

Travel insurance review

Summary of responses and next steps

June 2007



HM TREASURY



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ISBN 978-1-84532-314-1
PU309

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FOREWORD REGULATING TRAVEL INSURANCE

In August 2006 I announced that HM Treasury would launch an investigation into the sale of travel insurance sold along with a holiday or other related travel. This was followed by a call for evidence published last November. I am grateful to all those who responded to the call for evidence.

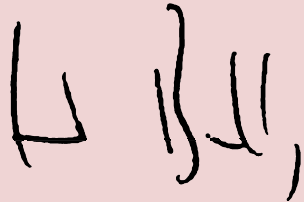
20 million people buy travel insurance every year and many will buy this from travel firms. It is an important purchase, offering financial protection and peace of mind when people travel abroad. However, travel insurance is a complex product and the evidence suggests there is often a gap between consumers' expectations of the way the policy will respond in different eventualities and the cover it actually provides. Travel insurance is not comprehensive and, like any insurance policy, there will be important exclusions that people will need to be aware of in order to understand whether or not they will be covered. So there is an emphasis on the seller, whatever the distribution channel, to navigate the consumer through the sales process.

Currently there are two different regulatory regimes covering the selling of travel insurance. Sales of stand-alone travel insurance are regulated by the Financial Services Authority (FSA), who set standards for firms selling insurance products. Consumers who purchase a stand-alone policy also have access to the Financial Ombudsman Service and the Financial Services Compensation Scheme should things go wrong. However, no such statutory protection accompanies travel insurance sold alongside a holiday. And whilst I recognise the efforts of the travel industry to improve sales standards over the past few years, the call for evidence has unearthed concerns regarding consumer detriment arising from these sales. There is a weight of evidence - including consumer survey evidence provided by the British Insurance Brokers' Association and mystery shopping evidence provided by *Which?* - that FSA regulated firms do a better job in terms of product disclosure and navigating the consumer through the sales process. Evidence, including from individuals' own experiences, also suggests that many consumers focus more on price than the quality of the insurance cover, especially when they are purchasing travel insurance as a secondary product bundled with a holiday.

In view of this potential for consumer detriment, alongside the relatively more complex nature of travel insurance products compared to other general insurances, I am proposing to extend the FSA's remit to regulate the selling of travel insurance sold alongside a holiday.

Whenever the Government decides to extend regulation there is a balance to be struck between the degree of consumer protection and additional costs associated with regulation. The legislative framework provided by the Financial Services and Markets Act 2000 gives the FSA the freedom to regulate in a principles-based and proportionate way, taking into account the specifics of the market. I am confident that the FSA will be able to ensure appropriate protection for consumers whilst minimising the burden on those travel firms that do become authorised. I encourage travel firms that do not wish to seek FSA authorisation to consider becoming an appointed representative, which will help reduce their costs, and regulated firms should also engage with the travel sector on this process. There are additional options available to travel firms that may allow them to provide information on insurance for remuneration and we are seeking views on whether these freedoms offer travel firms a viable alternative to continue offering insurance services to their customers.

In seeking to strike the right balance I have concluded that consumers buying travel insurance alongside a holiday do need the extra protection that FSA regulation will bring. But I have asked the FSA to proceed in a proportionate and risk-based way and I am confident that this approach will balance the interests of both consumers and travel firms. Subject to this consultation, my intention is for the new regime to be implemented by the FSA in January 2009.

A handwritten signature in black ink, appearing to read 'Ed Balls,' with a comma at the end.

ED BALLS MP

ECONOMIC SECRETARY TO THE TREASURY

INTRODUCTION

1.1 This document summarises the responses made to the call for evidence stage of HM Treasury’s review of the selling of travel insurance sold alongside a holiday or other related travel. The document also consults on the Government’s intended approach and on the detail of the draft legislation, in particular whether it achieves the stated policy objectives. A partial Regulatory Impact Assessment (RIA) assessing the costs and benefits of the available options is also provided.

1.2 The document is also intended as the Government’s response to the Treasury Select Committee’s report “*Are you covered? Travel insurance and its regulation*”, published on 25 February 2007.

1.3 The call for evidence¹, seeking views from all stakeholders, was launched on 23 November 2006 and closed on 22 February 2007. 77 responses were received. HM Treasury is grateful to all those who have contributed to the call for evidence.

QUESTIONS ASKED BY THE CALL FOR EVIDENCE

1.4 The call for evidence sought views on whether the selling of travel insurance along with a holiday should be subject to regulation by the Financial Services Authority (FSA), as is the case for the selling of stand-alone travel insurance products. Specifically, the call for evidence welcomed views on:

- factors to be taken into account in determining the nature and extent of regulation, including supporting evidence;
- the scale and nature of consumer detriment in relation to sales of travel insurance sold along with a holiday or related travel, with a particular emphasis on providing qualitative and quantitative evidence. The call for evidence asked specifically whether there are systematic problems with the selling of travel insurance;
- the most suitable regulatory framework for the selling of these products, i.e. whether they should be subject to:
 - Option 1: No statutory regulation – i.e. maintaining the status quo;
 - Option 2: Strengthened industry self-regulation;
 - Option 3: FSA conduct of business regulation.

1.5 The call for evidence also welcomed views on any other relevant considerations and whether there are other options that should be considered.

1.6 Chapter 2 summarises the responses received on these considerations and on other issues raised during the call for evidence period. Chapter 3 summarises the conclusions that the Government has reached following the call for evidence and sets out the proposed next steps. Chapter 4 gives details on how to respond to the next stage of consultation on the Government’s intended approach. Chapter 5 includes the partial RIA for the three options outlined above. Annex A lists respondents to the call for evidence. Draft legislation is also provided at Annex B.

¹ Travel insurance review – call for evidence, November 2006

1.7 HM Treasury is seeking stakeholders' views on its intended approach and on the costs and benefits presented in the partial RIA, in order to inform the final RIA. This next stage of consultation will run for 12 weeks and will close on 18 September 2007. Following the consultation, the Government will publish a further summary of consultation responses and a final RIA alongside the final legislation.

2

SUMMARY OF RESPONSES

CALL FOR EVIDENCE

2.1 The call for evidence sought views on whether the selling of travel insurance sold along with a holiday or related travel should be subject to regulation. It specifically asked for views and evidence relating to any consumer detriment arising from such sales and for views on three proposed options – i) no statutory regulation; ii) strengthened industry self-regulation; and iii) FSA regulation. The call for evidence also requested views on whether any other factors should be taken into consideration in assessing the options and whether there are any other options that could be considered.

2.2 77 responses were received to the call for evidence. These were from:

- individuals (33 responses)
- consumer associations (6)
- victims' groups (2)
- firms (19)
- regulatory bodies (5)
- another Government Department (1)
- representative bodies from the travel sector (4)
- a representative body from the insurance sector (1)
- representative bodies from the insurance intermediary sector (3)
- a representative body from the car hire sector (1)
- a representative body from the event management sector (1)
- Treasury Select Committee report into travel insurance and its regulation (1)

A list of those responding to the consultation who did not ask for their response to be kept confidential is attached at Annex A.

2.3 The responses to the consultation were varied, with many respondents using the opportunity to highlight problems they have experienced in buying travel insurance without specifically stating a preferred approach. In some cases it was not clear whether the respondent was referring to specific issues regarding non-regulated selling or to problems with travel insurance as a product more widely. And in certain other cases it was clear that the respondent was talking about problems with travel insurance as a product, or travel insurers' approach to claims handling, rather than specifically the sales process. HM Treasury has been careful to take into account only relevant evidence in forming its view on whether or not the exemption from regulation for the selling of travel insurance products sold alongside a holiday should be maintained.

2.4 Respondents expressed a variety of views over whether the selling of travel insurance sold along with a holiday should be subject to regulation and, if so, what form this regulation should take. Each of the three proposed options above were supported to some degree or another by the various respondents. Of those responses directly

expressing a preference for one of the options proposed, 9 supported Option 1 (maintaining the status quo), 4 supported Option 2 (strengthened industry self-regulation) and 13 supported Option 3 (regulation by the FSA). One additional option proposed by 2 responses was regulation of the selling of travel insurance alongside a holiday by local authority Trading Standards officers. In addition, 11 responses were in favour of some form of regulation, but did not provide a view on what form this regulation take. 12 responses were received that, whilst not supporting regulation explicitly, provided arguments that may reasonably be taken as supporting regulation (for instance, personal experiences of mis-selling of travel insurance by travel agents). In addition, 7 responses were received that, whilst not arguing against regulation explicitly, provided arguments that may reasonably be taken as favouring the status quo.

ARGUMENTS FOR AND AGAINST REGULATION

Consumer detriment

2.5 A number of respondents thought that there was significant potential for consumer detriment to arise from the selling of travel insurance alongside a holiday. Some respondents highlighted that, given that travel insurance can be a complex product, poor disclosure information at the point-of-sale (for example, failure by the seller to inform the customer of the need to disclose pre-existing medical conditions or of terrorism exclusions) is a key concern – see box below. This was supported by individual case studies alleging mis-selling, mystery shopping evidence and consumer survey evidence. Some responses also argued that mis-selling was more likely given that the travel insurance was a secondary product bundled with a primary product (i.e. the holiday), and the consumer was less likely to pay attention to the details of the insurance cover or to shop around.

2.6 The call for evidence noted that, in recent years, there have been growing concerns from consumer groups and sections of the industry that the market is not working as well as it could. A recent *Which?* report¹, provided in support of their call for evidence response, used mystery shopping techniques and real-life case studies to argue that travel insurance bought from travel agents is poor value and often mis-sold. The *Which?* report found that only 35% of the 26 travel agents surveyed asked medical questions (compared to 81% of banks and insurers), 19% explained what the policy covered (compared to 81% of banks and insurers) and 0% explained what the policy did not cover (compared to 56% of banks and insurers). *Which?* also provided details of mystery shopping conducted in 1996 and 2003, and a consumer survey conducted in 1999, that reached similar conclusions. Whilst these reports on their own do not form a comprehensive evidence base, they do indicate genuine concerns around the selling of travel insurance sold alongside a holiday.

2.7 As part of their response to the call for evidence, the British Insurance Brokers Association (BIBA) commissioned some consumer research by the independent polling company Populus. Populus polled 500 random adults who had bought travel insurance in the last 12 months. The research first sought to establish where people buy their travel insurance. The results showed the following breakdown:

- travel agents or tour operators 27%;
- direct from an insurance company (phone or internet) 26%;
- from a bank 23%;

¹ “Buy the right holiday cover” in July 2006 edition of *Which?* magazine.

- via an insurance broker or other intermediary 7%;
- from a supermarket 4%;
- other 13%.

