

UNITED AIR LINES INC
 Form 10-Q
 July 24, 2008

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**UNITED STATES
 SECURITIES AND EXCHANGE COMMISSION
 Washington, D.C. 20549
 FORM 10-Q**

(Mark One)

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)
 OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended **June 30, 2008**

OR

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d)
 OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from _____ to _____

Commission File Number	Exact Name of Registrant as Specified in its Charter, Principal Office Address and Telephone Number	State of Incorporation	I.R.S. Employer Identification No
001-06033	UAL Corporation	Delaware	36-2675207
001-11355	United Air Lines, Inc. 77 W. Wacker Drive Chicago, Illinois 60601 (312) 997-8000	Delaware	36-2675206

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

UAL Corporation Yes No
 United Air Lines, Inc. Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

UAL Corporation Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company
 (Do not check if a smaller reporting company)

United Air Lines, Inc. Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company
 (Do not check if a smaller reporting company)

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Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

UAL Corporation	Yes <input type="radio"/> No <input checked="" type="radio"/>
United Air Lines, Inc.	Yes <input type="radio"/> No <input checked="" type="radio"/>

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Section 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court.

UAL Corporation	Yes <input checked="" type="radio"/> No <input type="radio"/>
United Air Lines, Inc.	Yes <input checked="" type="radio"/> No <input type="radio"/>

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of July 18, 2008.

UAL Corporation	126,593,928 shares of common stock (\$0.01 par value)
United Air Lines, Inc.	205 (100% owned by UAL Corporation)
	There is no market for United Air Lines, Inc. common stock.

**UAL Corporation and Subsidiary Companies and
United Air Lines, Inc. and Subsidiary Companies**

Report on Form 10-Q

For the Quarter Ended June 30, 2008

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

UAL Corporation and Subsidiary Companies

Condensed Statements of Consolidated Operations (Unaudited)

(In millions, except per share amounts)

	Three Months Ended June 30,	
	2008	2007
Operating revenues:		
Passenger United Airlines	\$ 4,099	\$ 3,968
Passenger Regional Affiliates	797	804
Cargo	237	181
Other operating revenues	238	260
	5,371	5,213
Operating expenses:		
Aircraft fuel	1,848	1,206
Salaries and related costs	1,179	1,019
Regional affiliates	847	733
Purchased services	371	335
Aircraft maintenance materials and outside repairs	295	284
Depreciation and amortization	216	229
Landing fees and other rent	199	215
Distribution expenses	193	197
Aircraft rent	100	105
Cost of third party sales	65	77
Goodwill impairment (Note 3)	2,277	
Other impairments (Note 3)	223	
Other operating expenses	252	276
	8,065	4,676
Income (loss) from operations	(2,694)	537
Other income (expense):		
Interest expense	(126)	(139)
Interest income	28	62
Interest capitalized	5	4
Miscellaneous, net	28	1
	(65)	(72)
Income (loss) before income taxes and equity in earnings of affiliates	(2,759)	465
Income tax expense (benefit)	(29)	192
Income (loss) before equity in earnings of affiliates	(2,730)	273
Equity in earnings of affiliates, net of tax	1	1
Net income (loss)	\$(2,729)	\$ 274
Earnings (loss) per share, basic	\$(21.47)	\$ 2.31

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Earnings (loss) per share, diluted	\$ (21.47)	\$ 1.83
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See accompanying *Combined Notes to Condensed Consolidated Financial Statements (Unaudited)*.

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UAL Corporation and Subsidiary Companies

Condensed Statements of Consolidated Operations (Unaudited)

(In millions, except per share amounts)

	Six Months Ended June 30,	
	2008	2007
Operating revenues:		
Passenger United Airlines	\$ 7,644	\$ 7,232
Passenger Regional Affiliates	1,512	1,479
Cargo	455	349
Other operating revenues	471	526
	10,082	9,586
Operating expenses:		
Aircraft fuel	3,423	2,247
Salaries and related costs	2,225	2,087
Regional affiliates	1,626	1,425
Purchased services	720	636
Aircraft maintenance materials and outside repairs	612	565
Depreciation and amortization	436	449
Landing fees and other rent	429	453
Distribution expenses	377	385
Aircraft rent	199	205
Cost of third party sales	129	170
Goodwill impairment (Note 3)	2,277	
Other impairments and special items (Notes 3 and 4)	223	(22)
Other operating expenses	541	541
	13,217	9,141
Income (loss) from operations	(3,135)	445
Other income (expense):		
Interest expense	(261)	(345)
Interest income	76	120
Interest capitalized	10	9
Miscellaneous, net	9	(1)
	(166)	(217)
Income (loss) before income taxes and equity in earnings of affiliates	(3,301)	228
Income tax expense (benefit)	(32)	108
Income (loss) before equity in earnings of affiliates	(3,269)	120
Equity in earnings of affiliates, net of tax	3	2
Net income (loss)	\$ (3,266)	\$ 122
Income (loss) per share, basic	\$ (26.33)	\$ 1.00
Income (loss) per share, diluted	\$ (26.33)	\$ 0.88

See accompanying *Combined Notes to Condensed Consolidated Financial Statements (Unaudited)*.

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UAL Corporation and Subsidiary Companies

Condensed Statements of Consolidated Financial Position (Unaudited)

(In millions, except shares)

	June 30, 2008	December 31, 2007
<i>Assets</i>		
Current assets:		
Cash and cash equivalents	\$ 2,899	\$ 1,259
Short-term investments		2,295
Restricted cash	442	325
Receivables, less allowance for doubtful accounts (2008 \$28; 2007 \$27)	1,345	888
Prepaid fuel	749	493
Aircraft fuel, spare parts and supplies, less obsolescence allowance (2008 \$31; 2007 \$25)	257	242
Deferred income taxes		78
Prepaid expenses and other	489	515
	6,181	6,095
Operating property and equipment:		
Owned		
Flight equipment	9,502	9,335
Advances on flight equipment		102
Other property and equipment	1,748	1,669
	11,250	11,106
Less accumulated depreciation and amortization	(1,367)	(1,062)
	9,883	10,044
Capital leases:		
Flight equipment	1,209	1,449
Other property and equipment	34	34
	1,243	1,483
Less accumulated amortization	(181)	(168)
	1,062	1,315
	10,945	11,359
Other assets:		
Intangibles, less accumulated amortization (2008 \$293; 2007 \$324)	2,741	2,871
Goodwill		2,280
Aircraft lease deposits	334	340
Restricted cash	213	431
Investments	101	122
Other, net	821	722
	4,210	6,766
	\$21,336	\$ 24,220

See accompanying *Combined Notes to Condensed Consolidated Financial Statements (Unaudited)*.

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UAL Corporation and Subsidiary Companies

Condensed Statements of Consolidated Financial Position (Unaudited) (Continued)

(In millions, except shares)

	June 30, 2008	December 31, 2007
<i>Liabilities and Stockholders' Equity (Deficit)</i>		
Current liabilities:		
Advance ticket sales	\$ 2,786	\$ 1,918
Mileage Plus deferred revenue	1,350	1,268
Accounts payable	893	877
Accrued salaries, wages and benefits	793	896
Fuel purchase commitments	749	493
Long-term debt maturing within one year	694	678
Advanced purchase of miles	620	694
Current obligations under capital leases	112	250
Accrued interest	112	141
Distribution payable	6	257
Other	588	507
	8,703	7,979
Long-term debt	6,143	6,415
Long-term obligations under capital leases	1,047	1,106
Other liabilities and deferred credits:		
Mileage Plus deferred revenue	2,635	2,569
Postretirement benefit liability	1,848	1,829
Deferred income taxes	529	638
Other	926	895
	5,938	5,931
Commitments and contingent liabilities (Note 14)		
Mandatorily convertible preferred securities (Note 6)	75	371
Stockholders' equity (deficit) (Note 6):		
Preferred stock		
Common stock at par, \$0.01 par value; authorized 1,000,000,000 shares; outstanding 125,789,535 and 116,921,049 shares at June 30, 2008 and December 31, 2007, respectively	1	1
Additional capital invested	2,456	2,139
Retained earnings (deficit)	(3,116)	152
Stock held in treasury, at cost	(25)	(15)
Accumulated other comprehensive income	114	141
	(570)	2,418
	\$21,336	\$ 24,220

See accompanying *Combined Notes to Condensed Consolidated Financial Statements (Unaudited)*.

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UAL Corporation and Subsidiary Companies

Condensed Statements of Consolidated Cash Flows (Unaudited)

(In millions)

	Six Months Ended June 30,	
	2008	2007
Cash flows provided (used) by operating activities:		
Net income (loss)	\$(3,266)	\$ 122
Adjustments to reconcile to net cash provided (used) by operating activities		
Goodwill impairment	2,277	
Other impairments	223	
Increase in advance ticket sales	868	988
Increase in receivables	(461)	(316)
Depreciation and amortization	436	449
Increase in Mileage Plus deferred revenue and advanced purchase of miles	74	197
Deferred income taxes	(32)	131
Other, net	18	89
	137	1,660
Cash flows provided (used) by investing activities:		
Net (purchases) sales of short-term investments	2,295	(2,270)
Additions to property and equipment	(232)	(146)
(Increase) decrease in restricted cash	101	(24)
Proceeds from litigation on advance deposits	41	
Proceeds from the sale of property and equipment	14	11
Other, net	(22)	(26)
	2,197	(2,455)
Cash flows provided (used) by financing activities:		
Special distribution to common shareholders	(251)	
Repayment of Credit Facility	(9)	(986)
Repayment of other debt	(351)	(1,023)
Principal payments under capital leases	(200)	(48)
Decrease in capital lease deposits	154	
Increase in deferred financing costs	(111)	(20)
Proceeds from issuance of secured notes	84	694
Other, net	(10)	13
	(694)	(1,370)
Increase (decrease) in cash and cash equivalents during the period	1,640	(2,165)
Cash and cash equivalents at beginning of the period	1,259	3,832
Cash and cash equivalents at end of the period	\$ 2,899	\$ 1,667

See accompanying *Combined Notes to Condensed Consolidated Financial Statements (Unaudited)*.

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United Air Lines, Inc. and Subsidiary Companies

Condensed Statements of Consolidated Operations (Unaudited)

(In millions)

	Three Months Ended June 30,	
	2008	2007
Operating revenues:		
Passenger United Airlines	\$ 4,099	\$ 3,968
Passenger Regional Affiliates	797	804
Cargo	237	181
Other operating revenues	238	263
	5,371	5,216
Operating expenses:		
Aircraft fuel	1,848	1,206
Salaries and related costs	1,180	1,018
Regional affiliates	847	733
Purchased services	371	335
Aircraft maintenance materials and outside repairs	295	284
Depreciation and amortization	216	229
Landing fees and other rent	199	215
Distribution expenses	193	197
Aircraft rent	100	105
Cost of third party sales	64	76
Goodwill impairment (Note 3)	2,277	
Other impairments (Note 3)	223	
Other operating expenses	280	276
	8,093	4,674
Income (loss) from operations	(2,722)	542
Other income (expense):		
Interest expense	(126)	(139)
Interest income	28	64
Interest capitalized	5	4
Miscellaneous, net	28	
	(65)	(71)
Income (loss) before income taxes and equity in earnings of affiliates	(2,787)	471
Income tax expense (benefit)	(29)	194
Income (loss) before equity in earnings of affiliates	(2,758)	277
Equity in earnings of affiliates, net of tax	1	1
Net income (loss)	\$(2,757)	\$ 278

See accompanying *Combined Notes to Condensed Consolidated Financial Statements (Unaudited)*.

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United Air Lines, Inc. and Subsidiary Companies

Condensed Statements of Consolidated Operations (Unaudited)

(In millions)

	Six Months Ended June 30,	
	2008	2007
Operating revenues:		
Passenger United Airlines	\$ 7,644	\$ 7,232
Passenger Regional Affiliates	1,512	1,479
Cargo	455	349
Other operating revenues	471	533
	10,082	9,593
Operating expenses:		
Aircraft fuel	3,423	2,247
Salaries and related costs	2,226	2,086
Regional affiliates	1,626	1,425
Purchased services	720	636
Aircraft maintenance materials and outside repairs	612	565
Depreciation and amortization	436	449
Landing fees and other rent	429	453
Distribution expenses	377	385
Aircraft rent	200	206
Cost of third party sales	128	168
Goodwill impairment (Note 3)	2,277	
Other impairments and special items (Notes 3 and 4)	223	(22)
Other operating expenses	568	540
	13,245	9,138
Income (loss) from operations	(3,163)	455
Other income (expense):		
Interest expense	(260)	(345)
Interest income	76	124
Interest capitalized	10	9
Miscellaneous, net	8	(1)
	(166)	(213)
Income (loss) before income taxes and equity in earnings of affiliates	(3,329)	242
Income tax expense (benefit)	(33)	114
Income (loss) before equity in earnings of affiliates	(3,296)	128
Equity in earnings of affiliates, net of tax	3	2
Net income (loss)	\$ (3,293)	\$ 130

See accompanying *Combined Notes to Condensed Consolidated Financial Statements (Unaudited)*.

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United Air Lines, Inc. and Subsidiary Companies

Condensed Statements of Consolidated Financial Position (Unaudited)

(In millions, except shares)

	June 30, 2008	December 31, 2007
<i>Assets</i>		
Current assets:		
Cash and cash equivalents	\$ 2,836	\$ 1,239
Short-term investments		2,259
Restricted cash	442	291
Receivables, less allowance for doubtful accounts (2008 \$28; 2007 \$27)	1,335	880
Prepaid fuel	749	493
Aircraft fuel, spare parts and supplies, less obsolescence allowance (2008 \$31; 2007 \$25)	257	242
Receivables from related parties	165	151
Deferred income taxes		72
Prepaid expenses and other	489	513
	6,273	6,140
Operating property and equipment:		
Owned		
Flight equipment	9,496	9,329
Advances on flight equipment		91
Other property and equipment	1,748	1,669
	11,244	11,089
Less accumulated depreciation and amortization	(1,366)	(1,062)
	9,878	10,027
Capital leases:		
Flight equipment	1,209	1,449
Other property and equipment	34	34
	1,243	1,483
Less accumulated amortization	(181)	(168)
	1,062	1,315
	10,940	11,342
Other assets:		
Intangibles, less accumulated amortization (2008 \$293; 2007 \$324)	2,741	2,871
Goodwill		2,280
Aircraft lease deposits	334	340
Restricted cash	208	431
Investments	101	122
Other, net	810	710
	4,194	6,754
	\$21,407	\$ 24,236

See accompanying *Combined Notes to Condensed Consolidated Financial Statements (Unaudited)*.

