Lawyers give their views on pensions and restructuring trends

PwC's Pensions and Restructuring Lawyers Event 2023

September 2023

pwc

Introduction

The results of our lawyer survey show a significant shift in views from 2 years ago, reflecting the changes in the economic climate and pensions market.

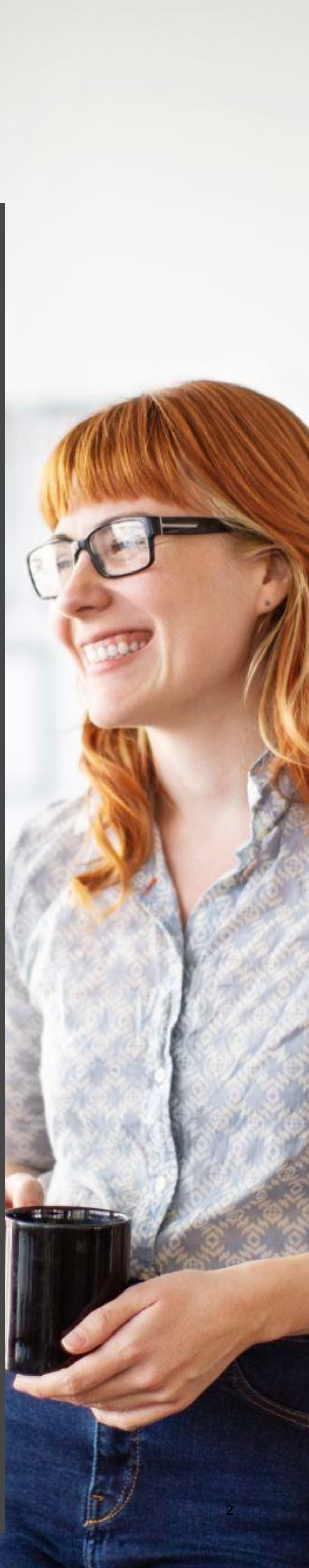
This was the seventh time over the last 15 years we have brought together over 300 pensions and restructuring lawyers from across the UK and surveyed them on key issues in the sector.

Our survey ranged from views on macroeconomic risks, anticipated levels of distress, Liability-Driven Investment, TPR powers and more.

Thank you to all the lawyers who participated and joined us for our event. We look forward to working with you and your law firms over the coming months in this evolving market.

Our full results are in the following pages, with some highlights below:

- **More than 9 out of 10 lawyers anticipate an increase in UK insolvencies over the next 12 months.**
- **A third of lawyers say you can ‘cross-class cram down’ a s.75 debt in a Part 26A Restructuring Plan. A third say you can’t. A third say they’re unsure.**
- **Distress, refinancing and interest rates are seen as the biggest risks facing clients.**
- **Inflation, interest rates, and lasting impacts of Brexit are the top 3 risks facing the UK economy.**
- **65% of lawyers believe their clients have the same or higher level of DB scheme risk compared with 2021.**
- **2 years on from implementation of the Pension Schemes Act 2021 and 38% of lawyers believe the Act is damaging the UK rescue and investment cultures.**
- **Only 11% of lawyers recommend using TPR Clearance to mitigate regulatory risks, placing more onus on legal and covenant advice.**
- **60% of lawyers believe an element of DB needs to be the future of pensions to address pensions poverty.**



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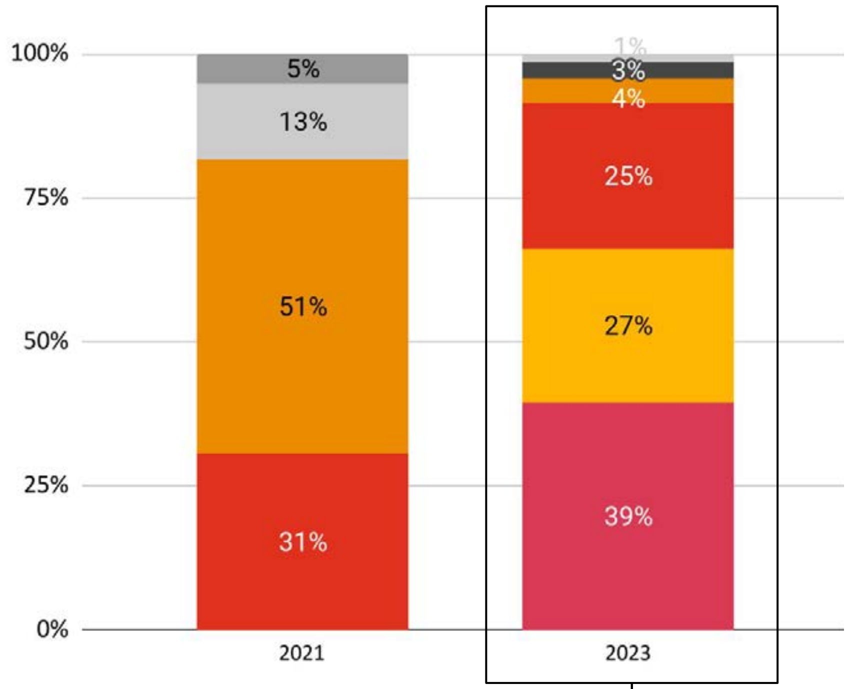
Lawyers’ views on the outlook for the UK economy

