

The complaint

Mr M is unhappy that Fairmead Insurance Limited intends to reduce the amount it will pay for a claim he made on his landlord insurance policy.

What happened

The details of this complaint are well known to both parties, so I will not repeat them again in detail here. But to briefly summarise, Mr M is a landlord of a property which he insures through Fairmead.

On 29 April 2022, the property suffered damage caused by an escape of water, so Mr M made a claim to Fairmead. Following investigations, Fairmead said the property was underinsured. It valued the cost of rebuilding the property at around £447,000, but Mr M had insured it for only £151,110.

Fairmead accepted the claim was covered under the terms of the policy. But because the property was underinsured, it said the claim would be settled proportionately. Fairmead accepted an amended rebuild figure supplied by Mr M of £363,000. Based on this, it offered 41.62% of the total repair costs as a settlement.

Mr M didn't agree this was fair. He said he should have been told he was underinsured. He also said that if he were over insured Fairmead wouldn't be looking to pay him money back. He brought his complaint to our service.

Our investigator considered the complaint but felt Fairmead's approach was in line with the policy terms and was fair and reasonable. She said it was Mr M's responsibility to ensure the sums insured were adequate, and that the policy documentation told him how he could do this, and how important it was.

Mr M didn't accept our investigator's opinion. So, as no agreement has been reached, the complaint was passed to me to decide.

I was minded to reach a different outcome to our investigator. So, I issued a provisional decision, to give the parties the opportunity to respond, before I reached my final decision.

Here's what I said in my provisional decision:

"What I've provisionally decided – and why

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

Having done so, I'm intending to reach a different outcome to our investigator. So, I'm issuing a provisional decision to give both sides the chance to reply before I reach my final decision.

The issue I need to decide here is whether it is fair for Fairmead to proportionately reduce the settlement of Mr M's claim, in the way that it has.

Based on everything I've seen, I agree that Fairmead can fairly and reasonably reduce the settlement Mr M is due. However, I don't agree that the specific reduction it has sought to apply is fair or reasonable in the circumstances. I'll explain why, addressing each issue in turn.

Why it is fair to proportionately reduce the settlement

The sales literature Mr M was provided with explains the importance of the building sum insured (rebuild value) being accurate. It also sets out how Mr M could obtain a reasonable estimate. In my view this information is sufficiently prominent as it's at the top of the document and highlighted by a black box. This explains:

"IMPORTANT INFORMATION

This policy may be based and rated upon the Buildings Sum Insured (BSI) which is the rebuild value or reinstatement values of your property as confirmed with us at the inception of this policy. Please read the following:

As the BSI is a major material fact of the policy we would advise that you check this value is correct to ensure that the cover provided under the policy is adequate as this may affect any claims which will be paid out on a pro rata basis if the building is deemed to be underinsured. We must advise that it is the policyholder's responsibility to ensure that the BSI is adequate. If you are unsure or do not know the correct figure, we recommend that you check the Building Cost Information Service website (calculator.bcis.co.uk) to obtain the rebuild value or refer to a recent survey report which details this figure."

Mr M is a commercial customer. This means the relevant law which applies is the Insurance Act 2015. This states that Mr M was required to make a fair presentation of the risk to Fairmead. Particularly relevant to this complaint, that meant providing a reasonable estimate of the cost of rebuilding the property.

The importance of the of the rebuild value, and how Mr M could obtain a reasonable estimate of it was sufficiently highlighted when Mr M bought the policy. But Mr M didn't follow the guidance. Instead, he provided the market value figure for the property instead. Based on this, I agree with Fairmead that Mr M failed to make a fair presentation of the risk.

The Insurance Act sets out the remedies available to Fairmead if Mr M breached the duty of fair presentation. For deliberate or reckless breaches, the Insurance Act entitles Fairmead to void the policy and decline all claims. But here Fairmead has accepted the claim, so it clearly doesn't think Mr M made a deliberate or reckless breach.

For all other breaches, the remedy available to Fairmead depends on what it would have done had a fair presentation been made. If Fairmead would have offered the policy for a higher premium, the Insurance Act says it may reduce the claim settlement proportionately – based on the amount of premium paid compared to the higher premium it would have charged.

