

# **Deregulating freight forwarding insurance**

## **Summary of responses**

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June 2007



HM TREASURY





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forwarding insurance  
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# INTRODUCTION

**1.1** This document summarises the responses to HM Treasury's consultation on removing the insurance activities of freight forwarders from the scope of Financial Services Authority (FSA) regulation. This consultation was launched on 21 December 2006 and closed on 22 March 2007. The relevant text from the near-final version of the SI is provided at annex B. A final Regulatory Impact Assessment (RIA) has also been published alongside this document.

**1.2** HM Treasury are grateful to all those who responded to the consultation document and commented on the partial RIA.

## QUESTIONS ASKED BY THE CONSULTATION AND RIA

**1.3** The consultation document and partial RIA outlined proposals to remove certain insurance activities undertaken by freight forwarders from the scope of FSA regulation.

### Consultation document

**1.4** The questions raised in the consultation document were:

- Do you have any evidence on the potential for consumer detriment arising from freight forwarders' insurance activities?
- Do you have any views on the impact of the current requirement for FSA regulation upon the international competitiveness of the UK's freight forwarding sector?
- Should the Government's proposed approach be widened to include an exemption from legislation for other activities which are similar in nature to freight forwarding and what are the arguments for doing so?
- Do you have any comments on the partial RIA accompanying the consultation document?
- Do you have any comments on the draft Statutory Instrument accompanying the consultation document?

### Partial RIA

**1.5** The questions raised in the partial RIA were:

- Do you agree with the analysis of costs and benefits for the different implementation options, as well as the impact on competition and small firms?
- Are there any alternative ways of removing freight forwarders from the scope of FSA regulation that should be considered?

**1.6** Chapter 2 summarises the responses received to these questions and on other issues raised during the consultation period. Chapter 3 summarises the conclusions and sets out the next steps.



# 2

## SUMMARY OF RESPONSES

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### CONSULTATION

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**2.1** The consultation sought views on the proposal to remove certain insurance activities of freight forwarders from the scope of FSA regulation.

**2.2** 14 responses were received to the consultation from individuals, firms or representative bodies. A list of those responding to the consultation is attached at Annex A.

**2.3** Respondents were generally supportive of the proposal to remove the insurance activities of freight forwarders from the scope of FSA regulation. Most respondents agreed that the risk of consumer detriment presented by removing freight forwarders' insurance activities from FSA regulation is low. Some of the arguments provided by respondents were:

- the limited scope of exclusions in typical policies;
- policies are typically offered on a 'non-advised' basis, i.e. the individual customer is responsible for assessing whether the policy is appropriate;
- if rights under the master insurance policy are passed on to the consumer, FSA regulation still applies to the settlement of the insurance policy and therefore still affords some protection to the customer – for instance, consumers still have access to the Financial Ombudsman Service (FOS) following a dispute with the insurer and the Financial Services Compensation Scheme (FSCS) following insolvency of the insurer (subject to eligibility limits).

**2.4** Most respondents agreed that the current requirement for FSA regulation put UK freight forwarders at a competitive disadvantage against international counterparts.

**2.5** A number of respondents thought that the proposal should be widened to include an exemption from legislation for retail customers of freight forwarders. Respondents suggested that consumers would, in fact, be better protected outside of regulation. This is because, in practice, many freight forwarding companies have reacted to the introduction of regulation by taking out 'extended' liability insurance on behalf of their customers. However, this means that the customer does not have any direct rights under the contract of insurance and, importantly, will not have any access to the FOS or the FSCS should things go wrong.

**2.6** Prior to the introduction of regulation in January 2005, many freight forwarders and similar firms adopted a system of 'limited' liability. This means that under the terms and conditions of the forwarding contract, and following the loss of or damage to the customer's assignment, the customer could only claim directly against the forwarder under certain circumstances, such as where the forwarder had acted negligently. However, the freight forwarder would also arrange with an insurer a 'master cover' insurance policy and the customer is offered more comprehensive cover under this policy. Under the master cover policy, insurance rights are passed on from the freight forwarder on behalf of the insurer to the client, giving the consumer the right to go directly to the insurer in the event of a claim, as well as being able to use the FOS or FSCS (subject to certain eligibility limits).

**2.7** However, one respondent noted that the proposal should not be extended to retail customers as, where freight forwarders had become FSA authorised, they did not want the quality of advice or disclosures available to retail customers reduced, especially through access to the FOS and FSCS. This will, however, only be the case where the freight forwarder has sought FSA authorisation rather than gone down the extended liability route. The FSA estimate that they currently authorise the insurance activities of approximately 150 freight forwarders. This would suggest that the majority of freight forwarding firms have not sought authorisation and, given the arguments outlined above, the customers of these firms could in fact benefit from a higher level of consumer protection since they will possess a direct right under the insurance contract.

**2.8** Some respondents also suggested that consumer detriment would arise if the costs of FSA regulation deter the forwarder from offering insurance and the owner of the goods takes the risk of not insuring, because of the high cost of arranging one-off insurance. Some noted that this might already be the case.