United Air Lines, Inc. and Subsidiary Companies

Condensed Statements of Consolidated Financial Position (Unaudited)

(In millions, except shares)

	June 30, 2008	December 31, 2007
<i>Liabilities and Stockholder's Equity (Deficit)</i>		
Current liabilities:		
Advance ticket sales	\$ 2,786	\$ 1,918
Mileage Plus deferred revenue	1,350	1,268
Accounts payable	891	882
Accrued salaries, wages and benefits	793	896
Fuel purchase commitments	749	493
Long-term debt maturing within one year	692	678
Advanced purchase of miles	620	694
Current obligations under capital leases	112	250
Accrued interest	112	141
Other	891	723
	8,996	7,943
Long-term debt	6,143	6,412
Long-term obligations under capital leases	1,047	1,106
Other liabilities and deferred credits:		
Mileage Plus deferred revenue	2,635	2,569
Postretirement benefit liability	1,848	1,829
Deferred income taxes	444	555
Other	926	895
	5,853	5,848
Commitments and contingent liabilities (Note 14)		
Parent company mandatorily convertible preferred securities (Note 6)	75	371
Stockholder's equity (deficit) (Note 6):		
Common stock at par, \$5 par value; authorized 1,000 shares; outstanding 205 at both June 30, 2008 and December 31, 2007		
Additional capital invested	2,315	2,000
Retained earnings (deficit)	(3,136)	415
Accumulated other comprehensive income	114	141
	(707)	2,556
	\$21,407	\$ 24,236

See accompanying *Combined Notes to Condensed Consolidated Financial Statements (Unaudited)*.

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United Air Lines, Inc. and Subsidiary Companies

Condensed Statements of Consolidated Cash Flows (Unaudited)

(In millions)

	Six Months Ended June 30,	
	2008	2007
Cash flows provided (used) by operating activities:		
Net income (loss)	\$(3,293)	\$ 130
Adjustments to reconcile to net cash provided (used) by operating activities		
Goodwill impairment	2,277	
Other impairments	223	
Increase in advance ticket sales	868	988
Increase in receivables	(459)	(309)
Depreciation and amortization	436	449
Increase in Mileage Plus deferred revenue and advanced purchase of miles	74	197
Deferred income taxes	(31)	137
Other, net	101	57
	196	1,649
Cash flows provided (used) by investing activities:		
Net (purchases) sales of short-term investments	2,259	(2,239)
Additions to property and equipment	(232)	(146)
(Increase) decrease in restricted cash	72	(29)
Proceeds from the sale of property and equipment	14	10
Other, net	(22)	(27)
	2,091	(2,431)
Cash flows provided (used) by financing activities:		
Dividend to parent	(258)	
Repayment of Credit Facility	(9)	(986)
Repayment of other debt	(350)	(1,022)
Principal payments under capital leases	(200)	(48)
Decrease in capital lease deposits	154	
Increase in deferred financing costs	(111)	(20)
Proceeds from issuance of secured notes	84	694
Other, net		30
	(690)	(1,352)
Increase (decrease) in cash and cash equivalents during the period	1,597	(2,134)
Cash and cash equivalents at beginning of the period	1,239	3,779
Cash and cash equivalents at end of the period	\$ 2,836	\$ 1,645

See accompanying *Combined Notes to Condensed Consolidated Financial Statements (Unaudited)*.

**UAL Corporation and Subsidiary Companies and
United Air Lines, Inc. and Subsidiary Companies**

Combined Notes to Condensed Consolidated Financial Statements (Unaudited)

(1) Basis of Presentation

UAL Corporation (together with its consolidated subsidiaries, "UAL"), is a holding company and its principal, wholly-owned subsidiary is United Air Lines, Inc. (together with its consolidated subsidiaries, "United"). We sometimes use the words "we," "our," "us," and the "Company" in this Form 10-Q for disclosures that relate to both UAL and United.

This Quarterly Report on Form 10-Q is a combined report of UAL and United. Therefore, these *Combined Notes to Condensed Consolidated Financial Statements (Unaudited)* apply to both UAL and United, unless otherwise noted. As UAL consolidates United for financial statement purposes, disclosures that relate to activities of United also apply to UAL.

Interim Financial Statements. The UAL and United unaudited condensed consolidated financial statements shown here have been prepared as required by the U.S. Securities and Exchange Commission (the "SEC"). Some information and footnote disclosures normally included in financial statements that meet accounting principles generally accepted in the United States ("GAAP") have been condensed or omitted as permitted by the SEC. UAL and United believe that the disclosures presented here are not misleading. The financial statements include all adjustments, including asset impairments, severance and normal recurring adjustments that are considered necessary for a fair presentation of the financial position and results of operations of UAL and United. These financial statements should be read together with the information included in the combined UAL and United Annual Report on Form 10-K for the year ended December 31, 2007 (the "2007 Annual Report").

Investments. The Company's cash equivalents and short-term investments are classified as held-to-maturity. In addition, the Company has \$67 million of debt securities that are reported as non-current investments, which are classified as available-for-sale. The non-current debt investments are some of the Company's previously issued debt instruments that were acquired in open market transactions during 2007.

Mileage Plus Accounting. Since the earnings process is not complete at the time miles are earned by Mileage Plus members or sold to third parties, a portion of the revenue from ticket sales that relates to earned miles and revenue from the sale of miles to third parties is deferred and recognized as revenue at the time the miles are redeemed by members. For those miles that the Company estimates will go unredeemed by members, the Company recognizes revenue over the expected customer redemption period.

In 2007, the Company's estimate of expired miles was limited to miles that were expected to deactivate after an 18 month period of account inactivity as defined in the Mileage Plus program rules ("deactivated miles"). United estimated the number of accounts that it expected to deactivate and ratably recognized revenue for these expected deactivated miles over the 18 month period of inactivity.

In 2008, the Company updated certain of its assumptions related to the recognition of revenue for expiration of miles. Based on additional analysis of mileage redemption and expiration patterns, the Company revised the estimated number of miles that are expected to expire from 15% to 24% of earned miles, including miles that will expire or go unredeemed for reasons other than account deactivation. In 2008, the Company also extended the total period of time over which revenue from the expiration of miles is recognized taking into consideration the estimated period of miles redemption. These changes are expected to result in the recognition of revenue from expired miles in proportion to

**UAL Corporation and Subsidiary Companies and
United Air Lines, Inc. and Subsidiary Companies**

Combined Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

(1) Basis of Presentation (Continued)

the pattern of revenue recognition from customer redemptions of miles. The Company does not expect these changes in estimate to materially impact Mileage Plus revenue recognition in 2008.

(2) Company Operational Plans

The unprecedented increase in crude oil spot prices to approximately \$140 per barrel in the second quarter of 2008, a weakening economic environment and a highly competitive industry with excess capacity have created an extremely challenging environment for the Company. The Company's results have been adversely impacted by these factors as indicated by its significant losses in the first and second quarters of 2008. In addition, the Company's results in the three and six month periods ended June 30, 2008 included asset impairment charges of approximately \$2.5 billion that resulted primarily from these unfavorable market and economic conditions as discussed in Note 3, "Impairments." The Company has begun implementing a plan to address its increased operating costs. Highlights of this plan include the following:

The Company is significantly reducing mainline domestic and consolidated capacity. By the fourth quarter of 2008, the Company expects mainline domestic and consolidated capacity to be down approximately 16% and 11% year-over-year, respectively.

The capacity reductions will be made through reductions in frequencies of routes and the elimination of unprofitable routes. These actions will result in the closure of a small number of airport operations where United cannot operate profitably at current fuel prices.

The Company has announced plans to permanently remove 100 aircraft from its mainline fleet by the end of 2009, including its entire B737 fleet and six B747 aircraft. The B737 aircraft being retired are some of the oldest and least fuel efficient in the Company's fleet.

United is eliminating its Ted product for leisure markets and will reconfigure that fleet's 56 A320s to include United First Class seats. The reconfiguration of the Ted aircraft will begin in spring 2009 and be completed by year-end 2009.

In connection with the capacity reductions, the Company is further streamlining its operations and corporate functions in order to reduce the size of its workforce to match the size of its operations as further discussed below.

The Company also recently entered into an alliance partnership with Continental Airlines that is expected to create revenue enhancements, costs savings and operational efficiencies.

The following is a discussion of expenses associated with implementing the Company's plans.

Severance. During the second quarter of 2008, the Company began reducing its workforce in operations and corporate functions through attrition and both voluntary and involuntary layoffs. The Company is streamlining its workforce to match the size of its operations. The Company is planning a workforce reduction of approximately 7,000 employees by the end of 2009. The Company's standard severance policies provide the affected employees with salary continuation as well as certain insurance benefits for a specified period of time. The Company recognizes its severance obligations in accordance with Statement of Financial Accounting Standards No. 112 (As Amended), *Employers' Accounting for Postemployment Benefits* an amendment of FASB Statements No. 5 and 43, except for voluntary

UAL Corporation and Subsidiary Companies and
United Air Lines, Inc. and Subsidiary Companies

Combined Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

(2) Company Operational Plans (Continued)

programs which are accounted for under Statement of Financial Accounting Standards No. 88, *Employers' Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits*.

The \$82 million of severance accrued in the second quarter of 2008 relates to both salaried and management employee positions and certain of the Company's unionized workforce. The Company's severance payments were immaterial in the second quarter of 2008, as most separations will occur after June 30, 2008 in accordance with the fleet reductions expected to begin in late summer 2008 and continuing into 2009. In addition to furloughs, the Company is currently offering furlough-mitigation programs, such as early-out options, to certain union groups. Termination benefits expected to be paid under such voluntary programs are not recognized until the employees accept the termination benefit offer. Therefore, as the Company continues to implement its reductions in force during the remainder of 2008 and 2009, additional severance costs will be incurred. The severance expense recorded in the three and six months ended June 30, 2008 is classified within salaries and related costs on the Company's *Condensed Statements of Consolidated Earnings (Unaudited)*. The severance charges are expected to be primarily within the Mainline segment where the fleet reductions will occur.

Aircraft. At June 30, 2008, UAL had 93 B737 aircraft consisting of 46 owned aircraft and 47 leased aircraft, which are planned to be grounded throughout 2008 and 2009. The leased aircraft are operated under leases accounted for as operating leases, and the Company may incur future charges associated with the early termination of certain of these aircraft leases. During the six months ended June 30, 2008, the Company entered into an agreement to sell three owned B737 aircraft, of which one aircraft was delivered during the period.

Other costs. The Company expects to incur costs, which have not been recognized in its consolidated financial statements, as the Company implements the plans discussed above. These costs may include various charges to convert its Ted aircraft, costs to close additional stations and severance benefits to be incurred under the furlough-mitigation plans, among others. In addition, as discussed in Note 3, "Impairments," the Company recorded significant asset impairments in the second quarter of 2008. Additional tangible and intangible asset impairments could occur in future periods.

(3) Impairments

In accordance with Statement of Financial Accounting Standards No. 142, *Goodwill and Other Intangible Assets* ("SFAS 142"), and Statement of Financial Accounting Standards No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets* ("SFAS 144"), as of May 31, 2008 the Company performed an interim impairment test of its goodwill, all intangible assets and certain of its long-lived assets (principally aircraft and related spare engines and spare parts) due to events and changes in circumstances during the first and second quarters of 2008 that indicated an impairment might have occurred.

Factors deemed by management to have collectively constituted an impairment triggering event included record high fuel prices, significant losses in the first and second quarters of 2008, a softening U.S. economy, analyst downgrade of UAL common stock, rating agency changes in outlook for the Company's debt instruments from stable to negative, the announcement of the planned removal from UAL's fleet of 100 aircraft in 2008 and a significant decrease in the fair value of the Company's

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Combined Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

(3) Impairments (Continued)

outstanding equity and debt securities during the six months ended June 30, 2008, including a decline in UAL's market capitalization to significantly below book value. The Company's consolidated fuel expense increased by more than 50%, or \$773 million and \$1.4 billion, in the three and six month periods ended June 30, 2008, respectively, as compared to the prior year respective periods.

As a result of this impairment testing, the Company recorded impairment charges during the three and six months ended June 30, 2008, as presented in the table below. All of these impairment charges are within the Mainline segment. All of the impairments other than the goodwill impairment, which is separately identified, are classified within "Other impairments" in the Company's *Condensed Statements of Consolidated Operations (Unaudited)*.

(In millions)	
Goodwill impairment	\$2,277
Indefinite-lived intangible assets:	
Codeshare agreements	60
Tradenames	20
Intangible asset impairments	80
Tangible assets:	
Pre-delivery advance deposits including related capitalized interest	105
B737 aircraft, B737 spare parts and other	38
Aircraft and related deposit impairments	143
Total impairments	\$2,500

Goodwill

For purposes of testing goodwill, the Company estimated the fair value of the mainline reporting unit (to which all goodwill is allocated) utilizing several fair value measurement techniques, including two market estimates and one income estimate, and using relevant data available through and as of May 31, 2008. The market approach is a valuation technique in which fair value is estimated based on observed prices in actual transactions and on asking prices for similar assets. The valuation process is essentially that of comparison and correlation between the subject asset and other similar assets. The income approach is a technique in which fair value is estimated based on the cash flows that an asset could be expected to generate over its useful life, including residual value cash flows. These cash flows are discounted to their present value equivalents using a rate of return that accounts for the relative risk of not realizing the estimated annual cash flows and for the time value of money. Variations of the income approach were used to determine certain of the intangible asset fair values.

Under the market approaches, the fair value of the mainline reporting unit was estimated based upon the fair value of invested capital for UAL, as well as a separate comparison to revenue and EBITDAR multiples for similar publicly traded companies in the airline industry. The fair value estimates using both market approaches included a control premium similar to those observed for historical airline and transportation company market transactions.

Under the income approach, the fair value of the mainline reporting unit was estimated based upon the present value of estimated future cash flows for UAL. The income approach is dependent on

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Combined Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

(3) Impairments (Continued)

a number of critical management assumptions including estimates of future capacity, passenger yield, traffic, operating costs (including fuel prices), appropriate discount rates and other relevant assumptions. The Company estimated its future fuel-related cash flows for the income approach based on the five-year forward curve for crude oil as of May 31, 2008. The impacts of the Company's aircraft and other tangible and intangible asset impairments were considered in the fair value estimation of the Mainline reporting unit.

