DRN-4450619

The complaint

Mr and Mrs S complain Financial & Legal Insurance Company Ltd turned down a claim they made under their 'after the event' (ATE) legal expenses insurance and cancelled the policy from the start.

What happened

Mr and Mrs S bought a property in November 2016. In May 2019 they became aware of the presence of Japanese knotweed. They entered into a conditional fee agreement with solicitors (C) to claim against the vendor of the property. Mr and Mrs S took out an ATE policy with Financial & Legal to cover costs in the event their claim wasn't successful.

Proceedings were issued against the vendor in September 2020. They made a 'drop hands' offer to settle the claim. Financial & Legal agreed that offer should be rejected. The following month C sent Financial & Legal a copy of the defence to the claim made by the vendor. A further 'drop hands' offer was made in August 2021. C says it didn't tell Financial & Legal about this because nothing had changed from the previous offer. In October 2021 Financial & Legal agreed an increase in the limit of indemnity for the policy. A further increase was agreed in February 2022.

C continued to provide Financial & Legal with progress updates and confirmed at the start of October 2022 the case had been scheduled for trial (in December). Later that month Financial & Legal queried why the claim had been raised against the vendor of the property and not the surveyor who acted for Mr and Mrs S (and didn't find knotweed). C explained its reasoning which included that an expert opinion didn't identify negligence on the part of the surveyor.

On 8 November Financial & Legal said it thought it likely the defence of the case would succeed given the surveyor hadn't found knotweed at the premises. And it said it hadn't been provided with the advice C had given Mr and Mrs S as to why a claim had been pursued against the vendor and not the surveyor. It said it only found out the day before about the further 'drop hands' offer which it hadn't been told about earlier and this was a breach of the policy terms. It said it would be cancelling the policy from the outset. I understand the case subsequently progressed to trial where Mr and Mrs S were unsuccessful. Costs were awarded against them in March 2023.

Our investigator noted Financial & Legal had cited four grounds for turning down the claim and cancelling the policy. Having considered those, she didn't think it had acted fairly. In summary she said:

- Financial & Legal said Mr and Mrs S hadn't made a fair presentation of risk because they didn't tell it when taking the policy out legal action had been considered against the surveyor rather than the vendor. And it wouldn't have agreed cover if it had known this.

- However, as this was a consumer contract the relevant law wasn't the Insurance Act 2015 (which refers to a fair presentation of risk) but the Consumer Insurance Disclosure and Representations Act 2012 (CIDRA). She didn't think there had been a qualifying

misrepresentation under its provisions and so didn't think Financial & Legal could avoid the policy or turn down the claim.

- She accepted the terms of business with Mr and Mrs S's solicitor included a requirement for a claim to have 60% prosects of success. But that didn't form part of the contract with Mr and Mrs S which referred to it being more likely than not it would win. There was legal advice to say that was the case and Financial & Legal hadn't provided a contrary legal opinion from someone qualified to do so.

- She agreed Financial & Legal wasn't told about the second 'drop hands' offer until some time after it had been made. That was a breach of the policy terms. However, she didn't think Financial & Legal had been prejudiced as a result. C said there had been no change in the circumstances of the case between the first and second offers. She thought it likely Financial & Legal would also have agreed to reject the second offer.

- C hadn't provided its full file to Financial & Legal when it requested it but they were only days away from the trial starting at that point and said they would send the information they could. Subsequent requests from Financial & Legal were some time after it had made the decision to decline the claim and cancel the policy. Financial & Legal shouldn't have cancelled the policy if it didn't have the information it needed to do so.

She said Financial & Legal should reinstate cover and consider the claim as if that hadn't taken place. Financial & Legal didn't agree. It made detailed comments which I've summarised as follows:

- It drew attention to points in the court judgment which showed Mr and Mrs S had initially sought to pursue a claim against the surveyor which was unsuccessful. It said C had accepted in another case it was involved with this would provide the vendors with a defence. It said it wouldn't have agreed to issue the ATE policy if it had been told about the surveyor claim when the policy was applied for. So it thought it was entitled to avoid this from the outset.

- It said the policy didn't require a legal opinion in order to decide a claim didn't have reasonable prospects of success and decline cover. It was only the decision of the insurer that was relevant here. It said that decision had been taken by an FCA authorised person and managing director of its claims handler who had wide experience.

- It didn't accept he was unqualified to review the prospects of success and said the subsequent outcome at trial supported the concerns he'd raised, in particular the issue of why the claim had been pursued against the vendor and not the surveyor. It thought it had reasonably concluded the chances of failure at trial were greater than the chances of success. It provided correspondence in which it set out concerns about this.

