DRN-4332460

The complaint

Mrs C, trading as S, complains about the settlement and handling 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 only as a brief summary of events. Additionally, whilst others have been involved in the events and communications, I have just referred to Mrs C, S, and Hiscox for the sake of simplicity.

S operates as a Hair and Beauty Consultant, and held a commercial insurance underwritten by Hiscox. This complaint relates to the policy period that ran from August 2019 to August 2020. The policy provided cover for a number of areas of risk. And when S's business was impacted by the COVID-19 pandemic, initially in March 2020, Mrs C claimed under the business interruption section of the policy.

After initially declining it, Hiscox ultimately agreed that the claim was covered. But said that the policy underinsured the potential losses S might suffer, so reduced the settlement it offered. Mrs C is unhappy with this and with some of the deductions that had been made from the settlement. And she is unhappy with the service she had received during the course of the claim. Hiscox did not change its decision on the settlement. But Hiscox did apologise for the level of service and offered some compensation for this.

Mrs C remained unhappy and brought her complaint to the Ombudsman Service. Since then, Hiscox has increased the compensation offered to £500.

Our Investigator thought it was reasonable for Hiscox to deduct the money Mrs C had received through the Coronavirus Job Retention Scheme ("furlough"), but that it was not fair for Hiscox to deduct money received through the Self-Employment Income Support Scheme ("SEISS"). Our Investigator thought interest should be payable on the settlement from the date the claim was made, and that Hiscox should pay Mrs C the £500 compensation for delays and customer service issues.

Hiscox did not agree that it was unfair to deduct the SEISS payments from the settlement. It also said that whilst it agreed it was appropriate to add interest to the settlement, this should not be calculated from the date the claim was made – as this was not when any settlement would have been payable even if the claim had been accepted without any undue delay.

As our Investigator was unable to resolve the complaint was passed to me for a decision. I issued my provisional decision on 18 August 2023 and invited both parties to provide any further evidence or comments.

The following is an extract from my provisional decision:

> "There are a number of key issues that I will focus this decision on, and I will deal with each in turn.

Underinsurance

Our Investigator did not overly comment on the underinsurance aspect of the claim settlement. It is true that this policy was sold via a third party, and that any complaints about this sale process would need to be taken up with this third party. However, Hiscox is also required to settle claims appropriately. So, I do need to consider whether this has happened.

Hiscox has assessed the amount of gross profit that should have been insured as being £168,167. Mrs C hasn't challenged this assessment as being inaccurate and I have no reason to doubt that it was correct. However, Mrs C's policy only provided cover for a maximum of £35,000 loss of gross profit. This means she was underinsured.

Mrs C's policy sets out how this underinsurance will be taken into account. It says:

> "If, at the time of any damage, insured failure, or restriction covered under this section, we establish that the relevant value does not represent the actual value, we will reduce the amount we pay for any claim or loss in the proportion that the premium you have paid bears to the premium we would have charged you if you had declared the actual value."

This largely accords with how the Insurance Act 2015 also sets out how matters of underinsurance need to be applied to claims.

In this case, Hiscox has said that the premium Mrs C actually paid was only 20.8% of the premium she would have been required to pay had the policy covered the correct amount.

So, Hiscox has applied this 20.8% rate of underinsurance to the settlement of Mrs C's loss of gross profit. I consider this generally to be fair and reasonable.

However, I also need to consider the treatment of accountant's fees Mrs C generated during the course of making her claim and providing Hiscox with the information it required. Hiscox has included a sum of £500 in its calculation. It has said that a proportion of this may be related to claims preparation and or assistance, which it does not consider the policy would cover. But that it has taken a pragmatic approach and has not requested a breakdown of this sum.

Hiscox though has applied the rate of underinsurance to this accountant's fee. So rather than paying £500, it is has paid Mrs C 20.8% of this - £104.

Technically, this is in line with the policy terms. The policy lists accountant's charges under the section setting out the amount that will be paid in relation to a claim, and the underinsurance term applies to "the amount [Hiscox will] pay".

However, Hiscox has also accepted that Mrs C had difficulties with the claim process, and that there were a number of financial aspects that meant the settlement of this claim was complex. So the amount that it would have cost Mrs C to produce the information Hiscox required to support the claim would likely have been incurred regardless. And, in the circumstances of this complaint, I do not consider it is fair and reasonable to reduce the level of fee Hiscox is willing to cover in relation to these fees in line with the rate of underinsurance.

