DRN-4365351

The complaint

W complains Covea Insurance plc avoided its business protection policy and declined to cover its claim under the directors and officers section.

W is represented in bringing this complaint by its director. I'll call him Mr M.

What happened

W ran a business under a franchise agreement with a third party. Mr M arranged insurance for W's business through a broker that started in mid-February 2020. An insurer, that I'll call Insurer A, provided the LEI cover. Covea provided business protection insurance that included directors and officers (D&O) cover. The Covea policy renewed in February 2021.

In August 2020 the third party issued legal proceedings against W, Mr M and others in relation to the franchise agreement. W submitted a claim to Insurer A. They declined the claim on grounds the LEI policy didn't cover disputes relating to franchise agreements. In around October 2020 W served a defence to the third party's claim. An amended defence and counterclaim were served in around September 2021.

In late May 2021 W made a claim under the D&O section of the Covea policy for cover in relation to the legal proceedings. Covea declined the claim on grounds of late notification and breach of policy terms and conditions. They said the proceedings were about events that had happened in 2019/2020 – including W's liability for management service fees (MSFs) - which had been going on since August 2020. They'd been deprived of the chance of investigating liability when the allegations were first made. And in breach of the terms and conditions of the policy, W had failed to notify them of the claim and taken steps in the proceedings by serving a defence.

Mr M complained but Covea continued to decline the claim. Mr M brought W's complaint to the Financial Ombudsman Service. That complaint was resolved on the basis Covea would continue to deal with W's claim by appointing a loss adjuster to investigate, whilst reserving their rights to decline the claim for late notification.

Covea reviewed their position following the loss adjusters' report. They said the legal proceedings and surrounding circumstances made it clear there had been a dispute that pre-dated the policy. That was a material fact W should have disclosed to comply with its obligations to present the risk fairly. Covea wouldn't have offered cover at all if they'd known the position and they avoided the policy from the start. W had also failed to tell Covea at renewal about the proceedings that had been issued in August 2020. If they'd known about them, they would have refused to renew the policy. They weren't notified until May 2021. And even if the policy had been in place, they would have declined the claim anyway based on breaches of policy conditions and exclusions.

Mr M said there were no grounds to avoid the policy. There was no pre-existing dispute as Covea had suggested and the proposal form had been signed in good faith. He'd understood he'd notified Covea of the claim as well as Insurer A when he'd initially submitted a claim form, so it wasn't fair to say it had been notified late.

Covea didn't change their minds and Mr M complained again. But Covea confirmed their policy decision was correct. So, Mr M brought W's new complaint to the Financial Ombudsman Service.

Our investigator came to the view there was a pre-existing dispute W should have told Covea about. But Covea had failed to provide sufficient evidence this was a breach that would have led to it refusing cover. In the circumstances, it wasn't fair to find the policy should be avoided from the start. Covea should reinstate the policy, confirm they'd done so in writing and update relevant databases to remove reference to the avoidance.

Our investigator noted Covea relied on certain exclusions. She said it wasn't clear W had been aware of a "claim" as defined in the policy before it took the policy out. And Covea had failed to show it had been prejudiced by the late notification. But she said the claim wasn't covered anyway since W couldn't claim under the D&O section, only the directors could.

Covea didn't agree our investigator's view about avoidance but agreed to take the action she'd suggested and otherwise accepted the outcome. Mr M on behalf of W didn't agree. Since the complaint wasn't resolved, it was passed to me to review afresh. I recently issued a provisional decision, an extract of which follows:

"What I've provisionally 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 acknowledge Mr M's strength of feeling about what's happened. I'm aware he's raised the possibility of claiming on the D&O policy in his capacity as a director of W. To be clear, I'm not addressing that issue. I'm only considering W's complaint about Covea's decision to avoid the policy and decline its claim under the D&O section.

