Ministry of JUSTICE

Claims Management Regulation

Impact of Regulation
One Year Assessment

A report by Mark Boleat for the Ministry of Justice
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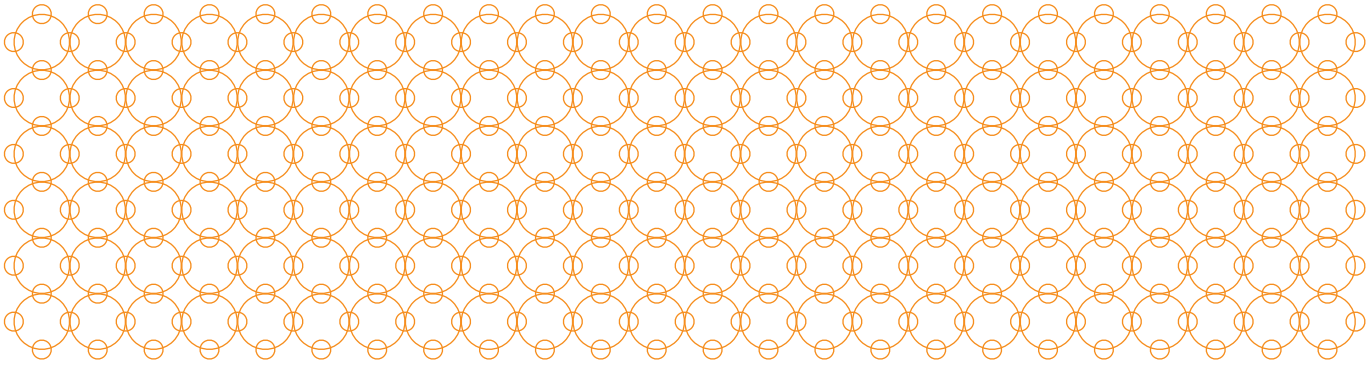

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Introduction

The Compensation Act 2006, providing for the regulation of claims management services, achieved Royal Assent on 25 July 2006. The Act was commenced; the regulatory regime including the regulations and rules were 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. This second study reviews the impact of regulation over its first full year of operation.

The approach has been to take the objectives of regulation, quantified to some extent in a Baseline Study, as the starting point. The various regulatory processes are then examined. The main part of the paper makes an assessment of the impact of regulation in each of the sectors subject to regulation.

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1. Executive summary

Background

1. There has been significant malpractice in the provision of claims management services, particularly for personal injury cases. 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 outsider was brought in as a temporary civil servant and Head of Claims Management Regulation for a year from August 2006; subsequently an established civil servant has had this role. 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 Department.

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.

5. Different approaches have been needed for the different markets; the approaches in the two principal markets - personal injury and financial services claims - have been very different.

6. A Baseline Study, published in April 2007, set out an analysis of the markets and the approach that would be adopted.

The authorisation process

7. The authorisation process worked well. There were no significant problems with the application form or the technology. Feedback from applicants indicated broad satisfaction with the arrangements. 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.
   - Deficiencies in websites and contracts were largely addressed. In itself this meant that much of the malpractice in respect of endowment claims had already been dealt with.
   - 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.

8. The process gave the necessary platform on which monitoring and compliance work could be effective.

9. One significant lesson was that many applications were of a very poor quality. Perhaps the degree of this could have been anticipated given that the businesses to which regulation was being applied had little or no previous experience of regulation. More account could also have been taken of the nature of the applicants.

Renewals process

10. The initial certificates of authorisation all ran to a specific date, 28 February 2008. The renewal process went smoothly for those authorised businesses that completed the renewal form in good time, and contributed significantly to achieving compliance with the Rules of Conduct. The process confirmed the high turnover of businesses in the market. 87 businesses surrendered their authorisation and 187 have either not returned renewal forms or have returned incomplete forms. Around half the businesses that renewed had not been trading for a full year to September 2007.

Monitoring and compliance

11. Monitoring and compliance work has been carefully 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 website and contracts. It has not yet been necessary yet to make significant use of formal enforcement powers.

Complaints handling

12. It was not anticipated that there would be a significant number of complaints to the Regulator, and this has proved to be the case. Almost all the complaints have been in respect of financial products and services, three businesses accounting for a significant proportion of the total. People with a complaint about an authorised business generally discover the Claims Management Regulator when doing an internet search, or as a result of the requirement for authorised businesses to publish their complaints procedures on their websites.

Personal injury

13. 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. The Rules of Conduct banned cold calling in person, required any other cold calling to be in accordance with industry codes and prohibited business being acquired in a way that would put the solicitor to whom the business was passed in contravention of the rules governing solicitors' conduct.

14. Misleading use of the expression "no win no fee" and other misleading advertising have largely been dealt with through the authorisation process.

15. A small number of businesses that actively engaged in cold calling were identified and action has been taken to ensure that they comply with the Rules. A close working relationship with the Solicitors Regulation Authority (SRA) has been essential for this to be achieved. This has achieved reasonable success. Cold calling is now on a much reduced scale and by individuals rather than businesses.

16. Vigorous action has been taken against unauthorised marketing in hospitals. Such marketing has largely been eliminated.

17. Malpractice in respect of personal injury cases is now predominantly the responsibility of solicitors. The SRA needs better regulatory tools to deal with malpractice.

Personal injury – contrived accidents

18. Contrived accidents lead to false insurance claims, predominantly personal injury, vehicle damage and related credit hire, in excess of £200 million a year and are connected with other criminal activity. While insurance fraud was on the agenda when the legislation was enacted, contrived and induced accidents were not. When its importance was realised, a strategy was developed involving co-operation with the SRA, the Insurance Fraud Bureau, the Insurance Fraud Investigators Group, the City of London Police and other relevant bodies. The Ministry of Justice cannot be the lead enforcement agency in this area, but it has played a valuable role in assisting other enforcement agencies and facilitating the development of a strategy.

Criminal injuries compensation

19. Criminal injuries compensation is a very small market (under £1 million a year) for claims management businesses. Some intermediaries have sought to give the impression that they are part of the official process and have also used unfair contracts. These issues have largely been addressed through the authorisation process.

Industrial Injuries Disablement Benefit

20. Industrial Injuries Disablement Benefit is also a small market (under £1 million a year). Most businesses are also in the personal injury market. There has been limited malpractice and this will have been partly addressed in the authorisation procedure.

Employment issues

21. Claims management companies have a small role in the employment market. This has not been a priority area for the first phase of regulation. The main issue appears to be quality of service.

Housing disrepair

22. The market seems very small and local in nature. The strategy is to work with social landlords who perceive this as being a significant problem. In practice, local authorities have largely dealt with the problem themselves. However, claims management regulation has played its part, particularly in reducing "door knocking".

Endowment claims

23. This is the second largest market after personal injury. Turnover was £68 million in the year to September 2006, but fell by more than a third in the following year as the number of outstanding potential claims fell sharply. The main problem areas have been misleading information on websites, in particular the use of scare tactics, and contracts that are weighted against the consumer. These issues have largely been dealt with through the authorisation process. The remaining problems relate to service issues and people being given misleading information by representatives of claims companies.

Other financial products

24. Reclaiming bank charges became a big market as the regulatory regime was being implemented. Malpractice is similar to that in the endowment market and was largely addressed through the authorisation process. The business has been substantially reduced following the commencement of a test case in the courts.

25. No significant market has developed in respect of other financial products. Payment protection insurance is the most likely area for new business.

Wider issues

26. Three wider issues have emerged in the analysis of the impact of regulation –

- The provision of basic information on the claims management regulation website has been useful to the Regulator, those who receive claims and the public.
- There has been some displacement of malpractice from business regulated under the Compensation Act 2006 to business that is not regulated under the Act.
- The expression "compensation culture" seems to have been less prominent, although claims management regulation cannot take all the credit for this.

Conclusions and future work

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

- Cold calling in person has been significantly reduced. This has reduced the number of frivolous claims and helped defuse the perception of a 'compensation culture'.

- Unauthorised marketing in hospitals has been largely eliminated
- A strategy has been developed for dealing with contrived accidents, with the Department also taking a co-ordinating role for the various enforcement agencies and the insurance industry.
- 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 win" 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.

28. There remains much work to be done, in particular –

- Combating unauthorised activity.
- Regular surveillance of websites and other marketing material to ensure that bad practices do not return.
- Eliminating all cold calling in person.
- Working with other agencies to tackle claims management businesses involved in crime.
- Reducing the scope for abuse of the "exempt introducer" concept.
- Ensuring that authorised businesses provide the necessary information about their ownership.
- Ensuring that contracts are not unfair and that customers are not subsequently treated unfairly.

