

II. BACKGROUND

If approved by the Court, the Agreement would allow the debtors (“United”) to enter into termination agreements with the Pension Benefit Guaranty Corporation (“PBGC”) as to all of United’s defined benefit plans, including the Pilots Plan (also referred to as the “A Plan”). The A Plan contains two components: a tax-qualified plan subject to the funding and benefit guarantee provisions of the Employee Retirement Income Security Act (“ERISA”) 29 U.S.C. § 1001, et seq.; and a non-tax-qualified component which enjoys no PBGC protection.

The pensions retired pilots receive from the Pilots Plan are a form of deferred compensation. The retired pilots gave up compensation when they were working in order to provide for themselves and their families after retirement. They have organized their financial commitments in retirement based on their pension income. Unlike most other Americans, they are prohibited by law from returning to work in their professions after their mandatory retirement age of 60 which limits their ability to obtain employment to supplement their retirement income.

The impact on retired pilots of a termination of the Pilots Plan is drastic. Nearly 60% of retired pilots will experience reductions from their current pension income if the PBGC takes over their plan. (Levy Dec., p. 5). And those reductions will be substantial - on average, 34% of what they presently receive will be lost. (*Id.*) Approximately 17% of the retired pilots will lose more than half of their retirement benefit. (*Id.*) Moreover, about 51% of the retired pilots receive non-qualified benefits and United will cease those payments in the event of a plan termination. (Levy Dec., p. 6).

III. ARGUMENT

A. The United/PBGC Agreement Is Not In The Best Interests Of The Estate

1. In Attempting to Support the Instant Motion, United Makes Unproven and Misleading Statements About the Necessity of Pension Plan Termination and the Lack of Alternatives to Termination

The “Background” section of United’s motion is replete with statements suggesting that pension plan terminations are necessary for exit financing. United’s necessity argument is contrived. It is based on a business plan (Gershwin 5.F) which was prepared by United and which eliminates pension plan liability. United then relies on the declarations of their financial consultant, Todd Snyder, who has opined that eliminating pension liability “will facilitate United’s ability to obtain firm exit financing commitments and meet anticipated exit financing requirements.” (Snyder Dec., p. 3).

These allegations are disputed and unproven. The evidence reveals that United’s discussions with exit lenders are preliminary, at best. There is no evidence of United presenting exit lenders with a business plan, which includes pension liabilities, and being turned-down.

Also, the “credit metrics”, which United states it must meet to obtain exit financing and which drives the elimination of pension liability from the business plan, are unreasonable. The report of Victor Caruso demonstrates, for instance, that other airlines and businesses, who do not meet the credit metrics United has imposed on itself, have obtained financing. (Caruso Dec., p. 21-29).

United also attempts to set-up its instant motion by arguing that it has considered “alternatives” to pension termination and that none is reasonable. United’s method of considering alternatives to pension termination is to simply reject all proposals made to them. (For instance, see AFA and IAM briefs in opposition to United’s request for 1113 relief). United

also rejected the proposal made by URPBPA as an alternative to termination of the Pilots Plan. URPBPA's proposal is known as the Split/Freeze Plan ("SFP").

2. URPBPA's Split/Freeze Plan ("SFP")

The SFP was devised by Thomas D. Levy, the chief actuary of the well-known and respected firm, The Segal Company. The SFP would allow the tax-qualified component of the Pilots Plan to be split into two plans, one for non-retired pilots (the active plan) and the second plan for retired pilots (the retired plan). (Levy Dec., p. 4-5). Once the split occurs, the active plan could be terminated by United and/or the PBGC and the active pilots would have the benefits available under the January 31, 2005 agreement reached between the Air Line Pilot Association ("ALPA") and United (which includes the benefits from \$550,000,000 in convertible notes). (*Id.*) The qualified portion of the retired plan would then be frozen (all benefits permanently fixed). (*Id.*) The benefit payments for the non-qualified portion of the retired plan would also continue on a frozen basis. (*Id.*) Levy then calculated the extent of United's contributions to the retired pilot plan, which are far less than what they would be under the current plan. (Levy Dec., p. 6-8). No IRS funding waivers would be required for the SFP. (Levy Dec., p. 7).

