

## LGPS Administering Authority Information Note

### Contracted-out reconciliation: pensioner overpayments

#### Aim of this information note

This Note has been prepared by the LGPC Secretariat, a part of the Local Government Association (LGA). Its aim is to assist administering authorities in determining what action to take following the discovery of an over-payment of pension during the course of the contracted-out reconciliation exercise.

#### Important please note disclaimer below

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## Background

In February 2016 HM Treasury (HMT) wrote to DCLG regarding the data reconciliation exercise which all Public Service Pension Schemes (PSPSs) are undertaking as a consequence of the end of contracting-out on 5 April 2016.

The letter: -

- explained that a small working group had been established by HMT to arrive at a number of collective decisions on which data should be reconciled and on what options are available to PSPSs to help simplify the reconciliation exercise, and
- stated that PSPSs have expressed a preference for consistency in treatment, where feasible, and
- recommended that the reconciliation criteria set out within the letter should be adopted.

In relation to overpayments of pension identified as a result of the contracted-out reconciliation exercise the letter stated *“For pensioners who have been historically overpaid, the working group recommends that you wait for evidence from the reconciliation exercise on the extent of overpayments. This would give more information on whether there will be value for money in recouping the overpayments”*.

## Current position (June 2017)

Since that letter was issued to administering authorities, the Secretariat has received a number of queries from administering authorities querying when they can expect to receive recommendations from HMT concerning the reduction of pensions in payment and recovery of any overpayments.

HMT have yet to make any recommendation regarding either the date by which any affected pensions should be reduced or as to whether or not any overpayments should be recovered. This is because HMT require ‘evidence’ of the extent of overpayments before they are able to make any recommendation to Ministers.

The current position places administering authorities in a difficult position for the following reasons:-

- administering authorities are obliged to correct any error they discover within a reasonable period of time. To do otherwise would render the continuing overpayments unauthorised under regulation 14 of the Registered Pension Scheme (Authorised Payments) Regulations 2009 [SI 2009/1171]. Furthermore any delay in reducing the pension to the correct level would increase the loss to the fund in the event overpayments are not recovered.
- administering authorities will have their own delegations with regard to the process and limitations of write off which will apply for overpayments and which they will have to follow.

## Considerations for administering authorities

The complexity surrounding Pension Increase and Guaranteed Minimum Pensions could be significant in determining an administering authority's approach. It is, in the view of the Secretariat, unlikely that Scheme members could have been aware that they were being overpaid, unless they have a good understanding of the interaction between the Pensions (Increase) Act 1971, the Social Security Pensions Act 1975 and the Pension Schemes Act 1993<sup>1</sup>. Therefore, administering authorities may wish to take into account the areas mentioned below, alongside their existing delegations, when making any decision to recover overpayments.

### Is the size of the overpayment relevant?

In its determination in the case of *Capita ATL Pension Trustees Ltd v Gellately* [2011] EWHC 485 (Ch) the High Court found that "In view of the small scale of the problem, the distress that any attempt to recover the sums would inevitably cause, and the likelihood that the exercise would anyway not be cost-effective" it was not necessary for the Trustees to take any steps to recoup the overpayments." In this case, the amount of the overpayments to three widows were relatively small (no more than £10,200 in total).

### Can 'Estoppel' be used to prevent the recovery of an overpayment?

The starting point used to be that if an overpayment had been made under a mistake of law it was generally not recoverable but if the employer could establish that the mistake, was a mistake of fact, the money was potentially recoverable. The Law Commissions in England, Wales and Scotland recommended that the distinction between mistakes of law and mistakes of fact should be removed. The House of Lords has already decided cases on this basis (see *Kleinwort Benson v Lincoln City Council and others* 1998 4 All ER 513). So, whether an overpayment results from a mistake of fact or law, it would seem that, potentially, it could now be recoverable unless estoppel applies (although, in the absence of an employee's consent to repayment, legal advice should be sought before instigating any formal recovery action).

The recipient may lodge the defence of *estoppel by representation* if they can show that:

- the administering authority made a representation of fact that led the recipient to believe that they were entitled to treat the money as their own;
- the recipient has changed their position, in good faith, in reliance of that representation; and
- the overpayment was not caused by the fault of the recipient.

