A new regulatory model – local and central government partnership

Mark Boleat

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Executive summary

- The regulatory structure under the Compensation Act 2006 uses a local authority trading standards service, under contract, to provide national frontline regulation services.
- Government is continually extending regulation to new areas.
- Having rules with no means of enforcement is ineffective and potentially dangerous.
- Government policy is that there should be "no new regulators" unless there is no alternative.
- Establishing a new regulator is an expensive and time consuming process.
- A local authority trading standards service can provide effective "frontline regulation" on a national basis at a significantly lower cost than traditional models.
- The model enables the local authority networks to be used effectively.
- The model is flexible, capable of being upsized or downsized at relatively short notice.
- To be effective a regulatory regime must –
    - Be based on a full understanding of the marketplace and the malpractice.
    - Effectively identify market participants.
    - Identify the "pressure points" though which regulation can be made effective.
    - Use the application process to capture essential information about market participants and require them to certify that they comply with the rules.
    - Take early enforcement action to demonstrate that the rules must be complied with.

Introduction

In July 2006 the Compensation Act became law, providing for the regulation of businesses conducting claims management activities. The Claims Standards Council, a trade body set up to provide self-regulation, was given the opportunity to demonstrate that it could be the regulator. In January 2006 it became clear that the Council could not fulfil this role. Other options were considered, including establishing a new NDPB, regulating by a unit within the Department for Constitutional Affairs (DCA) and using an existing regulator (the Law Society, the Financial Services Authority and the Office of Fair Trading were possibilities). For various reasons none was appropriate. The fallback position was that the Secretary of State would be the regulator, but the DCA recognised that it did not have all the skills and resources needed to exercise the whole of the regulatory function. Local authority trading standards services were looked at as an option for providing frontline services, particularly as the sort of malpractice that the Act was

intended to deal with (misleading advertising, aggressive selling, hidden costs etc) were the sort of activities that they dealt with all the time. This option gradually found favour, particularly as there was no obvious alternative, and as ministers were committed to introducing the regulatory regime by the end of the year.

The decision to go with the local authority option was taken in April 2006. Formally, the Secretary of State would be the Regulator. His powers would be exercised by a senior DCA official (a suitable qualified person on a short term contract) with frontline services (authorisation, monitoring, compliance and enforcement) being provided by a Monitoring and Compliance Unit (MCU) run by a local authority. Local authorities were invited to submit expressions of interest in running the MCU in July 2006 while the Bill was before Parliament. Three local authorities submitted proposals. Two local authorities were shortlisted and invited to submit proposals by September. Staffordshire County Council was appointed early in September and began work a few days later. DCA had meanwhile carried forward work on implementation and had appointed a Head of Regulation to be responsible for implementation. Applications for authorisation were invited from 30 November 2006, just five months after the Act received Royal Assent. It is intended that the offence of operating without authorisation will be implemented from April 2007.

The total cost of implementing the regulatory regime is around £0.8 million a year, most of which is in respect of the MCU. Most, if not all, of this will be recouped by authorisation fees. The Regulatory Impact Assessment that accompanied the Bill had estimated annual costs of £4.2 - £4.7 million for an NDPB and £1.5 - £2.1 million for a frontline regulator with oversight by the Secretary of State.

The speed and cost of putting the arrangements in place compare very favourably with the alternatives, particularly that of establishing a new NDPB.

The arrangements are described in more detail in the Appendix.

The inexorable spread of regulation

It may be argued that as the government is committed to reduce the regulatory burden there is no need to consider new regulatory models. However, this would be unwise. Even if the burden is reduced there is still a case for looking at more effective models for managing existing regulations. And in practice regulation will continually be extended to new fields, both as new issues arise which require regulation and as ministers respond to pressure to regulate when malpractice is identified.

Among the new regulatory regimes that have been set up over the last few years or which are in the process of being established are –

- Regulation of gangmasters under the Gangmasters Licensing Act 2004.
- Regulation of claims management businesses under the Compensation Act 2006.
- Further regulation of estate agents through the Consumers, Estate Agents and Consumer Redress Bill currently before Parliament.
- Regulation of money service businesses, on which the Treasury is currently consulting.
- A new regulatory structure for the legal services industry.
- Regulation of home reversion plans by the FSA.