- It didn't accept the legal opinions provided by C or a barrister should be preferred to this. It argued they had a vested interest in the case and were not providing objective advice. And it said C had given positive legal opinions on previous legal cases that hadn't been successful at trial.
- It thought it had formed a reasonable view that Mr and Mrs S were likely to lose at trial which was in line with policy requirements. And the policy didn't cover claims where an insurer informed an insured of that and they continued with the claim without approval.

- The requirement for a claim to have 60% prospects of success was the common benchmark in the ATE industry and was specified in the terms of business. If an insurer didn't have the power to withdraw cover from a policy that had been issued the industry

couldn't survive. It didn't accept Mr and Mrs S weren't aware of the requirement for their claim to meet that requirement as they thought C would have told them about it.

- Even on the basis of advice from counsel (which didn't identify the weakness in the case it believed it had identified) prospects of success were at 55% which didn't meet the requirements in the terms of business. So the case shouldn't have been progressed as a result.

- It was a policy requirement that it was informed of all offers so it had the opportunity to withdraw cover where the prospects of success were insufficient to continue to trial. It drew attention to the policy wording in relation to this. It also disputed C's reasons for not letting it know about this.

- It didn't accept it hadn't been prejudiced by the failure to notify it of the second offer and said if it had been able to review the file it might show that offer should have been accepted. It also said there had been a key change between receipt of the first and second offers which was that a defence to the claim had been filed.

- If the second offer had been presented with a copy of that (which showed the surveyor hadn't found evidence of knotweed) it said it would have insisted on acceptance of the offer which would have prevented the adverse costs that were subsequently awarded against Mr and Mrs S.

- In relation to access to C's file it said it was entitled to request this and quoted relevant sections of the policy. It queried what reason C would have for not providing this. It said it needed this to establish why the claim against the surveyor hadn't been pursued and whether the non-disclosure was reckless. And it said Mr S had been evasive in response to its requests for this information.

It said our outcome had been unfairly influenced by what Mr and Mrs S had told us about their financial circumstances. So I need to reach a 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.

The relevant rules and industry guidelines say Financial & Legal has a responsibility to handle claims promptly and fairly. It shouldn't reject a claim unreasonably

First, I note Financial & Legal has suggested Mr and Mrs S's financial circumstances have influenced our decision making. While I'm naturally sympathetic to what I understand is their difficult situation I want to be clear that has played absolutely no part in my decision on this complaint. I've explained my thinking in this decision and it's those reasons that provide the rationale for the outcome I've reached.

Misrepresentation

Financial & Legal say there was a misrepresentation when Mr and Mrs S took out this policy because it wasn't told a claim against the surveyor had been considered and not pursued. Their policy says the "*the Insured must make a fair presentation of the risk in proposing for, or proposing to vary, this Policy*". And it sets out remedies available to the insurer depending on whether the breach is deliberate or reckless or not. That wording reflects the approach set out in the Insurance Act 2015.

However, while I've taken that into account, I've also taken into account that this was a consumer contract and so the relevant law which applies here isn't the Insurance Act but CIDRA. And the duty of fair presentation isn't one that applies under CIDRA. Instead, it says a consumer has a duty to take reasonable care not to make a misrepresentation. When deciding whether they failed to do so a relevant consideration is how clear and specific an insurer's questions were. So in this case Financial & Legal would need to evidence what question was asked, what answer was given and that the answer given was incorrect.

But it doesn't appear Mr and Mrs S were asked any questions by Financial & Legal when taking out this policy. I've reviewed the information provided at the time which consists of an application form (signed by Mr and Mrs S and C) and a brief assessment of its merits along with supporting information.

I appreciate that form does contain a declaration which says *"we declare that all the information submitted in this form and any accompanying evidence is true and correct to the best of our knowledge and we have not missed out any facts which are likely to affect your decision to provide cover".*

However, Financial & Legal hasn't provided any evidence to show Mr and Mrs S were asked questions which informed their response to that. I don't think it was reasonable to expect Mr and Mrs S to have knowledge of what criteria Financial & Legal would apply when deciding whether to provide cover unless they were given further information about this. I think in particular if it had wanted to know about whether a claim could be brought against any other party it could have asked about this.

