DRN-5462687

The complaint

S, a limited company, complains about the way Covea Insurance plc handled a claim it made on its commercial property insurance policy following a theft.

S is being represented in bringing the complaint by Mrs S, a director of S. Any reference to S includes comments that she has made during the claim and complaint.

What happened

In September 2023 there was a theft at S' property. S made a claim for its losses, for items such as hand tools, laptops and damage to alarms and CCTV. The losses claimed for amounted to around £100,000.

Covea accepted the claim and was making enquiries. In early 2024 Covea issued a final response letter (FRL). This covered S' complaint about delays in the claim being settled, and that Covea had considered cancelling S' policy, before agreeing to provide cover under different terms. Covea didn't agree it had acted unfairly in the way it had handled matters. Following the FRL, Covea made an offer to settle the claim. However, it said the claim settlement would be reduced as the sums insured on the policy were inadequate. It said the building had a sum insured of £150,000, but it felt the reinstatement cost would be £300,000. It said other items, such as hand tools, were also significantly underinsured. Covea offered a settlement, based on its 'average clause' under the policy, of around £33,000.

S complained about the settlement. Covea didn't agree to change its position and so S referred its complaint to the Financial Ombudsman Service for an independent review. Our Investigator didn't think Covea had settled the claim fairly by applying an average clause. She said, as sums insured were set at policy inception and renewal, that principles of misrepresentation, set out in the Insurance Act 2015 (the Act), should be applied. She said whilst Covea considered the correct building sum insured to be 300,000, it hadn't shown this was the case. As such she felt it should settle S' claim for the buildings damage in full for around £10,000.

In relation to the other items, such as hand tools and diagnostic equipment that was stolen, our Investigator was satisfied there was an underinsurance issue. But she said rather than applying the average clause, the fair and reasonable thing to do would be to calculate settlement based on the premiums actually paid, versus what S would have paid if it had declared the true value of the items, in line with the Act. Based on underwriting evidence from Covea, she thought working out settlement this way would result in it needing to pay further £21,468.14, in addition to the claim settlement already paid for those items. Covea didn't accept the outcome and asked for an ombudsman to consider matters. It said settlement should be as per the policy terms, and that invoking the Insurance Act principles relating to fair presentation is a misapplication of the law.

In February 2025 I issued a provisional decision on this complaint. I said whilst I agreed with the general approach of our Investigator, I felt the claim should fairly be settled differently. I said, based on what Covea has already paid, it should pay a further £20,902.67 to resolve the complaint. As my provisional findings form part of my decision, I've copied them below.

Policy cancellation

S did complain that Covea had sought to cancel the insurance, having made the claim, and Covea did consider a complaint about that. However, I don't intend to make any findings in relation to this as part of my decision, as I can't see that this matter is still in dispute. Covea has since offered insurance to S, on slightly different terms. I haven't seen that S has complained about those change in terms, so I haven't considered this as part of my decision.

Should the Insurance Act 2015 apply?

Covea has said S is underinsured. It says the buildings sum insured was about 50% of what it should have been, and most other losses claimed for were also above the sum insured limits on the policy. So, it says, as per its policy terms, that an 'average' should apply to the claim pay out.

This Service takes the view that in order to decide, whether a policyholder took reasonable steps to be adequately insured and whether an insurer can have a remedy for any underinsurance that results, principles of misrepresentation need to be considered. What that means is we'll look at what happened when the policy was arranged and/or renewed, taking into account the relevant legislation in this area. Because this is a commercial policy, the legislation which applies is the Insurance Act 2015 (the Act).

The Act requires the policyholder to make a fair presentation of the risk they present, to the insurer. That means where any detail is given as to an estimated value, it should be given in good faith. I haven't seen any suggestion from Covea that it believes S intentionally set any of the sums insured too low, so I've assumed there isn't an argument as to whether S acted in good faith.

However, the Act also requires the policyholder to tell the insurer "every material circumstance which they know or ought to know", in relation to representation. A sum insured is often caught by that requirement. And in respect of the sum insured the policyholder would be expected to provide a reasonable, estimated value. That is regardless of whether or not the insurer asked a specific question about the sum insured.
It seems to me, at renewal, that Covea didn't ask a specific question about the sums insured. It did, however, set out in the renewal invitation that the sums insured on the policy was very important, and that professional help should be sought to ensure the policyholder isn't underinsured. It also said rebuild costs (for the buildings sum insured) needed to include the cost of clearing the site and professional fees. So that, I think, reasonably put S on notice that the sum insured was important or material to Covea's considerations as to cover. And as the Act, in any event, requires the policyholder to provide a reasonable, estimated value I've considered whether S did so.