The background to this complaint is well known to the parties. As I've already summarised the key events above, I'll focus here on the reasons for my decision. I've come to an outcome that's broadly the same as our investigator's. But since it differs in part, I'm issuing a provisional decision to give the parties the chance to make further comments before I come to a final decision.

In line with Financial Conduct Authority rules, we expect an insurer to consider claims promptly and fairly and not to decline claims unreasonably. I'll consider W's complaint against that background using headings to make things simpler.

- *Fair presentation of risk*

It was a term of the policy that W should make a fair presentation of the risk when taking out the policy and at renewal. It said:

> '*If **You** fail to make a fair presentation of the risk including failing to disclose or misrepresenting a material fact, or disclosing material facts to **Us** in a way which is not clear and accessible.*
>
> ***We** may avoid this policy and refuse all claims where:*
>
> *a) such failure was deliberate or reckless; or*
>
> b) ***We** would not have entered into this policy on any terms had **You** made a fair presentation of the risk.'*

And it went on to explain what would happen if the policy was avoided.

It's reasonable for an insurer to be presented with information before a policy starts and at renewal that might affect whether or not to provide the insurance and/or the terms and conditions it might agree to and/or the premium it might charge.

Section 4 of the proposal form required W to confirm certain statements about claims and losses were true including, broadly, that there hadn't been any claims against W, its directors or employees in the last five years. And if W was unable to comply with the statement, it was required to declare that as material information at section 7. W didn't provide any information at section 7. Mr M signed the declaration in February 2020 before the policy began.

Covea say W/Mr M knew about the dispute with the third party when Mr M signed the proposal form, they failed to give a fair presentation of risk and Covea wouldn't have offered the policy if they'd known the position.

I've considered what Mr M's said about the definition of claims and MSFs not being in dispute when the policy was taken out. But I can't reasonably ignore the fact Mr M signed the statement of truth to the defence in the court proceedings on W's behalf. It's reasonable to think that the information the defence set out is accurate. And it was reasonable for Covea to conclude from the defence that there was a dispute in relation to the December 2019 and January 2020 MSF invoices that predated the start of the policy that W was aware of, even if other issues in the legal proceedings were only raised at a later date.

W ought to have disclosed that dispute to Covea. So, the declaration in the proposal form was inaccurate. That said, based on Mr M's evidence and bearing in mind the policy terms about fair presentation of risk, I don't think it was deliberate or reckless. So, I've thought about whether Covea have provided sufficient evidence that they would have declined cover if they'd known about the dispute.

Although our investigator asked them to, Covea haven't produced any criteria, a statement from a senior underwriter or other evidence to confirm the non-disclosure induced them into offering insurance they wouldn't otherwise have offered. Since it's up to them to prove that, I don't think it's fair to reach the conclusion they wouldn't have offered insurance at all if they'd known about the dispute.

Mr M's evidence is contradictory about why he didn't pursue the policy claim after Insurer A had declined cover. But, on balance, I don't think he gave any more thought to it until May 2021. I don't think the failure to declare the ongoing proceedings at renewal was deliberate or reckless. Again, Covea haven't provided sufficient evidence to show they would have declined to renew the policy.

In the circumstances, I think Covea should reinstate the policy so that there is no gap in cover, confirm to W in writing that they have done so and take appropriate action to remove any reference to the avoidance from internal and external databases and other records.

From the information Mr M's provided, there's no evidence of any impact on W's insurance options as a direct result of the avoidance. Mr M says he had some difficulties in getting insurance for W, but its premiums don't appear to have been substantively higher. And I need to bear in mind that W would have had to declare the ongoing litigation in taking out insurance later on, which is likely to have affected its renewal terms in any event. In the circumstances, it wouldn't be fair to ask Covea to compensate W.

Since I think Covea unfairly avoided the policy and should reinstate it, I'll go on to consider whether it was reasonable for Covea to decline the claim.

