

Compensation Act 2006

Regulation of Claims Management Services

**Consultation on the
Application Form for seeking
authorisation and
Fee Scales**

August 2006

CP(L) 18/06

COMPENSATION BILL
Consultation on the
Application Form for seeking authorisation and
on Fee Scales

Introduction

1. The Compensation Act 2006 received Royal Assent on 25 July. The Act is in two parts: part 1 covers the law of negligence and part 2 covers the regulation of claims management services. A copy of the Act and papers issued during the Parliamentary passage can be found on the DCA website at: (<http://www.dca.gov.uk/legist/compensation.htm>).
2. DCA issued a consultation paper on 6 July 2006 (CP(L) 12/06: Compensation Bill (Claims Management Services)). This sought views on key aspects of the proposed regulation of claims management services. It included:
 - the draft Scope Order¹ due to be made under section 4(2)(e) (*previously clause 3(2)(e)*) of the Compensation Act which will define the activities and sectors covered by the legislation;
 - the draft regulations that will be made under section 9 (*previously clause 8*) and the Schedule which cover the requirements for authorisation and other related matters.

The paper also sought views on the conduct rules the regulator will prescribe under paragraph 8 of the schedule to the Act. A copy of the paper is on the DCA website at:
<http://www.dca.gov.uk/consult/claimsmang/cp1206.htm>

The Regulator

3. The Secretary of State for the Department for Constitutional Affairs will be the regulator initially. A senior civil servant will act as Head of Regulation with a small DCA unit providing support. An external monitoring and compliance unit will undertake the key administrative tasks. DCA is in the process of identifying a trading standards unit to fulfil this role.

Timetable

4. The timetable for establishing the regulation is as follows:
 - October 2006 Regulatory mechanism set up

¹ Scope Order will define the regulated activities and the sectors that will be subject to regulation. Anticipate that the sectors to be included in the Scope Order will be, Personal Injury, Misselling of a Financial Product, Employment, Housing Disrepair, Criminal Injuries Compensation, Industrial Injuries Disablement Benefit.

- November 2006 Applications for authorisation invited
- February 2007 Deadline for submitting initial applications
- April 2007 Offence of providing, or offering to provide regulated claims management services commences

Application form

5. The Regulator is responsible for approving the form for persons to complete who are seeking authorisation to provide a regulated claims management service. The draft form at **Annex A** should be completed by the person seeking authorisation on behalf of the business to provide claims management services in one or more of the regulated sectors. We have designed the form to make it simple and straightforward to complete. It asks a series of questions which in most cases need confirmation that the business complies or will comply with the requirements for authorisation.

Question 1 – Do you agree with the format of the form? Is it straightforward and simple to complete? If you do not think so, please can you give reasons.

Question 2 – Would you find it helpful to have an explanatory note to accompany the form?

Part 1 - Details of the business

6. This requires the applicant to provide details of the business, the sectors that the company operates in and details of turnover for the individual sectors.

Part 2 - General requirements

7. This part of the form requires the applicant to provide specified information that will enable the Regulator to assess the business's competence and suitability to provide a regulated claims management service. The form also seeks confirmation from the applicant that the business will comply with certain regulatory requirements which will be mandatory conditions of authorisation.

Question 3 - Do you envisage any difficulties with providing the information in Part 1 and 2 of the form?

Part 3 – Client Rules

8. Part 3 requires applicants to confirm that it will comply with the Conduct Rules and in particular that it has in place appropriate mechanisms to inform clients of all costs and charges. It also seeks details on the type of relationship the business has with clients and how it manages a claim.

9. Part 3 of the form also seeks details of those persons in a controlling capacity within the business including any directors (in the case of a

company), partners (in the case of partnerships), chief executive or controlling shareholder (in the case of a company).

Question 4 – Are there any others within the business who control or have a significant role in the management or decision-making that should be added to the list?

Fee Scales

10. Paragraph 7 of the Schedule to the Compensation Act 2006 provides that the Secretary of State may make regulations to enable the Regulator to charge –

- (i) fees in connection with applications for, or the grant, authorisation;
- (ii) periodic fees for authorised persons.

