EXPLANATORY MEMORANDUM TO

THE ESTATE AGENTS (REDRESS SCHEME) ORDER 2008

2008 No. 1712

and

THE ESTATE AGENTS (REDRESS SCHEME) (PENALTY CHARGE) REGULATIONS 2008

2008 No. 1713

1. This explanatory memorandum has been prepared by the Department for Business, Enterprise and Regulatory Reform and is laid before Parliament by Command of Her Majesty.

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

2. Description

2.l The Estate Agents (Redress Scheme) Order 2008 ("the Order") requires estate agents in the United Kingdom to belong to an approved redress scheme that will deal with complaints related to the buying and selling of residential property. The requirement to belong to an approved redress scheme will only apply to persons that undertake 'estate agency work' as this term is defined in section 1 of the Estate Agents Act 1979 ("the Act") and in relation to residential property as defined in section 23C of the Act.

2.2 The Estate Agents (Redress Scheme) (Penalty Charge) Regulations 2008 ("the Regulations") prescribe the amount of the penalty charge that may be imposed by a local trading standards officer on an estate agent who breaches the duty to belong to an approved redress scheme. The amount has been set at £1,000.

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

None.

4. Legislative Background

4.1 Section 23A(1) of the Act (as inserted by the Consumers, Estate Agents and Redress Act 2007 ("CEARA")) provides that the Secretary of State may make an Order requiring every person that undertakes relevant estate agency work to be a member of an approved redress scheme for the

purpose of dealing with complaints in connection with that work. The Order gives effect to that requirement. 'Relevant estate agency work' is estate agency work in relation to residential property.

4.2 There are further powers in section 23A enabling the Secretary of State to provide that such an Order may only apply to specified descriptions of persons who engage in estate agency work, that it may only apply to specified descriptions of work, that it may limit the types of complaint that may be made under a redress scheme and that it may exclude types of land from the definition of residential property contained in the Act. However, following consultation, the Secretary of State has decided not to exercise any of these powers at this time and, thus, the Order will apply to all persons undertaking relevant estate agency work and approved redress schemes will deal with all complaints in the UK from residential buyers and sellers. A complaint is defined in section 23A(8)(c) as that being made by a person being or having been a seller or buyer of residential property. Section 23C(2) provides a broad definition of residential property. The definition of 'seller' at section 23A(8)(d) and 'buyer' at section 23A(8)(e) makes clear that potential and actual buyers and sellers of residential property will be able to bring forward complaints under the approved redress schemes.

4.3 New Schedule 3 to the Act (as inserted by CEARA) provides that the Office of Fair Trading ("OFT") will have the responsibility of approving redress schemes and sets out minimum requirements which must be met before a redress scheme can be approved.

4.4 Pursuant to section 23B(1) of the Act, trading standards officers will have the ability to issue penalty charge notices to persons who act in breach of the duty to belong to an approved redress scheme. Paragraph 2 of new Schedule 4 to the Act (as inserted by CEARA) allows the Secretary of State to prescribe by Regulations the amount of the penalty charge specified in a notice (not exceeding £1,000).

5. Territorial Extent and Application

This instrument applies to the UK.

6. European Convention on Human Rights

As the instrument is subject to negative resolution procedure and does not amend primary legislation, no statement is required.

7. Policy background

7.1 Under section 23A(1) of the Act the Secretary of State may by Order require persons who engage in estate agency work in relation to residential property to be members of an approved redress scheme for the purpose of dealing with complaints in connection with that work.

7.2 Before making the Order, the Secretary of State must be satisfied under section 23A(6) of the Act that all persons who are subject to the duty will be eligible to join a suitable redress scheme before the duty applies to them. Approval of redress schemes is carried out by the OFT acting in accordance with paragraphs 2 to 8 of new Schedule 3 to the Act. Pursuant to this requirement the OFT has approved a redress scheme to be run by the Ombudsman for Estate Agents. The OFT is also considering two other applications to run redress schemes. Details of approved schemes are available on the OFT website.

7.3 The Order provides that persons who engage in estate agency work, as defined in section 1 of the Act, in relation to residential property will be required to join a redress scheme. Those who are excluded from the scope of the Act, such as solicitors, will not have to join a redress scheme, as they are already subject to controls at least as rigorous as those that will be imposed on estate agents.

7.4 Section 23A(1) of the Act provides that acting in contravention of the duty in the Order, to belong to an approved redress scheme, will be regarded as a breach of duty under the Act. Breach of the duty to belong to an approved redress scheme will be punishable by a penalty charge imposed by a local trading standards officer under a penalty charge notice for a sum of £1,000, as set by the Regulations. In addition, section 3(1)(ca) of the Act makes a breach of the duty to belong to an approved scheme a trigger event enabling the OFT to consider the fitness of an estate agent to practise estate agency work. This means that the OFT will be able to ultimately ban an agent if he is deemed to be unfit.

7.5 The Order will ensure that sellers and buyers of residential property in the UK will have access to free independent redress for complaints against estate agents in relation to the buying and selling of residential property. It is intended that complaints will include those related to the actions of estate agents in relation Home Information Packs (HIPs).

7.6 The Order is similar to the Home Information Pack (Redress Scheme) (No.2) Order 2007 (S.I. 2007/1946), which requires estate agents in England and Wales to belong to an approved redress scheme dealing with complaints related to HIPs. The Estate Agents (Redress Scheme) Order 2008, however, goes further by covering all estate agents in the UK and all

complaints about the buying and selling of residential property, and fulfils a long standing Government commitment to give all sellers and buyers (including potential sellers and buyers) of residential property access to independent redress. It is the Government's intention to repeal sections 172 to 174 of the Housing Act 2004 (under section 53(3) of CEARA) at the same time as the Order comes into force.

