

**Mandatory Client Money Protection Schemes for Property Agents
Consultation Response from ARLA Propertymark
December 2017**

Background

1. ARLA Propertymark is the UK's foremost professional and regulatory body for letting agents; representing over 9,000 members. ARLA Propertymark agents are professionals working at all levels of letting agency, from business owners to office employees.
2. Our members operate to professional standards far higher than the law demands, hold Client Money Protection (CMP) and we campaign for greater regulation in this growing and increasingly important sector of the property market. By using an ARLA Propertymark agent, consumers have the peace of mind that they are protected and their money is safe.

Question 1. Do you think that client money protection schemes should:

- a) **Be 'market led' – approved by Government in order to operate (similar to the redress and tenancy deposit protection schemes):**
- b) **Be administered by a Government body designated by the Secretary of State;**
- c) **A mixture of a Government administered scheme and Government approved schemes?**

3. ARLA Propertymark favours option A and believes that CMP schemes should be 'market led' but approved by Government in order to operate. This is on the basis that several CMP schemes already exist, the majority of agents are already members of a CMP scheme and the current regime creates competition in the market as some schemes, like Propertymark's, are part of the professional bodies operating in the industry and some are commercially available to the industry at large. A single scheme, operated by Government as proposed in option C would stifle competition in the market and may ultimately lead to agents paying a much higher CMP Levy than they current are without offering any greater protection or consumers.
4. By way of example, while regular independent inspections of members client accounts minimises the cases of fraud and financial mismanagement within Propertymark's membership, there are a small number of cases which demonstrate the track record of the Propertymark CMP scheme in supporting consumers. In December 2014, Janine Pickett of Stour Provost, took money from a branch of Dorset Lettings, which she ran under franchise. Police investigations found that financial records showed Ms Pickett paid for Mediterranean cruises and a £7,000 Welsh pony with the proceeds. The situation caused stress and worry for staff, landlords, tenants, suppliers and the franchisor.

However, because the organisation was a member of ARLA Propertymark, landlords and tenants were able to recoup the vast majority of their losses through Propertymark's CMP scheme.¹ The majority of these payments related to missing rental payments to landlords however there were a small number of deposits included in the overall total where Dorset Lettings had failed to register them.

5. Option A would also require minimal Government investment as we envisage the schemes operating under license in a similar manner to the way Government has approved the redress and tenancy deposit protection schemes. Indeed, the costs associated with any tendering process for the scheme providers could be self-funded with all applicants paying a fee to cover the Government's costs in administering the tendering process.
6. We would recommend, again similar to tenancy deposit protection and the redress schemes, the tendering process should result in five-year contracts being awarded and only Government-approved schemes should be able to provide CMP.

Question 2. Apart from the necessary requirement upon scheme providers to produce a certificate to enable a property agent to comply with s.133 (3), should the Government mandate:

- a. Any requirements for a client money protection scheme to be approved/designated?
- b. The conditions which must be complied with by scheme providers?

Please provide reasons

7. ARLA Propertymark believes that Government should mandate additional requirements. We believe that the Government should place requirements on both scheme providers, as outlined in our response to questions three and four and on the nature of CMP scheme membership that a property agent must obtain as outlined in our response to questions five and six.

Question 3. If requirements for a client money protection scheme to be approved/designated are mandated by Government, what do you think these should include? Where appropriate please specify financial amounts (e.g. in reference to minimum levels of cover and policy excesses).

8. A CMP scheme should cover loss of:
 - a. Rent;

¹¹ <http://www.bbc.co.uk/news/uk-england-dorset-30576212>

- b. Other client funds held by agents such as a float to pay for maintenance and repairs;
 - c. Unprotected deposits (i.e. those not registered or those that fall outside of the requirement to be registered); and
 - d. For properly protected insurance-backed deposits only, any deductions from the deposits that are due to the landlord. This is on the basis that with insurance-backed deposit protection, agents generally hold the deposit in their client account as stakeholder for the landlord. If the agent then misappropriates the deposit money, the deposit scheme will pay out any money due back to the tenant but will not pay out any agreed or adjudicated deductions to the landlord. This is not the case with the custodial schemes as the deposits are paid into the scheme at the outset of the tenancy.
9. Schemes should not be permitted to impose an excess on claims by tenants or landlords.
10. If Government choose to impose mandatory scheme requirements, they should stipulate that consumers are required to provide no more than a copy of their tenancy agreement (tenant), terms of business with the agent (landlord), bank statements illustrating rental payments or a pattern of payments and then non-payment by the agent and any supporting correspondence. We make this suggestion to ensure that schemes operate fairly for consumers and do not create unnecessary or overly complex barriers to avoid paying out.
11. In order to make a CMP claim, applicants (tenants and landlords) should be required to report any loss of funds to the police and request a crime number. This will ensure that the police do not see the matter as a civil offence when it comes to prosecution and will allow the scheme operators to make claims against the agent under the Proceeds of Crime Act 2002.

Question 4. If the conditions which must be complied with by scheme providers are mandated by Government, what do you think these should include? Where relevant please specify any financial amounts.

