

**The Actuarial Profession**  
making financial sense of the future

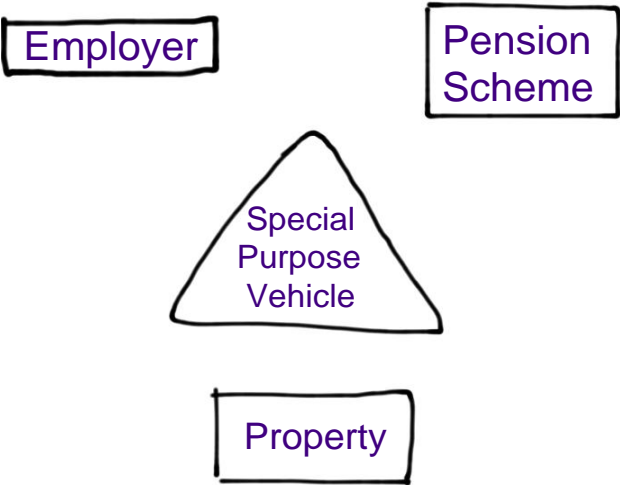
It's as easy  
as ABC

**Open Forum on Asset  
Backed Funding**

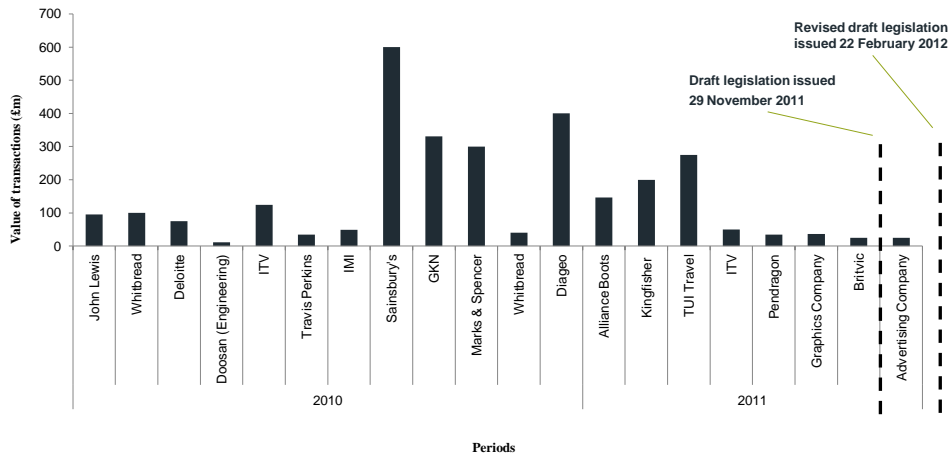
22 March 2012

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What is Asset Backed Funding?



## Timeline of ABCs



## Benefits for Employer

- ✓ Efficient
- ✓ Immediate reduction in scheme deficit
- ✓ No impact on balance sheet / income statement
- ✓ Complements de-risking
- ✓ Operational flexibility retained

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## Asset Considerations

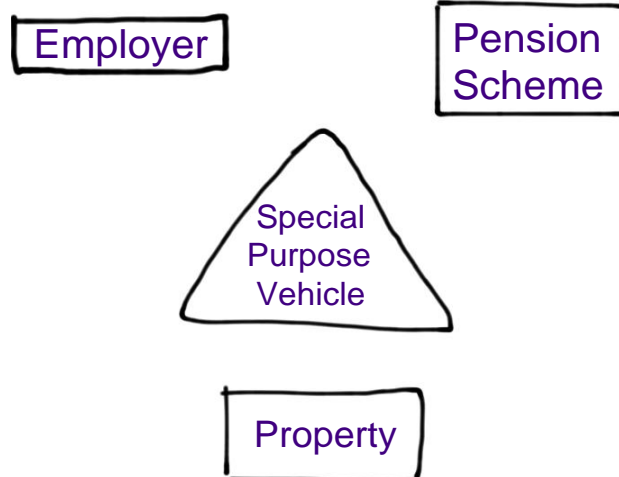
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- ☐ What assets can be used?
- ☐ Accessing value in a default
- ☐ Valuing the assets
- ☐ Banking restrictions
- ☐ Transfer to structure

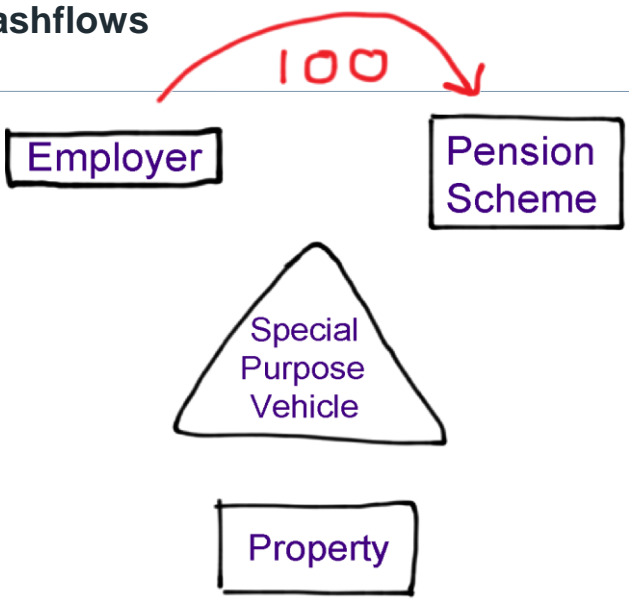
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## Initial cashflows