Inflation, interest rates, and lasting impacts of Brexit are the top 3 risks facing the UK economy, say lawyers

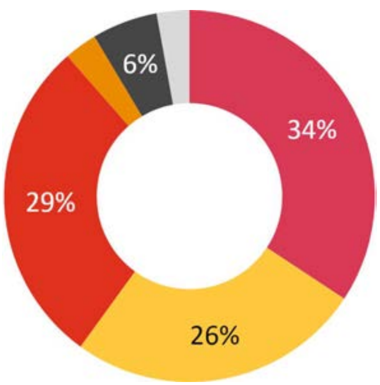
66% of lawyers believe the biggest risks to the UK economy are high interest rates and high inflation

- 2 years ago, 51% of lawyers were most concerned with lasting impacts of Covid. This has now decreased to just 4%, demonstrating the view that Covid is falling off the risk radar for companies and pension schemes.
- High inflation is the top risk for both pensions and restructuring lawyers.
- Interestingly, 7 years after the referendum, 1 in 4 lawyers still see Brexit as the biggest threat to the UK economy with it being the 3rd highest answer in the survey.

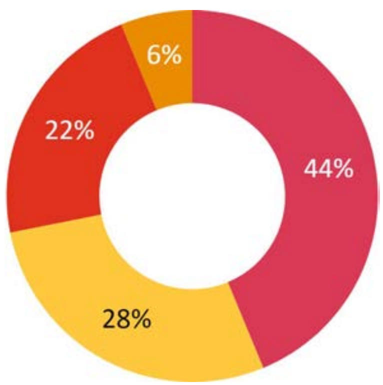
What is the biggest threat to the UK economy?



2023 Pension lawyers



2023 Restructuring lawyers



- US-China Trade War
- Climate Change
- Russia-Ukraine War
- Lasting Covid Impact
- Lasting Brexit Impact
- High Interest Rates
- High Inflation

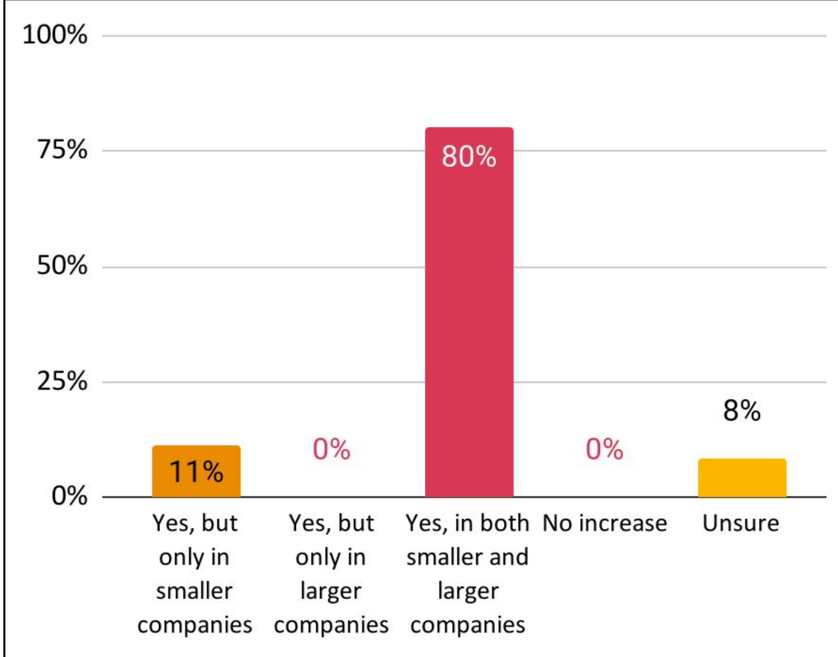
Lord Gavin Barwell and the Rt. Hon Alan Milburn debated why inflation is high during the event, they discussed how a number of factors, including Brexit, are driving high inflation in the UK. Click here for a recording.

More than 9 out of 10 lawyers anticipate an increase in UK insolvencies over the next 12 months

Lawyers believe that there will be an increase in insolvencies in the UK, impacting both smaller and larger companies

- 2023 has seen a significant uptick in the number of corporate failures. Whilst the UK may have avoided a technical recession so far, the continued inflationary pressures have driven challenging market conditions, while higher interest rates and the resultant increased cost of debt is likely to mean an increasing number of companies struggling to refinance - a potential problem amplified by the 2024 and 2025 maturity wall.
- We expect the volume of corporate insolvencies will continue to rise in the short term, especially as lenders reassess risk appetites. Winding up petitions are a key red flag of creditor sentiment and are on the rise.
- Whilst 97% of business failures in H1 2023 had an annualised revenue under £1m, larger businesses were not immune. 157 businesses entering insolvency in H1 2023 had revenue of over £10m.