If Hiscox considers that the full £500 did not relate to the costs of producing the required information, it should have queried this at the time. I appreciate it took a

pragmatic approach to this aspect. But I consider the application of the rate of underinsurance to be the reverse of this. And I consider Hiscox should pay the full £500 it agreed to cover.

Furlough and SEISS

Mrs C is also unhappy that Hiscox deducted money received from the Government through the Coronavirus Job Retention Scheme (“furlough”) and SEISS payments from the settlements of the claim.

Before discussing Hiscox actions here, it is helpful to set out some of the background to these schemes. The Government provided financial support to businesses during the pandemic via a number of different schemes. These included furlough, SEISS and also arange 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 will refer to them collectively as “business support grants”.

All of these forms of Government support were introduced to support businesses through the difficulties created by the COVID-19 pandemic.

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 these grants from claim settlements. Hiscox has agreed not to deduct money received from business support grants from settlements.

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

All three types of support needed to be reported as “income” on the relevant tax returns. However, the judgment in Stonegate Pub Company v MS Amlin and Others [2022] EWHC 2548 (Comm) ("Stonegate"), with reference to Riley on Business Interruption Insurance (11th ed) (“Riley”), suggests account classification in tax returns. etc. is not determinative for insurance purposes. So, I don’t think the tax position in relation to these payments is particularly helpful or determinative.

Hiscox has said that furlough and SEISS are analogous. And that these are different from the business support grants. I do not think it is as clearly defined as Hiscox believes. I think that there were some similarities and some differences between all three types.

Hiscox’s position on furlough is directly supported by the judgment in Stonegate. This judgment, in part, considered whether furlough payments should be deducted from relevant business interruption insurance claims. 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 policy 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…, less any business expenses or charges which cease or are reduced.”

This doesn’t specifically require that the reduction in expenses or charges 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, it seems 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, 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. And I don't currently consider it would be fair or reasonable to conclude that Hiscox acted inappropriately in deducting the furlough payments Mrs C received.

Hiscox has deducted over £10,000 from the claim settlement in relation to "general wage savings". It isn't clear exactly what this relates to. If savings were made on a usual expense Mrs C would have incurred had S not been interrupted, then these can be deducted from the claim settlement in line with the policy.

However, furlough payments would have only covered a maximum of 80% employee wages. If Mrs C continued to pay her employees their full wages throughout the indemnity period, even the maximum furlough payment would not have covered this entire cost. Hiscox would not be entitled to deduct any amount Mrs C was obliged to and did in fact continue to pay. This may be the 20% difference or may be more.

It isn't clear whether there is any issue in respect of this part of the settlement. There may be unrelated general wage savings that Mrs C achieved. But as I have outlined that furlough payments are deductible, I feel it is prudent to set out the limits of this.

The judgment in Stonegate did not involve any consideration of SEISS, as no payments under this scheme were made to the parties. However, I do need to consider the reasoning of the judge when thinking about SEISS.

In considering whether SEISS payments had a similar effect to that set out above, 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.

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 or partner, 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.

Whilst I accept much of what Hiscox has said, about the lack of separation between the 'person' and the 'business' in respect of a sole-trader/partner, there are scenarios where the money received through the Government support (either SEISS or business support grants) may have been spent in a manner that means there would not be a saving on an expense of the business that otherwise would have been 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[1] 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:
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> - 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."

It should be noted that this statement was made prior to the judgment in Stonegate. However, I don'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, whilst the Ombudsman Service's inquisitorial remit applies to complainants as well as respondents, it is ultimately 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 am not persuaded that Hiscox has demonstrated that the SEISS payment received by Mrs C has reduced any specific cost or expense. So, it follows that I do 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. The Ombudsman Service's understanding of what is fair and reasonable in relation to SEISS payments has been one that has evolved, much like the wider legal landscape around business interruption insurance claims. Previously, we have considered that an individual may not have considered a government grant, of the nature of those paid to businesses in relation to a novel situation such as the pandemic, to be "income".

However, as the judge in Stonegate indicated in paragraph 267 of the judgment, the clauses in Mrs C's policy should be construed, if there is any room for argument, to accord with the basic principle that the policy was a contract of indemnity.

So, 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 need to consider whether it is fair for Hiscox to cover Mrs C's loss of income where she 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 am not persuaded that Hiscox considering the money received from SEISS to be income was unfair or unreasonable. And whilst

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

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 claims, I consider it was fair and reasonable for Hiscox to treat the SEISS payments 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 set out in Directions[2] issued by the Government and 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 have noted above, the Treasury did make some comments of its own about government grants. However, this letter was issued in relation to discussions around the business support grants. 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, in relation to furlough the judge said at paragraph 286:

> "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 don't think the payor (the Government) intended to benefit the insured (Mrs C) only to the exclusion of the insurer (Hiscox). It follows that Hiscox can fairly and reasonably deduct the SEISS payment from the claim settlement.