2.8 This research² found that:

- 97% of the remaining 435 respondents believe that companies selling travel insurance should be required by law to explain to customers the details of the policy they are buying;
- only 42% of people who bought policies from travel agents and tour operators were advised about hazardous sports compared to 67% of those buying from insurance brokers and an average across the FSA regulated insurance market of 62%;
- when it comes to making a claim, 44% of travel agents explained what to do, compared to 69% of insurance brokers and 62% across the FSA regulated market;
- 45% of travel agents and tour operators failed to advise of the policy excess compared to 26% of the regulated firms;
- 46% of travel agents/ tour operators gave advice about policy limits in comparison with an average of 68% of regulated firms;
- 56% of travel agents and tour operators failed to advise on how to make a complaint, compared with 36% of regulated firms;
- 53% of those purchasing travel insurance from a travel agent/ tour operator relied on them to explain what is and is not covered. Only 47% of those buying from travel agents read the small print;
- 72% of travel agent/ tour operator customers had not been advised if terrorism cover was covered or excluded in comparison with 48% of regulated firms. However a larger proportion of customers of regulated firms could not remember whether they had been advised of terrorism exclusions (28% compared to 12% for travel agent/tour operator customers) – only 24% of customers of regulated firms were sure that they had been advised of terrorism exclusions. The Government believes that the issue of disclosure of terrorism exclusions applies across all distribution channels.

2.9 ABTA also commissioned a consumer survey as part of their response to the call for evidence. 101 responses were received to a survey of consumers by a leading firm of travel insurance brokers.

2.10 This survey found that:

- 89.5% of consumers buying travel insurance from a travel agent and 82.9% of consumers buying from a tour operator believed that the cover provided by the policy was sufficient to their needs, compared with 100% buying from an insurance broker;

² The 65 respondents in the “other” category were excluded from the summary statistics provided in BIBA’s response.

- 81.6% of those buying from a travel agent and 70.7% of those buying from a tour operator responded that they had been asked about pre-existing medical conditions before they purchased cover, in comparison with 92.3% buying from an insurance broker;
- 92.4% of those buying from the travel industry found the process of purchasing insurance either “easy” or “very easy”, compared with 92.3% buying from an insurance broker.

2.11 The survey also found that overall, across the different sales channels, about 64% of consumers had the main policy benefits explained to them. ABTA’s response also refers to anecdotal evidence that the majority of consumers were unwilling to go through all the policy wordings in detail with the supplier.

2.12 One distinction made by some respondents was the difference between sales of travel insurance by travel agents (the seller of the holiday) and by tour operators (the provider of the holiday). The key feature of this distinction was that tour operators maintain some degree of liability over their passengers whilst they are travelling abroad – they are therefore incentivised to ensure that adequate insurance cover is in place before the passenger travels. It was argued that this incentive applies less to travel agents. Additionally, it was argued that tour operators were more likely to arrange cover that was tailored to the specific needs of their customer profile.

2.13 One argument made was that it is odd, as a matter of principle, for regulation to be applied to the selling of travel insurance by insurance experts, i.e. direct insurers and insurance intermediaries, but not to travel firms, for whom insurance selling is not their principal professional activity. On the other hand, arguments were made by other respondents that travel firms’ expertise in providing holidays and other travel left them better placed to advise on the suitability of a certain insurance policy for the individual’s needs.

POTENTIAL FOR CONSUMER DETRIMENT TO ARISE THROUGH MIS-SELLING

A central theme among respondents calling for the regulation of travel insurance sold along with a holiday was that consumers are given poor information when they buy the holiday - leading them to believe that they are covered when they might not be.

A key concern was that sellers were not properly explaining what is and, more importantly, what is not covered by the insurance policy in question. This problem was highlighted by the *Which?* mystery shopping exercise and was reinforced by mystery shopping performed by the BBC's Watchdog programme. While the *Which?* report illustrated that all sellers of insurance could do more to improve the information given to the customer so they can make an informed choice, travel firms were less likely to ask the key questions.

With travel insurance, the key policy exclusions generally relate to pre-existing medical conditions. Some case studies follow where individuals thought they were covered, but it turned out that their claims were rejected on the grounds of a pre-existing medical condition.

Example one

The respondent booked a holiday for her partner and herself with a travel agent and purchased the insurance cover offered by the travel agent for an additional charge. The respondent states that she was told that the insurance would "cover her for everything". The respondent also states that she was asked whether she or her partner had any medical illnesses, but that she was not asked about the medical history of any relatives.

Unfortunately, the respondent was required to cut short her holiday following the death of her mother. The respondent registered a claim with the insurer, who subsequently rejected the claim on the basis of a pre-existing medical condition from which the respondent's mother had suffered. The respondent states that she would have informed the insurer of any family member's illnesses had she been informed that she needed to do so when she took out the insurance.

Example two

The respondent and her husband booked a holiday with a travel agent and were offered travel insurance, which they accepted. The respondent states that she was not informed by the travel agent of any exclusions to the policy - there was, in fact, no discussion about the policy at all.

Prior to travelling the respondent became too ill to travel and filed a cancellation claim with the insurer. This claim was rejected by the insurer on the grounds that a pre-existing medical condition had not been disclosed by the respondent. (The respondent also disputes that this pre-existing medical condition was related to the illness that forced her to cancel the holiday).

Example three

The respondent booked a holiday for his wife and himself and purchased travel insurance from the travel agent. The respondent states that at the time of booking, the only question asked was whether he or his wife had any pre-existing medical conditions – at no time were the policy cover or its restrictions explained.

Unfortunately the respondent's mother was later diagnosed with cancer. The respondent and his wife travelled abroad but, following the death of the respondent's mother, decided to curtail their travel plans and to return home. A claim was made with the insurer, but this was rejected on the grounds that the respondent had not informed them of his mother's condition prior to departure. The respondent states that he has recently visited the same travel agent to book another holiday. On this occasion he specifically asked whether he needed to inform them of relatives' pre-existing medical conditions, but was informed that they only required details about those travelling.

2.14 A recent report by the Treasury Select Committee³ focussed on the potential for consumers to be sold unsuitable travel insurance policies. The report gave examples of where detriment could arise and concluded that there is significant evidence of consumer detriment in the travel insurance market. The Committee also observed that there is evidence to suggest that problems in the sales process are likely to be accentuated when sales take place away from the professional regulated insurance environment through an intermediary such as a travel agent.

2.15 As noted in the call for evidence, the Financial Ombudsman Service (FOS) has concerns over the selling of travel insurance. The FOS stated in its most recent Annual Review that:

“The policy terms for travel insurance remain complicated, and the sales process is frequently limited – given the low value of transactions involved. As a result, whilst there is considerable competition on the pricing of travel insurance, there is also widespread misunderstanding on the part of consumers about the scope of the cover they have and the eligibility criteria that apply”⁴.

2.16 The FSA recently published the interim report of its review of its general insurance regulation⁵. Although this did not cover travel insurance sold along with a holiday it did reach the following conclusions with regard to the selling of stand-alone travel insurance:

- the travel insurance market was relatively small, but with a high penetration among travellers;
- travel insurance was a more complex product than motor or household insurance. When purchasing travel insurance, consumers might focus too much on price rather than the cover offered by the policy, although this is, in part, mitigated by consumers increasingly shopping around;
- there was cause for concern over consumers not focussing on the details of cover. The main area of detriment that might be remedied by FSA rules is mis-selling since cover does not always match consumers’ expectations;
- however, overall, the market for sales of stand-alone travel insurance works fairly well in the interests of consumers.

2.17 Some respondents argued on the other hand that consumer detriment arising from the sale of travel insurance alongside a holiday was low or negligible.

2.18 A primary argument offered by these respondents was the low number of recorded complaints received by individual travel firms, or the travel sector more widely, in relation to selling of travel insurance. The Association of British Travel Agent’s (ABTA) response to the call for evidence stressed that they had received only 95 complaints relating to insurance in 2006 out of a total of 16,676 complaints related to its Member firms. According to ABTA, the majority of these complaints related to the claims handling of insurance firms rather than the conduct of travel firms themselves. A survey by the Association of Independent Tour Operators (AiTO) of 50 of its members firms revealed that none of the 36 firms responding to a questionnaire on the level of

³ House of Commons Treasury Select Committee Fourth Report of session 2006-07 “Are you covered? Travel insurance and its regulation”, February 2007.

⁴ Financial Ombudsman Service Annual review 2005/6.

⁵ The Interim Report of the FSA’s review of its *Insurance: Conduct of Business* (ICOB) regulation was published on 21 March 2007.

consumer complaints had any history of a complaint regarding insurance mis-selling. The Co-operative Travel Trading Group's response pointed to the fact that, of the 500,000 policies sold annually by the four leading Co-operative travel businesses, the ratio of complaints ranges from 0.02% to 0.05%. Other responses also from individual travel firms also argued that the firm had never received a complaint relating to insurance mis-selling, or that such complaints were rare.

2.19 However, these statistics need to be treated with some care as they do not necessarily give the true story of any potential mis-selling, since problems will only crystallise if individuals have to make a claim and they are refused a payout. ABTA estimate that around 3% of travel insurance policies are claimed on. Additionally it could be that, in some instances where a consumer has been mis-sold a policy, this dispute is then taken up with the insurer as a claims dispute rather than with the travel firm as a mis-selling dispute. The FOS estimate that in 2005/06, around 25% of the 1,787 cases it received on travel insurance related to disputes against insurers where the policy was sold by an unregulated intermediary.

2.20 It was also argued by some respondents that the potential for consumer detriment arising from a face-to-face sales by a travel firm was lower than regulated off-the-shelf or internet sales of stand-alone travel insurance. The argument used was that consumers buying stand-alone products of this type did not necessarily understand the detail of the policy - for example, a consumer carrying out an internet purchase could simply tick a box saying that they have read the key terms and conditions and this did not necessarily mean that they had either read or understood the policy.

2.21 It was also pointed out that, if regulation resulted in fewer travel firms selling insurance, this would lead to increased consumer detriment through a higher number of individuals travelling uninsured. This argument is discussed further below.

Consumer protection

2.22 Some respondents pointed to the consumer protection currently provided by travel industry Codes of Conduct as an argument against introducing statutory regulation. ABTA's Code of Conduct imposes on ABTA Member firms certain requirements relating to, for example, insurance product disclosure, and Member firms' complaints handling procedures (including access to an independent dispute resolution mechanism). AiTO also offer an independent dispute settlement service. The ABTA scheme, for instance, requires consumers to pay a fee (which is refunded if the decision goes in their favour) and, unlike the FOS, the decision is legally binding on the consumer. The scheme is also limited in the level of any payment that it can require the Member firm to make to the individual.

2.23 The ABTA Code also includes a requirement for Member firms to ensure that all sales staff hold an appropriate qualification approved by the ABTA Board of Directors. ABTA have introduced their own training and examination scheme, which is accredited by the City and Guilds Institute. The ABTA Code imposes a further requirement for at least one member of staff at each of its Members offices or premises that sell insurance to hold an advanced "Level 2" qualification. 33,000 of ABTA Members' staff had taken the ABTA insurance training exams by the end of June 2006⁶. ABTA carry out mystery-shopping compliance tests to determine whether Member firms that have not registered staff as holding the appropriate qualifications do not in fact sell insurance. Some responses argued that ABTA's training regime was weakened by the lack of any requirement to undertake ongoing training or testing. There is also no proactive

⁶ Source: ABTA annual report for the year ended 30 June 2006

monitoring or enforcement to ensure that the standards required in ABTA's insurance training are upheld by Member firms.

