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ONE FOR TEN DOLLARS, TWO FOR THIRTY: THE VALUE OF THE NATIONAL FLOOD INSURANCE PROGRAM DWELLING POLICY FOR THE INSURED

*Matthew J. Kutner**

I. INTRODUCTION

Attaching “national” to flood insurance is a strange concept, if one really thinks about it. Insurance protection against flood damage is quite a different beast on coastal Long Island, New York, and Florida, than, say, an area within a desert climate in the southwest United States. Yet, geography does not play a role in the standard flood policy’s terms and conditions. A one-size-fits-all national program is what we have. Ninety percent of all natural disasters in the United States are flood-related,¹ and, for over forty years, the federal government has been intimately involved in the provision of flood insurance since the creation of the National Flood Insurance Program (“NFIP”).²

The insurance industry, in general, achieves profitability by taking in more money from policy premium payments than it pays out for claims from covered damages. The actuarial risk of having to pay claims determines, in part, what premium the insured is charged. This is also a strange concept for the federal government—we call its antithesis

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1. Saul Jay Singer, *Flooding the Fifth Amendment: The National Flood Insurance Program and the “Takings” Clause*, 17 B.C. ENVTL. AFF. L. REV. 323, 325 (1990).

2. The NFIP is codified at 42 U.S.C. §§ 4001–4129 (2006), and is implemented through the Federal Emergency Management Agency’s (“FEMA”) regulations at 44 C.F.R. §§ 59–79 (2013).

“deficit spending,” and this is current federal fiscal policy. Without being able to spend more than it receives, the federal government could not operate.³ Like the federal government, the NFIP is not profitable.⁴

It is because of the lack of profitability of the flood insurance market that the federal government occupied the void left behind by fleeing private flood insurers.⁵ However, government involvement in the insurance business is not for reasons of profitability, but for reasons of public policy.⁶ The Biggert-Waters Flood Insurance Reform Act of 2012 (“Biggert-Waters”)⁷ aimed to change this. Whereas NFIP policy premiums are set by federal law and, in large part, are subsidized, Biggert-Waters amended that policy to bring premium costs more in-line with the actual risk of flood damage using actuarial rates.⁸ Both conservative free-market groups and traditionally progressive environmental groups supported Biggert-Waters with enthusiasm;⁹ the typical “customer” probably never heard of it. Although Biggert-Waters was recently amended by the Homeowner Flood Insurance Affordability Act of 2014,¹⁰ NFIP premium increases are imminent. While paying more for something, by itself, is not necessarily a bad thing, paying more for the same, inadequate thing is; free-marketers and environmentalists would probably agree with that, too.

II. BEDFELLOWS

For New Yorkers impacted by Superstorm Sandy (“Sandy”) in late October 2012 and Hurricane Irene (“Irene”) in the summer of 2011, flood insurance coverage is an intimate topic. I experienced the NFIP beginning shortly after Sandy as a Staff Attorney in the New York Legal Assistance Group’s Storm Response Unit (“SRU”), where I, and approximately thirty other attorneys and advocates within SRU, currently assist and represent clients with Sandy-related legal issues and

3. See Doug Bandow, *Budget Reform in Reverse: Congress Prepares to Hike Flood Insurance Subsidies*, FORBES (Sept. 14, 2014, 10:00 AM), <http://www.forbes.com/sites/dougbandow/2014/02/24/budget-reform-in-reverse-congress-prepares-to-hike-flood-insurance-subsidies/2>.

4. See *id.*

5. § 4001(b).

6. Christine M. McMillan, Comment, *Federal Flood Insurance Policy: Making Matters Worse*, 44 HOUS. L. REV. 471, 486 (2007).

7. Pub. L. No. 112-141, 126 Stat. 916 (codified as amended at 42 U.S.C. §§ 4001–4130 (2012)).

8. See 126 Stat. at 921.

9. Eli Lehrer, *Strange Bedfellows: Smartersafer.org and the Biggert-Waters Act of 2012*, 23 DUKE ENVTL. L. & POL’Y F. 351, 353-54 (2013).

10. Homeowner Flood Insurance Affordability Act of 2014, H.R. 3370, 113th Cong. (2014).

disputes, at no cost, in all five boroughs of New York City and Long Island. When the second “flood” arrived after Sandy—clients with questions, and, later, disputes with their flood insurance carriers—we quickly learned of the NFIP’s limitations.

One would think that a flood insurance policy written and regulated by federal law would be friendly to homeowners given the public policy and not-for-profit motivations of the federal government. But this would be wrong. One would also think that, under such a government program, if property was lost or damaged because of a flood, no matter to what or where, flood insurance would pay for the repair or replacement. Wrong again. In fact, the flood policy explicitly excludes coverage for some of the most costly damages.¹¹ If two identical homes, with identical damage and flood coverage filed identical claims for damage, they should get the same amount of money for repairs or replacement, right? Not necessarily. In part, this is because of another quirk of the NFIP—most policies are purchased from Write Your Own (“WYO”) carriers, and the policies are *backed* by the federal government.¹²

WYO carriers, such as State Farm, Allstate, Travelers, and a host of other commonly known insurance companies, administer the NFIP by utilizing the services of the independent adjusting community.¹³ In exchange for the retention of a portion of the premium to cover costs, WYO carriers sell flood policies, and the remaining premium balance is then forwarded to the federal government.¹⁴ For example, despite a homeowner having purchased a flood policy from Allstate, it is really the federal government that retains the financial risk of insuring the home.¹⁵ It is also, ultimately, the obligation of the federal government to pay the claim.¹⁶ Allstate, for example, using the independent adjusting community, may be the entity responsible for adjusting, assessing, and processing claims, but the end-payor is the federal government. Allstate and State Farm, for example, using their own respective independent adjusting communities, may pay different settlements for identical claims—adjustors, like lawyers, differ as to opinions on interpretation and causation.

