DRN-3859330

The complaint

Mrs C, a sole-trader, complains about the handling and settlement of her business interruption insurance claim, made as a result of the COVID-19 pandemic, by Hiscox Insurance Company Limited.

What happened

The following is intended merely as a brief summary of the relevant events. Also, whilst other parties have been involved, I've just referred to Mrs C and Hiscox for the sake of simplicity. Additionally, this complaint relates to more than one claim. Normally, we would consider complaints about separate claims, separately. However, given the circumstances involved here, I consider it is appropriate to consider this as one complaint.

Mrs C operates a hair salon business and held a commercial insurance policy underwritten by Hiscox. The policy covered a number of areas of risk, including loss of profit as a result of business interruption in certain circumstances. In March 2020, Mrs C was forced to temporarily close her business as a result of the government-imposed restrictions introduced because of the COVID-19 pandemic. She contacted Hiscox to claim for her losses.

Hiscox initially declined the claim. However, following the Supreme Court's judgment in the Financial Conduct Authority ("FCA") test case[1], Mrs C resubmitted the claim in January 2021. At this point, Mrs C claimed for losses that had commenced in March 2020 ("lockdown one") and in November 2020 ("lockdown two").

Hiscox paid Mrs C an interim settlement of £2,500 in March 2021 and then made its final settlement offer at the end of April 2021. The offer was £6,666 (less the £2,500 already paid) for lockdown one and £1,171 for lockdown two. Mrs C felt she should be paid around £24,000 and rejected the offer in early May 2021, making a complaint about it. It does not seem that Hiscox immediately acted on this, and it was not until November 2021 that it responded to Mrs C's complaint.

Hiscox did not change its decision though. It explained that Mrs C had failed to adequately insure her potential losses. It said that her profits in the 12 months prior to lockdown one were more than three times the sum she had insured. And Hiscox said that as a result of this the settlement was reduced by a 32.65% rate of underinsurance. Mrs C did not believe this was fair, but Hiscox said this was an issue that she would have to take up with her broker.

Hiscox also deducted the sums Mrs C had received from the Coronavirus Job Retention Scheme (known as "furlough") and the Self-Employment Income Support Scheme ("SEISS"), which Mrs C considered to be unfair as well. Hiscox said it considered these were savings against costs Mrs C's business would otherwise have had. Mrs C brought her complaint to the Ombudsman Service.

Mrs C also raised a complaint about the handling of her claim generally. Hiscox upheld this complaint, apologising for the delays and level of service received. Hiscox offered Mrs C

[1] *The Financial Conduct Authority & Ors v Arch Insurance (UK) Ltd & Ors* [2021] UKSC 1

£300 compensation for this. For similar reasons of considering both claims together in this complaint, I have also taken into account the customer service issues even though technically these were raised separately.

Since Mrs C brought her complaint to the Ombudsman Service, Hiscox has increased the offer for the claims and complaint, adding interest to the claim settlements and a further £200 compensation. The interest was calculated at a rate of 8% simple per annum from the dates payments ought reasonably have been made in relation to the claims up to the date of final settlement, taking into account interim payments made.

Our Investigator partly upheld Mrs C's complaint. She felt that the total of £500 compensation for the service-related issues and the offer of adding interest to the claim settlement was appropriate. She also thought that Hiscox had acted reasonably when reducing the claim settlement on the issues of underinsurance and furlough. But the Investigator did not think it reasonable to deduct the SEISS payments.

Hiscox did not agree that it was unreasonable to deduct the money Mrs C had received in SEISS payments from the claim settlement. Hiscox has made detailed submissions on this point, both directly on this complaint and in relation to other similar complaints. In summary, Hiscox has said that the furlough payments and SEISS payments are analogous and should be treated in the same way. Hiscox considers the SEISS payments are different to the other funding the Government had provided to small businesses during the lockdowns, so the position on these other grants did not mean SEISS should not be deducted from settlements. Hiscox considers that the SEISS payments are a form of income that were received by businesses, such as Mrs C's, and so reduced the size of their losses. And Hiscox pointed to the judgments in a number of court cases – which I will refer to below.