2.24 A number of responses also picked up on the point raised in the call for evidence document that individuals purchasing travel insurance alongside a holiday did have a right of recourse to the FOS for disputes over the handling of claims by the (FSA regulated) insurer. However, it was also argued that this was only true where the insurer was based in the UK, and that this left a gap in consumer protection where cover from a non-UK insurer was arranged by a non-regulated seller.

2.25 The FSA also impose some requirements on insurers to provide certain information directly to the client, where the intermediary is not also regulated by the FSA. This required information includes details on the claims process and cancellation rights, but not a policy summary. Again, these requirements would not apply if the policy was underwritten by a non-UK insurer. Although the FSA, as part of its current review of the Insurance: Conduct of Business (ICOB) rules, are proposing to remove the explicit requirement for sellers of stand-alone travel insurance to provide a policy summary, this will instead be replaced by a high level principle that firms must provide information to consumers in a way that is "clear, fair and not misleading" when selling the product.

2.26 Doubts were raised over the ability of industry self-regulation to provide adequate consumer protection. These doubts focussed on differences between requirements on product disclosure in FSA regulated sales of travel insurance and the requirements placed on non-regulated sales by, for example, the ABTA Code. The independent dispute resolution mechanisms were also seen by some respondents as limited compared to the FOS scheme. Similarly, one response highlighted that consumers purchasing travel insurance alongside a holiday would have no recourse to the Financial Services Compensation Scheme (FSCS) following an insolvency of a travel firm. Questions were also asked about the apparent lack of monitoring of firms' compliance with industry Codes. The Treasury Select Committee's report also states concerns about the prospects of progress through self-regulation and expresses the view that there is not a convincing case for the maintenance of self-regulation in this market.

2.27 Some responses also pointed out that not all travel firms are or need to be members of a trade association. For instance, ABTA Members are responsible for around 80% of all package holidays sold in the UK⁷. Any trade association cannot of course be held responsible for the conduct of firms outside of its membership.

Level playing field

2.28 A number of responses suggested that the current situation led to an 'uneven playing field' in terms of consumer protection that was difficult to justify, given the potential for consumer detriment. This unevenness was seen by some respondents as a potential cause of high levels of misunderstanding for consumers, who would not be aware whether they were involved in a regulated or non-regulated sales process and, subsequently, of which protections were available to them. Some responses also felt that the current situation contributed to an uneven playing field in terms of the cost base of firms selling travel insurance. The results of BIBA's consumer survey indicate that 54% of consumers believe that all sellers of travel insurance are currently covered by the same regulations. It should be noted, however, that within FSA regulation there is scope for travel insurance products sold through different distribution channels to be regulated in a differential manner, where this is proportional and risk-based.

⁷ Source: ABTA *Travel Statistics and Trends 2005*.

Costs of regulation 2.29 A number of responses argued that statutory regulation of insurance sales would be burdensome for travel firms. This was generally felt to be a particular issue for smaller travel firms.

2.30 Two possible consequences of this burden were highlighted: firstly, that the costs of regulation would be passed on, at least to some extent, to the consumer through higher insurance premiums; and secondly, that, given the low margins involved in selling insurance along with a holiday, some travel firms would stop selling insurance products altogether. ABTA point out in their response that their Members are sensitive to increased costs imposed by additional regulation – for example, following the introduction of its training regime, around 280 Member firms elected to stop selling insurance rather than to incur the costs of around £25 per member of staff and the increased administration required. Responses to AiTO’s survey of its members indicate that in over 75% of cases, the profit generated from the selling of insurance accounted for less than 3% of total profits.

2.31 This issue was seen by many respondents as a particular problem as it would mean lower availability of travel insurance products for consumers and, potentially, more individuals travelling uninsured. Some responses argued on the other hand that travel firms were unlikely to stop selling insurance if statutory regulation was put in place. Even if they did, the UK’s mature stand-alone travel insurance market meant there would be only a negligible impact on the availability of travel insurance or the level of those travelling with appropriate cover.

2.32 Some responses also argued that travel firms offered important services to consumers in offering advice on the suitability of travel insurance products (given their knowledge of their customers’ typical insurance requirements) and also in advising their customers in the claims process. These responses argued that it would be detrimental to the consumer if statutory regulation resulted in these services being withdrawn by some travel firms.

2.33 The Government is aware that any increase in the regulation of the selling of travel insurance by travel firms might lead to some reduction in the number of firms selling travel insurance. Whilst fewer people travelling insured is one possible implication of fewer travel firms selling insurance, the Government believes that one potential advantageous implication is that more consumers will shop around for the most suitable policy, rather than relying on an inertia sale that might not provide the most appropriate cover. A more detailed analysis of this issue is provided in the partial Regulatory Impact Assessment at Chapter 5.

2.34 The argument was also made that, since the Package Travel Regulations⁸ require travel firms to advise the consumer about the availability of travel insurance, the introduction of FSA regulation would impose an unfair burden on travel firms since they have limited scope to simply withdraw from selling the insurance. However, the Government is unconvinced by these arguments – the Package Travel Regulations only require the travel firm to provide: “*information about an insurance policy which the consumer may, if he wishes, take out in respect of the risk of those costs being incurred*”⁹. One option is for the travel firm to act as an (unregulated) introducer by directing the customer to a regulated intermediary or insurer, who would sell the insurance to the client.

⁸ The Package Travel, Package Holidays and Package Tours Regulations 1992 (SI 1992/3288)

⁹ Regulation 8(2)(d) of the Package Travel Regulations

Other related travel **2.35** The call for evidence highlighted that the exemption from regulation for firms selling insurance products alongside a related travel service may apply in circumstances other than travel firms selling holidays. One response pointed out that vehicle leasing and car hire companies typically benefit from the exemption and another response noted that corporate event management companies typically benefit from the exemption.

2.36 These two responses argued that there was low potential for consumer detriment arising from insurance mis-selling in the two respective sectors, with the low level of complaints received by the sectors' respective trade associations provided as evidence of this. The response concerning event management companies pointed out that most sales were to commercial customers. The response relating to car hire firms underlined the British Vehicle Rental and Leasing Association's (BVRLA) Code of Conduct for Member firms, which includes an "Insurance Mediation Regulations" best practice guide setting out the required insurance advising and selling standards and a complaints handling procedure, including access for the consumer to the BVRLA's dispute resolution panel.

2.37 No responses were received that highlighted specific concerns relating to insurance mis-selling by either car hire or event management firms.

OTHER ISSUES RAISED DURING THE CONSULTATION

2.38 As outlined above, the call for evidence sought views on the selling of travel insurance sold alongside a holiday or other related travel. However, a number of issues were raised by responses relating to travel insurance more widely. These are addressed below.

Value for money **2.39** A number of responses argued that insurance sold by travel firms was poor value for money when compared against policies offered by FSA regulated sellers. As noted above, this review is concerned with the selling of travel insurance alongside a holiday or related travel and does not extend to consideration of "value for money" or competition issues. The Office of Fair Trading (OFT) would be responsible for assessing or addressing any competition issues in the market. It is however possible that if a change in the regulatory regime increased the transparency of the selling process, this would lead to value for money gains for consumers.

Terrorism exclusions **2.40** As highlighted in the call for evidence, some travel insurance policies include exclusions for claims arising from a terrorist incident. The Government believes that, where insurance policies do exclude cover for acts of terrorism, these exclusions should be adequately signposted so that consumers can make an informed decision on the type of cover that they wish to purchase. This is in line with the recommendations of the Treasury Select Committee report. A few responses argued that this approach did not go far enough and that Government intervention was required to inhibit the use of terrorism exclusions in travel insurance policies. One response also suggested that the Pool Re scheme could be extended to provide terrorism reinsurance for travel insurers¹⁰.

2.41 The Government urges insurers, insurance intermediaries and their trade associations to seriously consider what more they can do to highlight terrorism exclusions in travel insurance policies so consumers can make an informed choice about the cover they are purchasing. However, the Government does not feel at this

¹⁰ Pool Re is the Government backed mutual reinsurer of last resort providing commercial property reinsurance against acts of terrorism.

stage that it is appropriate to require insurers to cover claims arising from terrorist incidents. Travel insurance policies that do offer cover for at least medical expenses and repatriation claims arising from acts of terrorism are widely available in the market¹¹ and imposing a mandatory requirement on insurers could increase premiums and lead to less choice for individuals. A Pool Re type scheme is unnecessary - there is no general market failure, since terrorism cover is available.

2.42 The Government will continue to work with the insurance industry to ensure appropriate transparency in the selling of travel insurance products in order that consumers are fully aware of the level of terrorism cover that their policy provides. HM Treasury is taking this forward as part of a wider work-stream with the FSA and the Association of British Insurers to develop a better understanding of what the issues are around consumers' understanding of travel insurance policies, including whether people are aware of what they are and are not covered for. In particular, this work will look at whether industry guidance could help improve the quality of disclosure to consumers and better signpost customers through what is a relatively complex insurance policy.

2.43 In addressing the issue of consumer understanding of travel insurance products, the Government will also look to the potential role of generic financial advice. In particular, the Government will look at the applicability to this specific issue of future findings resulting from the Thoresen Review¹². This Review is currently examining the feasibility of delivering a national approach to generic financial advice. The aim is to ensure that there is greater access to high quality affordable financial advice for those most vulnerable to the consequences of poor financial decision-making.

2.44 One response to the call for evidence went further by arguing that the Government should introduce a compulsory requirement for those travelling to take out 'all risk' (i.e. comprehensive) travel insurance before they travel. However, the Government does not consider this approach to be practicable or appropriate in terms of the burdens it would place on consumers and the insurance industry. The Government's approach is that, whilst it encourages those travelling abroad to take out appropriate travel insurance cover, it is ultimately for individuals to make a decision based on an assessment of their own circumstances.

Industry claims handling **2.45** A few responses gave details of alleged poor claims handling by the insurance industry (for example, in terms of claims rejected by the insurer on spurious grounds). Those carrying out insurance business in the UK are regulated by the FSA and are subject to the FSA's Insurance: Conduct of Business Rules. In addition, as highlighted earlier, policyholders have a right of redress to the FOS where they are unable to resolve a dispute with the insurer over a claims decision.

Regulation in the travel industry **2.46** Some responses noted the level of regulation already imposed on travel firms through, for example, the Package Travel Regulations and Air Travel Organisers' Licensing (ATOL) bonding arrangements, which provide some financial protection to consumers following the insolvency of a travel firm that is registered with the scheme. In particular some respondents pointed out that the Package Travel Regulations require tour operators and travel agents to advise the consumer about the availability of insurance cover against the cost of cancellation and the cost of assistance in the event of accident or illness.

¹¹ The Association of British Insurers (ABI) estimate that around 60% of travel insurance policies in the market provide cover for at least medical expense and repatriation claims arising from acts of terrorism.

¹² See http://www.hm-treasury.gov.uk/independent_reviews/thoresen_review/thoresenreview_index.cfm.

