Summary
• With an overseas parent company, trustees may find it difficult to get access to the people who hold the purse strings, while an overseas parent may find the UK pensions landscape complex and overbearing.
• Generally, the greater the resources a foreign company might be able to call upon, the better for the UK pension scheme, but it doesn't mean it'll be willing to write a large cheque.
• US owners will look for the trustees to take a riskier investment approach, but they may not be willing to guarantee the scheme.
• The Pensions Regulator (TPR) has the scope to chase an ailing overseas parent, but legal questions remain over the strength of these powers.

A blessing or a curse?

UK-based pension schemes with a strong overseas parent may consider themselves lucky, and while having it may initially seem beneficial, regulatory and cultural hurdles may often prove off-putting for a foreign parent. Theo Andrew weighs up the pros and cons of an overseas parent company

A blessing or a curse? For many overseas parent companies with a UK pension scheme attached to the UK employer, the landscape can appear overbearing and unnecessarily complex.

On the other hand, some parent companies may need to nurture their UK pension scheme, even if it's economically unviable, in order to fulfil wider corporate strategies that may affect the global business.

The UK's distinct legislative framework, which determines how pension schemes should be managed, can often leave overseas employers confused, while trustees of the pension scheme may face difficulties engaging with their parent company on important issues, such as covenant assessment or increased contributions.

For trustees of the UK pension scheme, the amount at which they can benefit really depends on whether the overseas parent is willing to directly guarantee the pension scheme, thus putting themselves on the hook for any future funding crises.

Risk risk risk!

When an overseas parent looks at the investment strategy of the UK pension scheme, it will often question the prudency of the investment risks they are taking, which is often too risk averse, according to Aon partner, Aiden O'Mahoney.

Part of the reason a foreign parent, particularly those based in the US, will want the UK trustees to take more risk is because the pension scheme of the overseas parent is often perceived as an extension of the wider business, which can capitalise on its diverse financial security.

O'Mahoney says: "It's an accounting advantage for them to have a risky investment because they can say if you invest in bonds you can expect a return of 3 per cent but in equities you can expect 6 per cent, which they can show as income.

"So a lot of overseas parent companies like UK pension schemes to take more risk. The issue then is the regulator will say, 'that's fine and dandy but we want you to guarantee the shortfall if anything goes wrong', and that's where a lot will shy away."

One of the ways to enable the trustees to take more risk is by encouraging the overseas parent to become a direct sponsor of the scheme, something they are not always willing to do.

"Parent companies would sooner sell their children than give guarantees … it's like getting your teeth pulled, it causes issues with other lenders and it's a pain," O'Mahoney adds.

Despite this, Sackers partner, Tom Jackman, says that a guarantee can also have benefits when it comes to safeguarding the pension scheme if it was to collapse into the Pension Protection Fund (PPF).

"The other aspect is that a guarantee, if it satisfies certain requirements, can be certified with the PPF and reduce your PPF levy, which is dead money from a corporate perspective," he explains.

Lincoln Pensions managing director, Matt Harrison, agrees that despite overseas parents' reluctance to guarantee the scheme, it makes sense for them to become the direct sponsor as it "minimises the requirement to put cash in".

Drive to buyout

One obvious way an overseas parent can get their UK pension scheme off their books is by driving for buyout. However, most foreign parents may be reluctant to fork out.

"Most overseas companies don't go for buyout because they don't want to write a big cheque," explains O'Mahoney.

"It will have an impact on their balance sheet and profitability … they would like to get it off the books at no cost but if they have to write a whopping great big cheque then very few of them will want to do that."

Despite this, Redington managing director of integrated actuarial, Marian Elliott, believes that there are "no hard and fast rules" on whether or not overseas parents will aim for buyout, but like most companies, overseas firms will consider their corporate strategy, shareholder expectations, risk posed to the business of the pension scheme, views of the trustees and funding position.

Unlike most UK-based companies however, there are several factors that may push them to buyout, such as the devaluation of sterling, driving a cheaper buyout premium; a corporate restructure or sale of the business; and whether or not the overseas parent is a direct sponsor of the scheme.