So I don't think Financial & Legal has shown there was a failure to take reasonable care by Mr and Mrs S and hasn't demonstrated there was a qualifying misrepresentation. That means I don't need to consider whether Financial & Legal would have entered into the contract if it had known about the surveyor's report. Because there's no qualifying misrepresentation it has no remedy against them and wasn't entitled to cancel their policy.

Prospects of success – what threshold should apply?

The terms and conditions of Mr and Mrs S's policy say "*If the Insurer reasonably forms the view that the Insured is more likely than not to lose the Dispute it shall inform the Representative and provide reasons for their view. If, following receipt of that opinion from Insurer the Insured wants to continue the Dispute the Insured must obtain Insurer's Approval to do so."* So, on the basis of the policy terms, the assessment should be based on whether the claim is more likely than not to be successful.

I appreciate that Schedule 3 of the terms of business agreement between Financial & Legal, C and the broker says that "*prospects of success must be 60% or above based on [C's] due diligence process*". I also accept it's common for ATE policies to contain a prospects of success requirement at that level. And in principle I don't think it's unreasonable for an insurer to withdraw cover for a claim if it becomes clear it doesn't meet the policy requirements as they relate to prospects of success.
The difficulty for Financial & Legal is that Mr and Mrs S's policy doesn't contain the requirement for prospects of success to be 60% and there's no clear reference to them incorporating any separate agreement with their representative. And it's those terms which form the basis of the contract between Mr and Mrs S and Financial &t Legal. I don't know whether C passed on information about the terms of business to Mr and Mrs S but I don't think that's the issue here. I don't think it's fair or reasonable of Financial & Legal to seek to apply wording to the insurance contract it doesn't contain. And I think the assessment of prospects should therefore be based on the 'more likely than not' test the policy contains.

Prospects of success – how should this be assessed?

I appreciate Financial & Legal believes its claims handler was qualified to assess whether the claim had prospects of success. It also says there's no requirement in the policy to obtain a legal opinion in relation to this and it's not within our remit to insert words into the contract it doesn't contain.

However, under our rules (and in particular DISP 3.6.1) I'm required to determine a complaint by reference to what, in my opinion, is fair and reasonable in all of the circumstances of the case. And while I appreciate the policy doesn't specifically say an insurer should obtain a legal opinion on a claim's prospects of success it does say it needs to "*reasonably*" form the view that a claim doesn't have prospects.

It's our long-standing approach (which is clearly set out on our website - and has been for many years) that, because an insurer isn't a legal expert, a claim's prospects of success should be considered by a qualified lawyer who has suitable experience in the relevant area of law. I appreciate Financial & Legal says the managing director of its claims handler has wide experience of ATE policies but I've reviewed the CV it provided and it's clear he's not a qualified lawyer. So I agree with our investigator that he isn't in a position to review whether this claim has prospects of success or not.

I also don't agree with the reasons Financial and Legal gave for not relying on the legal opinions provided by C or the barrister in this case. We often see consumers arguing that because a legal opinion has been provided by a solicitor paid for by an insurer it shouldn't be relied upon. But although the insurer will have paid for the advice the solicitor (or barrister) is independent and acts in line with their professional duties. I don't see why the same logic shouldn't apply to the opinions produced by C and the barrister involved in this case.

If Financial & Legal nevertheless had genuine concerns as to whether the opinion on prospects from C was properly written and reasoned (or conflicted with advice they'd previously given) it might have been reasonable for it to seek its own legal advice. What I don't think it was entitled to do was to turn down the claim on the basis of a view from a claims handler who, whatever other experience he might have, isn't legally qualified, has no listed experience of property litigation and whose background is in finance and accountancy.

The fact his concerns might, to some extent, have been reflected in the subsequent judgment on the case doesn't make a difference to my thinking about the way the claim should have been handled prior to that outcome being reached. At that point the available legal opinions were from C which assessed prospects at 60% and from a barrister who assessed them at 55% both of which met the requirements of Mr and Mrs S's policy.

It follows that I don't agree Financial & Legal was entitled to turn the claim down on the basis the policy terms as they relate to prospects of success hadn't been met. And as I think Financial & Legal wrongly turned down the claim on the basis of insufficient prospects it can't fairly apply the exclusion for not providing cover where an insured continues with a claim after being told that.

The settlement offer

I don't think it's in dispute that although a 'drop hands' offer was made on 24 August 2021 Financial & Legal only appears to have found out about that when C provided a spreadsheet in November 2022 containing a list of offers made on this and other cases. C says it wasn't previously passed on because nothing had changed between the first offer being made (which Financial & Legal agreed could be rejected) and the second.