2.47 Two responses also noted that there was a general lack of awareness that cover against losses arising from the insolvency of an airline, or the insolvency of the provider of an important component of the holiday, such as hotel accommodation, is not typically offered by personal travel insurance policies. This causes a potential gap between an individual's travel insurance cover and the ATOL bonding arrangement, which only covers packaged travel arrangements. The Department for Transport (DfT) and the Civil Aviation Authority (CAA) are working with the Department of Trade and Industry, the airline industry and other relevant bodies to increase consumer awareness in this area.

2.48 The DfT and the CAA are currently consulting on proposed options to reform ATOL bonding¹³. This consultation closes on 29 June 2007.

¹³ Further details are available on the CAA and DfT websites (www.caa.org.uk and www.dft.gov.uk)

3

DECISION AND NEXT STEPS

THE REGULATION OF TRAVEL INSURANCE SOLD ALONG WITH A HOLIDAY

3.1 The wide variety of responses to the call for evidence show that there are arguments both for and against the regulation of the selling of travel insurance sold alongside a holiday. Evidence has also been provided to support both sides of the argument.

3.2 As summarised in chapter 2, the Government believes that the evidence suggests that there is a gap in consumers' understanding of travel insurance as a product and the cover that it provides. This is because:

- although the travel insurance market is highly competitive, policies tend to be more complicated than a simple household or motor policy;
- as a secondary purchase, consumers are less likely to be focussed on the details of their insurance policy than through a direct sale;
- the majority of consumers only really seem to consider price, not the details of the policy and the quality of cover that it provides, in deciding which policy to purchase.

3.3 In addition to this gap in consumers' understanding, and whilst all firms selling travel insurance could do more to explain to customers what the policy does and does not cover, the evidence also suggests that FSA regulated firms do a better job in terms of product disclosure and navigating the consumer through the sales procedure.

3.4 In addition to specific rules (soon to be high-level principles) in areas such as product disclosure and complaints handling, FSA regulated firms also have a high-level duty to treat their customers fairly. Furthermore, customers of FSA firms have access to statutory redress and compensation mechanisms if things go wrong. Given the relatively more complex nature of travel insurance products compared to other general insurances and the concerns around the lack of consumer awareness expressed above, the Government believes that it is in the public interest for these safety nets to be extended to all sales of travel insurance, irrespective of the distribution channel through which the product is purchased.

3.5 Therefore, the Government believes that, on balance, the scope of FSA regulation should be extended to include the selling of travel insurance sold along with a holiday. This will ensure that all those purchasing travel insurance, no matter through what distribution channel, will be protected by a core baseline of statutory protection. It will also ensure that consumers have access to the Financial Ombudsman Scheme and Financial Services Compensation Scheme should things go wrong. In the case of travel insurance, the Government does not see how the objective of consumer protection is best served by having the availability of statutory consumer protection dependent on the distribution channel through which the insurance has been bought.

The Financial Ombudsman Service

The Financial Ombudsman Service (FOS) is a free service to customers to help settle individual disputes with businesses providing financial services. It was set up under the Financial Services and Markets Act 2000 (FSMA) and can consider complaints about a wide range of financial matters – from insurance and mortgages to investments and bank accounts. Each year the FOS deals with half a million enquiries and settles 100,000 disputes.

The FOS is independent and impartial. It is not a regulator or a trade body or a consumer champion. Its role is to settle disputes, without taking sides.

Consumers do not have to accept a decision made by an Ombudsman and remain free to go to court instead. But if consumers do accept an Ombudsman's decision, it is binding both on them and on the firm.

The Financial Services Compensation Scheme

The Financial Services Compensation Scheme (FSCS) provides a consumer safety net in relation to financial services – it is the UK's statutory fund of last resort for consumers of authorised financial services firms, including persons affected by the default of such firms. The FSCS can pay compensation if a firm is unable, or likely to be unable, to pay valid claims against it. The FSCS is an independent body, set up under FSMA.

The FSCS covers business conducted by firms authorised by the FSA, and protects:

- deposits;
- insurance policies;
- insurance mediation (for business on or after 14 January 2005);
- investment business; and
- mortgage advice and arranging (for business on or after 31 October 2004).

The FSCS is funded by levies on authorised firms.

3.6 The Government will now consult on its intended approach and on the detail of the draft legislation, in particular whether it achieves the stated policy objectives. A partial Regulatory Impact Assessment (RIA) assessing the costs and benefits of the available options is also provided at Chapter 5 and views are also welcomed on the analysis within the partial RIA.

3.7 The Government is sensitive to the argument that regulating travel insurance could increase consumer detriment through a reduction in people taking out such insurance. A similar argument was advanced on the introduction of insurance regulation in 2005, although there has not been a substantial shrinkage in the market from the introduction of FSA regulation.

3.8 It should be noted that firms would not necessarily have to be authorised by the FSA in order to offer insurance services and that there is an alternative route open to travel agents and tour operators – the appointed representatives route. An appointed representative is allowed to carry on certain regulated activities by an authorised firm (his principal) under a contract by which the principal accepts responsibility for the regulated activities carried on by its appointed representative(s). Consumer protection is therefore maintained since the principal holds responsibility for anything that is

done, or omitted to be done, by the appointed representative. The Government strongly encourages firms who wish to carry on selling insurance, but do not want to become FSA authorised, to consider going down this route. The Government also strongly encourages regulated firms to engage with firms in the travel sector to discuss this option.

The FSA's appointed representatives regime

Under section 19 of FSMA, no person may carry on a regulated activity in the UK unless he is an authorised or exempt person.

However, a person may be exempt if he is an appointed representative. An appointed representative is allowed to carry on certain regulated activities by an authorised firm (his principal) under a contract by which the principal accepts responsibility for the regulated activities carried on by its appointed representative(s).

It is the responsibility of an authorised firm to ensure that its appointed representatives are fit and proper to deal with clients on behalf of the authorised firm. It is also the authorised firm's responsibility to ensure that any clients dealing with its appointed representative(s) have the same level of protection as if they had dealt direct with the authorised firm.

There are no direct costs of FSA regulation on the appointed representative, although there will be increased indirect and ongoing costs on the authorised firm.

3.9 Travel firms could also consider the potential for taking advantage of the exemption in article 72C of the Regulated Activities Order to provide information on insurance for instance, by teaming up with insurers and/or brokers to provide information on insurance to their customers. Further information on the scope of this exemption can be found in the *FSA Handbook Perimeter Guidance Manual – PERG 5*¹. The Government would welcome views on the scope of this exemption and whether it is likely to be of use to travel firms.

3.10 For those travel firms that decide to seek FSA authorisation, the FSA's move to a more risk-based and principles-based regime for the selling of general insurance announced in June 2006² will ensure a proportionate environment for ongoing regulation, with more emphasis on firms meeting high standards rather than detailed rules, where appropriate. It should be noted that Insurance Mediation Directive requirements would not necessarily be applicable to firms selling travel insurance along with a holiday since these sales are exempt from the Directive. Also, in asking the FSA to take on responsibility for regulating this sector, the Government has asked the FSA to look specifically for ways of smoothing the entry of such firms into its regime, working with the relevant trade bodies. The FSA is required by FSMA to conduct cost-benefit analysis when introducing new rules or amending its rulebook and to consult on these changes.

3.11 As noted in the call for evidence, the Government is aware that there are certain other sectors that also benefit from the current travel insurance exemption. These are the car hire and event management sectors. The Government has received no evidence of consumer detriment in relation to these two areas and can see no current benefit in extending regulation to these two sectors. It is therefore the Government's intention

¹ Available online at <http://fsahandbook.info/FSA/html/handbook/PERG/5>

² See FSA press notice at <http://www.fsa.gov.uk/pages/Library/Communication/PR/2006/057.shtml>

that FSA regulation is not extended to these two sectors. The Government expects the same high standards of selling as for other forms of insurance and will monitor the situation to ensure that the risk of consumer detriment does not arise. For event management companies, the exemption will only apply insofar as the company is dealing with a commercial counterpart. The Government would welcome views on the scope of this exemption as part of the consultation.

3.12 The Unfair Commercial Practices Directive will require that consumers in EU Member States are protected from unfair, misleading and aggressive selling practices. Implementation of the Directive in the UK is the responsibility of the Department of Trade and Industry³. The relevant enforcers, including the OFT and FSA are involved in discussions about how to ensure compliance in the sector the FSA covers.

3.13 In carrying out the consultation, the Government will have in mind the following issues:

- the potential future role of generic financial advice, including findings from the Thoresen Review;
- the implementation of the Unfair Commercial Practices Directive in the UK.

IMPLEMENTATION

3.14 The Government intends to achieve implementation of its chosen approach through the draft Statutory Instrument provided at Annex B. This Order will be subject to the affirmative resolution procedure. The Treasury will make and lay the Order before Parliament under paragraph 26(1) of Schedule 2 to the Financial Services and Markets Act 2000. This will then need to be approved by a resolution of both Houses of Parliament within 28 days, beginning with the day on which the Order was made.

3.15 The draft Statutory Instrument amends article 72B of the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (“the Regulated Activities Order”) to limit the exemption from regulation in respect of the activities specified in articles 21, 25(1) and (2), 39A and 53 of the Regulated Activities Order for travel insurance to circumstances where the contract of insurance is linked to: (a) travel to an event organised by the travel provider where the purchaser of the insurance is not an individual or a business with an annual turnover of less than £1,000,000; or (b) hire of a vehicle. The new regime will come into effect on 1 January 2009. This will allow the FSA time to consult on its draft rules, including conducting market failure analysis and cost-benefit analysis on these rules as required by FSMA, and to process applications from travel firms for authorisation.

3.16 To ease the transition into FSA regulation the draft Statutory Instrument also provides for an interim authorisation regime. This will allow travel firms to continue selling travel insurance if their application is still being processed once regulation starts. It is intended that travel firms will be able to apply for FSA authorisation from 30 June 2008 onwards, with a cut-off date for applications to be considered eligible to the interim authorisation regime of 15 November 2008. Completed applications made within this period will then be processed by the FSA within 6 months. The interim authorisation regime will remain in place until 31 December 2009, to allow any firms that have decided to appeal the FSA’s application decision to continue selling travel

³See <http://www.dti.gov.uk/consumers/buying-selling/ucp/index.html>

insurance whilst this appeals process is ongoing. The Government welcomes views on this proposed timetable as part of the next stage of consultation.

3.17 The FSA will be responsible for authorising firms to do business in line with FSMA and is required to consult on any rules or guidance that it will apply to firms. The FSA's ongoing ICOB review demonstrates its risk-based, proportionate approach to regulation and the flexibility provided within the Financial Services and Markets Act 2000.

Question 1

Do you have any comments on the Government's preferred approach?

Question 2

Do you have any comments on the partial Regulatory Impact Assessment (RIA) in Chapter 5?

Question 3

Do you have any comments on whether the draft Statutory Instrument in Annex B achieves the stated policy objective?

Question 4

Do you have any comments on the extent to which travel firms will be able to make use of the 'appointed representatives' route, or whether the "introducing exemption" offered by Article 72C of the Regulated Activities Order will be used by travel firms as an alternative business model?

