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Pension Protection Act's Special Treatment for Airlines and Other Industries Merits a Veto

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Some policies are so bad that they overshadow the good features of legislation. If Congress insists on including special treatment for airlines and or other industries in the Pension Protection Act (H.R. 4), President George W. Bush should veto it. A veto would reduce the chance that companies could transfer the costs of their pension obligations to the taxpayer.

A Dangerous Precedent

Under H.R. 4, Delta and Northwest, which have frozen pension benefits, would be allowed up to 17 years to repay the underfunding of their pension plans, while American and Continental, which have not, would be allowed to take 10 years. These periods are significantly longer than the seven years other sponsors of defined benefit pension plans would have to eliminate their plans' underfunding. In addition, Delta and Northwest would be allowed to use an unusually generous formula that would sharply reduce the amount that they would have to contribute to their pension funds.

American and Continental now want the same treatment that Delta and Northwest would receive and, after threatening to delay the pension bill, are likely to receive additional breaks in a "technical corrections" bill that is expected to be considered later this year.

Even more alarming, in addition to the special treatment for the airlines, certain defense contractors would receive an extra three years before the new pension funding requirements apply to them. Supposedly, this is to allow time for government contract accounting requirements to be adjusted. However, since the new funding requirements are gradually phased in for all companies, there is no reason why the additional time is needed. The suspicion that this is just special treatment for a powerful industry is reinforced by language that allows these contractors to use a generous funding formula that would reduce the amount that they have to contribute to their pension plans. This special treatment for certain government contractors alone is more than enough to justify a veto.

While other parts of H.R. 4 would strengthen pension funding and reduce the probability of a massive taxpayer bailout of the Pension Benefit Guaranty Corporation (PBGC), the airline and government contractor provisions would open a huge loophole that politically connected industries could use to underfund their pensions. Why should auto parts companies, and even auto manufacturers themselves, spend billions of dollars better funding their pensions if airlines don't have to do so? Given the precedent, they will lobby Congress for similar relief using the same arguments of their industry's importance to the national economy and the potential losses their retirees will face.

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Once Congress has fallen for that argument a single time, it will be unable to resist future requests for "parity." Company after company will bring its workers to Washington, where they will point to the treatment the airlines received and say that they should receive the same—or even better—treatment. It is hard to imagine Congress having the strength to resist such pleas. The result, in effect, would be to transfer the cost of paying for pensions from companies to the PBGC and, after the inevitable massive bailout of that agency, to the taxpayer.

Rather than signing such flawed legislation into law, the President should give Congress the opportunity to re-pass it without the offending provisions.

Airlines Come and Go Just Like Other Companies

Supporters of special treatment for the airlines argue that the continued existence of companies like Delta and Northwest is essential to our economy. However, this is contrary to the history of aviation in America. Some of the largest and most prominent American airlines have gone out of business, including such major carriers as Eastern Airlines, Braniff, Pan American, and TWA (the last remnants of which merged into American after three bankruptcies). In each case, other airlines took over the routes while new carriers started operations.

In addition, still other major airlines, some of which were in financial trouble, have merged, and most existing airlines have gone into bankruptcy at least once. If Delta and Northwest did go out of business, their demise, while regrettable, would hardly leave major cities unserved because their existing competitors or new ones would take their place.

Special Treatment Would Not Necessarily Save Money

The special treatment provision would allow airline pension plans to fully fund their pension promises over either 17 years or 10 years instead of the 7-year period that would be required for pension plans in other industries. Supporters claim that the extra time would make it less likely that the PBGC would have to take over the plan. They further claim that the provision would actually save the PBGC money because PBGC guarantees of unfunded pension promises would be frozen as of the provision date. However, these savings would not necessarily occur due to other details of the provision.

The special treatment gives the airlines two options: Either freeze the pension plan so that no new benefits are credited to employees or allow employees to build pension benefits but pay for those new benefit promises on an expedited basis. In either case, under the language that was included in the Senate bill, the current unfunded pension promises could be funded over 17 years using a much higher interest rate (8.85 percent) than the rate that other pension plans would be required to use. As a result, airline pension plans not only would have much longer to pay for the benefits, but also would have to contribute less money to be considered fully funded. The ability to use a different rate in calculating their payments could substantially change the amount that airlines would have to pay.

On top of that, even if airline pension plans do freeze their benefits, they will continue to pay out full promised benefits to current retirees and close to full promised benefits to employees who retire early within that 17-year period. However, their pension plans' underfunding would not be significantly reduced for many years. Thus, if an airline filed for bankruptcy again—and many of them have filed for bankruptcy a number of times—its pension plan could be even more severely underfunded than it is now.

Special treatment for industries with high risks of pension-plan default is not the way to deal with a changed business environment. While airline pension plans are extremely expensive, those plans are only one of many challenges that the airlines face. To make matters worse, the airline industry is only the latest to face massive failures due in part to poorly funded pension plans. In the past few years, most of the steel industry has gone into bankruptcy and passed its pension obligations on to the PBGC. Airline failures are already being followed by major bankruptcies in the auto parts industry, and eventually the auto manufacturers themselves could go bankrupt. All of these industries face or have faced expensive pension plans, and it is difficult to justify treating one industry better than another. Most importantly, why should an airline employee receive better treatment than a steel worker whose plan failed in 2003?

A Targeted Veto

Although the airline and government contractor provisions are so dangerous to pension funding that any bill containing them should be vetoed, H.R. 4 does contain many other important reforms. Among the most important is language removing any legal questions about the ability of employers to auto-enroll workers into 401(k)-type defined contribution pension plans.

President Bush's veto message should state clearly that he will not sign a bill that includes any provisions that offer special treatment to an industry. At the same time, he should also explicitly say that he would sign the same bill if such provisions were removed.

Finally, H.R. 4 also includes a number of provisions unrelated to pensions—such as $50 million to repair a scenic road in Montana (reportedly sought by Senator Max Baucus (D-MT)), a provision easing the funding of an Alaska dam, and dozens of tariff extensions and exemptions. None of these provisions has any place in a pension bill, and their inclusion in the final version only strengthens the case for a veto.

Conclusion

Pension promises made to workers should be kept and paid for by the companies that made those promises. The airline provisions and other special interest provisions of H.R. 4 are bad policy and even worse precedent. Signing such provisions into law would practically guarantee special treatment for any company or industry that runs into trouble funding its pension plans and has a decent lobbyist. This would lead to a massive taxpayer bailout.

President Bush should save Congress from itself by vetoing H.R. 4 if the airline provisions remain in the bill.

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