7.7 A three-month public consultation was held on the subject matter of the Order and the Regulations (as well as other estate agency matters under CEARA). The majority of those responding felt that it was not necessary to use powers in the Act to alter the scope of redress schemes, and that the penalty charge should be set at £1,000.

8. Impact

An Impact Assessment is attached to this memorandum.

9. Contact

Graham Noyce at the Department for Business, Enterprise and Regulatory Reform: Tel: 020 7215 2135 or e-mail: Graham.Noyce@berr.gsi.gov.uk can answer any queries regarding the instrument.

Summary: Intervention & Options

Department /Agency:	Title:	
Department for Business, Enterprise and Regulatory Reform	Impact Assessment of estate agents redress scheme order and penalty charge regulations	
Stage: **Final**	Version: **1**	Date: 26 June 2008
Related Publications: **Estate agents consultation on powers in CEARA 07 and other changes to secondary legislation and part 1 response to consultation**		

Available to view or download at:

http://www.berr.gov.uk/consultations/open-consultations/index.html

Contact for enquiries: **Graham Noyce** Telephone: **020 7215 2135**

What is the problem under consideration? Why is government intervention necessary?

The Government wants all estate agents in the UK engaged in residential estate agency work to belong to approved redress schemes, thereby ensuring that all buyers and sellers of residential property (and potential buyers and sellers) have access to independent redress. Without intervention a significant proportion of consumers will only have access to redress through the courts. Requiring all agents to belong to comprehensive redress schemes will improve consumer protection and enhance confidence in the industry.

What are the policy objectives and the intended effects?

Requiring all estate agents in the UK to belong to an approved comprehensive redress scheme will ensure that all consumers in the UK who have a relevant complaint against an estate agent dealing in residential property will have access to redress. It will also help to raise standards of service in the industry. A penalty charge regime provides a quick and simple deterrent for sanctioning estate agents that don't belong to approved redress schemes. It will also encourage agents to join redress schemes.

What policy options have been considered? Please justify any preferred option.

We have considered (1) doing nothing (2) make the order requiring redress scheme membership and the regulations setting the penalty charge and (3) encouraging estate agents to voluntarily comply with the proposed powers and changes. Option 2 is the preferred option as it will ensure that all estate agents in the UK engaged in residential estate agency work will join an approved redress scheme and that all consumers will have access to redress. Having a penalty charge regime will ensure that more estate agents join redress schemes and those reluctant to join a scheme, do so more quickly.

When will the policy be reviewed to establish the actual costs and benefits and the achievement of the desired effects? The order and regulations will be reviewed within a maximum of 5 years to ensure it has been effective and reduced detriment in the market.

Ministerial Sign-off For final proposal/implementation stage Impact Assessments:

I have read the Impact Assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options.

Signed by the responsible Minister:

Gareth Thomas

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Date 28 June 2008

Summary: Analysis & Evidence

Policy Option:	Description: Do nothing ie do not make the estate agents redress scheme order and penalty charge regulations

COSTS

ANNUAL COSTS

One-off	Yr
£ 0	

Average Annual Cost (excluding one-off)
£ 0

Description and scale of **key monetised costs** by 'main affected groups'

Total Cost (PV) **£ 0**

Other **key non-monetised costs** by 'main affected groups'

BENEFITS

ANNUAL BENEFITS

One-off	Yr
£ 0	

Average Annual Benefit
£ 0

Description and scale of **key monetised benefits** by 'main affected groups'

Total Benefit (PV) **£ 0**

Other **key non-monetised benefits** by 'main affected groups'

Key Assumptions/Sensitivities/Risks Under this option estate agents in England and Wales would continue to be required to belong to Home Information Pack (HIP) redress schemes. For complaints not related to HIPs, consumers would be reliant on agents belonging to voluntary redress schemes to gain redress. There are no costs or benefits.

Price Base	Time Period	**Net Benefit Range** (NPV) **£**	**NET BENEFIT** (NPV Best estimate) **£**

What is the geographic coverage of the policy/option?	UK
On what date will the policy be implemented?	UK
Which organisation(s) will enforce the policy?	NA
What is the total annual cost of enforcement for these	£
Does enforcement comply with Hampton principles?	Yes/No
Will implementation go beyond minimum EU requirements?	Yes/No

What is the value of the proposed offsetting measure per year?			£	
What is the value of changes in greenhouse gas emissions?			£	
Will the proposal have a significant impact on competition?			Yes/No	
Annual cost (£-£) per organisation (excluding one-off)	Micro	Small	Medium	Large
Are any of these organisations exempt?	Yes/No	Yes/No	N/A	N/A

Impact on Admin Burdens Baseline (2005 Prices)			(Increase - Decrease)
Increase £	Decrease £	**Net**	**£**

Key: **Annual costs and benefits: Constant Prices** **(Net) Present Value**

Summary: Analysis & Evidence

Policy Option: 2	Description: Exercise the the estate agents redress scheme order and penalty charge regulations

COSTS

ANNUAL COSTS

One-off	Yr
£ 0.015m	1

Average Annual Cost (excluding one-off)

£ 0.271m

Description and scale of **key monetised costs** by 'main affected groups' To estate agents in increased redress scheme membership costs (£108k pa and one-off £15k) and increased Professional Indemnity Insurance costs (£163k).