Question 5

Do you agree that, where currently exempt from FSA regulation, both car hire companies and event management companies (the latter when selling to commercial customers) should continue to be exempt from regulation?

Question 6

Do you have any comments on the proposed interim authorisation regime for travel firms selling insurance?

4

RESPONDING TO THE CONSULTATION

HOW TO RESPOND

4.1 The Government welcomes the views of all stakeholders on issues raised in this document. The consultation period begins with the publication of this document and will run for 12 weeks. Please ensure that responses to this consultation reach us by 18 September 2007. We cannot guarantee to consider responses received after this date. Responses should be sent to:

Eve Engledow
Financial Stability and Risk Team
HM Treasury
1 Horse Guards Road
London SW1A 2HQ
Fax: 020 7451 7524
Email: travel.review@hm-treasury.x.gsi.gov.uk

4.2 Enquiries relating to this consultation can be made to:

Richard Wronka
Financial Stability and Risk Team
Tel: 020 7270 5389
Email: travel.review@hm-treasury.x.gsi.gov.uk

4.3 This document can be found on HM Treasury's website:
<http://www.hm-treasury.gov.uk>.

4.4 When responding, please state whether you are responding on behalf of an individual or representing the views of an organisation. If responding on behalf of a larger organisation, please make it clear who the organisation represents and, where applicable, how the views of members were assembled.

CONFIDENTIALITY

4.5 HM Treasury reserves the right to make all written responses publicly available on its website unless the author specifically requests otherwise in writing.

4.6 Information provided in response to this consultation, including personal information, may be published or disclosed in accordance with the access to information regimes (these are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act (DPA) and the Environmental Information Regulations 2004). If you want the information that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals, amongst other things, with obligations of confidence. In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality will be maintained in all circumstances.

4.7 An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on HM Treasury. HM Treasury will process your personal data in accordance with the DPA, and in the majority of circumstances, this will mean that your personal data will not be disclosed to third parties.

4.8 Subject to paragraphs 4.5, 4.6 and 4.7 if you wish part (but not all) of your response to remain confidential, please supply two versions – one for publication on the website with the confidential information deleted, and another confidential version for use by HM Treasury.

PARTIAL REGULATORY IMPACT ASSESSMENT

4.9 The partial Regulatory Impact Assessment (RIA) follows this document and should be read in conjunction with it. The Government welcomes views on the partial RIA.

FREEDOM OF INFORMATION CONTACT

4.10 Any Freedom of Information Act queries should be directed to:

Correspondence and Enquiry Unit
Freedom of Information Section
HM Treasury
1 Horse Guards Road
London
SW1A 2HQ
Telephone: 020 7270 4558
Fax: 020 7270 4681
Email: public.enquiries@hm-treasury.x.gsi.gov.uk

HOW THIS CONSULTATION IS BEING CONDUCTED

4.11 This consultation is being conducted in line with the Code of Practice on Consultation. The criteria are listed below (a full version can be found at www.cabinetoffice.gov.uk/regulation/consultation/code.htm).

4.12 The six consultation criteria are:

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

4.13 If you have concerns as to how this consultation is being conducted, please contact:

Sowdamini Kadambari

Enterprise Team

HM Treasury

1 Horse Guards Road

London

SW1A 2HQ

Telephone: 020 7270 4867

Email: sowdamini.kadambari@hm-treasury.x.gsi.gov.uk

5

PARTIAL REGULATORY IMPACT ASSESSMENT

TITLE OF PROPOSAL

5.1 The regulation of the selling of travel insurance sold alongside a holiday and other related travel.

PURPOSE AND INTENDED EFFECT

Background, objective and rationale

5.2 The EU's Insurance Mediation Directive (IMD) requires the regulation of mediation activities in relation to all insurance contracts. However, regulation is not required by the Directive where a number of conditions are met – travel insurance products sold along with a holiday or related travel are typically capable of satisfying these conditions.

5.3 In 2003 the Government consulted on implementing the IMD in the UK and, as part of that consultation, specifically sought views on whether travel insurance sold along with a holiday or related travel should be subject to regulation.

5.4 Following this consultation the Government decided that, at that time, there was not sufficient justification to regulate travel insurance sold along with a holiday or related travel. However, it recognised that there were concerns with this market. Given these concerns, the Government committed to review its decision two years after the implementation of general insurance regulation - in early 2007.

5.5 This review fulfils that earlier commitment.

5.6 This review is also intended as a response to the Treasury Select Committee's Report of February 2007, "*Are you covered? Travel insurance and its regulation*".

SUMMARY OF RESPONSES AND INTENDED APPROACH

5.7 This consultation concerns the regulation of the selling of travel insurance sold alongside a holiday and other related travel. This consultation will run for 12 weeks and will close on 18 September 2007.

5.8 This partial Regulatory Impact Assessment (RIA) sets out the options and considers the qualitative, and where possible, quantitative costs and benefits. Risks, unintended consequences and any compliance and enforcement issues have also been incorporated as costs and benefits. Competition issues and the impact on small firms have also been considered.

5.9 When formally responding to the partial RIA, HM Treasury is seeking comments on the cost-benefit analysis, likely risks and unintended consequences of this proposal, including supporting evidence. If you feel that there are alternative options please suggest these. The feedback to this partial RIA, including any additional information on the costs and benefits estimated below, will provide valuable information that will feed into the final RIA following this consultation.

5.10 This partial RIA should be read alongside the original call for evidence¹ and the summary of responses document, which includes details of the next stage of consultation.

OPTIONS

Option 1 – no statutory regulation, i.e. maintain the status quo **5.11** HM Treasury has carefully considered the option of maintaining the status quo. However, given the lack of consumer protection afforded by this option, and the evidence of mis-selling of travel insurance sold alongside a holiday, the Government does not favour this option. Further analysis of the costs and benefits of this option are provided below.

Option 2 – strengthened industry self-regulation **5.12** The option of requiring strengthened industry self-regulation, including statutory access to the Financial Ombudsman Service (FOS) where there is a dispute over the selling of the insurance, has also been carefully considered. Compulsory access to the FOS would require primary legislation. Concerns exist over the ability of industry self-regulation to provide comprehensive consumer protection. Doubts have also been voiced over the selling standards of those firms who are not covered by a trade association. Given these concerns, the Government is not in favour of this option.

Option 3 – FSA regulation **5.13** This option involves giving the FSA responsibility for regulating the selling of travel insurance sold along with a holiday or other related travel. This would mean that all firms would require authorisation to sell travel insurance no matter what the distribution method used. This is the Government's preferred approach. Responses to the call for evidence show a clear gap in consumers' understanding of what travel insurance policies typically do and do not cover and the Government believes that this option will provide consumers with the necessary protection, including statutory redress mechanisms if things go wrong. The Government recognises that if travel firms decide to become authorised then this will add to their costs, although there will be other routes for travel firms to follow to continue to be able offer insurance services, such as becoming an appointed representative of a regulated firm. A detailed analysis of the costs and benefits is provided below.

Other options **5.14** One additional option proposed by two responses to the call for evidence was regulation of the selling of travel insurance alongside a holiday by local authority Trading Standards officers. This could be supported by access for consumers to the FOS, along similar lines as Option 2. The Government has concerns over the suitability of local authority Trading Standards to regulate the selling of a complex financial product. The FSA is the single unified regulator for financial services and has the greatest experience in regulating the selling of insurance products, whether by financial services firms or by firms for whom selling insurance is a secondary activity.

COST AND BENEFITS

Groups affected **5.15** The costs and benefits of the Government's three proposed options are provided below. No attempt has been made to quantify costs and benefits unless sufficient evidence is available with which to do so.

5.16 The following main groups have been identified as potentially being affected by these proposals:

- travel agents and tour operators;

¹ Travel insurance review – call for evidence, November 2006

- event management firms;
- vehicle rental firms;
- insurance customers of the above firms;
- insurance companies;
- insurance intermediaries.

5.17 Some 20 million consumers purchase travel insurance each year in a market worth £670m in 2006². Travel insurance sold by travel agents and tour operators accounted for just under 50% of all travel insurance sales in 2004³. However, more recent estimates by Mintel put the share of policies sold by travel agents at around one in four⁴. ABTA Member firms are responsible for the sale of around 80% of all package holidays sold in the UK⁵.

Option 1 – costs and benefits **5.18** Option 1 involves maintaining the status quo. Sales of travel insurance sold along with a holiday would remain unregulated, although subject to some degree of industry self-regulation, such as the ABTA Code of Conduct and the AiTO's Code of Business Practice.

5.19 The benefits of option 1 include:

- no additional costs of regulation to the travel sector;
- all travel agents/tour operators would be able to continue selling travel insurance.

5.20 The costs of option 1 include:

- The potential remains for consumer detriment, including:
 - a lack of statutory requirements on a travel firm to take steps to ensure that the consumer understands the policy, for example through providing disclosure information at the point-of-sale or explaining the features of the cover;
 - the complexity of travel insurance as a product means that bundling may be likely to lead to mis-selling, since there is little opportunity for customers to check that the policy meets his or her requirements, or to shop around and compare prices;
 - consumer difficulty in understanding the distinction between policies sold along with a holiday and those sold as a stand-alone product;
 - a lack of access to the Financial Ombudsman Service (FOS) whenever a dispute concerns the mis-selling of the insurance product by a travel firm, and there is no access to the FOS at all where cover is provided through a non-UK insurer. Anecdotal evidence suggests that non-UK insurers underwrite a significant proportion of the insurance policies offered by travel firms in the UK.

² Source: Mintel, *Travel Insurance, Finance Intelligence, February 2007*

³ Source: Datamonitor

⁴ Source: Mintel, *Travel Insurance, Finance Intelligence, February 2007*

⁵ Source: ABTA *Travel Statistics and Trends 2005*.

Option 2 – costs and benefits **5.21** Option 2 would involve some form of strengthened industry self-regulation along with access to the FOS. The travel industry would be responsible for ensuring high standards of selling, but consumers would ultimately have recourse through the FOS if things go wrong. Primary legislation would be required to make the jurisdiction of the FOS compulsory. An independent body would also be required to certify that the relevant industry Codes were of an appropriate standard.

5.22 The benefits of option 2 include:

- a market-led solution to improve consumer protection;
- possibility of improvement in selling practices by travel agents and tour operators through strengthened requirements on disclosure information;
- consumers have access to an independent, impartial and low cost method of redress through the FOS.

5.23 The costs associated with option 2 include:

- some (relatively low) cost to firms of implementing improvements, including an annual levy or per case fee (or combination of both) to fund disputes taken to the FOS;
- travel firms outside of trade association membership would not be required to comply with any non-statutory requirements;
- trade associations' ultimate sanction is only to expel the firm from membership of the trade association.

Option 3 – Costs and Benefits **5.24** This option involves giving the FSA responsibility for regulating the selling of travel insurance sold along with a holiday or other related travel. This would mean that all firms would require authorisation to sell travel insurance no matter what the distribution method used. Firms would be responsible for meeting high-level principles set by the FSA as well as any conduct of business rules. Consumers would have full access to the FOS as a method of redress and access to the Financial Services Compensation Scheme (FSCS) in the event of an insurer/travel agent insolvency in relation to travel insurance.