12. ARLA Propertymark believe that the Government should require scheme providers to deliver minimum levels of cover. As the largest provider of CMP in the market with scheme limits that have evolved based on experience of claims made against the scheme, we believe the minimum scheme requirements should underpin pay-outs up to:

- a. £25,000 on an individual application for reimbursement (i.e. from a tenant or landlord) on the basis that this figure will cover the vast majority of applicable rents or deposits;
 - b. £500,000 on a claim made against any single company or agency; and
 - c. Qualifying schemes should be able to demonstrate that they are equipped to pay up to an annual aggregate of £5,000,000 per year.
 - d. We would also recommend that landlords should only be able to claim up to three months' missing rent on the basis that landlords must take some level of personal responsibility for checking they have received their rental payments from their agent.
13. Each approved scheme should report to the Department for Communities and Local Government (DCLG) or the Lead Enforcement Authority (should the Lead Enforcement Authority take over responsibility for managing the tendering and renewal processes) using Key Performance Indicators and Service Level Agreements set out by DCLG or the Lead Enforcement Authority . These indicators should include the scale of the cover being provided, the number of claims and how many claimants are involved, along with the time taken to process claims.
14. Approved schemes should be insurance-backed to an appropriate level so they can pay out many times more than the income they receive through a CMP Levy. Excesses payable by the scheme providers to their insurer in the event of claims should be based on their business models and commercial decisions. However, it is essential that scheme providers report on and demonstrate their ability to meet these excesses in the event of claims being made.
15. The limits of the Propertymark scheme are based on experience of running the biggest scheme of its kind. Based on the track record since the inception of the scheme, this would cover 100 companies going out of business per year at the average claim rate. In the history of Propertymark (formerly NFoPP) CMP there have only been 12 major claims against the scheme. Provided claims meet the scheme rules, in all bar two occasions, all monies claimed have been repaid. The two exceptions were where the total claims exceeded the £500,000 per company rule but in both cases claimants received more than three-quarters of their money back.
16. As happened with the tenancy deposit schemes when they were first brought into force, we would recommend creating User and Provider Groups whilst the requirements become established in the market to ensure that the schemes are operating as expected

and any unanticipated issues are brought to light and dealt with swiftly and consistently across scheme providers.

17. Finally, there must be General Data Protection Regulations (GDPR) complaint Data Sharing Agreements between all CMP providers and DCLG / the Lead Enforcement Authority to ensure that if an agent is expelled from one scheme they are prevented from joining another scheme; as currently exists with the redress schemes.

Question 5. Do you think that the regulations should impose any requirements about the nature of client money protection scheme membership that a property agent must obtain? (For example, dependent upon the size of business that a property agent is operating (and therefore the sums of money they are likely to hold), property agents may be required to obtain a particular level of insurance, in order to ensure that all the money they hold is adequately protected.)

18. Yes, Propertymark does think that the regulations should impose requirements about the nature of CMP scheme membership that a property agent must obtain.

19. CMP should be the option of last resort for a consumer. It should only ever be needed in exceptional cases and scheme operators should have a responsibility to try and minimise the risk of an agent misappropriating their client funds. In our experience, in order to ensure the scheme itself is as robust as possible, has the ability to pay out in the event of a claim and is actively minimising the risk of claims for the tenants and landlords it protects, we would recommend the following conditions be placed on agents:

- a. All client funds should be deposited into a specifically designated client account held with a recognised bank or building society which should be kept separate from the firm's own money.
- b. Each transaction must be properly recorded so that it is clearly identifiable to an individual client.
- c. All transactions must be monitored and reconciled on a regular basis.
- d. Firms should be required by schemes to provide an annual independent review of their client account with the reviews vetted against set requirements.
- e. Firms should have Professional Indemnity Insurance which should include cover for theft by staff members. The limit of the indemnity should be based on the firm's fee income. For example, with Propertymark's CMP scheme, organisations with a total annual fee income of up to and including £150,000, the limit of indemnity for Professional Indemnity Insurance is a minimum of £150,000. For organisations with a total annual fee income over £150,000, the limit of indemnity must be at least £500,000.

20. Some agents will entrust the accounting functions of their clients' money to a Client Accounting Service Provider (CASP). This is where a separate legal entity manages client money on behalf of the agency. In order to protect the agency and therefore their landlord and tenant clients, we strongly believe all CASPs must be required to belong to a CMP scheme themselves. If they do not, then the client funds held by the CASP will not be covered by CMP.
21. We also believe that CASPs should be required to provide an annual independent audit of all of their client accounts; not just those holding the finances of members of a CMP scheme. This is because the health of the CASP's other accounts could impact on the wider fate of the CASP itself and should the CASP misappropriate its client's funds, it would therefore be misappropriating the agent's client funds. In addition, in order to further safeguard the larger sums of client funds held by CASPs, we would argue that CASPs require higher Professional Indemnity Insurance limits and should not have any exclusion or limitation in respect of fraud or dishonesty (fidelity cover relating to the CASP's own money may be limited or excluded). For example, Propertymark's CMP scheme requires CASPs to hold Professional Indemnity Insurance with a limit of indemnity of at least £2million.
22. Further, agencies using CASPs should still be required to join a CMP scheme but should not be required to have their accounts reviewed regularly on the basis that the CASP is managing the client funds on a day-to-day basis but the agency may occasionally handle client funds (as outlined in our response to question six below).
23. Finally, some letting agents who form part of a franchise model (but not all franchise networks) have centralised accounting with the franchisor managing the client account on behalf of their franchisees (this is to reduce the risk to the franchisor of a franchisee misappropriating client funds). However, the franchisees will still have the ability to handle client money for the reasons set out in response to question six below therefore should also be required to join a CMP scheme. In such situations, arrangements should be in line with those of agents using CASPs.

