AIRLINE PENSIONS: AVOIDING FURTHER COLLAPSE

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BEFORE THE

SUBCOMMITTEE ON AVIATION

OF THE

COMMITTEE ON TRANSPORTATION AND INFRASTRUCTURE

HOUSE OF REPRESENTATIVES

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CONTENTS

TESTIMONY

PREPARED STATEMENTS SUBMITTED BY MEMBERS OF CONGRESS

PREPARED STATEMENTS SUBMITTED BY WITNESSES

ADDITIONS TO THE RECORD

AIRLINE PENSIONS: AVOIDING FURTHER COLLAPSE

Wednesday, June 22, 2005

HOUSE OF REPRESENTATIVES, SUBCOMMITTEE ON AVIATION, COMMITTEE ON TRANSPORTATION AND INFRASTRUCTURE, WASHINGTON, D.C.

The subcommittee met, pursuant to call, at 2:30 p.m., in Room 2167, Rayburn House Office Building, Hon. John L. Mica [chairman of the committee] presiding.

Mr. MICA. Good afternoon. I would like to call this hearing of the House Aviation Subcommittee to order. We are going to go ahead and get started. Most members won't want to hear my opening statement, anyway. But in order to keep the proceedings—we are already behind schedule. We will go ahead with opening statements. Then the order of business will be two panels of witnesses this afternoon. Of course, the topic is dealing with our airline pensions and the particular emphasis on looking at how we can avoid further collapse.

So, with that, I have my opening statement, and then we will recognize other members as they arrive, if they have opening statements.

As I said, today's hearing will focus on the crisis facing many of our airline pension plans and the impact of recent plan terminations. Loss of jobs, benefits, and pensions in the airline industry are nothing new, in fact. Just ask former employees of Eastern, Pan Am, Braniff, TWA, and other defunct carriers. However, the scale of recent airline plan terminations is much greater than in the past, both in terms of lost benefits and also in terms of cost to the Pension Benefit Guaranty Corporation.

Over the past four years, the airline industry, as we know, has experienced a record $32 billion in losses, with an additional $5 billion in projected losses in 2005. I might just clarify that. It is not all airlines, it is mostly our legacy carriers that find themselves in this situation. Many factors have contributed to these losses, including the terrorist-inflicted slowdown in our economy, a decline in business travels, the SARS epidemic, and also the increased competition from low-cost carriers, and, last but not least and continuing, the problem of soaring fuel prices.

In addition to all of these difficulties, a combination of historically low interest rates and poor stock market returns have resulted in the pension plans of many airlines—and other companies as well—becoming significantly under-funded in a very short period of time. These unfavorable economic conditions have affected pension plans in many industries, not just the airline industry.

The General Accounting Office recently studied the hundred largest defined benefit pension plans in the United States and found that, overall, reported plan funding levels were generally stable and stronger over the late 1990s. No more than 9 of the 100 largest plans were less than 90 percent funded in any year from 1996 through 2000. However, by 2002, approximately one-fourth, a quarter of all the plans were less than 90 percent funded. Even if additional legacy airline pension plans go bust, our Pension Guaranty Fund should be able to deal with the multi-billion dollar potential shortfall.

However, when we really get into some difficult and questionable territory is if we have a collapse of some our automotive industry corporations and their plans. That addition to, again, the difficulty we find ourselves in with the airlines is of particular concern to our Pension Guaranty Fund. Assets of pension plan sponsored by this industry fall short of liabilities by some $55 billion to $60 billion. Credit rating agencies recently downgraded the debt of General Motors and Ford to below investment grade status, signaling potential trouble ahead. The cost to Pension Benefit Guaranty Fund of pension plan terminations in this industry could well exceed that of the airline industry.

By comparison, it is interesting to note that even our Federal Government's Defined Pension Benefit Plan—and this is the old CRS system, Civil Service Retirement system—is grossly underfunded. I chaired the Civil Service Subcommittee and remember trying to deal with this issue. As of the end of 2002, the total assets attributable to CRS amounted to some $417 billion, but the liabilities for future benefits amounted to $950 billion, almost a trillion dollars, resulting in an unfunded liability for our own CRS Federal employees retirement fund of some $533 billion.

I wanted to make those figures clear, because if you look at even the airlines and automotive liabilities, we have the potential for dumping on the taxpayers. The liability that we have just in our Federal retirement system is almost a half a trillion dollars unfunded.

As a result of this under-funding, the assets attributable to CRS are expected to be depleted by the year 2023. In contrast, the Federal Employees Retirement System, FERS, as it is called, which covers employees hired since 1984, is almost totally funded by employees and agencies. Although pension funding contributions have by no means caused the airlines current liquidity crisis, for many old carriers they have exacerbated it. Cash-strapped legacy airlines are having great difficulty coming up with the amounts necessary to return their pension plans to full funding. Already two airlines in bankruptcy, U.S. Airways and United Airlines, have either terminated their plans or are in the process of doing so.

The U.S. Airways plan had an unfunded termination liability of some $5 billion, of which our Pension Guaranty Fund would guarantee $2.9 billion. The remaining $2.1 billion in unfunded liability represents the value of lost benefits. U.S. Airways employees in the aggregate will lose about 27 percent of the benefits they earned under this plan.

The situation with United Airlines' plan is similar. They have plans with an unfunded termination liability of some $9.8 billion, of which the Pension Guaranty Fund will guaranty about $6.6 billion, and we end up with a remaining $3.2 billion, which is the value of lost benefits, and that translates into United Airline employees in the aggregate will lose about 19 percent of the benefits they had earned.

Pension plan terminations such as these create some real hardships for employees who have worked many years of their life and also counted on promises that certain pension benefits will be there to provide security in their retirement. For current retirees, the loss of earned benefits can be especially devastating because of their inability to increase earnings to make up for the loss of those benefits.

The Pension Benefit Guaranty Corporation guarantees benefits, but only to a certain level. This level is adjusted annually and is currently set at some $45,614, assuming retirement age is at age 65. Retirement at earlier ages results, of course, in lower guaranteed benefit levels. For example, workers who retire at age 60, which is the mandatory retirement age currently for our pilots, the guaranteed benefit level is $29,649.

While these levels of benefits may seem small, the Pension Guaranty Fund will eventually have trouble guaranteeing even these small amounts. With $62.3 billion in total liabilities against only $39 billion in total assets, the single employer pension insurance program lacks the funds to pay a significant portion of future benefits for which it is obligated. While the Pension Guaranty Fund has enough assets on hand to continue paying guaranteed benefits for a number of years, its unfunded liabilities continue to grow, and with each new plan of termination we get into more serious problem. At some point in the future the Pension Guaranty Fund will, of course, run out of money.

The Center for Federal Financial Institutions has projected, if no pension reform legislation is enacted, our Pension Guaranty Fund will run out of cash by the year 2021 and a $78 billion bailout will be required by the Federal Government. So clearly it is in the interest of workers, of taxpayers, and certainly the Federal Government to correct today's systemic pension under-funding.

The era of defined benefit pension plans may well be ending. The defined benefit system is under pressure not only from pension under-funding, but also under pressure from a changing workforce that requires more mobile retirement benefits and increased competition from many companies with lower cost structures that do not include these expensive defined benefit programs. So most airlines that offered defined benefit plans have either negotiated to freeze those plans and replace them with defined contribution plans or currently in negotiations to do so. We are going to see a lot more of that.

The terminations of U.S. Airways' and United's plans are going to have ripple effects, and also they are going to have competitive implications for other airlines. The so-called domino effect, in which other airlines terminate their own defined benefit plans in order to compete, will also cause further strain on our existing Pension Guaranty Fund. Enactment of pension reform legislation will also have competitive implications for the airlines.

While our Subcommittee and the Transportation Committee does not have specific legislative jurisdiction over pension laws, it is absolutely vital that this Subcommittee understand how these important pension issues uniquely impact our airline industry, their employees, and, of course, the taxpayer.

So I look forward to hearing the views of our witnesses and look forward to our two panels.

I am pleased to recognize at this time for his participation our ranking member, Mr. Costello.

Mr. COSTELLO. Mr. Chairman, thank you. Mr. Chairman, I ask unanimous consent that all members be allowed to submit their opening statements for the record.

Mr. MICA. Without objection.

Mr. Costello asks unanimous consent that Congressman Price of Georgia be permitted to participate in today's hearing. He is not a member, but has legislation pending relating to this issue as requested to the Subcommittee. So without objection, so ordered. And he will be, of course, last on the totem pole, but we welcome him.

Mr. COSTELLO. Mr. Chairman, as everyone in the room knows, we just had a series of votes and we are getting started late here. The witnesses and others have been here about 45 minutes, so I am going to submit my statement for the record.

I do want to thank you for calling this important hearing today. This is an extremely important issue for all of the employees of the airlines and for the American people. So I look forward to hearing from our witnesses today. I have a number of questions that I have that I will be asking our witnesses, and I thank you again for calling the hearing.

Mr. MICA. I thank the gentleman.

Mr. Ehlers?

Mr. EHLERS. Thank you, Mr. Chairman. I also will try to be brief, but I certainly want to thank you for calling this hearing, a very important topic. I am getting a double dose of it because not only am I on this Subcommittee, but I am also on the Education Workforce Committee, and tomorrow we are taking up the pension reform bill there, and full Committee next week.

I also want to commend you for inviting Bradley Belt to this hearing. I have been in meetings with him twice now, and he is a very fine public servant, one of the best I have met, has a very good view of what is wrong, and I think has some very valuable advice for us as to what the Congress should be doing regarding pension reform. It not only needs reform, but also revision in a number of ways.

But let us not forget in this whole process that there is another part of the puzzle that I think is needed, and that is reform of the bankruptcy laws. We already have reformed individual bankruptcy laws because we felt it was getting too easy for individuals to declare bankruptcy, and they were using it as a personal financing strategy. I have seen what is happening in the economy as a result of the difficult economic years of the last few years, particularly following a very boom period when everyone was possibly not making the wisest investment decisions.

But I see corporations now beginning to use bankruptcy as a business strategy. And it affects people in my district, not in the aviation industry so much as in the manufacturing industries, where smaller suppliers to bigger manufacturers are being severely hurt when the larger manufacturers declare bankruptcy, leaving the smaller companies with two or $3 million of unpaid bills, and their fiscal stability is questioned and they may end up in bankruptcy.

In this case, also, I am not accusing any airline of using bankruptcy as a business strategy, but when someone goes through Chapter 11 and emerges as a much more viable corporation at the expense of the employees, and then creates great difficulty for those airlines which are trying to meet their obligations to their employees, there is something wrong. And I have already suggested to the Chief of Staff from the Judiciary Committee they should begin investigating this, and I also will be speaking to Mr. Sensenbrenner, the chairman of that committee, urging him to do the same. It is clear that we need the same type of reform of corporate bankruptcy laws as we have done for individual bankruptcy laws.

So I look forward to the testimony we hear. I hope it will be fair and objective in regards to all parties concerned. And I, of course, have a very personal interest, being from Michigan. When we were talking about General Motors and some of their problems. And if in fact they have to go through bankruptcy, we are going to create such immense problems for Mr. Bent that even the Congress cannot save him. He will need help from a higher authority at that point.

With that, I yield back. Thank you.

Mr. MICA. I thank the gentleman.

Ms. Norton?

Ms. NORTON. Thank you, Mr. Chairman. Just very briefly, I wanted to welcome Mr. Belt, one of my own constituents, and thank him for the extraordinary job he is doing under quite impossible circumstances, a problem we keep calling urgent. I have stopped doing that because an urgent problem is something you get up and do something about right away. It is one thing to lose a job, but it is quite another to lose a pension; it is kind of like losing your Social Security or having it cut. That is the end of your work life.

This problem gets worse, not better. It has been there with the airlines. The more manufacturing has problems, the more we see it spreading. And now there is a triple hit here that we simply have to do something about. There is the Pension Benefit Guaranty Corporation, in this case, the airlines, and, of course, the workers. Everybody gets hit all around. I am not surprised that as companies fail, one of the first things they do, if we let them, is fail to make the necessary contributions to their pensions.

All I want to say, Mr. Chairman, is we all ought to be grateful to you for keep putting this problem forward because if we keep putting it off, we are looking at a huge taxpayer bailout. That is what is going to happen. They are going to come, the Pension Benefit Corporation, no Federal funds now. Watch out, because if it all goes up in the air, guess who is going to pay the bill.

Thank you very much, Mr. Chairman.

Mr. MICA. Thank you.

Mr. Diaz-Balart?

Mr. DIAZ-BALART. Thank you, Mr. Chairman. I actually also would like to thank you for holding this important hearing today.

The future of employee pensions is a vital issue that we obviously must address before employees and taxpayers are overly burdened.

Earlier today, Mr. Chairman, I had the opportunity to visit with a group of airline employees that represented just about every aspect of the airlines, including management. Their commitment to the industry and to their company is clearly unparalleled. All of them have faced huge actual pay reductions after 9/11 and, as much as anyone else, these employees have helped our airlines survive over the past few very difficult years.

I look forward to working with our Chairman and with the members of this Committee to find appropriate ways to ensure that the pensions of our airlines and their employees is appropriately protected. In doing so, I think we need to look at diverse economic and financial outlooks of each individual airlines. As with any industry, Mr. Chairman, of course, you know very well, airlines have varying and different financial situations, and different outlooks, and also different plans as to how to deal with their pension future and their pension solutions.

So, again, I look forward to working with the Committee and the Chairman. Mr. Chairman, again, thank you for bringing up to the forefront of this Congress I think a very important issue that we are going to have to deal with sooner or later.

Mr. MICA. I thank the gentleman.

Mr. Boswell.

Mr. BOSWELL. Thank you, Mr. Chairman. I too appreciate your calling this meeting. I would like to associate myself with your remarks. And I will follow the leadership of my Ranking Member by submitting my remarks for the record if he will assure me that he will read them. I submit them. I yield back.

Mr. MICA. I thank the gentleman.

Mr. Westmoreland.

Mr. WESTMORELAND. Thank you, Mr. Chairman. And I do, too, appreciate your having this hearing. I want to thank the Chairman for allowing Mr. Scott Yohe from Delta Airlines to come and testify. Delta Airlines is one of the reasons that Hartsfield-Jackson Airport is the busiest airport in the world. Delta has about 80,000 employees, both active and retired. Fifty-five hundred of those Delta employees live in my district, more than any other district in the United States. So I am very aware of what this hearing means to those folks.

I would also like to thank the Chairman for allowing my colleague, Dr. Price, to come, who has introduced a pension bill that I have happily tried to co-sponsor with him.

So I am anxious to hear what the witnesses have to say today, and I appreciate your time in waiting to be able to inform us of some of the things that we need to be doing.

And again, Chairman, I want to thank you for doing this.

Mr. MICA. I thank the gentleman. We did not have a vote, though, on whether or not Mr. Yohe could participate, but we will talk about that later.

Mr. Pascrell?

Mr. PASCRELL. Thank you, Mr. Chairman, Mr. Ranking Member. There are a lot of corporations out there that are cooking the books, as we have read, and I am very annoyed. I came to the Congress in 1996 to guaranty defined benefits for Social Security and to guaranty defined benefits for those who work hard and pay into pensions. And there is no corporate person in this Country that should be immune, as far as I am concerned.

That we allow companies to use legal accounting gimmicks at the expense of their employees is not acceptable. I think we have done a poor job, up here on this side of the desk, protecting employees who have no voice. The tentacles, for instance of Enron run throughout this Nation. Companies in New Jersey were affected by that. People lost everything. They worked 25, 30 years. They got screwed. And we should be darn angry about it.

We should be as angry about this as we are about the bankruptcy laws that we proselytized on last week and the week before. Same thing. Same concern. Efforts to take advantage of those who are voiceless. I am surprised that we are not seeing the same harsh talk about responsibility and accountability. This is a place of doublespeak, I can assure you. So welcome.

Our current system will encourage other airlines to follow in the path of United. To remain competitive is an obvious flaw. I support providing some flexibility, where needed, to ensure that more airlines do not have to be bailed out. But my father worked for 47 years for the railroads, and if you pick the most prominent subject matter at the supper table, when he was able to make his way home on time, it was his pension. He looked forward to that. He really did. Didn't talk about Social Security. He was counting on a lot of things, but he was counting on his pension.

Are baby-boomers are counting on their pensions? Apparently they are not counting on Social Security.

Let us be really concerned about making general statements about airlines dumping pensions on the PBGC. Not all airlines are alike, thank God. We must recognize that there are airlines that plan to stick to their deals. There are airlines that plan to uphold the commitment to their employees under current funding rules. Before we rush into Federal involvement, it is appropriate that we take a close look at how we can best protect airline workers. That is my commitment, and I aim to fulfill my commitment.

Thank you, Mr. Chairman.

Mr. MICA. I thank the gentleman.

Others seek recognition? Mr. Ehlers?

Mr. EHLERS. Thank you, Mr. Chairman. Just a very brief clarification of one of my comments. When I talked about bankruptcy as a business strategy, I was not in any way implying that anyone deliberately used that as a strategy.

My point is simply that because the bankruptcy laws and ERISA were written at different times, and totally independent of each other, companies find themselves in the situation that, when they enter bankruptcy, one of the best choices is to divest themselves of the pension responsibilities. And that is the issue we have to clarify and correct, so that that will not be the best available option to a company that enters bankruptcy.

Thank you.

Mr. MICA. No further opening statements?

Mr. Price, did you want to be recognized briefly?

Mr. PRICE. If I may, Mr. Chairman. I just wanted to thank you and Ranking Member Costello and the members of this Committee for allowing me to attend this important hearing. And in the interest of brevity and to demonstrate my appreciation, I ask permission to put my opening statement in the record.

Mr. MICA. Without objection, it will be included in the record.

With those opening statements, we will now turn to our first panel of witnesses. The first witness is Ms. JayEtta Z. Hecker, and she is the Director of Physical Infrastructure Issues in the Government Accountability Office. She is accompanied by Ms. Barbara D. Bovjberg, and she is the Director of Education, Workforce, and Income Security Issues also at GAO. And then Mr. Bradley D. Belt. He is Executive Director of the Pension Benefit Guaranty Corporation.

I would like to welcome our witnesses. We will go right to Ms. Hecker, Director of GAO, for your testimony.

Welcome, and you are recognized.

TESTIMONY OF JAYETTA Z. HECKER, DIRECTOR, PHYSICAL INFRASTRUCTURE ISSUES, GOVERNMENT ACCOUNTABILITY OFFICE; ACCOMPANIED BY BARBARA D. BOVJBERG, DIRECTOR, EDUCATION, WORKFORCE, AND INCOME SECURITY ISSUES, GOVERNMENT ACCOUNTABILITY OFFICE; AND BRADLEY D. BELT, EXECUTIVE DIRECTOR, PENSION BENEFIT GUARANTY CORPORATION

Ms. HECKER. Mr. Chairman and Mr. Costello and other members of the Committee, I am very pleased to be here today. As you may know, we have been doing continuing work on the financial condition of the airline industry at the request of Congress, and our current work is actually focusing on particular issues of bankruptcy and pensions. This work, however, is preliminary, and we will have a final report in September.

The three topics that I will cover basically address the ongoing debate that several of you have alluded to over the legacy airlines' use of Chapter 11 bankruptcy protection as a means to control cost, continue operations, and, in particular, shed pension cost. The three issues are: first, very briefly, some background of the financial difficulties; the second on the effect of bankruptcy; and the third on the effect of airline pension under-funding.

Now, the first topic, about the financial condition of airlines, it is not news to any of you that there are sever financial difficulties. And as you may recall from earlier work that we completed, the bottom line is that legacy carriers have not been able to reduce their costs sufficiently to profitably compete with low-cost carriers. There is a fundamental restructuring of this industry still going on in response to the deregulation of the industry in 1978.

The slide I have here was the bottom line of our review of the financial condition of carriers. It basically shows that legacy airlines, while they have worked very hard at it, have not sufficiently lowered their costs to be able to compete on a cost basis with the low-cost rivals. The blue line is the legacy carriers' unit costs, and you see it rising until 2001, and then the effort to try to control them, bringing them down by 2004.

And a somewhat similar pattern, but much lower, for the low-cost carriers. The main story is that there is a continuing and somewhat growing differential in the unit cost between legacy airlines and low-cost carriers. Defined benefit pensions account for about 15 percent of that 2.7 cent difference in unit costs. This cost difference really is at the heart of the legacy airlines continuing financial losses, as many of you know, nearly $30 billion since 2001, with another $5 billion expected this year.

The second point, then, is to look at the impact of bankruptcy, and the bottom line of this is that bankruptcy is and has been endemic to the industry for many years. It really reflects the long-standing structural issues and some of the unique characteristics of this industry. The main point, though, is that it is not really the cause of the industry ills, but, rather, reflects thoses problems.

This next chart has data since 1984 and shows that bankruptcy and liquidation have been more common in this industry. The beige little block is the percent of failures for all industries in total and the blue line is the airline failure rate. You can see that since 1968 there have been many bankruptcy filings, 160, in fact, since 1978; 20 in the last five years.

A key point here is that the airline industry has historically had the worst performance of any sector. So it is no surprise that bankruptcy has been endemic to this industry. Another point from our review of bankruptcy is that airlines rarely emerge successfully from bankruptcy. Of 146 Chapter 11 filings, only 16 carriers since 1979 are still in business.

Another key issue about bankruptcy is the argument that it leads to over-capacity. This chart basically examines whether the evidence supports that. The red line is the growth of industry capacity over time, and on it I have the blocks of all of the major bankruptcies; and the little gray bars are the periods of recession. Basically, the bottom line is that the historical growth of capacity in this industry has continued unaffected by major liquidations, and those slight downturns are more closely correlated with recessions. So you only get the drawback of the capacity when that overall demand decreases with a recession.

The basic conclusion of our review of bankruptcy is that, in fact, there is no clear evidence that bankruptcy has harmed competitors, either keeping excess capacity in the industry or lowering prices. They do, however, of course, shed costs in bankruptcy and pensions, as we are discussing here today. But while bankruptcy may not harm the financial health of the airline industry, it is of considerable concern to the Federal Government, to airline employees and retirees, and as you have all said, really brought into light by the recent terminations.

The bottom line here—I will have a few more slides on this issue—is that the legacy airlines in fact face significant near term liquidity pressures, and pensions are only a small part of that financial pressure.

This first one is no news to anyone, that there has been a severe and dramatic under-funding from an over-funding in as early as 1999. It went down to a $23 billion under-funding in 2002, and the only reason it picks up is not because pensions have now been reinvested in; those are the bankruptcies of U.S. Airways and, then in 2005, when the United pension plan was terminated that the under-funding is now approximately $13.7 billion.

Now, the main story I have is actually in this next chart. And if you don't like charts, this is one—even though it is busy—that I think tells the bottom line of our message today. The blue line in 2004 is basically the cash on hand of all of the legacy carriers. It is a little under $10 billion in 2004. The other blocks basically outline the fixed obligations of all the legacy carriers projected for the next four years.

Now, the big story, as I think I have already told you, is that pensions, that gray bottom block, accounts for only about one-sixth, or 17 percent, of the fixed obligations of carriers. Basically, this is a daunting, overwhelming, and severe crisis for airlines, and it is not just pensions. This is the threat really driving bankruptcy and the move toward bankruptcy, in our view.

Now, I might also tell you there is an interesting thing about the blue lines. It looks like, oh, they have got a lot of cash. That cash is debt-financed. That cash is being burnt. They are going through cash. They are losing money. So there is no new cash coming in. That cash is from all of the assets of the carriers, everything having been securitized. So this is a severe crisis in liquidity for all the carriers. And the pension crisis, which is real and is severe, is only about one-sixth of that problem.

I know I am running over. Oh, yes, there it is. I am running well over.

I have three quick factors that I want to tell you what has caused the airline pension problems. The first is market factors. Several of you have referred to that. There was a perfect storm of reduced assets and increased liabilities. The second is management and labor decisions. Basically, we saw a long period of very generous contracts and airlines not funding plans when they could.

This is an important slide visually showing that. The beige line, which you can barely see, is the actual contribution of legacy carriers during very profitable years. The profit is in the dark blue. So when you see that dark blue line above the line, those are very profitable years, historically profitable years for carriers. Airline funding was only 8.5 percent of the potential that they could, that was still tax deductible. So you have $2.4 billion in actual contributions, with a maximum of $29 billion. So they basically were not funding these plans even when they were making money.

The third factor—and I am sure Mr. Belt will go into this in more detail than I need cover—the pension benefit funding rules have not only not prevented under-funding, they have really contributed to the under-funding. We have seriously under-funded plans, including United, that appear to be fully funded and in compliance with current requirements, but in fact were grievously under-funded.

The next chart in fact is too complex, so I will just point your attention. This is looking at the pension problems and the pensions that have been turned over to PBGC. If you look in the first three lines—Eastern, Pan Am, TWA—look at the last two columns. The PBGC losses were $530 million, $700 million, $600 million. Participant losses were $100 million, $55 million, $45 million. U.S. Airways and United combined is a $9.6 billion loss for PBGC. Loss. That is net of the assets inherited. The loss to participants, again, is multiple orders of magnitude beyond prior bankruptcies.

The concluding observation is that the financial condition of the carriers is not sustainable and some carriers are likely to terminate under current conditions. An important part of the lesson here—because everyone really wants to look for a solution—is that terminating pensions, or, the option being proposed, to amortize pensions over longer periods, will not, in our view, solve the long-term fundamental restructuring and financial problems typified by that unit cost differential. The cost structure problem will not be solved, given the small portion that pensions represent, of other major obligations.

The other important thing is that the implications for PBGC are actually much broader than just the airline industry, and GAO has done substantial work on broad pension reform, and that is why I have my colleague, who has directed that work, here to address any issues about GAO's long-term advocacy for comprehensive pension reform.

That concludes my statement, and I would be very happy to take questions. I apologize for going beyond.

Mr. MICA. Thank you. You always do just a great job. And I guess what you showed us today is part of a larger report that is due out when?

Ms. HECKER. In September.

Mr. MICA. In September. Okay.

Well, we are going to withhold questions, but we are going to go next to—well, your colleague, Ms. Bovjberg, did she have some comments at this stage?

Ms. BOVJBERG. No, I don't, Mr. Chairman. But thank you for asking.

Mr. MICA. Okay. Thank you.

Then we will go to Bradley Belt, Executive Director of the Pension Benefit Guaranty Corporation. Thank you for your participation today. Welcome, and you are recognized, sir.

Mr. BELT. Thank you, Chairman Mica, Ranking Member Costello, members of the Subcommittee. I commend you for holding this timely hearing, and I very much appreciate the opportunity to briefly discuss the pension challenges facing the airline industry and the important role played by the Federal pension insurance program. I would also like to thank Mr. Ehlers and Ms. Holmes Norton for their very kind comments.

And I want to commend you, Mr. Chairman, for your extraordinarily comprehensive opening statement, which you well outlined all the key issues we are facing, has rendered much of my statement somewhat superfluous. But at the risk of some redundancy, I will forge ahead.

As you know, Mr. Chairman, this hearing is occurring against the backdrop of the largest pension default in the history of the United States. By the numbers, which you cited, United Airlines pension plans have assets of roughly $7 billion to cover liabilities of $16.8 billion, for a shortfall of almost $10 billion. The pension insurance program will be responsible for covering $6.6 billion of that gap, making it by far the largest claim in the 31-year history of the PBGC.

But the United default also sets another dubious record: the largest ever loss of earned pension benefits by workers and retirees. Weaknesses in the pension funding rules allowed United Airlines to dramatically under-fund its pension promises. As a result, the company's more than 120,000 workers and retirees now stand to lose roughly $3.2 billion in retirement income that they were promised and were counting on.

As tragic as these losses are, they are unique only in their size. As you noted, Mr. Chairman, United is merely the latest airline to default on obligations to its workers. In each round of airline bankruptcies, the pension insurance program has wound up responsible for benefits that companies promised but failed to adequately fund.

In the early 1980s it was Braniff; in the early 1990s it was Pan Am and Eastern; and in this decade it has been TWA, U.S. Airways, and United. Claims from just these six airlines come to $11.7 billion, or 38 percent of the total in the history of the pension insurance program, even though they have paid only 2.6 percent of total premiums.

There is no question that the airline industry faces substantial business challenges. And Congress and the Administration have previously acted to provide assistance to help deal with extraordinary events. After September 11th, Congress created the Air Transportation Stabilization Board to administer up to $10 billion in loan guarantees to help a then struggling industry get back on its feet.

Today, nearly four years later, and with passenger traffic at record levels, some carriers are asking for a different form of loan guarantee, in the form of pension funding relief. In economic terms, that is what weaker funding rules represent, a loan from the pension plan from the workers to the company, co-signed by the PBGC and underwritten by healthy companies whose premiums finance the insurance program.

This funding break would come up on top of the exemption Congress provided just two years ago, which allowed airlines to skip 80 percent of their required catch-up pension contributions for 2004 and 2005, in the amount of $2.4 billion. At the time the bill was enacted, the airlines suggested that the two-year temporary relief would see them through a difficult period without the need to either terminate their plans or to seek additional relief from Congress. In the interim, U.S. Airways and United both moved to terminate their plans. And now that the temporary funding holiday is set to expire, some legacy carriers are seeking to stretch out relief for 25 years.

Mr. Chairman, pension under-funding is not an accident, and it is not the result of forces beyond a company's control. On the contrary, it is the perfectly predictable and controllable product of decisions made by the company. In the case of the airlines, a series of missteps allowed pensions to become significantly under-funded. Companies did not contribute as much cash as they could in good times, as was noted by the GAO. In certain cases, they contributed no cash at all when it was most needed. And in still other cases labor and management agreed to generous benefit increases that are now proving difficult to afford.

The tragedy is not that any of this was illegal. The tragedy is that it was legal under our system of flawed pension funding rules. United and U.S. Airways would not have presented claims in excess of $3 billion each, and with funded ratios of less than 50 percent at termination, if the rules worked. Consider United. From 2000 onward, when the funded status of the company's pension plan was deteriorating and the financial health of the company itself was failing, the company put little cash into its plans, did not provide under-funding notices to workers and retirees, and for most years in plans did not pay a variable rate premium to the PBGC.

The Administration has proposed a sensible, balanced reform package to correct the flaws in the system. Key elements include: a more accurate measure plan liabilities that would reflect the financial condition of the sponsor and the risk of plan termination; asset and liability smoothing, which distort the true funded status of pension plans, would be eliminated; credit balances that allow companies to avoid making cash contributions for, in some cases, years on end, would be barred; companies that have failed to fund existing pension promises would be limited from making new unfunded promises; more accurate and timely plan funding information would be provided to plan participants, investors, and regulators; and, finally, PBGC premiums would be restructured to be more equitable, generate sufficient revenue to close the program's deficit and pay expected future claims. The flat-rate premium would be raised for the first time since 1991, an index to reflect wage growth and all under-funded plans would pay a variable rate premium.

Mr. Chairman, the Administration is committed to strengthening the pension insurance program and keeping defined benefit plans as a viable option for employers and employees. We believe the Administration proposal strikes an appropriate balance and will best protect the pension benefits earned by workers and retirees, minimize the need for premium payers and taxpayers to subsidize the system, and reduce the chances of another pension tragedy like United.

Thank you for your invitation to testify, and I would be pleased to answer any questions.

Mr. MICA. Thank you. I thank GAO and the Pension Benefit Guaranty. Witnesses have painted a very grim picture of what we are facing. I think it is actually a lot worse than I had suspected. And I don't think we are here to cast blame on airlines or any other employers. Same thing that I described with our own Federal employee benefit program, which is a half a trillion unfunded for Federal employees. We have mirrored some of the private sector.

Ms. Hecker, the picture you paint, I described in my opening statement what I thought would happen as a ripple effect as other carriers see what has happened with United and what may happen with U.S. Air. You testified, however, that this is only one-sixth of, really, their problem. Actually, what you are describing is legacy carriers in a lot more trouble than just the pension plan.

Ms. HECKER. Precisely.

Mr. MICA. That we should expect I guess a ripple effect not so much precipitated by their need to do something with their pension obligation, but much more serious issues. The charts you put on the cash, the liquidity, were outstanding I think in describing the problem, but is that an accurate depiction of their situation?

Ms. HECKER. Absolutely. There is basically a fundamental restructuring that is occurring. There are non-sustainable cost disadvantages that the legacy carriers have not been able to overcome, and that is also reflected in these very, very high fixed obligations. Part of it, of course, is a balloon from the pension deferral that was passed in 2004, for 2004 and 2005, so you have

Mr. MICA. And that expires—or has expired?

Ms. HECKER. No, at the end of this year.

Mr. MICA. Okay, that expires the end of this year. That was a reduction of 80 percent for that period of time, is that right?

Mr. BELT. That is correct.

Mr. MICA. Okay. What was even more disturbing—I had never seen the charts you put up—about their contributions, and I think that little beige line, the year 2000, when they were actually making money, their contributions were practically nothing. Did we allow that by law, they could make all the promises they wanted but weren't obligated to put anything in?

Ms. HECKER. That is right. It basically was because the funding rules allowed them to appear to be fully funded.

Mr. MICA. So whatever reform we adopt, we have got to have a real hammer and lock on what you promise, you also have to deliver.

Ms. HECKER. Precisely.

Mr. BELT. Mr. Chairman, if I can touch upon that one point.

Mr. MICA. Yes.

Mr. BELT. One of the key issues highlighted in the Administration's reform proposal are the issues related to so-called credit balances. An illustrative example is the United Airlines pilots' plan, which, when we assume it, will be underfunded by $3 billion. The company has not put a dollar into that pension plan since 2000, for five years, notwithstanding the fact that the liability and the gap grew over that period of time. But that was allowed by the rules.

And the particular rule that allowed them to avoid having to put in any cash was credit balances that were built up during the 1990s, during the boom years, when stock market gains were fairly good and sometimes companies did put a little bit of money into their plans. But they were able to use the availability of the credit balances to offset the otherwise required minimum funding contributions.

Mr. MICA. Okay, one last question. I want to try to let Mr. Costello get his questions in before these votes. There are a couple of proposals around that allow amortizing the pension debt over, I guess, five to seven, or up to 25 years I guess is another proposal. It doesn't sound like either of those are really going to make this work. What is your opinion, Ms. Hecker, and then Mr. Belt?

Ms. HECKER. We don't have an evaluation that is a specific position on the bill, but a lot of our work I think speaks to some points. First of all, there is an economy-wide problem with the defined benefit system, and singling out airlines really is likely to have precedence for other industries. GAO has really favored a comprehensive reform. The problem is, the way it has worked, the more under-funded you were, the less you paid.

So we now have a crisis where they are more severely financially strained than ever. But do you perpetuate this fiction that, by stretching it out, somehow they will really be fully funding their plans? There is just no clear impact on the ability to actually save the carrier or to salvage the benefits ultimately for the employees.

Mr. MICA. Pretty grim.

Mr. Belt.

Mr. BELT. Mr. Chairman, the Administration believes that the funding rules should be made more robust and strengthened, rather than weakened, and that the funding rules should apply to all participants in the system, and you would not have a separate set of funding rules for certain companies or industry sectors. Having said that, certainly the goals of any type of measure like that are laudable ones, that is, seeing if there is a way to maintain the pension plan for the benefit of the workers and retirees, and to avoid having losses incurred by the Federal pension insurance program.

But I think there are several issues that are raised in that context, one of which is are we, as noted by Ms. Hecker, putting off the problem to another day and there is a potential for the problem to be much larger at that point in time? The bill, as drafted, that you may be referring to—at least I have seen a couple of measures—would limit the liability exposure to the pension insurance program, but it would not cap the liability to the pension insurance program. There are a number of ways in which liability could grow over a period of time.

Another issue is what signal does it send. Does it exacerbate the moral hazards that already exist in the system? Does it send a message for a company that is perhaps modestly underfunded now, that the way to get special treatment is to get more underfunded, to not put in cash out of current resources, but use that for profit-making activities and get into a deeper hole and, that way, be able to more effectively make the case that special funding rules are needed?

I would also note that we are facing challenges from a risk perspective from a whole host of companies, not just the airline industry. There have been eight auto part suppliers that have filed Chapter 11 just in the past six or seven months. They would probably be looking at this issue and saying what about us? And there are other companies just outside Chapter 11. And it is not unique to the auto sector as well. We are dealing with companies in the textile industry, grocery companies chains, service companies, financial services companies and others that are similarly situated.

And I would also note, as I mentioned in my testimony, that relief was granted just two years ago in PFEA, and it was worth about $2.5 billion of being able to avoid pension contributions during that period of time. And it was represented at that time that the problem would then go away. In addition, some companies, including airlines, have taken advantage of rules under current law, funding waivers, to obtain additional funding relief.

And, as the General Accountability Officehas stated, that this is not primarily a pension problem; there are a host of other issues.

So I think we have to understand that those are all issues that are presented whenever we start talking about different kinds of relief measures.

Mr. MICA. Mr. Belt, Ms. Hecker, we do have two votes, so what we are going to do is recess. I do have one question, though, Mr. Belt, for you. In talking to you—and I think our staff have talked to you—you felt that you could sustain all the projected or potential losses you see now for the airline industry. Where it gets a little bit hairier is the potential of other—what we do here with airlines sort of has, again, this ripple effect. Can you sustain the ripple effect with other industries following suit?

Mr. BELT. We are already, in some respects, if we were a private sector insurer, technically insolvent.

Mr. MICA. You are broke.

Mr. BELT. Our liabilities, the commitments we have taken on in terminated pension plans, exceed our assets by more than $23 billion. But from a cash flow or liquidity standpoint, we can continue along this path for several years, but the hole gets deeper each and every day. So the question is how do you fill the hole at some point in time, and who pays for that?

And that is the challenge we are all facing and that we have got to try to resolve. I mean, in some respects—take United Airlines. We get $7 billion of assets in that pension plan. We, right now, pay out $3.5 billion a year in benefit payments. That gives us two years worth of benefit payments. The only problem is we are also taking on an additional $17 billion of liabilities that we don't have the ability to cover. And premiums are far insufficient to not only fill the current gap, the $23 billion, but also cover future expected claims. The loss on United alone is six years' worth of past premiums.

Mr. MICA. Thank you. To give everyone a fair shot at full questions, we will recess now for approximately 20 minutes. Thank you.

[Recess.]

Mr. MICA. The Subcommittee is back to order, and I would like to recognize Ranking Member Mr. Costello.

Mr. COSTELLO. Mr. Chairman, thank you.

Ms. Hecker, first let me compliment you on your testimony. As the Chairman said, it is always very informative. A couple of questions. On the chart that you put up on the overhead, on page 16 you talk about—and I understand that the agency will not go on the record supporting or opposing a particular bill, but you indicate that terminating pensions or amortizing pension contributions over a longer period will not solve legacy airlines' long-term fundamental problems. And then on chart number 4 you talk about that the legacy airlines have not sufficiently lowered their cost. We all know that employees have given pay raises, they have taken reductions in benefits in order to help the legacy airlines.

I wonder just how tight can you squeeze the orange to get more juice out of it. Give me some of your thoughts. What are the things that the legacy airlines should have been doing that they have not been doing in order to sufficiently reduce and lower their cost, as you indicate.

Ms. HECKER. I don't think I have a simple answer for that. It is an extremely important question, and I think from the perspective of our work I could see about it for the record and see if we can supply some insights, but off the top of my head I don't have some specific actions

Mr. COSTELLO. Well, we, of course, the Chairman and I and members of the Subcommittee, meet with CEOs and others from the various legacy airlines from time to time, and we ask that question, but in realizing your testimony that we are talking about pensions is only 17 percent or one-sixth of the legacy airline long-term obligations. But when you say that they haven't sufficiently lowered their cost, that is pretty obvious, but where in fact can they lower costs? And I would ask you to maybe get back with the Subcommittee and give us some answers or some recommendations.

Secondly, on number 16 again, page 16 of your chart, you say implications for the PBGC that you are recommending that the GAO supports broad pension reform that provides, and then one is meaningful incentives to adequately fund plans; two, additional transparency for participants; and, three, accountability for those firms that fail to match the benefit promises they make with the resources needed to fulfill those promises.

And I realize you are asking for broad pension reform, but it seems like a broad recommendation. And I wonder if you might narrow it down and give us some more specifics as to what they may do for, number one, meaningful incentives to adequately fund plans.

Ms. HECKER. I will have Ms. Bovjberg, who has worked on the summarizes, respond.

Ms. BOVJBERG. We have made those recommendations fairly general to give Congress some leeway. As time has gone on, we have also tried to make some more specific ones. For example, we think that the deficit reduction contribution, which we refer to more broadly in our report as the additional funding contribution, is something that really needs to be re-examined. That affected very few firms, and the firms it did affect didn't make that payment in cash. As Mr. Belt says, addressing the use of credit balances is urgent. Dealing with the way that we calculate and define funding assets and liabilities is crucial. This is not just for airlines, it is for all defined benefit pension sponsors.

I think that you will have before you this year at least two, if not more, proposals for comprehensive pension reform that will deal with funding rules, that will deal with premium issues, that will deal with better disclosure and transparency. And those are the areas that we would urge you to consider. I do want to say that in a forum that we had earlier this year we did discuss legacy costs, legacy pension costs separately from comprehensive pension reform and going forward. We thought it was important to make changes to the pension financing system and the pension insurance system going forward, but understand that our policy might have to address legacy costs separately. But I would encourage Congress to think about legacy costs as not only airlines, but there are other industries that we would put in that category. And there are different ways to think about supporting those.

Mr. COSTELLO. The third point under the broad pension reform proposals, accountability for those firms that fail to match the benefit promises they make with resources needed to fulfill those promises. It is pretty difficult for an employee of a particular legacy airline to know—for instance, Mr. Belt, in your testimony, which I am going to ask you about in a minute you indicated that one legacy airline had not made a contribution since 2000. And I guess my question is how difficult is it, since every legacy airline may have different bookkeeping accounting procedures, to determine how much a pension fund of a particular airline is under-funded?

Mr. BELT. Yes, Mr. Costello, I am happy to answer that. That is one of the issues that is directly addressed by the Administration proposal. We believe very strongly that you need to have accurate measures and liabilities so that all the system stakeholders—workers and retirees, shareholders of the company, as well as regulators—have an understanding of what the real financial condition of the pension plan is at any given point in time. That is not available to the system stakeholders under current law for a variety of reasons.

The calculation of assets and liabilities under ERISA is a study in obfuscation. We use these smoothing mechanisms that look at the value of assets going back from the present time back over several years. Same thing with calculating liabilities. That is like driving your car down the road looking in the rearview mirror. What happened three or four years ago has no relevance to the economic reality today. So it is vitally important that we have accurate measures of liabilities and that we report that information on a timely basis, and that we make that information available to all the system participants.

One of the issues right now is PBGC has relatively timely information about the financial status of pension plans under so-called Section 4010 that is filed with us each year. Those are the companies that are most underfunded. We are proscribed, precluded by law, from making that information publicly available. Workers and retirees are entitled to know that type of information.

Mr. COSTELLO. While I have you—and I will go back to Ms. Hecker with another question—let me ask you, Mr. Belt. You indicate in your testimony that two of the fundamental rules, in particular, the credit balances and the smoothing of assets and liabilities, have contributed to the pension crisis. I wonder if, for the record, that you might explain those two issues, credit balances and smoothing, and comment on what needs to be done with the rule.

Mr. BELT. I would be delighted to do so. The smoothing issue, as I just mentioned, is how, for ERISA funding purposes, when companies have to calculate how much they have to put into their pension plan under the funding rules, they get to calculate that based on a measure called current liability that really bears really very little relationship to economic reality. And it is comprised of both smooth assets and smooth liabilities, which, again, means that you are looking at the value of assets averaged over a period of several years.

So companies are still taking into account the fact that asset prices used to be higher than they are now, that interest rates used to be higher than they are now. That does not allow for an accurate picture of the financial status of the pension plan at this point in time.

The other issue I mentioned is credit balances, which is a mechanism, a separate account that companies are allowed to use to avoid making cash contributions. That is, if there is value in the credit balance account, they can offset that against actual required cash contributions. The interesting quirk about that is that credit balance account is a result of a variety of things, but if they paid more than minimum contributions in the year past and they get to assume that interest is assumed on those assets.

But even if, in the interim, the asset values have fallen substantially, so the plan has become more underfunded, that credit balance still remains. And that is exactly what happened when I mentioned United Airlines pilots' plan, which is a matter of public record, which was substantially underfunded in the year 2000 and has become substantially more underfunded. But because of the availability of credit balances, the company did not have to, legally under the ERISA rules, put any cash in in 2000, 2001, 2002, 2003, 2004, and will not have any monies owed until actually the end of 2005.

Mr. COSTELLO. I think, Ms. Hecker, on one of your charts—Mr. Belt, I want you to address this, if you would—one of the charts you indicated in the years when the legacy airlines were making money, they were not making contributions to their pension funds. My understanding is that the current law prohibits prepayments for future years into the pension funds. Is that correct?

Mr. BELT. Not quite correct, Mr. Costello. There are limits under current law on the amount of tax-deductible contributions that can be made into a pension plan, the maximum contribution limit. One of the Administration's proposals is in fact to raise the maximum contribution level to provide additional incentive for companies in good times to put additional monies in the pension plan to buffer against bad times.

While we do support that additional flexibility, the fact of the matter is in the vast majority of instances companies have not bumped up against the maximum contribution limit. And that varies from company to company, obviously, but for the system as a whole that is true. And the airlines themselves are very differently postured in that way. Some airlines and some of the legacy air carriers did, for a period of years, bump up against the maximum contribution limit.

If you look at a different set of years, either before or after that, that wasn't true, but in some years they did bump up against the maximum contribution limit. There were other legacy carriers that over the same period of time never hit the maximum contribution limit in any year for any plan.

Mr. COSTELLO. Last question—I have run out of time, but hopefully we will have an opportunity to come back—for you, Ms. Hecker. You indicate in your testimony that the very presence of the PBGC insurance may have created a moral hazard for incentives to not properly fund pensions, and I wonder if you might elaborate on that.

Ms. HECKER. The very availability of this program, in our view, changes the incentives. There are indications, we don't have smoking guns. You have an example of the machinists having their pensions increased at United 45 percent six months before United declared bankruptcy. Now, it is true there is a phase-in and, in fact, those didn't have the effect that on their face they might have. There appear to be indications that when you know you can have certain obligations taken over by the government that there is less funding and less commitment to those obligations.

Mr. COSTELLO. And, hence, that is why you made reference to going through cash, burning money?

Ms. HECKER. Well, the reference to burning money is that they are losing money through operations. They are not generating net cash. So that cash balance is in fact part of it is coming from increased borrowing and leveraging, and there is an end to that.

Mr. COSTELLO. And there are those who would suggest that some of the legacy airlines are attempting to get rid of whatever cash they have in order to file under Chapter 11. And you indicate in your testimony there is no clear evidence that the airlines use Chapter 11 bankruptcy protection that has harmed the industry. I wonder if you might comment on that.

Ms. HECKER. Well, the two presumptions are that they create extra capacity in the industry, and the second one is that they lead by lowering prices because they have been able to lower their costs. We found no evidence of either. We did the analysis I showed you about the capacity, how none of the bankruptcies or liquidations actually led to a turn-down in capacity, that in fact it kept going up. It was only recessions that led to reductions in capacity.

Basically, as soon as an airline fails, somebody else picks up the capacity. We did specific studies of specific markets that is in my written statement. In addition, there is a modest amount of academic research, and those are cited, and they found the opposite, that these carriers in bankruptcies are not price leaders, that the price leadership is coming from the low-cost carriers.

So we just didn't find the evidence that in fact bankruptcy was ever a first choice. We consistently heard that it is a last resort, that you lose control and that it is not a preferred model, and that was our observation.

Mr. COSTELLO. Mr. Chairman, thank you.

Mr. KENNEDY. [Presiding] Mr. Porter?

Mr. PORTER. Yes. Thank you, Mr. Chairman. And I thank the panel for being here.

I have really a three-part question for you, Mr. Belt, all related. It has to do with your authority and any possible changes. What existing authority do you have to deal with the situations that we have been discussing today? Is it possible to make changes to your authority to accomplish a similar end? And, if so, what specific authority would you need? So it is what authority do you have to deal with it today; what changes should we make, if necessary; and what authority would you need?

Mr. BELT. I am not sure quite where to start on that issue, it is a fairly broad one. I think it is fair to say that the PBGC has a rather limited set of tools and authorities to respond to marketplace changes and risks posed to the pension insurance plan compared, for example, to a private sector insurer, but some of that is statutorily based.

For example, if a company does not pay premiums or does not make contributions to its pension plan, I can't decline or deny insurance to them, I still have to cover them. Our tool sets are also fairly limited relative to other Federal insurers like the Federal Deposit Insurance Corporation that has a much broader range of capabilities to protect the interest of the banking system than does the Pension Benefit Guaranty corporation.

One of the areas where we encounter great difficulty is one alluded to by Mr. Ehlers, which is bankruptcy. There is no question, an inherent tension between ERISA (the Employee Retirement Income Security Act) and the Bankruptcy Code. And where a lot of these issues actually come to a head is when companies are in Chapter 11. They serve very different purposes. The interest of the Bankruptcy Code and the judge are to have the company emerge successfully from Chapter 11. And to the extent that they are weighing equities, the stakeholders that they are looking at are the creditors in the company, and first among equals there are the secured creditors, and we are a general unsecured creditor.

There are other issues that arise in the bankruptcy context as well. The bankruptcy judges really simply are not attuned, by dint of their responsibilities, to the interest of participants, workers and retirees, to the premium payers whom we are supposed to be responsible for, as well as the taxpayers. We are supposed to be self-financing.

One of the proposed changes in the Administration's proposal is to give PBGC the authority to be able to enforce liens in bankruptcy. And the situation that arose was one that, again, using United as an illustrative example, last summer the company was in Chapter 11, in bankruptcy, and they failed to make a $74 million payment that was required by law under ERISA. Now, if they weren't in Chapter 11, if they weren't covered by the Bankruptcy Code, PBGC would be able to step in, the lien would arise by the operation of law, and we would be able to enforce that lien and have a security interest against the company.

But under the Bankruptcy Code there are automatic stay provisions that kick in. And the lien arose, but we weren't able to do anything about that. It didn't give rise to a security interest, we stayed as a general unsecured creditor. So there was no practical consequence whatsoever to United skipping that pension payment that was required by Federal law under ERISA. That is another example of something that we think would be very useful on a go-forward basis.

Mr. PORTER. Mr. Chairman, to follow up.

So to have that specific authority to follow up in those cases, that is some of the authority you think you should have or do you have?

Mr. BELT. No, we do not have that authority in the bankruptcy context, and that is part of the Administration's proposal. As I understand it, it is not in the bill that is being marked up in the House Education and Workforce Committee.

Mr. PORTER. Now, are there some tools available to you that you currently have to deal with this situation?

Mr. BELT. The principal tool is to actually step in to terminate a pension plan. And it is an action that PBGC has taken and will take in extraordinary circumstances, when such action is necessary to protect the interest of the pension insurance program as a whole, and balancing the interests of all the stakeholders.

But it is obviously not a desirable option, and it is one that we do not take lightly because there are adverse consequences. If we step in to terminate an underfunded pension plan, then the workers and retirees lose; they stop accruing benefits, they may lose benefits because of the guaranty limitations. We take the liability on our books. Somebody has to pay for that, that is the other premium payers in the system or ultimately, potentially, the taxpayer.

But in some cases that action is necessary when the company is no longer supporting the pension plan. They are not putting any additional assets in the pension plan, they either don't have the ability to do so or are not willing to do so, and the liabilities continue to accrue each and every day that that plan is still out there.

So to protect the interests of the stakeholders as a whole, all the people that we are responsible for cutting benefit checks to in plans we have already taken over, as well as the premium payers and the taxpayers, we sometimes have to step in to terminate that pension plan, notwithstanding the fact that it has adverse consequences for the participants in that particular plan.

Mr. PORTER. And I know we were called away to a vote, but if I understand correctly, you stated that even in the good years United chose not to fund as they could have, from 2000 through today, correct?

Mr. BELT. That is true not only with respect to United, but the vast majority of companies that sponsor defined benefit plans could have put more money into their pension plans, above the minimum amounts that were required by law, and many of those companies, as we have talked about, took advantage of other loopholes in the funding rules—the way you calculate assets and liabilities and credit balances—to not put money in when they could have done so.

Mr. PORTER. I represent the community of Las Vegas and, of course, we feel a partnership between the airlines and their employees and, of course, our customers that are traveling on the airline industry, and I appreciate your comments today, and I know you are having to make some pretty decisions. But we appreciate what you are doing. Thank you.

Mr. KENNEDY. The gentleman's time has expired.

Ms. Tauscher?

Ms. TAUSCHER. Thank you, Mr. Chairman.

I don't think we have to look farther than this room to figure out who is responsible, at least in part, for the mess that we are in right now. When I was a small child, I spent 14 years on Wall Street, and prior to September 11th I think many of us were deeply concerned about what we considered to be unsustainable business models for especially the legacy carriers. And then after September 11th we created an airline stabilization board, who clearly have never scrubbed the books and still do not understand the ongoing practices of many of these airlines, and they certainly have not alerted Congress.

If American workers are working hard and playing by the rules, they believe they have laws that protect them. And we have been asleep at the switch. As much as there was an intelligence failure in many different ways on September 11, this is an example of a major, major oversight failure by Congress. We have got to get this right.

Mr. Belt, your testimony should say to anybody with a defined benefit plan to run not walk immediately to their executive row and demand that their CEO show them the books of their pension plan. This is not just about our friends in airlines industry. As you have testified, Ms. Hecker, there is a panoply of industries that are egregiously not only underfunding and not doing the right thing, but we have got laws that are incongruent with responsibilities, we have got Enron accounting. You have to have a Ph.D in accounting to understand ERISA to begin with and then you have got complicit with that a number of other basic gap rules that allow companies to slip the noose day in and day out.

And what we now find when we have lifted up this rock is a complete nightmare. What disturbs me is that we still apparently are not getting it right. We should be having hearings day in and day out, Mr. Belt, to provide you with what you need so that we at least have a sense from today going forward that we have a PBGC that is at least breathing.

Mr. BELT. Please do not invite me every day. I have done this eight times in the last two months.

[Laughter.]

Ms. Tauscher. Well, you are very popular, and we know why. I do not really have any questions for you because I am right now trying to control my blood pressure. I am stunned that knowing what we knew after September 11, many of us believed that we had to have a much more activist airline stabilization board. I have been a constant critic over what they have done on these bankruptcies, in and out, not supporting them, forcing people to write business plans day in and day out while they are hanging by a thread.

Now what we find is that they did not even scrub the books enough to understand that it was not just the business models and trying to fix a few weeks of having a ground stop. There was an overwhelming lack of responsibility in many different quarters, not only bad business models and things that were not going to work in the long term, but that there was fundamental funny business going on.

Mr. Belt, at the minimum, these plans need to mark to market, no more smoothing, that is crazy. At a minimum, everyone that is a beneficiary and paying into one of these plans needs to be notified by mail immediately once the company decides not to live up to their obligations. That I think will send a shock wave around the country in every boardroom.

What I do not understand is how one of the big carriers who was effectively owned by their employees, whoever those board people were representing the pilots and everybody else that helped that airline stay above water for a few hours should basically be taken to the woodshed because they were not doing their fiduciary responsibility to understand that one hand was not doing what the other hand thought they were doing and that they were complicit in allowing this to go on.

So there is a lot of blame to go around I believe in this room. We need to take responsibility and we need to act now, Mr. Chairman, to get this right. This is absolutely heinous. Americans need a Congress that is going to make sure that the laws are as responsible to them as they are responsible to themselves and their families and to this country to work hard and play by the rules. When they play by the rules, we have to have laws that protect them, and we obviously do not. Thank you, Mr. Chairman.

Mr. KENNEDY. The gentlewoman yields back her time. Mr. Ehlers.

Mr. EHLERS. Thank you, Mr. Chairman. First a specific question before I ask a more general one. Ms. Hecker, in your report you have this fascinating chart: Legacy airlines could have contributed more to plans during profitable years. My first question, did any of the airlines contribute less than they were legally required to contribute?

Ms. HECKER. I do not believe so. It all goes to these smoothing and these credit rules, so that even though most of them were not contributing anything for many of those years, it was in full compliance with the rules. I am sure Mr. Belt can tell you better.

Mr. EHLERS. That is what I thought. I just wanted to check because I wanted to make sure you are not saying that they were irresponsible or violating the law. And it is clear they did not violate the law. Now, I noticed you just quoted the source for this as PBGC and DOT. Did you check with any of the airlines to verify the figures that you had on this to make sure that they were accurate?

Ms. HECKER. No, we did not.

Mr. EHLERS. Okay. And as far as individual airlines are concerned, did any of them make more than the minimum amount of payments during that time period? Did you check that at all to see which ones contributed more and which ones did not?

Ms. HECKER. We have some information but it is actually summarizing a study that Mr. Belt's staff did.

Mr. EHLERS. All right. Maybe Mr. Belt can answer. I have the understanding that Delta paid more than the minimum and I believe Northwest did too. Is that correct or incorrect?

Mr. BELT. I do not have the figures, but we can certainly get them to you as to whether they paid more than a minimum. There are certainly some of the legacy carriers that in some years with respect to some plans bumped up against the maximum contribution limit. That is, they could not have put in any more on a tax deductible basis.

It is also true, for example, with one of the legacy carriers, that, as far as we could ascertain, over a several year period with respect to each of their plans they never bumped up against the maximum contribution limit. There were some companies, for example, you mentioned one of them, that if you looked from the period 1997 to 2002, there were years when they could have put in as much as $3 billion more than they did in an individual year and not bumped up against the maximum contribution limit.

Mr. EHLERS. All right. If you could send me that information, I would appreciate it. It would be interesting to see that.

My point is I just want the facts. I do not want to cast aspersions where they should not be cast, but I am willing to cast them where they should be cast. But I want to have the facts to make sure it is clear who did what and not just lump them together.

The second question is a more general one, and is again addressed to both of you. During my opening statement I made some comment about the need to rewrite bankruptcy laws at the same time we rewrite the pension laws. I would appreciate any comments that either of you could offer on that, in particular as to which you think we should be looking at changing in the bankruptcy laws to make it match better with the PBGC requirements and the new pension bills that are being offered just to make sure they mesh appropriately and we do not find ourselves in the same situation ten years from now because we reformed one and not the other.

Mr. BELT. If I can take that first. As I just discussed with Mr. Porter, one of the elements in the Administration's reform proposal is to give the PBGC the ability to enforce a lien in bankruptcy for missed contributions. We think that is critically important so as to avoid the situation that arose with United last year when they failed to make a contribution that was required by Federal law, the Employment Retirement Income Security Act, but the Bankruptcy Code, the automatic stay provisions, ended up trumping that and there was no practical consequence to that. My understanding is that is not in the bill that is being marked up in the House Education and Workforce Committee, it was marked up at Subcommittee level today. The Administration does believe that is an important element of reform.

There are a host of little but frustrating and vexing issues that tend to crop up all the time with respect to PBGC and pose an ongoing litigation risk because of the tension between ERISA and the Bankruptcy Code because they serve very different purposes. One of which is, for example, under ERISA, we are supposed to calculate the value of a claim in a particular way using a certain discount rate methodology. But that is not written into the Bankruptcy Code. So bankruptcy judges, depending on what jurisdiction they are in, will use very different ways for calculating liabilities.

In a recent case where we lost, the company was able to argue that the prudent investor rule, and assuming that the participants wanted actually to invest in the debt securities of that company, what they would have to be compensated to do that, and therefore that is the appropriate discount rate to use. The consequence was a 9.7 percent discount rate used in that instance which valued our liability from 100 cents on the dollar to almost nothing. But that is an issue that is out there that is a litigation risk and depends on what jurisdiction you are in and it is a disconnect between what is in ERISA and what bankruptcy judges look at.

Another example arose in the United Airlines context particularly with respect to the flight attendants. ERISA says that the determination of whether a plan can be off-loaded onto the federal pension insurance program in bankruptcy using the distress termination process has to be done on a plan-by-plan basis. At least ERISA speaks of a plan in the singular. But we just recently had in a Kaiser Aluminum case a court decision that said do not mind that, the company is able to look at the plans in the aggregate, can they afford all of their plans in the aggregate, they do not have to look at it on a plan-by-plan basis.

So there are a host of things like that that tend to arise because of the disconnect between ERISA and the Bankruptcy Code. And the bottom line is if bankruptcy judges do not find it in the Code, then they tend to discount it even if you find it elsewhere in federal law.

Mr. EHLERS. So you would agree then with my comment that we should be working on reforming bankruptcy law as well as the pension law?

Mr. BELT. There are certainly some changes that could be made. But there are obviously trade-offs in a balancing of interests that could better protect the interests of the pension insurance program relative to current law.

Mr. EHLERS. And if you would be kind enough to put that in writing to me and the Committee also, that would be helpful.

Ms. BOVJBERG. Mr. Ehlers, may I jump in for a moment. I know that the Government Accountability Office is on the record as saying that we should consider better aligning the bankruptcy law and ERISA for these purposes, this is from a pension perspective, where I come from, but that we also think that if you did that you could take some measures that would better protect the Government's insurance program and the participants it insures. I know that David Walker, the Comptroller General, has offered to work with Education and Workforce on some of these issues, and we would be happy to do that.

Mr. EHLERS. And I would appreciate, you said it is on the record, if you could send me that as well, I would appreciate that.

Mr. KENNEDY. The gentleman's time has expired.

Mr. DeFazio.

Mr. DEFAZIO. Ms. Hecker, just on the legacy airlines and the cost chart, I would just like to refer back to that for a minute because your prognostication here or the conclusions one would draw from some of your materials is a very grim future for the industry, and legacy carriers in particular.

I assume the fuel and oil advantage, I guess part of it is they have cash to buy hedges or futures but also some of those hedges and futures are going to be less advantageous given the current run-up in prices than they were in the last year or two for profits. So that one may narrow.

Labor, I would assume that even the non-legacy carriers have systems of seniority and/or graduated pay scales so that the longer you are there the more you earn, and I would assume that perhaps some of that labor advantage is going to go away plus a lot of the give-backs that we have seen.

Then when I look at pensions, I met recently with a legacy carrier with some other Members and they said that United is doing away with defined benefit pensions but they are going to defined contributions, and basically, this legacy carrier we talked to, their defined benefit is only one-half of one percent difference of payroll as opposed to the defined contribution, but theirs was not in as bad shape as United and then I do not know about others. Is there not some probability that 2.7 cents is going to narrow because of events?

Ms. HECKER. Well, we have not seen it. The fuel difference actually has consistently had the legacy carriers having higher unit fuel costs. They have older planes, they are less fuel efficient planes, and they do not have the money to get new planes. On labor, low-cost carriers tend to have often a younger workforce, just the demographics of the workforce, they have far more flexibility in the rules, and so there is substantially greater labor productivity.

I do not think that is naturally converging. And the pension issue, the low cost carriers from the get-go went with defined contribution. So I am not sure that our analysis would support that they are converging.

Mr. DEFAZIO. Okay. So then absent that, you are basically predicting the demise of one or more of the legacy carriers until such a time as there is some kind of return to so-called pricing power and fares can go up enough and capacity is strained enough even with the non-legacy carriers that people could raise prices and they might stop hemorrhaging?

Ms. HECKER. We do agree that it is very likely that some of the legacy carriers will enter bankruptcy and terminate.

Mr. DEFAZIO. And what does this say about the future of a system of universal air transport for the United States of America? And what does it say about whether or not we should revisit the deregulation and consider whether or not, at least in certain markets, the only way we are going to be able to provide air service is with some sort of limited form of regulation?

Ms. HECKER. There is absolutely a role for network carriers. The model that creates such efficiency for low cost carries, as we know, is based largely on the point-to-point service. Network carriers provide broader coverage, they provide a distinct service, and they provide online connectivity around the world, and they are the international carriers. We do not have low cost carriers for the most part providing any international service. So there is a distinct service that legacy airlines are providing.

The problem is that they are not getting the premium that is covering the differential costs they have. So the restructuring that is still needed is not so much to converge, but to get the cost differentials to a level where they can make it up in yields.

Mr. DEFAZIO. But what you are saying is the market, in a deregulated market, in a cut-throat market, does not value connectivity or a universal air transport system. It does not lead to that. It leads to the most efficient, cheapest way of providing service, which might well be something that says everybody in the Northwest will drive to Seattle to get on a plane, everybody in California will drive to Los Angeles or San Francisco to get on a plane because that could be really efficient for the carriers because they just provide point-to-point from those areas, and so no more Fresno, no more Sacramento, no more Eugene, no more Tacoma, sorry, not Tacoma, that is Seattle, but no more whatever.

Ms. HECKER. But it is not some objective model. These are consumers making decisions and that is really that so-called Southwest effect where people are choosing, preferring, even if they are near a small or community airport, they prefer to drive three, four, five hours for that lower cost.

Mr. DEFAZIO. But not business travelers. So the business travelers are all going to go to microjets? How are we going to continue to have a universal system that serves the business community and the leisure traveler which can involve a four or five hour trip to save a hundred bucks, although with gas prices, who knows, it is probably going to have a bigger differential to save these days.

Ms. HECKER. I do not think I have the crystal ball of how the market and the various segments of this market will evolve. But I do think we have seen tremendous innovation and tremendous benefits to consumers, to communities, and to growth.

Mr. DEFAZIO. Not to communities who lose their jet service or regular business service. It is kind of an economic disadvantage. I mean, sure, if you have got a hub, take advantage of it. If you have got some competing airlines, great. But if you happen to be one of these second tier airports, well, too bad, you used to have air service, now, if you want to attract a company just tell them they have either got to have their own jets or their executives are going to drive for four hours to the nearest airport. It is not going to work for most of America.

Mr. KENNEDY. I would say the gentleman's time has expired.

Mr. Westmoreland.

Mr. WESTMORELAND. Thank you, Mr. Chairman. Ms. Hecker, let me get this straight in my mind. If an airline goes bankrupt, files Chapter 11, do they get to jettison their pensions?

Ms. HECKER. With the approval of the bankruptcy court.

Mr. WESTMORELAND. So it really depends on the bankruptcy court. And is that determination made about how much of that pension they can jettison or how much the Federal Government is going to be responsible for?

Mr. BELT. If I might answer that. The discretion is ultimately in the bankruptcy judge's hands. The standard is whether the company would be able to successfully emerge from Chapter 11 with, and the issue we just talked about, one or more of its plans in tact. That is the process that exists under ERISA and the Bankruptcy Code right now.

Mr. WESTMORELAND. Okay. Now, have any of them emerged out of bankruptcy and taken up the pension plans or a part of the pension plans?

Mr. BELT. My apologies, I did not really finish the answer to your question. The process that courts use is actually an all or none proposition. It is a binary proposition right now. There is no mechanism available under current law for the bankruptcy judge saying, well, you can afford 50 percent of your pension obligation and you have to maintain the other 50 percent. It is you terminate the pension plans and they turn them over to PBGC, or you maintain them. So that kind of slicing the baby, as it were, is an option that is available under current law.

Mr. WESTMORELAND. So if I am hearing you correctly, if they file Chapter 11, get rid of their pension plans, come back out of Chapter 11, they have no obligation for those pension plans?

Mr. BELT. That is correct. That is the general construct of bankruptcy law, which is the fresh start. Now, we talked a moment ago about the inherent tension between ERISA and the Bankruptcy Code. There is a provision in ERISA under current law which gives the PBGC the authority to restore a pension plan in changed circumstances. We have done that in one instance where a company was still in bankruptcy.

The interesting question that is presented is, let us say an air carrier or somebody else emerges and becomes healthy several years down the road, can the PBGC step in and say now that you can afford this you have to have your plan back, you are supposed to restore it to the pre-termination condition. And it is not clear that can be done. And it is also not clear that that authority sets well with the basic construct of the bankruptcy code, which again, you expunge your debts and you get a fresh start.

Mr. WESTMORELAND. So the basic answer is that if they file Chapter 11 they can jettison their pension plan and not be responsible. And whether they are eventually responsible or not, it is kind of cloudy or unclear as to what maybe our laws might change.

Mr. BELT. The one thing I would note in that regard, that may be where you end up, that we would vigorously make the case to the bankruptcy court, if the facts and circumstances suggested this was the case, that if the pension plans were affordable or the company could obtain exist financing and still maintain those pension plans, looking at relevant cash flow and credit metrics, and we will hire financial advisors and investment banks to help us make that case, as will the company. But we will vigorously argue in appropriate circumstances in the bankruptcy court that the company does not meet the distress termination standards; that is, they should maintain one or more of their pension plans. Ultimately, we do not make that decision, however, we can only make our best case to the bankruptcy judge and we may need to make an evaluation as to how the judge is likely to rule at the end of the day.

Mr. WESTMORELAND. Earlier when I think the Chairman asked you a question about extending the payments five, seven, twenty-five years out, you made the comment that we need to strengthen these and not weaken the amount and that this could cause bad behavior with companies. What worse behavior can you get somebody to do than file bankruptcy, file Chapter 11, jettison their pension program, and then go back in business?

I am missing something. I know I am a little slow, but to me that is rewarding bad behavior and that has been kind of a line that we have fallen into. So rather than really honoring somebody who wants to do their best to keep their pension going and to participate and to keep money in that fund, whether they are doing it in two years or four years or twenty years, I think that is something good.

I think that is somebody trying to do good, rather than doing, as Ms. Hecker talked about, when 60 days or whatever it was before one of the airlines filed bankruptcy they increased the benefits 45 percent or whatever. To me, that is rewarding bad behavior. I think when somebody is trying to work out their problems and trying to do the right thing, we need to be of assistance to them and not really make a comment that we are trying to reward bad behavior. You can answer that if you want to. But if not, Mr. Chairman, that is my last comment.

Mr. KENNEDY. The gentleman's time has expired. Mr. Pascrell.

Mr. BELT. Mr. Chairman, if I may.

Mr. KENNEDY. You may answer. I am sorry.

Mr. BELT. Thank you. I think a couple of points to note in that regard. There is no question, I want to wholeheartedly agree with you, that current law leads to bad outcomes. We have seen that manifested in what is happening to the airlines industry, what happened to the steel industry, and perhaps that could happen in other industry sectors.

And when companies enter bankruptcy, off-load their pension plans, and then are able to emerge successfully, everybody loses—workers and retirees lose; other companies that have acted responsibly lose, they lose because they may have to pay higher premiums to cover those costs, they may lose because they are competing against a company that now has lower labor costs than they do; the system loses because the Government is subsidizing the ongoing labor costs of a company for as long as that company is around; and ultimately the taxpayer may be at risk. So there is no question there needs to be a better way.

There is a better way. The better way is to make sure that companies fully fund their pension plans on an ongoing basis. There is nothing from a governmental perspective in my view that we can or should do to change the business cycle; companies' business models are going to come and go, companies are going to occasionally fail. I am not sure we can or should do something to change that.

But what we can and should do something to change is the fact that if the company sponsors a defined benefit plan, making sure there are sufficient assets to cover the promises they have made so all the other stakeholders do not lose if that company does go into bankruptcy or it does liquidate. I think that is critically important.

I am also not trying to suggest that we are rewarding bad behavior. The point I was trying to make is there is a lot of moral hazard in the pension insurance system right now. You have socialization of private risk-taking, the public sector taking over private risk-taking. That is a risk in and of itself.

The concern is what message does it send to everybody else in the system that perhaps is 80 percent funded, 85 percent funded, that now has to operate under a tighter set of funding rules. In the Administration's proposal and in the bill marked up in the House Education and the Workforce Committee, they have seven years to make that up. Well, that is going to be an onerous call on cash for some of them. But that is because they are fairly underfunded right now.

If we give a lot longer period of time to certain companies, does that suggest every company that is similarly situated may engage in behavior to not responsibly fund their pension plans so as to get the ability to stretch out their pension obligations over a long period of time so they can devote those current resources, which if I were in their hat I would like to do, to other uses, building widgets and making profits for their shareholders. And I think that is the trade-off we have to work through.

Mr. KENNEDY. I thank you. Mr. Pascrell.

Mr. PASCRELL. I would like to start with where you just ended, Mr. Belt. And I want to refer to my friend from Georgia, I think you hit the nail right on the head. I think you were clear in break-ing down to very elemental parts what we are facing. Trade-offs. You cannot trade-off somebody. You cannot trade off the fact that we are talking here about a defined benefit that is not guaranteed. Figure that one out. And you wonder why we have lost—well maybe you do not wonder why—we have lost our credibility besides we have lost our way.

In 1974, if I interpret what you are saying, Ms. Hecker, correctly, ERISA set forth a pension plan and rules were established at that point, right, in 1974, to define how much a company had to put away to meet its pension obligations—1974.

So when I hear, in response to my good friend from Michigan that he is not so sure whether laws were broken, most of the problems we face down here are irresponsibility within the law. There is a law, Congress establishes that law with the President, and then within that law people are finding all kinds of way to get out of their original obligations. Now, we want to protect and we want the airline industry to grow. And that industry is really an odd bird if you look back over the past 30 years.

When you look at pensions, benefits, cost of oil, and working conditions, all of them have been blamed for every downturn we have ever had in the airline industry. In fact, you can go back to the early 1980s when the President fired all the air traffic controllers. The three worst years in the airline industry occurred after that. It obviously was not the air traffic controllers that were causing all the problems in the airline industry, was it, Ms. Hecker?

But when I look at this, I want to ask you, if I hear you correctly about these defined benefits that are not being guaranteed within the law and now we have proposals from the Administration to change the pension rules, some of them, I want to ask you a question. What do you think are the two most flawed rules dealing with the very pensions we are talking about today? What do you think are the two most flawed rules, and what would you recommend we do about those two rules since the system is not working?

Ms. HECKER. I will ask Ms. Bovjberg who has done this work to reply.

Mr. PASCRELL. Sure.

Ms. BOVJBERG. In answering your question, Mr. Pascrell, I want to talk a little bit about why the rules are a certain way.

Mr. PASCRELL. As long as you answer the question, sure.

Ms. BOVJBERG. I will be brief. They are designed for going concerns. They are designed for the long-run. They are designed to give sponsors flexibility to adjust contributions in response to a changing environment, to have a certain period in which to do that. And the presumption is that they will do that and 30 years down the road they will have the money to pay their pensioners. And if something unforeseen should occur, the PBGC would be there because they have paid their premiums to the PBGC.

Mr. PASCRELL. The pension is for the long run, too, besides the rule.

Ms. BOVJBERG. That is right. That is right. You want to protect your participants.

Mr. PASCRELL. So what are the two rules that are most flawed?

Ms. BOVJBERG. Credit balances, the use of credit balances. What we have seen is that this just does not work. When you have a run up in the stock market, you have assets that are skewed to stocks so there is a lot of risk in some of these plans either run up in the market and then the sudden fall off. The credit balances just do not work in that situation. That was not something foreseen in previous Congresses in writing these rules, and it is something that we clearly need to fix. That would be my number one.

Mr. PASCRELL. And what is the second one?

Ms. BOVJBERG. I think it is really a toss-up in terms of whether you deal with transparency and disclosure. It is very difficult for the PBGC and the Department of Labor to regulate pensions when it is difficult for them to get timely information and accurate measurement.

Mr. PASCRELL. Who do you get that information from?

Ms. BOVJBERG. From the sponsors.

Mr. PASCRELL. And why are they reluctant or why are they so slow to get the information to you?

Ms. BOVJBERG. Because we say that under the statute they have over 250 days to report their assets and liabilities on the Form 5500 to the Department of Labor. Now PBGC, as Mr. Belt mentioned earlier, can get better information more quickly through the 40-10 process. That is not even available to us at GAO. It is not available because it is considered proprietary information by law. We need better information, we need more accurate measurement, and we need it more quickly.

Mr. PASCRELL. One final question if I may, Mr. Chairman. Do you think that these pensions should be guaranteed in the same way that the Federal Government guarantees the dollars I put into a bank account up to a certain amount of money? Do you think that is the best way or it is a way, a good way to ensure credibility where there is much credibility lacking right now?

Ms. BOVJBERG. I am much less familiar with the banking system and the FDIC than with pensions and PBGC. But I do think that there is a range of approaches that the Federal Government has used with insurance. And the pension insurance program is not a real insurance program the way we operate it. I do think that we should look at that. Premiums really do not have very much to do with the risk that a company will go out of business and leave an underfunded plan, for example.

Mr. PASCRELL. Thank you very much. Thank you, Mr. Chairman.

Mr. KUHL. [Presiding] The gentleman's time has expired.

The Chair would recognize Mr. Costello.

Mr. COSTELLO. Let me just quickly follow up with two quick questions and then I will yield the balance of my time to Mr. DeFazio. To follow up on the gentleman's question, when you talk about the 250 days that they have to report, we are talking about legacy airlines that use different accounting practices and, depending on the interest rates they are using, it can be very deceiving if an airline wanted, for whatever purposes they had, to either hide or disguise or whatever their underfunding of their pension fund. Is that not true? There is not a uniform standard that must be followed.

Ms. BOVJBERG. There is a standard but there is a lot of flexibility within that standard.

Mr. COSTELLO. And is the flexibility in the interest rate?