**2.9** A few respondents suggested that self-regulation was necessary in light of the removal of regulation, as respondents were concerned that deregulation may leave consumers with no protection at all. Respondents suggested that trade association codes of conduct could be used, for example, to ensure the customer is told what the policy covers and excludes. Some responses went further to suggest trade association standards should be registered with the FSA. One response suggested that freight forwarders should be subject to the FOS for their activities, along with requirements to abide by the FSA's high-level principles and certain minimum 'conduct of business' rules including those in relation to segregation and treatment of client money.

**2.10** Some responses asked for the proposed approach to be widened to include an exemption from legislation for other activities which are similar to that of freight forwarders, such as storage companies. Respondents suggested that there is significant read-across between the two sectors, and that the risk of consumer detriment here is also low. They noted that as a result of regulation many of these companies are also taking out extended liability insurance, rather than obtaining FSA authorisation, and therefore consumers would be better protected outside of regulation for the same reasons as set out above.

**2.11** Most respondents thought that the draft Statutory Instrument met the policy intention set out in the consultation document. One respondent suggested that the draft Statutory Instrument should be redrafted, as there were concerns that the wording of paragraph 51(2) did not reflect the contents of the consultation paper. They felt that paragraph 51(2) suggested that the freight forwarder holds a freight liability policy and the customer is assigned rights under this policy. They considered that this was in conflict with paragraph 3.5 and 4.12 of the consultation paper, which refer to the freight forwarder taking out an "Open Cover" policy. Another respondent also suggested that the term "liability" be removed.

**2.12** Other comments received went wider than the specific issues being consulted on and are addressed below.

## **REGULATORY IMPACT ASSESSMENT**

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**2.13** Respondents were also asked to comment on the partial RIA. The partial RIA specifically asked whether respondents: a) agreed with the analysis of costs and benefits for the different implementation options, as well as the impact on competition and

small firms; and, b) whether there were alternative ways of removing freight forwarders from the scope of FSA regulation that should be considered.

**2.14** Most respondents who commented on the partial RIA were content that it dealt adequately with the expected regulatory impact. Respondents made the following additional points:

- customers who have faced higher premiums or difficulty in obtaining cover when getting a policy directly from an insurer/broker, as a result of the current regulation, are generally smaller companies or individuals;
- consideration should be given to allowing alternative arrangements to “Open Cover” within the draft Statutory Instrument. However, the respondent did not specifically refer to any of these alternatives.

**2.15** No alternative proposals for removing freight forwarders from the scope of FSA regulation were put forward.

## OTHER ISSUES RAISED DURING THE CONSULTATION

**2.16** The consultation specifically sought views on the exemption of freight forwarders insurance activities from the scope of FSA regulation. Respondents to the consultation also took the opportunity to put forward their wider views on deregulating insurance activities. A high level summary of the most commonly expressed views follows.

**2.17** Comments were received suggesting changes to the way these insurance activities could work outside of regulation, in order to increase protection for the consumer. This would make unregulated intermediaries subject to some elements of qualified regulation. For example it was suggested that insurers should approve all documentation shown or provided to customers. FSA rules already require insurers dealing with an unauthorised intermediary to provide the customer with certain information, such as the policy document and information on the claims handling process. Insurers are not, however, required to provide a policy summary in such circumstances.

**2.18** One respondent also noted that prior to FSA regulation, some freight forwarders increased the rates charged by the underwriter when calculating the premium to charge their customers. Respondents were concerned that this behaviour may return if deregulation were carried out. The FSA do not regulate firms’ price-setting decisions and, in that regard, this measure is not intended to impact directly on value-for-money considerations. However, the Government is concerned to ensure that the insurance activities of freight forwarders are carried out in an open and transparent way.

**2.19** Some respondents noted that other industries are also subject to an international competitiveness disadvantage as a result of regulation of their insurance mediation activities and asked for these industries to be considered for an exemption. These concerns have been acknowledged and we refer back to paragraphs 3.14 and 3.15 of the consultation document to explain why this proposal is focusing only on the specific insurance activities of freight forwarders. One respondent noted that it was particularly undesirable that introduction by a firm to an insurer or insurance broker is a regulated activity. However, the Government is only able to consider the case for the deregulation of activity that it is not required to regulate by the Insurance Mediation Directive.



# 3

## CONCLUSIONS AND NEXT STEPS

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### CONCLUSIONS

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**3.1** Given the responses received, the Government is content that there is a low risk of consumer detriment associated with the insurance activities of freight forwarders and intends to proceed with making the proposed change.

**3.2** The Government believes that, where storage firms arrange their insurance activities in the same way as freight forwarders, i.e. where rights under a master cover insurance policy are passed to the customer, these firms should also be exempted from regulation. This is due to the low risk of consumer detriment and also the desire to maintain a consistent approach for firms who conduct both traditional freight forwarding and storage activities.