29. 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.

30. The following table is reproduced from the Baseline Study (April 2007), with the addition of a final column on the right summarising impact.

Market sector	No of Businesses	Estimated annual size of market	Malpractice	Prognosis	Impact April 2008
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.	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	£1m	Claimants deceived into thinking they are dealing with CICA.	Good.	Significant; problem largely dealt with.
Industrial injuries disablement benefit	165	£1m	Claimants deceived into using intermediary.	Good.	Probably significant but little evidence.
Employment matters	130	£2m	Claimants deceived into using an intermediary.	Difficulty will be identifying malpractice.	Some evidence of poor quality advice and representation.
Endowment mis-selling	176	£75m	Scare selling tactics. Clients dropped if cases difficult.	Good, but a large sector to tackle.	Significant; malpractice largely eliminated.
Other financial products		£1m	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	£1m	Aggressive selling.	Local in nature, so problem will be to identify.	Little evidence other than "door knocking" reduced.
Total	1,256[1]	£275m			

[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.

2.3 In the personal injury sector four main types of malpractice have been identified –

- Misleading advertising, in particular suggestions that making a claim is easy and that large amounts of compensation can be quickly obtained.
- Opaque and unfair contracts that conceal the nature of the arrangement between client and claims management business and may also conceal costs that have to be paid.
- Cases being run for the benefit of intermediaries not the client.
- Outright fraud, particularly as a result of staged accidents.

2.4 The malpractice contributed to the two largest businesses, Claims Direct and The Accident Group, failing in 2003/04.

2.5 Similar malpractice could be found, on a lesser scale, in respect of claims for Industrial Injuries Disablement Benefit, criminal injuries compensation and housing disrepair.

2.6 In respect of endowment claims, malpractice has largely been misleading advertising, stressing how difficult it was for people to claim compensation directly, and opaque and unfair contracts.

2.7 The government initially responded to concerns about malpractice by seeking self-regulation from the industry. When it became clear that this could not be delivered, the government decided to legislate.

The Compensation Act 2006

2.8 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.

2.9 Claims in respect of the following are covered –

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

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

- lawyers;
- independent trade unions;
- insurance companies, insurance brokers and IFAs providing a claims management service which 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

2.11 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. Initially, it was hoped that a trade body, the Claims Standards Council, could be the Regulator. This was evaluated with the result was that this was not a realistic option. Existing regulators were considered but none was both willing and able. This left direct regulation by the Secretary of State as the only option.

2.12 An innovative structure was developed. While the Secretary of State was formally the Regulator, an external expert (the author of this report) was brought in for one year as a temporary civil servant to be Head of Claims Management Regulation and to exercise the powers on behalf of the Secretary of State. The purpose was to have an identified Head who would have a public profile above that normally associated with individual civil servants (and similar to that of the heads of NDPBs), in the first year of operation. After the first year an established civil servant became Head of Regulation. Much of the regulatory work was seen to be similar to that undertaken by local authority trading standards departments. It was considered that using such a service would enable the regulatory regime to be up and running as quickly as possible. Staffordshire County Council was selected, after an open tender process, to provide a Monitoring and Compliance Unit (MCU) under contract to the Department. It was appointed at the beginning of September 2006, began work a few days later and was in a position to deal with applications for authorisation within three months. The MCU reports directly to the Ministry of Justice and all regulatory decisions are made by the Department.

2.13 The final part of the regulatory structure is the non-statutory Regulatory Consultative Group. This Group comprises representatives of relevant major stakeholders including claims management businesses, other regulators, trade associations and consumer organisations. It has proved to be a very effective body in the consultation process, in particular by providing a forum in which all the parties are represented and are prepared to defend and argue their views. The Group has also helped to ensure support for the regulatory regime. This is not surprising. People are more likely to support something that they have been involved in and where they have had the chance to hear and debate the views of other stakeholders, than where they have only had a bilateral dialogue with the government department.

The objectives of regulation

2.14 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.

Understanding of the market

3.2 The first essential for regulating a market is to understand it. This was not easy in respect of claims management services. The overall market is small and not well documented. Also, there are, in effect, a number of different markets with little in common in respect of either issues or market participants. The approach was to talk to relevant people, both in bilateral meetings and at a series of consultation meetings, and to apply basic analytical tools to understand the dynamics of the market.

Understanding of the effects of regulation

3.3 There are a number of predictable effects of regulation in any sector –

- If possible, businesses will legitimately be restructured to avoid the need to be regulated.
- Existing businesses, particularly where they have been engaged in malpractice, will be closed down and new businesses started.
- Businesses will look for loopholes to exploit and will generally succeed.
- There will be the potential for turf wars between regulators or a clash of regulatory approaches, which again some businesses will seek to exploit.
- Government departments and regulators generally miss deadlines they set and take longer to implement regulation that they said or than was reasonable to expect.
- In order to get legislation through Parliament, departments sometimes have to agree to put certain provisions on the face of the legislation or to agree to introduce secondary legislation that in retrospect is inappropriate and which hinders the achievement of the objectives of the legislation.
- The consultation process will not be fully effective because most of those responding have vested interests and the views of some groups, particularly consumers, will not be represented at all. As a result regulations often fail to achieve their desired purpose.

3.4 These factors were consciously on board throughout the process. The primary legislation was relatively simple and flexible, providing sufficient scope for Regulations and Rules to be used (and amended quickly) to respond to and deal with most developments - and changes have been made where needed. There was an effective consultation process involving formal consultation exercises, bilateral meetings with major stakeholders, regional meetings and round table discussions at the Regulatory Consultative Group. As a result, there has been a broad measure of agreement on every major decision.

3.5 The ambitious timetable was met. This preserved the momentum, helping to ensure that Regulations and Rules would not be out of date by the time that they were implemented.

Identifying how regulation can be effective, in particular "pressure points"

3.6 Broadly speaking, regulators can try a broad brush or targeted approach. The broad brush approach is expensive, time consuming and generally ineffective. A targeted approach is better, but only if the targets are properly identified and the action efficiently delivered. The Claims Management Regulator could not hope to monitor and enforce rules by individually monitoring a few thousand businesses. The approach has been to identify how regulation could most effectively be implemented. The Department identified websites as a target across the board, simply because they are a major marketing channel and cannot be concealed. In individual markets the approach has been to seek to make it difficult for those engaging in malpractice to do business as well as seeking to enforce Rules of Conduct on them. Specifically –

- At the end of most personal injury claims is a solicitor. If there has been malpractice in the acquisition of business then the solicitor taking the business has breached the rules governing solicitors' conduct as well as the introducer breaching the Rules of Conduct under the Compensation Act. The Regulator has therefore sought to work closely with the SRA.
- At the end of every criminal injuries compensation claim is the Criminal Injuries Compensation Authority. The Department has worked with the Authority which has agreed to refuse to deal with unauthorised businesses and to report unauthorised businesses and businesses engaged in malpractice to the Regulator.
- The banks and the insurance companies have been asked to refuse to deal with unauthorised businesses and to report malpractice to the Department.
- The Department has engaged with a number of other stakeholders to attempt to deal with the problem of contrived accidents.

Rules of Conduct

3.7 The Rules of Conduct are very brief but deal specifically with malpractice. There has been no attempt to "throw in the kitchen sink" or to force "best practice". The Rules target identified malpractice, for example specifically covering cold calling in person and unauthorised marketing in hospitals.

Enforcement

3.8 Rules that are not enforced are worse than no rules. They simply give those engaging in malpractice a halo of respectability and call into question the credibility of regulation. The strategy from the beginning has been to enforce rigorously the Rules of Conduct and to demonstrate this. However, resource constraints have to be accepted. Enforcement activity has concentrated on the major issues with the expectation that the 'demonstration' effect would impact to some extent throughout the market.

Partnership working

3.9 The Claims Management Regulator is small, with limited resources, and is operating in markets where there are other, better-resourced regulators including the SRA, the FSA and the Police. The approach has been to work with other regulators, recognising that unless this is done, the Regulator cannot hope to be successful.

Baseline Study

3.10 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 as Appendix 1.

4. The authorisation process

Introduction

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 Authorisation process (dated 24 May 2007) has been prepared. The Executive Summary is reproduced below.

Objectives of the authorisation process

4.2 There were three principal objectives of the authorisation process –

- To set the tone for the whole regulatory regime so that the industry would know that this was a serious and professional regulator.
- To provide the platform on which monitoring and compliance work could be effective, in particular by obtaining the necessary information about authorised businesses.
- To provide aggregate data on the various markets subject to regulation.