Ms. BOVJBERG. Oh, yes. There is a corridor of interest rates that you can use. One thing I do want to say. Our funding rules report where we looked at the 100 largest plans over time and their funding situation and what they contributed suggested that when companies begin to have financial trouble themselves is when you see people putting in the most minimal contributions and relying entirely on credit balances and gradually becoming underfunded.

Mr. COSTELLO. So the issue of the interest corridors is an issue that you would recommend has to be addressed as well?

Ms. BOVJBERG. Yes. And it must be addressed because the same law that provided the DRC clause for the airlines that expires at the end of the year also temporarily altered the interest rate for those calculations.

Mr. COSTELLO. Thank you.

Mr. Belt, a final question, and then whatever time I have I will yield to Mr. DeFazio. I see the Chairman is back and maybe he will yield to him a full five minutes after I am finished. Mr. Belt, on the issue of the legacy airlines and the point that Mr. DeFazio made earlier about what we can expect in the future with those airlines that have not gone into bankruptcy, as a practical matter, if you are the CEO of airline A and I am the CEO of airline B, airline A files under Chapter 11, they are allowed to take their employees and their pension obligations and put them in the PBGC, and I am airline B, you certainly have a competitive advantage over me because I am still funding my defined pension plan, you no longer have the obligation to do that, you can set up a 401(k) or whatever you choose to do.

So as a practical matter, when we take an airline, if it is United or whoever it may be, U.S. Air, or any other airline, and they go to the PBGC because the bankruptcy court allowed them to do so and put their pension obligations on the PBGC, it presents major problems to the remaining airlines who have defined plans. Is that not correct?

Mr. BELT. It certainly does present a competitive pressure issue. Although as Ms. Hecker noted in her testimony, it is one of many cost elements or cost pressures facing a company.

Mr. COSTELLO. Sure, 17 percent, one-sixth. But all of these legacy airlines are very, very close to the margin. So if you offer them relief in the area of 16 or 17 percent of their revenue or somewhere in that area, it can make a difference.

Mr. BELT. That may be the case. I might suggest, Congressman, that the situation is not a homogenous one; that is, the financial status of the pension plan as well as the plan sponsor is different for each of the legacy carriers. Certainly, I am not an expert in this, as Ms. Hecker is, but if you read industry analysts, Wall Street analysts and others, they will suggest that the condition and the issues that are facing Delta versus Northwest versus American versus Continental both with respect to their overall business conditions, the degree of leverage in the company, their costs, their revenues, as well as their pension obligations are distinct from one another.

Mr. COSTELLO. When we talk about pension obligations and we use the one-sixth or approximately 17 percent, whatever it may be, are we talking about health care benefits as well? We are not, are we? So if a legacy airline files bankruptcy and this 17 percent of their overhead, so to speak, they are able to shed that by putting it into the PBGC, they also are getting rid of health care costs as well that my CEO of airline B has to continue with the defined benefit plan plus the health care for my retirees.

So that adds an additional element onto the cost and the competitive advantage of the airline that goes into Chapter 11 and dumps their obligations on the PBGC versus airline B who is trying to continue under the defined plan and to take care of their retirees with both pensions and health care. Is that not correct?

Mr. BELT. Of course, we do not insure health care benefits. That is something that would be covered by the collective bargaining agreement in a unionized context, and then it is ultimately a matter of whether the bankruptcy judge allows them to abrogate the collective bargaining agreement. They usually try to force management and the unions to sit down and negotiate out solutions or resolution of issues and you often see that happen at the last minute before the 1113 process begins.

Mr. COSTELLO. Let us take an example of U.S. Air. They went through the bankruptcy process. No longer do they have obligations to their defined benefit plan. Do they have obligations to their retired employees for health care costs? The point that I am trying to make is when we say that we are only talking about 16 percent of the operating cost or the fixed obligations, you have got a health care component here as well that is a substantial obligation that they are able to shift and get away from as well.

Mr. BELT. I simply do not know, perhaps GAO does, as to whether or not part of the agreements they have reached with their various unions whether they are paying health care benefits. I think clearly to have a workforce, to have people be willing to come to work, you have to provide at least some level of wages, you have to provide some level of benefits whether it is a DB or a DC, and probably some level of health care benefits. But that is something that is ultimately negotiated between the management and the workforce, and I simply do not know in the U.S. Airways context what level of health care coverage they provide.

Ms. HECKER. Perhaps we can supply something for the record to clarify that.

Mr. COSTELLO. The only point I am trying to make is that the 17 percent or the one-sixth is misleading. There are other obligations that they are able to walk away from in the area of health care. Mr. Chairman, thank you.

Mr. MICA. [Presiding] Thank you. Mr. DeFazio.

Mr. DEFAZIO. Thank you, Mr. Chairman. To Mr. Belt, on the previous line of questioning about companies emerging from bankruptcy becoming subsequently healthy, or the fact that you adjusted a settlement with a company because of conditions in bankruptcy. As I understand it, you have got some sort of equity basis negotiated with United in order to sign off on accepting the obligations of United.

Could you have a contingency that would say should this company emerge in the future they would be required to restore something beyond your guarantees and/or, on the other side of the equation, that they would be required to replace some of your guarantees?

Mr. BELT. Theoretically, yes. I think the practical question, Congressman, would be whether to put such an agreement in place the company would enter into such an agreement, or if such an agreement was in place they would be able to obtain exit financing and be able to emerge from the Chapter 11 process. That is the thorny issue in all of these situations.

Mr. DEFAZIO. Right. So basically the employees are always going to get screwed. Because when you go for exit financing they will say, oh, wait a minute, we will pay for your planes, we will give you some money to buy fuel, we will give you some money for the CEO's golden parachute, but I am sorry, we are not going to give you any exit financing to meet your pension obligations for your employees. Is that not basically the way it is working?

Mr. BELT. That was an issue that actually arose before. Earlier on in the United process we actually objected to a provision of the debtor in possession financing agreement, this was going back last year, that could have been read to say, and this is what the company said was imposed upon them by the debtor in possession lenders, do not put any of the money we are giving to you into the pension plan. And the company used the word it would be "irrational" from our standpoint, and this was in the information brief filed by the company, to put money into the pension plan. And I guess from a pure business financing perspective, that is perhaps the case.

Mr. DEFAZIO. Right. So basically the employees and PBGC are going to be the losers in every one of these bankruptcies.

Mr. BELT. That is why I suggest that there are bad outcomes given the way the current law works.

Mr. DEFAZIO. But you do have that theoretical negotiating authority. Would that need to be strengthened? Could we put a requirement on you that you attempt to negotiate those kinds of provisions? Could we put some sort of requirement on a bankruptcy judge that those things be looked upon favorably in order to provide future Federal bailouts of PBGC?

Mr. BELT. Along the spectrum right now you kind of have the binary outcomes, it is either an all or none proposition. And it seems to me that there might be some way to look at some possible middle ground. I mean, certainly any other lender, GE or anybody else, is willing to have a conversation with the debtor about restructuring an obligation on certain kinds of terms.

But I think one would need to be careful about how much is mandated or imposed, whether you actually throw the baby out with the bath water because you may forestall the ability to ever emerge and obtain exit financing. Again, that is part of the consideration of what is the Bankruptcy Code intended to do, which is outside my bailiwick.

Mr. DEFAZIO. For average consumers now or at least some consumers, we have said you cannot discharge your debts, you are going to pay forever to the credit card companies. Companies get a different leeway here when it comes to their pensions I guess.

Just one other question, and I know this is a policy area. Do you have any numbers on what it would cost if the pilots did not take a hit because of the fact that they cannot work past age 60 and they have to take a mandatory hit in their guarantees? You are going to reduce your guarantee because they cannot work to age 65, which is the point at which you would give your maximum guarantee, and/or have you ever looked at say a flight attendant who has got 30 years, who is fully vested, who is 53 years old, now you are going to have to say you have got to work to 65.

Has there ever been any review, discussion, or numbers on the fact that this is kind of a bad system where you are saying to people who have 30 years and they are in a stressful and difficult job, well, you have got to work until you are 65, or someone who has to retire at age 60 that you have got to work to 65 or reduce your guarantee?

Mr. BELT. We have our chief policy actuary here, Dave Gustafson. I do not know if he thinks those numbers can actually be calculated, and I invite him to answer that, as to whether it could be calculated so we can provide information for the record.

Mr. DEFAZIO. Yes. There are some issues of equity there.

Mr. BELT. I would note again, everything is ultimately a set of trade-offs. Our losses are

Mr. DEFAZIO. Right. I understand. But it is people's lives. Is there anything available now?

Mr. GUSTAFSON. We have not done anything so far. But it is something that we could provide an estimate for.

Mr. MICA. Someone is going to have to repeat that into the record.

Mr. BELT. Our policy actuary just noted that is he believes information that could be provided for the record that we could estimate.

Mr. DEFAZIO. Okay. Thank you. Thank you, Mr. Chairman.

Mr. MICA. Thank you. Long-waiting Mr. Price, you are recognized.

Mr. PRICE. Thank you, Mr. Chairman, and I once again want to thank you and the Ranking Member and the entire Committee for the opportunity to be with you. I just want to ask a couple of quick questions of Mr. Belt. The pension funding act of 2004 provided temporary reduction in the deficit reduction contribution schedule for the airline industry. That expires at the end of this year, as was stated. That was meant to be temporary, was it not, to allow time for a permanent solution to be found? It was not meant to be a permanent solution, was it?

Mr. BELT. That is correct. The anticipation, and I was not at the helm of the PBGC at the time, was that that relief would be temporary, would expire at the end of this year. And I think the expectation of all parties was that there would need to be comprehensive pension reform and that would allow sufficient time to

Mr. PRICE. If we would figure out what the solution is. When the relief expires though the airlines will face tremendous liquidity and cash flow problems, I do not think anybody would disagree with that, and many of them may find it difficult to operate and move them toward the bankruptcy that has been talked about. So I have a couple of very specific questions. One is, do you have a handle on what the expected fallout would be in the funding contributions of the airlines if the relief expires and nothing is done?

Mr. BELT. I believe they have made public statements as to what under current law would be their required pension contributions over the next few years, and they are substantial sums. I do not know whether in the numbers that they have used they are contemplating the continuation of the corporate bond rate, essentially the relief that was provided in PFEA, the 2004 Act, or snap back to the Treasury discount rate. In either event, it is a substantial number because they are within the DRC contribution rules at this point in time.

But I would note that that issue, as to what happens at the end of this year, is not unique to the airlines. That would in fact affect everybody that is in the defined benefit system. And again, there are eight or ten auto parts suppliers that have filed Chapter 11 recently that sponsor underfunded pension plans, and there are a host of other companies similarly situated. So it is not at all unique to the airlines. What is only perhaps unique is the size of the funding gap, the total dollars involved with respect to the legacy carriers.

Mr. PRICE. Do you all have a "what if" strategy, what the potential impact for the PBGC if another airline were to declare bankruptcy?

Mr. BELT. We certainly know our potential loss exposure from the remaining carriers, which is about $22 billion.

Mr. PRICE. You are currently underfunded at $23 billion, correct?

Mr. BELT. Correct.

Mr. PRICE. Just one final question. I know that PBGC has an opportunity to speak confidentially with airlines or with any company if there are problems. Can you say whether or not you are having any discussions right now with any airline company?

Mr. BELT. We have had meetings with all our best customers on a regular basis, including airline companies. We share information, we try to get a better of understanding of what the issues are, what the level of underfunding is, what the minimum contribution requirements are, what the plan of action is for meeting those.

We not only have conversations with airline executives, but any company that poses a potential risk of loss to the pension insurance program whether they are a high default risk and/or substantially underfunded. We get information from a variety of sources. We talk to industry analysts, investment bankers, and others about trend lines in industries, issues with respect to particular companies.

Mr. PRICE. Thank you. I want to thank the other panel members. And again, I appreciate the opportunity to join you today. Thank you.

Mr. MICA. Well, I certainly want to thank our panelists. It has been a long afternoon. But you can see that there is very serious interest in this critical issue. We will probably have additional questions, I have some myself, that we will submit to you for the record. So we will leave the record open for your responses. But I do want to thank you, all of you, for the outstanding information you provided our Subcommittee.

With that, we will excuse you. Thank you again for your participation.

As they are retiring, I will call our second panel.

Our second panel consists of Captain Duane E. Woerth, President of the Air Line Pilots Association; Mrs. Patricia A. Friend, International President of the Association of Flight Attendants, CWA, AFL-CIO; Mr. Mark S. Streeter, Managing Director of JP Morgan Securities; Mr. David Strine, he is Managing Director of Equity Research of Bear Stearns and Company, and we also have Scott Yohe, Senior Vice President, Government Affairs, also a communications specialist in distributing information about measures the Chairman does not like, and he is from Delta Air Line.

I would like to welcome all of our witnesses. Some of you have been here before, some of you have not. We appreciate your being available to the Subcommittee today.

With those introductions, I think everyone is ready. I will go ahead and recognize first Captain Duane Woerth, president of the Air Line Pilots Association. Welcome, and you are recognized.

TESTIMONY OF CAPTAIN DUANE E. WOERTH, PRESIDENT, AIR LINE PILOTS ASSOCIATION; PATRICIA A. FRIEND, INTERNATIONAL PRESIDENT, ASSOCIATION OF FLIGHT ATTENDANTS, CWA, AFL-CIO; MARK S. STREETER, MANAGING DIRECTOR, JP MORGAN SECURITIES; DAVID STRINE, DIRECTOR OF EQUITY RESEARCH, BEAR STEARNS & COMPANY; AND SCOTT YOHE, SENIOR VICE PRESIDENT, GOVERNMENT AFFAIRS, DELTA AIR LINES

Mr. WOERTH. Thank you, Mr. Chairman. Thank you for holding this hearing. What I would like to focus on is solutions. I have heard an awful lot about how we got here and all the problems with the rules, and I would like to focus on solutions and consequences of not getting the solutions.

Certainly the Air Line Pilots Association supports the bill that was introduced by Congressman Price. It is equivalent to the bill introduced in the Senate by Senators Isakson and Rockefeller. We believe that bill, which provides a pension freeze, long-term amortization, new interest rates, is the solution that does the three things we would want to do.

It protects worker's pensions, the pensions will not be lost; it can keep the airline out of bankruptcy so further damage to shareholders and creditors does not occur; and just as importantly I know for the interests of this Congress, it is probably the only solution that can stop another United or U.S. Airways where billions of dollars more end up being terminated and put on the Pension Benefit Guarantee Corporation. This bill will do all those things and prevent that. So that is the number one thing I would like to advocate.

I would like to also comment in this regard. Previous testimony, portrayed this legislation as doing something radical or something controversial. The very fact of the matter is that it is doing the common sense thing that has been part of ERISA since 1974. Long-term pension obligations need to be funded and amortized over a long period of time. All that money is not due next week, it is not all due next year.

Mr. Chairman, I think you made a very pertinent comment about the public sector, where if the public sector lived under the same problems, the Federal Government, State, municipalities and counties would have an awful serious problem and I do not think we want those going into bankruptcy. But I want to emphasize that point. This is not unreasonable long-term amortization. In fact, ERISA when it was formed in 1974 anticipated 30 year amortization in all of these things. So I think it is a very reasonable approach.

Another thing that must be addressed is the sheer numbers that we are talking about. At United Airlines it was 125,000 workers, with U.S. Airways it was nearly 80,000, Delta and Northwest would be another 200,000 combined, if downstream there was competitive problems for other legacy carriers, there would be another couple hundred thousand. We are talking over half a million workers exposed just in the airline industry with legacy carriers. I think that should be plenty of motivation to do something and do it in the near term.

I would mention this as well. We have an example just north of the border where the Canadians had a similar problem. Air Canada was in bankruptcy. Air Canada could not get exit financing, the things that Mr. DeFazio talked about. The credit markets, and we have people here from the capital markets who can speak to it, when they looked at these defined benefit plan amortization schedules and how much money was due over a very near period of time in Canada, Air Canada could not get its financing until the parliament acted.

When the parliament acted and gave them long-term amortization, they had competitive bids and they got their financing and exited bankruptcy within 41 days. Now, I am not predicting an exit in 41 days if somebody stumbles in, but I think I am going to leave it to Mr. Streeter and his colleagues to talk about what the capital markets think about the amortization schedule and why airlines are financeable either to get out of bankruptcy or to stay out of bankruptcy if we have long-term amortization at a new interest rate.

In the interest of time, Mr. Chairman, I would like to move on. I will take any questions you or your colleagues may have. Thank you.

Mr. MICA. Thank you for your points. We will hear from all the witnesses and then go to questions.

I will now recognize Patricia Friend, International President of the Association of Flight Attendants. Welcome back. You are recognized.

Ms. FRIEND. Thank you, Chairman Mica, and thank the Committee for the invitation to testify today on this pension crisis. The crisis in the airline industry is of particular importance to the people I represent, to the women and men who serve as flight attendants. We represent 46,000 active flight attendants at 24 airlines. Our active and retired flight attendants at United Airlines number approximately 28,000.

Over the past several weeks and again here today, we have heard some thoughtful and well-informed testimony on the financial status of pension plans in the airline industry and on the long-term viability of those plans. We have also heard about the ramifications of the United pension terminations, and potentially other pension terminations, on the financial health of the PBGC.

But I would like to remind the Committee that issue has a human dimension. To get a feel for how these individuals will be affected, I urge you to read just some of the thousands of testimonials that were submitted to Congressman George Miller's online hearing.

Some Members of the Congress have asked me if we really think that liquidation of our company would be better for us in the long run. That question implies that by seeking to save our pensions we will cause the eventual failure and liquidation of our employer. The fact is that the employees of this industry have made repeated financial concessions over the past several years just to keep our airlines alive and profitable.

We have much more at stake in the airline's survival than do most members of upper level management. In this industry management comes and goes, often with a huge financial incentive to do so. In fact, United's current CEO, Glenn Tilton, can leave the company and still collect his bankruptcy-proof $4.5 million pension.

Over the past several months AFA has worked with the PBGC and with United Airlines to find a solution to the termination of our pension plan. During this time the PBGC maintained that the flight attendant plan was affordable and that it could be retained in a successful reorganization. At the same time, we attempted in vain to engage United management in negotiations over alternatives to plan termination. United Airlines management demonstrated very little real willingness to engage in meaningful negotiations with us about saving our plan.

During February and March of this year, we regularly consulted with the PBGC as we developed a proposal that identified sufficient alternative funding to save our pension plan. On April 14th, the PBGC filed an emergency motion to postpone consideration of United's motion for distress terminations of its defined benefit plans, calling United's motion premature and arguing that United Airlines had failed to show that the plans were not salvageable.

Then, on April 22, United announced that it had reached an agreement with the PBGC, an agreement in which United agreed to provide $1.5 billion to the PBGC and the PBGC would agree to terminate all four employee pension plans.

Our concerns with United's termination of the flight attendant pension plan and the PBGC's decision to withdraw their challenge to the termination are numerous. However, simply put, we do not believe that the termination of our pension plan is necessary for the survival of United Airlines. We have tried repeatedly to negotiate with the company on alternatives. In fact, we are the only work group that has offered to pay for part of the plan ourselves.

If United management is successful in their efforts to terminate our pension plans, no one should be under any illusion—the other so-called legacy carriers will attempt to dump their pension plans as well. And if you, the distinguished members of this Committee, allow this to go forward, it is probable that there will soon be a need for a massive taxpayer bailout of the PBGC.

If something is not done now, it will be too late for the United employees. I am strongly urging each and every member of this Committee to cosponsor H.R. 2327, the Stop Terminating Our Pensions Act, or the STOP Act. This bill would put in place a six month moratorium for any termination of covered plans initiated by the PBGC under ERISA 4042. this would give the Congress valuable time to explore further solutions to the crisis at United, and it would also allow time for the employer and the unions to develop and agree on alternatives to plan termination.

We strongly believe that the United flight attendant pension plan is viable and can be saved, but we need your help in providing the time and the incentive for management to work with us to find the solution. United's pension termination is not the first nor will it be the last domino to fall on the path to the destruction of retirement security.

But you can help put a stop to it today and help prevent hundreds of thousands of other workers from losing their pension and prevent billions of dollars from being dumped on the taxpayers if you allow this moratorium to pass and if you find a legislative solution to halt the demise of the define benefit pension plans in this country.

I urge the Committee to please give us the time that we need to try to save our pension. I urge you to consider and pass H.R. 2327 as quickly as possible. Thank you.

Mr. MICA. Thank you for your testimony.

We will now hear from Scott Yohe, Senior Vice President for Delta Air Lines. Welcome, and you are recognized.

Mr. YOHE. Thank you, Chairman Mica, Congressman Costello, Congressmen Price and Westmoreland. Thank you for the opportunity to address the pension funding crisis threatening Delta's ability to honor the pension benefits our active employees and retirees have already earned.

A sensible resolution of this crisis is absolutely essential if Delta is to successfully restructure its business outside of bankruptcy. As a son of a Delta pilot and a 26 year employee of Delta, it is a real privilege for me to be here today to appear before you on behalf of 80,000 active and retired employees as well as another 80,000 dependents who are all members of the Delta family and who support very much the testimony that I am providing today.

We have also worked very closely with our employees and retirees in addition with Northwest and the Air Line Pilots Association to develop a response to what Congress did last year in providing a two-year moratorium, and that is to develop a sound and sensible solution to this pension funding crisis. Our shared goal is very sensible. It is a transition funding rule that helps us to meet our obligations and avoid transferring the liabilities to the Pension Benefit Guarantee Corporation and avoiding the tragedy that has already befallen the workers at U.S. Air and United.

Simply stated, without changes to the current funding rule, the prospects for restructuring outside of the bankruptcy process are poor. Delta wants to avoid bankruptcy for all the reasons that have been discussed here today, including, and not the least of which, is to avoid termination of our pension plans.

At this point, I would like to offer a brief explanation as to why Delta requires unique pension funding rules. Delta's two traditional defined benefit pension plans were actually overfunded as recently as 2000. But pension rules, as you have heard, discouraged us from making additional contributions. Since that time, a combination of historically low interest rates and significant declines in the equity market have created large funding deficits in the plan and they have triggered accelerated payments known as deficit reduction contributions. This has also coincided with the massive losses that we have incurred since 9-11 and our worst fiscal crisis in the 75 years of Delta, making access to capital markets absolutely impossible.

Contrary to what was implied and perhaps suggested earlier today, Delta has not neglected funding its plans. We have made payments above the minimum requirement during the 2001-2003 period, and we have made payments of $440 million in 2004. We have already made payments this year of over $200 million and additional contributions of $60 million will be made during the balance of 2005. However, without changes in the funding rules as they exist today, our contributions over the next three years are projected at $2.6 billion, a level that we simply cannot afford given our precarious financial liquidity condition.

The new rules proposed by the Administration and House Republicans in H.R. 2830 are not helpful to companies like Delta. It would only worsen the situation and make bankruptcy a probable outcome.

Delta recognized in 2003 that the traditional benefit plans that we had been offering our employees for over 20 years were no longer affordable and we set about to replace them with more affordable, manageable plans that more reflected the competitive cost structure that we found in the industry. We created a cash balance plan for our non-pilot workers in 2003, and last fall we concluded an agreement with our pilots to replace our defined benefit plan with a defined contribution plan. Fortunately, Congressmen Price and Westmoreland and 21 other cosponsors have introduced H.R. 2106 which we believes provides a pragmatic airline-specific rule that properly balances the interests of all stakeholders.

H.R. 2106 would allow airlines to fund outstanding pension obligations on a more affordable 25 year schedule using stable, long-term interest rates. It offers a solution to the crisis in the following ways:

First, employees and retirees would have a greater chance to receive their full pension benefits rather than see those benefits significantly reduced in a transfer of liabilities to the PBGC.

Second, the bill is designed to protect the PBGC from increased future liabilities by capping the agency's guaranteed payments at current levels. This decreases the risk of taxpayer bailout in the future.

Thirdly, we think it benefits the travelling public by providing stability in the aviation system as the industry undergoes massive change and restructuring.

Lastly, and certainly most importantly for us in the near term and why this is so urgently needed now, it would allow Delta to remove this pension benefit cloud which inhibits our ability to access capital markets, a key component in completing the transformation process outside of bankruptcy.

Let me state clearly and emphatically that Delta is not seeking a subsidy. Instead, we are pursing a course that significantly limits additional PBGC liability and allows us to meet our obligations. I would also point out that Delta and other network carriers that are carrying this heavy pension benefit provide the vast majority of international service and are the primary links to small, rural communities. To Congressman DeFazio's point earlier, 50 percent of Delta's 202 domestic destinations are small cities with very limited service options.

We certainly understand the need for transformation of our business and we have not been idle. We have taken responsibility for changing our business model to respond to the new marketplace. We have made tough but necessary changes starting in 2002, such that by the end of 2004 will achieve $2.3 billion in annual revenue and cost benefits. However, these changes really are inadequate and we have set on a course with our transformation plan to take out $5 billion by the end of 2006. We believe that with those changes we stand a very good chance of becoming a viable airline in the future and meeting our obligations.

We look forward to working with Congress to establish a solution that offers a more orderly restructuring of the industry and a stronger, healthier airline system. Thank you, Mr. Chairman, and I certainly look forward to answering any questions you or other members of the Subcommittee may have.

Mr. MICA. Thank you.

We will hear now from our two financial and securities experts. We will hear first from Mark Streeter with JP Morgan Securities. Welcome, sir, and you are recognized.

Mr. STREETER. Chairman Mica and members of the Committee, thank you for inviting me to speak this afternoon. My name is Mark Streeter and I am responsible for airline credit research at JP Morgan. Please note that my statements do not represent the official position of my employer. I will summarize my detailed statement which was submitted for the record.

Unfortunately for the airlines, the credit markets are very concerned about the airline industry's fundamental situation and looming pension obligations, particularly at Delta and Northwest. Based on current prices, the market implies 43 percent and 55 percent one year bankruptcy probability for Northwest and Delta, respectively. For AMR and Continental, implied default risk over the next four years is greater than 50 percent. Delta and Northwest bonds due in only four years offer annualized yields near 40 percent and trade at prices well below fifty cents to the dollar.

There are several reasons why the credit markets are worried. You have heard others testify about the disconnect between industry revenue and overall economic growth since the attacks of September 11. I estimate that the fare increases this year have thus far, at best, offset only half of the oil price increase. Counter-parties are not willing to engage the legacy airlines in fuel hedging without cash collateral, making it impossible for the legacy carriers to hedge fuel costs.

The legacy majors have not stood still and have increased their unit revenue premium relative to the low cost carriers while narrowing their cost disadvantage. But there is obviously more work to do. Nevertheless, legacy airline liquidity could decline significantly this year. We estimate that Delta and Northwest will burn more than $1 billion in 2005, inclusive of capital raised year to date unless cash reserves are replenished further.

The industry's ability to add incremental debt, although seemingly never quite exhausted, is rapidly diminishing. Since 2000, airlines have borrowed more than $27 billion. Delta credit ratings have fallen 10 notches since the day before the September 11 attacks. Northwest ratings have fallen seven notches, including yesterday's Moody's downgrade.

In order to raise capital, the legacy airlines have turned to non-traditional lenders such as hedge funds and vendors. The legacy airlines could perhaps tap some of these same sources for further additional liquidity if pension reform positively impacts their credit standing. Delta has disclosed that its projected minimum pension funding under the current rules will increase to $600 million in 2006, and to more than $1.5 billion in 2008. Our estimates for Northwest are similarly dire.

In my opinion, Delta and Northwest will be forced to seek Chapter 11 protection and the termination of defined benefit plans unless reform allowing for a longer term amortization of deficits for sponsors that agree to freeze plan liabilities is passed into law. Legacy Chapter 11 filings are not necessarily inevitable. I believe that Delta and Northwest would prefer to avoid the Chapter 11 process.

Most airline and industry observers believe, as I do, that too many legacy carriers exist today and that further consolidation is inevitable. But further rationalization does not necessarily need to occur in Chapter 11 if the Government allows the legacy airlines to pursue mergers that make economic sense.

For example, if the Government affords the flexibility to stretch payments out over a period of several years, the sponsors must be forced to maintain fiscal discipline in my opinion. I believe that airlines or other sponsors opting into a longer term deficit amortization payment option should not be allowed to repurchase stock, should not be allowed to pay dividends, and should not be allowed to offer increased defined benefits even if they are funded with cash.

Members of the Committee, if the proposed legislation not supported by the airlines is passed into law, I believe, as do the credit markets, that Delta and Northwest will likely file for Chapter 11 protection within the next 12 months. Nothing is guaranteed, but the ability of the legacy airlines to successfully structure outside the courts is almost directly tied to pension reform that does not result in onerous near-term deficit reduction contributions at this point.

The Government has one of two choices in my opinion. Either pension reform legislation will add to the already high level of cash flow uncertainty, or pension reform will provide some degree of comfort to creditors willing to participate in out-of-court restructuring solutions.

Thank you once again for allowing me to speak to you today.

Mr. MICA. Thank you.

I want to apologize to you, Mr. Strine, you are the last witness and I understand you were going to leave earlier and changed your plans. So we do appreciate your being with us and testifying before the Subcommittee. You are recognized.

Mr. STRINE. Thank you. I am honored to be here. Good afternoon Chairman Mica, Representative Costello, and other members of the Committee. Thanks for the invitation to testify today on the U.S. airline pension issue. I am responsible for airline equity research at Bear Stearns. But throughout my testimony I will be presenting my personal views, which are not necessarily those of my employer.

The airline industry is certainly in miserable financial condition and it is destroying shareholder value. Since 2000, the ten largest publicly traded airlines have lost $10 billion in market capitalization, and the market index is down 64 percent versus 20 percent for the S&P 500.

The airlines have evolved into what is virtually a commodity-equivalent business with little to no pricing power. The growth of low cost carrier market share has driven structural changes in the airlines' ability to price discriminate, and the legacy cost carriers have simply not moved fast enough to change their high fixed cost structures. Through the Darwinian forces of the free market, the industry appears ripe for a period of consolidation. If oil prices remain high, that may eventually occur regardless of whether or not there is a change in pension funding standards for the airline industry.

While there are many reasons for the airline industry's financial weakness, the defined benefit pension plan funding problem is the focus of my comments this afternoon. My conclusion is that the longer the period of amortization of pension funding requirements and the higher the interest rate benchmark the airlines are permitted to use in discounting plan obligations, the more access the legacy cost airlines will have to the capital markets in the near term.

I will cover three basic questions:

One, what are the financial implications of the existing pension funding deficits? Two, how would more lenient pension funding standards affect the airlines? Three, what would a change in pension funding standards for the airline industry mean for shareholders?

First question. Under ERISA, we estimate that the airlines' $14 billion defined benefit pension funding shortfall will require $1.2 billion in cash contributions in 2005. This is a significant number, but it is only meaningful when considered in light of the airlines' ability to make the contributions based on their operating cash flows and unrestricted cash balances. Keep in mind that cash flow can be quite volatile as it is dependent on oil prices, labor costs, as well as the revenue environment.

In the report I have submitted as part of my testimony I provide a sensitivity analysis with different assumptions for oil prices. Each $1 move in oil costs the airlines about $450 million annually. For 2005, the $1.2 billion in cash contributions represent about 90 percent of our operating cash flow forecast with oil at $50 a barrel, and 13 percent of the combined unrestricted cash balances of the legacy cost carriers.

This is troublesome, but matters do not improve next year. With the expiration of the Pension Funding Equity Act of 2004 at the end of the year, I estimate that the required cash contributions could increase 100 percent, to $2.4 billion in 2006, representing 60 percent of operating cash flow and 30 percent of our projected unrestricted cash balances with oil at $50 a barrel.

When examining the airlines individually, my analysis suggests that pension related risk among the legacy cost carriers operating outside of Chapter 11 differs substantially. Considering their ability to make the required pension contributions, in descending order, I rank the risks as follows: Delta Airlines, Northwest, Continental, American, and then Alaska.

All told, if fares do not increase and oil remains at current levels, without more lenient pension funding requirements, I believe both Delta Air Lines and Northwest Airlines face near-term bankruptcy risk and others could be at risk longer-term.

On the second question, how would more lenient pension funding standards affect the airlines? The longer the period of the amortization of pension funding requirements, and the higher the interest rate benchmark the airlines are permitted to use in discounting plan obligations, the lower the cash burn rates and the lower the probability of bankruptcies.

I estimate that pension cash contributions for the legacy airlines would fall 87 percent to about $300 million from $2.4 billion in 2006 if the amortization period for funding pension obligations were to change from four years to the twenty-five years which has been proposed in Representative Price's bill. Under this scenario, I believe bankruptcy risk declines significantly, even for the weakest legacy cost airlines, Delta and Northwest.

On the other hand, even excluding the potential increases in the funding requirements due to interest rate benchmark changes, using the seven year amortization periods that appear in the Bush Administration proposal and Representative Boehner's bill, I estimate that pension cash contributions would fall just 32 percent to $1.6 billion from $2.4 billion. Under this scenario, my cash-burn analysis suggests that Delta and Northwest have a very high risk of bankruptcy over the next year. Certainly the current equity market valuations reflect this risk.

The final question, what would the change in pension funding standards for the airline industry mean for shareholders? An exception to the funding requirements under ERISA for the airlines is not enough in itself to cure the ills of the airline industry and halt the destruction of shareholder value. Although shareholders and creditors of the airlines that face the most severe liquidity problems could benefit in the near term from more lenient pension funding requirements, such a change only extends the window of opportunity for these companies to remedy the inefficiencies in their businesses and reduce their operating costs so they can begin the hard work of repairing their terribly distressed balance sheets. Even excluding the pension issue, the operating cost structures of these companies remain uncompetitive.

What is more, if extending a life line in the form of pension relief serves to delay the reduction of other costs or keeps companies afloat that would otherwise shrink in Chapter 11 or by way of Chapter 7, thereby ringing some capacity out of the system, the result may well be disadvantageous to airlines that already have defined contribution plans or have enough operating cash flow to cover their required defined benefit plans. Of course, such an outcome is not probable given that Chapter 11 itself has been harmful to the overall welfare of the airline industry because it sets up a lopsided playing field and does not necessarily result in consolidation or reduction of supply.

Ultimately, I believe shareholders will benefit most if the natural forces of the free market determine the fate of the airline industry. Under such conditions, making decisions on how to invest is an easier process. However, without a change to the bankruptcy laws and antitrust hurdles that allow for easier consolidation of weak businesses, a laissez faire policy on pensions will do little to improve conditions for shareholders.

Accordingly, barring changes in other areas of law that would provide for swifter consolidation, I believe shareholders will benefit in the near term from a change in pension law that allows airlines to amortize their required contributions over a period well beyond the seven years noted in the Boehner bill and closer to the twenty-five year period noted in the Isakson bill. Of course, no measure of pension help will solve the structural operating cost and balance sheet problems facing the legacy carriers. Thanks very much for the opportunity.

Mr. MICA. Thank you again or your patience, and all of you for your testimony.

A couple of quick questions. I saw the charts that the General Accounting Office put up and the small amount of money that was being put into these pension plans. We have got a couple of employee representatives here, the Flight Attendants and the Pilots, were you all aware that they were putting in that little money? Did you have access to records, Mr. Woerth?

Mr. WOERTH. First of all, besides my duties as a union officer and now president for the last seven years, I was even on the Northwest Airlines board of directors from the period of 1993 to 1999, where they were making pension contributions, but also where, like Delta, they did in that period of time run up against the maximum legal amount that they could put in without incurring a tax penalty. And one of the proposals going forward is to eliminate that. But right now, that is water under the bridge where are companies are today. One of the things about that chart

Mr. MICA. My question was, were you aware, did you have access? I thought someone told me that the employees groups did not have access to contribution information.

Mr. WOERTH. I understood the problem.

Mr. MICA. You understood what was going on?

Mr. WOERTH. Yes, I did.

Mr. MICA. And what about you, Ms. Friend?

Ms. FRIEND. We have a process for a regular accounting on the report on the defined benefit plan. The fact is that the way the funding rules work, they did not have to put in any more. So, yes, we knew.

Mr. MICA. Did your folks look at it?

Ms. FRIEND. We knew what they were putting in. But that little amount made it a fully funded plan under the rules.

Mr. MICA. Did someone actuarially look at this and say this is not going to float in the future? They were just putting in the minimum that they could under the rules. They had promised both of your groups certain pension benefits and what I wanted to do was make certain that you had access. If we revise the law and you did not have access in the past, what can we do to make certain in the future that everything is done to protect your interest and the employees' interest. That is the purpose for that question.

Mr. Yohe, you said you were doing 260 this year, Sterns and Morgan representatives. We heard GAO say that this only accounts for about one-sixth of their costs I guess, and that even if we eliminated that, it looked pretty grim anyway. You did not have that take. You said the longer you could stretch it out, of course, the less they have to put in. So if we stretch it out and they still are filing for bankruptcy, do you think that will occur, that we putting off the inevitable?

Mr. YOHE. I think that what extending it over a longer period of time does is that it gives them the opportunity to rectify the structural problems they have with their cost structures. Ultimately, they need to be competitive with the folks out there who are setting the prices, and that is the low cost carriers. They need to get within their range on their unit costs that allows them to have parity in operating monies.

Mr. MICA. So the longer you stretch it out, the better shot they have got at some possibility of survival.

Mr. Streeter, do you think they will survive even if we stretch it out?

Mr. STREETER. Mr. Chairman, it would give the airlines and give the Government an option and an option of time for the airlines to continue lowering labor costs, to getting labor costs in line with the low cost carriers, to equitizing their balance sheets. Delta, for instance, has been pursuing a path of exchanging debt for equity and has indicated a desire to do so going forward. So asset sales, time to sell assets and to use proceeds to try to address the debt burden. But depending on your oil price forecast, bankruptcies may be inevitable.

Mr. MICA. Yes, I just saw that. A dollar is four hundred and fifty million. That is pretty substantial. If you do not increase prices, you are not going to stay in business.

Mr. Costello.

Mr. COSTELLO. Mr. Chairman, thank you. Ms. Friend, you mention in your testimony that your organization is seeking a six month moratorium on the United pension plan termination. I wonder if you might kind of tell us what the rationale and reasoning is for that, what you hope to accomplish if you get a six month moratorium.

Ms. FRIEND. Essentially, what we are hoping to do is stop the clock on the process that has been started at United. That would give us, the employees, the opportunity and hopefully give United management the incentive to work out an alternative to plan termination. It would also give the Congress the time that they need to review all the various proposals about funding rule changes, longer term or amortization of the debt. It would simply, as I said, stop the clock on this process that has started in the airline industry.

Mr. COSTELLO. I understand that you are saying that the moratorium would give Congress and others time to kind of work through all of this. Is that the goal here?

Ms. FRIEND. Exactly. That is the goal.

Mr. COSTELLO. Okay. Mr. Strine, if Delta and Northwest were to file bankruptcy and terminate their pension plans, what would the likely response be by American and Continental?

Mr. STRINE. Representative Costello, I think that if both Northwest and Delta were to file and then terminate their pension plans, the risk of Chapter 11 at American Airlines and Continental would increase substantially because ultimately they would be operating at a significant cash flow disadvantage and operating cost disadvantage to those other two companies.

Let me put it this way. If both of those companies were to file for bankruptcy, you would have 45 percent of the capacity out there in the industry operating without disadvantage of having a defined benefit pension plan. That is going to be tough to compete with for the remaining guys with it.

Mr. COSTELLO. What changes do the legacy airlines need to make in order to become competitive?

Mr. STRINE. That is the ultimate question.

Mr. COSTELLO. You heard me ask it earlier of the GAO. They said they had recommendations to reduce cost. It seems to me that the legacy airlines have; you have been through it, everyone at the table has, we have seen pay cuts, we have seen benefits given back. What else can be done in order to save money?

Mr. STRINE. I think there are two things. Other than continuing to lower wage rates, they can improve productivity. That does not mean just having people work more hours and changing work rules. It also means simplifying the businesses, increasing utilization rates of aircraft, having fewer types of aircraft so pilot training costs go down and maintenance expenditures go down, getting to a situation where there is enough operating cash flow to begin to pull down debt and therefore reduce interest expenses. Only through those types of measures will they ultimately be able to survive and compete with the likes of Southwest and Jet Blue and AirTran.

Mr. COSTELLO. Mr. Chairman, thank you.

Mr. MICA. I thank you. Mr. Westmoreland.

Mr. WESTMORELAND. Yes, sir. Thank you, Mr. Chairman. I know the hour is late and I will try to be brief.

Mr. Yohe, you mentioned, and Mr. Woerth also mentioned about Northwest, that those two airlines I guess in 1999 or 2000 were bumping the maximum that they could contribute. Did the Government set this maximum rate that could be put into the pension plans, Mr. Yohe?

Mr. YOHE. Yes. There is a maximum amount that is allowable in order to get tax deduction for those contributions. In the year 2000, our plan was at 114 percent funded at that point. I would just like to make a general comment too. There was a lot of conversation today about how carriers and companies' plan sponsors have funded their plans or not funded their plans in terms of the minimum or whatever. I think what is important to look at here is that we did not have a funding problem at all until 2002 when we saw this phenomena occur which was the deficit reduction contribution kick in because of low interest rates and the market.

Over a very long period of time Delta really never had a problem because, as Mr. Woerth said and others have said, you are talking about a pension program where you earn benefits over a long period of time, you pay them out over a long period of time. So there never really was a problem until 2002. The deficit reduction contribution requirement was written into law in 1987, and neither prior to that time nor subsequent to that time did we have the kind of bow wave of payments and obligations that is staring us in the face today.

Mr. WESTMORELAND. I know the director of education and workforce had given out a chart that showed that the airlines did not put in but just a very, very small amount. And from what I am hearing, during that period of time you were putting in what the law would allow you to put in. And from what I am hearing your liability is now, was that one reason you gave as the total reason that you are that short now? And the other part of the question is, what kicks in to tell you how much you have now got to pay? I mean the Government set the maximum, do they set the minimum also?

Mr. YOHE. Yes, there is a minimum and a maximum. But essentially the way the law works is that if you go below 90 percent or 80 percent in terms of total fundedness of the plan within any two to three year period, then these accelerated catch up payments kick in. So then in a very short period of time you have a very large payment to make in addition to the normal minimum payment as well as the premiums that you would be paying.

So that is really what we are confronted with right now is how to deal with those accelerated payments where essentially it is like a balloon payment on a mortgage where suddenly you owe the entire amount of the mortgage. What we are saying is we do not have that money to pay off the full amount, so let us amortize that over a payment schedule that is more manageable and practicable for us.

Mr. WESTMORELAND. And one last question. Mr. Yohe, is it not true that Delta really does not want to file Chapter 11 and put more responsibility on the taxpayers or on the Government retirement system, and that you all would really rather work out your problems and all you are asking for is a fair shot to do the right thing?

Mr. YOHE. Well, I appreciate the question. We have made a conscious effort and have established a transformation plan to try to restructure our company out of bankruptcy. And the reason is quite simple. When you go into bankruptcy there is a lot of bad outcomes associated with that over and above possible termination of your pension plan.

As was discussed here earlier today, the track record of airlines successfully reorganizing in bankruptcy is not very good. In addition to that, the creditors and lenders and the judge exercise enormous influence and control over a whole lot of business decisions of the company affecting pay of employees, how you fly your airline and where you fly, how many airplanes you have, what hubs you have, et cetera. So you lose control to a large degree over a lot of those kinds of issues.

So we felt that for a lot of different reasons, most importantly because we believe that the pension benefits in Delta for 75 years is a moral obligation that we have to pay what our employees have earned, we want to do everything we possibly can to avoid that.

Mr. WESTMORELAND. Thank you, Mr. Chairman.

Mr. MICA. Thank you. Mr. Price.

Mr. PRICE. Thank you, Mr. Chairman, I appreciate that. And I want to thank each of you for coming as well and for your patience today. It has been a long day. I had a number of questions, but I will just ask one of Mr. Strine and Mr. Streeter if I may, and that is to address, if you would, the need for industry-specific reform and whether or not you feel that is appropriate, whether that is necessary in this instance. Just your comments on industry-specific reform.

Mr. STRINE. Just as it pertains to the pension issue?

Mr. PRICE. Yes.

Mr. STRINE. Well, I think without it, we are looking at a much higher probability of bankruptcy at two of the big legacy carriers, Northwest and Delta, which, unless oil prices were to decline precipitously, could then result in a higher chance of bankruptcy at both American and Continental. So there is certainly a risk to the industry and then the rest of the industry because you will have such a big portion of it operating within Chapter 11 under that protection if action is not taken. But by no means is this a guarantee that there will not be bankruptcies because oil prices have been climbing every day.

Mr. STREETER. I would say that I cannot speak to the need for pension reform outside of the airline industry and whether or not the Government and the PBGC should be in the business of insuring defined benefit plans. That is a much broader policy issue. But I will tell you that for the airlines, without pension reform that allows for a longer term amortization of these deficits, Delta and Northwest, almost a fairly clear certainty, will file for Chapter 11 protection within the next 12 months, and others, namely, American and Continental, could follow depending on certain oil and revenue assumptions.

Mr. PRICE. So without that longer amortization, the exposure of the taxpayer to liability is significantly increased. Is that an accurate statement?

Mr. STREETER. Absolutely.

Mr. PRICE. Thank you, Mr. Chairman.

Mr. MICA. I want to thank all of our witnesses. Time has really run out because we did have about five votes pending on the floor. But as I told the first panel, we do have a whole host of additional questions which we are going to submit to you which will be made part of the record.

But certainly we want to thank each and every one of you. Your testimony has been a great contribution, and the previous panel. I think our whole Subcommittee learned a great deal and you have educated some of the Members of Congress on the very serious challenge facing Congress and really our entire american economy at this juncture. So we appreciate your participation. We will let you go at this time. Thank you again.

There being no further business before the Aviation Subcommittee, this hearing is adjourned.

[Whereupon, at 6:05 p.m., the committee was adjourned.]

Protecting America's Pensions

TESTIMONY OF BRADLEY D. BELT

Executive Director

PENSION BENEFIT GUARANTY CORPORATION

Before the Subcommittee on Aviation

Committee on Transportation & Infrastructure

United States House of Representatives

June 22, 2005

Chairman Mica, Ranking Member Costello, and Members of the Subcommittee: I appreciate the opportunity to discuss the pension challenges facing the U.S. airline industry and the important role played by the federal pension insurance program.

As you know, this hearing is occurring against the backdrop of the largest pension default in the history of the United States. As I will discuss more fully later in my testimony, United Airlines' default on its pension obligations is illustrative of fundamental flaws in the federal pension funding rules—flaws that must be addressed if we are to avoid additional pension tragedies in the future. The United Airlines case also illustrates the inadequacy of the current premium structure to insure pension promises and protect taxpayers against a potential bailout of the defined benefit pension system.

By the numbers, United Airlines' pension plans have assets of roughly $7 billion to cover liabilities of $16.8 billion on a termination basis, for a shortfall of $9.8 billion.[1] The pension insurance program will be responsible for covering $6.6 billion of the shortfall, by far the largest claim in the 31-year history of the PBGC. But the United default also sets another ignominious record – the largest-ever loss of earned pension benefits by workers and retirees. Because weaknesses in the pension funding rules allowed United Airlines to dramatically underfund its pension promises, the company's more than 120,000 plan participants now stand to lose roughly $3.2 billion in retirement income they were counting on.

The U.S. Airline Industry: A History of Pension Defaults

As tragic as these losses are, they are unique only in their size. Indeed, United is merely the latest airline to default on obligations to its workers. In each round of airline bankruptcies, the pension insurance program has wound up responsible for benefits that companies promised but did not adequately fund. In the early 1980s, it was Braniff (1982). In the early 1990s, there were Pan Am (1990) and Eastern (1991). And in the early 2000s, there were TWA (2001) and US Airways' pilots' plan (2003). Claims from just these five airlines total $2.9 billion. As a result, the PBGC is now responsible for paying more than $500 million a year to 80,000 retirees in these failed plans. Overall, these airlines accounted for 12.5 percent of all retirees and 14 percent of claims from failed plans as of September 30, 2004.

When the $2.3 billion claim from US Airways' other (non-pilot) plans and the $6.6 billion claim from United are included, airline claims will more than quadruple from $2.9 to $11.7 billion. As a result, airlines will account for 38 percent of claims from failed plans, vaulting airlines ahead of steel (33 percent). It is important to note that while these airlines will account for 38 percent of all claims, they have paid only 2.6 percent of total premiums in the history of the insurance fund. Beyond United Airlines, there is another $22 billion in unfunded pension liabilities among the legacy carriers.

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[1]The four plans are: the UA Pilot Defined Benefit Plan, which covers 14,100 participants and has $2.8 billion in assets to pay $5.7 billion in promised benefits; the United Airlines Ground Employees Retirement Plan, which covers 36,100 participants and has $1.3 billion in assets to pay $4.0 billion in promised benefits; the UA Flight Attendant Defined Benefit Pension Plan, which covers 28,600 participants and has $1.4 billion in assets to pay $3.3 billion in promised benefits; and the Management, Administrative and Public Contact Defined Benefit Pension Plan, which covers 42,700 participants and has $1.5 billion in assets to pay $3.8 billion in promised benefits.

The Challenge from Low-Cost Carriers and Pensions

There is no question that the legacy airlines are facing unprecedented challenges, both internal and external, as the Government Accountability Office[2] and other experts have attested. The commercial airline industry is capital-intensive, labor-intensive, and has high fixed costs, with revenues and profits closely tied to the nation's business cycle. Among the legacy carriers, these capital and labor costs are higher still; they have a more expensive hub-and-spoke route system, multiple and older fleets, a more senior workforce with defined benefit pensions, and more restrictive work rules. They are also suffering from unprofitable cheap fares largely driven by fierce competition from low-cost airlines, and the entire industry, legacy and non-legacy carriers alike, are suffering from soaring fuel costs. While the first generation of low-cost airlines did not survive, today's low-cost carriers are formidable competitors. In addition, consumers have benefited from the growing use of the internet as a point of sale for airline tickets, which has made it is easy for travelers to choose the lowest-price carrier. Low-cost carriers have increased their share of available seat miles (an industry measure of supply) from 10.8 percent in 1998 to 17.5 percent in 2003.

Congress and the Administration have been sympathetic to the plight of the airline industry. After September 11th, Congress created the Air Transportation Stabilization Board to administer up to $10 billion in loan guarantees to help a struggling industry get back on its feet. These loan guarantees and other types of federal relief were provided to help the airline industry recover from the impact of the terrorist attacks; they were not intended to remedy long-standing structural problems in the industry. Today, nearly four years later and with passenger traffic at record levels, the plea from certain carriers is for a different form of loan guarantee. In economic terms, that is what pension funding rule changes represent —a loan from the pension plan to the company, co-signed by the PBGC and underwritten primarily by financially healthy companies whose premiums finance the insurance program.

Delta and Northwest are seeking funding relief in exchange for freezing their workers' pensions to help prevent these liabilities from growing larger. American has expressed support for a longer amortization period but opposes freezing the pension plan. American's proposal would allow liabilities to grow at the risk that plan assets would fail to keep pace.

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[2] U. S. Government Accountability Office, "Commercial Aviation: Legacy Airlines Must Further Reduce Costs to Restore Profitability," GAO-04-836 (August 2004).

Clearly the financial and pension challenges facing each legacy carrier are unique: Two airlines have declared bankruptcy and offloaded their pensions onto the PBGC, several want to freeze their plans in exchange for special treatment, and others intend to fully fund their pension promises.

The airline industry has received substantial relief from its pension funding obligations from Congress. In the Pension Funding Equity Act of 2004 (PFEA)[3], Congress gave airlines a blanket exemption from their pension funding requirements under the Deficit Reduction Contribution (DRC) rules. Under PFEA, airlines and steel companies could elect to defer 80% of their DRC contribution, which is an additional catch-up contribution required for many underfunded plans. This allowed airlines to make little or no contributions for 2004 and 2005.

In 2004, six major airlines elected to receive this funding relief. As a result, these airlines' required pension contributions were about $1.3 billion less than would otherwise have been required. So far in 2005, required contributions for three of these airlines were more than $1.1 billion less than would otherwise have been required.

As Northwest Airlines has disclosed, it obtained additional relief from its pension funding obligations through a $454 million funding waiver granted by the Internal Revenue Service for its 2004 plan year. As a condition of the waiver, Northwest gave the PBGC a lien on certain corporate assets, including slots, routes, aircraft and engines. Other legacy carriers had waiver applications pending when Congress provided essentially the same funding relief in the PFEA. They declined to pursue these waivers after the enactment of PFEA.

This year, US Airways and United both have sought to terminate their ongoing plans. Now that the PFEA relief is about to expire, most of the other legacy airlines are seeking to extend the relief from two years to 25 years.

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[3] Pension Funding Equity Act of 2004 (P.L. 108-218, April 10, 2004). This law temporarily replaces the interest rate on 30-year US Treasury bonds with an interest rate based on the average rate of return on high-quality long-term corporate bonds. It also allows airlines to postpone part of their necessary contributions for 2004 and 2005.

The Source and Solution for Pension Underfunding

Pension underfunding is neither an accident nor the result of forces beyond a company's control. On the contrary, it is a largely predictable and controllable byproduct of decisions made by corporate management. In the case of the airlines, a series of decisions allowed pensions to become significantly underfunded. Companies did not contribute as much cash as they could when times were good, and in certain cases contributed no cash at all when it was needed most. In some cases, they granted generous benefit increases that are proving difficult to afford.

The tragedy is not that any of this was the result of illegal activity. The tragedy is that it was the result of perfectly legal activity under our system of flawed pension funding rules and inadequate premium structure. United and US Airways would not have presented claims in excess of $1 billion each—and with funded ratios of less than 50 percent—if the rules worked.

United's pilots' plan provides a case in point. During the period 1997 through 2001, United's debt rating was "BB+", the highest non-investment grade rating. When the company entered bankruptcy in 2002, its credit rating was dropped to "D." From 2000 onward, when the true funded status of each of the company's pension plans was deteriorating, the company:

- put no cash into the plan;
- never made a deficit reduction contribution;
- never provided any notices of underfunding to participants; and
- almost never paid a variable rate premium.

United was largely exempt from these rules because it could claim the pilots' plan was "fully funded" on a current liability basis. This rosy picture stands in sharp contrast with what we know to be the true status of United's pilots' plan—an aggregate shortfall of almost $3 billion and a funded ratio of only 50 percent.

United Airlines Pilot Plan

Termination Benefit Liability Funded Ratio 50%
Unfunded Benefit Liabilities $ 2.9 billion

	1998	1999	2000	2001	2002	2003
Current Liability Funded Ratio*	100%	98%	102%	98%	102%	80%
Was the company required to make a deficit reduction contribution?	N	N	N	N	N	N
Was the company obligated to send out a participant notice?	N	N	N	N	N	N
Did the company pay a Variable Rate Premium?	N	N	N	N	N	Y $6.7 million
Actual Contributions	$15.0 million	$40.0 million	$0	$0	$0	$0
Prior Year Credit Balance	$346.2 million	$393.3 million	$496.6 million	$513.1 million	$560.5 million	$525.5 million

* Current Liability Funded Ratio is based on five-year smoothing of assets and smoothed, four-year weighted average interest rate on liabilities.

Similarly, US Airways' pilots' plan was 94 percent funded on a current liability basis, but the plan was only 33 percent funded on a termination basis, with a $2.5 billion shortfall. US Airways was not subject to a deficit reduction contribution for six years leading up to the year of termination and relied on credit balances to avoid making any contributions for the four years immediately before terminating.

US Airways Pilots

Termination Benefit Liability Funded Ratio 33%
Unfunded Benefit Liabilities $2.5 billion

	1996	1997	1998	1999	2000	2001	2002
Current Liability Funded Ratio*	97%	100%	91%	85%	104%	94%	NR
Was the company required to make a deficit reduction contribution?	N	N	N	N	N	N	NR
Was the company obligated to send out a participant notice?	N	N	N	N	N	N	N
Did the company pay a variable rate premium?	$4 million	N	N	N	$2 million	N	N
Actual Contributions	$112.3 million	$0	$45 million	$0	$0	$0	$0

* Current Liability Funded Ratio is based on five-year smoothing of assets and smoothed, four-year weighted average interest rate on liabilities.

Several aspects of the current funding rules contributed to these disaster scenarios, but two should be singled out, as they also were in GAO's recently released report, "Recent Experiences of Large Defined Benefit Plans Illustrate Weaknesses in Funding Rules." [4]

One is the use of so-called credit balances. Just at the point in time when contributions to the plans were needed most, as asset values were falling and liabilities were growing, the company was able to use credit balances built up during the 1990s bull market to avoid putting cash into the plans. Remarkably, notwithstanding the fact that the United pilots' plan is underfunded by almost $3 billion, the company has not made, and has not been required to make, a cash contribution to that plan for the years 2000 through 2004 (and none would have been required until the end of this year).

The other aspect of the funding rules that merits mention is the ability to "smooth" assets and liabilities. Under current law, plans can smooth assets over five years and can smooth liabilities using a four-year weighted average interest rate. Those who want to retain these mechanisms argue that they reduce volatility, but they do not reduce it, they merely mask it—hiding it from the view of workers and retirees.

These issues are not unique to United Airlines, or even to the airline industry as a whole. We saw the same weaknesses lead to the same bad outcomes with the steel industry a few years ago, and there is substantial pension underfunding in other financially challenged industries. The pension insurance program recently has incurred large losses as a result of the pension defaults of companies in the financial services, among other sectors. And, while the program faces additional exposure from the airline sectors, the largest exposure is not from the airline or steel industries, but rather the automotive sector. Of particular concern, several automotive parts suppliers have filed for bankruptcy in recent months. These bankrupt companies sponsor defined benefit plans with more than $800 million in unfunded pension obligations that would become a loss to the pension insurance system should those companies' plans terminate during their bankruptcies.

[4] United States General Accountability Office, "Recent Experiences of Large Defined Benefit Plans Illustrate Weaknesses in Funding Rules," GAO-05-294, p. 22 (May 2005).

Effect of Plan Terminations on Stakeholders

Terminations of chronically underfunded pension plans adversely affect all the stakeholders in the defined benefit system—workers and retirees, companies that have acted responsibly in honoring their pension promises, and potentially U.S. taxpayers. These terminations can have particularly harsh consequences for workers and retirees. While the PBGC steps in to pay benefits to participants in terminated pension plans, because of limits on guarantees established in law by Congress, some workers and retirees may lose benefits they were counting on to provide economic security in retirement. Fortunately, most people receive all of their vested accrued benefits, but that isn't always the case. Expectations of a secure future may be shattered if promised benefits exceed guarantee limits and the plan is underfunded.

For example, workers at United Airlines, in the aggregate, should receive about 80 percent of their accrued benefits. But the United workers and retirees still stand to lose more than $3 billion in promised benefits. Some participants or their survivors may see benefits reduced by half or more because of statutory limits. That is the real tragedy of the current system of flawed funding rules.

Other companies that sponsor defined benefit plans also pay a price through higher premiums. Because the PBGC receives no federal tax dollars and its obligations are not backed by the full faith and credit of the United States, losses suffered by the insurance fund must, under current law, be covered by higher premiums. Not only will healthy companies be subsidizing weak companies with underfunded plans, they may also face the prospect of having to compete against a rival firm that has shifted a significant portion of its ongoing labor costs onto the government. This is clearly at issue in the airline industry. The CEOs of the legacy carriers have publicly stated that this scenario will give United an unfair advantage and may cause them to seek to terminate their pension plans.

In addition to the losses by workers and retirees and other companies that sponsor defined benefit plans, the single-employer insurance program is itself now in jeopardy. With more than $40 billion in assets, PBGC can continue paying benefits for a number of years. But with more than $60 billion in liabilities, PBGC will be unable to meet its long-term commitments without additional revenues beyond those mandated by current law. As a result, taxpayers are at risk of being called upon to bail out the pension insurance program if losses continue to mount.

Administration Reform Proposal

Unless we correct the inadequacies of the current funding rules we are on a course of more losses to all the stakeholders in the pension system. The system is not viable as it stands. On the other hand, with reform, we have a good chance of revitalizing the system.

The Administration has proposed a sensible, balanced reform package to correct the flaws in the system. Core elements include:

- A more accurate measurement of plan liabilities would be used to reflect the financial condition of the sponsor and the risk of plan termination. Two measures of liability—"at-risk liability" and "ongoing liability"—would be employed to require those at greater risk of termination to fund their promises more aggressively.

- Asset and liability smoothing, which distort the true funded status of pension plans, would be eliminated. Credit balances that allow companies to avoid making cash contributions would be barred. Companies that have failed to fund existing pension promises would be limited from making new unfunded promises.

- More accurate and timely plan funding information would be provided to plan participants, investors, and regulators.

- PBGC premiums would be restructured to be more equitable and to generate sufficient revenue to eliminate the $23 billion deficit over time and to pay future expected claims. The flat-rate premium would be increased to reflect wage growth and indexed, and all underfunded plans (based on at-risk or ongoing liability) would pay a variable premium.

Companies that sponsor pension plans have a responsibility to live up to the promises they have made to their workers and retirees. Yet under current law, financially troubled companies have shortchanged their pension promises by nearly $100 billion, putting workers, responsible companies and taxpayers at risk. As United Airlines noted in a recent bankruptcy court filing, "the Company has done everything required by law"[5] to fund its pension plans, which are underfunded by nearly $10 billion.

[5] Page 26, United Air Lines' Informational Brief Regarding Its Pension Plans, in the US Bankruptcy Court for the Northern District of Illinois, Eastern Division (Sept. 23, 2004).

It is difficult to imagine that healthy companies would want to continue in a retirement system, or that prospective employers would want to become part of a retirement system, in which the sponsor-financed insurance fund is running a substantial deficit. By eliminating unfair exemptions from risk-based premiums and restoring the PBGC to financial health, the Administration's proposal will revitalize the defined benefit system.

Mr. Chairman, the Administration is committed to strengthening the pension insurance program and keeping defined benefit plans as a viable option for employers and employees. This requires a careful balancing of interests and inevitably will require trade-offs among various stakeholder interests. We believe the Administration proposal strikes an appropriate balance and will best protect the pension benefits earned by workers and retirees, minimize the need for future premium increases, and lessen the possibility that taxpayers will have to be called upon to rescue the insurance program.

STATEMENT OF CONGRESSMAN LEONARD BOSWELL
AVIATION SUBCOMMITTEE HEARING ON AIRLINE PENSIONS
JUNE 22, 2005

The subject of today's hearing is a very important issue for thousands of people employed or retired in the U.S. airline industry. All of us know, the precarious economic condition of most air carriers. Most of them have been hemorrhaging red ink, at least since the terrorist attacks of September 11th, and many even before that tragic event. With a barrel of oil approaching $60, fuel prices are further hampering the air carrier's ability to find profitability. One tragic result of the airline industries financial free fall, has been an air carrier's pension plan.

In recent months, two carriers, USAirways and United have terminated their pension plan and the Pension Benefit Guarantee Corporation has assumed responsibility for their plans. This has, or will, result in significant reductions in expected pension compensation for most of the affected retirees. These are folks who played by the rules, showed loyalty to their employer, and were told they could expect to retire with a certain benefit. We see today that this will not be the case. Most of these retirees cannot unretire and start over. For many, their lifestyles will be severely disrupted. This is indeed a very sad situation.

For the air carriers, I ~~suspect~~ am sure they take no pleasure in seeing this devastation affect their loyal employees. The other remaining carriers are openly discussing, or have rumors suggesting they are about to follow USAirways and United in terminating their pension plans. This will bring about further hardship for those affected retirees or workers. The air carriers maintain they must pursue this path to remain competitive in the industry. ~~We have a case of "monkey see, monkey do."~~

As someone who understands the termination of these pension plans will not only hurt affected people, but other businesses who offer pension plans, we need to seriously evaluate how we can address this crisis. Healthier companies will see their PBGC premiums increase, because of the new unfunded liability being assumed. The system was never designed to absorb such enormous obligations.

I want to see our airline industry grow and prosper. They are an important component to our nation's economy. However, this pension situation has created tremendous hardship for thousands of people, and we must roll up our sleeves to address the many thousands of others who are watching and waiting for what's next. I stand ready to work with my colleagues to address this serious situation.

Thank you and I look forward to hearing today's testimony.

Congressman Russ Carnahan (D-MO)
House Transportation Committee
Aviation Subcommittee
Hearing on Airline Pensions: Avoiding Further Collapse
Opening Statement
June 22, 2005

- Thank you, Mr. Chairman.

- As we all know, the subject of airline pension plans has been in the news recently. The troubles faced by United Airlines and US Airways have become a source of great concern to airline employees across the country.

- Many of these employees will face hardship as a result of United's and US Airway's decision to terminate their pension plans.

- Although it is not the specific focus of this hearing, I suspect we will learn today that Congress needs to take steps to improve our nation's system of private pensions. Now, more than ever, it is important that we take steps to secure Americans' retirement. The experience of United and US Airways can be valuable learning tool in this process.

- I thank the Chairman and the Ranking Member for holding this hearing, and I look forward to hearing testimony from the witnesses today.

OPENING STATEMENT OF
THE HONORABLE JERRY F. COSTELLO
AVIATION SUBCOMMITTEE
AIRLINE PENSIONS: AVOIDING FURTHER COLLAPSE
JUNE 22, 2005

- I want to thank you, Chairman Mica, for calling today's hearing to examine the airline pension crisis. I fear that with the collapse of these airline pensions, and with the auto industry on the brink, companies will not be offering such benefits in the future.

- ERISA provided the framework for the Pension Benefit Guaranty Corporation (PBGC), which was created to protect the pensions of employees covered by private sector defined benefit plans. PBGC currently carries over 3,500 pension plans under its protection, which has given thousands of workers some measure of retirement security when their employer is no longer able to provide for their pension. However, the PBGC guaranteed benefits are often less than what the retirees expected to receive from their employer.

- As of September 2004, terminations by the steel and airline industries have accounted for over 67 percent of PBGC's claims. United's move to transfer its pensions to the PBGC is expected to prompt similar actions by other legacy air carriers, which are struggling to stay viable because of high costs, competition from airlines without substantial pension obligations and rising fuel costs. The PBGC is currently running a $23 billion deficit, with a potential exposure of billions more if other legacy airlines move to terminate their plans.

- A combination of factors contributed to the under-funding in defined benefit pension programs, including the dramatic slide in the stock market, low interest rates, and the steady decline of 30-year Treasury bond rates. However, a closer examination of the PBGC's current funding rules, which has allowed for the masking of the airlines' true pension deficiencies, is necessary.

- Under the PBGC rules, companies with under-funded pension plans were required to make additional contributions, the so-called "deficit reduction contributions (DRC)." In 2004, we provided relief for the airline and steel industries from having to make the full DRC payments so that these industries would have the ability to recover from financial distress. However, as we have seen with US Airways and United Airlines, that relief came a little too late to save their workers' pension plans.

- With continued pressure on the legacy airlines from low cost competition, high fuel costs and the end of the two-year moratorium on DRC pension contributions, we are coming dangerously close to seeing more bankruptcies in this industry, with the potential for further termination of worker's pension plans. I look forward to hearing from Air Line Pilots Association as well as the Association of Flight Attendants on the impact of the plan terminations at US Airways and United on their respective members, and their thoughts on moving ahead to protect remaining airline worker's pension benefits.

- There are also several bills that are currently under consideration this Congress to help prevent the further shedding of pension plans, not only by the airline industry, but by other industries as well. I am interested in the witnesses' views of these various bills and how they might aid in ensuring the continued viability of existing pension plans.

- Mr. Chairman, this hearing presents good opportunity to begin the discussion of how to provide employees retirement security, how to avoid future pension crises, and how to ensure the continued solvency of the PBGC. I look forward to the witness' testimony.

TESTIMONY OF

PATRICIA A. FRIEND
INTERNATIONAL PRESIDENT

ASSOCIATION OF FLIGHT ATTENDANTS –
CWA, AFL-CIO

BEFORE

THE SUBCOMMITTEE ON AVIATION OF THE
TRANSPORTATION AND INFRASTRUCTURE
COMMITTEE

U.S. HOUSE OF REPRESENTATIVES

WASHINGTON, DC

JUNE 22, 2005

Thank you, Mr. Chairman, for the invitation to testify today on the current serious pension crisis. I appreciate having the opportunity to share our views with the committee on this issue, an issue that has such a profound impact on hundreds of thousands of working women and men in the aviation industry. The pension crisis is especially important to the women and men who serve as flight attendants.

My name is Patricia Friend and I am the International President of the Association of Flight Attendants-CWA, AFL-CIO. AFA represents 46,000 active flight attendants at 24 airlines. Our active and retired flight attendants at United Airlines – numbering approximately 28,000 – are currently the only flight attendants at a major airline represented by AFA with a defined benefit pension plan. Let me repeat that only one, United Airlines, has the vestiges of a defined benefit plan.

As you all know, that changed early last month when a bankruptcy court judge ruled, at the request of United Airlines management, to approve an agreement between United and the Pension Benefit Guarantee Corporation under which the agency is expected to terminate our pension plan. We were shocked and outraged by this decision after the earlier announcement by the PBGC that our plan "can and should be maintained" as United emerges from bankruptcy. Instead of defending and preserving our pension plan, they announced in bankruptcy court that they intended to take over the flight attendant pension plan.

What changed? Why did the agency reverse course and abandon the flight attendant pension plan? There can be only one explanation: United agreed to pay the agency 1.5 billion dollars to settle its bankruptcy claim. That is not an outcome that this Congress ever envisioned when it enacted ERISA. That is an abuse that leaves thousands of flight attendants with only a fraction of the retirement they have earned.

We remain resolute in our determination to save our pension plan at United. For me, as a United flight attendant, and our members at United, both active and retired, this especially hits home.

Over the past several weeks and here today, we have heard some thoughtful and well-informed testimony today on the financial status of pension plans in the airline industry and the long-term viability of those plans. We have also heard about the financial ramifications of the United pension terminations – and potentially other pension terminations – on the financial health of the PBGC. Already over 20 billion dollars in debt, the PBGC will absorb as much as 9 billion dollars in additional debt from United's plans, and untold billions more as other airlines and other companies follow United's lead.

I would like to take a few moments to remind everyone here today that this issue has a human dimension, which so often gets overlooked in the important discussion of financial facts and figures. There are real people who are suffering or will suffer due to the profound reduction of promised retirement benefits. Many of our members are now looking at the possibility of working many years longer than they had intended. For those recently retired, many are now trying to determine how they can pay for the basic necessities of life. These are not careless people who failed to plan for their retirement. They did everything right – they worked hard, saved as much as they could, invested when possible. Their only mistake was one of trust: they trusted the retirement promises United made for decades.

United's decision, blessed by the bankruptcy court, to turn our pensions over to the PBGC means that over two thirds of United flight attendants will loose over one-half of their promised pension benefit. These same employees have made repeated financial concessions over the past several years to keep our airlines alive and profitable. Now they are trying hard just to survive and to provide for themselves and their families with a greatly reduced income. With the elimination of much of their guaranteed retirement income the burden is now even greater on them to save more for retirement. But, of course, saving more is nearly impossible because of the drastic reductions in salaries they have already been forced to agree to just to keep the airline flying.

For many, putting food on the table or setting aside money for retirement is a monthly decision. As one of our members recently stated, "The possible loss of hundreds of dollars a month in old age changes a dignified retirement into a subsistence-level retirement." Or, for another two of our members, a married couple that have together over 70 years of loyal service to the company, who had hoped to retire in seven years, find they now must work for at least an additional 15 years. For individuals who have had to work many years to finally make over $40,000 a year, a cut of hundreds of dollars and in some cases thousands of dollars a month is a severe blow. For some it means a rent payment will be missed, or a car payment, or that prescriptions will go unfilled. For others it means they must now re-enter the job market with skills that are no longer in demand.

I have had some Members of Congress ask me why we are fighting so hard to save our pensions. They say that United will not emerge from bankruptcy unless they terminate the pensions they promised to us and that we have earned over years of hard work and sacrifice. They've asked if we really think that liquidation of our company would be better for us in the long run. They have implied that we, as the obstinate labor union, by requesting that our pensions be saved, are only going to cause the eventual failure and liquidation of our employer. Let me remind the members of this Committee, that we, the employees that have given decades of our lives to this company, have much more at stake in seeing it survive than do most members of upper level management. They have come in to run the company for a few years and then leave and go to another industry. Or, in the case of United's Chief Executive Officer, Glenn Tilton, leave the company at any time and still collect his bankruptcy-court-protected $4.5 million pension plan, all while remaining the most highly compensated CEO in the industry even though he is at the helm of a carrier in bankruptcy. Where is the shared sacrifice in that equation?

As I stated, we have made hundreds and hundreds of millions of dollars in concessions to United management – and at other airlines – to see our carriers survive. We have borne the brunt of the bad business decisions made repeatedly by management at the airlines. We have reluctantly, but willingly, made those sacrifices at the bargaining table. Now, all we are fighting for at United is the one thing that we have worked so hard for over the years as a labor union – a guaranteed retirement income in return for years of dedicated service to the company.

Those most responsible for putting United and other airlines in the precarious financial situation they are in are refusing to make the management level cuts they promised. Or in the case of US Airways, where our members lost their pensions earlier this year, they are instituting management retention bonuses.

Again, I ask, where is the shared sacrifice? Why are those most at fault in driving our carriers into bankruptcy or near bankruptcy – management making bad business decisions based on bad business models – why are *they* the only ones not sharing in this sacrifice? They continue to line their pockets while we stand accused of wanting to see our lifelong employers go out of business, leaving us unemployed and with very few opportunities for new careers in the profession and industry we love. Unlike others, we cannot move from the oil industry to the airline industry to some other industry with a golden parachute to help us on our way.

When one of our members asked Glenn Tilton why he thought it was appropriate to keep his 4.5 million dollar pension when we were being asked to give up ours, he said simply: "it's part of my contract." Well, excuse me for thinking that remark a little arrogant, but you should know – and Mr. Tilton should know – my pension is part of my contract too.

<u>BACKGROUND AND TIMELINE OF PENSION TERMINATION</u>

Let me give you some background on the path we have taken over the past several months that have led up to this point. On January 8th, 2005, AFA and United reached a tentative agreement, providing the company with $130 million in additional annual savings between 2005 and 2010 ("2005-2010 Agreement"). In a side letter to the 2005-2010 Agreement, AFA and United agreed to "continue to meet and confer regarding the Defined Benefit Plan." That letter further provided that, if the parties were unable to reach agreement on the pension issue by April 11, United would re-file its Section 1113(c) motion specifically in regard to the pension issue.

On January 31, United flight attendants ratified the 2005-1010 Agreement by a margin of 56% to 44%. Over 70% of eligible flight attendants participated in the ratification vote, the highest turnout for any vote conducted by the Union in the course of United bankruptcy. The same day, immediately after the ratification vote was announced, the Bankruptcy Court approved the 2005-1010 Agreement.

In late January, even before the 2005-1010 Agreement was ratified, AFA initiated discussions with the PBGC, seeing to enlist the agency in its effort to find alternative funding for the flight attendant pension plan and avoid termination. PBGC has consistently maintained that the flight attendant plan was "affordable" and could be "retained in a successful reorganization." According to the PBGC's expert, Michael Kramer, "[u]nder the Gershwin 5.0F projections, the Company has sufficient liquidity and free cash flow to support at least one of the pension Plans currently in place, namely the F[light] A[ttendant] plan, even without application for any waivers." At a January 27, 2005 meeting with AFA, the PBGC indicated that it was willing to explore a wide range of options to plan termination.

At the same time, AFA attempted, largely in vain to engage the Company in negotiations over alternatives to plan termination. As the company itself recognized, the purpose of the three-month hiatus from litigation was to negotiate over "termination alternatives." Indeed, the Company told AFA that it "remain[ed] willing to consider any termination alternatives." Despite its professed openness to consider termination alternatives, United Airlines management demonstrated very little real willingness to engage in meaningful negotiations with the AFA about saving the flight attendant plan.

The PBGC, on the other hand, throughout this period, encouraged AFA's efforts to find alternative funding. During February and March, AFA regularly consulted with the

PBGC, as we developed a proposal that identified sufficient alternative funding to save our pension plan.

AFA outlined its proposal in a March 30 letter to Bradley Belt, the Executive Director of the PBGC. The proposal stated that "AFA is willing to contribute, or cause to be contributed to the Plan...a portion of the amounts necessary to fund the unfounded pension benefit obligation." The proposal in summary included:

> The value of UAL Common Stock to be received in bankruptcy based upon (1) AFA's unsecured claim arising from prior wage reductions, and (2) the estimated amount of the PBGC funding obligation if the Plan were terminated.
>
> The value of UAL's proposed payments to a Flight Attendant Defined Contribution Plan.
>
> Note of like tenor to the note received by the United Air Line Pilots Association from UAL in consideration for termination of the pilots' Defined Benefit Plan.
>
> PBGC contribution, either through a cash contribution, loan guarantee, pension bond or other acceptable consideration.

In his April 4 reply, Belt characterized AFA's proposal as "constructive" and reiterated the agency's position "that the AFA plan can and should be maintained by the company upon emergence from Chapter 11." Mr. Belt added that: "Based upon available information, we continue to believe that the interests of participants and the pension insurance program would best be served by the continuance of the AFA plan." In closing, he encouraged further work between the agency and AFA to resolve the pension funding issue.

