase Contract Pursuant to Section 365 of the Bankruptcy Code (the “Motion”) and, in support thereof, respectfully represents as follows:

**I. JURISDICTION**

1. This Court has jurisdiction over the subject matter pursuant to 28 U.S.C. §§ 157 and 1334. Venue is proper in this District pursuant to 28 U.S.C. § 1409. The instant proceeding is a core proceeding pursuant to 28 U.S.C. § 157(b). The Court possesses the requisite authority to grant the relief requested herein pursuant to 11 U.S.C. § 365.

**II. BACKGROUND**

2. On March 21, 2003 (the “Petition Date”), the Debtor filed a petition for relief under chapter 11 of title 11 of the United States Code (the “Bankruptcy Code”) in the United States Bankruptcy Court for the District of Hawaii (the “Bankruptcy Court”). Pursuant to sections 1107(a) and 1108 of the Bankruptcy

Code, the Debtor is operating its businesses and managing its properties as a debtor in possession. No trustee, examiner or committee of creditors has been appointed in the Debtor's chapter 11 case.

3. The Debtor was incorporated in January of 1929 under the laws of the Territory of Hawaii and is currently a subsidiary of Hawaiian Holdings, Inc. ("Hawaiian Holdings"), a Delaware corporation whose common stock is traded on the American Stock Exchange and Pacific Exchange under the ticker symbol "HA." As part of the regular Securities and Exchange Commission filings of Hawaiian Holdings, Hawaiian Holdings reports its financial and operating results with those of the Debtor on a consolidated basis.

### **The Debtor's Business**

4. The Debtor is engaged primarily in the scheduled transportation of passengers, cargo and mail. The Debtor's passenger airline business is its chief source of revenue. Principally all of the Debtor's flights either originate or end in the state of Hawaii. The Debtor provides passenger and cargo service from Hawaii, predominately Honolulu, to the cities of Los Angeles, Ontario, Sacramento, San Diego and San Francisco, California; Seattle, Washington; Portland, Oregon; Phoenix, Arizona; and Las Vegas, Nevada (the "Transpacific Routes"). The Debtor also provides non-stop service between and among the six major islands of the state of Hawaii (the "Interisland Routes") and weekly service

to each of Pago Pago, American Samoa and Pepeeete, Tahiti in the South Pacific (the "South Pacific Routes"). Charter service is provided from Honolulu to Anchorage, Alaska (the "Charter Routes"). Based upon the Debtor's operating revenues, the Debtor is the largest airline headquartered in Hawaii.

5. Based on its unaudited results, the Debtor had a net loss of approximately \$58 million for the twelve months ended December 31, 2002 ("Year 2002") on operating revenue of approximately \$632 million for the same period. In comparison, for the twelve months ended December 31, 2001 ("Year 2001"), the Debtor reported net income of approximately \$5 million on operating revenue of approximately \$612 million for the same period. The Debtor's assets and liabilities, as of December 31, 2002, were approximately \$256 million and \$399 million, respectively. The Debtor's reported assets and liabilities, as of December 31, 2001, were approximately \$305 million and \$327 million, respectively.

6. The Debtor is party to a network of agreements among airlines. Because of the interdependent nature of airline operations, coordination among airlines, provision of airline services, and efficient service by the airline industry to the traveling public, in general, would be virtually impossible without such agreements. Among other things, these agreements facilitate cooperation among airlines with respect to such critical activities as making reservations and transferring passengers, packages, baggage and mail among airlines.

## **The Debtor's Fleet**

7. Beginning in the fourth quarter of 1999, the Debtor initiated a plan to replace its entire fleet of McDonnell Douglas DC-9 aircraft used to service its Interisland Routes. This effort was completed in the first quarter of 2002, with the Debtor taking delivery of thirteen Boeing 717-200 aircraft (the "717 Aircraft").

8. Similarly, in the fourth quarter of 2001, the Debtor initiated a plan to replace, by June 2003, its entire fleet of McDonnell Douglas DC-10 aircraft (the "DC-10 Aircraft") used to service the Transpacific Routes, South Pacific Routes and Charter Routes (the "Overseas Routes") with sixteen Boeing 767-300ER aircraft (the "767 Aircraft"). To date, the Debtor has taken delivery of ten new and four used Boeing 767-300ER aircraft and has returned eleven DC-10 Aircraft leased from Continental Airlines, Inc. and a subsidiary of American Airlines, Inc ("American"). The Overseas Routes are currently serviced by fourteen Boeing 767-300ER aircraft.