Risk Framework

4.3 A risk framework was prepared, identifying the factors associated with malpractice; this was used to influence the design of the application form and to shape the authorisation process.

The application form

4.4 The application form was regarded as a vital part of the authorisation process. The FSA form was used as the starting point and there was both formal and informal consultation on the form.

4.5 Potential applicants had to provide contact details in order to obtain a copy of the form. A web-based form was used. Key features were –

- Where the form is completed online, all the necessary questions must be completed as the form is self-checking to some extent.
- Details are required of the business including principal place of business; registered address, if a company; and all website addresses.
- Details are required of the directors or partners and any other people able to have significant influence over the policy or management of the business.

- A requirement to state the sectors in which the business intended to operate and the turnover of the business.
- A detailed self-certification statement - businesses being required to confirm that they complied with or would comply with each of 26 provisions in the rules.
- A signed declaration that the information provided was correct.

The authorisation process

4.6 The information provided on the application form was exhaustively checked, including Companies House checks, Internet checks, and validation that the business was operating from the address on the application form on the business. Websites were checked for consistency with the information on the application form, the Rules of Conduct and the Electronic Commerce Regulations. In about 90% of applications it was necessary to go back to the business to request further information or to seek changes to websites or contracts.

Number and timing of applications

4.7 Applications were invited from 30 November 2006; a deadline of 16 February was set for applications to be received; and 6 April was provisionally set as the date the prohibition on operating without authorisation would be commenced. 1,007 applications were received by the deadline, 80% in the final two weeks. The commencement date was finally set for 23 April to provide more time to deal with this larger than expected number.

Assessment of the process

4.8 The initial assessment of the process is –

- Generally, the strategy to get the message over about the need to be authorised was successful.
- The informal deadline for applications worked well and maintaining deadlines generally was effective.
- The quality of applications was very poor, greatly increasing the work required in the application process.
- The application process had a desirable effect on businesses and generally businesses seemed content with the process.
- Using a web-based system had huge advantages as did the requirement on businesses to provide contact details when requesting a form.

- Website checks, and to a lesser extent contract checks, resulted in a significant increase in compliance with the Rules of Conduct and general legal requirements.
- Some businesses engaged in malpractice were probably deterred from seeking authorisation.
- The data provided on the application form enabled the market to be mapped for the first time.
- Those businesses that requested an application form but did not apply, or which started the application process but did not finish it, have been identified; some may seek to engage in unauthorised activity.
- How businesses handled the application process has been used in the risk assessment process.
- The authorisation process was less effective in scrutinising businesses that were not companies and businesses without websites.

Risks and issues

4.9 The IT system was fairly standard but nevertheless required some design and testing. The time frame meant that there was little margin for error or for full testing and the work was completed at the last minute. Had there been any errors or system failures this may have delayed the authorisation process. Ideally more time was needed although everything worked well.

4.10 The high number of applications necessitated increasing the number of staff and opening of a second office. This increased the risk of inconsistencies in dealing with applications. A clear procedure manual combined with quality controls minimised this risk.

4.11 The deadlines worked well. However, the number of applications was much higher than expected and 80% were received in the final two weeks. It was not possible to authorise late applicants and those that had applied before the deadline but that had failed to respond adequately to queries before 23 April. It had been assumed that there would be few applications after the deadline. In the event there have been more than 400. Resources had to be increased to handle the additional work and tactical decisions had to be taken on priorities.

Conclusion

4.12 The authorisation 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.

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

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

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

4.15 Key success factors are considered were –

- The requirement to provide contact details in order to obtain an application form.
- Using a web-based application form.
- The self-certification compliance statement.
- The thorough checking of everything on the application form and websites.
- The short time frame, which concentrated minds and maintained momentum.
- The relatively small sector.
- The built-in enforcement right though the distribution chain.

4.16 Some things could have been improved –

- Ideally the website and application form should have been ready a week or two earlier for full testing. However, the timescale was short and the system did work well.
- Although additional resources were provided to deal with the higher than expected workload these could have been increased even more around 23 April when volumes were at their absolute peak.
- Many applications were of a poor quality. Perhaps this could have been anticipated given that the businesses to which regulation was being applied had little or no previous experience of regulation. In retrospect the application form could have done more to require a better quality of application through forcing applicants to read the Rules of Conduct,

providing more explanation on the form itself rather than in a guidance note and perhaps some reordering of questions so that mistakes would be more difficult to make.

- The combination of application volumes greatly exceeding all government or industry estimates; the low standard of many applications received, which meant they took longer to process; and many applications being received after the deadline, could not have been foreseen at the outset. Given a longer implementation timescale, it may have been possible to identify the trends a little earlier but the advantages of quick implementation are clear.

5. The renewal process

5.1 When the regulatory regime was devised it was decided that all certificates of authorisation would run to a particular date, 28 February. The main reason for doing this was to encourage early applications for authorisation. All business seeking authorisation prior to the legislation being fully activated paid the same annual fee for the period to 28 February 2008.

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.

Annual fees

5.5 The initial impact study had as one its conclusions the need to reduce the regulatory burden on small businesses. The burden consists of both paperwork and costs. The documentation required for businesses to renew their authorisation was simple and should not have presented a problem to any business. The decision was taken to reduce the minimum authorisation fee for the smallest businesses from £400 to £100. It was recognised that £400 was a heavy burden on small businesses for whom regulated claims management services were only a small part of their total business.

The approach

5.6 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.

5.7 Recognising that many renewal forms would come in at the last minute, the appropriate arrangements were 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.

5.8 The process was influenced by the experience of the initial authorisation process. However, unlike on that occasion when there was no clear idea of how many businesses would seek authorisation, the number that would be seeking renewal could be fairly accurately forecast. It was assumed that many of the applications would come in at the last minute and that many would be inadequate and would require correspondence with the authorised business. The timescale adopted for the process was –

- November 2007 – letter sent to all authorised businesses including data that they had supplied on their application forms and seeking return of the forms by 31 December 2007. Businesses were required to sign a declaration that they had complied with the Rules of Conduct, to give details of any regulatory action taken against the business or people involved in the business and to give their turnover in the year to 30 September 2007.
- January 2008 – reminders sent to those businesses that had not responded to the first letter and invoices sent out to businesses based on their returns.
- 28 February 2008 – all initial authorisation certificates expired.

Operation of the process

5.9 The renewal process went well and there were no delays in dealing with renewal applications. A survey was undertaken in March 2008 of a sample of 30 businesses to assess how they found the renewal process. In response to a question "when you first read the form did you understand what you had to do", 80% replied "yes".

5.10 The following table sets out key details from the process as at 3 April 2008.

Number of businesses issued renewal notices	1,609
Number of renewal notices returned	1,452
Of which voluntary surrenders of authorisation	87
Of which forms incomplete	30
Number of forms not yet received	157

5.11 87 businesses have voluntarily surrendered their authorisation and it is probable that most of the 157 businesses whose forms have not been received and the 30 whose forms are incomplete have ceased providing regulated claims management services.

5.12 Two interesting points emerged from the process –

- The earlier the businesses returned the form the better the quality of the application. The late returns were the worst.
- There was large-scale non-compliance with the requirement to notify changes in information provided on applications forms. In about 70% of the 494 cases where forms were received with changes, these changes had not previously been notified as is required under the Rules of Conduct. This is not surprising; other regulators have a similar experience.

Changing nature of the market

5.13 Information obtained in the renewals process enables an assessment to be made of how the market for claims management services has changed since the regulatory regime began and also the nature of the market generally.

5.14 Turnover by businesses engaged in personal injury work seems to have increased by around 25%, while turnover in the financial services and products market fell by over 30%. The latter was expected given that endowment complaints work is now well past its peak. The changing nature of the market is examined in more detail in the chapters of the various sectors.

Improvements

5.15 The renewals process is largely a manual one. Businesses have to complete a form and post it to the Monitoring and Compliance Unit with a cheque. An online system would be preferable as it would prevent incomplete renewal applications being made and would speed up the process generally. Electronic payments would also be more efficient.

5.16 These points were confirmed in the survey of businesses in March 2008. 40% of the 30 businesses surveyed said that they would prefer to pay online and 63% said that they would prefer to complete the form online.