On April 11, United re-filed its Section 1113 motion, seeking authority to reject the collective bargaining agreements' contractual bar to a distress termination.

On April 14, PBGC filed an emergency motion to postpone consideration of United's motion for distress terminations of its defined benefit plans, calling United's motion "premature" and arguing that United Airlines had failed to show that the plans were not salvageable. The PBGC explained that, until United

> "provides an updated business plan…and file[s] its plan of reorganization…PBGC cannot even determine its position on whether United can afford to maintain the Pension Plans coming out of bankruptcy." On April 15, PBGC served written discovery on Untied requesting "[a]ll documents relating to the affordability of the Flight Attendant Plan."

Then, on April 22, United announced that it had reached an agreement with the PBGC, which would result in the termination of all four defined benefit plans. Pursuant to the Agreement, United is to provide three tranches of securities with a total value of $1.5 billion, ($500 million of which is contingent on certain conditions subsequent), to the PBGC in exchange for the PBGC terminating the four pension plans and settling certain other claims. By the terms of the Agreement, the PBGC agrees that "[a]s soon as practicable after the date that the Bankruptcy Court enters an order approving the Agreement…PBGC staff will initiate termination under 29 U.S.C. sect. 1342 of the Flight Attendant and MA&PC Plans." The agreement also provides that "United shall not establish any new ERISA-qualified defined benefit plans for a period of five years after the Exit Date."

The immediate consequence of the agreement approved by the Bankruptcy Court is that it would do away with the "need" for further Section 1113 negotiations and the hearing under Section 1113 and ERISA Section 4041. As the company says in its Motion, "[i]f United did not enter into the Agreement, it would have to run the risks associated with litigating a sharply contested ERISA Section 4041 sponsor-initiated distress termination of all four Pension Plans, together with the Section 1113(c) trial."

Further the public statements of the Company and the PBGC heralding the agreement leave no doubt that both parties entered in to the agreement fully intending and expecting that, pending Court approval, the agreement would result in termination. In the PBGC's April 22 press release, Executive Director Belt hailed the "reaching [of] a settlement," "[u]nder the terms [of which]...," according to the press release, "the PBGC would terminate and become the trustee of the company's four pension plans." Likewise, the company announced on April 22 that "the company and the [PBGC} have reached an agreement for the agency to terminate all of United defined benefit pension plans."

Our concerns with United's termination of the flight attendant pension plan and the PBGC's decision to not challenge the termination are numerous. However, simply put, we do not believe that termination of the pension is necessary for the survival of United airlines. As I have outlined in the background above, we have tried repeatedly to negotiate with the company on other alternatives to save our defined benefit pension plan or to explore means to preserve the plan. In fact, we are the only work group that even offered to pay for part of the plan ourselves. However, each and every time United has told us that there is no option available other than termination. They have refused to look at the pension plans individually, but rather, prefer to lump them all together. We believe that each plan should be judged on its own viability – both ERISA and the bankruptcy code envision such an evaluation. However, the deal struck between United and the PBGC pre-empted just such a review.

We were completely blindsided by the PBGC's decision, after accepting 1.5 billion dollars from United, to allow termination of our plan. This was especially troubling in light of the fact that on April 4th, the PBGC, in a letter to AFA's actuaries, which I highlighted above, stated that the PBGC believed that, and I quote again, "...the AFA plan can and should be maintained by the company upon emergence from Chapter 11.

Based upon available information, we continue to believe that the interests of the participants and the pension insurance program would best be served by the continuance of the AFA plan."

Why did the PBGC change its position so shortly after that letter? That is a question for which no one has an adequate answer. In fact, in a *USA Today* article from mid-May, a spokesperson for the PBGC stated that the PBGC still believed that it would be best for the flight attendants and the government if United did not terminate the plan. The spokesperson went on to reiterate that they believed that United would eventually convince the bankruptcy court judge to allow for termination over the agency's objections. Does this not go counter to the provisions of ERISA, when creating the PBGC outlined that the number one purpose of the PBGC was "to encourage the continuation and maintenance of voluntary private pension plans for the benefit of their participants?" Let me point out that it states "for the benefit of their participants" not "for the benefit of the corporation."

By accepting a 1.5 billion dollar payment and then standing silently by, I believe that the PBGC failed in its number one purpose of encouraging the continuation and maintenance of voluntary private pension plans for the benefit of their participants. The PBGC simply turned its back on its legal obligations and obligation to the participants of United's pension plans. This Congress should have been outraged by the action of the PBGC. Instead, the overwhelming majority of Congress, both Republicans and Democrats, has acted like the PBGC and, to date, stood silently by while hundreds of thousands of United employees and retirees see their pensions decimated.

If United management is successful in their efforts to terminate our pension plans, no one should be under any illusion: all the other legacy carriers *will* attempt to dump their pension plans as well. With an already huge deficit of $23 billion in unfunded liabilities, the PBGC will simply find itself deeper and deeper in debt. If you, the distinguished members of this Committee, and United States Representatives allow for this to go forward, you are simply creating the possibility of a massive taxpayer bailout of the

PBGC at a time when the federal government can least afford such an expense. That responsibility is in your hands.

As I stated at the beginning of my testimony, our members at United are the only remaining group at a major airline represented by AFA with a defined benefit pension plan. There has been much discussion today about how we can achieve a long-term fix to the pension crisis rocking the airline industry. There have been some reasonable proposals brought forward which deserve some serious debate and possible enactment into law. Ideas such as extending the amortization period for payments and allowing companies to pay in more during economically profitable years, among other suggestions that have been brought forward are all possibilities that deserve serious debate and may help solve the long term funding problems for pensions.

However, if something is not done immediately to stop the termination of United's pension plans, AFA cannot be a part of those long-term fix discussions. If nothing is done now, we will no longer represent any workers with a defined benefit pension plan. That is why I strongly urge each and every member of this Committee to cosponsor H.R. 2327, the Stop Terminating Our Pensions Act, or STOP Act. This legislation, versions of which have been introduced in both the House and Senate, would only cover those plans whose plan sponsors are in bankruptcy reorganization currently, and whose unfunded liability on a termination basis is $1 billion or more. All four union employee pension plans at United are covered by these caveats.

The bill would put in place a moratorium for any termination of covered plans initiated by the PBGC under ERISA 4042. It does not affect terminations under ERISA 4041. The essential difference between these sections is whether workers have a say in the process. Under 4041, a termination is voluntary and allowed only after the employer has fully bargained with the unions in good faith. Under 4042, the PBGC may ignore the collective bargaining process and terminate plans on its own. In the United case, the PBGC has struck a deal with the employer to terminate the plans without regard to the collective bargaining process.

The length of the moratorium is six months. This would allow Congress the valuable time needed to explore further solutions to the crisis at United. It allows time for the employer and the unions to honor the collective bargaining process and seek out alternative solutions to plan termination.

Passage of this legislation is needed immediately for us to return to the bargaining table with United Airlines in order to find an internal solution to this problem. We strongly believe that the flight attendant pension plan can be saved and is viable, as the PBGC itself recently stated. We simply want every available opportunity to find a consensus with the company. This six-month moratorium would give you, the distinguished members of the Committee and the rest of your House colleagues, the time to debate and consider the various proposals to strengthen and protect defined benefit pension plans in this country. You can help prevent hundreds of thousands of other workers from loosing their pensions and ten of billions of dollars being dumped on the taxpayers by allowing this moratorium to pass.

Please give us the time we need to try and save our pensions. I urge the House of Representatives to consider and pass H.R. 2327, the STOP Act as quickly as possible. If you do not, then you have turned your backs on the over 120,000 United employees who are now facing a bleak and uncertain retirement future.

I would in closing, like to leave you with just some of the testimony of the approximately 2,000 United employees that submitted their comments and personal stories to Representative George Miller's first ever online hearing on this issue, held by the Democrats of the House Education and Workforce Committee. I hope that as you read these personal stories that you will remember that this pension crisis has a profound human impact.

Dear Congressman Miller,

My name is Kathy Charron and I'm a retired F/A from UAL. I was injured on the airplane in April of 1999. After numerous and various types of therapy, I realized I probably wouldn't be able to return to flying and took the June 30, 2003 retirement with 2,500 of my flying partners to preserve my medical coverage. Three months later my husband was diagnosed with lung cancer. He passed away on March 16th of this year. While he was ill, he collected disability and Social Security. Now that's he's gone, the only income I have is my tiny pension of $1,400 a month, after 33 years of good, loyal service to my passengers and UAL. Even with medical insurance, I'm buried in medical bills from my husband's illness and now my doctor is talking surgery for my work related illness. I thought I had figured out how to make ends meet with my pension intact. Now, I don't know what I'm going to do. I can't return to flying, which I started doing when I was barely 20 yrs old. Any suggestion Mr. Tilton?

Sincerely,
Kathy Charron
San Leandro, CA

Dear Congressman Miller,

I retired from United Airlines with 30 years of service when they entered Chapter 11. I did this because I thought it would save my hard-earned pension benefits. I have made some significant life changes over the past few years to position my family and myself to be able to live on my pension plus my new employment. We moved to Florida, downsized, and paid our bills. My pension is $1,800 a month and it could be reduced by the PBGC to $800 a month, and I will not be able to make ends meet even in our modest lifestyle.

I can well remember as a young "stewardess" how rewarding it was to have pension guarantees added to our benefits. We were finally being acknowledged as wage earners and contributing to the long-term economic health of the corporation. In my 30-year airline career, I have watched America get richer and American workers get poorer, we must do something to stop this greed by the corporations and this precedent-setting decision to renege on their commitment to their retirees.

Thank you for taking a stand on this crucial issue.

Sincerely,
Judy Kersch
Punta Gorda, Florida

Dear Congressman Miller,

I am asking you to please not allow UAL to jeopardize our pensions. I have worked for United for 26 years. I am 50 now. I do not have the time to make up what I will lose if the pensions are passed to the PBGC. I have a disabled husband and three children, ages 19,17 and 15. I have worked long and hard to earn my promised pension. I am based in Denver, and have been for most of my career. Before United is allowed to unload our pensions, the executives who have run our airline into the ground should have to give up their promised pensions and executive bonuses. We have sacrificed wages, work rules, and more recently, for some, our lives for this company and were promised something in return. It is deplorable that such greed among our CEOs is allowed to run rampant. This should not be allowed to happen. No other industry rewards its leaders for mismanagement and poor business performance. Please do not allow this to happen. My life and the future of my family depend on our representative's actions. Thank you.

Sincerely,
Elizabeth Kelly
Golden, Colorado

Dear Congressman Miller,

I worked for UAL 31 years and in December 2002, I realized I had to retire if I wanted to save my pension and medical benefits. I decided to retire in March 2003 and in doing so I was penalized 21% for retiring before 60 years old. My husband was diagnosed with cancer March 1, 2004 and he died December 12,

2004. My house is up for sale because I cannot afford it anymore. My husband's illness devastated us financially. If my pension is reduced any more I will not be able to afford a small apartment. I am hoping Congressman Miller that you will be able to help us protect what little pension I have......thank you .

Sincerely,
Cheryl Lane
Darien, Connecticut

Dear Congressman Miller,

My name is Sharon Anthony, and I live in Carlsbad, Ca. I retired three years ago from UAL with 39 years and 9 months seniority. I was based out of LAX. The potential termination of my pension would greatly impact the security of my life. I am a single parent, with a mentally challenged son. Any reduction in my pension may mean that I would have to sell my home, and uproot son and myself.

Sincerely,
Sharon Anthony
Carlsbad, CA

Dear Congressman Miller,

My name is Penny Brill. I have been a United flight attendant since 4/4/77, and I am based in Los Angeles. With 28 years seniority and having been an employee eligible for the defined pension plan, I now stand to receive 52% of the benefit to be paid to a flight attendant that retires at 50 years old. (The PBGC lists that amount at approximately $1,340 per month, so I am eligible to receive $670.) Employees many years junior to me, who have contributed much less, but who are older will receive more than one thousand dollars more a month than me, simply because of their age. With our retirement fund only 33% underfunded, it is a puzzle to us who would like to preserve it, why United can't place the money with other institutions and then fund it when they become profitable again. It is curious that there is a bill to make individuals who are filing for bankruptcy accountable, and yet a large corporation that gives bonuses to senior management and officers, and protects the pension of it's newest CEO (4.5 million dollars), is able to walk away completely from a responsibility it has to over 120,000 current and retired employees. It also does not square with this Administration, who would like to privatize social security, to have a government formed agency to deal with the monies that employees have already worked for with the promise that they would be there for us to receive. Under the PBGC's table, I would have to fly for United for another 10 years, until I am 60, just to receive 100% of the benefit paid to a 50 year old! We have taken over a 20% pay decrease and are now flying 20% more to make the same amount of money. Where will we get the extra money we need to start preparing for a new retirement benefit in the form of a "defined contribution" plan? And how much can you possibly save when you only have 10-15 years more to work and a salary that has been lowered to 1991 levels?

My husband has always been self-employed and my retirement was "our retirement." This is unfair and unjust. United also disenfranchised thousands of us when they arbitrarily changed the early retirement age from what it had always been at 50 years old, to 55 years old in May of 2003. The federal government would not give us federal backing for a loan guarantee of 550 million dollars back in 2003 and now they are prepared to let the PBGC take over the responsibility of a pension plan that will cost 9.8 billion dollars to execute! Why?

The PBGC stated that it must consider each plan on an individual basis. The flight attendant group constitutes less than 7% of the total operating cost of United Airlines. It is not our pension plan that is preventing us from exiting from bankruptcy. Please stop this maneuvering to prevent us our earned benefit. Thank you!

Sincerely,
Penny Brill
San Pedro, California 90731

Dear Congressman Miller,

The deal made between United Airlines and the PBGC will leave me with little hope of ever retiring. The loss to my family and me will be approximately 50% of my income. It seems that many people are unaware of the effect, in conjunction with the enormous cuts to UAL employees' pay and benefits, this will have on my ability to contribute to my retirement in the future. It's not enough that we have made sacrifices along the way in lieu of pension promises, or that we have taken heavy pay cuts in bankruptcy while UAL management has guaranteed their own pensions with our pay cuts and concessions. But now I, as a taxpayer, have to pay for the shortfall of funds. And it seems there is no end in sight, for the likelihood of other corporations doing the same thing is imminent. Many people's lives will be devastated. Please Help!

Sincerely,
Esther Zavala
Dallas, Texas

Dear Congressman Miller,

When I began my flying career 23 years ago, it was because I had a true fascination with flying. I have always been a day late and a dollar short, when it came to timing in my life. I started a career as a Flight Attendant – a B-scale career that is – with half wages for my first five full years. It was at this time that all I could do was get by with the help of my parents and three fellow Flight Attendants sharing a one-bedroom apartment in Chicago. See, United Airlines management had just introduced a two-tier pay scale and I was once again a day late. So, I muddled through those five years believing things would only get better. Once I merged with the normal pay scale in my 6th year, it was then and only then that I was able to start saving a small amount into a 401k; with zero match from my employer. Most of my deductions went toward United Stock which later proved to be a very costly mistake.

Then, with the swipe of a bankruptcy pen I lost 90% of my 401k, but yet UAL executive had enough time to unload their precious UAL stock before the employees had a chance to realize what was happening. My 401K was now only worth $4,600 after 14 years of saving.

Well at least I have my pension, or so I thought. My $2,100 dollars a month I was to scheduled receive at age 62 could be reduced to a payment of $611 a month with the PBGC. As UAL Management walks freely with their salaries and pensions in tact, I walk around imprisoned by a management whose philosophy has always been let the beatings continue until morale improves.

My life has been turned upside down and I am in a state of shock I am currently on blood pressure medication and sedatives to get me through my days and nights while I figure out how a 43 year old man starts a new career and tries to cope with rising inflation while my salary takes drastic cuts.

Sincerely,
David Fournier
Biddeford ME

Dear Congressman Miller,

I am a 26 year Flight Attendant at United who is just returning from a 4.5 year absence. My wife Toni was also a Flight Attendant, joining UAL in 78. Sadly, she passed away this past November from ALS, better known as Lou Gehrig's disease. It is important that you know that I did not earn a penny for all the years I spent caring for my wife, which I was privileged to do. Aside from my pension, my social security has suffered as well. As I was focusing on my wife's care, I was comforted to know that my pension was at least going to be there when I returned.

The current situation is an outrage. In addition, there is the possibility that the pension that my wife worked so hard for might now be denied to me as well if United is allowed to get away with this thievery. Taking away the pension of my beloved wife is totally unacceptable. Do not let this happen! If you would like to read more about Toni, please visit www.wingsoverwallstreet.org.
Please Congressman, won't you help me and all the hardworking employees of United?

Sincerely,
Warren Schiffer
Long Beach, New York 11561

Dear Congressman Miller,

As a 27-year veteran of United Airlines, I thought that I had my future secure. I am a 51-year-old single female, living in Ruidoso, NM and based in Hong Kong. In nine more years, at our minimum retirement age of 60, I had planned to retire. To be financially ready, I had purchased my dream home and I had saved and planned carefully to have it paid off by the time I retired. After dedicating 36 years as a loyal employee to United, my golden years would be set. Now that United has been allowed to default my pension to the PBCG it seems that I stand to lose 47% of my retirement.

I can no longer afford to live in my dream home after I retire. Even with my mortgage paid off, I will have to sell. In fact, I will not be able to live on my retirement. At age 60, I will be forced to get another job for the rest of my life just to have a roof over my head and to eat. This is not the dream that I had planned and worked so hard to achieve. Please help to put a stop to this corporate greed.

Sincerely,
Cheri Breeding
Ruidoso, New Mexico

Dear Congressman Miller,

I would like to take just a moment of your time to address the potential termination of my retirement plan with United Airlines and to tell you a little bit about myself. As you know, this comes at a time when revisions to the overall Social Security system are being considered. I am a United Airlines Purser/Flight Attendant and a college graduate who by choice has pursued a career making a salary less than that of my colleagues. I have always lived below my means, and never planned to rely solely on my SS benefits. Since my 401k's inception I have invested in 100% in the company's stock fund; not brilliant, I agree. I am single with high medical bills to boot. I just wanted to express how sometimes even with the best intentions of being a responsible investor for my future the termination of United Airlines pension plan will no doubt have a huge detrimental impact on my future. I thank you for your time and consideration.

Sincerely,
Barbara Allen
Pompano Beach, Florida

Dear Congressman Miller,

I have worked for United Airlines and Pan Am for 16 years, which is most of my adult working life. I have worked very hard and I feel I have earned a decent pension. I have forgone many other opportunities because I felt that, at United Airlines, I was working towards a secure future for myself.

Now I find myself, at age 45, after devoting most of my best earning years to United, that I will receive a reduced pension. In order to be able to provide for myself in my retirement, I will have to change careers as United is taking everything from me.

Yes, I have saved. I have a 401(k) and a Roth IRA. But that will not be enough and this pension is something that I have earned - it is not charity. I feel I am being robbed, after so many years of hard work. Where is the American Dream? I was raised to believe that this was the land of opportunity, that if I worked hard I would get ahead. It seems this is no longer true, and that is the hardest thing for me to accept.

Sincerely,
Judith Cuneo

Dear Congressman Miller,

Thank you so much for taking an interest in the pension situation at United Airlines and doing your job as a Representative of the people to seek an alternative through HR2327. It is reprehensible that UAL management can finagle a deal with our current Administration to foster their own financial interests at the expense of thousands of loyal, hard working employees. We have kept faith in our company's management for too long. Ever the optimistic, trusting and proud workforce, we are now faced with financial ruin.

I have been a UAL Flight Attendant for over 20 years, based in Seattle, living in Olympia, WA. I now look at starting over in a new career or hanging on at UAL for undoubtedly more abuse and a meager $480/mo. retirement if the PBGC takes over. Yes, I have children. Yes, I have financial responsibilities, as does everyone. I haven't worked for UAL to become rich, as it seems our shameless parade of business managers have done. My pursuit of the American Dream has become merely finding a way to survive this American Nightmare.

All the employees of UAL have made extreme sacrifices in hopes that our company will regain solvency. But to what end? The actions of our management are certainly unethical, uncaring, and greed-driven. In my opinion they should also be criminal. Something must be done to stop these self-serving corporate rulers and politicians from continuing to scam decent American workers. I am ashamed by the disgraceful behavior of our elected officials and all of corporate America, who think they can abuse others to make themselves wealthier, eventually eliminating the middle class of our society. What morals do they have? Do they think we aren't noticing? Can they get away with this? Something must be done.

Sincerely,
Rita Sammons
Olympia, Washington

Dear Congressman Miller,

I worked for United Airlines for twenty-four years and five months. I retired knowing I'd get the pension I deserved. I'm now 57 years old and live in New York City. The monies promised to me were to go towards paying my monthly maintenance on my coop apartment. Without my full pension ($1,200/mo.), I shall be forced to sell my studio apartment and move out of the city.

Had I known that my pension would be cut I wouldn't have retired in spite of the worsening labor relations at United. Please assist me in holding United to the responsibility to pay out my full pension. The level of corporate greed in our country is regrettable.

I'm lucky because I can always sell my apartment and leave the city. But that is not what I want to do. I want to live in this great city for the rest of my life. I planned on it. Now, it looks as if I made a huge mistake in counting on my hard-earned pension. Your assistance in this urgent matter is greatly appreciated.

Sincerely,
James O'Connor
New York, New York

Dear Congressman Miller,

I am a retired United flight attendant, living on my United pension payment and one from Pan American World Airways, through the PBGC. They total approximately $1,170 per month. I worked for Pan Am for 16 years, and for United for 17.Obviously, if my United pension check were to be reduced, I would be severely impacted. I live with my elderly parents at this time, and the only thing that will allow me to live the rest of my life above the poverty level is the inheritance I will get from them. We live in San Diego CA, and I do not expect to be able to afford to live here after they are gone. If my pension is cut, I don't see how I could afford to live anywhere else either. That's pretty horrible to have to say after serving a career of 33 years.

Sincerely,
Helen Dowdy
La Mesa, California

Dear Congressman Miller,

I would like to thank you for recognizing the unfair & demoralizing atmosphere at United Airlines and for helping us hold on to what has been promised to us. I started my career as a flight attendant in 1967 flying out of DCA and retired 34.5 yrs. later in 2002 from our Chicago domicile. I loved my job, but had to retire since I could not return to work from a medical leave of absence. It was devastating, but I did have the guaranty of a small pension along with medical benefits. My husband works for our local park district and my pension has helped with expenses.

We have been blessed to adopt 2 little girls, ages 5 & 8. The knowledge that they would have medical benefits till age 21 has always been in the back of my mind. The thought of trying to pay medical premiums on a drastically reduced pension is frightening. The thought of no insurance keeps me awake at night. I am not certain anyone would insure me with my medical conditions, and I am unable to find a job. I did everything the way I was supposed to, fully expecting my retirement & benefits to be intact. I am so angry to think that management has no concern for our situation or us as people. Their words are so cheap and empty. They did not build this airline, nor have they continued to build it. They have only plundered this magnificent airline and degraded her employees while taking huge salaries and perks for themselves. This is the most unjust & unsettling situation & has caused so many traumas in all of our lives.

Thank you again for hearing my story.

Sincerely,
Anita Jalbert
Belvidere, Illinois

Dear Congressman Miller,

I retired in June 2003 because United Airlines was in bankruptcy and my flying career had changed drastically, commuting from Dallas to ORD where I was based. I have and did at the time have 3 teenagers to put through college. I was told my medical insurance would cost me $53.00/mo. which since has been doubled. Additionally, I was told that I would receive a pension check at so much per month, if I were to retire at that time (age 51). I did the figures and found that it would be worth the cut if I were home with my children. Right after I retired, my husband lost his tech job and he was without work for quite some time. We are still struggling to pay back what we owe from 2003. UAL's word was solid that if we retired we would be assured a pension and medical! I would have stayed longer with UAL if I know they would take away what was earned and promised for more than 27 years!

Sincerely,
Jean Ryan

Dear Congressman Miller,

After 34 years as a SFO-based United Airlines flight attendant, I was told in 2003 that if I felt I could not work until age 65/Medicare, then I should retire before the July 1st deadline. United said I would most likely not be able to afford the projected rise in health insurance rates they intended to impose. But they would not make changes in retiree rates. They lied.

When I considered my chronic respiratory problems (visualize debilitating nosebleeds at the end of most flights) paired with knee problems (34 years of deep knee-bends into food carts), I realized I could not hope to work to age 65 and would be forced to retire at age 56 even though I had a few good years still in me and hundreds of hours of sick leave bank. The promised health care premium only lasted a few months.

My husband, a United mechanic for 34 years, lost at least $75,000 of his pay into the failed ESOP. We anticipate that, should the PBGC take over United's pensions, our household "income" will decrease $1,200 per month, possibly more. We took less pay for 68 combined years to negotiate and secure our pension payments. United assured us the pension was overfunded. United would rather pay high-priced lawyers and use bankruptcy laws than provide financial security to the employees who earned it. I was also part of a discrimination lawsuit against United. The judge issued a multi-million dollar award and United has yet to pay a penny.

We have just completed a (balloon) re-finance of our home in Calif. At some time 3-5 years from now, we will be forced to sell our home and move to an area with less expensive housing. However, we will need to be here as long as possible to provide on-going attention for one parent diagnosed with Alzheimer's and whose health care insurance is not portable. These were supposed to be years of comfort. It is difficult to attempt to enter the work force as you near age 60. Every day is an emotional roller coaster as we wait for United and the bankruptcy court to "drop the rest of the shoes".

I feel assaulted and shell-shocked on a daily basis.

Sincerely,
Noreene Koan
Belmont, California

Dear Congressman Miller,

I worked as a flight attendant for United Airlines for 30 years and (at age 50) was forced to make the painful decision to retire 10 years earlier than my plan (even though I was not financially prepared to do so) due to the bankruptcy of United. Those of us who made the decision to retire under the old contract did so in order to preserve our pensions and health care benefits, which were being threatened. Immediately after retirement, both were threatened again. The pension that I now have is clearly not enough to live on (especially in California) and I am grateful that I am still physically able to work as I am now faced with starting a new career at age 50. If I had known this was going to happen, I would have made many different life decisions over the years. I would have invested differently, I would have pursued an education to prepare myself for a different career path. I probably wouldn't even have chosen United to work for if I'd known all the benefits I was promised when hired and worked so hard for my entire life would be taken away right when I was finally able to collect. This is the final slap in the face after a lifetime of commitment and service to a company who didn't even tell me goodbye or wish me well when I retired. My last trip came and went without even an acknowledgement from my supervisor. No one ever even missed me!

My heart has not only been broken by United Airlines, but also by a government whose corporate bankruptcy laws protect the interests of big business at the expense of working class American citizens whose consumer spending supports these big corporations. I am disillusioned and feel heaviness in my heart when I think about the retirees who are older than me, who are aged and in poor health and have no recourse of going back to work when their incomes are taken away. Not only are their pensions being threatened, but the government is threatening their Social Security as well. What will these people do?

The long-term effects of this cause me great concern. If United Airlines gets away with this, how long will it be before every corporation in America follows suit? The PBGC will not be able to handle claims of this magnitude, so it is being set up to fail at the very goal it was set up to achieve. I cannot believe this is happening at a time when the largest single segment of the population (the baby boomers) are reaching retirement age and facing spending their senior years in poverty. This is, indeed, a very sad time for American working families.

Sincerely,
Cathy Wright
Oxnard, California

Dear Congressman Miller,

When an individual has been working for, and shown dedication to a company for 27 yrs., as I have, one expects to receive a certain retirement. To all of a sudden be hit with the realization that , in 4-6 yrs., when I was planning to retire (between 60-62 yrs. old), my promised amount will now be cut by 1/3 to 1/2, is a frightening possibility. At 56 yrs. of age, I am too old to embark on a new career and even setting aside as much extra money as I can, will never equal all that I am losing.

How is it, that the worker bees of all these American corporations, can be asked to give, give and give some more and the upper management is allowed to walk off, with no reduction in pension, benefits, bonuses, etc.?!!? There is something wrong with the laws as they now exist, that protects the big shots, but does nothing to protect the people who toil and give their all, only to be left with nothing or a whole lot less. On behalf of all my flying partners, please help us, before it is too late!! Many thanks for your work on our behalf - it is so very appreciated!!

Sincerely,
Ilse Epple

Dear Congressman Miller,

Thank you for allowing me and my colleagues the opportunity to tell Congress what will happen if we lose our pensions. In my case, as I am under fifty, I stand to lose about two-thirds of my pension payment when I am actually eligible to receive it. I would have made approximately $2,000.00/month and with a PBGC takeover I will make as little as $700.00/month.

I want you to know that this pension is not an entitlement but something I have earned and paid for during my career at UAL. In 2003, my flying partners and I gave up 65 million dollars per year in our contract, as AFA agreed to reduce the pension formula, in the hope this would allow the company to exit bankruptcy. So far AFA has not seen a credible plan to exit and we are concerned the direction the management is taking with this

I turn 47 on May 27th and when my husband asked me what I wanted for my birthday, I looked at him and said, "I want my pension." This affects him, too. This termination will affect all Americans if United is allowed to proceed down this course.

Sincerely,
Terry Sousoures
San Mateo, California

Dear Congressman Miller,

Thank you for listening to United Airlines flight attendants this week. I live in Livermore, California and am based out of San Francisco. I have worked for United for 10 years and was proud to say that part of my salary included a pension. United also offers a 401k program, but never "matched" because they claimed to offer us a pension. Please note that my husband's company's pension plan was terminated last year (U.S. Foodservice). Both of us started working at companies under the impression that we'd retire with a pension.

Thank you very much for fighting to keep our pensions. You are a true politician by working for the people.

Sincerely,
Beth Rasmussen
Livermore, California

Dear Congressman Miller,

My name is Lolita Coppage and I had an early retirement due to illness. As a result of flying, I developed vertigo. Until I am back at 75% functioning somewhat normal, I will be depending on my pension 100%. I have 20 and one-half years of flying. I receive 980.00 per month, of which, 230.00 is taken out for health insurance. I have had to file bankruptcy, sell my furniture, and move out of the house I spent my life savings on. I'm ineligible for Social Security disability, since I can work to some extent. However, due to the limitations the illness puts on by abilities, I am unable to work much. What am I supposed to do? We have a government that speaks of morality, yet they allow CEO's to receive "Golden Parachutes."

Sincerely,
Lolita Coppage
Chicago, Illinois

Dear Congressman Miller,

I am an active United Airlines flight attendant with 16 years of service with the company. I thank you for your courage to step up to help preserve the future that many of us have worked so hard for. I stand to lose the most with my seniority since I am still 18 years from retiring age. To make matters worse, I can't collect full social security for another 25 years. I have a 7 year old and a husband who is self-employed with basic minimum IRA. We have been planning for our future retirement, but the real possibility of losing more than half my pension would affect us greatly. It saddens and angers me that 16 years of service will go to waste. It is hard for me to understand how a company can just decide one day to affect so many lives and futures with no conscience. All the employees have given so much already for our company's survival and management wants more without their pensions and compensation being affected. It makes me angry and I hope HR 2327 will send a message that enough is enough. I thank you for your support and understanding.

Sincerely,
Cindy Ahn-Thurber
Mesa, Arizona

Dear Congressman Miller,

I am a retired United Flight Attendant and I'm still in shock as to what has happened to my company. I flew for United for close to 40 years and had to retire for medical reasons that were the result of my job, which of course they denied. I had hoped to retire so we could do some traveling, but all of that has changed since my disability has become worse.

When I first started to fly for United I was so proud to be a part of this company but through the years I see that all upper management cared about was their salaries and bonuses. Now I am truly ashamed at what they are doing to their employees. My husband and I were counting on my pension to help pay for medical bills.

United has let me down big time and why the government can't see this makes me wonder. To let thousands of employees down like this is unbelievable. Of course they will get their pensions and bonuses even though the company is trying to get out of bankruptcy.

Thank you, Congressman Miller, for taking up this critical issue.

Sincerely,
Arleen Jasmer-Davidson
Tenino, Washington

Dear Congressman Miller,

I've been told that a personal face is needed to help us in our fight to preserve our pensions. Well, I'm one of those faces and what's happened at United Airlines will impact my future in a very real way. I've spent almost my entire adult life at United-- 21 years to be exact. I went into this thinking that United and I had an agreement. And due to some dire circumstances and poor decision-making, my security at retirement has been all but ruined.

I find myself now, at the age of 47, in graduate school, ready to start a new profession. This I must do since United has broken its promise to me and so many others who relied on them. I've always believed in self-sufficiency and independence. So three years before my 50th birthday, I must leave a job I've loved because I won't be able to live the way I'd hoped to in retirement.

The part that makes me angry, is that the pain has not been spread around at United. Those at the top have taken care of their futures, in spite of what they say is a necessary component to the company's survival. I've had it with the rhetoric and lies. It's just not fair, ethical, or moral. The face of United is its people, and we've been scammed. I gratefully respect your consideration in this matter.

Ita Luehrsen
La Grange, IL

Dear Congressman Miller,

I am writing you to tell you why I need my pension. I live in West Chester, PA and retired from UAL in 2004 after 40 years of service. I was injured twice in turbulence and now suffer from spinal stenosis and osteoarthritis. In addition, I had a stroke on September 11, 2001. Due to these events, I am unable to work. In fact, I was on disability for the last several years.

Due to uncertainty about the future of UAL, I retired in 2004 because I believed that was the best way to preserve my pension. Since then, the basic healthcare premium has increased and I'm being forced to pay $3,000 in additional premiums that UAL forgot to bill me for.

Now, UAL has turned my pension over to the PBGC and it is uncertain how my pension will be impacted. The senior executives who made the decisions to delay payments to the pension fund and ultimately to put my pension at risk are not being forced to share in the pain of those decisions. That's why we need the Pension Fairness Act in addition to the critical HR2327, the moratorium on pension plan terminations, both introduced by Congressman Miller.

Sincerely,
Kay Goldsworthy
West Chester, Pennsylvania

Dear Congressman Miller,

My husband Jim and I were hired by UAL in 1969. He is a retired pilot, age 63, and I am an active flight attendant, age 58. Most of our more than 30-year careers were spent flying out of LAX. We live in Orange County, California. In the 1990's, we moved into our dream home in Mission Viejo. Our future looked beautiful and secure. Then came a series of horrendous mistakes by United's upper management and their Board of Directors, followed by September 11th. The stock market drop devastated our 401ks. In 2002, Jim officially retired as a 737 captain (the lowest captain pay tier), seven years after his last flight due to throat cancer from which he was not expected to survive. In 2003, after the first round of pay and benefit cuts from United's bankruptcy, and with a daughter in law school, a son in college, and another in high school, we moved from our dream home to a more realistic one. Now, because of the further erosion of my pay and medical/dental benefits, my inadequately low future retirement pay, and the loss of most of Jim's pension, we will be forced to move again. I am a third generation Californian and I fear not being able to afford to live in this state where my family's roots go back over 150 years.

Because of financial hits we are forced to absorb due to circumstances beyond our control, I will be working for UAL until either United or I die. My husband and I played by the rules as employees of UAL and as citizens of the U.S. Why are we now in essence being robbed and forced to pay the price of an incompetent management and Board of Directors - one that union employees never hired? Why should we lose the secure retirement we have toiled honestly and hard for since 1969, while our 2 - year CEO Glenn Tilton is guaranteed a multi-million dollar package, as are others in top management? Why have the rules been changed when it's too late for working people like my husband and I to make the necessary financial changes to replace the loss of defined benefit pensions and devastated 401k's? What ever happened to fair play? Are these the MORAL VALUES voted into power last November? Thank you so much Congressman Miller for this opportunity to plead for our rapidly vanishing secure golden years.

Sincerely,
Susan and James Cronin
Dove Canyon, California

Dear Congressman Miller,

I have been a Flight Attendant for United Airlines for 38 years. When I began flying, there were no pensions for Flight Attendants because we were required to quit after age 32. That ended, thanks to age discrimination laws passed by Congress. However, it meant that Flight Attendants had to make up for lost time to build a decent retirement from the company. We gave up pay increases over the years to have United increase the amount they would contribute to our retirement fund. Now at age 60, I could receive a pension estimated at $2,500 a month. It is not a fortune, but combined with Social Security, I would be able to retire at age 65. Now United is using bankruptcy as a way to end all their pensions and let the government be responsible for them. This will have a tremendous impact on the lives of all retirees and all future retirees. It amazes me that United cares so little for those of us who have spent our lives building this company, while our CEO, who has been with the company for 3 years, maintains his 4.5 million dollar pension. What is to stop other airlines and other corporations from declaring bankruptcy so they can end their pensions? Why should the government be burdened with the pensions of thousands of workers, just because big business does not want the expense? What happens when the PBGC does not have the money to cover all these pensions? Some day these corporations will be profitable and can once again fund their Pensions. I urge all members of Congress to stop this raid on the pensions of employees. If you care about

Social Security, please care about the protection of our pensions. Do not let corporations cancel their employees' pensions.

Sincerely,
Janet Clark
Foster City, California

Dear Congressman Miller,

I have served as a UAL Flight Attendant for 28 years. I have always regarded my pension at United as an integral part of my future retirement. I had never seriously considered that my husband and I might retire before the age of 60 - but we fully expected that with my UAL pension and my husband's Social Security, that we could retire by 65. With the wanton dumping of our pension plan and the reduced benefit I will receive, it's looking likely that we won't be able to retire. I can't begin to tell you how cheated I feel. No one can give us back those years to save for retirement. This action by UAL should be illegal! Our pension was a part of the overall compensation package for years already worked. I am unable to make the trip to Washington DC and personally look my representatives in the eye, but that should not indicate to you a lack of interest or concern! I have a full work week which I'm unable to get out of, even if I could afford to! I am praying that Congress will come to our rescue in this "David and Goliath" battle. We are crying out for some justice!

My husband and I reside in California and have raised 2 children - our son recently served 41/2 years in the army and now lives at home, attending college full-time. Our daughter also lives at home, attending college full-time. Raising a family is expensive, as everyone knows, and we were unable to save much along the way due to my husband's health issues and resulting times without work. We consider ourselves conservative Republicans politically but recognize that this choice has not been helpful in the circumstance that we find ourselves. We are so hoping that our lawmakers will do the right thing and save our pensions - doing so might also prevent the avalanche of other companies hoping to ditch their employee pensions- an event which all Americans would wind up paying for!

Sincerely,
Elizabeth Frankle
Vista, California

Dear Congressman Miller,

We wish to thank you for your sponsorship of HR 2327. The uncontested cancellation of United Airlines defined benefit plans is tragic and catastrophic. Your introduction of this bill provides us with the hope and possibility that we may receive our day in court to right this terrible injustice. I worked as a Flight Attendant for UAL for 30 years and provided the professional service that was expected and provided for by our contractual agreement. My husband, Ret. Capt. Peter Crawford, provided 33 years of the same professional and friendly service that was expected by his contractual agreement. We are both retired and reside in Naples, Florida.

If the PBGC is allowed to take over our retirements our life as we now know it will be over. We have already lost several hundred thousand dollars in the loss of our ESOP stock in filing for bankruptcy but now they wish to abrogate the one true obligation that was critically negotiated and relied upon for our future at the end of our careers with one company. We will be forced to liquidate all of our assets, relocate our home to the least costly area we can find, and learn to live on less than 30% of our present pension. To be stripped of our duly negotiated and vested retirements is unconscionable.

If United Airlines were to cease operations, I could accept the PBGC as a safety net from capturing nothing. However, to allow United Airlines to cancel its duly negotiated defined benefit plans even though the PBGC said it is not needed to facilitate its emergence from bankruptcy is pure thievery. The decision of the PBGC and United Airlines for $1.5 billion payment to terminate all employee pension plans may trigger a total collapse of the defined benefit system nationwide. What is being done to prevent other companies from following suit? The line in the sand needs to be drawn that corporate profiteering at the expense of hardworking Americans must stop now. This approval of the backroom deal brokered by United and now approved by the court, pre-empted the United Airlines' employees' statutory right to defend their pension plan through the bankruptcy process based on the merits of the plan itself, as measured under the standards of pension law.

It would be appropriate for our Senators and Congressmen to realize the inherent danger of allowing the cancellation of defined benefit plans. All of corporate America will be standing in line to dump their pensions on the PBGC resulting in the largest taxpayer bailout in American history. This tragedy will make the Savings and Loan bailout look like a bad hangover.

We thank you Congressman Miller for your initiative, your serious concern, and will support your valiant efforts by contacting all of our Representatives. We are hopeful that the US Senate will pass a comparable bill in the very near future.

God bless you and God bless America.

Sincerely,
Susan Crawford
Naples, FL.

Dear Congressman Miller,

I am a constituent and I wish to alert you to the danger that exists regarding a precedent being set by the termination of UAL FLIGHT ATTENDANT pensions. It appears that the management of UAL, together with the PBGC and the Bankruptcy Court, have ignored the far reaching implications of terminating a defined benefit plan for Flight Attendant's without a truly comprehensive, fair analysis and hearing.

Clearly, Representative Miller's HR 2327 is an important step in protecting the future of pensions all over this nation. A six month moratorium would give Congress an opportunity to fully assess the federal pension guaranty system and pass a plan for strengthening defined benefit pensions in this country while giving the Flight Attendant's Union the opportunity to fight further in a court proceeding.

Quite frankly, I do not understand why the Board of Directors of UAL have not ousted the present management team (who have preserved their pension plan) for a conflict of interest and corporate misfeasance. Perhaps they are able to hide behind bankruptcy protection, however they should not be allowed to act in a fashion which compromises the interests of not only the Flight Attendants but also the owner-employees of UAL who have had their pensions jettisoned.

This issue is tantamount to the survival of unions and defined benefit plans in this country. This is a test case and the behavior of our elected leaders with regard to this matter will be scrutinized nationwide. The future of millions of Americans is at stake. The voting block concerned about this issue is vast and I believe the combined power of the AARP, AFA, and other union entities in this country have not only shown their displeasure with regard to the self-serving behavior of the UAL executives but will look with great disfavor on any elected representative who allows this injustice to go unabated. Please use every effort to support measures which protect pensions in this country for which Americans have worked so hard to preserve.

Sincerely,
Pasquale Crispo
New York, NY

Dear Congressman Miller,

I have been a Flight Attendant for almost 20 years for United Airlines, and if my pension is terminated I will be paid as if I terminated my employment at 47, even if I continue to work and retire from United

Airlines at 62. My retirement plans were for the full pension I was promised, a 401k, and Social Security. Now, I will have to live off of $400 monthly, approximately for my pension, instead of $2,800 monthly.

I can hardly contribute to my 401k due to pay cuts at United, and Social Security is no longer secure. I will be at poverty level and may have to be a burden on my son, who is only 16, but hopes will make a decent living to help me out.

What is happening to the working class? We have been deceived our whole lives about hard work paying off. The only ones paid off are the CEO and the Board of Directors, they don't have to work hard they come in with their guaranteed payoff and the company they have been hired to build or maintain can collapse right from under them, and they still have their pay protection, while the workers who built the companies lose everything and become a burden on their children, and or society. What has happened to our country? Thank you for your attention.

Sincerely,
Paula Carlson
Oak Lawn, Illinois

Dear Congressman Miller,

I am a Flight Attendant for United Airlines and started my career in 1965. Over the ensuing years, I married, had three children, divorced, remarried, and gained two more sons.

Our youngest is now 27 and living on his own. We spent most of my working career raising our sons and putting them through college. This left absolutely no money for a 401k or other savings plan.

I was hoping that in a few years hence I would have attained a comfortable pension so that I could retire. The events of this month have changed that dream.

The pay cuts agreed to because of the bankruptcy were so substantial, there is literally no money to put aside. My husband had a medical retirement years ago and since he had not attained tenure, his income is basically Social Security. I have been the main support for the family. Not only has my income been slashed, now I have very little pension to look forward to as well. I, as many other United Flight Attendants, am now in the process of studying for a new career to supplement my income. This is not an easy task at 60 years of age!

The airline that hired me respected its long time employees and was a fabulous place to work. Now it seems only the top management (most of which have very little seniority with the company) have any type of security and the rest of us who have devoted our lives to the company are being given the shaft.

I live in Las Vegas, Nevada and fly out of San Francisco.

I thank you for your time and efforts on behalf of the Flight Attendants and other employees of United Air Lines.

Sincerely,
KATHLEEN MCMAHON
Las Vegas, Nevada

Dear Congressman Miller,

I am writing to you to explain what the loss of pension dollars will mean to me. I was hired in 1968 by UAL and worked for 34 years and retired in 2002. I had the intent to work until I was 65 years old. September 11, 2001 was the end of my working career. The terrorists did a job on my psychological health. I was not able to return to work and after much therapy I retired.

My pension was part of an agreement I had with UAL and negotiated as part of my wages. I see Judge Wedoff's decision to approve the agreement between United and the PBGC to terminate our pensions as immoral and unconscionable. I see the obligation of UAL to its retired employees as something that should not be dropped. Judge Wadoff did not ask Tilton or other upper management people to turn their secured dollars over! At this stage of my life I am not able to start another career, so I am left with the option of a minimum wage job. I am thinking that as a single person I will probably have to sell my house in order to balance the loss of dollars and health insurance. Please consider what an injustice this is! Thank you, Congressman Miller, working Americans everywhere need Congress to act fast.

Sincerely,
Kathi Rockwell
Portland, Oregon

Dear Congressman Miller,

As a single mother of two teenagers and retired from UAL since 1990, I was anticipating enjoying my retirement paycheck of $800 per month to lift up my standard of living for my family. I am permanently disabled at this time and my pension means so much to us. I am outraged at this lack of accountability on United's part to uphold my pension that I worked 17 hard years to achieve. I live in CA and find it terrifying to think of what will become of us if I don't receive this pension.

If UAL is allowed to do this, think of all the other companies that will follow suit and then what will become of our country when we all need our retirement? Will Bush give us any money to live? It will all fall to the government and the taxpayers. Senior citizens will become homeless. Please help us keep what little dignity we have left in this world.

Sincerely,
Trudy Wolsky
Menifee, Calif.

Dear Congressman Miller,

I'm a retired United Air Lines Flight Attendant. I flew for United for over 38 years and, with much trepidation, I decided to retire in June 2003.

I've been a single mother for 22 years. When my daughter was a child, I not only worked for United, but on my days off from flying, I worked two other jobs for eight years. Then when she entered college, I moved to a state that was less costly in order to pay for her education. But in so doing, it was necessary for me to commute 2,500 miles to fly my trips.

Then 2003 arrived and United was in bankruptcy. Another decision---retire or not? In order to take retirement, I sold my home and moved to a smaller, more affordable home.

As United had always considered our retirement benefits to be part of our wages, I didn't mind working other jobs, commuting, moving, etc. as I had confidence that my retirement would be secure.

For a number of years United had been a wonderful company to work for. I trusted management to honor the agreements which had been made between the company and our work group. Now, with the possible termination of pensions, I feel I've been betrayed. Their poor policy decisions over a period of time have effectively destroyed a company that once was the bulwark of the airline industry. Simultaneously, their hostile attitude towards employees has eroded the spirit which once made United the standard for service in the air.

Sincerely,

Karen McLean
Melbourne, Florida

Dear Congressman Miller,

If United Airlines is allowed to get away with this outrageous scheme of theirs, I and other who came over from Pan Am will have been dealt a double whammy! I came to UAL from Pan American World Airways. After 17 years with PAA I am receiving $358 from the PBGC. I flew 16 years with UAL and am receiving $1,186. I am having a hard time financially, as my income is a lot less than what my expenses are per month. I am a native Californian and my pension has not kept up with the cost of living in the Bay Area. If I have to live on any less money than what I am receiving, I do not know what I am going to do. Who would have ever thought that we would be fighting for our pensions that we worked so hard for and were promised, just to have the greedy executives pull the pension from under us at age 60+? Congressman Miller, bless you and thank you so very much for taking our cause up. We need more people like you, who truly care, and are fighting for what is morally right!

Sincerely,
Jessie Gordon
Redwood City, California

Dear Congressman Miller,

I am a recently retired United Airlines Flight Attendant. I retired after 35 years due to health reason.

Like many others, I gave my life to United Airlines and hate to see this company torn apart by the "Tilton Gang." It is the employees that made United what it was and still can be again, and we are the ones deserving of the pensions promised to us. How anyone thinks it's fare for the "Tilton Gang" to walk into United, stay two years, take all the cutbacks they can from the people that care about the company, take away our hard earned pensions, while the "Tilton Gang" gets and keeps pensions that would pay over half the employees pensions for more than 5 years? You and I both know that is wrong as you have proven with this and other legislation.

Please vote to save the employee pensions at United. We are talking 120,000 people, not including the impact it would have on our families.

Sincerely,
Leyhe Wade
Oxford, North Carolina

Dear Congressman Miller,

I am 52 years old and single. I have been a United Airlines Flight Attendant for nine years and six months. When the Pension Benefit Guarantee Corporation takes over the pensions at UAL -- I will lose nearly everything because I do not yet qualify for retirement and my pension is subject to much more onerous reductions from the PBGC even if I continue to work at United Airlines until I qualify for retirement!

When I came to United Airlines in Nov. 1995, I felt I could retire here with a modest pension, Social Security and what little savings I have. What do I do now?

With the last two concessionary contracts at UAL since the bankruptcy (first in 2003 and again this year in January), my wages have diminished by nearly 18% and my medical and dental benefits premiums have increased (total benefit increases near 22%). I can only afford to contribute 5% into my non-matching 401K. My first of the month paycheck no longer covers my rent. I work a second job and am flying more hours to make up a little of the difference. There are no more days off and I am exhausted and worried.

I have 13 years to try and make a dent into what I thought was my retirement fund. The CEO at United

Airlines, Glen Tilton secured his $4.5 Million dollar pension trust in his first two months of employment. Mr. Tilton has been here less than 3 years.

This is a grave injustice. The PBGC said and still says that the Flight Attendant plan is viable. I truly will have to work into my grave just to survive if my pension is eliminated. You, our elected officials, are our only hope. STOP THIS NOW! The American Dream may be gone for me, but you can help save it.

Sincerely,
Nadine Ostroski
San Mateo, California

Dear Congressman Miller,

I was a Flight Attendant for United Airlines for 38 years... my entire working life. In 2003, along with 2,000 other FA's I chose to retire... remove my higher pay from UAL's labor cost so that lesser paid FA's wouldn't lose their jobs. For this I did not get an early out bonus... I paid 6% of my pension to leave 2 years before I was 60... I did it with a promise from UAL that my benefits as I knew them, would remain in tact!!

Before the ink was dry, I found myself fighting to save my medical benefits and NOW fighting to keep my meager pension! I chose my career at United because of the benefits. I spent my earned pay increases on improving my benefits and I have paid for this pension! Even though I spent almost 40 years with UAL, my pension would be greatly reduced under the PBGC maximums as I am still under the age of 65. I am a single woman with no partner to help offset my expenses and ask for your help... please ensure that UAL keeps their commitment to me!!

Sincerely,
Judy Rowe
Healdsburg, California

Dear Congressman Miller,

First off I'd like to thank you for the opportunity of letting us tell our story. Those who run our company seem to have forgotten that we are individuals working hard and doing our best for a company that seems to feel that we have no worth.

My name is Joyce Lynch and I have been with United Airlines since December 27, 1997 working as a Flight Attendant based out of Newark, New Jersey. For me, this termination of our Pension Plan means a breach of contract by those who make the decisions in our company. When we negotiated our contracts, the pension was a promise of deferred compensation for which we sacrificed other pay and benefits to secure.

It doesn't seem right that Mr. Tilton has the ability to terminate our pension when he has a pension plan that is non terminable for $4.5 million. As we have already given up life-altering sacrifices to help the company out of bankruptcy, it is very important that we can count on our pensions at retirement. Thank you again for all of your time and effort with our cause.

Sincerely,
Joyce Lynch
Shohola, Pennsylvania

Dear Congressman Miller,

I have been a Flight Attendant for United Airlines for 36 years and continue to fly simply because I love my career. As a young woman I helped put my husband through his final two years of undergraduate school and three years of law school. I then went on to raise my two children and have just watched my youngest graduate from college. I accomplished this while working hard, being away from home, having a different schedule every month, and being very proud and satisfied with my career. During all of this my husband and I were primary care givers of three elderly parents, two with Alzheimer's disease.

Now that it is finally our turn to enjoy the so-called golden years of our life, United Airlines has decided that my pension is too expensive to fund. However, they can continue to fund the gigantic salaries and bonus payments for many of the officers that have put this airline into bankruptcy.

I also fear for the entire population of hard working Americans that will face this same problem when the greed of corporate America realizes that the stoppage of pension funding is another way of financing the greed of corporate CEO's. Please help us stop the crushing of the American Dream. This is a society that will not operate with two social classes - the rich and the poor. Please ask the Senate and the House what plan is being considered to help the millions of destitute Americans that will be in our streets when both the PBGC and Social Security fail.

Sincerely,
ELAINE REILLY
Bound Brook, New Jersey

Dear Congressman Miller,

My spouse Stephanie and I are taking this opportunity to share the impact the pension cuts will have on our lives. Combined we have invested 55 years with UAL Donald (30) Stephanie (25). We have two teenage daughters ready to enter college during our retirement. We have been trying to save in our 401k's but with three pay cuts it's been difficult to save. My father is the recipient of a pension loss from bankrupt Montgomery Wards. He is 86 and we are also helping him. Facing future family medical, dental, housing expenses we and every citizen of this country, are going to need every penny of which we are being stripped. Please help enlighten all concerned to have mercy on our plight.

Sincerely,
Mr & Mrs Donald Wood
Federal Way, Washington

Dear Congressman Miller,

My name is Debra Cooke. I am 54 yrs. old and have been a United Flight Attendant for 32 years. I am based in Newark and I live in NJ. I was asked to make a statement as to how this pension termination has impacted my life. It has stressed me out in a way I can barely describe. Just so much ANXIETY over how my husband (who receives a pension from AT&T Corp.) and I, will pay our bills. We are by no means 'big spenders.' We have a home, with an equity loan mortgage. Nothing fancy. We have lived here for 30 yrs. We decided to add a second bathroom, a storage closet and a rec room in June 2002. When UAL filed for Bankruptcy protection in Dec. 2002, I had decided that I would fly through age 56, figuring I would get a part-time job to supplement my pension, which at that time, was adequate for that age.

But as time passed, my paycheck was cut twice, my vacation cut in half, my pension amount crept lower & lower, and then capped at $1800.00 a month (at age 60). Now, combine this with a necessary increase in flight time & days to make up lost money and its no wonder that I have become too ill to work any longer. I have to retire June 1, 2005 and expect to receive $1,434.00 a month, BEFORE taxes and medical are taken out. I feel as though I have no choice. Arthritis, bad feet, stress, and now possible heart problems, have FORCED me out. Now I am not even sure that I will get a pension! Hopefully I will, from the PBGC Fund. That is providing THAT stays solvent! I feel so betrayed!

I was PROMISED a pension at the end of my career. I gave 32 years of my life to this company and I expected to have my pension (there was NEVER any doubt) when I could no longer fly. As a result of that PROMISE, I paid the bills, and let my husband put a lot of his paycheck into AT&T's plan, because it was a BETTER plan. Now what do we do? We will be hard pressed to make it...but we will try.

It's OUTRAGEOUS that this company, actually that ANY company, should be able to vacate their responsibilities to their long-term employees. Corporate America executive are vultures, who will someday be picking at the bones of the hard working families that they have financially crippled. It will come down to being a country of the poor and the rich. No more middle class. At some point, much of working America will have to depend upon the government for everything to live, because fair wages, and fair pensions have been lost, and no one will be able to take care of their own families. Where does this end?! I feel it has only BEGUN, unless it is stopped here and now! Please help us, for the sake of all working families, and the very life-blood of this country!

Sincerely,
Debra Cooke
Brick, New Jersey

Dear Congressman Miller,

Let me begin by saying THANK YOU-THANK YOU - THANK YOU Congressmen Miller! My name is Linda Garrison. I am a recently retired Flight Attendant. My home is a rented apartment located in Laguna, Orange County, CA. I dedicated 38 years of my life in service to United Airlines. Many of those years did not include a pay increase. During those times, a raise was forfeited to insure future security through the Flight Attendant Defined Benefit Pension Plan, as well as continued Health Care. It's a slap in the face that after all the years of sacrifice, United Airlines, with the help of PBGC, intends to terminate everything we worked towards!

Terminating my pension is beyond devastating! With no other means of support, I count on pension income just to survive while continuing my education. The dream of becoming a NeuroBiofeedback Therapist as a second career will be gone forever. Even more disheartening, pension income plus Social Security is now in question?

The Flight Attendant Defined Benefit Pension Plan in no way prevents United from exiting bankruptcy, or surviving as the great airline it once was. Please do not stand by and watch as United ruins so many lives in the name of GREED!

Thank you, a most grateful constituent.

Sincerely,
Linda Garrison
Laguna Beach, CA

Dear Congressman Miller,

My mother is a retired United Airlines Flight Attendant. She worked for the company for 36 years, won Flight Attendant of the year, and served thousands of passengers along the way. In 2004 when United needed to cut their payroll in order to make ends meet, she along with many senior Flight Attendants retired early to ensure the well being of the company they worked for decades.

With the pension handover she will lose over $1,000 dollars a month while the million dollar payouts of former CEOs will be left in tact. Please take action so that my mom can continue paying her mortgage and living the life she worked so hard to build.

Sincerely,
Donovan Daughtry
Hermosa Beach, California

Dear Congressman Miller,

I am a 58-year-old female UAL retired Flight Attendant. In 2003 I took the UAL bait and switch retirement plan due to the fact that I am totally disabled as a result of injuries received while working for 16 years at UAL. My health insurance has increased 5 times more than the amount promised to me, and now my pension is at risk. Due to my work injuries, I cannot get another job or switch insurance coverage. I will be forced into low-income based housing. I have not received a workers' comp settlement because UAL attorneys continue to postpone my hearing. Please help us save our pensions. There are many injured Flight Attendants like myself, who cannot replace the income we are losing. Thank you so much for your continued support and help.

Sincerely,
Bonnie Harden
Palm Springs, California

Dear Congressman Miller,

I'm a former UAL Flight Attendant. I worked 34 yrs for United and thought that would ensure my future. I decided to retire two years ago when UAL informed me that if I retired by June 30, 2003, I would retain my medical benefits. Well, we all know how that turned out...now I find out I stayed at a job for all those years only to make sure my future would be safe and secure financially, and find out that it has been all for nothing...I now live on less than $2,000 a month. How does one at the age of 57 look to the future with inflation and medical expenses with any kind of hope?

I'm saddened by my company as well as the judgment of the courts that continue to play with our lives like they mean nothing. Please make our lives count for all the care and love we gave our passengers and our company...thank you.

Sincerely,
Leslie Kron

Dear Congressman Miller,

My name is Michael Adams. I have been a Flight Attendant for United Airlines since 1977 and currently I'm based at Chicago's O'Hare airport. I reside in Somerset, New Jersey.

For the last 28 years of my employment at United, I was promised a company provided pension upon my retirement. Regardless of which CEO, CFO or BOD was in place, I along with other United employees gave dedicated service to United. Despite bad times, we kept our word to perform our duties to the best of our abilities. Time and again, Flight Attendants were told we surpassed expectations of getting the customers to repurchase a ticket and come back to United.

Over the years, I gave up monthly wage increases in lieu of the security of a promised modest monthly pension amount upon retirement. Now, United Airlines wants to abrogate that promise.
This is especially outrageous when senior management has awarded itself with raises and bonuses while at the same time demanding concessions from workers; claiming it is needed to exit bankruptcy.

The court's approval of United's agreement to pay the PBGC $1.5 billion PBGC to terminate my pension will undoubtedly lessen the promised monthly amount. It will become more difficult and likely impossible for me to maintain my home and lifestyle, here in New Jersey. The potential combination of higher medical costs, higher prescription costs, higher property taxes and general inflation as well as a reduced pension will have a very negative impact on my day-to-day existence, never mind any unforeseen medical or other hardships. Reduced salaries conceded to United already have put a strain on the household budget.

Monies from United and paid to the PBGC could go towards salvaging my pension. Congressional help is sorely needed to stop this outrageous act contrary to the provisions of bankruptcy and pension law. Thank you for supporting the efforts to protect UAL employee pensions from becoming a burden of the American taxpayer.

Sincerely,
Michael Adams
Somerset, New Jersey

Dear Congressman Miller,

Please save the pensions of all hard working Americans starting with that of the United Airlines employees.

As you know, we are under the attack of UAL's corporate management trying to rid their obligation to workers for our "promised" pensions. I work out of the San Francisco office, but live in Honolulu. As you know, this is my personal choice but do so out of the love of this company, its employees and the service industry of the airlines bringing people together around the world.

I have two small children (ages 1 and 3), and to think that by the time I retire in 30 years (that would give me approximately 36 years service with UAL), there will be a dire future is frightening. Just like my father and everyone else, I was planning on a "decent" retirement plan, which would allow me to watch over my adult children and possibly grandchildren without becoming a burden to them. There were plans of living the American dream of a small home, loving family and a comfortable retirement.

Now, those plans must be changed due to the actions of our current management. The thing that bothers me isn't the fact that it's going to change my life drastically. It's the fact that this will change the lives of all workers around the country. Not just that of the airline industry, but others across the board. Only because of UAL's management decision to "cut costs" to an unimaginable level which affects blue collar and white-collar workers everywhere.

Congressman Miller, I pray for the sake of all American workers that something will be done in stopping this injustice to the American people. These incredible events which shape our industry, including the events of 9/11, have and will change the lives of Americans everywhere. I wish you success in getting other Members of Congress involved in what is happening to our country.

Thank you on behalf of our family and eventually yours down the line.

Sincerely,
Ronald Fukuchi
Honolulu, Hawaii

Dear Congressman Miller,

I retired early with 34 years under my belt from United Airlines almost 2 years ago. I still loved my job but had some serious health issues to contend with. They told us if we retired before July 1st we would pay little or nothing for medical insurance. This was my main reason to retire. Also I couldn't have done it if my pension wouldn't have allowed me to financially. I had everything figured out to the penny. The pension is all I have. I'm a single woman and do not get income elsewhere. I do have a 401k and IRA's but cannot touch these until I'm 59 1/2 years of age. My pension covers my expenses and that's about it. From the PBGC, I will receive approx. $600-800 less a month and I simply cannot live on this. I will have to seek employment and am concerned because with my health, I don't know how this is going to workout.

Sincerely,
Linda Sargent
Lake Oswego, Oregon

Dear Congressman Miller,

The impact of no pensions will devastate not only my family but is going to be the beginning of the end of decent middle class lives for most Americans. I started to work for United Airlines in 1986...I have been a customer service agent, reservations agent...I have been in computer development (IT) I have been a training instructor for both the reservations and customer service groups. Today I am a Flight Attendant where I contribute as a language of destination Flight Attendant in Spanish, French and Portuguese. I hold a 4-year degree and a 2-year postgraduate degree. I would have never stayed with UAL this long and given them so many years without the promise of retirement or pension. I cannot afford to pay for property taxes, the medication needed for my family, and also put food on our tables. Why is it legal to forgo a financial promise to employees? Please help us have a more secure and fair future after giving many years of hard work, dedication, and commitment. I am lucky if I will get $400.00 a month. (Assuming that the PBGC continues to survive) This means that I will have to work for the rest of my living life.

Your assistance is warmly appreciated!!

Sincerely,
Jean-marc Garcell
Palos Verdes Estates, California

United States Government Accountability Office

GAO

Testimony
Before the Committee on Transportation and Infrastructure, Subcommittee on Aviation

For Release on Delivery
Expected at 2:30 p.m. EDT
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COMMERCIAL AVIATION

Preliminary Observations on Legacy Airlines' Financial Condition, Bankruptcy, and Pension Issues

Statement of JayEtta Z. Hecker, Director
Physical Infrastructure Issues

and

Barbara D. Bovjberg, Director
Education, Workforce, and Income Security Issues

GAO
Accountability * Integrity * Reliability

GAO-PUB No. 05-835T

June 22, 2005

GAO
Accountability Integrity Reliability

Highlights

Highlights of GAO-05-835T, a report to Committee on Transportation and Infrastructure, Subcommittee on Aviation, House of Representatives

COMMERCIAL AVIATION

Preliminary Observations on Legacy Airlines' Financial Condition, Bankruptcy, and Pension Issues

Why GAO Did This Study

Since 2001, the U.S. airline industry has confronted unprecedented financial losses. Two of the nation's largest airlines—United Airlines and US Airways–went into bankruptcy, terminating their pension plans and passing the unfunded liability to the Pension Benefit Guaranty Corporation (PBGC). PBGC's unfunded liability was $9.6 billion; plan participants lost $5.2 billion in benefits.

Considerable debate has ensued over airlines' use of bankruptcy protection as a means to continue operations, often for years. Many in the industry and elsewhere have maintained that airlines' use of this approach is harmful to the industry, in that it allows inefficient carriers to reduce ticket prices below those of their competitors. This debate has received even sharper focus with pension defaults. Critics argue that by not having to meet their pension obligations, airlines in bankruptcy have an advantage that may encourage other companies to take the same approach.

GAO's testimony presents preliminary observations in three areas: (1) the continued financial difficulties faced by legacy airlines, (2) the effect of bankruptcy on the industry and competitors, and (3) the effect of airline pension underfunding on employees, retirees, airlines, and the PBGC.

www.gao.gov/cgi-bin/getrpt?GAO-05-835T.

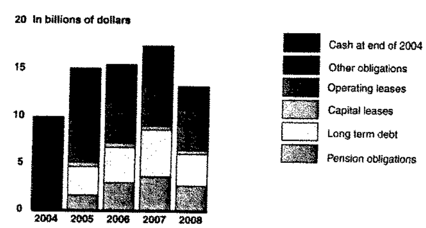
To view the full product, including the scope and methodology, click on the link above. For more information, contact JayEtta Hecker, (202) 512-2834 or heckerj@gao.gov.

What GAO Found

U.S. legacy airlines have not been able to reduce their costs sufficiently to profitably compete with low cost airlines that continue to capture market share. Internal and external challenges to the industry have fundamentally changed the nature of the industry and forced legacy airlines to restructure themselves financially. The changing demand for air travel and the growth of low cost airlines has kept fares low, forcing these airlines to reduce their costs. They have struggled to do so, however, especially as the cost of jet fuel has jumped. So far, they have been unable to reduce costs to the level of their low-cost rivals. As a result, legacy airlines have continued to lose money–$28 billion since 2001.

Although some industry observers have asserted that airlines undergoing bankruptcy reorganization contribute to the industry's financial problems, GAO found no clear evidence that historically airlines in bankruptcy have financially harmed competing airlines. Bankruptcy is endemic to the industry; 160 airlines filed for bankruptcy since deregulation in 1978, including 20 since 2000. Most airlines that entered bankruptcy have not survived.

While bankruptcy may not be detrimental to the health of the airline industry, it is detrimental for pension plan participants and the PBGC. The remaining legacy airlines with defined benefit pension plans face over $60 billion in fixed obligations over the next 4 years, including $10.4 billion in pension contributions – more than some of these airlines may be able to afford given continued losses (see figure). Various pension reform proposals may provide some immediate liquidity relief to those airlines, but at the cost shifting additional risk to PBGC. Moreover, legacy airlines still face considerable restructuring before they become competitive with low cost airlines.



Source: PBGC and SEC filings.

Note: Fixed obligations in 2008 and beyond will likely increase as payments due in 2006 and 2007 may be pushed out and new obligations are assumed.

Mr. Chairman and Members of the Subcommittee:

We appreciate the opportunity to participate in today's hearing to discuss the financial condition of the U.S. airline industry—and particularly, the financial problems of legacy airlines.[1] Since 2001, the U. S. airline industry has confronted financial losses of unprecedented proportions. From 2001 through 2004, legacy airlines reported losses of $28 billion, and two of the nation's largest legacy airlines—United Airlines and US Airways–went into bankruptcy,[2] eventually terminating their pension plans and passing the unfunded liability to the Pension Benefit Guaranty Corporation (PBGC).[3] Two other large legacy airlines have announced that they are precariously close to following suit.

In recent years, considerable debate has ensued over legacy airlines' use of Chapter 11 bankruptcy protection as a means to continue operations, often for years. Some in the industry and elsewhere have maintained that legacy airlines' use of this approach is harmful to the airline industry as a whole, in that it allows inefficient carriers to stay in business, exacerbating overcapacity and allowing these airlines to potentially under price their competitors. This debate has received even sharper focus with US Airways' and United's defaults on their pensions. By eliminating their pension obligations, critics argue, US Airways and United enjoy a cost advantage that may encourage other airlines sponsoring defined benefits plans to take the same approach.

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1 While there is variation among airlines in regards to the size and financial condition, we adhere to a construct adopted by industry analysts to group large passenger airlines into one of two groups—legacy and low cost. Legacy airlines (Alaska, American, Continental, Delta, Northwest, United, and US Airways) predate airline deregulation of 1978 and have adopted a hub and spoke network model that can be more expensive to operate than a simple point-to-point service model. Low cost airlines (AirTran, America West, ATA, Frontier, JetBlue, Southwest, and Spirit) have generally entered the market since 1978, are smaller, and generally employ a less costly point-to-point service model. The 7 low cost airlines have consistently maintained lower unit costs than the 7 legacy airlines.

2 Two other smaller carriers—ATA Airlines and Aloha—are also in bankruptcy protection. Hawaiian Airlines just emerged from bankruptcy protection earlier this month.

3 The Pension Benefit Guaranty Corporation's (PBGC) single-employer insurance program is a federal program that insures certain benefits of the more than 34 million worker, retiree, and separated vested participants of over 29,000 private sector defined benefit pension plans. Defined benefit pension plans promise a benefit that is generally based on an employee's salary and years of service, with the employer being responsible to fund the benefit, invest and manage plan assets, and bear the investment risk. A single-employer plan is one that is established and maintained by only one employer. It may be established unilaterally by the sponsor or through a collective bargaining agreement.

Last year, we reported on the industry's poor financial condition, the reasons for it, and the necessity of legacy airlines to reduce their costs if they are to survive.[4] At the request of the Congress, we have continued to assess the financial condition of the airline industry and, in particular, the problems of bankruptcy and pension terminations. Our work in this area is still under way.[5] Nonetheless, we can offer some preliminary observations about what we are finding. Our statement today describes our preliminary observations in three areas: (1) the continued financial difficulty faced by legacy airlines, (2) the effect of bankruptcy on the industry and competitors, and (3) the effect of airline pension underfunding on employees, retirees, airlines, and the PBGC. Our final report, which we expect to issue in September, will offer additional evidence and insights on these questions.

In summary:

- U.S. legacy airlines have not been able to reduce their costs sufficiently to profitably compete with low cost airlines that continue to capture industry market share. Challenges that are internal and external to the industry have fundamentally changed the nature of the industry and forced legacy airlines to restructure themselves financially. The changing demand for air travel and growth of low cost airlines has kept fares low, forcing legacy airlines to reduce their costs. However, legacy airlines have struggled to do so, and have been unable to achieve unit cost comparability with their low-cost rivals. As a result, legacy airlines have continued to lose money–$28 billion since 2001—and are expected to lose another $5 billion in 2005. Additionally, airlines' costs have been hurt by rising fuel prices – especially legacy airlines that did not have fuel hedging in place.

- Bankruptcies are endemic to the airline industry, the result of long-standing structural issues within the industry, but there is no clear evidence that bankruptcy itself has harmed the industry or its competitors. Since deregulation in 1978, there have been 160 airline bankruptcy filings, 20 of which have occurred in the last 5 years. Airlines fail at a higher rate

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[4] U.S. Government Accountability Office, *COMMERCIAL AVIATION: Legacy Airlines Must Further Reduce Costs to Restore Profitability* (GAO-04-836) August, 2004.

[5] We found all relevant data for assessing the financial condition of the airline industry, analyses of the effects of bankruptcy on the industry as a whole and six case studies of hub markets affected by airline

than most other types of companies, and the airline industry historically has the worst financial performance of any sector. This inherent instability that leads to so many bankruptcies can be traced to the structure of the industry and its economics, including the highly cyclical demand for air travel, high fixed costs, and few barriers to entry. The available evidence does not suggest that airlines in bankruptcy contribute to industry overcapacity or that bankrupt airlines harm competitors by reducing fares below what other airlines are charging. The history of the industry since deregulation indicates that past liquidations or consolidations have not slowed the overall growth of capacity in the industry. Studies conducted by others do not show evidence that airlines operating in bankruptcy harmed other competitors. Finally, while bankruptcy may appear to be a useful business strategy for companies in financial distress, available analysis suggests it provides no panacea for airlines. Few airlines that have filed for bankruptcy protection are still in business today. Bankruptcy involves many costs, and given the poor track record, companies are likely to use it only as a last resort.

- While bankruptcy may not harm the financial health of the airline industry, it has become a considerable concern for the federal government and airline employees and retirees because of the recent terminations of pensions by US Airways and United Airlines. These terminations resulted in claims on PBGC's single –employer program of $9.6 billion and plan participants (i.e., employees, retirees, and beneficiaries) are estimated to have lost more than $5 billion in benefits that were either not covered by PBGC or exceeded the statutory limits. At termination in May 2005, United's pension plans promised $16.8 billion in benefits backed by only $7 billion in assets (i.e., it was underfunded by $9.8 billion). PBGC guaranteed $13.6 billion of the promised benefits, resulting in a claim on the agency of $6.6 billion and an estimated $3.2 billion loss to participants. The defined benefit pension plans of the remaining legacy airlines with active plans are underfunded by $13.7 billion (based on data from the U.S. Securities and Exchange Commission, or SEC), raising the potential of more sizeable losses to PBGC and plan participants. These airlines face $10.4 billion in pension contributions over the next 4 years, significantly more than some of them may be able to afford given continued losses and their other fixed obligations. Spreading these contributions over more years, as some of these airlines have proposed, would relieve some

bankruptcy or service withdrawals, interviews with industry and subject area experts, and analyses of SEC and PBGC data to be sufficiently reliable for our purposes.

of this liquidity pressure but would not necessarily keep them out of bankruptcy because it does not fully address the fundamental cost structure problems faced by legacy airlines.

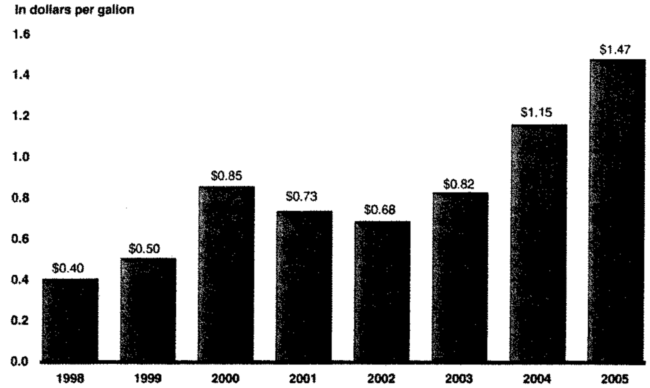
We have previously reported that the Congress should consider broad pension reform that is comprehensive in scope and balanced in effect. Under current conditions, the presence of PBGC insurance may create "moral hazard" incentives to not fund pensions knowing that PBGC will assume the payments in the future. In considering various proposals to reform pension requirements, the impact on airlines, PBGC, and plan participants will vary. Nevertheless, effective reform would at a minimum include meaningful incentives for sponsors to adequately fund their plans, provide additional transparency for participants, and ensure accountability for those firms that fail to match the benefit promises they make with the resources needed to fulfill those promises.

Legacy Airlines Must Reduce Costs to Restore Profitability

Since 2000, legacy airlines have faced unprecedented internal and external challenges. Internally, the impact of the Internet on how tickets are sold and consumers search for fares and the growth of low cost airlines as a market force accessible to almost every consumer has hurt legacy airline revenues by placing downward pressure on airfares. More recently, airlines' costs have been hurt by rising fuel prices (see figure 1).[6] This is especially true of airlines that did not have fuel hedging in place. Externally, a series of largely unforeseen events—among them the September 11th terrorist attacks in 2001 and associated security concerns; war in Iraq; the SARS crisis; economic recession beginning in 2001; and a steep decline in business travel—seriously disrupted the demand for air travel during 2001 and 2002.

[6] Legacy airlines' fuel costs as a percentage of total operating costs doubled from 11.5 percent during the 4th quarter of 1998 to 22.9 percent during the 4th quarter of 2004. Fuel costs for these airlines were $5 billion higher in 2004 than in 2003 – an amount roughly equal to their net operating losses.

Figure 1: Average Annual Spot Price for Gulf Coast Jet Fuel, 1998-2005

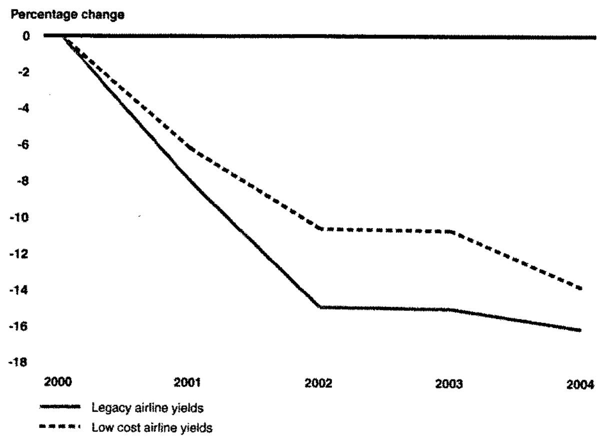


Source: GAO analysis of Department of Energy's Energy Information Administration data.