However, it is necessary to also think about how Hiscox has deducted the SEISS payments from the settlement. I am satisfied that Hiscox can treat the SEISS payment as effectively being income. But this means the deduction of this sum needs

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[2] See the Coronavirus Act 2020 Functions of Her Majesty's Revenue and Customs (Self-Employment Income Support Scheme) Direction

to have been made prior to the application of the rate of gross profit.

I appreciate Hiscox is likely to argue that, whilst this may be the case, the appropriate rate of gross profit to be used in this calculation is 100% as there were no costs that Mrs C incurred in generating this profit. Whilst I note Hiscox's position, I am not persuaded that this is fair and reasonable.

The policy defines "rate of gross profit" as:

> "The percentage produced by dividing gross profit by your income during the financial year immediately before any insured damage."

And when setting out what is covered in terms of a claim, the policy makes no mention of varying the rate of gross profit in relation to the period of indemnity. So, the required calculation is to apply the previous year's rate of gross profit to the reduction in income, less any reduction in expenses or charges.

Applying this formula without any adjustment isn't necessarily appropriate in all circumstances. I understand that Hiscox's position is that not taking into account the lack of costs involved in generating the SEISS payment results in an over indemnity for Mrs C (at least in this aspect). But, I am not persuaded that it is fair and reasonable in this case to apply a rate of gross profit of 100% to the SEISS payments. I do not consider this to be a situation where this is within a range of potentially fair outcomes.

The amount of SEISS payment a person received was based on the profit generated in previous years. But SEISS payments were not a direct replacement of the loss of profit a business suffered. These payments were not based on the amount of loss the business had incurred and, provided the business had been adversely affected, the actual level of loss wasn't relevant to the size of the payment. The payments were not a replacement of lost profit as such. They were merely money that was paid to the business. As such, they should be seen more akin to income than profit.

These payments were not money Mrs C generated direct through her business activities during the indemnity period. So, I do not consider it is appropriate to apply the cost of generating this money within the indemnity period. And that the fair and reasonable method of calculating this sum is to apply the terms above on the basis that the SEISS payment reduced the reduction in income Mrs C's business achieved.

Customer service issues and interest

As has been noted, Mrs C found the claims process to be complex. And it is also clear that she did not receive the level of customer service she was entitled to expect.

Hiscox, like all insurers, would have received a large number of claims at the same time relating to the pandemic. So, it is not overly surprising that it had difficulty providing the level of service that might reasonably be expected. I also appreciate that dealing with business interruption insurance claims is often complex and that this can take some time.

However, this does not change the fact that Mrs C did not receive the expected level of service. Hiscox initially declined the claim in 2020, and it is clear that there were delays, communication issues, including over requesting evidence in relation to a deceased third party, and difficulties with the claims portal Mrs C was required to use.

Hiscox has though already accepted and apologised for these issues. It has offered Mrs C £500 compensation in total, which I consider to be appropriate in the circumstances.

Our Investigator recommended that interest be added to the claim settlement at a rate of 8% simple. In the absence of any evidence to the contrary, I agree this is also appropriate. However, I do not agree with the Investigator's recommendation that this should be calculated from the date of claim.

Had things developed differently, Mrs C would have received a settlement offer for her claim much sooner than she did. However, no settlement would have been paid until a loss had crystalised, so expecting settlement on the day of the claim is not fair or reasonable.

Generally speaking, with ongoing claims of this nature, I would expect it to take a couple of months for the claim to be considered and a settlement offered. This initial settlement would be for the first months' losses. And then for interim monthly payments to be made until the full insured loss had been covered.

In this case, that means Mrs C ought to have received an initial settlement two months after making the claim. This settlement, on 26 May 2020, would cover the losses she incurred from 26 March to 25 April 2020. And then on 26 June 2020 she would have had settlement for the next month's losses. And so on.

As Mrs C did not receive the settlement in this manner, she is entitled to receive interest on each of these interim payments from when they ought to have been made until she did or does receive settlement. Mrs C did receive an interim payment of £2,500. And Hiscox is entitled to take this into account when calculating the overall settlement.

I understand Hiscox is in agreement with this process of calculating the interest. But as this differs from that recommended by our Investigator, I have set this out for Mrs C's consideration.