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 websites and contracts.
- Targeted audits and requests for information of businesses where there is some evidence of malpractice.
- Use of enforcement powers where necessary, but 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 Five businesses were formally refused authorisation, three because of previous criminal activity, one because of involvement of an undeclared individual and one because of previous conduct. However, this does not tell nearly the whole story. 205 businesses submitted applications for authorisation, including a cheque for the authorisation fee. These businesses 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 in 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 is seeking 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 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 300 businesses have been identified as potentially trading unauthorised. Each of these businesses has been approached with the following results as at March 2008 –

38 have applied for and obtained authorisation

11 have applied for authorisation

41 proved to be exempt from the need to be authorised

47 have been confirmed as no longer trading

91 are thought to be no longer trading, that is there no evidence of them trading but the businesses have not confirmed that they are not trading

50 businesses are now being pursued at various stages

14 were in a position in which it could not be proved that they were trading while unauthorised.

Review of contracts

6.7 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

6.8 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. Of 1,185 websites checked, 588 (50%) were initially non-compliant. The number non-compliant as at March 2008 was 168, 14% of the total. The remaining non-compliances are of a minor nature (for example a company saying that is "registered in the UK" rather than "registered in England & Wales") and have been checked in the renewals process. It is probably the case that the websites of claims management businesses are now among the most compliant of all sectors' websites as a result of the review. A comparable check in other sectors would yield much higher levels of non-compliance.

Cancellation of authorisation

6.9 One business's authorisation has been cancelled.

Audits

6.10 75 audits of businesses dealing with personal injury claims have been carried out. These have mainly been in West Yorkshire, Lancashire, Luton and Birmingham. Problems found included no VAT registration, undeclared turnover, and the business being a front for someone else. In some cases information has been passed to HMRC, eg where there is a suspicion of tax evasion. Otherwise, the businesses have been required to remedy any failings. Some businesses are still being investigated; more formal enforcement action may follow.

6.11 Three audits were carried out of companies dealing with bank charges, on the basis of complaints received about the businesses. The issues were cold calling by telephone, failure to respond to customer queries, clients being unable to contact the business, and unclear promises about the refund of upfront charges. Following the audits the companies made changes to their contracts, complaints handling procedures and communications with clients.

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. 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 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 The initial expectation was duly borne out. Up to March 2008 1,216 complaints had been received. Over 80% were in respect of financial products and services. Most of these complaints have been dealt with informally, with three being formally referred for consideration to the Regulator. In each case the Regulator found in favour of the company.

7.4 Over 70% of the complaints received 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; 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 One interesting point to come from the work on complaints is in respect of how people know to complain to the Claims Management Regulator given that there has been little publicity about the role of the Regulator in dealing with complaints. It seems that what most people have done when they are dissatisfied with the service provided by a claims management company is to look for details of the company on the Internet so as to be able to make a complaint. They then find the Claims Management Regulation website as the company will be listed on this site. When they go into the website they find that they are able to make a complaint. Alternatively, they find the complaints procedure on the business's website – the Rules of Conduct requires complaints procedures to be on websites. This usefully illustrates just how the Internet has transformed communications.

8. Personal injury

8.1 Personal injury was by far the largest sector being regulated. 1,385 businesses said that they intended to operate in this sector and the estimated annual size of the market was £174 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 "after the event" 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 did not make running the claim worthwhile.
- Outright fraud, particularly as a result of contrived accidents.

Misleading advertising

8.2 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). Problems were more apparent at a very local level, in particular leaflets, and also on websites. The Conduct Rules deemed websites to be advertising, and websites are also subject to the Electronic

Commerce Regulations. All websites were scrutinised as part of the application process. Businesses were required to –

- Comply with the ASA Help Note on use of the expression "no win no fee". Use of this expression has been sharply reduced and misuse almost eliminated.
- Comply with the Electronic Commerce Regulations by including a physical address.
- Remove any misleading content.

Cold calling in person

8.3 This area has been a high priority and a large amount of resources have been employed to achieve an impact on the market. The approach has been –

- Make the requirement clear and unambiguous, emphasising that the approaches of the SRA and the Department are identical.
- Deal vigorously with queries that seek to soften the definition of cold calling. Following a number of such challenges the Guidance Note on Marketing and Advertising Claims Management Services was amended to include the following –

  "Client specific rule 4 states that "cold calling in person is prohibited". There have been a number of questions on what is meant by cold calling in person. The term should need little explanation. Any face to face contact initiated by the claims management businesses is cold calling in person. This includes knocking on doors and approaching people in the street or shopping centres, including what is known as "clipboarding". It is permissible to have a booth or stand in a shopping centre or exhibition as long as the people manning it do not attempt to make the first contact."
- Seek evidence from other claims management businesses and solicitors, and also local authorities and town centre managers. In fact such evidence has frequently been volunteered.
- Pass on details of solicitors, who take cases from those engaged in cold calling, to the SRA with a request that the appropriate action be taken.

8.4 Almost all the larger businesses engaged in cold calling have ceased this activity as a result of enforcement activity. However, the problem has not been eliminated. It will continue as long as solicitors are prepared to pay upwards of £500 for cases procured in this way. The effect of regulation has been to fragment this procurement method such that it is undertaken by individuals rather than businesses and then laundered through claims management companies. Although this is on a much smaller scale than the organised businesses, it is more difficult to deal with. There is therefore an

ongoing need to take enforcement action and also to work with the SRA to deal with those solicitors prepared to take cases acquired in this way.

Unauthorised marketing in hospitals

8.5 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.

8.6 The rules of conduct specifically prohibited marketing in medical establishments without the approval of the establishment concerned. The MCU has sought evidence by, among other things -

- Requesting hospitals to send copies of unauthorised leaflets and details of when they were left.
- Collecting such evidence itself.
- Collecting information from other businesses.
- Collecting information from solicitors that have been approached to deal with the company.
- Requesting information from the businesses thought to be involved in such activity.

8.7 Enforcement action has been taken against businesses found to have been engaged in such activity. As a result unauthorised marketing in hospitals has been virtually eliminated. This is demonstrated by the number of incidents of unauthorised marketing in hospitals recorded by the Monitoring and Compliance Unit –

Nov 06 – Jan 07	33
Feb 07 – April 07	41
May 07 – Jul 07	23
Aug 07 – Nov 07	2
Dec 07 - Feb 08	0

Note: the two leaflets found between August and November 2007 were old material with inactive phone numbers.

Clients being pressurised to make a claim

8.8 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.

The changing market for personal injury claims

8.9 Provisional statistics suggest a substantial increase in turnover by companies handling personal injury claims of 25% from £174 million in the year to 30 September 2006 to £218 million in the year to 30 September 2007. However, the two figures are not strictly compatible. An analysis of the 20 largest businesses in the first year of regulation shows that their turnover increased by an average of 18% in the year to 30 September 2007; this percentage is probably a better indication of the year-on-year increase in business. The most significant market trend seems to have been an increase in business on the part of uninsured loss recovery and other insurance company related businesses at the expense of stand-alone companies.

Views of insurance companies

8.10 As part of this exercise the views of some liability insurance companies have been sought. They believe that claims management regulation has been effective, particularly through –

- Sharply reducing cold calling which in turn has had a beneficial effect in reducing the more spurious claims. This has contributed to a reduction in the perceived "compensation culture".
- Preventing "rogues" coming into the market.
- Changing attitudes from a start-up market to a more mature market.

8.11 The main concerns of the insurers in respect of personal injury claims are now primarily in respect of the claims process, which permits high referral fees, and the conduct of solicitors.

Views of local authorities

8.12 With the help of the Association of Local Authority Risk Managers (ALARM) a number of local authorities were consulted about the impact of claims management regulation. Local authorities receive "slip and trip" claims and where they are housing authorities, also housing disrepair claims. Most made the point that they had taken steps to resist invalid claims which had been very successful. However, it was also considered that claims management regulation had contributed to a significant reduction in cold calling.

Future work

8.13 In addition to continuing the existing regulatory work there are two other areas that need consideration –

- Removing any scope for abuse of the "exempt introducer" concept, particularly by claims farmers claiming to be exempt and "refer a

friend" schemes. However, it should be noted that this is not an area where there is significant consumer detriment.

- Ensuring that the rules governing solicitors conduct and the Rules of Conduct are applied throughout the whole supply chain to solicitors. This is not a matter for the Claims Management Regulator alone. It is covered in the appendix to this chapter.

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 Rules require 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 If these Rules were fully complied with then there would be limited scope for malpractice by introducers. However it is clear that the Rules are not complied with. A report to the Solicitors Regulation Authority (SRA) in September 2006 indicated the extent of non-compliance. 135 firms were visited. In 34% of cases there was a complete lack of disclosure of the referral fee arrangements; in 17% of cases inadequate disclosure; in 47% of cases a failure to obtain an undertaking from the introducer to comply with the Solicitors' Code, and in 61% of cases a failure of solicitors to ensure that introducers were complying with the Code.