Taking into consideration an equal weighting of the two market estimates and the income estimate, which has been the Company's practice when performing annual goodwill impairment tests, the indicated fair value of the Mainline reporting unit was less than its carrying value, and therefore, the Company was required to perform Step Two of the SFAS 142 goodwill impairment testing methodology.

In Step Two of the impairment testing, the Company determined the implied fair value of goodwill of the Mainline reporting unit by allocating the fair value of the reporting unit determined in Step One to all the assets and liabilities of the Mainline reporting unit, including any recognized and unrecognized intangible assets, as if the reporting unit had been acquired in a business combination and the fair value of the reporting unit was the price paid to acquire the reporting unit. As a result of the Step Two testing, the Company determined that goodwill was completely impaired and therefore recorded an impairment charge during the second quarter of 2008 to write-off the full value of goodwill. An adjustment to the fair values may be required in the third quarter of 2008, when the Company finalizes its testing.

Indefinite-lived intangible assets

The Company utilized appropriate valuation techniques to separately estimate the fair values of all of its indefinite-lived intangible assets as of May 31, 2008, and compared those estimates to related carrying values. Tested assets included trade names, international route authorities, London-Heathrow slots and code sharing agreements. The Company used a market or income valuation approach, as described above, to estimate fair values. Based on the preliminary results of this testing, the Company recorded \$80 million of impairment charges during the second quarter of 2008. An adjustment to the fair values may be required in the third quarter of 2008, when the Company finalizes its testing.

Long-lived assets

For purposes of testing impairment of long-lived assets at May 31, 2008, the Company determined whether the carrying amount of its long-lived assets was recoverable by comparing the carrying amount to the sum of the undiscounted cash flows expected to result from the use and eventual disposition of the assets. If the carrying value of the assets exceeded the expected cash flows, the Company estimated the fair value of these assets to determine whether an impairment existed. The Company grouped its aircraft by fleet type to perform this evaluation and used data and assumptions through May 31, 2008. The estimated undiscounted cash flows were dependent on a number of critical management assumptions including estimates of future capacity, passenger yield, traffic, operating costs (including fuel prices) and other relevant assumptions. If estimates of fair value were required, fair value was estimated using the market approach. Asset appraisals, published aircraft pricing guides and recent transactions for similar aircraft were considered by the Company in its market value determination. As

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Combined Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

(3) Impairments (Continued)

of May 31, 2008, based on the results of these tests, the Company determined that an impairment of \$36 million existed which was attributable to the Company's fleet of owned B737 aircraft and related spare parts. As described in Note 2, "Company Operational Plans," the Company is retiring its entire B737 fleet earlier than originally planned. The Company recorded an additional \$2 million impairment for other assets.

Due to the unfavorable economic and industry factors described above, the Company also determined that it was required to perform an impairment test of its \$105 million of pre-delivery aircraft deposits and related capitalized interest. The Company estimated that these aircraft deposits were completely impaired and wrote off their full carrying value. The Company believes that it is highly unlikely that it will take future aircraft deliveries and, therefore, the Company will be required to forfeit the deposits, which are also not transferable.

As a result of the impairment testing described above, the Company's goodwill and certain of its indefinite-lived intangible assets and tangible assets were recorded at fair value. In accordance with FASB Staff Position No. 157-2, *Effective Date of FASB Statement No. 157*, the Company has not applied SFAS 157 to the determination of the fair value of these assets. However, the provisions of SFAS 157 were applied to the determination of the fair value of financial assets and financial liabilities that were part of the SFAS 142 Step Two goodwill fair value determination.

Due to extreme fuel price volatility, tight credit markets, the decline in UAL's market capitalization and in the fair value of its debt securities, the uncertain economic environment, as well as other uncertainties, the Company can provide no assurance that a material impairment charge of aircraft or indefinite-lived intangible assets will not occur in a future period. The value of our aircraft could be impacted in future periods by changes in the market for these aircraft. Such changes could result in a greater supply and lower demand for certain aircraft types as other carriers announce plans to retire similar aircraft. The Company will continue to monitor circumstances and events in future periods to determine whether additional asset impairment testing is warranted.

(4) Voluntary Reorganization Under Chapter 11 of the United States Bankruptcy Code

Bankruptcy Considerations. UAL and United emerged from bankruptcy protection on February 1, 2006 (the "Effective Date"), the effective date of the Debtors' Second Amended Joint Plan of Reorganization Pursuant to Chapter 11 of the United States Bankruptcy Code (the "Plan of Reorganization") confirmed by the United States Bankruptcy Court for the Northern District of Illinois, Eastern Division (the "Bankruptcy Court"). The following discussion provides general background information regarding the Company's pending litigation related to the bankruptcy reorganization, and is not intended to be an exhaustive summary. Detailed information pertaining to the bankruptcy filings may be obtained at www.pd-ual.com.

Significant Matters Remaining to be Resolved in Chapter 11 Cases. The following matters remain to be resolved in the Bankruptcy Court or another court:

(a)

SFO Municipal Bond Secured Interest. HSBC Bank Inc. ("HSBC"), as trustee for the 1997 municipal bonds related to San Francisco International Airport ("SFO"), filed a complaint against United asserting a security interest in United's leasehold for portions of its maintenance base at SFO. Pursuant to Section 506(a) of the Bankruptcy Code, HSBC alleges

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Combined Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

(4) Voluntary Reorganization Under Chapter 11 of the United States Bankruptcy Code (Continued)

that it is entitled to be paid the value of that security interest, which HSBC had claimed was as much as \$257 million. HSBC and United went to trial in April 2006 and the Bankruptcy Court rejected as a matter of law HSBC's \$257 million claim. HSBC subsequently alleged that it was entitled to \$154 million, or at a minimum, approximately \$93 million. The parties tried the case and filed post-trial briefs, which were heard by the Bankruptcy Court. In October 2006, the Bankruptcy Court issued its written opinion holding that the value of the security interest is approximately \$27 million. United has accrued \$27 million as its estimated obligation as of June 30, 2008 and December 31, 2007. After the Bankruptcy Court denied various post-trial motions, both parties appealed to the U.S. District Court for the Northern District of Illinois ("the District Court") and on March 27, 2008 the District Court affirmed the Bankruptcy Court decision in all respects. HSBC filed a notice of appeal of the District Court's judgment on April 16, 2008.

(b)

LAX Municipal Bond Secured Interest. There is pending litigation before the District Court regarding the extent to which the Los Angeles International Airport ("LAX") municipal bond debt is entitled to secured status under Section 506(a) of the Bankruptcy Code. In 2007, the Bankruptcy Court issued its written opinion holding that the value of the security interest is approximately \$33 million. An appeal by both parties to the District Court resulted in an affirmation of this value on June 13, 2008. United has accrued this amount as its estimated obligation at both June 30, 2008 and December 31, 2007. The District Court's ruling is expected to be appealed to the U.S. Court of Appeals for the Seventh Circuit.

The special item of \$22 million in the six months ended June 30, 2007 relates to accrual reductions for pending SFO and LAX litigation.

Claims Resolution Process. As permitted under the bankruptcy process, the Debtors' creditors filed proofs of claim with the Bankruptcy Court. Through the claims resolution process, the Company identified many claims which were disallowed by the Bankruptcy Court for a number of reasons, such as claims that were duplicative, amended or superseded by later filed claims, were without merit, or were otherwise overstated. Throughout the Chapter 11 proceedings, the Company resolved many claims through settlement or objections ordered by the Bankruptcy Court. The Company will continue to settle claims and file additional objections with the Bankruptcy Court.

With respect to unsecured claims, approximately 112 million shares of UAL common stock were issued and distributed to holders of valid unsecured claims between February 2, 2006, the first distribution date established in the Company's Plan of Reorganization, and June 30, 2008. As of June 30, 2008, there are approximately 2.7 million remaining shares of UAL common stock being held in reserve to satisfy all of the remaining disputed and undisputed unsecured claim values, once the remaining claim disputes are resolved. The final distributions of shares will not occur until late 2008 or later, pending resolution of bankruptcy matters such as those discussed above. UAL and United currently estimate that the probable range of unsecured claims to be ultimately allowed by the Bankruptcy Court will be between \$29.3 billion and \$29.6 billion.

The table below includes the Company's activity related to the administrative and priority claims and other bankruptcy-related claim reserves including reserves related to legal, professional and tax matters, among others, for the six months ended June 30, 2008. These reserves are primarily classified

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Combined Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

(4) Voluntary Reorganization Under Chapter 11 of the United States Bankruptcy Code (Continued)

in other current liabilities in the *Condensed Statements of Consolidated Financial Position (Unaudited)*. As of June 30, 2008 and December 31, 2007, \$60 million of the administrative and priority claims accruals represents reserves for probable liabilities under the pending litigation to determine the extent to which security interests exist in the underlying facility leases for SFO and LAX, as described above.

(In millions)	
Balance at December 31, 2007	\$98
Payments	(3)
 Balance at June 30, 2008	 \$95

(5) New Accounting Pronouncements

In June 2008, the Financial Accounting Standards Board ("FASB") issued FASB Staff Position ("FSP") No. EITF 03-6-1, *Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities* ("EITF 03-6-1"). EITF 03-6-1 addresses whether instruments granted in share-based payment transactions are participating securities prior to vesting and, therefore, need to be included in the earnings allocation under the two-class method of calculating earnings per share. EITF 03-6-1, which is applied retrospectively, is effective for the Company beginning January 1, 2009. The Company is currently evaluating the potential impact of EITF 03-6-1 on its consolidated financial statements.

In May 2008, the FASB issued FSP No. APB 14-1, *Accounting for Convertible Debt Instruments That May Be Settled in Cash upon Conversion (Including Partial Cash Settlement)* ("APB 14-1"). APB 14-1 requires the issuer of certain convertible debt instruments that may be settled in cash (or other assets) on conversion to separately account for the liability (debt) and equity (conversion option) components of the instrument in a manner that reflects the issuer's nonconvertible debt borrowing rate. APB 14-1, which is applied retrospectively, is effective for the Company beginning January 1, 2009. The Company is currently evaluating the potential impact of APB 14-1 on its consolidated financial statements.

In March 2008, the FASB issued Statement of Financial Accounting Standards No. 161, *Disclosures about Derivative Instruments and Hedging Activities - an amendment of FASB Statement No. 133* ("SFAS 161"). This Statement changes the disclosure requirements for derivative instruments and hedging activities. Entities are required to provide enhanced disclosures about (a) how and why an entity uses derivative instruments, (b) how derivative instruments and related hedged items are accounted for under Statement of Financial Accounting Standards No. 133, *Accounting for Derivative Instruments and Hedging Activities* ("SFAS 133") and its related interpretations and (c) how derivative instruments and related hedged items affect an entity's financial position, financial performance, and cash flows. SFAS 161 is effective for the Company for periods beginning January 1, 2009, although early adoption is allowed. The Company has not determined whether it will adopt SFAS 161 prior to January 1, 2009, and is currently evaluating the potential impact of SFAS 161 on its consolidated financial statements.

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Combined Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

(5) New Accounting Pronouncements (Continued)

Effective January 1, 2008, the Company adopted Statement of Financial Accounting Standards No. 157, *Fair Value Measurements* ("SFAS 157"), with respect to its financial assets and financial liabilities. SFAS 157 does not require any new fair value measurements; rather it specifies valuation methods and disclosures to be applied when fair value measurements are required under existing or future accounting pronouncements. The adoption of SFAS 157 did not have a material impact on the Company's financial statements. FASB Staff Position No. FAS 157-2, issued in February 2008, delayed the effective date of SFAS 157 for nonfinancial assets and nonfinancial liabilities that are measured on a nonrecurring basis. The Company has not determined the impact, if any, that the adoption of SFAS 157 will have on its nonfinancial assets and nonfinancial liabilities. The Company will be required to apply SFAS 157 to these nonfinancial assets and nonfinancial liabilities effective January 1, 2009. See Note 13, "Fair Value Measurements and Derivative Instruments," for SFAS 157 disclosures related to financial assets and financial liabilities.

(6) Common Stockholders' Equity (Deficit) and Mandatorily Convertible Preferred Securities

Changes in the number of shares of UAL common stock outstanding and held in treasury during the six months ended June 30, 2008 were as follows:

UAL	Six Months Ended June 30, 2008
UAL common stock outstanding at beginning of period	116,921,049
Issuance of UAL common stock upon conversion of preferred stock	8,896,536
Issuance of UAL common stock to employees	208,164
Issuance of UAL common stock to creditors	60,200
Forfeiture of non-vested UAL restricted stock	(44,281)
Treasury shares acquired	(252,133)
 UAL common stock outstanding at end of period	 125,789,535
 Treasury shares at beginning of period	 396,595
Shares acquired for treasury	252,133
 Treasury shares at end of period	 648,728

As reflected in the table above, 8.9 million shares of UAL common stock were issued upon preferred stockholders' elections to exercise their conversion option of 4.0 million shares of 2% mandatorily convertible preferred stock during the first six months of 2008. The Company increased additional paid in capital by \$298 million and decreased the mandatorily convertible preferred stock by the same amount to record the impact of these conversions. See Note 4, "Voluntary Reorganization Under Chapter 11 of the United States Bankruptcy Code Claims Resolution Process" and Note 7, "Per Share Amounts" for information regarding shares of UAL common stock distributed to creditors in 2008 and 2.7 million shares that are reserved as of June 30, 2008 and will be distributed periodically to employees and holders of previously allowed claims and disputed claims that are pending final resolution. All treasury shares acquired during the six months ended June 30, 2008 were shares acquired for tax withholding obligations under UAL's share-based compensation plans.

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Combined Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

(7) Per Share Amounts (UAL Only)

In accordance with Statement of Financial Accounting Standards No. 128, *Earnings per Share* ("SFAS 128"), UAL basic per share amounts were computed by dividing earnings (loss) available to common shareholders by the weighted-average number of shares of common stock outstanding. Approximately 2.7 million shares of UAL common stock remaining to be issued to unsecured creditors and employees under the Plan of Reorganization are included in UAL outstanding basic shares, as the necessary conditions for issuance have been satisfied. UAL's \$530 million of 6% senior notes are callable at any time at 100% of par value, and can be redeemed with either cash or UAL common stock at UAL's option. These notes are not deemed potentially dilutive shares, as it is UAL's intent to redeem these notes with cash. The table below represents the computation of UAL basic and diluted

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Combined Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

(7) Per Share Amounts (UAL Only) (Continued)

per share amounts and the number of securities which have been excluded from the computation of diluted per share amounts as they have an anti-dilutive effect.