Most importantly, the cost to United of the SFP was considered by a financial expert retained by URPBPA, Victor Caruso, a Managing Director of the Gordian Group, a New York investment banking firm. Caruso reviewed the potential pension contributions which may be required of United under the SFP and factored those contributions into Gershwin 5.F ("GF5") of United and found:

"the conclusion is straight forward, every credit metric or target ratio as described by Snyder [United's expert] and attained in GF5, is likewise attained or is not materially different from 'required' levels (as defined by Snyder) in GF5 as adjusted for the SFP". (Caruso Dec., p. 10).

This means that the credit metrics in United's business plan which it claims it needs to secure exit financing are met if the SFP was implemented.²

3. The United/PBGC Agreement is Not in the Interests of the Retired Pilots and Other Creditor Groups and Will Create "Disharmony" at United

The retired pilots of United have a substantial creditor interest in this bankruptcy given their number, approximately 6,000, and the value of the benefits which will be lost if the Pilots Plan is terminated. The United/PBGC agreement is not in the best interests of the retired pilots and is extremely adverse and destructive to their welfare. The retired pilots are particularly vulnerable. They had to retire at age 60 and could not receive full government-sponsored retirement benefits at that time. Even the retired pilots healthy enough to work by law are precluded from working in the profession for which they were trained. Many retired pilots live on their pensions and their obligations and living expenses depend on that means of support. To take away from any retired person 30%, 40% or 50% or more of their retirement income will ruin them.

But the United/PBGC agreement disadvantages a number of other creditor groups besides the retired pilots. One need only review the § 1113 briefs of the Association of Flight Attendants ("AFA"), the International Association of Machinists and Aerospace Workers ("IAM"), or of the Aircraft Mechanics Fraternal Association ("AMFA") to see that the prospect of pension plan terminations injures many of the creditor groups. One can also see from those briefs an arrogance by United, who pays only lip service to considering alternatives to pension

² The above-described conclusions of Levy and Caruso regarding the SFP are not dependent on legislative relief. In its instant motion, United downplays the significance of pending legislation. But, in fact, on April 20, 2005, Senator Johnny Isakson (R-GA) introduced the "Employee Pension Preservation Act of 2005." If enacted, plans covering airline employees with frozen pensions could disregard deficit reduction contributions and fund their unfunded liabilities over 25 years. Using United's actuaries most recent projections, it appears that no contributions by United for qualified benefits would be required under the SFP proposal. Thus UAL's only pension expenditure for pilots would be the roughly \$60 million per year for non-qualified plan benefit payments. (Levy Dec., p. 5).

terminations and has never had any desire to do anything short of complete terminations of all pension plans.

United has previously stated that there would be “disharmony” among the workforce at United if it retains some plans or alternative plans rather than terminating all of the plans. (See United’s Supplemental Memorandum in Support of 1113 Relief and for Distress Termination of Pension Plans, page 88). But one need only read the briefs of the various employment groups to see that there is disharmony now. There are possibilities of job actions and strikes. There is growing discontent among a work force that has been pushed too far. The disharmony created by the United/PBGC agreement will devastate the business of United far beyond the estimates of “credit metric” benefits that would allegedly be realized by pension termination.

To satisfy § 363 of the Bankruptcy Code, the proposed transaction should “act to further the diverse interests of the debtors, creditors and equity holders alike.” In re Telesphere Communication, Inc., 179 B.R. 544, 552 (Bankr. N.D. Ill. 1994). The United/PBGC agreement would be destructive to this bankruptcy estate and would not further the diverse interests of the parties.

B. The United/PBGC Agreement May Not Be Approved Because the Agreement Violates ERISA

The proposed agreement may not be approved under ERISA. First, the agreement is inconsistent with the PBGC’s duty to protect plan beneficiaries and United’s fiduciary responsibilities as the plan administrator for the plans it seeks to terminate. Second, the PBGC does not have the authority to enter into this settlement agreement because it purports to require the PBGC to violate its statutory duties and it contains an unprincipled limitation on the PBGC’s duty to restore United’s pension plans under appropriate circumstances.

The PBGC was created by, and is required to exercise its authority in connection with, 29 U.S.C. § 1302 of ERISA, which states that “[t]here is established within the Department of Labor a body corporate to be known as the Pension Benefit Guarantee Corporation.” Section 1302(a) sets forth the three primary statutory duties of the PBGC, referred to as the “purposes of this subchapter,” which are:

- (1) to encourage the continuation and maintenance of voluntary private pension plans for the benefit of their participants;
- (2) to provide for the timely and uninterrupted payment of pension benefits to participants and beneficiaries under plans to which this subchapter [Title IV of ERISA, 29 U.S.C. §§ 1301-1461] applies; and
- (3) to maintain premiums established by the corporation under section 1306 of this title at the lowest level consistent with carrying out its obligations under this subchapter.