As Hiscox did not agree with the Investigator's opinion, this complaint was passed to me for a decision. On 21 June 2023, I issued a provisional decision. I explained my provisional findings as follows.

I said as Mrs C had not made any comments in relation to the parts of her complaint that were not upheld, I was minded to agree with the Investigator on these parts of the complaint, largely for the same reasons. I briefly set out my thoughts on these issues though.

Claim handling / service issues

I explained that Hiscox initially declined Mrs C's claim in 2020. It then did not act appropriately when Mrs C rejected the settlement offer and failed to respond to her on this for some months. However, Hiscox has accepted that it should have handled the claim better, and has offered Mrs C £500 compensation as well as interest on the claim settlement in line with what I would direct it to pay.

Parts of this offer were made after the complaint was referred to our Service. So, this is a change in the outcome of the complaint as it was made. But I considered Hiscox's full offer here to be reasonable and agreed it appropriately compensates Mrs C for the issues experienced.

Underinsurance

I said Mrs C took out her policy with Hiscox via a third-party broker. And has said that the broker did not explain certain aspects to her in terms of the amount she needed to insure. Whilst I appreciated this, I confirmed that if she is unhappy with an aspect of the sale of the policy Mrs C will likely need to raise this with her broker.

I explained that my role in this complaint is to consider whether or not Hiscox acted appropriately when dealing with the claim.

I said there are rules over what a customer and an insurer need to do where a policyholder may be underinsured. As a commercial customer, Mrs C was under a duty to make a fair presentation of risk at the time the policy was taken out. This means she needed to think about the risks her business posed to her insurer, and let them know about any relevant information. Whilst I noted the points she's raised about her understanding of this, I thought she ought to have appreciated that the size of her business and the level of profit it was making were things her insurer would likely consider important. So, she should have told Hiscox about these correctly.

Mrs C only insured her business for loss of profit for £50,000 for a 12-month period, even though it seems she generated over £150,000 per year in profit. And it does not appear she made Hiscox aware that the insured sum would not cover all of her potential losses. So, I considered Hiscox could fairly reduce the settlement payable on any relevant claim.

The Insurance Act 2015 sets out a mechanism for how this reduction might be calculated. The settlement reduction for underinsurance that Hiscox applied is in line with this. So, I considered this aspect of its settlement calculation was fair and reasonable.

Furlough and SEISS

This element formed the main discussion in my provisional decision. I explained that the Government provided financial support to businesses during the pandemic via a number of different schemes. These included furlough, SEISS and also a range of other grants - Local Authority Grant, the Small Business Grant and the Leisure/Retail/Hospitality grants, etc. Whilst there were differences between these 'other grants', for the sake of simplicity, I referred to them collectively as "business support grants".

I set out that, in 2020, the FCA, HM Treasury, a range of insurers and the Association of British Insurers, ("ABI") made a number of statements particularly in relation to these business support grants. They confirmed that how these grants were treated for tax purposes was not determinative of how they should be treated for insurance claims. And that, ultimately, insurers should not be deducting the amount of such grants from claim settlements. Hiscox has agreed not to deduct money received from business support grants from claim settlements.

However, no such statements were made by the FCA, Treasury or ABI in relation to furlough or SEISS. And Hiscox considers that payments through these schemes are deductible from claim settlements.

Hiscox's position on furlough is directly supported by the judgment in *Stonegate Pub Company v MS Amlin and Others* [2022] EWHC 2548 (Comm) ("Stonegate"). This judgment, in part, considered whether furlough payments should be deducted from relevant business interruption insurance claims. Hiscox considers SEISS payments to be analogous to furlough payments, and so considers the judgment to be relevant to both.

The judge in Stonegate determined that furlough payments were deductible from the relevant claim settlement, saying at para 270:

> "...*I hold that the CJRS* [furlough] *payments did reduce costs payable out of Turnover and are to be taken into account under the savings clause*."