(In millions)	Three Months Ended June 30,		Six Months Ended June 30,	
	2008	2007	2008	2007
Basic earnings (loss) per share:				
Net income (loss)	\$(2,729)	\$ 274	\$(3,266)	\$ 122
Preferred stock dividend requirements		(2)	(2)	(5)
Earnings (loss) available to common stockholders	\$(2,729)	\$ 272	\$(3,268)	\$ 117
Basic weighted average shares outstanding	127.1	117.4	124.1	117.2
Earnings (loss) per share, basic	\$(21.47)	\$ 2.31	\$(26.33)	\$ 1.00
Diluted earnings (loss) per share:				
Earnings (loss) available to common stockholders	\$(2,729)	\$ 272	\$(3,268)	\$ 117
Effect of 2% preferred securities		2		5
Effect of 4.5% senior limited-subordination convertible notes		5		10
Effect of 5% convertible notes		1		2
Earnings (loss) available to common stockholders including the effect of dilutive securities	\$(2,729)	\$ 280	\$(3,268)	\$ 134
Basic weighted average shares outstanding	127.1	117.4	124.1	117.2
Effect of non-vested restricted shares		1.1		1.0
Effect of 2% preferred securities		10.9		10.9
Effect of 4.5% senior limited-subordination convertible notes		20.8		20.8
Effect of 5% convertible notes		3.2		3.2
Diluted weighted average shares outstanding	127.1	153.4	124.1	153.1
Earnings (loss) per share, diluted	\$(21.47)	\$ 1.83	\$(26.33)	\$ 0.88
<i>Potentially dilutive shares excluded from diluted per share amounts:</i>				
Stock options	4.3	4.4	4.3	4.4
Restricted shares	1.4	0.9	1.4	1.0
2% preferred securities	2.2		5.2	
4.5% senior limited-subordination convertible notes	22.2		22.2	
5% convertible notes	3.4		3.4	
	33.5	5.3	36.5	5.4

(8) Share-Based Compensation Plans

2008 Incentive Compensation Plan

In the first six months of 2008, UAL's Board of Directors and stockholders approved the UAL Corporation 2008 Incentive Compensation Plan (the "2008 Plan"). The 2008 Plan is an incentive compensation plan that allows the Company to use different forms of compensation awards to attract,

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Combined Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

(8) Share-Based Compensation Plans (Continued)

retain and reward eligible participants. The 2008 Plan replaced the UAL Corporation 2006 Management Equity Incentive Plan (the "MEIP"), which was automatically terminated with respect to future grants and otherwise replaced and superseded by the 2008 Plan on June 12, 2008. Any awards granted under the MEIP prior to June 12, 2008 remain in effect pursuant to their terms. Awards may not be granted under the 2008 Plan after June 11, 2018.

Any officer or employee of UAL or its affiliates is eligible to participate in the 2008 Plan. The 2008 Plan provides for the grant of options intended to qualify as incentive stock options ("ISOs") under Section 422 of the Code, nonqualified stock options ("NSOs"), stock appreciation rights ("SARs"), restricted share awards, restricted stock units ("RSUs"), performance compensation awards, performance units, cash incentive awards and other equity-based and equity-related awards. Any shares of our common stock issued under the 2008 Plan will consist, in whole or in part, of authorized and unissued shares or of treasury shares.

Subject to adjustment for changes in capitalization, the aggregate number of shares of UAL common stock that are available for delivery pursuant to awards granted under the 2008 Plan is equal to (1) 8,000,000 plus (2) the shares of UAL common stock that remained available under the MEIP as of June 12, 2008, including shares of UAL common stock with respect to awards granted under the MEIP that are forfeited after June 12, 2008. Subject to adjustment for changes in capitalization, (1) each share with respect to which an option or stock-settled SAR is granted under the 2008 Plan reduces the aggregate number of shares that may be delivered under the 2008 Plan by one share, and (2) each share with respect to which any other award denominated in shares is granted under the 2008 Plan reduces the aggregate number of shares that may be delivered under the 2008 Plan by 1.5 shares. Of the shares of UAL common stock available for awards under the 2008 Plan, the maximum number of shares that is permitted to be delivered pursuant to ISOs granted under the 2008 Plan is 2,000,000.

If an award granted under the 2008 Plan is forfeited, or otherwise expired, terminated or cancelled without the delivery of shares or were settled in cash, then the shares covered by such award are again available to be delivered pursuant to awards under the 2008 Plan. However, shares that are surrendered or tendered in payment of the exercise price of an award or any taxes required to be withheld in respect of an award will not become available to be delivered pursuant to awards under the 2008 Plan. Subject to adjustment for changes in capitalization, the maximum number of shares of common stock available to be granted pursuant to awards to any single participant in any fiscal year is 500,000. In the case of awards settled in cash based on the fair market value of a share, the maximum aggregate amount of cash permitted to be paid pursuant to awards granted to any single participant in any fiscal year is equal to the per share fair market value as of the relevant vesting, payment or settlement date, multiplied by the maximum number of shares which can be granted, as described above. The maximum aggregate amount of cash and other property (valued at fair market value) permitted to be paid or delivered pursuant to awards under the 2008 Plan, the value of which is not determined by reference to the fair market value of our shares, to any single participant in any fiscal year is \$5,000,000.

The 2008 Plan provides that, unless otherwise provided in an award agreement, in the event of a change of control of the Company (as defined in the 2008 Plan):

any options and SARs outstanding as of the date the change of control is determined to have occurred become fully exercisable and vested, as of immediately prior to the change of control.

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Combined Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

(8) Share-Based Compensation Plans (Continued)

all performance units, cash incentive awards and other awards designated as performance compensation awards will be paid out at the "target" performance level on a prorated basis based on the number of days elapsed from the beginning of the performance period up to and including the change of control.

all other outstanding awards are automatically deemed exercisable or vested and all restrictions and forfeiture provisions related thereto lapse as of immediately prior to such change of control.

Compensation Expense

Compensation expense associated with the UAL share-based compensation plans has been pushed down to United. The Company recognized share-based compensation expense of \$7 million and \$18 million during the three and six months ended June 30, 2008, respectively, and \$11 million and \$26 million during the three and six months ended June 30, 2007, respectively. The Company's unrecognized share-based compensation expense was \$31 million and \$41 million as of June 30, 2008 and December 31, 2007, respectively. As of June 30, 2008, 8,339,284 awards were available under the 2008 Plan and 66,937 awards were available under the Director Equity Incentive Plan ("DEIP"). As of December 31, 2007, a total of 728,237 awards were available for grant under the MEIP and DEIP. The table below summarizes stock option activity for the six months ended June 30, 2008:

	Options
Outstanding at beginning of period	4,150,093
Granted	297,900
Exercised	(6,864)
Canceled	(141,737)
Outstanding at end of period	4,299,392
Exercisable (vested) at end of period	1,970,763

The table below summarizes UAL's restricted stock activity for the six months ended June 30, 2008:

	Restricted Stock
Nonvested at beginning of period	2,017,989
Granted	203,300
Vested	(736,178)
Terminated	(44,281)
Nonvested at end of period	1,440,830

(9) Income Taxes

In the 2008 periods, the Company had an insignificant effective tax rate, as compared to the U.S. federal statutory rate of 35%, principally because of goodwill impairment charges in the second quarter that are not deductible for income tax purposes and the tax benefits of the Company's remaining net operating losses for the periods were almost completely offset by a valuation allowance. The reversal of

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Combined Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

(9) Income Taxes (Continued)

the deferred tax liability was recorded due to an \$80 million intangible asset impairment. For the three and six month periods ended June 30, 2007, UAL and United both had effective tax rates of 41% and 47%, respectively, which were based on forecasted income for 2007. Those rates differed from the statutory rate due principally to certain expenses recorded for financial statement purposes that were not deductible for income tax purposes.

The Company's management assesses the realizability of its deferred tax assets, and records a valuation allowance when it is more likely than not that a portion, or all, of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income, including the reversals of deferred tax liabilities during the periods in which those temporary differences will become deductible. UAL had a valuation allowance against its deferred tax assets of \$2,171 million and \$1,815 million at June 30, 2008 and December 31, 2007, respectively, to reflect management's assessment regarding their future realization. United had valuation allowances of \$2,123 million and \$1,757 million at June 30, 2008 and December 31, 2007, respectively. The Company expects to continue to maintain a valuation allowance on deferred tax assets until there is sufficient positive evidence of future realization. Under the accounting rules in effect for UAL's and United's 2008 fiscal year, reductions in the portion of the total valuation allowance recorded prior to February 1, 2006, if any should occur, would be recorded as a reduction of goodwill, to the extent thereof, and then as a reduction of other intangible assets. Beginning January 1, 2009, under the provisions of FASB's Statement of Financial Accounting Standards No. 141 (revised 2007), *Business Combinations*, reductions in the valuation allowance attributable to all periods, if any should occur, will be recorded as an adjustment to income tax expense in the Company's *Statements of Consolidated Operations (Unaudited)*.

As a result of the Company's emergence from bankruptcy, the Company has an unrecorded tax benefit of \$802 million and \$801 million at June 30, 2008 and December 31, 2007, respectively, attributable to the difference between the amount of financial statement expense and the allowable tax deduction for UAL common stock issued to certain unsecured creditors and employees pursuant to the Plan of Reorganization. The Company is accounting for this unrecorded tax benefit by analogy to Statement of Financial Accounting Standards No. 123 (Revised 2004), *Share-Based Payment*, which requires recognition of the tax benefit to be deferred until it is realized as a reduction of taxes payable.

As of June 30, 2008, UAL and United had a federal net operating loss ("NOL") carry forward of approximately \$7.4 billion, and a combined federal and state income tax NOL carry forward tax benefit of approximately \$2.8 billion. These benefits, which originated primarily before the Company emerged from bankruptcy, will expire over a five to twenty year period. The Company's ability to utilize these benefits may be impaired if the Company were to have a change of ownership within the meaning of Section 382 of the Internal Revenue Code. To reduce the possibility of a potential adverse effect on the Company's ability to utilize its NOL carry forward benefits, the Company's certificate of incorporation contains a "5% Ownership Limitation," applicable to all stockholders except the Pension Benefit Guaranty Corporation ("PBGC"). The 5% Ownership Limitation remains effective until February 1, 2011. Generally, the 5% limitation prohibits (i) the acquisition by a single stockholder of shares representing 5% or more of the common stock of UAL and (ii) any acquisition or disposition of common stock by a stockholder that already owns 5% or more of UAL's common stock, unless prior written approval is granted by the UAL Board of Directors.

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Combined Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

(9) Income Taxes (Continued)

UAL's income tax returns for tax years after 2003 remain subject to examination by the Internal Revenue Service and state taxing jurisdictions. United is included in UAL's consolidated income tax returns.

(10) Retirement and Postretirement Plans

UAL and United contribute to defined contribution plans on behalf of most of their employees, particularly within the U.S. Internationally, the Company maintains a number of small pension plans covering much of its local, non-U.S. workforce. The Company also provides certain health care benefits, primarily in the U.S., to retirees and eligible dependents, as well as certain life insurance benefits to certain retirees, which are reflected as "Other Benefits" in the tables below. The Company has reserved the right, subject to collective bargaining and other agreements, to modify or terminate the health care and life insurance benefits for both current and future retirees.

The Company's net periodic benefit cost included the following components:

(In millions)	Pension Benefits				Other Benefits			
	Three Months Ended		Six Months Ended		Three Months Ended		Six Months Ended	
	June 30,		June 30,		June 30,		June 30,	
	2008	2007	2008	2007	2008	2007	2008	2007
Service cost	\$ 1	\$ 3	\$ 3	\$ 5	\$ 8	\$ 9	\$ 16	\$ 18
Interest cost	2	3	5	5	30	31	60	62
Expected return on plan assets	(3)	(3)	(6)	(5)	(1)	(1)	(2)	(2)
Amortization of unrecognized gain and prior service cost		(1)	(1)	(1)	(4)	(2)	(8)	(4)
Net periodic benefit costs	\$	\$ 2	\$ 1	\$ 4	\$ 33	\$ 37	\$ 66	\$ 74

(11) Segment Information

We manage our business by two reportable segments: Mainline and United Express. The table below includes segment information for UAL and United for the three and six month periods ended June 30, 2008 and 2007. See Note 3, "Impairments" and Note 4, "Voluntary Reorganization Under

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UAL Corporation and Subsidiary Companies and
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Combined Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

(11) Segment Information (Continued)

Chapter 11 of the United States Bankruptcy Code," for discussion of the impairments and special items presented in the table below.

(In millions)	Three Months Ended June 30,		Six Months Ended June 30,	
	2008	2007	2008	2007
<u>UAL segment information</u>				
Revenue:				
Mainline	\$ 4,574	\$ 4,409	\$ 8,570	\$ 8,107
United Express	797	804	1,512	1,479
Total	\$ 5,371	\$ 5,213	\$ 10,082	\$ 9,586
Segment income (loss):				
Mainline	\$ (208)	\$ 395	\$ (684)	\$ 154
United Express	(50)	71	(114)	54
Goodwill impairment	(2,277)		(2,277)	
Other impairments and special items	(223)		(223)	22
Less: equity earnings(a)	(1)	(1)	(3)	(2)
 Consolidated income (loss) before income taxes and equity in earnings of affiliates	 \$(2,759)	 \$ 465	 \$ (3,301)	 \$ 228

(In millions)	Three Months Ended June 30,		Six Months Ended June 30,	
	2008	2007	2008	2007
<u>United segment information</u>				
Revenue:				
Mainline	\$ 4,574	\$ 4,412	\$ 8,570	\$ 8,114
United Express	797	804	1,512	1,479
Total	\$ 5,371	\$ 5,216	\$ 10,082	\$ 9,593
Segment income (loss):				
Mainline	\$ (236)	\$ 401	\$ (712)	\$ 168
United Express	(50)	71	(114)	54
Goodwill impairment	(2,277)		(2,277)	
Other impairments and special items	(223)		(223)	22
Less: equity earnings(a)	(1)	(1)	(3)	(2)
 Consolidated income (loss) before income taxes and equity in earnings of affiliates	 \$(2,787)	 \$ 471	 \$ (3,329)	 \$ 242

(a) Equity earnings are part of the Mainline segment.

All of the above impairments and special items are only applicable to the Mainline segment. The Company's Mainline segment assets decreased approximately \$2.9 billion during the six month period

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Combined Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

(11) Segment Information (Continued)

ended June 30, 2008. The decrease in Mainline segment assets was largely due to the asset impairments discussed in Note 3, "Impairments."

