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| Title: Insolvency Practitioner fees regime IA No: BIS InsS009 Lead department or agency: BIS Other departments or agencies: Insolvency Service | Impact Assessment (IA) |
| | Date: 16 April 2014 |
| | Stage: Final |
| | Source of intervention: Domestic |
| | Type of measure: Primary legislation |
| | Contact for enquiries: 020 7637 6365 |

| | |
|--|---------------------------|
| Summary: Intervention and Options | RPC Opinion: Green |
|--|---------------------------|

| Cost of Preferred (or more likely) Option | | | | |
|---|----------------------------|--|------------------------------|----------------------|
| Total Net Present Value | Business Net Present Value | Net cost to business per year (EANCB on 2009 prices) | In scope of One-In, Two-Out? | Measure qualifies as |
| -£16.01 | -£16.01 | £1.55m | In | £1.55m |

What is the problem under consideration? Why is government intervention necessary?

A report by the OFT in 2010 into the market for corporate insolvency practitioners (IPs) and a recent review by Elaine Kempson of IP fees, found that the market does not work sufficiently where unsecured creditors are left to 'control' an office-holders fees and remuneration, which occurs in just over a third of cases. Both reports found that fees charged to unsecured creditors can be higher due to unsecured creditors being in a weaker bargaining position than secured creditors. This can result in over charging by the IP and inefficiencies in administering the case, which leads to fees being higher than they might otherwise have been. The OFT and Professor Kempson proposed reforms to the regulatory framework and fee monitoring process to assist the weak position of unsecured creditors.

What are the policy objectives and the intended effects?

The policy objective is to strengthen the regulatory framework for IPs and the Recognised Professional Bodies (RPBs) that authorise and regulate them. This will be achieved by the introduction of regulatory objectives for the RPBs (see IA BIS InsS001), in particular an objective which ensures there is appropriate oversight of the fees charged by IPs ensuring they offer value for money. This includes appropriate monitoring and adjudication of fee disputes. The intention is to increase confidence in GB's regulatory regime and insolvency framework, and ensure better and more consistent outcomes for all stakeholders in insolvency cases including creditors, debtors and IPs.

What policy options have been considered, including any alternatives to regulation? Please justify preferred option (further details in Evidence Base)

- 1. Do nothing** – this would not address the market failure identified by the OFT and Professor Kempson.
- 2. Option 1:** Introduction of a regulatory objective which ensures that fees charged by IPs represent value for money. **This is our preferred option as it addresses issues raised in OFT market study and Professor Kempson's recommendations.**
- 3. Option 2: Alternatives to regulation.** Work with the regulatory bodies for IPs to draw up a voluntary code to ensure that they deal with complaints about fees.

| | | | | | |
|---|---------------------|------------------------------|---------------------|----------------------|---------------------|
| Will the policy be reviewed? It will be reviewed. If applicable, set review date: 05/2020 | | | | | |
| Does implementation go beyond minimum EU requirements? | | | No | | |
| Are any of these organisations in scope? If Micros not exempted set out reason in Evidence Base. | Micro Yes | < 20 Yes | Small Yes | Medium Yes | Large Yes |
| What is the CO ₂ equivalent change in greenhouse gas emissions? (Million tonnes CO ₂ equivalent) N/A | | | Traded: | | Non-traded: |

I have read the Impact Assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options.

Signed by the responsible MINISTER

Jerry Sillett

Date: 12.06.2014

Summary: Analysis & Evidence

Policy Option 1

Description: Regulatory changes to bring value for money within the regulatory framework

FULL ECONOMIC ASSESSMENT

| Price Base Year 2013 | PV Base Year 2013 | Time Period Years 10 | Net Benefit (Present Value (PV)) (£m) | | |
|-------------------------|----------------------|-------------------------|---------------------------------------|-------------|-----------------------|
| | | | Low:- 107.42 | High: -2.67 | Best Estimate: -16.01 |

| COSTS (£m) | Total Transition (Constant Price) Years | Average Annual (excl. Transition) (Constant Price) | Total Cost (Present Value) |
|---------------|--|---|-------------------------------|
| Low | N/A | 0.3 | 2.7m |
| High | N/A | 12.5 | 107.4m |
| Best Estimate | N/A | 1.9 | 16m |

Description and scale of key monetised costs by 'main affected groups'

The additional costs to the regulators in reviewing fee complaints will be **£12.5m pa (£107.4m NPV)** in the high complaint scenario, **£1.9m pa (£16m NPV)** best estimate scenario and **£0.3m pa (£2.7m NPV)** in the low compliant scenario. The majority of these costs relate to staffing and overhead costs in hearing fee complaints. This cost would be split between the 7 RPBs but may be passed onto the IPs they regulate.