Harrison agrees, adding that "generally speaking" foreign firms are not "rushing to chuck loads of money into a scheme to get it bought out", except for when it is a modest amount of money.

"There are scenarios where foreign parents look to get the scheme off the books, I'm working with one at the moment where we are in an active discussion and that could be driven by a desire to maybe dispose of the UK business and they just want to tidy it up," he says.

"The foreign parents have generally got the resources if they want to, but there will be commercial drivers as to why they want to."

However, if a buyout is not a feasible option for the overseas parent, they may want the trustees of the UK pension scheme to be less ambivalent with their investment risk. With

overseas parents sometimes reluctant to become a guarantor of the pension scheme, and even more reluctant to write a large cheque in order to buyout, trustees face several complex challenges in dealing with the overseas parent.

Trustee considerations

These challenges can often emerge when a foreign parent is forced to understand the UK pensions landscape.

The complexity is unlike many other countries, as the UK operates a distinct regulatory legislative framework, placing strong obligations on trustees that overseas parent companies may not fully comprehend.

According to Elliott, trustees will have to work hard to engage overseas parents, which can "go a long way to mitigating the issues", but it is not that simple.

Harrison argues: "When you have a small UK scheme as part of a larger group, you often don't have access to people who make the decisions over capital allocation and pension scheme funding. You are talking to UK management who then have to get sign-off from any funding and commitments from anywhere else, one or two steps up the chain."

One element that trustees could find tricky is when assessing the covenant of the overseas parents, as if there are inter-company loans in place, it may be difficult to assess how the covenant will change in a range of circumstances.

To help mitigate these problems, Elliott says: "Understanding the strategy of the overseas parent as far as possible and communicating pension issues in a way that explicitly speaks to their objectives and constraints goes a long way towards fostering good engagement."

According to the regulator, the overseas parent may not understand the importance of assessing covenant in relation to valuations and should corporate transactions occur, meaning it is important for overseas companies to have UK-based advisers to support them, but this can draw its own problems.

"We would expect trustees, supported by independent covenant advisers where appropriate, to approach assessing the strength of covenant of the guarantor in the same way as with a UK-based company," TPR says.

"This would include reviewing recent financial performance, looking at the current financial position, and analysing forecasts. In addition to looking at the company itself, trustees might also consider the outlook for the markets the company operates in and the position of the company relative to its competitors."

A world apart

When it comes to offering guarantee for the scheme, the legislative landscapes can often blur the lines for an overseas parent.

Jackman explains: "Sometimes a UK sponsor has no money – but has a very strong parent company that has paid contributions for the past 30 years, or where the parent company has put in the necessary funds as needed, then you have the difficult conversation where the overseas parent will say, 'of course we are in good financial shape, here is our group accounts, we are doing really well and we've given you all the money you've ever needed' … the regulator does slightly want to have its cake and eat it."

Or perhaps it's the cultural differences in dealing with a Japanese parent, where even asking for guarantee for the pension scheme by their very nature implies that you think they are dishonest.

It is vital for an overseas employer to get their head around the complex UK pensions landscape, as the regulator has said on numerous occasions, it is not afraid to use its moral hazard powers in overseas jurisdictions.

Earlier in July, TPR wrote to the Work and Pensions Committee chair, Frank Field, to stress that should the recent commitment made by Lady Green and Philip Green to the Arcadia pension scheme fall through, then it would have the powers to pursue the firm's overseas assets.

Other high-profile cases include the Canadian telecommunications firm Nortel, in which the regulator secured roughly £1 billion of payments for the pension scheme and benefits above the PPF level for the scheme's 31,000 members in 2017.

Despite this, Harrison believes that the cases are to a certain extent "less tested", and in fact the regulator may find a challenge using its moral hazard powers in overseas jurisdictions.

As a result of this, he argues: "The regulator is less favourable for a guarantee now than it used to be, as it has realised that you can't fund a scheme with a guarantee, you actually need cash."

The regulator is clear on what it expects, and overseas parents are coming to terms with the complexity of the UK pensions landscape. Of course, trustees could benefit from diversified global revenues, but the route is less than smooth.

Written by Theo Andrew