**3.3** At first, this measure will only apply to commercial customers of freight forwarding and storage firms. The Government will therefore lay a SI that will exempt only insurance activities relating to commercial customers of these firms. The Government also considers that there is a case for extending the exemption to cover retail customers as well as commercial customers, since, somewhat counter-intuitively, it is likely that consumers will receive better redress and protection. As discussed above, in order to avoid regulation many freight forwarding and storage companies have chosen to use a system of extended liability insurance. In the event of a complaint, customers will only have a contract with the freight forwarder or storage firm and, importantly, will not have access to the FOS or the FSCS. Under the master cover policy commonly used prior to regulation, insurance rights are passed on from the freight forwarder on behalf of the insurer to the client, giving the consumer the right to go directly to the insurer in the event of a claim, as well as being able to use the FOS or FSCS. The Government believes that similar arguments also apply to storage firms.

**3.4** However, the Government wants to ensure that freight forwarders and storage firms maintain high standards during the course of their insurance activities. The Government will therefore use a two-stage approach and will only make the changes to exempt the retail insurance activities of freight forwarding and storage firms once these sectors have introduced and promoted an industry code of practice that ensures high standards and promotes transparency in connection with the insurance contract, as well as putting in place an appropriate independent complaints mechanism.

**3.5** The British International Freight Association (BIFA), the trade body representing freight forwarders, has indicated that it would be willing to introduce such self-regulation. The Government will also work with other relevant trade associations in the freight forwarding and storage sectors in order to develop codes of practice that will provide sufficient protection for retail customers. Once these codes are of satisfactory standard the Government will reconsider the case for extending this exemption to cover retail customers, through further secondary legislation.

**3.6** The Government will continue to monitor the insurance activities of freight forwarders and storage firms. The Government will not hesitate to act if evidence of mis-selling or consumer detriment emerges as a result of removing freight forwarders or storage firms from regulation.

## NEXT STEPS

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**3.7** A final RIA is published alongside this document. The relevant draft text from the proposed SI is also provided at annex B. As outlined above, this SI will deregulate freight forwarders' and storage firms' insurance activities only in relation to commercial customers. The legislation will be laid in due course and will also be made available on HM Treasury's website. Subject to Parliamentary approval, it is intended that these initial revised arrangements will apply as soon as possible.

**3.8** At the point that the Government is satisfied that the relevant trade associations have introduced appropriate self-policing measures it will consider laying a second SI before Parliament. This second SI will extend the de-regulation of insurance activities to retail customers of freight forwarding and storage firms.

**3.9** Please direct any enquiries to:

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# A

## RESPONSES TO THE CONSULTATION

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Abbott & Bramwell Insurance Brokers  
Aviva plc  
British Association of Removers  
British Insurance Brokers' Association  
British International Freight Association  
IFAct Services Limited  
Joint Cargo Committee  
Lockton Companies International Limited  
London Shipowners' and River Users' society  
The Maersk Company  
A Marine Insurance Consultant  
Movingetc  
The National Guild of Removers & Storers  
Self Storage Association of the UK



**Amendment of the Financial Services and Markets Act 2000 (Exemption) Order 2001**

- 1.—(1) The Financial Services and Markets Act 2000 (Exemption) Order 2001<sup>(1)</sup> is amended as follows.
- (2) In Part 4 of the Schedule, after paragraph 49 insert—

*“Freight forwarders and storage firms*

**50.**—(1) A freight forwarder or storage firm is exempt from the general prohibition in respect of any regulated activity of the kind specified by article 21, 25, 39A or 53 of the Regulated Activities Order<sup>(2)</sup> (dealing in investments as agent, arranging deals in investments, assisting in the administration and performance of a contract of insurance or advising on investments) in the circumstances referred to in paragraph 2.

(2) The circumstances are—

- (a) where a freight forwarder (“F”)—
- (i) holds a policy of insurance which insures F in respect of loss of or damage to goods which F transports or of which F arranges the transportation, and
  - (ii) makes available to a customer rights under that policy to enable the customer to claim directly against the insurer in respect of loss or damage to those goods; or
- (b) where a storage firm (“S”)—
- (i) holds a policy of insurance which insures S in respect of loss of or damage to goods which S stores or for which S arranges storage, and
  - (ii) makes available to a customer rights under that policy to enable the customer to claim directly against the insurer in respect of loss or damage to those goods.

(3) In this paragraph—

- (a) “freight forwarder” means a person whose principal business is arranging or carrying out the transportation of goods;
- (b) “storage firm” means a person whose principal business is storing goods or arranging storage for goods;
- (c) “customer” means a person who is not an individual who uses the service of a freight forwarder or storage firm.

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<sup>(1)</sup> S.I.2001/1201, amended by S.I.2001/3623 and 2007/125. There are other amending instruments but none is relevant to this Order.

<sup>(2)</sup> S.I.2001/544, amended by S.I.2003/1476; there are other amending instruments but none is relevant to this Order.





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