Total Cost (PV) **£ 2.3m**

Other **key non-monetised costs** by 'main affected groups'

BENEFITS

ANNUAL BENEFITS

One-off	Yr
£ 0	

Average Annual Benefit

£ 3.4m

Description and scale of **key monetised benefits** by 'main affected groups' To consumers in reduced detriment from estate agents joining approved redress schemes (£3.4m). Of the £3.4m benefit, 0.34m is obtained from imposing penalty charges on estate agents that don't join approved schemes.

Total Benefit (PV) **£ 29.3m**

Other **key non-monetised benefits** by 'main affected groups'

Key Assumptions/Sensitivities/Risks Under this option the redress order and penalty charge regulations are made and all estate agents in the UK carrying out residential estate agency work are required to join redress schemes. Those agents that don't join redress schemes are subject to penalty charges (and possibly enforcement action by the OFT).

Price Base	Time Period	**Net Benefit Range** (NPV) **£**	**NET BENEFIT** (NPV Best estimate) **£**

What is the geographic coverage of the policy/option?	UK
On what date will the policy be implemented?	1 October 2008
Which organisation(s) will enforce the policy?	OFT and TSDs
What is the total annual cost of enforcement for these	£
Does enforcement comply with Hampton principles?	Yes
Will implementation go beyond minimum EU requirements?	No

What is the value of the proposed offsetting measure per year?			£	
What is the value of changes in greenhouse gas emissions?			£	
Will the proposal have a significant impact on competition?			No	
Annual cost (£-£) per organisation (excluding one-off)	Micro	Small	Medium	Large
Are any of these organisations exempt?	No	No	N/A	N/A

Impact on Admin Burdens Baseline (2005 Prices)			(Increase - Decrease)
Increase £	Decrease £	**Net**	**£**

Key: **Annual costs and benefits: Constant Prices** **(Net) Present Value**

Summary: Analysis & Evidence

Policy Option: 3	Description: Encourage estate agents to vountarily to comply with the proposed powers and changes

COSTS

ANNUAL COSTS

One-off	Yr
£ 0	

Average Annual Cost (excluding one-off)

£ 0

Description and scale of **key monetised costs** by 'main affected groups'

Total Cost (PV) **£ 0**

Other **key non-monetised costs** by 'main affected groups'

BENEFITS

ANNUAL BENEFITS

One-off	Yr
£ 0	

Average Annual Benefit

£ 0

Description and scale of **key monetised benefits** by 'main affected groups'

Total Benefit (PV) **£ 0**

Other **key non-monetised benefits** by 'main affected groups'

Key Assumptions/Sensitivities/Risks Under this option the 10% of estate agents that don't belong to voluntary redress schemes would be urged to join such schemes in addition to statutory HIP redress schemes. We believe that this approach will be ineffective and membership levels will be unchanged. Consequently there are no costs or benefits.

Price Base	Time Period	**Net Benefit Range** (NPV) **£**	**NET BENEFIT** (NPV Best estimate) **£**

What is the geographic coverage of the policy/option?	UK
On what date will the policy be implemented?	NA
Which organisation(s) will enforce the policy?	NA
What is the total annual cost of enforcement for these	£
Does enforcement comply with Hampton principles?	Yes/No
Will implementation go beyond minimum EU requirements?	Yes/No

What is the value of the proposed offsetting measure per year?			£	
What is the value of changes in greenhouse gas emissions?			£	
Will the proposal have a significant impact on competition?			Yes/No	
Annual cost (£-£) per organisation (excluding one-off)	Micro	Small	Medium	Large
Are any of these organisations exempt?	Yes/No	Yes/No	N/A	N/A

Impact on Admin Burdens Baseline (2005 Prices)			(Increase - Decrease)
Increase £	Decrease £	**Net**	**£**

Key: **Annual costs and benefits: Constant Prices** **(Net) Present Value**

Evidence Base (for summary sheets)

[Use this space (with a recommended maximum of 30 pages) to set out the evidence, analysis and detailed narrative from which you have generated your policy options or proposal. Ensure that the information is organised in such a way as to explain clearly the summary information on the preceding pages of this form.]

Introduction

This Impact Assessment (IA) considers the costs and benefits of implementing the powers in the Consumers, Estate Agents and Redress Act 2007 (CEARA 07) requiring persons engaged in estate agency work in the UK in relation to residential property to join an approved redress scheme dealing with complaints from buyers and sellers of residential property, and specifying the level of the penalty charge payable for non membership of approved redress schemes.

Background

Existing regulatory regime

Estate agents in the UK are primarily regulated by the Estate Agents Act 1979 (EAA 79) and secondary legislation made under EAA 79, which:

- regulates the conduct of estate agents in the course of estate agency work, but does not cover the letting of properties;
- lays down the duties that agents owe to clients (such as the passing on of offers, handling money and giving details of charges) and to third parties (such as disclosure of a personal interest); and
- gives the Office of Fair Trading (OFT) the power to issue warning or prohibition orders against those persons they consider to be unfit to carry on estate agency work.

