Ministry of JUSTICE

Claims Management Regulation

Impact of Regulation Assessment – Update

A report by Mark Boleat for the Ministry of Justice
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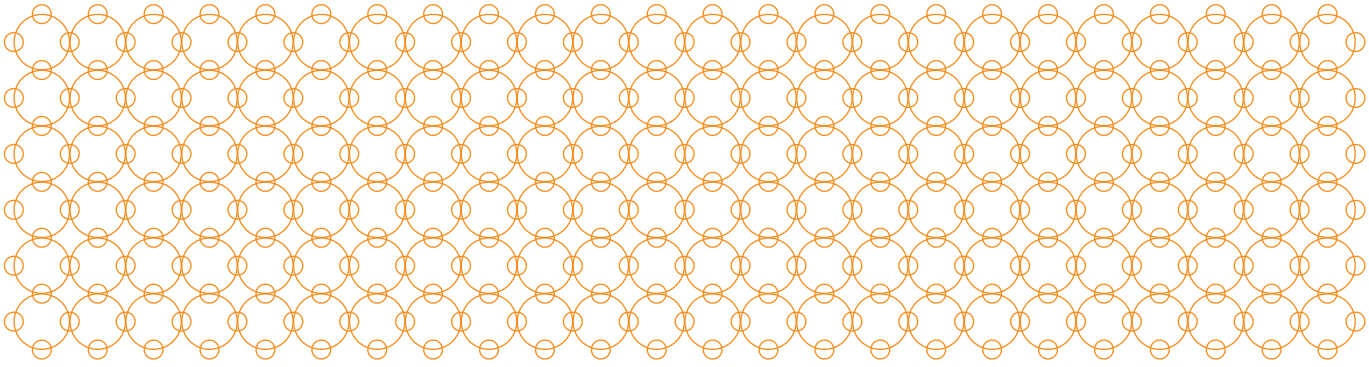

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Introduction

The Compensation Act 2006, providing for the regulation of claims management services, achieved Royal Assent on 25 July 2006. The regulatory regime, including the regulations and rules, was quickly put in place, applications for authorisation were invited from 30 November 2006, and the offence of operating without authorisation was commenced on 23 April 2007.

In August 2007 an initial assessment of the impact of regulation was published. In April 2008 a second study reviewed the impact of regulation over its first full year of operation. The approach was to take the objectives of regulation, quantified to some extent in a Baseline Study, as the starting point. The various regulatory processes were then examined. The main part of the paper made an assessment of the impact of regulation in each of the sectors subject to regulation.

This third study reviews the impact of regulation after two years. It is essentially a brief update of the one year study, but with a specific chapter on a new area – enforceability of consumer credit agreements. The author is grateful to the staff of the Claims Management Regulator, in both London and Burton-on-Trent, and to the various trade associations and individual businesses that fed in their views.

Mark Boleat

13 July 2008

1. Executive summary

Background

1. The Compensation Act 2006 provided for the regulation of claims management services in respect of personal injury, criminal injuries compensation, Industrial Injuries Disablement Benefit, employment, housing disrepair and financial products and services.

2. The Secretary of State for Justice is formally the Regulator. An established civil servant, the Head of Regulation, takes statutory decisions on behalf of the Secretary of State. Authorisation, monitoring and compliance work is handled by a Monitoring and Compliance Unit, provided by Staffordshire County Council under contract to and under the management of the Ministry of Justice.

The objectives of regulation

3. The overriding objective has been to increase the protection of consumers of claims management services. Other objectives include –

   - To tackle practices that have led to misperceptions and false expectations of compensation claims.
   - To improve the efficiency and effectiveness of the system for those who have genuine claims.

The approach

4. The approach to achieving the objectives has been

   - Understanding the market.
   - Understanding the effects of regulation.
   - Identifying how regulation can be effective, in particular "pressure points".
   - Drafting Rules of Conduct that address malpractice.
   - Devising authorisation and compliance procedures to ensure that the Rules of Conduct are complied with.
   - Working in partnership with other enforcement agencies.

The authorisation process

5. The authorisation process has continued to work well. The process has made a significant contribution to meeting the objectives of the legislation –

   - Claims management businesses realised that this was a serious regulatory regime that was likely to be enforced.
   - Deficiencies in websites and contracts were largely addressed.
   - A significant amount of information was gathered on businesses that might seek to trade without authorisation.
   - Authorised businesses that posed some risk to the achievement of the regulatory objectives were identified.

6. The number of new businesses seeking authorisation has been much higher than originally anticipated. The necessary additional resources have been provided to handle the increased work.

Renewals process

7. Authorisation certificates are issued annually. The renewal process in 2009 went smoothly as it had done the previous year. The process confirmed the high turnover of businesses in the market. 143 businesses surrendered their authorisation and at the end of June 2009 around 400 either had not returned renewal forms or had returned incomplete forms.

Monitoring and compliance

8. Monitoring and compliance work has been targeted at known problem areas. The objectives have been to prevent unauthorised activity and bring authorised businesses to compliance with the Rules of Conduct. This has been particularly successful in respect of websites and contracts. Malpractice has tended to shift to practices more difficult to detect and deal with and which are more resource intensive to handle. The authorisation of eight businesses has been suspended on grounds of malpractice. 94 businesses have had their authorisation cancelled, mainly because they have not paid the annual fee or have not complied with requests for information, but some because of malpractice. 502 reports of unauthorised trading have been investigated. Most have been satisfactorily resolved. There is no evidence of significant unauthorised trading.

Complaints handling

9. It was not anticipated that there would be a significant number of formal complaints to the Regulator, and this has proved to be the case, although the number of "informal" complaints has been much higher than anticipated.

Almost all the complaints have been in respect of financial products and services, and in any given period a small number of businesses account for a significant proportion of the total.

The claims management market

10. When regulation commenced it was anticipated that 500 businesses would seek authorisation. The number of businesses authorised has been much higher, increasing from 951 in June 2007 to 1,778 in July 2008, 2,456 in January 2009 and 2,928 at 30 May 2009. The total size of the market is quite small at under £400 million.

11. The business exists as a result of various legislative and regulatory actions which have opened the way for consumers to claim compensation, generally at little or no cost, and therefore to businesses that help them to do this. Turnover of businesses in the market is very high, reflecting the ease of entry. Many new businesses have been formed by people previously working in existing businesses. More recently, it seems that the downturn in activity in the financial services market has led mortgage brokers in particular to move into claims management.

Personal injury

12. The Baseline Study identified five principal problems – misleading advertising; improper acquisition of business; opaque contracts; cases being run for the benefit of the intermediary not the client; and fraud.

13. Misleading advertising, organised cold calling and unauthorised marketing in hospitals have largely been dealt with. However, a different type of cold calling – through call centres – has emerged which is proving difficult to deal with. And misleading advertising has been replaced by misleading information being given in sales calls.

14. Malpractice in respect of personal injury cases is now predominantly the responsibility of solicitors. Research by the SRA shows widespread non-compliance by solicitors with its rules of conduct in respect of referral fees, such that it is reviewing the rules.

Fraudulent motor accident claims

15. A number of accident management companies providing regulated claims management services have been involved in contrived accidents leading to false insurance claims, predominantly personal injury, vehicle damage and related credit hire. The Claims Management Regulator took a lead role in bringing all the various parties together to deal with this. Responsibility for co-ordination has now moved to the insurance industry and the Police. The Regulator has continued to play a valuable role in assisting other enforcement agencies.

Criminal injuries compensation

16. Criminal injuries compensation is a very small market (around £2 million a year) for claims management businesses. Some intermediaries had sought to give the impression that they are part of the official process and have also used unfair contracts. These issues were largely addressed through the authorisation process.

Industrial Injuries Disablement Benefit

17. Industrial Injuries Disablement Benefit is also a small market (around £3 million a year). Most businesses are also in the personal injury market. There has been limited malpractice, which has largely been addressed.

Employment claims

18. Claims management companies have a small role in the employment market. The main issue in this market is the quality of representation, but this is something that claims management regulation is not easily able to address. It is questionable whether there is any value is keeping this area of activity within the ambit of the Claims Management Regulator.

Housing disrepair

19. The market is very small and local in nature. In practice, local authorities have largely dealt with any problems themselves. However, claims management regulation has played its part, particularly in reducing "door knocking".

Consumer credit agreement claims

20. Over the last year a major new market – in respect of the enforceability of consumer credit agreements – has emerged. A number of businesses have argued that a high proportion of consumer credit contracts are deficient and therefore not enforceable. Some have sought to persuade consumers that their debts can be written off in exchange for a fee.

21. The collective response from the various regulators has so far not been sufficient. This partly stems from the number of regulators and other agencies involved. The succession of warnings by the Claims Management Regulator, the Office of Fair Trading and the Solicitors Regulation Authority have served a useful purpose but those engaged in serious malpractice are less likely to be influenced by warnings, but rather are influenced by enforcement action.

22. This issue needs to be tacked more urgently and to do so is likely to require significant additional resources, and in relation to the Claims Management Regulator beyond what is currently available. The SRA and the OFT both have a direct responsibility in this area. Solicitors are not only handling claims

passed on by claims management businesses but are also seeking claims directly, and the OFT has responsibility for regulating consumer credit and debt counselling and for consumer protection generally. A joint approach by these three bodies, with one clearly in the lead, accountable and providing the necessary resources, is needed.

Other financial products

23. Endowment claims were initially a large part of the claims management market. Such claims have now largely been exhausted. Reclaiming bank charges became a big market but the business remains on hold as this issue is going through the courts. Payment protection insurance has developed as a significant market given that mis-selling of single premium policies was endemic. This business is closely linked with the issue of unenforceable consumer credit agreements.

Wider issues

24. Some wider issues have emerged in the analysis of the impact of regulation. In particular, there has been some displacement of malpractice from business regulated under the Compensation Act 2006 to business that is not regulated under the Act and from overt malpractice to more subtle malpractice. Some businesses have become more astute in circumventing regulation.