The danger of regulation without enforcement

When something goes wrong there is always pressure on government to introduce legislation to regulate the activity. Legislation is sometimes seen as a solution in itself, as if by passing a law

against malpractice then that malpractice will automatically stop. Often there are calls to introduce legislation to regulate activities that are already regulated, but where there has been no enforcement.

The best example of this recently is the Gangmasters (Licensing) Act 2004. The legislation began as a Private Member's Bill introduced by Jim Sheridan MP. In making the case for the legislation, he said: "Rogue gangmasters are exploiting workers, undercutting legitimate labour providers, defrauding the taxpayer and engaging in a range of criminal activities. They are bad for workers, bad for business, bad for taxpayers and, more importantly, bad for our society, yet there is no law to regulate them." In fact, there is a battery of laws governing the provision of labour. And it is by definition wrong to argue that there are no laws dealing with criminal activities as such activities exist only if there are laws. Mr Sheridan's line was supported by the Minister: "lawbreakers are responsible for considerable Exchequer fraud, health and safety offences, failure to pay the minimum wage and the use – rather the abuse – of illegal labour. Other forms of non-compliance are often associated with the exploitation of gang workers." As a result a law was passed which basically requires labour providers to comply with other laws.

There are no specific mechanisms to enforce many laws. Rather the police or local authorities or other bodies are given the responsibility. They have limited resources and have to decide where to concentrate their efforts. Naturally they do so on areas where there is most consumer detriment and where they can be effective, although increasingly they now do so to meet government targets. This means that there are areas of the law where enforcement is negligible. The areas fall into two broad categories –

- Areas where there is no significant detriment. A good example is the legal requirement on those employing children of school leaving age to have written parental and local authority consent (a BRTF report indicated that this was not observed in about 90% of cases).
- Areas where enforcement is too difficult – legislation on employing illegal workers, and rogue estate agents, builders and garages. In the latter three cases the consumer is often not aware that he has been ripped off; mystery shopping and proactive enforcement is needed if the law is to be enforced.

Where there is no enforcement the legislation can worsen the problem. Crooks are generally are too willing to say that they are "strictly regulated under the XXXX Act" and even to advertise that they are government approved. This point has been illustrated with the Gangmasters (Licensing) Act 2004. The provision of labour lends itself to malpractice. Tax evasion is easy. A labour provider can engage workers, pay them cash so both evade tax, and supply them to a packhouse at a rate well below that of legitimate labour providers. Prior to the Act some labour users, pressurised by the supermarkets, at least did some due diligence on the labour users, as they did not want to be accused of involvement in illegal activities. However, a number of crooked labour providers had no trouble in obtaining licences and could in effect market themselves as government approved. Labour users could feel free to use labour providers that had been licensed even though they knew that the rates they were charging were such that tax evasion was taking place. Licensing can therefore give respectability to the illegitimate.

Government policy on regulatory structures

The Hampton Review of regulation was published on Budget Day in March 2005 and the conclusions were immediately accepted by the government as a whole without any external consultation. The proposals are now in the process of being implemented.

The report recommended that the administration of new policies and regulators should be based on a set of principles. These are reproduced below.

- "Regulators, and the regulatory system as a whole, should use comprehensive risk assessment to concentrate resources on the areas that need them most;
- Regulators should be accountable for the efficiency and effectiveness of their activities, while remaining independent in the decisions they take;
- All regulations should be written so that they are easily understood, easily implemented, and easily enforced, and all interested parties should be consulted when they are being drafted;
- No inspection should take place without a reason;
- Businesses should not have to give unnecessary information, nor give the same piece of information twice;
- The few businesses that persistently break regulations should be identified quickly, and face proportionate and meaningful sanctions;
- Regulators should provide authoritative, accessible advice easily and cheaply;
- When new policies are being developed, explicit consideration should be given to how they can be enforced using existing systems and data to minimise the administrative burden imposed;
- Regulators should be of the right size and scope, and no new regulator should be created where an existing one can do the work; and
- Regulators should recognise that a key element of their activity will be to allow, or even encourage, economic progress and only to intervene when there is a clear case for protection."

