

## **EXPLANATORY MEMORANDUM TO**

**The Compensation (Regulated Claims Management Services) Order 2006  
SI 2006/3319**

**The Compensation (Specification of Benefits) Order 2006  
SI 2006/3321**

**The Compensation (Claims Management Services) Regulations 2006  
SI 2006/3322**

1. This explanatory memorandum has been prepared by the Department for Constitutional Affairs and is laid before Parliament by Command of Her Majesty.

This memorandum contains information for the Joint Committee on Statutory Instruments.

### **2. Description**

2.1 The Compensation (Regulated Claims Management Companies) Order 2006 (the Scope Order) sets out what activities are to be regulated as claims management services and the type of claim for compensation that will be regulated under Part 2 of the Compensation Act 2006 (the Act). This includes claims relating to personal injury; criminal injuries compensation; employment; housing disrepair; claims in relation to certain financial products or services; and industrial injuries disablement benefits. Any person providing a claims management service in the regulated areas will need to be authorised, exempt by Order or have the benefit of a waiver.

2.2 The Compensation (Specification of Benefits) Order 2006 (the Benefits Order) specifies the group of benefits collectively called industrial injuries disablement benefits. A claim for such a benefit is to be treated as a compensation claim under the Act.

2.3 The Compensation (Regulated Claims Management Services) Regulations 2006 (the Regulations) set out the requirements to be met for service providers to obtain authorisation and other details about the operation of regulatory mechanisms such as granting waivers, fee charging, indemnity insurance, rules and codes of practice, complaint schemes, routine audits and enforcement.

### **3. Matters of special interest to the Joint Committee on Statutory Instruments**

3.1 None.

### **4. Legislative Background**

4.1 Part 2 of the Act establishes the regulatory framework which gives the Regulator the power to grant authorisation to carry on the regulated activities, to prescribe rules for the professional conduct of authorised persons, to investigate complaints about authorised persons and to take specified enforcement action. Providing a “regulated claims management service” is to be an offence under the Act unless the person who provides the service is authorised under the Act to do so, or is exempted from the

obligation to become authorised, or has the benefit of a waiver of the obligation to be authorised. If prosecuted on indictment, the offence is punishable by a maximum prison sentence of two years.

4.2 The Scope Order is made under the power in s 4(2)(e) of the Act.

4.3 The Benefits Order is made under section 4(5) of the Act. That section provides that the Secretary of State may by Order specify that claims for a specified social security benefit are to be regulated claims, if he is satisfied that the benefit is designed to provide compensation for industrial injury. Under section 94 of the Social Security Contributions and Benefits Act 1992 (the 1992 Act), industrial injuries benefit consists of disablement benefit, reduced earnings allowance, retirement allowance and industrial death benefit. Claims under certain historical schemes (mentioned in Schedule 8 of the 1992 Act and under the Pneumoconiosis etc (Workers' Compensation) Act 1979) are also to be treated as claims for the purposes of the Act. (These schemes are under Acts now repealed but under which a right to compensation for industrial injury or disablement arose before the 1992 Act commenced.)

4.4 The Regulations are made under the powers in sections 8(8) and 9 of, and the Schedule to, the Act.

## **5. Extent**

5.1 The Orders and Regulations apply to England and Wales.

## **6. European Convention on Human Rights**

6.1 The Parliamentary Under-Secretary of State for Constitutional Affairs has made the following statement regarding Human Rights:

In my view the provisions of the Compensation (Regulated Claims Management Services) Order 2006, the Compensation (Specification of Benefits) Order 2006 and the Compensation (Claims Management Services) Regulations 2006 are compatible with the Convention rights.

## **7. Policy Background**

7.1 Claims management businesses gather cases either by advertising or direct approach. They then act either directly for the client in pursuing the claim, or as an intermediary between the claimant and a legal professional or insurer. Claims management businesses make money from several sources—from referral fees from solicitors; from commission on auxiliary services; from the sale of after-the-event insurance; and sometimes from loans to their clients. Concerns have grown over the unprofessional conduct by those who are providing the service for commercial gain—particularly as the activities of claims management businesses have extended into many areas of litigation, well beyond personal injury, and even into claims for certain kinds of benefits even though no litigation is involved.

