CIC BUILT ENVIRONMENT PROFESSIONS TOGETHER

Risk Management Briefing

Advising on insurance

June 2017

Introduction

Professional advisers, be they individuals or large consulting practices, operating in the built environment will be familiar with the services of insurance brokers and insurance companies as such advisers will regularly engage with insurers and brokers to consider and acquire cover for their own professional activities. However, what may not be appreciated is that some insurance-related activities that a professional adviser may undertake could be “regulated activities” subject to the Financial Services and Markets Act 2000 (FSMA).

“Regulated activities” in the insurance sector can range from effecting and performing contracts of insurance (i.e. the service provided by an insurance company) to participating in the insurance marketing and sales process, so called “insurance mediation activities”[1]. This briefing note is primarily focused on insurance mediation activities as it is those that are most likely to catch out people or organisations advising on insurance matters as a seemingly-minor part of the other services that they would usually perform.

The General Prohibition

Under FSMA rules no person may carry on a regulated activity by way of business in the UK unless they are authorised or exempt under the Act. Breaching this so-called “general prohibition” is a criminal offence.

[1] Used as a defined term in the Financial Conduct Authority (FCA) Handbook of rules and guidance for the industry. Providers of such services are commonly referred to as "intermediaries" and so we often refer to "intermediary activities".

Due to the severe consequences that can arise from violation of the general prohibition, it is important to understand when a regulated activity may take place. Making this assessment is a tricky exercise, not least because of some of the grey areas between specific parts of the legislation or because of the range of specific exclusions that are available. Legal advice should be sought based on the particular facts applicable in each case. In all cases it is necessary to consider the following questions with respect to any particular activity:

- Does the activity concern a "specified investment"[2]? The legislation lists a number of types of investment, including insurance contracts, which constitute specified investments.

- Is the activity included in the list of regulated activities? An overview of the key insurance mediation activities is set out below.

- Does the activity take place in the UK? The FSMA regime only applies to activities carried on in the UK and whilst this can often be easy to answer, the use of different teams within a multinational corporation can sometimes lead to difficulty in determining where an activity actually takes place.

- Is the activity undertaken "by way of business"? Only activities performed by way of business will be subject to the FSMA regime and, in respect of insurance mediation activities, this means activities in respect of which some form of remuneration is received (direct or indirect) and that are otherwise pursued as a business. This is clearly the case for an insurance broker but may apply, for example, to a contract administrator who is advising on the appropriate type and amount of insurance as part of the overall services for which the contract administrator is paid.

- Do any of the statutory exclusions apply? The legislation contains a wide range of exclusions which allow certain activities (which would otherwise be regulated), some of which are discussed below, to be performed in certain circumstances without falling foul of the FSMA regime.

Insurance Mediation Activities

The Regulated Activities Order (RAO) sets out six "regulated activities" that are considered to comprise insurance mediation activities:

- dealing in investments (in this case, contracts of insurance) as agent (RAO, Article 21);

- arranging (bringing about) deals in investments (Article 25(1));

- making arrangements with a view to transaction in investments (Article 25(2));

- assisting in the administration and performance of investments (Article 39A);

[2] There is a whole part of the Regulated Activities Order dedicated to "specified investments. This term is also used by the FCA in its Handbook and FSMA refers to "investments of a specified kind" in s.22

- advising on investments (Article 53); and
- agreeing to carry on any of the above activities (Article 64)

By way of example only, the following activities are likely to constitute one or more of these activities:

- helping potential policyholders complete applications for insurance;
- introducing potential policyholders to:
    - another intermediary for advice or other help in arranging a policy; or
    - an insurer for the provision of a particular type of policy;
- assisting a policyholder to complete an insurance claim form and so help the policyholder to perform its obligation under the policy to notify the claim;
- advising a policyholder or potential policyholder on a particular contract of insurance, by providing an opinion or other advice on the merits of such person or organisation taking out a specific contract of insurance;
- as a contract administrator, advising the employer on the suitability of designers' and contractors' insurances.