His findings were made based partly on the fact that furlough payments were paid to businesses by the Government to cover part of the cost of paying employees' wages. They

could not be used for any other purpose (albeit the timing of the relevant payments may have meant businesses had already paid staff, and the furlough payments acted as a 'refund' of these amounts). Paying employees their wages is an expense a policyholder, including Mrs C, would normally have. As a result of the furlough payments, these policyholders saved on having to pay these wages.

The judge explained that the insurance contract involved in the judgment set out that where any costs normally payable out of 'Turnover' were reduced as a result of the insured event, it was fair to deduct these. Mrs C's policy provided cover for loss of gross profit and defined this as:

> "*The sum produced by applying the rate of gross profit to any reduction in income during the indemnity period plus increased costs of working and alternative hire costs, less any business expenses or charges which cease or are reduced*."

This doesn't specifically require that the reduction in expenses be as a result of the insured event – albeit that is likely to be a reasonable requirement. Regardless, the reason for Mrs C's claim was – in simple terms – the COVID-19 pandemic. The Government introduced the furlough payments scheme as a result of this pandemic. So, it follows that the saving on Mrs C's normal expenses was a consequence of the cause of her claim.

Based on this, I said it seemed clear that Hiscox was contractually entitled to calculate Mrs C's settlement taking into account the furlough payments being a saving – i.e. to deduct these from the settlement.

The judge in Stonegate considered not only the contractual position presented by the policy in the court case, but also the principle of indemnity and associated doctrine of subrogation. This is the basis which insurance, largely speaking, works. And effectively means that a claimant is only able to recover their losses and is not able to put themselves back in a better position that they otherwise would be. And where the circumstances mean the loss the claimant has suffered has been reduced – such as because of a payment made by a third party – the insurer may be entitled to benefit from this reduction in loss.

The judge explained this in detail, but ultimately said there were three matters to consider in terms of a payment received from a third party. He set these out at paragraph 284 as:

> *"(1) If a third party has made a payment which has eliminated or reduced the loss to the insured against which it had insurance, then, subject to the exception below, the insurers are entitled to the benefit of that payment, either in reducing any payment that they might have to make under the policy or, if they have already paid, by claiming the amount from the insured.*
>
> *(2) This will not be the case, however, if it can be established that the third party. In making the payment, intended to benefit only the insured to the exclusion of the insurers ...*
>
> *(3) In assessing the intentions of the third party payor, it does not matter whether that payor gave any thought to the position of insurers. A payment can still diminish the loss even if no such thought is given*."

In terms of the first of these, the judge in Stonegate reasoned that furlough payments had reduced the employment costs to the same extent as the size of those payments. They were payable to businesses that were required, effectively, to pay their employees the corresponding amount either before or after the furlough payments had been made. So, I provisionally considered it is fair that an insurer, including Hiscox, deduct a sum paid under the furlough scheme from the settlement payable to policyholders, including Mrs C.

In considering whether SEISS payments had a similar effect, I explained it is necessary to determine whether they reduced the loss suffered by Mrs C. This might either be because they reduced a cost that Mrs C otherwise would have had to meet – as the furlough payments did with employment costs. Or because the SEISS payments were a form of income that limited the reduction in income Mrs C's business experienced as a result of the pandemic.

Hiscox has said that furlough and SEISS are analogous. And that these are different from the business support grants. I did not think it is as clearly defined as Hiscox believes. So, I thought it was helpful at this point to consider these three types of Government funding, their similarities and differences.

All of these forms of Government support were introduced to support businesses through the difficulties created by the COVID-19 pandemic. All needed to be reported as "income" on the relevant tax returns. However, the judgment in Stonegate, with reference to Riley on Business Interruption Insurance (11th ed), suggests account classification in tax returns. etc. is not determinative for insurance purposes. And the FCA "Dear CEO" letter in relation to business support grants also stated that:

> "*We therefore do not consider the Government's treatment of* [business support grants] *for tax purposes is a proper basis for insurers treating those payments as turnover under the policies*"

So, I didn't think the tax position in relation to these payments is particularly helpful or determinative.

One of the key differences between furlough payments and both SEISS and business support grants, was that furlough payments were to be used specifically to cover part of the wages of employees. There was no restriction on the way the SEISS or business support grant payments could be used by the recipient, and these payments could be used in any way the business saw fit.