Do you think there will be an increase in the number of insolvencies in the UK over the next 12 months?



2023 Pension lawyers

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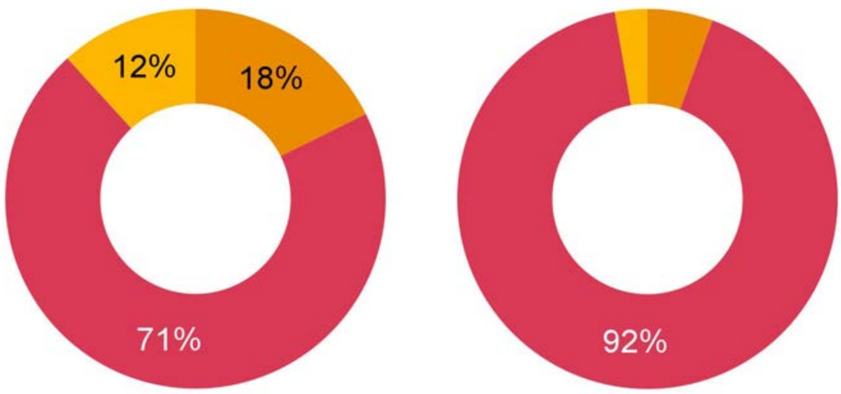


- Yes, but only in smaller companies
- Yes, in both smaller and larger companies
- Unsure

Catherine Atkinson and Ed Macnamara provided an overview of key sectors at risk – click here for a recording.

2

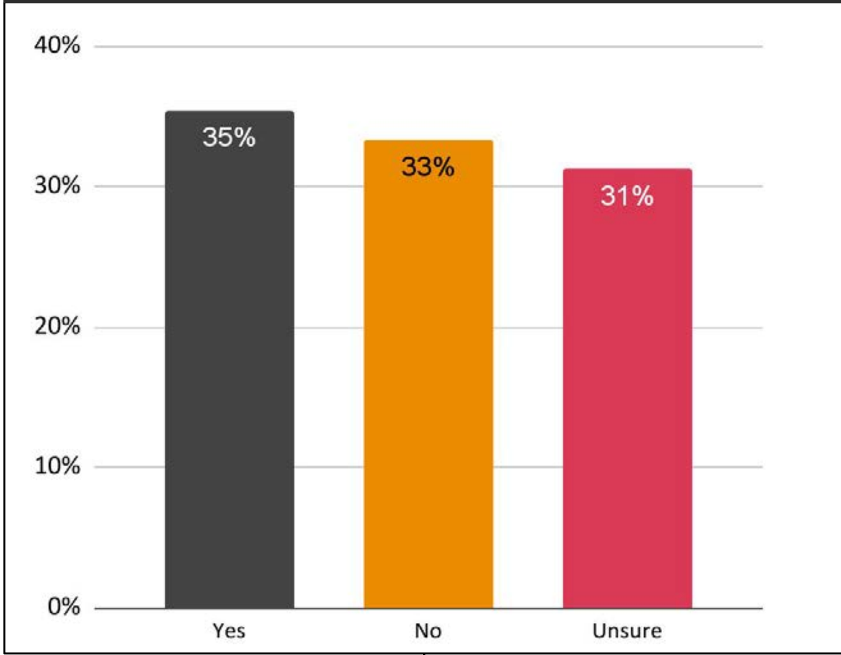
Part 26A Restructuring Plans – can you ‘cross-class cram down’ a pension scheme?

Lawyers have mixed views on the ability to ‘cross-class cram down’ a s.75 debt in a Part 26A Restructuring Plan

There is no consensus on whether a s.75 debt is at risk of being ‘cross-class crammed down’ in a Restructuring Plan

- After the introduction of Part 26A Restructuring Plans in 2021 as part of the Corporate Insolvency & Governance Act, the question of how the ‘cross-class cram down’ feature interacts with a DB pension scheme has been hotly debated.
- A key question in particular is whether a DB pension scheme’s s.75 debt can be compromised without trustee consent under the ‘cross-class cram down’ feature. This has yet to be fully tested in cases to date.
- Our survey shows lawyers have split views although, interestingly, the majority of restructuring lawyers (57%) believe it is possible.
- With such mixed views, there remains uncertainty and risks for DB pension schemes, the PPF and corporates in Part 26A Restructuring Plans.

Do you think it will be possible to ‘cross-class cram down’ a DB pension scheme’s s.75 debt in a Restructuring Plan?