One exclusion, which is available under the RAO, and which is particularly relevant to people or organisations whose main business does not involve regulated activities, applies to arranging activities and assisting in the administration and performance of a contract of insurance. This exclusion applies when such activity is provided by a person carrying on a business which does not otherwise consist of regulated activities and the activity amounts only to the provision of information which may reasonably be considered to be incidental to that business.

The Financial Conduct Authority (FCA) guidance describes "incidental" as meaning it "arises out of" or is "complementary to" the business of the persons seeking to rely on the exemption. For example, an architect introducing buildings insurance to its clients may be considered to be "incidental" to their business, whereas introducing motor insurance would not.

Please note that many other exclusions may be available based on the specific circumstances and it is not possible to cover all these in this briefing note.

Becoming authorised or exempt

Where activities are regulated and no exclusion exists a person or organisation may decide that it is necessary to obtain appropriate authorisation from the FCA to perform the relevant activity. In order to become authorised, it is necessary to satisfy the FCA's "threshold conditions" (which include having appropriate financial and non-financial resources and being suitable to be a regulated firm).

An alternative to authorisation is to become an exempt person for the purposes of the FSMA regime and there are two key ways in which a professional adviser operating in the built environment may become exempt:

- The first way is by becoming appointed as an authorised person's "appointed representative" e.g. becoming an agent of an authorised person such as an insurance company and in circumstances in which the authorised person accepts regulatory responsibility for the agent's acts and omissions. However, in most cases this would be impractical.

- The second way may apply if an adviser can take advantage of the "professional services exemption", which is available for members of professional bodies that have become "designated professional bodies" by order of the Treasury. At present, the list of designated professional bodies includes the Royal Institute of Chartered Surveyors (but not the Royal Institution of British Architects or the Institution of Civil Engineers). This allows members of RICS to carry on certain regulated activities without being authorised where those activities are incidental to their unregulated business activities and where such RICS members do not receive remuneration for their services other than from their client. In addition, in respect of "insurance mediation activities", the adviser must also be included on the FCA's register as an exempt professional firm.

It should be noted that the routes to achieving exemption from the rules are quite complex and there are multiple factors which must be taken into consideration before choosing this route as a means of navigating the general prohibition under FSMA rules.

Advising on insurance

Assuming the advice provided on insurance comes within the available exemptions or is provided by an authorised person, it is still necessary to ensure that such advice is correct and appropriate in the circumstances. Insurance is a specialist area and is subject to a separate body of laws, regulations and principles which cover areas such as the effect of joint names insurance, notification and disclosure obligations and subrogation rights.

Where a professional adviser – say, an architect or consulting engineer – performs services that include advising on insurance contracts, it is important that this is disclosed to that adviser's insurers, as it may be that the adviser needs additional wording to cover activities that are outside the usual scope of such an adviser's business. Negligence in the performance of an adviser's activities can, of course, be covered by insurance and this includes the performance of regulated activities (although such a policy would normally require that the company is appropriately authorised or exempt).

It should be noted that insurance will not be available to cover regulatory fines issued by, e.g. the FCA, but that the insurance may cover costs of defence or civil awards in the event of a finding of negligence.

Forthcoming changes to the regulation of insurance distribution

With effect from 23 February 2018, the UK will be required to comply with the EU Insurance Distribution Directive (IDD). This Directive replaces the Insurance Mediation Directive (IMD), upon which the regulatory regime described in this note has been built. The UK chose to gold-plate a number of the IMD requirements which means that much of the change being introduced on a Europe-wide basis by the IDD will be consistent with existing UK rules, but there are some specific changes, including in respect of activities that will and will not be regulated in future, that will impact on the UK market and may be of relevance to advisers in the built environment.

This Risk Management Briefing is for general guidance only and legal advice should be sought to cover any particular situation.

This briefing was originally compiled by Chris Riach of Pinsent Masons in conjunction with the CIC Liability Panel.

It is available at www.cic.org.uk

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