Consumers, Estate Agents and Redress Act 2007

The estate agents provisions in CEARA 07 take forward recommendations made by the OFT in its 2004 study on the market for estate agency services in England and Wales. The OFT concluded that whilst the estate agency market works well in many respects, there was significant consumer dissatisfaction with the services provided. Furthermore, the processes were not transparent and it was difficult for enforcers and consumers to substantiate that abuse had occurred in order that it might be dealt with. The OFT recommended among other things, a number of improvements to EAA 79 to improve the regulatory regime and called for estate agents to be encouraged to join an ombudsman scheme. The Government endorsed the OFT proposals in its response to the OFT report in July 2004, but said that it wished to require all estate agents to belong to an ombudsman scheme.

CEARA 07 amends EAA 79 and introduces measures to:

- require estate agents engaged in estate agency work in relation to residential property to belong to an independent approved redress scheme which will determine disputes between estate agents and buyers or sellers of residential property in the United Kingdom;
- require estate agents to keep permanent records of their dealing with a client for a period of six years;
- increase the OFT and Trading Standards Officers powers to inspect an estate agent's files on a transaction; and
- give the OFT more scope to consider the fitness of an estate agent, ultimately leading to a prohibition order banning an estate agent from practising, and to increase the grounds under which the OFT can issue warning orders to estate agents.

This IA deals with powers in CEARA 07 in relation to estate agency redress schemes. It does not deal with the implementation of provisions in CEARA 07 due for commencement on 1 October 2008, which is covered by the Consumers, Estate Agents and Redress (CEAR) Bill Regulatory IA. Penalty charges for non membership of approved redress schemes were previously discussed in the partial IA that accompanied the estate agents consultation in November 2007.

Estate agents redress scheme membership

CEARA 07 enables the Secretary of State by order to require persons engaged in estate agency work in relation to residential property to join an approved redress scheme dealing with complaints from buyers and sellers of residential property. Making membership of an ombudsman scheme compulsory will improve standards of service in the industry and provide a cost effective means for consumers to gain redress when things go wrong.

Estate agents in England and Wales are already required by order under the Housing Act 2004 (HA 04)[1] to belong to an approved redress scheme in relation to complaints about Home Information Packs (HIPs). Consumers therefore have access to independent redress should an estate agent fall short of any aspect of his duties as laid out in the Housing Act legislation.

The Government's intention in using HA 04 was to introduce the redress requirement quickly. However, the scope of the Bill meant that only estate agents in England and Wales could be required to join an approved redress scheme and such schemes could only consider complaints about HIPs. The redress provisions in CEARA 07 were specifically designed to extend the redress coverage under the HA 04.

As the Estate Agents (Redress Scheme) Order 2008 extends the redress requirement in the Home Information Pack (Redress Scheme) (No. 2) Order 2007 to all complaints about the buying and selling of residential property (including those about HIPS) and to estate agents throughout the UK, the Government will repeal the relevant provisions in HA 04 at the same time as the CEARA 07 redress order comes into force.

Under EAA 79, as amended by CEARA 07, failure to join an approved redress scheme is a trigger enabling the OFT to consider the fitness of an estate agent to operate. If found unfit the OFT may issue a prohibition order banning the estate agent from carrying out estate agency work. The banning process, however, can be a lengthy one; estate agents are given notice of the reasons for the proposed ban, have the right to make representations to the OFT including an oral hearing, and the right to appeal against the ban to the Secretary of State. Estate agents are allowed to continue operating pending the outcome of a fitness investigation. Excluding the more complex cases, the OFT take on average four to six months to investigate the fitness of an estate agent.

Redress scheme scoping powers

In addition to a general order making power requiring redress scheme membership, CEARA 07 contains a number of order making powers enabling the Government to further define the scope of redress schemes:

- a power to specify that the duty to belong to an approved redress scheme only applies to persons of a specified description who engage in estate agency work
- a power to specify the type of estate agency work carried out by persons required to belong to an approved redress scheme
- a power to specify the type of complaint that can be excluded from consideration by an approved redress scheme (which may be framed by reference to a description of person making a complaint)
- a power to exclude land of a specified description from the definition of residential property

[1] The Home Information Pack (Redress Scheme) (No.2) Order 2007

Following consultation, the Government has decided not to exercise the scoping powers in CEARA 07 as the scope of redress schemes are already well defined in the Act. The powers are reserve powers that could be used at a later date if necessary.

Penalty charge for non membership of an approved redress scheme

There is also a power in CEARA 07 to set the penalty charge for non membership of an approved redress scheme.

The Government intends to set the penalty charge for non membership of a redress scheme at £1,000, which is the maximum fee that can be charged under EAA 79.

A penalty charge is a quick and simple deterrent for sanctioning estate agents who are not members of a redress scheme, which can be repeated if necessary. It is, however, only part of the process for dealing with non membership – the ultimate sanction is that an estate agent can be banned from carrying out estate agency work if they refuse to join a redress scheme. But relying only on prohibition orders may lead to some agents not joining a redress scheme until threatened with a prohibition order, or not at all.

Rationale for Government intervention

Redress scheme membership

The OFT report on the estate agency market in England and Wales recommended that estate agents should be encouraged to join a redress scheme. The Government in its response to the OFT report went further and said that it would require all estate agents to belong to an ombudsman scheme. At the time only about 40% of estate agents belonged to voluntary redress schemes, which meant that many consumers with complaints about estate agents were unable to seek redress through a free and independent redress mechanism. Even with the main trading bodies requiring their members to join a redress scheme, which they subsequently did, the Government concluded a significant number of agents would remain outside redress schemes to the detriment of consumers. Making membership of a redress scheme compulsory should also have the effect of improving standards of service in the industry.