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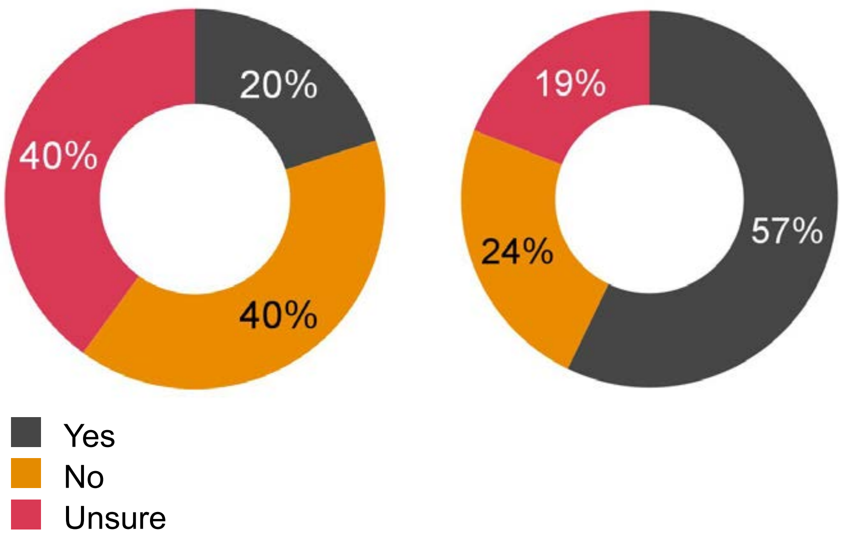


Atul del Tasso-Dhupelia was joined by Malcolm Weir of the PPF and Raquel Agnello KC who debated this topic in our session which you can listen to here.

3

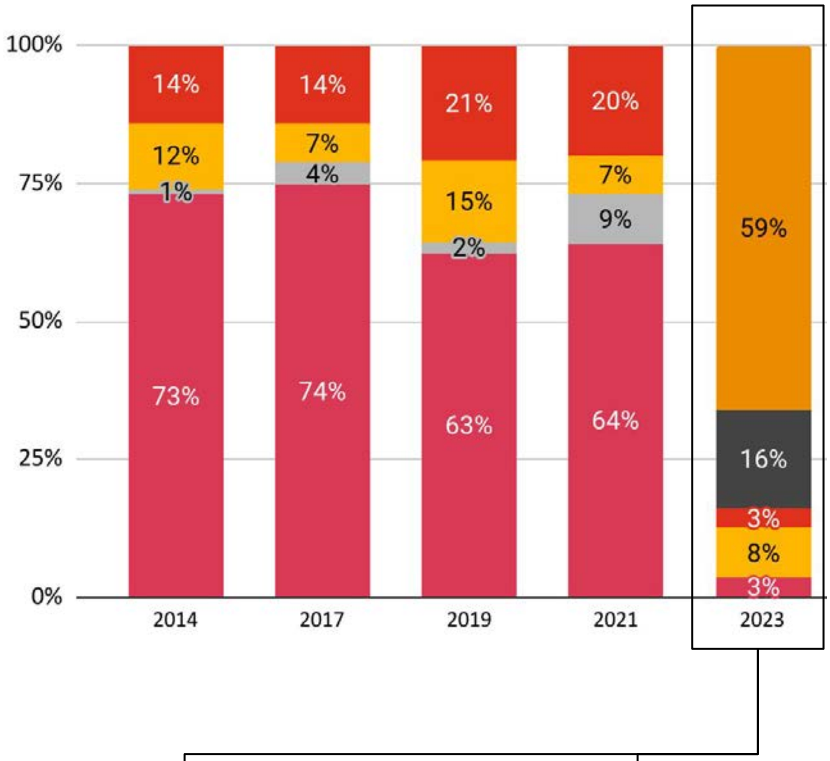
Lawyers believe clients are facing new risks that haven’t been a concern in the last 9 years

Distress, refinancing and interest rates are seen as the biggest risks facing your clients

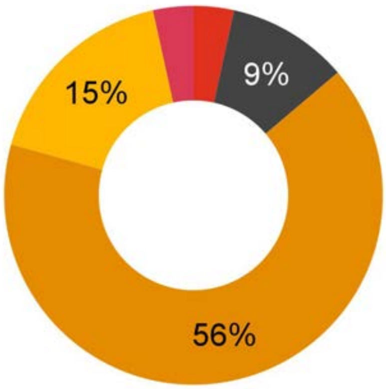
3 out of 4 lawyers say distress, refinancing and interest rates are the biggest risks to their clients

- Over the past 9 years, affordability of deficit repair contributions has been seen as the biggest risk facing your clients. This is likely linked to the low interest rate / high pension deficit environment over these years that drove up cash demands on corporates.
- In this year's survey, only 3% of lawyers voted affordability as the biggest threat, with 75% stating that refinancing risks and distress are the biggest risks.
- This is a significant shift in the key risks lawyers feel are currently facing their clients compared with over the past 9 years.
- With many pension schemes seeming better funded on an actuarial basis, many schemes are taking comfort from this potentially reduced scheme funding risk. However, at the same time many corporate sponsors are faced with significant risks, and these risks are ones that they haven't had to deal with for a number of years.

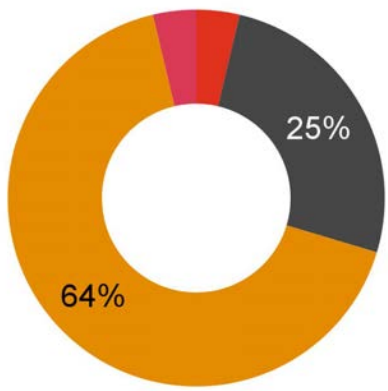
Which of the following do you see as the biggest risk currently facing your clients?



