

Business Law Update

October 2005

Pensions Act 2004 - Impact on Corporate Transactions and Capital Structure

By: Michael Berg a Partner at Lane Clark and Peacock LLP

Email: michael.berg@lcp.uk.com

Website: www.lcp.uk.com



Lane
Clark &
Peacock

Actuaries & Consultants

The Pensions Act 2004 has fundamentally changed the environment for companies sponsoring defined benefit pension plans. Trustees have been given radical new powers, and companies will now have to treat the trustees as a powerful creditor with the ability to exert significant leverage over the company.

What this legislation means in practice

Some of the changes in the Pensions Act 2004 are so far-reaching that they could undermine many corporate transactions, including transactions that were not previously thought of as presenting pension plan issues. In particular the new legislation will have a significant impact on:

- company mergers & acquisitions;
- the payment of special dividends;
- changes in corporate structures; and
- business restructuring or refinancing.

Discussions on issues that have previously been thought of as purely company matters may now need to include pension plan trustees.

It is even more crucial now for companies to obtain specialist pensions advice early in the process of change.

Overview of the new pensions legislation

Following a number of high profile cases where employees lost most of their pension, the security of pension plans members' benefits is the over-riding priority of the new legislation.

A key part of the new legislation is the Pensions Protection Fund ("PPF"). In essence, the PPF provides protection for a large proportion of an employee's defined benefit pension rights should the employer become insolvent. The PPF is being funded by a levy on all UK defined benefit plans.

In order to protect the PPF, the Pensions Act 2004 introduced provisions to strengthen pension plan funding. These new measures are likely to lead to more cautious actuarial assumptions being used, with deficits having to be met over shorter periods.

In addition, the new Pensions Regulator can intervene against actions aimed at avoidance of pensions liabilities. The

IN THIS ISSUE

- 2 How to Steal a Company.....
- 3 What is a Going Concern?
- 4 Re-Use of Public Sector Information

Need to Review Share Options and Pre-Emption Rights in your Articles Of Association: Valuation Provisions May No Longer Work!

Pensions - Tupe or Not Tupe?
- 5 Rectification - A Warning to All Company Officers
- 6 The Civil Partnerships Act and Business Taxation
- 7 The Implementation of The Market Abuse Regime
- 8 IR35 -The Implications of having a Middle Man

Pensions Regulator can, if it thinks it reasonable, take two actions: issue a Financial Support Direction; or issue a Contribution Notice. Long established principles for limited liability of companies can now be over-ridden.

Clearance statements - how to get comfort from the Regulator

The risk of receiving a Contribution Notice or Financial Support Direction is making it more difficult for companies to restructure or carry out normal corporate transactions.

The Regulator therefore has the power to issue Clearance Statements in relation to a corporate transaction.

The Regulator suggests obtaining clearance for a corporate transaction when the pension plan is in deficit, measured at this stage on an FRS17 basis (or buyout if there is a question mark over the employer's going concern status).

The Regulator expects companies to apply for a Clearance Statement when an event occurs which the Regulator considers would prejudice the pension plan's position as a creditor in the event of the employer becoming insolvent. These include:

- granting or extending a fixed or floating charge where this affects more than 25% of company assets (other than if it relates to new funding);
- certain large returns of capital or dividends to shareholders; and
- material changes to the control structure of a company.

Approach of trustees in the future

Trustees are being encouraged to take a more active role in managing the deficit, including being prepared to negotiate robustly with the company. Well-informed trustees are likely to take a similar approach to a lending bank, looking carefully into

the company's structure and financial condition, the impact of changes to it, and the ability of the company to generate cash to pay off the deficit. We expect some trustees to commission financial reports from specialist accountants to help them assess this. Where significant amounts of cash become available, we are already seeing trustees seeking a significant acceleration of the cash funding of the deficit.

From high profile cases such as WH Smith, and wider experience, it is clear that trustees have already been taking a more active role in company mergers and acquisitions. This is now rapidly extending to other corporate transactions such as restructurings, refinancings and the payment of special dividends.

Companies will therefore need to involve the trustees at an early stage in corporate activity, to make sure that the trustees and their advisers are satisfied from a pensions perspective.

The Regulator expects that applications for Clearance Statements will be made after the trustees' views have been taken into account, which again adds to trustees' leverage over sponsoring employers.

The issues which the trustees need to consider are complex and may be unfamiliar, requiring, among other things, that sufficient time must be made available for them to consider their options. Engaging the trustees at the earliest possible stage is therefore essential.

An interesting article by Michael Berg. The opinions expressed in this article are those of the author and not necessarily of Davenport Lyons who make no representations as to its accuracy or completeness. The article comprises general information only and should not be used as a substitute for specific professional advice.

How To Steal A Company.....

There is a new and disturbing trend - not of stealing from a company but actually stealing the company itself. It is simply done as the recent case of West Anglian Group Limited -v- Melnikov and Others proved. Mr Melnikov completed a change of directors and change of registered office form, lodged them at Companies House and then ordered a Certificate of Good Standing confirming that the company was solvent and identifying its new director and registered office. So far as third parties were concerned the fraudster then had apparent legitimate control of the company. The original genuine directors knew nothing about what had happened as the certificate and future correspondence were sent to the new

registered office. Once in control of the company Mr Melnikov was free to falsify board minutes, change bank mandates and to empty bank accounts and to sell company assets. He did just that and sold the company's main asset, an overseas subsidiary owning a large and valuable office block in Moscow. The purchaser of the subsidiary then sold off the office block floor by floor. The real English directors only found out when they went to the office in Moscow and were refused entry by armed security guards. However, when searches at Companies House revealed forms completed and lodged by Mr Melnikov, the real Mr Melnikov, who was traced, knew nothing about it as his identity had been stolen by a fraudster.

In this particular case because the directors found out by chance early on they were able to salvage the situation by litigation.

The Solution?

Companies House has introduced two new systems to combat the problem:

"Monitor" - by providing an email alert service (renewable annually). Subscribers to Companies House on-line can (at nominal cost), set up an email alert request to receive documents filed for a selected company. This can alert the subscriber to any fraudulent filings made and provide an opportunity of acting upon them quickly before any damage is done.