9. All of the Debtor's aircraft are leased from various lessors under either financing or operating leases. Three of the Debtor's 767 Aircraft are leased under fifteen-year operating leases with a subsidiary of Ansett Worldwide Aviation Services, Inc. ("Ansett") and were delivered to the Debtor in the fourth quarter of 2001. Four 767 Aircraft were delivered in 2002 under seven-year operating leases with International Lease Finance Corporation. Seven of the Debtor's 767 Aircraft

are leased under eighteen-year operating leases from Ansett and a subsidiary of Boeing Capital Corporation (“Boeing”). Each of the 717 Aircraft is leased under an eighteen-year leveraged financing lease with Boeing. The Debtor’s four remaining DC-10 Aircraft are leased under operating leases with American and B.C.I. Leasing.

### **Employees**

10. The Debtor has approximately 3,100 active employees, approximately 2,600 of which are employed on a full time basis. The majority of the Debtor’s employees are covered by labor agreements with the International Association of Machinists and Aerospace Workers (AFL-CIO) (“IAM”); the Airline Pilots Association, International (“ALPA”); the Association of Flight Attendants (“AFA”); the Transport Workers Union (“TWU”); or the Employees of the Communications Section (“Communications Section”). Each of these labor agreements, other than the contract with the seven-member Communications Section, was renegotiated in 2000 or 2001, and will be subject to renegotiation again in 2004 or 2005.

### **Previous Restructurings**

11. On September 21, 1993, the Debtor filed a voluntary petition for relief under chapter 11 of the Bankruptcy Code with the Bankruptcy Court (the “1993 Bankruptcy”). Following confirmation of the Debtor’s plan of reorganization in

the 1993 Bankruptcy on August 30, 1994, the Debtor successfully emerged from the 1993 Bankruptcy. Thereafter, on August 29, 2002, the Debtor was restructured from a public company into a wholly-owned subsidiary of Hawaiian Holdings and AIP (the “Restructuring”). As part of the Restructuring, the stockholders of the Debtor became stockholders of Hawaiian Holdings and Hawaiian Holdings assumed sponsorship of the Debtor’s existing stock agreements. Prior to the Restructuring, the common stock of the Debtor was publicly traded on the American Stock Exchange and Pacific Exchange under Hawaiian Holdings’ ticker symbol of “HA.”

### **The Debtor’s Current Financial Crisis**

12. The Debtor’s current financial crisis was precipitated by a confluence of factors relating, in large part, to the depressed economic conditions of both the United States and Japan. These factors include: (a) decreased fare revenue, (b) high aircraft lease costs, (c) high labor costs and (d) increased insurance, security and fuel costs. Although the terrorist attacks of September 11, 2001 are one of the most obvious and publicized reasons for the Debtor’s current financial crisis, it is the significant, though related, decline in the economies of the United States and Japan that has most contributed to the necessity of the Debtor’s chapter 11 filing.

13. Following the events of September 11, 2001, the Debtor has seen a marked and dramatic reduction in the demand for travel to and within the islands

of Hawaii. This reduced demand has been exacerbated by the flagging economies of the United States and Japan since that time. The demand for vacation travel, which historically has been the Debtor's greatest source of income, has been most affected by the economic decline. In order to attract passengers, airlines, including the Debtor, have been forced to lower their fares. The introduction of "low cost carriers," such as Jet Blue, has led to a further reduction in fare structure, as national airlines have been forced to reduce ticket prices to remain competitive. The combination of fewer ticket sales made at reduced fares continues to impact the Debtor's revenue and earnings negatively.

14. Beginning in late 1999, as discussed above, the Debtor began a refueling process under which its aging fleet of McDonnell Douglas DC-9 aircraft and DC-10 Aircraft would be completely replaced by the end of 2003. By July of 2001, the Debtor had entered into the last of its agreements with lessors that would provide the aircraft for this refueling. Although the terms of these agreements were considered to be fair and at market rates when agreed to, the subsequent and unforeseen decline in economic conditions in the United States and abroad have caused the terms of such leases to be highly unfavorable. Because its aircraft lease costs are grounded in economic assumptions that have failed to materialize, the Debtor has been forced to shoulder the crippling costs of over-market leases. For

the Year 2002, expenses associated with the Debtor's aircraft leases made up 12% of its total operating expenses.

