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Re Uniq plc [2011] EWCH 749 (Ch)

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The recent High Court judgment of David Richards J in *Re Uniq plc [2011] EWCH 749 (Ch)* sanctioned a ground breaking scheme of arrangement, which formed an integral part of a larger restructuring, allowing Uniq plc to undertake a pension deficit for equity swap effectively disposing of its defined benefit pension liabilities and avoiding insolvency.

This case is of importance to practitioners as it shows a willingness of the court to look beyond the terms of the scheme itself, in ascertaining whether a proposed scheme is a genuine compromise or arrangement, where the proposed scheme is an integral part of a wider restructuring. In addition, the pension deficit for equity swap was a novel arrangement and is likely to be explored by other employers looking to dispose of their defined benefit pension liabilities and avoid insolvency.

Background and facts

Uniq plc (formerly Unigate plc) (the 'Company') sponsored a very large defined benefit pension plan (the 'Pension Scheme'). Following the sale of its dairy and logistics business in 2000 the Company, despite significant downsizing of its business, retained responsibility for the Pension Scheme which had over 40,000 members.

A further reorganisation in 2001 resulted in the number of members of the Pension Scheme being reduced to approximately 21,000, most of whom were deferred members or pensioners. Various reorganisations of the business meant that there was a smaller business base from which the Company could fund any deficit in its Pension Scheme. Thus, the Pension Scheme was closed to new members in 2002 and to existing members in 2009.

The deficit in the company's balance sheet at 31 March 2006 was GBP 125 million. A sum of GBP 97 million was placed into a secure account by the Company in an attempt to meet the deficit. The economic crisis in 2008 resulted in a sharp decline in the value of the Pension Scheme assets (comprising a range of assets including equities, bonds and gilts) and as a result of this and changing assumptions the deficit, by the end of 2008, amounted to approximately GBP 170.9 million. As at 30 June 2010 the deficit calculated using the 'best estimate' assumptions used in the IAS 19 accounting valuation basis, was GBP 229 million. On buy-out assumptions adopted by the Pensions Trustee the net deficit was estimated at GBP 428 million, rising to GBP 473 million at 31 July 2010 (net of the GBP 97 million in the secure account).

The Pension Scheme deficit presented a serious threat to the business of the Company. Its continued growth combined with the smaller business base from which to fund it, led to the Company exploring possible funding options to provide a solution to the large deficit. Any funding solution had to be agreed between the Company and the Pension Scheme Trustee and approved by the Pensions Regulator.

In April 2010, the Pensions Regulator rejected an initial proposal agreed between the Company and the Pension Scheme Trustee. The initial proposal included a three year contributions holiday whereby the Company would not pay any contributions to the Pension Scheme until 2013 at which point the Company would pay the higher of 33% of EBITDA or GBP 10 million to the Pension Scheme until the deficit was cleared. At the time, the Company would not expand on the reasons for the rejection and merely stated that 'the Pensions Regulator has stated that the pensions framework, as currently constituted, does not meet all of its criteria for clearance.'[1]

Following further discussions, the proposed scheme of arrangement (the 'Scheme') was cleared by the Pensions Regulator on 9 February 2011. Despite meeting the requirements of the Pensions Trustee, the Pensions Regulator and preserving Pension Protection Fund (PPF) protection, the Scheme and the proposals to be implemented by it, also required approval from the shareholders (pursuant to the Listing Rules) and the High Court.

The restructuring was to be implemented by means of a regulated apportionment arrangement ('RAA') for

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1 <www.bbc.co.uk/news/business-10681840>.

the purposes of the Employer Debt Regulations and through a scheme of arrangement in accordance with sections 895 to 899 of the Companies Act 2006 (the 'Act').

The principal feature of the Scheme was a pension deficit for equity swap whereby the Pension Scheme Trustee agreed to release the Company, Uniq (Holdings) Limited (a wholly owned subsidiary of the Company) ('Uniq Holdings') and Uniq Prepared Foods Limited (a wholly owned subsidiary of Uniq Holdings) ('UPF') from their respective obligations in relation to the Pension Scheme in exchange for a 90.2% shareholding in the Company to be held by Angel Street Limited a newly incorporated non-Group company ('Newco') and a cash payment of GBP 14 million to the Pension Scheme including the payment of certain expenses.