Other key non-monetised costs by 'main affected groups'

None

| BENEFITS (£m) | Total Transition (Constant Price) Years | Average Annual (excl. Transition) (Constant Price) | Total Benefit (Present Value) |
|---------------|--|---|----------------------------------|
| Low | N/A | N/A | N/A |
| High | N/A | N/A | N/A |
| Best Estimate | N/A | 0 | 0 |

Description and scale of key monetised benefits by 'main affected groups'

None

Other key non-monetised benefits by 'main affected groups'

Unquantifiable benefits are increased efficiency in the market by addressing the market failure, IP market confidence, and consistency amongst regulators. This will also lead to benefits for creditors and debtors who should experience lower financial losses as IPs are less likely to over-charge knowing that the regulators have responsibility for ensuring fees represent value for money.

Key assumptions/sensitivities/risks

Discount rate (%) 3.5

Sensitivity analysis has been applied to the number of fee complaints that may be received by opening up the current system to such complaints. We have set out a **High scenario** (based on 2000 fee complaints being received and 340 appeals - 17% of total number of fee complaints), **Low scenario** (based on 50 fee complaints being received and 9 appeals - 17% of total number of fee complaints) and **Best estimate** (based on 300 fee complaints being received and 50 appeals - 17% of total number of fee complaints). As the only route to complain about fees currently is through the courts, which is costly, this is a best estimate on the data we have.

BUSINESS ASSESSMENT (Option 1)

| | | | | |
|---|-------------|-------------|--------------------------|----------------------------|
| Direct impact on business (Equivalent Annual) £m: | | | In scope of OITO? Yes | Measure qualifies as In |
| Costs: £1.6m | Benefits: 0 | Net: -£1.6m | | |

[TYPE TEXT]

Summary: Analysis & Evidence

Policy Option 2

Description: Voluntary code to bring value for money within the current regulatory framework

FULL ECONOMIC ASSESSMENT

| Price Base Year 2013 | PV Base Year 2013 | Time Period Years 10 | Net Benefit (Present Value (PV)) (£m) | | |
|-------------------------|----------------------|-------------------------|---------------------------------------|-----------|----------------------|
| | | | Low: N/A | High: N/A | Best Estimate: -2.67 |

| COSTS (£m) | Total Transition (Constant Price) Years | Average Annual (excl. Transition) (Constant Price) | Total Cost (Present Value) |
|---------------|--|---|-------------------------------|
| Low | N/A | N/A | N/A |
| High | N/A | N/A | N/A |
| Best Estimate | N/A | 0.3 | 2.7m |

Description and scale of key monetised costs by 'main affected groups'

Given the likely resistance from regulators to accept a voluntary code which requires them to deal with value for money issues and complaints, it is unlikely that they will consider all fee related complaints. It may be possible through continued negotiations to obtain agreement to open up the current system to some additional fee complaints (where evidence of excessive fee charging and abuse is extreme) but this is only likely to impact on a small number of cases and at best lead to an additional 50 complaints being considered (low complaint scenario).

The additional costs to the regulators in reviewing fee complaints will therefore be **£0.3m pa (£2.7m NPV)**. The majority of these costs relate to staffing and overhead costs in hearing fee complaints. This cost would be split between the 7 RPBs but may be passed onto the IPs they regulate.

Other key non-monetised costs by 'main affected groups'

No further costs to other groups are expected from this proposal.

| BENEFITS (£m) | Total Transition (Constant Price) Years | Average Annual (excl. Transition) (Constant Price) | Total Benefit (Present Value) |
|---------------|--|---|----------------------------------|
| Low | N/A | N/A | N/A |
| High | N/A | N/A | N/A |
| Best Estimate | N/A | Unknown | Unknown |

Description and scale of key monetised benefits by 'main affected groups'

None

Other key non-monetised benefits by 'main affected groups'

If this option was to be effective, it might deliver the same types of benefits as Option 1. However, given that there has been opportunity for the profession to take action voluntarily already, we do not think that this option would have sufficient impact and therefore the level of efficiency expected from this proposal is likely to be much lower than in Option 1.

Key assumptions/sensitivities/risks

Discount rate (%)

There have been opportunities for the profession to take voluntary actions in respect of fees, but little or no action has been taken. Therefore any benefits from a voluntary approach are expected to be minimal and much lower than any regulatory approach.

BUSINESS ASSESSMENT (Option 2)

| | | | | |
|---|--------------|-------------|-------------------|----------------------|
| Direct impact on business (Equivalent Annual) £m: | | | In scope of OITO? | Measure qualifies as |
| Costs: £0.3m | Benefits: £0 | Net: -£0.3m | Yes | In |

Summary

This is a final stage impact assessment, which relates to the primary legislative element of IA No. BIS InsS009 on Insolvency Practitioner fees regime. This final IA follows a 6 week consultation which closed on the 28th March 2014 and relates to the proposal to introduce a regulatory objective which ensures that fees charged by IPs represent value for money. The introduction of measures to improve the regulatory framework generally, in particular the introduction of statutory regulatory objectives, is dealt with by IA BIS InsS001.

