

## The sun sets on exemption for travel firms: FSA regulation of connected travel insurance

June 2008

**From 1 January 2009, the FSA's regulatory regime will be extended beyond the sale of travel insurance as a standalone product, to cover the sale of travel insurance alongside holidays and other travel products (connected travel insurance or "CTI"). The "travel exemption", routinely relied on by travel agents, airlines, tour operators and other travel service providers that have for years packaged travel insurance with the travel products and services offered, will be replaced by a much narrower exemption. This will obviously have a significant impact on such travel firms, who will need to consider whether to apply for FSA authorisation, an option that will become available from 30 June 2008.**

In order to assist travel firms in deciding how deal with the impact of the new regulations, this article summarises: the scope of the new regulations, the regulatory options available to travel firms, and some of the key regulatory obligations to be borne in mind.

### The scope of regulation

The new rules require that any person that carries on insurance mediation activities in relation to CTI contracts i.e. arranges, advises on, or administers CTI contracts for their customers, must be FSA authorised, or exempt.

A CTI contract is, to give it its full definition: "*a non-investment insurance contract which covers the risk of damage to, or loss of, baggage and other risks linked to the travel booked with the provider*". Excluded from the definition are the narrow circumstances where: "(A) *the travel booked with the provider relates to the 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 a small business; or (B) the travel booked with the provider is only the hire of an aircraft, vehicle or vessel which does not provide sleeping accommodation*".

Consequently, the new regulation will bite on the sale of virtually all travel insurance products commonly sold by travel firms. By contrast, car hire is explicitly excluded from the scope of regulation.

### The regulatory options for travel firms

Each travel firm will need to ask itself if it will in fact be carrying on insurance mediation activities in relation to CTI contracts. If the answer to this is "yes", then it will need to consider how it will position itself in the regulatory scheme. It can choose to: (1) become an FSA authorised firm; (2) be "exempt" by becoming an Appointed Representative ("AR") or an Introducer Appointed Representative ("IAR") of an FSA authorised firm; (3) become an Unregulated Introducer; or (4) simply cease to offer CTI. The decision it makes will determine what it is entitled to do, but also what regulatory burden it will be under.

### FSA authorised firms

As well as the authorisation application fee of GBP 1,500<sup>1</sup> and subsequent annual fees, an FSA authorised firm will be required to comply with the full panoply of the FSA's rules. In particular, it will need to comply with the FSA's Principles for Business, establish and maintain appropriate internal systems and controls, comply with prudential rules requiring a minimum level of capital and appropriate professional indemnity insurance arrangements to be put in place, and report to and notify the FSA of specified events and circumstances. It will be required to obtain FSA approval for certain of its employees (and those of its ARs, if applicable) under the FSA's approved persons regime, establish and maintain the required complaints and redress procedures, and contribute to and become a member of the Financial Services Compensation Scheme and the Financial Ombudsman Service. The obligations are, then, onerous and expensive.

<sup>1</sup> There is a 30% discount for firms that apply for FSA authorisation on or before 30 September 2008.

## Appointed Representatives

Becoming an AR or IAR will be seen by many travel firms as a far preferable alternative to obtaining FSA authorisation. An AR effectively has the freedom to do anything its FSA authorised principal may do. An IAR is much more limited in what it is permitted to do. It can only effect introductions and distribute non-real time information (e.g. leaflets). IARs cannot take premiums from their customers, assist customers in filling in application forms (as this may constitute "arranging"), or give advice on what CTI policy to take out. An IAR can, however, pass customer contact details to its FSA authorised principal.

An AR/IAR's relationship with the FSA authorised firm will be governed by a contract containing certain prescribed terms governing the AR/IAR's and the firm's respective responsibilities in relation to the mediation of CTI contracts. Importantly, the FSA authorised firm will be responsible for ensuring that the AR/IAR complies with the applicable FSA rules.

## Unregulated Introducers

An Unregulated Introducer will escape the bite of the regulation entirely, although the scope of what it is permitted to do is even more limited. It can display generic travel insurance leaflets in its outlet, or include generic information about travel insurance in its brochure or website. It can also state, in a generic manner, that customers should take out travel insurance. In addition, it can include a travel insurance application form in its brochure or website as long as the application forms are then sent by the customer to an FSA authorised firm. Unregulated Introducers can insist on customers taking out insurance that is comparable to that in its brochure or website as a condition of booking a particular holiday.

## Conduct of business

All travel firms that decide to obtain FSA authorisation to carry on insurance mediation activities in relation to CTI contracts (either directly to a customer or via an AR) will need to consider their compliance with the FSA's Insurance Conduct of Business Rules ("ICOBS"). ICOBS sets out rules and guidance relating to the entire sales process, including communications with

customers, provision of information about the firm, its services and remuneration, the identification of the customer's needs advising the customer accordingly, provision of product information, distance selling, cancellation, and claims handling. Notably, however, certain of the status and scope of service disclosure requirements do not apply in relation to CTI contracts.

## Financial promotions

All travel firms should be aware that documents relating to CTI (e.g. any promotional material or application forms in a brochure or on a website) are likely to be considered to be a financial promotion. Financial promotions must be clear, fair and not misleading, and would need to be approved by an FSA authorised firm before being distributed to customers.

## Passporting

Notably, because insurance mediation activities in relation to CTI contracts do not fall within the scope of the Insurance Mediation Directive, such permission to carry on such activities cannot be passported into other EU member states.

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