5.25 The benefits of option 3 include:

- the main benefits of FSA regulation are that firms will have to meet the FSA's high-level principles for conducting business, for instance on treating customers fairly, as well as meeting any rules or guidance issued by the FSA. At present, authorised firms selling insurance are required comply with the FSA's Insurance: Conduct of Business (ICOB) rules, especially on clear disclosure information. This means that firms need to ensure a high-standard in selling insurance, reducing the potential of consumer detriment through mis-selling;
- consumers would also get increased consumer protection through:
 - access to the FOS in the event of a dispute concerning the selling of travel insurance, rather than having to rely on: a) an industry trade body dispute resolution scheme which is sometimes perceived as being against the consumer; or, b) taking the travel agent or tour operator to court;

- access to the FSCS in respect of the travel insurance policy if a travel agent or tour operator becomes insolvent;
- more transparent information and moving away from an inertia (bundled) sale could have a positive impact on consumers if it encourages them to shop around and seek the best policy in terms of coverage and price;
- a core baseline of statutory protection for consumers when buying travel insurance, irrespective of the distribution channel. The results of BIBA's consumer survey indicate that 54% of consumers believe that all sellers of travel insurance are currently covered by the same regulations – i.e. evidence of consumer confusion regarding what protections are available when buying essentially the same type of insurance. However, it should be noted that it will be up to the FSA to determine how best to regulate the selling of travel insurance through different distribution channels;
- there is likely to be a benefit to regulated travel insurance intermediaries through some levelling of the cost base.

5.26 There are various monetary costs associated with being regulated by the FSA⁶. These costs are a matter for the FSA to determine. In the examples given below, FSA fees for general insurance intermediaries are used as a guide, although the FSA would be free to set up a different fee regime specifically for travel firms. The costs of option 3 include:

- **The initial direct cost of FSA regulation.** The FSA will charge a flat authorisation fee of £1500 for general insurance intermediaries in the financial year 2007/08⁷. Although there are no definitive figures for the number of travel agents, there are around 1600 ABTA Members. It also appears fair to assume that there are at least as many non-ABTA travel firms. Assuming all 3,200 travel agents and tour operators sought authorisation, the maximum initial cost would be around £4.8 million for the industry as a whole. Depending on the shape of any future regime introduced by the FSA, this may cover any transitional costs since the FSA already regulates similar insurance mediation activities;
- **Ongoing costs.** The FSA also charges firms a periodic fee to cover the ongoing costs of its regulation. This is based on: (i) the regulated activities that the firm undertakes; and (ii) the amount of business related to its regulated activities⁸. Based on certain assumptions on the sales of travel insurance by travel firms, and assuming that all firms seek authorisation, the total cost to the travel industry of these ongoing fees is £1.37 million or 28 pence per policy sold. The box below gives more detail on how this estimate was derived;
- **The indirect cost of FSA regulation.** This is uncertain and would depend on the regulatory regime that was introduced by the FSA and how firms who decided to get authorised adapted to the new regulation. It is likely that the

⁶ The latest on FSA fees is set out in the FSA's consultation paper 07/3 'Regulatory fees and levies 2007/08', published in February 2007.

⁷ See FEES 3 Annex 1R: *Authorisation fees payable* of the FSA's Handbook

⁸ For firms carrying out general insurance intermediation, this is the net amount retained by the firm of all brokerages, fees, commissions and other related income (e.g. administration charges, overrides, profit shares) due to the firm in respect of or in relation to insurance mediation activity. See FEES 4 Annex 1R *Activity groups, tariff bases and valuation dates applicable* of the FSA's Handbook.

indirect costs are significantly, perhaps an order of magnitude, more than the direct costs and would primarily comprise compliance costs for firms under the FSA regime. Estimates would depend on the regime that the FSA decided to introduce. The FSA are looking, as part of the current review of their Insurance: Conduct of Business (ICOB) rules, to move towards a more principles-based style of regulation for the majority of general insurance products, which will allow firms more freedom in the way they interpret and implement the high-level standards set by the FSA.

THE COSTS TO FIRMS OF BECOMING REGULATED

The FSA is an independent body and finances its work by charging fees on all authorised firms that carry out the activities that it regulates. As well as its own fees the FSA invoices on behalf of the FSCS and the FOS. The FSA charges firms:

- periodic fees (paid yearly), which provide most of the funding needed to carry out its statutory duties;
- application fees, which recover some of the costs of processing certain applications under its rules or FSMA;
- special project fees where activity is undertaken at the request of fee-payers.

The amount a firm pays as an annual fee depends on its potential impact on the FSA's statutory objectives. The FSA uses an appropriate size of business measure in each fee block as a proxy for potential impact. In general this means that the larger the firm is the more it has to pay. Application fees for authorisation are based on the complexity of the application, which is a product of the permission being applied for. More information on fees is available from the FSA's website: www.fsa.gov.uk.

DIRECT ONGOING COSTS ARISING FROM FSA REGULATION WHERE ALL TRAVEL FIRMS SEEK AUTHORISATION

The FSA's fee structure for general insurance intermediaries is based on a minimum fee plus a sliding scale of additional fees based on turnover from regulated activities. The minimum fee for general insurance intermediaries with an annual turnover from regulated activities of under £100,000 will be £410 for the financial year 2007/08. There is then a sliding scale of additional payments:

- for the firm's annual turnover from regulated activities between £100,000 to £1 million an additional fee of £3.88 per £1,000 income from regulated activities is payable;
- from £1m to £5m an additional periodic fee of £3.39 per £1,000 income from regulated activities is payable;
- from £5 to £15 million a further additional fee of £2.45 per £1,000 income from regulated activities is payable;
- from £15 to £100 million a further additional fee of £0.98 per £1,000 income from regulated activities is payable;
- and above £100 million a further additional fee of £0.40 per £1,000 income from regulated activities is payable.

ABTA figures show the following for the size and distribution of its members:

- £100m plus: 51 firms with total turnover of £21,556m;
- £50m – £100m: 28 firms with total turnover of £1,957m;
- £15m - £50m: 135 firms with total turnover of £3,621m;
- up to £15m: 1,329 firms with total turnover of £3,755m.

So, assuming that:

- travel agents sell 24% of travel insurance policies out of a total market worth £670m;
- travel agents earned, on average, 20% commission on each insurance policy sold;
- all ABTA's member firms become authorised, along with 1,600 non-ABTA members;

the total direct cost of ongoing regulation would be £1.37m per year or 28 pence per policy. This estimate is based on an average firm and does not take into account the different sizes of firms within the turnover brackets outlined above.

The numbers above are sensitive to the assumptions used. The following gives an idea of how the numbers would be affected by changing some of the assumptions:

- If the number of non-ABTA firms was instead 3,200, the total ongoing direct cost of FSA regulation would be £1.99m per year or 42 pence per policy sold;
- If the commission travel agents earned on travel insurance was 5% instead of 20% then the total direct cost of ongoing regulation would be £1.31m or 27 pence per policy sold. If commission was 40% then the total direct cost of ongoing regulation would be £1.45m or 30 pence per policy sold;
- If travel agents were responsible for 50% of all travel insurance sales then the total cost of ongoing regulation would be £1.45m or 15 pence per policy sold.

INDIRECT COSTS – AN ILLUSTRATION RELATING TO INSURANCE MEDIATION

On introducing the general insurance regime the FSA undertook a cost-benefit analysis of the impact of its ICOB Rules. This was undertaken by NERA and set out in the publication: *“Estimated compliance costs of conduct of business regulation for general insurance”*.

This report estimated costs associated with ICOB of £197.4 million one-off plus £163.9m ongoing. Costs associated with minimum Directive requirements (arising from notably the Distance Marketing Directive (DMD) and the Insurance Mediation Directive (IMD)) were estimated at £179.9m in one-off costs and £143.8m annually. It should be noted that IMD requirements would not necessarily be applicable to firms selling travel insurance along with a holiday since these sales are exempt from the Directive.

The NERA figures are based on a population of 45,220 firms selling insurance.

Uprating for inflation, and assuming the FSA introduces the same ICOB rules as estimated in the NERA report, this means that the initial indirect cost per firm was in the order of £4,750, while ongoing costs would be in the region of around £4,000. There are likely to be other indirect costs associated with being regulated – for example, authorisation costs, training and competence costs, although there is likely to be some overlap in costs. The FSA’s recent review of the selling of general insurance is proposing removing many of the ICOB rules, which may lead to cost reductions for firms.

Assuming there are 3,200 travel firms, and all of these firms seek FSA authorisation, this would result in indirect one-off costs of £15.2m and ongoing costs of £12.8m (£2.60 per policy sold, assuming travel firms sell around a quarter of all travel policies).

However, academic research⁹ suggests that the indirect costs of FSA regulation might be around four times the direct costs. Given the direct costs outlined above, this would suggest a one-off indirect cost to travel firms of around £19.2m and ongoing annual indirect costs of £5.48m.

5.27 Other costs associated with regulation include:

- **Financial Services Compensation Scheme** - the FSCS is funded by levies on firms authorised by the FSA. For levying purposes, FSCS business is split into sub-schemes, including one for insurance mediation (from 14 January 2005). For each sub-scheme there are one or more contribution groups, based on the "fee blocks" used by the FSA for allocating its own fees to regulated firms. Firms are allocated to a contribution group (or groups) according to their regulated permissions, i.e. the type of business they are authorised to transact¹⁰. There are limits to the amounts FSCS can levy in a financial year. For compensation payments the limit for general insurance intermediaries is currently no more than 0.8% of annual eligible income

⁹ *“The direct and compliance costs of financial regulation”* Franks, Schaefer and Staunton, Journal of Banking & Finance, Volume 21, Issues 11-12, December 1997

¹⁰ Full details of the funding rules for FSCS are available in the FSA’s Handbook.

(from regulated activities). It is estimated that travel firms' income from selling travel insurance policies is around £19.5m, which would mean that the maximum contribution in any one year to the FSCS would be £156,000 – although this is an upper limit and is only likely to be reached following several firm failures in that specific contribution group. The FSA is currently reviewing the funding of the FSCS and has proposed an increase in the maximum levy payable by insurance intermediaries, to 3.5%¹¹. If this is adopted, the maximum levy payable would rise to £682,500;

- **Financial Ombudsman Service** - there is an annual fee for access to the FOS. This is currently £50 for general insurance mediation. Each firm is not charged a case fee for the first two disputes in each year for which the FOS are required to reach a decision. For additional cases, charges are levied at £400 per case no matter what the outcome of the complaint;
- it has also been argued that regulation might lead to a loss of claims handling services and advice on the suitability of the product that may be provided by travel insurers;
- where travel firms decide to become an appointed representative of that firm there will also be additional indirect and ongoing costs on the authorised firm. However, authorised firms are only likely to enter into an appointed representative agreement if they believe that the contractual fee paid by the unregulated firm will more than compensate for these costs.

