Sackers

Pensions litigation briefing

December 2024

Sackers' pensions litigation team reviews recent case law and developments, examining the practical lessons for trustees and employers

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Abbreviations

TPO: The Pensions Ombudsman

TPR: The Pensions Regulator

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Overview

“We spoke at our recent webinar about overpayments, and the next few pages set out some of the key points coming out of that webinar.

Dealing with overpayments is a common refrain in practice for schemes and can be both tricky and time-consuming to resolve. And in light of a recent TPO decision, where a large overpayment was reduced to a very low recovery, trustees are having to tread carefully.

We saw a couple of important Court of Appeal decisions in the summer. In *Virgin Media* the Court of Appeal decided that amendments which altered certain rights in contracted-out schemes were void even in relation to benefits earned for future service, if they were made without a necessary actuarial confirmation. And in the *BBC* case the Court confirmed that the term “interests” in the context of a restriction on making amendments included an active member’s future service rights under the scheme.

We recently heard from TPO about a new expedited decision-making process. This process involves an initial decision by a caseworker being issued to all parties, with an option to trade up to an Ombudsman for a determination. TPO hopes this process will reduce waiting times by as much as 18 months. That would be a massive boon for schemes and members alike if it were to happen, as well as a gleaming feather in TPO’s cap.

Finally, and importantly, I wish you some peace and respite as we approach the end of what has been another busy year in pensions.”

Arshad Khan
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In this issue

Overpayments in practice

Trustees must take reasonable steps to recover an overpayment

The starting point is for trustees to seek recovery of an overpayment, as they are under a legal duty to pay the correct scheme benefits to members. Trustees must also be able to account to scheme beneficiaries for any payments made from scheme assets and, in the case of an overpayment, a scheme's assets will have been reduced below the level that they ought to be.

Where trustees decide not to seek recovery, they should have some basis for making that decision, eg demonstrating that it would be ineffective, disproportionate and/or impractical to seek recovery.

What is an overpayment?

An overpayment is any payment over and above what a person is legally entitled to receive.

What should trustees do if an overpayment has been made?

If an overpayment is discovered, trustees should:

- **understand the error and its impact** – establish if it is a one-off incident or whether there could be a systemic issue that needs resolving
- **check the scheme's overpayments policy** – a policy can be a useful starting point for trustees and their administrators, and can save time when an overpayment occurs
- **liaise with third parties** (administrator, employer, buy-in provider (if relevant)) – to help establish the facts and to work together to resolve the underlying issue
- **communicate with the affected member(s)** – be sympathetic about delivering bad news yet clear about what's happened and what the impact is on their benefits
- **correct the payment going forward** – correct the payment promptly, giving the member reasonable notice. However, depending on the circumstances, ceasing the overpayment may take longer or it may be that advance notice cannot be given (eg if a letter is returned undelivered and no email address is held for the member).

How do you recover an overpayment?

Repayment

Repayment is when the member returns money directly to the scheme. If they refuse, then the trustees can claim to recover via court proceedings. This is commonly used in cases where there is no ongoing legal relationship with the individual (see pages 6 and 7).

Recoupment

Recoupment involves making deductions from the member's future pension instalments. It is a self-help remedy. With the member's agreement, this can be a fairly straightforward process, offering the parties flexibility in agreeing a suitable solution. However, if the amount is disputed by the member, then recoupment can only be done with an order of a competent court.

Overpayments in practice cont.

How long should it take to repay the money?

The general principle is that the period of recovery should be the same duration as the period of the overpayment. However, this is just the starting point, and trustees should consider whether the rate and terms of recovery are fair, just and equitable. Factors to consider when setting the recovery period include:

- Age, health and financial circumstances of the member
- Amount and duration of the overpayment

Defences available to the member

Check whether any defences are available to the member

TPO expects trustees to have explored the potential defences available, explained them to the member and to have proactively sought relevant evidence to assess any defence the member might reasonably have. The most common defences raised are limitation and change of position.

Limitation

Trustees must make a claim with six years of becoming aware of the overpayment or from the date the overpayment could have been discovered with reasonable diligence. This time limit only applies to repayment, as recoupment is a self-help remedy. However, in recoupment cases, TPO will still consider what steps the trustees should have taken sooner to communicate with the member and to seek to recover the overpayment, as a matter of general fairness.

Change of position

In this defence, the member must have changed their position believing the payment was theirs to spend, such that it would be unjust or inequitable to require them to repay the overpayment, either in whole or in part. To make out a change of position defence:

- The member's circumstances must have changed detrimentally and irreversibly
- The change of circumstances must have been caused by receipt of the overpayment
- The member must not have acted in "bad faith" when changing their position

For example, turning a blind eye to receipt of what looks like an erroneous payment without querying it may be viewed as "bad faith" by TPO, and spending the overpaid sum on something the member would always have been liable to pay (eg an overpayment to an existing mortgage) would not be viewed as a detrimental change of position.