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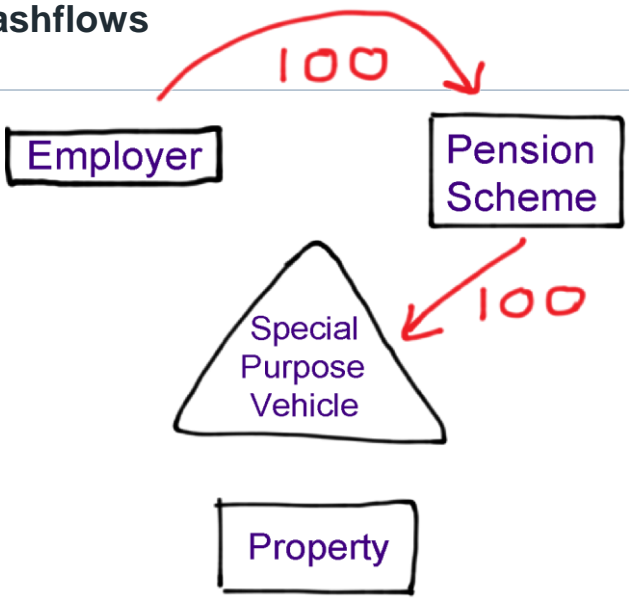
Initial cashflows



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6

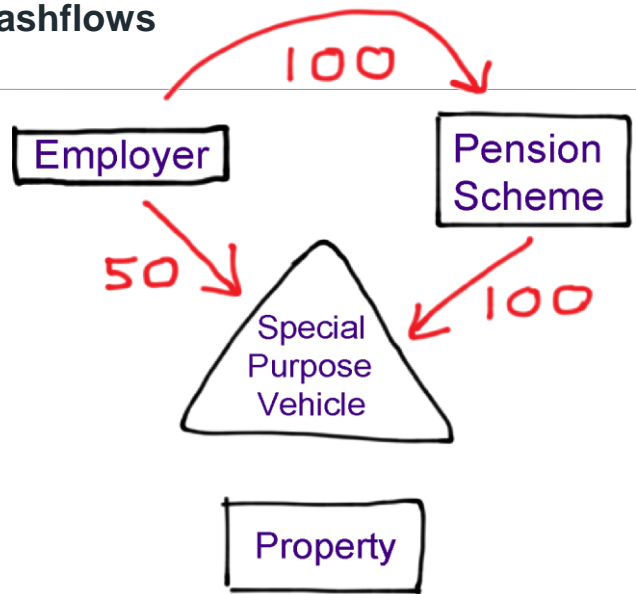
Initial cashflows



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7

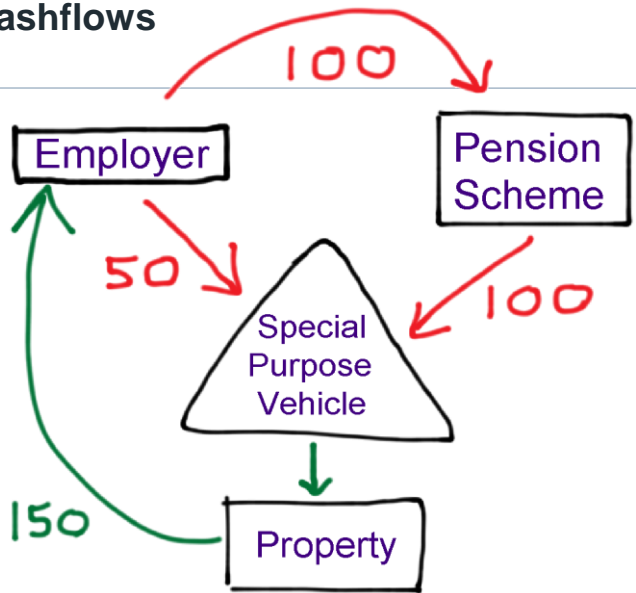
Initial cashflows



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8

Initial cashflows



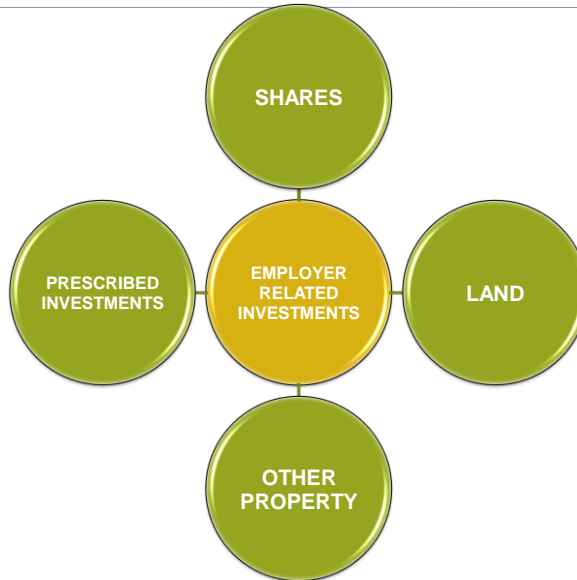
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9

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## Employer Related Investments