Buildings sum insured

The buildings sum insured was set at a declared value of £150,000. S says it carried out some research of how much it would cost to replace the building like for like.
Covea says based on aerial footage of the property showing the size of the main building, using an estimated cost of £750 per square metre, would mean rebuild of the premises would be around £277,000. It said with additional demolition and professional fees costs, this would push the total costs over £300,000.

Having weighed up the comments on both sides, I'm minded to decide S didn't give a fair

presentation of the risk when the policy renewed. Its comments don't persuade me that it took into account, as part of the sum insured, the costs of clearing the site and professional fees. And it hasn't given a reason as to why it considered a rebuild cost of £150,000 to be sufficient. It doesn't seem to have had a survey carried out on the property to determine this figure, for example.

Covea's loss adjuster did say a survey would be needed to accurately assess the correct rebuild cost, but the formula it has applied doesn't seem unreasonable based on an estimate per square metre of the property. So I'm more persuaded by Covea's comments that the correct sum insured would have been £300,000. Which means I don't think S gave a reasonable answer in relation to rebuild costs and so failed in its duty to make a fair presentation of the risk.

As set out above, there's been no suggestion from Covea that S deliberately didn't give a reasonable estimate. But the Act still allows a remedy to Covea of a qualifying breach of the Act. Covea says it is a qualifying breach because, had the sum insured been set at £300,000, it would have charged a higher premium. It's shown its underwriting criteria in support of that. And so, the Act allows, as a remedy, for Covea to proportionately reduce the amount to be paid on a claim.

However, a proportional settlement looks at the percentage of the premium charged for the sum insured chosen, as against that which would have been charged for a fairly presented sum insured. This is not the same as the 'average clause' which Covea has sought to rely on. And whilst an averaged settlement might result in a fair outcome in some circumstances, I'm satisfied that the starting point for Covea acting reasonably, having discovered an instance of underinsurance during a claim, should be to look at what remedy is allowed for by the Act, rather than applying its policy terms.

Having seen what Covea would have charged, had the sum insured been set at £300,000. I intend to decide S paid 51% of what the premium would have been. And so, I intend to say Covea can fairly settle this part of the claim at £5,438.21, which is 51% of the loss claimed for under this section. Contents claim

The policy sets out that other items claimed for are considered as 'contents'. For clarity, the losses claimed for in relation to contents were for the following (I've included the relevant sums insured next to the amounts):

- *Customer vehicles - £1,080 (£100,000)*
- *Diagnostic equipment - £12,771.56 (£10,000)*
- *Portable hand tools - £72,925.15 (£35,000)*
- *Electronic equipment - £7,670.37 (£4,500)*

In relation to "customer vehicles" Covea has paid this part of the claim in full, it was satisfied there was no underinsurance issue, so I haven't considered that further.
However, it's said the other items were underinsured, and so in line with the policy terms it has offered settlement for these using an average. So I've considered whether it acted fairly and reasonably in doing so, applying, as I have above, the principles of the Insurance Act 2015.

<u>Diagnostic equipment</u>

Having reviewed the available evidence, I'm minded to decide S gave a fair presentation of the risk in relation to this at renewal in 2022. The sum insured for this equipment was £10,000. The loss presented was for £12,771.56. When the loss adjuster attended S' premises at the start of the claim and reviewed the loss list for this equipment, his report is

noted to have concluded "the diagnostic sum insured…would appear to be marginally adequate on the basis of the policy cover". Given the comments that its marginally adequate, I'm minded to decide that S gave a reasonable estimate, in line with the Act, in relation to the value of the diagnostic equipment. And so I intend to decide it did give a fair presentation of the risk.

There were several diagnostic equipment items which added up to the total loss claimed. And I consider it reasonable that the value of those items may fluctuate over a policy year, and that small differences in value for each item have then added up to the difference between the sum insured amount, and the loss value claimed. But I'm not currently persuaded this means S gave an unreasonable estimate, in line with the principles of the Act. And as Covea's loss adjuster found the overall sum insured to be adequate, I intend to decide S gave a fair presentation of the risk. And so there is no remedy available to Covea under the Act for this claim amount. As such I don't think it would be fair or reasonable for Covea to apply the average clause, in the policy, to this part of the claim to proportionally settle it.

