



HM TREASURY

**REGULATING INSURANCE
MEDIATION**

CONSULTATION DOCUMENT



INVESTOR IN PEOPLE

REGULATING INSURANCE MEDIATION

1. On 12 December 2001, Ruth Kelly, the Financial Secretary to the Treasury announced that the Financial Services Authority (FSA) would be given responsibility for regulating various activities relating to the sale and administration of general insurance products, whether carried on by intermediaries or insurers. This represents an extension of the FSA's remit. The FSA already regulates insurers' business on a prudential basis – that is as to adequate financial resources and to appropriate financial systems and controls. The FSA also regulates mediation activities relating to some contracts of long-term insurance business.
2. Extending the FSA's remit will also implement the European Union's Insurance Mediation Directive ("the Directive") in the United Kingdom. Legislation in the shape of statutory instruments under the Financial Services and Markets Act 2000 (FSMA) will specify what the FSA's responsibilities are to be. This document sets out the Treasury's proposals and the draft instruments required to bring these decisions into effect. Implementation will be effective from October 2004 (although this will be reviewed if there is significant delay in publishing the directive in the Official Journal of the European Communities).
3. The Treasury would welcome feedback on the proposals explained here. Please write to:

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4. It would be helpful to receive your response by 31 January 2003. The Government cannot guarantee to consider your response if it is received after that date. Please explain in your reply if you represent an organisation, and, if so, its membership and coverage, and any further details about the organisation, for example if it is a business brief details of the nature of the business including volume, customers and products. Your answer may be made public unless you say you want it kept confidential.

EXECUTIVE SUMMARY

THE GOVERNMENT'S APPROACH

Background

1. This consultation document sets out the Government's intended approach to regulating the sale of general insurance products. FSA regulation will enhance consumer protection in an important sector of financial business. The UK has the largest insurance industry in Europe. In 2000 over £150 billion of general and long term premiums were written.
2. These measures will in some cases simplify and streamline regulation. The FSA will be given responsibility for regulating both mortgage business and the mediation of general insurance from the same date, October 2004, (although this may be reviewed if there is a significant delay in publication of the Insurance Mediation Directive in the Official Journal of the European Communities). Intermediaries selling a range of products – general insurance, pensions, or mortgages – will come under the FSA as single regulator, minimising compliance costs. The measures in this document, together with forthcoming FSA rules, will also implement the European Union's Insurance Mediation Directive. This is a key step in completing the single market in financial services.
3. The consultation document sets out the Government's proposals on a range of issues:
 - *Chapter 1* gives further background to the Government's intended approach and sets out the principal steps towards the introduction of regulation. A detailed timetable is included at Annex B;
 - *Chapter 2* sets out which contracts of insurance will be regulated and where the Directive provides exclusions;
 - *Chapter 3* details the activities the Treasury intends to regulate. Annex C contains decision trees which will help readers determine whether they are likely to be carrying on activities to be regulated;

- *Chapter 4* explains how the Treasury intends to modify the regulatory regime for appointed representatives and members of certain professional bodies and also covers a range of other issues including Lloyd's and issues of territorial scope;
- *Chapter 5* summarises the requirements of regulation for those authorised by the FSA.

Which contracts of insurance will be regulated?

4. The Directive requires the regulation of mediation activities in relation to all contracts of insurance. However the Directive provides certain exemptions for insurance sold as part of a package.
5. Sales of travel insurance as a stand alone product will be regulated. But the Directive does not require regulation of travel insurance sold as part of a package with a holiday. The Government is considering whether to extend regulation to these sales of travel insurance, and is seeking views on three options:
 - **no statutory regulation** of sales of travel insurance sold as part of a package;
 - **FSA regulation** to cover these sales in the same way as stand alone sales of travel insurance;
 - **industry specific regulation**, requiring sellers of these products to be authorised by the FSA unless they are subject to an ABTA code which would be certified by the FSA. Sellers who were subject to the ABTA code but who also carried on other FSMA regulated activity, including selling any insurance other than packaged travel insurance, would be subject to FSA authorisation in relation to all of their regulated activities (including the activities to which the ABTA code applied).
6. The Directive similarly provides an exclusion for *extended warranties* provided certain conditions are met, including that the warranty is for less than €500 (about £300) per annum. Whilst most *extended warranties for motor vehicles* will be covered by the Directive, those with a value of less than €500 are excluded. However the Government intends that the new regime should cover all extended warranties for motor vehicles, including

those which fall below the exemption threshold of €500. This is to avoid market distortions which might occur if some warranties for motor vehicles were regulated and some were not.

