DRN-3964809

The complaint

Mr and Mrs X have complained about the settlement offered by Society of Lloyd's in settlement of their business interruption insurance claim.

What happened

Mr and Mrs X run a guesthouse.

They made a claim to Lloyd's in March 2020 after the business was affected by Covid-19 lockdown restrictions.

Lloyd's accepted the claim in April 2021 following the Supreme Court judgment in a test case brought by the Financial Conduct Authority (the "test case"). In May 2021 Lloyd's made a settlement of £57,500 which Mr and Mrs X accepted as an interim payment.

Mr and Mrs X didn't accept the way the settlement had been calculated. They thought based on the wording of the policy they were entitled to a further £75,000 being 25% of the sum insured of £300,000 under Sub-section 2 of the Business Interruption part of the policy.

Lloyd's disagreed. It said this section didn't apply as it covered business interruption resulting from damage to property used at the premises for the purpose of the business and Mr and Mrs X's claim didn't arise from damage to property.

Mr and Mrs X brought their complaint to this service. They were also unhappy with the way their claim had been handled, in particular, the delays on the part of Lloyd's. They said they had had to take out a loan of £35,000 in August 2020 through the government's "bounce back loan scheme" (a "BBL") because of the delay in settling the claim.

I issued a provisional decision upholding the complaint in part. An extract from my provisional findings is set out below:

"*The Business Interruption part of Mr and Mrs X's policy isn't the easiest for a layman to understand and I note that some people in Lloyd's found it confusing as well. The core cover (described in the policy as "Automatic Cover" in Section A Sub-section 2 is for:*

*"Loss resulting from interruption of or interference with the **business** carried on by **you** at the **premises** following damage to property used by **you** at the **premises** for the purposes of the **business**."*

Words in bold are defined in the policy but for the purpose of the above clause the meaning is clear enough without me setting out the various definitions.

The policy schedule refers to Section A Automatic Cover Sub-section 2 Business Interruption as having cover of £300,000 for "Gross Profit/Loss of Net Takings (12 month indemnity period)".

As there is no evidence of damage to property at the premises, I agree that this automatic cover doesn't apply.

Further on in this section there are set out the four different methods of settling a claim. They are gross profit, additional cost of working, rent receivable and rent payable.

Then there are listed "Additional cover – automatically included". One of these is loss following:

*"any **notifiable disease** within a radius of 25 miles of the **premises**."*

It's not in dispute that there was an occurrence of Covid-19, being a notifiable disease within the terms of the policy, within a 25 mile radius of Mr and Mrs X's premises, and that this occurrence was a contributing cause to the Government's restrictions which caused Mr and Mrs X's loss.

The maximum indemnity period for business interruption loss caused by a notifiable disease is three months.

There are no separate provisions for the claim settlement of the additional covers. So it seems to me reasonable to assume that claims will be settled on the same basis as the Automatic Cover. The Schedule refers to settlement on the basis of Gross Profit. So I have looked at the wording in the policy regarding that. It says:

"Claims – basis of Settlement A – Gross Profit

*The insurance by this item is limited to loss of **gross profit** not exceeding the **limit of liability** due to:*

*a) reduction in **turnover**; and*

b) increase in cost of working

and the amount payable will be

1. *For reduction in **turnover**, the sum produced by applying the rate of **gross profit** to the amount by which the t**urnover** during the **indemnity period** will following the **damage** fall short of the **standard turnover***
2. *For increase in cost of working, the additional expenditure necessarily and reasonably incurred for the sole purpose of avoiding or diminishing the reduction in **turnover** which but for that expenditure would have taken place during the **indemnity period** following the **damage** but not exceeding the total of:*

    a) *The sum produced by applying the rate of **gross profit** to the amount of reduction avoided; plus*

    b) *25% of the **sum insured** by this item (but not more than **£250,000**)*

    *less any sum saved during the indemnity period for the charges and expenses of the **business** payable out of gross profit as may cease or be reduced following the **damage**."*

The term "Gross Profit" is defined as:

*"The amount of the **turnover** (net of discounts allowed), closing stock and work in progress less the amount of the opening stock, work in progress and specified working expenses."*

Based on information provided by Mr and Mrs X, Lloyd's calculated that the loss of gross profit due to reduction in turnover was £50,161. The parties seem to have been in agreement that the loss of gross profit was about £55,000. Mr and Mrs X haven't supplied any evidence that they incurred an increase in the cost of working to avoid or diminish a reduction in turnover. I think that is to be expected since the guesthouse was closed for the indemnity period.

I think if Mr and Mrs X had incurred an increase in cost of working, the policy wording meant that the amount Lloyd's would pay in respect of an increase in cost of working would not exceed the total of a) and b). It does not mean that Lloyd's was obliged to pay the total of a) and b) in any event.

The term "damage" is defined in the policy as:

"Loss or destruction of or damage to the property insured as stated in the schedule".

