United Airlines halts pension payments: a major attack on retirement programs in US

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United Airlines announced on July 23 that it was halting all payments to its pension plan while it remains under bankruptcy protection. The move came only a few days after the world's second largest airline announced that it would be deferring a $72.4 million payment to the plan.

The announcement by United that it is essentially unilaterally abandoning its pension program constitutes a major assault on the entire system of defined-benefit pensions in the United States. It comes after intense pressure from the Bush administration and Wall Street on United to place the burden of its economic distress on the backs of its workers.

There are some 44 million Americans covered by defined-benefit plans valued at over $1 trillion. According to these plans, retired workers receive a set amount, often related to the number of years the worker was employed at the company. The pensions are paid out of a pension fund managed by the company, a fund that generally includes investments in stocks, bonds and other securities. Companies are required by law to make regular contributions into their plans to ensure that the company has enough resources to cover its obligations.

The other main type of private pension plan in the US is the defined-contribution plan, or 401(k) plans. There has been a major shift away from defined-benefit plans to defined-contribution plans in recent years, as the latter generally cost corporations less.

United Airlines has four separate plans covering pilots, mechanics and ramp workers, flight attendants and salaried employees. Some 58,000 retired workers are covered by these plans, and United has 62,000 current workers. The pensions covering these workers are "underfunded" by about $7.5 billion, meaning that the company has obligations valued at $7.5 billion more than the plan's assets. The airline had previously committed to paying about $600 million into the plan by October of this year and more than $4 billion by 2008. The announcement last week effectively cancels these planned payments.

Last month, United was denied a federal loan guarantee from the Air Transportation Stabilization Board. The move by the ATSB was a deliberate attempt to force United to increase cost-cutting measures and in particular take action against its massive pension obligations. Private investors have demanded a sharp attack on the pension programs because they are a major drain on cash reserves, reserves necessary to pay off any loans given to the company.

The airline said in a statement issued last week, "In the absence of a federal loan guarantee, United's long-term business plan must have cash flow and liquidity levels that the capital markets are willing to finance. Because existing pension plan contributions will remain a huge financial burden after exit [from bankruptcy], it is incumbent on United to study all possible options and to determine whether United can sustain this burden and still attract exit financing."

For United to formally abandon its plans, it must gain approval from a bankruptcy court. If this happens, the pensions will be shifted onto the Pension Benefit Guaranty Corp. (PBGC), a federal agency that insures private pensions such as those offered by United. When a company abandons a pension plan, both the assets and liabilities are shifted to the PBGC. The PBGC continues to pay out benefits but often at a reduced rate. No new benefits are added, and benefits are frozen at the level accrued at the time of the default. This means that new employees and recently hired employees will have little or no coverage unless they are able to win a new plan from the bankrupt company. Workers who had been promised pensions above the PBGC cap of $44,000 a year will see their benefits reduced.

The PBGC does not receive any government funds. Rather, it is funded by fees from companies that participate in its insurance program.

Because of the reduction in obligations, if all four of United's plans were dumped on the PBGC, the agency would receive net liabilities amounting to $5 billion rather than the full $7.5 billion. Such a move would nevertheless probably deal a mortal blow to the agency, already deeply in debt. In a major understatement, PBGC Executive Director Bradley Belt wrote in a letter to Glenn Tilton, the chairman and CEO of United's parent, UAL Corp., "The decision to stop contributing to the pension plans is a serious matter that increases the risk of loss to plan participants and the federal pension-insurance program."

The PBGC has already accumulated a massive deficit. In September 2003, it reported a deficit of $11.5 billion, a figure that was revised downward to slightly less than $10 billion earlier this year. If United were to default on all of its plans, it would constitute the single largest loss for the agency since it was founded in 1974.

The position of the PBGC is the consequence of a series of massive defaults by steel companies and most recently US Airways, which shifted its pension plan to the agency in March 2003. In 2002, PBGC was forced to pick up $3.6 billion in liabilities when Bethlehem Steel went under, part of the $7.5 billion shifted to the agency in recent years by the steel industry.

