We Fight Any Claim Ltd

Submission to Carol Brady

CMC Review

November 2015

Executive Summary

1. This is a summary of what follows – it therefore omits detailed reference to evidence, but its assertions are all supported, in detail, in the main document.

2. A series of consultations has been announced by the Treasury. The reasonable conclusion is that they are intended to mitigate the impact on financial institutions of their own wrongdoing in misselling PPI, and making secret commissions.

First it is proposed that the impact of *Plevin* be restricted: the proposal appears incoherent; secondly, a time bar, on much less favourable terms than would normally apply, is also proposed for PPI claims.

3. The other aspect of this appears to be an attempt to curtail the success of CMCs in gaining redress for customers.

4. £50bn worth of PPI – or more - was sold. As Lord Turnbull said, the sales were close to fraudulent. The product was represented as providing valuable cover and peace of mind. In fact it was toxic: extremely expensive, with exclusions so onerous that a successful claim was (at best) improbable. This was reflected in Claims Ratios generally worse than 30% - and often much worse than that.

5. There has been a history of regulatory failure, both in allowing this to happen in the first place, and then in failing to enforce remedial action. Despite this, regulation looks set to become weaker rather than the reverse.

6. CMCs have accordingly been responsible for getting back the bulk of all that has been recovered. Those who used CMCs would generally not have recovered their money for themselves. In some cases they were paying someone else to do a job for them; in a large number of others they did not feel capable - and, given their vulnerability, the obstructiveness of the financial institutions, and the unnecessary difficulty of taking action, they were right. There is a perception that FOS would act as a safety net, but that is not true: mainly because claimants just would not even start claims, let alone refer them to FOS. (There are also some systemic issues in FOS's dealing with PPI cases).

7. CMCs in fact represent the most effective agency not just for getting back money misappropriated from ordinary people, but also for making financial institutions behave better.

8. The Banking lobby has persistently characterized CMCs as "ambulance chasers" and "rogues". They have disingenuously suggested their interest is in having customers retain more compensation; they have also suggested that there have been a lot of fraudulent claims: this is simply nonsense. The Treasury now appears to be going along with at least some of this. The approach of the Banks is simply founded on self-interest: they are paying out more because of CMCs and they would like to stop. The current package of measures seems to have the same objective. If so, this would be no more than a matter of preventing vulnerable people from getting back money that was taken from them illicitly.

9. The foregoing context is essential, because what is proposed seems to be based on the premise that CMCs are a bad thing and offer no value. In a better world, there would be less need for CMCs; but that is not the world we live in, and there seems no appetite on the part of the Treasury to change it for the better. CMCs are therefore essential. They are a market mechanism, which benefits consumers.

10. Better regulation of CMCs is desirable, if it is genuinely done to promote a vigorous, fair market for consumers. A regulator committed to this – whether the current one or a new one – would be welcome. But much of the rhetoric does not suggest that is the objective. Moreover, the views of the Banks about this could not be further from the point: one would not ask a fox for its views about the best way to build a chicken coop; and would not trust the consumer protection ideas of someone who had taken £50bn from vulnerable consumers. The idea of a regulatory transfer to FCA is also riven with obvious problems: there would appear to be a potentially untenable conflict in FCA's trying to regulate, fairly, both the firms who sell things and the CMCs who hold them to account for mis-sales.

11. A "price cap" is also proposed. The Banks are lobbying for a one at an unviable level: this is no more than obvious self-interest.

The justifications for "price caps" are that pricing is non-competitive or exploitative; there is no evidence of either of these things here. Pricing is clear, open and has a range of between 15% and 35% (unfortunately uplifted by the 20% VAT taken by the Treasury). The contrast with PPI claims ratios, or the 50% secret commissions which FCA proposes firms will be able to keep, is startling.

In any case, even if there were any justification for a "price cap" (which there is not, although one at a reasonable level might even be to the practical advantage of the CMC sector) there would then be the matter of fairness and reasonableness in setting it. This would require proper research as to things like the margins of CMCs, the investment made by them, their reasonable expectations when they made that investment, and so on. After all, some have invested millions of pounds; and had no reason to consider that their ability to recover this might be limited.

12. As well as benefitting consumers, CMCs provide a great deal of employment both directly and indirectly – it would be reasonable to estimate 50,000 jobs. This would not for a minute justify a bad industry; but it is a further reason to treat a good one fairly.

13. Given the current tenor of the proposals, Judicial Review in a number of areas looks likely.

Counsel's Opinion is being sought as to FCA's proposals on *Plevin* and the time bar, and the possibility of proposals as to a "price cap" and other regulatory change. It is fair to say that if the effect of these proposals is to make CMC business unviable, Judicial Review will be practically inevitable.

Introduction

This paper relates to PPI claims management business in the financial services sector.

It has been prepared by Davies Duffy Smith Consulting Limited on the instructions of We Fight Any Claim Limited ("WFAC"). Whilst it will refer particularly to WFAC, it considers the position of CMCs more generally.

The financial services regulator has been first FSA and then FCA. Where possible, we have referred to the regulator in existence at the material time. Where the relevant matters have pertained during the tenure of both regulators, references to one should be taken to include the other.

1. The Current Position

1.1 At present, a number of things are happening simultaneously. Consultation is about to take place with a view to the "capping" of the fees which CMCs can charge. A separate consultation about the more severe regulation of CMCs is also to be undertaken. This is linked to a proposal that the regulator for CMCs be changed, perhaps even to FCA.

