SQUIRE PATTON BOGGS

Pensions Quick Guide

Restructuring Plans

What Is a Restructuring Plan and Why Does It Matter?

The concept of a restructuring plan was introduced by the Corporate Insolvency and Governance Act 2020 (CIGA). Similar to a scheme of arrangement, it is a court-supervised process that allows a company to enter into a compromise with its creditors if at least 75% in value of creditors in each class vote in favour of it. A restructuring plan can bind both secured and unsecured creditors. Subject to various conditions being satisfied and the exercise by the court of its discretion, this is the case even where some classes do not vote in favour of the restructuring plan. If sanctioned, the restructuring plan is implemented and will bind each class of creditor affected by it.

The government's policy objectives for introducing restructuring plans made clear that restructuring plans were designed to facilitate restructuring proposals that might have previously been blocked by creditors. In its 2022 review, the government noted the following policy objectives in relation to restructuring plans:

- To address the scenario where a secured creditor can block a company rescue, despite the proposals being well supported
- To enable courts to sanction restructuring plans where it is fair and equitable to do so
- To enable companies with viable businesses that are struggling to meet debt obligations to restructure with limited disruption to their operations
- To provide an alternative measure to a scheme of arrangement in cases where the agreement of all classes of creditors is unlikely (as schemes of arrangement do not provide any mechanism for "cram down" between classes)

To the extent that obligations owed to trustees (on behalf of schemes) are not compromised by a restructuring plan, trustees may well welcome the sanctioning of a successful restructuring plan as a platform that an employer can use to restructure its liabilities and move forward with a stronger and more stable covenant. However, as this quick guide will detail, the process is not without risk for trustees and the schemes that they look after.

A guide produced by the Restructuring & Insolvency team provides more information on restructuring plans generally.

The Companies Act 2006 imposes obligations to notify the Pension Protection Fund (PPF) of restructuring plan proposals where the company is an employer of an eligible defined benefit (DB) scheme, and regulations provide for the PPF to exercise the rights of the pension scheme trustees in respect of voting on the proposals.

Why Should Pension Trustees Be Concerned?

The key difference between a restructuring plan and a scheme of arrangement or company voluntary arrangement is that the rules around restructuring plans include "cross-class cram down" provisions, which mean that the court can approve a restructuring plan if only one class of creditors with a real economic interest in the company votes in favour of it, and (broadly speaking) the court is satisfied that the other classes would not be prejudiced compared with the likely "relevant alternatives", e.g. administration. In these circumstances, the court can exercise its discretion to sanction the restructuring plan despite the opposition of any dissenting classes affected by the restructuring plan, and such dissenting creditors are effectively crammed down. Interestingly, a restructuring plan might also allow junior creditors (such as trustees with unsecured pension debt) to "cram up", forcing a plan on more senior creditors (such as the company's bankers who hold security), provided that they are no worse off than in the relevant alternative.

Could a Restructuring Plan Impact Pension Scheme Funding?

While any type of insolvency process of a sponsoring employer could have adverse consequences for pension schemes, the cross-class cram-down provisions bring new risks for pension trustees. Even if creditors within the same class as the pension trustees are in agreement that they should reject a proposed restructuring plan, the whole class could see itself crammed down and overruled by a different class of creditors with opposing interests.

There is nothing in the legislation that excludes pension debt from a restructuring plan. In theory, therefore, pension debt could be reduced or, perhaps more likely, payments of the debt rescheduled, under a restructuring plan, unless the court considers this to be unfair in the circumstances. This theoretical risk has yet to be tested in practice.

Will Pension Trustees Have a Seat at the Table?

Pension trustees will have to demonstrate that they have an economic interest in the company. If the court is satisfied that the pension trustees have no economic interest or that the restructuring plan does not seek to compromise the rights of the trustees on behalf of the schemes, the pension trustees (or, more accurately, the PPF, which would exercise the vote on the trustees' behalf) would not have a vote on any restructuring plan proposal.

Key from a pension scheme perspective, therefore, will be valuation of the debt attributable to the pension scheme. There is nothing in legislation that specifies how pensions debt should be valued for these purposes. The PPF has published guidance on its approach to CIGA, in which it says that it considers that the trustees' vote on a restructuring plan (which is exercised by the PPF) should have the value of the estimated debt that would be due from the employer if Section 75 of the Pensions Act 1995 applied. If the value of any deficit calculated on the full buyout basis is taken into account, not only would this give the pension trustees (and/or PPF) a seat at the table, but it might also give them the controlling interest in a class of creditors, and even the ability to force a cram down.

However, despite this guidance, there is the possibility that Section 75 liabilities would not be taken into account by a court. This is because a restructuring plan does not automatically trigger a Section 75 debt, so there is no certainty that Section 75 liabilities would qualify as relevant debt. It is also worth noting that a restructuring plan is not a qualifying insolvency event for PPF entry purposes.

But Wait – What About The Pensions Regulator (TPR) and the PPF?

