

The Actuarial Profession
making financial sense of the future

Momentum Conference 2011
Nick Graves and Michael Hayles



Corporate transactions and pensions issues

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Introduction

Speakers: Michael and Nick

Nick - Corporate Transactions

Michael - Pensions

Focus on your questions and issues

Recent work for trustees of the Great Lakes UK Pension Plan

Topics for discussion

- Corporate Transactions - Overview
- Private M&A
- Public M&A
- Group Re-organisations
- "Pre-packs"
- PPF Drop-ins

The impact of pension schemes on corporate transactions

Defined Benefit Scheme



Defined Contribution Scheme



Corporate Transactions - Overview

Corporate transactions – common structures

Private M&A – sale of a company

Transactions involving the sale and purchase of shares in private companies.

No prescribed format for the deal.

TUPE does not apply.

Public M&A – Takeover offer

Bidder makes an offer to shareholders in the Target company.

Parties must comply with the City Code on Takeovers and Mergers.

Takeover Panel supervises and regulates takeovers.

TUPE does not apply.

Private M&A – sale of a business

Package of assets, rights and liabilities transferred. TUPE applies – employee consultation required.

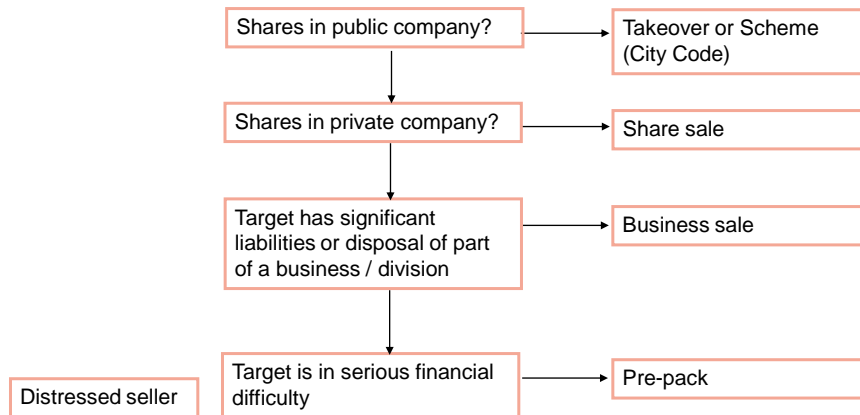
Public M&A – Scheme of Arrangement

Target company publishes a circular to shareholders setting out the scheme.

Parties must comply with City Code and provisions of Companies Act 2006 relating to schemes.

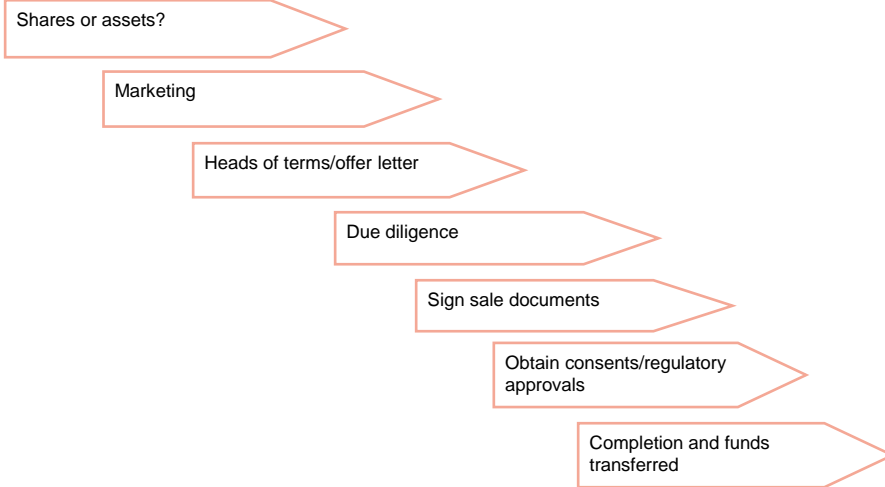
Takeover Panel and Court involved.

