Ministry of JUSTICE

Claims Management Regulation – Professional Indemnity Insurance

Summary of Responses
CP(R) 04/07: Part 1 of 2
01/08/2007

Claims Management Regulation

Professional Indemnity Insurance

Summary of responses to a consultation carried out by the Ministry of Justice.
This information is also available on the Ministry of Justice website at www.justice.gov.uk

Contents

Introduction	2
Background	3
Summary of responses	4
Responses to Specific Questions	7
Conclusion and Next Steps	12
Consultation Co-ordinator contact details	13
The Consultation Criteria	14
Annex A – List of Respondents	15

Introduction

This document is the post-consultation report for the consultation paper, Claims Management Regulation – Professional Indemnity Insurance.

It will cover:

- the background to the report;
- a summary of the responses to the report;
- a detailed response to the specific questions raised in the report; and
- the next steps following this consultation.

Further copies of this report and the consultation paper can be obtained by contacting **Niva Thiruchelvam** at the address below:

Ministry of Justice
Claims Management & Private Funding Branch
Legal Services Regulation & Redress Division
3.10 Selborne House
54-60 Victoria Street
London
SW1E 6QW

Telephone: 020 7210 1325
Email: niva.thiruchelvam@justice.gsi.gov.uk

This report is also available on the Department's website at: www.justice.gov.uk

Background

The consultation paper 'Claims Management Regulation – Professional Indemnity Insurance' was published on 23 February 2007. It invited comments on the introduction of compulsory Professional Indemnity (PI) insurance for businesses that provide regulated claims management services and included draft Rules.

Under the provisions of the Compensation Act 2006, businesses that provide regulated claims management service, without an exemption or a waiver, must be authorised and comply with rules prescribed by the Regulator. The Act expressly allows the Regulator to make rules in respect of PI insurance.

Respondents to the consultation on the Conduct Rules, published on 6 July 2006, favoured compulsory PI insurance but felt that the requirement should not apply to introducers and should not be introduced immediately as some businesses may have difficulty obtaining cover. The Ministry of Justice took these comments into consideration and consulted on the following proposals:

(a) Authorised businesses that have contracts with client, whether or not they represent clients, should be required to have PI insurance. The intention is to replicate the Financial Services Authority's requirement in respect of general insurance intermediaries.

(b) Cover should provide for individual claims up to £650,000 with an aggregate limit of £1 million or 10% of annual turnover, if higher.

(c) The excess should be not more than the higher of £5,000 or 3.0% of annual turnover.

(d) The requirements should apply from 1 January 2008.

The Consultation period closed on 25 May 2007. This report summarises the responses and outlines the Ministry of Justice's conclusions on the consultation.

A list of respondents is at Annex A.

Summary of responses

1. A total of 32 responses to the consultation paper were received. Of these, approximately two thirds of responses were from businesses that provided claims management services. Representatives of the legal and insurance industries also responded to the consultation.

2. Separately, the issue has been discussed with the Regulatory Consultative Group, which comprises representatives from the claims management sector, legal field, insurance industry, and consumer groups as well as other regulators.

3. In analysing the responses, we examined the purpose of PI insurance, its availability, the likely cost and impact to businesses, whether it provides protection to consumers and alternative ways consumers might be protected.

4. Claims management businesses have stated that they have never received a complaint based on negligence. Notably, responses in support of PI insurance only referred to theoretical situations in which PI insurance might be available and useful to consumers.

5. The Association of British Insurers' (ABI) response is particularly important as it considers the value of PI insurance to consumers and the effect it will have on the industry:

> "We do not believe that there is a clear-cut case for the introduction of a compulsory professional indemnity insurance requirement for claims management companies. This appears to be an attempt to bring in a layer of costs for these companies without any particular benefit to customers. It is important to remember what professional indemnity insurance does. It protects the wrongdoer against his/her own mistakes, and does not provide benefit directly to the consumer. Furthermore, it is not clear that there are significant risks to customers that would make such insurance a necessity, and we are not in favour of such a policy.
>
> In discussions with its members during the period of this consultation, the ABI has not found any who were involved in, or willing to become involved in, the market for PI for claims management companies. This is not to say that no insurer in the UK will eventually provide such a product, although it is very instructive. From this, one could easily infer that such PI insurance will be difficult to find, and premiums may therefore be high, and restrict the market.

> Overall, we oppose the consultation paper's findings in bringing in a requirement for PI insurance for claims management companies. We believe it may be an attempt to restrict the market by introducing unnecessary burdens where little potential risk exists for serious customer detriment."

6. There was strong opposition to the introduction of compulsory PI insurance by claims management businesses and the ABI, as it did not provide effective protection to consumers and placed a disproportionate burden on businesses.