The other proposals contained in the Insolvency Practitioner fee regime IA, are subject to further consultation with key stakeholders. As these relate to changes to secondary legislation, they are being taken forward separately on a different timetable. A final IA covering these proposals will be submitted for consideration once policy is finalised.

Evidence Base (for summary sheets)

Problem under consideration;

1. IPs act as office-holders in insolvency procedures. To be qualified to act as an IP, the Insolvency Act 1986 requires a person to be authorised as a member of a professional body which has been recognised for this purpose by the Secretary of State. There are currently 7 of these recognised professional bodies (RPBs). Once authorised, IPs are regulated through a system of self-regulation by the RPBs, overseen by the Insolvency Service. Each of the RPBs has a set of rules and regulations to ensure that those individuals they authorise to act as IPs are fit and proper persons with the necessary experience, qualifications and insurance in place.
2. The OFT report into the market for corporate IPs in 2010¹ found that in just over a third of insolvency cases, where unsecured creditors receive a pay-out and thereby bear the cost of the IPs fees, fees are estimated to be 9% higher in like-for-like cases than where secured creditors 'control' the IPs fees. The OFT estimated that in administration cases only, this amounted to £15m per year that unsecured creditors were paying in higher fees to IPs. Despite numerous discussions with the profession and the regulators little has changed to address this market failure and concerns continue to be raised by creditors about the fees (both remuneration and expenses) charged by IPs and the impact this has on the position of unsecured creditors in insolvency situations.
3. As a result of on-going concern, in December 2012 the Government announced a review, led by Professor Elaine Kempson, into IP fees to ensure that creditors are being charged fairly and to increase confidence in the insolvency regime. In July 2013 Professor Kempson published her report² which found that the current system of controls on IP remuneration works as intended where a secured creditor plays an active part in an insolvency. In this situation there is a degree of competition, as banks are repeat customers and IPs want to join and remain on Bank panels.
4. On the other hand there is evidence that where control lies in the hands of unsecured creditors collectively, the current control mechanisms do not work as intended. In such circumstances there is little competition for jobs, no 'identifiable' client (as the IP is working to a number of unsecured creditors, most of which have no involvement) and creditors are required to work together, in circumstances where they don't know, or find it difficult to contact, each other. This results in little effective oversight by unsecured creditors of the work undertaken by IPs. **The only current route for complaining about quantum of fees is through the courts which is costly.** For all these reasons, there is little control or oversight, and higher fees are paid where unsecured creditors are responsible for paying.
5. The decisions IPs make in any insolvency procedure, where they have wide powers, can have a substantial impact on the funds available to creditors. Creditors are reliant on IPs to act fairly in their best interests.

¹ http://www.of.gov.uk/shared_of/reports/insolvency/oft1245

² <http://www.bis.gov.uk/insolvency/insolvency-profession/review-of-ip-fees>

Background;

6. Each year IPs realise approximately £5bn worth of assets from corporate insolvency processes, and in doing so charge about £1bn in fees, and distribute some £4bn to creditors³. IPs can also advise on business restructuring and continuity prior to insolvency and are part of the wider business restructuring market.
7. The only existing route to challenge high fees is by an application to court but the process can be expensive and often outweighs the benefit for unsecured creditors to challenge. Given that both OFT and Professor Kempson believe that harm is occurring to unsecured creditors, the ability to effectively review fees has been identified as a significant reform.
8. Both the OFT report of 2010 and Professor Kempson's report acknowledge that there is no single solution to address the market failure for unsecured creditors and instead sets out a number of recommendations, which collectively would address the issues highlighted by the review.
9. The Kempson report offers a wide-ranging number of options that could be considered. These fall into three main categories:
 - Transparency Measures and increasing creditor engagement: these concentrate around ensuring that sufficient and clear information is available generally and specific to a particular case to encourage greater engagement by unsecured creditors. This could include an estimate at the start of the case of the likely fees that will be charged.
 - Simplifying the fee structure: here Professor Kempson says consideration should be given to changing the presumed basis for remuneration (which is time and rate in almost all administration, winding up and bankruptcy cases). She proposes two options; having percentage of realisations as the presumed basis for charging fees in all cases or using different bases for different aspects of a case. For example fixed fees could be charged for statutory work where the costs are known and a realisation percentage where the work involves asset realisation.
 - Enhanced monitoring of fee complaints by regulators: Professor Kempson raised the issue of whether a single regulator would be beneficial in this sector. Her main comment here is around the need for regulators to exercise a greater degree of compliance monitoring of fees.

Following review of the responses to our consultation, the first two elements of Professor Kempson's proposals are subject to further discussion with key stakeholders. As these relate to changes to secondary legislation, they are being taken forward separately and will be the subject of a further IA once the policy has been finalised.