(12) Comprehensive Income (Loss)

For the three and six month periods ended June 30, 2008 and 2007, UAL's total comprehensive income (loss) was \$(2,744) million and \$(3,293) million, respectively, and \$272 million and \$127 million, respectively. For the three and six month periods ended June 30, 2008 and 2007, United's total comprehensive income (loss) was \$(2,772) million and \$(3,320) million, respectively, and \$275 million and \$135 million, respectively. The 2008 and 2007 periods included activity related to an interest rate swap that was terminated in 2007 and the amortization of deferred net periodic pension and other postretirement benefit gains that were recorded as a component of accumulated other comprehensive income for the years ended December 31, 2007 and 2006, in accordance with Statement of Financial Accounting Standard No. 158, *Employers' Accounting for Pensions and Other Postretirement Plans, an amendment of FASB Statements No. 87, 88, 106 and 132R*. Comprehensive loss in the 2008 periods also includes changes in the fair value of the Company's available-for-sale EETC investments.

(13) Fair Value Measurements and Derivative Instruments

Fair Value Information. Effective January 1, 2008, the Company adopted Statement of Financial Accounting Standards No. 157, Fair Value Measurements ("SFAS 157"). SFAS 157 establishes a fair value hierarchy that prioritizes the inputs used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurement) and the lowest priority to unobservable inputs (Level 3 measurement). This hierarchy requires entities to maximize the use of observable inputs and minimize the use of unobservable inputs. The three levels of inputs used to measure fair value are as follows:

- | | |
|---------|---|
| Level 1 | Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities. |
| Level 2 | Observable inputs other than quoted prices included in Level 1, such as quoted prices for similar assets and liabilities in active markets; quoted prices for identical or similar assets and liabilities in markets that are not active; or other inputs that are observable or can be corroborated by observable market data. |
| Level 3 | Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. |

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Combined Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

(13) Fair Value Measurements and Derivative Instruments (Continued)

The table below presents disclosures about the fair value of financial assets and financial liabilities recognized in the Company's *Condensed Statements of Consolidated Financial Position (Unaudited)*.

(In millions)	Fair Value Measurements at Reporting Date Using				Total Gains/ (Losses)
	June 30, 2008	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
<u>Assets and Liabilities Measured at Fair Value on a Recurring Basis:</u>					
EETC available-for-sale securities	\$ 67	\$	\$ 67	\$	
Fuel derivative instruments(a)	258		249	9	\$ 9
Foreign currency receivables	1		1		
Total financial assets	\$ 326	\$	\$ 317	\$ 9	
 Total financial liabilities Foreign currency payables	 \$ 4	 \$	 \$ 4	 \$	

- (a) During the six months ended June 30, 2008, the net increase in the fair value of Level 3 fuel derivatives was \$9 million which was classified within aircraft fuel expense in the Company's *Condensed Statements of Consolidated Operations (Unaudited)*. See below for further discussion of fuel derivative gains and losses.

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Combined Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

(13) Fair Value Measurements and Derivative Instruments (Continued)

Fair value of the above financial instruments was determined as follows:

Description	Fair Value Methodology
<i>Enhanced Equipment Trust Certificates ("EETCs")</i>	The EETCs are not actively traded on an exchange. Fair value is based on the trading prices of similar EETC instruments issued by other airlines.
<i>Fuel Derivative Instruments</i>	United's fuel derivative contracts are privately negotiated contracts and are not exchange traded. The fair value of most of these contracts is determined based on models using energy related observable inputs that are either readily available in the public markets or can be derived from information in the public markets. The Company substantiates the reasonableness of their values through comparison to information received from counterparties and in certain cases multiple counterparties. The Company enters into derivative contracts where certain of the inputs utilized to determine the fair value of certain derivative contracts are unobservable and the Company has categorized these derivative contracts as Level 3. The Company's Level 3 derivative contracts consist of contracts that are extendible at the option of the counterparty. The fair value of these contracts was estimated using an income approach, that includes a simulation model.
<i>Foreign Currency Derivative Instruments</i>	Fair value is determined with a formula utilizing observable inputs.

Aircraft Fuel Hedges. We have a risk management strategy to hedge a portion of our price risk related to projected jet fuel requirements primarily through collar options. The collars involve the simultaneous purchase and sale of call and put options with identical expiration dates. In order for the Company to obtain more favorable terms for a portion of its hedge positions, the Company entered into collars with additional features. These hedge positions include extendable collars referred to above and collars that include twice the amount of put volume as call volume. In the three month periods ended June 30, 2008 and 2007, the Company entered into and settled various derivative positions that were accounted for as economic hedges rather than cash flow or fair value hedges under SFAS 133. In the three months ended June 30, 2008 and 2007, the Company recognized net hedge gains of \$238 million and \$17 million, respectively that were classified as Mainline fuel expense in the *Condensed Statements of Consolidated Operations (Unaudited)*. In addition, for the six months ended June 30, 2008 and 2007, the Company recognized net hedge gains of \$279 million and \$39 million, respectively that were classified as Mainline fuel expense in the *Condensed Statements of Consolidated Operations (Unaudited)*. In addition, the Company recorded \$22 million in fuel derivative gains, which are included in nonoperating income in both the three and six month periods ended June 30, 2008. As of June 30, 2008, fuel expense and nonoperating income included \$237 million and \$21 million, respectively, of unrealized mark-to-market gains for contracts settling after June 30, 2008.

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Combined Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

(13) Fair Value Measurements and Derivative Instruments (Continued)

As of June 30, 2008, the Company had hedged 40% of forecasted third quarter 2008 fuel consumption. Three-way collars hedged 30% of fuel consumption with upside protection, on a weighted-average basis, beginning at \$108 per barrel and capped at \$124 per barrel with payment obligations, on a weighted-average basis, beginning if crude oil drops below \$104 per barrel. Collars hedged 10% of fuel consumption with upside protection, on a weighted-average basis, beginning at a crude oil equivalent price of \$111 per barrel with payment obligations, on a weighted-average basis, beginning if crude oil drops below \$100 per barrel.

As of June 30, 2008, the Company had hedged 42% of forecasted fuel consumption for fourth quarter of 2008. Three-way collars hedged 26% of fuel consumption with upside protection, on a weighted-average basis, beginning at \$110 per barrel and capped at \$131 per barrel with payment obligations, on a weighted-average basis, beginning if crude oil drops below \$105 per barrel. Collars hedged 16% of fuel consumption with upside protection, on a weighted-average, beginning at a crude oil equivalent price of \$105 per barrel with payment obligations, on a weighted-average, beginning if crude oil drops below \$94 per barrel. As of June 30, 2008, approximately one-third of the Company's hedge positions for the last six months of 2008 were extendable collars or collars with twice the amount of put to call volume.

As of June 30, 2008, the Company had hedged 10% of forecasted fuel consumption for the year ended December 31, 2009. Three-way collars hedged 7% of fuel consumption with upside protection, on a weighted-average basis, beginning at \$112 per barrel and capped at \$141 per barrel with payment obligations, on a weighted-average basis, beginning if crude oil drops below \$99 per barrel. Collars hedged 3% of fuel consumption with upside protection, on a weighted-average, beginning at a crude oil equivalent price of \$113 per barrel with payment obligations, on a weighted-average, beginning if crude oil drops below \$104 per barrel.

Foreign Exchange. As of June 30, 2008, the Company hedged a portion of its expected foreign currency cash flows in the Australian dollar, Canadian dollar, British pound, European euro and Japanese yen. As of June 30, 2008, the notional amount of these foreign currencies hedged with the forward contracts in U.S. dollars terms was approximately \$243 million. These contracts expire at various dates through March 2009. For the three and six months ended June 30, 2008, a total realized and unrealized loss of \$1 million and \$9 million, respectively, was recorded in nonoperating expenses from these derivative positions. The Company began this hedging program in the second quarter of 2007 and realized no material gains or losses from these derivative positions during that period.

Fair Value of Debt. As of June 30, 2008, the fair value of the Company's debt declined to approximately \$5.2 billion, as compared to a carrying value of \$6.8 billion. As of December 31, 2007, the fair value of the Company's debt was approximately \$6.8 billion, as compared to its carrying value of \$7.1 billion. The decrease in fair value was primarily due to the impact of increased fuel expense on the Company's financial performance, as well as the tightening of the credit markets. The Company estimated the fair value of its debt at June 30, 2008 based on quoted market prices for the same or similar issues and discounted cash flow models using appropriate market rates.

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Combined Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

(14) Commitments, Contingent Liabilities and Uncertainties

General Guarantees and Indemnifications. In the normal course of business, the Company enters into numerous real estate leasing and aircraft financing arrangements that have various guarantees included in the contracts. These guarantees are primarily in the form of indemnities. In both leasing and financing transactions, the Company typically indemnifies the lessors, and any financing parties, against tort liabilities that arise out of the use, occupancy, operation or maintenance of the leased premises or financed aircraft. Currently, management believes that any future payments required under these guarantees or indemnities would be immaterial, as most tort liabilities and related indemnities are covered by insurance (subject to deductibles). Additionally, certain leased premises such as fueling stations or storage facilities include indemnities of such parties for any environmental liability that may arise out of or relate to the use of the leased premises.

Bankruptcy Matters. See Note 4, "Voluntary Reorganization Under Chapter 11 of the United States Bankruptcy Code Significant Matters Remaining to be Resolved in Chapter 11 Cases," for a discussion of contingencies associated with the Company's bankruptcy proceedings.

Legal and Environmental Contingencies. The Company has certain contingencies resulting from litigation and claims (including environmental issues) incident to the ordinary course of business. Management believes, after considering a number of factors, including (but not limited to) the information currently available, the views of legal counsel, the nature of contingencies to which the Company is subject and prior experience, that the ultimate disposition of these contingencies will not materially affect the Company's consolidated financial position or results of operations.

The Company records liabilities for legal and environmental claims when a loss is probable and can be reasonably estimated. These amounts are recorded based on the Company's assessments of the likelihood of their eventual disposition. The amounts of these liabilities could increase or decrease in the near term, based on revisions to estimates relating to the various claims.

The Company is currently analyzing whether any potential liability may result from air cargo/passenger surcharge cartel investigations following the receipt of a Statement of Objections that the European Commission (the "Commission") issued to 26 companies on December 18, 2007. The Statement of Objections sets out evidence related to the utilization of fuel and security surcharges and exchange of pricing information that the Commission views as supporting the conclusion that an illegal price-fixing cartel had been in operation in the air cargo transportation industry. United received a copy of the Statement of Objections and has provided written and oral responses vigorously disputing the Commission's allegations against the Company. Nevertheless, United will continue to cooperate with the Commission's ongoing investigation. Based on the Company's evaluation of the information currently available, no reserve for potential liability has been recorded as of June 30, 2008. However, penalties for violation of European competition laws can be substantial and a finding that the Company engaged in improper activity could have a material adverse impact on our consolidated financial position and results of operations.

Contingent Senior Unsecured Notes. UAL is obligated to issue up to \$500 million of 8% senior unsecured notes to the PBGC in up to eight equal tranches of \$62.5 million upon the occurrence of certain financial triggering events. Beginning with the Company's fiscal year ending December 31, 2009 and concluding with our fiscal year ending December 31, 2017, a triggering event may occur when,

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Combined Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

(14) Commitments, Contingent Liabilities and Uncertainties (Continued)

among other things, the Company's EBITDAR exceeds \$3.5 billion over a prior twelve month period. In certain circumstances, UAL common stock may be issued in lieu of issuance of the notes.

Commitments. At June 30, 2008, future commitments for the purchase of property and equipment, principally aircraft, approximated \$2.8 billion. The Company's current commitments include \$2.2 billion for the purchase of, in the aggregate, 42 A319 and A320 aircraft. These commitments for the 42 aircraft are cancellable by the Company and such action would require the forfeiture of \$91 million of advance deposits provided to the manufacturer for these purchase orders. As discussed in Note 3, "Impairments," the Company recorded an impairment charge to decrease the carrying value of the advance deposits in the Company's *Consolidated Statements of Financial Position (Unaudited)* to zero based on the Company's belief that it is highly unlikely that it will take future delivery of these aircraft. These aircraft purchase orders are still included in the Company's total commitment amount, as the Company has not formally terminated the orders. The Company's current commitments would require the payment of an estimated \$0.2 billion in 2008, \$0.4 billion for the combined years of 2009 and 2010, \$1.3 billion for the combined years of 2011 and 2012 and \$0.9 billion thereafter.

Municipal Bond Guarantees. The Company has entered into long-term agreements to lease certain airport and maintenance facilities that are financed through tax-exempt municipal bonds. These bonds were issued by various local municipalities to build or improve airport and maintenance facilities. Under these lease agreements, United is required to make rental payments in amounts sufficient to pay the maturing principal and interest payments on the bonds. However, as a result of the bankruptcy filing, United was not permitted to make payments on unsecured pre-petition debt. The Company was advised that these municipal bonds may be unsecured (or in certain instances, partially secured). In 2006, as a result of the final Bankruptcy Court decisions, certain leases (SFO and LAX) were considered to be financings resulting in the Company's guarantees being discharged in bankruptcy. The Denver International Airport ("DEN") lease related to the 1992 bonds was not rejected. The Company has guaranteed interest and principal payments on \$270 million of the DEN bonds, which were originally issued in 1992, but were subsequently redeemed and reissued in 2007 and are due in 2032 unless the Company elects not to extend its lease in which case the bonds are due in 2023. The outstanding bonds and related guarantee are not recorded in the Company's *Statements of Consolidated Financial Position* at June 30, 2008 or December 31, 2007. The related lease agreement is recorded on a straight-line basis resulting in ratable accrual of the final \$270 million lease obligation over the lease term. There remains certain bankruptcy-related litigation as to whether the LAX and SFO bondholders have a secured interest in certain of the Company's leasehold improvements. The Company has accrued an amount, which it estimates is probable to be approved by the Bankruptcy Court for these secured interests. See Note 4, "Voluntary Reorganization Under Chapter 11 of the United States Bankruptcy Code Significant Matters Remaining to be Resolved in Chapter 11 Cases," for a discussion of ongoing litigation with respect to certain of these obligations.

(15) Debt Obligations

Aircraft-related Transactions

In June 2008, United entered into an \$84 million credit agreement secured by three aircraft, including two Airbus A320s and one Boeing B777. Borrowings under the agreement are at a variable interest rate based on LIBOR plus a margin. The loan has a final maturity in June 2015.