- *Policy cover*

Under the terms of the Covea policy W had, amongst other things, D&O liability cover under section 9. It said:

> *'1.* ***Directors' and Officers' Liability***
>
> ***We*** *agree, subject to the terms, conditions, limitations and exclusions of this Section, to pay on behalf of an* ***Insured Person*** *in respect of his liability for:*
>
> a) *compensatory damages and costs awarded against such* ***Insured Person*** *by a court of tribunal to do so; or*
>
> b) *…*
>
> c) *multiple, exemplary or punitive damages…awarded by a court or tribunal…; or*
>
> d) *settlements comprising any actual or anticipated legal proceedings made with the* ***Insurer's*** *prior written consent (such consent not to be unreasonably withheld); arising solely from a* ***Claim*** *first made during the* ***Period of Insurance,*** *except to the extent that the* ***Company*** *has indemnified the* ***Insured Person*** *in respect of that* ***Claim****.*
>
> ***2. Company Reimbursement***
>
> ***We*** *agree, subject to the terms, conditions, limitations and exclusions of this Section, to indemnify the* ***Company*** *to the extent it has lawfully indemnified an* ***Insured Person*** *for a* ***Claim*** *otherwise* ***Insured*** *under Cover clause 1 of this Section.*
>
> *It is a condition precedent to* ***Our*** *liability that where cover is provided for this section* ***You*** *have complied with any subjectivities or condition precedents set out in* ***Our*** *quotation, unless* ***We*** *agree in writing and endorsed to the* ***Schedule*** *that any such subjectivity or condition precedent shall not be applicable to the* ***Insured****.'*

'***Insured***' meant 'the ***Company*** [W] and the ***Insured Person***'.

'***Insured Person***' meant, in summary, the directors, officers and employees of W, so included Mr M as director of W, but not W itself.

Under '***Clauses***' the policy said:

'*In respect of* ***Claims*** *covered by this Section* ***We*** *also agree, subject to the terms, conditions, limitations and exclusions of this policy, to pay* ***Defence Costs and Expenses*** *which are incurred by an* ***Insured Person*** *with* ***Our*** *prior written consent in the defence, negotiation and settlement of any* ***Claim****.'*

In broad terms the D&O section of the policy provided cover for any damages and third party costs a court might award or Covea might agree should be paid to settle a claim against Mr M and the costs of defending any claim that Mr M might incur. There was no cover for the costs of pursuing a counterclaim. And the cover didn't extend to W.

Section 9 did provide W with cover in respect of any damages and third party costs for which W had "lawfully" reimbursed Mr M. But it didn't cover any defence costs W had paid on Mr M's behalf. So, the policy would only respond to W's claim if it reimbursed Mr M for any third party damages and costs he became liable to pay and subject to the conditions set out.

From what I understand, W hasn't reimbursed Mr M for any third party damages or costs. And even though W may have paid the costs of the solicitors defending the claim on its and Mr M's behalf, W isn't covered for those costs under the policy. So, W has no claim under the policy.

Even if I'm wrong about that, and W does have a claim, I don't think Covea has to pay it. Only defence costs and expenses incurred with Covea's prior written consent were covered under the policy. As far as I'm aware, Covea hasn't authorised any costs and expenses here.

In addition, I think Covea fairly relied on other conditions and exclusions to decline the claim as I'll explain.

- *Policy conditions and exclusions*

Section 9 was subject to terms that were specific to section 9 as well as the general definitions, general conditions, claims conditions and general exclusions applying to the policy overall.

Under ***'Definitions'*** section 9 said:

> *'This section of the policy is on a **Claims** made basis. It applies only to **Claims** first made against the **Insured** during the **Period of Insurance** and notified to **Us** during the **Period of Insurance** or within 30 days thereafter.'*

I've noted Mr M's point that a claim as defined in the policy hadn't arisen until after the policy began. But the court proceedings were issued in August 2020 and included claims against W and Mr M. So, a claim had been made during the 2020/2021 policy period which began on 12 February 2020. And W had to notify the claim to Covea by mid-March 2021 to comply with the policy terms. Since it didn't notify them until May, the claim was notified late.

