WINNER:
AMERICAS RESTRUCTURING DEAL
UAL CORP

UAL, parent of United Air Lines, crash landed into bankruptcy court in 2002, a year after the catastrophic terrorist attacks of September 11 and was restructured amid weak demand for air travel. It emerged as an example for restructuring legacy carriers. UAL Corp is IFR's Americas Restructuring Deal of the Year.

WING AND A PRAYER

UAL Corp, working with NM Rothschild as financial adviser and Kirkland & Ellis as it attorney emerged from bankruptcy protection in February after more than four gruelling years. Initially UAL suffered comparisons to US Airways, which quickly restructured and emerged only to collapse back into bankruptcy protection.

Airlines have been notoriously bad investments – especially if you are an unsecured creditor. The payout to unsecureds in UAL could be considered paltry at 4% to 8%, but in a case where unsecured creditors felt lucky with any recovery at all, the return was considered comparable to bigger payouts in other cases. UAL unsecured creditors faced a perfect storm of recession, outmoded cost structure – the highest in the industry – unfunded pension liabilities and over capacity.

Even before the September 11 attacks, UAL and other so-called legacy carriers were being eaten alive by emerging low cost carriers. The grip of a SARS pandemic exacerbated the downturn in international air travel in the middle of the UAL restructuring and its ability to meet earnings metrics. A super spike in the cost of jet fuel as Hurricane Katrina slammed into the US Gulf Coast, a blow so extreme it hastened the collapse of Delta Air Lines and Northwest Air Lines, also threatened to upend UAL's restructuring.

In the final stretch of the restructuring, however, after the airline was forced to ask for repeated concessions from labour, most creditors were able to see the value of the deal as long as everyone was seen to be sharing the pain. In a final bit of wrangling, the unsecured creditors forced the company to cut the proposed stock award to its executives in half to about 8% of the outstanding shares.

The plan was overwhelmingly approved. Across eight consolidated classes, 89% of unsecured creditors – representing more than 93% of the claims outstanding – approved the final plan.

It was the largest, longest running and costliest airline bankruptcy in history, restructuring US$23bn in debt. In the final analysis the carrier cut costs by 20% across the board and eliminated US$13bn of debt and pension obligations.

In addition to shere size, the UAL reorganisation made history with the biggest ever pension rejections. Many restructuring advisers and institutional lenders point to the US$10.2bn pension rejection at UAL as the pivotal point when the US Pension Benefit Guaranty Corp (PBGC), the federal insurer of private pension plans which figures so prominently in most US bankruptcy cases, began to function as an investor.

Investors and restructuring advisers alike have looked at the PBGC as a wild card. The UAL case has proved pivotal in helping others to quantify the PBCG as a true player.

In UAL, the PBGC became an unsecured creditor and UAL's largest shareholder after the company negotiated to reject four plans with US$10.2bn in unfunded liabilities. The claim was converted into a 20% stake in UAL. Half of that holding was monetised almost immediately with the rest held for timed sales. The pilots union bought into the plan to reject the pension in exchange for a convertible note.

UAL ran into a brick wall with collateralised bondholders, however, who advanced the cause of aircraft financier rights. Holders of Enhanced Equipment Trust Certificates (EETCs), the asset-backed notes that financed United's fleet, created complicated alliances and negotiated beneficial terms for junior debt positions based on the strength of the senior debt. Secured bondholders also developed strategies of crossholding several series of EETC and ETC notes negotiating deals for poorer quality aircraft on the strength of superior quality planes. UAL sued arguing that the secured bondholders were colluding in an antitrust case that was ultimately decided in favour of bondholders establishing a bright line for airplane financiers' rights to collective bargaining.

The restructuring of UAL fleet to emphasise international travel also favoured the secured bondholders enhancing the value of their collateral to UAL.

"It was very difficult to get bondholders that held the leases to make a deal," said NM Rothschild managing director Todd Snyder.

In the end, these secured bondholders often holding senior and junior positions were able to negotiate beneficial terms but UAL was able to renegotiate deals that saved US$2.8bn on the leases.

"No other airline debtor has ever attempted, let alone achieved, a restructuring of public aircraft debt on a comparable scale," said Marc Kieselstein partner at Kirkland & Ellis. "We were pretty aggressive and creative."

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