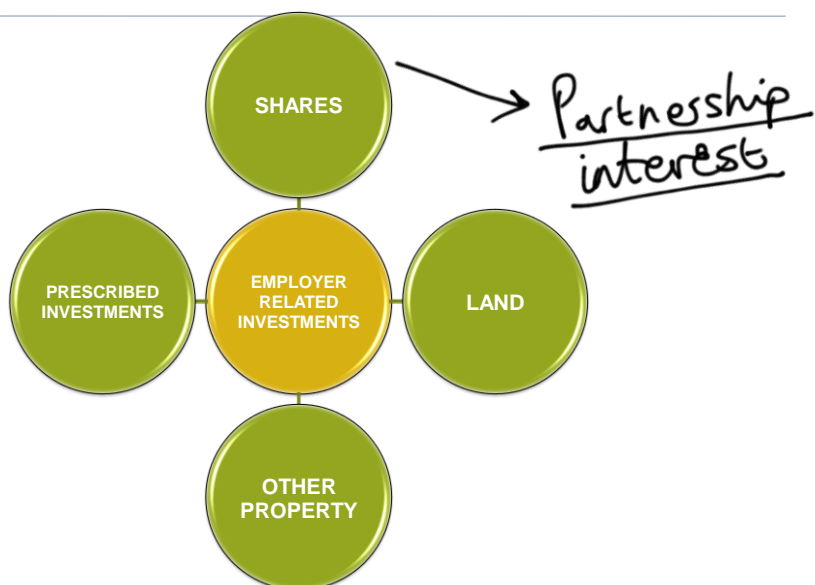
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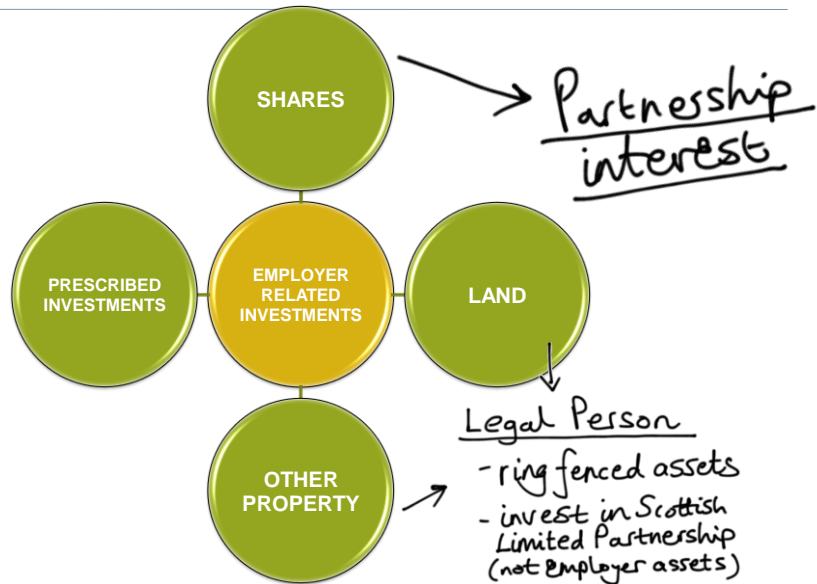
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## Employer Related Investments - Solution

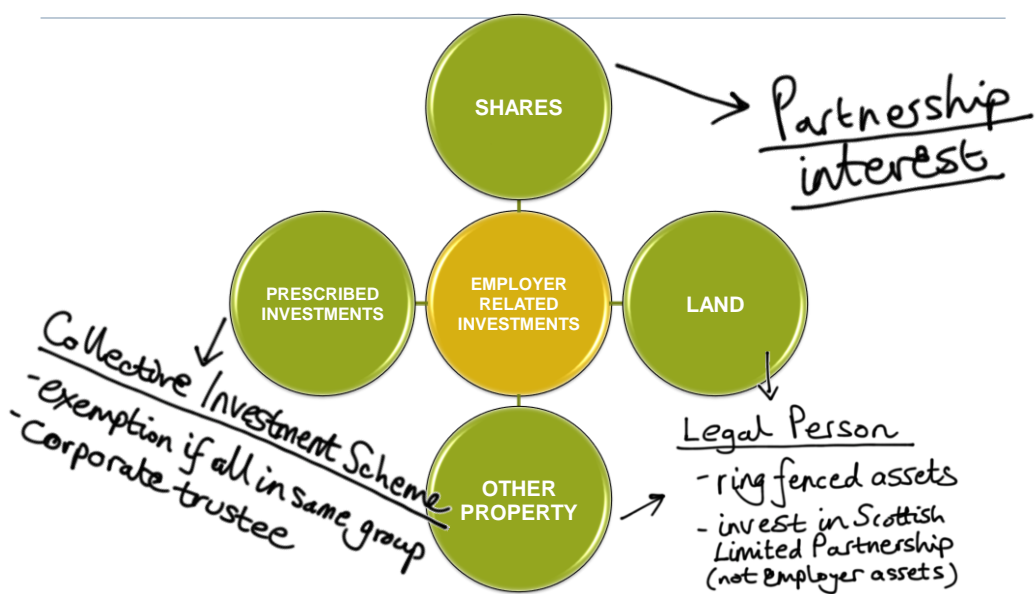
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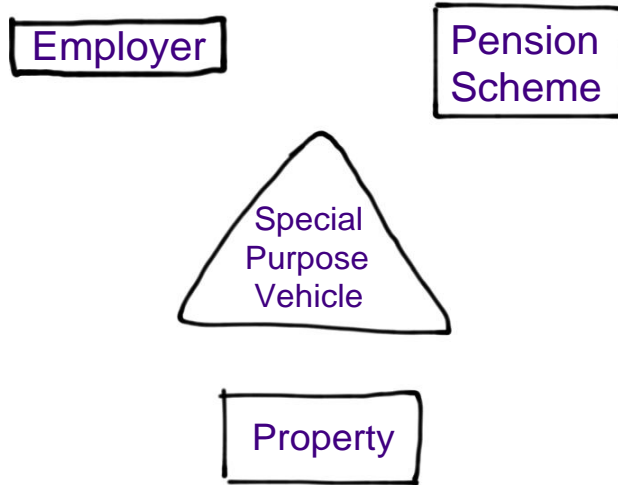
## Employer Related Investments - Solution



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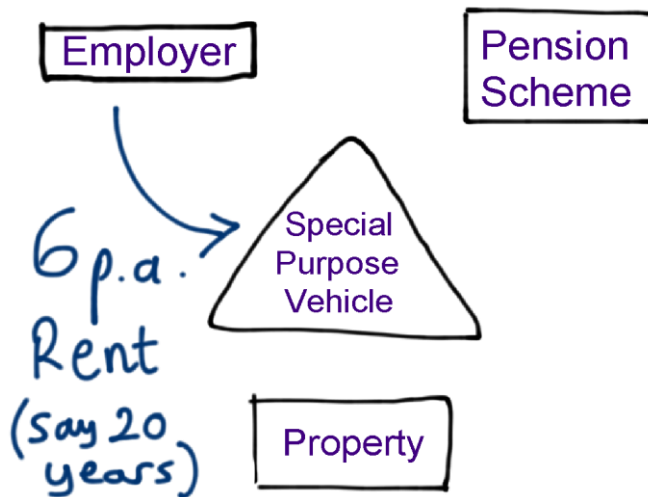


