October 2011

Report under s89 of the Pensions Act 2004

Issued by The Pensions Regulator in relation to the Polestar Pension Scheme

Background

The **Polestar Pension Scheme** (the 'Scheme') is a defined benefit (DB) occupational pension scheme. It has approximately 8,350 members.

The Scheme has a funding deficit. This can be measured on a number of bases. However, the most recent figures available show an estimated deficit as at 31 March 2010 on a 'buy-out' basis (ie the amount it would cost to buy out members' benefits by purchasing annuities) of approximately £529 million[1]; and the deficit on the Pension Protection Fund's (PPF) s179 measure at that time was £166 million[2].

The Scheme's original sponsoring employers operated in the printing sector and the group was formed by a private equity house utilising a highly leveraged capital structure. In 2006, the **Polestar Group** applied to The Pensions Regulator (the 'regulator') for clearance in respect of an operational and financial restructuring process, as a result of which third party lenders suffered a substantial write-down of their secured debt and all equity value was written off. The alternative to the proposed restructure was insolvency of the **Polestar Group**. In such event, the insolvency dividend for the Scheme would have been insignificant.

As mitigation for the separation of the **Polestar Group** from the Scheme, a contractual agreement was put in place which obliged **Polestar UK Print Limited ('PUPL')** to pay £45 million to the Scheme over 12 years. It was intended that these payments, together with investment returns, would support the Scheme.

Based on the company-specific information available, and in light of the prevailing economic circumstances, those payments appeared to the regulator to give the Scheme and the company a better outcome than insolvency.

The regulator also took into account the anticipated viability of the group post-restructure and the impact of insolvency on employment within the group. The regulator therefore issued a clearance statement, taking the view that, faced with a very challenging situation, agreeing to the restructuring was the best option for the Scheme and other stakeholders.

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1 As noted in the report upon the actuarial valuation of the Scheme as at 31 March 2010
2 As submitted to the regulator via **Exchange**

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As part of this restructure, all UK companies in the Polestar Group ceased to be participating employers in the Scheme. Print Pensions Limited ('PPL') became the sole sponsoring employer in relation to the Scheme. This company is non-operating and does not therefore generate any revenues to support the Scheme. Deficit recovery payments were to be made under a contractual arrangement by PUPL to PPL.

Whilst some of the payments were made, in 2010 it became apparent that (in common with other operators in the UK print sector) PUPL was experiencing financial difficulties and as a result some payments were deferred. The Scheme trustee (the 'Trustee') negotiated security for the Scheme in exchange for this deferral, and kept the regulator updated in respect of their actions to secure a positive outcome for the scheme.

PUPL's financial difficulties continued when they were unable to secure refinancing. In the first quarter of 2011, this reached crisis point and the main unsecured creditors were given a choice: creditors could accept a small part of the money owed to them in full and final settlement of their claims (which would allow PUPL to be sold to new owners and continue trading) or PUPL would enter administration, in which case unsecured creditors would receive nothing at all. The Trustee therefore chose the first option.

The Trustee secured a final payment from PUPL of £3.6million. The contractual claim was extinguished as a condition for this final payment being made.

Following settlement of the creditors' claims against PUPL, PUPL's parent company entered administration on 15 April 2011 and PUPL was purchased by Sun Capital.

Regulatory action

Following the April 2011 administration, the Trustee provided the regulator with information in relation to the future funding prospects of the Scheme. This included a 40-year recovery plan requiring a substantial degree of investment outperformance to be delivered over that period.

Based on this information, in August 2011, the regulator concluded that full funding of the Scheme over any reasonable period was unlikely. In light of this, the regulator also concluded that continuation of the Scheme would not be in the interests of the generality of the members. Furthermore, in the absence of an employer which could make payments to the Scheme, the PPF was exposed to any increase in the s179 liabilities. In turn, this means that levy payers are likely to be exposed to a growing deficit on the s179 basis.

On 9 September 2011, the regulator wrote to the Trustee outlining its belief that under any reasonable scenario the Scheme could never expect to pay the benefits promised to its membership, and so the Trustee should look to crystallise its position.

Outcome

The Trustee, having taken appropriate independent professional advice (including that of counsel), agreed with the regulator's position. The regulator believes that the Trustee has acted in a responsible manner in this regard, protecting the interests of the generality of the membership and limiting the PPF's liabilities. Had the Trustee not decided to wind up the Scheme, the regulator planned to exercise its own power to wind up schemes under Section 11 of the Pensions Act 1995.

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General

The regulator will continue to engage with trustees in cases where the ability to fund a scheme is so weak that there is little or no reasonable chance of paying the benefits promised under the scheme.

In such circumstances, trustees need to recognise the scheme position, take opportunities to capture and optimise value for the scheme, and consider the interests of the generality of members in any decision regarding the options open to them.

In certain circumstances, it may be appropriate for the regulator to consider a Regulated Apportionment Arrangement (RAA) or its anti-avoidance powers as a reasonable and appropriate means of supporting funding of the scheme benefits.

In any case, the regulator would not expect any scheme to take excessive investment risk, unsupported by the employer covenant, and to the detriment of younger scheme members and the PPF.

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