At the same time, FCA is consulting about rules greatly to limit the impact of the *Plevin* case on financial institutions which took and retained very large and undisclosed commissions: in a nutshell, the proposal is that they are to be allowed simply to keep most of what they misappropriated. The FCA has also proposed a "time-bar" for the making of PPI redress claims. The proposal is for a 2-year time-bar as from some time in 2016. The firm that sold the PPI will not have to contact the client to prompt action or warn them of the time-bar. Such an approach is at odds with that under the common law.

This set of potential measures was announced as a "package" by the Treasury. The announcements were accompanied by references to a "clampdown" on "rogue" firms in the claims management ("CMC") sector and to the "social nuisance" of calls by them. Although there is no evidence, or reason to believe, that PPI claims managers are generally "rogues", and business acquisition methods vary considerably, there was no attempt to limit these references: they appeared to be an attempt to characterize the whole CMC sector for positioning purposes.

1.2 The major banks are nevertheless still dissatisfied with this; and appear to be lobbying, actively and strongly, for further restrictions to be placed on CMCs, and for a "fee-cap" at a level that CMCs might find unviable. They would also like to bring in the time bar even sooner (*Sky News bulletin*, 26th October 2015). Their motives are transparent: they would like to pay out less compensation; and CMCs are the main reason they are having to pay out more. Any other explanation is not credible: not least because they are under a legal duty to their shareholders to reduce the redress bill as much as they can; and because they have a history of entirely self-interested, and self-serving, conduct.

1.3 The regulation of the banks thus far, in relation to PPI, has been weak and generally unsuccessful. This did not begin with the latest proposals. The signs of a major problem were clear from early this century. Indeed, there were warnings from "Which?" and the CAB, as from the late 90s. In 2005, the CAB's "Super Complaint" drew attention to the high cost of PPI, and, just as important, the low probability of making a claim, and unreasonable exclusions. The OFT summarized this eloquently on page 6 of OFT 869 (October 2006). The FSA nevertheless declined to intervene (Sue Edwards to Parliamentary Commission on Banking Standards, 9 January 2013).

1.4 In 2007, the FSA declined to take enforcement action against Lloyds in relation to PPI missales. According to sources in the FSA, this was because banks "fought all the way" and "the odds were stacked in favour of the industry". The FSA "lost its nerve" and the banks saw fines as a "cost of doing business": Lord McCall to Clive Briault, Parliamentary Commission on Banking Standards, 9 January 2013. (Mr Briault said he "recognized" some of these "sentiments".)

1.5 In 2008, FOS wrote to FSA to say it thought the problem was so serious, and general, as to mean there ought to be a redress exercise. FSA could have done this pursuant to section 404 of the Financial Services and Markets Act. This would have meant very large numbers of clients could be compensated without the need for a formal complaint by anyone: from a consumer perspective it would have been an ideal outcome. FSA said it did not think this was appropriate – there seems to have been little explanation of why not. It said the matter should be dealt with by proper complaint handling in the banks.

1.6 This was, of course, not forthcoming. There have been a series of FSA and FCA fines and interventions, but these too have been treated as costs of doing business rather than as reasons to modify behaviour. All the major banks – and a number of other major institutions - have been fined in relation to poor complaint handling, and Lloyds twice, most latterly this year. It is inconceivable that Lloyds (or the other institutions) were not aware of the shortcomings. One must presume they were in dialogue with FSA and then FCA; and a number of CMCs wrote to the relevant institutions to point out serious problems. A number of CMCs also wrote at length to FSA, with relevant evidence. But, as late as 2013, Lloyds were, for example, still systemically misusing the so-called "alternative redress method" artificially to reduce redress for many thousands of complainants: Hilary Osborne, *Guardian*, 25th March 2014. Barclays also used this approach; RBS are still trying to do so. (Systemic under-redress is a material issue, with which, of course, unrepresented clients have little hope of dealing: the efforts of Renaissance Easy Claim in exposing this practice by certain credit card providers are currently worthy of note: Michael Robinson, *Moneybox*, 25th July 2015.)

1.7 In fairness to FSA and FCA, their fears of being "outgunned" by large financial institutions were surely well founded. Their financial resources are dwarved by those of each of the major banks. Each of these banks has huge sums at stake. It is easy to see why FSA and FCA would have been, to put it kindly, extremely cautious. Nor was there much advantage to be gained, in political terms, when the Treasury's call was – and apparently remains – for "light touch" regulation. In other words, for the Banks to challenge the regulator is easy and financially rational; for the regulator to challenge the Banks is hard and risky, with, since it is a state body, no market incentive. Notably, FSA's one "success" was as defendant in judicial review proceedings (along with FOS) when, in 2011, the BBA challenged its rule making powers. One might see this as a case of arrogant corporate over-reach by the Banks, which back-fired because it forced FSA to defend itself. But even here, the cost to FSA, and the effort it had to expend, must have sapped it far more than the Banks. It is easy to see why, even following this "success", it had no appetite for conflict in future.

1.8 If anything, FCA looks set to become weaker. The proposals in relation to *Plevin* and the time bar, both deeply "bank-friendly", hardly inspire confidence. The removal of Martin Wheatley, to the dismay of the FCA's Consumer Panel https://www.fs-cp.org.uk/panel-reaction-martin-wheatleys-departure#sthash.JZ9ZxX5i.dpuf further indicates that a Treasury which must be interested in selling its bank shares, and, perhaps, in continuing to receive tax revenues from banks like HSBC, does not want more consumerist obstacles put in the way.

1.9 As the foregoing demonstrates, the considerable, well researched and closely reasoned efforts of Consumer Groups also appear to have had little effect. This is not a criticism of those efforts. If they had been acted upon more readily, harm would have been greatly reduced. But they weren't.