The restructuring, of which the Scheme was an integral part, involved the following steps:

1. Newco was formed to own the 90.2% shareholding which is intended to be sold for the benefit of the Scheme. These shares are to be held on charitable trust and are not expected to have any value.
2. The Scheme was segregated into defined benefit and defined contribution sections so that the defined contribution section would remain, so far as possible, unaffected by the restructuring.
3. The Company, Uniq Holdings, UPF, Newco, the Pension Trustee and the Pensions Regulator entered into an RAA deed. Pursuant to section 75 of the Pensions Act 1995 (as amended) ('Section 75') an employer participating in a defined benefit pension scheme is liable to make a payment to such scheme upon it ceasing to participate. In a multi-employer pension scheme such as this, such payment is broadly determined as the proportion of the total buy-out deficit attributable to employment with that employer. The object of an RAA is to permit a company to cease to participate without paying its full share of the Section 75 debt. The RAA in this case provided that each of the Company, Uniq Holdings and UPF would cease to participate in the Pension Scheme and their respective Section 75 liability upon ceasing to participate would be reduced to GBP 1 (except for UPF whose liability was reduced to GBP 12.445 million) and all other Section 75 liabilities of those companies be apportioned to Newco. The full operation of the RAA deed was conditional upon completion of the restructuring up to and including the making of the administration order for Newco.
4. The Scheme involved multiple steps, in summary; it involved the subdivision of shares held by the existing shareholders, a bonus issue of shares to the existing shares, cancellation of most of the shares held by the existing shareholders and the issue of new shares to Newco to facilitate the eventual shareholdings. Newco undertook to pay the nominal value of the shares in cash for a total amount of around GBP 66.6 million.
5. UPF paid GBP 897,000 and the GBP 66.6 million mentioned in point 4 to Newco in consideration for Newco assuming UPF's liability to the Pension Scheme. It also paid GBP 14 million to the Pension Trustee in order to discharge its statutory debt.
6. Newco applied the GBP 66.6 million in paying up the shares issued by the Company to it.
7. The Company terminated the Pension Scheme resulting in the winding up of the Pension Scheme. This in turn triggered the debt due from Newco to the Pension Trustee equal to the deficit under Section 75, as Newco would be unable to pay the debt it would be rendered insolvent.
8. Newco applied for appointment of administrators under Schedule B1 to the Insolvency Act 1986 constituting an 'insolvency event' under section 121 of the Pensions Act 2004.
9. RAA deed came into effect releasing the Company, Uniq Holdings and UPF from their respective liabilities under the Pension Scheme.

Following implementation of the Scheme, Newco owned 90.2% of the shareholding and, as a requirement of the City Code on Takeovers and Mergers Newco, would have to make a general offer to the other shareholders to acquire their shares in the Company. The Takeover Panel agreed to waive this requirement provided such waiver was approved by the shareholders at the General Meeting.

The Board of the Company anticipated that without implementation of the restructuring and the Scheme it was inevitable that the Company would be insolvent within the next twelve months. This anticipation was based on the knowledge that the Company was not, and was unlikely to be, in a position to be able to satisfy any request by the Pension Trustee or the Pension Regulator for the minimum level of pension contributions required to ensure the funding position did not deteriorate further and in any case could not fund the full pension deficit, which was in excess of GBP 400 million on the basis of the valuation assumptions adopted by the Pension Trustee.

In addition, the Company's Bank had refused to provide a new loan facility unless the Scheme became effective. The Company's cash at that time was unlikely to be sufficient to fund the Group's expected working capital requirements for the next twelve months.

The timing and severity of these actions were not in the Company's control and were entirely dependent on the action taken by the Pension Trustee and the Pension Regulator. This meant that failing implementation of the Scheme and the restructuring, the likelihood of there being any value for the shareholders was remote.

At 30 June 2010, in addition to the Pension Scheme deficit, the Company had unsecured trade debts of GBP 46.9 million. In the event of insolvency of the Company it was likely that only a small dividend would be paid whereas if the restructuring was implemented and the plans for the business delivered the Board of the Company anticipated that these creditors would be paid in full as and when the amounts owing to them fell due. Thus the restructuring and the Scheme were presented as being in the best interests of both shareholders and creditors.

Shareholder approval for the Scheme and the wider restructuring was obtained at a General Meeting held on 25 February 2011 and the Company then applied under section 899 of the Act for the court to sanction a scheme of arrangement between it and its members. The scheme was a crucial element of a complex business restructuring and was presented as the only way to prevent the insolvency of the Company.

Completion of the restructuring was announced on 24 March 2011 and the Company was released from its substantial pension deficit of more than GBP 400 million. Following this Newco appointed a corporate financial adviser and announced intention to undertake a process to realise all or part of its shareholding.

The decision

Sanctioning the Scheme

The High Court sanctioned the Scheme and confirmed the related reduction in capital. The court has an unfettered discretion as to whether to approve a scheme of arrangement and in exercising that discretion, David Richards J set out the criteria upon which a court is likely, but will not be required, to approve such a scheme:

(a) the requirements of statute have been satisfied;

(b) the class is fairly represented by those who attended the meeting and there has been no coercion of the minority; and

(c) the arrangement is such as an intelligent and honest man, a member of the class concerned and acting in respect of his interest, might reasonably approve.