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Combined Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

(15) Debt Obligations (Continued)

During the first six months of 2008, the Company acquired nine aircraft under existing lease terms. These aircraft were previously recorded as capital lease assets and are now owned assets. Aircraft lease deposits were utilized to make the final payments due under certain of these lease obligations. As of June 30, 2008, 116 aircraft with a net book value of \$2.0 billion were unencumbered. As of December 31, 2007, the Company had 113 unencumbered aircraft.

In July 2008, United completed a \$241 million credit agreement secured by 26 of the Company's owned A319 and A320 aircraft. Borrowings under the Agreement were at a variable interest rate based on LIBOR plus a margin. Periodic principal and interest payments are required until the final maturity in June 2019. The Company may not prepay the loan prior to July 2012. This agreement did not change the number of the Company's unencumbered aircraft as the Company used available equity in these previously mortgaged aircraft as collateral for this financing.

Amended Credit Facility

The Company has a \$255 million revolving loan commitment available under Tranche A of its credit facility. As of June 30, 2008 and December 31, 2007, the Company had used \$206 million and \$102 million, respectively, of the Tranche A commitment capacity for letters of credit. In July 2008, the Company used an additional \$34 million of the Tranche A capacity for letters of credit, which combined with a reassessment of required collateral, resulted in the release of \$50 million of restricted cash from a third party to the Company.

Amended Credit Facility Collateral

In March 2008, in accordance with the terms of its Amended and Restated Revolving Credit, Term Loan and Guaranty Agreement dated as of February 2, 2007 with JPMorgan Chase Bank, N.A., Citicorp USA, Inc., J.P. Morgan Securities Inc., Citigroup Global Markets, Inc. and Credit Suisse Securities (USA) LLC (the "Amended Credit Facility"), United provided notice to the lenders of its intent to remove certain assets from the collateral securing its outstanding loans. The release of such collateral was effective as of April 16, 2008. The release of collateral, which was valued at approximately \$650 million, was facilitated, in part, by the reduction in outstanding loans under the Amended Credit Facility following United's \$500 million prepayment in December 2007. United's assets released from the Amended Credit Facility collateral included all domestic slots, spare engines, flight simulators, owned real property and related fixtures previously securing the Amended Credit Facility. Following such release of collateral, the Amended Credit Facility is secured by certain of United's international route authorities, international slots, related gate interests and associated rights.

Amended Credit Facility Covenants

United's Amended Credit Facility requires compliance with certain covenants. The Company was in compliance with all of its Amended Credit Facility covenants as of June 30, 2008 and December 31, 2007. In May 2008, the Company amended the terms of certain financial covenants of the Amended Credit Facility. The Company paid \$109 million to amend the credit facility. These costs are being

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Combined Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

(15) Debt Obligations (Continued)

deferred and amortized over the remaining life of the agreement. A summary of financial covenants, after the May amendment, includes the following:

The Company must maintain a specified minimum ratio of EBITDAR to the sum of the following fixed charges for all applicable periods: (a) cash interest expense and (b) cash aircraft operating rental expense. EBITDAR represents earnings before interest expense net of interest income, income taxes, depreciation, amortization, aircraft rent and certain cash and non-cash charges as further defined by the Amended Credit Facility.

The requirement to meet a fixed charge coverage ratio was suspended for the four quarters beginning with the second quarter of 2008, and ending with the first quarter of 2009 and thereafter is determined as set forth below:

Number of Preceding Months Covered	Period Ending	Required Coverage Ratio
Three	June 30, 2009	1.0 to 1.0
Six	September 30, 2009	1.1 to 1.0
Nine	December 31, 2009	1.2 to 1.0
Twelve	March 31, 2010	1.3 to 1.0
Twelve	June 30, 2010	1.4 to 1.0
Twelve	September 30, 2010 and each quarter ending thereafter	1.5 to 1.0

The Company also must maintain a minimum unrestricted cash balance of \$1.0 billion at any time from the effective date of the May 2008 amendment. All other provisions of the Amended Credit Facility remain unchanged.

Failure to comply with any applicable covenants in effect for any reporting period could result in a default under the Amended Credit Facility unless the Company obtains a waiver of, or otherwise mitigates or cures, any such default. Additionally, the Amended Credit Facility contains a cross default provision with respect to other credit arrangements that exceed \$50 million. Although the Company was in compliance with all required financial covenants as of June 30, 2008, and the May 2008 amendment does not require the Company to comply with a fixed charge coverage ratio until the three month period ending June 30, 2009, continued compliance depends on many factors, some of which are beyond the Company's control, including the overall industry revenue environment and the level of fuel costs. There are no assurances that the Company will continue to comply with its debt covenants. Failure to comply with applicable covenants in any reporting period would result in a default under the Amended Credit Facility, which could have a material adverse impact on the Company depending on the Company's ability to obtain a waiver of, or otherwise mitigate, the impact of the default.

Credit Card Processing Agreement Covenants

The Company has agreements with financial institutions that process customer credit card transactions for the sale of air travel and other services. Under certain of the Company's card processing agreements, the financial institutions either require, or have the right to require, that United maintain a reserve (referred to as a "holdback") equal to a portion of advance ticket sales that have been processed by that financial institution, but for which the Company has not yet provided the air transportation (referred to as "relevant advanced ticket sales").

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Combined Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

(15) Debt Obligations (Continued)

As of June 30, 2008, such financial institutions maintained an aggregate holdback of \$382 million. This holdback amount was classified as restricted cash in the accompanying *Condensed Statements of Consolidated Financial Position (Unaudited)*.

Under the Company's largest credit card processing agreement, the amount of any such holdback is determined, based on, among other things, payment defaults with respect to any material indebtedness or any material trade payable, the amount of unrestricted cash held by the Company and the Company's fixed charge coverage ratio, both as defined under the Amended Credit Facility. This agreement currently requires a 25% holdback. In order for this holdback to not increase above 25%, the Company must maintain at least 90% of both the minimum required fixed charge coverage ratio and the minimum required unrestricted cash balance, as specified in the Amended Credit Facility for any applicable period for which such covenants are effective. If the Company fails to meet the 90% compliance level for either of these financial covenants when applicable, the card processor may increase its holdback of relevant advanced ticket sales in several successive stages from the current amount of 25% to up to 100% based on additional triggers. The card processing agreement's financial covenants automatically conform to the Amended Credit Facility's financial covenants as these may be amended, waived, or supplemented from time to time, and as a result, these financial covenants have automatically adjusted to conform to the May 2008 amendment to the Amended Credit Facility discussed above. In the May 2008 amendment, the fixed charge coverage ratio requirement was eliminated under the Amended Credit Facility for the four quarterly periods beginning with the second quarter of 2008 and ending with the first quarter of 2009; consequently, no fixed charge coverage ratio is in effect for this card processing agreement for those reporting periods.

On July 22, 2008 the Company announced that it had reached a non-binding agreement in principle to amend the above referenced credit card processing agreement to, among other things, reduce the amount of the holdback. If finalized in a definitive agreement, the amendment would reduce the amount of the holdback to \$25 million provided the Company maintains a specified level of unrestricted cash and cash equivalents. The Company has agreed that certain of its obligations under the agreement would be secured by certain non-cash collateral. The parties have agreed to use their best efforts to reach a definitive agreement and complete the transactions contemplated by the agreement in principle.

Under another of United's material card processing agreements there currently are no holdbacks; however, in the event United's business suffers a material adverse change, the card processor has the right to review and increase the holdback to up to 100% (and in some cases more than 100%) of relevant advanced ticket sales.

The Company's maximum exposure to credit card holdbacks generally consists of the amount of advance ticket sales that customers purchased with credit cards. An increase in the current holdback balances to higher percentages of relevant advanced ticket sales could materially reduce the Company's liquidity. As of June 30, 2008, the Company had advance ticket sales of \$2,786 million of which approximately \$2.3 billion relates to credit card sales.

(16) Subsequent Events

See Note 15, "Debt Obligations," for financing transactions completed after June 30, 2008, including the Company's \$241 million secured borrowing and the issuance of additional letters of credit

**UAL Corporation and Subsidiary Companies and
United Air Lines, Inc. and Subsidiary Companies**

Combined Notes to Condensed Consolidated Financial Statements (Unaudited) (Continued)

(16) Subsequent Events (Continued)

under the Company's Amended Credit Facility. In addition, the Company also received \$50 million of cash that was previously restricted. This return of cash was due, in part, to the issuance of letters of credit.

In July 2008, the Company announced that it had reached a non-binding agreement in principle with its Mileage Plus co-branded bankcard partner and its largest credit card processor to amend the terms of their existing co-brand and credit card processing agreements to, among other things, extend the terms of the agreements. If finalized in a definitive agreement, the Company would receive a payment of \$600 million relating to the advance purchase of frequent flyer miles and the extension of the contract and would expect to receive an additional \$200 million in cash flow over the next two years under the co-brand agreement. See Note 15, "Debt Obligations," for a discussion of the proposed amendment to the credit card processing agreement. The Company has agreed that certain of its obligations under the agreements would be secured by certain non-cash collateral. The parties have agreed to use their best efforts to reach definitive agreements and complete the transactions contemplated by the agreement in principle.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Overview

UAL Corporation (together with its consolidated subsidiaries, "UAL"), is a holding company and its principal, wholly-owned subsidiary is United Air Lines, Inc. (together with its consolidated subsidiaries, "United"). We sometimes use the words "we," "our," "us" and the "Company" in this Form 10-Q for disclosures that relate to both UAL and United. United's operations consist primarily of the transportation of persons, property, and mail throughout the U.S. and abroad. United provides these services through full-sized jet aircraft (which we refer to as its "Mainline" operations), as well as smaller aircraft in its regional operations conducted under contract by "United Express®" carriers.

United is one of the largest passenger airlines in the world. The Company offers over 3,000 flights a day to more than 200 destinations through its Mainline and United Express services, based on its flight schedule from July 2008 to July 2009. United offers nearly 1,400 average daily Mainline (including Ted^(SM)) departures to more than 120 destinations in 27 countries and two U.S. territories. United provides regional service, connecting primarily via United's domestic hubs, through marketing relationships with United Express carriers, which provide more than 1,700 average daily departures to more than 150 destinations. United serves virtually every major market around the world, either directly or through its participation in the Star Alliance®, the world's largest airline network.

Bankruptcy Matters. On December 9, 2002 (the "Petition Date"), UAL, United and 26 direct and indirect wholly-owned subsidiaries (collectively, the "Debtors") filed voluntary petitions to reorganize their businesses under Chapter 11 of the United States Bankruptcy Code in the United States Bankruptcy Court for the Northern District of Illinois, Eastern Division (the "Bankruptcy Court"). On January 20, 2006, the Bankruptcy Court confirmed the Debtors' Second Amended Joint Plan of Reorganization Pursuant to Chapter 11 of the United States Bankruptcy Code (the "Plan of Reorganization"). The Plan of Reorganization became effective and the Debtors emerged from bankruptcy protection on February 1, 2006 (the "Effective Date"). As of the Effective Date, UAL and United adopted fresh-start reporting in accordance with American Institute of Certified Public Accountants' Statement of Position 90-7, *Financial Reporting by Entities in Reorganization under the Bankruptcy Code* ("SOP 90-7") resulting in significant changes to their historical financial statements. See Note 4, "Voluntary Reorganization Under Chapter 11 of the United States Bankruptcy Code" in *Combined Notes to Condensed Consolidated Financial Statements (Unaudited)* for further information regarding bankruptcy matters.

Company Operational Plans. Crude oil spot prices significantly escalated in the second quarter of 2008 and reached new peak prices, at approximately \$140 per barrel. As described further below, the unprecedented increase in jet fuel prices has had a significant negative impact on our results of operations. The Company has begun implementing plans to address the increased cost of fuel. Highlights of these plans include the following:

The Company is significantly reducing mainline domestic and consolidated capacity. By the fourth quarter of 2008, the Company expects mainline domestic and consolidated capacity to be down approximately 16% and 11% year-over-year, respectively. For the full year of 2009, mainline domestic and consolidated capacity are expected to be approximately 20% and 12% lower than 2007, respectively.

The capacity reductions will be made through reductions in frequencies of routes and the elimination of unprofitable routes. These actions will result in the closure of certain stations where United cannot operate profitably at current fuel prices.

The Company has announced plans to permanently remove 100 aircraft from its mainline fleet, including its entire B737 fleet, and six B747 aircraft. The B737 aircraft being retired are some of

the oldest and least fuel efficient in the Company's fleet. This planned reduction reflects the Company's efforts to eliminate unprofitable capacity and divest the Company of assets that currently do not provide an acceptable return.

United is eliminating its Ted product and reconfiguring that fleet's 56 A320s to include United First class seats. The reconfiguration of the Ted aircraft will begin in spring 2009 and be completed by year-end 2009. We will continue to review the deployment of all of our aircraft in various markets and the overall composition of our fleet to ensure that we are using our assets appropriately to provide the best available return.

In connection with the capacity reductions discussed above, the Company is further streamlining its operations and corporate functions in order to match the size of its workforce to the size of its operations. The Company anticipates these efforts will result in a reduction in workforce of approximately 7,000 by the end of 2009. The workforce reduction is expected to occur through a combination of furloughs and furlough-mitigation programs, such as early-out options.

The Company has increased its 2008 cost reduction target by \$100 million to \$500 million and is also reducing previously planned 2008 capital expenditures of \$650 million by approximately \$200 million.

The Company is taking additional actions beyond the plans discussed above, including generating new revenue sources and taking certain other actions, as described below. However, the Company cannot provide assurance that these strategies will successfully mitigate the ongoing adverse impact of high jet fuel prices on its financial position, results of operations and liquidity.

Recent Developments. The increase in fuel prices and a weakening economy have created an extremely challenging environment for the industry. In addition, potential industry consolidation, such as the planned Delta Airlines and Northwest Airlines merger, may increase the competitiveness of the industry. In addition to the actions described above, the Company is taking a number of actions, described below, to respond to these challenges.

The Company continues to pass rising commodity costs to customers. The Company is creating new revenue streams through unbundling products, offering new a la carte services and expanding choices for customers. The Company's existing merchandising programs, such as Economy Plus and Premium Cabin up sell have been extremely successful and the Company continues to implement new revenue initiatives such as the \$15 fee for the first checked bag announced in June 2008. In addition, various ticket change fees have increased, including Mileage Plus close-in fees.

The Company is taking action with the objective to maintain adequate liquidity and minimize its financing costs during this challenging economic environment. In June and July 2008, the Company entered into approximately \$325 million of new financing agreements, as described in *Liquidity and Capital Resources Financing Activities*, below.