10. This impact assessment considers how we can enhance the monitoring of fee aspects of a case and include fee complaints within the current system by including within the proposed reforms to the regulatory regime generally (see The Impact Assessment for these proposals entitled 'Insolvency Practitioner Regulation – regulatory objectives and oversight powers' (BIS InnS001) a regulatory objective of providing value for money.

Overview of consultation responses;

11. Responses to the consultation concerning the introduction of an objective on 'value for money' were mixed. A number of respondents felt that this was already within the remit of responsibility of the RPBs so felt it was not necessary whilst others commented that they were generally supportive of the regulators becoming involved in fee related issues to improve confidence in the regime and enhance

³ Paragraph 1.5 'Market for Corporate Insolvency Practitioners – a market study' - http://www.of.gov.uk/shared_of/reports/Insolvency/oft1245

the reputation of IPs. One of the biggest concerns raised was that fee complaints represent a very small percentage of the overall complaints that are currently received (2%).

12. Paragraphs 42 to 45 below set out why the current system does not provide sufficient recourse for creditors, the main reason being that not all the RPBs view quantum of fees as within their remit. Currently complaints about fees are low as a result of RPBs stating publicly that they do not consider fee-related complaints. In the past 6 months 23% of all IP related ministerial correspondence has been in relation to fees.
13. Detailed comments included that value for money was a subjective concept and difficult to measure and that some statutory duties, that IPs are required to undertake, have no direct impact on value. A general concern that came across in a number of responses from the profession is that a free to use complaints system for creditors could allow a small but disgruntled creditor the opportunity to disrupt the process. These points are addressed in risk and assumptions below.
14. In general the costs set out in the IA were not commented on (apart from by the RPBs on whom they impact), but where they were, the majority of comments concerned the use of 2011 data. However no more recent data or costs were provided. Some comments were made as to the estimated level of additional complaints as they felt 300 was too low. However the majority of these respondents felt that given the low level of fee complaints, reform of the system was not needed.

Rationale for intervention;

15. Government intervention is necessary in this instance to combat potential **market failure** identified by the OFT and Professor Kempson. Their evidence says that unsecured creditors are unable to exercise effective control over IPs which leads to IPs taking advantage of their **market power**, which results in increased cost and/or reduced quality of work (by taking longer to do the same job) for unsecured creditors, for the same type of service.

Policy objective;

16. The overall aim is to increase confidence in the work of IPs and the insolvency framework. This will be achieved through a package of measures aimed at improving and strengthening the regulatory regime for IPs. This impact assessment concerns changes to the monitoring of fees and complaint handling process for fee complaints. It is anticipated that this measure, along with the other regulatory changes, will in the long term increase the confidence in the regulatory regime, which will, over time, lower the number of complaints about IPs' fees. IPs that are abusing the system will be sanctioned appropriately and creditors can have confidence that an IP is achieving the best outcome in the circumstances of a case. .

Description of options considered (including do nothing);

Do nothing option

17. Do nothing would be to continue with the status quo whereby IPs fees remain relatively unchecked. Given the weakness for unsecured creditors of the current regime, identified by the OFT and more recently by Professor Kempson's review, doing nothing is not considered a credible option as it would allow the current inefficiency and unfairness in the market to continue.

Option 1: Bringing quantum of fees within the remit of the regulatory framework by including value for money within the proposed regulatory objectives⁴.

18. Professor Kempson's review highlights that enhanced monitoring by the regulators of IPs RPBs is particularly important both for the reputation of the profession and to ensure that work is properly undertaken and the levels of remuneration are appropriate. She highlights that the starting point for reforms in this area should be on providing greater oversight, therefore reducing the numbers of complaints and challenges relating to fees.
19. Underpinning the regulation of IPs in Great Britain is the dual regulatory approach, combining both self-regulation by the profession and independent oversight regulation by Government. In practice, the Insolvency Service carries out oversight regulation acting on behalf of the Secretary of State.
20. Self-regulation is carried out by the RPBs that authorise IPs – these are bodies established by statute and some are trading companies and are therefore businesses for the purpose of this IA. These bodies are the:
- Association of Chartered Certified Accountants (ACCA);
 - Insolvency Practitioners Association (IPA);
 - Institute of Chartered Accountants in England and Wales (ICAEW);
 - Institute of Chartered Accountants in Ireland (CARB);
 - Institute of Chartered Accountants of Scotland (ICAS);
 - Solicitors Regulation Authority (SRA, formerly the Law Society); and
 - Law Society of Scotland (LSS).
21. We are proposing to introduce a number of measures **to reform the landscape of IP regulation** (see separate IA entitled 'Insolvency Practitioner Regulation – Regulatory objectives and oversight powers: BIS InsS001), by bringing in regulatory objectives and strengthening the Secretary of State powers of oversight. The RPBs do not currently monitor levels of IP fees. We would like them to do more in this respect and therefore intend to include **IP fees offering value for money as a regulatory objective**. The purpose of the regulatory objectives as a whole is not to introduce additional regulatory burdens but rather to direct and focus regulatory activity to produce better and more consistent outcomes and to tackle misconduct in the small minority of cases where regulatory action is required. Adding this objective will ensure that RPBs can direct and focus their regulatory activity onto the quantum of fees charged as well as the process in which fees were taken.
22. We do recognise that giving the RPBs a regulatory role in monitoring fees will increase the burden on them when dealing with complaints around the quantum of fees, the costs of which are set out below.
23. The costs and benefits of this option have been tested through consultation. In general respondents queried the estimated amount of fee complaints that would be received (300), the use of 2011 data (costs are reflected below as well as in covering sheets in 2013 prices – £1.9m) and that no costs were included for monitoring 'value for money'. The only additional data that was provided was reference to R3 response to our consultation in 2011, which estimated that by opening the system up to fee complaints there are likely to be 2000 complaints and 340 appeals at a cost of £11m. However we believe these figures are over inflated, with only 716 complaints in total being received in the 9 months to 6 March 2013 covering all other aspects of IP work. In response to this consultation R3 surveyed their members to ask how many complaints regarding fees they receive in a typical 12 month period, and the majority of R3 members said they received no complaints about their fee levels.⁵ Given the uncertainty over the level of fee complaints, we have included within this final IA