7. Various concerns about *extended warranties of domestic electrical appliances* have resulted in the Office of Fair Trading (OFT) asking the Competition Commission to investigate this market. The Commission expects to report in the second half of 2003. The Government intends to postpone a decision as to whether extended warranties for electrical goods and other goods such as jewellery and carpets should be subject to regulation by the FSA until after the Competition Commission reports.
8. For more details on the scope of regulation, see *Chapter 2*.

Which activities will be regulated?

9. The Government intends to give the FSA responsibility for regulating the following activities:
 - introducing, proposing or carrying out other work preparatory to the conclusion of contracts of insurance;
 - concluding contracts of insurance; and
 - assisting in the administration and performance of such contracts, in particular in the event of a claim;
10. However claims handling on behalf of insurance companies, expert appraisal and loss adjusting are excluded from the activities the Directive requires us to regulate. The Government does not intend to bring these activities within the scope of FSA regulation.
11. For more details on the activities to be regulated see *Chapter 3*.

Who will be regulated?

12. Individuals, partnerships or companies who want to carry on insurance mediation activity “by way of business” will have to apply to the FSA in order to be “authorised” to do so. The FSA will be consulting on the

requirements for authorisation shortly. Firms already authorised by the FSA for other regulated activities who want to carry on insurance mediation activity “by way of business” will need to apply to the FSA for a variation of their permission.

13. The Directive does not require regulation of ***direct sales by employees of insurance companies***. However the Government intends to regulate mediation activities carried on by employees of insurers in order to ensure clarity for the consumer and to avoid creating an unlevel playing field between insurers and intermediaries.
14. ***Appointed representatives*** of FSA authorised persons can carry on regulated activities without being authorised provided the authorised person has accepted responsibility for the conduct of those regulated activities. The Government intends to apply the appointed representatives regime to insurance mediation with the necessary modifications to make it compatible with the requirements of the Directive.
15. Members of ***Designated Professional Bodies*** (DBPs), such as accountants and solicitors can carry on certain regulated activities where those activities are incidental to their main profession, without being authorised by the FSA. Such persons must comply with the rules of their DPB. The Government intends to apply this regime to insurance mediation activities with the necessary modifications to make it compatible with the requirements of the Directive.
16. For more details on who will be regulated and how, see *Chapter 4*.

What will the requirements of regulation be?

17. Most individuals or companies who want to carry on insurance mediation activity by way of business will have to apply to the FSA in order to be “authorised” to carry on such business. In order to become an “authorised person” various requirements have to be met including being a “fit and proper person”.
18. The FSA will require those carrying on insurance mediation activities to ***disclose to the customer certain information*** prior to concluding, amending

or renewing a contract of insurance. The Directive imposes certain minimum pre-sale information requirements but it will be open to the FSA to adopt additional safeguards. The Directive requires the UK to set up procedures allowing customers and other interested parties (including consumer associations) to *register complaints* about insurance and reinsurance intermediaries. The Directive also requires the UK to take measures to protect customers against the inability of the insurance intermediary to transfer the premium to the insurance undertaking, or to transfer the amount of claim or return premium to the insured. It will be for the FSA to implement these provisions.

19. The Government intends to make insurance mediation activities regulated activities under FSMA, which means that a person who carries on these activities without being authorised or exempt would commit a criminal offence¹.
20. The FSA has a range of sanctions against authorised persons including the ability to issue fines, and statements of public censure. Authorised persons can challenge the decisions of the FSA in the Financial Services and Markets Tribunal (“the Tribunal”).
21. For more details on the requirements of regulation, see *Chapter 5*.

Draft legislation

Annex D contains draft legislation to implement the Government’s approach.

Regulatory Impact Assessment

Annex E contains the draft Regulatory Impact Assessment setting out the expected impact, costs and benefits of regulating insurance mediation activities.

¹ See Section 19 of the Financial Services and Markets Act 2000.