## Income stream



14

## Income stream



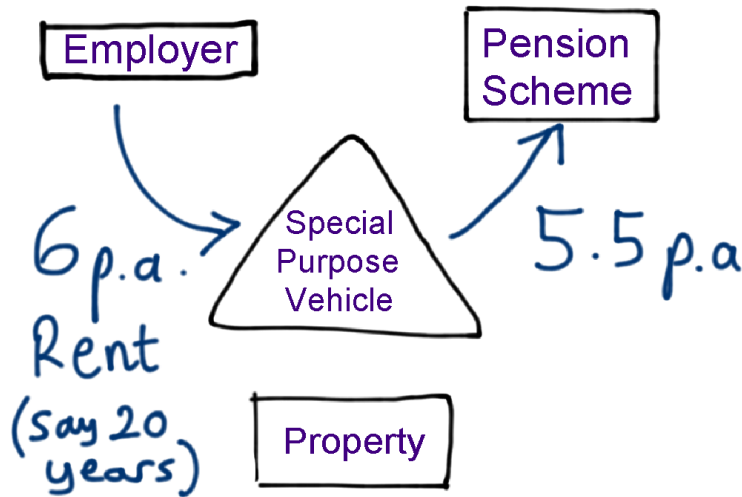
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**Income stream**

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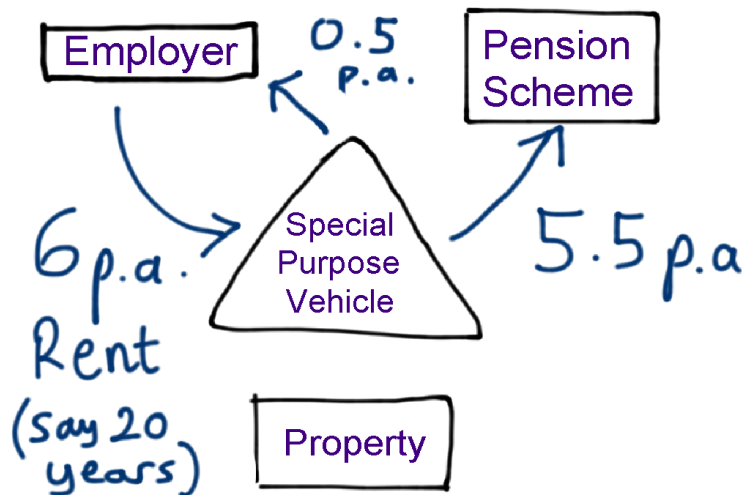


16

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**Income stream**

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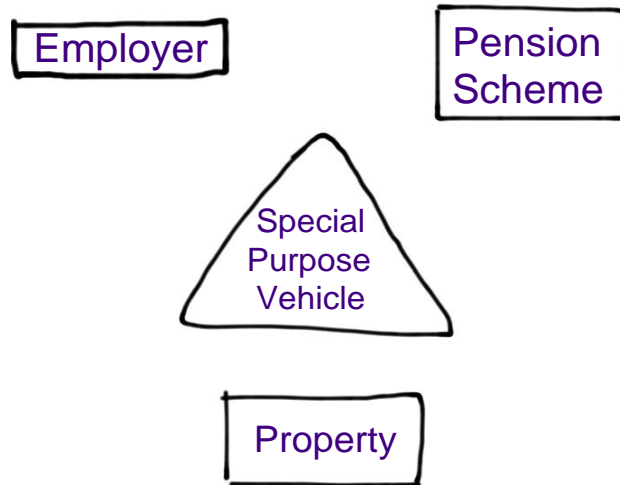


17

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### At the end of the term

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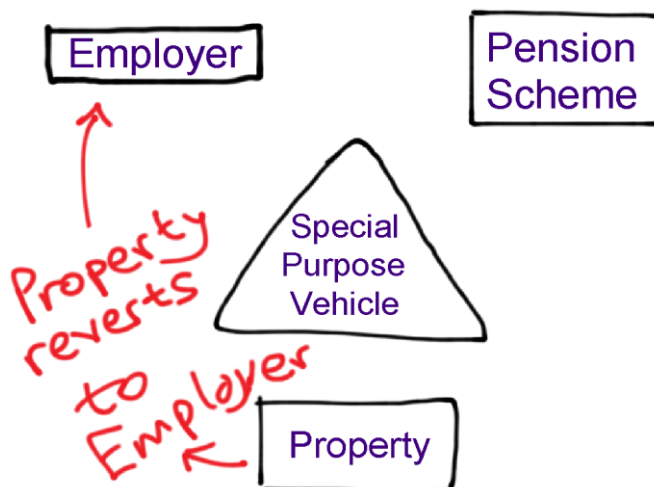


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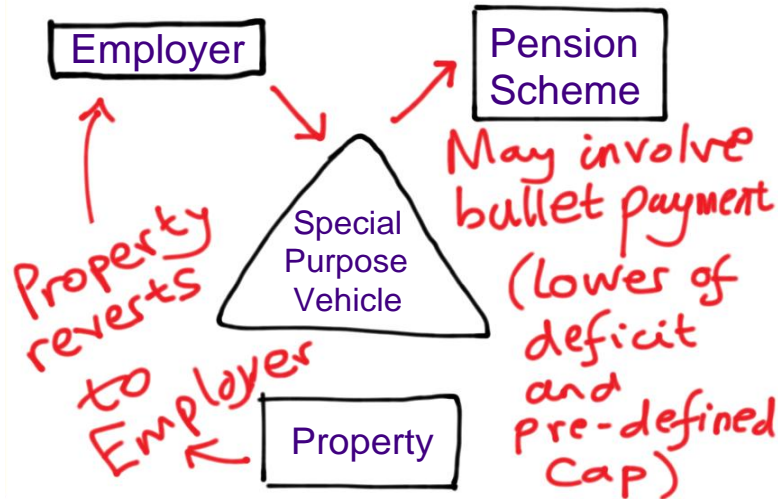
### At the end of the term

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19

## At the end of the term



20

## ABCs

### Tax treatment of asset transfers

- ❑ Simple, **contingent type** arrangements such as parent guarantees or legal charges, may help trustees to accept longer but entirely cash funded recovery plans.

