EXPLANATORY MEMORANDUM TO

THE LEGAL AID, SENTENCING AND PUNISHMENT OF OFFENDERS ACT 2012 (REFERRAL FEES) REGULATIONS 2013

2013 No. [XXXX]

1. This explanatory memorandum has been prepared by HM Treasury and is laid before Parliament by Command of Her Majesty.

2. Purpose of the instrument

2.1 To provide for enforcement by the Financial Conduct Authority, in relation to financial firms regulated by the Financial Conduct Authority, of the rules on referral fees contained in section 56 of the Legal Aid, Sentencing and Punishment of Offenders Act 2012 ("the 2012 Act"). To provide for the regulated financial firms that will be subject to the rules on referral fees. The regulations apply the rules against referral fees principally to those conducting insurance and insurance mediation and those in the same group as such persons.

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

3.1 None

4. Legislative Context

4.1 The provisions in sections 56 to 60 of the 2012 Act introduce rules against the payment and the receipt of referral fees for legal services in relation to personal injury cases. In the case of the financial firms regulated by the Financial Conduct Authority ("authorised persons"), these rules require implementation through secondary legislation to provide the Financial Conduct Authority with the necessary powers to investigate alleged breaches of the ban and to take action to ensure compliance with the ban. The regulations specify the description of authorised persons to whom the rules against referral fees apply, principally those conducting insurance and insurance mediation and those in the same group as such persons.

4.2 These are the first regulations made under the powers in sections 58 and 59 of the 2012 Act.

5. Territorial Extent and Application

5.1 This instrument applies to England and Wales.

6. European Convention on Human Rights

The Economic Secretary has made the following statement regarding Human Rights:

In my view the provisions of the Legal Aid, Sentencing and Punishment of Offenders Act 2012 (Referral Fees) Regulations 2013 are compatible with the Convention rights

7. Policy background

7.1 Referral fees can be paid by solicitors to third parties who 'refer' business to them. Most personal injury claims are referred to solicitors by claims management companies. However, others such as insurers are also often involved. There are no legislative controls on referral fees, which are estimated to be around £600-800 per case.

7.2 Rules against referral fees in personal injury cases were included in the Legal Aid, Sentencing and Punishment of Offenders Act 2012. The rules cover the payment and receipt of referral fees. Under the provisions of the 2012 Act, the individual regulators in each sector are required to effectively enforce the ban. For regulated financial services firms the relevant regulator is the Financial Conduct Authority (FCA).

7.3 The FCA can only carry out tasks that are given to it by statute or other legislation. Under the Financial Services and Markets Act 2000 the FCA has powers of monitoring and enforcement. These regulations apply the FCA's existing powers of monitoring and enforcement, with appropriate modifications, to the ban on referral fees. This will enable the FCA to use those powers to enforce the ban. If the FCA were not involved in enforcement of this ban there would be no monitoring of compliance by insurers with the ban and no sanctions in the event of insurers acting in breach of the ban.

7.4 These draft regulations also specify that authorised persons for the purposes of referral fees will be subject to the rules against referral fees.

7.5 These are the first regulations made under these provisions and therefore consolidation does not arise.

8. Consultation outcome

8.1 No separate consultation exercise was conducted on these regulations.

8.2 The introduction of the rules against referral fees is widely supported by both the legal profession and the insurance sector. These regulations provide for the enforcement of the ban in the financial services sector through the existing powers of the FCA.

9. Guidance

9.1 The FCA has issued guidance to firms affected by these regulations on how the FCA will supervise firms for the prohibition of referral fee activity in personal injury cases.

10. Impact

10.1 There will be an impact on business. The ban will apply to those conducting insurance and insurance mediation and those in the same group as such persons. It will mean that insurers and insurance brokers are likely to incur compliance costs to ensure firms are not breaching the regulations and can expect to face monitoring and enforcement of the prohibition of receipt of referral fees for personal injury business. The impact on charities or voluntary bodies will be nil.

10.2 The impact on the public sector is none.

10.3 A separate Impact Assessment has not been prepared for this instrument. This is because the impacts of enforcement by the FCA were included as part of the assessment of the wider ban as set out in primary legislation. The Impact Assessment for the relevant provisions in the 2012 Act can be found in the impact assessment produced by the Ministry of Justice titled 'Referral Fees in Personal Injury claims'. This is included as an annex.

11. Regulating small business

11.1 The legislation applies to small business in that the ban will apply to all firms within scope, irrespective of size.

11.2 If the proposals were not applied to small businesses then it is unlikely that they would be applied at all. Many of the firms involved in payment and receipt of referral fees are small claims management companies, insurance brokers and law firms. This means that partial application would be unlikely to meet the policy objectives and would generate competition issues. Partial application might also lead to some businesses reconfiguring in order to avoid the ban.

12. Monitoring & review

12.1 The ban on referral fees will be reviewed as part of the wider post implementation review of the 2012 Act. The Ministry of Justice have committed to undertaking a review in 3-5 years. This will seek to ascertain whether the payment and receipt of referral fees has been successfully stopped.

12.2 The Ministry of Justice will work with the relevant regulators, including the Financial Conduct Authority as part of work to develop an impact evaluation. Success of implementation will be judged on the basis of whether the payment and receipt of referral fees is continuing.

13. Contact

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bhavika.pinto@hmtreasury.gsi.gov.uk can answer any queries regarding the instrument.