Summary

In summary, I currently consider that Hiscox is entitled to apply the rate of underinsurance to the settlement of Mrs C's claim for loss of profit. However, it is not fair or reasonable for this to be applied to the accountant's fees.

Hiscox is entitled to deduct both furlough payments and SEISS payments from Mrs C's claim settlement. Furlough payments should be deducted as a saving her business made on its usual expenses. SEISS payments should reduce the loss of income her business incurred, so should be deducted prior to the application of the rate of gross profit.

Hiscox should pay Mrs C £500 to compensate her for the customer service issues she experienced, if it has not already done so. And should add interest to the claim settlement as set out above."

Mrs C did not respond to the provisional decision.

However, Hiscox did provide a response. It reiterated many of its existing arguments. It also said that its approach reflected:

- the actual costs incurred

- the usual and proportionate approach to adjusting claims
- any increased costs or those not incurred
- that SEISS payments were based on net profits
- the purpose of the policy and the principle of indemnity
- an outcome that provides clear and consistent result among policyholders

Hiscox said that the proposal above did not provide this, and applied an arbitrary deduction based on the historical results of the claimant.

Hiscox also said that the use of the historic rate of gross profit to estimate a loss was being confused with the use of the actual figures where income is earned. And Hiscox referred to the business trend clause which made provision for enabling the latter. Hiscox made a number of other points, that I have considered, but not specified here.

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.

No additional comments were received from either party in relation to the underinsurance, furlough, or customer service elements of the complaint. Having reconsidered the circumstances and evidence provided, I have come to the same conclusions on these points as above, for the same reasons.

In terms of the SEISS aspect, I understand that Hiscox considers that it would be acting fairly and reasonably when applying a 100% rate of gross profit to these payments. And that the provisional decision directing that the standard, unadjusted rate of gross profit should be applied does not lead to an appropriate outcome. I have noted the various comments made, but I am not minded to change the approach set out in my provisional decision.

I have previously set out to Hiscox that I do not consider SEISS payments would have been considered "insured income". Whilst I consider that it is fair and reasonable that the payments get taken into account in thinking about the overall picture – and so can be deducted from the settlement – I do remain of the view that this income cannot be treated in the way additional income generated within the indemnity period might normally be considered. It is not normal income, and the unique circumstances of the situation need to be taken into account.

The payments under this scheme were not a directly correlating replacement of any specific loss the enterprise encountered. Whilst the principle of indemnity does pay an important factor in terms of the insurance settlement, this was not the basis of the scheme. As I have set out, an enterprise might suffer only a small amount of loss, but may have received several thousand pounds through the scheme. Similarly, the level of loss may have far exceeded the SEISS payment. And, although the calculation of the payment was, in part, based on the level of profit the enterprise previously made, the payment was not a *replacement* of lost profit. So, calculating the insurance settlement on the basis that the payment was of pure profit is not a reasonable outcome.

Where a direct saving of a particular cost has not been established, the payment cannot be said to have reduced a cost. And so, the appropriate interpretation of the payment is that it was 'income' that reduced the level of loss.

Where there is clear evidence that the SEISS payment has been used for a specific purpose

though, it may be possible for it to be treated as a saving on a cost – or a reduction in an expense or charge as per the terms of Mrs C's policy. This in itself will lead to different outcomes for different claimants, but this is in line with both the Financial Ombudsman's requirement to assess each complaint on its own individual merits and also the comments of the FCA, albeit in relation to the 'business support grants', that a single, uniform approach may not be appropriate.

In the absence of evidence that the payment was used to reduce a cost, I consider the payment should be taken into account in the settlement calculation on the basis of it being income. How that income then needs to be treated will depend, to a large extent, on the policy wording.

In terms of a potential disparity between policyholders with a loss gross profit versus income cover, these policies insure different losses so it is not unexpected that they have different outcomes in certain situations. Whilst in most claim situations these two types of insurance will lead to very similar outcomes, this is reliant on what Hiscox often refers to as the 'variable costs' being appropriately factored in.

The current issue with this seems to stem from the fact that Hiscox calculates a claimant's loss of income related claim by applying a rate of gross profit. Whilst this may be more straightforward, this is not technically how such a claim ought to be calculated.

Mrs C's policy does not include any potential loss of income cover. But looking at another of Hiscox's wordings, the amount paid in relation to loss of income is:

> "The difference between your actual income during the indemnity period and the income it is estimated you would have earned during that period … less any savings resulting from the reduced costs and expenses you pay out of your income during the indemnity period..."

