

The complaint

Mr P complains that Society of Lloyd's has unfairly settled his claim on his residential let insurance.

What happened

Mr P had insurance for a property he owns and rents out that is underwritten by Lloyd's. He took out the policy through a broker.

In June 2020 he made a claim on the policy after he discovered an escape of water at the property and malicious damage caused by the tenants. Lloyd's sent someone out to investigate and accepted the claim. However it said the sum insured for the property wasn't a reasonable estimate. And it said the tenants were in receipt of housing benefit and this hadn't been declared when the policy was taken out. Lloyd's said that if both of these had been declared then it would have charged a total of 70% more for the policy. And due to this it said it would reduce the settlement by 70%, in line with the relevant law. This amounted to a settlement of £2,178.

Mr P didn't think this was fair. He said he'd based his estimate for the sum insured on the selling price of a similar property and didn't realise this was different to the re-build cost that was required. He also said he hadn't been asked about whether his tenants were in receipt of benefits so didn't agree he'd given incorrect information. He made a complaint.

Lloyd's didn't uphold the complaint so he brought it to this service.

After the complaint came to us, Lloyd's reassessed the settlement it had offered. Instead of reducing the settlement by 70% overall, it assessed the escape of water and malicious damage claims separately. It then applied the 'average clause' in the policy that allows it to reduce the settlement based on the amount the property was underinsured by. This resulted in a revised settlement offer of £3,368.04.

Our investigator considered the issues and agreed that as Mr P hadn't made a fair presentation of the risk when he took out the policy, then it was fair for Lloyd's to reduce the settlement paid proportionately as this is in line with the relevant law. However she didn't think it was fair for Lloyd's to apply the policy limit for malicious damage of £5,000 before calculating the settlement, but thought instead this would apply after. So she thought Lloyd's should pay the settlement without applying the policy limit first.

Lloyd's didn't accept the outcome. It said it didn't agree the policy limit should be applied after the calculation. Mr P accepted the outcome but didn't agree with it. He said it wasn't clear that the amount he was being asked for in answer to the sum insured was the rebuild cost rather than the value and he said he had never been asked about his tenants' benefits. So he didn't think it was fair he was penalised so strongly for giving wrong information when he didn't realise he was.

As agreement hasn't been reached, the complaint has come to me to decide.

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.

Lloyd's has said that Mr P was underinsured, as the value of the property covered by the policy was less than it should have been. Because of this, it's said it will apply the average clause in the policy and offer a proportionate settlement. It's also said that it would have charged more for the policy if it had known that the tenants were in receipt of benefits, so it reduced the settlement further because of this.

I can see the policy contains a term that allows Lloyd's to settle claims on a proportionate basis where underinsurance has occurred. However as this dispute has arisen due to the information that was provided when the policy was first taken out, I think it's fair to first consider whether Mr P fulfilled his duty under the relevant law. Mr P's policy is a commercial one so the law that applies here is the Insurance Act 2015.

Under the Act a commercial customer has a duty to make a fair presentation of the risk to the insurer. In order to fulfil a fair presentation of risk, the Act says a commercial policyholder must disclose everything they know, or ought to know, that would influence the judgment of an insurer in deciding whether to insure the risk and on what terms. If it is found that they didn't fulfil this duty then in order to say there has been a qualifying breach, the insurer needs to show that it would have either not offered the policy at all, or offered it on different terms.

Here Lloyd's has said Mr P failed to make a fair presentation of the risk with two bits of information provided when the policy was taken out – the sum insured and the fact the tenants were receiving benefits. So I'll consider each in turn.

Sum insured

Mr P estimated this to be £75,000 while Lloyd's say a reasonable estimate is £120,000. Mr P has said he wasn't aware that the sum insured represented the rebuild cost rather than the sale price, and because of this misunderstanding he used the price of a similar property that had sold in the area.

Mr P bought the policy through a broker, so he would have been provided with the information about the policy by them. However Lloyd's are responsible for providing enough information to make it clear to the broker what will influence its judgement when assessing the risk.