7. Many of the responses highlighted the difference in the range of claims management services available, depending on the sector in which the authorised business operated, and argued that this should be taken into consideration when setting requirements for PI insurance as it affected the risk of negligence and malpractice. Providing advice, representing claimants, having contracts with clients and holding client money were felt to be important factors in determining whether a business should have PI insurance.

8. Comments on the level of PI insurance needed varied. Some felt that authorised businesses should obtain a similar level of cover to Solicitors as they offered similar services; it was suggested that it would also create a level playing field and provide adequate protection to clients. Others were concerned that the draft Rules did not take account of the varying risks in the different sectors that authorised businesses operated in, e.g. there is a higher risk and higher amount of compensation recoverable in the personal injury sector than in the financial products and services sector.

9. A financial services claims handler's response stressed this concern:

> "A single level of cover is proposed for all claims management firms regardless of the sphere within which they operate. There is no doubt that, where claims are concerned with injury or accident, the sums involved can be very large indeed; for those handling claims of this type the proposal that cover should provide for individual claims up to £650,000 might well be reasonable. But in the case of those concerned solely with financial products and services, the sums involved are relatively low and it is difficult to see why such a high level of cover should be required. ... While it might be administratively more convenient to propose one level of cover for all claims management firms, the one size fits all approach is unfair. It is my view that the level of cover required by the regulations should reflect both the nature and the size of the business."

10. The availability and cost of PI insurance was also identified as a significant factor. New entrants to the market may well find it impossible to obtain PI insurance and, for very small risk, even if cover could be obtained the cost might be prohibitive.

11. Many responses felt that it may be appropriate for the requirement to be introduced later than 1 January 2008 as businesses may wish to obtain cover when they renewed other insurance or prove that they have cover when they renewed their application for authorisation to provide regulated claims management services. There was also the suggestion that a later date would benefit businesses that had already planned for the current financial year. One response proposed a six-month period between the publication and implementation of the Rules relating to PI insurance.

12. A claims management business suggested the introduction of a compensation scheme:

> "We believe a scheme such as the FSCS where firms pay 1% of their turnover would be more beneficial to the aims of better regulation than using the price of coverage and insurance through the private sector."

Responses to Specific Questions

1. **Is it accepted that those businesses that are only introducers should not be required to have PI insurance?**

   The majority of responses agreed with this proposal, citing the exemption of small-scale introducers and the minimal involvement of introducers.

   However, the Association of Personal Injury Lawyers (APIL) felt that introducers posed a risk as claims might not be referred within the time limit, which is vital in the personal injury field. The risks included the possibility that "witnesses may move away, evidence may be destroyed, and memories may fade" which could result in consumers not being able to obtain redress.

   The Solicitors Regulation Authority (SRA) felt that PI insurance should be a requirement if a duty of care existed. It was also suggested that there was confusion regarding the specific role of an introducer. The SRA recommended that if PI insurance is not made compulsory for introducers, then the Regulator should publish specific guidance on the role of an introducer and require introducers to disclose that they do not have PI insurance to consumers.

   The Legal Complaints Service (LCS) supported the proposal and suggested that the introduction of a mandatory system of recording payments would enable an effective audit to occur.

   Liverpool Law Society felt that the potential to cause detriment to consumers needed to be balanced against the cost of PI insurance to introducers.

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2. **Should businesses that represent clients have PI insurance?**

   Overall, there was a positive response to this question, as businesses that had a direct relationship with claimants would have an obligation to them.

   AXA Insurance suggested that businesses providing claims management services were similar to any other business offering advice to members of the public.

   Solicitors proposed similar levels of protection to themselves suggesting that representation of a client was similar to the services provided by them.

   Liverpool Law Society noted that "if all such businesses are compelled to have PI insurance, a better service would ultimately be provided to the consumer as

the businesses are likely to have to improve procedures and policies in order to be able to obtain the insurance at a reasonable premium."

The scope of negligence in managing a claim was identified as an important factor. Some claims management businesses in the financial products and services sector raised the difference in the representation in the personal injury and financial products and services sectors and the corresponding potential for liability. There is greater potential to harm a claim or limit the amount of compensation recoverable in the personal injury sector than in the financial products and services sector.

One claims management company said:

> "We believe that a firm offering Personal Injury Services, arranging insurance for their clients to cover court costs, arranging loans, advising regarding medical conditions or whether the compensation is sufficient to cover the costs of their disability, is very different from advising clients whether they may have a claim on their endowment policy and whether the compensation offered is compliant with FSA Rules."

However, APIL noted that few businesses represented claimants in the personal injury field.