The second part of this calculation relates to an actual reduction in costs and expenses that would have been payable had it not been for the insured event; the 'variable costs'. It may be a simpler calculation for Hiscox to apply a rate of gross profit to the calculation to establish the settlement in such cases. But this assumes that all the costs being included in this calculation have actually reduced. This will not always be the case.

So, for a loss of income calculation, the costs of generating 'normal' income are deducted where these have reduced (Hiscox does this by applying the historic rate of gross profit to the reduction in income). And then any SEISS payment is also deducted. The generation of SEISS payments was not at a (material) cost to the claimants. There was no existing cost from this that could cease or be reduced. As such, in these calculations it may be that the SEISS payment is effectively being treated as having a 100% rate of gross profit – but this ignores the fact that the insured loss is the loss of income, not the loss of gross profit.

This can be contrasted with the wording for loss of gross profit calculations which is:

> "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."

And which relies on a rate of gross profit definition based on the financial year prior to the insured event.

I have said above that there was no material cost to claimants in the generation of SEISS. And Hiscox has raised the question of why then it is appropriate for the 'historic' rate of gross

profit to be applied to this income. Put simply, this is the methodology set out in the policy wording.

The policy does include a Business trends clause, which makes provision for taking into account variation in circumstances or trends that mean a different sum might be payable. Such clauses will often allow insurers to adjust the historic rate of gross profit to take into account factors that mean, had the insured peril not occurred, the rate of gross profit would have been different.

However, in thinking about whether this can be applied to Mrs C's claim it is necessary to refer to the Supreme Court judgment in the FCA test case[3]. The court considered this type of clause and said, at paragraph 287 and 288:

> "… we consider that the trends clauses in issue on these appeals should be construed so that the standard turnover or gross profit derived from previous trading is adjusted only to reflect circumstances which are unconnected with the insured peril and not circumstances which are inextricably linked with the insured peril in the sense that they have the same underlying or originating cause.
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> … the trends clauses do not require losses to be adjusted on the basis that, if the insured peril had not occurred, the results of the business would still have been affected by other consequences of the COVID-19 pandemic."

The SEISS payments were only made due to the pandemic, so I consider that they were inextricably linked with the insured peril as they had the same underlying or originating cause. I do consider it is reasonable that they are included in the settlement calculation as they have reduced the loss to Mrs C. But, applying this reasoning to the current situation, it would not be appropriate to consider there was effectively no cost associated with this income as being a trend or other circumstance that Hiscox is able to take into account in adjusting the gross profit.

I do note that the Court, when making these comments, also distinguished between the various business activities an enterprise might have. And the indication is that the limitation on applying the trends clause only applies to the activity which has been interrupted by the relevant peril.

It may argued that being paid SEISS payments was not an activity that was interrupted, and that this is in fact a new activity. However, I consider that being paid a support payment by the Government is not a business activity as such – part of the reason why there are arguments over considering this as 'insured income'. But even if it is money received out of a business activity, then this is the normal activity of the enterprise. It was the fact that this activity had been adversely affected by reason of circumstances arising as a result of coronavirus or coronavirus disease that these payments were made.

In Mrs C's case this was hair and beauty treatment, and this was the business activity that had been interrupted. Given the Supreme Court reasoning above, it isn't possible to apply the trends clause to any revenue generated out of this activity where the reason for the variation in circumstances is the pandemic.

Ultimately, I do not consider it fair or reasonable in the circumstances of this complaint to treat SEISS payments received by Mrs C as a saving on an expense or charge. I do consider it reasonable to consider these payments as a form of income. However, as this was, at most, income generated due to the activity of Mrs C's business that had been interrupted I do not consider it would be appropriate to apply the business trends clause to

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

this income.

It follows that the appropriate methodology of calculating the settlement of Mrs C's claim is to deduct the relevant SEISS payment from the reduction in income, and then apply the rate of gross profit during the financial year prior to the claim.

Putting things right

Hiscox should pay Mrs C the full £500 accountant's fees included as part of the settlement rather than apply the rate of underinsurance to this sum.

Hiscox should calculate the claim settlement by deducting the SEISS payments Mrs C received, relevant to the indemnity period, prior to the application of the rate of gross profit. And the rate of gross profit applied should be the standard rate of gross profit based on the previous financial year.

Furlough payments should be deducted as a saving her business made on its usual expenses.

Hiscox should pay Mrs C £500 to compensate her for the customer service issues she experienced, if it has not already done so. And should add interest to the claim settlement as set out above.

My final decision

My final decision is that I uphold this complaint. Hiscox Insurance Company Limited should put things right as set out above.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mrs C, trading as S, to accept or reject my decision before 13 October 2023.

Sam Thomas
Ombudsman