*Scheme does not recognise a plan asset – **no tax relief**.*

- ❑ **Direct asset funding structures**, on the other hand, do transfer real value to schemes. Property can be sold or transferred directly to a scheme and recognised as a plan asset.

***Tax relief on the value of the contribution**, just as it would do with a cash contribution asset.*

- ❑ **ABCs** transfer real value to schemes but allow the sponsor to retain operational flexibility and achieves an affordable cashflow profile.

***Tax relief on the value of the contribution**, subject to HMRC's new ABC rules!*

21

## ABCs

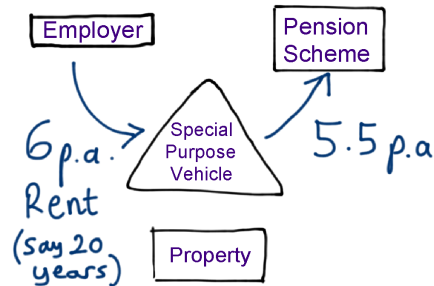
### HMRC tax rules

#### Key changes on rules announced on 22 February

❑ **For upfront tax relief to be available** for new ABC's, the structures must:

1. Be an 'Acceptable Structured Finance Arrangement'.
2. Recognise a financial liability that reduces to nil with regular, equal annual payments to the Scheme (i.e. a series of payments of a fixed amount, e.g. 5.5pa)
3. No final bullet payment.

❑ **If upfront tax relief is not required, more flexibility on structuring.**



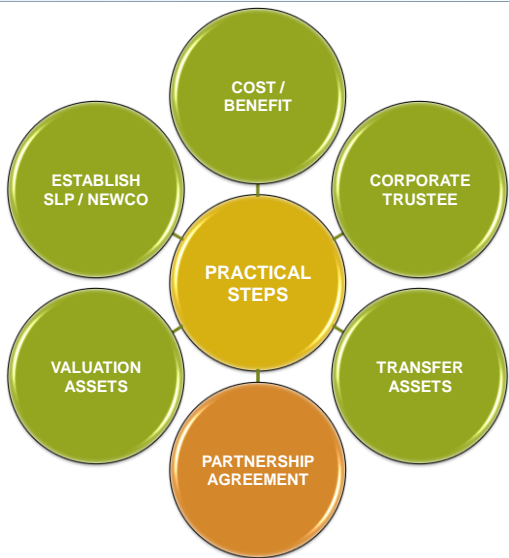
22

## Issues for Employer

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## Issues for Employer – Practical Steps

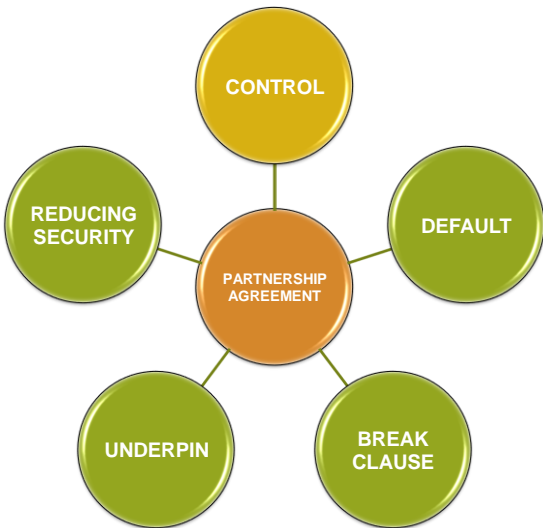
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## Issues for Employer – Partnership Agreement

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## Benefits for Trustees

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- ✓ Increased employer covenant strength
- ✓ Security
- ✓ Long term matching investment
- ✓ Attractive yield
- ✓ Guaranteed income stream

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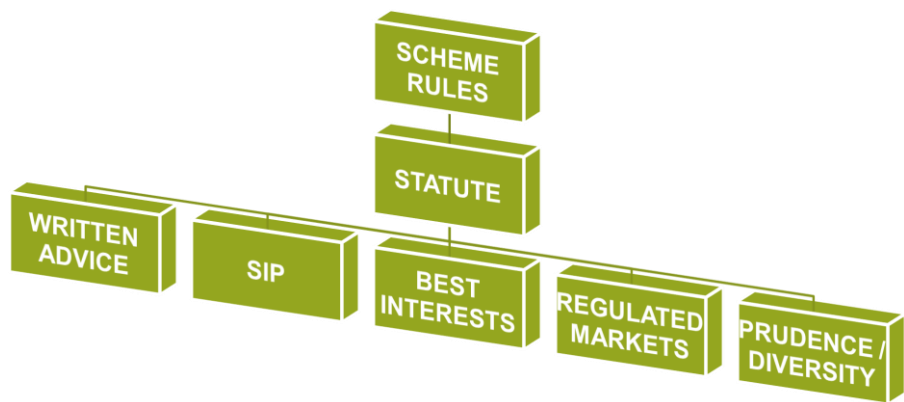
## Issues for Trustees

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## Issues for Trustees - Investment