15. Similarly, because the Debtor's union agreements were renegotiated in 2000 and 2001, the Debtor's labor costs have not been in line with current economic conditions. Based upon market assumptions made in 2000 and pre-September 11, 2001, the Debtor's labor costs have exceeded what the Debtor could realistically maintain based upon its revenues. This relative increase in labor costs, as compared to revenue, has negatively impacted the Debtor's ability to remain a viable enterprise. For the Year 2002, the Debtor's labor costs made up 30% of its total operating expenses.

16. As a direct result of the events of September 11, 2001 and the long-standing international crises in the Middle East, the Debtor has seen increases in several of its cost centers. For instance, insurance rates associated with airline operations have increased substantially as compared to pre-September 11, 2001 rates. Because of increased airline security requirements, the Debtor also has been faced with increased security expenditures. Moreover, fuel costs, which made up approximately 14% of the Debtor's operating expenses for Year 2002, also have steadily increased during this period. These increased costs, in the face of declining revenues, have further weakened the Debtor's ability to succeed as a going-concern.

## **Prepetition Activities**

17. The two largest controllable components of the Debtor's cost structure are labor and aircraft costs. These are, therefore, the two areas upon which the Debtor had focused prior to the Petition Date in trying to accomplish a successful out-of-court financial and operational restructuring. To that end, the Debtor has, particularly within the past year, been actively negotiating with both its aircraft lessors and labor unions to reduce its aircraft and labor costs, respectively. These negotiations have continued up until the Debtor's bankruptcy filing. On February 20, 2003, the Debtor's employees represented by IAM agreed to \$3.8 million in concessions. On March 6, 2003, the Debtor's employees represented by ALPA reached an agreement with the Debtor with respect to approximately \$8 million in concessions. Similarly, on March 11, 2003, the Debtor's employees represented by AFA agreed to approximately \$3.5 million in concessions. Although the Debtor and its labor unions have made great progress in these negotiations, it now appears that the only practicable way for the Debtor to reorganize is under the protection afforded to it under the Bankruptcy Code, as the Debtor has not been successful in its attempts to negotiate significant concessions from its aircraft lessors.

### **III. THE DEBTOR'S FUEL PURCHASE AGREEMENTS**

18. The Debtor intends, with Bankruptcy Court approval of this and other related motions, to continue to operate its flights and transportation services in the ordinary course of business during the pendency of this chapter 11 case.

19. The day to day operation of the Debtor's airline depends upon a steady supply of fuel. The importance of this cannot be over-emphasized; even a one day delay in the procurement of fuel would have disastrous effects on the Debtor's business. In order to provide for a steady and dependable supply of fuel at each airport at which the Debtor's aircraft land, the Debtor is party, in the ordinary course of its business, to various agreements with respect to (a) the purchase of fuel, (b) the storage of fuel and (c) the delivery of fuel from storage to the Debtor's aircraft (collectively, the "Fuel Purchase Agreements"). These agreements are entered into by the Debtor with third parties directly and through joint agreements with other airlines as part of fuel committee cost sharing cooperatives.

20. The Debtor has typically purchased its fuel for its operations at Honolulu International Airport ("HNL"), the Debtor's primary hub, from third parties who then deliver the fuel to the Debtor's storage facilities, under short term contracts. Although the Debtor also can purchase fuel on the open market for each of its required deliveries, the only way for the Debtor to be assured of sufficient fuel for operations, particularly during a time when fuel may be in short supply, is

through its Fuel Purchase Agreements. For example, if the Debtor were to purchase fuel in small quantities on the open market, the availability of fuel would be subject to the needs of other airlines that have contracted directly with such outside providers.

#### **IV. RELIEF REQUESTED**

21. By this Motion, the Debtor seeks entry of an order pursuant to section 365 of the Bankruptcy Code authorizing the Debtor to assume a certain executory jet fuel sale and purchase agreement with ITOCHU Petroleum Co. (Hong Kong), Ltd. (“ITOCHU”) (the “Fuel Agreement”)<sup>1</sup> and honor any obligations incurred with respect thereto, including the provision and maintenance of any letters of credit required under the Fuel Agreement, whether incurred prepetition or postpetition, including the provision of any letter of credit required under the Fuel Agreement. The Debtor also requests authority to cure any defaults under the Fuel Agreement in the ordinary course of business pursuant to section 365(b)(1)(A) of the Bankruptcy Code.