Dividing claims management businesses on the basis of those who used an Ombudsman and those who used Courts was suggested, as this would take account of the nature of the representation, the associated risks and the amount of compensation recoverable.

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3. Should businesses that have contracts with clients but do not represent them have PI insurance?

This proposal was supported on the whole, as PI insurance was thought to be useful if there was a breach of contract. It was also suggested that it might provide consumers with protection and confidence.

The LCS believed that PI insurance should be mandatory for those that accepted payment.

APIL felt that PI insurance would be appropriate in the event that a business fails "to arrange adequate after the event insurance for the client, leaving the client exposed to paying the defendant's cost if the case fails."

The SRA suggested that PI insurance should be mandatory if there was a risk of an actionable harm occurring.

Many suggested that the requirement be limited to those who provided services after referral of the claim to a Solicitor. Again, it was felt necessary to distinguish between businesses in different sectors.

There was also the suggestion that the requirement for PI insurance be dependent on the nature of the contract and scope for negligence, as the level of service differed from business to business. Some businesses investigated claims obtained evidence, advised in order to arrange after-the-event (ATE) insurance and offered loan finance and held client money.

Liverpool Law Society shared concerns over the nature of the contract and associated risks but commented:

> "This does, however, need to be balanced with the cost and availability of PI insurance to these businesses. An important factor in this regard is likely to be the size of the business and it should be noted that such businesses may experience problems obtaining PI insurance.
>
> The Managing Director of PYV, Ian Broscoe, has commented that some insurance providers will not want to encourage the work of claims management companies by offering them protection as many insurance providers view such businesses as being opportunistic and 'intent on provoking claims rather than helping the public'. As a result, even if cover is available, there are likely to be high premiums. A legal requirement for PI insurance may therefore result in some smaller businesses being forced out of the market place."

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4. What should the minimum levels of indemnity and excess be?

Many Respondents agreed to the proposal in the consultation document.

Solicitors felt that authorised businesses should be subject to the same level of cover as they dealt with the same claims in the personal injury field and offered similar services.

AXA Insurance suggested:

> "If the claims management company is representing the client, there should be a far higher limit of indemnity. In this instance, we believe the limit of indemnity should be at least £1m and possibly as high as £5m. This would put it in line with standard limit of indemnities within other liability insurance products and to help to ensure that there is adequate consumer protection.
>
> Where claims management companies are not representing clients, but there is a contractual relationship a lower limit of indemnity would seem

> more appropriate. The £650,000 proposed in the consultation document would appear more than adequate in this context.
>
> In terms of excess, to ensure consumer protection a relatively modest excess would seem appropriate and in this context we have no issues with the proposed maximum £5,000 excess."

Some respondents questioned the use of insurance intermediaries as a comparator as they posed different risks. One claims management company said:

> "I note that you have based the proposed figures on those which apply to general insurance intermediaries. I question whether this is an appropriate comparison given that the potential for loss arising from a error by an insurance intermediary is very much greater than the potential for loss arising from an error by a claims manager dealing with a financial services complaint. ... I believe that the average value of endowment mis-sale compensation claims is under £5,000. These claims are the bread and butter of those dealing with financial services complaints. If the excess is to be set at a figure which exceeds the value of the majority of individual cases then, in effect, the practitioner is paying for insurance that is unlikely to be capable of covering any claim that might be made against him or her. If the intention of the requirement to take out PII is to protect the consumer, it will fail to do so."

Many other responses stressed that different services in different sectors bore different risks.

There was concern over the cost, particularly to small businesses. However, it was also suggested that linking the level of excess to turnover did not take into account high value claims.

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5. Should the requirement be introduced from 1 January 2008 or at an earlier date?

The introduction of compulsory PI insurance for authorised businesses on 1 January 2008 was supported by some as it allowed businesses sufficient time to obtain cover.

Some wished for the requirement to be introduced as soon as possible as regulation is already in force. Those that supported the immediate introduction of PI insurance also acknowledged that businesses needed time to obtain cover.

AXA Insurance acknowledged that the date would be dependent on the market and ability to obtain PI insurance cover.

A claims management company suggested a later date as “given that we have already had to pay fees for the first year of regulation, it would be unreasonable if further costs associated with the regulatory process were to put us out of business before the completion of that first year.”

Many favoured a later date as businesses might have already planned for the current financial year.

Capita suggested that businesses could apply for PI insurance when renewing other insurance or applying for renewal of their authorisation. The LCS said that it should be a “mandatory requirement to produce a copy of their professional indemnity insurance certificate to the Regulator within a specified time of renewal or, preferably, prior to application for annual renewal of their registration.”

A claims management company suggested a six-month period between publication and implementation of Rules.