⁴ See Impact Assessment 'Insolvency Practitioner Regulation – regulatory objectives and oversight powers'.

⁵ 63% of members receive no complaints in a typical 12 months.

costs for 3 scenarios, high number of complaints (2000), low number of complaints (50) and best estimate, where we have continued with our original assumption that fee complaints will amount to 300 per annum (40% of total number of complaints in 2013). We appreciate that IPs may incur costs in relation to responding to complaints about fees – but this is the case in relation to all complaints to which IPs now have to set aside funds. We do not believe this would be a significant cost. We have based this assumption on full compliance with the regulatory framework.

24. Responses from the RPBs (on which the costs will have a direct impact) were mixed in relation to our assessment of costs. One RPB was generally satisfied that the costs stated reflected the additional costs in dealing with fee complaints; whereas others queried the assessment of costs but did not provide any alternative data. In general they raised particular concern over any additional costs that will be incurred through increased monitoring to ensure value for money. The regulatory objectives set a framework against which the RPBs can carry out their regulatory activities. The intention is for these objectives to refocus the work already undertaken by the RPBs, to produce outcomes which are consistent with them. Many of the RPBs have acknowledged that they already carry out an assessment of fees in the monitoring visits they currently undertake so we do not anticipate this objective will add additional costs to the RPBs in terms of monitoring but instead their efforts in this regard will be put in a different context and focused instead on value for money.
25. The objective makes it explicit that fee related complaints should be dealt with by the regulators. It is intended to set an over-arching framework for value for money issues (both fee complaints and monitoring of value) to be dealt with, it doesn't specify how this should be done. It will be for the RPBs, to create a system (whether within the existing complaints process or by combining resources to create a joint system) which adjudicates on fee issues. Concerns raised in the consultation regarding safeguards to prevent vexatious complaints and how the costs associated with fee complaints are allocated (whether absorbed by the RPBs or passed on IPs), will be for the regulators to decide.

Costs of Option 1

Costs:

26. This proposal is likely to have costs mainly to the regulators, although in practice any additional costs are likely to be passed onto IPs in higher licensing fees or recovered from those IPs sanctioned by the RPBs. One of the responses to the consultation estimated this to be £950 per annum per IP, which given the increased confidence and credibility to the industry which will result from a strengthened regulatory framework, is a proportionate cost for an industry which generates an estimated £1bn per annum⁶.
27. We have not included any set-up costs as this measure is based on fee complaints following the existing structure for all complaints. In terms of on going costs, the proposal is likely to have increased costs to RPBs in terms of dealing with increased complaints.
28. Currently there are very few fee related complaints handled by the RPBs, but this is likely to be a result of RPBs stating publicly that they do not consider fee-related complaints and does not reflect the current level of concern around fees. In the past 6 months 23% of all IP related ministerial correspondence has been in relation to fees.
29. To reflect uncertainty in consultation responses over the number of complaints that may be received once the system is opened up to fee-related complaints, we have provided data for three scenarios to provide a range of costs. These are:
 - **High number of complaints:** This scenario is based on 2000 fee complaints being received and 340 appeals (17% of total number of fee complaints).

⁶ Paragraph 1.5 'Market for Corporate Insolvency Practitioners – a market study' - http://www.ofc.gov.uk/shared_ofc/reports/Insolvency/ofc1245

- **Low number of complaints:** This scenario is based on 50 fee complaints being received and 9 appeals (17% of total number of fee complaints).
- **Best estimate:** This scenario is based on 300 fee complaints being received and 50 appeals (17% of total number of fee complaints).

