Deloitte.

M&A Briefing

Pensions Bill 2020: Impact on M&A

Outlook as at: March 2020

The Pension Schemes Bill 2020 is progressing through Parliamentary process on the way to becoming law in the UK. This Bill is likely to dramatically change M&A and restructuring where DB pensions are involved, especially when this is combined with the expected revised funding code and guidance being consulted on by TPR currently.

We expect there will be an intense period of adjustment and nervousness as the new rules are interpreted and applied. In the short term, there may be fewer players willing to operate in transactions involving pension schemes. These new measures show the Government and TPR's clear intent to act more strongly to protect the interests of pension schemes and their members' benefits. Timely guidance from TPR will be welcome and may help the industry adjust to these new expectations.

The key changes to the pensions regime affecting M&A and restructurings to be introduced by the Pension Schemes Bill that investors, companies and trustees need to be aware of are set out below. On top of this, a new funding code and guidance from the TPR may also cause a significant change to the value impact of pension schemes in transactions.

Context to the proposals:
Pensions have long been a difficult and complex topic to deal with during company M&A and restructuring. Prior to 2005, the pension issue in M&A was largely confined to assessing how best to take account of deficits in the purchase price. In 2005 this all changed following the Pensions Act 2004, which introduced The Pensions Regulator ("TPR") and the Moral Hazard regime. The regime armed TPR with strong powers to issue Contribution Notices ("CN") and Financial Support Directions ("FSD") against those associated and connected with pension schemes. The concept of Employer Covenant was born and Scheme Specific Funding valuations started to set their prudence levels with reference to Employer Covenant strength and investment strategy.
It took several years of hard learning and TPR Clearance Applications for the new pension world order to settle into place and for those involved to understand and even create the rules of the road.

Area	Summary of the change	Deloitte commentary
Criminal sanctions	Introduction of criminal offences for persons found to have: • engaged in an act or conduct that they knew or ought to have known would have a materially detrimental effect on a defined benefit pension scheme; or • committed an act that prevents the recovery of employer debt due to a defined benefit pension scheme or otherwise compromises or settles such a debt. An offence will not have occurred where the person has what the bill states is a "reasonable excuse".	The key concern here is many transactions will result in a materially detrimental effect on a pension scheme, for example the introduction of secured debt into a leveraged private equity transaction. It is yet to be seen whether the definition of reasonable excuse matches up to the original stated intention of the Government during consultation, where it talked of the offence of "wilful or reckless" behaviour in relation to a pension scheme. It's key that the rules around reasonable excuses are defined clearly, or buyers may avoid transactions/turnarounds involving company pension schemes altogether for fear of the risks. This outcome would be to the detriment of the pension schemes the Bill seeks to protect.
TPR Contribution Notice Powers	The new powers add 2 new tests to the Contribution Notice power: • An "employer resources test" where an act or failure to act has "reduced the value of the resources of the employer" and where the reduction is material relative to the Section 75 (insurer buyout measure) deficit of the scheme. • An "employer insolvency test" where an act or failure to act has materially reduced the expected outcome for a pension scheme on insolvency of the employer.	The new tests are now very specific in their focus and clearly highlight the areas of concern for TPR. The Contribution Notice power will still remain subject to an overriding reasonableness test, but it will now be easier for TPR to get to that stage. Previously, it may have been possible to argue the mitigation improved the position of the scheme in other ways and overall the detriment had been mitigated. This will probably no longer be possible as these new powers appear to require the mitigation to directly target specific detriments, for example a cash injection or security on assets to maintain the insolvency outcome. In particular, this could have a big impact on leveraged Private Equity transactions for companies with pension schemes.

Area	Summary of the change	Deloitte commentary
Statement of Intent	Secondary legislation will increase the number of notifiable events and the timing around when they must be notified. It is likely that M&A will need to be notified at some stage in advance of Completion with a "Statement of Intent" filed with the TPR. The Statement will cover the following areas: • the event • any adverse effects of the event on the eligible scheme, • any steps taken to mitigate those adverse effects, and • any communication with the trustees or scheme managers	This has not yet been widely reported on, perhaps as the details are unclear. However, we anticipate based on the White Paper that this could become a material game changer. It is expected that the items covered in the "Statement of Intent" will need to have been considered fully, the trustees of the scheme consulted and suitable mitigation agreed (as required) in advance of Completion. This may not sound much different from the current M&A best practice approaches, however, the devil will be in the detail of the requirements (for example whether Trustees need to be consulted with in advance of a confidential transaction or an auction process signing) and may make some transactions harder to execute.

Get in touch

Deloitte have a specialist team of pensions actuaries and covenant advisors who support many companies in managing pensions risk through M&A and restructuring. If you would like to discuss these issues further, feel free to get in touch with our M&A specialists or your usual Deloitte contact.

Louise Hunter
Tel: +44 20 7303 4244
Email: lohunter@deloitte.co.uk

Kyalo Burt-Fulcher
Tel: +44 20 7007 0584
Email: kburtfulcher@deloitte.co.uk

Paul Geeson
Tel: +44 20 7303 0878
Email: pgeeson@deloitte.co.uk

David Robbins
Tel: +44 20 7007 2810
Email: drobbins@deloitte.co.uk

Tom Partridge
Tel: +44 20 7007 4011
Email: tompartridge@deloitte.co.uk