Section 1302(b) sets forth the “powers” of the PBGC, all of which are granted to the PBGC in order to carry out the “purposes of this subchapter.”

The PBGC’s core responsibility is the protection of beneficiaries. As stated in Page v. PBGC, 968 F.2d 1310, 1317 (D.C.Cir. 1992) *citing* Rettig v. PBGC, 744 F.2d 133, 141 (D.C.Cir. 1984), ERISA

was passed with the overwhelming purpose of protecting the legitimate expectations harbored by millions of employees of a measure of retirement security at the end of many years of dedicated service. The other statutory purposes - encouraging the growth of private pension plans and keeping down the costs of termination insurance for those plans - are important but necessarily secondary: those purposes have meaning only in light of the need for a fair and reliable system of retirement income security for employees.

The court stated that the “cost of the guarantee, the equity of imposing on employers with adequately funded plans responsibility to compensate for underfunding by others, and the

administrative burden on the PBGC were it required to guarantee the benefits plaintiffs seek, are considerations subordinate to ERISA's core purpose." Page, 968 F.2d at 1317. On that basis, the Court of Appeals rejected PBGC's refusal to interpret Title IV's provisions broadly for the purpose of providing maximum feasible benefits to employees, and rejected PBGC's narrower interpretation of its duties, even though the PBGC sought such a narrow interpretation in order to protect its own budget.

The other party to this proposed unlawful bargain is United. When United acts in its capacity as a "plan administrator" it must observe the fiduciary duties it has to the plans it administers and the beneficiaries of those plans. 29 U.S.C. § 1002(14)(A) makes it clear that plan administrators are fiduciaries of defined benefit plans subject to the ERISA's fiduciary requirements set forth at 29 U.S.C. § 1104. Sections 1104(a)(1)(A) and (B) state that a fiduciary, under ERISA, must "discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries and for the exclusive purpose of providing benefits to participants and their beneficiaries; and defraying reasonable expenses of administering the plan."

Here, United and the PBGC seek approval to enter into the proposed agreement, which, in turn, would authorize United to enter into a § 1342(c) termination agreement. But a § 1342(c) termination agreement must be executed by the PBGC and a "plan administrator," which is, by definition, an ERISA fiduciary. Therefore, United cannot enter into a § 1342(c) termination agreement if doing so would constitute a breach of its fiduciary duties to one or more of the plans it seeks to terminate. In addition, the PBGC's execution of the instant settlement agreement constitutes a breach of its statutory duty to protect the rights of plan beneficiaries.

Neither the PBGC nor United validly entered into this settlement agreement, which sets up the wholesale termination of the Pilots Plan, because they have failed to give adequate

consideration to URPBPA's Split-Freeze Plan, which provides a feasible alternative to the termination of the Pilots Plan. The PBGC has the responsibility to protect United's retired pilots and the benefits they have earned and United, as a plan administrator and ERISA fiduciary, must also seek to protect the benefits it promised its now-retired pilots, who spent years earning their fixed pension incomes. If a feasible, affordable alternative to wholesale termination exists, the PBGC and United have a responsibility to work toward the implementation of that alternative. But the facts demonstrate that United has consistently refused to give any real consideration to the creative proposals its various labor groups have made that could save one or more of United's plans.

As it can be seen from the Caruso Report, even using United's metrics in Gershwin 5.F, United can afford the SFP. The SFP is compatible with the PBGC's statutory responsibilities because it would save the PBGC money and it would "encourage the continuation and maintenance of voluntary private pension plans for the benefit of their participants." Most importantly, though, the SFP would prevent the devastating loss of benefits that would otherwise be sustained by United's retired pilots, many of whom could lose up to 50 percent of their retirement income. Because the PBGC and United both have duties toward United's retired pilots, and because ALPA has already agreed that it would not contest the termination of the Pilot Plan, the PBGC and United have a duty to implement the SFP. United and the PBGC also have the responsibility to give real consideration to the proposals other employee and retiree groups may have that would prevent the termination of United's other defined benefit plans.