30. Our best estimate of the number of fee complaints is based on the number of complaints dealt with by RPBs over the past 3 years (748 in 2013, 578 in 2012 and 517 in 2011) and represents 40% of the total complaints received in 2013. We have assumed 50 appeals (17%) on fee related complaints. These figures were used for our assessment of the costs of RPBs taking fee complaints in our consultation on reforms to the regulation of IPs in 2011⁷. We appreciate that this might not reflect the total number of fee complaints received, but given that RPBs do not currently consider fee complaints and complaints to the court are very low due to the high cost, we believe this is a best estimate for opening up the current system of complaints to a new category. In addition the changes to strengthen the regulatory framework will give greater confidence in the work undertaken by IPs. This along with changes to the fee regime going forward, will give greater transparency to creditors and manage expectations upfront, which should reduce complaints about fees after-the-event.
31. The annual additional costs for RPBs to consider and investigate fee complaints, based on all three scenarios, are set out below. The main costs are staffing and panel costs as the structure is already in place⁸. This is the total costs so would be split between the 7 RPBs. These costs are likely to be passed onto IPs in higher regulatory costs:

⁷ <http://www.bis.gov.uk/assets/insolvency/docs/insolvency%20profession/consultations/ipconsult.pdf>

⁸ These figures were provided by one of the regulators in 2011 for the consultation 'reforms to the regulation of IPs' - <http://www.bis.gov.uk/insolvency/Consultations/IPConsultation?cat=closedwithresponse>

| | Best Estimate - 300 complaints £ | LOW scenario - 50 complaints £ | HIGH scenario - 2000 complaints £ |
|--|--|--------------------------------------|---|
| Annual costs: | | | |
| Initial Complaint: | | | |
| Staff and overhead cost ⁹ | 960,000 ¹⁰ | 160,000 | 6,400,000 |
| Investigation and discipline committee | 420,000 ¹¹ | 70,000 | 2,810,000 |
| Appeal Process:- | | | |
| Staff and oversight cost ¹² | 160,000 ¹³ | 30,000 | 1,090,000 |
| Appeals committee | 130,000 ¹⁴ | 20,000 | 870,000 |
| Other costs:- | | | |
| Legal contingency | 150,000 | 25,000 | 1,000,000 |
| Total Annual Cost (2011 prices) | 1,820,000 | 305,000 | 12,170,000 |
| Total Annual Cost (2013 prices) | 1,867,320 | 312,930 | 12,486,420 |

Benefits of Option 1

32. Benefits of the proposal are expected be:

- Increased efficiency in the market
- Increased IP market confidence
- Consistency amongst regulators

⁹ This cost is based on a cost of £2715 per case review, this figure was provided by one of the regulators in 2011. As we have been unable to break this figure down into staffing and overhead costs, or confirm whether staff costs include non wage labour costs, we have included a 17.8% increase on the total case review fee (£3,198) to account for non wage labour costs. However given that some of these costs relate to overheads, this is likely to be an over-estimation of the actual figure.

¹⁰ £3,198 multiplied by the 300 cases and rounded to the nearest £10,000.

¹¹ The costs associated with the investigation and disciplinary committees, which already exist within the RPBs, considering the case are calculated as;

150 cases going to investigation committee (50% of total number of fee complaints)

10% of the 150 cases being reviewed by the disciplinary committee (15)

5 committee members on each panel

£500 meeting attendance fee per committee member

Expenses of £50 per committee hearing

Total cost rounded = $(150+15*5*500) + (165*50) = £420,000$

¹² This cost is based on a cost of £2715 per case review, this figure was provided by one of the regulators in 2011. As we have been unable to break this figure down into staffing and overhead costs, or confirm whether staff costs include non wage labour costs, we have included a 17.8% increase on the total case review fee (£3,198) to account for non wage labour costs. However given that some of these costs relate to overheads, this is likely to be an over-estimation of the actual figure.

¹³ Calculations for appeal process: Staff and oversight cost rounded = $£3,198 * 50$ cases and appeals committee = $(£500 \text{ per committee member} * 5 \text{ members} * 50 \text{ cases}) + £50 \text{ expenses} * 50 \text{ cases}$

¹⁴ Calculations for appeal process: Staff and oversight cost rounded = $£3,198 * 50$ cases and appeals committee = $(£500 \text{ per committee member} * 5 \text{ members} * 50 \text{ cases}) + £50 \text{ expenses} * 50 \text{ cases}$

Non-quantifiable Benefits

33. The benefit would be an accessible and free route for creditors to dispute excessive fee charging and provide creditors with confidence that monitoring activities include an element of value for money. Once action is seen to be taken against IPs who have over-charged, the profession as a whole will be encouraged to charge fairly. This will lead to more funds available for distribution to creditors as fees are reduced. This will ultimately lead to an improved reputation of the profession.