In addition, the general policy conditions said W must notify Covea immediately of any impending civil proceedings. The claim was set out in a letter from the third party in late February 2020. It wasn't notified to Covea straight away. And W was in breach of that condition.

Even though Mr M thought he'd followed the right process in completing and submitting an Insurer A claim form, Covea weren't told about the claim at the time. Since they weren't responsible for that, it wouldn't be fair to treat the claim as if it had been notified to Covea on time.

In line with the relevant Financial Conduct Authority rules, we'd expect an insurer to show they'd been prejudiced by a late notification before they could decline the claim on that basis.

Here Covea say by the time they were notified the proceedings had gone beyond pleadings, W had made various offers, and had initiated a counterclaim without referring to them. They'd lost the chance of resolving the matter quickly and costs had grown significantly. Mr M said W had put in a valid and strong defence. And Covea had had the chance to be involved in the counterclaim as it wasn't served until October 2021, but they declined.

I've considered the loss adjusters' report. I've noted W made attempts to settle the claim. I've thought about the judge's comments that the parties' costs were already disproportionate when it gave directions in September 2021. And I've noted the costs of making a counterclaim weren't covered under the policy.

Covea had the right under the policy to take over and conduct in W's name the defence or settlement of any claim or to pursue a claim at their own expense. It's reasonable to think Covea would have wished to have input into the case to control the costs incurred and their potential liability to pay the third party's damages and costs if its claim against Mr M succeeded. I can't be certain it would have been possible to reach a settlement. But, on balance, I think Covea would have tried to bring about settlement on commercial terms at an early stage if they'd been involved sooner. Since they were prevented from doing that, and the parties' positions are likely to have become more entrenched as the proceedings have gone on, it's reasonable to say Covea's position is likely to have been prejudiced.

I also think Covea can reasonably decline the claim based on exclusion 4 in the D&O section, which said there was no cover for:

'***4. Existing Claims***

a) *notified or arising out of facts or any circumstance notified (or which ought to have been notified) under any previous policy;*

b) *made, threatened or intimidated against the **Insured** prior to the commencement of the **Period of Insurance**;*

c) *directly or indirectly arising out of facts or a circumstance of which the **Insured** first became aware prior to the **Period of Insurance**, and which the **Insured** knew or ought reasonably to have known had the potential to give rise to a **Claim** under this policy;…'*

As I've explained, based on the defence, there was a dispute about the MSFs that pre-existed the policy and which formed part of the later court proceedings. It's reasonable to think that W was aware or ought reasonably to have been aware that it might lead to a claim under the policy. So, I think it's fair for Covea to rely on the exclusion to decline the claim.

In addition, claims condition 3 said:

> *'**Action by The Insured***
>
> *It is a condition precedent to **Our** liability that **You** shall on the happening of any incident which would result in a claim under this policy:*
>
> *…*
>
> *(d) make no… offer… without **Our** written consent*

*(e) inform **Us** immediately of any … civil proceedings and send to **Us** immediately every relevant document*

…

*(g) produce to **Us** such books of account or other business books or documents or such other proof as may reasonably be required by **Us** for investigating or verifying the claim".*

I agree with Covea that W was in breach of this condition since it hadn't told Covea about the legal claim, it had been involved in negotiations that hadn't produced a settlement and it had taken formal steps in the proceedings. Given the stage the proceedings had reached and the points I've made about prejudice, it was reasonable for Covea to rely on this condition too in declining the claim.

Bearing everything in mind, in summary, I think Covea should reinstate the policy. But, from what I understand, the circumstances that might give rise to a claim under the policy don't currently exist. And, even if they did, for the reasons I've set out, I think Covea can fairly decline the claim.

My provisional decision

I uphold W's complaint in so far as it relates to the avoidance of the policy. To put things right Covea Insurance plc should reinstate W's policy so that there is no gap in cover, confirm to W in writing that they have done so and take appropriate action to remove any reference to the avoidance from internal and external databases and other records.