But the policy says "*The Insured agrees that throughout the Dispute the Insurer shall be allowed direct access to the Representative and that the Insured will instruct the Representative to… report as soon as reasonably practicable all settlement offers made by the Opponent to the Insurer*". And it also says under exclusions "*The Insurer shall not, unless stated otherwise in this Policy, pay any claim under this Policy directly caused by or attributable to… the Insured's decision to reject an offer of settlement without Insurer's Approval*". The policy says 'Insured' has the meaning set out in the policy schedule which is Mr and Mrs S.

I've not seen evidence to show Mr and Mrs S didn't instruct their representative to report settlement offers to Financial & Legal in line with the policy terms. As a result I'm not persuaded they didn't comply with that condition of their policy. But I accept the decision to reject the second settlement offer wasn't done with the approval of Financial & Legal. So I agree there has been a breach of the policy terms here.

However, in considering what's fair and reasonable I think it's also relevant to take into account whether Financial & Legal has been adversely affected (prejudiced) as a result of that. And whether it would have done anything different if it had been notified of the offer at the time it was made. Financial & Legal argues it would. It says while it agreed the first 'drop hands' offer could be rejected, by the time the second offer was made was the vendor had filed a defence which showed the surveyor hadn't found evidence of knotweed. If that had been provided with the second offer it would have insisted on acceptance of this.

I've considered that point. I accept it's possible Financial & Legal would have acted differently if told about the second offer but I don't think it's likely. I say that because the key piece of evidence it's referenced (the defence to the claim) was provided to it on 12 October 2020 which is 10 months prior to the second offer being made. And receipt of that information didn't make any difference to its decision to continue providing cover for the claim. In fact it went on to agree two requests from Mr and Mrs S for an increase to the policy indemnity limit.

Financial & Legal also says a key reason why the policy requires it to be notified of offers is so it can withdraw cover if the prospects of success are insufficient to continue to trial. But I've already found that assessment is one which should be carried out by a qualified lawyer. And the legal opinions available on this claim were supportive of its prospects (as defined in the policy) throughout. So I don't think a proper consideration of prospects would have given Financial & Legal grounds to withdraw cover even if had been notified of the offer as it should have been. It follows that I don't think it can fairly turn down the claim on the basis of this exclusion.

Access to C's file

Financial & Legal says under the terms of the policy it was entitled to see C's file. And the policy does say the Insured will instruct the Representative to "*comply with all requests by the Insurer for information and documents reasonably required by Insurer in connection with the Dispute*". It allows the insurer to cancel the policy if the Insured fails without good reason to meet one of its obligations under this section.

However, the comments Financial & Legal has made primarily focus on C's reasons for not providing information. That isn't the test in the policy. The question is whether Mr and Mrs S have complied with the requirement in the policy which is to instruct C to provide information Financial & Legal reasonably requires.

I don't think its evidenced that didn't happen. Financial & Legal has highlighted an email in which it says Mr S was "*evasive*" but I don't agree. In fact in that email Mr S confirmed he

would continue to instruct C in in line with the obligations set out in the policy and suggested Financial & Legal contact it for the information it needed; he suggested it set out exactly what it needed which I don't think was unreasonable.

In any event the key issue raised at the time of policy cancellation was why the claim hadn't been pursued against the surveyor. I can see C provided a detailed explanation on 11 November and the supporting evidence included the advice it provided to Mr and Mrs S in relation to this. It explained why it didn't think a claim against the surveyor would be successful but that a claim against the vendor could still be pursued.

So I don't think Financial & Legal has shown C didn't provide the information it asked for in November 2022 or that Mr and Mrs S were in breach of the term of their policy relating to this. And I don't think it can use that as a reason for turning down their claim or cancelling the policy. In addition, I don't see any issues it had in obtaining information from C in response to the complaint Mr and Mrs S made can be relevant here. By that stage it had cancelled the policy (and presumably thought it already had the evidence to do so).

Putting things right

For the reasons I've explained I don't agree Financial & Legal was entitled to cancel Mr and Mrs S's policy or to turn down their claim for the reasons it's given. Financial & Legal will therefore need to reinstate the policy from the date it was cancelled and consider Mr and Mrs S's claim in line with the remaining terms and conditions (as if cover hadn't been cancelled).

My final decision

I've decided to uphold this complaint. Financial & Legal Insurance Company Ltd will need to put things right by doing what I've said in this decision.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mrs S and Mr S to accept or reject my decision before 28 December 2023.

James Park
Ombudsman