25. When claims management regulation was conceived it was seen as being a minor regulatory function dealing predominantly with personal injury and endowment claims and designed to fill the gaps between other regulators. It was also seen as an interim solution pending the establishment of the Legal Services Board, the working assumption being that the Board would assume responsibility for claims management in due course. The situation that now exists is rather different from that had been envisaged, in particular the number of businesses being authorised is much higher than anticipated and most of the major problem areas are where other regulators are also involved. It will soon be necessary to review the scope and structure of regulation, including whether a significant regulatory regime can continue to be run from within a government department.

Conclusions and future work

26. The regulatory regime for claims management activities is considered to have had a significant effect in reducing malpractice in its first two years of operation. Specifically –

    - Cold calling in person has been significantly reduced. This has reduced the number of frivolous claims and helped defuse the "compensation culture".
    - Unauthorised marketing in hospitals has been largely eliminated.

- The Regulator has played a very full role in supporting the various enforcement agencies and the insurance industry in dealing with fraudulent claims relating to motor accidents.
- Malpractice by companies handling claims against the Criminal Injuries Compensation Authority has been significantly reduced, including through some companies voluntarily leaving the market.
- Misleading use of the expression "no win no fee" has largely been eliminated.
- Misleading claims on websites have been almost entirely removed and rules requiring websites to give a physical address are being complied with.
- What little malpractice there was in respect of handling endowment claims has largely been removed.
- The growth of claims handlers dealing with bank charges has been controlled, preventing significant malpractice from developing.

27. However, the nature of some of the issues has changed and some new issues have emerged. The following priorities have been identified –

- Being seen to be tougher on businesses operating without authorisation so as to be a deterrent to unauthorised operations.
- Ensuring that agency arrangements, franchise operations and the use of the exempt introducer concept are operated properly and do not become a means of circumventing regulation.
- Dealing with cold calling by call centres, including where it is alleged that consumers have consented to be called.
- Tackling abuse among businesses seeking to declare consumer credit agreements to be unenforceable.
- Identifying businesses that mislead consumers in telephone sales calls or face-to-face meetings and targeting enforcement action against them.

28. Very relevant to personal injury claims but outside the scope of the Claims Management Regulator is the need for more effective action to be taken to tackle solicitors who do not comply with the rules governing solicitors' conduct or for the rules to be changed.

30. Separately, the time is approaching when the scope and structure of the regulation need to be reviewed.

31. The following table is reproduced from the Baseline Study (April 2007), with the addition of a final column on the right summarising impact, a new row for unenforceable terms in consumer contracts and a second row of numbers in the second and third columns indicating the estimated position in June 2009. (It should be noted that the database use to record data about claims

management companies is not able to produce reliable aggregate figures so all the figures should be treated with some caution. The figures for numbers of businesses in particular are not calculated on a comparable basis.)

Market sector	No of Businesses	Estimated annual size of market	Malpractice	Prognosis	Impact June 2009
Personal injury	1,128 1,508	£190m £287m	Aggressive selling. Marketing in hospitals. Misleading contracts. Involvement in fraud.	Most difficult sector. Regulatory arbitrage and attempts to get round regulation are certain.	Marketing in hospitals, cold calling and misleading contracts largely dealt with. Arrangements in place to deal with aggressive selling and fraud.
Criminal injuries compensation	340 212	£1m £2m	Claimants deceived into thinking they are dealing with CICA.	Good.	Significant; problem largely dealt with.
Industrial injuries disablement benefit	165 102	£1m £3m	Claimants deceived into using intermediary.	Good.	Probably significant but little evidence.
Employment matters	130 153	£2m £4m	Claimants deceived into using an intermediary.	Difficulty will be identifying malpractice.	No significant impact.
Financial products and services total	176 404	£75m £65m			
Endowment mis-selling			Scare selling tactics. Clients dropped if cases difficult.	Good, but a large sector to tackle.	Significant; malpractice largely eliminated. Business sharply reduced.
Unenforceable consumer credit contracts			Misleading information at the sales stage.	Difficult to deal with because of number of regulators involved.	Misleading websites tackled but no impact on substance of problem as yet.

Market sector	No of Businesses	Estimated annual size of market	Malpractice	Prognosis	Impact June 2009
Other financial products			Claimants deceived into dealing with an intermediary.	Should be able to prevent malpractice being developed on a significant scale.	Malpractice prevented from being developed in respect of bank charges.
Housing disrepair	65 36	£1m -	Aggressive selling.	Local in nature, so problem will be to identify.	Little evidence other than "door knocking" reduced.
Total	1,256[1] 2,456	£275m £367m			

[1] Total is the total number of authorised businesses. Figures above the total shows the number of businesses active in each sector. Many businesses provide services in more than one sector.

2. Background

The need for claims management regulation

2.1 Over the last ten or so years a small industry has grown up of non-solicitor businesses that help people obtain compensation. This has been influenced by government policy initiatives – the introduction of conditional fee arrangements for personal injury cases and the requirement on insurance companies to respond in a particular way to complaints about the miss-selling of endowment policies.

2.2 Whilst solicitors are the principal providers of claims management services, the traditional culture of the legal profession, combined with the professional regulation to which solicitors are subject, allowed new entrants into the market who were subject to no regulation at all. Standards have varied from very good to very poor, but with no mechanism for excesses at the poor end of the scale to be addressed.

The Compensation Act 2006

2.4 The Compensation Act 2006 became law on 25 July 2006. The Act and subsequent secondary legislation provide for the following activities to be subject to regulation –

- advertising for, or otherwise seeking out (for example, by canvassing or direct marketing), persons who may have a cause of action;
- advising persons on the merits or handling of causes of action;
- making representations on behalf of claimants;
- referring details of potential claims or potential claimants to other persons, including persons having the right to conduct litigation;
- investigating, or commissioning the investigation of, the circumstances of, the merits of, or the foundations for, potential claims, with a view to the use of the results in pursuing the claim.

2.5 Claims in respect of the following are covered –

- personal injuries;
- criminal injuries compensation;
- Industrial Injuries Disablement Benefit;
- employment;
- housing disrepair;
- financial products and services.

2.6 A number of businesses are exempt from the need to be authorised under the Act –

- lawyers regulated in respect of claims management services by their respective regulators;
- independent trade unions;
- insurance companies, insurance brokers and IFAs providing a claims management service that is regulated under the Financial Services and Markets Act 2000;
- charities and advice agencies providing a service free of charge;
- certain very small scale introducers although they need to comply with the rules on advertising, marketing and soliciting business.

The regulatory structure

2.7 The time period from drafting the legislation to Royal Assent was very short. At the time the legislation was drafted no decision had been taken as to the regulatory structure. The legislation accordingly allowed any option. The Secretary of State could establish a new regulatory body, designate an existing regulatory body to be the regulator or be the regulator himself. This direct regulation option was selected.

2.8 An established civil servant in the Ministry of Justice takes decisions on behalf of the Secretary of State. Monitoring and compliance is outsourced to Staffordshire County Council. A non-statutory Regulatory Consultative Group, comprising representatives of relevant major stakeholders including claims management businesses, other regulators, trade associations and consumer organisations, acts as a sounding board for the Regulator and as a forum for discussion.

The objectives of regulation

2.9 The objectives of regulation were set out in the Regulatory Impact Assessment for the Compensation Bill –

"This proposal aims to provide better safeguards for consumers of claims management services. It is designed to encourage the provision of quality services, to enhance consumer protection and to provide consumers with a clear route to redress. In particular, the proposal aims to improve the effectiveness and efficiency of the system for those who have a genuine claim to compensation, and to tackle practices that have helped to spread the misperceptions and false expectations of compensation claims amongst consumers. This will help to build consumer confidence and promote effective competition within the sector, whilst ensuring that the sector will be able to contribute effectively to the widening of access to justice."

3. The approach

3.1 Success in any field depends on having the right strategy. The success of claims management regulation depends largely on the work done between June and October 2006 in developing the structure and the secondary legislation, writing the rules and planning enforcement.

3.2 The approach can be summarised as follows –

- Gaining as comprehensive as possible understanding of the market.
- Understanding the effects of regulation, in particular the risks of businesses reorganising their activities to circumvent the effects of regulation.
- Identifying how regulation can be effective, in particular "pressure points" through which regulation can most effectively be targeted,
- Drawing up Rules of Conduct which are very brief but which deal specifically with malpractice in the market for claims management services.
- Vigorous enforcement of the Rules of Conduct.
- Working in partnership with other regulators.

3.3 Different approaches have been needed for different markets.

3.4 Impact can be measured only if there is an assessment of malpractice prior to regulation. Such a baseline study was duly completed and published on the website in April 2007. The Executive Summary of that study is reproduced in the Appendix.

4. The authorisation process

4.1. The authorisation process has always been seen as a key part of the overall regulatory regime. It is, in itself, able to help ensure compliance with the various rules. A separate review of the initial authorisation process (dated 24 May 2007) has been published on the claims management regulation website.

4.2 The overall conclusion was that the process was very successful. The application form and authorisation process both worked well. There were no significant problems with the form or the technology. Feedback from applicants indicated broad satisfaction with the arrangements by businesses.

4.3 The process made a significant contribution to meeting the objectives of the legislation –

- Claims management businesses realised that this was a serious regulatory regime that was likely to be enforced.
- Major deficiencies in websites and contracts were addressed. In itself this meant that much of the malpractice in respect of endowment miss-selling had been addressed.
- A significant amount of information had been gathered on businesses that might seek to trade without authorisation.
- Authorised businesses that posed some risk have been identified.

4.4 The process gave the necessary platform on which monitoring and compliance work can be effective.

4.5 When regulation was introduced it was anticipated that authorisation would be a one-off event, the initial surge being followed by a relatively small number of businesses seeking authorisation subsequently. In the event this has proved not to be the case. Rather, there has been a steady stream of new businesses seeking authorisation – up to 100 a month. This has had significant resource implications, although these have been manageable as the regulatory structure was deliberately scalable and as the authorisation fees cover the costs. However, the combination of a continued unexpectedly high number of businesses seeking authorisation with all renewal certificates being at the same time has proved challenging, and some resources have had to be diverted from monitoring and compliance work. Steps have now been taken to provide a dedicated resource to handle authorisations.

5. The renewal process

5.1 All certificates of authorisation run to a particular date, 28 February in the first two years and 31 March subsequently.