I thought this was potentially quite significant when thinking about the definition of loss of gross profit above. Has an expense of the business been reduced by the receipt of SEISS where the payment wasn't required to be used for any specific expense? I returned to this point later in my provisional decision.

I explained there are other differences between furlough and SEISS. These included the amount of money paid. The payment made under the first version of SEISS, introduced in April 2020, was the lower of £7,500 or 80% of the business' estimated profit for a three-month period.

Under the furlough scheme (at least as this applied to lockdown one), employers could claim a maximum of 80% of an employee's wages and this was also capped at £2,500 per month for each employee.

I said that, initially, this looks fairly similar. For each individual 'working for' a relevant business – whether this be employee, sole-trader, or partner – the business essentially received 80% of their 'employment costs' capped at £7,500 for the three-month period. (I deliberately used the term 'employment costs' here as this is what Hiscox consider SEISS to effectively be covering, but I also later returned to the issue of whether this is correct for a sole-trader or partnership.)

However, under the furlough scheme, businesses only received the payment if the relevant employee had ceased working. All that was required to claim SEISS was for an eligible business to have "been adversely affected by reason of circumstances arising as a result of

coronavirus or coronavirus disease". A business need not have suffered either a £7,500 or 80% loss of profit in order to receive this sum from the Government. Later iterations of the scheme provided that a business suffering a 30% reduction in turnover would be entitled to a payment equivalent of 80% loss of profit. So, a self-employed person could continue working and their business could generate the majority of its normal income, yet would still be able to claim up to £7,500 under SEISS.

In some circumstances, SEISS payments may have been received by a business that was only moderately “adversely affected” by the pandemic and which meant that the business actually ended up receiving more money during the relevant period that it otherwise would have. Regardless of whether such a business may or may not have had an insurance policy which might provide cover for the situation, the SEISS payment would already have put them in a ‘better position’ than they otherwise would be. The indemnity principle did not apply to sole-trader businesses directly in relation to the government scheme though. This is a principle that relates to insurance. However, I thought it is worth pointing this aspect of SEISS payments out, to demonstrate that the proper treatment of these is not a clearly defined matter.

I said that, in this regard, the SEISS seems more akin to the business support grants. These were payments made to support businesses with their cashflow and fixed costs. A business need not have suffered a loss of expected income that matched the amount they received from the Government.

Yet, there were also differences between the SEISS and business support grants. To receive a payment under the business support grants, there was no need for that business to demonstrate that it had been adversely affected by the pandemic – albeit the businesses targeted by some of the grants were those in industries subject to specific restrictions and thus almost certainly affected. Businesses received a fixed sum, rather than one based on their profits. And the business support grants were administered by local authorities, whereas the SEISS (and furlough) were administered by HMRC.

These are only some of the features of these different types of government support. But, it is clear that there were some similarities and some differences between all three types. As I had also said, insurers (generally) have treated the money received through furlough differently to that received through business support grants, and this position has been supported respectively by the courts and the FCA, etc. The question in Mrs C’s case is how SEISS should be treated.

Thinking about the issues raised above around whether or not SEISS should be considered as being received to cover an ‘employment cost’ and so whether the receipt of this payment has reduced an expense of the business, with a sole-trader such as Mrs C, there is a limited distinction between the person and the business. Whilst some businesses would have used the money, either partially or wholly, to provide a personal income to the owner of the business, others would not. The money may have been spent on operating costs, invested into the business, or saved for use outside of the indemnity period.

Hiscox has made detailed arguments over the lack of separation between the ‘person’ and the ‘business’ in respect of a sole-trader. Whilst I accepted much of what Hiscox has said, there are scenarios where a sole-trader may have spent the money received through the Government support (either SEISS or business support grants) in a manner that means there would not be a saving on an expense of the business that otherwise would have been incurred. For example, some businesses may have made the decision to increase spending on advertising to make up for the loss of business they incurred during the lockdown period.