Note: 2005 prices reflect average through June 7.

Low fares have constrained revenues for both legacy and low cost airlines. Yields, the amount of revenue airlines collect for every mile a passenger travels, fell for both low cost and legacy airlines from 2000 through 2004 (see figure 2). However, the decline has been greater for legacy airlines than for low cost airlines.

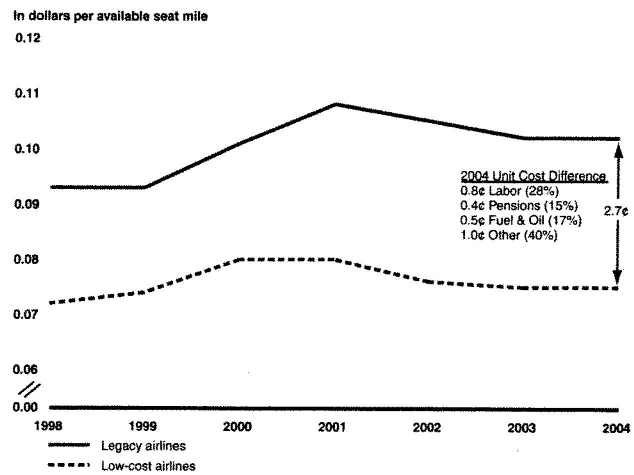
Figure 2: Percentage Change in Passenger Yields Since 2000



Source: GAO analysis of Department of Transportaion (DOT) Form 41 data.

Legacy airlines, as a group, have been unsuccessful in reducing their costs to become more competitive with low cost airlines. Unit cost competitiveness is key to profitability for airlines because of declining yields. While legacy airlines have been able to reduce their overall costs since 2001, these were largely achieved through capacity reductions and without an improvement in their unit costs. Meanwhile, low cost airlines have been able to maintain low unit costs, primarily by continuing to grow. As a result, low cost airlines have been able to sustain a unit cost advantage as compared to their legacy rivals (see figure 3). In 2004, low cost airlines maintained a 2.7 cent per available seat mile advantage over legacy airlines. This advantage is attributable to lower overall costs and greater labor and asset productivity.

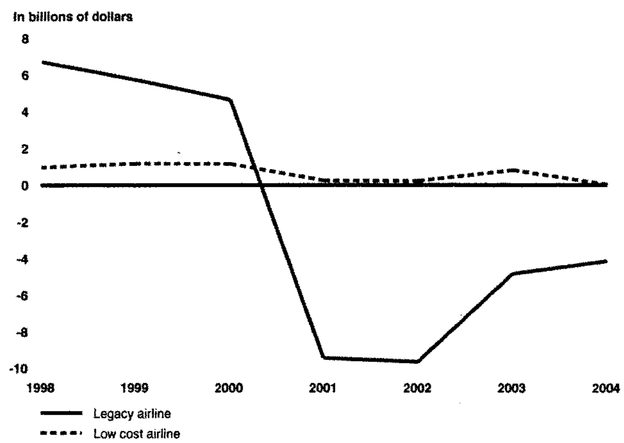
Figure 3: Legacy vs. Low Cost Airline Unit Cost Differential, 1998 2004



Source: GAO analysis of DOT Form 41 data.

Weak revenues and the inability to realize greater unit cost-savings have combined to produce unprecedented losses for legacy airlines. At the same time, low cost airlines have been able to continue producing modest profits as a result of lower unit costs (see figure 4). Legacy airlines have lost a cumulative $28 billion since 2001 and are predicted to lose another $5 billion in 2005, according to industry analysts.

Figure 4: Airline Operating Profits and Losses, 1998-2004



Source: GAO analysis of DOT Form 41 data.

Since 2000, as the financial condition of legacy airlines deteriorated, they built cash balances not through operations but by borrowing. Legacy airlines have lost cash from operations and compensated for operating losses by taking on additional debt, relying on creditors for more of their capital needs than in the past. In the process of doing so, several legacy airlines have used all, or nearly all, of their assets as collateral, potentially limiting their future access to capital markets.

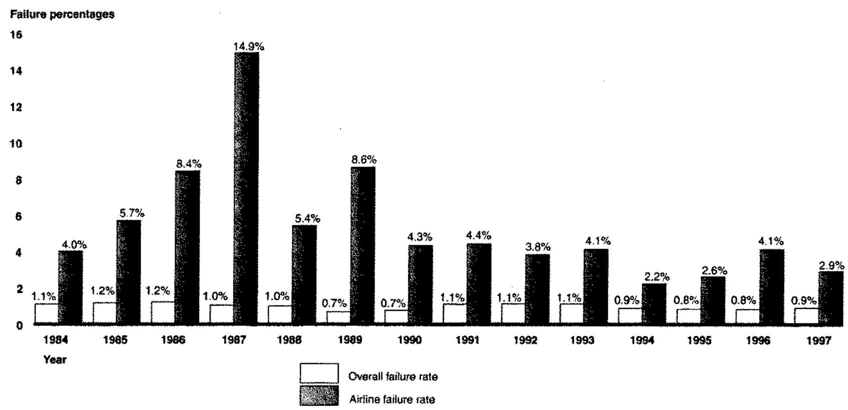
In sum, airlines are capital and labor intensive firms subject to highly cyclical demand and intense competition. Aircraft are very expensive and require large amounts of debt financing to acquire, resulting in high fixed costs for the industry. Labor is largely unionized and highly specialized, making it expensive and hard to reduce during downturns. Competition in the industry is frequently intense owing to periods of excess capacity, relatively open entry, and the willingness of lenders to provide financing. Finally, demand for air travel is highly cyclical, closely tied to the business cycle. Over the past decade, these structural problems have been exacerbated by the growth in low cost airlines and increasing consumer sensitivity to differences in airfares based on their use of the Internet to purchase tickets. More recently airlines have had to deal with persistently high fuel prices—operating profitability, excluding fuel costs, is as high as it has ever been for the industry.

Bankruptcy is Common in the Airline Industry, but There is No Evidence that it is Harmful to the Industry or Competitors

Airlines seek bankruptcy protection for such reasons as severe liquidity pressures, an inability to obtain relief from employees and creditors, and an inability to obtain new financing, according to airline officials and bankruptcy experts. As a result of the structural problems and external shocks previously discussed, there have been 160 total airline bankruptcy filings since deregulation in 1978, including 20 since 2000, according to the Air Transport Association.[7] Some airlines have failed more than once but most filings were by smaller carriers. However, the size of airlines that have been declaring bankruptcy has been increasing. Of the 20 bankruptcy filings since 2000, half of these have been for airlines with more than $100 million in assets, about the same number of filings as in the previous 22 years. Compared to the average failure rate for all types of businesses, airlines have failed more often than other businesses. As figure 5 shows, in some years, airline failures were several times more common than for businesses overall.

[7] Airlines may file for two types of bankruptcy. Chapter 7 of the bankruptcy code governs the liquidation of the debtor's estate by appointed trustees of the court. Chapter 11 of the code governs business reorganizations and allows, among other things, companies to reject collective bargaining agreements and renegotiate contracts and leases with creditors with the approval of the court. Companies may also convert from a Chapter 11 reorganization into a Chapter 7 liquidation or may liquidate within Chapter 11.

Figure 5: Comparison of Airline and Overall Business Failure Rates, 1984-1997



Source: GAO analysis of DOT and Dun & Bradstreet data.

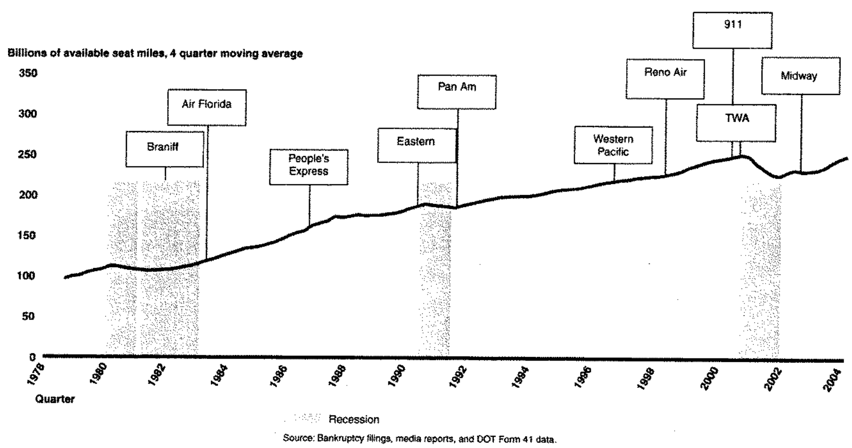
Note: Dun & Bradstreet data were only available through 1997.

With very few exceptions, airlines that enter bankruptcy do not emerge from it. Of the 146 airline Chapter 11 reorganization filings since 1979, in only 16 cases are the airlines still in business. Many of the advantages of bankruptcy stem from legal protection afforded the debtor airline from its creditors, but this protection comes at a high cost in loss of control over airline operations and damaged relations with employees, investors, and suppliers, according to airline officials and bankruptcy experts.

Contrary to some assertions that bankruptcy protection has led to overcapacity and under pricing that have harmed healthy airlines, we found no evidence that this has occurred either in individual markets or to the industry overall. Such claims have been made for more than a decade. In 1993, for example, a national commission to study airline industry problems cited bankruptcy protection as a cause for the industry's overcapacity and weakened revenues.[8] More recently, airline executives have cited bankruptcy protection as a reason for industry over capacity and low fares. However, we found no evidence that this had occurred and some evidence to the contrary.

First, as illustrated by Figure 6, airline liquidations do not appear to affect the continued growth in total industry capacity. If bankruptcy protection leads to overcapacity as some contend, then liquidation should take capacity out of the market. However, the historical growth of airline industry capacity (as measured by available seat miles, or ASMs) has continued unaffected by major liquidations. Only recessions, which curtails demand for air travel, and the September 11th attack, appear to have caused the airline industry to trim capacity. This trend indicates that other airlines quickly replenish capacity to meet demand. In part, this can be attributed to the fungibility of aircraft and the availability of capital to finance airlines.

Figure 6: Growth of Airline Industry Capacity and Major Airline Liquidations
Billions of ASMs, Moving Quarterly Average, 1978-2004



Note: Figure does not show liquidations of smaller airlines.

Similarly, our research does not indicate that the departure or liquidation of a carrier from an individual market necessarily leads to a permanent decline in traffic for that market. We contracted with Intervistas/GA[2], an aviation consultant, to examine the cases of six hub cities

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8 The National Commission to Ensure a Strong Competitive Airline Industry, Change, Challenge, and

that experienced the departure or significant withdrawal of service of an airline over the last decade (see table 1). In four of the cases, both local origin-and-destination (i.e., passenger traffic to or from, but not connecting through, the local hub) and total passenger traffic (i.e., local and connecting) increased or changed little because the other airlines expanded their traffic in response. In all but one case, fares either decreased or rose less than 6 percent.

Table 1: Case Examples of Markets' Response to Airline Withdrawals

Market	Year	Airline	Effect on passenger traffic	Change in fares
Nashville, TN	1995	American Airlines eliminated hub	Other airlines' traffic increased. Origin and destination traffic increased.	-10.2%
Greensboro, NC	1995	Continental Lite eliminated hub	Other airlines' traffic increased. Origin and destination traffic decreased.	+5.5%
Colorado Springs, CO	1997	Western Pacific moved operations to Denver	Other airlines' traffic decreased Origin and destination traffic decreased.	+43.6%
St. Louis, MO	2001	TWA acquired by American Airlines	Other airlines' traffic decreased. Little change in origin and destination traffic.	+5.4%
Kansas City, MO	2002	Vanguard Airlines suspended service	Little change in other airlines' traffic. Little change in origin and destination traffic.	+4.2%
Columbus, OH	2003	America West eliminated hub	Other airlines' traffic increased. Little change in origin and destination traffic.	+3.6%

Source: Intervistas/GA[2].

Note: Little change in traffic means that traffic increased or decreased less than 5 percent and that origin and destination traffic increased or decreased less than 10 percent. Changes in passenger traffic and fares are measured from 4 quarters prior to the airline departure to 8 quarters after.

We also reviewed numerous other bankruptcy and airline industry studies and spoke to industry analysts to determine what evidence existed with regard to the impact of bankruptcy on the industry. We found two major academic studies that provided empirical data on this issue. Both studies found that airlines under bankruptcy protection did not lower their fares or hurt competitor airlines, as some have contended. A 1995 study found that an airline typically reduced its fares somewhat before entering bankruptcy. However, the study found that other airlines did not lower their fares in response and, more importantly, did not lose passenger traffic

Competition, A Report to the President and Congress, August 1993.

to their bankrupt rival and therefore were not harmed by the bankrupt airline.[9] Another study came to a similar conclusion in 2000, this time examining the operating performance of 51 bankrupt firms, including 5 airlines, and their competitors.[10] Rather than examine fares as did the 1995 study, this study examined the operating performance of bankrupt firms and their rivals. This study found that bankrupt firms' performance deteriorated prior to filing for bankruptcy and that their rivals' profits also declined during this period. However, once a firm entered bankruptcy, its rivals' profits recovered.

Legacy Airlines Face Significant Near-term Liquidity Pressures, including $10.4 Billion in Pensions Contributions over the Next 4 Years

Under current law, legacy airlines' pension funding requirements are estimated to be a minimum of $10.4 billion from 2005 through 2008.[11] These estimates assume the expiration of the Pension Funding Equity Act (PFEA) at the end of this year.[12] The PFEA permitted airlines to delay the majority of their deficit reduction contributions in 2004 and 2005; if this legislation is allowed to expire it would mean that payments due from legacy airlines will significantly increase in 2006. According to PBGC data, legacy airlines are estimated to owe a minimum of $1.5 billion this year, rising to nearly $2.9billion in 2006, $3.5 billion in 2007, and $2.6 billion in 2008. In contrast, low cost airlines have eschewed defined benefit pension plans and instead use defined contribution (401k-type) plans.

However, pension funding obligations are only part of the sizeable amount of debt that carriers

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[9] Do Airlines In Chapter 11 Harm Their Rivals?: Bankruptcy and Pricing Behavior in U.S. Airline Markets National Bureau of Economic Research Working Paper 5047, Severin Borenstein and Nancy L. Rose, February 1995.

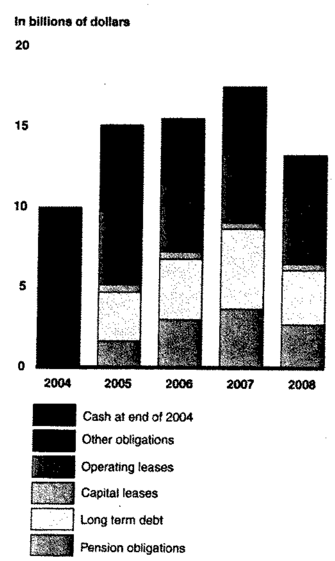
[10] The Effect of Bankruptcy Filings on Rivals' Operating Performance: Evidence From 51 Large Bankruptcies, Robert E. Kennedy, International Journal of the Economics of Business; Feb. 2000; pp. 5-25.

[11] These estimates include only legacy airlines that continue to sponsor defined benefit pension plans and reported their estimated pension obligations to PBGC. Pension law provisions prohibit publicly identifying the airlines that have reported this information.

[12] Pension Funding Equity Act of 2004 (P.L. 108-218, April 10, 2004). The PFEA also changed the interest rate used to calculate future liability from the 30-year Treasury bond to a corporate bond rate, which effectively reduces future liabilities.

face over the near term. The size of legacy airlines' future fixed obligations, including pensions, relative to their financial position suggests they will have trouble meeting their various financial obligations. Fixed airline obligations (including pensions, long term debt, and capital and operating leases) in each year from 2005 through 2008 exceed total cash balances of these same legacy airlines by a substantial amount. Legacy airlines carried cash balances of just under $10 billion going into 2005 (see figure 7). These airlines fixed obligations are estimated to be over $15 billion in both 2005 and 2006, over $17 billion in 2007, and about $13 billion in 2008. Fixed obligations in 2008 and beyond will likely increase as payments due in 2006 and 2007 may be pushed out and new obligations are assumed. If these airlines continue to lose money this year as analysts predict, this picture becomes even more tenuous.

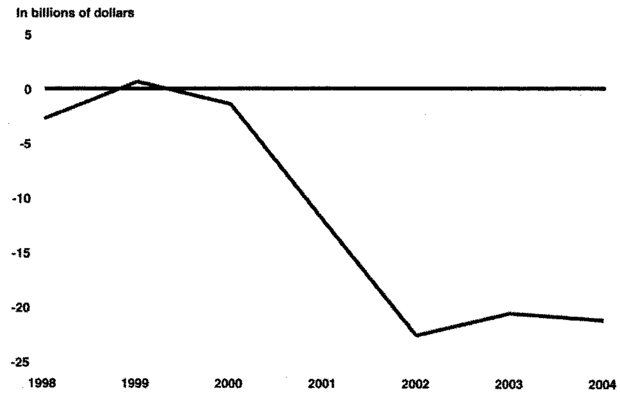
Figure 7: Comparison of Legacy Airline Year-end 2004 Cash Balances with Fixed Obligations, 2005-2008



Source: PBGC and SEC filings.

The enormity of legacy airlines' future pension funding requirements is attributable to the size of the pension shortfall that has developed since 2000. As recently as 1999, airline pensions were overfunded by $700 million based on Security and Exchange Commission (SEC) filings; by the end of 2004 legacy airlines reported a deficit of $21 billion (see figure 8), despite the termination of the US Airways pilots plan in 2003. Since these filings, the total underfunding has declined to approximately $13.7 billion, due in part to the termination of the United Airline plans and the remaining US Airways plans.[13]

Figure 8: Funded Status of Legacy Airline Defined Benefit Plans, 1998-2004



Source: GAO analysis of SEC filings.

Note: The termination of the United Airlines and remaining US Airways defined benefit pension plans in 2005 reduced the total shortfall to approximately $13.7 billion, based on 2004 year-end data.

The extent of underfunding varies significantly by airline. At the end of 2004, prior to terminating its pension plans, United reported underfunding of $6.4 billion, which represented over 40 percent of United's total operating revenues in 2004. In contrast, Alaska reported pension underfunding of $303 million at the end of 2004, or 13.5 percent of its operating revenues. Since United terminated its pensions, Delta and Northwest now appear to have the most significant

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[13] SEC data and PBGC data on the funded status of plans can differ because they serve different purposes and provide different information. The PBGC report focuses, in part, on the funding needs of each pension plan. In contrast, corporate financial statements show the aggregate effect of all of a company's pension plans on its overall financial position and performance. The two sources may also differ in the rates assumed for investment returns on pension assets and in how these rates are used. As a result, the information available from the two sources can appear to be inconsistent. PBGC data also are not timely.

pension funding deficits—over $5 billion and nearly $4 billion respectively—which represent about 35 percent of 2004 operating revenues at each airline.

The growth of pension underfunding is attributable to 3 factors.

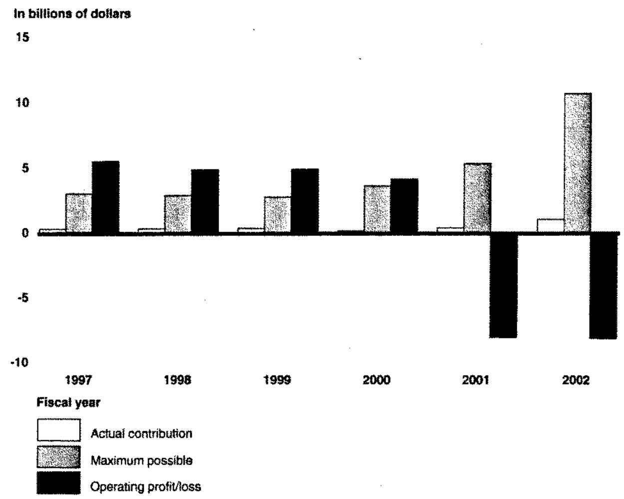
- Assets losses and low interest rates. Airline pension asset values dropped nearly 20 percent from 2001 through 2004 along with the decline in the stock market, while future obligations have steadily increased due to declines in the interest rates used to calculate the liabilities of plans.
- Management and labor union decisions. Airline management has funded their pension plans far less than they could have. For example, PBGC examined 101 cases of airline pension contributions from 1997 through 2002; these cases covered 18 pension plans sponsored by 5 airlines.[14] During this time, $28.2 billion dollars could have been contributed to these pension plans on a tax-deductible basis; actual contributions amounted to $2.4 billion, or about 8.5 percent of what they could have contributed, despite earning profits in 1997-2000 (see figure 9).[15] The maximum deductible contribution was made in only 1 of the 101 pension contribution cases examined by PBGC. In addition, management and labor have sometimes agreed to salary and benefit increases beyond what could reasonably be afforded. For example, in the spring of 2002, United's management and mechanics reached a new labor agreement that increased the mechanics' pension benefit by 45 percent, but the airline declared bankruptcy the following December.

For more information, see GAO, *Private Pensions: Publicly Available Reports Provide Useful but Limited Information on Plans' Financial Condition* (GAO-04-395) March 31, 2004.

[14] Of 108 possible cases, 4 were eliminated because the carrier was in bankruptcy; in 3 cases data was missing.

[15] Pension funding rules permit sponsors to choose the interest rate used to determine the maximum deductible pension contribution permitted from an interest rate "corridor" – a limited range of interest rates. In calculating the maximum deductible contribution, a higher interest rate produces a lower contribution limit. In the 101 cases PBGC examined from 1997 through 2002, airlines used the highest interest rate permitted in 86 cases, and the lowest interest rate permitted in 1 case. Using the interest rates chosen by the airlines, the maximum deductible contribution was calculated to be $9.1 billion for these 101 cases. PBGC recalculated the maximum deductible contribution in each case using the lowest interest rate the airline could have chosen to determine the maximum deductible contribution of $28.2 billion.

Figure 9: Comparison of Legacy Airline Pension Maximum and Actual Contributions and Operating Profits, 1997-2002 (Billions of dollars)



Source: PBGC and DOT.

- Pension funding rules are flawed. Existing laws and regulations governing pension funding and premiums have also contributed to the underfunding of defined benefit pension plans. As a result, financially weak plan sponsors, acting within the law, have not only been able to avoid contributions to their plans, but also increase plan liabilities that are at least partially insured by PBGC. Under current law, reported measures of plan funding have likely overstated the funding levels of pension plans, thereby reducing minimum contribution thresholds for plan sponsors. And when plan sponsors were required to make contributions, they often substituted "account credits" for cash contributions, even as the market value of plan assets may have been in decline. Furthermore, the funding rule mechanisms that were designed to improve the condition of poorly funded plans were ineffective.[16]

[16] For further information, see U.S. Government Accountability Office, *PRIVATE PENSIONS: Recent Experiences of Large Defined Benefit Plans Illustrate Weaknesses in Funding Rules*, GAO-05-294, (Washington, D.C.: May 31, 2005).

Other legal plan provisions and amendments, such as lump sum distributions and unfunded benefit increases may also have contributed to deterioration in the funding of certain plans. If large numbers of participants in an underfunded plan elect to receive their pension benefits in a lump sum, it can create the effect of a "run on the bank" and exacerbate the possibility of a plan's insolvency as plan assets are liquidated more quickly than expected. Plan funding can also be worsened by unfunded benefit increases. When a pension plan is underfunded and the plan sponsor is also in poor financial condition, there is an incentive, known as moral hazard, for the plan sponsor and employees to agree to pension benefit increases because at least part of the benefit increases may be insured by PBGC.[17]

Finally, the premium structure in PBGC's single-employer pension insurance program does not encourage better plan funding. While PBGC premiums may be partially based on plan funding levels, they do not consider other relevant risk factors, such as the economic strength of the sponsor, plan asset investment strategies, the plan's benefit structure, or the plan's demographic profile.[18] In addition, current pension funding and pension accounting rules may also encourage plans to invest in riskier assets to benefit from higher expected long-term rates of return.[19]

The cost to PBGC and participants of defined benefit pension terminations has grown in recent years as the level of pension underfunding has deepened. When Eastern Airlines defaulted on its pension obligations of nearly $1.7 billion in 1991, for example, claims against the insurance program totaled $530 million in underfunded pensions and participants lost $112 million. By comparison, the US Airways and United pension terminations cost PBGC $9.6 billion in

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17 Currently, some measures exist to limit the losses incurred by PBGC from newly terminated plans. PBGC is responsible for only a portion of all benefit increases that the sponsor adds in the 5 years leading up to termination.

18 The current premium structure relies heavily on flat-rate premiums, which are unrelated to risk. PBGC also charges plan sponsors a variable-rate premium based on the plan's level of underfunding; however, not all underfunded plans are required to pay it.

19 In determining funding requirements, a higher expected rate of return on pension assets means that the plan needs to hold fewer assets in order to meet its future benefit obligations. Under current accounting rules, the greater the expected rate of return on plan assets, the greater the plan sponsor's operating earnings and net income. However, with higher expected rates of return comes greater risk of investment loss.

combined claims against the insurance program and reduced participants' benefits by $5.2 billion (see table 2).

Table 2: Airline Pension Termination Information (in millions of dollars)

Airline	Fiscal year of plan terminations	Benefit liability	PBGC liability	Net claim on PBGC	Estimated participant losses
Eastern	1991	1,686	1,574	530	112
PanAm	1991, 1992	1,267	1,212	753	55
TWA	2001	1,729	1,684	668	45
US Airways	2003, 2005	7,900	5,926	3,026	1,974
United	2005	16,800	13,600	6,600	3,200

Note: "Benefit liability" is the full value of the benefits promised to participants and their beneficiaries immediately prior to plan termination. "PBGC liability" is the amount that PBGC pays after agency limits are imposed. "Net claim on PBGC" is the difference between the PBGC liability and the assets PBGC obtains from the plan. "Estimated participant losses", the difference between the Benefit Liability and the PBGC liability, and equals the value of the benefits that plan participants and their beneficiaries lose when PBGC takes over a plan.

Source: PBGC.

In recent pension terminations, active and high salaried employees generally lost more of their promised benefits compared to retirees and low salaried employees because of statutory limits. For example, PBGC generally does not guarantee benefits above a certain amount, currently $45,614 annually per participant at age 65.[20] For participants who retire before 65 the benefits are even less; participants that retire at age 60 are currently limited to $29,649. Commercial pilots often end up with substantial benefit cuts when their plans are terminated because they generally have high benefit plans and are also required by FAA to retire at age 60. Far fewer nonpilot retirees are affected by the maximum payout limits. For example, at US Airways fewer than 5 percent of retired mechanics and attendants faced benefit cuts as a result of the pension termination. Tables 3 and 4 summarize the expected cuts in benefits for different groups of United's active and retired employees.

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[20] This guarantee level applies to plans that terminate in 2005. The amount guaranteed is adjusted (1) actuarially for the participant's age when PBGC first begins paying benefits and (2) if benefits are not paid as a single-life annuity. Because of the way the Employee Retirement and Income Security Act of 1974 (ERISA), as amended, allocates plan assets to participants, certain participants can receive more than the PBGC guaranteed amount.

Table 3: United Airlines Active Employee Pension Termination Benefit Cuts

Plan	Active employees in plan	Actives employees with benefits cuts	Extent of benefit cut		
			1% to <25%	≥ 25% to < 50%	≥ 50%
Management, Administrative, and Public Contact Employees	20,784	19,231	1,696	15,885	1,650
Ground Employees	16,062	16,062	11,448	3,441	1,173
Flight Attendants	15,024	11,109	1,305	7,067	2,737
Pilots	7,360	7,270	3,927	2,039	1,304

Source: PBGC.

Note: Calculation estimates made with 1/1/2005 seriatim data

Table 4: United Airlines Retiree Pension Termination Benefit Cuts

Plan	Retirees in plan	Retirees with benefits cuts	Extent of benefit cut		
			≥1% to <25%	≥25% to <50%	≥50%
Management, Administrative, and Public Contact Employees	11,360	2,996	2,816	104	76
Ground Employees	12,676	4,961	4,810	121	30
Flight Attendants	5,108	29	27	1	1
Pilots	6,087	3,041	1,902	975	164

Source: PBGC.

Note: Calculation estimates made with 1/1/2005 seriatim data

It is important to emphasize that relieving legacy airlines of their defined benefit funding costs will help alleviate immediate liquidity pressures, but does not fix their underlying cost structure problems, which are much greater. Pension costs, while substantial, are only a small portion of legacy airlines' overall costs. As noted previously in figure 3, the cost of legacy airlines' defined benefit plans accounted for a 0.4 cent, or 15 percent difference between legacy and low cost airline unit costs. The remaining 85 percent of the unit cost differential between legacy and low cost carriers is attributable to factors other than defined benefits pension plans. Moreover, even if legacy airlines terminated their defined benefit plans it would not fully eliminate this portion of the unit cost differential because, according to labor officials we interviewed, other plans would replace them.

Widely reported recent large plan terminations by bankrupt sponsors such as United Airlines and US Airways and the resulting adverse consequences for plan participants and the PBGC have pushed pension reform into the spotlight of national concern. The effect of various proposals to reform pension requirements on airlines, PBGC, and plan participants will vary. The funding relief afforded by PFEA will expire at the end of this year and many agree that the current rules are flawed and must be fixed. Various proposals have been made to correct these rules and shore up the PBGC guaranteed plans, and these proposals are still being debated. The administration has proposed tightening the funding rules among other changes. Some of the legacy airlines with large shortfalls have endorsed another bill in the Senate for a 25-year payback period if current plans are frozen. However, one legacy airline that has better funded its plan, while supporting a longer payback period, opposes freezing their plan.

Concluding Observations

While the airline industry was deregulated 27 years ago, the full effect on the airline industry's structure is only now becoming evident. Dramatic changes in the level and nature of demand for air travel combined with an equally dramatic evolution in how airlines meet that demand have forced a drastic restructuring in the competitive structure of the industry. Excess capacity in the airline industry since 2000 has greatly diminished airlines' pricing power. Profitability, therefore, depends on which airlines can most effectively compete on cost. This development has allowed inroads for low cost airlines and forced wrenching change upon legacy airlines that had long competed based on a high-cost business model.

The historically high number of airline bankruptcies and liquidations is a reflection of the industry's inherent instability. However, this should not be confused with causing the industry's instability. There is no clear evidence that bankruptcy has contributed to the industry's economic ills, including overcapacity and underpricing, and there is some evidence to the contrary. Equally telling is how few airlines that have filed for bankruptcy protection are still doing business. Clearly, bankruptcy has not afforded these companies a special advantage.

Bankruptcy has become a means by which some legacy airlines are seeking to shed their costs and become more competitive. However, the termination of pension obligations by United Airlines and US Airways has had substantial and wide-spread effects on the PBGC and thousands of airline employees, retirees, and other beneficiaries. Liquidity problems, including $10.4 billion in near term pension contributions, may force additional legacy airlines to follow suit. Some airlines are seeking legislation to allow more time to fund their pensions. If their plans are frozen so that future liabilities do not continue to grow, allowing an extended payback period may reduce the likelihood that these airlines will file for bankruptcy and terminate their pensions in the coming year. However, unless these airlines can reform their overall cost structures and become more competitive with low cost competition; this will be only a temporary reprieve.

As we have previously reported, the Congress should consider broad pension reform that is comprehensive in scope and balanced in effect.[21] Revising plan funding rules is an essential component of comprehensive pension reform. For example, we testified that Congress should consider the incentives that pension rules and reform may have on other financial decisions within affected industries. Under current conditions, the presence of PBGC insurance may create certain "moral hazard" incentives – struggling plan sponsors may place other financial priorities above "funding up" its pension plan because they know PBGC will pay guaranteed benefits. Further, because PBGC generally takes over underfunded plans of bankrupt companies, PBGC insurance may create an additional incentive for troubled firms to seek bankruptcy protection, which in turn may affect the competitive balance within the industry.

In light of the intrinsic problems facing the defined benefit system, meaningful and comprehensive pension reform is required to ensure that workers and retirees receive the benefits promised to them. Ideally, effective reform would incorporate many elements, among them:

- improving the accuracy of plan funding measures while minimizing complexity and maintaining contribution flexibility;
- revising the current funding rules to create incentives for plan sponsors to adequately finance promised benefits;
- developing a more risk-based PBGC insurance premium structure and providing incentives for sponsors to fund plans adequately;
- addressing the issue of underfunded plans paying lump sums and granting benefit increases;
- modifying PBGC guarantees of certain plan benefits
- resolving outstanding controversies concerning hybrid plans by safeguarding the benefits of workers regardless of age; and
- improving plan information transparency for pension plan stakeholders without overburdening plan sponsors.

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[21] See GAO-04-90; GAO-05-108T; GAO, *Pension Benefit Guaranty Corporation: Single-Employer Pension Insurance Program Faces Significant Long-Term Risks,* GAO-03-873T (Washington, D.C.: Sept. 4, 2003); *Pension Benefit Guaranty Corporation: Long-Term Financing Risks to Single-Employer Insurance Program Highlight Need for Comprehensive Reform,* GAO-04-150T (Washington, D.C.: Oct. 14, 2003); *Private Pensions: Changing Funding Rules and Enhancing Incentives Can Improve Plan Funding,* GAO-04-176T (Washington, D.C.: Oct. 29, 2003).

The various proposals for comprehensive reform advanced by the Administration and various members of Congress could be a critical first step in addressing part of the long-term stability of the private defined benefits system. While we understand the legacy airline's liquidity pressures and their request for assistance, the uncertain efficacy of industry-specific relief needs to be weighed against the potential effects on both the industry and the government. At this point, because of a lack of a thorough understanding of those effects, particularly as they might change under various specific legislative proposals, we would suggest proceeding carefully, relying on sound fiduciary principles as a guide.

This concludes my statement. I would be pleased to respond to any questions that you or other Members of the Subcommittee may have at this time.

***

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(544108)

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Opening Statement for the Honorable Eddie Bernice Johnson
House Subcommittee on Aviation
Airline Pensions: Avoiding Further Collapse
Wednesday, June 22, 2005 – 2167 RHOB

EB Johnson

Thank you Mr. Chairman.

I want to thank you and Ranking Member Costello for holding this important and timely hearing examining the status of airline pension plans.

Obviously, the recent pension default by United Airlines brings a totally new meaning to the term "shock and awe".

The airline's pension dump adversely impacts one-hundred and twenty thousand current and former employees and shifts $6.6 billion to an already deficit-laden Pension Benefit Guaranty Corporation.

The corporation's deficit on September 30th of last year was at an all-time high of $23 billion. Further, because of risks to the entity's long-term financial health, the GAO has placed the PBGC's single-employer program on its high-risk list of agencies with significant vulnerabilities to the federal government.

This type of retirement threat is a shot across the bow to every hardworking American who has ever contemplated retirement.

In her testimony before the Senate Finance Committee two weeks ago today, Patricia Friend, International President of the Association of Flight Attendants summed it best this way, "These are not careless people who failed to plan for their retirement. <u>They worked hard</u>. <u>They saved as much as they could</u>, <u>and they invested when possible</u>.

Their only mistake was one of trust: They trusted the retirement promises United made for decades."

Mr. Chairman, hardworking Americans that place trust in their employers deserve better than waking up to the morning news and discovering that their retirement security has just been kicked out the door.

Often times, pensions make the difference between adequacy in retirement and poverty in retirement. Real pensions are workers best bet for retirement security on top of Social Security.

Unfortunately, less than half of the American workforce does not have a pension to supplement Social Security.

We must find a way to keep large corporations from using the bankruptcy courts to dump pension plans.

Companies should not be allowed to abuse the system and dump the plans only to be picked up by the Private Pension Insurance Program.

Employees must be given meaningful and reliable information about their pensions.

As I close, I want to thank our witnesses that have come before us to testify this afternoon.

I look forward to their testimony, as I am particularly interested in their thoughts on strengthening funding rules for pension plans, improved transparency for employees, and what we as a body may do to assist them.

Thank you.

OPENING STATEMENT OF
THE HONORABLE JAMES L. OBERSTAR
AVIATION SUBCOMMITTEE
AIRLINE PENSIONS: AVOIDING FURTHER COLLAPSE
JUNE 22, 2005

I want to thank you, Chairman Mica and Ranking Member Costello for calling today's hearing to examine the airline pension crisis. I was here in Washington, as Administrative Assistant to my predecessor John Blatnik, when Congress approved the Employee Retirement Income Security Act of 1974, commonly known as ERISA. ERISA provided the framework for the Pension Benefit Guaranty Corporation (PBGC), which was created to protect the pensions of participants and beneficiaries covered by private sector, defined benefit plans. Because of the PBGC, thousands of workers have been able to enjoy a measure of retirement security when their employer is no longer able to provide for their pensions. PBGC has carried out its mandate very well, with over 3,500 pension plans under its protection.

As of September 30, 2004, the steel industry accounted for 49 percent of all claims in PBGC trusteed plans. However, when you include claims for probable terminations that have become trusteed or announced since September, airlines now eclipse steel. The PBGC is currently running a $23 billion deficit, with a potential exposure of billions more if other airlines move to terminate their plans.

A combination of factors contributed to the under-funding of defined benefit pension programs, including the dramatic slide in the stock market, low interest rates, and the steady decline of 30-year Treasury bond rates. However, a closer examination of the PBGC's current funding rules, which has allowed for the masking of the airlines' true pension deficiencies, is warranted. I look forward to hearing from Bradley Belt, Executive Director of the PBGC, regarding the current airlines pension crisis, changes that need to be made to protect those employees with viable defined benefit pension plans, and how to ensure the continued solvency of the PBGC.

Under the PBGC rules, companies with under-funded pension plans were required to make additional contributions, the so-called "deficit reduction contributions (DRC)." In 2004, we provided relief for the airline and steel industries from having to make the full DRC payments so that these industries would have the ability to recover from financial distress. However, as we have seen with US Airways and United Airlines, that relief came a little too late to save their workers' pension plans. With continued pressure on the legacy airlines from low cost competition, high fuel costs and the end of the two-year moratorium on full DRC pension contributions, we are coming dangerously close to seeing more bankruptcies in this industry, with the potential for further termination of worker's pension plans. To that end, I look forward to hearing from Air Line Pilots Association as well as the Association of Flight Attendants on the impact of the plan terminations at US

Airways and United on their respective members, and their thoughts on moving ahead to protect remaining airline worker's pension benefits.

There are also several bills that are currently under consideration this Congress to help prevent the shedding of pension plans, not only by the airline industry, but by other industries as well. I am interested in the witnesses' views of these various bills and how they might aid in ensuring the continued viability of existing pension plans.

I look forward to hearing from the witnesses regarding their thoughts about how to avoid further collapse of airline pensions.

Statement of Rep. Jon Porter (R-NV)
House Transportation and Infrastructure Committee
Subcommittee on Aviation
Airline Pensions: Avoiding Further Collapse
Wednesday, June 22, 2005

Mr. Chairman, I thank you for holding this hearing today to examine the current status of airline pension plans, the impact of the termination of both United's and US Airways' plans, and how further terminations may be avoided.

Over the last four years, the airline industry has recorded over $32 billion in losses, with an additional $5 billion in losses projected in 2005. A variety of factors have contributed to these losses including the economic slowdown, a decline in business travel, the aftermath of the 9/11 attacks, the SARS epidemic, increased competition from low-cost carriers, and soaring fuel prices.

In addition to all of these difficulties, a combination of historically low interest rates and poor stock market returns have resulted in the pension plans of many airlines becoming significantly underfunded in a short period of time. Given that defined benefit pension plans on average held approximately half of their assets in stocks from 1995 to 2000, the decline in stock prices meant a sharp decline in the value of many plans' assets.

In addition, 30-year Treasury bond rates, which served as the benchmark for the rate used by plans to calculate pension liabilities, generally fell steadily, raising liabilities. The combination of lower asset values and higher pension liabilities had a serious adverse effect on overall defined benefit funding levels.

Airlines are having great difficulty coming up with the funding contributions required to return their pension plans to full funding. Already, two airlines in bankruptcy – US Airways and United Airlines -- have either terminated their plans, or are in the process of doing so. As part of US Airways' two bankruptcies, the Pension Benefit Guaranty Corporation (PBGC) agreed to assume responsibility for all of its defined benefit plans, and will pay US Airways' current and future retirees an estimated $3 billion worth of benefits. United's total pension shortfall is estimated at $9.8 billion. The PBGC is expected to take over United's plans, as well.

PBGC generally does not guarantee benefits above a certain amount, currently $45,614 annually per participant at age 65. Because of this limit, higher-paid employees, such as pilots, may experience significant pension cuts if their plan is taken over by the PBGC. Additionally, benefit increases arising from plan amendments in the five years immediately preceding plan termination are not fully guaranteed, although PBGC will pay a portion of such increases. Further, PBGC's guarantee is limited to the monthly straight life annuity the participant would receive if he or she were to commence the annuity at the plan's normal retirement age. Therefore, employees who retired at an early age may experience significant benefit reductions under the PBGC.

On average, United employees, should receive about 80 percent of their accrued pension benefits, while US Airways employees should receive about 73 percent.

Because the PBGC receives no federal tax dollars and its obligations are not backed by the full faith and credit of the United States, losses suffered by the insurance trust fund must, under current law, be covered by higher premiums. Therefore, healthy companies subsidize weak companies with underfunded plans, and may also face the prospect of having to compete against a rival firm that has shifted a portion of its labor costs onto the government.

Mr. Chairman, this is a complex issue with a multitude of different factors that must be considered. I thank you again for holding this hearing and I look forward to hearing from the witnesses. I yield back.

Statement Rep. Tom Price
House Committee on Transportation and Infrastructure
Subcommittee on Aviation Hearing: Airline Pensions: Avoiding Further Collapse
Wednesday, June 22, 2005

Thank you, Chairman Mica, Ranking Member Costello, and the rest of the Aviation Subcommittee for allowing me to attend this very important hearing on airline pensions. With your permission I will submit my statement for the record so that we can move along quickly.

The airline industry continues to amass losses as the industry becomes more dynamic both externally and internally. Losses of over $30 billion during the last four years have proven that the business model used by legacy carriers is outdated and under duress by high fuel prices and post 9/11 repercussions.

A primary component playing into the equation of legacy carrier viability is the pension systems currently in place. The current model of defined benefit pension plans and the rules associated with it have come under scrutiny as two legacy carriers; making up approximately twenty-percent of the domestic airline market recently terminated their employee pension plans.

There are no winners when airlines default on their pension plans. Employees now are planning for a retirement with a fraction of what they were originally promised; furthermore, the Pension Benefit Guaranty Corporation (PBGC) – the government agency and guarantor of all pension plans is put more and more into the red. Eventually, the point will be reached when taxpayers have to bailout the PBGC if no action is taken.

The need for industry-specific reform couldn't be greater. The statement made last week before the House Committee on Education and the Workforce by Mr. Bart Pushaw, an actuary with Milliman, Inc., and an expert on pensions, addressed this best:

> *"It seems to make a lot of sense that if there's one or two bad apples – and I don't mean to say bad in a sense of malfeasance or anything like that – but there's one or two bad apples in the barrel and the rest of the apples as both my panelists have mentioned are really doing very, very well, then perhaps it does make sense to deal very surgically and in a very limited way with those industries that you've mentioned."*

Dumping pension obligations onto the PBGC will only exacerbate the current underfunding crisis. The PBGC does not receive any federal tax dollars and its obligations are not backed by the full faith and credit of the United States. Under current law, these obligations must be met with higher premiums. Therefore, healthy companies wind up bailing out weaker companies.

The solution that I have proposed, H.R. 2106 – The Employee Pension Preservation and Taxpayer Protection Act, provides airlines with the flexibility needed to fund their defined benefit pension systems.

Under the voluntary plan, an airline must freeze its plan or fund any new benefits in the year that they accrue. Then the airline is given 25 years to spread out their plan's unfunded accrued liability and pay it down using stable, long-term assumptions. If an airline does falter, the Pension Benefit Guaranty Corporation's benefit guarantees are fixed at the time of the pension freeze, thus insulating the PBGC and American taxpayers.

This common-sense initiative is a responsible approach to the airline industry's current pension funding problems. Airline carriers are not exempted from their obligations. In fact, they have to make sizeable contributions each year in order to reduce their liability and ensure accrued benefits are being paid. Moreover, the Employee Pension Preservation and Taxpayer Protection Act does not provide any form of subsidy from the federal government.

By addressing the airline pension problem in this manner, it decreases the likelihood for a taxpayer bailout of the Pension Benefit Guaranty Corporation. Moreover, airlines maintain their pension programs and fund these promises without shedding the liabilities.

Airline employees benefit because they will receive the full benefits accrued prior to the freeze. The measure is also beneficial for the economy because it preserves a vital source of jobs and keeps the economy humming.

Mr. Chairman, industry-specific reform that protects employees and taxpayers alike is what H.R. 2106 is all about. The dynamics of the airline industry have proven that the business model used to fund pension plans with a defined benefit system are no longer a viable option. My initiative offers a solution to this crisis, a solution that ensures the retirements of those who have worked hard to earn their pensions.

###

Congressman John T. Salazar
Opening Statement
Subcommittee on Aviation: Airline Pensions Hearing
June 22, 2005

- Thank you Chairman Mica and Ranking Member Costello for holding this important hearing today.

- I am hopeful this committee can be a part of the conversation regarding airline pension plans and the future of the airlines industry.

- I was disappointed last month when the Federal Bankruptcy Court released United Airlines from its pension obligations.

- I fear this unprecedented decision could have wide ranging consequences on both the economic security of airline workers and retirees, and the financial health of the Pension Benefit Guaranty Corporation.

UNITED EMPLOYEES

- United's employees will face a $3 billion cut in benefits if the court decision is allowed to go through – that's nearly a 20% deduction.

- These are employees who have been loyal to their company, who have made wage concessions in the interest of the company's long term financial health…

- …And they believed their company would honor its promise to a secure retirement.

- But the Court's decision allows United to turn its back on employees in an attempt to emerge from bankruptcy.

PBGC FINANCIAL SOUNDNESS

- Now I am a reasonable man and I believe we cannot allow the airline industry to continue its spiral downward.

- I represent a rural area that relies on the presence of multiple carriers to bring down prices for consumers and to expand into new service areas.

- But I am concerned that if we continue down this path, we will grind down the financial soundness of the PBGC.

- Given the fund's current deficit, I worry about its ability to sustain another round of bankruptcy filings and the dumping of additional pension plans on the back of the US taxpayer.

- I have cosponsored legislation, HR 2327, that would trigger a six-month moratorium on any pension plan dumping.

- A moratorium would give United workers time at the bargaining table to save what they worked a lifetime for -- their retirement security.

- And during this time, Congress should work towards meaningful pension reform legislation to address future pension crises.

- I look forward to hearing from the representatives of both the PBGC and the GAO on this topic.

CONCLUSION

- Again, I thank the Chairman and Ranking Member for their leadership on this issue. My hope is that Congress, industry and the employees of the airline companies can work together to secure defined benefit plans and ensure promises are kept.

Testimony of Mark S. Streeter, CFA
Managing Director
North American Credit Research
JP Morgan Securities
Before the Subcommittee on Aviation
United States House of Representatives
June 22, 2005

Chairman Mica and Members of the Committee, thank you for inviting me to speak this afternoon. My name is Mark Streeter and I am responsible for airline credit research at JPMorgan. I would like to provide the Committee with a credit perspective on the airline industry and how the pension issue and other economic factors will continue to impact airline credit quality and access to capital. I will focus my comments on the remaining legacy airline defined benefit plan sponsors, specifically Delta Air Lines, Northwest Airlines, Continental Airlines, and AMR Corp. Please note that my testimony and statements are my personal views and do not represent the official position of JPMorgan.

Are the credit markets concerned?
Unfortunately for the airlines, the credit markets are very concerned about airline industry fundamentals and looming pension obligations, particularly at Delta and Northwest.

Using credit default swaps, it is fairly easy to estimate market implied default probabilities (Exhibit I).

Exhibit I: Credit Market Implied Cumulative Default Probabilities

Cumulative Default Probability Before Time Period Expires

	0.5-Yr	1-Yr	2-Yrs	3-Yrs	4-Yrs	5-Yrs
AMR Corp	6.9%	13.1%	32.2%	45.0%	57.0%	61.2%
Continental	7.3%	13.9%	33.4%	46.5%	58.5%	62.8%
Northwest	24.7%	43.1%	59.9%	70.8%	77.8%	82.9%
Delta	32.8%	54.6%	69.2%	79.4%	85.4%	89.5%

Source: JPMorgan, based on 16-June-05 credit default swap quotes assuming 10% recovery in bankruptcy

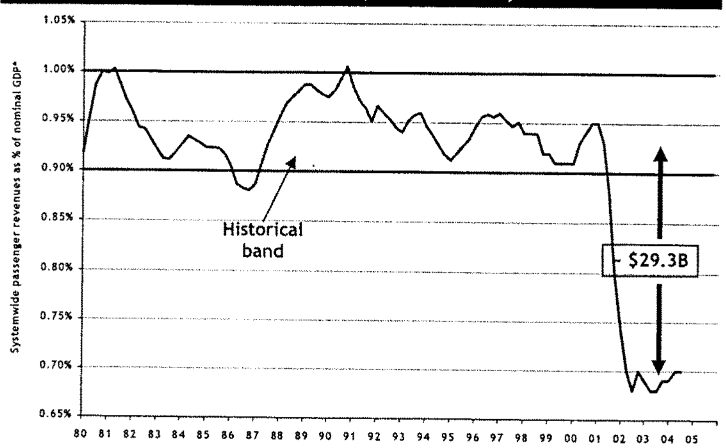
Based on current prices, the market believes with about 43% certainty that Northwest will file for Chapter 11 protection by June 10, 2006. For Delta, the implied one-year default risk is nearly 55%. Implied one-year default risk for AMR and Continental is relatively low, but rising to more than 50% when I extend the time frame to four years. These figures are slightly skewed by the sheer number of investors looking to hedge existing exposure to the airlines, but nonetheless the data are rather startling.

Yields on unsecured debt obligations are incredibly high. Delta bonds due in 2009 offer an annualized 40% yield and are trading at 35 cents to the dollar. Northwest bonds due that same year offer a 37% annual yield and are trading at 46 cents to the dollar.

Why are the credit markets worried?
There are several reasons why the credit markets are worried. You have heard others testify about the disconnect between industry revenue and overall economic growth since the attacks of September 11 (Exhibit II). Increased low cost competition, the decline in business travel, internet-driven pricing transparency, and SARS are major factors.

Exhibit II: Industry revenue may not recover from the dislocation of 9/11

Historically exceeding 0.90% of GDP, portion retained by U.S. Airlines now only 0.70%

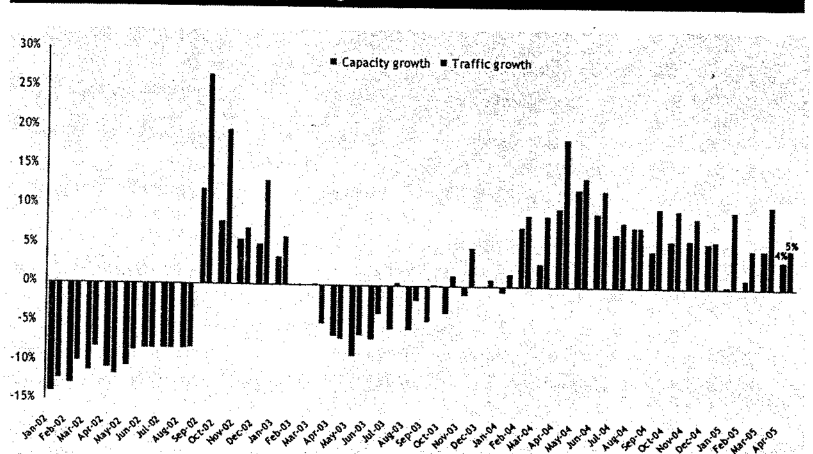


*Four-quarter rolling passenger revenue derived from government filings of major and national passenger airlines.
Source: Air Transport Association, U.S. Bureau of Economic Analysis; U.S. Department of Transportation Form 41 reports.

The industry has responded to the new environment by cutting costs and shifting capacity to more profitable international routes. For 24 months running, traffic growth has exceeded capacity growth (Exhibit III). Load factors are at record levels, yet yields remain fairly anemic despite numerous successful fare increases year-to-date (Exhibits IV-V).

Exhibit III: Traffic continues to grow faster than capacity

Capacity (ASM) and traffic (RPM) y/y % change



Source: Air Transport Association.

Exhibit IV: People flying more, more passengers stuck in middle seats

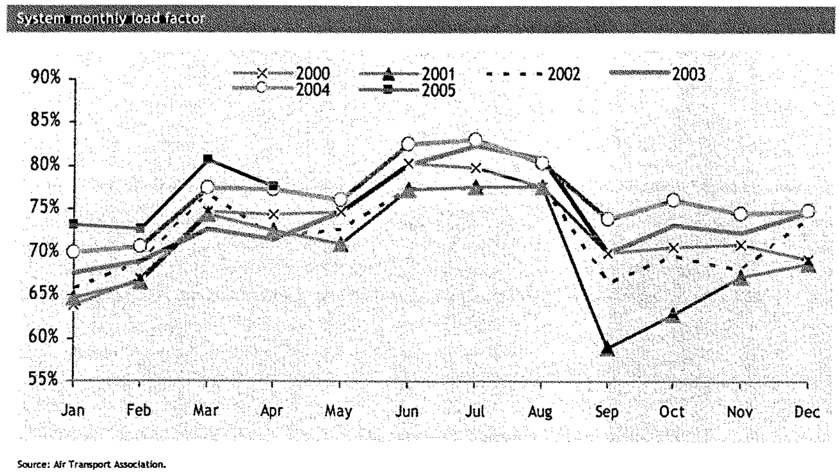
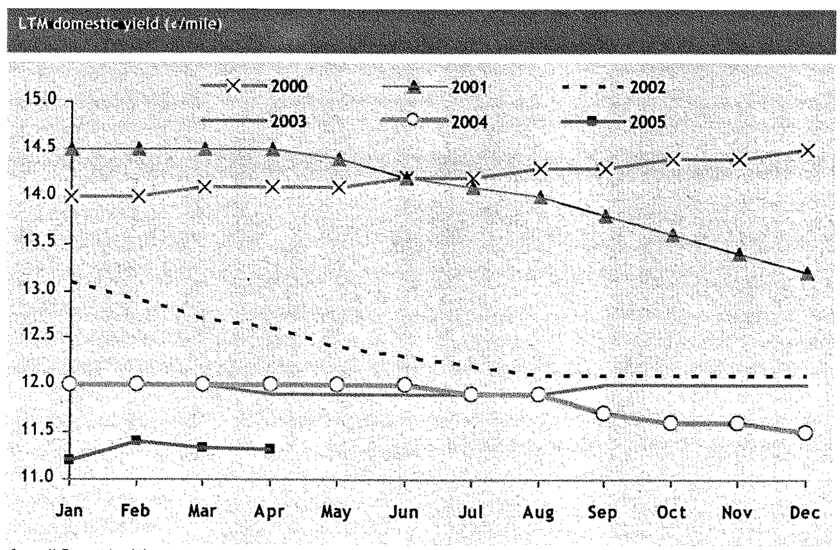
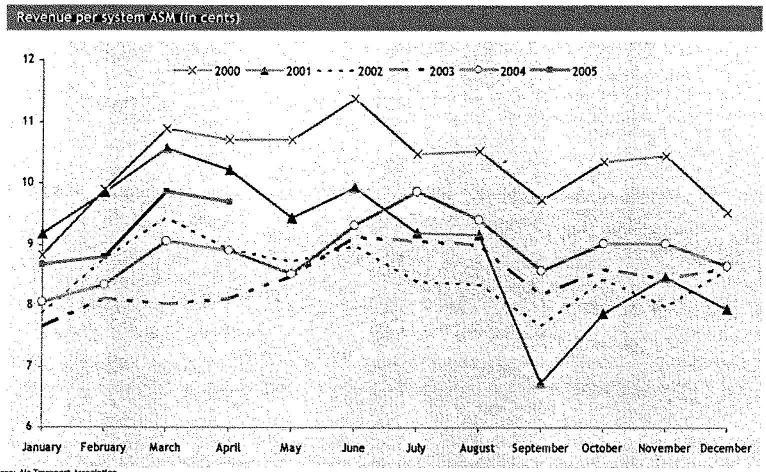


Exhibit V: However, airfares have not kept pace with U.S. inflation



One bit of good news is that unit revenues are higher year over year as a result of the strong traffic performance despite the stagnant yield environment (Exhibit VI).

Exhibit VI: Traffic drives improving unit revenue trends despite weak yields

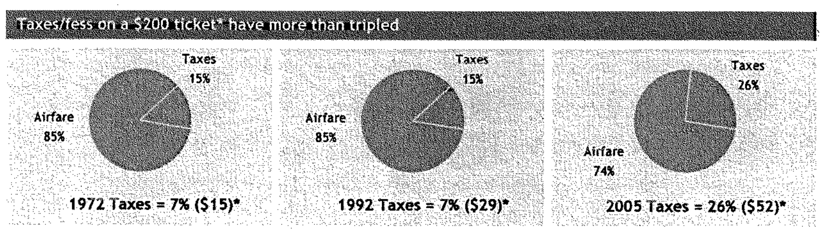


Source: Air Transport Association.

Nevertheless, rising passenger taxes and fuel costs, which are beyond the immediate control of the airlines, have had a pronounced impact on bottom line profits.

The industry's tax burden is compounded by the lack of pricing power to effectively offset the government's need to raise proceeds to fund security measures (Exhibit VII).

Exhibit VII: Is airline travel a sin? Tax burden suggests so...



*Sample itinerary assumes one-stop domestic round-trip with maximum passenger facility charge (PFC) per airport; $200 total price includes taxes and fees.
Source: ATA research.

Federal consumption taxes and fees on flyers*

PRODUCT	%
Plane Ticket: One-Stop ($100)[1]	44.9
Plane Ticket: Non-Stop ($100)[1]	26.0
Plane Ticket: One-Stop ($200)[1]	26.0
Plane Ticket: One-Stop ($300)[1]	19.6
Pack of Cigarettes ($4.50)[2]	18.2
Plane Ticket: Non-Stop ($200)[1]	16.5
Plane Ticket: Non-Stop ($300)[1]	13.3
Heavy Truck / Trailer / Tractor	12.0
Gallon of Gasoline ($1.60)[3]	11.5

PRODUCT	%
Heavy Firearms / Ammunition	11.0
Distilled Spirits ($20)[4]	10.7
Pistol or Revolver	10.0
Can of Beer ($1.00)[5]	5.0
Telephone Service	3.0
Ship Ticket ($1,000)[6]	0.3
Bus Ticket	0.0
Rail Ticket	0.0
Luxury Vehicle[7]	0.0

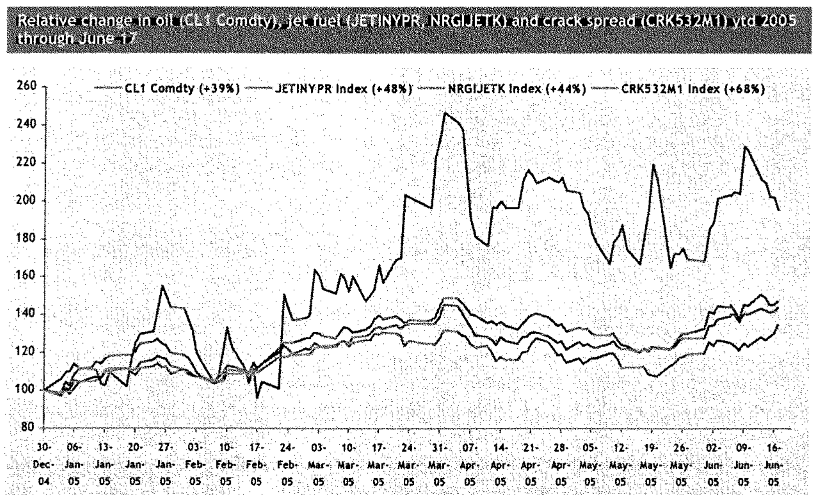
[1] Round-trip with federally approved $4.50 PFC
[2] Taxed at 82¢ per pack
[3] Taxed at 18.4¢ per gallon
[4] Taxed at $2.14 per 750-milliliter bottle
[5] Taxed at 5¢ per can
[6] Taxed at $3.00 per ticket
[7] Until 2003, 3.0% on value > $40,000

* The federal government also taxes the sale of tires over 40 pounds, coal, wine, vaccines, foreign-issued insurance and selected other items; analysis considers federal taxes and fees only - does not examine state and local taxes, which can be especially high on alcohol and tobacco.

Sources: ATA research; U.S. Internal Revenue Service; Bureau of Alcohol, Tobacco and Firearms (ATF).

It is no secret that oil prices have risen dramatically. More importantly, jet kerosene has been impacted severely by the shortage of refinery capacity. Year-to-date as of June 17, crude oil had risen 39% while jet fuel had increased 48% given the 68% increase in crack spreads (Exhibit VIII). I estimate that the eight successful fare increases in 2005 have thus far at best offset only half of the $16 per barrel increase in raw crude oil.

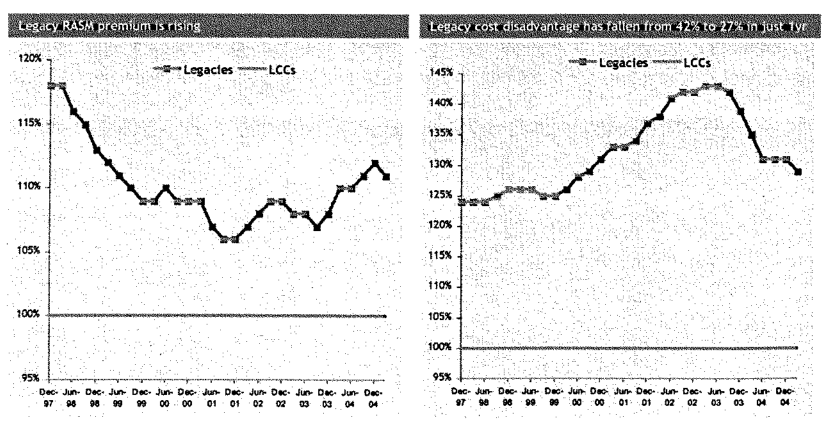
Exhibit VIII: Crack spreads have risen faster than crude prices ytd



Source: Bloomberg and JPMorgan.

Are the legacy airlines standing still?
Despite accusations to the contrary, the legacy airlines are not standing still. The legacy majors have increased their unit revenue premium relative to the low cost carriers by about five percentage points while narrowing the cost disadvantage by more than one third (Exhibit IX).

Exhibit IX: Legacy RASM premium rising, cost disadvantage falling

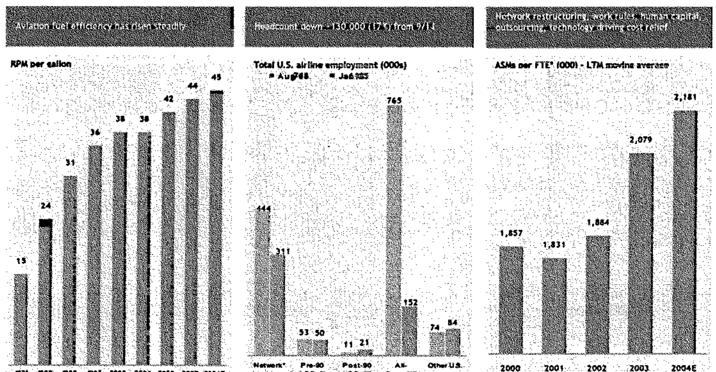


Source: Company reports and JPMorgan estimates.

Source: Company reports and JPMorgan estimates.

Fuel and employment productivity have improved, but not fast enough to offset the rise in input prices (Exhibit X).

Exhibit X: Fuel and employment productivity improving, but not fast enough



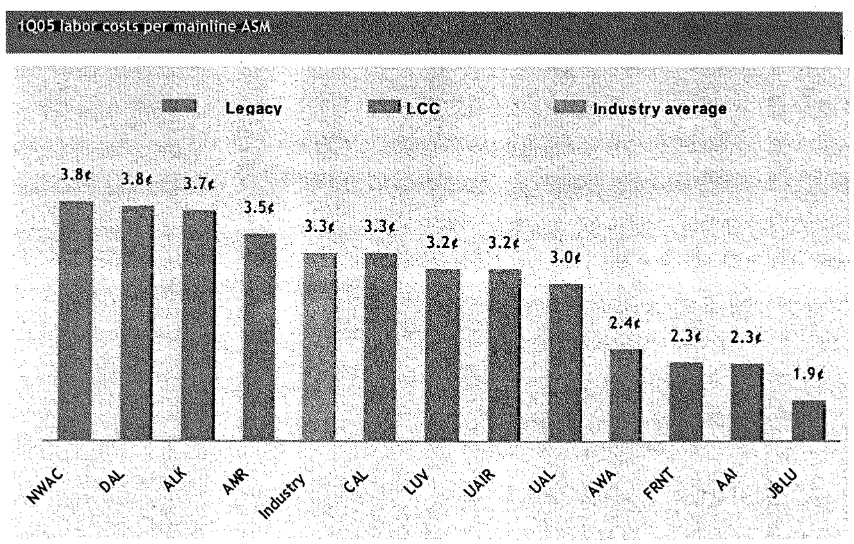
Source: ATA Cost Index for major/national carriers.

* ALK, AMR, CAL, DAL, NWAC, UALAQ, and UAWGQ.
** AWA, ATAH, and LUV.
*** AAI, FRNT, JBLU, and Spirit.
**** Air Transport Int'l, ASTAR/DHL, Express Net, Evergreen, FedEx, Gemini, Kalitta, Kitty Hawk, Polar, Ryan Int'l, Southern, Tradewinds, UPS, World.
Sources: Air Transport, Association, U.S. Department of Transportation P1a employment report; carrier reports for full-time and part-time workers.

*full-time equivalent.
Source: ATA Cost Index for major/national carriers.

The difference between legacy and low cost carrier labor costs has narrowed (Exhibit XI). Nevertheless, the pace of change has been frustratingly slow, evidenced by the current battle at Northwest between mechanics and management and the Continental flight attendants' refusal to approve a new contract.

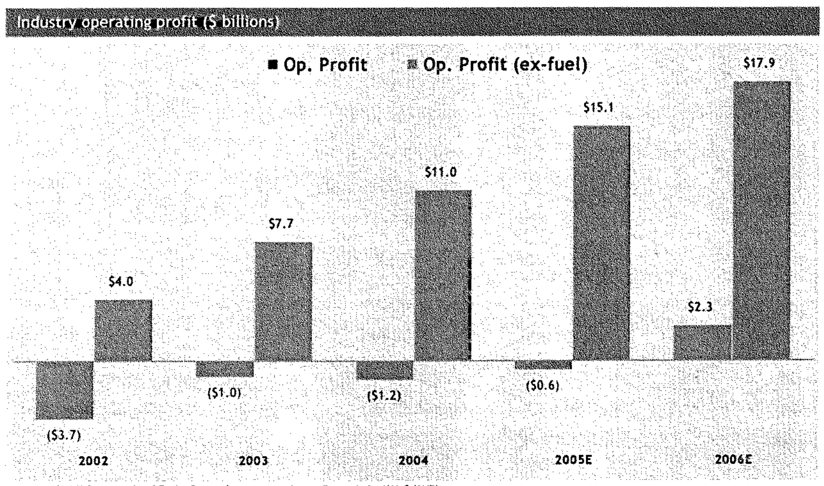
Exhibit XI : Labor costs converging, still higher for legacy carriers



Source: JPMorgan and company reports.

Given the state of the airline credit markets, counterparties are not willing to engage the legacy airlines in fuel hedges without cash collateral. As a practical matter, this makes it impossible for the legacy carriers to hedge fuel costs. I cannot overstate the impact of current and projected oil prices on profits. Based on oil prices from a few weeks back, I estimated then that the difference between operating profits and operating profits excluding fuel in 2005 for the mainline carriers will total more than $15 billion (Exhibit XII).

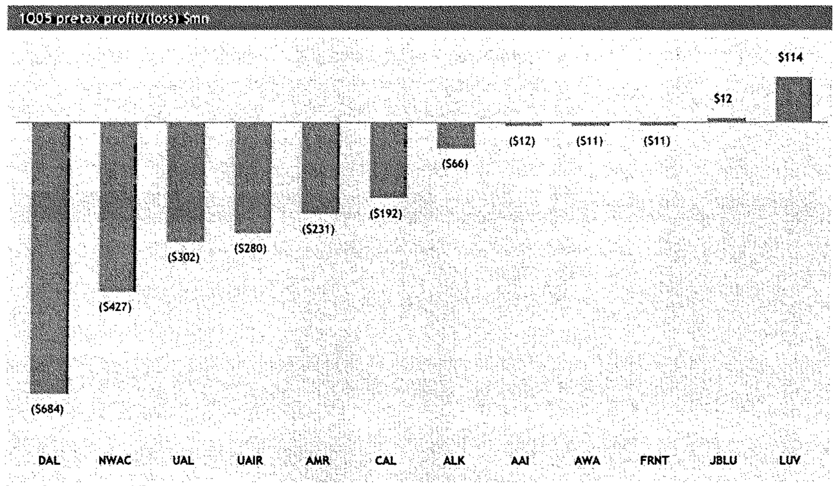
Exhibit XII: Ex-fuel profitability should continue to rise quickly



Note: Based on U.S. non-regional Equity Research coverage universe (ie. excludes UAL & UAIR).
Source: Company reports and JPMorgan estimates.

Results for 1Q05 were bifurcated (Exhibit XIII). The legacy airlines lost hundreds of millions each, while the low cost carriers reported much closer to break-even results in the seasonally weak quarter.

Exhibit XIII: 1Q05 profitability was weakest at legacy carriers



Source: Company reports and JPMorgan.

How severe is the cash burn?
My published base case year-end forecast of airline liquidity at the big four non-Chapter 11 legacy majors, assuming average fuel costs for the year that are about 14% lower than current prices, shows significant declines in unrestricted cash and investments absent any further incremental capital initiatives (Exhibit XIV). Specifically, AMR will burn more than $700 million net, Continental more than $200 million, and Delta and Northwest each more than $1 billion. Again, these cash burn estimates are inclusive of capital raised year-to-date.

Exhibit XIV: Base case YE05 airline liquidity snapshot

MAINLINE ASSUMPTIONS	AMR	CAL	DAL	NWAC
RPMs (M)	135,673	72,128	106,599	76,953
yr/yr % chg	*4.2%*	*9.7%*	*8.5%*	*5.0%*
ASMs (M)	178,509	89,919	137,929	94,424
yr/yr % chg	*2.6%*	*6.2%*	*6.1%*	*3.3%*
Load Factor	76.0%	80.2%	77.3%	81.5%
yr/yr % chg	*1.2%*	*2.6%*	*1.7%*	*1.3%*
Yield	11.70¢	11.25¢	10.74¢	11.40¢
yr/yr % chg	*1.3%*	*-0.2%*	*-3.0%*	*-0.9%*
Mainline RASM	8.89¢	9.03¢	8.30¢	9.29¢
yr/yr % chg	*3.0%*	*3.1%*	*-0.8%*	*0.7%*
Mainline CASM	9.82¢	9.85¢	9.43¢	10.87¢
yr/yr % chg	*1.0%*	*3.9%*	*-7.9%*	*5.4%*
Mainline CASM ex-fuel	7.34¢	7.46¢	7.06¢	8.25¢
yr/yr % chg	*-3.7%*	*-2.6%*	*-15.8%*	*0.9%*
Fuel Cost/gal.	$1.501	$1.569	$1.474	$1.471

INCOME STATEMENT ($Mn)	AMR	CAL	DAL	NWAC
Total Revenue	$19,847	$10,804	$15,831	$11,929
yr/yr % chg	*6.4%*	*10.9%*	*5.5%*	*5.8%*
EBIT	$102	$4	($766)	($686)
yr/yr % chg	*NM*	*NM*	*-48.0%*	*204.7%*
EBITDA	$1,282	$396	$492	($158)
yr/yr % chg	*10.6%*	*22%*	*303.3%*	*NM*
EBITDAR	$1,917	$1,121	$1,203	$628
yr/yr % chg	*8.4%*	*15%*	*293.8%*	*-40.7%*
Net Income	(682)	(263)	(1,824)	(1,293)
EPS	($4.23)	($3.93)	($12.94)	($14.86)

CASH FLOW ITEMS ($Mn)	AMR	CAL	DAL	NWAC
Beginning unrestricted cash	$2,929	$1,409	$1,799	$2,459
Net Income (Loss)	($682)	($263)	($1,824)	($1,293)
+ Depreciation & amortization	1,180	392	1,258	528
+/- Working capital	0	0	0	0
+ I/S Pension expense	390	235	700	500
- Cash pension expense	(310)	(136)	(450)	(420)
Net operating cash flow	$578	$228	($316)	($685)
- Non-aircraft capex	(400)	(175)	(375)	(100)
- Aircraft capex	(460)	(45)	(570)	(400)
+ Aircraft back-up financing	345	20	563	300
- Debt & capital lease payments	(807)	(688)	(758)	(601)
+ Debt issued	0	425	675	291
+ Asset sales	0	23	200	160
+/- Other	350	300	0	0
Ending unrestricted cash	$2,535	$1,497	$1,218	$1,425

Source: JPMorgan estimates and company reports.

AMR
- We assume AMR raises incremental $350 mn in capital in '05 although not necessary

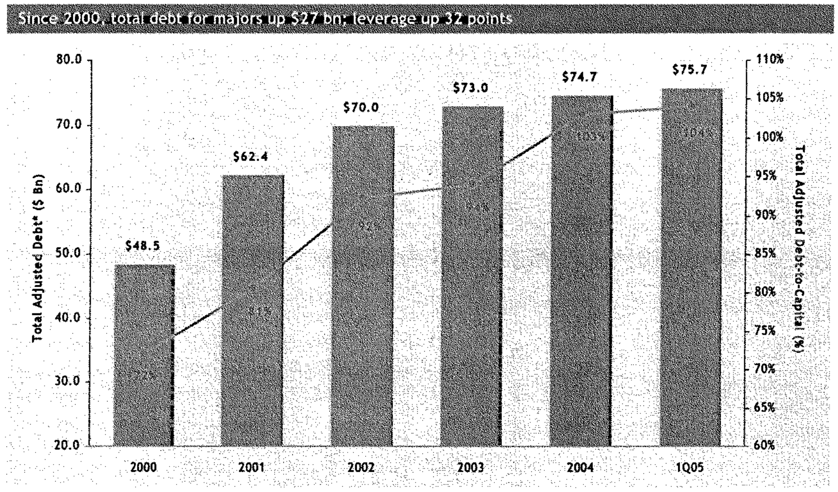
CAL
- We assume CAL would need to raise an incremental $300 mn in capital in '05 to reach mgt.'s $1.5 bn YE05 target
- $425 mn of debt issued includes $75 mn of OnePass and $350 mn of Air Mike deal in 2Q05.

DAL
- $875 mn of capital raised in '05 includes $295 mn of Amex draw in 1Q05, estimated $300 mn GE second lien in 2Q05, estimated $80 mn other debt raised in 3Q05 and estimated $200 mn asset proceeds in 3Q05

NWAC
- Estimated $450 mn of capital raised in '05 debt issued includes $118 mn Pinnacle note in 1Q05, $101 mn Tokyo real estate deal in 2Q05 and estimated $160 mn from asset sales.

The industry's ability to add incremental debt, although seemingly never quite exhausted, is rapidly diminishing. Since 2000, airlines have borrowed more than $27 billion. Leverage adjusted for aircraft leases has increased from 72% of adjusted capital to 104% (Exhibit XV).

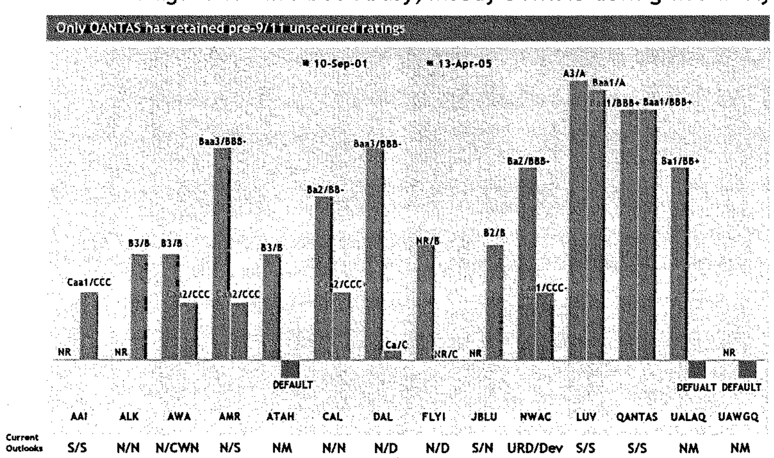
Exhibit XV: Industry added >$27 billion in debt since 2000



*Total balance sheet debt plus operating leases capitalized at 8x rent (annualized for 1Q05) for AAI, ALK, AWA, AMR, CAL, DAL, JBLU, NWAC, and LUV.
Source: Company reports and JPMorgan.

