

Pensions: Asset Backed Contributions (ABCs)

Using corporate assets to efficiently fund pension scheme deficits

The issue

For many UK Defined Benefit pension schemes, an increased deficit will be an unavoidable outcome of a 2016 funding valuation. As a result, companies are anticipating increased cash demands from pension scheme trustees and seeking efficient ways to fund these increased deficits.

The latest Deloitte CFO survey* shows these increased cash demands will come at a time when companies are feeling more uncertain about the future and are increasingly looking for ways to reduce costs.

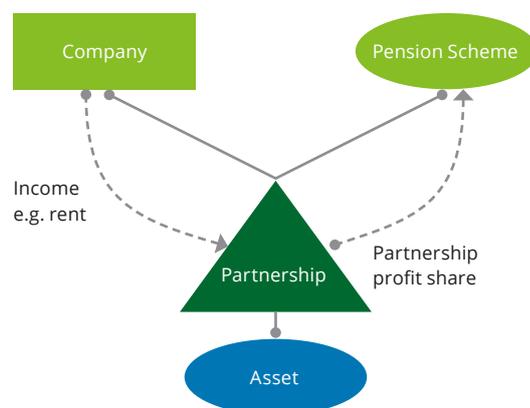
Asset Backed Contributions (ABCs) utilise group assets (e.g. property, brand, loan notes, receivables, stock) and can provide a means of immediately funding a significant amount of pension deficit, whilst preserving corporate cashflow.

ABCs typically work by the company and the pension scheme establishing a Partnership into which group assets (e.g. property, brand, loan notes, receivables, stock) are transferred. These assets will be leased or licensed back to the company, to generate an income stream to provide cash distributions to the pension scheme.

The pension scheme holds an interest in the partnership of an agreed nominal value, which typically delivers a profit share (e.g. fixed annual payments over a 15 to 25 year period). The interest is collateralised by assets which have value independent of the corporate and are ring-fenced for the benefit of the scheme.

The key benefits of using an ABC are set out below. They can also be used to facilitate other objectives, such as pension scheme merger or changes to investment strategy.

An illustrative ABC



Why use an ABC?

Cash preservation	Immediate deficit reduction	Overfunding protection	Security of member benefits	Control
ABCs enable cashflows to be spread over a longer period than a typical recovery plan. Upfront tax relief may also be available	ABCs enable an immediate improvement to the cash funding position	ABCs can be designed to reduce the risk of paying too much into a pension scheme	Scheme trustees gain access to a valuable corporate asset, with a value independent of the Employer's circumstances	The company maintains operational control of the underlying corporate assets

Deloitte Insight

Increased pension deficits and a renewed focus on cost reduction are causing a significant increase in interest in ABCs to fund pension schemes. Deloitte predicts the next few years will bring a resurgence in ABCs.

ABCs have historically been limited to some of the largest pension schemes, but we have seen a significant trend towards lower cost implementation and smaller schemes using ABCs to fund deficits. For schemes with a deficit of more than £5m, ABCs are now a viable funding solution.

* <http://www2.deloitte.com/uk/en/pages/finance/articles/deloitte-cfo-survey.html>

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