Estate agents marketing properties with HIPS are already required to belong to an approved redress scheme, but very few complaints about the buying and selling of residential property specifically concern HIPs[2]. Not extending the redress requirement to cover all complaints about the buying and selling of residential property in the UK, will leave the majority of consumer complaints outside the scope of statutory schemes.

Without the requirement to join statutory redress schemes, it is unlikely that membership of voluntary redress schemes would go above the current high level - about 90% of estate agents currently belong to the voluntary Ombudsman for Estate Agents (OEA) Scheme and the Surveyors Ombudsman Scheme (SOS), both of which include HIPs redress membership. When the Government announced its intention in 2004 to require estate agents to belong to statutory schemes, only about 40% of agents belonged to voluntary schemes. The announcement, together with the later requirement to join a HIPS redress scheme, clearly had a major impact on membership levels. There is a danger that if the Government does not go through with its commitment to require all estate agents in the UK to belong to comprehensive statutory redress schemes, membership levels of voluntary schemes may fall as a agents rely on HIPS redress scheme membership, thereby reducing access to redress.

Penalty charge

[2] The OEA and SOS HIPs redress schemes have received two complaints between them about HIPs since their introduction on 1 August 2007.

Under EAA 79, as amended by CEARA 07, estate agents engaging in residential estate agency work that don't join an approved redress scheme, risk being banned from practising by the OFT. But the banning process can be lengthy, and a few agents may think that there is no real detriment to them if they don't join a scheme until faced with the imminent threat of a prohibition order. To counter this, the CEARA 07 provides for an automatic penalty charge to be levied against any agent who has not joined an approved redress scheme, which can be repeated if necessary. This will increase the costs of non-membership from the outset, and should lead to fewer estate agents finding it profitable to remain outside the scheme for as long as possible.

Objectives of intervention

The objective of the intervention is to exercise powers contained in EAA 79, as amended by CEARA 07, in order to reduce consumer detriment in the estate agency sector.

The intervention will have succeeded if (1) all consumers have access to redress and standards of service in the industry improve; and (2) fewer estate agents remain outside of redress schemes than would have been the case if there was no penalty charge regime.

Options

This IA considers the costs and benefits of implementing the redress powers in CEARA 07. The requirement to join an approved redress scheme can be implemented with or without a penalty charge regime for non membership of redress schemes, but the penalty charge regime is dependant on there being a redress scheme order.

Option 1: Do nothing.

Under this option, estate agents marketing properties requiring HIPs would still be required to belong to a HIPs redress scheme.

Option 2: Make the redress scheme order and penalty charge regulations.

This would result in all estate agents in the UK engaged in residential estate agency work being required to join an approved redress scheme dealing with complaints from buyers and sellers of residential property; and the introduction of a penalty charge regime for non membership of approved redress schemes.

Option 3: Encourage estate agent to voluntarily comply with the proposed powers and changes.

The remaining estate agents who do not belong to voluntary redress schemes would be encouraged to sign up to such schemes, and those agents who already belong to them, encouraged to remain members. As per Option 1, estate agents marketing properties requiring HIPs would still be required to belong to a HIPs redress scheme.

Business sectors affected

The main impact of costs resulting from legislative changes will fall on estate agents. In 2004 the OFT estimated there were about 12,000[3] estate agency offices in the UK. According to the OEA at the start of 2008, this had increased to about 13,000[4]. We have gone with this later estimate, although it is likely the number of branches has dropped since then with recent downturn in the property market. Some of these are members of large chains or groups of independent estate agents, but the majority are small businesses,

[3] OFT report - Estate agency market in England and Wales - page 28, paragraph 3.43
[4] Ombudsman for Estate Agents Annual Report 2007 - page 24

typically employing around 5 people[5]. It is estimated that around 60% of estate agents are small independent firms[6].

Devolution

Estate agency is a reserved matter, so changes to legislation will impact upon estate agents practising in Scotland and Northern Ireland, as well as England and Wales.

Assumptions

Some of the costs and benefits build on those contained in the Partial IA that accompanied the recent estate agents consultation[7] that considered proposals for exercising powers in CEARA 07 and the CEAR Bill Regulatory IA[8].

For convenience we have assumed that all estate agency firms do some form of residential estate agency work. We have also assumed that both OEA and the SOS have been approved to run estate agents redress schemes[9].

Option 1 – Do nothing

Redress scheme order

Not exercising the power to make an order requiring agents to belong to an approved scheme would leave estate agents subject to the provisions in EAA 79, as amended by CEARA 07. While the redress provisions would be set out EAA 79, they would have no impact on estate agents – only by exercising the general order making power requiring redress scheme membership, would estate agents engaged in residential estate agency work be required to join approved schemes for the purpose of CEARA 07. Estate agents in England and Wales marketing properties for which a HIP is required would still have to belong to a HIP redress scheme. Consumers seeking redress for complaints not related to HIPs would be reliant on agents belonging to voluntary redress schemes such as the OEA, or seeking redress through the courts.

The do nothing option is similar to that set out in Option 3, in that the Government would be reliant on those estate agents that belong to voluntary redress schemes remaining members. Without the threat of mandatory scheme membership there is a danger that some estate agents will leave voluntary schemes and rely on HIP redress scheme membership, leaving their clients without access to redress for non HIP complaints. The danger of such an approach is spelt in more detail in Option 3 below.

Summarised costs and benefits:

None.