5.28 It is possible that these costs may be passed onto the consumer through travel agents charging higher premiums. This could have a negative impact in terms of its impact on the number of people taking out insurance for trips abroad, although the UK has a very well developed stand-alone travel insurance market. However, travel firms would remain under an obligation under the Package Travel Directive to advise on the availability of travel insurance, so are likely to consider taking advantage of the exemption in article 72C of the Regulated Activities Order to team up with insurers and/or brokers to provide information on insurance to their customers.

5.29 Costs imposed by FSA regulation will not all be additional costs. Travel firms should already be providing staff training and firms that are members of a trade association, such as ABTA, will need to comply with its rules. It is also worth pointing out that, under the requirements of the Distance Marketing Directive¹² (DMD), where travel firms make a 'distance' insurance sale, for example, over the telephone or on the internet, they are already required to provide the consumer with certain information, including a description of the main characteristics of the product.

5.30 It is not possible at this stage to split the costs associated with this option into policy compliance costs and administrative burdens. This will only be possible when the FSA has indicated the regime that it intends to apply. At this point, the Government expects that policy compliance costs (such as the costs of ensuring that the details of insurance policies are disclosed in a fair and transparent way, FSA authorisation fees, FOS case fees) will constitute a higher proportion of total costs than administrative burdens.

¹¹ See the FSA's *Consultation Paper 07/15: Financial Services Compensation Scheme Funding Review* at http://www.fsa.gov.uk/pages/library/policy/cp/2007/07_05.shtml. The consultation period closed on 20 June 2007.

¹² Implemented in the UK by SI 2004 No. 2095: The Financial Services (Distance Marketing) Regulations 2004.

5.31 Subject to the underlying assumptions, these figures for the costs of regulation are maximum figures since it is likely that the introduction of regulation will cause firms to alter their business models. It would of course be optional whether or not travel agents or tour operators decided to become authorised to continue to sell travel insurance. Other routes available to travel agents and tour operators would be to become an appointed representative of an insurer or an insurance intermediary. Travel agents and tour operators could also look to team up with others selling insurance services to ensure insurance is still offered to their customers or simply provide information to consumers. Under this option it is not possible to determine how many travel agents will go down the appointed representatives route, although anecdotal evidence suggests that some are actively considering it. The appointed representatives route is generally seen as a cheaper way of ensuring regulatory compliance without becoming directly authorised by the FSA. Another option would be for the travel firm to undertake an 'introducer' role, whereby the travel firm simply directs the individual to a regulated intermediary or insurer in return for a fee from the regulated firm. **The number of firms actually seeking FSA authorisation may actually turn out to be quite low given these alternative routes available.** The box below gives an indication of costs where not all firms decide to seek authorisation.

COSTS ARISING FROM FSA REGULATION WHERE NOT ALL TRAVEL FIRMS SEEK AUTHORISATION

It is unlikely that all travel firms will choose to become authorised. Firms may consider other options including becoming an appointed representative of a regulated firm or ceasing to sell insurance altogether, perhaps instead taking on an introducer role. The costs of FSA authorisation provide an upper bound of the costs imposed on travel firms by this measure since otherwise the firm would be best served by seeking authorisation. It is difficult to be certain about the direct costs of seeking appointed representative (AR) status since they will be determined by a commercial contract between the regulated firm and the AR. The Government would welcome any indicative information on such contracts in order to inform its final RIA.

Maintaining the core assumptions outlined above, and assuming that: (i) 30% of travel firms seek FSA authorisation; 30% become ARs; and 40% stop selling insurance; and, (ii) the cost of becoming an AR is 75% of the total ongoing costs under FSA authorisation:

- there will be a total direct one-off cost to travel firms of £2.52m;
- there will be a total direct ongoing cost to travel firms of £0.72m;
- there will be total indirect one-off costs to travel firms in a range of £7.98m and £10.08m, based on the range of indirect one-off costs above;
- there will be total indirect ongoing annual costs in a range of £2.87m and £6.72m, based on the range of indirect ongoing annual costs above.

This suggests that the total costs to travel firms following the introduction of FSA regulation amount to one-off costs of between £10.5m and £12.6m and ongoing annual costs of between £3.59m and £7.44m. These costs are sensitive to the assumptions made and would depend on the nature of the regime the FSA decide to introduce.

There may be a further cost to travel firms who stop selling insurance through lost profit streams that had been provided through insurance sales. It is not possible to quantify this effect. However, responses to the call for evidence have suggested that many travel firms make only a small margin from sales of insurance alongside a holiday and so it seems reasonable to assume that, if firms do stop selling insurance products as a result of this decision, this will not have a large impact on the profitability of the sector. There may also be an opportunity for travel firms to offset any lost income by advertising or introducing travel insurance.

5.32 ABI research¹³ looking at the overall costs and benefits of general insurance regulation concluded that regulation has had a positive effect for customers who purchase insurance alongside other goods or services.

SMALL FIRMS IMPACT TEST

5.33 Some responses to the call for evidence argued that smaller travel firms would be less able to meet the additional costs imposed by a requirement for travel firms selling travel insurance to be regulated.

5.34 It is likely that the smaller firms will not seek to become authorised, but to look for alternative methods of providing insurance services, either through becoming an appointed representative of a regulated firm or by undertaking an introducer role. The

¹³ *The Regulation of General Insurance Sales: One Year On*, March 2006.

Government believes that the benefits afforded by proper consumer protection, coupled with these options for travel firms to continue providing insurance services, justify seeking to have the selling of travel insurance products taking place in a regulated environment.

COMPETITION ASSESSMENT

5.35 It has been argued that a requirement for the selling of travel insurance alongside a holiday to be regulated would lead to fewer firms selling travel insurance, and hence lower competition in this area. However the UK's travel insurance market is widely regarded as being competitive and presents an obvious alternative route for consumers to purchase cover, should the number of travel firms selling insurance shrink. These firms would also have the opportunity to introduce customers to brokers and insurers who sell travel insurance. Given the benefits of regulation, the Government does not feel that this is a compelling reason to not regulate in this area.

Question 1

Do you agree with the analysis of costs and benefits for the different implementation options, and in particular with the assumptions made in quantifying these costs, as well as the impact on competition and small firms?

ENFORCEMENT, SANCTIONS AND MONITORING

5.36 The FSA will be responsible for monitoring, enforcement and sanctions of those firms entering the regulatory perimeter.

HOW TO RESPOND

5.37 The Government welcomes the views of all stakeholders on issues raised in this document. The consultation period begins with the publication of this document and will run for 12 weeks. Please ensure that responses to this consultation reach us by 18 September 2007. We cannot guarantee to consider responses received after this date. Responses should be sent to:

Eve Engledow
Financial Stability and Risk Team
HM Treasury
1 Horse Guards Road
London SW1A 2HQ
Fax: 020 7451 7524
Email: travel.review@hm-treasury.gov.uk

5.38 Enquiries relating to this consultation can be made to:

Richard Wronka
Financial Stability and Risk Team
Tel: 020 7270 5389
Email: travel.review@hm-treasury.x.gsi.gov.uk

5.39 This document can be found on HM Treasury's website:
<http://www.hm-treasury.gov.uk>.

5.40 When responding, please state whether you are responding on behalf of an individual or representing the views of an organisation. If responding on behalf of a larger organisation, please make it clear who the organisation represents and, where applicable, how the views of members were assembled.

CONFIDENTIALITY

5.41 HM Treasury reserves the right to make all written responses publicly available on its website unless the author specifically requests otherwise in writing.

5.42 Information provided in response to this consultation, including personal information, may be published or disclosed in accordance with the access to information regimes (these are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act (DPA) and the Environmental Information Regulations 2004). If you want the information that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals, amongst other things, with obligations of confidence. In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality will be maintained in all circumstances.

5.43 An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on HM Treasury. HM Treasury will process your personal data in accordance with the DPA, and in the majority of circumstances, this will mean that your personal data will not be disclosed to third parties.

5.44 Subject to paragraphs 5.41 - 5.43 if you wish part (but not all) of your response to remain confidential, please supply two versions – one for publication on the website with the confidential information deleted, and another confidential version for use by HM Treasury.

FREEDOM OF INFORMATION CONTACT

5.45 Any Freedom of Information Act queries should be directed to:

Correspondence and Enquiry Unit
Freedom of Information Section
HM Treasury
1 Horse Guards Road
London
SW1A 2HQ
Telephone: 020 7270 4558
Fax: 020 7270 4681
Email: public.enquiries@hm-treasury.x.gsi.gov.uk

CONSULTATION DOCUMENT

5.46 The consultation document is published with this document and should be read in conjunction with it. A copy of the consultation document can be found on HM Treasury's website (www.hm-treasury.gov.uk).

HOW THIS CONSULTATION IS BEING CONDUCTED

5.47 This consultation is being conducted in line with the Code of Practice on Consultation. The criteria are listed below (a full version can be found at <http://www.cabinet-office.gov.uk/regulation/consultation/code.html>). The six consultation criteria are:

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

5.48 If you have concerns as to how this consultation is being conducted, please contact:

Sowdamini Kadambari
Enterprise Team
HM Treasury
1 Horse Guards Road
London
SW1A 2HQ
Telephone: 020 7270 4867
Email: sowdamini.kadambari@hm-treasury.x.gsi.gov.uk

A

RESPONDENTS TO THE CALL FOR EVIDENCE

Air Transport Users' Council
Association of British Insurers
Association of British Travel Agents
Association of Independent Tour Operators
Association of Travel Insurance Intermediaries
AVIVA
AXA
British Insurance Brokers' Association
British Vehicle Rental and Leasing Association
British Victims of Terrorism Abroad
The Caravan Club
Citizens Advice
Civil Aviation Authority
Co-operative Travel Trading Group
Department for Transport
Eventia
Financial Ombudsman Service
Financial Services Authority
Financial Services Consumer Panel
Global Travel Insurance
Gower Tours Ltd.
HBOS
Holiday TravelWatch
Institute of Insurance Brokers
Last Frontiers Ltd.
MAMMA
Meltemi Travel
MGTIS
Milkovics & Co.
PJ Hayman & Co.
RBS Insurance
Royal Mail
Scottish Passenger Agents' Association
Select Sites Ltd.
The Ski Company
Special Pilgrimages Christian Tours
Towergate Chase Parkinson
Treasury Select Committee
Trading Standards Institute and LACORS (Local Authorities Coordinators of Regulatory Standards) joint response

TUI UK (Thomson Holidays)

Voyager Insurance Services

Which?

Zurich Financial Services

33 responses were also received from individuals

Order made by the Treasury and laid before Parliament under paragraph 26 of Schedule 2 to the Financial Services and Markets Act 2000 (c.8) for approval by resolution of each House of Parliament within twenty-eight days beginning with the day on which the Order is made, subject to extension for periods of dissolution, prorogation, or adjournment of both Houses for more than four days.

STATUTORY INSTRUMENTS

2007 No.

FINANCIAL SERVICES AND MARKETS

Financial Services and Markets Act 2000 (Regulated Activities) (Amendment No. 2) Order 2007

Made - - - - *******

Laid before Parliament *******

Coming into force in accordance with article 1(2).