In addition, the PBGC does not have the authority to enter into this settlement agreement because it requires the PBGC to violate its statutory duties and contains an unprincipled

limitation on the PBGC's duty to restore United's pension plans under appropriate circumstances. This is another reason why the agreement may not be approved.

Under 29 U.S.C. § 1363(b), when a plan with unfunded liability terminates, that liability is owed to the PBGC as a matter of statute. The liability to the PBGC is owed as a matter of law and is not dependent on any agreement. And the liability is joint and several among all of United's affiliates. The proposed agreement gives much of that liability away, as follows.

First, paragraph 7(a) of the agreement waives the PBGC's joint and several claim, thereby releasing each and every one of United's affiliates from all liability under § 1363(b) (a provision under which each affiliate is separately liable for the full amount of termination liability, thereby increasing the recovery for the benefit of the plan and its participants).

Second, paragraph 13 of the agreement provides that "[a]t United's option, PBGC shall assign 45% of the distribution that it receives or is to receive on account of its claims in the Chapter 11 cases as directed in writing by United." The account receivable for termination liability under § 1363 is money that belongs not just to PBGC but also to the plan participants and beneficiaries. The statute so provides. Under 29 U.S.C. § 1322(c), the statute sets forth a formula for sharing this specific recovery between PBGC's own treasury and the plan's participants, including United's retired pilots. So a portion of this money owed under § 1363 is a plan asset that would be shared with participants. But under the proposed agreement between United (the current fiduciary of the plan) and PBGC (the future fiduciary of the plan if it is terminated and PBGC becomes "trustee") this distribution can be assigned to anyone United selects. This is improper and inconsistent with ERISA's recovery provisions.

Performance of that agreement would be a prohibited transaction under 29 U.S.C. § 1106(a)(1)(A) and (D), which prohibits a plan fiduciary from transferring plan assets to or for the

benefit of a party in interest (and United, as employer, and as a fiduciary, is clearly a “party in interest” under ERISA § 3(14)(A) and (C)). Thus, the performance of this agreement would constitute a prohibited transaction. This Court should not approve an agreement that calls for a violation of the law.

Further, an agreement to release assets that would otherwise increase the benefits of participants is also a breach of fiduciary duty under 29 U.S.C. § 1104(a)(1)(A), which requires a plan fiduciary to perform its duties “solely in the interests of the participants” and “for the exclusive purpose of providing benefits to participants and beneficiaries.”

Any argument that United is behaving as a “settlor” and not as a fiduciary in this context violates both the spirit and letter of the law. The entire agreement has as its quid pro quo the making of a termination agreement (Exhibit A to the settlement agreement), and that termination agreement is by its own terms an agreement between PBGC (which will become successor trustee under that agreement) and United of the terminating plan. A plan administrator is a fiduciary by definition, under 29 U.S.C. § 1002(14)(A) and 29 CFR § 2509.75-8 (Q & A FR-12Q). The proposed agreement cannot escape the test of fiduciary responsibility by putting key operative provisions in a cover agreement which refers to a termination agreement.

In addition, under paragraph 6 of the proposed agreement, the PBGC purports to waive its right to restore any of the defined benefit plans that United and the PBGC seek to terminate. But 29 U.S.C. § 1347 is one of the essential tools the PBGC can use to protect plan beneficiaries and to promote the “continuation and maintenance of voluntary private pension plans for the benefit of their participants.” According to the proposed agreement, even if United reorganizes, fuel prices drop, other market conditions improve and United becomes a very profitable enterprise, the PBGC would not have any right to restore one or more of the plans United and the

PBGC seek to terminate. The PBGC may not waive its ability to restore plans under § 1347 because doing so would violate the PBGC's primary statutory purpose, which is the protection of plans and their participants.

C. The United/PBGC Agreement Constitutes a Sub Rosa Plan of Reorganization

A sub rosa plan of reorganization arises where the debtor seeks approval of a transaction that has the "practical effect of dictating some of the terms of any future organization plan" or precludes "the possibility of alternate methods of reorganization." In re Braniff Airways, Inc., 700 F.2d 935, 940 (5th Cir. 1983); In re DRW Property Co., 54 B.R. 489, 498 (N.D. Tex. 1985). When a transaction goes so far as to substantially determine the terms of a plan in advance of and without the protections of the Chapter 11 plan confirmation requirements, the proposed transaction should be rejected as sub rosa. Braniff, 700 F.2d at 940. Sub rosa plans are not permitted because the debtor should not be able to short circuit the requirements of Chapter 11 for confirmation of a reorganization. Braniff, 700 F.2d at 940.