The report said that a major problem with the current regulatory structure was the problems caused by complexity, in particular overlapping areas of responsibility and small bodies having limited efficiency in the use of resources. The organisational problems of small bodies are analysed in paragraphs 4.26 and 4.27 which are reproduced below.

> "4.26 While smaller regulators can create small centres of expertise, they do not benefit from the sharing of experience and expertise that larger organisations can more readily embrace. The complexity of structure at a national level can be seen in the proliferation of small regulators – 31 regulators within the review's remit have fewer than 100 staff, and twelve have fewer than 20. Regulators of that size are unlikely to be able to allocate resources efficiently, and lack political and institutional prominence. Within themselves, they cannot carry out broad risk assessments, or easily understand the cumulative burden of the regulations they are imposing. More broadly, it is difficult for Government to allocate resources to areas of importance if funding for regulation is balkanised among so many different bodies.
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> 4.27 Further, the existence of a large number of national regulators, with their different cultures, approaches and focus on specific market segments or business activities, significantly inhibits the prospect of introducing a collectively agreed approach to risk assessment of inspection programmes and form filling requirements. A more consolidated regulatory landscape would allow not only the introduction of a more uniform approach to risk, but also simplify the process of ensuring that the national regulations adopt and mainstream Hampton principles."

Hampton concluded that no new regulator should be created where are existing one can do the work and that consolidation of regulators should take place around key regulatory themes. One of the themes was "consumer protection and trading standards". The intention was that a new body would bring together the consumer protection work of the Office of Fair Trading with the responsibility of overseeing the work of local authorities on trading standards issues. However, at the end of 2005 in the Pre Budget Report the Chancellor announced that the proposal to establish a new body had been abandoned. Instead, a Local Better Regulation Office would be established and that he OFT would take over the other functions envisaged for the new regulator.

Regulatory bodies

Where an activity is being subject to regulation an existing regulator can take on the task. The Financial Services Authority has had its remit steadily extended in this way, taking on for example insurance intermediaries and mortgage intermediaries and lenders.

The more usual model where a new activity is subject to regulation is to establish a new regulator. This normally, although not always, takes the form of a non-departmental public body (NDPB). Typically, the primary legislation will provide for regulations to prescribe the detail of the constitution and method of operation of the regulatory body. After the Regulations have been made the chairman and other members of the regulatory body are recruited, using the standard public appointments procedures. The first chief executive may well be a departmental appointment or may be recruited at the same time as the Chairman. The whole process is likely to be quite protracted, as can be illustrated by one of the smaller regulatory bodies, the Gangmasters Licensing Authority –

- June 2004 Gangmasters (Licensing) Act received Royal Assent.
- July 2004 consultation begins of the constitution and structure of the Gangmasters Licensing Authority.
- January 2005 Chairman and Chief Executive appointed.
- October 2005 Consultation begins on rules of conduct.
- March 2006 Rules of conduct finalised.
- May 2006 Applications for licences begin.
- October 2006 Offence of operating without a licence.

It was therefore 28 months between enactment of the legislation and the legislation being fully implemented. This procedure and the timescale have a number of disadvantages –

- The long timescale mean that the nature of the problem may change between enactment of the legislation and the legislation coming into effect. In particular businesses at which the regulation is targeted have ample time to work out how to minimise the impact of the legislation and to reorganise their activities accordingly.
- The people responsible for implementing the legislation are often different from the people responsible for its content. Practical implementation issues may not be given sufficient weight, and there is scope for the two groups of people to blame each other when things begin to go wrong.

Establishing a new regulatory body is itself expensive; generally new resources are acquired rather than existing resources being used. The Gangmasters Licensing Authority has a board of 30 (admittedly all but the Chairman unpaid), a staff of 45, an office in Nottingham, a human resource function, a corporate service function and an IT function. Finance and corporate services alone are budgeted at £359,000 in 2007/08.