Penalty charge regulations

[5] OFT report - page 30, paragraph 3.46
[6] OFT report - Annex C, page 121, paragraph 10.57 - Council of Mortgage Lenders research
[7] Estate Agents: A consultation on proposals for exercising powers in the Consumers, Estate Agents and Redress Act 2007 and other changes to secondary legislation relating to estate agents http://www.berr.gov.uk/files/file42348.pdf
[8] Consumers, Estate Agents and Redress Bill: Regulatory Impact Assessment http://www.berr.gov.uk/files/file35347.pdf
[9] The OEA was approved by the OFT to run a redress scheme on 19 June 2008. As of 24 June 2008 the OFT was still considering the application from the SOS. The SOS is already approved to run a HIPs redress scheme, so it is very likely it will be also approved to run a CEARA 07 redress scheme.

Without the order requiring redress scheme membership, estate agents would not be subject to penalty charges for non membership of approved schemes. On its own the penalty charge order would have no effect.

Summarised costs and benefits:

None.

Option 2 – Exercise the redress scheme order and penalty charge regulations

Redress scheme order

Option 2 will require all estate agents in the UK engaged in estate agency work in relation to residential property to join an OFT approved redress scheme. Consumers will benefit from getting redress for complaints against estate agents.

Mandatory redress scheme membership will ensure that the benefits, in terms of reduced consumer detriment, set out in the CEAR Bill RIA are met. The CEAR Bill RIA estimated that overall net detriment from consumers failing to get redress and the time spent trying to do so was £20.5m[10]. Introducing a requirement for estate agents to belong to approved redress schemes reduces the grounds for customers having complaints, reduces the cost of complaining, increases the numbers who complain and increases the number of successful outcomes. This (together with changes to the OFT's enforcement regime) leads to benefits of approximately £15.7m pa. Of this £13.7m[11] is attributable to redress scheme membership.

At the time of the CEARA Bill RIA 60% of estate agents were assumed to be members of voluntary schemes. The figure is now about 90%. If we assumed that the benefit is spread pro rata amongst the non member estate agents, 75% of the projected £13.7m benefit (£13.7m*(30/40)) has already been achieved. Getting the remaining 10% of agents to sign up to comprehensive approved schemes will ensure that the remaining 25% benefit (£13.7m*(10/40) is obtained. Requiring estate agents to join approved schemes will therefore achieve an additional £3.4m benefit. This is probably a conservative estimate, as it is likely that those agents who have held out against joining voluntary schemes are responsible for more detriment than those agents who have joined schemes in the past two years.

The redress requirement will also boost consumer confidence. Consumers, who have not had grounds for complaint, will feel even more confident about property transactions. Those who had been deterred from buying or selling property will feel more confident to do so.

There will be costs for estate agents in terms of membership fees – full fees for agents that do not belong to redress schemes and higher fees for agents who belong to HIP only schemes. But as the OEA and the SOS will provide CEARA 07 redress scheme membership as part of their voluntary schemes, only those agents outside the schemes will have to pay new membership fees. The cost of membership of HIP only schemes is slightly lower than the voluntary schemes, so those agents who belong to such schemes will have to pay slightly higher fees. We estimate that about 5% of agents are not members of any redress scheme and 5% belong to HIP only schemes.

[10] CEAR Bill RIA – page 48 http://www.berr.gov.uk/files/file35347.pdf

[11] The £13.7m benefit is obtained by subtracting the Option 2 benefit (enforcement changes in EAA 79) from the Option 4 benefit (enforcement changes in EAA 79 and mandatory redress scheme membership) (£15.7m - £2m = £13.7m). The benefit resulted from grounds for complaint falling from 20% to 13%, numbers complaining rising from 63% to 82%, successful outcomes increasing from 25% to 88% and the cost of complaining falling from £10 to £8. The value of high value complaints (£10,000) the value of average complaints (£50) and the number of transactions (1.8m) remain unchanged.

The OEA is to charge £141[12] for membership of its CEARA 07 scheme plus a one-off joining fee of £23.50. Membership of the OEA HIP only scheme is £117.50[13] plus the joining fee.

The SOS will not charge a membership fee for RICS members. It will, however, charge non RICS members £188[14]. Non RICS members also have to pay a £300 case fee plus VAT where the Ombudsman makes a decision. These fees also apply to the SOS HIP only scheme. From January 2009 RICS members will also have to pay a case fee, but at the lower figure of £150 plus VAT.

For convenience we have used the OEA charges to estimate the membership costs. We have done this for several reasons: the OEA is the dominant scheme in the sector with 85% of agents belonging to its voluntary scheme compared to about 5% in the SOS[15]; there is significant overlap in terms of members between schemes (it is not uncommon for agents to belong to both schemes for estate agency purposes[16]); and the SOS does not currently charge RICS members (who make up most of its members) a fee for membership.

We estimate that the annual cost of membership for the 5% of agents that don't belong to redress schemes will be in the region of £92k pa (13,000*5%*£141) with one-off joining costs of £15k (13,000*5%*£23.50). The increased membership costs for the 5% of agents that belong to HIP only schemes will be £16k pa (13,000*5%*£24.50).

It should be noted that membership costs were included in the CEAR Bill RIA, but this was based on there being 12,000 estate agency offices, 40% of which were required to join approved redress schemes. The CEAR Bill RIA also assumed the cost of joining approved schemes would be £120 pa[17]. Based on 13,000 estate agency offices and a £141 joining fee, the CEAR Bill RIA underestimated membership fees (previously offset by cost savings) by about £390k[18]. The overall total should have been about £900k.