A.4 The claims management strategy for dealing with personal injury claims has been designed to help achieve compliance with the Rules Governing Solicitors' Conduct. Initially, solicitors played a valuable role in helping to ensure that introducers were authorised, as the SRA issued a helpful warning to solicitors that they must ensure that this was the case. The Rules of Conduct were drafted so that they dovetailed with the Rules Governing Solicitors' Conduct, in particular by the inclusion of a rule which requires that an introducer must not do anything which would put a solicitor in breach of the Conduct Rules. The Ministry of Justice has also had regular meetings with the SRA and has passed on relevant information to solicitors where appropriate.

A.5 However it remains the case that enforcement of the Rules Governing Solicitors' Conduct is ineffective. This was confirmed in a Report to the Board of the SRA in December 2007. The SRA visited 45 firms that had referral arrangements. In about two-thirds of the firms there was some

intelligence about the conduct of the firm that warranted investigation but in the remaining third of the firms visited there was no intelligence. The visit showed substantial non-compliance. Twelve of the 45 firms which had referral arrangements were recommended to be referred to the Solicitors' Disciplinary Tribunal with a note that the number "is likely to increase as casework progresses". It is significant that of ten firms selected on the basis of no intelligence, eight were considered to have committed misconduct. Of the 45 firms 20 had not acted in clients' best interests, 13 were breaching the Accounts Rules, 13 had compromised their integrity and in 11 cases there was a failure to account properly for commission.

A.6 The Report included an analysis of the results of 512 visits to solicitors' firms, which looked at compliance with the Solicitors' Introduction and Referral Code. A total of 815 introduction arrangements were examined with the following results –

- 315 (39%) involved failure to obtain an undertaking from the introducer to comply with the Code.
- 245 (30%) involved failure by firms to disclose their referral arrangements to clients in writing.
- 405 (50%) involved failure by firms to ensure that introducers provided clients with all relevant information.
- 672 (82%) involved failure by firms regularly to obtain evidence that introducers were providing clients with relevant information.
- 641 (79%) involved failure by firms to have copies of referrers marketing material.

A.7 This Code has now been replaced by the Solictors' Code of Conduct 2007. A further 149 introduction arrangements were examined after the new code was introduced with the following results –

- 72 (48%) involved systematic failure to obtain an undertaking from introducers to comply with the Code.
- 68 (46%) involved systematic failure by firms to ensure that introducers provided clients with all relevant information.
- 61 (41%) involved failure to give a client a statement that the solicitor's advice was independent and that they could raise questions on the transaction.
- 59 (40%) involved failure to confirm to clients that information would not be disclosed without the client's consent.
- 39 (26%) involved failure by firms to have copies of referrers' marketing material.

A.8 The Report concluded that, "there is evidence of systematic and persistent problems in solicitors properly managing their relationship with introducers, probably because of concern about potential loss of the flow of referrals".

A.9 The Board Report concluded "the dangers of non-compliant referral arrangements suggest that it will be necessary to continue close monitoring, particularly because of the potential conflict between the interests of clients, solicitors and introducers." The Board agreed to consider five different measures, none of which involved enforcement, and to conduct an information campaign.

A.10 The SRA as a Regulator operates in a very different way from many other regulators. The Ministry of Justice in its capacity as Claims Management Regulator, like many regulators, when it finds misconduct is able to take enforcement action including closing the business down. By contrast the SRA has to prosecute before a Tribunal. This is a lengthy and costly business and the SRA is able to embark on only a small number of such prosecutions in any year.

A.11 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.

9. Induced and contrived accidents

The problem

9.1 All regulators, however well they have planned, discover unexpected issues. For the Claims Management Regulator the main unexpected issue was induced and contrived accidents. There are several variations including cars being deliberately crashed, innocent people being induced into having accidents and fictitious accidents.

9.2 Based on these accidents, multiple claims are made for personal injury, vehicle damage, replacement car hire and vehicle towing and storage. Organised gangs are responsible for much of this activity, with a heavy concentration in certain parts of the country, notably West Yorkshire, Lancashire and North West London.

9.3 This is an attractive way for criminals to make money as it is relatively easy to earn large amounts and even if the insurance companies, who are generally the victims in such cases, are aware that there is fraud the most that they can do is to refuse to pay a claim. As with any enforcement agencies there are many competing priorities and the public are often not directly impacted by this kind of fraud, and fraud is not one of the Home Office targets for police forces. Therefore, most police forces do not tackle the issue. It is generally left to the insurance industry as best it can to deal with claims that they might perceive to be fraudulent.

Dealing with the problem

9.4 The Claims Management Regulator became aware of the issue as soon as applications for authorisation were received. There seemed to be an inordinately large number from small businesses describing themselves as accident management companies based in certain towns. Because they handled personal injury claims these businesses had to seek authorisation under the Compensation Act. Solicitors played a significant role in ensuring that such introducers sought authorisation.

9.5 The Claims Management Regulator made contact with the Insurance Fraud Bureau (IFB), the central body set up by the insurance industry to deal with organised fraud, and also the City of London Police (CoLP), which is the lead police force with responsibility for economic crime.

9.6 A short term strategy was agreed –

- Seeking information sharing agreements with the IFB, Insurance Fraud Investigators Group (IFIG), the Solicitors Regulation Authority (SRA) and the CoLP.

- Analysing claims management businesses, seeking to identify areas with an excessive concentration of businesses and evidence of informal franchise arrangements.
- Surveys of businesses in selected areas followed up by visits to businesses about which there were concerns.
- Using specialists from the insurance industry to participate in specific investigations.
- Working with the SRA, the Police and other enforcement agencies on specific cases.

9.7 This strategy was duly implemented. Support has been given to a number of police forces in specific operations and information has been supplied on request to police forces and to other enforcement agencies. A leading insurance company agreed to second one of its officials to the Monitoring and Compliance Unit. His input and assistance has proved to be invaluable in helping the Unit understand the issues and to deal with companies where there was some evidence of involvement in organised crime.

9.8 A series of visits took place to authorised businesses, particularly in West Yorkshire, the Midlands and Lancashire. Significant breaches of the rules were found in a number of cases. Where possible, the businesses were provided with the necessary advice to bring them into compliance with the rules and subsequent checks have been made to ensure that they continue to comply. In a number of cases information was passed on to other enforcement authorities, in particular HMRC in respect of evasion of VAT. More formal enforcement action is being considered in a number of cases.

9.9 In such areas, formal enforcement action is often difficult to implement and both costly and time consuming. A more successful tactic is disruption. Action taken by the Regulator significantly disrupted a number of claims management businesses where there was some evidence or involvement in criminal activity. One rather predictable consequence has been that some of the businesses have pulled out of referring personal injury claims, concentrating instead on vehicle damage and credit hire claims, the latter often being of very high value.

Co-ordinating a joint-up approach

9.10 Other agencies recognised that the Claims Management Regulator was in a pivotal position in respect of contrived and induced accidents, because many of the businesses involved in such activity had no choice but to seek authorisation and the Regulator had the power to seek information from and to audit them. Such powers are not available to the insurance industry or even to the Police unless there is clear evidence of criminal activity.

9.11 The Head of Regulation was asked by a number of agencies to convene an informal group of the various agencies with an interest in the subject. The group was duly convened and has met four times. Membership has gradually widened as other agencies have sought to become involved. Representation currently comprises a number of police forces and police agencies, the Serious and Organised Crime Agency, the Solicitors Regulation Authority, the Financial Services Authority, the Insurance Fraud Investigators Group, the Insurance Fraud Bureau and the Association of British Insurers, as well as the Ministry of Justice. These informal meetings have been useful in promoting contact between the various agencies and in sharing information about best practice and also specific businesses. The group agreed on an informal strategy with five elements –

- Identification of the major targets, primarily through the Insurance Fraud Bureau and police forces.
- Some prosecutions by police forces to send out the message that this is not a low risk crime.
- Spreading knowledge and best practice. There is recognition here that the problem is resources and priorities rather than evidence. In addition to the enhanced sharing of knowledge between members of the group, the City of London Police prepared a problem profile which was circulated widely, and the group agreed definitions of the various types of fraudulent accident.
- Appropriate regulatory action by the Claims Management Regulator and the SRA. Fraudulent personal injury claims are channelled through solicitors. The processes that the SRA has to use do not lend themselves to easy action, but the SRA is taking enforcement action against a number of solicitors. The role of the Claims Management Regulator has already been covered.
- Target hardening and disruption so that it becomes more difficult to make fraudulent claims. There is a role here for the insurance industry in spreading information about anti-fraud work and in developing best practice.