22. The Fuel Agreement, in particular, is of great importance to the Debtor. The Debtor estimates that all of the Debtor’s fuel needs for its HNL operations, the Debtor’s primary hub, will be fulfilled with the fuel to be provided under the Fuel Agreement. In 2002, the Debtor’s total fuel costs for the year were

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<sup>1</sup> Pursuant to the Fuel Agreement, the Debtor has agreed to keep the terms of Fuel Agreement confidential.

approximately \$95 million, with fuel consumption at HNL accounting for a substantial portion of this expense.

23. Assumption of the Fuel Agreement is necessary to ensure that the Debtor has access to sufficient fuel to meet its needs at HNL. In addition, the Debtor believes that, because of the quantity of fuel purchased and lack of intermediate fuel servicing parties, the terms of purchase, including purchase price, are highly advantageous to the Debtor. Moreover, if the Debtor was required to seek alternative fueling sources, it would be forced to enter into numerous smaller fuel supply contracts at prices and on terms that would be substantially less favorable than the terms the Debtor has negotiated with ITOCHU. Moreover, the quantity of fuel required by the Debtor for its HNL operations may not be available at any price.

#### IV. APPLICABLE AUTHORITY

24. The Debtor is authorized to assume the Fuel Agreement pursuant to section 365 of the Bankruptcy Code. Section 365(a) of the Bankruptcy Code provides that a debtor in possession, “subject to the court’s approval, may . . . reject any executory contract or unexpired lease of the debtor.” 11 U.S.C. § 365(a). The decision to assume or reject an executory contract or unexpired lease is a matter within the “business judgment” of the debtor. *See Durkin v. Benedor Corp. (In re G.I. Indus., Inc.)*, 204 F.3d 1276, 1282 (9<sup>th</sup> Cir. 2000); *National Labor*

*Relations Board v. Bildisco (In re Bildisco)*, 682 F.2d 72, 79 (3d Cir. 1982) (“The usual test for rejection of an executory contract is simply whether rejection would benefit the estate, the ‘business judgment’ test.”), *aff’d*, 465 U.S. 513 (1984); *In re Hawaii Dimensions, Inc.*, 47 B.R. 425, 427 (D. Haw. 1985). This “business judgment” is not a strict standard; it merely requires a showing that either assumption or rejection of the lease or contract will benefit the debtor’s estate. *See Borman’s, Inc. v. Allied Supermarkets, Inc.*, 706 F.2d 187, 189 (6th Cir. 1983).

25. If a debtor’s business judgment has been reasonably exercised, a court should approve the assumption or rejection of an unexpired lease or executory contract. *See, e.g., NLRB v. Bildisco and Bildisco*, 465 U.S. 513, 523 (1984); *Durkin v. Benedor Corp. (In re G.I. Industries, Inc.)*, 204 F.3d 1276, 1282 (9<sup>th</sup> Cir. 2000); *In re Orion Pictures Corp.*, 4 F.3d 1095, 1099 (2d Cir. 1993); *In re Southern California Sound Systems, Inc.*, 69 B.R. 893, 896 (Bankr. S.D. Cal. 1987); *Johnson v. Fairco Corp.*, 61 B.R. 317, 320 (Bankr. N.D. Ill. 1986).

26. The Fuel Agreement is an executory contract under section 365 of the Bankruptcy Code because the parties under the Agreements have continuing obligations to perform.

27. The Fuel Agreement was negotiated at arm’s length and provides fuel to the Debtor on competitive market rate terms. Due to the importance of the Fuel Agreement to the Debtor’s continued operations, and because performance of this

Agreement has and will be beneficial and will likely result in cost savings to the Debtor and its estate, the assumption of this Agreement represents sound business judgment and, therefore, should be approved by the Court.

28. Also, because ITOCHU is a foreign entity, there may be some question as to, among other things, the enforceability of the automatic stay under section 362 of the Bankruptcy Code and the ipso-facto clause protections of section 365(e) of the Bankruptcy Code. If ITOCHU were to terminate the Fuel Agreement, the Debtor would likely incur substantially increased fuel related expenses in its attempt to provide for the fuel needs of its HNL operations.