1.10 The scale of the problem is massive. According to FSA, in written evidence given in 2013 to the Parliamentary Commission on Banking Standards, the Banks alone sold approximately 45m PPI policies (the number was provided by the BBA). This leaves out of account, for example, sales by specialist credit card and store-card providers. The FOS estimates 50 billion pounds worth of PPI sales. If anything, these look like under-estimates. (Sales took place over many years, and many records have been systemically destroyed; and even today, providers fail to locate PPI sales when asked specifically to do so.) In any case, it is plain that the total number of complaints so far made represents a modest proportion – almost certainly fewer than half, and probably substantially less than that - of the complaints that could be made. The vast bulk of such complaints would certainly be valid: that is unarguably the case today, as redress and FOS uphold rates demonstrate. There is no reason to believe the sales to those who have not yet complained were any better than the sales to those who have. Even more to the point, the flaws in this product mean that selling it properly was practically impossible. PPI was, almost without exception, a toxic product. As Peter Vicary-Smith remarked in 2005 to the Parliamentary Commission on Banking standards, its designers must have been "…either incompetent or venal." The Claims Ratio for PPI was typically rooted below 20% and was seldom better than 30%. In other words, most, and in some cases virtually all, the "insurance" premium was simply going straight into the pockets of the banks and other financial institutions.

1.11 Lord Sumption, in *Plevin*, was talking about commission when he said that commission of 71.8% went "a long way" beyond what a customer might consider fair; and that the customer would accordingly need to be told in terms that less than 30% of her premium was being used to pay benefits. But whether 71.8% was being taken by way of commission, or other profit to the firm, was immaterial to the customer. The conclusion which follows inexorably is that where a consumer was induced to pay a premium, the bulk of which was not going to provide any benefit at all, and was not told about this, the sale was an unfair one; and anyone who understood what was being sold to him or her would not have bought it.

The Claims Ratio of course is the product of premiums received as against claims made. The very low claims ratios for PPI policies can therefore be best understood as an expression of the extremely low likelihood of making a successful claim. Back and psychological complaints were often excluded explicitly. They are the main causes of long term absence from work. Pre-existing conditions (of course including existing back and psychological problems) were almost always excluded. Short term illness was excluded. Pregnancy was excluded. It is fair to describe these products as profit centres rather than insurances in any meaningful way. But they were sold as providing meaningful protection.

One might see this as little short of fraud. (This was also, explicitly, Lord Turnbull's view: Parliamentary Commission on Banking Standards, 9 January 2013). Again, it is virtually impossible to see how a properly informed customer, with any level of understanding, would have bought, or could fairly have been sold, a product like this.

1.12 Cost also was seldom properly disclosed. Most notably, the usual method of disclosing the (extremely high) cost of credit card PPI was recognized by FSA as inadequate (PS 07/24). It typically presented a charge of 9.5% per year, plus interest at credit card rates, as being "just" 79p per £100 of balance per month. The reality was that the effect, over a 10 year period, might be to **treble** (or worse) an otherwise stable balance. The standard presentation was certainly misleading. It is impossible to imagine that those who used it did not know this; and were greatly enriched. Again, the conclusion is obvious, and damning.

1.13 The vast majority of PPI complaints are submitted by CMCs. (According to Lloyds, the biggest wrongdoer, two thirds of PPI complaints are made by 200 CMCs: which must imply a total, including other CMCs, substantially in excess of 70%.) CMCs are also responsible for the bulk of PPI referrals to FOS (79% according to the most recent FOS annual report). It has also sometimes been suggested (or implied) that those who instructed CMCs would generally have complained on their own without the involvement of a CMC: that is nonsense, and we will address it further in section 3 below.

1.14 It is also fair to add that the extensive marketing undertaken by CMCs has raised awareness generally; and that a proportion of those who complained directly might not have done so without that increased awareness. Some of that marketing has of course been unattractive and irritating, particularly to those who did not have PPI, and we will address that problem below as well.

1.15 Indeed, none of the foregoing is meant to imply that the CMC sector has always functioned well, or that improvements could not be made. If it were not for the Banks (and, arguably, the Treasury), CMCs might well have been their own worst enemies. The relevant matters are examined in section 5 below.

1.16 They should however be separated from the anti-CMC propaganda (which is not too strong a word). This has been relentless, and powerful. The Banking sector has a small number of big players and is hugely funded (in some instances with public money, which the Treasury would like to get back by selling its shares). It has a well-developed approach to PR, and an effective mouthpiece in the BBA. A great deal of this lobbying has been disingenuous in the extreme: see section 3 below. But it has never been meaningfully countered by a CMC sector too young, internally competitive and fragmented to speak for itself in an effective way. PPI claims management is also tainted by association with that relating to "slips and trips" and accident claims, with which, in its most important aspects, it has nothing in common: again, we return to this below (section 3).

1.17 The current position can be summarized as follows:

(a) Financial institutions, primarily the Banks, have taken, perhaps, £50 bn – or more - from in excess of 10m people, by sales which were in many cases close to fraudulent.

(b) Most of this has still not been given back, and if the financial institutions can help it, will not be.

(c) Regulatory intervention has been ineffective.

(d) The well-meant, and reasoned, arguments of consumer organizations have also had only limited effect.

(e) 70% - or more – of what has been recovered has been won by CMCs. This would not have been recovered otherwise.

(f) The Banks have lobbied relentlessly and effectively against CMCs. The reasons are obvious.

(g) Martin Wheatley was removed in July. In the view of the FCA's Consumer Panel, this will further weaken the FCA in protecting consumers.