9.12 Generally, this is an area where the Claims Management Regulator can claim considerable success, primarily in acting as a catalyst to bring other agencies together and to help develop an agreed strategy. This was opportunist but appropriate. However, there is still unfinished business. There is no effective national strategy for dealing with such crime. While the insurance industry has got its act together in respect of sharing information and providing evidence to the enforcement authorities, there is little joined-up activity by police forces, and the SRA has not yet been effective in dealing with solicitors involved in such activity. The Claims Management Regulator has more work to do to ensure that authorised businesses are not involved in criminal activity. Again this is primarily a matter of resources.

10. Criminal Injuries Compensation

10.1 The Criminal Injuries Compensation Authority (CICA) pays out about £200 million a year. Claims management companies have a small part of the market. 160 applicants for authorisation reported turnover in criminal injuries and 438 indicated that they intended to operate in this market. Total turnover was £1.1 million. No individual business had turnover in excess of £100,000. The three largest companies were specialists, the remainder were predominantly personal injury businesses.

10.2 The Baseline Study identified that the main concern was "websites run by businesses that imply that they are part of CICA or have a connection with it."

10.3 The strategy for dealing with the sector, as set out in the Baseline Study, was –

- Scrutinise the websites of companies in the sector to ensure that they comply with the Rules of Conduct and advertising rules.
- Scrutinise the contracts used by companies in the sector to ensure that they are transparent and that there are no hidden costs.
- Use the client account rules to make it more difficult for businesses to conceal their costs.
- Ask the CICA to refer to the Department examples of businesses not complying with the rules. After it became an offence to operate without authorisation, the CICA could legitimately refuse to deal with unauthorised businesses.

10.4 This strategy has been implemented. Four companies were identified that were engaged in significant malpractice. Two of these have stopped trading and the conduct of the other businesses has improved.

10.5 The Regulator has worked closely with the CICA, which has duly refused to deal with unauthorised businesses and passed on useful information about businesses in the market.

10.6 Malpractice is this sector has been largely eliminated. 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. Significantly, the CICA is also advising businesses that only operate in Scotland that it would like them voluntarily to apply for authorisation under the Compensation Act.

11. Industrial Injuries Disablement Benefit

11.1 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 business is small scale. 60 applicants for authorisation reported turnover in the year to 30 September 2006, with 234 saying they intended to operate. Total turnover was £1.2 million. Five businesses reported turnover in excess of £100,000.

11.2 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 Department examples of businesses not complying with the rules.

12. Housing disrepair

12.1 The market seems small and local in nature. Just 21 businesses reported activity in the housing disrepair sector although 92 said that they intended to operate. Two companies accounted for most of the turnover of £0.3 million. There was some activity by claims farmers who sold cases on to solicitors. Malpractice has been addressed in the same way as for personal injury business.

12.2 Proactive compliance activity will be possible only with the co-operation of one or more large social landlords to facilitate the process. The offer of such co-operation has been made to social landlords.

12.3 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. Perhaps the main contribution of claims management regulation has been through the substantial reduction in "door knocking".

13. Employment claims

13.1 Again this is a small sector. 87 applicants for authorisation reported turnover in this sector, with 233 stating that they intended to operate. Turnover was £3.8 million. 13 businesses had turnover of over £100,000, but 30 were very small with turnover of under £5,000. Almost all the businesses were specialist and did not operate in the other sectors.

13.2 There were some initial difficulties contacting businesses in this sector while the regulatory regime was being put in place. There was no trade body to speak for the sector and many of the businesses were not known about. Most were also sole traders.

13.3 The contact difficulties with businesses in the sector meant that many did not know that they had to seek authorisation. Some Tribunals have taken the view that an unauthorised business could not represent a client. For these two reasons the decision was taken to fasttrack applicants in this sector. A second issue then emerged. Many employment advice businesses largely serve defendants, and may perhaps do a handful of cases a year for claimants. Only a small proportion of their turnover derives from regulated activities. A business turning over say £3,000 a year from representing claimants is unlikely to be willing to pay a £400 application fee and a £400 annual fee. A number of such businesses indicated that they would stop serving claimants to avoid the need to be authorised. It was partly to address this that the minimum annual fee was reduced from £400 to £100 in the second full year of regulation.

13.4 As part of the compliance programme contracts were requested from businesses in this market. The contracts generally were of a better standard than the financial products and services contracts. There were some unfair terms including cancellation/unfair penalty clauses, limitation/exclusion of liability clauses, entire agreement clauses and consumer 'read and understood' declarations. These are being addressed with the companies concerned.

13.5 It is as yet too early to assess any impact on the sector. The issues are around knowledge of the need for regulation and the quality of the service provided by claimants. These points have been discussed with the President of the Employment Appeals Tribunals and BERR. It has been agreed that the claim form will be modified to include reference to claims management regulation. Work is also being done to communicate with and through the employment tribunals.

14. Endowment claims

14.1 Handling endowment claims is the second largest market regulated under the Compensation Act. 145 applicants for authorisation reported turnover in financial services and products with 427 saying that they intended to operate. Total turnover was £67.7 million. However, most endowment mis-selling cases have now been dealt with and time barring is having an effect. The business has probably fallen by about 40% and is likely to fall further.

14.2 The Financial Services Consumer Panel published some research in November 2006 on consumers' experience with the endowment compensation companies. This showed a high level of consumer satisfaction. There seemed to be few complaints about the level of charges or the transparency. Two thirds of consumers were satisfied with the value for money they had obtained. 63% of consumers rated the service as good or extremely good, 17% as average and only 16% as poor.

14.3 The only significant negative comment was that 37% were concerned about an apparent lack of contact when the company had decided not to pursue a case. This is reflected in comments by insurance companies that many of the claims management companies do little other than write a single letter. They often refuse to provide the additional information needed to assess whether a claim is valid. If they are required to do some work on a claim, then they may well drop it knowing that there is easy money to be made on other cases.

14.5 A scrutiny of websites during preparation of the Baseline Study also indicated issues that needed to be addressed –

- Scare tactics, implying that it is difficult to make a claim directly.
- Failure to comply with the Electronic Commerce Regulations, in particular by not including a physical address.
- Misrepresentation of the chances of success if claiming directly. The ABI has 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.

14.6 There have also been allegations of cold calling by telephone contrary to the Direct Selling Association code.

14.7 The strategy for this sector, set out in the Baseline Study, has been –

- Scrutinising websites when applications for authorisation are made, in particular to remove scare stories about the difficulty of claiming directly and misleading comparisons.

- Requiring compensation to be held in client accounts.
- Reviewing contracts to ensure that they are transparent and to remove unfair contract terms.
- Using the complaints mechanism to limit the scope for companies to claim a share of the compensation when they have provided little service and the claimant has pursued the case himself.
- Working with the Association of British Insurers to encourage insurers to refuse to deal with unauthorised businesses, but protecting consumers through an assurance that the insurers would deal directly with claimants in such circumstances. Insurers have also been asked to report malpractice to the Department.

14.8 The Department has also worked closely with the Financial Ombudsman Service, which has been a useful source of intelligence about the development of the market and the nature of any malpractice.

14.9 This strategy has been fully implemented and is considered to have eliminated a great deal of the malpractice –

- Client Account rules were made in January 2007, coming into operation in April 2007. In practice insurance companies now generally insist in paying compensation directly to the client so the Rules are of relatively minor importance.
- During the authorisation process the websites of all, and the contracts of most, companies in this market were scrutinised. Significant changes were required, particularly to remove misleading claims about the benefits of using a claims handling company. A small number of companies had onerous clauses in their contracts, particularly where a fee was being paid up-front. These have been removed.
- The number of businesses in the market seems to be declining. Marginal participants may well have decided that a combination of falling business and the advent of regulation were too much for them to cope with.

14.10 It was anticipated that the complaints mechanism would deal with companies that tried to claim a fee when they had done little work. The first two formal complaints were duly along these lines. In both cases the complaints were rejected. The companies had a proper complaints mechanism in place and there was no evidence that the companies had acted improperly in handling the respective cases. It is in fact encouraging that the two companies had put in place effective complaints handling procedures, a welcome consequence of the introduction of regulation.

14.11 After authorisation, contracts were requested from all businesses in the financial products and services market. They were reviewed against the conduct rules and other relevant regulations. 16 contracts were identified as requiring substantial changes. The main problems were –

- Failing to give proper information in contracts.
- Failing to allow a 14 day cooling off period.
- Unfair penalty clauses.
- Contracts not in clear language.