11. Paragraph 14 of the draft regulations provide the necessary detail –

- (1) The Regulator must, by written instrument, determine—
 - (a) fees, or a scale of fees, for the making of applications under Part 3; and
 - (b) annual fees, or a scale of annual fees, for authorisations.
 - (2) A determination under paragraph (1)(b) may provide for the fee to be calculated by reference to the annual turnover or expected annual turnover of the business of the applicant or authorised person concerned.
 - (3) A determination under paragraph (1)—
 - (a) may make provision that applies generally, or only in specified cases or circumstances;
 - (b) may make different provision for different cases or circumstances; and
 - (c) may include transitional, incidental or consequential provisions.
 - (4) Before making such a determination, the Regulator must consult such persons as appear to him to represent the views of persons engaged in the provision of regulated claims management services, and such consumer organisations, as he considers appropriate.
 - (5) A determination under paragraph (1) may provide for an applicant or authorised person to pay a reduced fee if the Regulator is satisfied that the applicant or authorised person's total income from claims management activities is, or is likely to be, less than an amount specified in the determination.
 - (6) A determination under paragraph (1) has no effect unless—
 - (a) except in the case of a determination by the Secretary of State while exercising functions of the Regulator, it has been approved in writing by the Secretary of State; and
 - (b) the instrument has been published in accordance with paragraph 0.
- The Regulator must publish the determination on its website, and must send a copy to each authorised person.

12. This paper sets out proposals for the fee formula that will be prescribed by the Regulator for the first year up to April 2008.

Entities that will seek authorisation

13. It is difficult to estimate how many businesses will seek authorisation and what size those businesses will be. The starting point is the RIA assumption of 500 claims management businesses. However, the number seeking to be authorised may be smaller because –

- Some businesses will not want to be subject to the regulatory regime and will cease operating
- Some businesses may merge
- Some businesses may re-organise their activities so as legitimately to avoid regulation

14. In addition the scope of the legislation goes beyond claims management companies, and includes individuals, some insurance companies and intermediaries and other organisations. This adds to the difficulty of making any estimates of total fee revenue at this stage. There will be a further consultation on exemptions shortly.

15. Other regulators have found that their estimates of the number of businesses that will seek to be authorised have been inaccurate. It is not possible to make a precise estimate of the number of businesses that will seek to be authorised or their size. It is proposed that fees will instead initially be set according to reasonable comparisons with the fees charged by comparable regulators and the work involved in regulation. It will soon become clear what income the fee scale will produce. DCA plans to underwrite the costs of introducing regulation and to support the initial costs of operating the regime.

Fees charged by comparable regulators

16. The fees charged by other Regulators provide a benchmark which can be used in determining the fees to be charged to claims management companies. There is also a sense in which a “level playing field” is appropriate given that claims management companies to some extent compete with other regulated organisations, in particular insurance companies, insurance intermediaries and solicitors. It is therefore appropriate to concentrate on fees charged by the Financial Services Authority (particularly as the FSA has been considered as a potential regulator for claims management activities), the Law Society and other legal services regulatory bodies.

17. The fees charged by the FSA in the current year are –

- Mortgage administrators and managers pay a minimum fee of £635. The scale runs from 0.538% of turnover to 0.225%.
- General insurance intermediaries pay a minimum fee of £400. The scale runs from 0.386% of turnover down to 0.039%.
- Independent financial advisers pay a fee in respect of each authorised person. The minimum fee is £1,605 and the scale is then £878 per

person for between 2 and 4 persons, £856 per person for between 5 and 10, £821 per person between 11 and 25, £757 per person between 26 and 150, £696 per person between 151 and 1,500, and £657 per person for more than 1,500.

18. The FSA also charges an authorisation fee of £1,500.

19. Looking at legal services –

- The Law Society charges an annual fee of £1,020 for a practising certificate.
- The Council of Licensed Conveyancers charges a flat fee of £880 per authorised conveyancer.
- The Office of the Immigration Services Commissioner charges an initial fee and then an annual re-registration fee. For “level 1” both fees are £555. For Level 2/3, for 1 – 4 advisers the fee is £1,700 initially and £1,250 annual re-registration fee; for between 5 – 9 advisers, £1,900 initially and £1,550 annual re-registration; and for 10 or more advisers £2,300 initially and £2,050 annual re-registration fee.
- The Institute of Legal Executives charges an annual fee of £156.

20. Other relatively small regulators charge the following fees –

- The Gangmasters Licensing Authority is levying a fee in its first year on a scale from £250 to £4,000, but the figures will more than double in its second year. There is also an initial inspection fee which costs between £1,600 and £2,500.
- The Commission for Social Care Inspection charges a registration fee ranging from £518 for small care homes to £1,901 for large homes. The annual fee ranges from £173 for small care homes up to £864 for children’s homes and £1,080 for domiciliary care services.
- The Security Industry Authority, which regulates the private security industry, has a standard fee of £190 for individuals. For its approved contractor scheme, there is an application fee of between £400 and £2,400 and an annual fee of £20 for licensable employee (£20 probably equates to about 0.1% of turnover). Using DTI definitions of the size of firms, a small firm has up to 25 employees and would pay annual fee at that level of £500. A medium sized firm has between 26 and 250 employees and would pay between £520 and £5,000. Companies also have to pay fees to independent assessing bodies.