The partnership model using a trading standards service

The trading standards model can be summarised as follows –

- The legislation provides for the relevant Secretary of State (or the Office of Fair Trading for which the model is equally applicable) to be the regulator.
- The Secretary of State appoints an official (who may an outsider with suitable regulatory experience) to exercise his powers. That official is in effect "the regulator" and needs to have a public profile as such rather than being an anonymous civil servant.
- A specification is drawn up for a trading standards service to provide frontline services – conducting the authorisation process, monitoring, compliance and enforcement. Local authorities are invited to submit expressions of interest; a short list is then drawn up for a formal evaluation process and an appointment duly made. The specification should provide for the service to begin within a short time of selection and should be flexible. There should be no requirement for a detailed listing of inputs but there should be a requirement for upsizing or downsizing during the life of the contract. Three years is probably the right time for the initial contract. The timescale for inviting expressions of interest and then for making full proposals should deliberately be tight; local authorities unable to respond quickly are not the sort of organisations that are capable of running frontline regulatory services.
- A contract is duly entered into between the Department and the local authority.

The model is not appropriate for all type of activity. The activity must be one for which the skillset of local authority trading standards services is appropriate. The characteristics of such services include –

- A licensing or authorisation regime.
- A large number of market participants – certainly over 300.
- Businesses in the market being relatively small scale with most operating locally.
- Malpractice largely being in respect of dealings with the public.

A key issue is the price of the contract. There are two broad approaches that can be used in the tender exercise –

- Specifying tasks and outcomes and the price within which they must be achieved and asking local authorities to explain how they would approach the task and with what resources – the approach used for the Compensation Act.
- Specifying tasks and outcomes and asking local authorities to quote a price.

With either approach the department has to have in its own mind a reasonable price for the contract. It will need to look at the experience of other regulators, come to a view about the sort of regulation it wants (basically how intrusive) and also make an assumption about the number of businesses that will seek authorisation or licences. On the final point is it sensible for the contract to be based on a range of possibilities with an agreement that if the number is higher then extra funding will be provided (which should not be difficult to fund as extra revenue will be obtained from those seeking authorisation or licences).

The official appointed as regulator and the head of the local authority unit will between them draw up the policies and procedures needed to implement the regulatory regime and a business plan to implement them. The official has a crucial role to play. He or she must ensure that that the local authority "delivers" and that the requirements of the department are met.

The benefits of the model are –

- The local authority will to some extent be able to draw on its existing resources – offices, IT and staff. This will be cheaper that starting afresh, and the operation can be up and running within a month.
- Local authority officers will have experience in dealing with the sort of malpractice the regulation is concerned with.
- The trading standards service can use its contacts in the local authority and in the trading standards community to ask for information and help.

Effective regulation

The substance of regulation is more important than the structure, although the right structure makes effective regulation easier to implement. There are some general lessons to be learned from the establishment and operation of regulatory regimes -

- Establishing a new regulatory regime takes too long. Four years from a decision being taken and two years from Royal Assent to the offence of operation without authorisation is not unusual. Momentum is lost, top quality staff tend to be moved on to the next project and there is a risk that by the time regulation is introduced the world has changed significantly.
- The market adapts to regulation. The regulatory framework is a factor any business has to take into account in planning and implementing its strategy. It may reorganise its business to circumvent regulation. Predictions of the number of businesses that will be regulated can prove wide of the mark for this reason (the Security Industry Authority and the Gangmasters Licensing Authority both suffered this problem). This point is connected with the previous one; the longer the lead-in time the more the market is able to adapt.
- Policing the perimeter is always a problem. Wherever the line is drawn there will always be those just on the other side of it and those able to move to the other side. This factor combines with the previous one – one of the key judgements is where to draw the line.
- There is often a failure to understand the nature of the business being regulated with no adequate market analysis being undertaken. A comprehensive analysis is necessary at an early stage of the process as an essential input into the design and operation of the regulatory regime. The regulator should take responsibility for this study, using consultants only to provide an input.
- Regulation invariably tends to go wider than was initially intended (the Gangmasters Licensing Authority covers high street employment agencies and in the security industry there was a debate as to whether stewards at cricket matches should be covered).
- While regulators all claim to focus on substance, in practice there is a focus of process. This is largely because the people responsible for monitoring and compliance work are by nature experts on process.
- Related to the previous point, regulators tend to focus on those who are most visible and who have records that can be inspected.
- Enforcement is more important than rules or penalties. If people believe they will not be caught the penalty is of little significance.
- Regulation is a very blunt instrument.
- Regulation has unintended, although frequently predictable, consequences. The regulator needs to be able to adapt to these.

