

Claims management regulation – financial claims

Ministry of Justice

RPC rating: fit for purpose

The IA is now fit for purpose as a result of the department's response to the RPC's initial review. As first submitted, the IA was not fit for purpose.

Description of proposal

The proposals aim to tackle “exploitative pricing structures” that are adopted by claims management companies (CMCs) in their pursuit of claims, on behalf of consumers, relating to the mis-selling of financial products. These pricing structures involve significant direct costs to consumers and, by encouraging speculative claims, can result in wider costs to consumers, businesses and the Financial Ombudsman service.

The department's preferred option includes a number of measures. These include:

- A cap on completion fees of 15 per cent of the net amount of the final compensation awarded, for one or more payment protection insurance (PPI) or packaged bank accounts (PBA) claims with a lender, where the total net value of all relevant claims equals £2,000 or less. Where claims exceed £2,000 there is an overall total charge cap of £300.
- A ban on CMCs charging up-front fees.
- A maximum ‘cancellation’ fee of £300 where a consumer cancels his contract with a CMC after an initial 14-day ‘cooling off’ period.

Impacts of proposal

The proposals would affect CMCs operating in the financial claims sector. This is estimated to be about half of the total number of 1,700 authorised CMCs, i.e. around 850 companies.

Based upon data from the Financial Conduct Authority and the Financial Ombudsman, the department estimates the total number of upheld PPI claims to be about 950,000 each year. The average completion fee is estimated to be £500, giving total revenue to CMCs from these fees of £480 million each year. Assuming

an unchanged volume of claims, and based upon data on compensation awards, the department estimates that the 15 per cent cap would reduce the revenue from completion fees to around £250 million, i.e. a loss of £230 million.

Based upon data provided by the Citizens' Advice Bureau, the department estimates that up-front fees are currently charged in 24 per cent of cases. Applying this to 950,000 claims gives an estimate of 220,000 claims where up-front fees are charged. The average up-front fee is estimated to be around £720, giving total revenue to CMCs from these fees of £160 million. Since these fees would be banned by the proposals, this is the estimated cost to CMCs from this measure.

The department does not presently have evidence to make estimates of the cost of the other elements of the policy package. However, it makes it clear that the consultation will be used to try to fill these gaps. Overall, therefore, the department currently estimates the proposals to cost business around £390 million each year. Consumers benefit by this amount, resulting in an overall net present value of zero.

Quality of submission

As initially submitted, the IA was not considered fit for purpose by the RPC, for a number of reasons. Following the RPC's initial review, the department submitted a revised IA that responds satisfactorily to the points as follows:

Appraisal of alternative options

The IA now includes an assessment of an alternative fee cap and provides a much more detailed assessment of the non-regulatory options of a voluntary code and improving consumer awareness. These are now shown as full options in the IA (options 2, 4 and 5, respectively). With this additional analysis, the IA now provides an adequate consideration of alternative options.

Small and micro business assessment (SaMBA)

The department estimates that 71 per cent of the 850 claims management companies in the financial claims sector are small or micro businesses. (This estimate is down from 97 per cent in the previous IA.) The IA now includes an expanded SaMBA. This estimates that, in aggregate, the proposals could cost small businesses around £97 million each year and micro businesses around £70 million each year. The cost to a small business and a micro business is estimated at around £1.1 million and £0.1 million, respectively. These figures are now compared against the turnover of these companies. Depending upon different data and assumptions, the cost is between 60 and 85 per cent of total turnover. The

department states that it will use the consultation to try to gather further data to make a fuller assessment at the final stage of the impact of the proposals on small and micro businesses.

Business impact target classification

The IA now provides an assessment of how the measures will be considered against the business impact target. The RPC expects that this will be a qualifying regulatory provision, scoring as an IN against the business impact target.

Impact on the Claims Management Regulation Unit (CMRU)

In its initial review, the RPC commented that, since the CMRU is funded from fees levied on CMCs, any increase in costs to the CMRU from implementing and enforcing the proposals would be considered as a direct impact on business at the final stage. The department has explained that it is presently unable to assess these potential impacts but will seek further information through consultation.

As indicated in the IA, the department should use the consultation to strengthen the estimates of the direct impacts on business, including taking account of cost recovery by the CMRU. Given the very large impact on small and micro businesses, the department should also seek to strengthen the SaMBA for the final stage. At the final stage, the department should also address the more specific comments listed below.

Future volume of PPI claims

The department should provide further consideration of whether the IA's current estimate for the number of claims each year, which is based upon 2014-15 data, is a reasonable assumption for the annual number of claims over the appraisal period.

Relationship to Financial Conduct Authority proposal

The IA refers (at paragraph 6.22) to an FCA consultation on a proposal to place a deadline of 2018 on mis-sold PPI claims. The IA states that, if this proposal is implemented, the present proposals would then impact on CMCs and consumers for only two years. The department will need to provide greater clarity at the final stage on the relationship between these two proposals and explain how the two measures will be scored against the business impact target.

Risk of CMCs leaving the market

The IA includes an assessment (under 'Risks', pages 21-22) of the possible dynamic effects of the proposals, for example in CMCs potentially leaving the market. The department should seek to use the consultation to strengthen this assessment.

Societal NPV

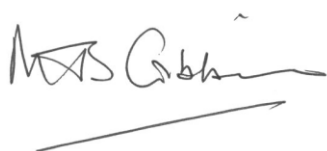
The IA presents the proposals as having a zero NPV, on the basis that the costs to CMCs are offset by benefits to consumers. The final stage IA would benefit from further discussion of the proposals' likely impact on overall societal welfare.

Initial departmental assessment

Classification	Qualifying regulatory provision
Estimated equivalent annual net cost to business (EANCB)	£383 million
Business net present value	-£3,300 million
Societal net present value	Zero

RPC assessment

Classification	Qualifying regulatory provision
Small and micro business assessment	Sufficient
RPC rating (of IA as initially submitted)	Not fit for purpose



Michael Gibbons CBE, Chairman