Covea aren't liable to meet W's claim since W isn't covered under the D&O section of the policy unless and until they "legally" reimburse the "Insured Persons" as defined in the policy for any damages and costs they become liable to pay the third party. Even if W had a valid claim for defence costs they'd paid on Mr M's behalf under that section, Covea could fairly decline it since they hadn't authorised any of the costs incurred. In any event, Covea have fairly declined the claim overall because of W's breaches of the terms and conditions of the policy."

Developments

Mr M responded to my provisional decision on behalf of W. In summary, he made the following points:

1. From what I understand, W has reached or is negotiating a settlement with the third party under which W and Mr M will have to pay some costs.

2. Covea didn't authorise costs as things didn't reach that stage since they didn't accept the claim. W and Mr M still have a valid claim.

3. Covea haven't explained to W how their position has been prejudiced. By the time Covea were notified, only the defence had been filed; permission to file a counterclaim was requested later. Covea weren't prejudiced by late notification since W was in the early stages of litigation and they were notified soon after a strong defence had been filed. Mr M thinks Covea were in a much better position then to reach a settlement but chose not to. Another insurer agreed to pay the costs of another defendant to the third party's claim in similar circumstances.

4. The evidence W has provided relating to previously unpaid MSFs not being chased, the extension of the franchise agreement in February 2020 and the third party not asking for payment until August 2020 show there was no pre-existing dispute about the MSFs that W should have disclosed.

Covea have sent us confirmation from a senior underwriter that had Covea been aware of the true position and been presented with all the information they would not have offered cover at all.

I'll now go on to give my final decision bearing in mind what the parties have said.

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 points Mr M has raised in response to my provisional decision carefully. As I've said, I'm only considering W's complaint, not Mr M's position.

I appreciate W may be responsible for some costs under the terms of the settlement agreement it's been negotiating with the third party, although it's not clear what those costs are. I note too Mr M's point that since the claim hadn't been accepted by Covea, they weren't in a position to authorise any costs. But I don't think that affects the outcome of the complaint. As I explained, W had limited cover. And, in any event, I still think Covea declined the claim fairly for the reasons I set out in my provisional decision.

I explained why I didn't think Covea should be held responsible for the late notification and there's no new information that leads me to change my mind about that.

I'm not persuaded to change my mind either that Covea's position was prejudiced. I've noted what Mr M's said about how a different insurer acted, but I need to consider the individual circumstances of W's case here. I appreciate the court proceedings were at a fairly early stage. And Mr M considers W had a strong defence to the claim putting Covea in a good position to negotiate. But there'd been activity in relation to the dispute before that. And, for the reasons I set out in my provisional decision, I still think Covea's position was prejudiced by what had already happened.

Mr M hasn't made any substantively new points about why he says the MSFs weren't in issue before August 2020. And I've previously noted Mr M signed a statement of truth to the defence from which it was reasonable for Covea to conclude they had been. I'm not persuaded to change my conclusion that W ought to have notified Covea about that before it took out the policy.

I appreciate Covea providing confirmation from a senior underwriter that they wouldn't have offered cover if they'd been aware of all the facts. But they haven't provided any reasons. Without more, I'm not persuaded to change my mind about the avoidance.

Bearing everything in mind, I see no reason to change my provisional outcome. For the reasons I set out in my provisional decision I uphold the complaint in part.

Putting things right

Covea Insurance plc should reinstate W's policy so that there is no gap in cover, confirm to W in writing that they have done so and take appropriate action to remove any reference to the avoidance from internal and external databases and other records.

My final decision

For the reasons I've set out, I uphold this complaint in part and direct Covea Insurance plc to take the action I've set out above to put things right.

Under the rules of the Financial Ombudsman Service, I'm required to ask W to accept or reject my decision before 25 October 2023.

Julia Wilkinson
Ombudsman