The credit rating agencies have been busy downgrading airline credit ratings (Exhibit XVI). Delta senior unsecured ratings have fallen 10 notches to Ca/C since the day before the September 11th attacks. Northwest ratings have fallen five and seven notches respectively to Caa1/CCC-. Continental ratings have fallen six and four notches to Caa2/CCC+. Even AMR, which is in the best credit shape of the legacy majors, has seen its credit ratings cut by eight steps.

Exhibit XVI: The agencies have been busy; Moody's NWAC downgrade likely



Ratings assigned numerical value from 1 (for lowest rating Ca/CC) to 20 (for highest rating Aaa/AAA), half point increments for split ratings.
Source: Bloomberg, S&P, and Moody's.

How can the legacy airlines raise capital?
In order to raise capital, the legacy airlines have turned to non-traditional lenders. Delta has sold frequent flier miles forward to American Express and tapped General Electric for a securitized loan. Continental recently sold miles forward as well and borrowed against its last major unencumbered assets (Air Micronesia).

It remains to be seen whether or not other vendors and manufacturers are willing to invest in their airline partners. Nevertheless, the proposed America West /US Airways capitalization includes proceeds from an airframe manufacturer (Airbus), hedge fund, traditional money manager, and airline maintenance provider (Air Canada). Therefore, we can conclude that the legacy airlines could perhaps tap some of these same sources for additional liquidity, especially if pension reform positively impacts the credit standing of the legacy airlines.

Will pension reform force additional legacy airline Chapter 11 filings?
Under some pension reform proposals, the airlines that sponsor defined benefit plans will face incredibly onerous payments. Relative to the 2005 required minimum contribution of $450 million, Delta has disclosed that its projected minimum funding under the current rules will increase by 33% in 2006 to $600 million, by 111% in 2007 to $950 million, and by 255% in 2008 to $1.6 billion. Northwest has yet to disclose minimum payments but I estimate similar figures relative to Delta (Exhibit XVII).

Exhibit XVII: Pension reform/stock market rally needed for legacy survival

US major airlines operating profit/(loss), $Bn

	PBO			Fair Value of Plan Assets			PBO % Funded			Underfunded Amount		
	2004	2003	2002	2004	2003	2002	2004	2003	2002	2004	2003	2002
CAL	$2,863	$2,362	$2,059	$1,281	$1,280	$866	44.7%	54.3%	42.1%	$1,582	$1,079	$1,193
NWAC	$9,254	$8,554	$7,638	$5,425	$4,806	$3,690	58.6%	56.2%	48.3%	$3,829	$3,748	$3,948
AMR	$10,022	$8,894	$8,757	$7,335	$6,230	$5,323	73.2%	70.1%	60.8%	$2,687	$2,664	$3,434
DAL	$12,140	$12,477	$11,682	$6,842	$6,818	$6,775	56.4%	54.6%	58.0%	$5,298	$5,659	$4,907
UALAQ	$13,577	$13,117	$12,673	$7,152	$6,961	$6,298	52.7%	53.1%	49.7%	$6,452	$6,156	$6,375

	Discount Rate			Expected Rate of Return			Actual Plan Return			Minimum Payments*		
	2004	2003	2002	2004	2003	2002	2004	2003	2002	2005	2006	2007
CAL	5.75%	6.25%	6.75%	9.00%	9.00%	9.50%	8.8%	25.2%	-12.0%	$266	$360	$450
NWAC[1]	5.90%	6.75%	7.50%	9.50%	9.50%	10.50%	15.0%	28.2%	-12.5%	$420	$700	$975
AMR[2]	6.00%	6.25%	6.75%	9.00%	9.00%	9.25%	17.8%	23.8%	-0.3%	$310	$600	$800
DAL	6.00%	6.125%	6.75%	9.00%	9.00%	10.00%	12.0%	14.6%	-8.7%	$450	$600	$950
UALAQ[3]	5.84%	6.25%	6.75%	9.00%	9.00%	9.75%	12.1%	22.2%	-9.3%	TBD	TBD	TBD

* without pension reform.
Source: JPMorgan and company reports.
1. NWAC 2006/207 minimum payments are estimated.
2. AMR 2006/2007 minimum payments are estimated.
3. UAL's 401K/defined contribution costs are far from $0 and may total >$200 million per annum.

In my opinion, Delta and Northwest will be forced to seek Chapter 11 protection and the termination of defined benefit plans (likely during 2006 and perhaps sooner if oil prices rise materially from current levels) unless reform allowing for a longer-term amortization of deficits for sponsors that agree to freeze plan liabilities is passed into law.

Continental is not as exposed to rising payments given the nature of the airline's defined benefit plan relative to Northwest and Delta. Nevertheless, the combination of the current oil price environment, current industry revenue, and higher required pension payments could force Continental to consider Chapter 11 as well in 2006.

AMR has enough liquidity-raising options and current liquidity to perhaps bridge the gap between today's environment and one where industry revenue and stock market improvement make required pension payments more manageable.

The issues surrounding credit balances and annual premiums, while important, are secondary to both the length of the amortization period and the interest rate to value liabilities in the cases of Delta and Northwest.

For AMR, the interest rate assumption and premium payments are most critical given the company's and its workers' desire to maintain defined benefit plans rather than the freezing approach embraced by Delta and Northwest management.

UAL is AMR's largest competitor. Although UAL's replacement defined contribution plan costs are significant, I nonetheless am concerned that AMR (and other legacy majors) will be at a strategic disadvantage to UAL going forward because of UAL's successful elimination of its defined benefit plans.

Are more legacy airline Chapter 11 filings inevitable?
Legacy Chapter 11 filings are not necessarily inevitable. I believe that Delta and Northwest would prefer to avoid the Chapter 11 process. Management's ability to do so is predicated on favorable airline specific pension reform and lower oil prices.

Delta's situation is fairly straightforward. I believe that management will continue to pursue an out of court restructuring. Delta is pursuing options to lower costs further and to bolster liquidity. The company just last week executed another $20 million debt for equity exchange in an ongoing attempt to reduce cash outflows. My view is that Delta will not file for Chapter 11 protection until the pension reform issue is settled if cash reserves remain adequate.

Northwest is dealing with an unsustainable labor situation, especially in regards to its current mechanic costs relative to peers. I expect that Northwest will eventually reach consensual deals on wage reductions with its labor unions. Management has yet to pull many of the liquidity strings that others have executed. I believe that with favorable pension reform and lower labor costs, Northwest's ability to avoid Chapter 11 rises dramatically.

For both Delta and Northwest, the variable with the most direct impact on survivability is oil.

Would pension reform delay necessary industry rationalization?
Most airlines and industry observers believe, as do I, that too many legacy carriers exist today and that further consolidation is inevitable. There are too many hubs and too many airline pricing departments, not too many mainline aircraft in my opinion.

Legacy airline hub and spoke networks were built to provide convenience that the consumer is no longer willing to subsidize through high fares. The legacy network rationalization process is already underway through initiatives such as hub de-peaking and more point-to-point flying.

Further rationalization does not necessarily need to occur in Chapter 11 if the government allows the legacy airlines to pursue mergers that make economic sense. The government could also relax foreign ownership provisions, thereby affording domestic airlines the ability to seek capital from global alliance partners.

If the government affords sponsors the flexibility to stretch payments out over a period of several years, the sponsors must be forced to maintain fiscal discipline in my opinion. I believe that airlines or other sponsors opting into a longer-term deficit amortization payment option should not be allowed to repurchase stock, pay dividends, or offer increased defined benefits even if funded with cash.

Conclusion
If the proposed pension legislation not supported by the legacy airlines is passed into law, I believe in what the credit markets are telling us, specifically that Delta and Northwest will likely file for Chapter 11 protection in 2006. If the airline defined benefit plan sponsors seek court protection, the PBGC's shortfall will obviously grow dramatically and taxpayers and other defined benefit plan participants will suffer as a result. Nothing is guaranteed, but the ability of the legacy airlines to successfully restructure outside the courts is almost directly tied to pension reform that does not result in onerous near-term deficit reduction contributions. In order to function efficiently, the airline equity and credit markets require some degree of cash flow stability. The government has one of two choices in my opinion. Either pension reform legislation will add to the already high level of cash flow uncertainty or pension reform will provide some degree of comfort to creditors willing to participate in out-of-court restructuring solutions.

Thank you once again for allowing me to speak to you today.

Statement of
David R. Strine before the
Committee on Transportation and Infrastructure
Subcommittee on Aviation
U.S. House of Representatives
June 22, 2005

Chairman Mica, Representative Costello, and distinguished members of the Subcommittee on Aviation, thank you for the invitation to testify on the U.S. Airline pension issue. I am honored to be here. Throughout my testimony, I will be presenting my personal views, which are not necessarily those of my employer, Bear Stearns & Co.

Summary & Introduction

The U.S. airline industry is in miserable financial condition, and it is destroying shareholder value. Since 2000, the ten largest (in terms of traffic) publicly traded airlines have lost $10 billion in market capitalization, and the airline index (XAL) is down 64% vs. 20% for the S&P 500. I estimate that the industry has lost $30 billion since 2000, and balance sheets have weakened such that debt-to-equity ratios have increased to an aggregate 300% from 80% while net-debt-to-total-invested-capital ratios have risen to over 100% from 67%.

The airlines have evolved into what is virtually a commodity-equivalent business with little to no pricing power. The growth of low-cost carrier market share has driven a structural change in the airlines' ability to price discriminate, and the legacy cost carriers have not moved fast enough to change their high fixed cost structures.

Through the Darwinian forces of the free market, the industry appears to be ripe for a period of consolidation. If oil prices remain high, that may occur regardless of whether or not more lenient standards for pension funding are applied to the airline industry.

Nevertheless, while there are many reasons for the industry's financial weakness, the defined benefit pension plan funding problem is the focus of my comments this afternoon. I will cover three basic questions:

1) What are the financial implications of the airlines' funding deficits?

2) How would more lenient pension funding standards affect the airlines?

3) What would a change in pension funding standards for the airline industry mean for shareholders?

1) What are the financial implications of the airlines' funding deficits?

Under ERISA (Employee Retirement Income Security Act) guidelines, we estimate that the airlines' $14 billion defined benefit pension funding shortfall will require $1.2 billion in cash contributions in 2005. This is a significant number, but it is only meaningful when considered in light of the airlines' ability to make the contributions based on their operating cash flows and unrestricted cash balances. Cash flow, of course, can be rather volatile as it is dependent upon oil prices, labor costs, and the revenue environment, so in this report, I provide a sensitivity analysis with different assumptions for oil prices. Each $1/bbl move in oil costs the airlines about $450 million annually.

For 2005, the $1.2 billion in cash contributions represent about 90% of our operating cash flow forecast with oil at $50/bbl, and 13% of the combined unrestricted cash balances of the legacy cost airlines. Considering the airlines' other obligations, such as principal debt maturities and capital expenditures, I estimate the legacy cost airlines could potentially burn about $4.3 billion in cash this year.

This is awful, but matters do not improve next year. With the expiration of the Pension Funding Equity Act of 2004 at the end of the year, I estimate that the required cash contributions could increase 100%, to $2.4 billion in 2006, representing 60% of operating cash flow and 30% of projected unrestricted cash with oil at $50/bbl. To provide some perspective on the importance of fuel costs, I estimate that, with oil costing $40/bbl, pension contributions would consume 38% of operating cash flow, while, with oil costing $60/bbl, the contributions would consume 150% of operating cash flow. *(Absent a replacement of PFEA 2004, pension discounting next year would revert to the 30-year Treasury yield, and current-year DRC [deficit reduction contribution] requirements would be due in full.)*

When examining the airlines individually, my analysis suggests that pension-related risk among legacy cost carriers operating outside of Chapter 11 differs substantially. Considering the airlines' ability to make the required pension contributions, in descending order, I rank the risk as follows: Delta Air Lines, Northwest Airlines, Continental Airlines, AMR Corp., and Alaska Airlines.

All told, if air fares don't increase (thereby helping airlines' yield) and oil remains at current levels, without more lenient pension funding requirements, I believe both Delta Air Lines and Northwest Airlines face near-term bankruptcy risk, and others could be at risk longer term.

Exhibit 1. Pension Summary — Cash Impact ($ in millions, except per share data)

($ in millions), except 2004 ABO per FTE	ALK	AMR	CAL [1]	DAL [2]	NWAC	
Plan Type	DB/DC	DB/DC	DB/DC	DB/DC	DB Plan	Total/ Average
Dec-04						
Plan Assets (GAAP)	607	7,335	1,281	6,842	5,425	21,490
Plan Benefit Obligations (PBO) (GAAP)	910	10,022	2,863	12,140	9,245	35,180
PBO Pension Overfunded (Underfunded)	(303)	(2,687)	(1,582)	(5,298)	(3,820)	(13,690)
ABO Pension Overfunded (Underfunded)	(161)	(1,823)	(1,131)	(5,239)	(3,565)	(11,919)
Post Retirement Obligations (APBO)	(76)	(3,152)	NA	(1,835)	(921)	(5,984)
2004 Assumed rate of return on plan assets	8.00%	9.00%	9.00%	9.00%	9.50%	8.90%
2004 Assumed discount rate for obligations	5.75%	6.00%	5.75%	6.00%	5.90%	5.88%
2004 Asset Allocation: Equity/Fixed Income (remainder=other)	71%/29%	52%/38%	66%/28%	50%/28%	74%/20%	63%/29%
2005E Revenue	2,901	19,797	10,703	15,794	11,873	61,068
2005E Operating Cash Flow (oil at $50/bbl Base Assumption)	306	896	270	-157	48	1,362
2006E Revenue	3,004	20,489	11,359	16,761	12,436	64,050
2006E Operating Cash Flow (oil at $50/bbl Base Assumption)	343	1,528	673	513	918	3,976
2006E Operating Cash Flow (oil at $40/bbl)	407	2,336	914	1,189	1,379	6,225
2004 GAAP PBO Funding Status	67%	73%	45%	56%	59%	61%
2004 GAAP ABO Funding Status	79%	80%	53%	57%	60%	66%
2004 ABO per 2004 FTEs	12,448	20,099	29,422	75,763	90,616	47,569
2004 P&L DB Pension Expense[3]	78	427	293	549	444	1,791
2005E P&L DB Pension Expense[3]	89	380	196	440	530	1,636
2005E DB Pension CASM	0.34¢	0.20¢	0.22¢	0.28¢	0.57¢	0.29¢
2005E After-Tax EPS Impact	(2.12)	(1.51)	(1.90)	(2.22)	(3.93)	(2.34)
2004 DB Expense	78	427	293	549	444	1,791
2004 Defined Contribution & Profit Sharing Expense	25	163	30	150	NA	368
2004 Retirement (Healthcare) Costs	9	264	NA	76	98	447
2004 DB CASM	0.31¢	0.23¢	0.35¢	0.38¢	0.49¢	0.34¢
2004 DC & Profit Sharing CASM	0.10¢	0.09¢	0.04¢	0.10¢	NA	0.07¢
2004 OPEB CASM	0.04¢	0.14¢	NA	0.05¢	0.11¢	0.08¢
2004 Total DB, DC, OPEB CASM	0.44¢	0.46¢	0.38¢	0.53¢	0.59¢	0.49¢
Unrestricted Cash Balance (3/31/05)	764	3,017	1,380	1,815	2,132	9,108
2004 DB Pension Cash Contributions	49	467	0	455	253	1,224
2005E DB Pension Cash Contributions[3]	58	310	136	285	420	1,209
2006E DB Pension Cash Contributions[4] Plan Freeze and 20yr Amort.	1	30	31	150	112	325
2006E DB Pension Cash Contributions[4] Bush Proposal (7yr Amort.)	62	269	248	400	644	1,623
2006E DB Pension Cash Contributions[4] PFEA expires (5yr Amort.)	66	345	330	700	930	2,370
2005E After-Tax Projected Pension Cash per Share Impact	(1.38)	(1.24)	(1.32)	(1.44)	(3.11)	(1.70)
2005E Pension Cash Contribution to 1Q:05 Cash Balance	8%	10%	10%	16%	20%	13.3%
2005E Pension Cash Contribution to 2005E Op. Cash Flow	19%	35%	50%	-181%	883%	88.7%
2005E Pension Cash + Debt Mat.+ Net Capex to 2005E Op. Cash Flow	92%	194%	373%	-900%	2567%	415.9%
2006E (20yr Amort.) Pension Cash Contribution to 2006E Op. Cash Flow	0%	2%	5%	29%	12%	8.2%
2006E (7yr Amort.) Pension Cash Contribution to 2006E Op. Cash Flow	18%	18%	37%	78%	70%	40.8%
2006E (5yr Amort.) Pension Cash Contribution to 2006E Op. Cash Flow	19%	23%	49%	137%	101%	59.6%
2006E (20yr Amort.) Pension + Debt Mat. + Net Capex to '06E Op. Cash Flow	57%	103%	110%	276%	145%	132.1%
2006E (7yr Amort.) Pension + Debt Mat. + Net Capex to '06E Op. Cash Flow	75%	118%	142%	324%	203%	164.7%
2006E (5yr Amort.) Pension + Debt Mat. + Net Capex to '06E Op. Cash Flow	76%	123%	154%	383%	234%	183.5%

Note: DB = defined benefit pensions where employer bears investment risk and DC = defined contribution pensions plan such as 401 (k) where the employee assumes the investment risk. PBO= projected benefit obligation (assumes future wage inflation); ABO= accumulated benefit obligation (pension obligations already accrued, if a plan were frozen this would be GAAP analogous amount); APBO= accumulated post retirement benefits obligation; OPEB includes:–Postemployment Health Care Benefits: medical, dental, vision, hearing, and other health-related benefits whether provided separately or through the pension plan–Other benefits: Life insurance, disability, long-term care, etc., when provided separately from a defined benefit pension plan. Operating Cash Flow = Net Income + D&A+ pension expense; assumes no impact from change in net working capital.

1) Continental's 2005E required pension contribution is $266 million; however, in the table above, which focuses on cash we exclude $130 million in stock contributed to the plans year-to-date. Similarly, pension expense is $235 million, though we exclude $43 million in curtailment charges.

2) Delta froze its DB plan as of 12/31/04, eliminating future service accruals, though wage increases will still be factored into benefit calculations. 2004 pension expense excludes curtailment charges.

3) Based on company 2004 10k, 1Q:05 10Q data, 1Q:05 conference calls, company guidance, and Bear Stearns estimates.

4) Bear Stearns' Forecasts: 2006 Forecasted pension cash contributions assume expiration of the Pension Funding Equity Act of 2004. Three scenarios (assuming an even amortization repayment schedule): 1) assumes plan freezes and a 20-year DRC amortization, 2) assumes a 7-year DRC amortization (Bush proposal), and 3) assumes PFEA expires and a 5-year DRC amortization.

Actual company results may vary considerably. Please see our Sept. 2003 Airline Pension report for more information.

Note: Firms may be able to contribute limited amounts of stock in certain circumstances instead of cash. In addition, firms may apply for IRS waivers that could allow them to spread payments out over five or so years. Furthermore, interest rate changes, asset returns, and legislative changes could have significant impacts on these forecasts.

Sources: Bear Stearns & Co. Inc. estimates; company reports; company guidance.

Source: Bear, Stearns & Co. Inc. estimates; company reports; company guidance; First Call.

While ERISA and the Internal Revenue Code rules dictate funding periods ranging from as few as three to as many as 30 years, after surveying our companies and for purposes of this report, we assume for simplifying reasons that deficit reduction contributions are repaid in five years under current law and would continue to be due in this time frame should PFEA expire without replacement.

2) How would more lenient pension funding standards affect the airlines?

The longer the period of amortization of pension funding requirements, the lower the cash burn rates and the lower the probability of bankruptcies at the legacy cost airlines.

When viewed in the context of operating cash flow, I believe that most airlines will survive outside of bankruptcy even without any change to pension law given that many carriers have defined contribution plans rather than defined benefit plans. However, assuming oil at $50/bbl and no change to labor costs, I estimate that both Delta and Northwest's operating cash flow could be insufficient to fund their pension plans and also meet debt obligations and capital expenditures in 2006 without more lenient pension funding requirements.

I estimate that pension cash contributions for the legacy airlines would fall 87% to $300 million from $2.4 billion in 2006 if the amortization period for funding pension obligations were to change from four years to the 25 years which has been proposed in Representative Price's bill — the Employee Pension Preservation and Taxpayer Protection Act of 2005 (the companion to Senator Isakson's bill — the Employee Pension Preservation Act of 2005). Under this scenario, I believe bankruptcy risk declines significantly, even for the weakest legacy cost airlines — Delta and Northwest.

On the other hand, using the seven-year amortization period that appears in both the Bush Administration proposal and Representative Boehner's (R. Ohio) bill (Pension Protection Act of 2005), I estimate that the pension cash contributions would fall 32% to $1.6 billion from $2.4 billion. Under this scenario, my cash-burn analysis suggests that Delta and Northwest would likely file for bankruptcy.

If both Delta and Northwest were to file for Chapter 11 and execute distressed terminations of their defined benefit pension plans, the risk of eventual bankruptcy at American Airlines and Continental Airlines increases as they will have a significant cost disadvantage. In combination with the recent terminations of pension plans at United Airlines and US Airways, this would result in 45% of the industry's capacity operating with the advantage of having eliminated defined benefit pension plans.

That said, if either Delta or Northwest is unable to lower other costs, refinance principal debt maturities in 2006, or raise funds through other means, even a 20-year or longer amortization may not be enough to prevent bankruptcy. However, I believe that more lenient funding requirements would likely make it easier for the airlines, and for Delta and Northwest in particular, to attract funds from the capital markets, which would thereby reduce the probability of Chapter 11 filings.

Exhibit 2. Pension Catch-up Payment (Deficit Reduction Contribution) — sensitivity to Varying Amortization Periods

Key Assumptions

1. GAAP ABO approximates ERISA Current Liability.
2. GAAP ABO Funding Deficit is comprised solely of unfunded new liabilities.
3. Asset returns and interest rates are neutral during 2005.
4. Excludes any assumptions about 2006 normal costs.

Illustration of Straight-line Amortization Schedules (per year contribution)
Based on GAAP Pension Disclosures

(US$ millions)	ALK	AMR	CAL	DAL	NWAC	Total
2004 Plan Assets (GAAP)	$607	$7,335	$1,281	$6,842	$5,425	$21,490
2004 Plan Accumulated Benefit Obligation (GAAP)	$768	$9,158	$2,412	$12,081	$8,990	$33,409
2004 ABO Funding Level	**79%**	**80%**	**53%**	**57%**	**60%**	**64%**
2004 ABO Shortfall	**(161)**	**(1,823)**	**(1,131)**	**(5,239)**	**(3,565)**	**(11,919)**
2005E DB Contribution	$58	$310	$266	$285	$420	$1,339
2005E YE ABO 90% Funding Gap	($26)	($597)	($624)	($3,746)	($2,246)	($7,239)
2006E DRC Funding Requirement Based on Above						
4 years 2006-2009 (absent new law)	($7)	($149)	($156)	($936)	($562)	($1,810)
7 years 2006-2012 (Bush/Rep.Boehner proposal)	**($4)**	**($85)**	**($89)**	**($535)**	**($321)**	**($1,034)**
15 years 2006-2020	($2)	($40)	($42)	($250)	($150)	($483)
20 years 2006-2025	($1)	($30)	($31)	($187)	($112)	($362)
25 years 2006-2030 (Senate bill)	($1)	($24)	($25)	($150)	($90)	($290)

Note: Assumes 2004 ABO shortfall is equal to 2004 current liability funding level and funding level rises to 90% over stated period.
Note: 2004 likely reduced funding gaps a touch as assets rose, offset by declining interest rates.
Note: CAL reached new labor agreements in March, which could reduce future funding obligations.
Note: Includes estimated 2005 DB contributions and assumes no interest rate impact.
Note: the four year amortization is an example of the pension funding timing for deeply underfunded plans under the present pension law.
Note: Delta disclosed that its current liability funding deficit at July 1, 2004 (its most recent data) was $2.6 billion and its plans were 75% funded.
Source: Bear Stearns estimates, company reports.

3) What would a change in pension funding standards for the airline industry mean for shareholders?

A special exception to the funding requirements under ERISA for the airlines is not enough in itself to cure the ills of the airline industry and halt the destruction of shareholder value. Although shareholders and creditors of the airlines that face the most severe liquidity problems, particularly Delta Air Lines and Northwest Airlines, could benefit in the near term from more lenient pension funding requirements, such a change only extends the window of opportunity for these companies to remedy the inefficiencies in their businesses and reduce their operating costs so they can begin the hard work of repairing their terribly distressed balance sheets. Even excluding the pension issue, the operating cost structures of these companies are uncompetitive.

What's more, if extending a life line in the form of pension relief serves to delay the reduction of other costs or keeps companies afloat that would otherwise shrink in

Chapter 11 or via Chapter 7, thereby wringing some capacity out of the system, the result may well be disadvantageous to airlines that already have defined contribution plans or have enough operating cash flow to cover their required defined benefit pension contributions. Of course, Chapter 11 itself has been harmful to the overall welfare of the airline industry because it sets up a lopsided playing field and does not necessarily result in consolidation or a reduction of supply.

Ultimately, I believe shareholders will benefit most if the natural forces of the free market determine the fate of the airline industry. Under such conditions, making decisions on how to invest is an easier process. However, without change to the bankruptcy laws and antitrust hurdles, which would allow for the consolidation of weak businesses, a laissez faire policy on pensions will do little to improve conditions for shareholders. Accordingly, barring changes in other areas of law that would provide for a more efficient marketplace, I believe shareholders will benefit from a change in pension law that allows airlines to freeze defined benefit pension plans and amortize their required cash contributions over a period well beyond the seven years noted in the Bush proposal and the Boehner bill and closer to the 25-year period noted in the Isakson (S. 861)/Price (H.R. 2106) bills. Of course, if oil prices continue on their current trajectory, it may not matter.

Thank you.

Appendix: Cash Burn Sensitivities:

Scenario: NO Debt Refinancing

As of 08/03/05

Cash Flow/Burn for 2Q-4Q:2005E (US$ mn)	AMR[2]	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT[3]
2Q-4Q:2005E Operating Cash Flow[1]										
Operating CF (after tax) $35/bbl	$1,766	$693	$862	$745	$140	$775	$37	$330	$155	$36
Operating CF (after tax) $40/bbl	$1,476	$566	$616	$562	$126	$763	$22	$306	$113	$28
Operating CF (after tax) $45/bbl	$1,186	$439	$371	$378	$113	$751	$9	$283	$71	$21
Operating CF (after tax) $50/bbl (Base Case)	$896	$312	$125	$194	$100	$740	($1)	$259	$29	$13
Operating CF (after tax) $55/bbl	$606	$186	($121)	$10	$86	$728	($10)	$236	($13)	$6
Operating CF (after tax) $60/bbl	$316	$59	($367)	($173)	$73	$716	($20)	$212	($55)	($0)
Operating CF (after tax) $65/bbl	$26	($68)	($613)	($357)	$60	$704	($29)	$189	($97)	($6)
Cash Obligations										
Net Capex	$361	$169	$420	$150	$56	$148	$61	$68	$30	$26
DB Pension Contributions[4]	$172	$136	$95	$336	NA	NA	NA	$39	NA	NA
Cash From Financings	$0	($529)	$0	$0	$0	$0	$0	$0	($13)	$0
Debt Maturities	$675	$563	$500	$328	$79	$38	$12	$45	$67	$13
Liquidity										
Unrestricted Cash Balance at Calendar 1Q:05	$3,017	$1,380	$1,815	$2,132	$616	$1,908	$364	$764	$254	$175
Unrestricted Cash Balance at Calendar 4Q:04	$2,929	$1,458	$1,799	$2,459	$449	$1,305	$334	$874	$306	$149
2Q-4Q:2005E Cash Flow (Burn) Oil @ $35/bbl	**$557**	**$354**	**($153)**	**($69)**	**$4**	**$589**	**($35)**	**$179**	**$72**	**($3)**
Cash Flow (Burn) per Day $35/bbl	$2.0	$1.3	($0.6)	($0.3)	$0.0	$2.2	($0.1)	$0.7	$0.3	($0.0)
2005E End of Year Unrestricted Cash $35/bbl	$3,574	$1,734	$1,662	$2,063	$620	$2,497	$329	$942	$325	$172
Mth of Cash Left with oil at $35/bbl from 1Q:05 end to threshold[5]	CF Pos.	CF Pos.	9+	9+	CF Pos.	CF Pos.	9+	CF Pos.	CF Pos.	9+
2Q-4Q:2005E Cash Flow (Burn) Oil @ $40/bbl	**$267**	**$227**	**($399)**	**($253)**	**($9)**	**$577**	**($51)**	**$155**	**$30**	**($11)**
Cash Flow (Burn) per Day $40/bbl	$0.7	$0.6	($1.1)	($0.7)	($0.0)	$1.6	($0.1)	$0.4	$0.1	($0.0)
2005E End of Year Unrestricted Cash $40/bbl	$3,284	$1,607	$1,416	$1,879	$606	$2,485	$313	$919	$283	$164
Mth of Cash Left with oil at $40/bbl from 1Q:05 end to threshold[5]	CF Pos.	CF Pos.	7	9+	9+	CF Pos.	9+	CF Pos.	CF Pos.	9+
2Q-4Q:2005E Cash Flow (Burn) Oil @ $45/bbl	**($22)**	**$100**	**($644)**	**($436)**	**($23)**	**$565**	**($63)**	**$132**	**($12)**	**($18)**
Cash Flow (Burn) per Day $45/bbl	($0.1)	$0.3	($1.8)	($1.2)	($0.1)	$1.5	($0.2)	$0.4	($0.0)	($0.0)
2005E End of Year Unrestricted Cash $45/bbl	$2,995	$1,480	$1,171	$1,696	$593	$2,473	$301	$895	$241	$157
Mth of Cash Left with oil at $45/bbl from 1Q:05 end to threshold[5]	9+	CF Pos.	4	9+	9+	CF Pos.	9+	CF Pos.	9+	9+
2Q-4Q:2005E Cash Flow (Burn) Oil @ $50/bbl (Base Case)	**($312)**	**($27)**	**($890)**	**($620)**	**($36)**	**$554**	**($73)**	**$108**	**($54)**	**($26)**
Cash Flow (Burn) per Day $50/bbl	**($0.9)**	**($0.1)**	**($2.4)**	**($1.7)**	**($0.1)**	**$1.5**	**($0.2)**	**$0.3**	**($0.1)**	**($0.1)**
2005E End of Year Unrestricted Cash $50/bbl	**$2,705**	**$1,353**	**$925**	**$1,512**	**$580**	**$2,462**	**$291**	**$872**	**$199**	**$149**
Mth of Cash Left with oil at $50/bbl from 1Q:05 end to threshold[5]	**9+**	**9+**	**3**	**9+**	**9+**	**CF Pos.**	**9+**	**CF Pos.**	**9**	**9+**
2Q-4Q:2005E Cash Flow (Burn) Oil @ $55/bbl	**($602)**	**($153)**	**($1,136)**	**($804)**	**($49)**	**$542**	**($82)**	**$85**	**($96)**	**($33)**
Cash Flow (Burn) per Day $55/bbl	($1.7)	($0.4)	($3.1)	($2.2)	($0.1)	$1.5	($0.2)	$0.2	($0.3)	($0.1)
2005E End of Year Unrestricted Cash $55/bbl	$2,415	$1,227	$679	$1,328	$566	$2,450	$282	$848	$157	$142
Mth of Cash Left with oil at $55/bbl from 1Q:05 end to threshold[5]	9+	9+	2	9+	9+	CF Pos.	9+	CF Pos.	5	9+
2Q-4Q:2005E Cash Flow (Burn) Oil @ $60/bbl	**($892)**	**($280)**	**($1,382)**	**($988)**	**($63)**	**$530**	**($92)**	**$61**	**($139)**	**($39)**
Cash Flow (Burn) per Day $60/bbl	($2.4)	($0.8)	($3.8)	($2.7)	($0.2)	$1.5	($0.3)	$0.2	($0.4)	($0.1)
2005E End of Year Unrestricted Cash $60/bbl	$2,125	$1,100	$433	$1,144	$553	$2,438	$272	$825	$115	$136
Mth of Cash Left with oil at $60/bbl from 1Q:05 end to threshold[5]	9+	9+	2	9+	9+	CF Pos.	9+	CF Pos.	3	9+
2Q-4Q:2005E Cash Flow (Burn) Oil @ $65/bbl	**($1,182)**	**($407)**	**($1,628)**	**($1,171)**	**($76)**	**$518**	**($101)**	**$38**	**($181)**	**($45)**
Cash Flow (Burn) per Day $65/bbl	($3.2)	($1.1)	($4.5)	($3.2)	($0.2)	$1.4	($0.3)	$0.1	($0.5)	($0.1)
2005E End of Year Unrestricted Cash $65/bbl	$1,835	$973	$187	$961	$539	$2,426	$263	$801	$73	$129
Mth of Cash Left with oil at $65/bbl from 1Q:05 end to threshold[5]	9+	8	2	8	9+	CF Pos.	9+	CF Pos.	3	9+

(1) Operating Cash Flow = Net Income + D&A+ pension expense; assumes no impact from change in net working capital.

Assumes crude price of $50/bbl in 2Q-4Q:05. Incorporates hedge positions.

(2) Assumes AMR has to repurchase $104mn facilities bond due in 4Q:05.

(3) Cash burn analysis is for nine-month ended Dec 2005 (base assumption oil at $50/bbl).

(4) Assumes no additional non-cash (stock of subsidiary) contribution to DB pension plans.

(5) Where months of cash left exceed 9 months, please see 2006.

Source: Bear Stearns & Co., and company reports.

(US$ in millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT
Estimated Unrestricted Cash Concern Level	**$1,500**	**$1,000**	**$1,500**	**$1,100**	**$150**	**$750**	**$100**	**$300**	**$200**	**$75**

Source: Bear Stearns' estimates

As points of reference, we note that AMR achieved its last-minute deal with labor last April with $1.2 billion (7% of LTM sales) in unrestricted cash and equivalents,

UAL filed for Chapter 11 on 12/9/02 with $1.3 billion (9% of LTM sales) in unrestricted cash and equivalents (YE 2002),

and US Air entered Chapter 11 on 8/11/02 with close to $900mn in cash (3Q:02 balance was $900mn) (13% of LTM sales).

Scenario: NO Debt Refinancing & PFEA Expiration (5-Yr Amortization)
As of 06/03/05

Cash Flow/Burn 2006E (US$ millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT[5]
2006E Operating Cash Flow[1]										
Operating CF (after tax) $35/bbl	$2,713	$1,045	$1,526	$1,633	$252	$1,095	$99	$439	$108	$50
Operating CF (after tax) $40/bbl	$2,336	$914	$1,189	$1,379	$226	$1,058	$73	$407	$72	$39
Operating CF (after tax) $45/bbl	$1,932	$788	$850	$1,124	$200	$1,021	$47	$376	$36	$27
Operating CF (after tax) $50/bbl (Base Case)	$1,528	$666	$512	$870	$174	$985	$21	$344	$0	$16
Operating CF (after tax) $55/bbl	$1,125	$493	$173	$615	$148	$948	($5)	$312	($35)	$4
Operating CF (after tax) $60/bbl	$721	$319	($165)	$361	$122	$911	($30)	$281	($71)	($7)
Operating CF (after tax) $65/bbl	$317	$146	($503)	$106	$96	$874	($54)	$249	($107)	($19)
Cash Obligations										
Net Capex	$210	$175	$530	$228	$186	$426	$30	$138	$59	$35
DB Pension Contributions[2]	$345	$330	$700	$930	NA	NA	NA	$66	NA	NA
Debt Maturities	$1,328	$533	$733	$994	$108	$604	$15	$57	$101	$18
Liquidity										
Estimated Unrestricted Cash Balance at Calendar 4Q:05[3]	$2,705	$1,353	$925	$1,512	$580	$2,462	$291	$872	$199	$149
Unrestricted Cash Balance at Calendar 4Q:04	$2,929	$1,460	$1,799	$2,459	$449	$1,305	$334	$874	$306	$149
2006E Cash Flow (Burn) Oil @ $35/bbl	**$830**	**$7**	**($437)**	**($519)**	**($44)**	**$65**	**$55**	**$179**	**($52)**	**($3)**
Cash Flow (Burn) per Day $35/bbl	$2.3	$0.0	($1.2)	($1.4)	($0.1)	$0.2	$0.1	$0.5	($0.1)	($0.0)
2006E End of Year Unrestricted Cash $35/bbl	$3,535	$1,361	$488	$993	$535	$2,527	$346	$1,050	$147	$146
Mth of Cash Left with oil at $35/bbl from YE 2005 to threshold[4]	CF Pos.	CF Pos.	Ch. 11 Risk	10	116	CF Pos.	CF Pos.	CF Pos.	Ch. 11 Risk	338
2006E Cash Flow (Burn) Oil @ $40/bbl	**$453**	**($124)**	**($774)**	**($773)**	**($70)**	**$29**	**$29**	**$147**	**($88)**	**($14)**
Cash Flow (Burn) per Day $40/bbl	$1.2	($0.3)	($2.1)	($2.1)	($0.2)	$0.1	$0.1	$0.4	($0.2)	($0.0)
2006E End of Year Unrestricted Cash $40/bbl	$3,158	$1,230	$151	$739	$509	$2,490	$320	$1,019	$111	$135
Mth of Cash Left with oil at $40/bbl from YE 2005 to threshold[4]	CF Pos.	33	Ch. 11 Risk	6	73	CF Pos.	CF Pos.	CF Pos.	Ch. 11 Risk	63
2006E Cash Flow (Burn) Oil @ $45/bbl	**$49**	**($250)**	**($1,113)**	**($1,028)**	**($96)**	**($8)**	**$3**	**$115**	**($124)**	**($26)**
Cash Flow (Burn) per Day $45/bbl	$0.1	($0.7)	($3.0)	($2.8)	($0.3)	($0.0)	$0.0	$0.3	($0.3)	($0.1)
2006E End of Year Unrestricted Cash $45/bbl	$2,754	$1,104	NM	$484	$483	$2,454	$294	$987	$75	$123
Mth of Cash Left with oil at $45/bbl from YE '05 to threshold[4]	CF Pos.	16	Ch. 11 Risk	5	54	2,524	CF Pos.	CF Pos.	Ch. 11 Risk	35
2006E Cash Flow (Burn) Oil @ $50/bbl (Base Case)	**($355)**	**($372)**	**($1,451)**	**($1,282)**	**($122)**	**($45)**	**($23)**	**$84**	**($160)**	**($37)**
Cash Flow (Burn) per Day $50/bbl	**($1.0)**	**($1.0)**	**($4.0)**	**($3.5)**	**($0.3)**	**($0.1)**	**($0.1)**	**$0.2**	**($0.4)**	**($0.1)**
2006E End of Year Unrestricted Cash $50/bbl	**$2,350**	**$982**	**NM**	**$230**	**$457**	**$2,417**	**$268**	**$955**	**$40**	**$112**
Mth of Cash Left with oil at $50/bbl from YE 2005 to threshold[4]	**41**	**11**	**Ch. 11 Risk**	**4**	**42**	**458**	**98**	**CF Pos.**	**Ch. 11 Risk**	**24**
2006E Cash Flow (Burn) Oil @ $55/bbl	**($758)**	**($545)**	**($1,790)**	**($1,537)**	**($148)**	**($82)**	**($49)**	**$52**	**($195)**	**($49)**
Cash Flow (Burn) per Day $55/bbl	($2.1)	($1.5)	($4.9)	($4.2)	($0.4)	($0.2)	($0.1)	$0.1	($0.5)	($0.1)
2006E End of Year Unrestricted Cash $55/bbl	$1,946	$808	NM	NM	$432	$2,380	$242	$924	$4	$100
Mth of Cash Left with oil at $55/bbl from YE 2005 to threshold[4]	19	8	Ch. 11 Risk	3	35	252	47	CF Pos.	Ch. 11 Risk	18
2006E Cash Flow (Burn) Oil @ $60/bbl	**($1,162)**	**($719)**	**($2,128)**	**($1,791)**	**($174)**	**($118)**	**($74)**	**$20**	**($231)**	**($60)**
Cash Flow (Burn) per Day $60/bbl	($3.2)	($2.0)	($5.8)	($4.9)	($0.5)	($0.3)	($0.2)	$0.1	($0.6)	($0.2)
2006E End of Year Unrestricted Cash $60/bbl	$1,542	$635	NM	NM	$406	$2,343	$217	$892	NM	$89
Mth of Cash Left with oil at $60/bbl from YE 2005 to threshold[4]	12	6	Ch. 11 Risk	3	30	174	31	CF Pos.	Ch. 11 Risk	15
2006E Cash Flow (Burn) Oil @ $65/bbl	**($1,566)**	**($892)**	**($2,466)**	**($2,046)**	**($200)**	**($155)**	**($99)**	**($11)**	**($267)**	**($72)**
Cash Flow (Burn) per Day $65/bbl	($4.3)	($2.4)	($6.8)	($5.6)	($0.5)	($0.4)	($0.3)	($0.0)	($0.7)	($0.2)
2006E End of Year Unrestricted Cash $65/bbl	$1,138	$461	NM	NM	$380	$2,307	$192	$860	NM	$77
Mth of Cash Left with oil at $65/bbl from YE 2005 to threshold[4]	9	5	Ch. 11 Risk	2	26	132	23	607	Ch. 11 Risk	12

(1) Operating Cash Flow = Net Income + D&A+ pension expense; assumes no impact from change in net working capital.

Assumes crude price of $50/bbl in 2006. Incorporates hedge positions.

(2) Assumes no additional non-cash (stock of subsidiary) contribution to DB pension plans.

(3) Assumes crude price of $50/bbl in 2Q-4Q:05. For NO debt refinancing scenario in 2006, assumes no debt refinancing in 2005. For debt refinancing scenario in 2006, assumes debt refinancing in 2005.

(4) Chapter 11 risk: operating with cash burn and cash balance is below threshold cash level.

(5) FRNT is in 2007 March-ending Fiscal Year, base assumption oil at $50/bbl for calender 2006.

Source: Bear Stearns & Co., and company reports.

(US$ in millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT
Estimated Unrestricted Cash Concern Level	**$1,500**	**$1,000**	**$1,500**	**$1,100**	**$150**	**$750**	**$100**	**$300**	**$200**	**$75**

Source: Bear Stearns' estimates

As points of reference, we note that AMR achieved its last-minute deal with labor last April with $1.2 billion (7% of LTM sales) in unrestricted cash and equivalents,

UAL filed for Chapter 11 on 12/9/02 with $1.3 billion (9% of LTM sales) in unrestricted cash and equivalents (YE 2002),

and US Air entered Chapter 11 on 8/11/02 with close to $900mn in cash (3Q:02 balance was $900mn) (13% of LTM sales).

Scenario: NO Debt Refinancing & Bush/Boehner Proposal (7-Yr Amortization)

As of 06/03/05

Cash Flow/Burn 2006E (US$ millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT[5]
2006E Operating Cash Flow [1]										
Operating CF (after tax) $35/bbl	$2,713	$1,045	$1,526	$1,633	$252	$1,095	$99	$439	$108	$50
Operating CF (after tax) $40/bbl	$2,336	$914	$1,189	$1,379	$226	$1,058	$73	$407	$72	$39
Operating CF (after tax) $45/bbl	$1,932	$788	$850	$1,124	$200	$1,021	$47	$376	$36	$27
Operating CF (after tax) $50/bbl (Base Case)	$1,528	$666	$512	$870	$174	$985	$21	$344	$0	$16
Operating CF (after tax) $55/bbl	$1,125	$493	$173	$615	$148	$948	($5)	$312	($35)	$4
Operating CF (after tax) $60/bbl	$721	$319	($165)	$361	$122	$911	($30)	$281	($71)	($7)
Operating CF (after tax) $65/bbl	$317	$146	($503)	$106	$96	$874	($54)	$249	($107)	($19)
Cash Obligations										
Net Capex	$210	$175	$530	$228	$188	$426	$30	$138	$59	$35
DB Pension Contributions[2]	$269	$248	$400	$644	NA	NA	NA	$62	NA	NA
Debt Maturities	$1,328	$533	$733	$994	$108	$604	$15	$57	$101	$18
Liquidity										
Estimated Unrestricted Cash Balance at Calendar 4Q:05[3]	$2,705	$1,353	$925	$1,512	$580	$2,462	$291	$872	$199	$149
Unrestricted Cash Balance at Calendar 4Q:04	$2,929	$1,460	$1,799	$2,459	$449	$1,305	$334	$874	$306	$149
2006E Cash Flow (Burn) Oil @ $35/bbl	**$906**	**$90**	**($137)**	**($233)**	**($44)**	**$65**	**$55**	**$182**	**($52)**	**($3)**
Cash Flow (Burn) per Day $35/bbl	$2.5	$0.2	($0.4)	($0.6)	($0.1)	$0.2	$0.1	$0.5	($0.1)	($0.0)
2006E End of Year Unrestricted Cash $35/bbl	$3,610	$1,443	$788	$1,279	$535	$2,527	$346	$1,054	$147	$146
Mth of Cash Left with oil at $35/bbl from YE 2005 to threshold[4]	CF Pos.	CF Pos.	Ch. 11 Risk	21	116	CF Pos.	CF Pos.	CF Pos.	Ch. 11 Risk	338
2006E Cash Flow (Burn) Oil @ $40/bbl	**$529**	**($41)**	**($474)**	**($487)**	**($70)**	**$29**	**$29**	**$150**	**($88)**	**($14)**
Cash Flow (Burn) per Day $40/bbl	$1.4	($0.1)	($1.3)	($1.3)	($0.2)	$0.1	$0.1	$0.4	($0.2)	($0.0)
2006E End of Year Unrestricted Cash $40/bbl	$3,233	$1,312	$451	$1,024	$509	$2,490	$320	$1,022	$111	$135
Mth of Cash Left with oil at $40/bbl from YE 2005 to threshold[4]	CF Pos.	100	Ch. 11 Risk	10	73	CF Pos.	CF Pos.	CF Pos.	Ch. 11 Risk	63
2006E Cash Flow (Burn) Oil @ $45/bbl	**$125**	**($168)**	**($813)**	**($742)**	**($96)**	**($8)**	**$3**	**$119**	**($124)**	**($26)**
Cash Flow (Burn) per Day $45/bbl	$0.3	($0.5)	($2.2)	($2.0)	($0.3)	($0.0)	$0.0	$0.3	($0.3)	($0.1)
2006E End of Year Unrestricted Cash $45/bbl	$2,829	$1,186	$111	$770	$483	$2,454	$294	$990	$75	$123
Mth of Cash Left with oil at $45/bbl from YE '05 to threshold[4]	CF Pos.	25	Ch. 11 Risk	7	54	2,524	CF Pos.	CF Pos.	Ch. 11 Risk	35
2006E Cash Flow (Burn) Oil @ $50/bbl (Base Case)	**($279)**	**($290)**	**($1,151)**	**($996)**	**($122)**	**($45)**	**($23)**	**$87**	**($160)**	**($37)**
Cash Flow (Burn) per Day $50/bbl	**($0.8)**	**($0.8)**	**($3.2)**	**($2.7)**	**($0.3)**	**($0.1)**	**($0.1)**	**$0.2**	**($0.4)**	**($0.1)**
2006E End of Year Unrestricted Cash $50/bbl	**$2,426**	**$1,064**	**NM**	**$515**	**$457**	**$2,417**	**$268**	**$959**	**$40**	**$112**
Mth of Cash Left with oil at $50/bbl from YE 2005 to threshold[4]	**52**	**14**	**Ch. 11 Risk**	**5**	**42**	**458**	**98**	**CF Pos.**	**Ch. 11 Risk**	**24**
2006E Cash Flow (Burn) Oil @ $55/bbl	**($883)**	**($463)**	**($1,490)**	**($1,251)**	**($148)**	**($82)**	**($49)**	**$55**	**($195)**	**($49)**
Cash Flow (Burn) per Day $55/bbl	($1.9)	($1.3)	($4.1)	($3.4)	($0.4)	($0.2)	($0.1)	$0.2	($0.5)	($0.1)
2006E End of Year Unrestricted Cash $55/bbl	$2,022	$890	NM	$261	$432	$2,380	$242	$927	$4	$100
Mth of Cash Left with oil at $55/bbl from YE 2005 to threshold[4]	21	9	Ch. 11 Risk	4	35	252	47	CF Pos.	Ch. 11 Risk	18
2006E Cash Flow (Burn) Oil @ $60/bbl	**($1,087)**	**($637)**	**($1,828)**	**($1,505)**	**($174)**	**($118)**	**($74)**	**$24**	**($231)**	**($60)**
Cash Flow (Burn) per Day $60/bbl	($3.0)	($1.7)	($5.0)	($4.1)	($0.5)	($0.3)	($0.2)	$0.1	($0.6)	($0.2)
2006E End of Year Unrestricted Cash $60/bbl	$1,618	$717	NM	$6	$406	$2,343	$217	$895	NM	$89
Mth of Cash Left with oil at $60/bbl from YE 2005 to threshold[4]	13	6	Ch. 11 Risk	3	30	174	31	CF Pos.	Ch. 11 Risk	15
2006E Cash Flow (Burn) Oil @ $65/bbl	**($1,491)**	**($810)**	**($2,166)**	**($1,760)**	**($200)**	**($155)**	**($99)**	**($8)**	**($267)**	**($72)**
Cash Flow (Burn) per Day $65/bbl	($4.1)	($2.2)	($5.9)	($4.8)	($0.5)	($0.4)	($0.3)	($0.0)	($0.7)	($0.2)
2006E End of Year Unrestricted Cash $65/bbl	$1,214	$543	NM	NM	$380	$2,307	$192	$864	NM	$77
Mth of Cash Left with oil at $65/bbl from YE 2005 to threshold[4]	10	5	Ch. 11 Risk	3	26	132	23	841	Ch. 11 Risk	12

(1) Operating Cash Flow = Net Income + D&A+ pension expense; assumes no impact from change in net working capital.

Assumes crude price of $50/bbl in 2006. Incorporates hedge positions.

(2) Assumes no additional non-cash (stock of subsidiary) contribution to DB pension plans.

(3) Assumes crude price of $50/bbl in 2Q-4Q:05. For NO debt refinancing scenario in 2006, assumes no debt refinancing in 2005. For debt refinancing scenario in 2006, assumes debt refinancing in 2005.

(4) Chapter 11 risk: operating with cash burn and cash balance is below threshold cash level.

(5) FRNT is in 2007 March-ending Fiscal Year, base assumption oil at $50/bbl for calender 2006.

Source: Bear Stearns & Co., and company reports.

(US$ in millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT
Estimated Unrestricted Cash Concern Level	**$1,500**	**$1,000**	**$1,500**	**$1,100**	**$150**	**$750**	**$100**	**$300**	**$200**	**$75**

Source: Bear Stearns' estimates

As points of reference, we note that AMR achieved its last-minute deal with labor last April with $1.2 billion (7% of LTM sales) in unrestricted cash and equivalents,

UAL filed for Chapter 11 on 12/9/02 with $1.3 billion (9% of LTM sales) in unrestricted cash and equivalents (YE 2002),

and US Air entered Chapter 11 on 8/11/02 with close to $900mn in cash (3Q:02 balance was $900mn) (13% of LTM sales).

Scenario: NO Debt Refinancing & Pension Plan Freeze / 20-Yr Amortization Proposal

As of 06/03/05

Cash Flow/Burn 2006E (US$ millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT[5]
2006E Operating Cash Flow [1]										
Operating CF (after tax) $35/bbl	$2,713	$1,045	$1,526	$1,633	$252	$1,095	$99	$439	$108	$50
Operating CF (after tax) $40/bbl	$2,336	$914	$1,189	$1,379	$226	$1,058	$73	$407	$72	$39
Operating CF (after tax) $45/bbl	$1,932	$788	$850	$1,124	$200	$1,021	$47	$376	$36	$27
Operating CF (after tax) $50/bbl (Base Case)	$1,528	$666	$512	$870	$174	$985	$21	$344	$0	$16
Operating CF (after tax) $55/bbl	$1,125	$493	$173	$615	$148	$948	($5)	$312	($35)	$4
Operating CF (after tax) $60/bbl	$721	$319	($165)	$361	$122	$911	($30)	$281	($71)	($7)
Operating CF (after tax) $65/bbl	$317	$146	($503)	$106	$96	$874	($54)	$249	($107)	($19)
Cash Obligations										
Net Capex	$210	$175	$530	$228	$188	$426	$30	$138	$59	$35
DB Pension Contributions[2]	$30	$31	$150	$112	NA	NA	NA	$1	NA	NA
Debt Maturities	$1,328	$533	$733	$994	$108	$604	$15	$57	$101	$18
Liquidity										
Estimated Unrestricted Cash Balance at Calendar 4Q:05[3]	$2,705	$1,353	$925	$1,512	$580	$2,462	$291	$872	$199	$149
Unrestricted Cash Balance at Calendar 4Q:04	$2,929	$1,460	$1,799	$2,459	$449	$1,305	$334	$874	$306	$149
2006E Cash Flow (Burn) Oil @ $35/bbl	**$1,145**	**$306**	**$113**	**$299**	**($44)**	**$65**	**$55**	**$243**	**($52)**	**($3)**
Cash Flow (Burn) per Day $35/bbl	$3.1	$0.8	$0.3	$0.8	($0.1)	$0.2	$0.1	$0.7	($0.1)	($0.0)
2006E End of Year Unrestricted Cash $35/bbl	$3,850	$1,660	$1,038	$1,810	$535	$2,527	$346	$1,115	$147	$146
Mth of Cash Left with oil at $35/bbl from YE 2005 to threshold[4]	CF Pos.	CF Pos.	CF Pos.	CF Pos.	116	CF Pos.	CF Pos.	CF Pos.	Ch. 11 Risk	338
2006E Cash Flow (Burn) Oil @ $40/bbl	**$768**	**$175**	**($224)**	**$44**	**($70)**	**$29**	**$29**	**$211**	**($88)**	**($14)**
Cash Flow (Burn) per Day $40/bbl	$2.1	$0.5	($0.6)	$0.1	($0.2)	$0.1	$0.1	$0.6	($0.2)	($0.0)
2006E End of Year Unrestricted Cash $40/bbl	$3,473	$1,529	$701	$1,556	$509	$2,490	$320	$1,083	$111	$135
Mth of Cash Left with oil at $40/bbl from YE 2005 to threshold[4]	CF Pos.	CF Pos.	Ch. 11 Risk	CF Pos.	73	CF Pos.	CF Pos.	CF Pos.	Ch. 11 Risk	63
2006E Cash Flow (Burn) Oil @ $45/bbl	**$364**	**$49**	**($563)**	**($210)**	**($96)**	**($8)**	**$3**	**$180**	**($124)**	**($26)**
Cash Flow (Burn) per Day $45/bbl	$1.0	$0.1	($1.5)	($0.6)	($0.3)	($0.0)	$0.0	$0.5	($0.3)	($0.1)
2006E End of Year Unrestricted Cash $45/bbl	$3,069	$1,402	$361	$1,301	$483	$2,454	$294	$1,051	$75	$123
Mth of Cash Left with oil at $45/bbl from YE '05 to threshold[4]	CF Pos.	CF Pos.	Ch. 11 Risk	-23	54	2,524	CF Pos.	CF Pos.	Ch. 11 Risk	35
2006E Cash Flow (Burn) Oil @ $50/bbl (Base Case)	**($40)**	**($73)**	**($901)**	**($465)**	**($122)**	**($45)**	**($23)**	**$148**	**($160)**	**($37)**
Cash Flow (Burn) per Day $50/bbl	**($0.1)**	**($0.2)**	**($2.5)**	**($1.3)**	**($0.3)**	**($0.1)**	**($0.1)**	**$0.4**	**($0.4)**	**($0.1)**
2006E End of Year Unrestricted Cash $50/bbl	**$2,665**	**$1,280**	**$23**	**$1,047**	**$457**	**$2,417**	**$268**	**$1,020**	**$40**	**$112**
Mth of Cash Left with oil at $50/bbl from YE 2005 to threshold[4]	**366**	**56**	**Ch. 11 Risk**	**11**	**42**	**458**	**98**	**CF Pos.**	**Ch. 11 Risk**	**24**
2006E Cash Flow (Burn) Oil @ $55/bbl	**($443)**	**($247)**	**($1,240)**	**($719)**	**($148)**	**($82)**	**($49)**	**$116**	**($195)**	**($49)**
Cash Flow (Burn) per Day $55/bbl	($1.2)	($0.7)	($3.4)	($2.0)	($0.4)	($0.2)	($0.1)	$0.3	($0.5)	($0.1)
2006E End of Year Unrestricted Cash $55/bbl	$2,261	$1,107	NM	$792	$432	$2,380	$242	$988	$4	$100
Mth of Cash Left with oil at $55/bbl from YE 2005 to threshold[4]	33	17	Ch. 11 Risk	7	35	252	47	CF Pos.	Ch. 11 Risk	18
2006E Cash Flow (Burn) Oil @ $60/bbl	**($847)**	**($420)**	**($1,578)**	**($974)**	**($174)**	**($118)**	**($74)**	**$85**	**($231)**	**($60)**
Cash Flow (Burn) per Day $60/bbl	($2.3)	($1.2)	($4.3)	($2.7)	($0.5)	($0.3)	($0.2)	$0.2	($0.6)	($0.2)
2006E End of Year Unrestricted Cash $60/bbl	$1,857	$933	NM	$538	$406	$2,343	$217	$956	NM	$89
Mth of Cash Left with oil at $60/bbl from YE 2005 to threshold[4]	17	10	Ch. 11 Risk	5	30	174	31	CF Pos.	Ch. 11 Risk	15
2006E Cash Flow (Burn) Oil @ $65/bbl	**($1,251)**	**($594)**	**($1,916)**	**($1,228)**	**($200)**	**($155)**	**($99)**	**$53**	**($267)**	**($72)**
Cash Flow (Burn) per Day $65/bbl	($3.4)	($1.6)	($5.2)	($3.4)	($0.5)	($0.4)	($0.3)	$0.1	($0.7)	($0.2)
2006E End of Year Unrestricted Cash $65/bbl	$1,453	$760	NM	$283	$380	$2,307	$192	$925	NM	$77
Mth of Cash Left with oil at $65/bbl from YE 2005 to threshold[4]	12	7	Ch. 11 Risk	4	26	132	23	CF Pos.	Ch. 11 Risk	12

(1) Operating Cash Flow = Net income + D&A+ pension expense; assumes no impact from change in net working capital.

Assumes crude price of $50/bbl in 2006. Incorporates hedge positions.

(2) Assumes no additional non-cash (stock of subsidiary) contribution to DB pension plans.

(3) Assumes crude price of $50/bbl in 2Q-4Q:05. For NO debt refinancing scenario in 2006, assumes no debt refinancing in 2005. For debt refinancing scenario in 2006, assumes debt refinancing in 2005.

(4) Chapter 11 risk: operating with cash burn and cash balance is below threshold cash level.

(5) FRNT is in 2007 March-ending Fiscal Year, base assumption oil at $50/bbl for calender 2006.

Source: Bear Stearns & Co., and company reports.

(US$ in millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT
Estimated Unrestricted Cash Concern Level	**$1,500**	**$1,000**	**$1,500**	**$1,100**	**$150**	**$750**	**$100**	**$300**	**$200**	**$75**

Source: Bear Stearns' estimates

As points of reference, we note that AMR achieved its last-minute deal with labor last April with $1.2 billion (7% of LTM sales) in unrestricted cash and equivalents,

UAL filed for Chapter 11 on 12/9/02 with $1.3 billion (9% of LTM sales) in unrestricted cash and equivalents (YE 2002),

and US Air entered Chapter 11 on 8/11/02 with close to $900mn in cash (3Q:02 balance was $900mn) (13% of LTM sales).

Scenario: With Debt Refinancing of 80% of Maturing Amount

As of 06/03/05

Cash Flow/Burn for 2Q-4Q:2005E (US$ mn)	AMR[2]	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT[3]
2Q-4Q:2005E Operating Cash Flow[1]										
Operating CF (after tax) $35/bbl	$1,766	$693	$862	$745	$140	$775	$37	$330	$155	$36
Operating CF (after tax) $40/bbl	$1,476	$566	$616	$562	$126	$763	$22	$306	$113	$28
Operating CF (after tax) $45/bbl	$1,186	$439	$371	$378	$113	$751	$9	$283	$71	$21
Operating CF (after tax) $50/bbl (Base Case)	$896	$312	$125	$194	$100	$740	($1)	$259	$29	$13
Operating CF (after tax) $55/bbl	$606	$186	($121)	$10	$86	$728	($10)	$236	($13)	$6
Operating CF (after tax) $60/bbl	$316	$59	($367)	($173)	$73	$716	($20)	$212	($55)	($0)
Operating CF (after tax) $65/bbl	$26	($68)	($613)	($357)	$60	$704	($29)	$189	($97)	($6)
Cash Obligations										
Net Capex	$361	$169	$420	$150	$56	$148	$61	$68	$30	$26
DB Pension Contributions[4]	$172	$136	$95	$336	NA	NA	NA	$39	NA	NA
Cash From Financings	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Debt Maturities	$135	$113	$100	$66	$16	$8	$2	$9	$13	$3
Liquidity										
Unrestricted Cash Balance at Calendar 1Q:05	$3,017	$1,380	$1,815	$2,132	$616	$1,908	$364	$764	$254	$175
Unrestricted Cash Balance at Calendar 4Q:04	$2,929	$1,458	$1,799	$2,459	$449	$1,305	$334	$874	$306	$149
2Q-4Q:2005E Cash Flow (Burn) Oil @ $35/bbl	**$1,097**	**$276**	**$247**	**$194**	**$68**	**$619**	**($26)**	**$215**	**$112**	**$7**
Cash Flow (Burn) per Day $35/bbl	$4.0	$1.0	$0.9	$0.7	$0.2	$2.3	($0.1)	$0.8	$0.4	$0.0
2005E End of Year Unrestricted Cash $35/bbl	$4,114	$1,656	$2,062	$2,326	$683	$2,527	$339	$978	$365	$182
Mth of Cash Left with oil at $35/bbl from 1Q:05 end to threshold[5]	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	9+	CF Pos.	CF Pos.	CF Pos.
2Q-4Q:2005E Cash Flow (Burn) Oil @ $40/bbl	**$807**	**$149**	**$1**	**$10**	**$54**	**$608**	**($41)**	**$191**	**$70**	**($0)**
Cash Flow (Burn) per Day $40/bbl	$2.2	$0.4	$0.0	$0.0	$0.1	$1.7	($0.1)	$0.5	$0.2	($0.0)
2005E End of Year Unrestricted Cash $40/bbl	$3,824	$1,529	$1,816	$2,142	$670	$2,516	$323	$955	$323	$174
Mth of Cash Left with oil at $40/bbl from 1Q:05 end to threshold[5]	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	9+	CF Pos.	CF Pos.	9+
2Q-4Q:2005E Cash Flow (Burn) Oil @ $45/bbl	**$518**	**$22**	**($244)**	**($174)**	**$41**	**$596**	**($54)**	**$168**	**$28**	**($8)**
Cash Flow (Burn) per Day $45/bbl	$1.4	$0.1	($0.7)	($0.5)	$0.1	$1.6	($0.1)	$0.5	$0.1	($0.0)
2005E End of Year Unrestricted Cash $45/bbl	$3,535	$1,402	$1,571	$1,958	$657	$2,504	$310	$931	$281	$167
Mth of Cash Left with oil at $45/bbl from 1Q:05 end to threshold[5]	CF Pos.	CF Pos.	9+	9+	CF Pos.	CF Pos.	9+	CF Pos.	CF Pos.	9+
2Q-4Q:2005E Cash Flow (Burn) Oil @ $50/bbl (Base Case)	**$228**	**($105)**	**($490)**	**($357)**	**$28**	**$584**	**($64)**	**$144**	**($14)**	**($15)**
Cash Flow (Burn) per Day $50/bbl	**$0.6**	**($0.3)**	**($1.3)**	**($1.0)**	**$0.1**	**$1.6**	**($0.2)**	**$0.4**	**($0.0)**	**($0.0)**
2005E End of Year Unrestricted Cash $50/bbl	**$3,245**	**$1,275**	**$1,325**	**$1,775**	**$643**	**$2,492**	**$300**	**$908**	**$239**	**$159**
Mth of Cash Left with oil at $50/bbl from 1Q:05 end to threshold[5]	**CF Pos.**	**9+**	**6**	**9+**	**CF Pos.**	**CF Pos.**	**9+**	**CF Pos.**	**9+**	**9+**
2Q-4Q:2005E Cash Flow (Burn) Oil @ $55/bbl	**($62)**	**($232)**	**($736)**	**($541)**	**$14**	**$572**	**($73)**	**$121**	**($56)**	**($22)**
Cash Flow (Burn) per Day $55/bbl	($0.2)	($0.6)	($2.0)	($1.5)	$0.0	$1.6	($0.2)	$0.3	($0.2)	($0.1)
2005E End of Year Unrestricted Cash $55/bbl	$2,955	$1,148	$1,079	$1,591	$630	$2,480	$291	$884	$197	$152
Mth of Cash Left with oil at $55/bbl from 1Q:05 end to threshold[5]	9+	9+	4	9+	CF Pos.	CF Pos.	9+	CF Pos.	9	9+
2Q-4Q:2005E Cash Flow (Burn) Oil @ $60/bbl	**($352)**	**($359)**	**($982)**	**($725)**	**$1**	**$561**	**($83)**	**$97**	**($99)**	**($29)**
Cash Flow (Burn) per Day $60/bbl	($1.0)	($1.0)	($2.7)	($2.0)	$0.0	$1.5	($0.2)	$0.3	($0.3)	($0.1)
2005E End of Year Unrestricted Cash $60/bbl	$2,665	$1,021	$833	$1,407	$616	$2,469	$282	$861	$155	$146
Mth of Cash Left with oil at $60/bbl from 1Q:05 end to threshold[5]	9+	9+	3	9+	CF Pos.	CF Pos.	9+	CF Pos.	5	9+
2Q-4Q:2005E Cash Flow (Burn) Oil @ $65/bbl	**($642)**	**($486)**	**($1,228)**	**($909)**	**($13)**	**$549**	**($92)**	**$73**	**($141)**	**($35)**
Cash Flow (Burn) per Day $65/bbl	($1.8)	($1.3)	($3.4)	($2.5)	($0.0)	$1.5	($0.3)	$0.2	($0.4)	($0.1)
2005E End of Year Unrestricted Cash $65/bbl	$2,375	$894	$587	$1,223	$603	$2,457	$272	$837	$113	$140
Mth of Cash Left with oil at $65/bbl from 1Q:05 end to threshold[5]	9+	7	2	9+	9+	CF Pos.	9+	CF Pos.	3	9+

(1) Operating Cash Flow = Net Income + D&A+ pension expense; assumes no impact from change in net working capital.

Assumes crude price of $50/bbl in 2Q-4Q:05. Incorporates hedge positions.

(2) Assumes AMR has to repurchase $104mn facilities bond due in 4Q:05.

(3) Cash burn analysis is for nine-month ended Dec 2005 (base assumption oil at $50/bbl).

(4) Assumes no additional non-cash (stock of subsidiary) contribution to DB pension plans.

(5) Where months of cash left exceed 9 months, please see 2006.

Source: Bear Stearns & Co., and company reports.

(US$ in millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT
Estimated Unrestricted Cash Concern Level	**$1,500**	**$1,000**	**$1,500**	**$1,100**	**$150**	**$750**	**$100**	**$300**	**$200**	**$75**

Source: Bear Stearns' estimates

As points of reference, we note that AMR achieved its last-minute deal with labor last April with $1.2 billion (7% of LTM sales) in unrestricted cash and equivalents,

UAL filed for Chapter 11 on 12/9/02 with $1.3 billion (9% of LTM sales) in unrestricted cash and equivalents (YE 2002),

and US Air entered Chapter 11 on 8/11/02 with close to $900mn in cash (3Q:02 balance was $900mn) (13% of LTM sales).

Scenario: With Debt Refinancing of 80% of Maturing Amount & PFEA Expiration (5-Yr Amortization)
As of 06/03/05

Cash Flow/Burn 2006E (US$ millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT[5]
2006E Operating Cash Flow [1]										
Operating CF (after tax) $35/bbl	$2,713	$1,045	$1,526	$1,633	$252	$1,095	$99	$439	$108	$50
Operating CF (after tax) $40/bbl	$2,336	$914	$1,189	$1,379	$226	$1,058	$73	$407	$72	$39
Operating CF (after tax) $45/bbl	$1,932	$788	$850	$1,124	$200	$1,021	$47	$376	$36	$27
Operating CF (after tax) $50/bbl (Base Case)	$1,528	$666	$512	$870	$174	$985	$21	$344	$0	$16
Operating CF (after tax) $55/bbl	$1,125	$493	$173	$615	$148	$948	($5)	$312	($35)	$4
Operating CF (after tax) $60/bbl	$721	$319	($165)	$361	$122	$911	($30)	$281	($71)	($7)
Operating CF (after tax) $65/bbl	$317	$146	($503)	$106	$96	$874	($54)	$249	($107)	($19)
Cash Obligations										
Net Capex	$210	$175	$530	$228	$188	$426	$30	$138	$59	$35
DB Pension Contributions[2]	$345	$330	$700	$930	NA	NA	NA	$66	NA	NA
Debt Maturities	$266	$107	$147	$199	$22	$121	$3	$11	$20	$4
Liquidity										
Estimated Unrestricted Cash Balance at Calendar 4Q:05[3]	$3,245	$1,275	$1,325	$1,775	$643	$2,492	$300	$908	$239	$159
Unrestricted Cash Balance at Calendar 4Q:04	$2,929	$1,460	$1,799	$2,459	$449	$1,305	$334	$874	$306	$149
2006E Cash Flow (Burn) Oil @ $35/bbl	**$1,893**	**$434**	**$150**	**$276**	**$42**	**$549**	**$66**	**$224**	**$28**	**$12**
Cash Flow (Burn) per Day $35/bbl	$5.2	$1.2	$0.4	$0.8	$0.1	$1.5	$0.2	$0.6	$0.1	$0.0
2006E End of Year Unrestricted Cash $35/bbl	$5,137	$1,709	$1,474	$2,051	$685	$3,041	$367	$1,132	$268	$171
Mth of Cash Left with oil at $35/bbl from YE 2005 to threshold[4]	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.
2006E Cash Flow (Burn) Oil @ $40/bbl	**$1,516**	**$303**	**($187)**	**$22**	**$16**	**$512**	**$40**	**$193**	**($7)**	**$0**
Cash Flow (Burn) per Day $40/bbl	$4.2	$0.8	($0.5)	$0.1	$0.0	$1.4	$0.1	$0.5	($0.0)	$0.0
2006E End of Year Unrestricted Cash $40/bbl	$4,760	$1,578	$1,137	$1,796	$659	$3,004	$341	$1,100	$232	$160
Mth of Cash Left with oil at $40/bbl from YE 2005 to threshold[4]	CF Pos.	CF Pos.	Ch. 11 Risk	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	65	CF Pos.
2006E Cash Flow (Burn) Oil @ $45/bbl	**$1,112**	**$177**	**($527)**	**($233)**	**($10)**	**$475**	**$14**	**$161**	**($43)**	**($11)**
Cash Flow (Burn) per Day $45/bbl	$3.0	$0.5	($1.4)	($0.6)	($0.0)	$1.3	$0.0	$0.4	($0.1)	($0.0)
2006E End of Year Unrestricted Cash $45/bbl	$4,356	$1,451	$798	$1,542	$633	$2,967	$315	$1,069	$196	$148
Mth of Cash Left with oil at $45/bbl from YE '05 to threshold[4]	CF Pos.	CF Pos.	Ch. 11 Risk	35	600	CF Pos.	CF Pos.	CF Pos.	11	89
2006E Cash Flow (Burn) Oil @ $50/bbl (Base Case)	**$708**	**$55**	**($865)**	**($487)**	**($36)**	**$438**	**($12)**	**$129**	**($79)**	**($23)**
Cash Flow (Burn) per Day $50/bbl	**$1.9**	**$0.1**	**($2.4)**	**($1.3)**	**($0.1)**	**$1.2**	**($0.0)**	**$0.4**	**($0.2)**	**($0.1)**
2006E End of Year Unrestricted Cash $50/bbl	**$3,952**	**$1,329**	**$460**	**$1,287**	**$607**	**$2,930**	**$289**	**$1,037**	**$161**	**$136**
Mth of Cash Left with oil at $50/bbl from YE 2005 to threshold[4]	**CF Pos.**	**CF Pos.**	**Ch. 11 Risk**	**17**	**166**	**CF Pos.**	**209**	**CF Pos.**	**6**	**44**
2006E Cash Flow (Burn) Oil @ $55/bbl	**$304**	**($119)**	**($1,203)**	**($742)**	**($62)**	**$402**	**($37)**	**$98**	**($114)**	**($34)**
Cash Flow (Burn) per Day $55/bbl	$0.8	($0.3)	($3.3)	($2.0)	($0.2)	$1.1	($0.1)	$0.3	($0.3)	($0.1)
2006E End of Year Unrestricted Cash $55/bbl	$3,549	$1,156	$121	$1,033	$582	$2,894	$263	$1,005	$125	$125
Mth of Cash Left with oil at $55/bbl from YE 2005 to threshold[4]	CF Pos.	27	Ch. 11 Risk	11	96	CF Pos.	64	CF Pos.	4	29
2006E Cash Flow (Burn) Oil @ $60/bbl	**($100)**	**($292)**	**($1,541)**	**($996)**	**($88)**	**$365**	**($63)**	**$66**	**($150)**	**($46)**
Cash Flow (Burn) per Day $60/bbl	($0.3)	($0.8)	($4.2)	($2.7)	($0.2)	$1.0	($0.2)	$0.2	($0.4)	($0.1)
2006E End of Year Unrestricted Cash $60/bbl	$3,145	$982	NM	$778	$556	$2,857	$238	$974	$89	$113
Mth of Cash Left with oil at $60/bbl from YE 2005 to threshold[4]	210	11	Ch. 11 Risk	8	68	CF Pos.	38	CF Pos.	3	22
2006E Cash Flow (Burn) Oil @ $65/bbl	**($504)**	**($466)**	**($1,879)**	**($1,251)**	**($113)**	**$328**	**($87)**	**$34**	**($186)**	**($58)**
Cash Flow (Burn) per Day $65/bbl	($1.4)	($1.3)	($5.1)	($3.4)	($0.3)	$0.9	($0.2)	$0.1	($0.5)	($0.2)
2006E End of Year Unrestricted Cash $65/bbl	$2,741	$809	NM	$524	$530	$2,820	$213	$942	$53	$102
Mth of Cash Left with oil at $65/bbl from YE 2005 to threshold[4]	42	7	Ch. 11 Risk	6	52	CF Pos.	28	CF Pos.	3	18

(1) Operating Cash Flow = Net Income + D&A+ pension expense; assumes no impact from change in net working capital.
Assumes crude price of $50/bbl in 2006. Incorporates hedge positions.
(2) Assumes no additional non-cash (stock of subsidiary) contribution to DB pension plans.
(3) Assumes crude price of $50/bbl in 2Q-4Q:05. For NO debt refinancing scenario in 2006, assumes no debt refinancing in 2005. For debt refinancing scenario in 2006, assumes debt refinancing in 2005.
(4) Chapter 11 risk: operating with cash burn and cash balance is below threshold cash level.
(5) FRNT is in 2007 March-ending Fiscal Year, base assumption oil at $50/bbl for calender 2006.
Source: Bear Stearns & Co., and company reports.

(US$ in millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT
Estimated Unrestricted Cash Concern Level	**$1,500**	**$1,000**	**$1,500**	**$1,100**	**$150**	**$750**	**$100**	**$300**	**$200**	**$75**

Source: Bear Stearns' estimates
As points of reference, we note that AMR achieved its last-minute deal with labor last April with $1.2 billion (7% of LTM sales) in unrestricted cash and equivalents,
UAL filed for Chapter 11 on 12/9/02 with $1.3 billion (9% of LTM sales) in unrestricted cash and equivalents (YE 2002),
and US Air entered Chapter 11 on 8/11/02 with close to $900mn in cash (3Q:02 balance was $900mn) (13% of LTM sales).

