

R e c o v e r y

Fixing pension overpayments



Gareth Stears, technical consultant at Aries Insight, explains what is required and best practice when in the awkward position of asking for money back

In pensions, paying someone too much can prove as unpopular and controversial as paying them too little. This is because schemes usually need to ask for the money back. I've been involved in more exercises to correct overpayments – as an administrator and as a mediator for the Pensions Ombudsman Service – than I care to remember. Let me tell you, it isn't much fun for schemes either.

Pension trustees have a duty to ensure their scheme is administered in line with its rules, which includes paying the correct level of benefits. They also have a duty to act impartially. If one member receives (and gets to keep) more than they are due, this could be at the expense of other members. Therefore, overpayments usually require some corrective action, including changing any ongoing payments to the right level and asking members to return any excess they weren't due. It doesn't matter whether the scheme made the mistake.

Schemes will sometimes make an exception. They might write-off overpayments if the cost of recovery is likely to exceed what they expect to receive back. It can be expensive if members are non-responsive and recovery is only possible through the courts. Sometimes trustees can make a claim against their professional advisers instead, or ask for an indemnity from the scheme's sponsoring employer.

Responsive members have some legal defences against recovery, too. Sometimes they can even secure the right to an incorrect benefit going forward. The most common defences against reclaim are 'change of position', 'estoppel', and 'limitation'. The first two are similar. Broadly, the member must prove that correcting the mistake would leave them worse off than if the scheme had acted correctly from the outset. They might have committed to outlays (which cannot be refunded) because

they believed the overpayment was due to them.

The Limitation Act 1980 may restrict the scheme to recovering only overpayments made within six years of the mistake being discovered (or when the scheme ought to have discovered it). For this reason, regular audits of benefits can pay for themselves. But it can damage any defence if the member ought to have spotted it themselves.

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Schemes must act fairly and impartially throughout. Members should be made aware of their right to dispute the overpayment. And schemes ought to consider whether the member has a sound defence, rather than expecting the member to fight it up to the Ombudsman.

Members shouldn't be pressured into repayment and should be allowed time to adjust. Where overpayments took place over a prolonged period, the scheme should ideally offer the member at least the same duration to repay. The speed and level of repayment should not be such that it causes the member financial hardship.

Allowing repayment in instalments may be sensible. If the member is due further payments from the scheme, 'recoupment' is a helpful option. This means deducting a proportion of those future payments, with due consideration to what the member can afford, until the debt is repaid. One benefit to the scheme is that the Limitation Act does not appear to apply to recoupment. It may also be possible to begin recoupment without the member's consent, unless the

amount is disputed. This should be a last resort, however, and the member must always be sent a repayment schedule before any recoupment begins.

Overpayments generate several tax considerations, depending on whether they are written-off or reclaimed. If written-off, establishing whether an 'unauthorised payment' has occurred can be complicated (and mostly outside the scope of this article). Trustees may have the option to augment the entitlement though, neatly removing the problem.

If reclaimed, the test against a member's lifetime allowance may need to be revisited. Correcting a pay as you earn (PAYE) record can be onerous, especially if the pension was overpaid in multiple tax years. HM Revenue & Customs (HMRC) prefer schemes to reclaim the net amount from the member and reclaim the tax from them. If any overpayment was made in an earlier tax year, schemes can send corrected figures to HMRC via an earlier year update. They should also send these to the member in writing, ideally in a revised P60 certificate marked 'replacement'.

During any recoupment, schemes usually operate PAYE on the amount due (ignoring the deduction), offsetting against the net payment. This can be hard to sell to members but is appropriate. It does mean that when considering what the member can afford to repay the net rather than gross amount should be considered.

There is more to consider. For example, a significant mistake might need to be reported to The Pensions Regulator as a breach. I haven't even mentioned reputational concerns. And members might be due compensation for any distress and inconvenience they have suffered. If this compensation (coincidentally) equals the amount of overpayment, that might solve some problems. ■