

CLIENT UPDATE

PBGC'S WEAPON OF LAST RESORT BRINGS VICTORY IN ST. GOBAIN

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As we reported in a Client Alert last summer,¹ the Pension Benefit Guaranty Corporation (the "PBGC") initiated proceedings to terminate the pension plan of St. Gobain Containers, Inc. ("St. Gobain") in connection with the sale of St. Gobain's U.S. metal and glass containers business to Ardagh Group. Initiation of a plan termination is an extraordinary action by the PBGC, which the PBGC has to date undertaken only when the acquisition of a company with an underfunded pension plan has presented the risk of a significant increase in the contingent liability faced by the PBGC as the U.S. federal guarantor of corporate pension plans.

The PBGC's extraordinary action succeeded in protecting the interests of the plan. Its action to terminate the St. Gobain plan in the face of the proposed \$1.7 billion sale to Ardagh, an Irish company with a below investment grade credit rating, has resulted in St. Gobain agreeing to make a \$207 million contribution to its significantly underfunded plan.

St. Gobain had apparently refused to engage in a dialogue with the PBGC when the agency expressed its concerns regarding the "at risk" plan and the proposed sale to Ardagh Group. In light of the risk posed and the absence of any constructive dialogue, the PBGC used its statutory authority to try to force a plan termination that would

¹ "Upping the Ante: PBGC Initiates Pension Plan Termination in Leveraged Acquisition", <http://www.debevoise.com/clientupdate20130603b>

have resulted in a lien on a St. Gobain's assets. The Federal Trade Commission had separately acted to block the sale on antitrust grounds, but Ardagh Group had recently settled that action by agreeing to certain divestitures. Below we discuss lessons to be learned from PBGC's actions.

More Aggressive Action to Come? So the obvious question is: will this successful attack lead to more aggressive action by the PBGC in other transactions? Not necessarily. St. Gobain presented a no-lose scenario for the PBGC. The plan was significantly underfunded, the buyer was perceived as a vastly inferior creditor and the current sponsor had significant net worth. The PBGC likely assumed they would have to take over the plan if the transaction proceeded and opted to act rather than lose access to the assets of a solvent sponsor. The \$207 million settlement suggests the PBGC rightly concluded that a forced termination, and corresponding lien against St. Gobain's assets, was its best – and perhaps only – option.

Lessons to Be Learned. However, there are still lessons to be learned from the St. Gobain situation. The PBGC monitors transactions involving sponsors with underfunded plans. In any financial transaction where an underfunded plan is present, the PBGC is an economic constituent that shouldn't be ignored. Its real leverage – forcing a plan termination – has economic consequences for the agency, as it must assume responsibility for at least a lion's share of the plan's underfunding. Thus, the PBGC can be expected to use this leverage judiciously. But we have seen that the PBGC will use this weapon of last resort if backed into a corner and left with no viable alternatives.

A plan sponsor engaging in a transaction (including a spin-off or restructuring) at a time at which it has significant unfunded pension liabilities should anticipate that the PBGC will reach out and express concerns about the consequences of the transaction for the plan. Once the PBGC has reached out, a prudent sponsor should engage in a constructive dialogue with the PBGC. To the extent possible, the sponsor should provide the PBGC with financial data demonstrating that the transaction will not significantly disadvantage the plan and the agency. If the financial data shows the transaction does create such a detriment for the plan and the PBGC, the sponsor should be prepared for the dialogue to move onto possible funding alternatives, such as incremental contributions or additional security for the plan.

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Please do not hesitate to contact us with any questions.

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