Efficiency

34. There should also be efficiency gains by the removal of the IPs market power versus unsecured creditors means that they would be forced to produce efficiently (in order to demonstrate value for money), given they had previously been able to operate without needing to minimise costs. Effectively productive efficiency could increase.

Market confidence

35. One of the benefits the OFT anticipated from reforms in this area, is an increased market confidence in IPs, leading to businesses making more use of IPs other services. The OFT expects this to lead to businesses in trouble seeking earlier advice from IPs than they currently do. This is expected to lead to better business outcomes for these businesses, potentially saving a business from an insolvency proceeding and leading to a positive impact on the economy. It would also lead to an increase in demand for IP advisory services increasing their fees.

36. Generally responses to the consultation agreed that this proposal would lead to greater market confidence and an improved reputation of the insolvency profession.

Risks and Assumptions

37. Monitoring of value for money will be closely linked to any changes that are made to secondary legislation in relation to the fee regime, which we are currently working with interest parties to develop/refine. However the introduction of IP fees offering value for money in the regulatory objectives will, through their monitoring activity, enable RPBs to be able to monitor what is happening in relation to fees.

38. Some responses to the consultation raised concern that providing a free to use route for complaints about fees will open the flood gates to numerous complaints and may increase creditor apathy during the insolvency process. We appreciate that safeguards will be needed to prevent vexatious complainants, for example making it a requirement to bringing a complaint about fees that the complainant must have taken an active role in the approval of fees during the case. One of the RPB responses to the consultation made reference to a low cost but binding fee arbitration system, which is currently in operation. We would encourage such a scheme as the first stage of any fee related complaint. The new objective does not specify how fee complaints should be dealt with but we would encourage the RPBs to work together to provide a system which is consistent and accessible for creditors.

39. A further concern raised in the consultation was that monitoring value for money gives creditors an unrealistic expectation that they will get more back from an insolvency than they do now. We do not believe this would be the case, instead we feel it will build confidence in the profession generally. This will result in the long term in creditors being confident that an IP is achieving the best possible outcome in the circumstances. .

40. It can be argued that creditors already approve fees during the process of the case so should not have an additional opportunity to question fees at a later date. However statutory powers to agree the basis of remuneration and approve fees are 'after the event' powers, with fees being approved after they have already been incurred by the office-holder.

41. There is a risk that IPs will increase their charge out rates to cover the costs of the system as well as to mitigate any potential loss in claims made against excessive fee charging. However we believe this risk is small and any increase is likely to be minimal.

Option 2: Introduce voluntary code which ensures that RPBs will look at complaints about their members' fees where they are deemed to be excessive.

42. This option would be to reach agreement with the RPBs which set out best practice for monitoring value for money and dealing with fee complaints, including quantum of fees, rather than using the regulatory route described above.

43. Following on-going discussions with the RPBs they say that they already consider complaints of alleged excessive fees where there is a suggestion that this could be due to IP misconduct. An enquiry into possible misconduct might then look at whether the IP was charging levels of fees that were clearly out of proportion to the work done (e.g. excessive hours being falsely charged to the estate), although RPBs were concerned that this would be difficult to evidence in all but the most obvious of cases. **However the approach taken by RPBs currently to complaints about fees as being potential misconduct is different and inconsistent and we are aware that they are restricted by not having a specific requirement to consider fee related complaints. The voluntary route would not address this gap.**

44. We have experienced working with the RPBs to set up voluntary measures. For example, in tandem with setting up the Complaints Gateway (whereby all complaints about IPs come through one portal before being passed over to the relevant RPB) we tried working with the RPBs to set up a list of common sanctions that would be used by RPBs when taking action against IPs following complaints. However, we have not been able to get agreement from all 7 RPBs and there are differences in the "common" sanctions.

45. Increased monitoring of fees was first raised in 2010 in the OFT market study. RPBs maintain the view that ensuring their members offer value for money is not part of their role. Therefore, they will not take this forward voluntarily.

Costs of Option 2

46. If we were to pursue this option, we would continue on-going discussions and negotiations with the regulators to open up their current remit for dealing with fee complaints. As we have set out above the regulators already consider complaints of alleged excessive fees where there is a suggestion that this could be due to IP misconduct, this amounts to very few complaints a year (approx. 10). In the past getting agreement across the RPBs has proved extremely difficult and time consuming and given the regulators do not consider value for money issues within their current remit, they are unlikely to accept this role voluntarily.

47. It may be possible through continued negotiations to obtain agreement to open up the current system to some additional fee complaints (where evidence of excessive fee charging and abuse is extreme) but this is only likely to impact on a small number of cases and at best lead to an additional 50 complaints being considered (low complaint scenario). However we do not believe that this would result in as many fee complaints being dealt with as would be if there were clear regulatory guidance on what the regulators should be doing.