14.12 The deficiencies were communicated to the businesses, which were required to demonstrate that they had taken the necessary remedial action.

14.13 There remain concerns about some malpractice mainly attributed to a handful of companies. The areas that have caused the most concern are –

- Taking an advance fee with a promise, which may not be reflected in the contract, that it would be refunded if the claim was unsuccessful and then either no refund being made if the claim was unsuccessful or it taking an inordinately long time to pay a refund.
- Where compensation is paid to the claims management company then a delay in passing this on to the customer.
- Claims companies not passing on details of all offers made by the insurance company.
- Poor service generally.

14.14 These problems have mainly come to light as a result of complaints and also reports from insurers. They are more difficult to deal with than problems in contracts or websites where the evidence is immediately available. They have been handled on an individual basis.

14.15 Insurers have found the regulatory arrangements to be helpful. They automatically check that any business that refers a case to them is authorised and they are prepared to report to the Regulator any evidence of malpractice. The authorised businesses know this and generally it has led to an increase in the quality of the service that they provide. However the insurers still report some malpractice as outlined earlier in this chapter.

14.16 The Association of British Insurers (ABI) has conducted a survey of its members on the impact of regulation in this sector. The main conclusion was that: "generally members were of the opinion that the new regulatory environment, together with significant shifts in the market, has had a positive impact and reduced serious malpractice. However, many still feel that CMCs do act in a manner that is detrimental to the interests of consumers."

The ABI continued –

"the most positive messages received from members can be adequately summarised from the quote below –

"Overall our experience since regulation has been positive, the CMCs have definitely taken on board the underlying messages included within regulation and now appear to be more professional in their approach. In addition the websites have improved and have become more professional with more appropriate information being advertised."

"A number of other firms echoed this positive view, with many recognising that since regulation the standard of websites has improved and the level of cold calling, that they are aware of, has reduced. However, a number did maintain that persistent cold calling still exists."

A specific point mentioned by the ABI was the "scatter gun approach", with CMCs submitting generic letters listing a large number of items.

14.17 The changing nature of the market is illustrated by figures extracted from the renewal process. Total turnover for financial products and services fell by 38% between the year to September 2006 and the year to September 2007.

14.18 The fall in endowment claims business was even greater as bank charge business increased significantly in the year to 30 September 2007. Seven out of the largest ten businesses reported a fall in turnover of in excess of 45%. Just two businesses that had been in the largest 20 in the year to 30 September 2007 recorded an increase in turnover in the following year. A number of companies seemed to have left the market completely.

14.19 The sharp downturn in business generally can cause problems for some companies in respect of cash flow and meeting fixed costs, modestly increasing the risk of fraud and malpractice generally. However the downturn was expected and this should have made it easier for businesses to deal with.

15. Other financial products

Bank accounts

15.1 In April 2006, the Office of Fair Trading held that default charges on credit cards contravened unfair contract terms legislation. Under the Unfair Terms in Consumer Contracts Regulations (1999) all penalty charges have to truly reflect the cost of administering them. The OFT's finding indicated that default charges in other consumer agreements, such as bank current accounts, may be unfair. In September 2006, the OFT launched an investigation into bank current account charges in agreements with consumers. The action encouraged the claiming back of 'unfair' bank charges. This happened as the regulatory regime was being put in place. This usefully illustrates the flexibility of the legislation. While the Compensation Bill was going through Parliament the issue was endowment claims, and the intention was to cover miss-selling of insurance products in the Scope Order. This would not have covered bank accounts as there is no miss-selling. Accordingly, the scope was widened to covered "financial products and services", which brought in bank charges.

15.2 From about September 2006 a significant number of businesses, perhaps 100 in total, began to offer a service in respect of bank charges. Some of these were companies that previously dealt with endowment claims. The business is fairly similar and the endowment claims companies were already aware of the Act. Surprisingly, a number were also in the personal injury market, where there is little synergy with financial products, but again at least they were aware of the Act. However, the majority have been newly established businesses seeing a market opportunity. The turnover figures reported in the year to September 2007 showed a number of companies in the bank charge market reporting turnover in excess of £500,000.

15.3 The strategy for dealing with these companies has been similar to that for the endowment claims companies. Websites and contracts were scrutinised and the British Bankers Association agreed to inform its members that they should not deal with unauthorised businesses, that they should deal direct with customers in such cases and that malpractice should be reported to the Regulator.

15.4 The first priority was therefore to ensure that such businesses went through the authorisation process. A website survey revealed some businesses, and others came forward as a result of banks refusing to deal with them. This coincided with the peak period for processing applications. This put such companies in a difficult position as after 23 April 2007 banks began to refuse to deal with them.

15.5 The strategy is considered to have been largely successful in stopping malpractice developing. As with endowment miss-selling, changes have been required to websites and contracts as a condition of authorisation. As any compensation is paid directly into bank accounts there is no chance of claims handlers hanging on to compensation. However, there has been a concern about some companies asking for payments up-front and some pretending to be acting on behalf of the MoJ or OFT.

15.6 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 Ministry of Justice immediately issued a Guidance Note to authorised businesses about handling of bank charge claims.

15.7 There are four possible final outcomes from the court case –

- The banks win, in which case the market for claims management businesses will disappear.
- The banks lose and agree proactively to refund charges in specified circumstances, in which case the market for claims management business also disappears.
- The banks lose but it is left to people to reclaim their bank charges, in which case a market for claims management companies will exist, although the press will probably explain how easy it is for people to claim directly.
- There is no definite ruling, each case having to be considered in the light of the specific contract and the circumstances of the case, in which case there will be a substantial market but handling claims will itself be a complex issue.

15.8 Many companies have a large number of outstanding complaints for which in many cases they will have taken a modest initial fee in order to obtain access to the bank records. There is naturally a concern that by the time the case is resolved the business may have been quietly forgotten about. Given that the fee paid by people to allow the claims company to have access to their bank record has been fairly small even if this happens it will not represent significant consumer detriment. However, there does remain a concern about the ability of all companies in this market to handle the business when eventually the legal uncertainties are cleared up. This is an area which will require careful monitoring. There is also concern where clients have paid a large up-front fee.

15.9 There remain some reports of telephone cold calling, with people given misleading information about the prospects of claiming. These reports are pursued.

Payment Protection Insurance

15.10 Payment Protection Insurance (PPI) is sold to borrowers alongside many standard credit arrangements including mortgages, car insurance and personal loans. The policy is intended to protect the consumer by covering repayments in the event that they are unable to work through illness or disability. Concerns about selling of PPI first arose in 2005. The Financial Services Authority published three reports between November 2005 and September 2007, each of which led to media reports that the miss-selling of PPI would be the next big compensation claim industry in the UK. In February 2007 the Office of Fair Trading (OFT) referred to the Competition Commission the supply of all PPI services. This reference was based on evidence that the features of the market prevent, restrict or distort competition and lead to poor value for consumers.

15.11 A number of claims management businesses providing services in the area of bank charges and endowment policies have expanded their services to include PPI claims. A few businesses dealing only with PPI claims have also been established. They generally charge on the basis as for endowment claims, that is taking 20 – 30% of compensation. However, a few charge a large up-front fee and then take a lower percentage. While it is clear that there has been miss-selling, it is less clear that there is scope for a significant viable compensation market. Unlike for endowment claims there is no procedure that insurers have to go through when a complaint is made. Also in the early years of a policy, premiums paid will be quite modest and therefore compensation is also likely to be modest. The market needs to be kept under close review, with the main concern being where up-front fees are taken. It is relevant that the ABI has identified a significant increase in PPI complaints in the last few months.

Other financial products

15.12 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. Wider issues

16.1 This chapter covers three impacts of regulation that are not specific to any sector but rather which have relevance to public attitudes and the impact of regulation generally.

The Provision of Information

16.2 One of the benefits of any regulatory regime is that those providing the goods or service are identified. In order to be authorised businesses have to give full contact details, and the regulator would normally provide that these are also fully accessible to customers by ensuring that websites, stationery and other documents comply with general legal requirements and that authorised businesses are listed on the Regulator's website. The Claims Management Regulator has duly done this. There is a list of authorised businesses on the claims management regulation website. This list includes trading names and addresses and is searchable by these variables and also by sector. Having information about those providing claims management services has proved to be useful to three different groups –

- The Regulator, who of course has very much more information than that published on the website.
- Those who receive claims, in particular insurance companies, but also other bodies such as employment tribunals, the Department for Work and Pensions and the Criminal Injuries Compensation Authority. It is understood that a number of insurers and the CICA always check any claim that comes from a claims company to ensure that it is authorised, and they refuse to deal with it and report it to the Regulator if it is not. Some businesses use a variety of trading names, sometimes to conceal their true identify, and again the website has made this more difficult.
- While the existence of claims management regulation cannot be expected to be known to the vast majority of the public who would ever deal with such a business, there will be a small number who have concerns about somebody providing claims management services. Through the website they can identify the business and if necessary report them to the Claims Management Regulator. The point has already been made that the flow of complaints to the Regulator has stemmed almost entirely from people finding details of the business on the list of authorised businesses on the Claims Management Regulation website when simply doing a search for the business name or by finding the business's complaints procedure on its own website.