A new regulator to bear these points in mind, partly to ensure that expectations are realistic and partly to factor then into the design of the regulatory structure, in particular by seeking the most effective way of securing compliance.

There are some basic rules for establishing an effective regulatory regime –

- Careful planning and appropriate project management.

- Extensive efforts to understand the activities being regulated, mainly through contact with the industry and other stakeholders.
- Concentration on the main objective and the big issues.
- Liberally borrowing from others and avoiding the "not invented here syndrome". For example, the Claims Management Regulator borrowed the application form, professional indemnity insurance rules and the fee scale from the FSA and the client account rules from the Council for Licensed Conveyancers.
- Setting a realistic timetable and sticking to it.
- Taking full account of practical issues in drafting the legislation. Often it is only by drafting the final rules that what is required in legislation becomes clear.
- Engaging in extensive and meaningful consultation. The primary objective of the consultation programme is to ensure that the final rules achieve the objectives of the regulation. The consultation process serves an additional purpose of helping inform claims management businesses about the legislation and helps secure their buy-in. Effective consultation must include –
    - Formal consultation exercises.
    - One-to-one meetings with the leading industries bodies and individual companies.
    - If there is not an effective trade association for the sector being regulated then helping to create one by leaning on the major industry participants. An effective trade association can make a major contribution to the introduction of a new regulatory regime by acting as a channel for communications and providing a useful sounding body for early stage consultation.
    - Commissioning expert reports were appropriate.
    - Holding meetings of all interested parties where competing views can be debated. Bilaterals enable stakeholders to express views that go unchallenged and do not expose them to the views of others. A consultative group is far more likely to lead to outcomes which will have broad support. DCA established a Regulatory Consultative Group in July 2006; it has since met approximately monthly and has had a very valuable input into the secondary legislation and the implementation of regulation.
- The application process should be a key part of the regulatory process. The application form (which itself should be the subject of formal consultation) should be designed to give the regulator the information he needs about the business and also to force the business to confirm that it complies with the conduct of business rules.
- The monitoring and compliance programme must be capable of having an immediate impact. It needs to be designed so that businesses will understand immediately that enforcement is built into the system.
- A comprehensive communications programme, built around a website.

Using the principle to enforce existing rules

The paper so far has dealt with a new regulatory regime. However, there is a slight variation which should be considered which is based on three critical assumptions –

- Legislation is already in place to deal with most forms of malpractice.
- Rules are not enforced because there is no means to do so.
- Registration provides a valuable function in itself by providing essential information about market participants and facilitating the enforcement of rules.

The variation involves a legal requirement on businesses to register and to pay a registration fee the proceeds of which would be used to fund a monitoring and compliance unit that could be

based either in the OFT or more likely in one or more trading standards services. The registration form would require essential information about the business and the people running it and could also require the business to confirm that it complies with specific legal requirements. The monitoring and compliance unit would devise a strategy for dealing with malpractice that might include paper returns, inspections on a risk assessed basis and mystery shopping followed by prosecutions using existing laws and procedures. Such a model could work effectively in sectors such as the building trade, car repairs, estate agency, travel agency and undertakers.

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Mark Boleat
Head of Claims Management Regulation
Department for Constitutional Affairs
Tel: 07770 441377
E-mail: mark.boleat@btinternet.com

Appendix The Compensation Act Structure

The Compensation Act 2006 was enacted very quickly. The decision to legislate was taken by the Department for Constitutional Affairs (DCA) in May 2005; by July 2006 the Act had become law. Its basic purpose is to regulate the activities of those who provide claims management services. It was thought that there were about 500 such businesses, together many small scale introducers. The activities ranged from representation — similar to a service provided by a lawyer — through to case management and referral. Most such businesses were not already regulated for any purpose; some were regulated by the FSA for their insurance activities. Basically however, the regulation was of a fairly small number of businesses in a small market, worth no more than £400 million a year.