The possibility of retrospective PI insurance was raised by the SRA but strongly opposed by a claims management company. It was suggested that PI insurance only be available to claims processed after the introduction of the Rules as the cost of PI insurance would increase fees and costs tend to be agreed with clients from the outset.

One claims management company highlighted that “It would be difficult to get cover for claims already in progress, because, as the DCA has itself identified, the insurers may insist on changes to process before it will provide cover. It would also seem appropriate that a training and competence scheme should be introduced and have time to bed-in before PII becomes compulsory. Otherwise each insurer is likely to have their own requirement for staff competence and thereby leading to inconsistencies across the industry.”

Some responses referred to the Financial Services Compensation Scheme and one response suggested that a similar scheme be established for those businesses that are unable to obtain PI insurance by the deadline.

Conclusion and Next Steps

1. The introduction of rules that would require some or all authorised businesses to have professional indemnity insurance is a serious matter. Such requirements should only be introduced where it would be proportionate and clearly in the interests of consumers to do so. The consultation responses raise a number of important points often based on different interpretations of what professional indemnity insurance actually covers and how it operates in relation to different types of claims management businesses.

2. The Department has therefore commissioned an independent insurance expert to review the potential requirements, the market position and to consider the consultation responses. His report provides an objective examination of the practicalities of introducing compulsory insurance in this area, in what form and in respect of what types of businesses. The Report identifies the role of PI insurance as protecting the interests of the policyholder rather than the client. The issues raised were considered further, in consultation with the Regulatory Consultative Group.

3. From discussions with the Regulatory Consultative Group, it is accepted that regulation has already made considerable progress and is able to deal with any emerging issues robustly. However, it is necessary to determine whether any actionable risks remain outside the regulatory ambit and if such a risk does exist, whether PI insurance would be available, provide a remedy to consumers, and be a proportionate burden on businesses.

4. One of the issues consulted on in the consultation was the timing of the introduction of any compulsory PI insurance. The consultation had suggested January 2008. While some favoured an earlier date, most acknowledged that it is simply not functional to introduce a PI requirement at short notice. If some businesses are to be required to have PI insurance then the earliest functional date is April 2008. It is already clear that a requirement cannot be made for introducers to have PI cover as there is no insurable risk and the level of consumer detriment is technical and slight. The high-risk categories appear to be those representing clients in criminal or personal injury claims.

5. Final recommendations and PI insurance Rules will be published in the autumn.

Consultation Co-ordinator contact details

If you have any complaints or comments about the **consultation process** rather than about the topic covered by this paper, you should contact the Ministry of Justice Consultation Co-ordinator, Laurence Fiddler, on 020 7210 2622 or email him at consultation@justice.gsi.gov.uk

Alternatively, you may wish to write to the address below:

Laurence Fiddler
Consultation Co-ordinator
Ministry of Justice
5th Floor Selborne House
54-60 Victoria Street
London
SW1E 6QW

If your complaints or comments refer to the topic covered by this paper rather than the consultation process, please direct them to the contact given on page 3.

The Consultation Criteria

The six consultation criteria are as follows:

1. Consult widely throughout the process, allowing a minimum of 12 weeks for written consultation at least once during the development of the policy.
2. Be clear about what your proposals are, who may be affected, what questions are being asked and the timescale for responses.
3. Ensure that your consultation is clear, concise and widely accessible.
4. Give feedback regarding the responses received and how the consultation process influenced the policy.
5. Monitor your department's effectiveness at consultation, including through the use of a designated consultation co-ordinator.
6. Ensure your consultation follows better regulation best practice, including carrying out a Regulatory Impact Assessment if appropriate.

These criteria must be reproduced within all consultation documents.

Annex A – List of Respondents

1. AAG Plc
2. Accident & Claims Specialists
3. ACM ULR
4. Aqualibra Claims Ltd
5. Association of British Insurers (ABI)
6. Association of Personal Injury Lawyers (APIL)
7. Autocrash Services
8. AXA Insurance
9. Bob the Bankbuster
10. Browne Jacobson LLP
11. Caroline Ley
12. CLAIMS UK
13. Direct 2 Solicitors
14. Endowment Investigations Ltd
15. Forum of Insurance Lawyers (FOIL)
16. Freeclaim Midlands
17. Friends Provident
18. Interactive Law
19. John Eastwood
20. Justice Direct
21. Kennedys

22. Law Society
23. Legal Complaints Service (LCS)
24. Liverpool Law Society
25. MorganGreen Ltd
26. National Accident Helpline
27. Renaissance Endowment Review Services Ltd
28. Solicitors Regulation Authority
29. Sterling West & Associates Ltd
30. The Capita Group Plc
31. Three Branch Place Ltd
32. Whitehall Randall

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CP(R) 04/07: Part 1 of 2