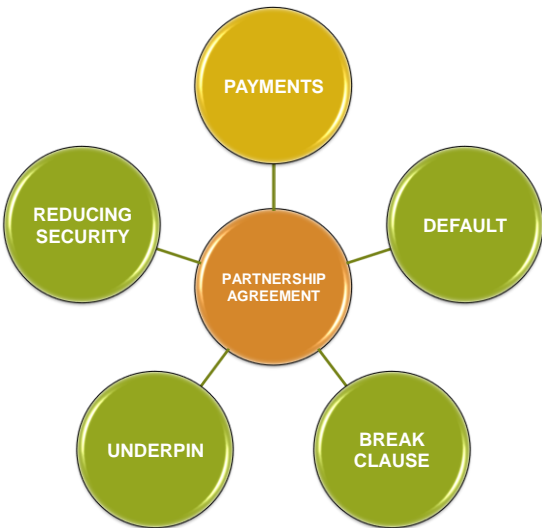
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## Issues for Trustees – Partnership Agreement

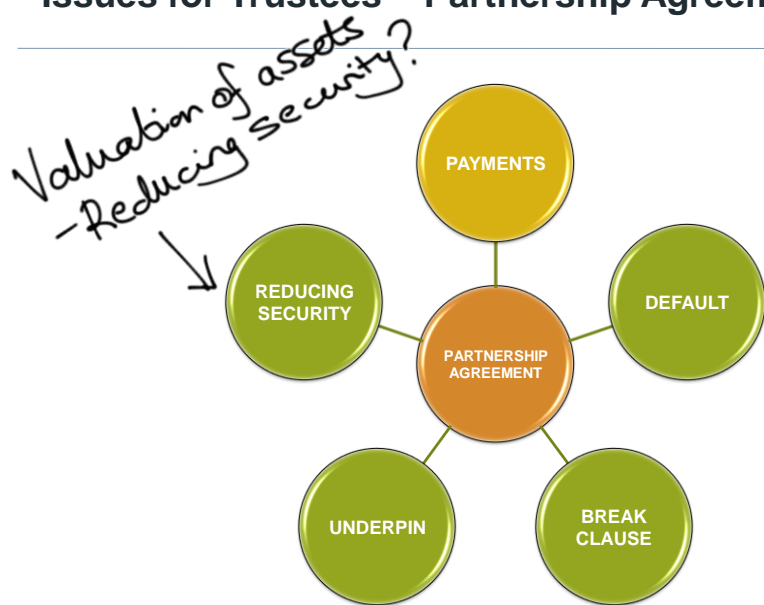
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## Issues for Trustees – Partnership Agreement

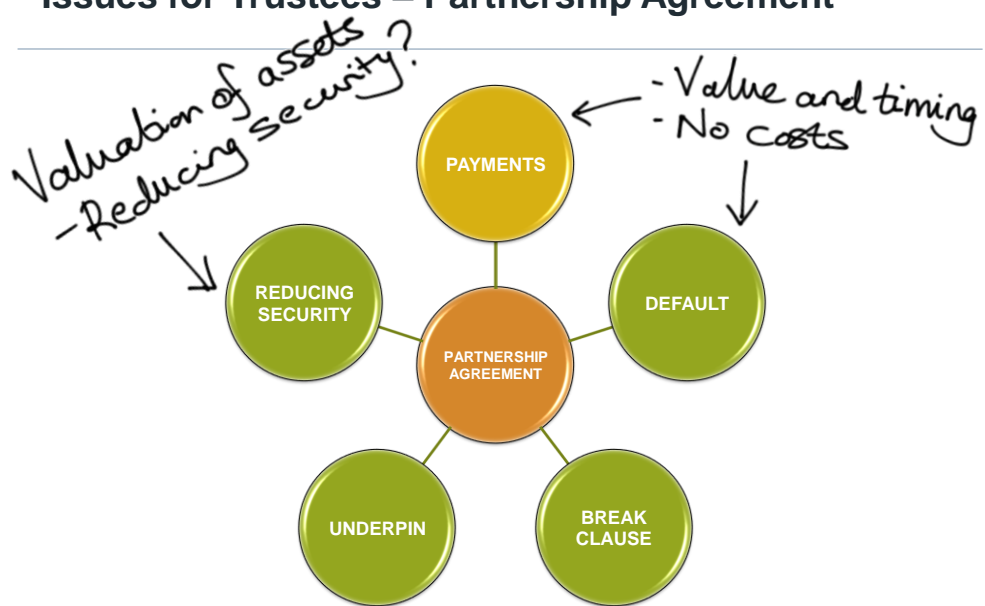
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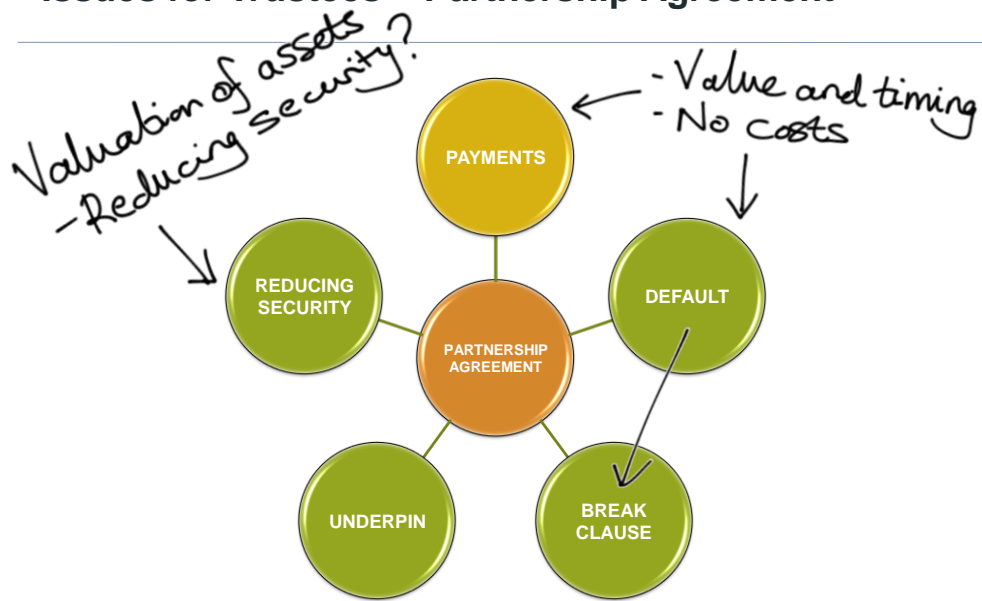
## Issues for Trustees – Partnership Agreement