The number of companies seeking to transfer their pension obligations onto the government is likely to increase in the coming years. A successful move by United will encourage other airlines to try as well. Moreover, many companies in other industries that provide defined-benefit plans—in particular, the automotive industry—may follow suit. General Motors has repeatedly complained about the cost of its pension plan, which covers about 370,000 retirees. The company estimates that it paid out about $6.2 billion in pension and health care costs to retirees in 2003, a major drain on its cash reserves.

Many of these plans are already heavily underfunded. The PBGC reported in June that 1,000 underfunded pension plans had a total shortfall of $278.6 billion in 2003. Of this, $31 billion was concentrated in the airline industry and $6 billion in steel. The number of underfunded plans has increased sharply, from 166 in 1999 (with a deficit of $18 billion) to 1,050 in 2003.

An article in the July 19 issue of *BusinessWeek*—”The Benefit Trap” by Nanette Byrnes—notes, “According to the PBGC, as of September, 2003, there was at least $86 billion in pension obligations promised by companies deemed financially weak. That’s up from $35 billion the year before. And it’s on top of a record number of companies that managed to dump their troubled pension plans on the PBGC last year: 152. In 2003, a record 206,000 people became PBGC pensioners, including 95,000 from its biggest takeover ever, Bethlehem Steel Corp.”

The growing troubles for defined-benefit pension plans are a product of growing strains on many of the industries that provide the plans. It is also in part a consequence of the sharp decline in the stock market in 2001 and 2002, since the assets of the plans are often held in stocks. During the late 1990s, companies took advantage of the stock market boom to reduce contributions to their plans. After the boom collapsed, the plans were left heavily underfunded.

As the *BusinessWeek* article notes, “Combined with the rise in retirees, [poor] market conditions have led to two years of record underfunding in company-sponsored plans. A recent study by analysts at CreditSights Ltd. found that 85% of the defined-benefit plans in the S&P 500 don’t have enough assets to cover their pension obligations. Together the underfunding equals 15% of their 2003 cash flow. As a result, companies will have to put billions of dollars of cash into these plans this year to help close the gap.

“The cost of honoring PBGC’s commitments could be higher than anyone is expecting. The government bailout fund has relied on having enough healthy companies to pony up premiums to cover plans that fail. But in a scenario of rising plan terminations, healthy companies with strong plans still in the PBGC system would be asked to pay more. For corporations already fretting that pensions have become a competitive liability and a turnoff to investors, this could be the tipping point. Faced with higher insurance costs, they could opt out, rapidly accelerating the system’s decline as the remaining healthy participants become overwhelmed by the needy.”

What will happen if United bails out on some or all of its pensions as now seems almost certain? If that move by itself does not render the PBGC completely insolvent, the follow-up likely will, as more and more companies follow United’s lead.

The head of the PBGC has talked about the necessity of a government subsidy on the scale of the savings-and-loan bailout in the 1980s. Such a bailout would be paid by taxpayers, and in the context of recent massive tax cuts for the rich, would constitute a massive transfer of wealth from ordinary Americans in order to cover the failure of corporations to meet their obligations.

There is no guarantee, however, that the government would actually bail the agency out, and if it did, no doubt conditions would be placed on the agency to sharply reduce benefits to present and future pensioners. Indeed, the heavily underfunded position of both the PBGC and corporate pension plans is in part a consequence of government policy. Earlier this year, Congress passed a bill that through an accounting manipulation reduced the amount of money that companies would be required to pay into pensions by $80 billion over the next two years.

Indeed, the whole process bears the distinct mark of a deliberate attempt by the American ruling elite to abandon gains won by workers through decades of struggle. The companies go bankrupt and shift their obligations to the government, and the government goes bankrupt and shifts its obligations onto...no one, leaving the pensioners without a pension.