

The complaint

E, a limited company, complains about the settlement offered by ERGO Versicherung Aktiengesellschaft following a claim on its commercial property insurance policy.

What happened

E took out an insurance policy for an unoccupied commercial property, which was being renovated. Before the work was completed there was a fire which caused extensive damage.

E made a claim on the policy but ERGO rejected the claim and said the policy was void as E had failed to disclose information when renewing the policy. Following a complaint to this Service, an ombudsman issued a decision saying the policy should not have been declared void. He directed ERGO to consider the claim in line with the policy terms.

ERGO later said it would settle the claim on the basis a reasonable cost for the repairs was £180,611. And it said the property was underinsured as the true value of the property was £1,285,868 but the sum insured was £500,000 – 39% of its value. So it paid £70,000, being 39% of the value of the claim.

E didn't agree with the valuation and complained but ERGO didn't change its decision, so the complaint was referred to this Service.

E is represented in the complaint by a claims assessor, who has made a number of submissions in support of the complaint. I won't set them out in full but the key points include:

- E accepts the property was underinsured and is only covered for 39% of the value and ERGO will pay 39% of the claim. It doesn't dispute this.
- The true cost of the repairs is much higher than the figure used by ERGO. As the repairs have been done, it should use the costs incurred, not estimated figures that don't reflect what it actually cost to get the repairs done
- E had to act quickly to deal with the repairs needed to the building and put it to the use originally intended. The work was carried out by a contractor known to the directors of E. As E couldn't finance the repairs itself, that person offered to help. And one of the directors of E carried out work himself to keep the costs down.
- E made payments to contractors totalling £329,919 (excluding VAT) leaving a balance of £156,312 (excluding VAT) which was effectively loaned to E by the contractor.
- The total cost of work done was £486,231 and they have provided copies of invoices confirming this. It's not an estimate – this is the actual cost.
- By refusing cover in the first instance, ERGO prejudiced both its own position and E's position, creating the situation where E had to get the work done without any assistance from its insurer.

- The policy covers “the cost of reinstatement of the property insured” and that’s what should be paid.
- When it calculated the settlement, ERGO said E hadn’t provided any expert evidence in support of its claim. E instructed surveyors to provide an estimate. Their report is more detailed than ERGO’s and the figure they have calculated for the cost of repairs is £517,387. This shows the settlement paid is far too low.

Our investigator said the amount paid by ERGO wasn’t reasonable; E had provided an independent report which provides an estimate that’s very close to the amount claimed. He said the report from E’s surveyors is more detailed and he found it more persuasive than ERGO’s evidence. He recommended that ERGO:

- provide a new offer – based on 39% of the cost, but using the figure of £569,125.78 provided by E’s surveyors, with 8% interest added; and
- pay £500 compensation for the inconvenience E was put to.

E accepted the investigator’s view but said the net figure (not including VAT) for the repairs is £486,456.88. So it is only seeking 39% of that. And E said while it was seeking other costs, if ERGO accepted the view and settled the claim with interest, it would accept that.

ERGO didn’t accept the investigator’s view and requested a decision. It made a number of points, including:

- It had not previously seen the report from E’s surveyor. It considers the claim includes some costs that were associated with the original refurbishment work. It would be ridiculous to suggest the fire caused £500,000 worth of damage.
- It has concerns about the amounts claimed, in particular that the invoices don’t reconcile with the entries on E’s bank statements or show payments made by E for VAT. Bank statements have been redacted and it’s not clear why. Some of the initial invoices are from around the time of the fire and likely covered work done before the fire. So these shouldn’t be included.
- There was no tender and no contract for the works, which is very surprising given how extensive they were.

I issued a provisional decision saying I intended to uphold the complaint but proposing a different remedy from that recommended by the investigator. I set out my reasons as follows:

We provide an informal alternative dispute resolution service and our role is to provide an impartial review, quickly and with minimal formality. I use my judgement to decide what’s fair, based on the main crux of a case. So I won’t comment in detail on every single point that has been raised and will focus on the key points that are relevant to the outcome I’ve reached.

The relevant industry rules and guidance say insurers must deal with claims promptly and fairly; provide reasonable guidance to help a policyholder make a claim and appropriate information on its progress; and not unreasonably reject a claim. They should settle claims promptly once settlement terms are agreed.

E has accepted the property was underinsured and doesn’t dispute that any settlement will be based on 39% of the value of the claim. As that’s not in dispute I don’t need to make a finding on this. What I need to decide is the amount to be used for calculating the settlement.

I’d expect the settlement to put the customer, as far as possible, back in the position they were in before the loss or damage.

The policy terms say claims will be settled by paying “the Cost of Reinstatement of the Property Insured...”

The Cost of Reinstatement is defined as

- I) the rebuilding or replacement of property lost or destroyed which provided Underwriters' liability is not increased may be carried out in any manner You and the Underwriters agree...*
- II) the repair or restoration of property damaged in either case to a condition and design equivalent to or substantially the same as but not better or more extensive than its condition when new...*

So the starting point is that ERGO should be covering what it would cost to carry out repairs to reinstate the property. This should be done in the manner agreed between E and ERGO.

In this case, that didn't happen. Because ERGO initially rejected the claim and said it would void the policy, it had no involvement in the works. This meant it was left to E to sort things out. And due to its financial position the works were done on an ad hoc basis with the contractor, who provided financial support.