Fairmead seems to understand this, as its policy contains the following term, with my added emphasis on the key wording, which is in line with approach set out in the Insurance Act:

“If the cost of rebuilding the buildings is more than your Sum Insured at the time of any loss or damage, then we will proportionally reduce the amount of any claim payment made by the percentage of under payment of premium which has arisen as a result of the shortfall in the sum insured. For example, if the premium you have paid for your buildings insurance is equal to 75% of what your premium would have been if your buildings sum insured was enough to reconstruct your buildings, then we will pay up to 75% of the claim made by you.”

To summarise, I'm satisfied that Mr M breached the duty of fair presentation with regard to the rebuild value of the property. The Insurance Act allows Fairmead to proportionately reduce the claim settlement, based on the premium shortfall, in these circumstances. And doing so is specifically in line with the terms and conditions of Mr M's policy. So, taking everything into account, I think Fairmead can fairly and reasonably proportionately reduce the settlement Mr M is due.

Why the proportionate reduction applied by Fairmead is unfair

Fairmead initially said the BCIS estimate of the rebuild cost was around £447,000. But Mr M later obtained an estimate using the same tool which came out at £363,000. Fairmead agreed to use that valuation when calculating a fair settlement for the claim.

Fairmead has offered to settle the claim by paying 41.62% of the full cost of the claim. However, this percentage seems to be based on the difference between the rebuild cost declared by Mr M – £151,110 – and the rebuild cost of £363,000. This approach is not in line with the remedies set out in the Insurance Act or the terms of Mr M's policy.

The remedy set out in the Insurance Act, and the terms of Mr M's policy, clearly state that any proportionate reduction will be based on the difference between the premium paid and the higher premium which would have been charged if the breach didn't happen/the property wasn't underinsured.

Fairmead has recently provided breakdown showing that the premium it would have charged, based on a rebuild value of £363,000, would have been £353.88. The premium Mr M actually paid was £166.32. This amounts to 47% of the premium which ought to have been paid.

What this means is that Mr M has paid 47% of the premium due, yet Fairmead is only seeking to cover 41.62% of the claim. This doesn't seem fair and it isn't in line with the Insurance Act or Mr M's policy. So, unless anything changes as a result of the responses to this provisional decision, I'm minded to decide that Fairmead needs to increase the settlement to 47% of the total repair costs, rather than 41.62%.

Fairmead should also add 8% simple interest to any part of the 47% settlement that remains unpaid, from 29 May 2022 to the date of settlement. This is to compensate Mr M for being without funds he was entitled to under the terms of the policy but also recognising Fairmead would have needed a reasonable period of time to investigate, consider and pay the claim.

I've also considered whether to award any compensation for the distress and inconvenience Mr M will have suffered as a result of Fairmead's incorrect approach. But as Mr M's concern was with Fairmead seeking to apply any proportionate reduction at all, rather than with the amount, I don't think we'd be in a fundamentally different position now, even if Fairmead had calculated the reduction in line with the Insurance Act and policy wording. So, in these circumstances, I don't think it would be fair or reasonable to direct Fairmead to pay any compensation for distress or inconvenience."

I said I was intending to partially uphold Mr M's complaint and to direct Fairmead to increase the claim settlement to 47% of the quote for reinstatement, plus 8% simple interest from 29 May 2022 to the date of settlement. I asked both sides to provide any further comments or evidence they wanted me to consider by 11 April 2022.

Both sides have already responded to say they accepted my provisional conclusions. So, as both responses have been received, I'm moving forward with my final decision.

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.

Both sides confirmed their agreement with my provisional conclusions. So, in the absence of any new evidence or arguments to consider, I've reached the same conclusions I reached in my provisional decision – for the same reasons.

My final decision

For the reasons explained above, and in my provisional decision, I partially uphold Mr M's complaint.

Fairmead Insurance Limited must:

- Increase the settlement offer to 47% of the quote for reinstatement, less the policy excess.
- Add 8% simple interest* to the amount due to Mr M from 29 May 2022 to the date of settlement.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr M to accept or reject my decision before 3 May 2023.

**If Fairmead Insurance Limited considers that it's required by HM Revenue & Customs to deduct income tax from that interest, it should tell Mr M how much it's taken off. It should also give Mr M a tax deduction certificate if he asks for one, so he can reclaim the tax from HM Revenue & Customs if appropriate.*

Adam Golding
Ombudsman