5.2 One of the benefits of having a single date is to enable the Regulator to collect aggregate data on activity in the market and therefore to be able to assess the changing nature of the market.

5.3 From a compliance point of view the renewal process can be used to get the same message over to all authorised businesses at the same time about the need to comply with the Rules of Conduct. A single date also reduces the opportunities for restructuring of businesses to circumvent regulatory requirements.

5.4 The downside of a single date is that the fairly routine work of handling the renewals is heavily concentrated at a particular point of time. It follows that there is a risk that work may slip in other important areas, in particular enforcement.

5.5 The approach to the renewals process was to make it part of compliance work. The form required businesses to confirm the key details that they had supplied in their application form and also to confirm that they complied with the Rules of Conduct. This was seen as being a useful part of the overall compliance programme.

5.6 Recognising that many renewal forms would come in at the last minute, the appropriate arrangements have been made to ensure that the volume of business could be adequately handled partly by staff working overtime and partly by diverting some resources from enforcement work.

5.7 The process went smoothly in 2008, and the experience gained was used to refine the process for 2009, when, again, the renewal process went well although there were some minor delays in dealing with renewal applications.

5.8 The following table sets out key details from the process as at 4 July 2009.

Number of businesses issued renewal notices	2,441
Number of renewal notices returned	2,053
Of which voluntary surrenders of authorisation	143
Of which forms incomplete or not processed	158
Number of forms not yet received	246
Renewal completed	1,503

5.9 143 businesses have voluntarily surrendered their authorisation. It is probable that many of the 400 or so businesses whose forms have not been received or which are incomplete have ceased providing regulated claims management services.

5.10 As in 2008 there was large-scale non-compliance with the requirement to notify changes in information provided on applications forms, for example about the directors of the business. This is not surprising; other regulators have a similar experience. The renewal process is essential in order to keep information up to date.

6. Monitoring and compliance

6.1 The monitoring and compliance strategy has comprised several related elements –

- Use of the authorisation process to draw the attention of businesses to the Rules of Conduct, in particular to help achieve compliance with the rules on marketing.
- Use of the renewals process to remind businesses of the Rules of Conduct and to establish any changes in the ownership or management of the business.
- Vigorous pursuit of businesses thought to be trading while unauthorised.
- Use of complaints and public queries to inform targeting of particular businesses.
- Regular reviews of website and contracts.
- Targeted audits and requests for information on businesses where there is some evidence of malpractice.
- Use of enforcement powers where necessary, but a preference for stopping malpractice and bringing businesses to compliance.

Authorisation and renewals processes

6.2 The authorisation and renewals processes have already been analysed in previous chapters. The authorisation process played a key role in increasing awareness of the regulatory regime and ensuring that websites and other marketing literature were compliant. The renewals process reinforced these.

6.3 Eight businesses were formally refused authorisation, because of previous criminal activity, involvement of an undeclared individual and previous conduct. However, this does not tell nearly the whole story. 304 businesses submitted applications for authorisation, including a cheque for the authorisation fee, but failed to respond adequately to requests for information, and their applications have been terminated. Little is known about these businesses. However, it is reasonable to assume that many thought that authorisation could be obtained simply by filling in a form and sending a cheque. When they discovered that information they provided was carefully checked, websites examined, Companies House checks done etc some may have realised that they would not be authorised or that they would be unable to continue operating as they had done. Accordingly, they decided not to proceed with authorisation. To this extent the authorisation process was successful if removing from the market some businesses that otherwise would have been involved in malpractice.

6.4 However, it is equally reasonable to assume that some of the people behind the businesses whose applications were terminated are either now involved in authorised businesses or are trading while unauthorised. The monitoring work seeks to identify where this has occurred.

Unauthorised trading

6.5 In this area, unlike many others, unauthorised trading is fairly easy to identify. This is because the person to whom claims management businesses are making a claim has an interest in ensuring that they are authorised. In respect of financial services and products, the insurance companies and banks have played a useful role by refusing to deal with and reporting unauthorised businesses. In respect of personal injury cases solicitors have been warned that they must not deal with unauthorised or non-exempt businesses.

6.6 The Monitoring and Compliance Unit has received a steady stream of reports of unauthorised trading. It has also monitored websites and local advertising. A total of 502 businesses have been identified as potentially trading unauthorised. Each of these businesses has been approached with the following results as at June 2009 –

369 were not trading unauthorised, of which 99 were authorised, 191 were no longer trading and 79 were exempt.

Of the remaining 133, 113 had not been confirmed and the 20 that had been confirmed were being pursued.

There is a regular flow of reports of unauthorised trading all of which are investigated and go through one or more of the stages identified as above. On average there are about 50 reports a month of businesses alleged to be trading without authorisation. There is no evidence of significant extended trading without authorisation, partly for the reasons set out in paragraph 6.5.

6.7 It is relevant to note that a number of stakeholders said that they had evidence of businesses trading without authorisation for an extended period of time despite this being reported to the Regulator and that such businesses subsequently obtained authorisation. If this has been happening then it undermines the Regulator, both with the businesses that are permitted to "get away with it" and with the businesses that receive claims. While it is in order to take a lenient approach with a business that legitimately did not know it had to be authorised, knowingly trading without authorisation should be automatic grounds for refusal of authorisation. The evidence in facts suggests that there is no significant issue in this respect. This points to the need for the Regulator to communicate effectively with those who make reports of unauthorised trading.

6.8 When regulation was introduced it was recognised that it would not be appropriate to require very small introducers to obtain authorisation. The concept of an exempt introducer was formulated to cover businesses that

introduced fewer than 25 cases a quarter where this was incidental to the mainstream business of the introducer. The concept was not perfect but was seen as the best solution to a difficult problem. There is scope for the concept to be abused, either because the introducing is not incidental to mainstream business or because the 25 a quarter rule is circumvented by referrals being made to a number of solicitors. Policing this area is inevitably difficult. Some industry sources suggest that the concept is indeed being abused. This rather ties in with the policing of the solicitors' rules of conduct, in particular in respect of disclosure of referral fees. While there is probably little consumer detriment resulting from the present position it is unsatisfactory if there is widespread abuse of the concept. This needs to be reviewed and the appropriate action taken, either through a change in the rules or through enforcement of the existing rules.

Review of contracts

6.9 As part of the authorisation process, businesses where there was cause for concern were asked to provide their contracts. Significant changes were required before some of the businesses could be authorised. It would not have been feasible to review all contracts at this stage because of the resource implications. Rather, separate exercises were undertaken after the authorisation process had largely been completed. These are covered in the sector chapters.

Review of websites

6.10 Following the initial review of websites as part of the authorisation process, subsequent checks have been made to ensure that sites remain compliant. The checks have covered the Rules of Conduct, in particular use of the expression "no win no fee", and also the Electronic Commerce Regulations and requirements made in regulations under the Companies Act 2006. Generally, websites of authorised businesses are compliant – far more so than those of businesses in other sectors. In late 2008 a review of websites found 192 that were not compliant. 52 of these have been closed down and the remainder brought to compliance. The deficiencies were generally of a minor nature. Policing of websites has meant that malpractice has tended to shift towards areas that are more difficult to monitor, in particular sales calls and face-to-face contact. As a general rule businesses that have had websites that have been significantly misleading should be identified as high risk and closely monitored. If a business chooses to put misleading information on a website, only removing it under regulatory pressure, it is very likely to provide misleading information in other ways.

Audits

6.11 Audits are carried out whether there are concerns about the way a business may conduct itself. These may arise during the authorisation process or as a result of complaints or intelligence received from partner agencies.

Prosecutions

6.12 In practice the only grounds for prosecution are that a business has been trading without authorisation. No business has been prosecuted. Outsiders tend to see prosecutions and refusal of authorisation as signs of the effectiveness of a regulator. This is inappropriate. As the chapter on the authorisation procedure showed, the procedure itself weeds out businesses that, if authorised, would engage in malpractice. Businesses that are likely to be refused authorisation know this and rather risk having the status of formally being refused allow their application to lapse. The claims management market is such that a business that is not authorised will find it difficult to do a substantial amount of business. Prosecution is very expensive for any regulator, particularly a small regulator like the Claims Management Regulator, and generally cannot be justified.

7. Complaints handling

7.1 Authorised businesses are required to comply with rules on complaints handling. These rules include referring a complaint to the Claims Management Regulator. The Regulator has limited powers in dealing with complaints, and does not act in the same way as an Ombudsman, able to impose a settlement if certain requirements have not been complied with. The Regulator does have the power to require fees to be repaid if they have been unjustifiably charged and can require the authorised business to reconsider the complaint. In practice however, where a Regulator does deal with complaints in this way then normally businesses respond favourably.

7.2 It was not envisaged that there would be many formal complaints. In respect of personal injury cases the client is very seldom paying any money to a claims management company and has no contract with the company and therefore is unlikely to have any grounds for complaint. It was considered that complaints were most likely in respect of financial services and products, where clients were paying a significant proportion, generally 25% or 30%, of any compensation to a claims company.

7.3 There has in fact been a relatively high number of complaints although only a handful reached the stage of formal referral to the Regulator. In 2008/09 2,634 complaints were received, 90% of which were in respect of financial products and services.

7.4 70% of the complaints came under the heading of "fair and reasonable dealings with clients", and typically concerned matters such as a company claiming a fee when it had done little work; a client being misled into dealing with a company; difficulty in contacting a company; and information given to clients in telephone calls or face to face meetings being different from what was stated in marketing literature or contracts.

7.5 There has been a general trend for a small number of companies to account for a high proportion of complaints at any one time. These companies are dealt with in various ways. Some ceased trading either voluntarily or because their authorisation has been suspended while others have changed their policies and practice such that the number of complaints has dropped. Being at the top of the "complaints league" is automatically a trigger for more general scrutiny of the business.

8. The Claims Management Market

8.1 This chapter sets out the key statistics about businesses regulated under the Compensation Act 2006 and, therefore, also on the nature of the claims management market.

