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Pensions Clearance – sense and sensibility

Share sales from an administration

ADVISORY

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A welcome decision from the Pensions Regulator may give comfort to lenders and corporate groups in distressed situations. Where circumstances allow, clearance may be available to protect subsidiary companies from Financial Support Directions (FSDs) where the holding company is insolvent, thus allowing viable companies to be subject to share sales. Lenders and corporates can also be reassured that the Regulator is displaying a reasonable and proportionate attitude.

Issues

The Regulator is able to issue a financial support direction to any company in a group where:

- there is a defined benefit pension scheme which has a deficit
- the employer company has net assets of less than 50 percent of the S75 (full buy-out) deficit
- any one other company within the group has net assets sufficient to cover the difference between the employer's net assets and 50 percent of the S75 deficit and
- it is reasonable to do so.

In a situation where the holding company is insolvent (net assets by definition zero) but subsidiaries may have net assets of more than 50 percent of the S75 deficit, then in principle the Regulator can seek to impose FSDs on any one of the subsidiaries if they do not enter any form of protection.

Once issued, an FSD is indefinite in time, but may be limited in amount. It is essentially an open-ended commitment to support the pension scheme. It is not curtailed or ended by the sale of the company on which the FSD is imposed, even though that company may leave the group which sponsors the pension scheme, although a revocation or variation of the FSD can be applied for.

Facts

In the case of Courts plc, ("Courts") the holding company and another UK company went into administration. The pension scheme was a substantial creditor of Courts. The vast majority of Courts' subsidiaries remained outside insolvency and, in the absence of FSDs, are viable companies. The preferred strategy of the office-holders to maximise realisations for the creditors of the administrations was to undertake share sales of the subsidiaries, rather than to place them in insolvency. There could well have been a material reduction in value if business and asset sales had been undertaken from insolvency.

Clearance was sought from the Regulator that FSDs would not be issued in the above circumstances. This was a necessary step in the sales process in order to reassure potential buyers that they would not 'inherit' an ongoing cash outflow to a pension scheme in which they had no stake.

The Regulator considered both the specific facts of the Courts case and the public policy arguments which it raised. Key facts in the application for clearance were:

- that there had been no evidence that Courts had supported the subsidiaries in a way which was detrimental to its creditors, including the pension scheme and
- that the subsidiaries had been recharged for shared services and were paying dividends up to the holding company in a fashion deemed normal within groups.

The public policy argument was essentially that the Regulator should not seek to help the pension scheme 'leapfrog' the statutory order of priorities for distributing funds to creditors in an insolvency. Were the Regulator to order FSDs to be imposed, the pension scheme would benefit but the other creditors of the administrations would lose out, as the sale proceeds of the subsidiaries would be likely to be reduced. This would not be consistent with a pari passu treatment of creditors.

The Regulator considered that it would not be appropriate for the pension scheme to gain 'super priority' over other creditors where there was a formal insolvency process on foot.

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Conclusions

This decision is encouraging for lenders and other stakeholders. It largely removes the concern that all companies in a group must go into an insolvency process to protect them from potential liabilities to a pension scheme and allows insolvency officeholders to pursue effective strategies to help realise value for all creditors. It also shows that the Regulator may be prepared to take account of the individual circumstances of each case and is likely to exercise commercial judgement. This again should provide reassurance to lenders and stakeholders that the Regulator can help to promote the rescue culture.

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