Had it not been for the lockdown period, this advertising would not have been required, so this was a 'new' cost to the business but one which was met by the government support the business received. In such circumstances I didn't think it could be argued that this was an 'employment cost' or that the support payment reduced an existing business cost.

On the other hand, if a sole-trader used the money from the Government support to pay for their personal expenses (food, household rent, etc.) the business would likely be using the money to cover the 'employment costs' of this person (noting that the business and individual are effectively one in the same). The individual would likely have needed to take this sum of money from the business even had there been no pandemic. So, this has reduced the expenses the business would otherwise have incurred.

So, it may be that in order to fairly assess whether or not SEISS payments can been considered by an insurer as reducing the expenses of the business, it is necessary to assess what this payment has been used for.

This is supported to an extent by what the FCA said[2] about assessing government funding:

> "*The insurer will need to assess this for some or all of each type of government support received by the policyholder with a case by case assessment. The assessment should consider:*
>
> - *the exact type and nature of the Government support*
> - *how the policyholder used this support*
> - *the type of policy and its precise terms, including any set methodology for calculating the value of a claim set out under the relevant section of the policy*
>
> *Some of these factors will be case and claim specific. Even where it is appropriate in principle to deduct these amounts, a single, uniform approach to deductions is still unlikely to be appropriate*."

I said it should be noted that this statement was made prior to the judgment in Stonegate. However, I didn't consider that this judgment fundamentally changes this situation. In order to assess whether or not a SEISS payment has reduced a loss by virtue of reducing a cost to the business, it must be established which cost has been reduced. And it is for Hiscox to demonstrate that a cost or expense has been reduced in order to apply either the insurance contract or the doctrine of subrogation to the claim on this basis.

I was not persuaded that Hiscox had demonstrated that the SEISS payment received by Mrs C has reduced any specific cost or expense. So, it followed that I did not consider it is fair or reasonable for this sum to be deducted from the settlement on this basis.

However, the other way of considering the SEISS payments is that they were a form of income. This is how they are considered for tax purposes, although the above comments from the Dear CEO letter, about this not being a proper basis for how they should be considered in terms of an insurance claim, should be noted.

I explained that, in connection with another complainant's case involving SEISS payments, I had previously said that in relation to the policy wording Mrs C had, a reasonable person would consider "income" to refer to "insured income". This comment was made whilst noting that the policy itself includes a definition of income as, "*The total income of the business*." But also taking the rest of the policy wording into account, including that the insured loss in the policy is based on the difference between expected and realised income (with the rate of

---

[2] https://www.fca.org.uk/news/statements/non-damage-bi-settlements-deductions-relation-government-support

gross profit, etc. then applied).

I was not satisfied in that case that a reasonable person would consider a government grant, of the nature of those paid to businesses in relation to a novel situation such as the pandemic, to be insurable income. So, I was not persuaded SEISS payments would be considered as income in terms of the policy.

However, whilst this was a conclusion I had previously reached, I confirmed that I had thought about this further in light of Hiscox's comments and the rest of the circumstances in Mrs C's complaint.

Thinking about the principle of indemnity and the fact that insurance is, effectively, there to cover losses of a policyholder that can't otherwise be recovered, I needed to consider whether it is fair for Hiscox to cover Mrs C's loss of income where Mrs C has received money from a different source. More precisely, I need to ask whether Hiscox's decision to deduct this sum from the settlement was fair and reasonable.

Thinking about the situation holistically, I was not persuaded that Hiscox considering the money received from SEISS to be income was unfair or unreasonable. And whilst it may not be considered insured income, the receipt of this money did provide Mrs C with funds she otherwise would not have had and which acted to reduce the overall losses she sustained as a result of the pandemic.

So, for the purposes of Mrs C's claim, I considered it was fair and reasonable for Hiscox to treat the SEISS payment(s) as "*a payment which has eliminated or reduced the loss to the insured against which it had insurance*" – i.e. as income.

The second matter that the judge in Stonegate listed was whether the third-party making the payment intended to benefit only the insured to the exclusion of the insurers. I.e. whether the Government intended to benefit Mrs C only and not Hiscox. If Hiscox deducts the SEISS payment from the settlement, the payment will have benefitted Hiscox in that it has reduced the sum it needs to pay Mrs C.