The recipient may lodge the defence of *Estoppel by convention* if they can show that:

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<sup>1</sup> Or unless an error had been made that should have been obvious to the member e.g. the member's pension on attaining GMP age was £300 p.m. of which £40 p.m. was GMP. The member had been notified that the pension at GMP age (£300) would be made up of £40 GMP and £260 pension. However, payroll had inadvertently input a GMP figure of £400, with the pensioner then receiving a total of £660 pm instead of £300 pm.

- even if the administering authority had not made a representation of fact that led the recipient to believe that they were entitled to treat the money as their own, the administering authority and the recipient had acted on an assumed state of facts or law, the assumption being shared by both parties or assumed by one and acquiesced to by the other (as demonstrated in subsequent mutual dealings between both parties)

However, estoppel is an inflexible, all or nothing defence. A successful plea of estoppel acts as a total bar to recovery. This can lead to unjust enrichment so that the recipient can keep all of the money even if it exceeds the detriment they suffered. In recognition of this, the courts have developed the more flexible 'change of position' defence (see below).

### **Can 'change of position' be used to make a partial claim for recovery of an overpayment?**

The change of position defence means that it is no longer necessary to show that there had been a representation made by one party on which the other had placed reliance and had acted to his detriment. More importantly, it only prevents recovery of that part of the overpayment in respect of which the recipient has changed his position and the requirement for them to repay the sum would outweigh the injustice of denying the paying employer restitution - see *Lipkin Gorman v Karpnale Ltd* [1991] 2 AC 548.

Even if the recipient had spent some of the money, this would not necessarily prevent recovery if they would have incurred such expenditure anyway. This concept was followed in *Derby v Scottish Equitable* [Court of Appeal, Civil Division, 16 March 2001] which limited the use of the defence of estoppel to the amount used in changing the recipient's position. In this case, Mr. Derby was only able to retain the sum he spent on improving his lifestyle (£9,661) and not the full sum of the overpayment (£172,000).

### **Is 'relevance of member awareness' important?**

In the determination in the case of *Professor B Kenny and Teachers Pensions Scheme* [determination 28034/5] the Pensions Ombudsman placed a further limit on the change of position test. Professor Kenny had been quoted a pension of £13,000 a year but was paid £21,000 a year. The Pensions Ombudsman found that "one of the essential elements of a defence of change of position is that the individual must have changed his position in good faith. In other words, Professor Kenny could not rely on such a defence if he was either aware of the error, or should have been..... I am happy to accept that Professor Kenny was not 'a pension's expert'. Nevertheless, the discrepancy is so great that I find that Professor Kenny should have been aware that something was amiss. I find, therefore, that the defence of change of position cannot succeed in Professor Kenny's case." This line was upheld in the High Court in *Webber v DfE* (Chancery Division, 19<sup>th</sup> December 2014).

### **Should the 'cost effectiveness' of recovery be considered?**

Although paragraph 7.10 of the HM Treasury document "Managing Public Money" (July 2013 as revised in August 2015) suggests that the document does not directly apply to local government, that is not to say that the

principles within the document are not appropriate in considering the cost effectiveness of reclaiming any overpaid monies. The document states that: “public sector organisations should take decisions about their tactics in seeking recovery in particular cases on the strength of cost benefit analysis of the options”.

### **Should any resultant ‘hardship’ be considered when deciding whether or not to seek recovery?**

Although paragraph 7.10 of the HM Treasury document “Managing Public Money” (July 2013 as revised in August 2015) suggests that this does not directly apply to local government, that is not to say that the principles within are not appropriate in considering any resultant hardship, when seeking to reclaim overpaid monies. The document states that: “Public sector organisations may waive recovery of overpayments where it is demonstrated that recovery would cause hardship. But hardship should not be confused with inconvenience. Where the recipient has no entitlement, repayment does not in itself amount to hardship, especially if the overpayment was discovered quickly. Acceptable pleas of hardship should be supported by reasonable evidence that the recovery action proposed by the paying organisation would be detrimental to the welfare of the debtor or the debtor's family. Hardship is not necessarily limited to financial hardship; public sector organisations may waive recovery of overpayments where recovery would be detrimental to the mental welfare of the debtor or the debtor's family. Again, such hardship must be demonstrated by evidence”.