## **Compensation Act 2006**

7.2 Although claims management companies have to comply with a range of general consumer legislation, there was no sector-specific legislation. The Better Regulation Task Force report “Better Routes to Redress” published in May 2004 recommended that the Government give the industry one last chance to clean up its act. The industry failed to implement effective self-regulation and consumers continued to suffer as a result. The Compensation Act provides a flexible framework for the regulation of claims management services to tackle poor practice in the claims management sector and provide additional safeguards for the public against rogue companies. The framework has been developed in accordance with the principles of Better Regulation: the regulation will be proportionate and targets areas where there is the greatest risk of consumer detriment.

7.3 The Secretary of State for Constitutional Affairs will be the Regulator and formal decisions about regulatory matters including authorisations will be taken in his name. A Head of Claims Management Regulation will have day to day responsibility for the operation of the regulation and DCA is establishing a dedicated monitoring and compliance unit to undertake the administrative function. A Regulatory Consultative Group has been established to ensure adequate stakeholder involvement in the development and operation of the regulatory regime. The group comprises representatives from a wide range of interests including the legal profession, trade unions, consumer groups, insurers, solicitors and the claims management industry.

7.4 Regulation by the Secretary of State is intended as an interim measure. The proposed Legal Services Bill will establish a new framework for legal services regulation, including the establishment of a Legal Services Board and an Office of Legal Complaints. It is intended that powers will be taken in the Bill to enable claims management regulation to be integrated into the new structure.

7.5 The Government consulted on key aspects of the regulatory framework including the proposed Scope Order and Regulations during the summer (6 July – 28 August), although the intended sectors which would be subject to regulation had been announced during the passage of the Act. This together with a series of meetings with key stakeholders as well as regional workshops facilitated a more effective consultation process. The drafts have been amended where necessary to reflect stakeholders’ comments and views.

### **Scope Order**

7.6 The definition of claims management services in the Act is wide to allow new areas to be brought within the scope of regulation where problems arise, and for areas to be removed from scope where problems subside. The intention is that the regulation be applied initially in the areas where there is the greatest potential for consumer detriment. The Scope Order specifies the activities that will be regulated. The activities are those characteristically provided by claims management companies and have been described in such a way as to ensure that similar services provided outside the area of the claims management industry are not inadvertently regulated as claims management services. In particular, services provided to a defendant are outside the intended scope, and are not regarded as being within the definition of “claims management services” in the Act—see section 4(2)(b). The kinds of claim can generally be described as claims for injury, damage or loss that have resulted in

consumer detriment. The consultation provided unanimous consensus that it was appropriate to include the sectors proposed in the draft Order.

### **Benefits Order**

7.9 Claims management businesses typically charge a flat fee for any service provided in relation to claims for industrial injuries disablement benefits. Claims of this kind would be likely to be made at a time when a person is already suffering from the trauma of the injury and thus are more vulnerable. The Benefits Order will ensure that such consumers are better protected.

### **Regulations**

#### **Waivers**

7.10 Part 2 sets up a scheme for the Regulator to waive, in certain circumstances, the obligation on a person who provides regulated claims management services to be authorised to do so. The Regulator may grant such a waiver to a person if the Secretary of State intends to amend the Order exempting the person from the obligation to become authorised, and the Regulator is satisfied that no consumer detriment will result. A waiver cannot last longer than 6 months and cannot be renewed. It is intended simply to allow time for the making of the necessary Exemption Order and its consideration by Parliament.