On July 22, 2008, the Company announced that it had reached a non-binding agreement in principle with its Mileage Plus co-branded bankcard partner and its largest credit card processor to amend the terms of their existing agreements to, among other things, extend the terms of the agreements. If finalized in a definitive agreement, the Company would expect its cash position to increase by approximately \$1.0 billion in 2008, which would include the release of approximately \$350 million in previously restricted cash under the credit card processing agreement, and an additional \$200 million over the next two years. The Company has agreed that certain of its obligations under the agreements would be secured by certain non-cash collateral, and the parties have agreed to use their best efforts to reach definitive agreements and complete the transactions contemplated by the agreement in principle.

Continental Alliance

In June 2008, United and Continental announced their plan to form a new partnership that will link the airlines' networks and services worldwide to the benefit of customers, employees and shareholders, creating new revenue opportunities, cost savings and other efficiencies. In addition, Continental plans to join United and its 19 other partners in the Star Alliance, the most comprehensive airline alliance in the world. Also, Continental will request the U.S. Department of Transportation to allow it to join United, Lufthansa, Air Canada and six other carriers in their already established anti-trust immunized alliance. This will enable the immunized carriers to work closely together to establish trans-Atlantic and other international joint ventures to deliver highly competitive flight schedules, fares and service.

In the U.S. market, where antitrust immunity for solely domestic travel would not apply, customers will benefit as the two airlines plan to begin broad codesharing, which eases travel for customers flying on itineraries using both carriers and cooperation on frequent flyer programs, elite customer recognition and airport lounges, subject to regulatory notice and Continental exiting certain of its current alliance relationships.

Continental's and United's route networks are highly complementary, with little overlap, so they add value to each other and to customers who are planning domestic and international itineraries. Under codesharing, customers will benefit from a coordinated process for reservations/ticketing, check-in, flight connections and baggage transfer. Frequent flyer reciprocity will allow members of Continental's OnePass program and United's Mileage Plus program to earn miles in their accounts when flying on either partner airline and redeem awards on both carriers.

Continental's plans to join the Star Alliance and other planned cooperation are subject to certain regulatory and other approvals and the termination of certain contractual relationships, including Continental's existing agreements with SkyTeam members that restrict its participation in another global alliance.

Summary of Financial Results. The air travel business is subject to seasonal fluctuations and, historically, the Company's results of operations are better in the second and third quarters as compared to the first and fourth quarters of each year, since our first and fourth quarter results normally reflect weaker travel demand. The Company's results of operations can be impacted by fuel price volatility, adverse weather, air traffic control delay, economic conditions and other factors in any period.

As highlighted in the table below, the Company's results in the three and six months ended June 30, 2008 were significantly less favorable as compared to the year-ago periods. The most significant contributors to these negative variances were increased fuel prices, and, in the second quarter, asset impairments. The table below also highlights that the Company, through its past and on-going cost reduction initiatives, was able to effectively manage costs in non-fuel and other areas,

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although the benefits of these cost savings initiatives and higher revenues were not sufficient to offset the dramatic increase in fuel cost.

(in millions)	Three months ended June 30,				Six months ended June 30,			
	2008	2007	Favorable (unfavorable)		2008	2007	Favorable (unfavorable)	
			\$	%			\$	%
UAL Information								
Total revenues	\$ 5,371	\$ 5,213	\$ 158	3	\$ 10,082	\$ 9,586	\$ 496	5
Mainline fuel expense	1,848	1,206	(642)	(53)	3,423	2,247	(1,176)	(52)
Regional affiliate fuel expense(a)	355	224	(131)	(58)	633	418	(215)	(51)
Asset impairment charges (see below)	2,500		(2,500)		2,500		(2,500)	
Severance and other charges (see below)	107		(107)		113	(22)	(135)	
Other operating expenses	3,255	3,246	9		6,548	6,498	(50)	(1)
Nonoperating expense	65	72	7	10	166	217	51	24
Income tax expense (benefit)	(29)	192	221		(32)	108	140	
Net income (loss)	(2,729)	274	(3,003)		(3,266)	122	(3,388)	
United net income (loss)(b)	(2,757)	278	(3,035)		(3,293)	130	(3,423)	

(a) Regional affiliates' fuel expense is classified as part of Regional Affiliates expense in the statements of operations.

(b) In 2008, the primary difference between net income of UAL and United is due to a \$29 million gain recorded as a credit to operating expenses by a direct subsidiary of UAL as a result of a litigation settlement applicable to that UAL subsidiary. Therefore, the gain is not reflected in United's financial statements.

Additional details related to the variances above include:

UAL recorded the following impairment and other charges, as further discussed below, during the three and six months ended June 30, 2008:

(In millions)	Period Ended June 30, 2008		Income statement classification
	Three Months	Six Months	
Goodwill impairment	\$ 2,277	\$ 2,277	Goodwill impairment
Intangible asset impairments	80	80	
Aircraft and related deposit impairments	143	143	
Other impairments and charges	223	223	Other impairments and special items
Total asset impairments	2,500	2,500	
Severance			Salaries and related costs
	82	82	
Employee benefit obligation adjustment	28	34	Salaries and related costs
Litigation-related settlement gain	(29)	(29)	Other operating expenses
Charges related to terminated/deferred projects	26	26	Purchased services

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Severance and other charges	107	113
Pre-tax impairments and other charges	2,607	2,613
Tax benefit on intangible asset impairments	(29)	(29) Income tax benefit
Total impairments and other charges	\$ 2,578	\$ 2,584

As described in the *Combined Notes to Condensed Financial Statements (Unaudited)*, in accordance with Statement of Financial Accounting Standards No. 142, *Goodwill and Other Intangible Assets* ("SFAS 142"), and Statement of Financial Accounting Standards No. 144,

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Accounting for the Impairment or Disposal of Long-Lived Assets ("SFAS 144"), as of May 31, 2008 the Company performed an interim impairment test of its goodwill, all indefinite-lived intangible assets and certain of its long-lived assets (principally aircraft and related spare engines and spare parts) due to events and changes in circumstances during the second quarters of 2008 that indicated an impairment might have occurred.

The three and six month periods ended June 30, 2008 includes operating and nonoperating fuel hedge gains of \$260 million and \$301 million, respectively, a significant portion of which was unrealized at June 30, 2008, as discussed further below.

Special items during the six month period ended June 30, 2007 included the benefit of a \$22 million decrease in the accrual for bankruptcy litigation associated with potential security interests in the Company's San Francisco International Airport ("SFO") and Los Angeles International Airport ("LAX") facility leases, based on an updated analysis of its contingent liabilities under this litigation.

The three and six month periods ended June 30, 2007 included an estimated benefit of \$39 million and \$62 million, respectively, for mainline revenues and \$8 million and \$13 million, respectively, in regional affiliate revenues due to the Company's policy change in the Mileage Plus expiration period from 36 months to 18 months for inactive accounts, effective December 31, 2007. The 2008 period did not include a similar benefit.

As compared to the year-ago periods, in the three months ended June 30, 2008 UAL interest expense, net of interest income, increased \$21 million; and, in the six months ended June 30, 2008, interest expense, net of interest income, decreased \$40 million. In the second quarter of 2007, UAL interest expense included a debt extinguishment gain which negatively impacts the comparison to the second quarter of 2008 net interest expense. In the six-month period of 2008, interest expense benefited from debt reductions of over \$2.0 billion throughout the year ended December 31, 2007 and several debt refinancings in 2007. In addition, lower benchmark rates on variable-rate debt also contributed to a year-over-year interest expense reduction in the year-to-date period.

In the three and six month periods ended June 30, 2008, the Company recorded a small income tax benefit, because the goodwill impairment charges were not deductible for income tax purposes and most of the remaining tax benefit generated during these periods was offset by a valuation allowance. In the three and six month periods ended June 30, 2007, UAL recognized income tax expense of \$192 million and \$108 million, respectively. In the three and six month periods ended June 30, 2007, United recognized income tax expense of \$194 million and \$114 million, respectively.

Liquidity. At June 30, 2008, UAL had total cash and restricted cash and short-term investments of \$3.6 billion, of which \$3.5 billion was held by United. UAL's and United's cash from operations were \$137 million and \$196 million, respectively, during the six month period ended June 30, 2008, a decrease of \$1.5 billion from the first half of 2007. Although cash from operations was positive in the first six months of 2008, net cash used by financing and investing, activities, excluding short-term investment activity, more than offset cash generated from operations resulting in a net decrease in cash and short-term investments in the first six months of 2008. Lower cash and short-term investment balances at June 30, 2008 as compared to December 31, 2007, and lower operating cash flow in the first half of 2008 as compared to the first half of 2007, were mainly a result of higher fuel costs. While the Company expects its cash flows from operations and its available capital to be sufficient to meet its near-term operating expenses, lease obligations and debt service requirements, the Company's future liquidity could be impacted by high fuel prices, inability to adequately increase revenues to offset high fuel prices, failure to meet future debt covenants and other factors, as further discussed in the *Results of Operations* and *Liquidity and Capital Resources* sections below.

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Capital Commitments. At June 30, 2008, the Company's future commitments for the purchase of property and equipment, principally aircraft, approximated \$2.8 billion. Our current commitments are primarily for the purchase of 42 A319 and A320 aircraft. These 42 aircraft purchase orders are included in the Company's total commitment amount; however, the orders may be cancelled resulting in the forfeiture of \$91 million of advance payments provided to the manufacturer. United believes it is highly unlikely that it will take delivery of these aircraft in the future, and therefore believes it will be required to forfeit its \$91 million of advance delivery deposits. Based on this determination, the Company recorded an impairment charge to decrease the value of the deposits and related capitalized interest of \$14 million to zero on the Company's *Condensed Consolidated Statements of Financial Position (Unaudited)*. For further details, see Note 14, "Commitments, Contingent Liabilities and Uncertainties" in *Combined Notes to Condensed Consolidated Financial Statements (Unaudited)*.

Contingencies. During the course of the Company's Chapter 11 proceedings, we successfully reached settlements with most of our creditors and resolved most pending claims against the Debtors. The following discussion provides an overview of the status of unresolved bankruptcy matters as well as other contingencies. For further details on these matters, see Note 4, "Voluntary Reorganization Under Chapter 11 of the United States Bankruptcy Code Bankruptcy Considerations" and Note 14, "Commitments, Contingent Liabilities and Uncertainties" in *Combined Notes to Condensed Consolidated Financial Statements (Unaudited)*.

Municipal Bond Obligations & Off-Balance Sheet Financing. We are a party to numerous long-term agreements to lease certain airport and maintenance facilities that are financed through tax-exempt municipal bonds issued by various local municipalities to build or improve airport and maintenance facilities. United had been advised that these municipal bonds may have been unsecured (or in certain instances, partially secured) pre-petition debt. In 2006, certain of United's municipal bond obligations relating to LAX and SFO were conclusively adjudicated through the Bankruptcy Court as financings and not true leases; however, there remains pending litigation to determine the value of the security interests, if any, that the bondholders at LAX and SFO have in our underlying leaseholds.

United has guaranteed \$270 million of the City and County of Denver, Colorado Special Facilities Airport Revenue Bonds (United Air Lines Project) Series 2007A (the "Denver Bonds"). This guarantee replaces our prior guarantee of \$261 million of bonds issued by the City and County of Denver, Colorado in 1992. These bonds are callable by United. The outstanding bonds and related guarantee are not recorded in the Company's *Condensed Statements of Consolidated Financial Position (Unaudited)*.

Legal and Environmental. The Company has certain contingencies resulting from litigation and claims (including environmental issues) incident to the ordinary course of business. Management believes, after considering a number of factors, including (but not limited to) the views of legal counsel, the nature of the contingencies and prior experience, that the ultimate disposition of these contingencies will not materially affect the Company's consolidated financial position or results of operations. When appropriate, United accrues for these matters based on its assessments of the likely outcomes of their eventual disposition. The amounts of these liabilities could increase or decrease in the near term, based on revisions to estimates relating to the various claims.

The Company is currently analyzing whether any potential liability may result from air cargo/passenger surcharge cartel investigations following the receipt of a Statement of Objections that the European Commission (the "Commission") issued to 26 companies on December 18, 2007. The Statement of Objections sets out evidence related to the utilization of fuel and security surcharges and exchange of pricing information that the Commission views as supporting the conclusion that an illegal price-fixing cartel had been in operation in the air cargo transportation industry. United received a copy of the Statement of Objections and has provided written and oral responses vigorously disputing the Commission's allegations against the Company. Nevertheless, United will continue to cooperate

with the Commission's ongoing investigation. Based on the Company's evaluation of the information currently available, no reserve for potential liability has been recorded. However, penalties for violation of European competition laws can be substantial and a finding that the Company engaged in improper activity could have a material adverse impact on our consolidated financial position and results of operations.

Many aspects of United's operations are subject to increasingly stringent federal, state and local laws protecting the environment. Future regulatory developments in the U.S. and abroad could adversely affect operations and increase operating costs in the airline industry. For example, potential future actions that may be taken by the U.S. government, state governments within the U.S., foreign governments, or the International Civil Aviation Organization to limit the emission of greenhouse gases by the aviation industry are uncertain at this time (in terms of either the regulatory requirements or their applicability to United), but the impact to the Company and the industry would likely be adverse and could be significant, including the potential for increased fuel costs, carbon taxes or fees, and/or a requirement to purchase carbon credits. The Parliament of the European Union (EU) has approved legislation that would bring all flights to/from the EU into the EU's emission trading scheme for CO₂ and it is expected that the EU Council will finalize passage of the legislation by year end. The legislation is expected to go into effect in 2012; however, significant questions remain as to the legality of applying the scheme to non-EU airlines. Therefore, it is unclear at this juncture whether the scheme will apply to United's EU operations. There are also some limited circumstances in which greenhouse gas requirements impacting United have already gone into effect, including environmental taxes for certain international flights. In addition, some U.S. states (such as California) have incorporated a review of greenhouse gases into their land-based planning laws, which could apply to airports and ultimately impact airlines depending upon the circumstances.

Results of Operations

Second Quarter 2008 Compared to Second Quarter 2007

United's operating revenues and operating expenses comprise nearly 100% of UAL's revenues and operating expenses. Therefore, the following qualitative discussion is applicable to both UAL and United, unless otherwise noted. Any significant differences between UAL and United results are separately disclosed and explained.