Scenario: With Debt Refinancing of 80% of Maturing Amount & Bush/Boehner Proposal (7-Yr Amortization)
As of 06/03/05

Cash Flow/Burn 2006E (US$ millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT[5]
2006E Operating Cash Flow [1]										
Operating CF (after tax) $35/bbl	$2,713	$1,045	$1,526	$1,633	$252	$1,095	$99	$439	$108	$50
Operating CF (after tax) $40/bbl	$2,336	$914	$1,189	$1,379	$226	$1,058	$73	$407	$72	$39
Operating CF (after tax) $45/bbl	$1,932	$788	$850	$1,124	$200	$1,021	$47	$376	$36	$27
Operating CF (after tax) $50/bbl (Base Case)	$1,528	$666	$512	$870	$174	$985	$21	$344	$0	$16
Operating CF (after tax) $55/bbl	$1,125	$493	$173	$615	$148	$948	($5)	$312	($35)	$4
Operating CF (after tax) $60/bbl	$721	$319	($165)	$361	$122	$911	($30)	$281	($71)	($7)
Operating CF (after tax) $65/bbl	$317	$146	($503)	$106	$96	$874	($54)	$249	($107)	($19)
Cash Obligations										
Net Capex	$210	$175	$530	$228	$188	$426	$30	$138	$59	$35
DB Pension Contributions[2]	$269	$248	$400	$644	NA	NA	NA	$62	NA	NA
Debt Maturities	$266	$107	$147	$199	$22	$121	$3	$11	$20	$4
Liquidity										
Estimated Unrestricted Cash Balance at Calendar 4Q:05[3]	$3,245	$1,275	$1,325	$1,775	$643	$2,492	$300	$908	$239	$159
Unrestricted Cash Balance at Calendar 4Q:04	$2,929	$1,460	$1,799	$2,459	$449	$1,305	$334	$874	$306	$149
2006E Cash Flow (Burn) Oil @ $35/bbl	**$1,968**	**$516**	**$450**	**$562**	**$42**	**$549**	**$66**	**$228**	**$28**	**$12**
Cash Flow (Burn) per Day $35/bbl	$5.4	$1.4	$1.2	$1.5	$0.1	$1.5	$0.2	$0.6	$0.1	$0.0
2006E End of Year Unrestricted Cash $35/bbl	$5,213	$1,791	$1,774	$2,337	$685	$3,041	$367	$1,135	$268	$171
Mth of Cash Left with oil at $35/bbl from YE 2005 to threshold[4]	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.
2006E Cash Flow (Burn) Oil @ $40/bbl	**$1,591**	**$385**	**$113**	**$308**	**$16**	**$512**	**$40**	**$196**	**($7)**	**$0**
Cash Flow (Burn) per Day $40/bbl	$4.4	$1.1	$0.3	$0.8	$0.0	$1.4	$0.1	$0.5	($0.0)	$0.0
2006E End of Year Unrestricted Cash $40/bbl	$4,836	$1,660	$1,437	$2,082	$659	$3,004	$341	$1,103	$232	$160
Mth of Cash Left with oil at $40/bbl from YE 2005 to threshold[4]	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	65	CF Pos.
2006E Cash Flow (Burn) Oil @ $45/bbl	**$1,187**	**$259**	**($227)**	**$53**	**($10)**	**$475**	**$14**	**$164**	**($43)**	**($11)**
Cash Flow (Burn) per Day $45/bbl	$3.3	$0.7	($0.6)	$0.1	($0.0)	$1.3	$0.0	$0.4	($0.1)	($0.0)
2006E End of Year Unrestricted Cash $45/bbl	$4,432	$1,534	$1,098	$1,828	$633	$2,967	$315	$1,072	$196	$148
Mth of Cash Left with oil at $45/bbl from YE '05 to threshold[4]	CF Pos.	CF Pos.	Ch. 11 Risk	CF Pos.	600	CF Pos.	CF Pos.	CF Pos.	11	89
2006E Cash Flow (Burn) Oil @ $50/bbl (Base Case)	**$783**	**$137**	**($565)**	**($201)**	**($36)**	**$438**	**($12)**	**$133**	**($79)**	**($23)**
Cash Flow (Burn) per Day $50/bbl	**$2.1**	**$0.4**	**($1.5)**	**($0.6)**	**($0.1)**	**$1.2**	**($0.0)**	**$0.4**	**($0.2)**	**($0.1)**
2006E End of Year Unrestricted Cash $50/bbl	**$4,028**	**$1,412**	**$760**	**$1,573**	**$607**	**$2,930**	**$289**	**$1,040**	**$161**	**$136**
Mth of Cash Left with oil at $50/bbl from YE 2005 to threshold[4]	**CF Pos.**	**CF Pos.**	**Ch. 11 Risk**	**40**	**166**	**CF Pos.**	**209**	**CF Pos.**	**6**	**44**
2006E Cash Flow (Burn) Oil @ $55/bbl	**$380**	**($37)**	**($903)**	**($456)**	**($62)**	**$402**	**($37)**	**$101**	**($114)**	**($34)**
Cash Flow (Burn) per Day $55/bbl	$1.0	($0.1)	($2.5)	($1.2)	($0.2)	$1.1	($0.1)	$0.3	($0.3)	($0.1)
2006E End of Year Unrestricted Cash $55/bbl	$3,624	$1,238	$421	$1,319	$582	$2,894	$263	$1,008	$125	$125
Mth of Cash Left with oil at $55/bbl from YE 2005 to threshold[4]	CF Pos.	87	Ch. 11 Risk	18	96	CF Pos.	64	CF Pos.	4	29
2006E Cash Flow (Burn) Oil @ $60/bbl	**($24)**	**($210)**	**($1,241)**	**($710)**	**($88)**	**$365**	**($63)**	**$69**	**($150)**	**($46)**
Cash Flow (Burn) per Day $60/bbl	($0.1)	($0.6)	($3.4)	($1.9)	($0.2)	$1.0	($0.2)	$0.2	($0.4)	($0.1)
2006E End of Year Unrestricted Cash $60/bbl	$3,220	$1,065	$83	$1,064	$556	$2,857	$238	$977	$89	$113
Mth of Cash Left with oil at $60/bbl from YE 2005 to threshold[4]	860	15	Ch. 11 Risk	11	68	CF Pos.	38	CF Pos.	3	22
2006E Cash Flow (Burn) Oil @ $65/bbl	**($428)**	**($384)**	**($1,579)**	**($965)**	**($113)**	**$328**	**($87)**	**$38**	**($186)**	**($58)**
Cash Flow (Burn) per Day $65/bbl	($1.2)	($1.1)	($4.3)	($2.6)	($0.3)	$0.9	($0.2)	$0.1	($0.5)	($0.2)
2006E End of Year Unrestricted Cash $65/bbl	$2,816	$891	NM	$810	$530	$2,820	$213	$945	$53	$102
Mth of Cash Left with oil at $65/bbl from YE 2005 to threshold[4]	49	8	Ch. 11 Risk	8	52	CF Pos.	28	CF Pos.	3	18

(1) Operating Cash Flow = Net Income + D&A+ pension expense; assumes no impact from change in net working capital.

Assumes crude price of $50/bbl in 2006. Incorporates hedge positions.

(2) Assumes no additional non-cash (stock of subsidiary) contribution to DB pension plans.

(3) Assumes crude price of $50/bbl in 2Q-4Q:05. For NO debt refinancing scenario in 2006, assumes no debt refinancing in 2005. For debt refinancing scenario in 2006, assumes debt refinancing in 2005.

(4) Chapter 11 risk: operating with cash burn and cash balance is below threshold cash level.

(5) FRNT is in 2007 March-ending Fiscal Year, base assumption oil at $50/bbl for calender 2006.

Source: Bear Stearns & Co., and company reports.

(US$ in millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT
Estimated Unrestricted Cash Concern Level	**$1,500**	**$1,000**	**$1,500**	**$1,100**	**$150**	**$750**	**$100**	**$300**	**$200**	**$75**

Source: Bear Stearns' estimates

As points of reference, we note that AMR achieved its last-minute deal with labor last April with $1.2 billion (7% of LTM sales) in unrestricted cash and equivalents,

UAL filed for Chapter 11 on 12/9/02 with $1.3 billion (9% of LTM sales) in unrestricted cash and equivalents (YE 2002),

and US Air entered Chapter 11 on 8/11/02 with close to $900mn in cash (3Q:02 balance was $900mn) (13% of LTM sales).

Scenario: With Debt Refinancing of 80% of Maturing Amount & Pension Plan Freeze / 20-Yr Amortization Proposal
As of 06/03/05

Cash Flow/Burn 2006E (US$ millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT[5]
2006E Operating Cash Flow[1]										
Operating CF (after tax) $35/bbl	$2,713	$1,045	$1,526	$1,633	$252	$1,095	$99	$439	$108	$50
Operating CF (after tax) $40/bbl	$2,336	$914	$1,189	$1,379	$226	$1,058	$73	$407	$72	$39
Operating CF (after tax) $45/bbl	$1,932	$788	$850	$1,124	$200	$1,021	$47	$376	$36	$27
Operating CF (after tax) $50/bbl (Base Case)	$1,528	$666	$512	$870	$174	$985	$21	$344	$0	$16
Operating CF (after tax) $55/bbl	$1,125	$493	$173	$615	$148	$948	($5)	$312	($35)	$4
Operating CF (after tax) $60/bbl	$721	$319	($165)	$361	$122	$911	($30)	$281	($71)	($7)
Operating CF (after tax) $65/bbl	$317	$146	($503)	$106	$96	$874	($54)	$249	($107)	($19)
Cash Obligations										
Net Capex	$210	$175	$530	$228	$188	$426	$30	$138	$59	$35
DB Pension Contributions[2]	$30	$31	$150	$112	NA	NA	NA	$1	NA	NA
Debt Maturities	$266	$107	$147	$199	$22	$121	$3	$11	$20	$4
Liquidity										
Estimated Unrestricted Cash Balance at Calendar 4Q:05[3]	$3,245	$1,275	$1,325	$1,775	$643	$2,492	$300	$908	$239	$159
Unrestricted Cash Balance at Calendar 4Q:04	$2,929	$1,460	$1,799	$2,459	$449	$1,305	$334	$874	$306	$149
2006E Cash Flow (Burn) Oil @ $35/bbl	**$2,208**	**$733**	**$700**	**$1,094**	**$42**	**$549**	**$66**	**$289**	**$28**	**$12**
Cash Flow (Burn) per Day $35/bbl	$6.0	$2.0	$1.9	$3.0	$0.1	$1.5	$0.2	$0.8	$0.1	$0.0
2006E End of Year Unrestricted Cash $35/bbl	$5,452	$2,008	$2,024	$2,868	$685	$3,041	$367	$1,196	$268	$171
Mth of Cash Left with oil at $35/bbl from YE 2005 to threshold[4]	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.
2006E Cash Flow (Burn) Oil @ $40/bbl	**$1,831**	**$602**	**$363**	**$839**	**$16**	**$512**	**$40**	**$257**	**($7)**	**$0**
Cash Flow (Burn) per Day $40/bbl	$5.0	$1.6	$1.0	$2.3	$0.0	$1.4	$0.1	$0.7	($0.0)	$0.0
2006E End of Year Unrestricted Cash $40/bbl	$5,075	$1,876	$1,687	$2,614	$659	$3,004	$341	$1,165	$232	$160
Mth of Cash Left with oil at $40/bbl from YE 2005 to threshold[4]	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	65	CF Pos.
2006E Cash Flow (Burn) Oil @ $45/bbl	**$1,427**	**$475**	**$23**	**$585**	**($10)**	**$475**	**$14**	**$225**	**($43)**	**($11)**
Cash Flow (Burn) per Day $45/bbl	$3.9	$1.3	$0.1	$1.6	($0.0)	$1.3	$0.0	$0.6	($0.1)	($0.0)
2006E End of Year Unrestricted Cash $45/bbl	$4,671	$1,750	$1,348	$2,359	$633	$2,967	$315	$1,133	$196	$148
Mth of Cash Left with oil at $45/bbl from YE '05 to threshold[4]	CF Pos.	CF Pos.	CF Pos.	CF Pos.	600	CF Pos.	CF Pos.	CF Pos.	11	89
2006E Cash Flow (Burn) Oil @ $50/bbl (Base Case)	**$1,023**	**$353**	**($315)**	**$330**	**($36)**	**$438**	**($12)**	**$194**	**($79)**	**($23)**
Cash Flow (Burn) per Day $50/bbl	**$2.8**	**$1.0**	**($0.9)**	**$0.9**	**($0.1)**	**$1.2**	**($0.0)**	**$0.5**	**($0.2)**	**($0.1)**
2006E End of Year Unrestricted Cash $50/bbl	**$4,267**	**$1,628**	**$1,010**	**$2,105**	**$607**	**$2,930**	**$289**	**$1,101**	**$161**	**$136**
Mth of Cash Left with oil at $50/bbl from YE 2005 to threshold[4]	**CF Pos.**	**CF Pos.**	**Ch. 11 Risk**	**CF Pos.**	**166**	**CF Pos.**	**209**	**CF Pos.**	**6**	**44**
2006E Cash Flow (Burn) Oil @ $55/bbl	**$619**	**$180**	**($653)**	**$76**	**($62)**	**$402**	**($37)**	**$162**	**($114)**	**($34)**
Cash Flow (Burn) per Day $55/bbl	$1.7	$0.5	($1.8)	$0.2	($0.2)	$1.1	($0.1)	$0.4	($0.3)	($0.1)
2006E End of Year Unrestricted Cash $55/bbl	$3,864	$1,455	$671	$1,850	$582	$2,894	$263	$1,069	$125	$125
Mth of Cash Left with oil at $55/bbl from YE 2005 to threshold[4]	CF Pos.	CF Pos.	Ch. 11 Risk	CF Pos.	96	CF Pos.	64	CF Pos.	4	29
2006E Cash Flow (Burn) Oil @ $60/bbl	**$215**	**$6**	**($991)**	**($179)**	**($88)**	**$365**	**($63)**	**$130**	**($150)**	**($46)**
Cash Flow (Burn) per Day $60/bbl	$0.6	$0.0	($2.7)	($0.5)	($0.2)	$1.0	($0.2)	$0.4	($0.4)	($0.1)
2006E End of Year Unrestricted Cash $60/bbl	$3,460	$1,281	$333	$1,596	$556	$2,857	$238	$1,038	$89	$113
Mth of Cash Left with oil at $60/bbl from YE 2005 to threshold[4]	CF Pos.	CF Pos.	Ch. 11 Risk	45	68	CF Pos.	38	CF Pos.	3	22
2006E Cash Flow (Burn) Oil @ $65/bbl	**($189)**	**($167)**	**($1,329)**	**($433)**	**($113)**	**$328**	**($87)**	**$99**	**($186)**	**($58)**
Cash Flow (Burn) per Day $65/bbl	($0.5)	($0.5)	($3.6)	($1.2)	($0.3)	$0.9	($0.2)	$0.3	($0.5)	($0.2)
2006E End of Year Unrestricted Cash $65/bbl	$3,056	$1,108	NM	$1,341	$530	$2,820	$213	$1,006	$53	$102
Mth of Cash Left with oil at $65/bbl from YE 2005 to threshold[4]	111	19	Ch. 11 Risk	19	52	CF Pos.	28	CF Pos.	3	18

(1) Operating Cash Flow = Net Income + D&A+ pension expense; assumes no impact from change in net working capital.
Assumes crude price of $50/bbl in 2006. Incorporates hedge positions.
(2) Assumes no additional non-cash (stock of subsidiary) contribution to DB pension plans.
(3) Assumes crude price of $50/bbl in 2Q-4Q:05. For NO debt refinancing scenario in 2006, assumes no debt refinancing in 2005. For debt refinancing scenario in 2006, assumes debt refinancing in 2005.
(4) Chapter 11 risk: operating with cash burn and cash balance is below threshold cash level.
(5) FRNT is in 2007 March-ending Fiscal Year, base assumption oil at $50/bbl for calender 2006.
Source: Bear Stearns & Co., and company reports.

(US$ in millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT
Estimated Unrestricted Cash Concern Level	**$1,500**	**$1,000**	**$1,500**	**$1,100**	**$150**	**$750**	**$100**	**$300**	**$200**	**$75**

Source: Bear Stearns' estimates
As points of reference, we note that AMR achieved its last-minute deal with labor last April with $1.2 billion (7% of LTM sales) in unrestricted cash and equivalents,
UAL filed for Chapter 11 on 12/9/02 with $1.3 billion (9% of LTM sales) in unrestricted cash and equivalents (YE 2002),
and US Air entered Chapter 11 on 8/11/02 with close to $900mn in cash (3Q:02 balance was $900mn) (13% of LTM sales).

IMPORTANT DISCLOSURES

Frontier Airlines[FRNT], JetBlue Airways Corp.[JBLU], Northwest Airlines Corp.[NWAC]: Bear, Stearns & Co. Inc. is a market maker in this company's equity securities.

For important disclosure information regarding the companies in this report, please contact your registered representative at 1-888-473-3819, or write to Sandra Pallante, Equity Research Compliance, Bear, Stearns & Co. Inc., 383 Madison Avenue, New York, NY 10179.

BEAR STEARNS

Equity Research

MARCH 2005

Airlines

Fear and Loathing on the Pension Front

Competitive and Legislative Uncertainties Abound

- **PENSION FUNDING DEFICITS DRIVE UP LIQUIDITY RISK.** We estimate the non-bankrupt U.S. network airlines' defined benefit (DB) pension plan funding shortfall at $14 billion, with plan benefit obligations of $35 billion and plan assets of just $21 billion. Combined with weak yields and high oil prices, the status quo on pension cash contributions could drive more legacy-cost airlines into Chapter 11.

- **FEARING LARGER CASH CONTRIBUTIONS.** We estimate aggregate pension cash contributions should rise just 3% in 2005, to $1.3 billion; however, 2006 contributions could rise another 113%, to $2.7 billion, barring a legislative remedy. Given the limitations of pension accounting/modeling and the uncertainty surrounding the year-end expiration of the Pension Funding Equity Act of 2004 (PFEA), we provide detailed sensitivity tests in this report.

- **LOATHING UNITED TERMINATIONS AND PFEA EXPIRATION.** We believe airline managements must abhor the idea of United Airlines terminating its DB pension plans and emerging from bankruptcy leaner, meaner, and free of billions in liabilities. Worry is also growing about the expiring PFEA, which currently allows for lower cash contributions via postponed deficit reduction contributions and a higher discount rate.

- **CAPITOL HILL: A CRITICAL FACTOR.** Congressional action (or inaction) in the next 12 months will play a key role in whether airlines contribute more than 40% of projected operating cash flow to employee pension plans in 2006. We see meaningful differences in pension-related risk and, in descending order, rank the carriers as follows: Delta, Northwest, Continental, AMR, and Alaska Air.

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BEAR
STEARNS

Table of Contents **Page**

All pricing is as of the market close on March 10, 2005, unless otherwise indicated.

BEAR STEARNS

Executive Summary

Lingering in the back of every airline CEO's mind is the following worst-case pension scenario:

United Airlines succeeds in terminating its defined benefit pension plans, ridding itself of billions in obligations and eventually emerging from Chapter 11 with unit costs within range of low-cost carriers (LCCs). Then, at year-end, the Pension Funding Equity Act expires without any follow-on legislative relief. Combined with the cash flow pressures from weak yields and high oil prices, the required cash contributions to pension plans take liquidity down to bankruptcy risk levels. At the same time, the cost of capital rises (or access to capital shuts down) because the capital markets view legacy airlines as having an even greater margin disadvantage versus a swath of the industry beyond just the LCCs, and, ultimately, it is much tougher to go on outside of Chapter 11, let alone begin the long, hard work of repairing over-leveraged, distressed balance sheets.

From an equity market perspective, such a scenario could be part of what the industry needs — no more life lines and another liquidity crunch, so that more costs are stripped out and/or consolidation takes place, essentially letting the natural forces of the free market work more efficiently. However, if history is any guide, legislators won't be able to resist stepping into the ring, and some additional measure of relief will be granted.

In this report, we examine pension and other post-employment benefit problems facing the U.S. airline industry, with detailed analysis of the following:

- **Pension Funding: An Awful Situation That Could Become Worse.** We examine pension funding deficits and required cash contributions, with breakdowns and comparisons of defined benefit, defined contribution, profit sharing, and health care costs.
- **The Sizable Valuation Implications of Pension Funding Deficits.** We test earnings, cash flow, and valuation sensitivity to changes in interest rates, market return assumptions, and unfunded liability capitalization.
- **Pension Plans in Limbo.** There is uncertainty about the fate of United Airlines' defined benefit pension plans and the expiration of the Pension Funding Equity Act at year-end.
- **Legal Ruminations.** We discuss current law, new legislative proposals, access to funding waivers, and the potential effect of all on cash flows.
- **Retiree Health Care: A Growing Problem.** We explore the potential health care funding crisis.
- **How Do the Airlines Stack Up?** We measure the meaningful differences between pension and OPEB (retiree health care obligations) costs, and their relationship to operating cash flow and unrestricted cash balances.

- **Company Pension Profiles.** We present pension summaries for Alaska Air, AMR, Continental, Delta, and Northwest, with comments on United Airlines and US Airways.

- **Pensions 101.** A fast tutorial on this complicated subject should help those in need of a primer.

- **Appendix.** In a series of exhibits, we focus on cash burn and oil sensitivity.

Pension Funding

AN AWFUL SITUATION THAT COULD BECOME WORSE

Pension Contributions Should Represent 50% of 2005 Operating Cash Flow with Oil at $46, 78% with Oil at $50

We estimate that the legacy airlines have defined benefit pension plans that are underfunded to the tune of $14 billion ($35 billion in plan benefit obligations versus $21 billion in plan assets) and will require about $1.3 billion in cash contributions this year, or $1.79 per share on average (assuming UAL does not terminate its plans, the total could be $2 billion, or $3 per share). These contributions represent about 50% of our operating cash flow forecast and 13% of the combined unrestricted cash balances.

This appears awful, but matters could become much worse next year. In 2006, barring a new legislative remedy, we believe the required cash contributions could increase 113%, to $2.7 billion, representing 45% of operating cash flow and 36% of existing cash with oil at $40/bbl and 79% of operating cash flow and 47% of cash with oil at $50. (Absent a replacement of PFEA 2004, pension discounting next year would revert to the 30-year Treasury yield, current-year DRC [deficit reduction contribution] requirements would be due in full, and the DRC deferrals from 2004-05 would need to be repaid in the near term.)

With regard to aggregate noncash P&L pension expenses, the outlook is also troublesome, since we project $1.6 billion in expenses in 2005 for Alaska Air, AMR, Continental, Delta, and Northwest ($2.35 per share on average).

We Believe Delta and Northwest Have the Greatest Pension Risk

Our analysis suggests that pension-related risk among legacy carriers operating outside of Chapter 11 is as follows, in ascending order: Alaska Air, AMR, and Continental, with Northwest and Delta bringing up the rear. In Exhibit 1 below, we set out our estimates for each carrier's funding deficit, defined benefit contributions, and pension expenses. We look at the costs on a unit basis for easy comparison and consider the relationship of the cash contributions/expenses to operating cash flow, unrestricted cash balances, and net earnings.

All told, if yields don't improve and oil remains above $45/bbl, the lack of a legislative band-aid for the pension funding problem could drive at least one more legacy carrier into bankruptcy, in our opinion:

- **Delta.** Based on our cash burn analysis, with $50 oil, Delta will be down to $1.1 billion by the end of this year (below its critical $1.5 billion level); however, even if we assume the carrier sells Comair and ASA for as much as $500 million, $50/bbl oil and pension obligations (barring a legislative fix) will chew up that cash by second-half 2006.

- **Northwest.** Northwest's situation is also troubling. Although the carrier has a larger unrestricted cash balance than Delta, without debt refinancing and pension law change, $50 oil could bring the carrier down to a critical $1.1 billion by mid-

2006 (with an 80% debt refi assumption, the carrier could survive until 2008), based on our analysis.

- **Continental.** Continental is only slightly better off. We estimate the carrier will be down to $1.1 billion (its bankruptcy risk valuation level) by early 2008 if we assume 80% debt refi and $50 oil. If the carrier fails to get its tentative labor deals ratified and is unsuccessful in refinancing its principal debt maturities in 2005, then the carrier will reach a bankruptcy-risk cash level in second-half 2005, in our estimation.

- **AMR.** AMR looks considerably stronger. Not even including the potential value from AMR's subsidiaries (American Eagle and American Beacon), with oil at $50, no change in pension law, and no debt refinancing, the carrier has enough cash to remain above its critical $1.5 billion level until 2007. Assuming AMR can refinance 80% of its principal debt maturities, we believe the carrier has a several-year liquidity cushion.

- **Alaska Air Group.** By any measure, Alaska Air Group has substantially less liquidity and pension risk, and we rank the carrier at the top of the heap. Even without any debt refinancing, we believe Alaska Air Group is nearly cash flow neutral with $50/bbl oil.

For more detail, please see our company pension profile section beginning on page 29 and our oil sensitivity cash burn in Exhibits 31-38 in the Appendix.

Our estimates are based on a generic pension model, which is highly dependent on assumptions about year-end discount rates, annual market performance, and contribution levels. Actual company results may differ.

Exhibit 1. Pension Summary — Cash Impact ($ in millions, except per share data)

	ALK	AMR	CAL[1]	DAL[2]	NWAC	Total/	UAL[3]	US Air[4]	AAI	AWA	FRNT[5]	JBLU	LUV
Plan Type	DB/DC	DB/DC	DB/DC	DB/DC	DB Plan	Average	DB/DC	DB/DC	DC Plan	DC Plan	DC Plan	DC Plan	DC Plan
12/31/2004													
Plan Assets (GAAP)	607	7,335	1,281	6,842	5,425	21,490	6,961	1,749	NA	NA	NA	NA	NA
Plan Benefit Obligations (PBO) (GAAP)	910	10,022	2,863	12,140	9,245	35,180	13,117	2,748	NA	NA	NA	NA	NA
PBO Pension Overfunded (Underfunded)	(303)	(2,687)	(1,582)	(5,298)	(3,820)	(13,690)	(6,156)	(999)	NA	NA	NA	NA	NA
ABO Pension Overfunded (Underfunded)	(161)	(1,823)	(1,131)	(5,239)	(3,565)	(11,919)	(5,692)	(971)	NA	NA	NA	NA	NA
Post Retirement Obligations (APBO)	(76)	(3,152)	NA	(1,835)	(921)	(5,984)	(3,069)	(1,369)	NA	NA	4	NA	80
2004 Assumed Rate of Return on Plan Assets	8.00%	9.00%	9.00%	9.00%	9.50%	8.90%	9.00%	8.01%	NA	NA	NA	NA	NA
2004 Assumed Discount Rate for Obligations	5.75%	6.00%	5.75%	6.00%	5.90%	5.88%	6.25%	6.00%	NA	NA	NA	NA	NA
2004 Asset Allocation: Equity/Fixed Income (remainder=other)	71%/29%	52%/36%	66%/28%	50%/28%	74%/20%	63%/29%	60%/35%	50%/41%	NA	NA	NA	NA	NA
2005E Revenue	2,847	19,638	10,352	15,701	11,854	60,393	NA	NA	1,326	2,467	843	1,647	7,183
2005E Operating Cash Flow (Oil at $46/bbl Base Assumption)	302	1,089	307	454	333	2,485	NA	NA	19	-12	-6	135	864
2005E Operating Cash Flow (Oil at $50/bbl)	278	784	181	208	147	1,598	NA	NA	6	-54	-13	120	853
2006E Revenue	2,967	20,161	10,837	16,662	12,315	62,942	NA	NA	1,646	2,602	NA	2,225	7,828
2006E Operating Cash Flow (Oil at $40/bbl Base Assumption)	332	1,982	798	1,558	1,214	5,884	NA	NA	60	24	NA	197	998
2006E Operating Cash Flow (Oil at $50/bbl)	267	1,149	511	546	897	3,371	NA	NA	11	-48	NA	145	923
2004 GAAP PBO Funding Status	67%	73%	45%	56%	59%	61%	53%	64%	NA	NA	NA	NA	NA
2004 GAAP ABO Funding Status	79%	80%	53%	57%	60%	66%	55%	64%	NA	NA	NA	NA	NA
2004 ABO per 2004 FTEs	12,448	20,099	29,383	75,763	90,616	47,560	98,991	39,427	NA	NA	NA	NA	NA
2004E P&L DB Pension Expense[6]	78	427	293	549	444	1,791	508	66	NA	NA	NA	NA	NA
2005E P&L DB Pension Expense[6]	89	380	227	440	500	1,637	NA	NA	NA	NA	NA	NA	NA
2005E DB Pension CASM	0.34¢	0.20¢	0.26¢	0.28¢	0.53¢	0.29¢	NA	NA	NA	NA	NA	NA	NA
2005E After-Tax EPS Impact	(2.12)	(1.51)	(2.20)	(2.22)	(3.70)	(2.35)	NA	NA	NA	NA	NA	NA	NA
2004 DB Expense	78	427	293	549	444	1,791	593	66	NA	NA	NA	NA	NA
2004 Defined Contribution & Profit Sharing Expense	25	163	30	150	NA	368	40	186	9	11	5	19	200
2004 Retirement (Health Care) Costs	9	264	NA	76	98	447	364	105	NA	NA	1	NA	18
2004 DB CASM	0.31¢	0.23¢	0.35¢	0.38¢	0.49¢	0.34¢	0.48¢	0.12¢	NA	NA	NA	NA	NA
2004 DC & Profit Sharing CASM	0.10¢	0.09¢	0.04¢	0.10¢	NA	0.07¢	0.03¢	0.33¢	0.08¢	0.04¢	0.07¢	0.10¢	0.26¢
2004 OPEB CASM	0.04¢	0.14¢	NA	0.05¢	0.11¢	0.08¢	0.25¢	0.19¢	NA	NA	0.01¢	NA	0.02¢
2004 Total DB, DC, OPEB CASM	0.44¢	0.46¢	0.38¢	0.53¢	0.59¢	0.49¢	0.75¢	0.63¢	0.08¢	0.04¢	0.08¢	0.10¢	0.28¢
Unrestricted Cash Balance (12/31/04)	874	2,929	1,460	1,799	2,459	9,521	1,300	738	334	306	149	449	1,305
2004E DB Pension Cash Contributions[6]	49	467	0	455	253	1,224	127	29	NA	NA	NA	NA	NA
2005E DB Pension Cash Contributions[6]	58	310	192	275	420	1,255	NA	NA	NA	NA	NA	NA	NA
2006E DB Pension Cash Contributions[7] Plan Freeze and 20-Yr Amort.	4	45	44	202	133	429	NA	NA	NA	NA	NA	NA	NA
2006E DB Pension Cash Contributions[7] Bush Proposal (7-Yr Amort.)	71	314	288	726	704	2,103	NA	NA	NA	NA	NA	NA	NA
2006E DB Pension Cash Contributions[7] PFEA expires (5-Yr Amort.)	76	377	356	962	901	2,672	NA	NA	NA	NA	NA	NA	NA
2005E After-Tax Projected Pension Cash per Share Impact	(1.38)	(1.24)	(1.86)	(1.39)	(3.11)	(1.79)	NA	NA	NA	NA	NA	NA	NA
2005E Pension Cash Contribution to 4Q04 Cash Balance	7%	11%	13%	15%	17%	13.2%	NA	NA	NA	NA	NA	NA	NA
2005E Pension Cash Contribution to 2005E Op. Cash Flow	19%	28%	63%	61%	126%	50.5%	NA	NA	NA	NA	NA	NA	NA
2005E Pension Cash + Debt Mat.+ Net Capex to 2005E Op. Cash Flow	93%	159%	327%	310%	411%	233.3%							
2006E (20-Yr Amort.) Pension Cash Contribution to 2006E Op. Cash Flow	1%	2%	6%	13%	11%	7.3%	NA	NA	NA	NA	NA	NA	NA
2006E (7-Yr Amort.) Pension Cash Contribution to 2006E Op. Cash Flow	21%	16%	36%	47%	58%	35.7%	NA	NA	NA	NA	NA	NA	NA
2006E (5-Yr Amort.) Pension Cash Contribution to 2006E Op. Cash Flow	23%	19%	45%	62%	74%	45.4%	NA	NA	NA	NA	NA	NA	NA
2006E (20-Yr Amort.) Pension + Debt Mat. + Net Capex to '06E Op. Cash Flow	57%	80%	94%	94%	112%	90.7%	NA	NA	NA	NA	NA	NA	NA
2006E (7-Yr Amort.) Pension + Debt Mat. + Net Capex to '06E Op. Cash Flow	77%	93%	124%	128%	159%	119.2%	NA	NA	NA	NA	NA	NA	NA
2006E (5-Yr Amort.) Pension + Debt Mat. + Net Capex to '06E Op. Cash Flow	78%	97%	133%	143%	175%	128.9%	NA	NA	NA	NA	NA	NA	NA

DB = defined benefit pensions, where employer bears investment risk. DC = defined contribution pensions plan such as 401(k), where the employee assumes the investment risk. PBO = projected benefit obligation (assumes future wage inflation). ABO = accumulated benefit obligation (pension obligations already accrued; if a plan were frozen, this would be GAAP analogous amount). APBO = accumulated post retirement benefits obligation. OPEB includes post-employment health care benefits — medical, dental, vision, hearing, and other health-related benefits, whether provided separately or through the pension plan. Other benefits include life insurance, disability, long-term care, etc., when provided separately from a defined benefit pension plan. Operating cash flow = net income + D&A + pension expense; assumes no impact from change in net working capital.

(1) Continental's 2005E required pension contribution is $307 million; however, in the table above, which focuses on cash, we exclude $65 million in stock contributed in the first quarter and assume $50 million in savings from ratification of labor deals. Similarly, pension expense is $315 million, though it is expected to decline by $90 million upon ratification of tentative labor agreements.

(2) Delta froze its DB plan as of 12/31/04, eliminating future service accruals, though wage increases will still be factored into benefit calculations. 2004 pension expense excludes curtailment charges.

(3) UAL contributed $17 million and $110 million during the first and second quarters of 2004 ($700 million was estimated to be due last year), respectively, to its plans; however, the carrier currently does not expect to make any contributions to its pension plans before exiting from bankruptcy and intends to terminate its plans. UAL's information is as of 2003 except for cash.

(4) Effective February 1, 2005, the PBGC was appointed trustee of US Airways AFA, IAM, and CE plans. In 2004, prior to entering Chapter 11, the carrier had been obligated to contribute $155 million to its plan.

(5) FRNT is on a March fiscal year-end. FY2006 = 2005.

(6) Based on 2004 company 10k, third-quarter 2004 10Q data, fourth-quarter 2004 conference calls, company guidance, and Bear, Stearns & Co. Inc. estimates.

(7) Bear Stearns' forecasts: 2006 forecasted pension cash contributions assume expiration of the Pension Funding Equity Act of 2004. Three scenarios (assuming an even amortization repayment schedule): 1) assumes plan freezes and a 20-year DRC amortization, 2) assumes a seven-year DRC amortization (Bush proposal), and 3) assumes PFEA expires and a five-year DRC amortization.

Actual company results may vary considerably. Please see our September 2003 Airline Pension report for more information.

Note: Firms may be able to contribute limited amounts of stock in certain circumstances instead of cash. In addition, firms may apply for IRS waivers that could allow them to spread payments out over five or so years. Furthermore, interest rate changes, asset returns, and legislative changes could have significant impacts on these forecasts.

Source: Bear, Stearns & Co. Inc. estimates; company reports; company guidance; First Call.

While ERISA and the Internal Revenue Code rules dictate funding periods ranging from as few as three to as many as 30 years, after surveying our companies and for purposes of this report, we assume for simplifying reasons that deficit reduction contributions are repaid in five years under current law and would continue to be due in this time frame should PFEA expire without replacement.

The Sizable Valuation Implications of Pension Funding Deficits

SHOULD INVESTORS CAPITALIZE THE UNFUNDED PORTION OF THE PENSION LIABILITY?

Pension funding deficits pose some important valuation considerations. Should investors capitalize the unfunded portion of a company's pension liability, which would be tantamount to assuming it has to issue debt to fund its plans? This is not an easy decision, as interest rates, pension asset returns, and many other variables could reduce or even eliminate current funding deficits down the road.

As a tool for those who choose to book the funding shortfall, we provide our current EV/EBITDAR forecasts with and without the 2004 ABO funding gap in the context of the carriers' historical means. Not surprisingly, inclusion of pension deficits leads to more expensive valuations, with Northwest's and Delta's expanding by roughly 30% each.

Exhibit 2. Pension Deficit Could Affect Valuation

	2006E EV/EBITDAR			Historical EV/EBITDAR
	Without Pension	Incl. Pension	% Chg.	Without Pension
AMR	6.0x	6.6x	10%	5.2x
CAL	7.5x	8.1x	9%	5.6x
DAL	6.8x	8.7x	27%	4.6x
NWAC	5.6x	7.5x	34%	4.7x
ALK	4.9x	5.2x	6%	7.8x

Note: Only includes the 2004 ABO underfunding amount, assumes borrowed underfunded amount to make plan whole.
EV= equity market capitalization + total debt, incl. operating leases less unrestricted cash.

Source: Bear, Stearns & Co. Inc. estimates.

VALUATION SENSITIVITY TO DISCOUNT RATES AND MARKET RETURN ASSUMPTIONS

What are the implications for P/E, P/EBITDA, and EV/EBITDAR as discount rate and market return assumptions change? In the exhibit below, we isolate the EPS and P/E impact of a 50-basis-point (bp) change in the discount rate or the rate of return assumption used to measure pension plan expenses. All told, valuations could appear to be 3%-35% more expensive or 3%-21% cheaper thanks to a 0.5%-point change in the underlying pension expense input.

Exhibit 3. Valuation Sensitivity to Discount Rate Changes

	2006/7 P/E Sensitivity:								
		0.5% Change in the Pension Discount Rate				0.5% Change in the Assumed Rate of Return			
	No Change	-50 Bps	% Chg.	+50 Bps	% Chg.	-50 Bps	% Chg.	+50 Bps	% Chg.
AMR	8.5x	11.5x	33%	7.5x	-20%	9.4x	15%	7.2x	-12%
CAL	9.5x	12.5x	35%	7.5x	-21%	9.5x	6%	8.5x	-5%
DAL	4.5x	5.5x	22%	3.5x	-15%	4.7x	19%	3.4x	-14%
NWAC	6.5x	7.5x	31%	5.5x	-19%	6.6x	19%	4.8x	-14%
ALK	9.5x	9.5x	7%	8.5x	-6%	9.0x	3%	8.6x	-3%

Note: ALK, AMR, CAL, and NWAC are off of 2006 estimates. DAL assumes a hypothetical normalized 7% op. margin in 2007.

Source: Bear, Stearns & Co. Inc. estimates; company reports; First Call.

STOCK OPTIONS WILL ALSO HIT VALUATIONS THIS YEAR

Per SFAS No. 123R, U.S. airlines will be required to expense stock options using a fair value method beginning in the third calendar quarter this year. As a result, we expect some valuation headwinds for the profitable segment of the industry that utilizes stock options to a greater extent than the legacy carriers. Our 2005 and 2006 EPS estimates already take into account option expense for the U.S. airlines in our coverage; however, we suspect that the First Call mean may not fully reflect fair value option expense at present. Therefore, all else equal, estimates may be susceptible to downward pressure as the Street begins to incorporate option expenses into its second-half 2005/full-year 2006 estimates.

Further, option expense has broader implications than just added labor expense and hence lower net income. For instance, JetBlue expects to book a higher tax rate this year (47% versus 40% in previous years) due to its heavy reliance on incentive stock options, which generally do not provide for corporate tax deductibility.

Exhibit 4. Beware! Stock Option Expense Should Affect Valuation this Year

Stock Options Expenses: SFAS 123R			2004		First Call 2006 Mean P/E	
	Co. Disclosed 2H05E		Per Share	$ Mil.	Assuming No Option Expense	Less Option Expense
AMR	undisclosed		$0.40	$64	NM	NM
CAL	$9-15mn	$0.13	$0.09	$6	12.9x	18.2x
DAL	"may be material"		$0.29	$38	NM	NM
NWAC	already expensed		already expensed		NM	NM
AAI			$0.03	$2	19.5x	19.5x
ALK	$2-3mn	$0.09	$0.17	$5	9.3x	9.9x
AWA	"material impact"		$0.16	$6	NM	NM
FRNT			$0.05	$2	NM	NM
JBLU	$11mn	$0.10	$0.17	$19	30.0x	45.0x
LUV	$20mn	$0.02	$0.08	$74	22.6x	24.2x

Note: Net of tax figures. FRNT is FY 2004.

Source: Company reports; Bear, Stearns & Co. Inc. estimates; First Call.

Pension Accounting in SEC Crosshairs

In October 2004, the SEC began an informal inquiry into the accounting assumptions used for pension plans. Northwest Airlines and five other large defined benefit plan sponsors were among those queried for internal information regarding their pension and other post-retirement plans. While the criteria for the SEC's selection remain unclear, a cursory observation suggests that the aggregate pension obligation relative to a company's market capitalization may have been one screen applied. At first blush, Northwest stands out because of its expected rate of return assumption, which has exceeded that of its peers and the S&P 500 average by 50-150 basis points (bps) over the past three years. Nevertheless, when we examine plan asset allocations (see Exhibit 5 below), we discover that Northwest is more heavily weighted to equities than its peers.

Exhibit 5. Pension Accounting (GAAP) Assumptions

	Actual Discount Rates					Actual Expected Rate of Return				
	2000	2001	2002	2003	2004	2000	2001	2002	2003	2004
ALK	7.50%	7.25%	6.75%	6.00%	5.75%	10.00%	10.00%	8.00%	8.00%	8.00%
AMR	7.75%	7.50%	6.75%	6.25%	6.00%	9.50%	9.50%	9.25%	9.00%	9.00%
CAL	8.00%	7.50%	6.75%	6.25%	5.75%	9.50%	9.50%	9.50%	9.00%	9.00%
DAL	8.25%	7.75%	6.75%	6.13%	6.00%	10.00%	10.00%	10.00%	9.00%	9.00%
NWAC	7.90%	7.50%	6.75%	6.25%	5.90%	10.50%	10.50%	10.50%	9.50%	9.50%
S&P 500 Average		7.12%	6.59%	6.07%	NA	NA	9.07%	8.86%	8.34%	NA

Source: Bear, Stearns & Co. Inc. estimates; company reports.

Pension accounting has often been the subject of investor concern, since changes in assumptions and realized market rates can materially affect a company's P&L. However, all the red ink in the airline industry in recent years seems to suggest that carriers are hardly making aggressive assumptions in order to boost net profits. In addition, if the SEC inquiry results in any sort of corrective action, it should only be a

GAAP accounting issue, since the SEC does not oversee pension cash funding guidelines — the Department of Labor (through ERISA) and the IRS do.

Exhibit 6. Pension Plan Asset Allocation

	ALK	AMR	CAL	DAL	NWAC	UAIR	UAL
Total Equity	71%	52%	66%	50%	74%	50%	60%
Fixed Income	29%	38%	28%	28%	20%	41%	35%
Other: Private Equity, Real Estate, Etc.	NA	10%	6%	22%	7%	9%	5%
Total	100%	100%	100%	100%	100%	100%	100%

Note: ALK, AMR, CAL, DAL, NWAC, and UAIR as of 2004; UAL as of 2003.

Source: Bear, Stearns & Co. Inc. estimates; company reports.

That said, should companies feel the need to reduce their expected rate of return assumptions as a result of the SEC's scrutiny, the income statement effect could be noticeable. For example, using our pension forecasting models, leaving all else equal, we estimate the expense impact could range from $3 million to $36 million, or $0.07-$0.20 per share, for each one-half-percentage-point (50-bp) decrease in the expected rate of return assumption used for GAAP pension accounting. For example, should Continental lower its expected rate of return assumption by 50 bps, we would expect a $7 million increase in costs, or a $0.07 per share negative impact.

Exhibit 7. Pension Expense and Pension Liability Sensitivity

	50-Basis-Point Decline in Assumptions:				
	ALK	AMR	CAL	DAL	NWAC
	Effect on P&L Pension Expense from Change in Expected Return Assumption				
(mns)	($3)	($36)	($7)	($35)	($27)
EPS	($0.09)	($0.14)	($0.07)	($0.18)	($0.20)
	Effect on P&L Pension Expense from Change in Discount Rate Assumption				
(mns)	($9)	($68)	($35)	($40)	($40)
EPS	($0.21)	($0.27)	($0.34)	($0.20)	($0.30)
	Effect on GAAP PBO Pension Liaibility				
(mns)	$55	$623	$256	$750	$700
% 2004 PBO	6%	6%	9%	6%	8%

Note: Assumes 36% tax rate.

Source: Bear, Stearns & Co. Inc. estimates; company reports.

Pension Plans in Limbo

UAL/US AIR AND LEGISLATIVE UNCERTAINTY

Fear surrounding airline pension funding deficits is exacerbated by uncertainty about the fate of United Airlines' defined benefit pension plans and the expiration of the PFEA at year-end. United Airlines' DB plans are about $6 billion underfunded, and the carrier has about $4 billion in minimum cash contributions due through the end of the decade. In July 2004, the carrier began skipping its required cash contributions and is working toward terminating its pension plans this May. While the carrier announced it has four offers for $2-$2.5 billion in exit financing, our sense is that the delivery of those funds is predicated on a successful resolution of the pension matter. At the same time, investors are concerned about the expiration of the PFEA and the potential for increases in already onerous pension cash contributions.

While United works toward a May termination of its pension plans (US Airways terminated its plans in January), the nonbankrupt airlines painfully watch their progress and reiterate the mantra of labor parity to their own work groups. By the end of the second quarter, we expect to have a better idea about UAL's attempt to scuttle its plans, but legislative uncertainty could linger through the year and even up until April 15, 2006, the deadline for calendar 2006's first pension installment.

HOW DID IT GET SO BAD?

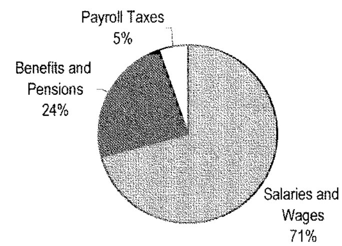
A Perfect Storm

There are three major forces behind the airlines' pension problems:

- First, during the good times, the airlines negotiated generous packages with the unions — more than they can deliver through a full business cycle.
- Second, pension law effectively caps funding levels, which limits companies' ability to fortify plan assets during good years. (Despite running sizable funding deficits, many companies were not required to contribute much cash, if any, to their pensions prior to 2003.)
- Third, the combination of poor stock market performance and low interest rates helped to widen the gap between plan assets and liabilities. The market declines of 2000-02 shrank pension plan assets at the same time that lower interest rates boosted liabilities. (Lower interest rates increase the present value of projected benefit obligations [PBO] and poor market returns decrease the value of plan assets, while higher interest rates lower the present value of obligations and higher stock market returns increase the value of plan assets.)

Exhibit 8. Pension and Benefits Account for a Quarter of All Labor Costs

Employment Cost for 2004 = 33% of Total Operating Expenses and Operating Revenues



Note: Major and national passenger airlines for 12 months ended 3Q04.
Source: ATA.

What's more, despite positive asset returns in 2004, our 60%/40% pension fund proxy had pension assets up 8% (however, the average airline DB plan returned 12% last year), and interest rates finished down from 2003 levels, largely negating asset returns by increasing the present value of plan obligations and leaving pension plan funding levels right around last year's low water mark (see Exhibits 9 and 10 below). Hence, pension plans are still in dire straits. For example, Northwest mentioned that its plan assets rose more than 14% in 2004, yet its ABO shortfall was still $3.5 billion, up from $3.3 billion in 2003. Looking out to 2005 discount rates, due to the four-year weighted average calculation methodology, it is unclear how much rates might change by year-end even though more Fed rate hikes are coming down the pike.

Exhibit 9. Interest Rate Decline Could Offset Asset Gains in 2004

Interest Rates for Current Liability Funding Calculations

Basis-Point Change from Previous Year-End		
12/31/2004	6.10%	***-0.45***
12/31/2003	6.55%	*-0.56*
12/31/2002	7.11%	*-0.23*
12/31/2001	7.34%	

2004 Proxy Pension Fund Return

		Weighting
Lehman U.S. Bond Composite Index	4.5%	*40%*
S&P 500 Index Total Return	11%	*60%*
Aggregate Return	**8.4%**	

Note: Corporate bond weighted average interest rate as per the Pension Funding Equity Act of 2004. Lehman Allocation = 33% U.S. government, 33% investment grade corporates, 33% mortgages. The average airline DB plan returned 12% in 2004.
Source: Bear, Stearns & Co. Inc. estimates; Internal Revenue Service; Bloomberg.

Exhibit 10. Interest Rate Decline Could Offset Asset Gains in 2004

	2004E Incremental Funding Level Impact (in % points)					
	Discount Rate for 2004					
2004 Forecasted Market Return	6.0%	6.2%	6.4%	6.6%	6.8%	7.0%
1%	-6%	-4%	-2%	1%	3%	6%
4%	-5%	-2%	0%	2%	5%	8%
7%	-3%	-1%	2%	4%	7%	10%
10%	-1%	1%	3%	6%	9%	12%
13%	0%	3%	5%	8%	11%	14%
16%	2%	4%	7%	10%	13%	16%

Composite = ALK, AMR, CAL, DAL, NWAC.

Source: Bear, Stearns & Co. Inc. estimates.

Legal Ruminations

In response to the looming year-end expiration of a temporary fix to funding rules, players in several corners have espoused remedies of both a short- and long-term nature. In early January, the Bush Administration unveiled a set of proposals to simplify and strengthen funding rules (shore up the federally insured pension funding system [PBGC]), including: 1) higher premiums, 2) duration-matched discount rates, 3) risk-based liability measures, and 4) more leverage for the PBGC in the Chapter 11 process. ALPA, the largest pilots union, as well as Northwest Airlines CEO Douglas Steenland, have called for freezing DB plans and much longer amortization periods for making up funding shortfalls (versus today's often much shorter time frame).

While ERISA and the Internal Revenue Code rules dictate funding periods ranging from as few as three to as many as 30 years, after surveying our companies and for purposes of this report, we assume for simplifying reasons that deficit reduction contributions are repaid in five years under current law and would continue to be due in this time frame should PFEA expire without replacement.

For its part, Congress could proffer its own set of measures and/or embrace the Administration's proposals to one degree or another. Rep. John Boehner (R-Ohio) is expected to continue the charge for pension reform in the House this term. In the Senate, Finance Committee Chair Chuck Grassley (R-Iowa) has already reintroduced pension legislation. While we applaud moves to freeze DB plan liabilities, we note that the trend to offer generous replacement DC plans can be just as costly, if not more so, in terms of current pension expenses and contributions.

CURRENT LAW TO EXPIRE IN 2005

The Pension Funding Equity Act (PFEA) of 2004

The PFEA, signed into law in April 2004, provided for significant deficit reduction contribution deferrals, which are ERISA-mandated accelerated pension funding requirements. The airlines received an 80% DRC reprieve in 2004 and 60% this year. In addition, the law changed the discount rate benchmark used to determine normal contributions from the 30-year Treasury to a 20-plus-year high-grade corporate bond series (AAA, AA, A). (A rise in the discount rate has the effect of lowering the present value of future liabilities, in turn reducing annual cash funding requirements.) We believe that the combined effect of switching to a corporate bond discount rate and an 80% deferral saved the airlines an estimated $1 billion in cash last year.

This year, despite the 60% DRC deferral and higher discount rate, the carriers ex UAL will still need to fund $1.3 billion in pension contributions, up from $1.2 billion in 2004, or 50% of our estimated operating cash flow for the group. Absent a replacement of PFEA 2004, pension discounting next year would revert to the 30-year Treasury yield, the current-year DRC requirements would be due in full, and the DRC deferrals from 2004-05 could become due in as short as three to five years. All of this could set the stage for a massive cash crunch in the next year or two unless oil prices crater and yields suddenly rebound.

LEGISLATIVE PROPOSALS

Bush Administration Proposes Pension Overhaul, But Not Enough to Spare Airlines

On January 10, Secretary of Labor Elaine Chao outlined the Bush Administration's pension reform initiatives. In our view, the salient issues for airline pensions in the President's proposal are: 1) higher standard premiums (from $19 per participant up to $30), plus additional risk-based premiums for severely underfunded plans; 2) seven-year amortization periods for making up unfunded liabilities versus today's potentially shorter time frame; 3) duration-matching yield curves for liability discounting; 4) requiring financially-weak sponsors to use a more conservative funding measure; 5) empowering the PBGC to perfect liens in bankruptcy proceedings; 6) disallowing lump-sum distributions at severely underfunded plans; and 7) freezing PBGC guarantee levels once a sponsor enters bankruptcy.

Exhibit 11. Administration's Proposals Seen as Largely Negative for Airlines

	Impact on Airlines	Notes
DRC Amortization (7 years)	Positive	Better than today's 3-5 year minimum
Duration-matched discount rate	Unclear	Plans with durations over 23 years could benefit
At-Risk Liability Measure	Negative	Non-investment grade likely = higher liabilites = higher DRC payments
Increase in Flat-Rate Premiums	Negative	Would increase to $30 from $19 per participant
Change in Variable-Rate Premiums	Unclear/Negative	Today, $9 per $1,000 of underfunding vs. weak financial sponsors' pay based on at-risk liability
PBGC Lien Perfection in Ch. 11	Negative	Could reduce assets available for other creditors

Note: U.S. legacy carriers are rated non-investment grade by the major credit agencies as of February 2005.

Source: Bear, Stearns & Co. Inc. estimates.

While the full potential effect of enacting the Administration's proposals is uncertain at this time, our initial take is that the airlines would see little benefit, and could perhaps suffer even more financial pressure under the Bush plan. For example, under the Bush proposal, the seven-year amortization period would likely leave carriers such as Delta and Northwest (and UAL, if does not succeed in terminating its plans in Chapter 11) with hefty pension cash obligations each year. Similarly, requiring duration matching could in fact enervate funding levels, depending on plan duration levels. For example, a plan with a duration under 23 years as of December 2004 would have used a lower rate than the current corporate bond rate had the Administration's plan been in effect at the time.

Further, other provisions, such as higher premiums, PBGC superpriority in bankruptcy proceedings, and prohibition of lump-sum payouts at deeply underfunded plans should strengthen plans; however, should early retirement-eligible employees fear enactment of the anti-lump sum payout provision, a cascade of early retirements could ensue, similar to what occurred at Delta last year, which could serve to weaken a sponsor's financial position.

Exhibit 12. Administration's Seven-Year Amortization Offers Scant Relief and Would Need to Double to Provide Meaningful Cash Flow Assistance

Illustration of DRC Burden: Hypothetical Amortization Schedules (per year contribution)

	ALK	AMR	CAL	DAL	NWAC	UAL
ABO Shortfall	(161)	(1,823)	(1,131)	(5,239)	(3,565)	(5,692)
5 Years 2006-2010	(17)	(181)	(178)	(806)	(533)	(885)
7 Years 2006-2012 (Bush proposal)	(12)	(130)	(127)	(576)	(381)	(632)
15 Years 2006-2020	(6)	(60)	(59)	(269)	(178)	(295)
20 Years 2006-2025	(4)	(45)	(44)	(202)	(133)	(221)
25 Years 2006-2030	(3)	(36)	(36)	(161)	(107)	(177)

Note: Assumes 2004 ABO shortfall is equal to 2004 current liability funding level and funding level rises to 90% over stated period. 2004 likely reduced funding gaps a touch as assets rose, offset by declining interest rates. CAL has reached tentative labor agreements, which, if ratified, could freeze its DB plans and significantly lower pension funding requirements. UAL figures use 2003 ABO.

Source: Bear, Stearns & Co. Inc. estimates; company reports.

Airline employees have also taken a less-than-favorable view of the Administration's plan, as evidenced by United's pilot union chief, Mark Bathurst, who remarked that "taken as a whole, [the Bush proposal] would make it much more costly for United to maintain its current pension plans." Nor is it just the unions — Scott Yohe, Delta's senior vice president of government affairs, declared, "The Administration's proposal would not help us. The primary reason is not the seven years, but the interest rate assumption, which would not give us the kind of relief we are looking for in terms of the funding obligations we have got in the near term."

Northwest Airlines CEO and ALPA President Make Proposal

One of the more outspoken airline executives on pension issues has been Northwest's CEO, Douglas Steenland. Along with Duane Woerth, president of ALPA and a former PBGC director, Northwest's chief penned a *Wall Street Journal* article espousing a three-phase process:

- First, companies and their unions would agree to freeze the existing defined benefit plan accruals (i.e., no further benefit accruals would be allowed).
- Next, concurrent with the defined benefit freeze, the parties would establish a replacement defined contribution plan. While a replacement plan would likely be partially company funded, the investment performance risk rests with the employees.
- Last, Congress would need to amend ERISA to permit plan sponsors to meet their DRC requirements over a much longer time period than today's potentially shorter time frame (e.g., three to five years).

The first two steps can be accomplished by the companies under existing law, as evidenced by Delta's November 2004 pilot contract and Continental's recent tentative agreements. However, the ultimate success of such a move, from a cash flow perspective, appears to rest on the extension of DRC amortizations.

Senate Finance Bill Reintroduced: NESTEG (S.219)

On January 31, 2005, Senate Finance Committee Chairman Chuck Grassley and ranking member Max Baucus reintroduced their pension reform legislation from last year, titled The National Employee Savings and Trust Equity Guarantee (NESTEG) Act. For airlines, the main thrust of NESTEG is replacing the 30-year Treasury Bond-based discount rate with a corporate bond-based yield curve. As we mentioned earlier in regard to the Administration's proposal, depending upon the duration of a given pension plan, a switch to a yield curve could adversely affect plan sponsors by raising liabilities and, in turn, plan expenses. For example, at a Senate Finance Committee hearing on March 1, 2005, witnesses from The Business Roundtable noted that the Administration's yield curve proposal could "increase pension liabilities for a typical mature plan by 10% or more. In some cases, the immediate liability increase could be even greater. For large plans, this could cost billions of dollars."

FUNDING WAIVERS — ADMINISTRATIVE RELIEF

In times of duress, airlines can petition federal administrative agencies for pension funding waivers. The Department of Labor's (DOL) Employee Benefits Security Administration has the authority to allow exemptions to certain ERISA rules, such as contributions of in-kind securities to a DB plan. For its part, the IRS has the authority to grant waivers deferring current contribution requirements to the following year. Northwest Airlines was a beneficiary of these agencies' administrative power in 2003, when the IRS permitted it to defer $454 million in 2003 minimum funding requirements. Funding waivers are limited to three in 15 years, and repayments are generally made over a five-year period. In return for this deferral, Northwest's plans received liens on some Northwest planes, landing slots, and routes.

Similarly, the DOL emphasized that its decision to exempt additional firms would be made on an individualized basis after a thorough review of each situation. However, in order to obtain a waiver, a sponsor must demonstrate that it is experiencing *temporary* hardship, and given the current state of the industry, it may be more challenging to convince the government of such a transitory misfortune. As United highlighted in its court filings (see exhibit below), the medium-term effect of a waiver is likely to only enlarge cash funding needs, as sponsors are required to repay the waived amount plus interest to the plan generally over five years.

Exhibit 13. Waivers Only Delay Funding Temporarily, Leading to Increased Total Contributions
($ in billions)

United Airlines Minimum DB Funding Contributions		
	No Waiver	**Waiver**
2005E	$1.2	$0.2
2006E	$1.0	$0.4
2007E	$1.5	$1.0
2008E	$0.6	$1.4
2009E	$0.1	$1.2
2010E	$0.0	$0.5
Total	**$4.4**	**$4.8**

Source: United Airlines.

Exhibit 14. Waivers Remain a Possible Near-Term Funding Alternative: 2006-08?

IRS Waivers Remaining	
(sponsors permitted to 3 per 15 year period for each plan, spreads payment out over 5 years)	
ALK	3
AMR	3
CAL	3
DAL	3
NWAC	2 or 3
UAL	3

Note: NWAC used one waiver in 2003 for its contract and salaried plans, leaving two for those plans and three for other plans.

Source: Bear, Stearns & Co. Inc. estimates; company reports.

Nevertheless, we would not be surprised if most carriers applied for IRS waivers for 2006 plan-year contributions, especially if Congress is slow to enact replacement legislation for PFEA 2004.

NONCASH CONTRIBUTIONS

In-kind contributions are another avenue available for satisfying some contribution needs, though they may require DOL approval. For example, in 2003, the DOL authorized Northwest to contribute stock in its then-privately held subsidiary, Pinnacle, to its DB plans in lieu of cash to satisfy its $223 million of 2002 funding requirements. Our sense is that the DOL is leery of allowing illiquid, noncash asset contributions to meet funding requirements.

AMR possesses several assets that it could monetize to meet some of its pension funding needs. For example, sole ownership of American Beacon Advisors, a money manager (with $37 billion in assets under management as of January 2005), could provide a decent cash boost. As a reference, see Exhibit 15 below, which illustrates potential values for asset management firms based on assets under management. It is difficult to home in on the true value of American Beacon Advisors as more than 50% of the assets are related to AMR, while a similar percentage is also managed by third parties, suggesting lower margins for the company as opposed to actively managed in-house funds. In addition, AMR could spin off its regional affiliate, American Eagle, which it also owns outright, similar to what its legacy peers Continental and Northwest did in 2002-03 with their regional entities. (See Exhibit 16 below for theoretical regional affiliate values based on publicly available revenue and market values for publicly traded peers.)

Exhibit 15. Hypothetical Values for Asset Management Firms

		Assets Under Management (AUM) (US$ in billions)			
		$15	$20	$25	$30
		Implied Value of Asset Management Unit (US$ in millions)			
Price to AUM Ratio	1.5%	$225	$300	$375	$450
	2.0%	$300	$400	$500	$600
	2.5%	$375	$500	$625	$750
	3.0%	$450	$600	$750	$900
	3.5%	$525	$700	$875	$1,050
	4.0%	$600	$800	$1,000	$1,200

American Beacon Advisors directly managed or served as fiduciary or financial advisor for $37.6 billion in assets at 1/31/05 consisting of $17.3 billion under active management and $20.3 billion as named fiduciary or financial adviser.

Source: Bear, Stearns & Co. Inc. estimates; company reports.

Exhibit 16. Regional Units Could Potentially Help Fund Pension Plans

Parent (former)	CAL	NWAC	**AMR**		**DAL**	
	XJT	PNCL	**Eagle + Exec.**	SKYW	**ASA + Comair**	**Mean**
ASMs (billions)	4.77	2.22	4.54	1.70	8.59	
Revenue (millions)	$1,461	$581	$1,820	$1,067	$2,117	
EBT Margin Actual **(Assumed)**	13%	11%	**6%**	12%	**6%**	**12%**
P/E Actual **(Assumed)**	6.6x	4.2x	**7.1x**	10.4x	**7.1x**	**7.1x**
Actual **(Implied)** Market Cap.	$604	$223	**$496**	$1,012	**$577**	
Assuming 12% EBT Margin			**$988**		**$1,149**	
10% of 2003 DB Plan Assets = Potential Contribution Ceiling			**$734**		**$684**	

Note: Second-half 2004 Scheduled ASMs from OAG via BACK Aviation; Revenue = 12 months ended 9/30/04. Comair and ASA revenues 12 months ended 6/30/04 using OD1A data. Market capitalization for XJT, PNCL, and SKYW as of 3/10/05. As reference, NWAC contributed $350 million (roughly 7% of total GAAP plan assets at 12/03) worth of privately held Pinnacle shares to its defined benefit plans in 2003. CAL contributed $100 million of XJT to its DB plans (approximately 8% of GAAP plan assets at 12/03), which was freely tradable. DAL paid over $2 billion for Comair and ASA according to media reports. Assumes 36% tax rate for wholly owned subsidiary implied market value calculations.

Source: Bear, Stearns & Co. Inc. estimates; company reports.

Ins and Outs of Noncash Contributions

Publicly traded securities — such as those of a sponsor's own equity, an affiliate, or other marketable securities — do not require a special exemption from the DOL, as was the case in Northwest's contribution in 2003. However, limitations still exist. For instance, the pension fund cannot own more than 25% of the entire equity, at least 50% of the equity must be in hands of shareholders unaffiliated with the parent company, and no more than 10% of plan assets may be invested in employer (and subsidiary) stock. That said, Continental contributed shares in former subsidiary ExpressJet in 2003 and did so again in January 2005 to mitigate the pension cash outflow. While recognizing the strategic value of regional subsidiaries, Delta CEO Gerald Grinstein acknowledged on December 15, 2004 that "you do not have to own them to get all of the benefits."

As in Northwest's case, companies may also try to obtain a DOL exemption that permits them to contribute prohibited transactions (illiquid, nontradable assets). For instance, U.S. Steel was permitted to contribute timber rights to its pension plans in 2003. However, a sponsor that proposes using a cashless asset with no ready market would need to supply an appraisal of the asset's worth, as well as convince the DOL that the assets could not be liquidated and that the pension plan would undertake no undue risk by accepting those assets (Northwest gave its pension plan put options so that it could put the Pinnacle stock back to Northwest at a given price).

Freezing DB Plans a la Delta Provides Little Help for Funding Levels

Delta Air Lines' latest pilot deal, signed in November 2004, provided for a freeze of the pilots' defined benefit plans as of December 31, 2004, eliminating future service accruals; however, future wage increases will still get factored into pilots' final pension obligations. As a result of the partial freeze, Delta's DB liabilities should only grow due to salary inflation and interest accretion. Underscoring the uncertain future of airline DB benefits, on February 11, 2005, Northwest's pilot union leadership resolved to explore the possibility of freezing its plan to better protect its long-term viability. Momentum for plan freezes has seemingly picked up, as Continental disclosed that its recent tentative labor agreements contain some defined benefit plan freezes. While freezing a plan is most certainly more palatable for labor than termination, we believe that freezes do not go far enough to shore up cash flow needs and would still leave carriers that implement them at massive disadvantages to others that *do* terminate their plans.

UAL acknowledged in court filings (September 2004) that freezing its plans as of December 31, 2004 would only reduce its total cash outlay through 2008 by $875 million, leaving total cash contribution needs at $3.2 billion, a still-hefty sum that could certainly crimp liquidity. What's more, the estimated savings *exclude* the costs associated with any replacement plans that would most likely be established (north of $100 million per year). Recent history suggests some sort of company contributory defined contribution plan (some carriers' plans only match employees' contributions to a certain extent, while other plans contribute a specified amount of a person's salary). In addition, cash contribution needs are still driven by asset returns (the average return assumption was 8%-9%) and interest rates.

Furthermore, we examined carriers' PBO and ABO funding levels to get a sense of the potential funding level benefit should carriers freeze the salary inflation portion of their DB plans. For most of the carriers (see Exhibit 1), we found an average five-percentage-point improvement in 2004 funding levels (from 61% funded to 66% funded), which, in our view, underscores the limited improvement in funding levels (which determine cash funding needs) likely to be derived from the DB plan freeze in the near term.

Plan Terminations

While three types of plan terminations exist under current law (distress, involuntary, and standard), for all intents and purposes, only the former two are relevant to the airline industry.

First of all, a standard termination requires a plan sponsor (in this case, an airline) to fully fund its plans either through lump-sum payouts or the purchase of annuities sufficient to satisfy all of its liabilities. In light of the substantial funding deficits (totaling $14 billion at Alaska Air, AMR, Continental, Delta, and Northwest) and the likely high cost required to acquire annuities, this form of termination appears to be out of reach.

Second, involuntary terminations arise when the PBGC itself terminates a pension plan after it reaches a certain level of distress (inability to make current payments to retirees, etc.), which would be a dream come true for plan sponsors, though the sponsor (and its equity) would likely find itself in a terminal condition before the PBGC would step in (e.g., PBGC taking over pension plans for United's pilots and ground workers). Distressed terminations, on the other hand, require carriers to demonstrate to the PBGC their inability to continue operations without abrogating their pension plans (to pass the distress test, a bankrupt sponsor may try to prove that "unless the plan is terminated [the plan sponsor], will be unable to pay all its debts pursuant to a plan of reorganization and will be unable to continue in business outside the chapter 11 reorganization process.").

In addition, since airline pension plans are part and parcel of collective bargaining agreements, union consent is needed unless a bankruptcy judge nullifies the contract, all of which suggests that a distress termination outside of Chapter 11 is highly unlikely.

Retiree Health Care — A Growing Problem

ANOTHER DRAIN ON THE CARRIERS' COFFERS

While smaller in size than defined benefit pension obligations, another percolating benefit cost/liability problem for legacy airlines is retiree health care obligations. We estimate aggregate retiree health care obligations will be $726 million this year. While ERISA requires that pension plans meet established funding levels, retiree health care plans lack any similar funding requirement. For that reason, most carriers also have substantial unfunded accumulated post-retirement benefit obligations.

For example, 4% was the highest funding level among the legacy carriers with retiree health care (OPEB) obligations shown below at year-end 2004. As a result, retiree funding needs are met almost entirely from the corporate balance sheet and operating cash flow (as opposed to plan assets set aside, as in the case of pension plans). In addition, health care costs have been growing at a steady clip (up 8% in 2004) and are expected to rise an additional 6.6% this year, according to the bellwether Mercer survey. Some carriers began limiting their OPEB exposure several years ago by capping annual benefits. Nevertheless, the obligations loom large.

Based on the latest data available, AMR, Delta, and UAL each anticipated $190-$235 million in annual retiree health care funding needs through 2008. Given the meaningful sums of cash that these benefits divert from a carrier's coffers and the moves at UAL and US Airways in bankruptcy to streamline these expenses, we suspect that the other carriers will need to address these issues in the short to medium term.

Without ERISA funding guidelines, this is a pay-as-you-go scheme that could run into trouble as companies shrink and retirees' population rise. In addition to the carriers shown below, both Alaska and Frontier offer OPEB, although future payment forecasts are unavailable at this time (for historical information, see Exhibit 1). Further, Continental Airlines disclosed that its recent tentative labor agreements provide for some medical benefits to "eligible retirees" until they are eligible for Medicare, an apparent departure of past practice, wherein, unlike its legacy peers, the carrier did not offer retiree medical benefits (though this likely made the DB freeze more palatable for labor). As a result of offering retiree medical coverage, Continental expects to record $25 million in expenses in 2005 related to this plan.

Exhibit 17. Retiree Health Care (OPEB) Funding Liabilities and Plan Payout Forecast

	AMR	Delta	Northwest	US Airways	UAL	LUV
	Postretirement Benefit Payments from Plan Assets and Current Assets					
2005	$193	$188	$45	$63	$225	$2
2006	$187	$189	$48	$66	$235	$3
2007	$195	$191	$52	$71	$230	$5
2008	$201	$171	$55	$75	$235	$7
2009	$208	$163	$60	$74	$235	$9
2010 to 2014	$1,119	$669	$360	$421	$1,152	$78
Total - 2014	**$2,103**	**$1,571**	**$620**	**$770**	**$2,312**	**$104**
2004 APBO Unfunded Liability ($ mns)	($3,152)	($1,835)	($921)	($1,369)	($3,069)	($80)
2004 APBO Funded Status (%)	**4%**	**0%**	**1%**	**0%**	**4%**	**0%**
2004 P&L Expense	$264	$76	$98	$105	$364	$18
2004 P&L Expense per Share	**$1.05**	**$0.38**	**$0.73**	**$1.23**	**$2.05**	**$0.01**
2004 OPEB CASM	**0.14¢**	**0.05¢**	**0.11¢**	**0.19¢**	**0.25¢**	**0.02¢**
2005E Payment as % of 4Q Cash Balance	**7%**	**10%**	**2%**	**NA**	**NA**	**0%**
2005E Payment as % of '05 Op. Cash Flow	**18%**	**41%**	**14%**	**NA**	**NA**	**0%**
2005E Payment as % of '05 Pension Contribution	**62%**	**68%**	**11%**	**NA**	**NA**	**NA**

Note: UAL's information is as of 2003. In addition, the payment schedule is through 2004-08 and 2009-13.
OPEB includes post-employment health care benefits: medical, dental, vision, hearing, and other health-related benefits whether provided separately or through the pension plan; other benefits: life insurance, disability, long-term care, etc., when provided separately from a defined benefit pension plan. APBO = accumulated postretirement benefit obligation. Assumes 36% tax rate for 2004 expense per share.

Source: Bear, Stearns & Co. Inc.; company filings.

How Do the Airlines Stack Up?

WE FIND MEANINGFUL DIFFERENCES BETWEEN PENSION AND OPEB COSTS

Last year, all the carriers in our coverage satisfied their required pension contributions. Nevertheless, the latest company guidance suggests hefty sums will be required in 2005, with Northwest leading the pack with $420 million in contributions. AMR, Delta, and Continental are not far behind with $310 million, $275 million, and $192 million (helped by a $65 million contribution in stock in January 2005 and its tentative labor agreements), respectively, in projected pension funding requirements in 2005, while Alaska should contribute close to $60 million.

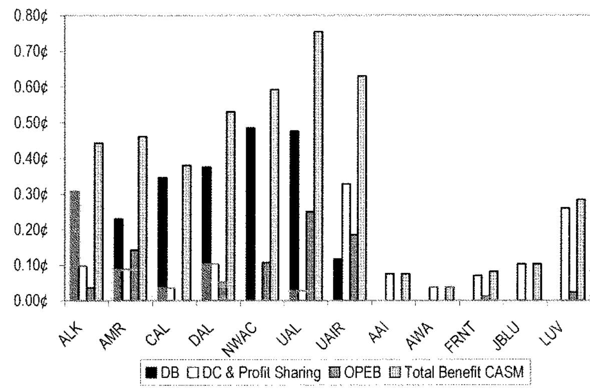
We believe that these contribution requirements should be considered in light of operating cash flow and other potential cash uses, such as debt maturities and unfinanced capital expenditures. Viewed in this way, we see that pension cash contributions will eat up a substantial portion of operating cash flow in 2005 (an aggregate 50%) and also represent a meaningful percentage of most carriers' unrestricted cash balances, 13% in total.

Based on our current 2005 estimates, Alaska appears to have the lowest pension cash contribution-to-operating-cash-flow ratio (19%) as well as the best pension cash-to-unrestricted cash balance ratio (7%). Northwest Airlines, on the other hand, has both the highest pension cash contribution-to-operating cash flow ratio (126%) and a pension contribution-to-cash balance ratio of 17%. Overall, we expect airlines to have an average $1.79 per share cash drag in 2005 due to DB pensions, representing 50% of their estimated 2005 operating cash flow and 5%-45% of their recent share prices. As we detail below, it could get much worse in 2006.

Pension, 401(k), Profit Sharing, and Retiree Health Approach $0.01 of CASM at Some Carriers

In the exhibit below, we depict the components of non-salary labor unit costs. For some airlines, these non-wage benefits amount to close to $0.01 of cost per available seat mile (CASM). Nevertheless, we also note that for LCCs such as Southwest and JetBlue, which utilize defined contribution and profit-sharing schemes, their respective non-salary labor CASM approximates the legacies' DB CASM. Put another way, replacing DB plans with healthy DC and profit-sharing programs may not be the answer to the near-term cash crunch, though the longer-term benefits are less disputable.

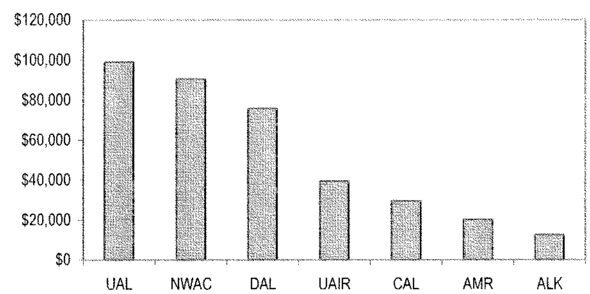
Exhibit 18. 2004 Pension, Profit-Sharing, and Retiree CASM (as reported)



Note: UAL is as of 2003.

Source: Bear, Stearns & Co. Inc. estimates.

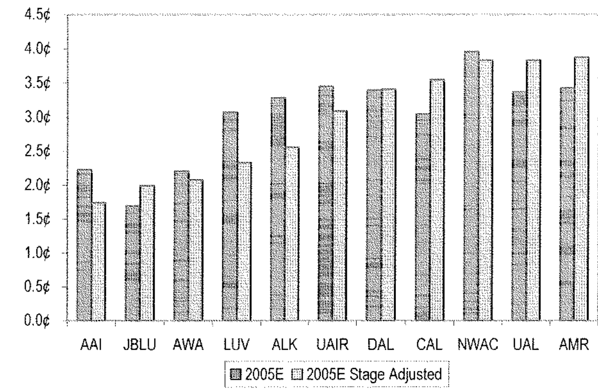
Exhibit 19. 2004 Unfunded ABO per Employee



Note: UAIR's defined benefit plans were terminated effective February 1, 2005 and UAL is attempting to do the same. UAL is calculated using 2003 ABOs and 2004 FTEs.

Source: Bear, Stearns & Co. Inc. estimates; company reports.

Exhibit 20. 2005E Labor CASM



Note: Stage-adjusted to 1,000 miles. UAIR and UAL are Not Rated. Using third-quarter 2004 stage as per Form 41 data

Source: Bear, Stearns & Co. Inc. estimates.

In 2005, given expiring pension legislation (plan years beginning after December 28, 2005 would revert to prior pension law), we expect Congress to attempt to replace current discount rate guidelines. In addition, airline labor leaders have recently espoused a mechanism whereby airlines could spread out their deficit reduction contributions over many years. Further, with UAL working to terminate its DB pension plans and US Airways having successfully ditched its own, those carriers not operating under the auspices of Chapter 11 (22), could find themselves at a substantial disadvantage, particularly given the significant hurdles required for terminating a plan outside of bankruptcy: 1) meeting PBGC's "financial distress" test, and 2) obtaining labor union consent to the changes.