Corporate transactions: decision tree



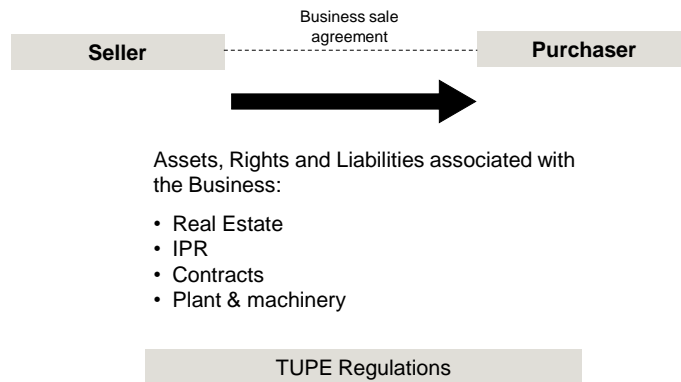
Private M&A

Private M&A – key stages

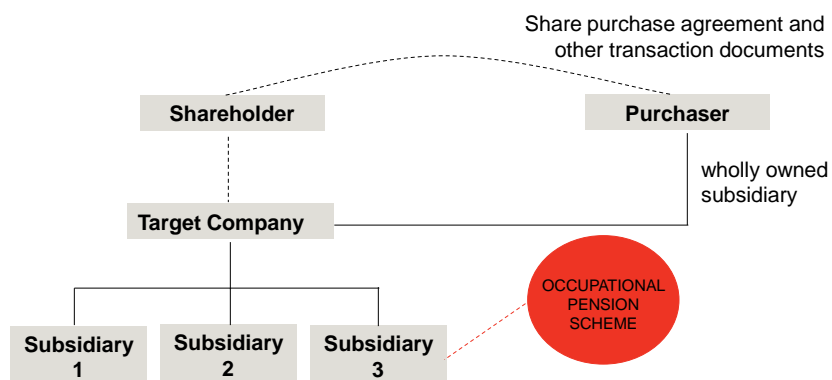


Private M&A: common deal structures

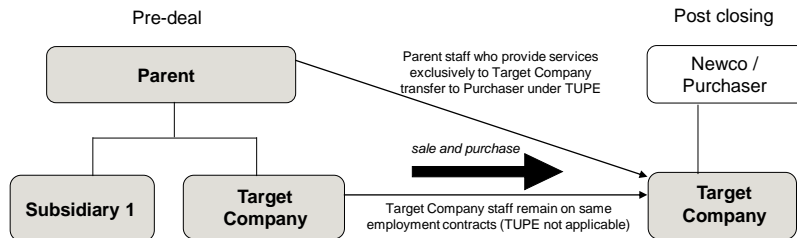
Private M&A: Sale of a business



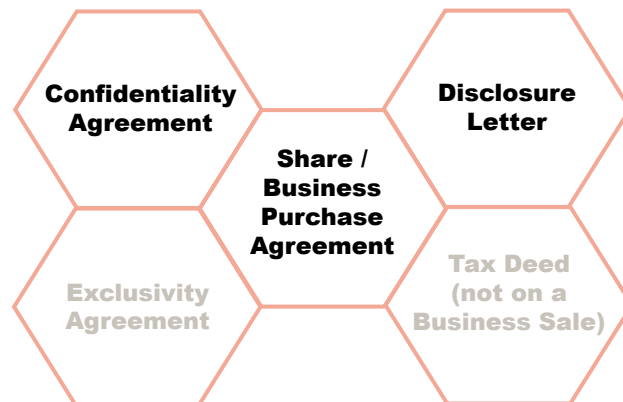
Private M&A: Sale of a company



Private M&A: Combination of share sale and business sale



Private M&A – transaction documents



Private M&A: Shares or assets?

Shares or assets?

What should be purchased: shares or assets?

Advantages of a share sale	Advantages of an asset sale
<ul style="list-style-type: none"> A share sale provides continuity for the business being sold. It avoids the practical pain in the neck of identifying and transferring individual assets and liabilities. Share sales, therefore, are usually easier and faster. A share sale will usually avoid the need to obtain third party consents for particular asset transfers – e.g. landlord's consent for assignment of leases. Do bear in mind, however, the possibility of change of control provisions in any contract. It is usually easier to deal with employment issues on a share sale – no consultation requirement. 	<ul style="list-style-type: none"> It is easier to cherry pick which assets are to be transferred. With a share sale, all assets owned by the company will go across as part of the sale unless transferred out pre-completion. Perhaps even more important is the ability to pick and choose which liabilities are to be assumed by the Buyer.

Tax factors – many and varied.

Most transactions are structured as share sales.