8.2 The regulatory impact assessment for the Compensation Bill, published in November 2005, noted that there were no exact figures on the number of claims management companies operating in the claims management market but quoted the Claims Standards Council is estimating that there were about 400 companies in 2005. The regulatory impact assessment based its calculations on the new regulatory authority regulating about 500 companies. In the event, the number has proved to be much higher than this and has also continued to grow rapidly.

8.3 Table 8.1 shows key statistics for the claims management market.

Table 8.1 Size of the claims management market

Sector	June 2007		June 2009	
	Number of businesses	Turnover £m	Number of businesses	Turnover £m
Personal injury	1,128	190	1,508	287
Criminal injuries	340	1	212	2
Industrial injuries	165	1	102	3
Employment	130	2	153	4
Finance	176	75	404	65
Housing disrepair	65	1	36	-
Total	**1,656**	**275**	**2,456**	**382**

Notes:

1. The figures for numbers are taken from two different sources and are not strictly comparable.
2. The amount figures are the turnover in the particular sector in the year to September 2006 in respect of the third column and September 2008 in respect of the final column.

8.4 The figures should be treated with considerable caution, in particular changes between the two years. Information on turnover provided on application forms and renewal forms is of questionable accuracy, and there is no way of checking it. The turnover figures include actual figures for businesses that have been trading and estimated figures in the year in question or the following year in respect of business that are newly authorised. To this extent the turnover figures overstate the size of the market. The table purports to do no more that give approximate orders of magnitude.

8.5 The total size of the market is quite small, at under £400 million in the year to September 2008. The table also shows that business is heavily concentrated in just two sectors, personal injury and financial products and services. The table suggests a substantial increase in the size of the personal injury market, both in respect of the number of businesses and turnover. This probably reflects a number of factors including a steady increase in referral fees and businesses that previously operated as exempt introducers (with or without justification) becoming authorised. The more interesting statistics are in respect of financial services and products. The reduction in turnover is probably correct and reflects the running down of endowment claims business. The increase in the number of businesses reflects activity in the bank charges and consumer credit agreement markets where as yet the substantial amount of marketing has not been transformed into actual business.

8.6 That the number of businesses has been much higher than had been anticipated and that there has been a steady growth merits attention. The number of businesses actually authorised increased steadily from 951 in June 2007 to 1,778 in July 2008, 2,456 in January 2009 and 2,928 at 30 May 2009. The trend in the number of new business authorised is shown in Table 8.2.

Table 8.2 Number of businesses authorised

Period	Personal Injury	Financial Services	Total
2007 Q1	394	89	428
2007 Q2	660	216	830
2007 Q3	219	131	326
2007 Q4	122	36	146
2008 Q1	133	45	159
2008 Q2	136	53	167
2008 Q3	209	121	285
2008 Q4	260	220	398
2009 Q1	184	135	285
2009 Q1	299	220	445

Note:
The total figure is the number of businesses authorised. The figures in the second and third columns are the numbers that said that they intended to operate in the respective markets. The total column is not equal to the sum of the second and third columns because some businesses said they intended to operate in both markets and some also intended to operate only in one of the other markets, particular employment claims.

8.7 The market for claims management services exists largely because of legislation and regulation that creates the possibility of compensation and, therefore, the demand for services to assist people entitled to compensation. In brief –

- The market for personal injury claims exists because of conditional fee arrangements which allow people to bring a claim at little or no cost to themselves.
- The market for endowment claims exists because the Financial Services Authority requires businesses that have sold endowment policies to investigate complaints they receive in a specified manner.
- The market for compensation in respect of bank charges exists because of regulatory action by the Office of Fair Trading and the Financial Services Authority.
- The market for claims in respect of consumer credit contracts exists because of the wording of the Consumer Credit Act 1974 and the dispute resolution rules of the FSA.

8.8 Entry into the financial services is easy and low-cost and there is the potential for substantial profits to be made simply through writing one or more standard letters to a party that may be liable to provide compensation, and entry into the personal injury sector is easy through just introducing claims. The product offered by the claims management companies is popular with the public who generally perceive that they are getting something for nothing. Claims management regulation has probably given a boost to the market by giving official recognition to businesses providing claims management services, which can be used for marketing.

8.9 It is necessary to analyse why there has been such a rapid increase in the number of businesses seeking authorisation which, by definition, must be new businesses in the market. The general expectation had been that after the initial surge of businesses wanting to be authorised when regulation came in, there would be relatively few new businesses seeking authorisation. The Regulator considers that a number of factors have played their part –

- Particularly in respect of personal injury it seems that businesses grow and when they reach a certain size some of the people involved in the business split off to run their own business. Many of the businesses involve family members and there may well be support from a business being newly established for the business with which those concerned with the new business were previously working. The VAT threshold may play some part in encouraging the fragmentation of business.
- When new opportunities such as Consumer Credit Agreements are seen to arise it is very easy for businesses to get into this market.

- Businesses in related markets see claims management as a useful additional market to get into and in some cases it has proved more profitable than their mainstream market. The downturn in the housing market may have accentuated this trend by encouraging mortgage brokers in particular to become claims management companies.
- Some people who have lost their jobs in the recession have seen claims management as a good business opportunity.

8.10 It is worth quoting the 2008/09 report of the Chief Ombudsman of the Financial Ombudsman Service on this point.

"One of the significant drivers of consumer complaints is the now substantially increased number and activity of claims-management companies, encouraging disadvantaged consumers to complain. The Ministry of Justice reports that it has authorised over 900 of these companies to trade in the areas of financial products and services. And apparently the number of companies applying for authorisation has been growing rapidly during the past year. No figures are available for the number of complaints these companies have made on behalf of their clients – or the extent to which the companies have given their clients appropriate advice.

The vast majority of claims-management companies operate in well-trodden territory where consumer detriment has been already identified. So they are a symptom of the problem and not its cause.

Consumers can make a complaint direct to a business – or to the ombudsman service – free of charge. If they make their complaint through a claims-management company, on the other hand, that company will charge a fee – usually a percentage of any compensation awarded. These fees have been criticised as being disproportionate – especially in relation to the effort or expertise that some claims management companies actually deploy. So it is questionable what advantage consumers gain by using such companies.

But it is also undeniable that the marketing activities of claims-management companies have succeeded in identifying a very large number of consumers who have suffered loss. And this has resulted in many people being paid redress when they would otherwise have received nothing. Indeed, over half of the complaints we received during the year about payment-protection insurance (PPI) were brought to us on behalf of consumers by claims-management companies. And, as we report in this annual review, we upheld a very high proportion of these cases. So it is clear that the wider system is not working as it should."

8.11 There would be no claims management businesses if there were no grounds for compensation. A primary reason for the industry existing is that there are grounds for compensation and that many of those who are liable for compensation will not, of their own accord, seek out those who are entitled to compensation and pay it. Now that the industry has been firmly

established, and given some official recognition by the Compensation Act 2006, it must be anticipated that the business will continue to grow as long as the current arrangements for conditional fee arrangements are maintained in respect of personal injury and in the financial services sector if financial companies continue not to comply with legislation and regulation thus opening the way for compensation claims.

9. Personal injury

9.1 Personal injury is by far the largest sector being regulated. Over 1,500 businesses are in this market and the estimated annual size of the market is nearly £300 million. The baseline study identified five main types of malpractice in respect of personal injury cases –

- Misleading advertising, in particular suggestions that making a claim was easy and that large amounts of compensation could be obtained quickly. The expression "no win no fee" has been used without the necessary qualifications rather too often. More generally, many websites of claims management businesses failed to comply with legal requirements governing electronic commerce generally.
- Improper acquisition of business through aggressive marketing techniques and misuse of personal information. At its worst this included cold calling on the high street, on the doorstep and in hospitals. However, it could also include an insurance broker, a garage or an accident management company pressurizing a client to make a claim.
- Opaque contracts that concealed the nature of the arrangement between a client and claims management business and possibly also concealed costs that had to be paid. Contractual relationships may include an ATE policy and a loan taken out to finance the purchase of the policy (although this is now unusual), the business making its money through selling cases to solicitors and other fees. The contractual terms may well not be transparent.
- Cases being run for the benefit of intermediaries not the client. "No win no fee" was often not adequately qualified. Also significant was the "win but little compensation" scenario in which a claimant won compensation but most of it was taken away in costs leaving the claimant with a small amount that does not make running the claim worthwhile.
- Outright fraud, particularly as a result of contrived accidents.

9.2 As the previous chapter noted the market seems to have increased significantly in size over the past two years, both in respect of the number of businesses and the turnover of those businesses. Some useful research that helps to explain this trend is in the report by Oxera Consulting Ltd Marketing costs for personally injury claims (ABI Research Paper 15, 2009) -

"The final dynamic in the market is competition between solicitors for a relatively stable supply of PI work from referral companies. Referral fees have indeed increased over time. Evidence suggests that the payment of explicit referral fees began in 1999, at a level of approximately £50 per referral. For some BTE referral companies, this explicit referral fee was paid in addition to

the solicitor accepting a number of unprofitable, non-injury, cases for every PI case referred. As the business model of such referral companies altered, and the non-injury cases were handled in-house, referral fees for the PI cases rose quickly to around £250. By 2006, fees of approximately £600 were considered typical and, more recently, fees of £850–£1,000 were considered not uncommon."

However, the Oxera analysis is not universally accepted. Some claims management businesses suggest that £600 is a typical fee for a lead while the fee for a case in a form that a solicitor can pursue is likely to be over £1,000.

9.3 Oxera went on to analyse the factors behind this increase –

"This section concludes that legal fees charged by claimants' solicitors are not subject to sufficient market constraints; therefore, the expenses incurred in marketing are not constrained by the claimant's willingness to pay. Within this structure, referral fees paid by solicitors (or the level of marketing costs they are willing to incur in-house) are likely to be the residual between the costs of actually executing the case and the costs that can be recovered via the administrative procedure from the defendants.

Both theory and practice indicate that, under the prevailing system, marketing costs will expand to take up the difference between the costs incurred by solicitors in actually executing the case and the costs they can recover. This is likely to induce a higher level of marketing spend than what would be observed in competitive markets where prices and costs are subject to a market constraint."

Misleading advertising

9.4 The problem of misleading advertising was largely dealt with in the authorisation process. In practice there has been little misleading national media advertising as such advertising is well controlled by the Advertising Standards Authority (ASA).