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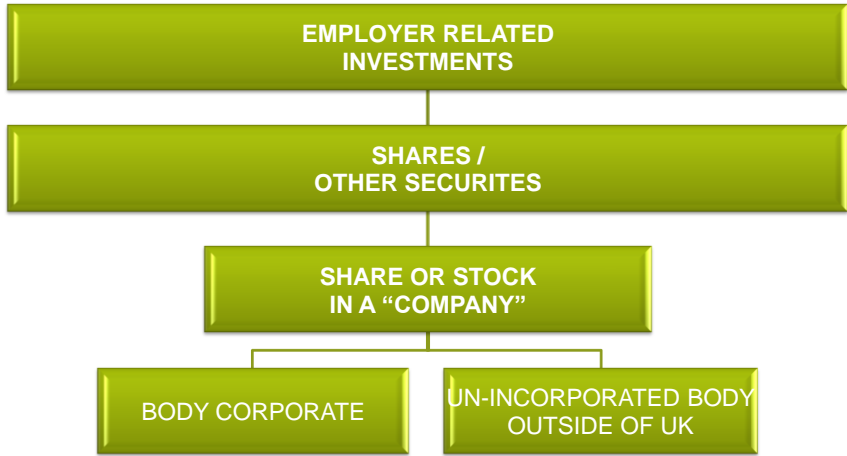




Issues for Trustees – Partnership Agreement



Scottish Independence



Deficit before and after

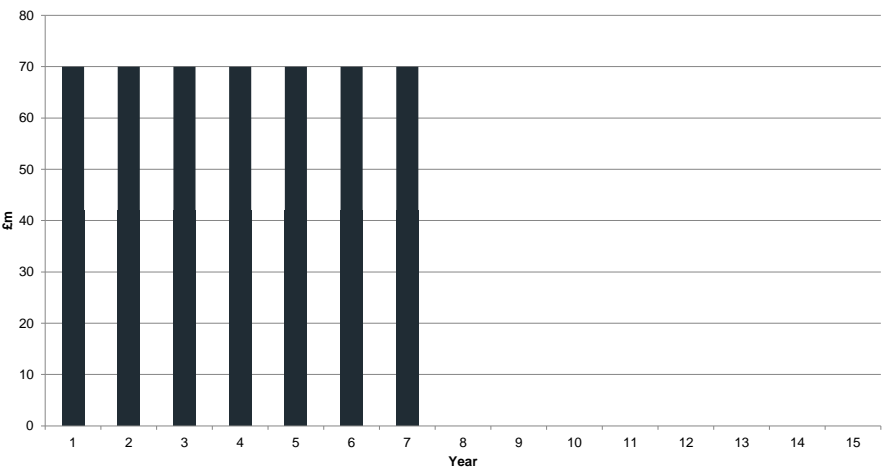
Deficit before funding vehicle	£400m
Value of funding vehicle (treated as an asset)	£250m
Deficit after funding vehicle	£150m

Deficit before and after

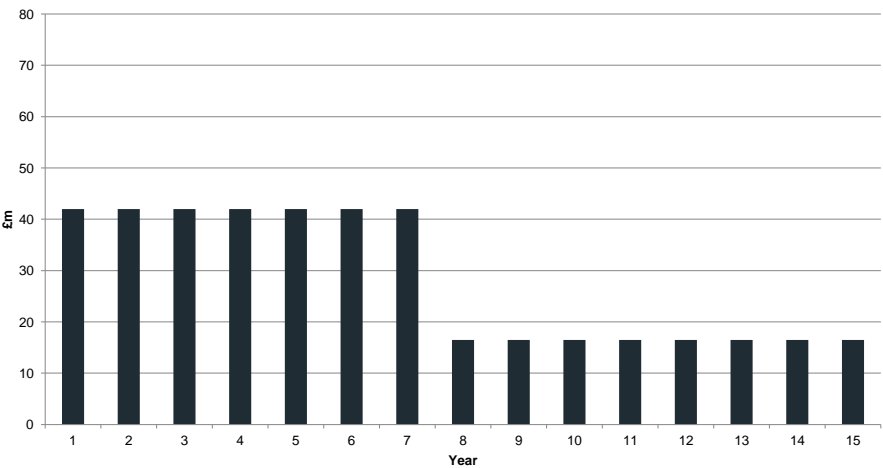
Deficit before funding vehicle	£400m
Value of funding vehicle (treated as an asset)	£250m
Deficit after funding vehicle	£150m

Looks as if a large proportion of the deficit has been paid off by this new asset