There will also be insurance costs for agents that don't have Professional Indemnity Insurance (PII), which is a requirement of OEA and SOS membership. The OEA will require members to have PII of £100k, the same level as its voluntary scheme. The SOS will require PII of £250k. The HIP (Redress Scheme) Order 2007 RIA[19] estimated that the cost per branch of obtaining PII cover of £100k would be in the region of £250[20], although this would vary depending on the amount of business conducted, geographical location, management structure, type of business and level of past claims. Once again we will use this figure. Assuming that the 5% of estate agents do not have PII, the cost of obtaining insurance cover will be £163k (13,000*5%*£250). It is likely that this is an overestimate as few estate agents operate without PII regardless of redress scheme requirements.

PII costs were included the HIP (Redress Scheme) Order 2007 RIA, although for England and Wales only. It too assumed that 5% of estate agents needed to obtain PII. Based on the figure of 11,000 estate agents this came too £138k. Based on a national total of 13,000 estate agency offices and there being 12,000 offices in England and Wales, the HIP (Redress Scheme) Order

[12] £120 plus VAT per branch, excluding the £23.50 joining fee
[13] £100 plus VAT per branch, excluding the £23.50 joining fee
[14] £160 plus VAT per branch
[15] According to RICS there are 750 firms carrying out estate agency work that use the SOS.
[16] Members of the RICS must belong to the SOS for their surveying work, but can join either the OEA or SOS for their estate agency work.
[17] CEAR Bill RIA – paragraph 3.60
[18] £141k (£141*(13,000 - 12,000)) + 252k (£21*12,000) = £393k)
[19] Home Information Pack (Redress Scheme) Order 2007: Regulatory Impact Assessment http://www.berr.gov.uk/files/file37999.pdf
[20] The National Association of Estate Agents estimated the cost for a start-up company obtaining PII cover of £100k to be £250.

2007 RIA underestimated PII costs by about £13k[21]. The overall total should have been about £150k.

There will be no costs to consumers as the criteria for approving redress schemes required that access to redress must be free to consumers.

Summarised costs:

Membership costs for agents not belonging to voluntary schemes will be £92k pa and one-off payments of £15k. Increased membership costs for members of HIP only redress schemes will be £16k pa. Costs obtaining PII will be £163k.

Summarised benefits:

Mandatory redress scheme membership will produce £3.4m benefits in terms of reduced consumer detriment.

Increased consumer confidence will lead to greater revenue for estate agents.

Penalty charge regulations

The imposition of a penalty charge regime is likely to increase the number of estate agents joining approved redress schemes.

Where an estate agent has failed to join an approved redress scheme, the imposition of a penalty charge will be a more effective remedy for the consequences of failing to join a scheme, than simply leaving a notice informing the agent that continued non membership may lead to a prohibition order. The fact that a penalty charge can be repeated should also help to concentrate minds.

With 90% of estate agents signed up to voluntary redress schemes and all estate agents in England and Wales marketing properties with HIPs required to belong to HIPs redress schemes, we expect the number of estate agents to sign up to CEARA 07 redress schemes to be very high even without the threat of penalty charges.

As mentioned above, requiring the remaining 10% of estate agents not in voluntary schemes to join comprehensive approved schemes will result in annual benefits of £3.4m. If the penalty charge regime persuades 10% of the remaining estate agents (1% overall) to sign up to approved redress scheme who would otherwise not do so, 10% of the benefit (£0.34m) that would have been lost if the agents remained non-members, is achieved (£3.4m*10%).

There will of course be costs in terms of penalty charges for those estate agents found not to be members of redress schemes.

We envisage that local Trading Standards Officers (TSOs) will visit estate agents upon the receipt of a complaint. Upon finding that the firm does not belong to an approved redress scheme, the TSO will impose a penalty charge and report the finding to the OFT. We would expect the TSO to allow the firm sufficient time (about four weeks) to apply to join an approved scheme, before following up the visit. If the firm has not joined by then (or given sufficient proof that the process is under way) a second penalty charge will be imposed, the OFT notified and a fitness investigation commenced.

If we estimate that 1% of the 13,000 estate agency branches in the UK are found not to be members of redress schemes and receive a penalty charge and 10% of those agents

[21] (12,000 - 11,000)*5%*£250 = £12.5k)

subsequently receive a second penalty charge, the total cost in terms of fines will be £143k based on a £1,000 penalty charge[22].

Summarised costs:

Any penalty charges paid by non-member estate agents (estimated at £143k) will turn up as corresponding benefits for the collecting organisation. IA guidance is that only additional costs – excluding transfers – should be quantified in cost-benefit analysis[23]. Any penalty fees paid are therefore not counted as additional costs/benefits above the do nothing option.

Summarised benefits:

Some to consumers in reduced consumer detriment resulting from estate agents signing up to redress schemes faster than would be the case without a penalty charge regime. It is expected that reduced consumer detriment will amount to £0.34m pa. This figure forms part of the overall benefit attributable to mandatory redress scheme membership.

Option 3: Encourage estate agents to voluntarily comply with the proposed powers and changes

Option 3 assumes that instead of the redress scheme order and penalty charge regulations the Government instead publishes its recommended course of action and relies on estate agents to comply with this guidance.

Redress scheme order

This course of action has limitations for redress scheme membership as the Government would be reliant on encouraging the remaining estate agents who do not belong to voluntary redress schemes to sign up to such schemes, and those agents who already belong to them to remain members.