Fixed or banded scale

21. Regulators can charge either a fixed fee, a modest scale or a scale related to the volume of business, either tapered or proportionate. The following factors are relevant in deciding between these options –

- The costs of regulation do not rise proportionately with the scale of the business.
- The more proportionate the scale the more that the regulatory fee reflects ability to pay.
- A small number of fixed fees with a low maximum makes administration easier and limits the scope for manipulation.
- A small number of fixed fees with a low maximum may create a barrier to entry for small businesses.
- The more that fees are proportionate to business the greater the fee income that will be derived.
- The small size of the claims management market is such that the Regulator is unlikely to be able to cover his costs.

22. Those regulators that regulate businesses as opposed to individuals generally adopt a scale related to the volume of business with a taper. It is proposed that this should be adopted for claims management businesses.

23. Claims management businesses are comparable in many ways to general insurance intermediaries. There is merit in simply using the FSA scale for these intermediaries. This is unlikely to produce revenue in excess of the costs of regulation. However, revenue should be sufficient and any shortfall can be met by the sum the DCA has budgeted for in the first year of operation of the Regulator. The current intention is to use apply the FSA scale for 2006/07 which is as follows -

FSA fee scale for general insurance intermediaries 2006 - 07

Annual income	Fee (%)
£0.1 - £1 million	0.386
£1 - £5 million	0.332
£5 - £15 million	0.240
£15 - £100 million	0.096
Over £100 million	0.039

Note: There is a minimum fee of £400. The figures apply to turnover within the band.

24. The following table shows how this translates into the actual fee paid by particular organisations.

Fee paid by general insurance intermediaries to FSA, 2005 - 06

Turnover	Fee £	%
£50,000	400	0.80
£100,000	400	0.40

£1 million	3,872	0.38
£5 million	17,100	0.35
£10 million	29,100	0.29
£20 million	45,900	0.23
£50 million	74,700	0.15

Calculation of turnover

25. The base should be turnover in the sector that is regulated under the Act. Depending on the business this could be commission (particularly in respect of introducers) or total turnover (in the case of stand alone claims management companies). In case cases a business may receive services (such as reciprocal business) in exchange for referring a claim. The value of such services needs to be included in the turnover figure.

Discounted fees

26. It is clear that there are a number of different business models in the sector. While it would be impractical to tailor fees precisely to each specific model it may be feasible to allow for discounts from the overall turnover generated fee linked to simple/broad categories of claims management activity. Views on this would be welcome.

Application fee

27. There is a cost involved in handling initial applications. Most regulators recognise this by charging an application fee in addition to an annual licence fee. The FSA charges a flat fee of £1,500 for “straightforward cases”. Such a fee should be based on the work involved. There is a minimum amount of work regardless of the size of the business being authorised. The work increases the larger the size of the organisation. It is proposed to levy application fees according to the following scale –

Turnover up to £1 million	£400
Turnover £1 – 5 million	£1,000
Turnover over £5 million	£2,000

Consultation questions on fee scales:

Question 1 - Should the annual fee be a fixed amount, a sharply truncated scale with a fairly low maximum or a tapered scale?

Question 2 - If a tapered scale is used is it appropriate to use the FSA scale for general insurance intermediaries initially? If not what should the scale be?

Question 3 - Is turnover in the regulated sector the appropriate base for levying fees? How should turnover be defined so as to ensure fairness between regulated businesses? In particular how can receiving services in exchange for referring claims be caught?

Question 4 - Any views you may have on applying a discounted fee rate linked to simple/broad categories of claims management activity.

Questions 5 - Is the proposed application fee scale from £400 to £2,000 appropriate?

Question 6 – If you are a claims management company please indicate how any views you have expressed would affect the fees you would pay and include evidence on the volume of activity in that sector of the market. This will help DCA make a more informed judgement on the final fee scale. Please state clearly if any information provided is considered market sensitive and therefore should be treated as a confidential annex to a public submission.

Summary

28. The questions above are just a general indication of the issues where we specifically would like further information but would welcome any general comments.

Comments

29. Comments on the application form and fee scales should be sent by **Monday 18 September 2006**. Comments can be sent by post or e-mail to:

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