The Act
When the legislation was introduced a trade body, the Claims Standards Council, expressed a desire to turn in itself into a regulatory body, although there was no certainty that this could be achieved. The Act accordingly allowed for every type of regulatory structure. The Secretary of State was empowered to —

- Establish a new regulator.
- Designate an existing body to take on the role of regulator.
- Undertake the role of regulator.

Exploring the options
DCA explored all the options. A consultant was retained to advise on whether the Claims Standards Council could turn itself into an effective regulator. The report, and the Council's response to it, were conclusive - that the Council could not be the regulator.
DCA then explored the option of using an existing regulator. There were three possibilities: the Law Society, the Office of Fair Trading and the Financial Services Authority. However, none proved able and willing to take on the role.

This left direct regulation as the only option. DCA had no wish to provide frontline regulatory services itself and therefore looked at the outsourcing option.

The selected model
The model adopted has the following structure –

- The Secretary of State is formally the regulator.
- The Secretary of State has appointed an individual as "Claims Management Regulator" ("the Regulator"). That individual has responsibility for the implementation of the regulatory regime. However, he is not the designated "regulator" (although this would be an option) but rather exercises the powers on behalf of the Secretary of State. The individual must be a DCA official. A suitably qualified outsider was appointed as a temporary civil servant to hold this position.
- A Regulatory Consultative Group was established. This has no legal status or powers. It comprises nominees of relevant stakeholders. Its function is to oversee the operation of the regulatory regime and to provide advice and guidance to the Regulator.
- The administration of the regulatory regime and compliance and enforcement activity is outsourced on a three year contract to a Monitoring and Compliance Unit (MCU). This is responsible for handling and vetting applications for authorisation, maintaining a public register of authorised persons, monitoring authorised persons including running or managing an inspection process, enforcing the authorisation conditions, policing the perimeter and taking enforcement action. It has no responsibility that has formally been

delegated to the Regulator. Rather, it advises the Regulator when he has to take any decision, for example on the granting of authorisation, the removal of authorisation or prosecutions.

Consultation

The claims management industry was not an easy industry to understand let alone consult with –

- It was not a single industry; the businesses dealing with endowment compensation are not in the same market as those dealing with personal injury compensation. In effect there are two separate industries.
- Claims management businesses had little experience of regulation of any sort.
- There were, as always, substantial vested interests.
- There was no effective trade association.

The strategy for consultation involved –

- Formal consultation documents in accordance with normal practical.
- A series of seven consultation meetings around the country aimed at claims management businesses. In practice this was the only way that most of the industry was involved.
- One to one meetings with the major businesses in the sector and with other stakeholders such as insurers and representatives of the legal profession.
- Encouraging leading industry players to establish a proper trade association and involving that association in the consultation process. DCA officials attended all the early meetings of the association and spoke at its first annual meeting.
- The establishment of a regulatory consultative group comprising representatives of all relevant stakeholders – the industry, other regulators, trade bodies, consumer groups etc. In practice this was the forum in which the key issues were thrashed out. It is all too easy for a trade body or a consumer group to promote untenable arguments and to make a nuisance of itself in doing so. However, it is more difficult for it to do so when it has to defend its position from those with a different point of view. The consultative group also helped to ensure that each participant was aware of the views of the others. The consultative group helped ensure that there was a broad consensus in support of the final outcome.

Rules of conduct

There are only two predictable consequences of regulating an activity or a sector for the first time –

(a) the nature of the market will change as some businesses leave the market, some stay in the market but seek to avoid regulation and others restructure to take account of regulation;
(b) the regulation will have unintended and unpredictable consequences.

In devising the regulatory approach these factors have been taken fully into account. The regulations and rules have been drawn up on the expectation that people will seek to avoid them. The rules are simple and concentrate on a few key points –

(a) prohibition of high pressure selling, including cold calling in person;
(b) transparent contracts with no hidden or misleading charges;
(c) no misleading advertising or marketing material;
(d) disclosure of referral fees;
(e) a cooling off period;

(f) a complaints procedure;
(g) client accounts where client money is held.