2023 Pension lawyers



2023 Restructuring lawyers



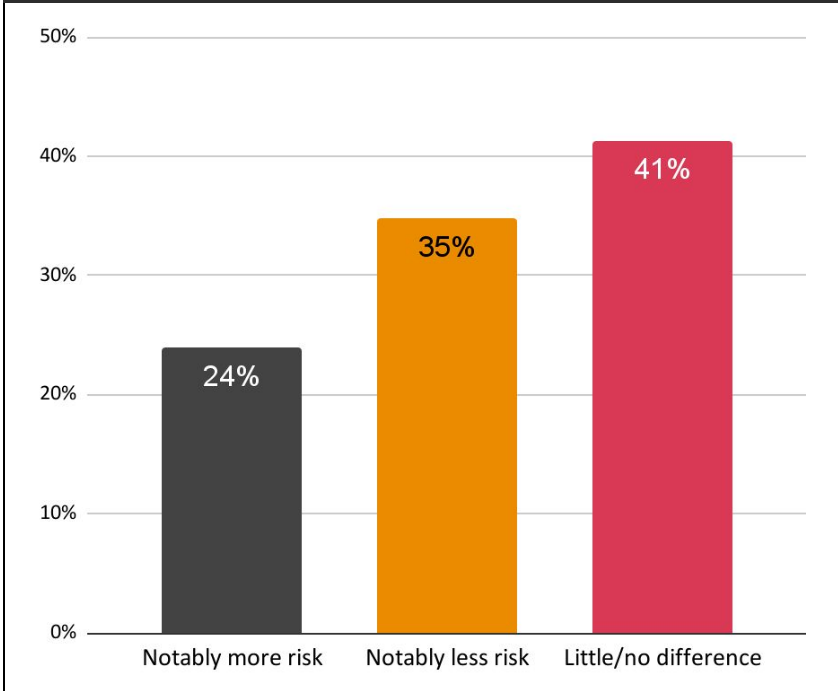
Refinancing/Interest rates
Distress
Regulator interference
Benefit Provision
Affordability and cashflow
Transaction/Corporate Activity

65% of lawyers believe their clients have the same or higher level of DB scheme risk compared with 2021

41% of lawyers believe DB scheme risk levels are the same as in 2021, with 24% of lawyers assessing DB scheme risk levels to be higher currently

- Some observers in the pensions market have been commenting recently that the majority of DB pension schemes are “out of the woods”. Our survey results show this isn’t believed to be the case by lawyers.
- It is true that some schemes are currently facing less risk than two years ago with 35% of our audience believing this to be the case for their clients.
- However, the majority of lawyers believe that DB risk levels have not improved for their schemes. This reflects the fact that many schemes remain exposed to significant covenant, funding and investment risks, with corporates of these schemes continuing to underwrite these risks.

How would you compare the overall risk for your DB schemes in 2023 compared to 2021?



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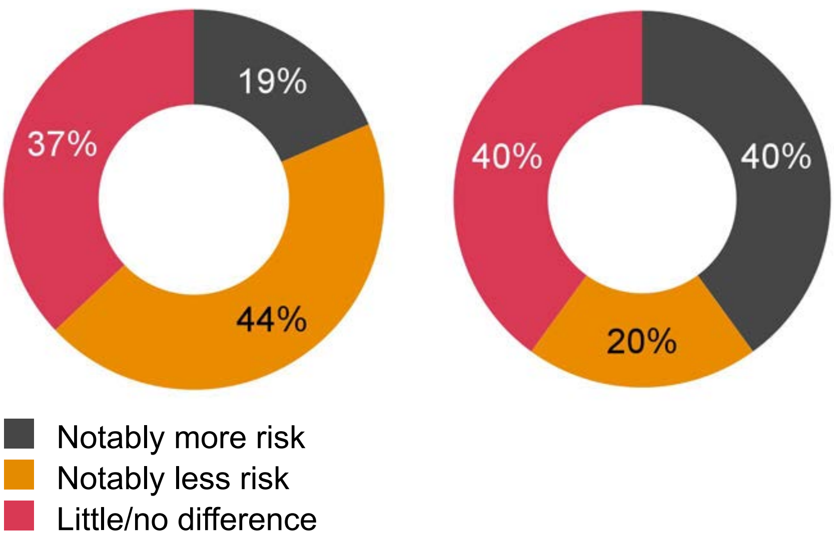
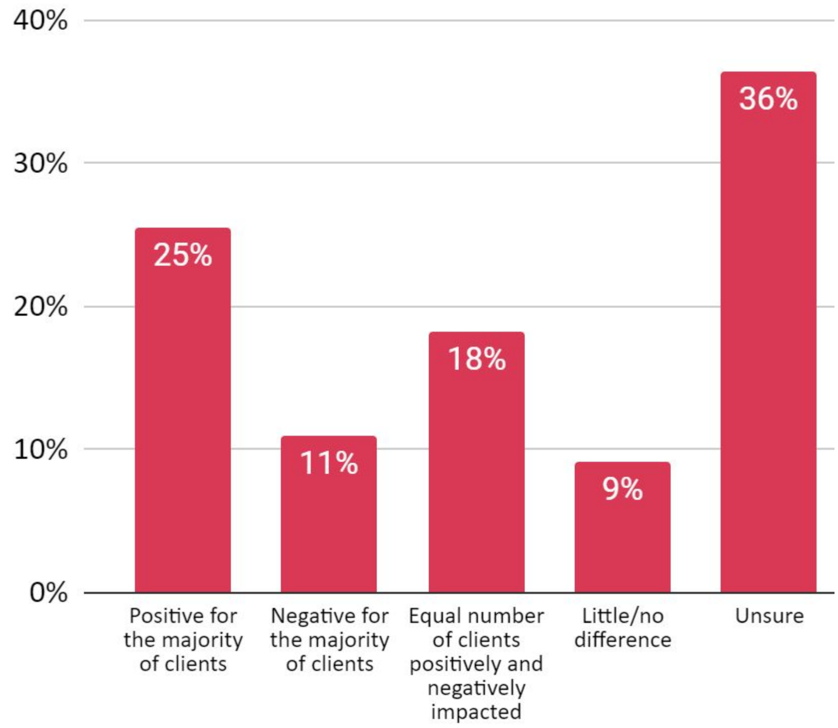