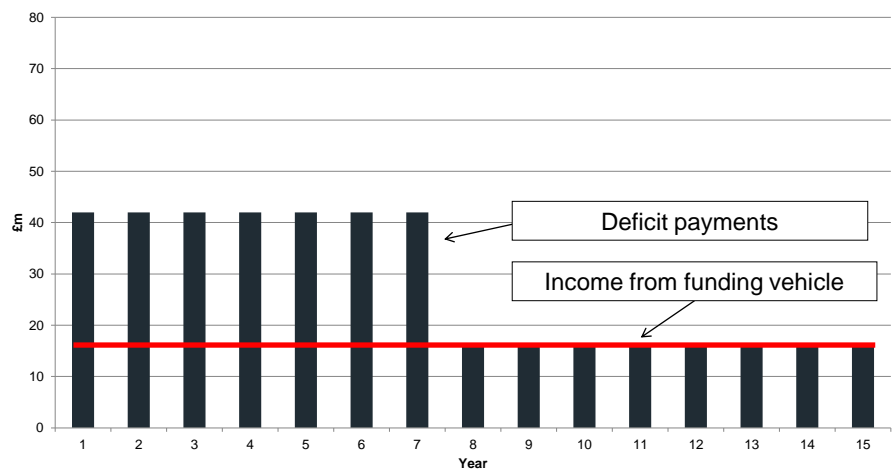
## Recovery payments - before



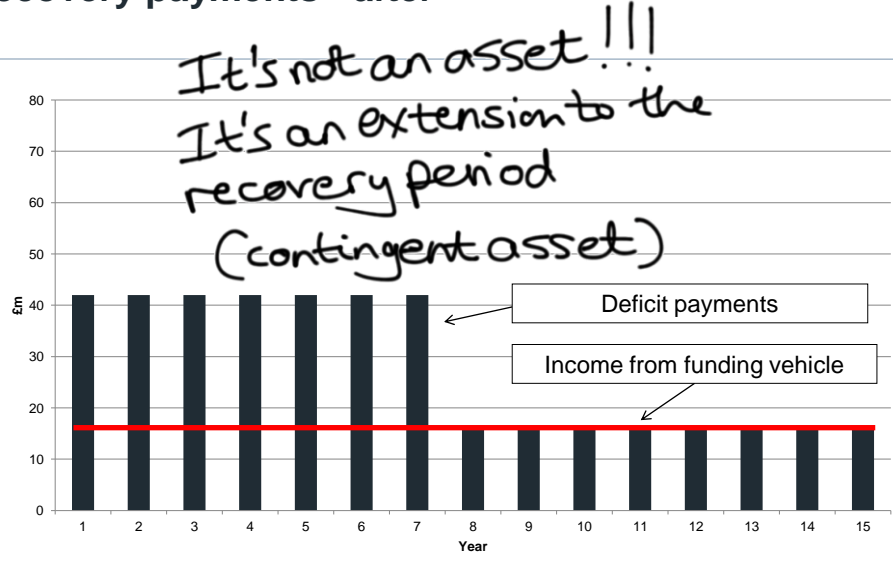
## Recovery payments - after



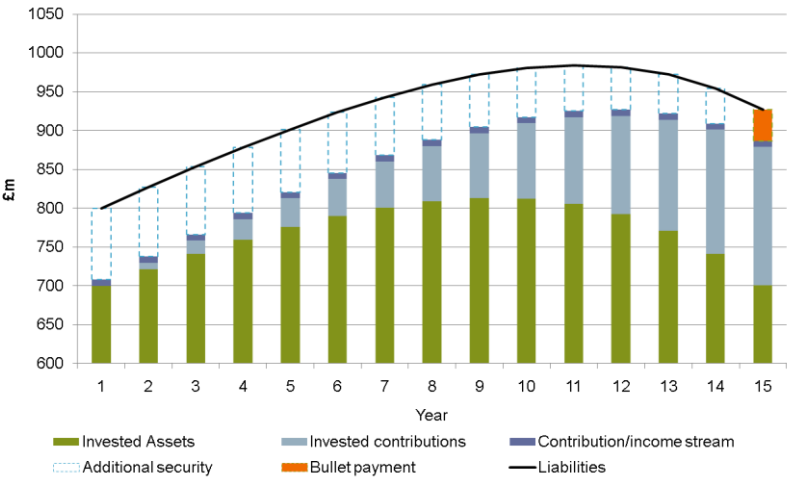
Recovery payments - after



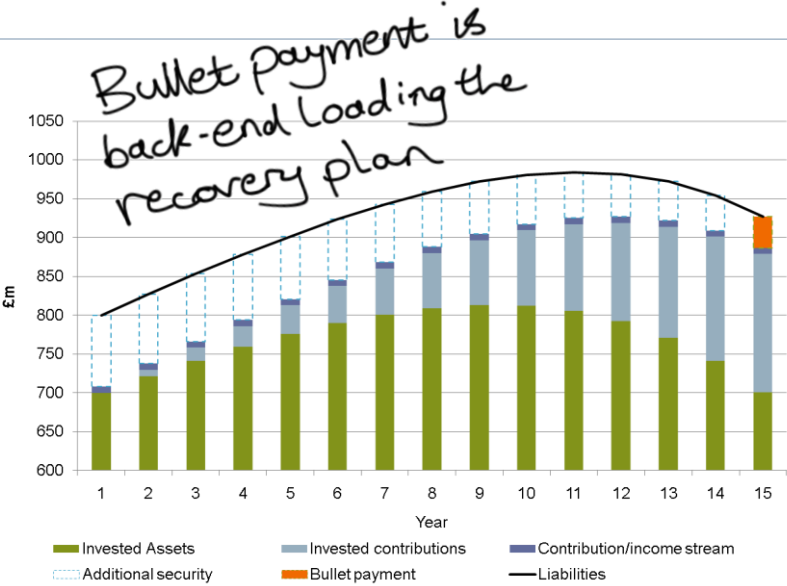
Recovery payments - after



Recovery Plan – funding vehicle with bullet payment



Recovery Plan – funding vehicle with bullet payment



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# ABCs

## Tax and accounting issues

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1) Upfront contribution	<ul style="list-style-type: none"><li>- Is the ABC within the SFA legislation</li><li>- Is it an acceptable SFA?</li><li>- Is the investment by the Scheme at arm's length?</li></ul>
2) Tax treatment on establishing structure	<ul style="list-style-type: none"><li>- Capital gains</li><li>- Stamp Duty</li><li>- VAT</li></ul>
3) Ongoing taxation	<ul style="list-style-type: none"><li>- Is the structure an ABC?</li><li>- Deductibility of 'coupon' payments</li><li>- Underlying source of income</li></ul>
4) Accounting	<ul style="list-style-type: none"><li>- Treatment at group level – consolidate SPV?</li></ul>

42

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Final thoughts

43

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Thank you and  
goodnight