David Richards J ruled that each of these conditions was satisfied in relation to the proposed Scheme and that this was a scheme which an 'intelligent and honest member acting in his interests as such might reasonably approve'.

Benefit to existing members

The court was satisfied that there was a benefit to existing shareholders.

A scheme of arrangement must constitute a compromise or arrangement between a company and its members or creditors or a relevant class of the same. If said members or creditors surrender all of their rights and receive no benefit, there can be no compromise or arrangement.[2]

The effect of the Scheme was to significantly dilute the existing shareholders' present shareholdings reducing such that they only retained an interest of 9.8% and to leave them in a position where their shares could be acquired compulsorily in the event of a general offer accepted by Newco for its 90.2% interest.

The Scheme was an integral part of the restructuring which, if implemented, was expected to confer substantial benefit on the members bound by the scheme. It was possible, but unlikely, that the Scheme could be implemented without the rest of the restructuring coming into effect and in considering whether the proposed scheme constituted a benefit to existing members, David Richards J held that it would be 'artificial to confine the analysis to the terms of the scheme itself' when the restructuring in its entirety represented the only 'viable means of enabling the group to continue in business ... permitting the existing members to retain some value in their shares'.

David Richards J held that, despite the substantial dilution of their rights, the shareholders retained an interest in a viable company which was more than they would have achieved had the Company been rendered insolvent.

Attendance at general meeting and error in the special resolution

Whilst the scheme was approved by the requisite majority of shareholders the turn-out of shareholders by number was only 14.8% which meant that around 85% of shareholders did not vote. The court is obliged to ensure that the class of shareholders to be bound by a scheme of arrangement is fairly represented at the relevant meeting. A low turn-out can be a matter for concern however, the court acknowledged that the Company had an unusually high number of shareholders with very small shareholdings and thus the judge held that it was neither a surprise nor a concern that the turn-out by members was relatively small.

The special resolution approving, amongst other things, the restructuring and the Scheme contained an

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2 *Re NFU Development Trust Ltd* [1972] 1 WLR 1548.

error. David Richards J held that although there is no scope for amending a resolution under section 283(6)(a) of the Act where a mistake is clear from the text of the resolution, when read in conjunction with the accompanying circular, it can be read as a matter of construction as if the error had not been made. The correct procedure for ensuring this is the case is to notify the chairman in advance of the meeting, pass the resolution as it is set out in the notice but minute at the meeting that the resolution should be read as relating to the corrected text. The error in this instance was unambiguous and an appropriate procedure had been followed thus there was no issue.

Financial assistance

The court was obliged to consider whether the Scheme constituted unlawful financial assistance under section 678(1) of the Act. Two provisions of the Scheme required consideration. The first was the payment of GBP 66.6 million by UPF to Newco in consideration of the release of UPF's liability to the defined benefit section of the Pension Scheme and the second were the obligations of Uniq to give certain indemnities and pay certain costs.

David Richards J held that the sum paid by UPF to Newco could potentially constitute unlawful financial assistance but only if it reduced UPF's net assets (in accordance with section 677(1)(d) of the Act). However, the judge was satisfied that the purpose of this payment was to secure the release of the liabilities of UPF in respect of the defined benefit section of the Pension Scheme despite the fact that it was known and intended that this amount will be used by Newco to pay up the new shares therefore it fell within the exemption in section 678(2) of the Act.

The court also held that the giving of indemnities or the payment of costs by the Company insofar as they related to or arose out of Newco's acquisition of the shares in the Company would not constitute unlawful financial assistance if they were done in pursuance of an order of the court sanctioning a scheme of arrangement (under section 681(2)(e) of the Act). David Richards J held that the power of the court under section 681(2)(e), to sanction financial assistance as part of the scheme, was not qualified by reference to particular criteria and that a general approach would emerge on a case by case basis. On the basis that in reality these sums could only be paid by Uniq and were commercially necessary for the restructuring, which would substantially improve the position of members and creditors, David Richards J exercised the courts power under section 681(2)(e) to approve the sums.

Conclusion

The High Court's sanction of what is considered an innovative and ground breaking scheme of arrangement is likely to lead to other employers considering similar arrangements in attempts to dispose of their defined benefit pension liabilities. As the first pension deficit for equity swap involving a UK listed company, this judgment provides important guidance as to when the court will be willing to take into account the integral nature of a scheme of arrangement to a wider restructuring. It is worthy of note, that the fundamental basis on which the Company succeeded in gaining approval for the Scheme was that it represented the only viable means for the Company to avoid insolvency and did not prevent the scheme being eligible for admission to the PPF.

International Corporate Rescue

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