### **Limitation Act 1980**

#### **How does the Limitation Act 1980 affect what monies may be recovered?**

Section 5 of the Limitation Act 1980 states that “*An action founded on simple contract shall not be brought after the expiration of six years from the date on which the cause of action accrued*”. However, section 32(1) of the Limitation Act 1980 ‘postpones’ the date by which an administering authority may make a claim to recover monies. It states “*the period of limitation shall not begin to run until the plaintiff has discovered the fraud, concealment or mistake (as the case may be) or could with reasonable diligence have discovered it*”.

The combination of sections 5 and 32(1) of the Limitation Act 1980 mean that a claim to recover overpayments caused by a mistake (or by fraud or act of deliberate concealment committed by the defendant) has to be made within 6 years of the date when the mistake, fraud or act of concealment was first discovered or could, with reasonable diligence, have first been discovered. Where a claim is made within the 6 year period, all of the overpayment can be recovered.

If the claim for recovery is made more than 6 years after the date when the overpayment(s) could with reasonable diligence first have been discovered then, as each monthly overpayment payment is treated as a separate

overpayment, only overpayments made within the 6 years prior to the “cut-off date” are recoverable. The question of what constitutes the “cut-off date” was considered in the High Court case of *Webber v DfE* (Chancery Division, 8<sup>th</sup> July 2016).

The result of the above is shown in the following examples (please note that the examples within the table below assume that an overpayment claim is a quasi-contractual one and that a restitutionary claim is not possible)

Scenario	Limitation Period	Overpayment Period Which Can Be Claimed <sup>2</sup>
<ul style="list-style-type: none"> <li>• Overpayments began in April 2008 (the first Mistake Date)</li> <li>• Overpayments discovered, or could have been discovered with reasonable due diligence, in August 2010 (the Discovery Date under Section 32 of the Limitation Act 1980)</li> <li>• Overpayments made for period between April 2008 and August 2010</li> <li>• Formal claim<sup>3</sup> for recovery made in January 2015 (the Cut Off Date as referred to in <i>Webber</i>)</li> </ul>	<ul style="list-style-type: none"> <li>• No issues in principle with the Limitation Period as formal claim for recovery commenced within 6 period after the Discovery Date</li> <li>• claims are therefore valid and should proceed</li> </ul>	<ul style="list-style-type: none"> <li>• Overpayments back to when they began in April 2008 until August 2010 may be claimed</li> </ul>
<ul style="list-style-type: none"> <li>• Overpayments began in April 2003 (the first Mistake Date)</li> <li>• Overpayments discovered, or could have been discovered with reasonable due diligence, in November 2009 (the Discovery Date under Section 32 of the Limitation Act 1980)</li> </ul>	<ul style="list-style-type: none"> <li>• No issues in principle with the Limitation Period as formal claim for recovery commenced within 6 year period after the Discovery Date</li> <li>• claims are therefore valid and should proceed</li> </ul>	<ul style="list-style-type: none"> <li>• Overpayments back to when they began in April 2003 until November 2009 may be claimed</li> </ul>

<sup>2</sup> While this refers to the period which can be claimed, this is not the same as the period which will definitely be recovered in light of the other defences which are available to scheme members who face such claims for repayment of Overpayments.

<sup>3</sup> Reference to the ‘formal claim’ in this appendix means the commencement of formal proceedings to recover the Overpayment.