Overpayments in practice cont.

What happens where trustees have continued to pay a pension after the death of a member?

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- The same principles apply (ie the starting point is to seek to recover any overpayments).
- However, pension instalments continued for up to six months after a member's death will generally be authorised payments if the scheme wasn't informed of the death. This is useful for pensions tax purposes as, in practice, schemes are often not told of a member's death immediately.
- If trustees decide to recover the payment, they typically have to seek payment from the member's estate. Doing so in a timely and well-evidenced manner is more likely to help in recovery (ie while the estate is collecting assets and paying debts etc).
- If the member's pension was being paid to a joint account then the surviving account holder can be asked to repay without needing to involve the estate.
- If the member died within five years of retirement, a lump sum might be payable. If so, it may be permissible, subject to the scheme rules, to take account of the overpaid pension when determining the amount of the lump sum.
- It is not possible for trustees to "set-off" member overpayments against any spouse's or child's pension unilaterally, nor to withhold such a pension pending repayment. However, in practice, having a sensible dialogue with the spouse can help get to an agreed position for the overpayment to be recovered if the spouse benefitted from the overpayment via the estate.

Thinking about tax

Future payments

Where an overpayment is ongoing, eg a pension, schemes will typically stop the overpayment and correct it going forward. Continuing with an overpayment when it has been identified as such would generally result in the excess amount being an unauthorised payment, and subject to a tax charge, unless it is possible to amend the rules or a discretion is exercised to validate the higher pension.

Past overpayments

There are generally no adverse tax sanctions for a genuine error in paying the past overpayment, as past overpayments will be deemed "authorised payments" for tax purposes, provided that the payment is genuinely intended to represent an authorised payment and that trustees believed that the member was entitled to the payment, in that amount. The position is different for overpayments following the death of a member (see box above).

Claims against the administrator

If the administrator was at fault, trustees might be able to claim against them

Trustees should also consider claims against third parties for sums paid in error which cannot be reasonably recovered from the member. If the administrator is at fault, then the trustees should engage with the administrator to understand its position, particularly in respect of mitigating the loss. Administrators will often wish to see evidence of the trustees' actions in the context of recovery from the member before agreeing to pay anything. A document trail will help with this, as will involving the administrator in the wider recovery process, where appropriate.

The trustees should also check any relevant contractual terms, particularly those regarding liability.

Overpayments: transfer values

Overpaid transfer value cases are slightly different from standard overpayments as the sums are typically much higher and, following the transfer, the individual generally has no scheme benefits from which amounts can be recouped and no ongoing relationship with the trustees. The "self-help" remedy of recoupment therefore isn't available.

Individuals who are not (or are no longer) members

The content of this section applies generally to any scenario where an overpaid beneficiary doesn't have an ongoing interest in the scheme, eg where a death benefit lump sum is paid to the wrong beneficiary or is overpaid.

Options for recovery

Trustees seeking the repayment of an overpaid transfer value need to consider whether the individual can (and is willing to):

- repay from the receiving scheme. However, this is only possible where there are sufficient funds in that scheme, the individual agrees to it and authorises the payment, or
- repay the overpaid amount from other sources of funds.

In our experience, individuals who don't have any remaining scheme benefits are generally less co-operative than scheme members, as:

- They have no ongoing relationship with the trustees
- The sums in question tend to be higher
- The trustees must take direct action to secure repayment

If the individual isn't engaging with the process and the overpayment is due to an error by the scheme administrator, then trustees can pursue it instead. However, given that the amounts at stake are typically higher, it is more likely that the administrator would look to defend those claims and expect trustees to take steps in mitigation.

Taking an individual to Court

Trustees can take individuals to Court to recover overpayments

If the individual refuses to engage, and pursuing the administrator isn't viable or appropriate, then trustees should consider whether to pursue a legal claim against the individual. Trustees don't have the option to bring a complaint to TPO, so if the individual doesn't complain, then the trustees' only option may be to issue a Court claim.

