

The complaint

Mr W complains about the value of a claim for fire damage under his leisure home insurance policy from his insurer, American International Group UK Limited (AIG).

References to AIG include their agents who administer the policy and handle claims.

What happened

Mr W had a caravan on a static caravan park, insured through a home and contents policy underwritten by AIG. The policy was on a 'new for old' basis with the caravan insured for a buildings sum of £25,500. In April 2021 there was a fire in an adjacent caravan that caused damage to Mr W's caravan. Mr W contacted AIG to make a claim for the damage. AIG appointed loss adjusters, who visited the site and agreed the damage was covered under the policy. The damage was estimated at £14,955 and based on this AIG assessed the caravan to be economically repairable.

However, the loss adjusters estimated the 'new for old' value of the caravan was likely to be about £50,000. As the buildings sum insured was £25,500 AIG thought this meant Mr W had under-insured. So, they told Mr W they'd only pay for a proportion of the estimated cost of repairs. Mr W challenged AIG's view, saying the retail cost of an equivalent new caravan to his own was in line with the sum insured. He said the difference was a result of the profits charged by the management of the caravan site for the caravan being on their site. As this element wasn't included in the cost of purchase from the caravan manufacturer, he thought AIG should cover the full estimated cost of repairs.

AIG considered Mr W's view but rejected it. In their final response they said Mr W had been advised on several occasions that the insured value was too low for a 'new for old' policy, but he hadn't reflected the additional costs of having a caravan on the site. AIG went on to say the policy terms and conditions made it clear that if a policyholder is under-insured, then the full value of a claim might not be paid.

Mr W then complained to this service. He maintained his view that he wasn't under-insured, based on the replacement cost of a new caravan from the manufacturer. Different sites would charge different amounts for a caravan bought on-site. He also said the policy didn't say that 'new for old' replacement was dependent on the specific site the caravan was located and the policy was insuring the replacement cost of the caravan (not the value including the pitch it was located on). He said he'd been affected financially by being unable to use the caravan - but he was still having to pay the fees for the pitch. He also said the stress and anxiety had affected his wife's health. He wanted AIG to cover the full estimated cost of repair to his caravan and to compensate him for the stress and anxiety, together with the loss of use of his caravan.

Our investigator upheld the complaint in part. On the issue of whether the caravan had been under-insured, he thought a 'new for old' policy was intended to provide an equivalent caravan in the same location. That would be higher than the simple replacement cost from the manufacturer. Based on this, he thought Mr W was under-insured. The investigator also thought Mr W had made a careless misrepresentation under the Consumer Insurance

(Disclosure and Misrepresentation) Act 2012 (CIDRA) when he based the insured sum on the replacement cost from the manufacturer. The investigator thought this meant AIG acted fairly in offering a proportionate reduction of the claim value.

However, the investigator didn't think AIG had fairly calculated the proportionate reduction. That's because they calculated the proportion based on the ratio of the sum insured (£25,500) to the 'correct' sum insured (estimated at £50,000). That meant a figure of 51%, when applied to the estimated repair cost of £14,955 gave a figure of £7,627 (less the policy excess). However, the investigator thought AIG should have calculated the reduction based on the ratio of the actual premium paid (£170.93) compared to the 'correct' premium (for the 'correct' sum insured). Information from AIG indicated the 'correct' premium should have been £246.96 (meaning Mr W had paid 69.2% of the 'correct' premium). So, Mr W should have received 69.2% of the estimated repair cost (£10,351 less the policy excess).

AIG disagreed with the investigator's conclusions and requested an ombudsman review the complaint. They said they'd acted correctly in basing the proportionate reduction on the ratio of the sum insured to the 'correct' sum insured. They also disagreed with the investigator's view the claim should be settled in line with CIDRA, given they'd contacted Mr W on several occasions about the sum insured being too low. They also said they'd told Mr W of the consequences should he be under-insured.

What I've decided – and why

I've considered all the available evidence and arguments to decide what's fair and reasonable in the circumstances of this complaint.

My role here is to decide whether AIG have acted fairly towards Mr W.

The key issue in this complaint is whether AIG acted fairly in applying a proportionate reduction to the claim for damage from Mr W. Following on from this – if AIG acted fairly in applying a proportionate reduction - there's the issue of how the reduction should be calculated. I've noted Mr W accepted the view of our investigator, that he was under-insured. I've also noted AIG, in disagreeing with the investigator's view, challenged the issue of how the proportionate reduction should be calculated. While it seems the second issue is therefore the more important one here, I have considered both issues.

When making his complaint to this service, Mr W said he'd used a replacement cost for an equivalent caravan from the manufacturer. Referring to their website, for a model with the same floor plan as his caravan, he noted a replacement cost of £24,600 (which is close to the £25,500 figure he used as the sum insured). He also argues the policy didn't say that 'new for old' replacement was dependent on the specific site the caravan was located and the policy was insuring the replacement cost of the caravan (not the value including the pitch it was located on). AIG say Mr W had been advised on several occasions the insured value was too low for a 'new for old' policy, and he hadn't reflected the additional costs of having a caravan on the site.