The arrangements for SEISS were introduced under powers granted by sections 71 and 76 of the Coronavirus Act 2020. The arrangements were set out in Directions issued by the Government in April 2020. The Direction relating to SEISS said:

> "*The purpose of SEISS is to provide for payments to be made to persons carrying on a trade the business of which has been adversely affected by the health, social and economic emergency in the United Kingdom resulting from coronavirus and coronavirus disease*."

No comment was made about this payment being intended only to benefit the businesses receiving these sums though.

As I had noted above, the Treasury did make some later comments of its own about government grants. In a letter to the ABI[3], it said:

---

3 https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/921682/EST_letter_to_Huw_Evans.pdf

> "*The principle of these grants is to provide emergency support and help businesses survive. The practice of making these deductions would mean that taxpayer funds are being channelled into savings for insurers, rather than supporting businesses to ride out the disruption brought on by this pandemic… I strongly encourage those insurers who are making these deductions to follow this example, to respect the spirit of these government support schemes, and to consider the difficulties being faced by businesses during this time*."

However, this letter was issued in relation to discussions around the business support grants. Insurers, including Hiscox, agreed not to deduct payments from these grants from claim settlements. The letter did not reference, and was not in relation to a conversation concerning, furlough or SEISS.

Thinking about this in relation to the judgment in Stonegate, which was issued some time after these comments from the Treasury, the judge said in relation to furlough:

> "*As to the intention of the Government in paying, Stonegate has not shown that this was with the intention of benefiting Stonegate alone to the exclusion of insurers. There is no express statement by the Government to that effect. The Government did not indicate that the payment was being made only in respect of uninsured losses*."

So, it does not seem the judge considered the Treasury letter to be relevant to furlough. And, given the Government hasn't said anything different in relation to SEISS than it did to furlough, it seems likely that the judge would not have considered the Treasury letter was relevant to SEISS either.

Taking these points into account, I didn't think the payor (the Government) intended to benefit the insured (Mrs C) only to the exclusion of the insurer (Hiscox). It followed that I considered Hiscox can fairly and reasonably deduct the SEISS payment from the claim settlement.

<u>The settlement calculation</u>

However, I also explained that it is necessary to also think about how Hiscox has deducted the SEISS payment from the settlement.

Hiscox has calculated the loss of profit suffered by Mrs C and then deducted from this amount certain sums. Largely, these are the savings Hiscox considers Mrs C to have made – on things like utilities bills. This makes sense as these are savings on costs that Mrs C would have normally had to pay out of her profits. And this also makes sense for furlough payments; as these were in effect a saving on the wages normally payable to employees.

But, as above, I did not consider Hiscox has demonstrated that the SEISS payments Mrs C received were a saving on a cost or expense she otherwise would have had to meet. I was satisfied that Hiscox can treat this money as effectively being income. But this means the deduction of this sum needs to have been made prior to the application of the rate of gross profit.

In Mrs C's case, her rate of gross profit has been calculated at 67.3%. For lockdown one, this has been applied to her loss of revenue/income of just over £65,000. And then the 'savings' have been deducted from this loss of gross profit sum. I considered Hiscox should have deducted the SEISS payment of just over £2,000 from the revenue loss before applying the rate of gross profit. The difference works out to be around £737 – albeit this is prior to any application of the rate of underinsurance.

I invited both parties to respond to my provisional decision.

Mrs C queried the sums used to calculate the underinsurance. However, after I had clarified that the sum insured is the *gross* profit, rather than *net* profit, of her business this issue was resolved.

Hiscox disagreed that the historic rate of gross profit should be applied to the SEISS payment to work out the settlement. I will comment on this below.

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.

Neither party responded disagreeing with the fundamental parts of my provisional decision. So, having considered everything in full, I have come to the same conclusion on these points as in my provisional decision, for the reasons set out above.