Exhibit 21. Pension Cash Contribution Estimates ($ in millions)

	Required Pension Cash Contributions				
	ALK	**AMR**	**CAL**	**DAL**	**NWAC**
2004	$49	$467	$0	$455	$253
2005E	$58	$310	$192	$275	$420
2005E Pension Cash as % of Op. Cash Flow	19%	28%	63%	61%	126%
2006E Plan Freezes and 20-Yr Amort.	$4	$45	$44	$202	$133
2006E Bush Proposal (7-Yr Amort.)	$71	$314	$288	$726	$704
2006E PFEA Expires and 5-Yr Amort.	$76	$377	$356	$962	$901
2006E Plan Freezes and 20-Yr Amort. as % of Op. Cash Flow	1%	2%	6%	13%	11%
2006E Bush Proposal (7-Yr Amort.) as % of Op. Cash Flow	21%	16%	36%	47%	58%
2006E PFEA Expires and 5-Yr Amort. as % of Op. Cash Flow	23%	19%	45%	62%	74%

Note: 2004 and 2005 from company guidance and Bear Stearns estimates. 2006 hypothetical figures from Bear Stearns. Calculation methodology: Uses 2004 ABO funding level for ALK, AMR, CAL, DAL, and NWAC; 2006 DRC amortization is arrived at by assuming funding needed to achieve 90% ABO funding level (analogous to ERISA's current liability measure): 1) begin 2006 with 2005 estimated contribution amount, and haircut by 50% to arrive at non-DRC assumed contribution for 2006; 2) add estimated DRC amortizations deferred from 2004 and 2005 (2003 as well if any); and 3) add 2006 DRC amortization estimate. NWAC includes amortization from 2003 waived amount of $454 million. CAL has reached tentative labor agreements, which, if ratified, could freeze its DB plans and significantly lower pension funding requirements.

Source: Bear, Stearns & Co. Inc. estimates.

Company Pension Profiles

ALASKA AIR GROUP

Exhibit 22. Alaska Air's Pension Summary
($ in millions, except CASM data)

2004 PBO Funding Status	67%
2004 PBO Underfunding	($303)
2004 Defined Benefit Pension Expense	$78
2004 Defined Contribution + Profit-Sharing Expense	$25
2004 Retirement Health Care Expense (OPEB)	$9
2004 DB, DC, OPEB CASM	0.44¢
2005E DB Pension Cash Contributions	$58
2005E Operating Cash Flow (oil avg. $46/bbl)	$302
2004 Unrestricted Cash Balance	$874
2006E DB Pension Cash Contributions Base Case	$71
2006E Operating Cash Flow (oil avg $40/bbl)	$332

Source: Bear, Stearns & Co. Inc. estimates; company reports.

We believe Alaska Air Group has the least pension risk among our legacy carrier coverage universe. Our estimates suggest that Alaska Air's pension is underfunded by $300 million, or 33% on a PBO basis (21% on an ABO basis), better than the 41% average among the legacies; also, the $58 million in required cash contributions as a percentage of operating cash flow is 19%, well below the 50% group aggregate. Further, our estimated required contributions over the next two years are just 15% of the carrier's fourth-quarter 2004 unrestricted cash balance, versus the 34% group average.

For example, 2005 cash contributions are only expected to rise 18%, to $58 million, versus 66% at Northwest. In addition, the smaller carrier has lower absolute pension liabilities (liabilities are one-tenth the size of AMR's) and cash pension contributions are likely to be less meaningful for Alaska Air than the rest of the bunch. For instance, Alaska Air's 2005 cash contributions amount to just 7% of its fourth-quarter 2004 unrestricted cash balance, roughly one half of the other carriers' 13% average. Looked at as a percentage of 2005 estimated operating cash flow, Alaska Air's cash funding needs are half those of its nearest competitor.

Our sense is that given Alaska Air's relatively superior funding levels, stronger balance sheet (71% net debt to total invested capital versus the 114% average at the four nonbankrupt legacy airlines), and less burdensome near-term cash funding needs, the carrier is less likely to freeze its plans despite being in contract negotiations with the majority of its labor groups. While we estimate that Alaska Air enjoys a 28% labor CASM advantage to the network carriers, plan terminations at other carriers would reduce its current advantage to 19% for 2005 on a stage-adjusted basis.

Exhibit 23. AMR's Pension Summary
($ in millions, except CASM data)

2004 PBO Funding Status	73%
2004 PBO Underfunding	($2,687)
2004 Defined Benefit Pension Expense	$427
2004 Defined Contribution + Profit-Sharing Expense	$163
2004 Retirement Health Care Expense (OPEB)	$264
2004 DB, DC, OPEB CASM	0.46¢
2005E DB Pension Cash Contributions	$310
2005E Operating Cash Flow (oil avg. $46/bbl)	$1,089
2004 Unrestricted Cash Balance	$2,929
2006E DB Pension Cash Contributions Base Case	$314
2006E Operating Cash Flow (oil avg $40/bbl)	$1,982

Source: Bear, Stearns & Co. Inc. estimates; company reports.

We rank AMR's pension risk behind Alaska's, but ahead of Northwest's, Delta's, and Continental's. We estimate that AMR's pension is underfunded by $2.7 billion, or 27% on an PBO basis (20% on an ABO basis), better than the 41% average among the legacies; also, the $310 million in required cash contributions as a percentage of operating cash flow is 28%, below the 50% group aggregate. Further, our estimated required contributions over the next two years are 21% of the carrier's fourth-quarter 2004 unrestricted cash balance, versus the 34% group average.

AMR will likely contribute $310 million (absent legislative relief in 2005, the sum would have been much greater) in cash to its pensions in 2005, 11% of the company's unrestricted cash level, according to its December 31 balance sheet. This sizable cash outlay equates to roughly 28% (better than the group aggregate of 50%) of our 2005 operating cash flow estimate, equivalent to $1.24 in cash per share.

With its credit facility recently renegotiated, AMR should be able to easily meet 2005's cash obligations. In fact, AMR made a first installment in January 2005 of $42 million. However, looking to 2006, assuming no new pension legislation, we forecast cash contributions will rise 22%, to $377 million, or 19% of our operating cash flow estimate (our 2006 cash flow estimate assumes $40/bbl oil). To relieve this burden, AMR could seek IRS waivers should Congress fail to produce additional laws that benefit airlines with DB plans.

In addition, we expect AMR to seriously consider selling its investment arm, which it attempted to do in 2003, but pulled it off the market when bids failed to meet expectations. As a reference to that unit's potential value, we looked at M&A activity in the asset management industry over the past couple of years and concluded that its current assets under management imply a value of $400-$750 million for the money manager depending on the amount of assets ultimately transferred and relative performance (assumes price to assets under management of 2%-3% and total assets sold of $20-$25 billion).

Exhibit 24. Hypothetical Values for Asset Management Firms

		Assets Under Management (AUM) (US$ in billions)			
		$15	$20	$25	$30
		Implied Value of Asset Management Unit (US$ in millions)			
Price to AUM Ratio	1.5%	$225	$300	$375	$450
	2.0%	$300	$400	$500	$600
	2.5%	$375	$500	$625	$750
	3.0%	$450	$600	$750	$900
	3.5%	$525	$700	$875	$1,050
	4.0%	$600	$800	$1,000	$1,200

American Beacon Advisors directly managed or served as fiduciary or financial advisor for $37.6 billion in assets at 1/31/05, consisting of $17.3 billion under active management and $20.3 billion as named fiduciary or financial adviser.

Source: Bear, Stearns & Co. Inc. estimates.

In addition, AMR might be tempted to spin off part of its regional subsidiaries, just as Continental and Northwest did in 2002 and 2003. Given the right market conditions, that could conceivably raise $500 million to $1 billion, depending on the carrier's profit margin. (See the table below for potential margins and multiples.)

Exhibit 25. Regional Units Could Potentially Help Fund Pension Plans

Parent (former)	CAL XJT	NWAC PNCL	**AMR** **Eagle + Exec.**	SKYW	**DAL** **ASA + Comair**	**Mean**
ASMs (billions)	4.77	2.22	4.54	1.70	8.59	
Revenue (millions)	$1,461	$581	$1,820	$1,067	$2,117	
EBT Margin Actual **(Assumed)**	13%	11%	**6%**	12%	**6%**	**12%**
P/E Actual **(Assumed)**	6.6x	4.2x	**7.1x**	10.4x	**7.1x**	**7.1x**
Actual **(Implied)** Market Cap.	$604	$223	**$496**	$1,012	**$577**	
Assuming 12% EBT Margin			**$988**		**$1,149**	
10% of 2003 DB Plan Assets = Potential Contribution Ceiling			**$734**		**$684**	

Note: Second-half 2004 Scheduled ASMs from OAG via BACK Aviation; Revenue = 12 months ended 9/30/04. Comair and ASA revenues 12 months ended 6/30/04 using OD1A data. Market capitalization for XJT, PNCL, and SKYW as of 3/10/05. As reference, NWAC contributed $350 million (roughly 7% of total GAAP plan assets at 12/03) worth of privately held Pinnacle shares to its defined benefit plans in 2003. CAL contributed $100 million of XJT to its DB plans (approximately 8% of GAAP plan assets at 12/03), which was freely tradable. DAL paid over $2 billion for Comair and ASA according to media reports. Assumes 36% tax rate for wholly owned subsidiary implied market value calculations.

Source: Bear, Stearns & Co. Inc. estimates; company reports.

Exhibit 26. Continental's Pension Summary
($ in millions, except CASM data)

2004 PBO Funding Status	45%
2004 PBO Underfunding	($1,582)
2004 Defined Benefit Pension Expense	$293
2004 Defined Contribution + Profit-Sharing Expense	$30
2004 Retirement Health Care Expense (OPEB)	NA
2004 DB, DC, OPEB CASM	0.38¢
2005E Required DB Pension Contributions	$307
2005E DB Pension Cash Contributions	$192
2005E Operating Cash Flow (oil avg. $46/bbl)	$307
2004 Unrestricted Cash Balance	$1,460
2006E DB Pension Cash Contributions Base Case	$288
2006E Operating Cash Flow (oil avg $40/bbl)	$798

Note: 2005 pension contributions exclude $65 million in stock and assume $50 million in savings from labor deals.
Source: Bear, Stearns & Co. Inc. estimates; company reports.

We believe Continental's pension risk is higher than Alaska Air's and AMR's, but lower than both Northwest's and Delta's. We estimate that Continental's pension is underfunded by $1.6 billion, or 55% on a PBO basis (47% on an ABO basis), worse than the 41% average among the legacies; also, the $192 million in required cash contributions as a percentage of operating cash flow is 63%, a touch above the group aggregate of 50%. Further, our estimated required contributions over the next two years are 33% of the carrier's fourth-quarter 2004 unrestricted cash balance, in line with the group average.

Continental started out 2004 with the best-funded pension plan of the legacy carriers, on a current liability basis (cash purposes). Originally, Continental intended to contribute $300 million to maintain a 90% current liability status (a level that precludes DRC requirements). (Current liabilities are measured using ERISA/IRC formulas analogous to the GAAP ABO [Accumulated Benefit Obligation], which differs from the PBO [Projected Benefit Obligation], since it makes no assumption about future compensation levels, making it generally lower than the PBO.) However, bruising fuel prices and weak yields made liquidity preservation a top priority, and, in turn, Continental availed itself of the Pension Funding Equity Act (PFEA) of 2004, thereby eliminating its cash contribution in 2004.

The year 2005 looks more troublesome, though the carrier did use $65 million of ExpressJet equity as an initial contribution in January. Assuming Continental achieves its stated $50 million in pension contribution savings resulting from tentative labor agreements, we estimate cash contributions of $192 million, or $1.86 per share, representing 63% of our operating cash flow estimate, higher than 50% group aggregate. Nevertheless, as a percentage of its December 2004 unrestricted cash balance, 2005's pension requirements amount to a more manageable 13%, in line with the group's average. After January's ExpressJet contribution, based on ownership levels as of February 7, we estimate that Continental could potentially contribute another $65 million in ExpressJet shares (at which point we estimate plan assets would hit ERISA's 10% ownership cap permissible for pension plans) to its DB plans, further reducing cash outflow to roughly $127 million. (Continental has publicly stated its intention to unwind its ownership of XJT shares.)

DELTA AIR LINES

Exhibit 27. Delta's Pension Summary
($ in millions, except CASM data)

2004 PBO Funding Status	56%
2004 PBO Underfunding	($5,298)
2004 Defined Benefit Pension Expense	$549
2004 Defined Contribution + Profit-Sharing Expense	$150
2004 Retirement Health Care Expense (OPEB)	$76
2004 DB, DC, OPEB CASM	0.53¢
2005E DB Pension Cash Contributions	$275
2005E Operating Cash Flow (oil avg. $46/bbl)	$454
2004 Unrestricted Cash Balance	$1,799
2006E DB Pension Cash Contributions Base Case	$726
2006E Operating Cash Flow (oil avg $40/bbl)	$1,558

Source: Bear, Stearns & Co. Inc. estimates; company reports.

We believe Delta has one the highest pension risk profiles among the legacy carriers operating outside of Chapter 11. While its funding deficit is the worst in the industry, its contributions as a percentage of cash flow are slightly below Northwest's. We estimate that Delta's pension is underfunded by $5.3 billion, or 44% on a PBO basis (43% on an ABO basis), greater than the 41% average among the legacies; also, the $275 million in required cash contributions as a percentage of operating cash flow is 61%, a notch above the 50% group aggregate. Further, our estimated required contributions over the next two years are a sizable 56% of the carrier's fourth-quarter 2004 unrestricted cash balance, versus the 34% group average.

On November 11, 2004, Delta's pilots ratified a new labor agreement principally calling for a 32.5% wage cut combined with a partial freezing of its defined benefit plan and subsequent creation of a defined contribution replacement plan. While the contract permitted Delta to avoid a potential fourth-quarter 2004 bankruptcy filing, the carrier has only scratched the surface regarding its pension underfunding. Despite freezing its pilot DB plan, Delta will still need to contribute hundreds of millions of dollars per year as a result of the $4 billion plus funding gap. What's more, the latest collective bargaining agreement established a new defined contribution requiring company funds, which will likely offset some of the potential cash savings.

For 2005, we estimate defined benefit pension cash contributions of $275 million (nonqualified DB plans will add another $65 million, while defined contribution plans could total $110 million), which is roughly 60% of our projected operating cash flow in that year. Further, as a percentage of its fourth-quarter 2004 cash balance, Delta's 2005 pension needs sit at roughly 15%, in line with the group average.

In light of the still-substantial pension obligations, Delta continues to face a formidable challenge — meeting its legally mandated funding requirements. The company posted the largest absolute funding gap of the nonbankrupt carriers in 2004, with an ABO underfunding of $5.2 billion versus runner-up Northwest's $3.6 billion in already-accrued unfunded liabilities. That said, we expect the company to pursue any and all non-termination outlets available to mitigate its pension burden. For example, in mid-December 2004, CEO Gerald Grinstein indicated Delta would work with Congress to devise a mechanism that would stretch out pension funding payments. Similarly, CFO Michael Palumbo has drawn analogies to funding deferrals obtained at both TWA and PanAm. In addition, we would not be surprised if Delta looked to spin off part of its regional subsidiaries, Comair and ASA, which it paid $2 billion-plus for in the 1980s and 1990s. (For more on this topic, see the exhibit below.)

Exhibit 28. Regional Units Could Potentially Help Fund Pension Plans

Parent (former)	CAL XJT	NWAC PNCL	**AMR** **Eagle + Exec.**	 SKYW	DAL **ASA + Comair**	 **Mean**
ASMs (billions)	4.77	2.22	4.54	1.70	8.59	
Revenue (millions)	$1,461	$581	$1,820	$1,067	$2,117	
EBT Margin Actual **(Assumed)**	13%	11%	**6%**	12%	**6%**	**12%**
P/E Actual **(Assumed)**	6.6x	4.2x	**7.1x**	10.4x	**7.1x**	**7.1x**
Actual **(Implied)** Market Cap.	$604	$223	**$496**	$1,012	**$577**	
Assuming 12% EBT Margin			**$988**		**$1,149**	
10% of 2003 DB Plan Assets = Potential Contribution Ceiling			**$734**		**$684**	

Note: Second-half 2004 Scheduled ASMs from OAG via BACK Aviation; Revenue = 12 months ended 9/30/04. Comair and ASA revenues 12 months ended 6/30/04 using OD1A data. Market capitalization for XJT, PNCL, and SKYW as of 3/10/05. As reference, NWAC contributed $350 million (roughly 7% of total GAAP plan assets at 12/03) worth of privately held Pinnacle shares to its defined benefit plans in 2003. CAL contributed $100 million of XJT to its DB plans (approximately 8% of GAAP plan assets at 12/03), which was freely tradable. DAL paid over $2 billion for Comair and ASA according to media reports. Assumes 36% tax rate for wholly owned subsidiary implied market value calculations.

Source: Bear, Stearns & Co. Inc. estimates; company reports.

Northwest Airlines

Exhibit 29. Northwest's Pension Summary
($ in millions, except CASM data)

2004 PBO Funding Status	59%
2004 PBO Underfunding	($3,820)
2004 Defined Benefit Pension Expense	$444
2004 Defined Contribution + Profit-Sharing Expense	NA
2004 Retirement Health Care Expense (OPEB)	$98
2004 DB, DC, OPEB CASM	0.59¢
2005E DB Pension Cash Contributions	$420
2005E Operating Cash Flow (oil avg. $46/bbl)	$333
2004 Unrestricted Cash Balance	$2,459
2006E DB Pension Cash Contributions Base Case	$704
2006E Operating Cash Flow (oil avg $40/bbl)	$1,214

Source: Bear, Stearns & Co. Inc. estimates; company reports.

Northwest's cash contributions as a percentage of operating cash flow rank the highest among the legacy carriers. We estimate that Northwest's pension is underfunded by $3.8 billion, or 41% on a PBO basis (40% on an ABO basis), in line with the legacy average; also, the $420 million in required cash contributions as a percentage of operating cash flow is a whopping 126%, well above the 50% group aggregate. Further, our estimated required contributions over the next two years total

46% of the carrier's fourth-quarter 2004 unrestricted cash balance, versus the 34% group average.

In 2002-03, Northwest demonstrated to the markets its ability to tackle near-term pension requirements through cash, pension waivers, and noncash contributions. However, in doing so, the Minneapolis-based carrier expended several precious resources that may be difficult, if not impossible, to replicate this time around. In 2003, Northwest sought administrative relief and received permission to fund its pension plans with $223 million (for the 2002 plan year) in a subsidiary's stock and amortize 2003's payment of $454 million over five years. The Pension Funding Equity Act of 2004 reduced Northwest's 2004 cash contribution to $253 million. For 2005, the carrier expects pension needs to rise to $420 million, which amounts to 126% of our forecasted operating cash flow for the same year (more than double the group aggregate). However, as a percentage of fourth-quarter 2004's unrestricted cash balance, Northwest's pension cash requirements come in at 17%, only a touch north of the group average.

After successfully monetizing its regional subsidiary in 2003, Northwest is left with only an 11% stake, valued at roughly $25 million, hardly enough to make a meaningful dent in pension cash needs. Meeting 2005's pension needs should not present any extreme difficulties for the carrier, though turning to 2006, things may get uncomfortable should Congress allow the current legislation to expire without any replacement. The pilots union appears to understand the severity of the situation, as it recently agreed to discuss a possible DB freeze with the company in order to ensure the plan's sustainability. The pilots' freeze initiative could establish an important precedent for other unions that are in negotiations.

Aside from union concessions, the carrier still possesses two pension waivers (three remain for the pilots' plan) that it could apply for beginning in 2006 should Congress not act.

Notwithstanding the availability of additional pension waivers, we believe it could be more difficult to convince the IRS of the carrier's temporary financial hardship this time around (are the industry's current woes truly temporary?) as well as meet any additional collateral requirements that could be required. We note that in the first waiver application, Northwest was obligated to grant its pension plans liens on some domestic slots, international routes, aircraft, and engines, likely leaving less unencumbered assets for another round of waivers.

On a related front, Northwest received an informal request from the SEC regarding its pension plan accounting (GAAP) assumptions. Our initial take is that while it is a noncash issue, Northwest's asset allocation (74%-20% equities/fixed income versus 63%-29% average at other carriers) is likely behind the higher return expectation. Should Northwest move to reduce its expected rate of return assumption by 50 bps, all else equal, we estimate that it could negatively affect expenses by roughly $27 million, or $0.20 per share.

United Airlines and US Airways (Both Not Rated)

US Airways terminated its remaining defined benefit plans in January 2005 (in its first stint in bankruptcy, US Airways terminated its pilots' defined benefit pension plan). The much larger United appears to be in a more tenuous situation, as the PBGC preemptively moved in late December 2004 to terminate the pilots' plan, in hopes that relief from cockpit crew DB plans would allow the airline to maintain the remainder of its plans, something UAL vigorously opposes. United's pilots union agreed in its latest contract (ratified in January) not to fight its DB plan's termination, in return for a healthy DC plan and a $550 million convertible note to supplement the pension benefit losses. The large convertible note could pose a sticking point for other unions and potential exit financiers. However, punting the pilots' plan alone could save $1.3 billion (30% of total pension cash obligations due through 2008) in cash contributions. Subsequently, the PBGC also moved in mid-March to take over the UAL ground workers pension plan, which is estimated to require the greatest funding contributions of all of UAL's plans through 2008, at $1.4 billion. Relieved of the responsibility for its two costliest plans, UAL could find it tougher to convince a judge of the need to terminate the remaining plans.

UAL faces substantial pension contributions in the coming years. It continues to hemorrhage cash, similar to the other legacy airlines, and the difficulty in attracting exit financing has all but sealed the fate of its defined benefit plans, in our view. Through 2009, UAL estimated it would have to contribute more than $4 billion. Should UAL also succeed in terminating all of its defined benefit plans, while also reducing wage rates, and exit with low-cost carrier-like costs, the second-largest U.S. airline would pose a formidable challenge for fellow legacy and LCC carriers alike, in our opinion. In addition, any changes made to UAL's pension plans are likely to ripple through the industry given the carrier's size, spurring modifications at other airlines.

Exhibit 30. There Appears to Be No Way Around Huge Cash Drain Except Termination

UAL Minimum DB Funding Contributions (US$ in millions)[1]	No Waiver	Waiver
2005E	$1,200	$200
2006E	$1,000	$400
2007E	$1,500	$1,000
2008E	$600	$1,400
2009E	$100	$1,200
2010E	$0	$500
Total	**$4,400**	**$4,800**

US Airways Minimum DB Funding Contributions (US$ in millions)[2]	No Waiver	Freeze & Waiver
2005E		$32
2006E		$59
2007E		$177
2008E		$213
2009E		$248
Total	**$987**	**$728**

(1) Company reports dated 12/15/04; due to rounding, breakdown as shown in millions does not foot with company-disclosed total of $4.8 billion.

(2) Court fillings 12/13/04; assumes IAM/AFA plan freezes 1/1/05 and waivers from 2004-06 as well as waivers for the CE plan from 2007-09.

Source: Bear, Stearns & Co. Inc. estimates; company reports.

Pensions 101

A QUICK OVERVIEW

As plan assets fall at the airlines, pension obligations become an issue, particularly for those carriers with "defined benefit" plans, which differ from 401k plans because the DB sponsor bears all the investment risk by guaranteeing a retirement amount. Carriers with defined benefit plans include Alaska Air Group, American Airlines, Continental, Delta, Northwest, United, and US Airways. Southwest, JetBlue, AirTran, Frontier, and America West do not offer defined benefit plans, though they do provide defined contribution plans partially funded by the carriers themselves.

On top of regular maintenance contributions, federal pension law requires companies to contribute additional assets unless the pension plan's funded status is at least 90% or the funded liability is currently at least 80% and was at least 90% in two consecutive years out of the past three. However, DRC funding rules are such that companies often have limited amounts of time to make up the shortfall and, under some circumstances, may contribute limited amounts of stock rather than cash. (In 2003, and again in January 2005, Northwest and Continental used stock to fund portions of their pension plans, and we expect AMR, Continental, and Delta to consider future cash funding alternatives.)

Over on the P&L, pension accounting permits the use of smoothing mechanisms that spread out recognition of income and expenses. Accordingly, it reduces the volatility of pension earnings (costs). What's more, the income or expense items in a given year are largely determined by the previous year's assumptions and plan realizations. For the most part, this suggests that companies have substantial visibility with regard to their current-year pension expense (and contributions) and to a lesser extent for the following year. Of course, the variability of key inputs, such as the discount rate, in pension forecasting makes longer-term estimates much less reliable. In addition, the legislative uncertainty only adds to the uncertainty of contribution forecasts beyond this year.

In terms of the balance sheet, if a plan's Accumulated Benefit Obligation (ABO) exceeds plan assets, then, at a minimum, the company must record the unfunded amount on its balance sheet.

Another important factor in pension calculations is the mortality rates mandated by federal law. Pension plans currently use the 1983 Group Annuity Mortality Table, which some argue fails to accurately reflect current longevity norms. The Secretary of the Treasury is empowered to update mortality figures based on projected trends and DB plans' actuarial experience. As a result, the Department of Treasury and the IRS are reviewing the mortality tables, which could lead to longer benefit stream assumptions.

In summary, defined benefit plans affect earnings through net pension costs (found in labor expenses at airlines), cash flows due to required cash contributions, and balance sheet equity due to any minimum pension liability charges (excess of accumulated benefit obligations over the fair value of plan assets). Conversely, pension accounting can provide a boost to earnings, as occurred in the late 1990s, when assets outperformed return expectations.

ERISA: Background

There are three federal entities that administer and enforce ERISA for corporate pension plans: the Department of Labor (DOL), the Internal Revenue Service (IRS), and the Pension Benefit Guaranty Corporation (PBGC). The DOL's Employee Benefits Security Administration has the authority to allow exemptions to certain ERISA rules, such as contributions of in-kind securities to a DB plan. For its part, the IRS has the authority to grant waivers deferring current contribution requirements to the following year. The PBGC was created by ERISA to insure continuity of defined benefit plans and the orderly payment of benefits. Often this entails the PBGC taking over a failed DB plan. For example, as part of US Airways' two bankruptcies, the PBGC agreed to assume responsibility for all of its DB plans and ensure that retirees receive benefits. For this insurance, plan sponsors pay premiums to the PBGC, which increase with the size of their funding gap.

We note that pension payments are required on a quarterly basis. Each quarterly payment must be 25% of the annual amount, and it is due within 8.5 months of the plan's year-end. These payments are due on the fifteenth day of the fourth, seventh, tenth, and thirteenth month from the beginning of the plan year. Thus, a December year-end company would make its quarterly payments on April 15, July 15, October 15, and January 15, one month after the plan's year-end.

Appendix: Cash Burn and Oil Sensitivity

BEAR STEARNS

Exhibit 31. Cash Burn with No Debt Refinancing

With NO Debt Refinancing
As of 3/11/05

Cash Flow/Burn 2005E (US$ millions)	AMR[2]	CAL	DAL[3]	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT[4]
2005E Operating Cash Flow[1]										
Operating CF (after-tax) $30/bbl	$2,004	$686	$1,191	$889	$182	$897	$61	$375	$114	$16
Operating CF (after-tax) $35/bbl	$1,699	$560	$945	$704	$166	$886	$46	$351	$72	$9
Operating CF (after-tax) $40/bbl	$1,394	$433	$699	$518	$151	$875	$32	$327	$30	$1
Operating CF (after-tax) $45/bbl (Base Case)	$1,089	$307	$454	$333	$135	$864	$19	$302	($12)	($6)
Operating CF (after-tax) $50/bbl	$784	$181	$208	$147	$120	$853	$6	$278	($54)	($13)
Operating CF (after-tax) $55/bbl	$479	$55	($38)	($38)	$104	$842	($7)	$254	($96)	($21)
Cash Obligations										
Net Capex	$517	$170	$500	$200	$100	$380	$73	$170	$45	$35
DB Pension Contributions[5]	$310	$192	$275	$420	NA	NA	NA	$58	NA	NA
Cash From Financings	$0	$0	($250)	($107)	$0	($296)	$0	$0	($20)	$0
Debt Maturities	$910	$688	$630	$749	$105	$146	$14	$54	$102	$17
Liquidity										
Unrestricted Cash Balance at Calendar 4Q04	$2,929	$1,460	$1,799	$2,459	$449	$1,305	$334	$874	$306	$149
Unrestricted Cash Balance at Calendar 3Q04	$3,135	$1,539	$1,446	$2,541	$517	$1,876	$339	$879	$417	$160
2005E Cash Flow (Burn) Oil @ $30/bbl	**$267**	**($364)**	**$36**	**($373)**	**($24)**	**$668**	**($25)**	**$94**	**($12)**	**($36)**
Cash Flow (Burn) per Day $30/bbl	$0.7	($1.0)	$0.1	($1.0)	($0.1)	$1.8	($0.1)	$0.3	($0.0)	($0.1)
2005E End of Year Unrestricted Cash $30/bbl	$3,196	$1,096	$1,835	$2,086	$425	$1,973	$309	$968	$294	$113
Months of Cash Left with Oil at $30/bbl from YE 2004 to Threshold	CF Pos.	12+	CF Pos.	12+	12+	CF Pos.	12+	CF Pos.	12+	12+
2005E Cash Flow (Burn) Oil @ $35/bbl	**($38)**	**($490)**	**($210)**	**($559)**	**($39)**	**$656**	**($40)**	**$70**	**($54)**	**($43)**
Cash Flow (Burn) per Day $35/bbl	($0.1)	($1.3)	($0.6)	($1.5)	($0.1)	$1.8	($0.1)	$0.2	($0.1)	($0.1)
2005E End of Year Unrestricted Cash $35/bbl	$2,891	$970	$1,589	$1,900	$410	$1,961	$294	$943	$251	$106
Months of Cash Left with Oil at $35/bbl from YE 2004 to Threshold	12+	11	12+	12+	12+	CF Pos.	12+	CF Pos.	12+	12+
2005E Cash Flow (Burn) Oil @ $40/bbl	**($343)**	**($617)**	**($456)**	**($744)**	**($55)**	**$645**	**($54)**	**$45**	**($97)**	**($51)**
Cash Flow (Burn) per Day $40/bbl	($0.9)	($1.7)	($1.2)	($2.0)	($0.1)	$1.8	($0.1)	$0.1	($0.3)	($0.1)
2005E End of Year Unrestricted Cash $40/bbl	$2,586	$843	$1,343	$1,715	$395	$1,950	$280	$919	$209	$98
Months of Cash Left with Oil at $40/bbl from YE 2004 to Threshold	12+	9	8	12+	12+	CF Pos.	12+	CF Pos.	12+	12+
2005E Cash Flow (Burn) Oil @ $45/bbl (Base Case)	**($648)**	**($743)**	**($701)**	**($930)**	**($70)**	**$634**	**($68)**	**$21**	**($139)**	**($58)**
Cash Flow (Burn) per Day $45/bbl	**($1.8)**	**($2.0)**	**($1.9)**	**($2.5)**	**($0.2)**	**$1.7**	**($0.2)**	**$0.1**	**($0.4)**	**($0.2)**
2005E End of Year Unrestricted Cash $45/bbl	**$2,281**	**$717**	**$1,098**	**$1,529**	**$379**	**$1,939**	**$266**	**$895**	**$167**	**$91**
Months of Cash Left with Oil at $45/bbl from YE '04 to Threshold	**12+**	**7**	**5**	**12+**	**12+**	**CF Pos.**	**12+**	**CF Pos.**	**9**	**12+**
2005E Cash Flow (Burn) Oil @ $50/bbl	**($953)**	**($869)**	**($947)**	**($1,115)**	**($86)**	**$623**	**($81)**	**($3)**	**($181)**	**($65)**
Cash Flow (Burn) per Day $50/bbl	($2.6)	($2.4)	($2.6)	($3.1)	($0.2)	$1.7	($0.2)	($0.0)	($0.5)	($0.2)
2005E End of Year Unrestricted Cash $50/bbl	$1,976	$591	$852	$1,344	$364	$1,928	$254	$871	$125	$84
Months of Cash Left with Oil at $50/bbl from YE 2004 to Threshold	12+	6	4	12+	12+	CF Pos.	12+	12+	7	12+
2005E Cash Flow (Burn) Oil @ $55/bbl	**($1,258)**	**($995)**	**($1,193)**	**($1,301)**	**($101)**	**$612**	**($93)**	**($27)**	**($223)**	**($73)**
Cash Flow (Burn) per Day $55/bbl	($3.4)	($2.7)	($3.3)	($3.6)	($0.3)	$1.7	($0.3)	($0.1)	($0.6)	($0.2)
2005E End of Year Unrestricted Cash $55/bbl	$1,671	$465	$606	$1,158	$348	$1,917	$241	$847	$83	$76
Months of Cash Left with Oil at $55/bbl from YE 2004 to Threshold	12+	6	3	12+	12+	CF Pos.	12+	12+	6	12+

(1) Operating Cash Flow = Net Income + D&A + pension expense; assumes no impact from change in net working capital.
Assumes crude price of $49/bbl in 1Q05 and $45/bbl in 2Q-4Q05. Incorporates hedge positions.
(2) Assumes AMR has to repurchase $104 million facilities bond due in 4Q05.
(3) Assumes drawdown on $250 million of available Amex prepayment.
(4) FRNT is in 2006 March-ending fiscal year, base assumption oil at $43.75/bbl for FY2006.
(5) Assumes no additional noncash (stock of subsidiary) contribution to DB pension plans.

(US$ in millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT
Estimated Unrestricted Cash Concern Level	**$1,500**	**$1,000**	**$1,500**	**$1,100**	**$150**	**$750**	**$100**	**$300**	**$200**	**$75**

As points of reference, we note that AMR achieved its last-minute deal with labor last April with $1.2 billion (7% of LTM sales) in unrestricted cash and equivalents, UAL filed for Chapter 11 on 12/9/02 with $1.3 billion (9% of LTM sales) in unrestricted cash and equivalents (YE 2002), and US Air entered Chapter 11 on 8/11/02 with close to $900 million in cash (3Q02 balance was $900 million) (13% of LTM sales).

Source: Bear, Stearns & Co. Inc. estimates; company reports; company guidance.

Exhibit 32. Cash Burn Assuming 80% Debt Refinancing

With Debt Refinancing of 80% of Maturing Amount
As of 3/11/05

Cash Flow/Burn 2005E (US$ millions)	AMR(2)	CAL	DAL(3)	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT(4)
2005E Operating Cash Flow(1)										
Operating CF (after-tax) $30/bbl	$2,004	$686	$1,191	$889	$182	$897	$61	$375	$114	$16
Operating CF (after-tax) $35/bbl	$1,699	$560	$945	$704	$166	$886	$46	$351	$72	$9
Operating CF (after-tax) $40/bbl	$1,394	$433	$699	$518	$151	$875	$32	$327	$30	$1
Operating CF (after-tax) $45/bbl (Base Case)	$1,089	$307	$454	$333	$135	$864	$19	$302	($12)	($6)
Operating CF (after-tax) $50/bbl	$784	$181	$208	$147	$120	$853	$6	$278	($54)	($13)
Operating CF (after-tax) $55/bbl	$479	$55	($38)	($38)	$104	$842	($7)	$254	($96)	($21)
Cash Obligations										
Net Capex	$517	$170	$500	$200	$100	$380	$73	$170	$45	$35
DB Pension Contributions(5)	$310	$192	$275	$420	NA	NA	NA	$58	NA	NA
Cash From Financings	$0	$0	($250)	($107)	$0	($296)	$0	$0	($20)	$0
Debt Maturities	$182	$138	$126	$150	$21	$29	$3	$11	$20	$3
Liquidity										
Unrestricted Cash Balance at Calendar 4Q04	$2,929	$1,460	$1,799	$2,459	$449	$1,305	$334	$874	$306	$149
Unrestricted Cash Balance at Calendar 3Q04	$3,135	$1,539	$1,446	$2,541	$517	$1,876	$339	$879	$417	$160
2005E Cash Flow (Burn) Oil @ $30/bbl	**$995**	**$186**	**$540**	**$226**	**$61**	**$784**	**($14)**	**$136**	**$69**	**($22)**
Cash Flow (Burn) per Day $30/bbl	$2.7	$0.5	$1.5	$0.6	$0.2	$2.1	($0.0)	$0.4	$0.2	($0.1)
2005E End of Year Unrestricted Cash $30/bbl	$3,924	$1,646	$2,339	$2,685	$510	$2,089	$320	$1,010	$375	$127
Months of Cash Left with Oil at $30/bbl from YE 2004 to Threshold	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	12+	CF Pos.	CF Pos.	12+
2005E Cash Flow (Burn) Oil @ $35/bbl	**$690**	**$60**	**$294**	**$41**	**$45**	**$773**	**($29)**	**$112**	**$27**	**($30)**
Cash Flow (Burn) per Day $35/bbl	$1.9	$0.2	$0.8	$0.1	$0.1	$2.1	($0.1)	$0.3	$0.1	($0.1)
2005E End of Year Unrestricted Cash $35/bbl	$3,619	$1,520	$2,093	$2,500	$494	$2,078	$305	$986	$333	$119
Months of Cash Left with Oil at $35/bbl from YE 2004 to Threshold	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	12+	CF Pos.	CF Pos.	12+
2005E Cash Flow (Burn) Oil @ $40/bbl	**$385**	**($66)**	**$48**	**($145)**	**$30**	**$762**	**($43)**	**$88**	**($15)**	**($37)**
Cash Flow (Burn) per Day $40/bbl	$1.1	($0.2)	$0.1	($0.4)	$0.1	$2.1	($0.1)	$0.2	($0.0)	($0.1)
2005E End of Year Unrestricted Cash $40/bbl	$3,314	$1,394	$1,847	$2,314	$479	$2,067	$291	$962	$290	$112
Months of Cash Left with Oil at $40/bbl from YE 2004 to Threshold	CF Pos.	12+	CF Pos.	12+	CF Pos.	CF Pos.	12+	CF Pos.	12+	12+
2005E Cash Flow (Burn) Oil @ $45/bbl (Base Case)	**$80**	**($192)**	**($197)**	**($330)**	**$14**	**$751**	**($57)**	**$64**	**($57)**	**($44)**
Cash Flow (Burn) per Day $45/bbl	**$0.2**	**($0.5)**	**($0.5)**	**($0.9)**	**$0.0**	**$2.1**	**($0.2)**	**$0.2**	**($0.2)**	**($0.1)**
2005E End of Year Unrestricted Cash $45/bbl	**$3,009**	**$1,268**	**$1,602**	**$2,129**	**$463**	**$2,056**	**$278**	**$938**	**$248**	**$105**
Months of Cash Left with Oil at $45/bbl from YE '04 to Threshold	**CF Pos.**	**12+**	**12+**	**12+**	**CF Pos.**	**CF Pos.**	**12+**	**CF Pos.**	**12+**	**12+**
2005E Cash Flow (Burn) Oil @ $50/bbl	**($225)**	**($319)**	**($443)**	**($516)**	**($1)**	**$740**	**($69)**	**$40**	**($100)**	**($52)**
Cash Flow (Burn) per Day $50/bbl	($0.6)	($0.9)	($1.2)	($1.4)	($0.0)	$2.0	($0.2)	$0.1	($0.3)	($0.1)
2005E End of Year Unrestricted Cash $50/bbl	$2,704	$1,141	$1,356	$1,943	$448	$2,045	$265	$914	$206	$97
Months of Cash Left with Oil at $50/bbl from YE 2004 to Threshold	12+	12+	8	12+	12+	CF Pos.	12+	CF Pos.	12+	12+
2005E Cash Flow (Burn) Oil @ $55/bbl	**($530)**	**($445)**	**($689)**	**($702)**	**($17)**	**$729**	**($82)**	**$16**	**($142)**	**($59)**
Cash Flow (Burn) per Day $55/bbl	($1.5)	($1.2)	($1.9)	($1.9)	($0.0)	$2.0	($0.2)	$0.0	($0.4)	($0.2)
2005E End of Year Unrestricted Cash $55/bbl	$2,399	$1,015	$1,110	$1,757	$432	$2,034	$252	$890	$164	$90
Months of Cash Left with Oil at $55/bbl from YE 2004 to Threshold	12+	12+	5	12+	12+	CF Pos.	12+	CF Pos.	9	12+

(1) Operating Cash Flow = Net Income + D&A + pension expense; assumes no impact from change in net working capital.
Assumes crude price of $49/bbl in 1Q05 and $45/bbl in 2Q-4Q05. Incorporates hedge positions.
(2) Assumes AMR has to repurchase $104 million facilities bond due in 4Q05.
(3) Assumes drawdown on $250 million of available Amex prepayment.
(4) FRNT is in 2006 March-ending fiscal year, base assumption oil at $43.75/bbl for FY2006.
(5) Assumes no additional noncash (stock of subsidiary) contribution to DB pension plans.

(US$ in millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT
Estimated Unrestricted Cash Concern Level	**$1,500**	**$1,000**	**$1,500**	**$1,100**	**$150**	**$750**	**$100**	**$300**	**$200**	**$75**

As points of reference, we note that AMR achieved its last-minute deal with labor last April with $1.2 billion (7% of LTM sales) in unrestricted cash and equivalents, UAL filed for Chapter 11 on 12/9/02 with $1.3 billion (9% of LTM sales) in unrestricted cash and equivalents (YE 2002), and US Air entered Chapter 11 on 8/11/02 with close to $900 million in cash (3Q02 balance was $900 million) (13% of LTM sales).

Source: Bear, Stearns & Co. Inc. estimates; company reports; company guidance.

Exhibit 33. Cash Burn with No Debt Refinancing and PFEA Expiration (Five-Year Amortization)

With NO Debt Refinancing & PFEA Expiration (5-Yr Amortization)
As of 3/11/05

Cash Flow/Burn 2006E (US$ millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT[2]
2006E Operating Cash Flow[1]										
Operating CF (after-tax) $30/bbl	$2,787	$1,045	$2,232	$1,531	$249	$1,073	$108	$398	$95	$35
Operating CF (after-tax) $35/bbl	$2,398	$919	$1,895	$1,373	$223	$1,035	$84	$365	$60	$24
Operating CF (after-tax) $40/bbl (Base Case)	$1,982	$798	$1,558	$1,214	$197	$998	$60	$332	$24	$12
Operating CF (after-tax) $45/bbl	$1,566	$679	$1,220	$1,056	$171	$961	$36	$300	($12)	$1
Operating CF (after-tax) $50/bbl	$1,149	$511	$883	$897	$145	$923	$11	$267	($48)	($10)
Operating CF (after-tax) $55/bbl	$733	$344	$546	$739	$119	$886	($13)	$234	($84)	($22)
Cash Obligations										
Net Capex	$210	$170	$530	$228	$188	$426	$10	$128	$59	$35
DB Pension Contributions[3]	$377	$356	$962	$901	NA	NA	NA	$76	NA	NA
Debt Maturities	$1,328	$533	$733	$994	$108	$604	$10	$57	$100	$18
Liquidity										
Estimated Unrestricted Cash Balance at Calendar 4Q05[4]	$2,281	$717	$1,098	$1,529	$379	$1,939	$266	$895	$167	$91
Unrestricted Cash Balance at Calendar 4Q04	$2,929	$1,460	$1,799	$2,459	$449	$1,305	$334	$874	$306	$149
2006E Cash Flow (Burn) Oil @ $30/bbl	**$871**	**($14)**	**$7**	**($592)**	**($47)**	**$43**	**$89**	**$137**	**($63)**	**($18)**
Cash Flow (Burn) per Day $30/bbl	$2.4	($0.0)	$0.0	($1.6)	($0.1)	$0.1	$0.2	$0.4	($0.2)	($0.0)
2006E End of Year Unrestricted Cash $30/bbl	$3,152	$703	$1,105	$937	$332	$1,983	$355	$1,033	$104	$73
Months of Cash Left with Oil at $30/bbl from YE 2005 to Threshold[5]	CF Pos.	Ch. 11 Risk	CF Pos.	9	59	CF Pos.	CF Pos.	CF Pos.	Ch. 11 Risk	11
2006E Cash Flow (Burn) Oil @ $35/bbl	**$483**	**($139)**	**($330)**	**($751)**	**($73)**	**$6**	**$65**	**$105**	**($99)**	**($29)**
Cash Flow (Burn) per Day $35/bbl	$1.3	($0.4)	($0.9)	($2.1)	($0.2)	$0.0	$0.2	$0.3	($0.3)	($0.1)
2006E End of Year Unrestricted Cash $35/bbl	$2,764	$578	$767	$779	$306	$1,945	$331	$1,000	$68	$62
Months of Cash Left with Oil at $35/bbl from YE 2005 to Threshold[5]	CF Pos.	Ch. 11 Risk	Ch. 11 Risk	7	38	CF Pos.	CF Pos.	CF Pos.	Ch. 11 Risk	7
2006E Cash Flow (Burn) Oil @ $40/bbl (Base Case)	**$67**	**($260)**	**($667)**	**($909)**	**($99)**	**($31)**	**$40**	**$72**	**($135)**	**($41)**
Cash Flow (Burn) per Day $40/bbl	**$0.2**	**($0.7)**	**($1.8)**	**($2.5)**	**($0.3)**	**($0.1)**	**$0.1**	**$0.2**	**($0.4)**	**($0.1)**
2006E End of Year Unrestricted Cash $40/bbl	**$2,348**	**$457**	**$430**	**$620**	**$280**	**$1,908**	**$307**	**$967**	**$32**	**$50**
Months of Cash Left with Oil at $40/bbl from YE '05 to Threshold[5]	**CF Pos.**	**Ch. 11 Risk**	**Ch. 11 Risk**	**6**	**28**	**454**	**CF Pos.**	**CF Pos.**	**Ch. 11 Risk**	**5**
2006E Cash Flow (Burn) Oil @ $45/bbl	($350)	($380)	($1,004)	($1,067)	($125)	($69)	$16	$39	($171)	($52)
Cash Flow (Burn) per Day $45/bbl	($1.0)	($1.0)	($2.8)	($2.9)	($0.3)	($0.2)	$0.0	$0.1	($0.5)	($0.1)
2006E End of Year Unrestricted Cash $45/bbl	$1,932	$337	$93	$462	$254	$1,871	$283	$934	($4)	$39
Months of Cash Left with Oil at $45/bbl from YE 2005 to Threshold[5]	27	Ch. 11 Risk	Ch. 11 Risk	5	22	207	CF Pos.	CF Pos.	Ch. 11 Risk	4
2006E Cash Flow (Burn) Oil @ $50/bbl	**($766)**	**($547)**	**($1,342)**	**($1,226)**	**($151)**	**($106)**	**($8)**	**$6**	**($207)**	**($63)**
Cash Flow (Burn) per Day $50/bbl	($2.1)	($1.5)	($3.7)	($3.4)	($0.4)	($0.3)	($0.0)	$0.0	($0.6)	($0.2)
2006E End of Year Unrestricted Cash $50/bbl	$1,515	$170	NM	$304	$228	$1,833	$258	$902	($40)	$28
Months of Cash Left with Oil at $50/bbl from YE 2005 to Threshold[5]	12	Ch. 11 Risk	Ch. 11 Risk	4	18	134	253	CF Pos.	Ch. 11 Risk	3
2006E Cash Flow (Burn) Oil @ $55/bbl	**($1,182)**	**($715)**	**($1,679)**	**($1,384)**	**($177)**	**($144)**	**($32)**	**($26)**	**($243)**	**($75)**
Cash Flow (Burn) per Day $55/bbl	($3.2)	($2.0)	($4.6)	($3.8)	($0.5)	($0.4)	($0.1)	($0.1)	($0.7)	($0.2)
2006E End of Year Unrestricted Cash $55/bbl	$1,099	$2	NM	$145	$202	$1,796	$234	$869	($76)	$16
Months of Cash Left with Oil at $55/bbl from YE 2005 to Threshold[5]	8	Ch. 11 Risk	Ch. 11 Risk	4	16	99	62	272	Ch. 11 Risk	3

(1) Operating Cash Flow = Net Income + D&A + pension expense; assumes no impact from change in net working capital.
Assumes crude price of $40/bbl in 2006. Incorporates hedge positions.
(2) FRNT is in 2007 March-ending fiscal year, base assumption oil at $40/bbl for calendar 2006.
(3) Assumes no additional noncash (stock of subsidiary) contribution to DB pension plans.
(4) Assumes crude price of $49/bbl in 1Q05 and $45/bbl in 2Q-4Q05. For no debt refinancing scenario in 2006, assumes no debt refinancing in 2005. For debt refinancing scenario in 2006, assumes debt refinancing in 2005.
(5) Chapter 11 risk: operating with cash burn and cash balance is below threshold cash level.

(US$ in millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT
Estimated Unrestricted Cash Concern Level	**$1,500**	**$1,000**	**$1,500**	**$1,100**	**$150**	**$750**	**$100**	**$300**	**$200**	**$75**

As points of reference, we note that AMR achieved its last-minute deal with labor last April with $1.2 billion (7% of LTM sales) in unrestricted cash and equivalents, UAL filed for Chapter 11 on 12/9/02 with $1.3 billion (9% of LTM sales) in unrestricted cash and equivalents (YE 2002), and US Air entered Chapter 11 on 8/11/02 with close to $900 million in cash (3Q02 balance was $900 million) (13% of LTM sales).

Source: Bear, Stearns & Co. Inc. estimates; company reports; company guidance.

Exhibit 34. Cash Burn with No Debt Refinancing and Bush Pension Proposal (Seven-Year Amortization)

With NO Debt Refinancing & Bush Proposal (7-Yr Amortization)
As of 3/11/05

Cash Flow/Burn 2006E (US$ millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT[2]
2006E Operating Cash Flow[1]										
Operating CF (after-tax) $30/bbl	$2,787	$1,045	$2,232	$1,531	$249	$1,073	$108	$398	$95	$35
Operating CF (after-tax) $35/bbl	$2,398	$919	$1,895	$1,373	$223	$1,035	$84	$365	$60	$24
Operating CF (after-tax) $40/bbl (Base Case)	$1,982	$798	$1,558	$1,214	$197	$998	$60	$332	$24	$12
Operating CF (after-tax) $45/bbl	$1,566	$679	$1,220	$1,056	$171	$961	$36	$300	($12)	$1
Operating CF (after-tax) $50/bbl	$1,149	$511	$883	$897	$145	$923	$11	$267	($48)	($10)
Operating CF (after-tax) $55/bbl	$733	$344	$546	$739	$119	$886	($13)	$234	($84)	($22)
Cash Obligations										
Net Capex	$210	$170	$530	$228	$188	$426	$10	$128	$59	$35
DB Pension Contributions[3]	$314	$288	$726	$704	NA	NA	NA	$71	NA	NA
Debt Maturities	$1,328	$533	$733	$994	$108	$604	$10	$57	$100	$18
Liquidity										
Estimated Unrestricted Cash Balance at Calendar 4Q05[4]	$2,281	$717	$1,098	$1,529	$379	$1,939	$266	$895	$167	$91
Unrestricted Cash Balance at Calendar 4Q04	$2,929	$1,460	$1,799	$2,459	$449	$1,305	$334	$874	$306	$149
2006E Cash Flow (Burn) Oil @ $30/bbl	**$935**	**$54**	**$243**	**($395)**	**($47)**	**$43**	**$89**	**$143**	**($63)**	**($18)**
Cash Flow (Burn) per Day $30/bbl	$2.6	$0.1	$0.7	($1.1)	($0.1)	$0.1	$0.2	$0.4	($0.2)	($0.0)
2006E End of Year Unrestricted Cash $30/bbl	$3,216	$771	$1,340	$1,135	$332	$1,983	$355	$1,038	$104	$73
Months of Cash Left with Oil at $30/bbl from YE 2005 to Threshold[5]	CF Pos.	CF Pos.	CF Pos.	13	59	CF Pos.	CF Pos.	CF Pos.	Ch. 11 Risk	11
2006E Cash Flow (Burn) Oil @ $35/bbl	**$547**	**($72)**	**($95)**	**($553)**	**($73)**	**$6**	**$65**	**$110**	**($99)**	**($29)**
Cash Flow (Burn) per Day $35/bbl	$1.5	($0.2)	($0.3)	($1.5)	($0.2)	$0.0	$0.2	$0.3	($0.3)	($0.1)
2006E End of Year Unrestricted Cash $35/bbl	$2,828	$645	$1,003	$976	$306	$1,945	$331	$1,005	$68	$62
Months of Cash Left with Oil at $35/bbl from YE 2005 to Threshold[5]	CF Pos.	Ch. 11 Risk	Ch. 11 Risk	9	38	CF Pos.	CF Pos.	CF Pos.	Ch. 11 Risk	7
2006E Cash Flow (Burn) Oil @ $40/bbl (Base Case)	**$130**	**($193)**	**($432)**	**($711)**	**($99)**	**($31)**	**$40**	**$77**	**($135)**	**($41)**
Cash Flow (Burn) per Day $40/bbl	**$0.4**	**($0.5)**	**($1.2)**	**($1.9)**	**($0.3)**	**($0.1)**	**$0.1**	**$0.2**	**($0.4)**	**($0.1)**
2006E End of Year Unrestricted Cash $40/bbl	**$2,411**	**$524**	**$666**	**$818**	**$280**	**$1,908**	**$307**	**$972**	**$32**	**$50**
Months of Cash Left with Oil at $40/bbl from YE '05 to Threshold[5]	**CF Pos.**	**Ch. 11 Risk**	**Ch. 11 Risk**	**7**	**28**	**454**	**CF Pos.**	**CF Pos.**	**Ch. 11 Risk**	**5**
2006E Cash Flow (Burn) Oil @ $45/bbl	($286)	($313)	($769)	($870)	($125)	($69)	$16	$44	($171)	($52)
Cash Flow (Burn) per Day $45/bbl	($0.8)	($0.9)	($2.1)	($2.4)	($0.3)	($0.2)	$0.0	$0.1	($0.5)	($0.1)
2006E End of Year Unrestricted Cash $45/bbl	$1,995	$405	$329	$660	$254	$1,871	$283	$940	($4)	$39
Months of Cash Left with Oil at $45/bbl from YE 2005 to Threshold[5]	33	Ch. 11 Risk	Ch. 11 Risk	6	22	207	CF Pos.	CF Pos.	Ch. 11 Risk	4
2006E Cash Flow (Burn) Oil @ $50/bbl	**($702)**	**($480)**	**($1,106)**	**($1,028)**	**($151)**	**($106)**	**($8)**	**$12**	**($207)**	**($63)**
Cash Flow (Burn) per Day $50/bbl	($1.9)	($1.3)	($3.0)	($2.8)	($0.4)	($0.3)	($0.0)	$0.0	($0.6)	($0.2)
2006E End of Year Unrestricted Cash $50/bbl	$1,579	$237	NM	$501	$228	$1,833	$258	$907	($40)	$28
Months of Cash Left with Oil at $50/bbl from YE 2005 to Threshold[5]	13	Ch. 11 Risk	Ch. 11 Risk	5	18	134	253	CF Pos.	Ch. 11 Risk	3
2006E Cash Flow (Burn) Oil @ $55/bbl	**($1,119)**	**($648)**	**($1,443)**	**($1,187)**	**($177)**	**($144)**	**($32)**	**($21)**	**($243)**	**($75)**
Cash Flow (Burn) per Day $55/bbl	($3.1)	($1.8)	($4.0)	($3.3)	($0.5)	($0.4)	($0.1)	($0.1)	($0.7)	($0.2)
2006E End of Year Unrestricted Cash $55/bbl	$1,162	$70	NM	$343	$202	$1,796	$234	$874	($76)	$16
Months of Cash Left with Oil at $55/bbl from YE 2005 to Threshold[5]	8	Ch. 11 Risk	Ch. 11 Risk	4	16	99	62	337	Ch. 11 Risk	3

(1) Operating Cash Flow = Net Income + D&A + pension expense; assumes no impact from change in net working capital.
Assumes crude price of $40/bbl in 2006. Incorporates hedge positions.
(2) FRNT is in 2007 March-ending fiscal year, base assumption oil at $40/bbl for calendar 2006.
(3) Assumes no additional noncash (stock of subsidiary) contribution to DB pension plans.
(4) Assumes crude price of $49/bbl in 1Q05 and $45/bbl in 2Q-4Q05. For no debt refinancing scenario in 2006, assumes no debt refinancing in 2005. For debt refinancing scenario in 2006, assumes debt refinancing in 2005.
(5) Chapter 11 risk: operating with cash burn and cash balance is below threshold cash level.

(US$ in millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT
Estimated Unrestricted Cash Concern Level	**$1,500**	**$1,000**	**$1,500**	**$1,100**	**$150**	**$750**	**$100**	**$300**	**$200**	**$75**

As points of reference, we note that AMR achieved its last-minute deal with labor last April with $1.2 billion (7% of LTM sales) in unrestricted cash and equivalents, UAL filed for Chapter 11 on 12/9/02 with $1.3 billion (9% of LTM sales) in unrestricted cash and equivalents (YE 2002), and US Air entered Chapter 11 on 8/11/02 with close to $900 million in cash (3Q02 balance was $900 million) (13% of LTM sales).

Source: Bear, Stearns & Co. Inc. estimates; company reports; company guidance.

Exhibit 35. Cash Burn with No Debt Refinancing and Pension Plan Freeze/20-Year Amortization Proposal

With NO Debt Refinancing & Pension Plan Freeze / 20-Yr Amortization Proposal
As of 3/11/05

Cash Flow/Burn 2006E (US$ millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT[2]
2006E Operating Cash Flow[1]										
Operating CF (after-tax) $30/bbl	$2,787	$1,045	$2,232	$1,531	$249	$1,073	$108	$398	$95	$35
Operating CF (after-tax) $35/bbl	$2,398	$919	$1,895	$1,373	$223	$1,035	$84	$365	$60	$24
Operating CF (after-tax) $40/bbl (Base Case)	$1,982	$798	$1,558	$1,214	$197	$998	$60	$332	$24	$12
Operating CF (after-tax) $45/bbl	$1,566	$679	$1,220	$1,056	$171	$961	$36	$300	($12)	$1
Operating CF (after-tax) $50/bbl	$1,149	$511	$883	$897	$145	$923	$11	$267	($48)	($10)
Operating CF (after-tax) $55/bbl	$733	$344	$546	$739	$119	$886	($13)	$234	($84)	($22)
Cash Obligations										
Net Capex	$210	$170	$530	$228	$188	$426	$10	$128	$59	$35
DB Pension Contributions[3]	$45	$44	$202	$133	NA	NA	NA	$4	NA	NA
Debt Maturities	$1,328	$533	$733	$994	$108	$604	$10	$57	$100	$18
Liquidity										
Estimated Unrestricted Cash Balance at Calendar 4Q05[4]	$2,281	$717	$1,098	$1,529	$379	$1,939	$266	$895	$167	$91
Unrestricted Cash Balance at Calendar 4Q04	$2,929	$1,460	$1,799	$2,459	$449	$1,305	$334	$874	$306	$149
2006E Cash Flow (Burn) Oil @ $30/bbl	**$1,203**	**$298**	**$768**	**$176**	**($47)**	**$43**	**$89**	**$209**	**($63)**	**($18)**
Cash Flow (Burn) per Day $30/bbl	$3.3	$0.8	$2.1	$0.5	($0.1)	$0.1	$0.2	$0.6	($0.2)	($0.0)
2006E End of Year Unrestricted Cash $30/bbl	$3,484	$1,015	$1,865	$1,705	$332	$1,983	$355	$1,104	$104	$73
Months of Cash Left with Oil at $30/bbl from YE 2005 to Threshold[5]	CF Pos.	CF Pos.	CF Pos.	CF Pos.	59	CF Pos.	CF Pos.	CF Pos.	Ch. 11 Risk	11
2006E Cash Flow (Burn) Oil @ $35/bbl	**$815**	**$172**	**$430**	**$17**	**($73)**	**$6**	**$65**	**$176**	**($99)**	**($29)**
Cash Flow (Burn) per Day $35/bbl	$2.2	$0.5	$1.2	$0.0	($0.2)	$0.0	$0.2	$0.5	($0.3)	($0.1)
2006E End of Year Unrestricted Cash $35/bbl	$3,096	$889	$1,528	$1,547	$306	$1,945	$331	$1,071	$68	$62
Months of Cash Left with Oil at $35/bbl from YE 2005 to Threshold[5]	CF Pos.	CF Pos.	CF Pos.	CF Pos.	38	CF Pos.	CF Pos.	CF Pos.	Ch. 11 Risk	7
2006E Cash Flow (Burn) Oil @ $40/bbl (Base Case)	**$398**	**$51**	**$93**	**($141)**	**($99)**	**($31)**	**$40**	**$143**	**($135)**	**($41)**
Cash Flow (Burn) per Day $40/bbl	**$1.1**	**$0.1**	**$0.3**	**($0.4)**	**($0.3)**	**($0.1)**	**$0.1**	**$0.4**	**($0.4)**	**($0.1)**
2006E End of Year Unrestricted Cash $40/bbl	**$2,680**	**$768**	**$1,191**	**$1,388**	**$280**	**$1,908**	**$307**	**$1,039**	**$32**	**$50**
Months of Cash Left with Oil at $40/bbl from YE '05 to Threshold[5]	**CF Pos.**	**CF Pos.**	**CF Pos.**	**37**	**28**	**454**	**CF Pos.**	**CF Pos.**	**Ch. 11 Risk**	**5**
2006E Cash Flow (Burn) Oil @ $45/bbl	($18)	($69)	($244)	($299)	($125)	($69)	$16	$111	($171)	($52)
Cash Flow (Burn) per Day $45/bbl	($0.0)	($0.2)	($0.7)	($0.8)	($0.3)	($0.2)	$0.0	$0.3	($0.5)	($0.1)
2006E End of Year Unrestricted Cash $45/bbl	$2,263	$648	$854	$1,230	$254	$1,871	$283	$1,006	($4)	$39
Months of Cash Left with Oil at $45/bbl from YE 2005 to Threshold[5]	526	Ch. 11 Risk	Ch. 11 Risk	17	22	207	CF Pos.	CF Pos.	Ch. 11 Risk	4
2006E Cash Flow (Burn) Oil @ $50/bbl	**($434)**	**($236)**	**($581)**	**($458)**	**($151)**	**($106)**	**($8)**	**$78**	**($207)**	**($63)**
Cash Flow (Burn) per Day $50/bbl	($1.2)	($0.6)	($1.6)	($1.3)	($0.4)	($0.3)	($0.0)	$0.2	($0.6)	($0.2)
2006E End of Year Unrestricted Cash $50/bbl	$1,847	$481	$516	$1,072	$228	$1,833	$258	$973	($40)	$28
Months of Cash Left with Oil at $50/bbl from YE 2005 to Threshold[5]	22	Ch. 11 Risk	Ch. 11 Risk	11	18	134	253	CF Pos.	Ch. 11 Risk	3
2006E Cash Flow (Burn) Oil @ $55/bbl	**($850)**	**($404)**	**($918)**	**($616)**	**($177)**	**($144)**	**($32)**	**$45**	**($243)**	**($75)**
Cash Flow (Burn) per Day $55/bbl	($2.3)	($1.1)	($2.5)	($1.7)	($0.5)	($0.4)	($0.1)	$0.1	($0.7)	($0.2)
2006E End of Year Unrestricted Cash $55/bbl	$1,431	$313	$179	$913	$202	$1,796	$234	$940	($76)	$16
Months of Cash Left with Oil at $55/bbl from YE 2005 to Threshold[5]	11	Ch. 11 Risk	Ch. 11 Risk	8	16	99	62	CF Pos.	Ch. 11 Risk	3

(1) Operating Cash Flow = Net Income + D&A + pension expense; assumes no impact from change in net working capital.
Assumes crude price of $40/bbl in 2006. Incorporates hedge positions.
(2) FRNT is in 2007 March-ending fiscal year, base assumption oil at $40/bbl for calendar 2006.
(3) Assumes no additional noncash (stock of subsidiary) contribution to DB pension plans.
(4) Assumes crude price of $49/bbl in 1Q05 and $45/bbl in 2Q-4Q05. For no debt refinancing scenario in 2006, assumes no debt refinancing in 2005. For debt refinancing scenario in 2006, assumes debt refinancing in 2005.
(5) Chapter 11 risk: operating with cash burn and cash balance is below threshold cash level.

(US$ in millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT
Estimated Unrestricted Cash Concern Level	**$1,500**	**$1,000**	**$1,500**	**$1,100**	**$150**	**$750**	**$100**	**$300**	**$200**	**$75**

As points of reference, we note that AMR achieved its last-minute deal with labor last April with $1.2 billion (7% of LTM sales) in unrestricted cash and equivalents, UAL filed for Chapter 11 on 12/9/02 with $1.3 billion (9% of LTM sales) in unrestricted cash and equivalents (YE 2002), and US Air entered Chapter 11 on 8/11/02 with close to $900 million in cash (3Q02 balance was $900 million) (13% of LTM sales).

Source: Bear, Stearns & Co. Inc. estimates; company reports; company guidance.

Exhibit 36. Cash Burn with Debt Refinancing of 80% of Maturing Amount and PFEA Expiration (Five-Year Amortization)

With Debt Refinancing of 80% of Maturing Amount & PFEA Expiration (5-Yr Amortization)
As of 3/11/05

Cash Flow/Burn 2006E (US$ millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT[2]
2006E Operating Cash Flow[1]										
Operating CF (after-tax) $30/bbl	$2,787	$1,045	$2,232	$1,531	$249	$1,073	$108	$398	$95	$35
Operating CF (after-tax) $35/bbl	$2,398	$919	$1,895	$1,373	$223	$1,035	$84	$365	$60	$24
Operating CF (after-tax) $40/bbl (Base Case)	$1,982	$798	$1,558	$1,214	$197	$998	$60	$332	$24	$12
Operating CF (after-tax) $45/bbl	$1,566	$679	$1,220	$1,056	$171	$961	$36	$300	($12)	$1
Operating CF (after-tax) $50/bbl	$1,149	$511	$883	$897	$145	$923	$11	$267	($48)	($10)
Operating CF (after-tax) $55/bbl	$733	$344	$546	$739	$119	$886	($13)	$234	($84)	($22)
Cash Obligations										
Net Capex	$210	$170	$530	$228	$188	$426	$10	$128	$59	$35
DB Pension Contributions[3]	$377	$356	$962	$901	NA	NA	NA	$76	NA	NA
Debt Maturities	$266	$107	$147	$199	$22	$121	$2	$11	$20	$4
Liquidity										
Estimated Unrestricted Cash Balance at Calendar 4Q05[4]	$3,009	$1,268	$1,602	$2,129	$463	$2,056	$278	$938	$248	$105
Unrestricted Cash Balance at Calendar 4Q04	$2,929	$1,460	$1,799	$2,459	$449	$1,305	$334	$874	$306	$149
2006E Cash Flow (Burn) Oil @ $30/bbl	**$1,934**	**$413**	**$594**	**$203**	**$40**	**$527**	**$97**	**$183**	**$17**	**($3)**
Cash Flow (Burn) per Day $30/bbl	$5.3	$1.1	$1.6	$0.6	$0.1	$1.4	$0.3	$0.5	$0.0	($0.0)
2006E End of Year Unrestricted Cash $30/bbl	$4,943	$1,680	$2,195	$2,332	$503	$2,583	$374	$1,121	$265	$101
Months of Cash Left with Oil at $30/bbl from YE 2005 to Threshold[5]	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	109
2006E Cash Flow (Burn) Oil @ $35/bbl	**$1,545**	**$287**	**$256**	**$45**	**$13**	**$489**	**$72**	**$150**	**($19)**	**($15)**
Cash Flow (Burn) per Day $35/bbl	$4.2	$0.8	$0.7	$0.1	$0.0	$1.3	$0.2	$0.4	($0.1)	($0.0)
2006E End of Year Unrestricted Cash $35/bbl	$4,555	$1,555	$1,858	$2,173	$477	$2,545	$350	$1,088	$229	$90
Months of Cash Left with Oil at $35/bbl from YE 2005 to Threshold[5]	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	30	24
2006E Cash Flow (Burn) Oil @ $40/bbl (Base Case)	**$1,129**	**$166**	**($81)**	**($114)**	**($13)**	**$452**	**$48**	**$118**	**($55)**	**($26)**
Cash Flow (Burn) per Day $40/bbl	**$3.1**	**$0.5**	**($0.2)**	**($0.3)**	**($0.0)**	**$1.2**	**$0.1**	**$0.3**	**($0.2)**	**($0.1)**
2006E End of Year Unrestricted Cash $40/bbl	**$4,138**	**$1,433**	**$1,521**	**$2,015**	**$451**	**$2,508**	**$326**	**$1,056**	**$193**	**$79**
Months of Cash Left with Oil at $40/bbl from YE '05 to Threshold[5]	**CF Pos.**	**CF Pos.**	**15**	**109**	**298**	**CF Pos.**	**CF Pos.**	**CF Pos.**	**10**	**14**
2006E Cash Flow (Burn) Oil @ $45/bbl	$713	$46	($418)	($272)	($39)	$414	$24	$85	($91)	($38)
Cash Flow (Burn) per Day $45/bbl	$2.0	$0.1	($1.1)	($0.7)	($0.1)	$1.1	$0.1	$0.2	($0.2)	($0.1)
2006E End of Year Unrestricted Cash $45/bbl	$3,722	$1,314	$1,183	$1,856	$425	$2,471	$302	$1,023	$157	$67
Months of Cash Left with Oil at $45/bbl from YE 2005 to Threshold[5]	CF Pos.	CF Pos.	3	45	97	CF Pos.	CF Pos.	CF Pos.	6	9
2006E Cash Flow (Burn) Oil @ $50/bbl	**$297**	**($121)**	**($755)**	**($431)**	**($65)**	**$377**	**$0**	**$52**	**($127)**	**($49)**
Cash Flow (Burn) per Day $50/bbl	$0.8	($0.3)	($2.1)	($1.2)	($0.2)	$1.0	$0.0	$0.1	($0.3)	($0.1)
2006E End of Year Unrestricted Cash $50/bbl	$3,306	$1,146	$846	$1,698	$399	$2,433	$278	$990	$121	$56
Months of Cash Left with Oil at $50/bbl from YE 2005 to Threshold[5]	CF Pos.	27	2	29	58	CF Pos.	CF Pos.	CF Pos.	5	7
2006E Cash Flow (Burn) Oil @ $55/bbl	**($120)**	**($289)**	**($1,092)**	**($589)**	**($91)**	**$340**	**($24)**	**$19**	**($163)**	**($60)**
Cash Flow (Burn) per Day $55/bbl	($0.3)	($0.8)	($3.0)	($1.6)	($0.2)	$0.9	($0.1)	$0.1	($0.4)	($0.2)
2006E End of Year Unrestricted Cash $55/bbl	$2,889	$979	$509	$1,540	$372	$2,396	$253	$957	$85	$44
Months of Cash Left with Oil at $55/bbl from YE 2005 to Threshold[5]	151	11	1	21	41	CF Pos.	88	CF Pos.	4	6

(1) Operating Cash Flow = Net Income + D&A + pension expense; assumes no impact from change in net working capital.
Assumes crude price of $40/bbl in 2006. Incorporates hedge positions.
(2) FRNT is in 2007 March-ending fiscal year, base assumption oil at $40/bbl for calendar 2006.
(3) Assumes no additional noncash (stock of subsidiary) contribution to DB pension plans.
(4) Assumes crude price of $49/bbl in 1Q05 and $45/bbl in 2Q-4Q05. For no debt refinancing scenario in 2006, assumes no debt refinancing in 2005. For debt refinancing scenario in 2006, assumes debt refinancing in 2005.
(5) Chapter 11 risk: operating with cash burn and cash balance is below threshold cash level.

(US$ in millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT
Estimated Unrestricted Cash Concern Level	**$1,500**	**$1,000**	**$1,500**	**$1,100**	**$150**	**$750**	**$100**	**$300**	**$200**	**$75**

As points of reference, we note that AMR achieved its last-minute deal with labor last April with $1.2 billion (7% of LTM sales) in unrestricted cash and equivalents, UAL filed for Chapter 11 on 12/9/02 with $1.3 billion (9% of LTM sales) in unrestricted cash and equivalents (YE 2002), and US Air entered Chapter 11 on 8/11/02 with close to $900 million in cash (3Q02 balance was $900 million) (13% of LTM sales).

Source: Bear, Stearns & Co. Inc. estimates; company reports; company guidance.

Exhibit 37. Cash Burn with Debt Refinancing of 80% of Maturing Amount and Bush Pension Proposal (Seven-Year Amortization)

With Debt Refinancing of 80% of Maturing Amount & Bush Proposal (7-Yr Amortization)

As of 3/11/05

Cash Flow/Burn 2006E (US$ millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT[2]
2006E Operating Cash Flow[1]										
Operating CF (after-tax) $30/bbl	$2,787	$1,045	$2,232	$1,531	$249	$1,073	$108	$398	$95	$35
Operating CF (after-tax) $35/bbl	$2,398	$919	$1,895	$1,373	$223	$1,035	$84	$365	$60	$24
Operating CF (after-tax) $40/bbl (Base Case)	$1,982	$798	$1,558	$1,214	$197	$998	$60	$332	$24	$12
Operating CF (after-tax) $45/bbl	$1,566	$679	$1,220	$1,056	$171	$961	$36	$300	($12)	$1
Operating CF (after-tax) $50/bbl	$1,149	$511	$883	$897	$145	$923	$11	$267	($48)	($10)
Operating CF (after-tax) $55/bbl	$733	$344	$546	$739	$119	$886	($13)	$234	($84)	($22)
Cash Obligations										
Net Capex	$210	$170	$530	$228	$188	$426	$10	$128	$59	$35
DB Pension Contributions[3]	$314	$288	$726	$704	NA	NA	NA	$71	NA	NA
Debt Maturities	$266	$107	$147	$199	$22	$121	$2	$11	$20	$4
Liquidity										
Estimated Unrestricted Cash Balance at Calendar 4Q05[4]	$3,009	$1,268	$1,602	$2,129	$463	$2,056	$278	$938	$248	$105
Unrestricted Cash Balance at Calendar 4Q04	$2,929	$1,460	$1,799	$2,459	$449	$1,305	$334	$874	$306	$149
2006E Cash Flow (Burn) Oil @ $30/bbl	**$1,997**	**$480**	**$829**	**$401**	**$40**	**$527**	**$97**	**$188**	**$17**	**($3)**
Cash Flow (Burn) per Day $30/bbl	$5.5	$1.3	$2.3	$1.1	$0.1	$1.4	$0.3	$0.5	$0.0	($0.0)
2006E End of Year Unrestricted Cash $30/bbl	$5,006	$1,748	$2,431	$2,529	$503	$2,583	$374	$1,126	$265	$101
Months of Cash Left with Oil at $30/bbl from YE 2005 to Threshold[5]	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	109
2006E Cash Flow (Burn) Oil @ $35/bbl	**$1,609**	**$354**	**$492**	**$242**	**$13**	**$489**	**$72**	**$155**	**($19)**	**($15)**
Cash Flow (Burn) per Day $35/bbl	$4.4	$1.0	$1.3	$0.7	$0.0	$1.3	$0.2	$0.4	($0.1)	($0.0)
2006E End of Year Unrestricted Cash $35/bbl	$4,618	$1,622	$2,093	$2,371	$477	$2,545	$350	$1,093	$229	$90
Months of Cash Left with Oil at $35/bbl from YE 2005 to Threshold[5]	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	30	24
2006E Cash Flow (Burn) Oil @ $40/bbl (Base Case)	**$1,193**	**$233**	**$155**	**$84**	**($13)**	**$452**	**$48**	**$123**	**($55)**	**($26)**
Cash Flow (Burn) per Day $40/bbl	**$3.3**	**$0.6**	**$0.4**	**$0.2**	**($0.0)**	**$1.2**	**$0.1**	**$0.3**	**($0.2)**	**($0.1)**
2006E End of Year Unrestricted Cash $40/bbl	**$4,202**	**$1,501**	**$1,756**	**$2,212**	**$451**	**$2,508**	**$326**	**$1,061**	**$193**	**$79**
Months of Cash Left with Oil at $40/bbl from YE '05 to Threshold	**CF Pos.**	**CF Pos.**	**CF Pos.**	**CF Pos.**	**298**	**CF Pos.**	**CF Pos.**	**CF Pos.**	**10**	**14**
2006E Cash Flow (Burn) Oil @ $45/bbl	$776	$114	($182)	($75)	($39)	$414	$24	$90	($91)	($38)
Cash Flow (Burn) per Day $45/bbl	$2.1	$0.3	($0.5)	($0.2)	($0.1)	$1.1	$0.1	$0.2	($0.2)	($0.1)
2006E End of Year Unrestricted Cash $45/bbl	$3,785	$1,381	$1,419	$2,054	$425	$2,471	$302	$1,028	$157	$67
Months of Cash Left with Oil at $45/bbl from YE 2005 to Threshold[5]	CF Pos.	CF Pos.	7	165	97	CF Pos.	CF Pos.	CF Pos.	6	9
2006E Cash Flow (Burn) Oil @ $50/bbl	**$360**	**($54)**	**($520)**	**($233)**	**($65)**	**$377**	**$0**	**$57**	**($127)**	**($49)**
Cash Flow (Burn) per Day $50/bbl	$1.0	($0.1)	($1.4)	($0.6)	($0.2)	$1.0	$0.0	$0.2	($0.3)	($0.1)
2006E End of Year Unrestricted Cash $50/bbl	$3,369	$1,214	$1,082	$1,896	$399	$2,433	$278	$995	$121	$56
Months of Cash Left with Oil at $50/bbl from YE 2005 to Threshold[5]	CF Pos.	60	2	53	58	CF Pos.	CF Pos.	CF Pos.	5	7
2006E Cash Flow (Burn) Oil @ $55/bbl	**($56)**	**($221)**	**($857)**	**($391)**	**($91)**	**$340**	**($24)**	**$25**	**($163)**	**($60)**
Cash Flow (Burn) per Day $55/bbl	($0.2)	($0.6)	($2.3)	($1.1)	($0.2)	$0.9	($0.1)	$0.1	($0.4)	($0.2)
2006E End of Year Unrestricted Cash $55/bbl	$2,953	$1,046	$745	$1,737	$372	$2,396	$253	$963	$85	$44
Months of Cash Left with Oil at $55/bbl from YE 2005 to Threshold[5]	322	15	1	32	41	CF Pos.	88	CF Pos.	4	6

(1) Operating Cash Flow = Net Income + D&A + pension expense; assumes no impact from change in net working capital.
Assumes crude price of $40/bbl in 2006. Incorporates hedge positions.
(2) FRNT is in 2007 March-ending fiscal year, base assumption oil at $40/bbl for calendar 2006.
(3) Assumes no additional noncash (stock of subsidiary) contribution to DB pension plans.
(4) Assumes crude price of $49/bbl in 1Q05 and $45/bbl in 2Q-4Q05. For no debt refinancing scenario in 2006, assumes no debt refinancing in 2005. For debt refinancing scenario in 2006, assumes debt refinancing in 2005.
(5) Chapter 11 risk: operating with cash burn and cash balance is below threshold cash level.