So, I intend to decide that Covea should settle the claim for diagnostic equipment in full, but up to the policy limit of £10,000. Whilst I understand the loss suffered was greater than this amount, S paid its premium on the basis of £10,000 worth of cover. I also think the policy documents adequately put S on notice that in the event of the value of the contents exceeding £10,000, £10,000 would be the most Covea would be liable to pay for an accepted claim. Which means I think it would be fair, in this instance, for the settlement Covea needs to pay, to be capped at £10,000.

<u>Portable hand tools</u>

Like our Investigator I'm minded to decide that the sum insured for the hand tools was incorrect, and that there has been a breach in the duty to make a fair presentation of the risk in relation to the portable hand tools. The sum insured was £35,000, S had asked (as part of the 2023 renewal process) to increase the sum insured for these tools to in excess of £100,000. So I think this shows its most likely it didn't give a fair presentation of the risk at the previous renewal, as the value of the tools it owned was significantly higher than what it had insured for. And I intend to say there has been a qualifying breach of the Act, as Covea has shown it would have offered the insurance on different terms and charged a higher premium for the cover.

However, S has said many of those tools claimed for were purchased in the policy year of 2022, so the value presented at the start of the policy was the right one. Even if I accept that it did make a fair presentation in 2022, but then purchased additional tools during the policy year which accounted for the change in value, I think S should have made Covea aware of the purchase of those additional tools. I say this as I consider it most likely that would be a fundamental change to the risk, given the increase in the value of tools held on site.

S' policy terms also say it must tell Covea of any changes which affect insurance since the policy started or last renewed. I intend to decide that such an increase in the value of tools held on site would be something Covea would want to know about, and S should have disclosed during the policy term. Had S done so, I think it's most likely Covea would have altered the terms of the policy and charged a higher premium to reflect the increase in risk. So whether I find there was a breach of fair presentation at renewal, or a breach of the policy terms to notify Covea of changes, I consider it most likely that the outcome would be the same.

Covea has shown it would have acted differently had it known the value of the tools was over £100,000, and it would have charged a much higher premium. So, under the Act, it's

shown S' breach would be a qualifying one, or that it presented a fundamental change to the risk. As such I think the fair and reasonable outcome would be for Covea to proportionately settle the claim, in line with the principles set out in the Insurance Act 2015. Covea has said if it had known the value of the tools, it would have charged a higher premium, such that S only paid 48.9% of what the premium should have been for adequate cover.

When calculating the proportional settlement on this basis, our Investigator said the amount to be paid under this part of the claim would be £35,660.40. However, there is a policy limit that applies to this section of £35,000. And as S only paid the premium equivalent to this level of cover, I consider the fair and reasonable outcome would be for Covea to pay £35,000 for this part of the claim.

Electronic equipment

The sum insured for electronic equipment was £4,500. The loss presented to Covea was for £7,670.37. Again, applying the principles of misrepresentation based on the Act, I think the information provided by S at renewal in relation to this figure was incorrect. And I think it's most likely S didn't give a fair presentation of this risk at renewal or provide a reasonable answer in relation to this. S hasn't given a reason as to why it thought £4,500 was a reasonable estimate for those tools. And Covea has shown that, had S given a fair presentation, it would have charged a higher premium for the cover, so it has shown there was a qualifying misrepresentation under the Act. And as such it has the available remedy of proportionate settlement. Based on the premiums paid compared with what Covea would have charged had a fair presentation been given, I'm minded to decide S paid 37% of the premium it would have been charged. And so Covea can fairly settle the claim for electronic equipment costs at £2,838.04.

Putting matters right

I intend to decide Covea should settle the claim on the following basis (including items already agreed):
- *£5,438.21 for buildings*
- *£1,080 for customer vehicles*
- *£10,000 for diagnostic equipment*
- *£35,000 for hand tools*
- *£2,838.04 for electronic equipment*

Responses to my provisional decision

S said it accepted what I'd set out in my provisional decision. Covea didn't. It said there was caselaw (*Economides v Commercial Assurance Co plc 1997)* which supported that a average clause should be applied to instances of underinsurance. It said I was confusing an insurer's ability to avoid a policy due to misrepresentation, and the ability to apply a contractual claims condition.

