



Lehman, Nortel, and a More Certain Future for Bankrupt Company Pensions

The UK's Supreme Court has ruled that the UK's Pensions Regulator does not have priority over other creditors when a company becomes insolvent.

(July 24, 2013) -- Chasing pension money from parent companies who have gone bust has been materially weakened, after the Supreme Court ruled that the UK Pensions Regulator's financial support directions (FSDs) and contribution notices no longer have priority in a line of creditors. Overturning a previous Court of Appeal judgment from 2011, Lord Neuberger, Lord Mance, Lord Clarke, Lord Sumption, and Lord Toulson concluded that the Pensions Regulator does not rank ahead of any creditors, including unsecured creditors, banks, and bondholders, and should instead be considered *pari passu*: that is, equal.

The ruling, which happened this morning, in the matter of the [Nortel Companies](#), in the matter of the Lehman Companies, and in the matter of the Lehman Companies (No. 2), has widely been heralded as a success for common sense. If the court had decided to uphold the Court of Appeal's findings, any large pension deficit would likely have swallowed up all assets recovered after an insolvency, leaving all other creditors with nothing.

Another unintended consequence of the original judgment was that businesses with final salary pension schemes may have found it more difficult to borrow money, as the decision of the lower courts saw liabilities ranking as an expense, increasing the costs of lending. This should also have been dealt with by the court's decision today.

"The concern before today's decision was that the Pensions Regulator had the power to boost the ranking of its claim simply by waiting for a target company to enter administration. The Supreme Court unanimously agreed that Parliament cannot have intended such an unfair and arbitrary result," said Tony Bugg, global head of restructuring and insolvency at Linklaters, who also advised the Lehman Brothers' administrators.

"An insolvency pits employees, pensioners, suppliers and other creditors against one another each fighting for a share of a limited pool of funds. The Supreme Court rightly decided that only the clearest of legislative intent should enable one group of creditors to claim priority over another.

"In the context of an insolvency regime which already gives some creditors preferential treatment, it is right that these decisions should be for Parliament to decide."

A Pyrrhic Victory for the Regulator?

Jennie Kreser, partner at law firm Silverman Sherliker, told *aiCIO* the judgment meant the likelihood of recovery for pension schemes has been "somewhat reduced".

"The Supreme Court said that in coming to its decision, it has overturned a line of cases (which the court below couldn't do) as they were contradictory and not consistent with corporate insolvency situations, having been based on individuals who were insolvent.

"This will be a disappointment to the Pension Regulator and to the members of pension schemes who will, as a result, find their position weakened when trying to bolster schemes with significant deficits, who would otherwise look to other group companies for help."

But the Regulator's statement suggested it welcomed the clarity the Supreme Court had provided, and cheered the fact it had successfully argued against a suggestion that an FSD issued against an insolvent company would be ineffective and "disappear down a black hole".

The Regulator had originally pushed for FSD liabilities to be considered an administration expense or as a provable debt. Even though the administrative expense argument was ruled out by the Supreme Court, the regulator was happy to have the provable debt argument sustained.

Stephen Soper, the Pensions Regulator's executive director for defined benefit funding, said: "This will be welcome news for many thousands of pension scheme members and will provide clarity to insolvency practitioners on how to treat a pension scheme liability.

"Since the challenge was first made, we have made clear that we have no intention of frustrating the proper workings of the administration process. Today's judgment will provide clarity to the UK's restructuring and rescue practitioners that FSD liabilities have to be recognised in insolvent situations but do not have priority over administration expenses or secured debts."

Another potential downside was highlighted by law firm Allen and Overy: the surrounding legislation needed fixing in a number of areas, including in relation to overseas enforcement of FSDs.

"Because this decision now makes it work for FSDs in UK insolvencies, I can't see a root and branch reform of the FSD aspect being likely now,"

Jason Shaw, senior associate at the firm, said.

The Pension Protection Fund's head of restructuring and insolvency, Malcolm Weir, said the PPF had always argued FSDs and contribution notices should be treated as provable debts, and that the organisation would now look at the judgment to assess the implications for the Nortel and Lehman schemes, and any future recoveries it may make as an unsecured creditor.

The full judgment can be read [here](#).

What does this mean for Lehman and Nortel Network's pension schemes?

In a nutshell, don't expect a swift happy ending.

Both schemes are currently in the [Pension Protection Fund](#) assessment period, with Nortel entering in March 2009, and Lehman Brothers' entering in two separate tranches in October 2008 and August 2009.

The Pensions Regulator has issued FSDs to target companies associated with both pension funds-Lehman Brothers' targets were issued with an FSD in September 2010 and Nortel's targets received their FSD on June 25, 2010.

Both sets of targets referred the matter to the Upper Tribunal court, contesting the grounds for the FSD issuance, and both cases were then stayed, awaiting the outcome of the Supreme Court hearing. Following today's judgment, those Upper Tribunal cases can now resume, resulting in one of two options: either the Upper Tribunal sides with the Regulator and grants permission to hand down the FSD, or it sides with the targets.

Both results could also find themselves subject to appeal, if a point of law can be found, meaning the cases could escalate to the [Court of Appeal](#). There's also parallel cases being heard in the US and in Canada to determine the claims of the Nortel trustees, which were submitted off the back of the FSD issuance. Those are listed to take place in January, 2014.

All of which means it's unlikely the members of both schemes will have closure on the ongoing legal rows for many months to come, if not years.

Related Content: [UK's Court of Appeal Upholds Landmark Pensions Ruling Backing The Pensions Regulator](#) and [Is this the Toughest Job in Pensions?](#)

Contact the writer of this story:

Charlie Thomas

Assistant European Editor, aiCIO

(44) 207 397 3827

cthomas@assetinternational.com

Follow on Twitter at [@ai_CIO](#)

Copyright 1989-2012 Asset International, Inc. All Rights Reserved. No Reproduction without

Prior Authorization