HM Treasury

Financial Services (Banking Reform) Bill

Claims Management Regulation – Financial Penalties

Briefing for Peers **November 2013**

Claims Management Regulation – Financial Penalties

This amendment will give the Claims Management Regulator ("the Regulator") powers to impose financial penalties on non-compliant Claims Management Companies (CMCs).

Bad practice by CMCs operating in the financial services sector has created poor outcomes for both consumers and businesses. As the scale of potential claims for payment protection insurance (PPI) compensation has become clear, CMCs have charged consumers a fee to help them pursue their claim. Some CMCs have submitted illegitimate claims, which has led to delays in receiving compensation for consumers who have legitimate claims, and has increased costs for defendant financial services firms where claims are unsubstantiated. Enforcement powers have not been sufficient to deter CMCs from carrying out this speculative behaviour. This issue is most prevalent in, but not limited to, the financial services sector and the PPI claims market in particular.

Bringing in a power to impose financial penalties on non-compliant CMCs will act in the best interests of both consumers and businesses by ensuring that the regulator has the proper tools to deter this behaviour. This will bring the Regulator on par with similar regulatory authorities such as the Financial Conduct Authority (FCA), Solicitor's Regulation Authority and the Office of Fair Trading, amongst others.

The framework for enforcement action

Those CMCs providing regulated claims management services in England and Wales must be authorised to do so by the Regulator which forms part of the Ministry of Justice (MoJ). CMCs are active in a broad number of sectors as well as financial services and products (such as PPI) including; personal injury, employment matters, criminal injuries, industrial injuries disablement benefit and housing disrepair.

Regulated CMCs must pay an annual regulation fee based on their turnover, which must be reported to the Regulator upon application for authorisation and annually upon renewal of authorisation. Once authorised, regulated CMCs are required to adhere to certain conditions of authorisation. These include providing information or documents to the Regulator upon request, obtaining a policy of professional indemnity insurance (if operating in the personal injury sector), adherence to any codes of practice and compliance with the Conduct of Authorised Persons Rules (CAPRs). Where breaches of the conditions of authorisation have been identified by the Regulator, enforcement action can be taken.

The Compensation Act 2006 contains provisions for regulatory enforcement by the Regulator. The Schedule to the Act enables provision to be made by Regulations, including that the Regulator may impose conditions on, suspend or cancel authorisations of regulated persons. The Schedule also specifies that the Regulator can investigate complaints about the professional conduct of an authorised person. All statutory enforcement decisions made by the Regulator can be appealed at the First-Tier Tribunal (General Regulatory Chamber) (Claims Management Services).

There is currently no provision within any of the legislation, however, for the use by the Regulator of financial penalties as a regulatory enforcement tool against authorised businesses proven to have breached the CAPRs and other conditions of being authorised.

Proposed new power to issue financial penalties

There are currently around 2,300 regulated CMCs in operation. A small proportion of these firms engage in poor business practices, including making speculative claims which can clog up the system. This tends to be most prevalent in the financial products and services sector and the PPI claims market in particular.

Some non-compliant CMCs have generated avoidable costs for defendant businesses (e.g. financial services providers, banks) as well as other organisations such as the FCA, the Financial Ombudsman Service (FOS) and the Financial Services Compensation Scheme (FSCS), whose operating costs are essentially funded by levies on financial businesses rather than by general taxation. Non-compliant CMCs can tie up the resources and administration costs of defendant businesses by making unmeritorious claims or not carrying out due diligence when assessing potential claims. This can also delay the payment of compensation to consumers with legitimate claims.

In addition, there are instances where it can be disproportionate to vary, suspend or cancel the authorisation of a CMC despite it not being compliant. Where a CMC's authorisation is suspended or cancelled, for example, it can no longer act on behalf of its clients and this can lead to further consumer detriment.

A new power to impose financial penalties for breaches of the conditions of authorisation will provide an alternative enforcement option to be used by the Regulator.

Where a financial penalty is imposed on a regulated CMC for breaches of the conditions of authorisation as an alternative to the other available regulatory sanctions the CMC will be able to continue assisting its clients as appropriate. This will reduce the risk of further consumer detriment being caused specifically by the imposition of other formal enforcement action, and serve as an additional deterrent for those that may be engaged in malpractice.

Amendments to the Compensation Act 2006

It is proposed that the Act be amended to give the Secretary of State power to make regulations to enable the Regulator to impose a financial penalty in the following circumstances:

- as a consequence of failure to comply with rules prescribed by the Regulator about the professional conduct of authorised persons (the Conduct of Authorised Persons Rules);
- as a consequence of failure to comply with a code of practice;
- in relation to investigating complaints about professional conduct;

- as a consequence of failure to comply with a requirement to take out a policy of professional indemnity insurance; or
- as a consequence of failure to comply with certain requirements regarding the provision of information or documents.

The amendments also provide that regulations shall include provision about determining the amount of a penalty imposed by the Regulator, and in particular may include provision specifying a minimum and maximum amount.

The intention is that when setting the amount of the financial penalty in any case, the Regulator will take account of factors such as, but not necessarily limited to: consumer detriment, length and severity of breach, conduct of the business during investigation, and third party detriment to those other than consumers such as solicitors, banks, the FOS and the FCA.

The amendments also provide that regulations may allow enforcement costs to be deducted from financial penalty receipts before being passed to the Consolidated Fund.

Amendments to the Act are also to be made to provide a right of appeal to the First-Tier Tribunal against:

- The imposition of the financial penalty;
- The amount of the financial penalty; and
- Any date by which a penalty or any part of it must be paid.

It is intended that the ability to impose a financial penalty will be implemented by way of amendments to the existing regulations, the Compensation (Claims Management Services) Regulations 2006. A full, public consultation regarding the detail of the necessary changes to facilitate a Claims Management Regulation Financial Penalty Scheme will be launched in early 2014. Changes to these Regulations, including the measure of the financial penalties to be imposed, are subject to the affirmative Parliamentary procedure, which will allow for additional scrutiny of the detail of the proposals.

Further Enquiries

1. For further information, please contact the Bill Manager Tom Wipperman (020 7270 6180, tom.wipperman@hmtreasury.gsi.gov.uk) or the Bill Team Leader Ian Ginsberg (020 7270 5967, ian.ginsberg@hmtreasury.gsi.gov.uk)

2. For access to publications please go to http://www.gov.uk/government/policies/creating-stronger-and-safer-banks