

The complaint

Mr and Mrs A are unhappy that AXA Insurance UK Plc is seeking to proportionately reduce the settlement they are due under a claim they made for subsidence damage to their home.

What happened

Mr and Mrs A held a home insurance policy with AXA which was inceptioned in February 2021 and renewed in February 2022. In October 2022, Mr and Mrs A logged a claim with AXA for cracking damage to their home.

AXA appointed various experts to investigate the damage and validate the claim on its behalf. It was accepted that the damage likely resulted from subsidence, which is an insured peril covered under the policy. But concerns arose over the level of cover Mr and Mrs A had. When they took out the policy, Mr and Mrs A said the cost to rebuild their home was £200k, whereas AXA's experts initially estimated this ought to have been closer to £530k.

It later became clear that the £530k estimate was based on incorrect measurements. AXA said using the correct measurements, the cost to rebuild Mr and Mrs A's property using the same materials would be around £622k. But it also acknowledged their home wasn't listed, and so wouldn't necessarily need to be rebuilt using the same materials. If it wasn't, AXA said the rebuild cost would be around £445k. Based on this, AXA concluded Mr and Mrs A were underinsured.

Mr and Mrs A complained that they got the rebuild figure from the calculator they were provided with at the point of sale. AXA maintained that they were underinsured but ultimately agreed to settle 81% of their claim, which it felt was fair in the circumstances. Mr and Mrs A didn't accept this, and so brought their complaint to the Financial Ombudsman Service.

Our investigator thought Mr and Mrs A's complaint should be upheld. She agreed that Mr and Mrs A were underinsured, and that in principle it was fair for AXA to proportionately reduce the settlement based on the difference between the premiums they paid, and the premiums they would have paid had they given a more reasonable estimate of the cost to rebuild their property. But she said the figures AXA was relying on to demonstrate what the premium would have been weren't fair, because they were based on rebuild costs at the point she requested evidence of them, rather than the point of the 2022 renewal. Our investigator said it was for AXA to demonstrate the impact Mr and Mrs A being underinsured would have had on the premiums at the point of the relevant renewal and, if it couldn't do this, it was unfair to proportionately settle the claim.

AXA said it can only ever obtain a live rebuild cost from the tools it uses and so it couldn't recalculate the rebuild cost from the point of renewal. But it said it had treated Mr and Mrs A more than fairly by offering 81% of the claim, given that under its "average" clause, it would be entitled to settle the claim based on the difference between declared rebuild cost and the "actual" rebuild cost, which would result in a proportionate settlement of 30%.

Our investigator maintained that any proportionate reduction should only fairly be based on the difference between the premiums, not the difference between the rebuild estimates. She maintained that AXA needed to demonstrate what the rebuild estimate ought to have been (and the premiums it would have charged as a result) from the point of renewal. And she maintained that because it couldn't do this, it should pay 100% of the claim.

AXA didn't accept our investigator's opinion. So, as no agreement has been reached, the complaint has been passed to me to decide.

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.

Mr and Mrs A's policy was sold via a broker. I want to be clear here that this complaint focuses solely on AXA and the things it was responsible for as Mr and Mrs A's insurer. So, I'll not be making any findings on anything the broker was responsible for under this complaint.

Mr and Mrs A's subsidence claim was made in October 2022 and so it's the information provided at the February 2022 renewal which is key. It's not in dispute that AXA made it clear to the broker that it wanted to know the rebuild cost of Mr and Mrs A's property, nor that they understood this was what they needed to provide.

I should acknowledge here that the estimated cost to rebuild a building is a matter of opinion, rather than a matter of fact. I say this because multiple qualified experts could be asked to estimate the rebuild cost of a building, and it would be unlikely that they'd all arrive at the exact same figure. This wouldn't mean that any were correct or incorrect, and all could be considered reasonable estimates, as they'd have been made by someone with adequate expertise. So, when considering this complaint, I'm not deciding whether Mr and Mrs A provided an incorrect or inaccurate figure. Instead, I'm considering whether they provided a reasonable estimate made in good faith. What I mean by this, is an estimate with sufficient reasonable basis.

At the point of the 2022 renewal, the rebuild figure Mr and Mrs A provided was £200k. They say this was based on the rebuild calculator they were provided when they first took out the policy in 2021. But I've not been provided with any evidence to support that this same figure from 2021 would be a reasonable estimate of the rebuild cost in February 2022, such as evidence of the tool being used again at that stage. Based on this lack of evidence, I'm persuaded that Mr and Mrs A didn't provide a reasonable estimate of the rebuild cost during the 2022 renewal.