Private M&A: Pensions issues

Share Sale

- Purchaser inherits Target Company's pension arrangements (including historic pension arrangements) whether DB or DC.
- **Section 75** risk for purchaser/vendor?
- Pension liabilities in a DB scheme retained by the “statutory employer” but now liability within new group:
 - **inter-group guarantees**; and
 - “**moral hazard**” provisions under Pensions Act 2004 (contamination risk!)
- New group could inherit significant liabilities!

Private M&A: Pensions issues

- Due diligence is key.
 - DB funding level (contribution rule)*
 - balance of powers (amendment, winding up etc.)
 - equalisation? (other nasties?)*
- Trustees: although no change in “statutory employer” trustees will be keen to understand any change to the “employer covenant”
- What you will be looking at as actuaries?

Private M&A: Pensions issues

Asset Sale

- (Unless agreed otherwise) the Purchaser will not acquire current/historic occupational pension schemes whether DB or DC
- **Section 75** risk for vendor?
- TUPE: terms and conditions of employment transfer excluding
 - rights to “benefits for old age, invalidity or survivors”
- No pension issues? – Unfortunately:
 - **Beckmann** (ECJ) – redundancy benefits
 - **Martin** (ECJ) – enhanced early retirement
 - **Monster** – targeted benefits

Private M&A: Pensions issues



Private M&A: Pensions issues

- Pensions Act 2004 (s 257/258)
 - minimum protection
 - matching employer contributions to DC of up to 6% of basic pay
- Personal pensions
 - rates maintained as contractual term
- Auto-enrolment – is there a qualifying scheme available with the receiving employer?
- “**Fair Deal**” on outsourcing?
- DB: Issues for Vendor/Trustees:
 - Vendor – “What can I do with sale proceeds?” – “Type A Event” on distribution?
 - Trustees – Would the transaction weaken the “employer covenant”? (Is this scheme abandonment?)

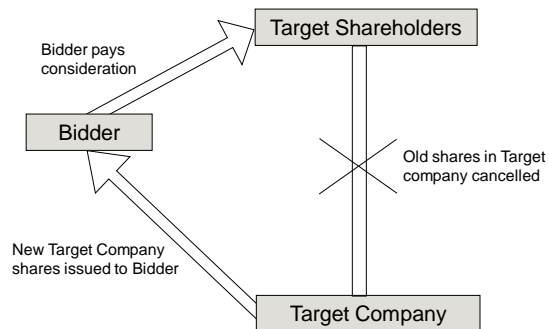
Public Company M&A

Public M&A: deal structures for quoted companies

Public M&A: Takeover offer



Public M&A: Scheme of arrangement



Public M&A: Pensions issues

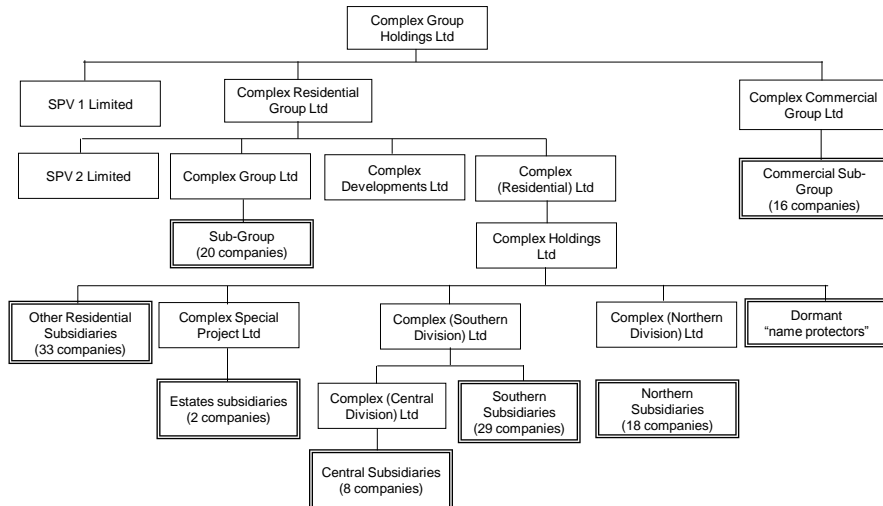
- Purchaser inherits pension arrangements
- Pension liabilities retained by the “statutory employer”:
 - inter-group guarantees; and
 - “moral hazard”
- Due diligence is critical as no warranties will be given by the shareholders or the company
- Trustees: change in “employer covenant”?
 - “*Boots pension trustees seek to block takeover in court*”
 - “*Pension row threatens Sainsbury takeover deal*”

M&A Transactions: Do we need clearance on this deal?