(h) A "package" of measures has now been proposed by the Treasury and FCA. These simultaneously would:

- allow the banks and other institutions to keep the bulk of the secret commissions made by them, despite the decision in *Plevin*;
- introduce a limitation period shorter than that under the common law for PPI claims; and allow it to be "triggered" by some sort of "publicity campaign" rather than any direct contact with clients;
- apply a "fee cap" – and further regulation - to CMCs. It is suggested the CMCs' regulator might become the FCA. The Banks are lobbying for such a "fee cap" to apply at a level that would make many CMCs unviable (and their suggestions for further regulation are, of course, calculated to cause further problems in doing business – see section 3 below).

2. Some Myths

2.1 As we have pointed out above, a number of plainly untrue, and in some cases absurd, propositions have been advanced. The purpose has been to characterize the work of CMCs as predatory "ambulance chasers" who add no value. This makes it easier to lobby against CMCs or to suggest that they should, for example, be subject to an unviable "price cap": the implicit question becomes "why should they be paid anything?" rather than "why should we intervene in the transparent pricing of a worthwhile business?". (We return to "price caps" in section 7 below.)

Some of the main myths are addressed in the remainder of this section.

2.2 <u>Customers could just as easily complain by themselves, so CMCs are simply depriving them of their money</u>

This is both misguided and wrong in fact.

CMC pricing is clear. Those who deal with CMCs are deciding that they either do not want – "you should do it because in practice I won't get round to it" – or believe they are unable to, complain for themselves. They are accordingly prepared to pay somebody else. Since this is the case, it is, as a matter of logic, incontrovertible that if, CMCs had not been involved, most of the recoveries to date simply would not have taken place.

The other fundamental point is that, for a large number of potential complainants, it simply is not just as easy – or even, in practice, possible - to complain on their own.

The CAB's 2011 report, "The Cost of Redress" encapsulates the problem. In essence, it says that if Banks behaved better there would be no need for CMCs, and hence customers would be able to keep 100% of their redress. But it then deduces that, accordingly, both banks and CMCs are bad. The statements are true, but the deduction is invalid. Unfortunately, as Banks have behaved poorly, and there is no reason at all to believe they are going to stop, CMCs are both necessary and valuable.

That same report points out that PPI was sold to “many” people without their knowledge. Self-evidently, a large number of people in this category would not even have thought to complain without a CMC’s prompting and investigation. Indeed, it appears that, even today, over 43% of the population does not even know there is a PPI problem (according to the FCA, 2 October 2015, only 74% of those surveyed had heard of PPI, and only 77% of those understood there might be a problem with it). Given the volume of PPI sold, it is improbable that many of this 43% did not at some time have it. In practice, their best hope is to be prompted and represented by a CMC.

Moreover, contrary to the myth, a PPI complaint is, for many of the population, prohibitively frightening and complicated. With the greatest respect to those who, for example, read “Which?”, they are unlikely to be typical.

The Money Advice Service has established that 25% of the population cannot read a bank statement. A third cannot calculate the effect of applying interest at a rate of 2% to a sum of £100 (Independent on Sunday, 2 November 2015). One might reasonably infer that as PPI was a toxic product, the most vulnerable were most at risk of being sold it (an assumption supported by the latest FOS Annual Report which shows that complainants about PPI come in greatest numbers from socio-economic groups D&E). But even if they are simply a proportionate part of its victims, they need active, practical help. Only CMCs offer this – at least, on any scale.

The need for CMCs is probably further increased by the fact that the complaint process is more complicated than it needs to be. Financial institutions frequently ask for the completion of a long FOS form (11 pages). This form and another (3 pages) in any case have to be completed if the case is to be referred to FOS. (According to the last FOS annual report, 58% of those who did not refer their cases to it thought either that it would not be worthwhile to do so or would be too stressful; and this includes those non PPI complainants who would have to complete only the short, 3 page form. Little wonder then that 79% of PPI complaints referred to FOS come from CMCs.)

Both the FOS form and the complaint handling processes of the firms (like the Lloyds’ “Lighthouse”) ask for answers to detailed questions – for example “how long had you been working there when the PPI was sold to you?” – which are irrelevant. The consequence, if not the intent, is to put the complainant through what feels like an exam process. For ordinary people this will plainly be a deterrent.

In reality, if the FCA rules (in particular DISP Appendix 3) were properly applied, the matter would not need to be complicated at all. The relevant questions are almost always about what the client was ***not*** told. According to DISP Appendix 3, if the most important matters - in particular the costs or exclusions - were not explained, in a clear way, there was a breach of duty – the sale was “substantially flawed”. In this event, says DISP Appendix 3, it should be presumed that the customer would not have proceeded and hence ought to be redressed. (A presumption like this could, in theory, be displaced by evidence that a properly informed customer would have gone ahead, knowing the product was extremely expensive, and the exclusions were onerous, and hence the product was extremely poor value, but this is, to say the least, extremely unlikely.)

However, although the process should be much simpler, one will wait for a long time before financial institutions simplify it: because it will, after all, cost them money to do so. It is hard to imagine the institutions, regulator and FOS did not understand this was an issue, but things have been done in much the same way for a number of years, so there would seem to be little appetite for change there either.

Since customers have to deal with the process as it is, rather than as it might be, for many a CMC is a practical necessity.

The approach of the banks here is disingenuous, and, if one takes a step back, appears risible. Their purported concern that a CMC not take a proportion of the customer's redress (which by implication they would be only too happy to pay) bears no inspection. If their real worry were that customers be properly redressed, without paying for a CMC, they would be happy to write to all customers to offer them their money back, or at least to invite them to complain, pointing out, in very clear terms, the high cost, onerous exclusions, and poor value of the product. As we have said above, a section 404 review would have dealt with this problem without any need for CMCs – and CMCs could certainly have no complaint about that. The only reason a financial institution could credibly have for trying to minimize CMC involvement (and, indeed, the only one consistent with its duty to its shareholders) would be to minimize redress. This could only be the case because CMCs are winning for customers cases they could not win for themselves.