Cold calling in person

9.5 This area has been a high priority and a large amount of resources have been employed to achieve an impact on the market. Last year's report noted that this had been largely successful and that almost all the larger businesses engaged in cold calling have ceased this activity as a result of enforcement activity. Small scale localised cold calling continues and is dealt with although it can never be fully eradicated.

Unauthorised marketing in hospitals

9.6 This was identified as a specific problem in the Baseline Study. It has included placing thousands of leaflets, some containing the NHS logo, in hospitals

without authority, and sometimes face-to-face marketing as well. The activity has been a significant nuisance to hospitals. Again the issue has been successfully dealt with.

Clients being pressurised to make a claim

9.7 This malpractice is very difficult to identify; it is likely to come to light only through complaints. The scale of malpractice is not known but is probably modest.

New issues

9.8 It is no surprise that as some malpractice has been removed so those businesses that seek to gain advantage by engaging in malpractice seek other means of doing so. Regulation typically leads to some displacement of malpractice as well the removal of some. In the personal injury market there is evidence of this, much of the analysis also applying to companies in the financial services market.

9.9 Overt misleading advertising and inappropriate marketing have largely been stopped. Websites are largely compliant (and much more compliant than in most other comparable sectors), there is no organised cold calling in person, contracts are compliant and unauthorised marketing in hospitals has ceased.

9.10 There is now a different cold calling problem. Marketing companies use call centres to farm personal injury claims. This is often on the back of a lifestyle questionnaire which people may be paid to complete. After a number of fairly innocent questions, towards the end of the questionnaire may come questions such as "have you had a personal injury in the last three years" followed by "would it be helpful for a solicitor to contact you to help you get compensation". The cases are then sold to claims companies or directly to solicitors. This sort of issue is more difficult to tackle as there is scope for argument as to whether the practice is contrary to the rules and if so who is conducting the business.

9.11 Similarly, overt misleading advertising has been replaced by misleading information given in sales calls in response to advertising, which is far more difficult to monitor. Even where there is a complaint it is often difficult to substantiate. A programme of mystery shopping targeting at businesses suspected of using such tactics is the appropriate regulatory action, but this has significant resource implications.

9.12 The following chapter deals with contrived and induced accidents. Claims management businesses engaged in such activity have typically made only a relatively small part of their profits from personal injury claims, a higher proportion coming from vehicle damage and replacement vehicle hire. If those companies perceive being regulated under the Compensation Act as

increasing the likelihood of regulatory action against them (as is probably the case) a natural reaction is to hive off personal injury business to a separate business with no overt links to the original business. While there is no definite proof that this has occurred it is very likely.

9.13 Almost all personal injury claims are handled by solicitors who under their own rules of conduct have to ensure that cases introduced by intermediaries have not been obtained by means which if practised by a solicitor would be contrary to the rules of conduct. If this had been effective then separate regulation of claims management businesses would not be necessary. To the extent that claims management regulation is more successful than the regulation of solicitors one would expect malpractice to shift from claims management companies to solicitors. The first year impact study concluded that "to the extent that there are problems in respect of the handling of personal injury claims these are now largely problems caused not by claims management companies but rather by solicitors." There is no reason to change this conclusion.

9.14 There is a wider issue here. Referral fees paid by solicitors have been a contentious issue for many years. However, the real issue is not referral fees but rather the fact that market conditions allow very high marketing costs - whether referral fees paid to a third party or direct marketing costs incurred by solicitors, individually or in joint arrangements. There are comprehensive rules governing referral fees, but these are widely ignored.

9.15 The appendix to this chapter sets out in more detail the position in respect of solicitors.

Appendix
Personal Injury – Solicitors

A.1 The large majority of personal injury claims are eventually handled by solicitors and therefore any analysis of the impact of regulation has to cover the role of solicitors.

A.2 The Rules under which solicitors operate explicitly cover referrals from introducers. Broadly speaking the relevant rule (Rule 9) requires the solicitor –

- to ensure that any introducers comply with the rules relating to obtaining business that apply to solicitors generally;
- to disclose any referral fee paid to the client; and
- to be satisfied that the introducer also discloses the referral fee to the client; has not acquired the client as a consequence of activities which if done by a solicitor would breach the Rules Governing Solicitors' Conduct and does not influence or constrain the solicitor's professional judgment in relation to the advice given to the client.

A.3 The monitoring work carries out by the Solicitors Regulation Authority has consistently shown significant non-compliance with the Rule. Most recently, in December 2008 the Board of the Solicitors Regulation Authority considered a report from its Rules and Ethics Committee which included the results of monitoring of solicitors in respect of their compliance with the rules on referral fees. 146 firms had been visited since September 2007. This report showed substantial non-compliance with the rules. 34% were in breach of the rule on all agreements being in writing, 59% in respect of failure to obtain an undertaking from introducers that they would comply with the rules, 52% in respect of failure to put in place satisfactory arrangements to ensure that introducers provide the client with all relevant information, 66% in respect of not providing a statement that the solicitors' advice is independent and 66% on the firm failing to comply with the requirement that information disclosed to the client will not be disclosed without the client's consent. The conclusion in the report was that –

"of the 146 firms visited in the above analysis, PSU considered that there was evidence of a breach in respect of at least one of the nine rules identified above in 134 of the firms (91.8%). Of these 146 firms, 35 visits were due to a random visit selection and there was evidence of a breach in respect of at least one of the nine rules identified above in thirty-three of the firms (94.3%)."

A.4 The report to the SRA Board noted that although the level of breaches of Rule 9 was high, only a small number appeared to involve potentially serious misconduct. The report also noted that it appeared that in the majority of cases, clients' interests were not being harmed by the breaches that

were currently being found. The report considered a number of options for improving compliance with the Rule. It also suggested that in view of the continuing high level of breaches of Rule 9 the Board might wish to consider a more fundamental review of the Rule. One possible approach was simply to replace the Rule with a much simpler rule that required solicitors to act in accordance with their core duties when entering into referral arrangements, removing all the detailed requirements, for example that the agreement should be in writing and in respect of referral fees.

A.5 In terms of the issues the Board agreed with the Committee's analysis.

"The question of harm was key. If breaches of Rule 9 did not directly and seriously damage client interests, it was arguably proportionate to take a commensurately relaxed view of enforcement and/or to review the rule itself to moderate or remove the requirements that were being breached. On the other hand, if there was a risk to clients and harm to the public interest resulting from the failure of a large part of the profession to comply with the rule's reasonable requirements, especially in areas such as transparency and disclosure, more vigorous enforcement action would be required."

A.6 The Board resolved –

1. To ask the Rules & Ethics Committee to review in the light of the Board's discussion what, if any, changes (including those referred to in the paper) need to be made to Rule 9, including consideration of the relationship between Rule 9 and Rule 1.

2. To refer to Rules & Ethics Committee the continued prohibition on arrangements with introducers that charge contingency fees for them to consider in the light of the Civil Justice Council review.

3. To authorise the development of a further compliance, enforcement and communications strategy in consultation with the Compliance Committee.

A.7 The position is unsatisfactory for the Claims Management Regulator, whose rules require that businesses must not act in a way that puts a solicitor in breach of the rules governing solicitors conduct. If the SRA cannot or will not enforce its rules then the Claims Management Regulator cannot be expected to enforce them in respect of introducers.

10. Fraudulent motor accident claims

10.1 The first year impact report included a very full section on this issue. It noted that fraudulent personal injury claims had not been on the agenda when claims management regulation was devised. However, once the nature of the problem became evident, the Claims Management Regulator had taken the lead in bringing together the various enforcement agencies, regulators and industry bodies with an interest in the subject and it facilitated the development of a strategy to deal with the problem.

10.2 The Claims Management Regulator cannot be the lead agency in this area. Fraudulent insurance claims are a matter primarily for the Police and the insurance industry. The role of the Claims Management Regulator should be to work cooperatively with the Police in particular, and also the Solicitors Regulation Authority, to take firm action against authorised businesses engaged in fraudulent activity. Such is the nature of Police operations that sometimes the Regulator will not take immediate action against a claims management business for fear of upsetting a major Police operation aimed at getting to those behind significant criminal organisations.

10.3 It was never appropriate for the Claims Management Regulator to maintain the coordinating role on this important matter. During the course of 2008 the lead responsibility moved to the insurance industry through the Insurance Fraud Bureau. The Claims Management Regulator continues to play an important role supporting other agencies wherever it can. Significant developments during the year included improved information sharing with the SRA and the signing of memoranda of understanding with a number of police forces and the Insurance Fraud Bureau.

10.4 However, it is appropriate to note here the difficulty in dealing with this problem which involves organised crime, in some cases on a very large scale, operating throughout the country committing a series of different types of fraud closely connected with more direct criminal activity. This is an area in which many Police forces, the Serious and Organised Crime Agency, the Claims Management Regulator, the Solicitors Regulation Authority and the insurance industry all have a legitimate interest and role to play. However, such is the nature of law enforcement in Britain, that there is no clear lead agency. The informal coordination and cooperation that takes place, welcome though it is, is not adequate to deal with this organised criminal activity. As an example, the Claims Management regulator is unable to access the Police National Computer as a matter of course and therefore is restricted on the checks that it can do on people involved in claims management businesses.

11. Criminal Injuries Compensation

11.1 The Criminal Injuries Compensation Authority (CICA) pays out about £200 million a year. Claims management companies have a small part of the market, with a turnover of around £3 million a year. Specific areas of malpractice in this sector, largely relating to businesses claiming to have a connection with or even be part of the CICA, were largely eliminated in the first year of regulation. This was comparatively easy because every case is considered by the CICA, which can both monitor that businesses are authorised and that the Rules of Conduct are being complied with.

11.2 Almost all businesses operating in this sector are also in the personal injury sector so there are no specific monitoring and compliance activities specific to this sector.

12. Industrial Injuries Disablement Benefit

12.1 This sector is similar in some respects to criminal injuries. Again, there is a single recipient of claims, this time the Department for Work and Pensions, which pays out about £800 million a year. The claims management business is small scale with turnover of about £3 million.