Hiscox did disagree that the historic rate of gross profit should be used to calculate the claim settlement in relation to the SEISS payment. It has referred to the question set it used for claimants when calculating claims relating to the COVID-19 pandemic. However, whilst this may demonstrate Hiscox might be applying the same criteria to each of its claimants, the existence of this does not in itself mean this process was fair and reasonable for all situations. So, I am not persuaded this question itself set adds a great deal to the current issue.

However, Hiscox also said that the rate of gross profit to be applied had to be reflective of the actual rate of gross profit / costs incurred in generating this income. And that as Mrs C hadn't incurred any such costs during the indemnity period, the rate of gross profit should be 100%. Whilst I do appreciate the points Hiscox has made here, which do accord in many respects with common industry practice, I am not persuaded by its argument in the case of SEISS payments to Mrs C.

This is because I don't consider it fair and reasonable to consider the SEISS payments exactly the same way as other income. Although I am satisfied these payments reduced the loss to the insured, and so can be deducted from the settlement, this was not money generated by the business' activities within the indemnity period. So, the cost of any activities within this period are not directly relevant to the cost of generating this money.

The Coronavirus Act 2020 Functions of Her Majesty's Revenue and Customs (Self-Employment Income Support Scheme) Direction set out how SEISS payments should be calculated (for the first version of the scheme). Paragraph 6.1 gave the general formula for this, and then the Direction explained what each of the elements of that formula meant. Essentially, this was based on the average business income of the individual over the previous three years. So, it is arguable that it is the average rate of gross profit for the business over this period that is most relevant to calculating the cost of generating this money.

However, this isn't necessarily fair either. SEISS payments were made to individuals, rather than to their businesses. For example, each partner of a partnership would receive a separate payment. Due to the lack of legal separation between, for example Mrs C as a sole-trader and her business, these payments can be seen as reducing the losses the business has experienced – for the reasons set out above. But the size of the SEISS payment is based on the amount of, effectively, net profit the business generated in previous years. It is this net profit of the business that forms, in simple terms, the trading profit of the

individual (albeit the Direction included further specific details defining this trading profit).

This is essentially the reason for Hiscox's argument that the SEISS payment should be considered a saving on an expense; that the payment of the business' net profit to the individual sole-trader was an expense that was saved. I have set out above why I don't consider this is correct.

However, this situation does complicate how the SEISS payment should be considered in terms of the claim settlement. It is arguable that the SEISS payment was not "income" of the business, but was in fact a payment equivalent to "net profit". The calculation of the claim settlement as well as the reasons for making such a payment are different to the calculation of and reasons for the SEISS payment. So, a direct correlation is not appropriate. But neither is a direct comparison between this payment and the income generated by a business through its own activities during the period of the claim.

Taking all of this into account, I consider that the fair and reasonable way to account for SEISS payments in the claim settlement calculation is to consider them as income generated based on the rate of gross profit prior to the claim event. In Mrs C's case, this is the 67.3% previously referred to.

I do recognise that there are shortcomings with this approach, and that this may not be the outcome a court would reach. But having considered all of the circumstances of the complaint, I am satisfied that this is the fair and reasonable outcome.

Putting things right

Hiscox should have handled the claim and complaint better than it did. And so, it should compensate Mrs C for this. However, I consider that the offer made by Hiscox during the course of this complaint is appropriate. So, Hiscox should add interest to the settlement in the manner it has suggested and should pay Mrs C £500 compensation, if it has not already done so.

I also think it is reasonable for Hiscox to apply a rate of underinsurance to the claim, and that its methodology for doing so is appropriate. And Hiscox can fairly and reasonably deduct the amount Mrs C received in furlough payments from the claim settlement as these acted to save Mrs C paying a cost or expense she otherwise would have had to.

Additionally, I think Hiscox can deduct the amount Mrs C received from the Government in SEISS payments. However, Hiscox should treat these SEISS payments as income, and should deduct these sums prior to applying the rate of gross profit to Mrs C's losses. The rate of gross profit applied to these payments should be based on the same rate of gross profit that Hiscox has applied to the lost revenue.

My final decision

My final decision is that I uphold this complaint in part. Hiscox should put things right as set out above.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mrs C to accept or reject my decision before 24 August 2023.

Sam Thomas
Ombudsman