2.3 <u>The Ombudsman will sort it out</u>

The most fundamental problem with this is obvious. Without the CMC the complaint would not be made, let alone reach FOS.

As a secondary matter, and as we have just demonstrated above, unrepresented clients appear far more likely to drop out after receiving an initial adverse finding.

The foregoing 2 matters mean that even if FOS were perfect, it would be nonsense to suggest that its existence reduced the value of CMCs.

But with great respect to FOS, it is not perfect; and, in fairness to FOS, it would be unreasonable to expect this. When, in 2008, it said it thought that a section 404 review was the right answer, it was surely recognizing the organisational nightmare that dealing with enormous numbers of PPI complaints would become, and foreseeing the potential result.

In any case, it is certainly clear that large numbers of staff with limited levels of training have been deployed. It is also certainly the case that some of FOS's institutional approaches do not reflect an application of the relevant rules and principles, in particular DISP Appendix 3. This may be because of a perceived need for "short cuts"; or a sense that at least some of these sales must have been "alright"; or some other reason. But, in any case, they are misguided.

As examples of some of the problems which have arisen, one might look at FOS's oft-repeated assertion, in adjudications, that credit card PPI represented "reasonable value" (the precise formulation varies, but the substance is certainly this); or its repeated assertion that most clients were not affected by exclusions or limitations, when, in fact, they were, in the vast majority of cases. (WFAC is currently engaged in challenging these propositions.)

The fact that problems are systemic is clear. Aside from the repeated use of the same or similar verbal formulae in adjudications, one might also, for example, point to the "uphold" and "rejection" percentages for Capital One (a conspicuously expensive provider, specialising in sub-prime credit cards). FOS initially upheld over 90% of Capital One complaints referred to it (98% in 2009); but subsequently *rejected* over 90% (94% in the second half of 2012). Such a *volte face* is statistically impossible as a matter of the normal variance of cases. It could arise only from a "corporate" change in approach. Any suggestion that FOS simply looked at "each case on its merits" is not credible. (We know that at least two CMCs made extensive representations about the position here, and the uphold rate is now much higher again; we do not have proof of causation, but if it is a coincidence, it is a striking one.)

One might also reflect that Susan Plevin's complaint was rejected by FOS.

The purpose here is not to pick fault with FOS. But, as with any decision-making body, the possibility of challenge from organizations that can see patterns, and understand why there might be an issue with them, is a necessary corrective. (Of course individual clients can neither see a pattern – because they see only their own case – nor, in fairness, be in a position to challenge; and nor do they have any incentive to pursue more general issues, because their only concern is their own complaint.)

The point is not to deny that FOS is a good thing. Nor is it to suggest that CMCs should not work to improve their performance in dealing with FOS. The point is first, and mainly, that FOS is absolutely not a safety-net which makes CMCs irrelevant or unnecessary; and, in addition, a closer concentration at FOS on the relevant rules would benefit both represented and unrepresented clients. It would also simplify the process of making a referral.

2.4 <u>CMCs add little or no value when making a complaint</u>

Again this does not stand up. At risk of being a little repetitive, and most fundamentally, even a CMC which does no more than write down what the client says and send the form – an exercise which takes no little time, because the process is needlessly complicated - will have added substantial value by actually getting the complaint made.

However, it is also wrong that, as is currently the case, all CMCs be obliged to say that the client's chances of success are no better when using the CMC than by going it alone. (We do not know what evidence was used in making this regulatory rule, nor what reasonable purpose the rule might have been thought to have.)

Of course, the first problem is that all CMCs are different, and that there are a lot of them, which means that even if the average were the same, some CMCs would inevitably have better results than unrepresented clients. (The alternative is statistically impossible.)

However, and although data is currently scarce, it is, even now, demonstrable that the results of particular CMCs are better than those of unrepresented clients. (For example, WFAC takes on cases for unrepresented clients who have already lost, and were going to do nothing further, and reverses that outcome in 40% of cases.)

More to the point, better data could readily be obtained. We do not have access to the uphold rates of all CMCs, but it would be straightforward for the CMR to obtain this; and it is hard to imagine that financial institutions, and FOS, could not provide the relevant information, broken down into represented and unrepresented categories.

In addition to all the other problems to which we have alluded above, the idea that the outcome will necessarily be the same whether one goes it alone, or with the help of one or another CMC, is anti-competitive as well as detrimental to customers. A CMC with very good results should be able to say so. After all, such information is profoundly relevant to the customer's decision about how to proceed. A customer's course of action will primarily be determined by price and likelihood of success. Both these pieces of information should therefore be available to the customer.

2.5 <u>Financial institutions will deal "fairly" or "impartially" with complaints, so a CMC is unnecessary</u>

This statement is made frequently by financial institutions, although the precise formulation varies. The evidence (see 2 above) shows beyond peradventure that it is nonsense. Indeed, it is surprising the regulator ever allowed them to say this at all: because the notion that it is possible to be fair, whilst judging in one's own cause, is obviously questionable. They are saying they will consider fairly whether or not to give financial redress to a complainant, whilst under a primary duty to maximise returns to their shareholders. The conflict of interest could hardly be more profound.

2.6 <u>There have been a lot of "fraudulent claims"</u>

This has been repeated *ad nauseam* by financial institutions, most notably by Lloyds.

Quite apart from the obvious irony of this assertion's being made by the UK's biggest mis-seller of PPI, which took secret commissions in excess of 80% of premium, and has been fined twice by FSA/FCA for failing to deal properly with complaints, it is, quite literally, nonsense.