#### **Grant of authorisation**

7.11 Part 3 makes provision in relation to the application for, and grant of, authorisations. An applicant for authorisation must provide enough information to enable the Regulator to consider the application properly and to be satisfied that the applicant is likely to be competent as an authorised person and is a suitable person to be authorised. The Regulations set out a range of matters that the Regulator may have regard to in making a decision about an applicant's competence and suitability. Consideration of suitability may include a director or partner of an applicant who will have significant influence over the business as well as the applicant. The Regulator can impose conditions on an authorisation, and some conditions are mandatory and imposed directly by the regulations. The Act provides a right of appeal to the Claims Management Services Tribunal against a decision of the Regulator concerning an application, and an appeal from the Tribunal to the Court of Appeal.

#### **Fees**

7.12 Part 4 authorises the Regulator to determine fees. A determination is to be by instrument in writing. There will be an application fee and an annual fee for an authorisation. The fees will be set at a level to cover, as near as possible, the scheme's operating costs. However, it is not intended that the regulator would prescribe or regulate the fees which authorised person may charge.

#### **Professional indemnity insurance**

7.13 Part 5 allows the regulator to require authorised persons to hold Professional Indemnity Insurance. The requirements may vary between authorised persons depending on the type of service they provide, and will be determined by the Regulator in each case.

## **Rules and Codes of practice**

7.14 The Act provides (in paragraphs 8 and 9 of the Schedule) that the Regulator must prescribe rules, and may issue codes of practice, for the professional conduct of authorised persons. Part 6 sets out the procedures for doing so, including a requirement for consultation before rules are prescribed or a code issued, and their publication after being prescribed or issued. Proposed rules and codes must be approved by the Secretary of State. Rules or a code of conduct may be amended or revoked, but if so the Regulator must publish both the text of the amending or revoking instrument and (in the case of an amendment) the text as amended. A rule or code, or an amendment of a rule or code, cannot take effect before it is published.

## **Complaints**

7.15 The rules may require authorised persons to set up complaints handling schemes. Part 7 sets out the Regulator's power to review the handling by an authorised person of a complaint and requirements for making a direction and related matters. There is a limited power in article 27 to require redress where an authorised person has failed to comply with the rules or code of practice. There is to be no power to order a cash payment, although there will be a power for the Regulator to direct the repayment of unjustified fees where such fees should not have been charged.

7.16 The power to require redress is based on paragraphs 8(2)(b) and 9(2)(b) of the Schedule to the Act, which require the Regulations to include provision about the consequences of failure to comply with the rules or codes of practice, specifically including provision for rules to be treated as conditions of authorisation and provision for the Regulator to suspend, cancel or impose conditions on authorisations. The implication is that there are other possible consequences of failure to comply with rules or codes of practice. The power to require redress to be given is seen as a significant part of the Regulator's power to protect consumers from unsatisfactory work or other improper practices by those providing claims management services.

## **Routine Audit**

7.17 Part 8 provides for a limited power of inspection of an authorised person's business records, on reasonable notice, except for items subject to legal privilege within the meaning given by section 23 of the Police and Criminal Evidence Act 1984 (PACE). This is the same definition of "items subject to legal privilege" as is relied on for the purposes of the search warrant provisions, described below.

## **Investigations**

7.18 Part 9 sets out the Regulator's investigation powers. The powers are exercisable in relation to an allegation or a suspicion that a person is providing a regulated claims management service without being an authorised person or an exempted person or having the benefit of a waiver of the obligation to be authorised, or that an authorised person is acting in contravention of the rules or a code of practice. The intention is that in either case the Regulator will, before undertaking an investigation, examine the suspicion, or the substance of the allegation, and consider whether an investigation is warranted.

7.19 The Regulator must first seek information from the person or authorised person by serving a notice requiring the provision of specified information or documents. If the information or documents are not provided, or they reveal further

grounds for investigation, the Regulator may apply to a judicial officer (that is, a justice of the peace, a Circuit judge or a Judge of the High Court) for a search warrant. The Regulator may also apply for a search warrant directly if there is reason to believe that, if a notice to provide information were served, evidence would be concealed or destroyed. The Act deals separately with search warrants in relation to investigating breaches of the Act (in section 8(5)) and for the purpose of investigating the professional conduct of an authorised person (under paragraph 14(2) of the Schedule).