12.2 Most, if not all, of the businesses in this sector also handle personal injury claims and therefore have been subject to the strategy for that sector. In addition, the DWP has been asked to refer to the Regulator examples of businesses not complying with the rules.

13. Employment claims

13.1 Employment compensation claims are different from all of the other claims covered by the Claims Management Regulator. There is a considerable overlap of the businesses engaged in all of the other markets, even in seemingly diverse markets such as personal injury and bank charge, endowment or consumer credit claims. By contrast, the businesses involved in representing claimants in employment cases are not involved in any of the other markets. It is also a very small market with about 150 businesses being authorised and total turnover being no more £4 million a year.

13.2 In practice, this sector has received little attention from the Claims Management Regulator, mainly because the major problem areas have been in other sectors. Contracts were examined, and generally found to be better than in other sectors. However, there is an unsatisfactory position, a view held by employment judges. People appearing before employment tribunals are entitled to be represented by anyone they choose, and quite properly the employment judges have no wish to fetter the rights of people to be represented. It follows that if a claimant is represented by an unauthorised claims management business, which is committing an offence under the Compensation Act, then they cannot be preventing from acting by the judge.

13.3 Some claims management businesses, particularly those not authorised, provide a very poor quality of service which is causing problems for the tribunals in managing their case-loads. The issues are not those of misrepresentation or poor contracts, but rather simply a poor quality of work. This is more difficult for the Claims Management Regulator to tackle than other issues, partly because of lack of resources and also because there are no requirements in respect of training and competency. Also, as far as the tribunals are concerned, they have as much, if not more, of a problem with the quality of representation of defendants (often very small businesses) as they do with the quality of representation of claimants.

13.4 Generally, employment judges conclude that there has been no significant impact of regulation, although it is probably the case that at the margin the performance of some businesses has been improved by the actions of the Regulator. If there is to be a significant impact on poor quality representation, then this would probably require competency tests, which would take years to establish and also more resources being devoted by the Regulator. Generally, this is an area where the present position is not tenable in the long term. The options are to remove the area from the scope of regulation or to devote substantially more resources to it either as a standalone activity on the part of the Claims Management Regulator or through another regulatory mechanism.

14. Housing disrepair

14.1 The market is small and local in nature with just 36 businesses operating and turnover of under £1 million. Malpractice, mainly cold calling, has been addressed in the same way as for personal injury business.

14.2 In practice, local authorities have largely dealt with the problem themselves, by rigorous scrutiny of claims so that they are not seen as a "soft touch", and by challenging solicitors rather than claimants where the conduct of solicitors has suggested that they are not complying with the rules governing solicitors' conduct. The main contribution of claims management regulation has been through the substantial reduction in "door knocking".

15. Consumer credit agreement claims

15.1 During the second half of 2008 a major new area of claims management activity emerged in the form of the alleged unenforceability of consumer credit agreements. This area of business is capable of bringing benefit to some consumers, but also of causing damage to others. It also causes problems to the businesses that have provided consumer credit loans. It is, therefore, sensible to analyse why the market developed, the regulatory response and the impact of regulation. However, it should be noted at the outset that malpractice in this area is very different from that for which the Claims Management Regulation regime was designed and that lead responsibility properly rests with OFT.

The Issue

15.2 The Consumer Credit Act 1974 is worded such that if lenders do not comply with its provisions then they are unable to enforce repayment of the loan. It can be argued that for purely technical reasons some consumer credit agreements are not enforceable. Some businesses are seeking to help people seek relief from the debts on the grounds that the documentation is not in the prescribed form. The consumer credit industry disputes both the legal arguments and the implications of the legislation. It believes that there is a misconception about the nature of the documentation requirements and claims that in practice there have been very few cases where credit agreements have been found by the Court to be unenforceable, although a number have been settled out of court.

15.3 Given that the Consumer Credit Act has been in place since 1974, it is necessary to ask why the issue suddenly arose in 2008. The reasons are a combination of the climate being created in which financial products are alleged to have been mis-sold thus creating a demand for compensation, claims management businesses seeking to compensate for the decline in activity in respect of endowment claims, an increasing number of claims in respect of payment protection insurance sold on the back of consumer credit agreements, and businesses in the property market seeking new income streams to compensate for the decline in mortgage business. Paradoxically, steps taken to modify the overly-strict requirements in the 1974 Act may have contributed to the problem. The Consumer Credit Act 2006, implemented in 2007, exposed the quite rigid requirements on creditors when drawing up loan agreements which the courts must deem unenforceable if not complied with under the 1974 Act.

15.4 Once the market began to develop, it mushroomed as more businesses jumped on the bandwagon. Some quite large businesses in the market use agents (not always with a proper agency agreement) and in some cases those

agents decided to set up their own businesses, seeing the opportunity to make even more money.

15.5 Whatever the merits of the arguments, by the autumn of 2008 the business was in full swing with widespread advertising, much of it misleading, and many consumers either directly, through claims management companies or through solicitors beginning the process of seeking to have their loans declared unenforceable by making an information request to their lenders.

The Issue for Lenders

15.6 Lenders have naturally been concerned about these developments. They have faced a massive increase in the number of requests for information followed up by letters stating that the agreement is unenforceable and asking for the debt to be written off. Lenders complain that generally they receive no more than standard letters which show a less than complete understanding of the legal position, and that requests for more specific information are often met by a repeat of the allegation that the agreement is unenforceable. However, as in other financial services sectors some product providers have had a cavalier attitude to compliance with the legislation and as yet there is probably considerable denial in the industry about whether there has really been non-compliance. Significantly, the information and presentation of information about credit cards and loan statements has improved markedly in the last year or so perhaps partly prompted by the claims for compensation.

Impact on Consumers

15.7 For some consumers, the development of this sector of the market is welcome and gives them an opportunity to secure relief from a debt which they should never have incurred in the first place, because the credit agreement should never have been entered into and was not compliant with regulations then in force. There are probably cases where PPI was mis-sold on the back of a credit agreement which itself was mis-sold through the consumer being misled as to the nature of the agreement. However, in order to pursue a particular case a claims management company has to do a great deal of work to analyse whether the loan agreement is unenforceable, before taking action directly or through a solicitor to seek to have the loan written off. A number of companies have entered this market having done all the necessary research and using the appropriate expert legal advice and a panel of suitably qualified solicitors.

15.8 However, in addition to this desirable development there is a tail of business which clearly is less desirable. A major concern has been a huge volume of advertising, mainly on the internet, which has given the impression to people that their credit agreements are unenforceable. Among the misleading

statements highlighted in a Claims Management Regulator release in January 2009 were –

- "80% of credit agreements are unenforceable". Fifty million credit agreements are created every year, at least 25 million are unenforceable".
- "We are currently handling over 5,000 cases!" "We are currently managing £30 m of claims!"
- "We will get your credit cards written off within six weeks!" "Fast results guaranteed".
- "We have a 100% success rate". "A positive outcome is guaranteed".
- "We can write off all your outstanding debt, all previous payments could be returned, and you could keep any goods purchased".

15.9 Although overt misleading advertising has now largely, although not wholly, been dealt with, misleading information is still given in other ways. It is probable that even more outrageous claims have been made in telephone sales calls.

15.10 For some consumers these unreasonable expectations have been further compounded by advice given by a few companies that consumers can stop making payments, and even that they should immediately spend up to the maximum on their credit card because the agreement would not be enforceable (including paying a fee to the claims management company through the credit card). An even more distinct and dangerous variation has been for businesses to purport to take an assignment of the debt, something which is legally not possible. A number of businesses have also charged quite substantial up-front fees to consumers.

15.11 The business models used by claims companies vary. The "good" model, outlined earlier in this section, is for the claims company to do a comprehensive assessment of whether the agreement is enforceable and if it is found to be enforceable then passing it on to a solicitor to take the appropriate action. However, there appear to be a number of other business models –

- Taking a significant up-front fee with the promise of a full refund less an administration cost if the agreement is found to be enforceable. The company then does little more than take in the advance fee, do virtually no work and then pocket the administration fee leaving the consumer feeling that he may well have got a good deal.
- Bombarding the lender with information requests but not then engaging properly by responding to requests for more specific information. The next stage is simply to assert that the agreement is unenforceable.

- Going straight to the Ombudsman, or threatening to do so, effectively using the levy imposed by the Ombudsman on a per-case basis to persuade the lender to accept that the agreement is unenforceable.

15.12 It also seems to be the case that some claims management companies have attracted a large number of cases but do not have arrangements in place with solicitors to pursue the cases.

15.13 There is scope here for more direct consumer detriment significantly greater than for any other claims management activity. There are three main areas of detriment –

- Contrary to the expectation given to the consumer, the lender will enforce the loan, including taking possession of an asset in the case of hire purchase or leasing arrangements, or taking court action to recover the debt.
- Registering the default with the credit reference agencies such that the borrower will find it difficult, if not impossible, to obtain credit in the future.
- Many people, including some with limited income or debt problems, have paid significant up-front fees with the likelihood of them never receiving the service that they have paid for.

The third area is of lesser impact than the other two, but may well be combined with them.

The Regulatory Regime

15.14 This particular issue, as with so many others, does not fall clearly within the ambit of a single regulator. Rather, there are no fewer than four relevant regulators and three other agencies that are significant –

- The Office of Fair Trading is responsible for the licensing of businesses that provide consumer credit and for regulating debt counselling.
- The Claims Management Regulator is responsible for regulating businesses that provide claims management services, some of which are or should be also authorised by the OFT in respect of consumer credit or debt counselling services.
- The Solicitors Regulation Authority is responsible for regulating solicitors including in respect of activities which done by businesses other than solicitors would require authorisation under the Compensation Act.
- The Financial Services Authority regulates businesses that provide consumer loans and requires all authorised regulated businesses to comply with its rules on dispute resolution.

- The Financial Ombudsman Service hears complaints against businesses regulated by the FSA. The way that it charges, on a per-case basis, together with the procedures it follows, form part of the regulatory framework.
- The Department for Business, Innovation and Skills is responsible for the consumer credit legislation.
- The Courts are responsible for interpreting the law and dealing with specific cases.