I've looked at the documents provided. The statement of fact shows details of the information Mr P has provided when taking out the policy and would have been given to Mr P directly at inception. It states as follows:

'You must take reasonable care to provide complete and accurate answers to the questions we ask when you take out, make changes to or renew your Policy. If you fail to do so, your Policy may be void, or may be cancelled, or your claim may be rejected or not fully paid. If

you are in doubt as to whether you have answered any questions completely and accurately, you should check your records rather than guess'

It then goes on to say:

'If at the time of a loss the sum insured is only half of the amount required to fully cover all

the property, then we will only pay up to half of the claim, less any excess applicable. Sums insured must be enough to fully cover all the property, throughout the life of the policy including after each renewal. Otherwise a claim payment may be reduced by the application of average.

Please consider taking professional advice to help you set adequate sums insured, eg from a surveyor in respect of buildings insurance.

A guide to setting buildings sums insured is available from the BCIS website.'

From this, I think it would have been clear to the broker and Mr P that the information given at the point of taking out the policy is important and the particular importance of getting the sum insured right. The fact that the document highlights that guidance should be sought, suggests that it is likely to be a difficult number to calculate. The document also points to a website that would give Mr P an estimate for the sum insured.

Based on this, I think Lloyd's provided clear enough information to show what was required to provide a reasonable estimate for the sum insured. And as this document was not only provided to the broker but to Mr P directly when he bought the policy, I think he should have been aware that his estimate wasn't accurate and he hadn't made a fair presentation of the risk. So I agree he's made a misrepresentation according to the act.

Tenants

As part of the same document the following question is included:

'(c) to tenants receiving unemployment, housing or disability benefits? No'

Mr P has confirmed he was aware, and had agreed to, his tenants paying rent through housing benefits. And I think the statement of fact makes it clear that this information is something Lloyd's take into account when assessing the risk. I therefore think Mr P made a misrepresentation in not disclosing this information as well.

Qualifying breach

In order to determine if these amount to a qualifying breach under the Act, Lloyd's has provided details of the premiums it would have charged Mr P if he had made a full disclosure. Based on this I can see it would have charged a total of 70% more for the policy. I'm therefore satisfied that there has been a qualifying breach.

Under the Insurance Act, where an insurer has shown that it would have charged a higher premium if the correct information had been provided, it allows the insurer to settle the claim on a proportionate basis based on the proportion of premiums that were paid, compared to those that should have been.

Lloyd's originally offered a settlement based on the remedy outlined in the Insurance Act. However it has since offered a higher settlement by applying this combined with the average clause contained in the policy.

The Insurance Act allows firms to 'contract out' from the remedies in the act, as long as certain requirements are met that are called the 'transparency requirements'. This means it can provide a different remedy in the policy terms that isn't covered by the act if it makes this clear enough.

However this applies to where the term is disadvantageous to the customer. Here, Lloyd's

has shown that by applying the average clause, rather than just relying on a proportionate settlement based on the premiums as laid out in the act, the customer is in a better position than they would have been. I therefore don't need to consider whether it has met the transparency requirements as it hasn't disadvantaged the customer.

Based on this I think Lloyd's has acted fairly by reducing the claim settlement based on the proportion of the premiums paid and the average clause. And I won't interfere in its decision to do so.

Policy limit

As part of its calculations for the settlement for the malicious damage, Lloyd's has applied the policy limit before working out the proportion of the claim it will pay. As the full amount was over £6,000 and the policy limit for this section is £5,000.

However I don't agree this is a fair way to calculate the settlement. The policy limit applies as the policy won't pay out above that amount. And as the full value of the claim is not what Lloyd's will pay under the policy, due to the qualifying breach, it's not fair to reduce the claim amount based on that. If the reduced claim value (once the proportionate reduction is applied) was over £5,000 then I'd think it fair to reduce the amount paid based on this, as that's in line with the policy terms. But I don't think it's fair to apply the limit before this is calculated.

For these reasons, I require Lloyd's to recalculate the claim settlement without applying the policy limit before reducing the settlement proportionately.

My final decision

For the reasons I've given, I require Society of Lloyd's to:

- Pay the settlement based on its most recent offer, but without applying the policy limit for malicious damage before the proportionate settlement is calculated.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr P to accept or reject my decision before 10 November 2022.

Sophie Goodyear
Ombudsman