<ul style="list-style-type: none"> <li>• Overpayments made from April 2003 to November 2009</li> <li>• Formal claim for recovery made in December 2011 (the Cut Off Date as referred to in <i>Webber</i>)</li> </ul>		
<ul style="list-style-type: none"> <li>• Overpayments began in January 1999 (the first Mistake Date)</li> <li>• Overpayments discovered or could have been discovered with reasonable due diligence in September 2016 (when the date was received from HM Treasury in relation to the GMP equalisation exercise) (the Discovery Date under Section 32 of the Limitation Act 1980)</li> <li>• Overpayments made for the period from January 1999 to September 2016</li> <li>• Formal claim for recovery made in February 2017 (the Cut Off Date as referred to in <i>Webber</i>)</li> </ul>	<ul style="list-style-type: none"> <li>• No issues in principle with the Limitation Period as formal claim for recovery commenced within 6 year period after the Discovery Date</li> <li>• claims are therefore valid and should proceed</li> </ul>	<ul style="list-style-type: none"> <li>• Overpayments back to when they began in January 1999 until September 2016 may be claimed</li> </ul>
<ul style="list-style-type: none"> <li>• Overpayments began in April 2006 (the first Mistake Date)</li> <li>• Overpayments discovered, or could have been discovered with reasonable due diligence, in August 2009 (the Discovery Date under Section 32 of the Limitation Act 1980)</li> <li>• Overpayments made for period between April 2006 and August 2009</li> <li>• Formal claim for recovery made in</li> </ul>	<ul style="list-style-type: none"> <li>• Issue with the Limitation Period as formal claim for recovery commenced more than 6 years after the Discovery Date</li> <li>• claims are therefore out of time and should not proceed</li> </ul>	<ul style="list-style-type: none"> <li>• Overpayments cannot be claimed back as the formal claim for recovery was made more than 6 years after the Discovery Date</li> </ul>

January 2017 (the Cut Off Date as referred to in <i>Webber</i> )		
<ul style="list-style-type: none"> <li>• Overpayments began in April 2006 (the first Mistake Date)</li> <li>• Overpayments discovered, or could have been discovered with reasonable due diligence, in August 2009 (the Discovery Date under Section 32 of the Limitation Act 1980)</li> <li>• Overpayments made for period between April 2006 and August 2016</li> <li>• Formal claim for recovery made in January 2017 (the Cut Off Date as referred to in <i>Webber</i>)</li> </ul>	<ul style="list-style-type: none"> <li>• Issue with the Limitation Period as formal claim for recovery commenced more than 6 years after the Discovery Date</li> <li>• claims for overpayments between April 2006 and January 2011 are therefore out of time and should not proceed</li> <li>• however, as each monthly overpayment is a separate overpayment, the effect of the <i>Webber</i> case is that overpayments made in the 6 years prior to the Cut Off Date (i.e. the overpayments made in February 2011 to August 2016) can be recovered</li> </ul>	<ul style="list-style-type: none"> <li>• Overpayments for the period April 2006 to January 2011 cannot be claimed back as the formal claim for recovery was made more than 6 years after the Discovery Date</li> <li>• Overpayments for the period February 2011 to August 2016 may be reclaimed.</li> </ul>

## Tax

### Where a pension is overpaid, from what date should the pension be reduced?

As mentioned previously administering authorities are obliged to correct any error they discover within a reasonable period of time. To do otherwise would render payments unauthorised under Section 14 of the Registered Pension Scheme (Authorised Payments) Regulations 2009 [SI 2009/1171]. We understand that HMRC have provided a clear steer with regards to timing, in so much that “*When a scheme discovers an overpayment it immediately become unauthorised and is subject to an unauthorised tax charge*”.

Bearing the above in mind, administering authorities should carefully consider the implications for themselves and the scheme member **before** making any decision not to amend pensions to the correct level as soon as they are aware of any errors.

### Would sums written off be unauthorised payments?

We understand that any overpayment that is not recovered will not be unauthorised if it falls within regulations 13 or 14 of the Registered Pension Schemes (Authorised Payments) Regulations 2009 [SI 2009/1171].

Regulation 13 says that a payment made in error will be an authorised payment if the:

- payment was genuinely intended to represent the pension payable to the person,
- administering authority believed the recipient was entitled to the payment, and
- administering authority believed the recipient was entitled to the amount of pension that was paid in error.

However, there is a presumption in the regulations that once the error has been determined the administering authority must take reasonable steps to prevent any further overpayment to the recipient (except, by virtue of regulation 14, during any period where the scheme is taking a reasonable period of time to determine whether to change the scheme rules and, if so, during a reasonable period of time to actually amend the scheme rules, in order that the higher level of pension will be paid as normal authorised payments).

In addition to the above, there is a further exemption where the overpayment is a 'genuine error' as described in PTM146300 and the aggregate overpayment (paid after 5<sup>th</sup> April 2006) is less than £250. In such circumstances, if the overpayment is not recovered it remains an unauthorised payment but it does not have to be reported to HMRC and HMRC will not seek to collect tax charges on it.