29. The Debtor has satisfied the other requirements of section 365 of the Bankruptcy Code. The Debtor requests authority to cure any defaults under the Fuel Agreement pursuant to section 365(b)(1)(A) of the Bankruptcy Code in the ordinary course of business. The Debtor is not aware of any default existing under the Fuel Agreement. However, to the extent any such defaults exist, the Debtor has provided adequate assurance of future performance under section 365(b)(1)(C) of the Bankruptcy Code because the Debtor has met all of its obligations to ITOCHU under the Fuel Agreement and expects to meet all such obligations in the future.

**V. NO PRIOR REQUESTS**

30. The relief requested in this Motion has not previously been requested from this Court or any other court.

**VI. NOTICE**

31. Notice of this Motion has been provided to: (i) the Office of the United States Trustee for District of Hawaii; (ii) parties appearing on the Debtor's list of creditors holding the twenty largest unsecured claims; (iii) the Securities and Exchange Commission; and (iv) the Internal Revenue Service. Given the circumstances, the Debtor submits that no other or further notice need be given.

WHEREFORE, the Debtor respectfully requests that the Court enter an order, substantially in the form attached hereto, granting the relief requested herein and such other and further relief as is just.

Respectfully submitted this 21<sup>st</sup> day of March, 2003.

By: Nicholas C. Dreher  
NICHOLAS C. DREHER, ESQ.  
THEODORE D.C. YOUNG, ESQ.  
CADES SCHUTTE LLC

and

By: Lisa G. Beckerman  
LISA G. BECKERMAN, ESQ.  
DAVID P. SIMONDS, ESQ.  
AKIN GUMP STRAUSS HAUER & FELD LLP

Proposed Counsel for Debtor and Debtor in Possession

IN THE UNITED STATES BANKRUPTCY COURT

DISTRICT OF HAWAII

In re

HAWAIIAN AIRLINES, INC.,  
a Hawaii corporation,

Debtor.

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

**ORDER AUTHORIZING THE DEBTOR TO  
ASSUME JET FUEL SALE AND  
PURCHASE AGREEMENT PURSUANT TO  
SECTION 365 OF THE BANKRUPTCY  
CODE**

Date: March 21, 2003

Time:

Judge: Hon. Robert J. Faris

Upon consideration of the Motion for Entry of Order Authorizing the Debtor to Assume Jet Fuel Sale and Purchase Agreement Pursuant to Section 365 of the Bankruptcy Code (the "Motion"),<sup>1</sup> filed by Hawaiian Airlines, Inc., the debtor and debtor in possession in the above-captioned chapter 11 case (the "Debtor"), by and through its proposed co-counsel; and it appearing that notice of the Motion was appropriate and no further notice of the relief requested in the Motion is required; and upon consideration of the evidence presented to the Court in support of the Motion; and after due deliberation; and sufficient cause appearing therefor; the Court is of the opinion that the Motion is well-founded and should be granted in all respects.

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<sup>1</sup> All capitalized terms not defined herein shall be as defined in the Motion.

IT IS HEREBY ORDERED THAT:

1. The Motion is granted in its entirety.

2. The Debtor's business judgment to assume and ratify the Fuel Agreement is reasonable and appropriate, and the assumption and ratification of such agreement is hereby approved pursuant to section 365 of the Bankruptcy Code.

3. The Debtor is hereby authorized to cure any defaults under the Fuel Agreement pursuant to section 365(b)(1)(A) of the Bankruptcy Code.

4. The Debtor is authorized to take any and all actions necessary or desirable to perform its obligations and the transactions contemplated under the Fuel Agreement.

5. Notwithstanding the possible applicability of Bankruptcy Rules 6004(g), 7062, 9014, or otherwise, the terms and conditions of this Order shall be immediately effective and enforceable upon its entry.

Dated: Honolulu, Hawaii, \_\_\_\_\_, 2003.

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UNITED STATES BANKRUPTCY JUDGE

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In re Hawaiian Airlines, Inc., Chapter 11, Case No. 03-\_\_\_\_\_;  
ORDER AUTHORIZING THE DEBTOR TO ASSUME JET FUEL SALE AND  
PURCHASE AGREEMENT PURSUANT TO SECTION 365 OF THE  
BANKRUPTCY CODE