Lawyers believe their clients have been impacted differently by an LDI investment strategy, with many unsure of lasting impact

Lawyers believe the impact of LDI investment strategies on their clients has varied between individual schemes

- 25% of lawyers say an LDI investment strategy has been positive for the majority of their clients.
- 11% of lawyers say an LDI investment strategy has been negative for the majority of their clients.
- 36% of lawyers are unsure on the overall impact of an LDI investment strategy on their clients.
- This shows there does not seem to be consensus on the impact of LDI investment strategies.

Has an LDI investment strategy had a material impact on your clients?



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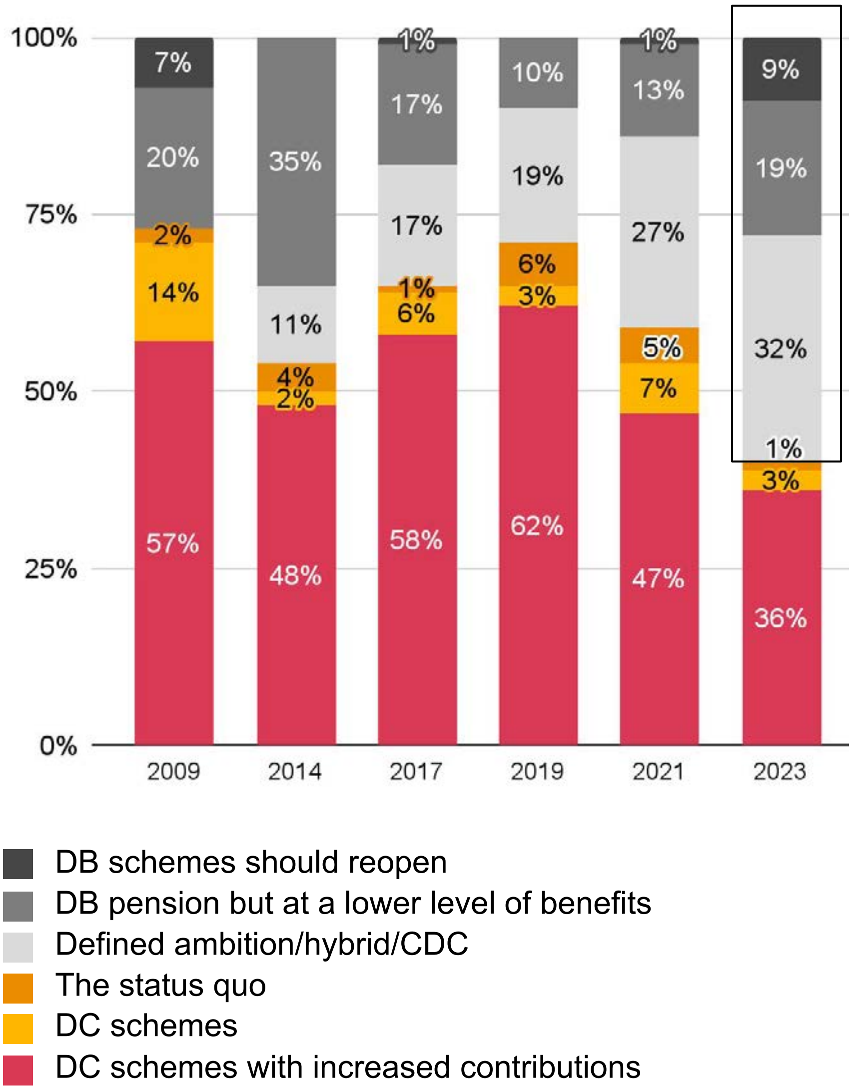
What needs to be done to address pensions poverty?