Regulatory Action

15.15 Regulators have taken a number of actions to deal with emerging problems in this sector, largely announcements aimed primarily at consumers and businesses. In August 2008 a first "consumer alert" was published by the OFT and the Claims Management Regulator. On 6 January 2009 the Claims Management Regulator issued guidance on marketing and advertising claims management services in respect of unenforceable credit agreements. It noted a list of statements that were causing concern in advertising literature and warned businesses that failure to comply with the rules on this matter could lead to enforcement action. In February 2009 there was a joint Claims Management Regulator/OFT press release publicising the January guidance. In May 2009 the SRA warned solicitors not to accept business from introducers which mislead consumers about the prospects of getting loans, credit cards and other debts written-off. The SRA reported that it was currently investigating ten solicitors firms and commented that it was liaising closely with the Ministry of Justice.

15.16 In addition to this activity, the Claims Management Regulator has also been taking some enforcement action. Most of the misleading advertising, particularly on websites, has now been removed, although a quick web-search reveals that quite a lot remains. A number of businesses have been asked to change their practices and it is understood that stronger enforcement action has been initiated in some cases.

The Impact of Regulation

15.17 The collective response from the various regulators has so far not been sufficient. This partly stems from the number of regulators and other agencies involved, but this is a matter to be sorted out within Government. Consumers are entitled to expect a joined-up response.

15.18. The succession of warnings by the Claims Management Regulator, the Office of Fair Trading and the Solicitors Regulation Authority have served a useful purpose but those engaged in serious malpractice are less likely to be influenced by warnings but rather are influenced by enforcement action.

15.19 While some enforcement action has been taken, particularly in respect of misleading advertising, much more needs to done in the circumstances. Removing misleading advertising from websites is desirable but not nearly sufficient if sales calls are even more misleading. At present, there seems a real danger that a number of consumers have been led to believe that their consumer credit debts are unenforceable when they probably are enforceable, that unknown to them they are putting themselves in a position whereby they may find it more difficult to obtain credit in the future and they may well have parted with up to £500 in an up-front fee on the basis of misrepresentation at what could be achieved.

15.20 This issue needs to be tacked more urgently and to do so is likely to require significant additional resources, and in relation to the Claims Management Regulator beyond what is currently available. The SRA and the OFT both have a direct responsibility in this area. Solicitors are not only handling claims passed on by claims management businesses but are also seeking claims directly, and the OFT has responsibility for regulating consumer credit and debt counselling and for consumer protection generally. A joint approach by these three bodies, with one clearly in the lead, accountable and providing the necessary resources is needed.

16. Other financial products

Endowment claims

16.1 Handling endowment claims is the second largest market regulated under the Compensation Act, turnover in 2008/09 probably being around £60 million. A number of areas of malpractice were identified in the Baseline Study, mainly relating to scare tactics and misrepresentation of the chances of success if claiming directly. The Association of British Insurers reported that in 2006 71% of complaints made directly were upheld compared with 51% received through claims management companies. Most of the websites claimed a very different position, typically arguing that fewer than 40% of those who claim directly succeed.

16.2 A strategy for this sector, set out in the Baseline Study, has been implemented and the first year Impact Study noted that this had been broadly successful, particularly in respect of misleading information on websites and unfair terms in contracts.

16.3 There was a finite stock of potential endowment claims and time barring rules by the FSA and the Financial Ombudsman Service have reduced the market even further. The decline in the market is amply illustrated by the fall in the number of new cases handled by the Financial Services Ombudsman –

2004/05	69,737
2005/06	69,149
2006/07	46,134
2007/08	13,778
2008/09	5,798

16.4 Very few claims management businesses have entered the market in the last year or two, many have left the market and the remaining business is generally being handled by a small number of businesses that also handle other financial claims.

16.5 The Claims Management Regulator has dealt effectively with areas of malpractice specific to this industry, in particular cold calling from foreign call centres, failing to refund upfront fees in accordance with contracts and failure to communicate with clients. The worst offending firms have left the market largely as a result of regulatory action.

Bank accounts

16.6 The market for handling bank charge claims developed rapidly during the course of 2006 in response to regulatory action by the FSA and the OFT. The strategy for dealing with these businesses was similar to that for the endowment claims companies, in particular scrutiny of websites and contracts. The strategy is considered to have been largely successful in stopping malpractice developing.

16.7 On 26 July 2007 the Office of Fair Trading announced that a test case on bank charges was being referred to the High Court. This was done in agreement with seven major banking groups. In the light of this agreement the Financial Ombudsman Service stated that it would put on hold its own work on complaints about these charges pending the outcome of the legal proceedings. The FSA issued a "waiver" from its Complaints Handling Rules, which meant that until the test case was resolved any bank or building society would not be required to handle complaints relating to unauthorised overdraft charges. The effect of these announcements was substantially to reduce the scope for claims management work in respect of bank claims. The Claims Management Regulator immediately issued a Guidance Note to authorised businesses about handling of bank charge claims.

16.8 Court action is still ongoing and is likely to continue for some time. As a result the scale of business is modest. Some claims management businesses are handling a small number of claims and a number have been building up a stock of claims to progress depending on the results of the court action. Few businesses charge significant upfront fees so the scope for malpractice is limited.

Payment Protection Insurance

16.9 Complaints in respect of Payment Protection Insurance have risen substantially over the past year. The first year Impact Report noted that while there had clearly been substantial mis-selling in this market, it was less clear that there was an obvious market for claims management companies. It noted that, unlike for endowment claims, there was no procedure that insurers had to go through when a complaint was made. It is also the case that many consumers are not aware that they have Payment Protection Insurance.

16.10 The situation changed during 2008 as knowledge about mis-selling of Payment Protection Insurance became more widespread, aided by various regulatory and Government reports and substantial fines levied by the FSA. Also, as the FSA gradually took action to require insurance companies to deal properly with complaints about mis-selling so the scope for claims management companies increased. The report of the Financial Ombudsman Service for 2008/9 noted that there had been a substantial rise in the proportion of complaints referred by claims management companies, from

19% the previous year to 26% in that year, largely reflecting the substantial increase in Payment Protection Insurance. 14% of cases bought by claims management companies in 2007/8 related to PPI complaints, whereas the following year the figure had risen to over 50%. The Ombudsman's report confirmed the validity of many of the complaints. It reported that in an exceptionally high proportion (89%) of cases that came before it, the outcome was changed in favour of the complainant following its intervention. It went on to say that this suggested that "there was still a widespread problem involving businesses rejecting complaints that they know, or should know, we will uphold". The FSA went on to say that it seemed that "few businesses have conducted the kind of 'root cause' analysis into the background to these complaints that they are required to carry out under the FSA's complaints handling rules".

16.11 These comments are a useful repost to those in the insurance industry who claim that the claims management companies are unnecessary because once a complaint is made to them they will handle it effectively. However, the Ombudsman went on to say that many of the cases brought forward by claims management companies simply took the form of claims presented in the standard format with little information about the specific circumstances in which individual polices were sold.

16.12 As the previous chapter noted complaints about mis-selling of PPI are often handled in conjunction with complaints about the loan connected with the PPI.

Other financial products

16.13 The First year Impact Report commented –

"As yet no significant market has emerged for other financial products. There is a very limited market in pensions opt outs. The companies in this market are already in the endowment claims market so are already regulated. These markets, and other markets where compensation claims may arise are closely monitored, including through liaison with the Financial Ombudsman Service. There is always a risk that a market will develop suddenly with the capability of consumers suffering detriment because the Department is not up to speed. There are adequate arrangements in place to prevent this happening."

16.14 This conclusion remains.

17. Wider issues

Provision of information

17.1 The First Year Impact Report noted that one of the benefits of any regulatory regime is that those providing the goods or service are identified. Having information about those providing claims management services has proved to be useful to three different groups: the Regulator; those who receive claims, who are easily able to check the details of a business bringing forward; and the public, particular those dissatisfied with service they have received from a claims management business.

Displacement

17.2 The report also noted that is an inevitable consequence of any regulatory system is that malpractice will be displaced to some extent, and commented that there had been displacement –

- In respect of personal injury cases from businesses providing claims management services to solicitors.
- In the field of contrived and induced accidents from regulated personal injury claims to unregulated vehicle hire and vehicle damage claims.
- From regulated business to exempt introducers, sometimes not fully in accordance with the rules.

17.3 Over time new forms of displacement become evident, and more generally those who benefit from malpractice have become more confident that they can re-organise their business and "get away with it". In addition to the exempt introducer concept being misused there has been increasing use of agency agreements and franchising which can serve to obscure the relationship between business and consumer and which considerably complicate the task of the Regulator. The Regulator has to be as nimble as the businesses to keep on top of the situation.

Management information

17.4 The database used by the Claims Management Regulator is sufficient for most regulatory purposes but is deficient in respect of management information. Statistical analyses have to be done on an individual basis. This means that trends in the market may take some time to become apparent. The database should be configured so as to produce regular reports on businesses being authorised and on the renewal process and also on regulatory action so as to enable trends over time to be quickly identified and if necessary acted upon. It is recognised that a problem here has been that the number of businesses

being regulated is well above that originally envisaged and the priority has been to ensure that the IT system has been upgraded to meet regulatory needs.

The Big Picture

17.5 Claims management regulation has now been in place for over two years and it is appropriate to look beyond the impact of regulation and identify issues that need to be addressed in respect of the scope and structure of the regulatory system.

17.6 When claims management regulation was conceived it was seen as being a minor regulatory function dealing predominantly with personal injury and endowment claims and designed to fill the gaps between other regulators. It was also seen as an interim solution pending the establishment of the Legal Services Board, the working assumption being that the Board would assume responsibility for claims management business in due course.

17.7 The situation that now exists is rather different than that had been envisaged, and while it is being successfully managed it is sufficiently different as to cause questions to be asked.

17.8 Claims management regulation is no longer a small niche issue dealing with 500 small businesses, but rather quite a substantial regulator dealing with 2,500 businesses and having 35 staff in Burton-on-Trent and 8 in London.

17.9 The Legal Services Board has been established and is in the process of building the framework which will regulate all legal services, but the prospect of claims management regulation being included within this framework is looking increasingly less likely. This is not surprising. Claims management business is unlike the legal services that the Legal Services Board is responsible for regulating.