When the Government announced its intention in 2004 to make membership of approved redress schemes mandatory only about 40% of estate agents belonged to voluntary redress schemes. Currently about 90% of estate agents belong to these schemes (and a further 5% to HIP only schemes). While redress scheme membership was on the rise anyway, a large part of this increase can be put down to the threat of statutory action. Relying on persuasion to get the 5% of agents not belonging to redress schemes and the 5% belonging to HIP only schemes to sign up to voluntary schemes is likely to be ineffective leaving redress scheme membership at 90%. Consequently there will be no costs or benefits from adopting this option.

Without the threat of mandatory scheme membership there is a danger that some estate agents will leave voluntary schemes and rely on the statutory minimum of HIP redress scheme membership, leaving their clients without access to redress for non HIP complaints.

Raising awareness of redress schemes and the benefits of dealing with scheme members would result in advertising and publicity costs. These costs would fall mainly on the redress schemes but we would also expect to see some campaigning by the OFT.

Summarised costs and benefits:

None.

Penalty charge regulations

[22] ((13,000 x 0.01) x 1,000) + ((13,000 x 0.01 x 0.1) x 1,000) = £143,000.
[23] http://www.cabinetoffice.gov.uk/regulation/ria/toolkit/analysis_cost_benefits.asp

As mentioned above, the penalty charge for non-membership of redress schemes is dependant on there being a redress scheme order. Without the order requiring redress scheme membership, estate agents would not be subject to penalty charges for non membership.

Summarised costs and benefits:

None.

Small firms impact test

It is estimated that 60% of estate agencies are small businesses. The costs of belonging to a redress scheme are on a per branch basis and will not therefore have a disproportionate impact on small estate agency firms that have comparatively few branches. In addition, the costs of belonging to a redress scheme are small compared to overall turnover, so it is not expected to have a discernable impact on the industry. The cost of PII cover is packaged according to the level of fees received by an estate agency business, at least at the lower level of fee levels, so smaller firms will pay a smaller premium for the same level of PII compared to a larger firm. Penalty charges should only apply to those firms not part of a redress scheme.

Competition assessment

All estate agency firms engaged in residential estate agency work will be required to join an approved redress schemes. By requiring the 10% of agents outside voluntary schemes to sign up, it will help create a level playing field in terms of redress provision. With both approved redress schemes accepting applications from all estate agents, individual firms will have a choice of schemes to join, although we expect few non RICS members to join the SOS. The penalty charge regime will not affect those firms that join an approved redress scheme. Estate agencies will retain incentives to compete vigorously, perhaps more so, given that consumers will have an independent body with which to seek redress. This should open up additional competition among firms to provide high-quality services and minimise practices that lead to consumer detriment and complaints.

Other tests

We do not believe that there will be any impacts in the areas of legal aid, sustainable development, carbon use, the environment, health, race equality, disability equality, gender equality, human rights and rural affairs.

Compensatory simplification measures

As the Estate Agents (Redress Scheme) Order 2008 extends the redress requirement in the Home Information Pack (Redress Scheme) (No. 2) Order 2007, to all complaints about the buying and selling of residential property (including those about HIPS) and to estate agents throughout the UK, the Government will repeal the relevant provisions in HA 04 at the same time as the CEARA 07 redress order comes into force.

Enforcement and sanctions

The redress scheme powers will be enforced by the OFT and local Trading Standards Departments. They already enforce similar powers in England and Wales with regard to HIP redress schemes.

Following the changes, Trading Standards Officers will be able to impose penalty charges on estate agents that do not belong to an approved redress scheme. Those agents that refuse to join a scheme may ultimately be banned from carrying out estate agency work.

The penalty charge regime should reduce the amount of enforcement action needed, by galvanising those agents who are unaware of the need to join a redress scheme or unwilling to do so quickly, into doing so. This will enable the OFT to concentrate on the rogue agents who have no intention of signing up.

Compliance and monitoring

We expect compliance to be very high as failure to belong to a redress scheme will mean that estate agents face the possibility of multiple penalty charges as well as being subject ultimately to a prohibition order. It is a criminal offence for estate agents to continue to practise once they have been banned from engaging in estate agency work by the OFT.

Consultation

The OFT consulted widely with stakeholders in putting together its report on the estate agency market in England and Wales (2004) which recommended that estate agents should voluntarily belong to a redress scheme. The redress measures in CEARA 07 were widely debated in Parliament during the passage of the Bill. The redress scheme scoping powers and level of the penalty charge were the subject of a public consultation.

Post implementation review

As with all the estate agents provisions in CEARA 07, the redress requirement and penalty charge regime will be reviewed within a maximum of 5 years of their introduction to ensure that the changes have been effective and reduce detriment in the estate agency market.

When the redress requirements come into force, the Government will repeal the HIPs redress provisions in HA 04

Table 1: Summary of costs and benefits

Option	Costs	Benefits	Net total
Option 1	None	None	0
Option 2	Membership costs £108k pa and one-off £15k PII costs £163k pa	Reduced consumer detriment £3.4m pa (including £0.34m attributable to penalty charges)	£3.1m
Option 3	None	None	0

Specific Impact Tests: Checklist

Use the table below to demonstrate how broadly you have considered the potential impacts of your policy options.

Ensure that the results of any tests that impact on the cost-benefit analysis are contained within the main evidence base; other results may be annexed.

	Yes	No
	Yes	No
	Yes	No
	Yes	No
	Yes	No
	Yes	No
	Yes	No
	Yes	No
	Yes	No
	Yes	No
	Yes	No
	Yes	No

Annexes