It also meant ERGO didn't assess the cost of the repairs at the time. It was only some time later – after repairs works had been carried out – that ERGO instructed surveyors. They estimated the cost of repairs to be around £215,000.

E says the actual cost of the work was much higher and it should be reimbursed for those costs rather than an estimate. I appreciate ERGO had concerns about some of the costs and the invoices provided. This is mentioned in the surveyors' report, which said the invoices don't describe the specific elements of work but provide sums for 'materials' or 'labour'. I can see why ERGO would have wanted to look into this.

Having said that, ERGO suggested E obtain its own expert report and that's what it did. Their report estimates a total repair cost of £569,125.78. This is a long report which provides a summary and then a detailed breakdown of costs item by item. It includes comments from a structural engineer setting out the extent of the damage – including that the vast majority of the roof was destroyed, along with other damage including the loss of some floors and stairs.

There's conflicting evidence about what would be reasonable in terms of repair costs. On balance, I find the report from E's expert more persuasive. The level of detail is greater and provides a better account of the costs involved in repairing this property. And the figure they give is close to the amounts E says it has spent; so it is consistent with that.

ERGO has raised concerns about VAT and questions whether payments were made by E for VAT. E has explained that it is only seeking a settlement based on net figures, not including VAT. We generally think it's fair for the insurer not to include VAT in the settlement but would expect the insurer to pay the VAT added to any insured work if the policyholder has shown it has paid it. In this case, E isn't claiming for VAT so it isn't an issue.

Much of the difficulty in agreeing a settlement figure is down to the fact the claim wasn't initially covered and E was left in the position of having to go ahead with the work without ERGO's involvement. There is some challenge in estimating what would be a reasonable cost of repairs after the event. But overall, I think E and its cost assessor have engaged with ERGO, provided explanations for what was done and obtained an expert report when that was suggested. In the circumstances I think it's fair to base the settlement on the evidence they have provided.

Our investigator recommended that ERGO reconsider its offer using the figure provided by E's expert. As a figure has been given I think it would be fair to direct a payment rather than leave it to ERGO to make a fresh offer. That will bring finality for both parties and avoid the risk of any further dispute.

If the settlement is based on the net figure (not including VAT) of £486,456.88, 39% of that is £189,718. ERGO has already paid £70,000 which would leave a balance of £119,718 which should be paid. As E has been without the use of that money, interest should be added.

I've thought about the period interest should cover. Even if the claim had been accepted earlier, it would have taken some to investigate in any event, particularly given the high value and the concerns ERGO had about some elements. But from the point when E provided the report from the surveyors the claim could have been resolved. In the circumstances I think it would be fair to add interest from then.

Due to the uncertainty around the claim, E had to deal with arrangements for the work and make arrangements with their finance company to restructure the loan that was supporting this. This would have taken the directors away from other activities and caused additional time and effort running their company. So I agree a payment of £500 is fair to compensate E for the inconvenience caused.

For these reasons, I said I intended to uphold the complaint and direct ERGO Versicherung Aktiengesellschaft to pay to E:

- £119,718 to settle the claim, together with simple interest at 8% per year from 14 November 2022 to the date of payment.
- £500 compensation for the inconvenience caused.

Replies to the provisional decision

E's representative has replied saying it welcomed the provisional decision and had only one further comment – that I consider directing ERGO to cover the fee E incurred as a result of having to instruct surveyors to provide a valuation.

The representative says this was a significant cost that was only incurred because ERGO failed to engage with the claim and then refused to settle costs in a reasonable manner.

ERGO has provided some additional comments, including:

- It hasn't seen the report E relied on and so wasn't given the chance to comment on this.
- It repeats the comments about the invoices submitted by E and the issues relating to VAT; the costs could not have been as high as the figure put forward, and it should not have to accept paying a claim which hasn't been substantiated.
- It had offered to resolve the issues about the value of the claim by proposing a joint referral to the RICS Dispute Resolution Service.

ERGO said these were initial comments, subject to considering E's surveyor's report, but no further comments have been received.

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.

Having considered the replies to my provisional decision, I see no reason to change my decision.

ERGO still says E hasn't substantiated its claim. I appreciate ERGO says the figure put forward by E is too high but E obtained expert evidence – as recommended by ERGO – and that evidence was consistent with the value it had put forward.

I set out in my provisional decision why I thought the report E obtained was the more persuasive. ERGO has had a chance to comment on that but hasn't provided any further submissions that persuade me to reach a different conclusion. In the circumstances my view about the weight to be given to the different reports remains the same.

The only additional point made on E's behalf concerns the cost of the surveyor's report. The representative says this was raised in the original complaint submission but hasn't been mentioned.

While this may have been mentioned in the original complaint, in response to the investigator's view E said if ERGO were to progress the claim in line with his recommendations and pay interest, it would accept that in full and final settlement. It seemed to me any additional costs were not, therefore, being pursued. In any event, it's for a policyholder to prove their claim. The claim wasn't agreed and it was reasonable to expect E to provide evidence to support the amounts claimed, particularly given the amounts involved. In the circumstances I don't think it would be fair to expect ERGO to cover that cost.

My final decision

My final decision is that I uphold the complaint and direct ERGO Versicherung Aktiengesellschaft to pay to E:

- £119,718 to settle the claim, together with simple interest at 8% per year from 14 November 2022 to the date of payment.
- £500 compensation for the inconvenience caused.

Under the rules of the Financial Ombudsman Service, I'm required to ask E to accept or reject my decision before 7 June 2024.

Peter Whiteley
Ombudsman