May 2013

Revised report under s89 of the Pensions Act 2004

Issued by The Pensions Regulator (the regulator) in relation to the Uniq plc Pension Scheme

Background

The **Uniq plc Pension Scheme** (the Scheme) is an occupational pension scheme. It has approximately 20,000 defined benefit (DB) members.

The Scheme's employers at the time of the transaction, **Uniq plc, Uniq (Holdings) Limited** and **Uniq Prepared Foods Limited** (the Group), were chilled food producers.

Following the Group's restructuring, the Scheme has now received confirmation that the section 143 valuation, showing it is funded above **Pension Protection Fund (PPF)** levels, is binding (final).

It will formally remain in an assessment period for the next 6 months during which time the Scheme's trustee (the Trustee) must determine whether the Scheme can wind up outside of the PPF. If this is the case, its members will receive more than the PPF levels of compensation – although their benefits will still be reduced from their full scheme entitlement. This report explains how the regulator's actions and approach helped to facilitate this outcome for members.

Following a number of transactions and corporate events (which mainly took place between 2000 and 2002) the size of the Group significantly reduced relative to the size of the Scheme.

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The Pensions Regulator

At 31 March 2010, the Scheme had a large deficit relative to the size of the Group. The Scheme's buyout deficit was estimated at £431 million against its assets of £619 million. By contrast the Group's 2009 results were a loss from continuing operations of £21 million on turnover of £287 million. It was apparent to all parties that even if the Group returned to profitability, its operations were not on a scale to address the Scheme's deficit.

At that time, Uniq plc was listed on the London Stock Exchange, but its market capitalisation had fallen to below £10 million. It faced market difficulties because of the perception of an insurmountable pension problem posed by the Scheme. This perception had a negative impact on potential investors, customers, suppliers and creditors.

Given its position relative to the size of the Scheme, the Trustee took the view that the employer covenant (ie the Group's ability to support the scheme) was extremely weak.

Regulatory action

The regulator's initial objective, when faced with schemes in these kinds of situations, is to help employers and trustees identify whether the scheme is viable without a strong enough employer covenant to cope with the risk of the scheme's adverse funding performance. Excessive funding or investment risk exposes all members (especially the younger scheme members) and the PPF.

It was apparent from an early stage in the negotiations surrounding the 31 March 2009 valuation that a conventional funding solution was not realistic. A number of radical options were considered, including actions which would constitute 'abandonment'. The Trustee and the Group engaged with the regulator to discuss how they should approach the matter.

The Trustee, the Group and the regulator worked together through a series of preliminary questions, which the regulator asks when faced with schemes in this predicament. This is to reach a shared understanding of the scheme's position and allows the parties to explore a solution within that understanding.

Is a recovery plan viable?

The Trustee explored a range of recovery plans (including a plan of more than 40 years) and the corresponding level of investment performance, and related risk, needed in each scenario.

However, it was clear that the Group's ability to support even these plans was dependent on its ability to raise fresh capital. There was recognition on the part of all parties that the Scheme was the Group's dominant creditor. In the event of insolvency, any shareholder value would be wiped out due to the size of the debt owed to the Scheme. As a consequence, the economic reality was that the Scheme effectively owned the Group. The threat that the pension deficit posed to the Group's solvency made it too difficult to find suitable terms for raising fresh capital.

Without a solution to the Scheme issues, the Group's covenant could not be strengthened and it remained too weak to tolerate risky investments and support a viable recovery plan.

Is insolvency inevitable?

The Group's view was that, without the Scheme to support, it would have a reasonable prospect of future growth, thereby maintaining employment and generating value which would be lost in insolvency. Both the Trustee's and the Group's position was that insolvency appeared inevitable if the Group did not undergo a restructuring, with an injection of fresh capital.

Are moral hazard powers available?

Having considered the circumstances of the Scheme and the Group, the regulator came to the view that its 'moral hazard' powers (ie sections 38-51 of the Pensions Act 2004) were not available. This view was informed by the fact that the key transactions and corporate events affecting the size of the Group took place before those powers were in place[1].

