Stopping accrual

Some scheme rules contain an express power that allows the employer to stop future accrual of benefits. If a scheme does not contain such a provision then the employer will need to amend the rules. In most cases this will require the consent of the trustees, giving the trustees the potential power to veto the cessation of accrual. Even where the consent of the trustees is not required to change the rules, an employer may still wish to have the trustees on board before proceeding with any changes.

Where the employer wants to cease accrual by amending the scheme rules, the trustees should seek legal advice on the effect of their scheme’s amendment power.

General trustee considerations

As with any decision, trustees should act in accordance with their trustee duties when deciding whether to agree to the employer’s proposal to terminate future accrual. The trustees have two fundamental trust law duties: to further...
the purpose of the scheme in the light of changing circumstances; and to hold the assets of the scheme in accordance with the terms of the trust.

But what does this mean in practice? Trustees may be surprised to learn that in reaching their decision they may consider the interests of the sponsoring employer as a beneficiary and contributor under the scheme and take into account the effect their decision will have on the employer’s business. Indeed, the trustees will need to perform a delicate balancing act between the interests of the employer and the scheme’s members.

Statutory debt

An important consideration for trustees is whether stopping accrual would trigger a statutory debt on the employer payable to the scheme. The law relating to statutory debts is complex and trustees should therefore seek legal advice as to whether stopping accrual would trigger such a debt.

Negotiations with the employer

If trustee consent is required to amend the scheme rules, this gives the trustees power to bargain with the employer. The trustees should enter into a dialogue with the employer to try and agree a proposal which is acceptable to both parties.

The trustees should take the opportunity to quiz the employer about its business reasons for ceasing accrual. They should ask the employer to explain the business implications if the changes are not made, other options it has considered and why it has rejected those options. They should also consider negotiating some advantage for members as compensation for the loss of future service and death benefits. For example, trustees could insist that the employer offers affected employees generous money purchase benefits for future service, maintains final salary linkage or provides the same level of death benefits going forwards. They could also ask the employer or its parent company to provide some form of additional security for the scheme such as extra funding or a parental guarantee if the scheme is not being wound up.

If, during the course of negotiations, the trustees feel that the employer is behaving unreasonably or they have concerns the employer may become insolvent, they should consider approaching the Pensions Regulator. This should only be done as a last resort. In exceptional circumstances, the Regulator can require companies within the employer’s group to put in place financial support for the scheme.
Obtaining legal, actuarial and (if necessary) financial advice at an early stage will assist trustees in their negotiations with the employer and their decision-making process.

**Consequences of stopping accrual**

If the pension scheme is not being wound up, trustees also need to bear in mind the effect that stopping of accrual will have on the funding of the scheme. If no additional security for the scheme is being provided, they should consider this issue very carefully with the scheme actuary.

The trustees should also obtain investment advice. In some circumstances, the trustees may be advised to adopt a more conservative investment strategy.

**Conflicts of interest**

If any of the trustees also hold senior positions within the employer or another group company, or are involved in employer decision making in relation to the scheme and its funding, they are likely to have a conflict of interest between their two roles. It is important that the trustees address any potential conflict issues early so that they are able to demonstrate to members that any decision in relation to the employer’s proposal was a fair one and was not prejudiced by other factors.

One way to avoid or reduce such conflicts of interests is for the trustees to set up a sub-committee to deal with the employer’s proposals, with any conflicted trustees not participating in the sub-committee. Alternatively, the conflicted trustees could step down as trustees (either permanently or while negotiations are in progress). Trustees in such a position should discuss the options with their legal advisers.

**Consultation and communication**

The employer has a statutory obligation to consult its workforce over the cessation of accrual and the establishment of any new money purchase scheme. Trustees will be keen to ensure this obligation is satisfied. The employer should consult with its employees for at least 60 days and should complete the consultation before making any decision to implement the change.

If trustees do agree to the employer’s proposal to close the scheme, they should not forget that they also have a legal duty to notify scheme members.