Ordinarily, if an event occurs that would reduce the amount that trustees could recover by way of a Section 75 debt, the parties involved would find themselves on the receiving end of TPR's powers. TPR has a full armoury available to it, including power to require a connected or associated party to make a financial contribution to a DB pension scheme or to require a connected company to put in place financial support for a DB pension scheme.

Additionally, the Pension Schemes Act 2021 introduced two new offences of "avoidance of an employer debt" and "conduct risking accrued scheme benefits". These two offences carry the risk of a criminal penalty of an unlimited fine and/or imprisonment of up to seven years. Alternatively, TPR could issue a civil penalty of up to £1 million in relation to these offences. The interesting element to these two offences is that anybody could fall foul of them – they are not limited to persons connected or associated with a pension scheme employer. Could TPR fine or imprison a judge for sanctioning a restructuring plan? It seems highly unlikely, but the interaction between TPR's powers and the power of the court to sanction a restructuring plan is yet untested.

Where a restructuring plan is proposed, and the company is or has been an employer of a DB pension scheme, Section 901I of the Companies Act 2006 requires notice to be given to TPR and the PPF in the same way that it would be given to the pension trustees. TPR and the PPF are clear that they expect to receive the same restructuring documents in parallel with the pension trustees. As noted above, regulations go further, and provide that any voting rights in relation to a restructuring plan are exercisable by the PPF instead of by the pension scheme trustees.

The PPF's guidance says that it will consider various factors when deciding its approach to voting on any restructuring proposal, including:

- Whether the proposal complies with the published PPF restructuring guidance
- Whether the proposals are being used as a tool to adjust pension scheme liabilities or payments of deficit repair contributions under a recovery plan
- Whether there is anything in the restructuring plan that would disadvantage pension scheme members, such as potentially compromising the pension scheme's eligibility for PPF protection
- Whether there is anything contained in the plan that would adversely affect or bind future negotiations
- Whether the restructuring plan ensures that the scheme is no worse off in the future than today, e.g. by guaranteeing the current insolvency outcome, the extent to which PPF "drift" is fully covered by the proposed restructuring plan
- Whether the restructuring plan presents an adverse precedent risk to the PPF

While it is useful to know what factors the PPF would consider when reviewing proposals for a restructuring plan, PPF approval is not required before the court sanctions a restructuring plan.

What Can Trustees Do To Improve the Scheme's Position?

Trustees should have a full understanding of the strength of the employer covenant and take robust covenant advice from specialist advisers as to the likely impact of a restructuring plan on the scheme. Trustees will also need to have a good understanding of:

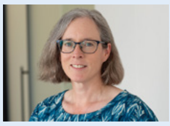
- Their scheme's balance of powers. If the power to wind up the scheme currently rests with the employer, trustees may wish to seek greater power over windup triggers as part of scheme funding negotiations. If, for example, trustees have the power to trigger scheme windup when the company puts forward proposals for a restructuring plan, the full Section 75 debt might come into play.
- Whether the trustees are being asked to compromise something and, if so, is there something the company can give in return? Security, escrow, similar?
- What are other creditors giving up/receiving? How does this compare with how the trustees are being treated?
- Dividend blocks and the potential to use blocks on repayment of intercompany debt as a condition.
- Whether a proper and robust process has been followed for the restructuring by the employer. What level of disclosure and transparency has been offered?
- How what is being proposed compares with the most likely/relevant alternative.

Finally, trustees should open dialogue with TPR and, if necessary, the PPF to discuss what is being proposed.

Some Practical Points

Do	Don't
Do ensure that there is an information sharing protocol in place between the company and pension trustees. This is something that should be put in place now, if one does not already exist. It will act as an early warning system for pension trustees if the company is considering a restructuring plan or any other insolvency process in the future.	**Don't** be left without a quorum! If some of the trustee board are also senior management, they will not be able to participate in trustee discussions about the restructuring plan. Urgent consideration might need to be given to number and level of expertise of the remaining trustees. Consider whether it might be appropriate to onboard an independent trustee for a limited time.
Do review the pension scheme rules – these may affect whether or not you can put the Section 75 liabilities into the mix.	**Don't** assume that the company will automatically make a notifiable event submission to TPR when considering proposals for a restructuring plan. If the company fails to make a notifiable event submission, for whatever reason, and one is required, the trustees should make the submission.
Do take professional advice. This will be crucial to formulate evidence to demonstrate that the trustees have an economic interest in the company and to put the trustees in the best possible position.	**Don't** leave everything to the PPF to handle. The trustees have a trust law duty to act for the purposes of the scheme and in the best interests of members. The PPF is required to consult with the trustees before voting on any proposals, so you need to form your own view on any proposed restructuring plan.

Contacts



Wendy Hunter
Partner, London
T +44 20 7655 1119
E wendy.hunter@squirepb.com

Charlotte Møller
Partner, London
T +44 20 7655 1664
E charlotte.moller@squirepb.com