Where a customer fails to provide a reasonable estimate of the rebuild costs/sums insured, most home insurance policies (including Mr and Mrs A's) include an "average clause". This is a term which explains that insurers will proportionately settle any claims made based on the difference between the declared rebuild cost and the "correct" or more reasonable estimate of the rebuild cost.

However, the Financial Ombudsman Service has a well-established approach to dealing with this type of underinsurance. That is that where a consumer is underinsured, and the insurer can demonstrate that the underinsurance would have increased the cost of the policy, insurers can fairly and reasonably proportionately reduce any claim settlement based on the difference between the premiums it received, and the premiums it would have received had they made a reasonable estimate of the rebuild cost. This approach is in line with the relevant insurance law which covers the sale and renewal of insurance contracts.

AXA has argued that the relevant law around sales and renewals doesn't supersede its average clause, and so it would be entitled to apply its average clause in this case. However, it says it has treated Mr and Mrs A fairly by basing its proportionate settlement offer on the difference between the premiums, in line with our service's approach.

To be clear, I accept that on a strict application of the policy terms, AXA could apply its average clause. But as an ombudsman I'm not bound by a strict application of the policy terms. Rather, my role is to decide what is fair and reasonable in all the circumstances. And I don't consider that it would be fair for AXA to apply its average clause in circumstances where this would mean it had received (based on its calculations) 81% of the required premiums but would only be paying 30% of the claim as I don't think this would be equitable or reasonable. However, as explained, despite making this argument, AXA has made an offer based on the difference in premiums anyway.

Mr and Mrs A paid £414.87 in premiums for the 2022 policy year based on the £200k rebuild cost they declared. AXA says that had they provided the "correct" rebuild cost of £622,693, it would have charged £480.76. Based on this it says a fair, proportionate settlement is 81% of the claim.

Our investigator highlighted some concerns with AXA's calculations, including how insurance premium tax had been factored into the figures it based its calculations on. But primarily, she said the rebuild cost AXA was basing its settlement calculation on didn't represent the rebuild cost at the point of the renewal and so this wasn't fair to Mr and Mrs A.

Notwithstanding the other potential issues with AXA's calculations, which AXA has subsequently clarified, I agree with our investigator that it's ultimately for AXA to demonstrate how the premium it received has been impacted by Mr and Mrs A's rebuild cost being inadequate, if it wants to proportionately reduce the settlement. And this needs to be based on what the declared rebuild cost ought to have been at the point of renewal (February 2022) not after the point of the claim and complaint, in January 2023, when AXA ran these calculations. This is because it's likely the rebuild cost would have increased in that time, and so relying on a more recent estimate of the rebuild cost is likely to be unfairly detrimental to Mr and Mrs A.

In my experience, insurers are usually able to provide rebuild estimates from a set point in time. They typically do this by using older rebuild rates, deducting for rebuild inflation, getting a professional to make a judgement or a combination of these. But AXA hasn't done any of these and has instead relied on an estimate of the rebuild cost from 2023 which as explained I don't think is fair.

AXA has recently said that if it were to deduct the rebuild inflation, it would bring the rebuild cost down to £321,362.13. It says this would bring the premium down to below what Mr and Mrs A actually paid. I'm unsure how or why this is the case, given they declared £200k which is still somewhat lower than the inflation adjusted figure above. But regardless, I think it supports that AXA has been unable to sufficiently demonstrate that the premiums it would have charged in February 2022 would have been impacted in such a way as to make it fair for it to proportionately reduce Mr and Mrs A's claim settlement.

So, while I accept Mr and Mrs A were underinsured, and that this would likely have had an impact on the premiums AXA would have charged, AXA hasn't been able to demonstrate that it would have charged a higher premium (or what that higher premium would have been) based on a more reasonable estimate of the rebuild cost being provided in February 2022. Because it hasn't, I don't think it would be fair or reasonable to proportionally settle Mr and Mrs A's claim, at all, in the circumstances of this complaint.

Aside from the claim decision, AXA has accepted that it wasn't as clear as it could have been when communicating the proportionate reduction to Mr and Mrs A, which left them avoidably unclear about what was going on at one point. When it referred its complaint file to us, it acknowledged this and offered to pay Mr and Mrs A £25 compensation to reflect this. I think this offer is fair for this issue.

My final decision

For the reasons explained above, I uphold Mr and Mrs A's complaint.

AXA Insurance UK Plc must:

- Settle Mr and Mrs A's claim without applying any proportionate reduction for underinsurance.
- Pay Mr and Mrs A £25 compensation for the distress and inconvenience it has caused them – if it hasn't already done so.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr and Mrs A to accept or reject my decision before 29 July 2024.

Adam Golding
Ombudsman