The idea of a 'fraudulent' PPI claim is close to an absurdity. In fact, the proposition is that PPI claims have been submitted where no PPI had been sold. According to the CAB, 'many' customers did not know whether they had PPI or not. In such cases, it is not unreasonable to submit a complaint on the basis it might have been sold to them. It is also entirely straightforward for the bank to deal with this by pointing out there was no PPI (although, of course, according to the FOS, 20% of the time when an institution states this, it is not true).

The words "fraudulent claim" imply someone is trying to be enriched dishonestly. But here there is no possibility of that whatsoever. The opposite is the case. It is, simply, not in a CMCs interest to make a redress claim where there is no policy. It is just a waste of time and money.

There is a final, important, point. The idea of a "fraudulent PPI claim" might have been fuelled by an inappropriate equation with personal injury claims. There is certainly a perception that "slips and trips" and "whiplash" claims are often not well founded. We will leave aside whether there might be any evidence for that, but, in any case, it has nothing to do with PPI. Personal injury claims arise from accidents. The claimant's account of harm is to some degree subjective. PPI claims do not arise from any accident. They arise from the calculated mis-selling of a toxically designed product to an uninformed customer. The breach of duty in failing to inform the customer of the product's toxic features can generally be established clearly. The loss to the customer is financial and can be precisely quantified. It is not a matter of what the customer says, but a matter of hard, monetary loss.

In these circumstances, to suggest that there have been a significant number of fraudulent claims would appear not just misleading but calculatedly disingenuous.

3. **The value of CMCs**

3.1 We will not repeat at length what we have said above. But it is worth summarizing it, and adding a further point.

3.2 CMCs have been responsible for obtaining the vast bulk of PPI redress thus far. This redress was owed, and without the CMCs it would not have been obtained. The customers who dealt with CMCs were not making a choice between keeping 100% of the redress and that percentage reduced by the CMC's fee (and the VAT added by the Treasury). They were choosing between what they received, net, and nothing. Without CMCs the volume of claims would have been a great deal lower and financial institutions would simply have kept money which they should never have taken in the first place.

3.3 CMCs have also been responsible for the addressing and resolution of a number of issues which would otherwise have caused systemic detriment, and thus have benefited both those who used them and those who did not.

3.4 The history of regulatory failure and the fact that, if anything, banking regulation looks set to be weakened, makes the CMC sector the most credible disincentive to the moral hazard of future misbehaviour by financial institutions. Some may find this contention startling, but that is because of the "Alice in Wonderland" world that much of the commentary and lobbying has been allowed to create. As we have said above, given assertive regulation and decent behaviour by financial institutions, there would be a substantially reduced need for the CMC sector; but that is not the world in which we have lived; and there is no reason to believe it will be along any time soon.

There are, in essence, 2 ways of controlling poor corporate behaviour: regulation and a strong "opposing" sector, paid to hold the corporations to account. One is statist; the other free-market. One would expect the current administration to favour a market-based solution. In truth, it appears to want neither strong regulation nor a vibrant CMC sector. This looks more like cronyism than Toryism.

3.5 There is one other point, which would not matter if CMCs were not providing a highly valuable service. One might reasonably estimate that CMCs provide, directly and indirectly, somewhere over 50,000 jobs. (The estimate is conservative, because data has so far been hard to come by; and it also ignores the employment created when redress money is spent.)

These jobs are often concentrated in places where employment is otherwise scarce.

A wholesale threat to the sector – and the package of proposals just made looks intended to be precisely that – would therefore both damage consumers and, as well, have deeply toxic economic effects. It would also reduce competition in the sector: which flatly contradicts one of the stated purposes of the CMR (in section 5(2)(c) of the Compensation Act 2006: see section 5.8 below).

The MPs for the relevant areas must of course be made aware of the importance of the matter to them. (We know this process has already begun: WFAC is, for example, lunching next week with Nick Thomas Symonds. We understand others are similarly engaged.)

4. Improved Regulation

4.1 Any further action genuinely aimed at improving the CMC sector is of course to be welcomed. But this is to be distinguished from proposals aimed at hobbling it: the latest suggestion from the banks that “cooling off” periods be extended is such an example. (Since they have no interest in benefitting the customer, one must presume their objective is to try to use the time to attack the relationship of CMC and client because, as is plainly the case, they would prefer to deal with unrepresented customers.)

4.2 In fact though, a number of reasonable tools are already available. With regard to the matter which has attracted most comment, “nuisance” calls, the current regulations provide that there can be no “cold-calling” in person, that nobody on the TPS list can be called, and that the CMC has to comply with the applicable code of practice. In other words, CMCs are subject to much the same rules as insurance sales people. It is hard to see why, as a matter of fairness, CMCs should be subject to more onerous rules than this. There are certainly technical problems: notably in that the registration of a landline number with the TPS does not “protect” the same individual’s mobile ‘phone. These issues should be addressed, and CMCs should – and should be expected – to take all reasonable steps to help resolve them. Again, it is germane to add that no CMC would want to make an unwelcome call: it wastes time and money, damages reputation, and accomplishes nothing else.

4.3 Similarly, the use of nonsensical, unsubstantiated statements like “you are owed £X” is already against the rules. At the most basic level, CMCs should tell the truth. But this is a matter of enforcement - which the CMC sector should welcome - rather than rule change.

4.4 The CMC sector, as a whole, should also consider whether to offer to take two further steps: first, an outright ban on up-front fees; and, secondly, a ban on the use of automated recorded messages. (It may be that these two steps are not within the rule making powers of the CMR, because, if they are, and given some of the comment in this area, one might have expected action already.)