48. The costs for this option therefore reflect the costs of the low complaint scenario.

Benefits of Option 2

49. It is expected that this option, if implemented effectively, could have similar type of benefits as option 1. That is efficiency and market confidence benefits. However, we do not believe that agreement or consistency of approach would be reached by taking this forward on a voluntary basis. Therefore, the level of efficiency and fairness expected from this proposal is likely to be much lower than in Option 1.

Rationale and evidence that justify the level of analysis used in the IA (proportionality approach);

48. We asked questions as part of the consultation process and have included a summary of the evidence provided. However, the lack of alternative data has led us to remain confident in the data submitted in the consultation stage IA, but to take account of uncertainty over the number of fee complaints that may be received by opening up the complaint process to fee-related issues, we have included a high, low and best estimate scenario.

Direct costs and benefits to business calculations (following OITO methodology);

49. The preferred option is likely to impose costs and benefits to businesses. These are the following:

- An annual net cost of including fee related complaints within the current complaints system, which is estimated at £1.9m across all RPBs. This is largely attributable to increased staff and panel costs for the RPBs to investigate complaints about fees. This cost will be wholly borne by the 7 regulatory bodies, although may be passed onto IPs in higher membership costs.

50. The benefits stated in this impact assessment are wider benefits to the overall functioning of the market and therefore are not considered to be direct to businesses (although they will have an impact on businesses).

51. Hence, based on the analysis stated above, this proposal constitutes an **In of £1.55m** under the OITO methodology.

Small and micro business assessment;

52. The introduction of a regulatory objective to provide value for money is part of a wider package of reforms around insolvency regulation, such as the introduction of regulatory objectives and increased powers of oversight (which require primary legislation). None of the measures will come into force until after 31 March 2014.

Changes to regulatory regime

53. The changes to the regulatory regime to ensure the RPBs consider fee related complaints are not targeted directly at IPs, instead the requirement and cost would be binding on the 7 independent RPBs. However we do recognise there is an onward impact on IPs in terms of tighter regulation over what they charge and possibly transfer of the cost of the system.

54. To assess whether any of the RPBs fall in to the definition of a micro or small business we have considered information published by the RPBs (e.g. annual reviews) and contacted them directly for confirmation of staff numbers.

55. None of the RPBs are micro-businesses (fewer than 10 employees) and one falls into the definition of a small business (fewer than 50 employees). Three of the RPBs have between 100 and 150 staff and three have in excess of 500 staff. We propose that the same requirement to consider complaints in relation to excessive fee charging is applied to all the RPBs regardless of size. It would be inappropriate and unworkable to distinguish between the RPBs on the basis of scale as different complaints systems would then apply to different IPs depending on the status of their licensing body. This would create confusion and uncertainty for debtors, creditors and other stakeholders in insolvency cases. In addition, it is likely that at least some IPs would switch to an institution outside the scope of considering complaints (potentially resulting in a merry-go-round of IPs between the RPBs) which would be to the further detriment of perceptions around the insolvency profession generally.

56. R3, The Association of Business Recovery Professionals which represents 97% of the IP profession, estimate that a **significant proportion** of its IP members can be classified as micro and small businesses. Figures provided by R3 in response to consultation show that there are 403 small firms (based on a firm having five or fewer insolvency appointment takers) of which 135 (37%) are micro-businesses (fewer than 10 employees).

57. If the RPBs do transfer the additional costs of considering fee complaints onto IPs in higher regulatory fees, this would amount to approximately £950 pa per IP. If this is the case it is reasonable to assume that at least 50% of the total costs will fall on small and micro firms.

58. In practice, the changes to the regulatory regime to allow complaints about fees should have minimal impact for individual IPs, particularly for those who already act in compliance with the existing legal and regulatory framework. If the costs of doing this are passed on to IPs it is highly likely they will pass these costs onto creditors in increased fees.

Wider Impacts;

Economic/Financial

57. *Competition:* The proposals aim to address the market failure for unsecured creditors by increasing competition between IPs. We do not however anticipate that these reforms will have a negative impact on IPs ability to compete or reduce the number of IPs in the market. A separate impact assessment has not been completed for this reason.

58. *Justice:* there is no impact on legal aid or criminal offences. As fee complaints will now be dealt with by the RPBs rather than the courts, this measure will have a positive effect on the workload of the courts.

59. *Small firms:* This is dealt with under the small and micro business assessment

There are no further wider impacts identified.

Social

Health and well being: No impact

Equality: The policy will not have any negative impact on all identified equality groups.

Human rights: No impact

Environmental

Rural proofing: No impact

Sustainable development: no impact

Environment: no impact

Summary and preferred option with description of implementation plan;

60. Our preferred option is option 1 – introduction of a regulatory objective which ensures fees charged represent value for money. This would open up the ability for RPBs to consider fee complaints within the existing framework. Progressing the non regulatory route has been attempted over the past few years with no success.