One possible means by which this can be mitigated is to attempt to agree that a certain amount of costs can be incurred without prior consent in emergency situations. The alternative is to leave the effectiveness of the cover dependent upon the insurers' response time – a somewhat uneasy state of affairs.

> "The alternative is to leave the effectiveness of the cover dependent upon the insurers' response time – a somewhat uneasy state of affairs"

### The Companies Act 2004

This is a significant piece of legislation which requires all directors to give careful consideration to the scope of the protection they have via corporate indemnities and D&O insurance.

In overall terms, the most significant impact of the Act upon D&O insurance may be in the allocation of losses between Side A and Side B. For instance, the Act permits companies to advance defence costs to directors as and when they are incurred, subject to the ability to recoup in certain circumstances. On one level this might be seen as an answer to the 'prior approval' issue discussed under the previous heading. From a director's perspective that may be true. However, from the company's perspective it merely transfers the potential for cover for defence costs into Side B. Prior approval for incurring costs will still need to be sought if the company is to recover from insurers its advancement of those costs to the director. However, even if it overcomes that hurdle, the company will only recover to the extent that those costs exceed the deductible. In this instance, the combination of the Act and standard form D&O cover may leave companies more financially exposed than they were before.

The Act also serves to underscore the critical importance of the Insured vs Insured provision of policies given the Act's clear prohibition on any form of corporate indemnity against certain breaches of duty to the company. Given this, and given the potential problems with the approach of policies to claims arising from such breaches (as identified in the first part of this article), policy wordings need to be revisited in light of the Act in order to ensure that the directors have the comfort they need. Some renegotiation of policy terms may be required if that is to be achieved. Both insurers and insureds may need to reconsider the issues to be balanced when it comes to such cover, and look to new wordings to express better the cover (for insureds) and the safeguards (for insurers) which are required. ●

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# Insurance mediation – is it time to register?

## New rules mean many companies must register with the FSA, says Jennifer Donohue*

The Financial Services Authority (FSA) has recently assumed a new role as regulator for insurance mediators. Many companies which currently sell, arrange or advise on insurance policies in the UK are having to chose whether to become regulated under the FSA or to scale down their activities.

*The Times* recently expressed its concerns about the number of insurance providers who had failed to apply for authorisation by January 14. It highlighted the number of companies which should have applied for authorisation but had failed to do so.

Firms which continue to sell or arrange insurance without the required authorisation could face criminal penalties including fines and, in the worst cases, individuals involved could face imprisonment.

Our experience in this field is that the failure to register is not an attempt to evade regulation. Many businesses have found it difficult to judge whether they need to be authorised, market rumour has been misleading or they are not aware that the new regulations even exist.

This is not surprising given the nature of many of the businesses which are caught by the new regulations. Many are providers of day-to-day consumer goods and services who also advise on related insurance cover. Examples are storage companies, removal firms, mobile phone companies, medical practitioners and vets. Most have never had to deal with a regulator before or get to grips with a compliance regime.

The regulations apply in a broad range of areas. For example, firms cannot arrange or advise on insurance on behalf of a customer unless authorised. 'Arranging' effectively includes anything which may lead to someone entering into an insurance policy. It catches administrative activities such as making telephone enquiries on a customer's behalf.

Firms cannot handle an insurance claim on behalf of a customer unless authorised. A storage company which experiences a fire in its warehouse would be unable to complete the paperwork for a claim in respect of a customer's damaged possessions unless authorised.

The regulations have attempted to address this problem with certain exemptions. If a business is looking to rely on an exemption, this needs careful planning and constant monitoring.

Retailers who are selling warranty products covering their own goods and services (other than motor warranty insurance) and travel agents offering travel insurance as part of holidays may not need to be authorised, subject to specific criteria.

Businesses may provide a means by which customers and insurance companies may communicate (for example, by operating an internet portal) without authorisation.

Businesses are also exempt from authorisation if they do no more than provide generic information to a customer about types of insurance cover and this is ancillary to the business' main activity. The scope of 'ancillary' can be uncertain. Businesses need to be careful they do not slip into advising customers about specific insurance products.

In practice it is by no means clear how to avoid crossing the line. Suppose you are a vet who wants to be able to tell your customers about pet insurance. If you tell a customer that you have a policy available, this constitutes making 'arrangements'. In theory, if all you do is display leaflets about pet insurance in your practice, you will not need to be authorised. But you will still need to be careful that you are not implicitly adding your own endorsement to a particular product. If you did allow insurance companies to advertise at your offices, you would need to make sure it is clear it is their advertisement and do not change their advertising copy in any way.

According to guidelines, a business can give an opinion on whether a customer should take out insurance cover but not on which product.

Exemptions to the regulations are limited. There are significant grey areas, particularly while the regulations are new, and the penalties for a wrong decision are high.

If a business chooses to become authorised, the new regulatory regime can be expensive to implement and the learning curve is steep. Some matters they have to consider include maintaining professional indemnity insurance and a minimum level of capital resources. Their workforce must be large enough and sufficiently qualified to carry out authorised activities. Individuals who will carry out certain high level functions must first be vetted by the FSA. Certain management controls must also be put in place including adequate procedures for handling customer complaints.

An alternative to becoming authorised is to become an appointed representative of a firm which is authorised. We have found some firms are reluctant to chose this option, however, including because they are concerned that it may in practice tie them to a specific insurer.

**"An alternative to becoming authorised is to become an appointed representative of a firm which is authorised"**

As a final option, we have been involved in exploring with several businesses the possibility of setting up their own insurance companies. When an insurance intermediary becomes FSA regulated, this can result in new capabilities which could equally be directed towards providing insurance themselves. This option can be lucrative. ●

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