As described above in the Summary of Financial Results, UAL and United had losses from operations of \$2.7 billion and net losses of \$2.7 billion and \$2.8 billion, respectively, in the three months ended June 30, 2008. The difference between UAL's and United's results is primarily due to a \$29 million settlement gain recorded at UAL, but not United. These results are significantly less favorable as compared to the year-ago period. The most significant factors were fuel, goodwill and other asset impairments, severance and other charges, as discussed below.

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Operating Revenues. The table below illustrates the year-over-year percentage change in UAL and United operating revenues.

(In millions)	Three Months Ended June 30,		\$ Change	% Change
	2008	2007		
Passenger United Airlines	\$4,099	\$3,968	\$ 131	3.3
Passenger Regional Affiliates	797	804	(7)	(0.9)
Cargo	237	181	56	30.9
Other operating revenues	238	260	(22)	(8.5)
UAL total	\$5,371	\$5,213	\$ 158	3.0
United total	\$5,371	\$5,216	\$ 155	3.0

The table below presents selected UAL and United passenger revenues and operating data from our mainline segment, broken out by geographic region, and from our United Express segment, expressed as second quarter period-to-period changes.

2008	North America	Pacific	Atlantic	Latin	Mainline	United Express	Consolidated
Increase (decrease) from 2007:							
Passenger revenues (in millions)	\$ 20	\$ 14	\$ 83	\$ 14	\$ 131	\$ (7)	\$ 124
Passenger revenues	0.9%	1.7%	13.0%	11.2%	3.3%	(0.9)%	2.6%
Available seat miles (ASMs)	(4.8)%	(0.7)%	12.1%	(4.1)%	(1.3)%	(1.1)%	(1.3)%
Revenue passenger miles (RPMs)	(7.1)%	(5.6)%	7.6%	(3.4)%	(4.5)%	(7.0)%	(4.8)%
Passenger revenues per ASM (PRASM)	5.9%	2.4%	0.8%	16.0%	4.7%	0.3%	3.9%
Yield(a)	8.6%	7.8%	4.2%	13.5%	8.2%	6.6%	7.7%
Load factor (points)	(2.2) pts.	(4.1) pts.	(3.4) pts.	0.6 pts.	(2.7) pts.	(4.7) pts.	(3.0) pts.

(a)

Yield is a measure of average price paid per passenger mile, which is calculated by dividing passenger revenues by RPMs. Yields for geographic regions exclude charter revenue and RPMs.

Mainline and United Express passenger revenues increased/(decreased) by \$131 million and \$(7) million, respectively, in the 2008 period as compared to the same period in 2007. In the second quarter of 2008, revenues for both Mainline and United Express benefited from yield increases of 8.2% and 6.6%, respectively, as compared to the second quarter of 2007. The yield increases are due to industry capacity constraint and fare increases, including fuel surcharges. However, the benefit of higher fares was partially offset by 4.5% and 7.0% decreases in traffic for the Mainline and United Express segments, respectively. Revenues for both segments were negatively impacted by decreases in Mileage Plus revenue of approximately \$20 million and \$3 million for Mainline and United Express, respectively, in the 2008 period as compared to 2007. A change in the Mileage Plus expiration period from 36 months to 18 months provided an estimated benefit of \$47 million in the second quarter of 2007. Mileage Plus customer accounts are deactivated after 18 months of inactivity, effective December 31, 2007.

International PRASM was up 3% year-over-year on capacity growth of 4%. While Latin America PRASM growth was strong, growth in other regions has decelerated as the industry has added significant capacity. In the Pacific region, China has been particularly hard hit as industry capacity has grown by over 25%. China represents over 40% of our Pacific capacity. In the Atlantic region, industry growth in London was approximately 20% and significant industry growth in our core areas of strength in Germany, resulted in Atlantic region PRASM growth of only 0.8% this quarter.

Cargo revenues increased by \$56 million, or 31%, in the three month period ended June 30, 2008 as compared to the same period in 2007, partly due to revenues from a new long-term contract with

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the U.S. Postal Service for the carriage of domestic mail, which commenced in April 2007. Since this contract began in April 2007, revenues from this contract were not as significant in the year-ago quarter as compared to the second quarter of 2008. In addition, higher fuel surcharges and improved fleet utilization contributed to higher revenue in the second quarter of 2008 as compared to the prior year. A weaker dollar also benefited cargo revenues in 2008 as a portion of cargo services are contracted in foreign currencies.

UAL other operating revenues decreased by \$22 million, or 9%, in the three month period ended June 30, 2008 as compared to the same period in 2007. Lower jet fuel sales to third parties by our subsidiary, United Aviation Fuel Corporation ("UAFC") accounted for \$7 million of the other revenue decrease. The decrease in UAFC revenue had no material impact on our operating margin because UAFC cost of sales simultaneously decreased by \$8 million in the three months ended June 30, 2008 as compared to the year-ago period.

Operating Expenses. The table below includes data related to UAL and United operating expenses. Significant fluctuations are discussed below.

(In millions)	Three Months Ended June 30,		\$ Change	% Change
	2008	2007		
Aircraft fuel	\$ 1,848	\$ 1,206	\$ 642	53.2
Salaries and related costs	1,179	1,019	160	15.7
Regional affiliates	847	733	114	15.6
Purchased services	371	335	36	10.7
Aircraft maintenance materials and outside repairs	295	284	11	3.9
Depreciation and amortization	216	229	(13)	(5.7)
Landing fees and other rent	199	215	(16)	(7.4)
Distribution expenses	193	197	(4)	(2.0)
Aircraft rent	100	105	(5)	(4.8)
Cost of third party sales	65	77	(12)	(15.6)
Goodwill impairment	2,277		2,277	
Other impairment and special items	223		223	
Other operating expenses	252	276	(24)	(8.7)
 UAL total	 \$ 8,065	 \$ 4,676	 \$ 3,389	 72.5
 United total(a)	 \$ 8,093	 \$ 4,674	 \$ 3,419	 73.1

(a) United operating expenses were the same as UAL except as follows: (1) in 2008 and 2007, United's cost of third party sales was \$1 million lower than UAL's; (2) in 2008 and 2007, United's salaries and related costs were \$1 million higher and \$1 million lower, respectively, than UAL's; and (3) in 2008, United's other operating expenses were \$28 million higher than UAL's, as described below.

Mainline aircraft fuel increased \$642 million, or 53%, in the three month period ended June 30, 2008 as compared to the same period in 2007. This net fuel variance was due to a 55% increase in the average price per gallon of jet fuel from \$2.08 per gallon in the second quarter of 2007 to \$3.24 per gallon in the second quarter of 2008. This increase was attributable to increased market prices for crude oil and related fuel products. Crude oil prices exceeded \$130 per barrel for much of the second quarter of 2008. Partially mitigating the negative aircraft fuel variance was a \$221 million increase in realized and unrealized economic hedge gains that were \$238 million and \$17 million in the 2008 and 2007 periods, respectively. As of June 30, 2008, \$237 million of unrealized fuel hedge gains for contracts settling after June 30, 2008, have been recorded in Mainline fuel expense. Fuel hedge gains or losses are not allocated to the fuel costs included within Regional affiliates expenses.

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The table below presents the significant changes in Mainline and Regional Affiliate aircraft fuel prices from the year-ago period.

(In millions, except per gallon)	Three Months Ended June 30,		%
	2008	2007	Change
Mainline fuel expense	\$ 1,848	\$ 1,206	53.2
Regional affiliates fuel expense(a)	355	224	58.5
UAL system fuel expense	\$ 2,203	\$ 1,430	54.1
Mainline fuel consumption (gallons)	571	579	(1.4)
Mainline average jet fuel price per gallon (in cents)	323.6	208.3	55.4
Regional affiliates fuel consumption (gallons)	94	96	(2.1)
Regional affiliates average jet fuel price per gallon (in cents)	377.7	233.3	61.9

(a)

Regional affiliate fuel costs are classified as part of Regional affiliate expense.

Salaries and related costs increased \$160 million, or 16%, in the second quarter of 2008 as compared to the year-ago period. The Company experienced the negative impact of average wage increases and higher benefits expense, as well as severance expense for salaried and management positions of \$82 million due to the Company's planned reduction in workforce. In addition, the Company recorded \$28 million of expense to increase certain employee benefit obligations.

Regional affiliate expense increased \$114 million, or 16%, during the second quarter of 2008 as compared to the same period last year. Regional affiliate expense increased primarily due to a \$131 million increase in Regional Affiliate fuel, which was due to an increase in the average price of regional affiliates fuel of 62% while consumption remained relatively constant. The regional affiliate operating loss was \$50 million in the 2008 period, as compared to income of \$71 million in the 2007 period, due to the aforementioned fuel impacts which could not be fully offset by higher ticket prices, as Regional Affiliate revenues decreased 1% in 2008 as compared to 2007.

Purchased services increased 11% in the second quarter of 2008, as compared to the year-ago period, primarily due to \$26 million of charges related to certain projects that have been terminated or indefinitely deferred by the Company.

UAL landing fees and other rent decreased \$16 million in the second quarter of 2008 as compared to the year-ago period due to a reduction in the amount of facilities rented based upon our ongoing efforts to optimize our rented facilities consistent with our operational needs and favorable differences in the timing and amount of annual airport credits.

The decrease in UAL cost of sales of \$12 million in the 2008 period as compared to the 2007 period was primarily due to lower UAFC third party fuel sales as discussed above.

As described in the *Combined Notes to Condensed Financial Statements (Unaudited)*, in accordance with SFAS 142 and SFAS 144, as of June 30, 2008 the Company performed an interim impairment test of its goodwill, all intangible assets and certain of its long-lived assets (principally aircraft pre-delivery deposits, aircraft and related spare engines and spare parts) due to events and changes in circumstances during the first and second quarters of 2008 that indicated an impairment might have occurred.

Factors deemed by management to have collectively constituted a potential impairment triggering event included record high fuel prices, significant losses in the first and second quarters of 2008, a softening U.S. economy, analyst downgrade of UUA common stock, rating agency changes in outlook from stable to negative, the announcement of the planned removal from UAL's fleet of 100 aircraft in 2008 and a significant decrease in the fair value of the Company's outstanding equity and debt securities during the six months ended June 30, 2008, including a decline in UAL's market capitalization to significantly below book value.

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As a result of this testing, the Company recorded asset impairment charges of \$2.5 billion consisting of the items in the table below. All of these impairment charges are within the Mainline segment. All of the impairments other than the goodwill impairment, which is separately identified, are classified with "Other impairments" in the Company's *Condensed Statements of Consolidated Operations (Unaudited)*. See Note 3, "Impairments," in the *Combined Notes to Condensed Financial Statements (Unaudited)* for additional information.

(In millions)	
Goodwill impairment	\$2,277
Indefinite-lived intangible assets:	
Codeshare agreements	60
Tradenames	20
Intangible asset impairments	80
Tangible assets:	
Pre-delivery advance deposits including related capitalized interest	105
B737 aircraft, B737 spare parts and other	38
Aircraft and related deposit impairments	143
Total impairments	\$2,500

In the second quarter of 2008, UAL recorded a gain of \$29 million for a litigation settlement resulting in a reduction of other operating expenses; all other items within this classification increased by approximately \$5 million, or 2%, during the second quarter of 2008 as compared to the year-ago period. As discussed above under *Overview*, the \$29 million gain does not relate to United's operations.

Other income (expense). The following table illustrates the year-over-year dollar and percentage changes in UAL and United other income (expense).

(In millions)	Three Months Ended June 30,		Favorable/(Unfavorable) Change	
	2008	2007	\$	%
<u>UAL</u>				
Interest expense	\$(126)	\$(139)	\$ 13	9.4
Interest income	28	62	(34)	(54.8)
Interest capitalized	5	4	1	25.0
Miscellaneous, net	28	1	27	NM
	\$ (65)	\$ (72)	\$ 7	9.7
<u>United</u>				
Interest expense	\$(126)	\$(139)	\$ 13	9.4
Interest income	28	64	(36)	(56.3)
Interest capitalized	5	4	1	25.0
Miscellaneous, net	28		28	
	\$ (65)	\$ (71)	\$ 6	8.5

NM Not meaningful.

UAL interest expense, net of interest income, increased \$21 million in the quarter ended June 30, 2008 as compared to the year-ago period. Interest expense in the 2007 period included a gain of \$22 million due to a debt extinguishment. The 2008 period did not include any such gains. The 2008 period was favorably impacted by the \$500 million Amended Credit Facility prepayment in December

2007 and scheduled debt obligation repayments throughout 2007 that reduced interest expense in the 2008 period as compared to the year-ago period. The Company has a significant amount of variable-rate debt. Lower benchmark interest rates on these variable-rate borrowings also reduced the Company's interest expense in 2008 as compared to 2007. Interest income decreased significantly due to lower cash and short-term investment balances, as well as lower investment yields due to lower market rates.

Included in Miscellaneous, net in the 2008 period are fuel derivative nonoperating gains of \$22 million. These hedge gains include \$21 million of unrealized gains for contracts settling after June 30, 2008. See Note 13, "Fair Value Measurements and Derivative Instruments" in *Combined Notes to Condensed Consolidated Financial Statements (Unaudited)* for further discussion of these hedges.

Income Taxes. The tax benefit in the 2008 period is primarily due to the reversal of certain deferred tax liabilities related to indefinite-lived intangible assets established at fresh-start. This reversal was recorded as a result of an \$80 million intangible asset impairment. UAL and United recorded income tax expense of \$192 million and \$194 million, respectively, for the three months ended June 30, 2007 based on an estimated effective tax rate of 41%. See Note 9, "Income Taxes," for additional information.

First Six Months of 2008 Compared to First Six Months of 2007

As described above in the *Summary of Financial Results*, UAL and United had net losses of \$3.1 billion and \$3.2 billion, respectively, in the six months ended June 30, 2008, with the difference in net losses due to a \$29 million litigation settlement gain recorded by a direct subsidiary of UAL. These results are significantly less favorable as compared to the year-ago period. The most significant factors were fuel, asset impairment charges and special items, as discussed below.

Operating Revenues. The table below illustrates the year-over-year percentage change in UAL and United operating revenues.

(In millions)	Six Months		\$	%
	2008	30, 2007		
Passenger United Airlines	\$ 7,644	\$7,232	\$ 412	5.7
Passenger Regional Affiliates	1,512	1,479	33	2.2
Cargo	455	349	106	30.4
Other operating revenues	471	526	(55)	(10.5)
UAL total	\$ 10,082	\$9,586	\$ 496	5.2
United total	\$ 10,082	\$9,593	\$ 489	5.1

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