60% of lawyers believe an element of DB is the future to address pensions poverty

There's an increasing view that DC schemes on their own are not the solution, and an element of DB is needed

- For the first time in our 15 years of holding this survey, the majority of lawyers voted for an element of DB being required for future pensions.
- This included reopening DB schemes (28% of lawyers) as well as creating Collective Defined Contribution / Hybrid / Defined Ambition schemes (32% of lawyers).
- Continuing with the 'status quo' and DC schemes received the lowest number of votes in the history of our survey.

What do you think is the right answer for the long-term provision of UK pension benefits?



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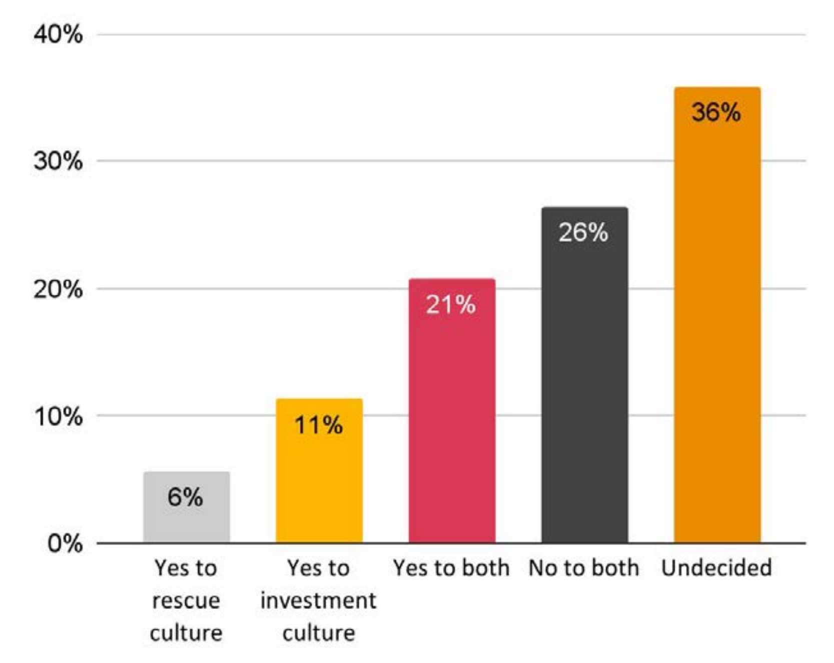
Are TPR Powers having a greater impact?

2 years after the Pension Schemes Act 2021 and uncertainty remains – but more distressed cases on the horizon will test the Act further

38% of lawyers believe the Act has negatively impacted either the UK's rescue or investment cultures

- We last held our Pensions and Restructuring Lawyers event in 2021 when this Act had just come into law, and this topic was debated on a panel hosted by Atul del Tasso-Dhupelia with guests from Natwest, Wilberforce Chambers and TPR.
- At the 2021 survey, 48% of lawyers believed the Act would damage the UK's rescue culture.
- Two years on and it is positive to see that this number has reduced to 27%, potentially reflecting experience of operating under the Act in this period.
- However, with 36% still undecided, there is significant uncertainty over the impact of the Act. This could be due to the fact that there have been low levels of distress and restructurings over the past two years to test how the Act will operate in these situations in practice.
- With increased levels of distress and restructurings anticipated (and already being felt), the Act will be tested further.

Do you think the Pension Schemes Act 2021 has negatively impacted either the UK rescue culture or investment into corporates with DB schemes?



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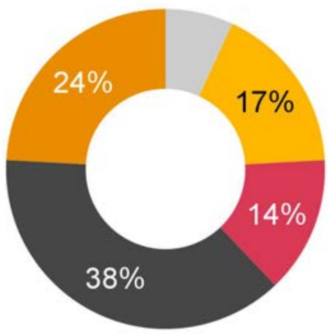

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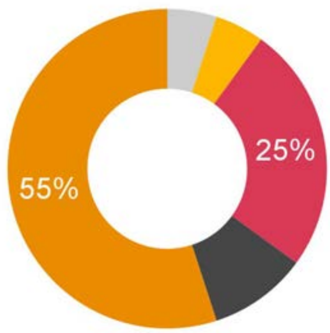


- Undecided
- No to both
- Yes to rescue culture
- Yes to investment culture
- Yes to both