Question 6 – If the regulations impose requirements about the nature of client money protection scheme membership that a property agent must obtain, please specify what you think such requirements should include (detailing financial amounts where appropriate).

24. All agencies handle client money as, alongside let-only services, they will also offer a rent collection and fully-managed service. Even on a let-only basis, agents will generally require

the tenant to pay the deposit and first months' rent to the agency so they can protect the deposit (or remit the deposit to a custodial scheme) to ensure compliance with the Housing Act 2004 and take their commission from the first months' rent before remitting the remainder to the landlord.

25. We also have to factor in that under the Draft Tenant Fees Bill, the holding deposit will be client funds until it is either forfeited or is returned as part of either the tenancy deposit or first month's rent.² Therefore, any agent taking a holding deposit after the ban comes into force will be handling client funds.
26. Even if an agency's business model is that it doesn't routinely handle client money, there will be circumstances where they do hold client funds. For example, if a tenant pays their deposit or first months' rent in cash or cheque or directly to the agency for a short period of time before it is processed by a CASP. In these cases, the risk to the consumer remains the same as if the agency were managing their client funds themselves and therefore such agencies should also be required to belong to a CMP scheme.
27. The Government should use the definition of a letting agent as set out in Section 83 of the Enterprise and Regulatory Reform Act 2013.³ This is to ensure a consistent approach with existing legal requirements and to prevent the possibility of an agent only having to be a member of either a CMP scheme or a redress scheme. In order to fully protect consumers, letting agents need to be members of both.

Question 7. Enforcement of the requirement to be a member of a client money protection scheme will be carried out by local authorities. Do you think that responsibility should be at:

- a. District council level i.e. by local housing authorities**
- b. County Council level i.e. Trading Standards?**

28. We believe that enforcement should be carried out at County Council level by Trading Standards. This would mean that enforcement responsibility is in line with other lettings law such as the legal requirement for letting agents to display all fees, charges and penalties under the Consumer Rights Act 2015.⁴
29. Furthermore, Trading Standards are designed to work with and enforce against businesses and whilst CMP protects consumers, it is businesses that are required to have CMP.

² <https://www.gov.uk/government/publications/draft-tenants-fees-bill>

³ <http://www.legislation.gov.uk/ukpga/2013/24/contents>

⁴ <http://www.legislation.gov.uk/ukpga/2015/15/contents>

Conversely, Environmental Health at District Council level is more concerned with property standards.

30. Where enforcement is carried out, the money collected from fines should go back to the enforcing body and be ring-fenced for further enforcement activities in order to adequately resource enforcing departments to ensure the new requirements are complied with by the whole market and all consumers are protected.

Question 8. Do you think that the penalty of non-compliance with the requirements to be a member of a client money protection scheme should be:

- a. A civil penalty of up to £5,000 in line with the penalty for non-compliance with the requirement to belong to a Government-approved redress scheme or non-compliance with the transparency requirements of the Consumer Rights Act 2015;**
- b. A civil penalty of up to £30,000 in line with the civil penalty for committing a banning order offence;**
- c. Other (please specify)**

31. It is vital that the fine is reflective of the amount of money at risk of misappropriation and that the likelihood of enforcement is an actual deterrent to rogue operators rather than being seen as “the cost of doing business”. Therefore, ARLA Propertymark believe that the penalty for non-compliance with the requirement to be a member of a CMP scheme should be a civil penalty of up to £30,000 and a Banning Order offence.

32. By ensuring that the penalty for non-compliance includes a Banning Order offence this would be consistent with the Government’s approach to enforcement under the Housing and Planning Act 2016; where Banning Orders have been extended to rogue landlords and agents who commit serious offences against tenants.⁵

Question 9. Please provide any further comments or concerns that you have regarding the implementation and enforcement of mandatory client money protection scheme membership that have not been covered in this consultation document.

33. There should be at least a six-month lead in time before enforcement of the rules commences to allow agents to assess their current state of businesses finances and ensure they are registered with an approved scheme.

⁵ <http://www.legislation.gov.uk/ukpga/2016/22/contents>

34. We recommend that the requirements to join a CMP scheme are introduced from April 2018 with enforcement commencing from April 2019 so that CMP comes into force either before or at the same time as the ban on tenant fees. This is to ensure that consumers are protected should an agent use their client funds to try and keep their business afloat once they lose their tenant fees.