In the opinion of the Treasury one of the effects of the following Order is that an activity which is not a regulated activity (within the meaning of the Financial Services and Markets Act 2000⁽¹⁾) will become a regulated activity;

The Treasury make the following Order in exercise of the powers conferred by sections 22(1) and (5), 426, 427 and 428(3) of, and paragraph 25 of Schedule 2 to, the Financial Services and Markets Act 2000:

PART 1

GENERAL

Citation, commencement and interpretation

1. This Order may be cited as the Financial Services and Markets Act 2000 (Regulated Activities) (Amendment No. 2) Order 2007.

(1) This Order comes into force—

- (a) for the purposes of enabling applications to be made, pursuant to the amendments made to article 72B of the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001⁽²⁾ by article 2 of this Order, for—
 - (i) a Part IV permission, or a variation of a Part IV permission, in relation to activities of the kind specified by article 21, 25(1), 25(2), 39A or 53 of the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001; or

⁽¹⁾ 2000 c. 8.

⁽²⁾ S.I. 2001/544; article 39A was inserted by S.I. 2003/1476 and article 72B was inserted by S.I. 2003/1476.

- (ii) the Authority’s approval under section 59 of the Financial Services and Markets Act 2000 in relation to any of those activities, on 30th June 2008;
- (b) for all other purposes, on 1st January 2009.

PART 2

AMENDMENT OF THE REGULATED ACTIVITIES ORDER

Amendment of the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001

2.—(1) Article 72B of the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (activities carried on by a provider of relevant goods or services) is amended as follows.

(2) For paragraph (1)(d)(ii) substitute—

- “(ii) damage to, or loss of, baggage and other risks linked to the travel booked with the provider (“travel risks”) in circumstances where—
 - (aa) the travel booked with the provider relates to attendance at an event organised or managed by that provider and the party seeking insurance is not an individual (acting in his private capacity or for a small business) or a small business; or
 - (bb) the travel booked with the provider is the hire of an aircraft, vehicle or vessel.”

(3) In paragraph (1) after the definition of “provider” insert —

““small business” means a business whose group turnover in the last financial year was less than £1,000,000;

“turnover” means the amounts derived from the provision of goods and services falling within the person’s ordinary activities, after deduction of trade discounts, value added tax and any other taxes based on the amounts so derived.”.

PART 3

TRANSITIONAL PROVISIONS

Interpretation

3. In this Part—

“the Act” means the Financial Services and Markets Act 2000;

“commencement” means the beginning of 1st January 2009;

“the Regulated Activities Order” means the Financial Services and Markets Act 2000 (Regulated Activities Order) 2001.

Interim permission

4.—(1) This article applies where—

- (a) a person who is a provider within the meaning of article 72B of the Regulated Activities Order (“the applicant”) has submitted to the Authority an application for Part IV permission or a variation of a Part IV permission to the extent that the application—
 - (i) relates to an activity of the kind specified in any of the following articles of the Regulated Activities Order—
 - (aa) article 21 (dealing in investments as agent);
 - (bb) article 25(1) and (2) (arranging deals in investments);

- (cc) article 39A (assisting in the administration and performance of a contract of insurance); or
- (dd) article 53 (advising on investments);
- (ee) article 64 (agreeing to carry on specified kinds of activity) in so far as it relates to any of the activities mentioned in (aa) to (dd); and
- (ii) is made pursuant to the amendments made to article 72B of the Regulated Activities Order by article 2 of this Order;
- (b) the Authority received the application on or before 15th November 2008; and
- (c) the application has not been finally decided before commencement.
- (2) The applicant is to be treated as having on commencement the permission to which the application relates.
- (3) A permission which an applicant is to be treated as having is referred to in this Part as an “interim permission”.
- (4) Without prejudice to the exercise by the Authority of its powers under Part 4 of the Act, an interim permission lapses —
 - (a) when the application has been finally decided; or
 - (b) at the beginning of 31st December 2009,

whichever is the earlier.

- (5) In this article “finally decided” means—
 - (a) when the application is withdrawn;
 - (b) when the Authority grants permission under section 42 of the Act (giving permission) to carry on the activity in question;
 - (c) when the Authority varies a permission under section 44 of the Act (variation etc. at request of authorised person) to add the activity in question;
 - (d) where the Authority has refused an application and the matter is not referred to the Tribunal, when the time for referring the matter to the Tribunal has expired;
 - (e) where the Authority has refused an application and the matter is referred to the Tribunal, when—
 - (i) if the reference is determined by the Tribunal (including a determination following remission back to the Tribunal for rehearing in accordance with section 137(3)(a) of the Act (appeal on a point of law)), the time for bringing an appeal has expired; or
 - (ii) on an appeal from a determination by the Tribunal on a point of law, the Court itself determines the application in accordance with section 137 of the Act.
- (6) An applicant who is treated as having an interim permission may not withdraw the application without first obtaining the consent of the Authority.
- (7) Where—
 - (a) the Authority exercises its powers under section 45 (variation etc. on the Authority’s own initiative) in relation to an authorised person who holds an interim permission; and
 - (b) as a result of the variation there are no longer any regulated activities for which the authorised person has permission,

the Authority must, once it is satisfied that it is no longer necessary to keep the interim permission in force, cancel it.

Interim approval

5.—(1) This article applies where—

- (a) the applicant (within the meaning of article 4(1)(a)) has submitted to the Authority an application made under section 60 of the Act (applications for approval) pursuant to the amendments made to article 72B of the Regulated Activities Order by article 2 of this Order; and

- (b) the application has not been finally decided before commencement.
- (2) The person in respect of whom the application is made is to be treated as having on commencement the approval of the Authority for the purposes of section 59 of the Act (approval for particular arrangements) in relation to the functions to which the application relates.
- (3) An approval which a person is to be treated as having is referred to in this Part as an “interim approval”.
- (4) Without prejudice to the exercise by the Authority of its powers under Part 5 of the Act, an interim approval lapses—
 - (a) when the application has been finally decided; or
 - (b) at the beginning of 31st December 2009,

whichever is the earlier.

- (5) In this article, “finally decided” means—
 - (a) when the application is withdrawn;
 - (b) when the Authority grants the application for approval under section 62 of the Act (applications for approval: procedure and right to refer to the Tribunal);
 - (c) where the Authority has refused an application and the matter is not referred to the Tribunal, when the time for referring the matter to the Tribunal has expired;
 - (d) where the Authority has refused an application and the matter is referred to the Tribunal, when—
 - (i) if the reference is determined by the Tribunal (including a determination following remission back to the Tribunal for rehearing in accordance with section 137(3)(a) of the Act), the time for bringing an appeal has expired; or
 - (ii) on an appeal from a determination by the Tribunal on a point of law, the Court itself determines the application in accordance with section 137 of the Act.

Application of the Authority’s rules etc to persons with an interim permission or an interim approval

6.—(1) The Authority may direct in writing that any relevant provision which would otherwise apply to a person by virtue of his interim permission or interim approval is not to apply or is to apply to him as modified in the way specified in the direction.

- (2) Where the Authority makes a rule, gives guidance or issues a statement or code which applies only to persons with an interim permission or an interim approval (or only to a class of such persons), sections 65 (statements and codes: procedure), 155 (consultation) and 157(3) (guidance) of the Act do not apply to that rule, guidance, statement or code.
- (3) For the purposes of paragraph (1) a “relevant provision” is any provision made as a result of the exercise by the Authority of any of its legislative functions mentioned in paragraph 1(2) of Schedule 1 to the Act (the Financial Services Authority).

Application of the Act to persons with an interim permission or an interim approval.

7.—(1) This article applies to every person with interim permission.

- (2) For the purpose of section 20 (authorised persons acting without permission), a person’s interim permission is treated as having been given to him under Part 4 of the Act.
- (3) A person’s interim permission is to be disregarded for the purposes of—
 - (a) section 38(2) (exemption orders);
 - (b) section 40(2) (application for permission);
 - (c) subject to article 8(4), section 42 (giving permission);
 - (d) section 43 (imposition of requirements); and
 - (e) section 44(1), (4) and (5) (variation etc. at request of authorised person).

8.—(1) This article applies to a person who falls within section 31(1) (authorised persons) by virtue only of having an interim permission.

- (2) A person with an interim permission is to be treated on or after commencement as an authorised person for the purposes of the Act (and any provision made under the Act), unless otherwise expressly provided for by this Part.
- (3) For the purposes of section 21(2) (restrictions on financial promotion), a person with an interim permission is not to be treated as an authorised person for the purposes of communicating or approving the content of a communication except where the communication invites or induces a person to enter into (or offer to enter into) an agreement the making or performance of which constitutes a controlled activity which corresponds to a regulated activity which is covered by his interim permission.
- (4) A person with an interim permission may still be an appointed representative within the meaning of section 39(2) (exemption of appointed representatives) (and hence may be treated as exempt from the general prohibition as a result of section 39(1) for the purposes of section 42(3)(a) (giving permission)).
- (5) Subsection (3)(a) of section 213 (the compensation scheme) does not apply to—
 - (a) a person who is a relevant person, within the meaning of that section, by virtue only of having an interim permission; or
 - (b) an appointed representative of such person.

9. A person with an interim approval is to be treated on or after commencement as an approved person for the purposes of the Act (and any provision made under the Act).

	<i>Name</i>
	<i>Name</i>
Date	Two of the Lords Commissioners of Her Majesty's Treasury

EXPLANATORY NOTE

(This note is not part of the Order)

This Order amends article 72B(1)(d)(ii) of the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (“the Regulated Activities Order”) to limit the exemption from regulation in respect of the activities specified in articles 21, 25(1) and (2), 39A and 53 of the Regulated Activities Order for travel insurance to circumstances where a contract of insurance is linked to (a) travel to an event organised by the travel provider where the person seeking insurance is not an individual or a business with a group annual turnover of less than £1,000,000; or (b) the hire of a vehicle.

Article 4 confers an interim permission on certain applicants who have applied for permission under Part 4 of the Financial Services and Markets Act 2000 (“FSMA”) to carry on activities specified in article 21, 25(1), 25 (2), 39A or 53 of the Regulated Activities Order in relation to the sale of travel insurance and whose application is pending on the commencement of Part 2 of this Order (1st January 2009).

Article 5 confers interim approval, in similar terms to those in article 4, on people who are the subject of an application for approval under Part 5 of FSMA which his pending on 1st January 2009.

Article 6 enables the Financial Services Authority to modify, amongst other things, its rules in their application to persons with an interim permission or approval.

Articles 7 and 8 provide for the application of provisions in FSMA to persons with an interim permission, indicating where such provisions are to be treated as including or not including such persons.

Article 9 provides for the application of provisions in FSMA to persons with an interim approval.

A Regulatory Impact Assessment of the effect of this instrument on the costs of business has been prepared and may be obtained from the Financial Stability and Risk Team, HM Treasury, 1 Horse Guards Road, London SW1A 2HQ. It is also available on HM Treasury’s website (www.hm-treasury.gov.uk). A copy has been placed in the library of both Houses of Parliament.

ISBN 978-1-84532-314-1



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