4.5 There is no coherent justification for a ban on up-front fees – after all, most professionals just call them “fees”. But that is not really the point. PPI customers have been savagely abused once, and are likely both to be rather more vulnerable, and more indebted, than others. It would therefore be both ethical, and commercially sensible, to exclude the possibility that a client could ever be worse off as a result of dealing with a CMC.

4.6 The use of automated messages is a cause of great irritation. It is impossible to say for sure without further research, but the returns must surely be diminishing. It is hard to imagine that the gain to the sector in getting rid of these would not be worth whatever might be lost.

4.7 There are two straightforward points: if customers do not want, or benefit from, using CMCs, the market will die; and, thus, if a particular course of action causes more harm than good, for those consumers, it is both ethical and commercially sensible to stop doing it. These principles should always inform the behaviour of CMCs.

4.8 However, something else follows from paragraph 5.7 above.

We will deal briefly with the possibility of Judicial Review, in a number of areas, in section 7 below. These matters are subject to Counsel's Opinion, and we will neither prejudice nor pre-empt that. But it is obvious that, in a nutshell, whatever the CMR's power to make rules, it should do so only to give effect to the CMR's statutory purpose: which is in order to promote the interests of those who use claims management services. (Further detail is provided in section 5(2)(c) of the Compensation Act 2006.)

In other words, like the conduct of the CMCs it regulates, the CMR's objective, in making rules, should be to further the interests of the users of claims management services, not third parties. Whatever the other implications of that, it certainly means that paying regard to the wishes or commentary of banks and financial institutions would be manifestly inappropriate. As has been justly remarked, it would be asking for the fox's view about the best way to build the chicken coop; and anything founded on this would be tainted.

4.9 Finally, improved regulation of course does not simply mean adding more rules. If any current rule is not good, it should be changed. For example, as we have pointed out above, the rule against saying that a CMC cannot do better than an unrepresented client is problematic. (Notably, section 5(2)(c) of the Compensation Act 2006 provides specifically that competition should be furthered; and the current rule is inimical to that.)

5. A New CMC Regulator – FCA?

5.1 Consultation is also to take place on a possible change to the regulator for CMCs. A series of possibilities have been adumbrated, which include continuing with the CMR, and a wholly new regulator, but the dominant suggestion appears at present to be that FCA take on the regulatory role. (The "list" is completed by "joint regulation" by the FCA and the CMR, but this does not look like a workable suggestion: "joint" regulation – whatever that would mean and however it would work - would surely increase bureaucracy, cost, confusion and uncertainty.)

5.2 Comment has to be highly qualified and contingent, because the proposals themselves are so inchoate. However, one might point out that the idea of FCA's taking on the role looks riven with problems.

5.3 An independent regulator, whether the CMR or another, whose objectives are to promote the functioning of a robust, effective, CMC market, in which customers can have confidence and are treated fairly, would seem profoundly desirable. To object, one would have to do so out of a predisposition against the CMC sector. Such predispositions are, of course, also called biases.

5.4 There is an obvious risk of, if not a conflict of interest, then an unmanageable contradiction, in FCA's trying to regulate the financial firms who sell products, at the same time as the CMCs who hold them to account for mis-sales. How, for example, could it simultaneously promote confidence in both markets? Or not appear either to CMCs, or financial firms, as favouring, or disadvantaging, one at the expense of the other (with the result that there might be a very high volume of complaints and challenges from one, or the other, or even both, groups)?Furthermore, FCA clearly has plenty to do: as we have said above, one of its problems to date might have been trying to regulate an industry whose big players can each "outgun" it financially and in resources. To place it in a situation in which, in addition to everything else, it has to regulate how potential adversaries relate to each other, as well as how each of them relates to customers, would seem simply to compound that problem.

5.5 However, the main issue for CMCs is clear. Given that the prospective changes appear to be part of a "package" of proposals intended to favour institutions and curtail and disempower CMCs, one might fairly be concerned that whomever the regulator turns out to be, its remit will, in fact, be to limit the effectiveness of CMCs, rather than see to "fair play" as between the CMCs and financial institutions, for the benefit of consumers.

6. A "Price Cap"

6.1 Paradoxically, a "price cap" at a reasonable level might in some ways benefit the sector, by providing some customers with reassurance. Nobody should want to charge excessively, and there would be little practical value in a judicial review of the "principle" of a "cap" which allowed businesses a reasonable return, but eliminated the possibility of over-charging by any unscrupulous outlier. But the concept nevertheless looks deeply flawed; and the CMC sector is well entitled to believe, at present, that the purpose is to decimate it (or worse) for the benefit of the Banks. Again, Counsel's Opinion is being taken, but it is safe to say that such an approach would certainly be subject to judicial review, both because it would be *ultra vires* and unreasonable, and because the affected CMCs would have everything to gain, and nothing to lose, by doing it.

6.2 The "classic" rationale for "price caps" is to deal with uncompetitive, non-transparent, markets: the purpose is to emulate the effect of competition. The other, for example that applicable to payday lenders, is to stamp out oppressive charging of vulnerable people. Anything else just looks like an unwarranted interference in a market.

The CMC sector is competitive – indeed, much is made of the number of CMCs by those who do not like them. And its charges are transparent.

This seems to mean that the "justification" for proposing a "cap" must be that the charges made by CMCs are generally oppressive. At risk of being blunt, this looks like offensive nonsense driven by a banking lobby which does not want customers to be redressed at all.

CMCs typically charge between 15% and 35% of redress, with a mean of around 25%. (WFAC is at the top end, and undoubtedly loses a large number of potential clients as a result, which simply means the market works well.)