I agree with Lloyd's that there is no evidence of damage to the property insured. But even if there had been damage to property insured, I don't think Mr and Mrs X would have been automatically entitled to an additional £75,000 (being 25% of the sum insured) for the reason explained above, namely that the sum of a) and b) is only relevant for calculating the limit of Lloyd's liability for any increase in cost of working incurred by Mr and Mrs X.

Lloyd's said that it settled the claim for £57,500 following "amicable discussions". I haven't seen any evidence that Mr and Mrs X's reduction in turnover and increase in cost of working for the three-month indemnity period exceeded £57,500. So, I'm not persuaded that Lloyd's treated Mr and Mrs X unfairly in the way it calculated the settlement amount.

I've noted Lloyd's point that it felt it needed to wait until the outcome of the test case but I am not persuaded by it. This delay in dealing with business interruption insurance claims was permitted under the guidance issued by the Financial Conduct Authority to insurers at the time but not required by law. Additionally, the guidance did not suggest that, for customers whose claims were found to have been incorrectly declined, interest should not be awarded. I recognise that there was uncertainty about the interpretation of the wording in certain policies, including ones like Mr and Mrs X's, which required the loss to have been caused by an outbreak of Covid-19 within a specified distance of the premises. However, I think it was always open for Lloyd's to have accepted the claim sooner and ultimately the Supreme Court found that Lloyd's initial decision not to provide cover was incorrect.

I've also taken account of the fact that Lloyd's has had the benefit of the money it should have paid Mr and Mrs X. The rules governing this service allow me to make, amongst other things, a money and interest award for what I consider to be fair compensation if a complaint is determined in favour of the complainant. In this case, my decision is based on what I think is fair compensation to put Mr and Mrs X back in the position it would have been in if Lloyd's had accepted the claim originally. I acknowledge that my decision might be different from one which a court might make. But in this case I think it is fair and reasonable to do so.

In relation to an ongoing claim of this nature, it is reasonable that an insurer should wait for losses to accrue before making settlement. However, it is not necessarily reasonable for an insurer to wait for the end of an indemnity period before making any settlement. Generally speaking, I would expect regular monthly payments to be made.

It is also reasonable that an insurer will need some time to assess a claim and make a settlement. I consider a reasonable time to do this for a claim of this nature would be around two months from when Mr and Mrs X first made their claim in March 2020 in order to wait for losses to accrue and to give Lloyd's a reasonable amount of time to assess the claim. I don't consider the bringing of the test case alters this in the circumstances of this complaint.

I currently think it is fair and reasonable that Lloyd's should add interest to the first month's loss from two months after the claim was made, the second month's loss from three months after the claim was made and the third month's loss from four months after the claim was made in each case until 11 May 2021 being the date of settlement but adjusted as mentioned below. Interest is simple interest at the rate of 8% a year.

Because of the delay in settling the claim Mr and Mrs X took out the BBL of £35,000 on 7 August 2020. I understand that no interest would have been payable on this for the first year of the loan. As Mr and Mrs X had taken out this loan to cover part of the settlement that Lloyd's should have made, they weren't without that amount of the settlement from that point in time. So, I think the amount on which interest is calculated for the period from 7 August 2020 to 11 May 2021 should be reduced to £22,500 (being the settlement amount less the BBL)."

Mr and Mrs X had no comment on my provisional decision. Lloyd's didn't agree that it should pay interest.

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.

I've considered the point made by Lloyd's that it shouldn't be required to pay interest because it was entitled to wait for the judgment of the Supreme Court in the test case but for the reasons explained in my provisional decision I am not persuaded by this argument. Whilst I appreciate the difficulties that insurers faced with claims of this nature, that doesn't alter the fact that Mr and Mrs X had a valid claim which should not have been declined initially.

Because an incorrect decision was made on the claim, Mr and Mrs X were left without funds that they should otherwise have had. As they have been without this money, I believe it is fair and reasonable to require Lloyd's to compensate them for this financial loss.

Putting things right

Society of Lloyd's should pay Mr and Mrs X interest on the first month's loss from two months after the claim was made, interest on the second month's loss from three months after the claim was made and interest on the third month's loss from four months after the claim was made, in each case until 11 May 2021 being the date of settlement but adjusted as mentioned below. Interest is simple interest at the rate of 8% a year.

As Mr and Mrs X took out the interest-free BBL of £35,000 on 7 August 2020 to cover part of the settlement that Lloyd's should have made, they weren't without that amount of the settlement from that point in time. So, the amount on which interest is calculated for the period from 7 August 2020 to 11 May 2021 should be reduced to £22,500 (being the settlement amount less the BBL).

My final decision

For the reasons set out above, I uphold this complaint and require Society of Lloyd's to put things right as I have set out above.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr and Mrs X to accept or reject my decision before 15 March 2023.

Elizabeth Grant
Ombudsman