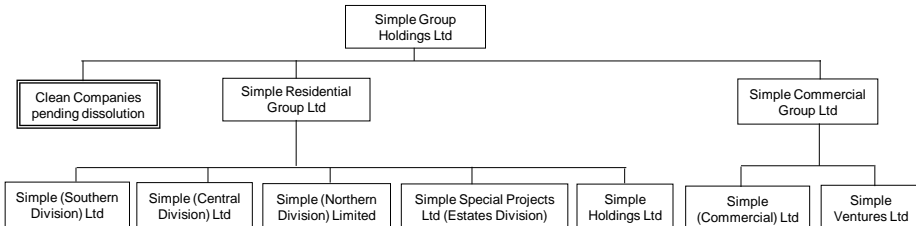


Group Re-organisation

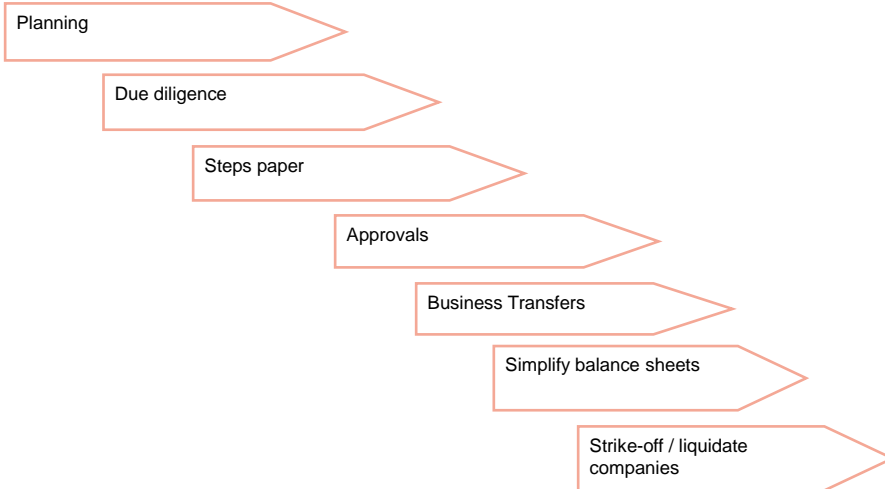
Existing Group Structure - Overview



Post re-organisation: Target Structure



Group re-organisation: key stages



Pensions issues on Group Re-organisation

Section 75 Risk

- Section 75 Pensions Act 1995 provides for certain trigger events when a “buy-out” debt is triggered:
 - “employment-cessation event” (e’er ceases to employ active members when another e’er continues to employ active members) (“ECE”);
 - scheme wind-up
 - insolvency events

Share Transfer

- E’er cease to participate? ECE?
- “Change in control” winding up trigger

Business Transfer

TUPE creates ECE (where all active members transfer)
 “Change in control” winding up trigger
 What to do with “shell companies”?

Covenant risk

- Transfer of shareholding below “statutory employer”
- Transfer of business from or below “statutory employer”
- Additional debt or liability?
- Trustee engagement
- Clearance?

Companies in financial difficulties

PPF Drop-ins



PPF Drop-Ins - Pensions

PPF Drop-Ins - Pensions

- Employer liable to fund DB scheme (with deficit)
- Liability to DB scheme likely to result in insolvency for employer
- Newco created and adopts all pension liabilities
- Newco suffers an “insolvency event” and DB scheme enters PPF assessment
- Original employer continues in business without pension liability
- PPF, tPR and trustee consent required
- PPF (through scheme) typically receives cash payment and often retains equity stake in continuing business (anti-embarrassment clause)

“Pre-packs”

What is a “pre-pack”?

- Pre-packs are a fairly commonplace tool
- Means of effecting sale through an insolvency process
- Sale negotiated in conjunction with proposed administrator
- Sale negotiated BEFORE administration takes place, and completed immediately on appointment
- This ensure certainty and CONFIDENTIALITY – can be very important

Key messages

- Get to grips with the overall structure
- Understand what each party is doing
- Identify key pension risks
- Develop solution to mitigate those or potentially abandon transaction
- If the Buyer does not have operations in UK – they will need a lot of support
- ROLE OF THE ACTUARY IS KEY

Questions?

If you have any further questions, please do not hesitate to contact:



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