The risk of loss is borne entirely by the CMC, and there are losses: many more than there should be, because of the defects in the complaint "system" and the intransigence of financial institutions (see section 4 above).

The cost of investigating "no PPI" cases is also borne by the CMC, and these might amount to a third of those instigated. (We take it that no-one - except, perhaps Lloyds and RBS - would suggest that in circumstances where very high volumes of PPI were sold without customers knowing it, this investigation should not be made.)

Whatever the CMC fee, it is only ever taken out of money which has been won, and which, at risk of labouring the obvious, a client not generally have received otherwise.

In order to earn these fees, the investment has in many cases been extremely large – often millions of pounds - and been made in circumstances where there was no "price cap" and no reason to expect one would be introduced.

Finally, it should be noted that when talking about the fee, those who would attack CMCs often speak in "VAT inclusive" terms. The cost to the customer certainly includes VAT, but only because the CMC is acting as an unpaid tax collector.

6.3 The ironies here are inescapable. A "price cap" is proposed for CMCs, who openly charge no more than 35% of redress, leaving the client with the rest, net of VAT. FSA declined (or was unable) to regulate price, and the "price" of PPI, i.e. the margin over the cost of providing the insurance, was about 80%. Despite the *Plevin* judgement, FCA is currently proposing that firms be able to retain the greater part of very large illicitly taken commissions. On top of this, the exorbitant insurance costs, and commissions, were both exempt from VAT, but when CMCs recover these, the Treasury adds 20% to the CMC fee and keeps it – in effect taking it straight from the client. Of course one might ask why, if the welfare of customers is the primary concern, the Treasury does not at least examine a VAT exemption for CMC fees. Again, the proposition sounds startling, but only because of the "Alice in Wonderland" environment that currently obtains.

6.4 There are some further points about "price caps" and about some of the discussion that has hitherto taken place.

Even if one were to acknowledge that a "price cap" might be appropriate, a number of matters would certainly need to be considered in setting one.

The initial announcement seems to have been made without any research as to the margins of CMCs, their particular business models, or the investment they might typically be having to recover, which was made in an "uncapped" environment. This would surely have to be undertaken.

Given the statutory need to support effective competition, any "cap" would surely have to be set at a level which permitted different types of offering in return for different prices. Service levels can differ, but service has a cost.

Of course, minimum regulatory standards would have to be met, and, again, the greater the regulatory burden, the greater the cost. (This is not to say that high standards should not be required; it is to say that imposing more regulation at the same time as setting an unrealistic "price cap" would simply be unreasonable; and appear to be an attempt to eliminate the sector rather than improve it.)

Moreover, the “structure” of any “cap” would certainly be important, and merit serious consideration.

To take just two points out of a number that would certainly have to be considered:

(a) Should a CMC be able to charge more if a case had to go to FOS before being won?

The answer would seem to be “yes”. The CMC would have had to do more work. If the case had to be argued at length, much more; but, to put it crudely, the fault would plainly be that of the financial institution that rejected a complaint when it should not have done; and the CMC ought to be able to tell the client this.

A differential charge would encourage good CMCs to argue cases better, and harder, which would give them a competitive edge over the others. It would also be helpful in improving understanding of the applicable rules and principles amongst both FOS and the CMCs. It would not encourage the pursuit of poor cases (which should not have been sent to FOS anyway) because no matter what the fee, it would depend on success. There would no point in flogging a dead horse.

(b) What about an “absolute” maximum fee?

This would not work and have deeply destructive effects for consumers. It incentivises the worst result. It would simply mean that the financial institutions would direct the greatest effort at rejecting the largest cases. This would be entirely rational. They would save the greatest amount by doing so; and by doing this could make it harder, or even unviable, for CMCs to pursue them, increasing even further the number of cases in which the institutions kept the customer’s money. The effect would be that those who had lost most, and were most in need of representation, might not get it; and would, in any event, have significantly worsened outcomes.

7. Judicial Review in Various Areas

7.1 Counsel has been instructed in regard to the following matters:

(a) The scope of the regulatory rules the CMR can impose and the matters it has to take into account in doing so – we have talked about this above, and need not add any more;

(b) The scope and extent of, and limitations on, any power to “cap” fees under section 58 of the Courts and Legal Services Act 1990 – again, we have talked about this above, and need not add any more;

(c) The possibility of a judicial review if FCA proceeds as it has indicated it will in regard to *Plevin*. (A separate note has already been sent to FCA pointing out some of the glaring problems here; and a Freedom of Information request – which FCA is resisting – has been made to see how it reached the position it currently occupies.) It is fair to say that unless understood solely as an attempt to limit the consequences for financial institutions, FCA’s position looks, at least to us, arbitrary and incoherent.

Counsel will be asked to opine on FCA’s proposals by reference to, in particular, FCA’s operational objectives: securing an appropriate degree of protection for consumers; promoting efficiency and choice; and protecting and enhancing the integrity of the UK financial system.

(d) A 2 year “time-bar”, without direct client contact to prompt action, appears to us almost as problematic as FCA’s position on *Plevin.* Again Counsel will be asked to opine by reference to, *inter alia*, FCA’s operational objectives.

7.2 Counsel will also be asked to give a preliminary view in regard to the possibility of a change of regulator, in particular a “transfer” to FCA.

7.3 A final thought, and a point CMCs might make: if, as one is entitled to conclude, the real purpose of the foregoing measures is to benefit banks at the expense of consumers, by eliminating the CMC sector, delegated legislation is no way to do it. Nor should a campaign of lobbying and whispering be allowed to disguise this objective. Proper parliamentary debate, and an acknowledgement that, actually, the Banks are such a priority they have to be allowed to keep what they took from 10 million people, should take place. The electorate can then decide what it thinks about that.