17.9 Most importantly, the major issues that the Claims Management Regulator is dealing with are all in areas where other regulators also have a role, and there is a risk of regulatory overlap, under-lap and conflicting priorities. Specifically –

- Almost all personal injury business is passed on to solicitors and, as Chapter 8 has shown, claims management regulation in this area cannot be conducted in isolation of what the SRA is doing or not doing.
- The Claims Management Regulator has become involved in dealing with fraudulent motor accident claims, something which was not envisaged at all when the legislation was enacted. Initially, the Claims Management Regulator took the lead in coordinating the work of various agencies, and more recently a more proper relationship has developed with the lead being taken by Police forces and the insurance industry.

- Endowment business is now substantially reducing but here the Claims Management Regulator has been operating in an environment created by a combination of the Financial Services Authority and the Financial Ombudsman Service. The same applies with bank charge business which is now largely on hold.

- The major new area to emerge during the year was consumer credit agreement claims, where regulatory responsibility rests with a combination of the SRA, the Claims Management Regulator and the OFT, with the FSA, the Financial Ombudsman Service and the Department for Business Innovation and Skills also having a role.

17.10 The innovative structure created for claims management regulation still works but is under pressure. The structure was never optimal but was the only one capable of delivering regulation in the required timescale, which it has done effectively. The structure has been significantly upscaled in scope and size, but in the long term this makes it even less optimal for the issues it is now dealing with. It is exceptional for regulation to be conducted from within a Government department, as this does not give the necessary operational framework in which regulation can be effective. Claims management regulation does not sit comfortably within the Ministry of Justice and in due course needs to be moved to where it does sit comfortably. Similarly, Staffordshire County Council has provided a reasonable service in respect of monitoring and compliance, and the model is one that could usefully have application in other sectors. However, the scale is now much larger than was envisaged when the Council took on the role.

17.11 The contract that the Ministry of Justice has with Staffordshire County Council expires in 2011, and by then it should be clear as to whether or, as seems likely, not, the LSB is capable of taking over responsibility for claims management regulation.

17.12 This points the need for serious consideration to be given during 2010 to the regulatory structure. Among the issues that will need to be considered are –

- Should employment continue to be within the scope of the claims management legislation given the present unsatisfactory position or, rather, should this responsibility be given to another regulator?

- Personal injury business is inextricably tied to the framework for conditional fee arrangements and the regulatory regime for solicitors. Should handling of personal injury claims therefore rest with the LSB directly, the SRA or continue to be handled as at present within the Ministry of Justice?

- Handling financial services claims and also claims in relation to housing disrepair, and to a lesser extent criminal injuries compensation and industrial injury disablement benefit, are trading practice issues that

seem naturally to belong within the Office of Fair Trading, alongside the responsibility it has for regulating other areas such as estate agents and consumer credit. The issue is whether there is a case for the OFT taking over as the designated regulator for part, if not all, of the claims management business.

18. Conclusions and future work

18.1 The regulatory regime for claims management activities is considered to have had a significant effect in removing malpractice less than two years after the Compensation Act 2006 received Royal Assent. Specifically –

- Cold calling in person has been significantly reduced. This has reduced the number of frivolous claims and helped defuse the "compensation culture".
- Unauthorised marketing in hospitals has been largely eliminated.
- Significant progress has been made in co-operative working arrangements to deal with fraudulent motor accident claims.
- Malpractice by companies handling claims against the Criminal Injuries Compensation Authority has been significantly reduced, including through some companies voluntarily leaving the market.
- Misleading use of the expression "no win no fee" has largely been eliminated.
- Misleading claims on websites have been almost entirely removed and rules requiring websites to give a physical address are being complied with.
- What little malpractice there was in respect of handling endowment claims has largely been removed.
- The growth of claims handlers dealing with bank charges has been controlled, preventing significant malpractice from developing.
- The growth of claims handlers dealing with consumer credit claims has similarly been controlled, although here the scope and complexity of the issue are such that significant malpractice may have developed.

18.2. However, the nature of some of the issues has changed and some new issues have emerged. The following priorities have been identified –

- Being seen to be tougher on businesses operating without authorisation so as to be a deterrent to unauthorised operation.
- Ensuring that agency arrangements, franchise operations and the use of the exempt introducer concept are operated properly and do not become a means of circumventing regulation.
- Dealing with cold calling by call centres, including where it is alleged that consumers have consented to be called.
- Tackling abuse among businesses seeking to declare credit agreements to be unenforceable.

- Identifying businesses that mislead consumers in telephone sales calls or face-to-face meetings and targeting enforcement action against them.

18.3. Very relevant to personal injury claims but outside the scope of the Claims Management Regulator is the need for more effective action to be taken to tackle solicitors who do not comply with the rules governing solicitors' conduct or for the rules to be changed.

18.4. Separately, the time is approaching when the scope and structure of the regulation need to be reviewed.

Appendix

Summary of Baseline Study – April 2007

Personal injury

Personal injury claims cost around £6 billion a year, motor accounting for nearly 70%, employer's liability for 20% and general liability for 10%. The way claims are handled is complex. Almost all ultimately are handled by solicitors. Some solicitors attract business through their own marketing or by using joint marketing companies. However, much business is referred by intermediaries. Solicitors will pay around £600 for a good personal injury case. There are about 1,000 intermediaries in this market, mainly specialists in claims management but including over 200 accident management companies. Their annual turnover is around £190 million.

There is substantial scope for malpractice. There are two principal problems - selling practices, in particular cold calling, and misleading contracts. There are also two specific problems – marketing in hospitals and contrived accidents leading to fraudulent claims.

Mystery shopping, surveys, inspections of businesses and intelligence information will be used to help enforce the rules. However, success is dependent on the solicitors' Practice Rules being more effectively enforced and the exempt introducer concept working satisfactorily. The Regulator will be working closely with the Solicitors Regulation Authority to ensure that the work of the two regulators is complementary.

Regulation is likely to have significant effects on the nature of the market, including on solicitors that specialise in handling personal injury claims. The market is also likely to be affected by the Government's proposed reforms to the claims process, published on 20 April.

Criminal injuries compensation

The Criminal Injuries Compensation Authority (CICA) pays out about £200 million a year. Regulated intermediaries play only a small role in the market; their turnover is under £1 million a year. Most are also in the personal injury market. Intermediaries can add little value to the process. Some intermediaries have sought to give the impression that they are part of the official process. In co-operation with the CICA, it should be comparatively easy to deal with malpractice.

Industrial Injuries Disablement Benefit

The Department for Work and Pensions (DWP) pays out around £800 million in Industrial Injuries Disablement Benefit a year. Regulated intermediaries play only a small role in the market; their turnover is under £1 million a year. Most are also in the personal injury market. Intermediaries can add little value to the process. There

is scope for malpractice through misleading contracts, which the authorisation process and subsequent monitoring should be able to address.

Employment issues

Employment tribunals award around £500 million a year, and many other cases are settled before going to a tribunal. Claims management companies have a very small role in this market; it should be possible to deal with any malpractice.

Endowment policies

Compensation payments in respect of miss-sold endowment policies exceed £1 billion a year. Intermediaries can earn an average of £800 a case. Their turnover is estimated at £75 million a year. The main problem areas are misleading information on websites, in particular the use of scare tactics, and contracts that are weighted against the consumer. These issues are being dealt with at the application stage. This, combined with scrutiny of contracts and the client account rules, should remove much of the scope for malpractice.

Other financial products

There is limited activity in respect of payment protection insurance, bank charges and opting out of SERPS. However, the scope does not currently exist for a market anything like the size of the endowment compensation market. Recent activity in respect of bank charges means that this is likely to become the most significant new financial services market. The issues will be dealt with in the same way as for endowment miss-selling.

Housing disrepair

The market seems very small and local in nature. There is some activity by claims farmers who sell cases on to solicitors. Malpractice will be addressed in the same way as for personal injury business; the co-operation of one or more large social landlords will facilitate the process.

Summary

The following table summarises the analysis and makes a preliminary assessment of the chances of success. Unreasonable selling tactics is the one common theme. The most difficult sector to tackle will be personal injury, because it offers most scope for businesses to seek to circumvent the rules and because, unlike in the other sectors, the malpractice is generally paid for by the defendant and his insurers rather than by the client.

The following points should be noted –

- The first column shows the number of businesses that applied for authorisation, by 19 February 2007, indicating that they intended to operate in this market. The number adds up to over 2,000, many businesses saying that they intended to operate in more than one sector. In practice almost all the businesses in the criminal injuries, industrial injuries and housing disrepair sector (570) were also in the personal injuries sector.
- Not all the businesses that said they intended to operate in a particular market have operated in the market. For example, of the 130 saying that they intended to operate in the employment sector only 43 reported turnover in the previous year.
- 604 businesses, nearly half the total, said that they had not been trading for the full year to 30 September 2006. This indicates both a rapidly changing sector, and probably also some re-organisation to take account of the introduction of regulation.
- The turnover figures are estimates for the size of the markets, in the year to 30 September 2006, for business subject to regulation under the Act.

Market sector	No of Businesses	Estimated annual size of market	Malpractice	Prognosis
Personal injury	1,128	£190m	Aggressive selling. Marketing in hospitals. Misleading contracts. Involvement in fraud.	Most difficult sector. Regulatory arbitrage and attempts to get round regulation are certain.
Criminal injuries compensation	340	£1m	Claimants deceived into thinking they are dealing with CICA.	Good.
Industrial injuries disablement benefit	165	£1m	Claimants deceived into using intermediary.	Good.
Employment matters	130	£2m	Claimants deceived into using an intermediary.	Difficulty will be identifying malpractice.
Endowment mis-selling	176	£75m	Scare selling tactics. Clients dropped if cases difficult.	Good, but a large sector to tackle.
Other financial products		£1m	Claimants deceived into dealing with an intermediary.	Should be able to prevent malpractice being developed on a significant scale.
Housing disrepair	65	£1m	Aggressive selling.	Local in nature, so problem will be to identify.
Total	**1,256**	**£275m**		