The United/PBGC Agreement should be rejected as sub rosa. The agreement offers the PBGC \$1.5 billion in notes and preferred stock that could otherwise be used to fund proposals that have been submitted to United and would help prevent the termination of one or more of United's defined benefit plans. As previously asserted by the PBGC in its objection to the approval of Letter Agreement 05-01, the Court should not approve an agreement that denies creditors the protections of the confirmation process and which infects virtually every aspect of any future plan of reorganization, while removing "the hurdles erected in Chapter 11, such as those found in 11 U.S.C. § 1129(a)(7) (best interest of creditors test). Braniff, 700 F.2d at 940.

In fact, some of the strongest arguments against the approval of this agreement have already been set forth in the PBGC's objection to the approval of Letter Agreement 05-01. In the

PBGC's objection to Letter Agreement 05-01, the PBGC argued that courts recognize that looking only at the fairness to the settling parties "contravenes a basic notion of fairness." In re Quality Beverage Co., 181 B.R. 887, 894 (S.D. Tex. 1995). While United argues that its agreement with the PBGC is in the best interest of the estate, United fails to consider the interest of the estate as a whole - which includes the interests of the creditors. In re Telesphere Communications, Inc., 179 B.R. 544, 552 (Bankr.N.D.Ill. 1994). The United/PBGC agreement fails to demonstrate any benefit to be had by creditors other than the PBGC.³

In its objection to Letter Agreement 05-01, the PBGC argued that the Court should not approve a proposed action under § 363 where it, "either in fact or effect, encroaches on a right afforded creditors" in the Chapter 11 process. In re Crowthers McCall Pattern, Inc., 114 B.R. 877, 885 (S.D.N.Y. 1990). A motion for approval of a sale or other use of property under § 363 must be denied if it has the practical effect of dictating even *some* terms of a future plan of reorganization. Braniff, 700 F.2d at 939-40. Just as the PBGC argued that Letter Agreement 05-01 did not provide any value to the estate but merely diluted the pool available to the other creditors, the United/PBGC agreement contains the same flaws. The agreement provides for \$1.5 billion to be provided only to the PBGC while the other groups receive nothing.

In short, the United/PBGC agreement impermissibly seeks to dictate the course of these proceedings by dramatically affecting the Debtor's capital structure on emergence and

³ In approving settlements in a bankruptcy proceeding, the court must "determine whether the proposed compromise is fair and equitable and in the best interests of the estate." In re Donald Weinhoft, 1999 WL 33593715 (C.D. Ill. Dec. 27, 1999)(citing Depoister v. Mary M. Holloway Foundation, 36 F.3d 582, 586 (7th Cir. 1994)). In exercising its discretion, the bankruptcy court must weigh all factors bearing on the reasonableness of the settlement including: 1) the probability of success in the litigation; 2) the difficulties, if any, to be encountered in the matter of collection; 3) the complexity of the litigation involved, and the expense and inconvenience in delay necessarily attending it; and 4) *the paramount interest of the creditors and a proper deference to their reasonable views.* In re Antonio Del Grosso, 106 B.R. 165, 168 (N.D. Ill. 1989).

determining the treatment of one creditor to the detriment of other creditors. Just as in Braniff, such an agreement warrants judicial disapproval because of its sub rosa nature.

IV. CONCLUSION

For the foregoing reasons, URPBPA requests that United's motion be denied.

UNITED RETIRED PILOTS BENEFIT
PROTECTION ASSOCIATION, ROGER D.
HALL, DENNIS D. DILLON, GERARD
TERSTIEGE, EUGENE M. CUMMINGS,
RAYMOND P. FINK, JAMES M. KRASNO and
WILLIAM L. RUTHERFORD

By: 

One of Their Attorneys

Jack J. Carriglio
Eric E. Newman
James G. Argionis
Meckler Bulger & Tilson
123 North Wacker Drive, Suite 1800
Chicago, Illinois 60606
(312) 474-7900 (phone)
(312) 474-7898 (fax)

Frank Cummings
LeBoeuf, Lamb, Greene & MacRae, L.L.P.
1875 Connecticut Avenue, NW
Washington, DC 20009-5728
(202) 986-8000 (phone)
(202) 986-8102 (fax)