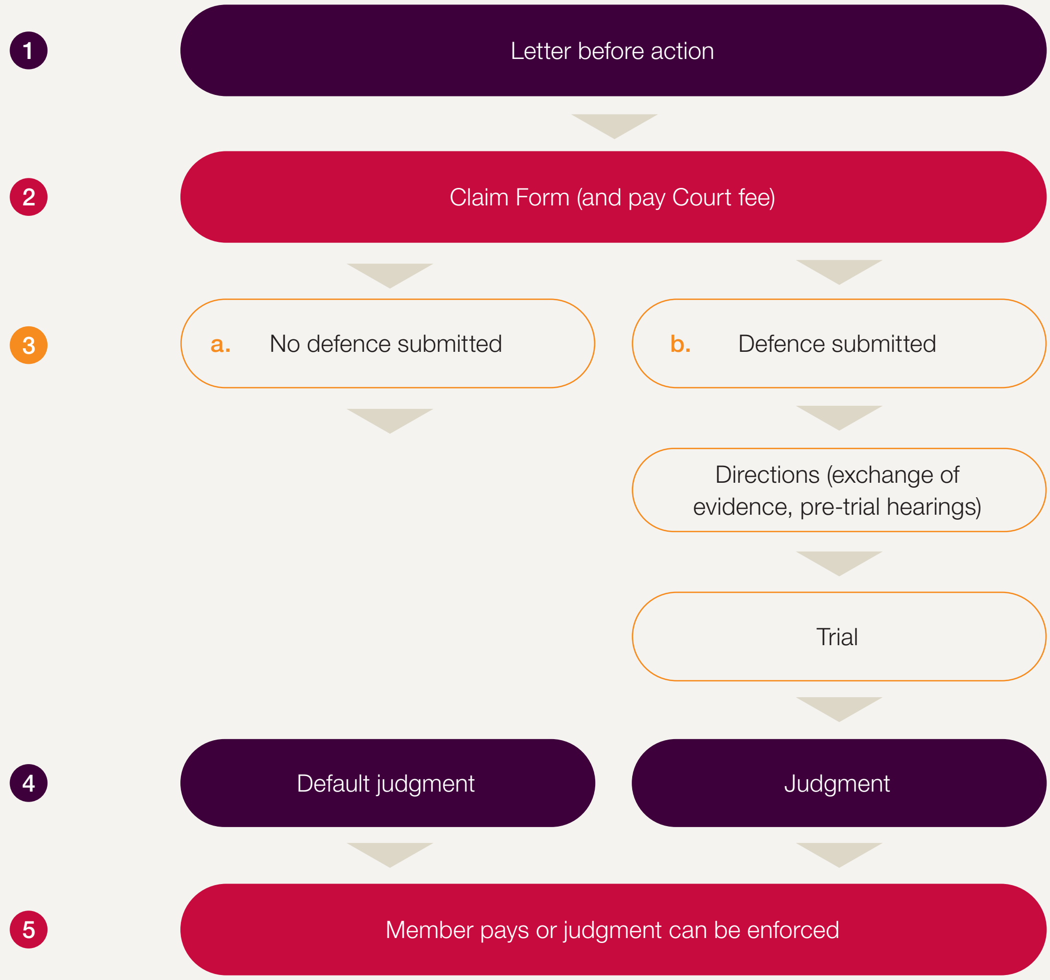
Whilst this may seem like a drastic action, trustees' duties are clear and the amounts involved in transfer overpayments can be significant, making it appropriate in some situations to take such action. However, it's important to understand the individual's financial position, where possible, as there is no point going to Court if they don't have the funds to repay the overpayment.

What about costs?

If a claim is successful then the general rule is that trustees can recover reasonable legal costs from the individual, including the Court fee paid at the outset. However, if a claim is unsuccessful then trustees can be ordered to pay the individual's costs. Any settlement agreed with the individual would make provision for who pays the costs or agree that each party pays its own costs.

Overpayments: transfer values cont.

The diagram below sets out the process:



Notes

1. Trustees send a "Letter Before Action". This is a formal letter telling the individual that the trustees will be bringing a claim if payment isn't made. Issuing this letter doesn't commit the trustees to issuing court proceedings.
2. Trustees file the Claim Form at Court either on paper or electronically, setting out the basis of the claim.
3. a. If the individual doesn't submit a defence, then the trustees will be able to apply for a "default judgment" by virtue of the individual not responding.
   b. If the individual does defend the claim, then:
      - the Court will give directions on what happens next eg exchanging evidence and possibly some procedural hearings, before a trial then takes place
      - the parties can settle the claim in the meantime (indeed at any time), and in our experience that tends to be the case in the majority of claims.
4. If the claim is successful at trial then the trustees will obtain a judgment against the individual.
5. Once the trustees have a judgment the individual is obliged to satisfy that judgment. If they still don't pay then the trustees can enforce the judgment against the individual's assets.

Contact

Our market leading pensions litigation team is highly ranked by both Legal 500 and Chambers UK. Our team of pension litigators provides "first-class advice" (Chambers & Partners, 2024) and is experienced in handling cases before TPR, the High Court and TPO, and acts for both claimants and respondents in all forms of pensions litigation.

Sackers is the UK's leading commercial law firm for pension scheme trustees, employers and providers. Over 60 lawyers focus on pensions and its related areas. For more information on any of the articles in this briefing, please get in touch with Peter or any of the team below, or your usual Sackers' contact.

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Very competent team

They have a deep understanding of the market

Legal 500, 2025

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