Displacement

16.3 It is an inevitable consequence of any regulatory system that malpractice will be displaced to some extent. The task of those framing the regulatory regime is to limit the extent of that displacement, and it is equally important that there is some understanding of what displacement has subsequently occurred as this might be relevant to other government agencies and to government policy more generally. There is no hard evidence on displacement as a result of claims management regulation but a reasonable amount of anecdotal evidence, in line to a large extent with what was anticipated when the regulatory regime was put into place.

16.4 The most important displacement has probably been that some malpractice has shifted from businesses providing claims management services to solicitors. The monitoring and compliance arrangements of the Claims Management Regulator are more rigorous and effective than those of the Solicitors Regulation Authority. Those solicitors that in the past have obtained business that has been procured through intermediaries not fully in accordance with the rules governing solicitors' conduct may have found this more difficult following the implementation of claims management regulation. The logical response for such solicitors is to take the procurement activities in-house where they will be outside of the reach of the Claims Management Regulator. There have been some reports, particularly from local authorities, that this has happened in respect of 'slip and trip' and to a lesser extent housing disrepair. The difficulties that the Solicitors Regulation Authority has in enforcing its rules have already been noted, and this displacement point adds to that.

16.5 A second form of displacement has been in the field of contrived and induced accidents. Personal injury claims are just one of a number of insurance and compensation claims made by those committing this fraud, and it is the only activity that is subject to any regulation. The logical response of an accident management company handling fraudulent claims is either to cease handling personal injury claims, but at the expense of foregoing some of the profits of the activity, or to distance himself from the personal injury claims, which would mean those claims being handled by another business with whom there would be no formal business relationship. Normally one would expect this form of displacement to happen before the implementation of regulation. However, such was the speed with which claims management regulation was implemented that this seems not to have happened and some accident management companies engaged in fraudulent activity sought authorisation initially.

16.6 This form of displacement can be seen as part of a wider form of displacement from the regulated sector to the unregulated sector, in this case from personal injury claims which are regulated to motor vehicle and credit hire claims which are not. There are other compensation claims, for example in respect of holidays or white goods, to which potentially those engaged in malpractice could switch. However, these are small and do not lend

themselves to the sort of business that has happened in respect of personal injury and financial services.

16.7 The exempt introducer concept, while being necessary, gives scope for some displacement from authorised businesses to businesses that are not authorised, even though the Rules of Conduct require that those accepting business from exempt introducers ensure that they comply fully with the Rules of Conduct. More generally, where business is regulated then an extended supply or distribution chain is sometimes used to disguise malpractice. This probably has not happened in respect of claims management regulation, because the business is not large enough. However, there has probably been some fragmenting of the introduction chain to seek to take advantage of the exempt introducer rule. This may not be done in a way that complies with the rules in that the exempt introducer must be introducing cases that are incidental to his main business rather than being small scale. The Regulator has identified that this particular issue needs close watching.

16.8 Finally, it is worth noting another form of displacement which is partly relevant to claims management regulation but primarily has happened for other reasons. Over the years local authorities have been the targets for large numbers of compensation claims in respect of 'slip and trip' and housing disrepair. The extent to which the authorities have sought to resist such claims has influenced the extent to which they are targeted. Those authorities that have a comprehensive programme for dealing with claims, which typically would include seeking to meet claimants at the place where they allege the slip and trip occurred, challenging evidence which looks suspect and challenging the lawyers if they seem not to be complying with the rules governing solicitors' conduct, have been successful in cutting back claims, sometimes dramatically. The effect has initially been for malpractice to move to another local authority, such that it has been always the weakest local authorities that have been targeted. Generally, local authorities have considerably improved their performance in this respect but those that have not done so will remain vulnerable.

Compensation culture

16.9 The expression "compensation culture" means different things to different people, and whether there is such a culture is open to debate. No one wants to deny those legitimately entitled to compensation from seeking such compensation, but no one can support claims being made without justification because of the possibility of obtaining compensation from a soft target. While there is no hard evidence the impression seems to be that speculative claims have fallen, to some extent as a result of claims management regulation but also because defendants have been more rigorous in challenging such claims and the courts have been tougher on those making fraudulent claims. The expression "compensation culture" also seems to be less prominent than it was a few years ago.

Conclusions and future work

17.1 The regulatory regime for claims management activities is considered to have had a significant effect in removing malpractice less than one year after the Compensation Act 2006 received was fully implemented. 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.
- A strategy has been developed for dealing with contrived accidents, with the Department also taking a co-ordinating role for the various enforcement agencies and the insurance industry.
- 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 win" 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.

17.2 There is little hard evidence from other stakeholders on the impact of regulation. Some of these views have been covered in the chapters on specific sectors. A survey by the Monitoring and Compliance Unit of 30 authorised businesses in March 2008 included the question: "Do you feel regulation is improving the claims management market?" 87% said that they did.

17.3 The overall success can be attributed to a number of factors –

- The small size of the sector being regulated.
- The speed with which the regulatory regime was implemented; normally those engaged in malpractice have several years to rearrange their businesses before legislation is implemented.
- The interest that those receiving claims have in curbing malpractice and their willingness to refuse to deal with businesses that have not been authorised.
- The Regulator's strategy for achieving compliance with the Rules of Conduct.

17.4 There remains much work to be done, in particular –

- Combating unauthorised activity.
- Regular surveillance of websites and other marketing material to ensure that bad practices do not return.
- Eliminating all cold calling in person.
- Working with other agencies to tackle claims management businesses involved in crime.
- Reducing the scope for abuse of the "exempt introducer" concept.
- Ensuring that authorised businesses provide the necessary information about their ownership.
- Ensuring that contracts are not unfair and that customers are not subsequently treated unfairly.

17.5 Very relevant to personal injury claims but outside the scope of the Claims Management Regulator is the need to deal with the issue of the inability to tackle solicitors who do not comply with the rules governing solicitors' conduct.

Appendix 1

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 mi-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		

Appendix 2

Statistical analysis

Regulation has facilitated the development of a fairly accurate picture about the nature of the markets for claims management services. The regulatory regime has been designed so as to enable the necessary data to be captured and analysed.

Initially it was expected that 300 – 500 businesses would seek authorisation. In fact by February 2008 1,740 businesses had been authorised.

There is a rapid turnover of businesses in the market, not surprising given the low entry costs. Of the 1,740 authorised businesses, 979 were authorised after the initial deadline. Many of these were new businesses. Of the 1,740 businesses 1,036 (60%) said they were not trading in the whole of the year to 30 September 2006. Similarly, of the companies that renewed their authorisation about half said that they had not traded in the full year to 30 September 2007.

Of the 1,740 businesses that were authorised 414 (24%) were sole traders. Many of the 1,208 private limited companies were in effect one man businesses.

The flaky nature of many businesses in the sector was well illustrated by the poor quality of many of the applications for both authorisation and renewal. In addition 104 cheques bounced, 59 in respect of the application fee and 45 in respect of the annual authorisation fee. It might be expected that a business applying to be authorised would at least ensure that it did not send a cheque which bounced. It is also clear that many businesses that reported that they had contracts with clients, represented clients and held client money did not in fact do any of these things.

The "headline" statistics for the claims management industry are –

- About 1,700 businesses in total, of which about 420 are in the financial products and services markets and 1,400 in the personal injury market, some of the latter also being in the other markets. There is a rapid turnover of businesses.
- Total turnover of about £250 million. In 2005/06, 70% of this turnover was in personal injury and 27% in financial products and services. In 2006/07 these percentages changed significantly to 81% and 17%, reflecting a sharp decline of about 40% in financial products and services business and an increase of 20% in personal injury business.
- A fragmented industry in respect of personal injury claims. In the first year the largest ten businesses account for 70% of turnover in the financial products and services sector and 39% in the personal injury sector.

A more detailed statistical analysis will be possible when the outcome of the renewals work has been fully assessed.