7.20 Part 9 chapter 1 contains general interpretative provisions having effect throughout the Part. Part 9 chapters 2 and 3 contain provisions about requiring the provision of information, and the grounds on which a search warrant may be applied for, in the respective cases of a person suspected of, or alleged to be, providing regulated claims management services although not authorised, exempted or having the benefit of a waiver, and an authorised person suspected of contravening, or alleged to have contravened, the rules or a code of practice.

7.21 Part 9 chapter 4 contains general provisions regarding the issue and execution of search warrants. The scheme set out in chapter 4 basically mirrors that in PACE as far as possible. The relevant provisions of PACE have been copied into the Regulations, so far as necessary, and rewritten to some extent by omitting provisions not required for the present limited purpose (particularly provisions relating to arrest of persons, and those related to seizure).

7.22 The extent of the powers available to an investigator has also been reduced somewhat from the powers in PACE—multiple entry warrants cannot be issued; warrants cannot be issued authorising entry to and search of all premises under the control of a specified person; and entry must be at a reasonable hour. In addition, a warrant can be issued for entry to a residence only in very limited circumstance. The Act does not provide for the issue of a warrant authorising seizure; only copying is permitted. Also, the search provisions authorise only warrants authorising a search for documents, not a general search for things that might be used as evidence. Before issuing a warrant, a justice or judge must be satisfied that no other justice or judge has refused to issue a warrant on the basis of an application that is in substance the same.

7.23 When executing a warrant, an officer must have regard to any relevant code of practice issued by the Home Secretary under section 66 of PACE. (The current code, “Code of Practice for Searches of Premises by Police Officers and the Seizure of Property Found by Police Officers on Persons or Premises”, referred to as Code B, was issued with effect from the first moment of 1 January 2006.) This is the same obligation as is placed on a police officer to comply with such a code. The Home Office has been consulted on the search warrant provisions.

7.24 The Regulations also provide a power for the Regulator to cancel, suspend or vary an authorised person’s authorisation. (A variation may be by imposing a new condition or by varying an existing condition of the authorisation.) The relevant provisions are in Part 10.

7.25 As with the power to strike off a solicitor or medical practitioner, the purpose of the cancellation, suspension or variation power is to protect the public. Before cancelling, suspending or varying an authorisation, the Regulator must a) give the

authorised person written notice of the proposal to cancel, suspend or vary the authorisation, and an outline of the Regulator's case; b) give the authorised person a reasonable opportunity to make a submission in relation to the proposal; and c) in making the decision, take any submission made into account.

7.26 The Regulator must give written notice of cancellation, suspension or variation, and a cancellation, suspension or variation takes effect when notice of it is served on the authorised person or a later date stated in the notice. The Act requires the Tribunal's rules to make provision for the Tribunal to suspend the effect of a decision of the Regulator—see section 12(4)(d) of the Act. The Rules are now in an advanced stage of drafting. An authorised person whose authorisation is cancelled, suspended or varied may appeal to the Claims Management Services Tribunal and, if the Tribunal grants leave, to the Court of Appeal.

## **8. Impact**

8.1 A Regulatory Impact Assessment has not been produced for these statutory instruments. However, a full Regulatory Impact Assessment for claims management regulation was published to accompany the Compensation Bill 2006 and this covered the impact of Orders and Regulations to be made under the primary legislation. The RIA is available at <http://www.dca.gov.uk/legist/compensation.pdf>.

## **9. Contact**

9.1 Jan Farenden at Department for Constitutional Affairs, Tel: 020 7210 8847 or e-mail [Jan.Farenden@dca.gsi.gov.uk](mailto:Jan.Farenden@dca.gsi.gov.uk) can answer any queries regarding the instruments.