It also said that it had spotted an error in the way it had previously calculated the 'hand tools' settlement. It said once that was corrected, the difference between settlement based on the average clause or by applying the principles of misrepresentation was very little. It also said given the amounts it had paid, and the excess, that the remaining payable was £20,802.67, rather than the figure quoted in my provisional findings (which was £20,902.67). It said would raise the payment.

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'm aware of the case of *Economides v Commercial Assurance Co plc 1997* as quoted by Covea. I'd already taken that into account when providing my provisional findings. And I don't agree that I am confusing an ability to avoid a policy based on misrepresentation principles with an insurer's ability to apply contractual terms. I recognise these are two different options an insurer can take. However, there may be situations in which one option is relevant to the other, or they otherwise overlap or interact with one another.

I accept some comments were made in the *Economides* judgment relating to underinsurance and averaging. However, I also note that that caselaw predates the Insurance Act 2015 ("The Act)". The Act significantly changed the legal position in relation to commercial misrepresentation cases.

In summary, Covea has reduced the claim settlement offer because it considers some of the sums insured set at the 2023 renewal were insufficient. The Act sets out the duty on the commercial customer to provide certain information at the renewal – and the remedies available to the insurer if the commercial customer doesn't fulfil that duty. That information can include, amongst other things, sums insured. As a result, I consider it relevant to consider the Act, as well as what's fair and reasonable in all the circumstances.

If I didn't consider the Act, a position could be reached whereby S fulfilled the duty set out by the Act at the 2023 renewal in relation to the sum insured. And that would mean, under the Act, Covea had no remedy – and couldn't reduce the claim settlement. Yet, by relying on a policy term, Covea could nonetheless reduce the claim settlement because of the sum insured. In such a position, the policy terms would effectively give Covea rights it doesn't have under the Act – and could mean Covea acts contrary to the Act, and in a way which disadvantages S compared to the Act. I'd have to consider whether that treated S fairly.

The Act contains a section which says a contractual term which puts the insured in a worse position than it would be under the terms of the Act is of no effect, unless the transparency requirements are met. So, I consider that the Act is clear that *any* term which may disadvantage a commercial customer – beyond the remedies set out in the Act – can *only* be applied if the transparency requirements are met. As such I'm persuaded it's most likely the Act has contemplated the possibility that policy terms may exist which would put a commercial customer in a worse position that the Act. And as a result it has specified that such terms can only be applied if certain requirements have been met.

I consider Covea's average clause is disadvantageous compared to the Act. For example, in relation to diagnostic tools, following the principles of the Insurance Act S will receive a settlement of £35,000. Whereas under the policy terms, applying an average clause would mean the settlement for this part of the claim would be around £16,700. So clearly, S is disadvantaged by Covea acting outside of the Act by applying policy terms that puts it in a worse position than what the Act allows for.

As far as I've seen, Covea hasn't suggested in response to my provisional findings that it has met, or tried to meet, the transparency requirements, as noted in the Act. As such, I consider it hasn't shown that it has acted in compliance with the Act. So it follows that it must follow the remedies set out in the Act, as I've set out in my provisional decision.

I accept the policy term allows for averaging, and I accept that the caselaw provided by Covea might be considered as an endorsement of that. But my role is to consider whether it would be fair and reasonable for Covea to rely on its policy term, given the particular circumstances of this complaint. And I'm not persuaded it would be. To say it was fair for Covea to rely on its averaging clause would, I consider, disregard the current law and the disadvantages that would result for S. So I don't consider that to be a fair and reasonable

outcome. As such my provisional findings, as well as my comments set out above, form part of this, my final decision.

In relation to the settlement, it seems I did do a slight miscalculation in my provisional findings. I'm satisfied the outstanding amount for Covea to pay to settle the claim is £20,802.67 (if it hasn't done so already, as it suggested it would on receipt of my provisional decision). It will also need to add 8% simple interest* onto that amount from the date the claim was settled, until the date of settlement.

My final decision

My final decision is that Covea Insurance plc needs to pay the remaining 20,802.67 in order to resolve the complaint, unless it has done so already.

*Interest is at a rate of 8% simple per year and paid on the amounts specified and from/to the dates stated. HM Revenue & Customs may require Covea to take off tax from this interest. If asked, it must give S a certificate showing how much tax it's taken off.

Under the rules of the Financial Ombudsman Service, I'm required to ask S to accept or reject my decision before 5 May 2025.

Michelle Henderson
Ombudsman