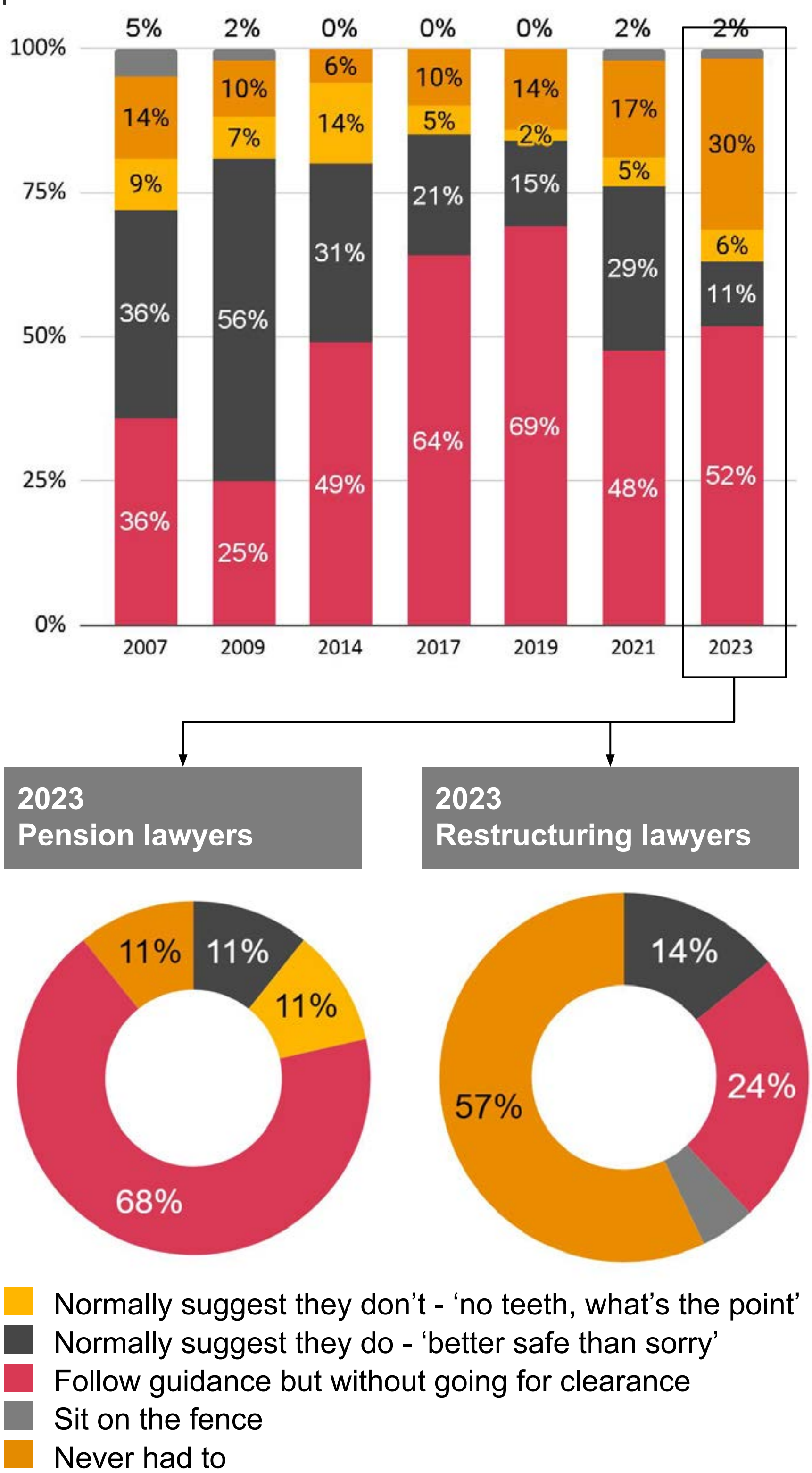
Clearance route rarely used to mitigate regulatory risks, placing more onus on legal and covenant advice

29% of lawyers in 2021 suggested clients go for TPR Clearance.

This has fallen to 11% in 2023.

- Despite the broad new powers under the Pension Schemes Act 2021 and increased levels of distress anticipated, applying for TPR clearance remains a rarely recommended route by lawyers to deal with regulatory risks.
- Pensions lawyers are more confident to 'follow the guidance but without going for clearance' with 68% choosing this route versus 24% of restructuring lawyers.
- Clearance will likely remain a relevant route for schemes in specific circumstances. However for the majority of situations, regulatory risks will need to be mitigated by lawyers and financial advisors working together collaboratively to ensure and evidence the equitable treatment of pension schemes.

In light of the Pension Schemes Act 2021, in terms of advising a client to go for Clearance, would you...



Summary of PwC's Pension and Restructuring Lawyers Event 2023

We brought together a group of over 300 pensions and restructuring lawyers to discuss 3 key topics:

- A macroeconomic update on the UK, delivered by Rt Honorable Alan Milburn and Lord Gavin Barwell, giving their views on the political environment, the outlook in advance of the 2025 General Election in the UK and what the future looks like for the UK economy.
- Catherine Atkinson and Ed Macnamara provided an update on the changes in the restructuring and insolvency market and how this is being seen in different industries.
- Atul del Tasso-Dhupelia hosted a panel debate entitled "Are UK Pensions in Distress?" with Raquel Agnello K.C. (Wilberforce Chambers), Malcolm Weir (Pension Protection Fund) and Richard Clarke (Davidson Kempner European Partners LLP).

You can watch recordings of our live event in the following link.

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Thank you

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