I've considered both views carefully, including the information and evidence provided. On balance I agree with AIG. In coming to this conclusion I've noted what AIG have provided about the information provided when the policy was taken out and how to provide the appropriate figure for the sum insured (both for policies based on 'market value' and those on a 'new for old' basis, as was the case with Mr W's policy. I've also noted the definition of "New for Old" in the policy document:

"The cost of replacing the Home with its brand new equivalent in the event of total loss taking into account fees and associated costs as applicable."

Looking at this, I think it's clear that the figure isn't just the 'brand new equivalent' (from the manufacturer (as Mr W sees it). I think it's reasonable to take the definition to include the additional costs of locating the home (the caravan) on the site where the caravan was located (the pitch). Based on this, I've concluded Mr W was under-insured under the 'new for old' basis of his policy.

Having come to this conclusion, I've also looked at whether it was clear to Mr W what the consequences of being under-insured would be. AIG say it was clear that under-insurance would mean a proportionate reduction in the value of a claim for damage or loss. They've referred to what the Insurance Product Information Document (IPID) contains. It includes a statement under the heading *Are there any restrictions on cover?* that says:

"If the sum insured is less than the full replacement cost, we will pay the same proportion of the loss or damage as the sum insured bears to the full replacement cost"

Together with separate letters to Mr W saying the sum insured looked low and consequently should he need to make a claim he would be unlikely to receive sufficient funds (to replace his caravan), I think it was clear what the consequences of under-insurance would be.

Having reached these conclusions, I've then considered the second issue of the basis of the proportionate reduction.

Our investigator thought Mr W had made a careless misrepresentation under CIDRA when he based the insured sum on the replacement cost from the manufacturer. AIG disagree with that view and that the claim should be settled in line with CIDRA, given they'd contacted Mr W on several occasions about the sum insured being too low. They also said they'd told Mr W of the consequences should he be under-insured.

I've considered this point carefully. CIDRA requires consumers to take reasonable care not to make a misrepresentation when taking out (or renewing) a consumer insurance contract (a policy). The standard of care is that of a reasonable consumer. If a consumer fails to do this, the insurer has certain remedies provided the misrepresentation is - what CIDRA describes as - a qualifying misrepresentation. For it to be a qualifying misrepresentation the insurer has to show they would have offered the policy on different terms or not at all if the consumer hadn't made the misrepresentation.

CIDRA sets out a number of considerations for deciding whether the consumer failed to take reasonable care. And the remedy available to the insurer under CIDRA depends on whether the qualifying misrepresentation was deliberate or reckless, or careless.

Given my conclusion that Mr W should have been aware that he was under-insured (despite AIG contacting him about the issue) then I think he failed to take reasonable care when providing the sum insured figure he did. From what AIG have said, had Mr W provided a 'correct' sum insured figure they'd still have provided cover – but charged a higher premium. Based on this, I'm satisfied Mr W made a qualifying misrepresentation.

Mr W says he provided what he thought was an appropriate sum insured based on the cost of a replacement caravan from the manufacturer. While AIG wrote to Mr W to query the amount (as they thought it looked low for a 'new for old' policy) they haven't said why they consider CIDRA doesn't apply. In the circumstances, I think his misrepresentation should be treated as careless (rather than deliberate or reckless). Under the latter two categories, AIG would have been entitled to avoid Mr W's policy (that is, treat it as though it had never existed) and decline his claim in full (which they haven't done).

As I'm satisfied Mr W's misrepresentation should be treated as careless, I've looked at the remedies available under CIDRA. CIDRA states where there's a careless misrepresentation the insurer may still avoid the policy where it wouldn't have offered the cover at all. But as AIG would have offered cover (albeit at a higher premium) this isn't applicable.

As AIG would have offered cover (at a higher premium) then CIDRA provides for the insurer to apply a proportionate reduction based on the proportion of the premium the policyholder paid compared to what they should have paid. Given what I've said about Mr W making a misrepresentation, I've concluded that AIG should follow the principles of CIDRA when applying a proportionate reduction – rather than applying the terms of the policy by basing the proportionate reduction on the ratio of the actual sum insured to the 'correct' sum insured. That is, CIDRA should take precedence over the terms of the policy.

As the premium paid by Mr W was £170.93 and the 'correct' premium AIG would have charged - had the 'correct' sum insured been provided – is £246.96 then the proportionate reduction should be 30.8%. Applying this proportion to the estimated repair cost of £14,955 gives a proportionate reduction of £4,604. That is, Mr W should receive £10,351 (less the policy excess).

My final decision

For the reasons set out above, it's my final decision to uphold Mr W's complaint in part. I require American International Group UK Limited AIG Insurance plc to:

- Settle Mr W's claim on the basis of a proportionate reduction of 30.8% (£4,604) of the estimated repair cost of £14,955 (less the policy excess).

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr W to accept or reject my decision before 2 June 2022.

Paul King
Ombudsman