

Mistaken overpayments - what should trustees do?

August 2010

Briefing note

HIGHLIGHTS

No matter how good a scheme's administration process, there will be occasions where mistakes occur and members receive more benefit than they are entitled to under the scheme rules. This briefing note summarises the key things trustees should consider.

Highlights are:

- An overpaid member has no right to the overpayment. The starting point is that pensions in payment should be reduced to the correct level and overpayments reclaimed from the member/survivor.
- Members/survivors may have a defence to a claim for repayment of the overpaid amount if they have changed their position in reliance on the incorrect payment.
- Overpayments may be recovered by reducing future instalments of pension (where applicable).
- Trustees may legitimately decide to write off or compromise some overpayments.
- A member's benefits may be increased to the level of the overpayment, if the sponsoring employer pays additional contributions in respect of the increase.



OVERPAYMENTS - THE LEGAL POSITION

Members are not entitled to overpayments

Members are only entitled to the benefits due to them under the scheme rules. Trustees have a duty to administer the scheme in accordance with the rules and in the interests of all members: this includes ensuring that scheme funds are not depleted by making payments to members to which they are not entitled. The starting point for trustees is that they should reclaim the overpayments from the members concerned and should discontinue payments of the overpaid benefit. Understandably, this is not an easy message to give to members.

Defence to claims for repayment - change of position

A member asked to repay an overpayment may defend the claim if it can be demonstrated that he or she has changed position in reliance on either the overpayment, or on a statement that the member was entitled to the inaccurate greater sum. The member must also demonstrate that the hardship of demanding repayment outweighs the right of the trustees to recovery. Case law has shown that the change of position defence does not work where the overpaid member has spent the overpayment on an item that may be sold to recoup the overpayment, for example on a new car or a pension that may be unwound. In contrast, members who have spent overpayments on holidays, meals out or a general improvement in lifestyle may be able to defeat a claim for repayment.

In addition, the defence of change of position will fail if the overpayment was so great that the member should have been aware of the error and cannot claim to have changed his position in good faith. In cases where overpayments have been significant it may be that the member could not legitimately argue that he or she was not aware of the error. Any particular case would need to be considered on its facts, including whether previous benefit statements might suggest that the subsequent payments were excessive.

HOW TO RECLAIM THE OVERPAYMENT?

Reducing future instalments of pension

Where an individual's pension is ongoing, the trustees may decide to recover the overpayments by reducing future pension instalments until the debt is repaid. Section 91(5) of the Pensions Act 1995 specifically exempts such reductions from the general prohibition on giving up pension rights. In addition, the Pensions Ombudsman has held that trustees do not need an explicit power in their trust deed and rules to set off overpayments against future pension. It is not necessary to obtain the members' consent to the reductions.

Recovering the overpayment from the member/survivor

It is also possible to ask the overpaid individual to repay the overpayment direct. In all but the smallest cases, it would be reasonable to offer the option of repaying by instalments over a period of time.

Recommended approach

The most practical approach in many cases can be to recover payments through reductions to future benefits, except where the member disputes the claim or gives notice that he or she would prefer to repay the amount due in a single payment or in instalments.

To avoid hardship it would be preferable to spread repayments over a number of pension instalments, rather than reducing an individual's pension to zero for a period of time. However, trustees dealing with mistaken overpayments to a number of beneficiaries would be well-advised to draw up some guidelines as to how repayments are to be managed, especially where the member has very limited life expectancy or owes a significant amount.

A DECISION NOT TO SEEK RECOVERY OF OVERPAYMENTS

Compromise of amounts owed

Trustees can properly decide to write off a loss where they believe that its recovery would involve greater expense than the amount which might be regained. This is more likely to be the case where a member has died and there are no future pension payments against which the amounts owed by the member could be offset. Trustees should not follow this path unless they have at least requested repayment (from the member's personal representatives, where the member has died) and asked the employer if it wishes to fund the augmented benefits (please see below).

Augmentation of benefits

An alternative to seeking repayment or writing off a loss is to augment the individual's benefits to the level of the incorrect overpayment. Most scheme rules contain a power to augment benefits where the employer provides additional funding to cover the increased cost. In some cases, employers prefer to pay additional contributions to fund overpayments rather than risk the ill-will of members when the trustees seek repayment. Employers are not obliged to fund overpayments and the approaches of individual employers to such situations vary. However, as a matter of courtesy it is proper to give employers the option of augmenting benefits before writing to members requesting repayment.

De minimis overpayments

In some cases, overpayments may be extremely small. Trustees could justifiably set a cut off point, for example, £20, below which they consider it uneconomic to seek repayment even through reducing future pension payments.

ARE THE OVERPAYMENTS UNAUTHORISED PAYMENTS?

Regulations in force in 2009 mean that overpayments made in genuine error since 6 April 2006 may be treated as authorised payments. If the payments are to continue at the higher level following discovery of the error, the rules should be amended to reflect this.

SENSITIVITY

Claims for repayment of overpaid pension are never easy to make. Trustees should be aware that, no matter how carefully handled, the claims may result in bad feeling and potential disputes. Members should be informed of their right to seek advice from The Pensions Advisory Service (TPAS). However, TPAS advisers receive training in matters of this nature and are usually well aware that the law sides with trustees in asserting their right to repayment.

PRACTICAL STEPS

In a typical scenario in which a number of overpayments have come to light, the sequence for remedying the situation might be:

- The trustees ask the relevant employers whether they would like to fund the overpayments to augment benefits to the level incorrectly paid. It should be emphasised that the employers are under no obligation to do this.
- If the employers decline to fund the additional benefits, the trustees write to the affected members, explaining (in appropriate cases) that the amounts due will be recovered through reductions of stated amounts to future benefits, unless the member disputes the claim or proposes an alternative payment plan within a specified time.
- Where the member has died, the trustees write to the member's personal representatives requesting repayment.
- The trustees respond appropriately to any responses disputing the claim or requesting alternative methods of payment.
- After a period of, say, two months, the trustees commence the reduction of future benefits where there is no dispute or request for alternative payment, to continue in each case until the amount due is repaid.
- The trustees may decide to write off or compromise claims in particular cases.

This note is written as a general guide only. It should not be relied upon as a substitute for specific legal advice.

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