This work led to the Trustee concluding that no viable scheme funding solution could be found. The Scheme could never realistically expect to pay the full benefits promised to its membership without successful execution of an inappropriately risky investment strategy. The regulator agreed with this view on reviewing the available information. At around this time, the investment strategy risk in the Scheme was reduced by the Trustee. The next stage was to negotiate the terms of the restructuring.

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The timing of the key transactions and events was relevant because acts can only be relied on for the purposes of a section 38 contribution notice case if they take place on or after 27 April 2004. As a result of the timing of the events, the only entities of interest which were associated or connected with employers of the Scheme after the moral hazard powers became available were themselves employers in respect of the Scheme. There was not considered, in the circumstances of the case, to be good reason to seek to exercise moral hazard powers in respect of those employers. This footnote was added to the report by way of clarification in May 2013.

A full range of potential solutions were identified and considered. During discussions, the regulator applied the following principles in the context of this case, to test the merits of the different options:

- the scheme members and the PPF are significantly better off than if insolvency takes place
- the scheme members and the PPF get a sufficient stake in the surviving business to ensure no exploitation of them post-restructuring. Where gain is available, the scheme members and the PPF get no less than a proportionate amount of this gain
- the risks to the PPF are acceptable in the context of our broader duties to members as well as the PPF
- the option demonstrates that proper account has been taken of the members' interests, especially where the risks have increased, and appropriate ongoing arrangements are in place to manage those risks
- costs are proportionate and fairly shared.

The principles reflect the regulator's thinking about how the legislative framework should operate. Although each case will be considered on its own facts, the regulator anticipates that these principles will guide its decision-making in this area. When approaching other cases of this nature, in addition to the principles listed above the regulator is informed by the PPF's appetite for risk as well as the potential for the deficit on a PPF basis to widen over time.

The regulator, together with the PPF, worked with all parties which resulted in a deficit-for-equity proposal. This solution positively answered all of the regulator's questions above and met the principles. Early in 2011, the regulator issued a clearance statement to facilitate the restructuring and gave approval for a Regulated Apportionment Arrangement, ie regulation 7A of the Occupational Pension Schemes (Employer Debt) Regulations 2005 (as amended), a rarely-used mechanism which needs regulator approval and the PPF to agree.

Under the arrangement, the Scheme (via an SPV) received the value of 90.2% of the equity in Uniq plc, then listed on the Alternative Investment Market, and received significant cash. The Group's shareholders also backed this arrangement, taking the view that ownership of the remaining 9.8% of equity, shorn of the Scheme, was better than getting back no value in the event of the Scheme's deficit bringing about insolvency.

Outcome

On 12 July 2011, Greencore Foods Limited, a wholly owned subsidiary of Greencore Group plc, made a cash offer of £113 million for the entire issued share capital of Uniq plc which was declared unconditional on 23 September 2011. This resulted in £100.8 million flowing to the Scheme. The Scheme's Trustee entered into a 'buy-in' contract on 12 December 2011, thereby ensuring that members would ultimately receive benefits at least equal to PPF compensation levels from a Financial Services Authority (FSA)-regulated insurance company.

As the value of the Scheme's assets at the PPF Assessment Date (24 March 2011) exceeded its liabilities on the s143 valuation basis, the Trustee will now seek to secure member benefits above PPF compensation levels.

General

In situations where the sponsoring employer's ability to fund the scheme is so weak that there is little or no reasonable chance of paying the benefits promised with acceptable levels of risk, the regulator, alongside the PPF, is ready to work closely with trustees and sponsors to achieve the best possible outcome for members and PPF levy payers in the particular circumstances. The Uniq case is a good illustration of a trustee and sponsoring employer working closely and collaboratively with the regulator, and the PPF, to achieve this end.

However, every situation remains specific to its own circumstances, and the solution in this case will not be appropriate in most cases. It remains the regulator's view that, where an employer is able to provide appropriate long-term funding for a viable recovery plan for its DB scheme, this is the best outcome for scheme's members and the PPF.

In situations where the scheme's continuation is not in the interests of the generality of the members (because there is little or no chance of paying the benefits promised under it), capturing and maximising the value of the scheme's interest in the employer and delivering that value for the benefit of the members should become the trustee's priority. Failing to reach this satisfactory resolution may lead to the regulator considering exercising its own power to wind up these schemes under Section 11 of the Pensions Act 1995.

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