The conduct rules are very brief, do not reproduce the laws or rules that already apply, concentrate on substance not process and do not go into fine detail.

The authorisation process

The authorisation process was seen at the outset as the being the critical part of the regulatory regime. A good authorisation process should –

- Deter those who engage in malpractice from applying because they know that they will not be authorised.
- Help to achieve compliance with the rules primarily through a self-certification statement.
- Provide essential information about the businesses that can be used subsequently in monitoring and compliance work.

Some regulatory regimes are built on the premise that companies are responsible for malpractice. They are not; people are. Accordingly a series of risk factors was drawn up –

(a) a history in respect of prosecutions, regulatory action etc;
(b) involvement in a large number of different businesses undertaking similar activity, particularly where some of the companies have ceased trading;
(c) involvement in businesses that have misleading marketing material or misleading contracts;
(d) involvement in high pressure selling and the improper generation of leads;
(e) involvement in businesses about which there have been a significant number of complaints;
(f) lack of transparency and competence.

These factors were applied both to the individuals and the companies concerned. That is –

(a) businesses that scored significantly on these factors were regarded as high risk as were the individuals involved in them, even if the individuals did not score on the indicators;
(b) individuals that scored significantly on these factors were regarded as high risk as were the businesses they were involved in, even if the businesses themselves did not score on the indicators.

The risk factors were used in the design of the application form. In particular the form asked for –

(a) details of directors, partners and anyone else capable of having a significant influence on the policy or management of the business;
(b) details of regulatory action against both the business and the individuals involved in it;
(c) details of all claims management businesses in which those involved with an applicant have been involved in the previous five years;
(d) self-certification that the business complies with the rules of conduct.

To enable the risk factors to be used in the authorisation process a database was constructed of all known claims management businesses and the individuals involved in them. The database includes evidence of the risk factors previously identified. The database was constructed from –

(a) complaints made to DCA and the Regulator;
(b) press reports;
(c) intelligence provided by interested parties (the nature of the activity being regulated means that there is no shortage of intelligence);
(d) a request for relevant information from trading standards services and other sources;

(e) some mystery shopping;
(f) an analysis of websites;
(g) an analysis of local advertising (there is little unsatisfactory national advertising);
(h) information provided by the Claims Standards Council.

All of the individuals identified on the application form, businesses they had previously been associated with and the applicant itself were checked against the database and other sources of information.

The application form requires applicants to certify that they comply with the rules of conduct. There are about 25 specific questions that applicants must answer. For example, applicants are asked to confirm that their advertising, marketing and other soliciting of business complies with the rules of conduct. Signing a false declaration will itself be adequate grounds for refusing authorisation.

Monitoring, compliance and enforcement
Some rules and regulations are difficult to enforce. The rules under the Compensation Act should be relatively easy to enforce. All claims for compensation are received by someone who is being asked to pay the claim and, other things being equal, would prefer not to, or at least would prefer not to have to pay costs to lawyers and other intermediaries. One would therefore expect that an insurance company or a defendant receiving a claim will check that any intermediary is authorised and is acting according to the rules. If not, they can refuse to deal with the intermediary and pass details on to the Regulator for action to be taken.

However, the Regulator will not be passive. Its monitoring and compliance work will include requesting information relevant to the risk factors. Such a request may be made to all authorised businesses, all businesses considered medium risk or all businesses undertaking a particular activity or working in a particular sector. A request could be for information such as –
(a) all marketing material and contracts (most relevant for endowment and criminal injuries compensation cases);
(b) all local advertising;
(c) complaints procedures and details of complaints;
(d) details of arrangements for client accounts;
(e) details of exempt introducers and the volume of business introduced by them.
(f) call centre scripts;
(g) annual accounts – in the case of companies;
(h) arrangements for ensuring that staff are competent and suitably trained.

The Regulator will also be doing its own monitoring work. This will include –
(a) mystery shopping, both on high streets and through responding to advertisements by phone;
(b) monitoring advertising in local markets;
(c) monitoring websites;
(d) working with other regulators;
(e) working with trading standards services in local markets.

Where there are reasonable grounds for concern about a particular business it can request specific information or can inspect the business.