(US$ in millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT
Estimated Unrestricted Cash Concern Level	**$1,500**	**$1,000**	**$1,500**	**$1,100**	**$150**	**$750**	**$100**	**$300**	**$200**	**$75**

As points of reference, we note that AMR achieved its last-minute deal with labor last April with $1.2 billion (7% of LTM sales) in unrestricted cash and equivalents, UAL filed for Chapter 11 on 12/9/02 with $1.3 billion (9% of LTM sales) in unrestricted cash and equivalents (YE 2002), and US Air entered Chapter 11 on 8/11/02 with close to $900 million in cash (3Q02 balance was $900 million) (13% of LTM sales).

Source: Bear, Stearns & Co. Inc. estimates; company reports; company guidance.

Exhibit 38. Cash Burn with Debt Refinancing of 80% of Maturing Amount and Pension Plan Freeze/20-Year Amortization Proposal

With Debt Refinancing of 80% of Maturing Amount & Pension Plan Freeze / 20-Yr Amortization Proposal
As of 3/11/05

Cash Flow/Burn 2006E (US$ millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT[2]
2006E Operating Cash Flow[1]										
Operating CF (after-tax) $30/bbl	$2,787	$1,045	$2,232	$1,531	$249	$1,073	$108	$398	$95	$35
Operating CF (after-tax) $35/bbl	$2,398	$919	$1,895	$1,373	$223	$1,035	$84	$365	$60	$24
Operating CF (after-tax) $40/bbl (Base Case)	$1,982	$798	$1,558	$1,214	$197	$998	$60	$332	$24	$12
Operating CF (after-tax) $45/bbl	$1,566	$679	$1,220	$1,056	$171	$961	$36	$300	($12)	$1
Operating CF (after-tax) $50/bbl	$1,149	$511	$883	$897	$145	$923	$11	$267	($48)	($10)
Operating CF (after-tax) $55/bbl	$733	$344	$546	$739	$119	$886	($13)	$234	($84)	($22)
Cash Obligations										
Net Capex	$210	$170	$530	$228	$188	$426	$10	$128	$59	$35
DB Pension Contributions[3]	$45	$44	$202	$133	NA	NA	NA	$4	NA	NA
Debt Maturities	$266	$107	$147	$199	$22	$121	$2	$11	$20	$4
Liquidity										
Estimated Unrestricted Cash Balance at Calendar 4Q05[4]	$3,009	$1,268	$1,602	$2,129	$463	$2,056	$278	$938	$248	$105
Unrestricted Cash Balance at Calendar 4Q04	$2,929	$1,460	$1,799	$2,459	$449	$1,305	$334	$874	$306	$149
2006E Cash Flow (Burn) Oil @ $30/bbl	**$2,266**	**$724**	**$1,354**	**$971**	**$40**	**$527**	**$97**	**$255**	**$17**	**($3)**
Cash Flow (Burn) per Day $30/bbl	$6.2	$2.0	$3.7	$2.7	$0.1	$1.4	$0.3	$0.7	$0.0	($0.0)
2006E End of Year Unrestricted Cash $30/bbl	$5,275	$1,992	$2,956	$3,100	$503	$2,583	$374	$1,193	$265	$101
Months of Cash Left with Oil at $30/bbl from YE 2005 to Threshold[5]	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	109
2006E Cash Flow (Burn) Oil @ $35/bbl	**$1,877**	**$598**	**$1,017**	**$813**	**$13**	**$489**	**$72**	**$222**	**($19)**	**($15)**
Cash Flow (Burn) per Day $35/bbl	$5.1	$1.6	$2.8	$2.2	$0.0	$1.3	$0.2	$0.6	($0.1)	($0.0)
2006E End of Year Unrestricted Cash $35/bbl	$4,886	$1,866	$2,618	$2,941	$477	$2,545	$350	$1,160	$229	$90
Months of Cash Left with Oil at $35/bbl from YE 2005 to Threshold[5]	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	30	24
2006E Cash Flow (Burn) Oil @ $40/bbl (Base Case)	**$1,461**	**$477**	**$680**	**$654**	**($13)**	**$452**	**$48**	**$189**	**($55)**	**($26)**
Cash Flow (Burn) per Day $40/bbl	**$4.0**	**$1.3**	**$1.9**	**$1.8**	**($0.0)**	**$1.2**	**$0.1**	**$0.5**	**($0.2)**	**($0.1)**
2006E End of Year Unrestricted Cash $40/bbl	**$4,470**	**$1,745**	**$2,281**	**$2,783**	**$451**	**$2,508**	**$326**	**$1,127**	**$193**	**$79**
Months of Cash Left with Oil at $40/bbl from YE '05 to Threshold	**CF Pos.**	**CF Pos.**	**CF Pos.**	**CF Pos.**	**298**	**CF Pos.**	**CF Pos.**	**CF Pos.**	**10**	**14**
2006E Cash Flow (Burn) Oil @ $45/bbl	$1,045	$358	$342	$496	($39)	$414	$24	$156	($91)	($38)
Cash Flow (Burn) per Day $45/bbl	$2.9	$1.0	$0.9	$1.4	($0.1)	$1.1	$0.1	$0.4	($0.2)	($0.1)
2006E End of Year Unrestricted Cash $45/bbl	$4,054	$1,625	$1,944	$2,624	$425	$2,471	$302	$1,094	$157	$67
Months of Cash Left with Oil at $45/bbl from YE 2005 to Threshold[5]	CF Pos.	CF Pos.	CF Pos.	CF Pos.	97	CF Pos.	CF Pos.	CF Pos.	6	9
2006E Cash Flow (Burn) Oil @ $50/bbl	**$628**	**$190**	**$5**	**$337**	**($65)**	**$377**	**$0**	**$124**	**($127)**	**($49)**
Cash Flow (Burn) per Day $50/bbl	$1.7	$0.5	$0.0	$0.9	($0.2)	$1.0	$0.0	$0.3	($0.3)	($0.1)
2006E End of Year Unrestricted Cash $50/bbl	$3,637	$1,458	$1,607	$2,466	$399	$2,433	$278	$1,062	$121	$56
Months of Cash Left with Oil at $50/bbl from YE 2005 to Threshold[5]	CF Pos.	CF Pos.	CF Pos.	CF Pos.	58	CF Pos.	CF Pos.	CF Pos.	5	7
2006E Cash Flow (Burn) Oil @ $55/bbl	**$212**	**$23**	**($332)**	**$179**	**($91)**	**$340**	**($24)**	**$91**	**($163)**	**($60)**
Cash Flow (Burn) per Day $55/bbl	$0.6	$0.1	($0.9)	$0.5	($0.2)	$0.9	($0.1)	$0.2	($0.4)	($0.2)
2006E End of Year Unrestricted Cash $55/bbl	$3,221	$1,290	$1,270	$2,308	$372	$2,396	$253	$1,029	$85	$44
Months of Cash Left with Oil at $55/bbl from YE 2005 to Threshold[5]	CF Pos.	CF Pos.	4	CF Pos.	41	CF Pos.	88	CF Pos.	4	6

(1) Operating Cash Flow = Net Income + D&A + pension expense; assumes no impact from change in net working capital.
Assumes crude price of $40/bbl in 2006. Incorporates hedge positions.
(2) FRNT is in 2007 March-ending fiscal year, base assumption oil at $40/bbl for calendar 2006.
(3) Assumes no additional noncash (stock of subsidiary) contribution to DB pension plans.
(4) Assumes crude price of $49/bbl in 1Q05 and $45/bbl in 2Q-4Q05. For no debt refinancing scenario in 2006, assumes no debt refinancing in 2005. For debt refinancing scenario in 2006, assumes debt refinancing in 2005.
(5) Chapter 11 risk: operating with cash burn and cash balance is below threshold cash level.

(US$ in millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT
Estimated Unrestricted Cash Concern Level	**$1,500**	**$1,000**	**$1,500**	**$1,100**	**$150**	**$750**	**$100**	**$300**	**$200**	**$75**

As points of reference, we note that AMR achieved its last-minute deal with labor last April with $1.2 billion (7% of LTM sales) in unrestricted cash and equivalents, UAL filed for Chapter 11 on 12/9/02 with $1.3 billion (9% of LTM sales) in unrestricted cash and equivalents (YE 2002), and US Air entered Chapter 11 on 8/11/02 with close to $900 million in cash (3Q02 balance was $900 million) (13% of LTM sales).

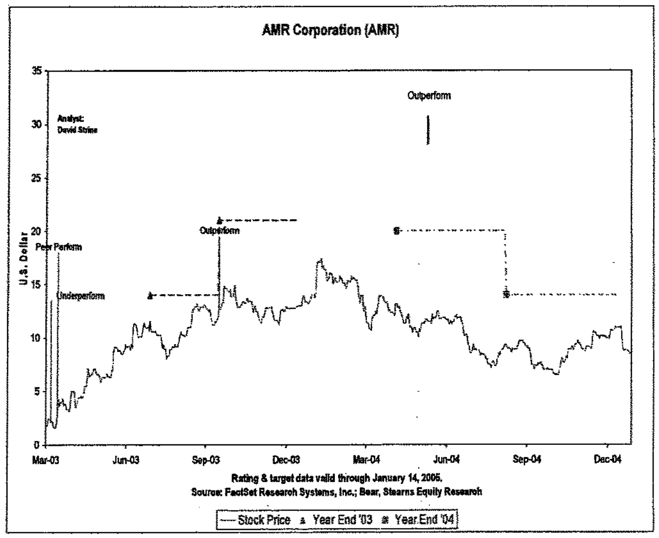
Source: Bear, Stearns & Co. Inc. estimates; company reports; company guidance.

Subject companies under coverage mentioned in this report:
Sector Rating — Market Weight

Alaska Air Group (ALK-29; Outperform)
AMR Corp. (AMR-8.97; Peer Perform)
Continental Airlines (CAL-12; Peer Perform)
Delta Air Lines (DAL-4.33; Peer Perform)
Northwest Airlines (NWAC-6.98; Outperform)

Addendum

Important Disclosures

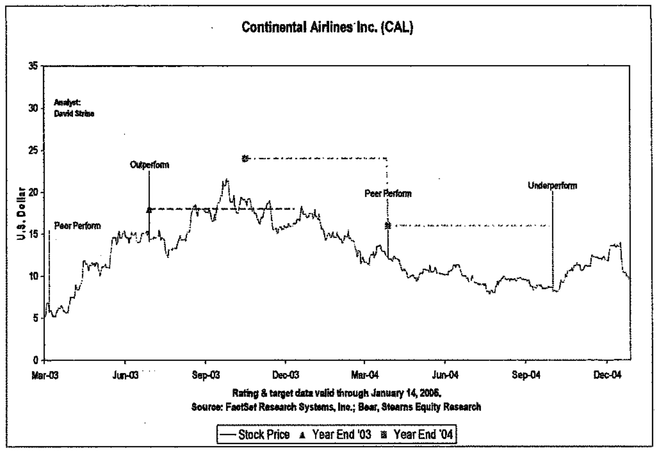


BSC Recommendation History since March 19, 2003 for:
AMR Corporation (AMR) - U.S. Dollar

Date	Stock Price	Rating	Target
**Analyst: David Strine			
24-Mar-03	2.38	UNDERPERFORM	—
01-Apr-03	2.10	PEER PERFORM	—
16-Jul-03	10.56	PEER PERFORM	14.00
03-Oct-03	11.75	OUTPERFORM	21.00
22-Apr-04	13.12	OUTPERFORM	20.00
26-Aug-04	9.42	OUTPERFORM	14.00
20-Oct-04	6.49	PEER PERFORM	—

Addendum

Important Disclosures

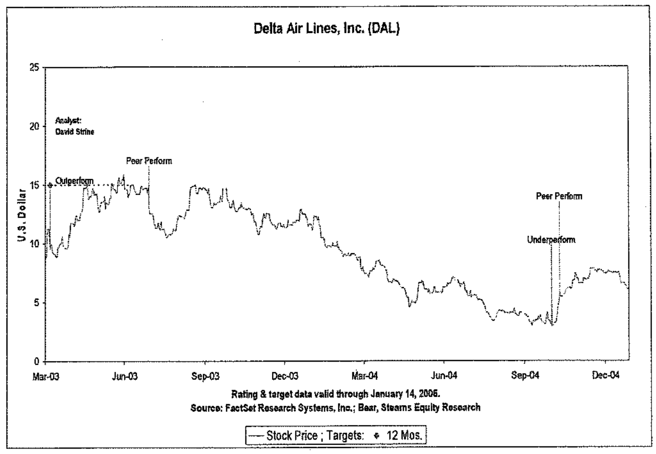


BSC Recommendation History since March 19, 2003 for:
Continental Airlines Inc. (CAL) - U.S. Dollar

Date	Stock Price	Rating	Target
**Analyst: David Strine			
24-Mar-03	6.82	PEER PERFORM	—
17-Jul-03	15.47	OUTPERFORM	18.00
03-Nov-03	19.10	OUTPERFORM	24.00
15-Apr-04	12.36	PEER PERFORM	—
19-Oct-04	8.71	UNDERPERFORM	—
25-Jan-05	9.51	PEER PERFORM	—

Addendum

Important Disclosures

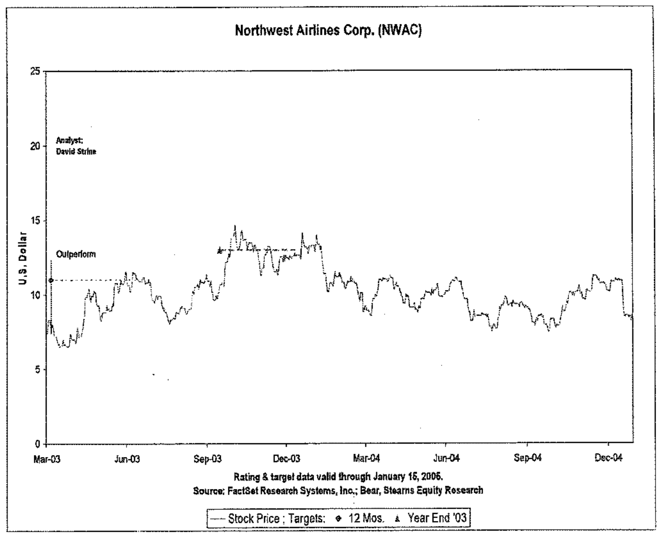


BSC Recommendation History since March 19, 2003 for:
Delta Air Lines, Inc. (DAL) - U.S. Dollar

Date	Stock Price	Rating	Target
**Analyst: David Strine			
24-Mar-03	11.25	OUTPERFORM	15.00
17-Jul-03	14.85	PEER PERFORM	15.00
19-Oct-04	3.11	UNDERPERFORM	---
28-Oct-04	4.94	PEER PERFORM	---

Addendum

Important Disclosures



BSC Recommendation History since March 19, 2003 for:
Northwest Airlines Corp. (NWAC) - U.S. Dollar

Date	Stock Price	Rating	Target
**Analyst: David Strine			
24-Mar-03	8.30	OUTPERFORM	11.00
03-Oct-03	10.16	OUTPERFORM	13.00
10-Mar-05	7.10	OUTPERFORM	11.00

Addendum

Important Disclosures

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Outperform (O) — Stock is projected to outperform analyst's industry coverage universe over the next 12 months.
Peer Perform (P) — Stock is projected to perform approximately in line with analyst's industry coverage universe over the next 12 months.
Underperform (U) — Stock is projected to underperform analyst's industry coverage universe over the next 12 months.

Ratings for Sectors (vs. regional broader market index):
Market Overweight (MO) - Expect the industry to perform better than the primary market index for the region (S&P in the U.S.) over the next 12 months.
Market Weight (MW) - Expect the industry to perform approximately in line with the primary market index for the region (S&P in the U.S.) over the next 12 months.
Market Underweight (MU) - Expect the industry to underperform the primary market index for the region (S&P in the U.S.) over the next 12 months.

Bear, Stearns & Co. ratings distribution as of December 31, 2004
(% rated companies/% banking client in the last 12 months):
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Peer Perform (Neutral): 49.1%/11.1%
Underperform (Sell): 12.7%/6.3%

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David Strine

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STATEMENT OF

CAPTAIN DUANE E. WOERTH, PRESIDENT

AIR LINE PILOTS ASSOCIATION, INTERNATIONAL

BEFORE

THE AVIATION SUBCOMMITTEE

OF

THE TRANSPORTATION AND INFRASTRUCTURE COMMITTEE

UNITED STATES HOUSE OF REPRESENTATIVES

WASHINGTON, DC

June 22, 2005

AIRLINE PENSIONS: AVOIDING FURTHER COLLAPSE

Air Line Pilots Association, International
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Washington, DC 20036
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STATEMENT OF

CAPTAIN DUANE E. WOERTH, PRESIDENT

AIR LINE PILOTS ASSOCIATION, INTERNATIONAL

BEFORE THE AVIATION SUBCOMMITTEE

TRANSPORTATION AND INFRASTRUCTURE COMMITTEE

ON

AIRLINE PENSIONS: AVOIDING FURTHER COLLAPSE

June 22, 2005

Good afternoon. I am Captain Duane Woerth, President of the Air Line Pilots Association, International, which represents 64,000 airline pilots who fly for 41 U.S. and Canadian airlines. On behalf of ALPA, I want to thank the Subcommittee for giving us the opportunity to present our views about the pension funding crisis facing the U.S. airline industry today.

We firmly believe that H.R. 2106, introduced by Representative Tom Price (R-GA) and a bipartisan group of 20 members of the House, and its companion bill in the Senate, S. 861, introduced by Senator Johnny Isakson (R-GA) and Senator Jay Rockefeller (D-WVA), provide the pension funding reforms that we need now to avoid the devastating consequences that distress pension plan terminations wreak on employees, their families and the Pension Benefit Guaranty Corporation.

Pension Crisis Affected by Financial State of U.S. Airline Industry

It is impossible for me to discuss the airline pension funding crisis without starting with the overall financial condition of the domestic airline industry, which remains quite dismal. Our industry has lost over $30 billion in the last four years and is projected to lose at least $5 billion this year. The immediate future does not look much brighter given the volatility in fuel prices and yield performance. Yields continue to deteriorate at an alarming rate, with domestic yields showing no sign of increasing. In fact, domestic yields declined 20% from 2000 to 2004. There is hardly any pricing power in this industry. In the last several weeks, we have seen fuel surcharges take hold. A $2 per barrel swing in jet fuel prices can be offset by a 1% change in unit revenue, yet while fuel was up over $18 a barrel in the first quarter of 2005, unit revenues rose only by 2%. The fuel surcharges may have been successful in offsetting only $4 to $6 of that increased fuel cost.

The outlook remains grim. Recent projections for 2006 are for industry losses of over $1 billion, and that's only if fuel averages $45 a barrel. Every $1 per barrel increase in the price of oil translates into an additional $450 million loss in passenger industry pretax profits and $1 billion in additional losses for the global airlines. IATA, which had been expecting a break-even year for the global airline industry, is now forecasting over $6 billion in losses for 2005.

For the airline industry, the economic factors are compounded by the lingering 9/11 effect: the use of commercial aircraft as weapons of mass destruction depressed the economy and reduced the number of passengers we fly, at the same time security taxes were added to our ticket prices and oil skyrocketed to historic market highs. While traffic and capacity are now back to pre-9/11 levels, we continue to be subjected to burdensome taxes and security fees and now the administration wants to impose another $1.5 billion worth of taxes. The U.S. airlines are already expected to pay the government and airports $15 billion in taxes and fees this year.

When we add to this grim financial condition the factors of historically low interest rates and poor stock market returns, we have a "perfect storm" for the pension woes we currently face. As a result of this witches' brew, we are on guard for even more pension plan terminations and their attendant devastating consequences, potentially affecting hundreds of thousands of workers and their families. But despite this stark reality, ALPA believes these drastic results can be avoided with creativity and foresight – and appropriate legislative reforms, specifically, the reforms set forth in H.R. 2106.

Pension Funding Crisis Created by the "Perfect Storm"

Much has been said and written about the "perfect storm" that has undermined the funding of private defined benefit plans in America. The two key elements of the "perfect storm" are historically low interest rates and poor returns in the stock market. Low interest rates impact pension funding because, as interest rates decline, the value of a pension plan's liabilities increases. And when stock market returns move downward, the value of the plan's assets decreases.

In a perfect world, a plan's funding ratio would always equal 100%, meaning that the plan's assets exactly equal the plan's liabilities. But with historically low interest rates driving plan liabilities up, and investment performance driving plan assets down, the "perfect storm" has set the stage for funding disaster. The more the plan's liabilities exceed the plan's assets; the worse off is the plan's funded status.

Contribution Volatility Created by "Deficit Reduction Contribution" Rules

If a plan's liabilities exceed its assets, ERISA's *regular* funding rules for pension plans were designed, in general, to allow employers to make up that gap with more or less level contributions over extended periods of time. But when a plan's funding gap drops down to a certain level, a *special* funding rule kicks in, requiring the employer to make much larger contributions over a much shorter period of time. This special contribution, known as a "deficit reduction contribution," makes it especially difficult for the employer to close the widening gap between assets and liabilities.

Logically, since a pension plan is a long-term proposition, it should be funded over the long term. This would require reasonably predictable, level, periodic contributions, similar to the way homeowners expect to pay their mortgage. But when a deficit reduction contribution is required, the pattern of required funding shifts in the opposite direction. That is, required funding amounts become extremely volatile, with extraordinarily large contributions required over very brief periods of time – the exact opposite of predictable, periodic contributions over a reasonably longer period of time.

A deficit reduction contribution is always required when a pension plan's funded ratio for the year falls below 80%, and is often required when the plan's funded ratio falls below 90%. Deficit reduction contributions are designed to bring the plan back to the 90% funded level, and while that is a laudable goal, the time the employer is allowed to get there is only three to five years. This is like asking homeowners to pay off their 30-year house mortgage as if it were a car loan – over only three to five years – far too short a time to meet far too large an obligation.

Because of this short time horizon, the contributions an employer must make to a plan when the plan is subject to the special deficit reduction contribution rule are often enormous, and can end up being unaffordable, especially when compared to the amount that would have been required if only the regular funding rules applied. The deficit reduction contribution rule was added to the funding laws in 1987 and strengthened in 1994, in an effort to help prevent underfunded plans from being terminated and their liabilities dumped on the PBGC. Although this is a desirable goal in theory, the strategy to achieve it backfires in the real world if the employer is unable to afford the deficit reduction contribution. In that case, the employer, now in bankruptcy, is forced to terminate the underfunded plan and dump liabilities on the PBGC anyway. No one wins, and the participant certainly loses.

Pension Plans in Bankruptcy

The scenario just discussed is precisely what happened in US Airways' first bankruptcy with respect to the pilots' pension plan. The pilots' plan was the only pension plan of the four maintained by US Airways that was terminated at that time. The Company was unable to emerge from bankruptcy without a distress termination of the pilots' pension plan, due in large part to the deficit reduction contributions projected to be required over the next few years – and a significant portion of that burden was transferred to the PBGC, precisely opposite to the law's intent.

Sadly enough, the US Airways pilots' plan had been soundly funded just *two years* before the Company filed for bankruptcy. The plan went from being over 100% funded in 2000 to only 74% funded by 2002 – due to the "perfect storm" and the funding rules in place which allowed the corporation to bank payment credits due to high pension funding levels. Once the funding level decreased, the requirement for deficit reduction contributions kicked in. However, the Company could not afford to make those payments and emerge from bankruptcy with financing and a viable reorganization plan. As a result, the pilots acquiesced to the Company's "distress termination" of their pension plan. Although a new defined contribution plan was established, it could not replace the benefits active pilots lost under the prior program and it provided nothing to restore what retired pilots had lost.

All told, the active and retired pilots of US Airways lost $1.9 billion in accrued benefits that were not funded by the plan and were not insured by the PBGC. This loss amounts to just over *one-half* of the $3.7 billion in total benefits that pilots had *already earned* as of the time the plan terminated.

With US Airways' second bankruptcy, the three pension plans covering the rest of US Airways' employees have now been terminated and taken over by the PBGC. PBGC has estimated that the assets of these three plans cover only 40% of liabilities. As a result, PBGC has taken on another $2.3 billion in unfunded liabilities for these plans.

We are now witness to the same scenario being played out in the current bankruptcy of United Airlines. All four of United's defined benefit plans are being terminated and taken over by the PBGC. Although the benefits employees and retirees have earned under these plans total approximately $16.8 billion, the plans' assets total only about $7 billion, leaving $9.8 billion in unfunded liabilities. PBGC estimates that it will be on the hook for approximately $6.6 billion of the unfunded amount.

In terms of retirement security, the results for United's employees are devastating. In total, they will lose more than *$3 billion* in accrued benefits – benefits that are neither funded by the plans nor insured by the PBGC. United's pilots alone will bear fully one-half of this amount, losing *$1.5 billion* in accrued benefits. *On an individual basis the situation is dire, with many pilots completely losing more than 60% of the retirement benefits they had already earned.*

Freezing Plans to Reduce Pension Costs

ALPA's pilots and leaders have not stood idly by and watched as these events threatening their pensions have unfolded. Since the beginning of this pension funding crisis, the pilots and our airlines have taken active and creative steps to explore all available means of reducing or delaying pension costs, within the bounds of current law.

Of course, there is only so much the parties can do through collective bargaining. Most significantly, the parties cannot agree to reduce the benefits that employees have already earned to date under a pension plan, pursuant to the "anti-cutback rule." Since accrued benefits cannot be reduced, the most that ALPA and the airlines can do in collective bargaining, in order to reduce future plan costs, is to agree on changes that eliminate future accruals under the plan. Also known as "freezing" the plan, this is the most drastic step that may be taken to reduce future plan costs, short of a distress plan termination.

Over the past eight months, the pilots of Delta Airlines and Continental Airlines have agreed to freeze their defined benefit plans, thereby eliminating any future accruals under those plans. They have done this with the goal of lowering their airline's costs, which in turn will increase the chances of their airline staying out of bankruptcy and preserving benefits accrued under the pension plans. Pilots at several other airlines are currently considering whether to freeze their defined benefit plans, also.

<u>Funding Even a Frozen Plan Can Be Too Burdensome</u>

Even though a total plan freeze provides the largest possible cost savings to an employer, the employer must *continue to fund the benefits that were earned prior to the freeze.* Funding of accrued benefits under a frozen plan can be extremely burdensome, however, under the deficit reduction contribution rules.

For illustration, let me review a situation involving one of the legacy airlines, one that we believe is typical of the funding results achieved by freezing the defined benefit plan. This airline compared the amount of contributions that would be required over the next 15 years if the plan remained unchanged, to the amount that would be required if the plan were frozen. Over the 15-year period, the contributions required if the plan were frozen would be *less than 1/3* of the contributions required if the plan were not frozen. These are substantial savings, to be sure. But the curious thing is that, due to the deficit reduction contribution rules, fully *100%* of these lower contributions would be due over the next five years only, with *zero* contributions required in the following 10 years, hardly short-term relief.

We believe this example stands as strong evidence that the current funding rules, with the poorly designed deficit funding contribution requirement and resulting volatility of contributions, are simply illogical and do not function as intended.

Pension Funding Equity Act of 2004

In April 2004, Congress passed the Pension Funding Equity Act. In addition to provisions applicable to all defined benefit plans, PFEA contains a special rule for certain defined benefit plans maintained by commercial passenger airlines. In general, the Act granted deferral, for two years only (2004 and 2005 for most airlines), of a portion of the deficit reduction contribution otherwise due for those two years. We understand that most, if not all, of the eligible airlines have elected to use the special rule for their eligible plans. As you know, the temporary nature of the special rule has the effect of exacerbating the plans' funding requirements in 2006 and beyond. We appreciate the fact that Congress was willing to work with us last year to address this problem; but without further reforms, the increased deficit reduction contributions required for 2006 and beyond will be even more costly.

The Solution – H.R. 2106

The devastating consequences of more pension plan terminations in the airline industry can be avoided, if appropriate legislation is enacted now. We firmly believe that H.R. 2106 provides the required reforms.

We believe the current pension funding crisis is only temporary. Given sufficient time, we believe that interest rates will rise, stock market performance will improve, and airline profitability will return. Sound retirement policy should not allow an employer to break its pension promise to employees, just because of negative economic and financial conditions expected to last only a few short years. This is especially so when such negative conditions are viewed in the context of a pension plan, the duration of which is measured in decades.

Our two-pronged solution is to allow airlines to amortize their pension plans' unfunded liabilities over a longer term and to measure their plans' liabilities using realistic interest rate assumptions determined by the plans' actuaries. The legislation now pending would accomplish this much-needed reform.

We believe that allowing long-term amortization of the present funding gap creates a situation in which all stakeholders win.

First and foremost, it is a win for workers, who will have a greater likelihood of actually receiving the benefits they have already earned under their pension plans. After all, over the course of their careers, employees have given up direct wage compensation in exchange for the promise of deferred retirement benefits.

Secondly, it is a win for the PBGC. Making the reforms available will greatly reduce the chances of more distress plan terminations. A plan that is allowed to become well-funded over time will never be dropped on the PBGC's (and taxpayers') doorstep. But if such a distress plan termination should later occur, the legislation provides the PBGC a significant limitation on its possible future liability. For a plan that elects coverage under the new rules and later undergoes a distress termination, the PBGC's guarantees are capped at the limits in place during the first year the plan was covered by the new rules.

Finally, it's a win for the airline industry and the traveling public. Of course, it will allow airlines to deliver the benefits they promised to employees. But just as importantly, it will allow the airlines to better manage their cash flow and prepare feasible business plans without being sabotaged by unpredictable deficit reduction contributions. A feasible business plan will, in turn, unlock the door to long-term capital financing of the airlines' business needs and endeavors, and should, in the case of some legacy carriers, help them avoid bankruptcy altogether.

Under current law, the only way an airline can avoid burdensome pension costs is by entering bankruptcy and terminating the plans. But if more and more airlines choose to shed their pension liabilities in bankruptcy, it sets up the potential for the "domino effect," in which all the other legacy carriers are incentivized, or even forced, to file bankruptcy, in order to achieve the same cost savings and "level the playing field." We believe that providing relief from the deficit reduction contribution rules will go a long way toward removing the pension plan termination incentive to enter bankruptcy, and will, as a result, help prevent further bankruptcies in the U.S. airline industry.

Allowing airlines additional time to fund employees' accrued benefits will also give the parties time to step back, review and in some cases completely alter the design of their retirement program – all without the threat of a distress plan termination hanging over their heads. Given the sufficient breathing room made possible by longer amortization of the defined benefit plan liabilities, airlines and employees can craft creative solutions that may provide secure alternatives to pure defined benefit plans. Each airline and employee group must create an individual solution to their individual pension challenge. For some groups, but by no means all, the solution may lie in gradually shifting away from excessive reliance on defined benefit plans as the primary sources of retirement benefits, either by replacing them, or by devising combination plans with a larger defined contribution plan component.

There is one separate but related issue that I must mention, because it is specific to the airline pilot profession. By FAA regulation, we *must* retire at age 60. Therefore, a pilot's "normal retirement age" under our pension plans is defined as age 60. That is the age when a pilot may retire and receive a full, unreduced pension. However, in the case of a pension plan undergoing a distress termination, the PBGC determines its insurance guarantees by applying age 65 as the normal retirement age. As a result, benefits that begin at age 60 are treated as "early retirement" benefits and the PBGC's guarantees for those benefits are reduced. The PBGC's guarantees for benefits beginning at age 60 is only 65% of the amount it guarantees for benefits beginning at age 65. Therefore, we support S. 685, introduced by Senator Daniel Akaka (D-HI) on March 17, 2005. The "PBGC Pilots Equitable Treatment Act" proposed in S. 685 would apply the PBGC's normal retirement age guarantee limit to pilots at their normal retirement age – age 60.

Summary

In summary, we believe that the simple solution of H.R. 2106 to allow long-term funding of pension plan liabilities will allow the airline industry the time it needs to undertake a strategic, deliberate approach that provides employees with a secure retirement, keeps defined benefit plans out of the hands of the PBGC, and maintains healthy airlines. Again Mr. Chairman, I appreciate this opportunity to appear before you, and I would be happy to answer any questions the Subcommittee may have.

TESTIMONY OF DONALD SCOTT YOHE

Senior Vice President,
Government Affairs

DELTA AIR LINES

BEFORE A HEARING OF THE

COMMITTEE ON TRANSPORTATION & INFRASTRUCTURE, THE AVIATION SUBCOMMITTEE

U.S. HOUSE OF REPRESENTATIVES

On

Airline Pensions: Avoiding Further Collapse

June 22, 2005

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1275 K Street NW
Suite 1200
Washington, DC 20005

Testimony of Donald Scott Yohe
Senior Vice President, Government Affairs
Delta Air Lines

Before a Hearing of The Committee on Transportation & Infrastructure,
The Aviation Subcommittee
U.S. House of Representatives

Washington, DC
June 22, 2005

On behalf of the 80,000 active and retired employees of Delta Air Lines and their families, we welcome the opportunity to provide our views on the crisis confronting airline industry pension plans. The current pension funding rules are not workable in the current airline environment and they need to be fixed. Those rules require funding contributions on a schedule that can be volatile and unmanageable, with the most significant contributions often occurring at precisely the time a company can least afford it. For an airline like ours that is transforming itself -- thanks in large part to the sacrifice and hard work of Delta people -- to survive in the rapidly evolving world of commercial air transportation, the pension funding quagmire creates a potentially insurmountable barrier to our ability to restructure successfully outside of court supervision.

Congress must act swiftly to a set of rules that allow Delta and possibly other traditional national network carriers to pay their employees the retirement benefits they have earned over many years of work while at the same time providing the Pension Benefit Guaranty Corporation (PBGC) a greater margin of protection from unexpected liabilities. Such liabilities have arisen recently as competitive pressures reshaping our industry have caused some airlines to enter bankruptcy, then to transfer their very large pension obligations to the PBGC as part of their effort to exit the process. We are supporting legislation H.R. 2106 that provides a narrow, targeted solution to the unique pension situation facing some of our nation's airlines as they work hard to transform themselves outside of bankruptcy.

Delta stands ready to meet the challenges of a permanently and fundamentally changed aviation marketplace. We have a business strategy that sets us firmly on course for long-term viability and we have accomplished much over the last few years. However, one of the two biggest factors that will determine whether we can successfully complete our transformation outside of bankruptcy is the pension cloud now hanging over our company and many other traditional legacy carriers.

In 2004, Congress provided airlines with temporary relief from the current law "deficit reduction contribution" requirements. These difficult requirements threatened to exhaust our airline's liquidity reserves by forcing large, immediate contributions to our pension plans when we could least afford it. Congress recognized that bankruptcies would have a greater adverse impact on employees and could result in the transfer of unfunded pension benefit obligations to the PBGC. Because everyone understood that a comprehensive solution was needed, the 2004 funding relief for airlines was intended to be only a temporary, stopgap measure.

The Employee Pension Preservation and Taxpayer Protection Act introduced by Congressman Tom Price with 21 cosponsors[1], provides a framework that balances the need for reasonable and affordable pension funding requirements for airlines, while still protecting the PBGC. Under this legislation, airlines that limit their pension liabilities by freezing pension benefits (or agreeing to immediately fund any future benefit accruals) and freezing growth in the PBGC guarantee, would still be required to fund their unfunded pension liabilities. However, they would be allowed to do so on an affordable schedule over the next 25 years using stable, long-term assumptions. The legislation would give airlines a greater chance to transition to a less volatile pension plan structure in a way that fully honors the benefits earned by airline workers over many years.

H.R. 2106 provides airlines the time to complete the transformation required to survive in today's economy in a responsible fashion that protects employees, the government and our national economy. Let me emphasize at the outset that the bill does not involve any kind of a Federal bailout for Delta or any of the other airlines. Delta is not seeking to avoid its obligations to our employees; what we seek is a solution that helps us to honor them. In contrast, two carriers now in bankruptcy -- United and US Airways -- have received court recognition of the immense competitive pressure to eliminate pension obligations in order to attract financing. The termination of those pension plans – which involves shifting of massive liabilities to the PBGC – might be characterized as a bailout but H.R. 2106 will simply allow airlines to meet their pension plan obligations.

DELTA'S LONG ROAD TO RECOVERY

The nation's airlines have been hit by a series of crises, starting with September 11 and its aftermath to the latest plague on our industry – record high fuel costs. Since the year 2000, the nation's airlines have lost close to $33 billion – Delta alone has lost $8.5 billion and now has over $20 billion in long term debt. Several carriers, including two that represent over 20 percent of the U.S. airline market, are operating in bankruptcy. With newer low-cost carriers now claiming 30 percent of the domestic travel market, it is clear that the traditional legacy carriers must bring their operating costs into line with these competitors -- competitors that do not provide defined benefit pension plans. The traditional national network airlines understand that we have no choice but to reduce costs or cease to exist.

Delta began making tough but necessary changes in 2002, and by the end of 2004, we had achieved $2.3 billion in annual revenue and cost benefits. However, appreciating that we were not in a cyclical downturn, but rather in a permanently and fundamentally changed aviation

[1] Rep Baker, Richard H. [LA-6]; Rep Barrow, John [GA-12; Rep Chabot, Steve [OH-1]; Rep Davis, Geoff [KY-4] -; Rep Deal, Nathan [GA-10]; Rep English, Phil [PA-3] -; Rep Gingrey, Phil [GA-11]; Rep Hostettler, John N. [IN-8; Rep Kingston, Jack [GA-1; Rep Lewis, John [GA-5; Rep Linder, John [GA-7]; Rep Manzullo, Donald A. [IL-16; Rep Marchant, Kenny [TX-24]; Rep Marshall, Jim [GA-3]; Rep Norwood, Charlie [GA-9]; Rep Platts, Todd Russell [PA-19]; Rep Ramstad, Jim [MN-3]; Rep Schwarz, John J.H. "Joe" [MI-7]; Rep Scott, David [GA-13]; Rep Simmons, Rob [CT-2]; Rep Westmoreland, Lynn A. [GA-8]

marketplace – due, in part, to changed customer preferences, low-cost carriers and online fare shopping – we launched a new strategic plan in September 2004 that focuses on winning back customer trust and achieving viability. We are on our way to doing both. Our goals are to improve the customers' travel experience and also build on the $2.3 billion already achieved to reach a total of $5 billion in annual revenue and cost improvements by 2006, as compared to 2002. In the face of harsh financial realities and increasingly fierce competition, the people of Delta Air Lines are proving their mettle as we transform our company into the right airline for a new era. While a long, tough road still lies ahead, we already have made remarkable progress. We have now targeted all components of that $5 billion goal. A crucial element of the savings has been the shared sacrifice of all of Delta's employees, including, regrettably, the loss of jobs. Today, Delta's workforce is about 56,000 – a decrease of 23,000 employees since September 11, 2001. The job reductions have been spread across the entire company, with our executive ranks trimmed by 25 percent during that period. Delta now has the lowest ratio of total Officer and Director level positions to total employees among the six largest airlines.

In 2001, Delta was a leader in compensation in our industry. Since that time, our people have taken the painful steps necessary to adjust our pay and benefits going forward to levels more realistic for the changed environment in which we operate. Last fall, Delta pilots approved a contract providing a crucial $1 billion in annual savings including a one third pay cut for five years with no snap back provisions. Delta's other employees also have experienced their fair share of pay cuts – with a company wide pay cut of 10 percent in January – following 5 years with no general increase to our pay plans. As of April 1, 2005, Delta's frontline employee groups rank in the bottom tier of the largest airlines in top of scale pay rates. In 2004, Delta's top five executives ranked third to last in total cash compensation among major carriers, including Southwest, AirTran and Jet Blue.

Part of our plan has also been to trim benefits across the board. We have achieved substantial savings in our health care benefits – totaling more than $300 million over the 2003-2005 period. Premiums for family coverage for Delta employees increased from zero in 2002 to approximately $2400 per year in 2005.

We have also reduced future pension benefit accruals for both pilots and non pilots in order to proactively rein in our future expenses for retirement benefits. In 2003, Delta converted its traditional defined benefit final average earnings plan for non-pilots to a cash balance plan, which resulted in significant pension cost reduction. Unlike many companies who have undertaken such a transition, however, we did not ignore the interests of our employees in this conversion. To address the concerns of long term employees who are close to retirement, Delta is providing a seven year transition period during which employees will earn the better of the two benefits. It is important to both Delta and its employees that H.R. 2106 preserves Delta's ability to maintain this transition period.

As part of the pilot negotiations concluded last year, Delta's pilots agreed to freeze service accrual under their defined benefit plan and implement a much less costly defined contribution plan. This freeze will also result in significant annual savings for Delta. Because of the significant pay reductions agreed to by the pilots, there is minimal benefit accrual expected in this plan for several years. Once again however, it is important to both Delta and its pilots that H.R. 2106 preserves this "soft freeze" approach agreed to in good faith by both parties.

In addition to these steps, we have reduced other benefits such as paid vacation and sick leaves with the net effect that Delta employees are working longer and harder for much less – all in an effort to regain a competitive position in a marketplace that has fundamentally changed.

We have also attained significant savings and debt restructuring assistance from vendors, suppliers, aircraft lessors, debt holders and others.

These actions have already made our airline fully one-third more productive and cost-effective, without diminishing Delta's ability to generate revenue. At the same time, Delta has achieved high levels of customer satisfaction despite the sometimes massive changes occurring throughout our operations. Delta was ranked among the top three airlines by J.D. Power and Associates 2005 Airline Satisfaction study and second in customer satisfaction in a recent Department of Transportation report.

Delta has made great progress in improving our cost structure -- and those accomplishments have been possible only with the support of Delta people at every level, throughout the company. Despite this extraordinary effort, however, our company's most recent financial results show continued high losses. A primary cause of those disappointing results is skyrocketing fuel prices – which have jumped by as much as 30 percent since the first of the year. Fuel is Delta's second highest expense after salary and benefits, representing nearly 20% of total operating costs. With every one cent increase in average jet fuel cost per gallon adding $25 million to Delta's annual costs, higher fares can offset only a fraction of the impact of the increased fuel costs. If you factor out the high fuel costs, a dramatically different financial picture emerges at Delta. Excluding fuel and special items, Delta has succeeded in reducing unit costs for mainline operations by almost 13 percent during the last quarter when compared to the previous year.

The low-cost carriers' basic advantage is just that – low costs. While the going is rough and often painful, Delta and other legacy carriers are tenaciously pursuing their own cost reductions and we show no signs of stopping. We can and will continue to work to control our costs – and, as I have said – the employees of Delta have stepped up to make cost control a reality. When we finally reach our desired cost structures, we will be a formidable competitor, but we cannot achieve that end if the problems and uncertainty surrounding our pension plans are not resolved.

THE PENSION CLOUD

Without changes in the pension funding rules, all of our efforts to transform ourselves out of court could be to no avail. The single biggest uncertainty that may well determine whether or not Delta can successfully restructure outside of bankruptcy court is the pension cloud that hangs over the company.

At Delta, we maintain two primary defined benefit pension plans – the Pilots Retirement Plan and the Delta Retirement Plan for our non-pilot employees and these plans have historically been well funded. We measure the ERISA funded status of these plans as of July 1 of each year. As recently as July 1, 2001, both these plans had a funded status ratio of 100% or better for ERISA current liability purposes. Largely as a result of a short period of negative and below expected investment returns and a steady fall in the interest rate used for measuring liabilities, however, the funded status of our defined benefit plans has taken a turn for the worse. The result is that the funded status for both plans declined to about 75% for current liability purposes at July 1, 2004, the most recent ERISA funding measurement date. Thus, Delta's qualified defined benefit pensions, which had no current liability under-funding as of July 1, 2001, are under-funded by approximately $2.6 billion dollars on a current liability basis as of July 1, 2004. This increase in liability did not result from failing to make contributions to the plans. We have not sought a funding waiver and have always made required contributions. For 2005, the estimated funding for those plans is about $275 million, most of which has already been paid. Without changes in the funding rules, we project that we will be required to contribute a total of $2.6 billion to our qualified defined benefit pension plans from 2006 to 2008. Simply put, we cannot afford a cash crunch of this magnitude, certainly not in the current economic environment confronting airlines, and no amount of sacrifice of future compensation can solve this problem since the vast majority of this funding relates to benefits accrued in the past.

Now, some have asked why we didn't put more money in the pension trusts in the late 1990s when we were making money. That is a good question, and the simple answer is that the pension funding rules discouraged additional funding of plans that were determined to be fully funded. Pension funding rules are designed both to keep plans funded, by requiring a minimum annual funding, and also to keep companies from avoiding income tax by putting excess cash into plans on a tax-favored basis. The determination of minimum and maximum tax deductible funding is completed once per year and for the late '90s, the minimum required contribution as well as the maximum deductible contribution for Delta's plans were both zero.

Although the House and Education and Workforce Committee Chairman Boehner has proposed various reforms to the pension funding rules, including lower required contributions for some plans, these proposals will not be sufficient to solve the unique and immediate problems for the airlines. Indeed, some of these proposals could push airlines into bankruptcy and accelerate the transfer of unfunded pension liabilities to the PBGC.

As recent events amply demonstrate, transferring such liabilities to the PBGC has a number of onerous results.

- Employees and retirees can lose benefits they have already earned because PBGC's insurance program covers only basic pension benefits and is subject to annual dollar caps.
- In a bankruptcy scenario, airline employees (and employees of companies dependent on airlines) are likely to suffer further reductions in pay, benefits and jobs and airline creditors and investors will inevitably lose money.
- Each new airline bankruptcy exacerbates the risk of a downward spiral where airlines race to shed their pension obligations because courts have approved their competitors doing so.

- A further string of bankruptcies among the national network carriers – and the resulting disruption and chaos that would ensue – will hurt the economy and weaken our vital air transportation network, especially service to smaller cities which are generally not served by low-cost carriers.

- Finally, transferring further liabilities to PBGC will, at a minimum, lead to higher PBGC premiums on those employers that voluntarily maintain plans (potentially undermining the entire defined benefit system) and could ultimately lead to a taxpayer bailout of the agency.

Absent an appropriate legislative resolution, economic reality and competitive pressures are likely to force other major airlines with defined benefit pensions to follow the bankruptcy path that United and US Airways have recently followed. We at Delta do <u>not</u> want that result and are working very hard to avoid it. It is not what is best for our company, for our employees, for our customers, for our shareholders or for our country.

A SOUND AND SENSIBLE SOLUTION, (H.R. 2106)

We are at a crossroads. We cannot control the world we live in, but we must adapt to it. There are two paths Delta and other traditional carriers can follow. The first path some would paint as the easy road for corporate executives to take – file bankruptcy, dump pension liabilities on the PBGC and emerge a nimbler competitor on the other side. That view ignores the many painful realities that bankruptcy entails, but the fact is that bankruptcy courts have recognized that obtaining additional financing necessary to exit the process successfully is nearly impossible when legacy pension funding costs have not been dealt with. Court actions in the United and US Airways cases have further altered the competitive landscape in a profound way by helping those carriers rid themselves of billions in liabilities, which positions them to be much more effective competitors.

The second path is to evolve and adapt to the new world in which airlines must survive. Delta is committed to making the tough choices that will make it possible for our company to survive. The path we want to follow involves honoring the commitments we have made to our employees and retirees over the 75 years that Delta has been in existence. Our ability to follow this path is directly linked to Congressional action to give us pension funding rules that will enable us to resolve this crisis responsibly.

H.R. 2106, the Price bill, and its Senate companion – S. 861 – provide the type of change in pension law that is needed to allow airlines to take the right path. The theory of the bill is quite simple. When an airline commits to freeze a plan or immediately pay for any newly accrued benefits and institutes protection for the PBGC, the government will not require deficit reduction contributions to be so large that they may have the counterproductive effect of driving the airline into bankruptcy. Under this legislation, airlines that freeze pension accruals would still be required to fund the existing unfunded pension liabilities, but would be allowed to do so under a more affordable schedule over the next 25 years using stable, long-term assumptions. Under the bill, the airlines would continue to make sizeable contributions each year to reduce their otherwise frozen unfunded liability, thus reducing the potential future liability for the PBGC. The goal is to establish a payment schedule for the unfunded liability that is both more affordable and practical -- properly balancing the interests of four stakeholders – employees, the federal government, the companies and the traveling public.

A number of strict requirements -- beyond the required freeze -- would be imposed on airlines that choose this approach – all designed to protect the PBGC. For example, any benefit increases above the frozen level would have to be funded immediately and no successor defined benefit plan would be permitted. In addition, the PBGC's guaranteed level of benefits would be limited to the amount the PBGC would have guaranteed had the plan terminated instead of freezing. In other words, the PBGC monthly benefit guarantee would not increase beyond the level in effect when the plan froze.

The approach taken in H.R. 2106 (and S.861, a Senate companion bill) has a number of advantages for employees, the federal government and the parties that finance the PBGC, and it decreases the likelihood of PBGC insolvency.

- **For Employees and Retirees.** Employees benefit because they will receive the full benefits they have accrued prior to the freeze rather than often seeing their benefits reduced if liabilities were transferred to the PBGC. Moreover, finding a solution to the airlines' current pension crisis means that airlines are more likely to return to economic health (by restructuring outside of bankruptcy), preserve jobs and fund their own pension commitments rather than relying upon the PBGC to do so.

- **For the Financial Backers of the PBGC.** The PBGC and those companies paying PBGC premiums benefit because the approach in H.R. 2106 provides airlines with a way to maintain their pension programs and continue to fund their pension benefits and pay PBGC premiums without having to resort to shifting liabilities to the PBGC. Just as important, addressing the airline pension problem significantly decreases the likelihood of the need for a taxpayer bailout of the PBGC. Even if an airline electing to use the provisions of H.R. 2106 should later falter, the PBGC (and the taxpayers) should be better off because PBGC's benefit guarantees are fixed at the time of the pension freeze, airlines will have made intervening contributions to close their pension funding gaps, and any subsequent benefit accruals will have been immediately 100 percent funded.

- **For the Traveling Public and the Economy.** The traveling public which relies on our nation's air transportation system for business and personal travel and as the engine of our economy would benefit from a stable, healthy, competitive airline industry which includes the network carriers who provide the vital link to and from small cities as well as an important source of jobs.

- **For Delta and Other Major Network Airlines.** Once the pension funding schedule is based on a more manageable, affordable schedule, the nation's carriers would be able to honor employees' already hard-earned pension benefits and, at the same time, continue to pursue, outside of court supervision, the transformation plans now underway that are essential for survival in the new aviation marketplace.

Let me emphasize once again that the path we propose does not involve Federal subsidies for Delta. To the contrary, we believe it is the other path – the one that others have been forced to follow – that involves a form of subsidy by relying on the PBGC to fulfill benefit promises that the bankrupt company cannot. We think the path we want to take is a better path -- better for the PBGC, better for our employees, better for our customers, better for the overall air transportation system and better for the economy as a whole.

ACTION IS NEEDED NOW

Congressional help is required to follow that better path. Existing pension rules require airlines to make huge contributions at a time when we can least afford it. In order to have a much greater chance to transform ourselves outside of bankruptcy, the existing rules must be changed. As they are today and as they would be under the Administration's proposals, pension funding rules only push us closer to following in the footsteps of United and US Airways – and we have seen where the realities of the marketplace lead when that happens.

To some extent, legacy airlines are responsible for the situation we now face – not having adequately anticipated the impact of low-cost carriers or internet fare shopping. However, the problems faced by the airline industry are clearly not entirely of our own making. No one could have anticipated the attacks of September 11, 2001 or its aftermath. We could not have anticipated fuel costs rising to unprecedented levels. We could not have anticipated a string of our major competitors marching into bankruptcy court and shedding billions of dollars of pension obligations and potentially emerging from bankruptcy free of those liabilities to compete with us.

Our industry has fundamentally and structurally changed and we need the help of Congress to walk the path that makes sense – for all our stakeholders. Excess capacity, fuel prices, the economy, bankruptcy developments, possible sales of assets or other actions, plus a hundred more possibilities, all could create long chains of actions and reactions within the airline industry. But if we can know that our future pension funding obligations will be reasonable and affordable, then we will have the opportunity to compete with discount carriers (and with United and US Airways) on a more level playing field, while also having the chance to provide the pension benefits our employees and retirees have earned over their careers.

CONCLUSION

The perilous issues facing our industry, including those I've just reviewed, matter not only to airlines and airline employees, but also to the public who depends upon them. The U.S. air transportation system provides a vital service for businesses and other organizations as well as families and friends across our nation.

It is clear that airlines must transform in order to survive in today's economy. Delta has embraced that change. With prompt adoption of S. 861, this can be done in a responsible fashion that protects employees, the government and our national economy. The alternative may be an industry in continued distress and a wholesale shift of airline pension liabilities to the PBGC.

Mr. Chairman and members of the Committee, we thank you for the opportunity to present our views. We look forward to working with Congress on a resolution of the pension funding challenges facing our nation's airlines.

WRITTEN STATEMENT FOR THE RECORD REGARDING

"AIRLINE PENSIONS: AVOIDING FURTHER COLLAPSE"

SUBMITTED BY

AIRLINE PILOTS AGAINST AGE DISCRIMINATION

BEFORE THE

U. S. HOUSE COMMITTEE on TRANSPORTATION AND INFRASTRUCTURE

JUNE 22, 2005

Introduction

Airline pilots from carriers with terminated, or threatened, pensions find themselves in the untenable position of forced retirement at age 60 with no Social Security income, no MediCare, and substantially reduced PGBC income. To remain competitive airlines will need to replace pensions with more affordable retirement savings plans. Allowing pilots the right to work until they reach their Social Security retirement age offers the pilots, and their carriers, the flexibility to transition from defined benefit plans to defined contribution plans.

Airline Pilots Against Age Discrimination (APAAD) represents thousands of active and retired commercial airline pilots and their families, from many airlines, who seek change to the FAA's Age 60 Rule. The history, statistics, and studies that have followed this Rule throughout its existence have clearly shown that safety is not enhanced by a blanket age Rule. We advocate change that will allow experienced, healthy, qualified airline pilots to continue their careers beyond their 60th birthday.

The Economic Predicament of the Airline Pilot

APAAD membership has soared during the past few years with an influx of airline pilots that are faced with declining incomes, pensions, benefits, and job security. A recent survey completed by the Air Line Pilots Association (ALPA) on the subject of pilot retirement at age 60 has been represented as demonstrating that a majority of airline pilots wish to retain the Age 60 Rule. However, the underlying findings show that the discussion remains economic and these findings are somewhat misleading.

The demographics of this survey reveal younger pilots opposed to older pilots, first officers opposed to captains, and pilots at large airlines with pensions opposed to pilots at other airlines. Only 8.5% of respondents stated that safety is their primary concern, the remainder of respondents expressed concerns of their economic uncertainty. Many of our members are also members with ALPA and they have joined APAAD to have a collective voice in the eventual solution to eroding airline employee benefits, wages, and working rules.

Two years ago the pilots at United Airlines and US Airways would have supported a forced retirement policy at age 60. Today, many new members of APAAD come from the ranks of these two airlines. In two more years our ranks will have swelled further due to the dire need of pilots at Northwest Airlines, Continental Airlines, Delta Airlines, American Airlines, and Alaska Airlines because their existing pension plans will fail to produce the nest egg they expected.

The cost of a defined benefit retirement plan is just too expensive for today's commercial airlines to sustain. The discussions before this committee today, and before the Senate Finance Committee on the same subject two weeks ago, clearly mark pensions as the one expense that must be addressed if airlines are to remain competitive and out of Chapter 11 bankruptcy.

Social Security, the PBGC, and the Airline Pilot

The health of the Social Security (SS) system and the Pension Benefit Guarantee Corporation (PBGC) are also integral in this discussion. Airline pilots must retire before they can receive SS income. If allowed to continue in their airline careers, many pilots would willingly work well beyond their 60^{th} birthday. Those that can, and do, will continue to contribute to the SS fund. Pilots that work past age 62 would postpone the withdrawal of SS income, and increase their SS incomes with each year they continue to earn wages. Likewise, employers would continue to contribute into pilot retirement accounts, pensions, and the SS funds as long as their pilots remain actively employed.

When an airline forfeits their pension plans to the PBGC pilots suffer the largest reduction in retirement income because of the reduced PBGC income at age 60. If airline pilots are allowed the option to work until their SS retirement age they would have the same opportunity of other airline employees to work until the are able to earn the maximum SS and PGBC incomes.

The PBGC will potentially absorb enormous sums of under funded pensions from airlines that will seek protection in Chapter 11 bankruptcy in order to shed unsustainable costs. The federal budget can ill afford to absorb these additional costs.

Retirement savings plans offer financial relief to the carriers and their pilots

It appears that the few remaining airline pension plans will have to migrate to more affordable defined contribution plans if air carriers are to remain viable. Although a small segment of the airline employee population, pilots require a disproportionately large balance in their pension plans. Dwefined Contribution retirement plans have existed at a majority of airlines for many years. Airlines and pilots gain additional latitude to negotiate alternative retirement plans if pilots are allowed to fly until their Social Security retirement age.

As this transition occurs many airline pilots will want the option to work until their retirement accounts will provide them a comfortable retirement. Older airline pilots in particular will require additional years to recover from diminished pension income. Younger pilots will have longer to save for their personal retirement goals.

Efforts to address airline problems should affect all airlines and their pilots

ALPA is supporting legislation that would alter pension funding guidelines and address the plight of airline pilots who must retire at a reduced PBGC income. This is only a partial solution at best. The pilots at US Airways and United Airlines will not benefit from any future fixes to pension plans. Their future is one of a poverty level retirement income, no health insurance until qualified for MediCare, and very little opportunity for employment as they must reenter the job market in their 7th decade.

Pilots at Southwest Airlines, JetBlue, and many other airlines must rely on their savings for retirement, and they too, need relief. In the past 4 years money invested in stock funds and interest income accounts have all suffered a reduction in balances and returns.

Any airline relief legislation must offer equal opportunity to all airline pilots, not just pilots at the large airlines that want to protect their threatened pensions. Legislation should include provisions that will allow airline pilots the equal opportunity to work until they too can receive their federal entitlements. Forcing airline pilots, and only airline pilots, out of work for the sole reason that they celebrate their 60th birthday defies common sense, is illegal, and violates our innate desire and right to be productive.

Removing the artificial age barrier, that is the Age 60 Rule, would permit airline pilots the ability to negotiate a wage, retirement, and benefit package that would be the most beneficial to all parties over the long term. Eliminating the Age 60 Rule does not obligate the pilots at the large legacy carriers to automatically alter their retirement plans. Rather it allows any other airlines to not be encumbered by this needless restriction.

The perfect solution

ALPA represents pilots with a Canadian airline where no age 60 restrictions exist. In this environment ALPA negotiated a contract that allows pilots to retire with reduced benefits beginning at age 55, full benefits at age 60, and the option to work until age 65.

Any solution to the airline predicament in this country should include provisions that allow pilots the opportunity to work until they can no longer perform in the cockpit to the same standards as they have demonstrated in the past. Retirement should be negotiated without artificial barriers that inhibit the productivity and earnings of pilots.

I thank you for this opportunity to express the wishes of thousands of American citizens that are asking for the right to remain productive at a time when many are seeking a government handout. We ask for a solution applicable to all pilots.

Respectfully Submitted,

Stan Sutterfield
Chairman, APAAD
Captain, Southwest Airlines
Lt Col, USAF, Retired

Michael Oksner

Captain Mickey Oksner, Retired
Regional Director APAAD

WRITTEN STATEMENT OF BERT M. YETMAN

PRESIDENT

PROFESSIONAL PILOTS FEDERATION

AIRLINE PENSIONS: AVOIDING FURTHER COLLAPSE

BEFORE THE

HOUSE TRANSPORTATION AND INFRASTRUCTURE COMMITTEE

UNITED STATES SENATE

JUNE 22, 2005

Introduction

The Professional Pilots Federation (PPF) has, since being established in 1991, represented pilots encumbered by FAR 121.383(c), known as the Age 60 Rule. This Federal Aviation Regulation forces the safest, most experienced pilots from our airline cockpits at 59 years, 364 days, regardless of health or competence. Although the Federal Aviation Administration has held the regulation to be a "safety rule", the evidence has shown that the Rule was promulgated as an economic favor to the airlines. Safety was the only 'fortress' which would allow such a Rule to endure for 45 years. 44 or more nations have eliminated age 60 as a pilot retirement age and have no age limit, or 65, relying on medical and practical testing (simulator and enroute checks). They have experienced no problems with the over-60 pilots.

Airline Crisis

No one would deny that the American airline industry is suffering one of its worst crisis ever. Many familiar airlines have disappeared. Still others are fighting for their very existence, such as legacy carriers US Airways, United AirLines and Delta. American Airlines is struggling to keep its head above financial waters. A 1993 study showed one of these carriers would save more than $53,000,000 for each year the age Rule was extended, mostly in training costs for upgrading to replace the retiring captain.

Through collective bargaining agreements, pilots salaries are no longer a factor in the maintenance of the Age 60 Rule. After 12 years, a pilot has reached the top of the seniority pay increase scale. Equipment changes and contract negotiations are his only pay increases. The single economic reason for implementation of an Age 60 Rule has gone the way of the dinosaur.

Airline Pensions

Employee pensions have been hard hit by airline management's striving to cut costs. Pilot pensions, in particular, have been the hardest hit. Employee concessions, negotiated over the past few years, have not been enough to satisfy airline financial losses. Airlines entering bankruptcy are defaulting on underfunded pension plans, in turn placing the substantial financial burden on the Pension Benefit Guaranty Corporation (PBGC). Even this is not an assurance of a comfortable retirement, certainly not the retirement expected after many years of faithful airline employment. In some cases pilots are expected to receive 1/3 or less of their anticipated pension, and that may be reduced further by the PBGC policy of reducing payments for early retirement, which pilots are forced to take upon reaching Age 60. Those closest to retirement are in the worst position, with no time to recoup losses even if they were allowed to continue their careers. A total restructuring of retirement planning is necessary for those retirees, with the selling of homes, scaling down of living standards, acquiring medical coverage, the expenses of college age children, etc.

Social Security will not help airline pilots at age 60 retirement. In fact they will lose benefits for each quarter year they fail to contribute. In other words, after many years of contributing at the highest possible level, their benefits will decline for each year of noncontributing until Social Security begins. And, of course, Medicare is unavailable until reaching 65. At age 65 that would be 20 quarters of reduced benefit, or hundreds of dollars each month. The only solution to that problem is to find alternate means of work. Not an easy task at age 60.

Conclusion

The answer to this 45 year old antiquated, illogical and unfounded problem of pilot pensions is simple. Follow Europe, Australia, Japan and the rest of the world (the USA used to lead) by allowing pilots to continue their careers at least until full Social Security and Medicare benefits begin, presently age 65. If they choose to retire at 55 or 60, it should be allowed without unnecessary restrictions or undue loss of benefits. Certainly present medical and proficiency standards would still apply.

According to the 1993 study*, titled Economic Impact of the FAA's "Age-60 Rule", if pilots were allowed to continue beyond their 60th birthday, the realized annual savings at one major carrier, now in bankruptcy, would have been:

Real Permanent Savings:

Staffing levels:	$2,251,320.00
Pay differentials:	$16,380,000.00

Temporarily Deferred Expenditures:

Training costs:	$34,579,124.00
Savable/Deferrable in 1993	**$53,210,444.00**

Those savings would have easily exceeded $250 millions over 5 years for just this one carrier largely through savings in transition training costs - which are available to most carriers.

The Professional Pilots Federation thanks you for the opportunity to allow pilots to be part of the solution, not the problem. We wish to continue supporting our airlines. We wish to continue contributing to Social Security. We wish to continue to bolster the economy of this great country.

Thank you.

Respectfully submitted.

Bert M. Yetman

Bert M. Yetman

* Economic Impact of the FAA's "Age-60 Rule", S.D. Woolsey, 1993

STATEMENT OF

GLENN F. TILTON, CHAIRMAN, PRESIDENT AND CEO

UNITED AIRLINES

SUBMITTED BEFORE THE

UNITED STATES HOUSE OF REPRESENTATIVES

HOUSE TRANSPORTATION AND INFRASTRUCTURE COMMITTEE

SUBCOMMITTEE ON AVIATION

WASHINGTON, DC

June 22, 2005

Airline Pensions: Avoiding Further Collapse

UNITED

- ✓ We have better focused our products to meet the demands of the U.S. market, and reallocated our fleet to international markets where yields are higher.
- ✓ We are posting industry-competitive revenue performance.
- ✓ And we now have a normal governance structure.

During this time, our employees have set record operating performance results. That's counterintuitive for a company in restructuring, and that is to our employees' credit.

We have maintained our service for the flying public in our hub cities, and in the medium and small towns we serve from coast to coast, providing important commercial connectivity and critical access to global markets.

Throughout our restructuring, United has worked tirelessly to preserve our employees' defined benefit pension plans. We devoted 14 months to constructing a business plan to secure an Air Transportation Stabilization Board (ATSB) loan guarantee on terms that would have allowed United to keep its pension plans. In fact, I testified before this Subcommittee last year that our employees agreed to reductions in pension benefits to aid in funding our pension plans.

Shortly after my testimony before this Subcommittee, the ATSB rejected United's final loan guarantee application for $1.1 billion, advising us instead to pursue exit financing with the financial and capital markets. When we did, it was very clear that, given continued pressures on revenue and record fuel prices, United could not meet the financial targets necessary to be finance-able without the termination of pension plans and further labor cuts.

Even so, we worked with our unions, actuarial experts, financial and legal advisors, Board of Directors, Creditors' Committee – in fact, all stakeholders – to scrutinize every alternative that would allow us to meet our financial targets and keep our pensions.

Last year, we told our labor groups and other constituents that we would examine any alternative to pension termination and replacement to see if it was viable. By January of this year, no workable alternatives were found. We extended the search for another four months, and despite everyone's efforts, we failed to find viable alternatives to termination and replacement.

When it became clear to the management team and the Board of Directors that the termination and replacement of our pension plans was the only viable option, we prepared to go to court. At the same time, we were in discussion with the Pension Benefit Guaranty Corporation (PBGC). It was decided that the best route at this time was an involuntary termination by the PBGC, whereby the PBGC obtained securities and a share in United's future potential.

The PBGC agreement is fair and equitable to all, provides cost savings and stability necessary for United to exit from bankruptcy. But that does not change the fact that this has been extremely difficult for our employees and retirees and is not an outcome to be desired.

Since United began offering pension plans to its employees in 1941, we have done everything required by law – and more – to safeguard those plans for United's employees. And since the Employee Retirement Income Security Act's inception in 1974, we followed fully the rules and regulations and paid our PBGC premiums and plan contributions even while in bankruptcy, until the ATSB's final rejection of our loan guarantee application last summer.

From the outset of the bankruptcy process, our mission has been to enable United as a whole to succeed. Without success for the enterprise, the rest is academic.

To quote Bankruptcy Court Judge Wedoff on the United/PBGC agreement: "The least bad of the available choices here has got to be the one that keeps an airline functioning, that keeps employees being paid."

Without termination and replacement of pensions, United's future and the jobs of 62,000 employees would disappear, along with the economic contributions to hundreds of communities, our business relationships with hundreds of suppliers and partners, and United's continuing wage and benefit payments, including replacement retirement plans... and the pension plans would still be terminated.

United's unions understand the industry and economic realities that we are facing, and all but one have agreed to the retirement plan changes that must be made. We now have agreements on long-term labor cost savings with all our union groups, ratified or considering ratification, and with every union group but the Association of Flight Attendants on pension changes.

These agreements have moved United forward significantly in our restructuring and set the stage for our exit from bankruptcy.

The impact of this action on our retirees and employees will not be as dramatically negative as some have portrayed. All vested participants will continue to receive guaranteed benefit payments. In particular, most current retirees will not see dramatic reductions in their monthly benefits, and many retirees will not experience any reductions at all.

For example, retired flight attendants, the group that is by far the least impacted – represented or not – will receive approximately 100 percent of everything they are receiving today.

For current employees (except pilots), the impact of a termination could be substantially mitigated by working until age 65, the traditional retirement age in most pension plans.

The choice we faced for our employees was keeping jobs and replacing their existing pension plans with consensually negotiated replacement plans... or losing jobs and terminating pensions.

Unlike most of our competitors, United is in Chapter 11, seeking exit financing in order to keep our company in business for our employees, retirees and our customers. We know for certain that the cost of continuing our defined benefit pension plans was not finance-able ...the cost is simply unsustainable.

We at United agree with many of the policy issues that have been identified by House Education and Workforce Chairman John Boehner and House Ways and Means Chairman Bill Thomas. In particular, we support taking a comprehensive approach to solving these problems. We have learned from United's restructuring that reform of the pension laws cannot succeed if it is done piecemeal. There is no "quick fix."

Pension reform must consider the daunting economic reality and volatility the airline industry and other U.S. industries are facing today. Short-term moratoriums are falsely based on the hope that "if you wait it out, things will get better."

A lesson we at United have certainly learned is that there is no moratorium on business and financial reality.

# # #

THE COLLAPSE OF UNITED AIRLINES' PILOTS PENSION PLAN – IT COULD HAVE BEEN SAVED, AND, IN LARGE PART, IT STILL CAN BE SAVED

Statement of Roger D. Hall,[1] President of the United Retired Pilots Benefit Protection Association, prepared for inclusion in the record of a hearing on "Airline Pensions: Avoiding Further Collapse," before the United States House Aviation Subcommittee of the U.S. House Committee on Transportation and Infrastructure, June 22, 2005

Mr. Chairman and Committee Members, the retired United Airlines pilots stand to be the big losers in this collapse. The United Retired Pilots Benefit Protection Association ("URPBPA")[2] represents the largest segment of United's retired pilots – Pilots who worked their entire careers building this airline, relying on United's promise to provide decent security in retirement, and who are now told that they will lose huge portions of their pensions -- in many cases more than 60 percent. For a retiree, that large a percentage loss of income is catastrophic, leading to forced sales of homes and other terrible economic consequences. Our files and member correspondence contain many such heartbreaking stories, and the worst part of it is this: ***it did not need to happen.*** In fact, it still does not need to happen. If you examine what has happened at United, there is a better way -- a way out – and it's still there.

What Actually Happened? A Three-Way Bad Bargain

What actually happened? Clearly, ***this was a bargain.*** It was a bargain between (1) the Air Line Pilots Association ("ALPA," which had renounced any obligation to represent its own retirees), (2) United (which was determined to cut the benefits of its retirees), and (3) the Pension Benefit Guaranty Corporation ("PBGC," which went along with the deal).

Under the bargain, ALPA agreed not to oppose termination of the Pilots Pension Plan, and in exchange United agreed to grant greatly enhanced new pension benefits to active pilots (only), and then to set aside $550 million in debt obligations for later make-ups to active pilots (only). The bargain gave nothing to the retirees – it just cut their pensions, almost to the bone.

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[2] The United Retired Pilots Benefit Protection Association (URPBPA) is a non-profit Corporation registered in the State of Illinois. It was formed by retired United Airlines pilots who have extensive experience in representing the pilots of United Airlines. All of the officers and directors of the Association work without any financial compensation for the benefit of its members. The Association currently represents over 3,100 of United Airlines retired pilots.

PBGC went along with the deal, and expects to absorb unfunded pilot benefit obligations of over $1 billion. ***But PBGC had a way out of most of it, and they still do, today.***

A Plan Split/Partial Termination Could Save the Retired Pilots' Pensions,
Save Money for the PBGC,
and Still Leave United With the Benefits of Its Bargain

URPBPA has explained to United and PBGC that United can "split" the Pilot Plan into two plans – one for the actives and one for the retirees – and then terminate only the plan for the actives. The allocation of current assets between the two plans is controlled by a provision of ERISA (4044(a)). The split is allowed by a provision of the Internal Revenue Code (IRC 414(l), and Reg 1.414(l)). And the results would be this:

The Retired Pilots Plan would continue, but, using United's actuarial assumptions, it would be fully funded.

And PBGC's absorption of unfunded Pilot pension obligations would be reduced by over $750 million.

And, since the Pilots Plan is still not actually terminated, they can still do this – now.

Why didn't United do it this way, since the main pension funding cost would be eliminated anyway?

Why didn't ALPA demand it, since they could have achieved a decent retirement for their own retirees, without changing the deal for the active pilots?

Why didn't PBGC force this split into the deal it made with United, since it would have lowered the Government's new debt obligation by and saved PBGC over $750 million?[3]

The answers to these questions are difficult to smoke out. United Airlines views their current bankruptcy position as an excellent opportunity to deny retirees and employees the benefits they worked many years to obtain. United maintains that termination of their defined benefit pension plans is the only alternative. They have even gone so far as to insist in their agreement with the PBGC that none of United's Defined Benefit Plans can ever be restored in the future. This means that, even if United emerges from bankruptcy and generates massive profits, retirees will never recover what was taken from them. Such actions are clearly punitive and are not necessary for United to emerge from bankruptcy.

URPBPA would urge the Committee to consider changes to current law that would require companies in bankruptcy to work toward alternatives to outright plan termination

[3] And ***why*** doesn't this Committee demand detailed answers to these questions? URPBPA believes that the proposal we have developed is a viable alternative to catastrophic plan terminations, and we urge the Committee to consider expanding its feasibility and perhaps requiring it when plan sponsors pursue needless plan terminations of defined benefit plans.

thereby avoiding these devastating losses for retirees. Current law makes outright termination an easy way out of their obligations for companies and leaves retirees to suffer financial hardships for the rest of their lives.

Other Changes in Existing Law

The recent actions of United Airlines and PBGC seeking to terminate United's defined benefit plans for all of United's retirees and employees clearly highlight the deficiencies in current laws governing plan termination, plan funding and reporting requirements. Current law needs to be changed to require companies to maintain the funding of the plans at or near full funding levels and to provide strict requirements for plans to return to full funding over a period of time when deficiencies occur. The law should also require that plan participants be provided with quarterly reports on the funding status of their pension plans. And of course, termination needs to be the absolute last resort, not the easy way out.

This Committee obviously recognizes that if United's plans are terminated, other airlines will seek to follow suit. The termination of additional airline defined benefit plans will place greater stress on the PBGC's resources, and even greater stress on the resources of the retirees whose pensions are cut back. URPBPA urges your immediate consideration of changes to current law to prevent these types of occurrences from devastating other retirees and employees.

URPBPA also strongly supports S.1158, the bill introduced by Senator Edward Kennedy and others, that proposes a six-month moratorium on involuntary plan terminations under ERISA 4042, in bankruptcy cases. This ought not to be a mindless stampede, particularly when there are solutions that can be found, and that work.

But first and foremost, we ask this Committee to look at what is happening at United and consider imposing more stringent plan termination standards when there is a feasible alternative to full plan termination. Pension benefit devastation imposes not just a government cost, and not just a corporate cost – there is a human cost that should not be overlooked – particularly when with the application of some intelligence, the parties can achieve a result that is so much better for all concerned.

We have told United this: We understand that in insolvency situations ***business leaders must sometimes make hard and painful decisions.*** If they must, they must, and reasonable people understand that. ***But when devastating cuts are not necessary and management hacks away at retirement security anyway, that is neither understandable nor acceptable. It is an outrage!***