11. See 44 C.F.R. pt. 61 app. A(1) (2013).

12. FED. EMERGENCY MGMT. AGENCY, NATIONAL FLOOD INSURANCE PROGRAM ADJUSTER CLAIMS MANUAL, at I-1 (2013), available at http://www.fema.gov/media-library-data/77c3a96a9c5e2e4b50bc9e1f958c5c48/adjclaimsmanual_part1_508rev_12sep13.pdf (“The WYO Program now accounts for approximately 90 percent of all flood policies.”); McMillan, *supra* note 6, at 489.

13. See FED. EMERGENCY MGMT. AGENCY, *supra* note 12, at II-1.

14. McMillan, *supra* note 6, at 489; see also 44 C.F.R. §§ 62.23–.24.

15. 44 C.F.R. pt. 62 app. A (2013).

16. *Id.*

III. NATIONAL FLOOD INSURANCE PROGRAM POLICY SPECIFICS

There are two main types of coverage that a standard NFIP Dwelling¹⁷ Form (“Policy”) offers: (1) coverage for the structure of the property of up to \$250,000; and (2) coverage for contents or personal property of up to \$100,000.¹⁸ The Policy pays for direct physical damage to the insured property, as a result of a “flood,”¹⁹ up to the replacement cost or actual cash value of the actual damages of the Policy.²⁰

In addition to exclusions caused by carve-outs within specific coverage provisions and narrowly defined terms, the Policy explicitly lays out exclusions.²¹ The Policy excludes a common, costly occurrence: “earth movement even if the earth movement is caused by flood.”²² In other words, if a tidal surge (a flood) washed away the “earth” that encased a home’s foundation, causing the foundation and the home to destabilize, shift, or crack, despite sustaining potentially hundreds of thousands of dollars in damages, the insured, under the Policy, could be paid *nothing* for this damage. To be clear, the Policy excludes additional types of occurrences and property from coverage that a reasonable homeowner would assume to be covered under a “flood” insurance policy, and this is but one example. I have little doubt that these exclusions are policy determinations by NFIP administrators to save money—odd, given the federal government’s public policy motivations.

As a result of the apparent flood insurance public policy to make homeowners whole as infrequently as possible, homeowners are left with large funding gaps for repairs, rebuilding, and recovery, and few options to rely upon to fill that gap. After Sandy, and, in no small part because of New York Governor Andrew Cuomo (a former United States Secretary of Housing and Urban Development (“HUD”)), the federal government made billions of dollars available to

17. “Dwelling,” under the Policy, is defined as: “A building designed for use as a residence for no more than four families or a single-family unit in a building under a condominium form of ownership.” 44 C.F.R. pt. 61 app. A(1) (2013).

18. *Id.*

19. “Flood,” under the policy, is defined to mean:

1. A general and temporary condition of partial or complete inundation of two or more acres of normally dry land area . . . from: a. Overflow of inland or tidal waters, b. Unusual and rapid accumulation or runoff of surface waters from any source, c. Mudflow. 2. Collapse or subsidence of land along the shore of a lake or similar body of water as a result of erosion or undermining caused by waves or currents of water exceeding anticipated cyclical levels that result in a flood as defined in A.1.a. above.

Id.

20. *See id.*

21. *Id.*

22. *Id.*

New York through Community Development Block Grant Disaster Recovery (“CDBG-DR”).²³

With these funds, two programs for disaster recovery assistance arose: Build It Back (“BIB”), the program specifically for Sandy victims in New York City; and NY Rising, the program for Sandy victims in every Sandy-impacted area *other than* New York City,²⁴ including Long Island. Like many programs funded by federal taxpayer dollars, the federal government released the CDBG-DR funds with a host of restrictions and regulations, which must be followed.²⁵ Some of these restrictions are beneficial, while others are onerous. Operating according to these rules, it becomes the responsibility of the receiving municipality (New York State and New York City) to design, create, and implement these programs—which is no small task.²⁶ Bear in mind, however, that like the NFIP, these funds draw from the very same account from which NFIP claims pay, the U.S. Treasury. As we will see, a homeowner that filed a claim for flood damages under their NFIP policy, but received *nothing* because of the Policy’s “earth movement” exclusion,²⁷ could be eligible to receive the full amount of money necessary for repairs under programs funded by CDBG-DR funds.²⁸

IV. COMMUNITY DEVELOPMENT BLOCK GRANT DISASTER RECOVERY FUNDS

In this Part, I will focus on the NY Rising program’s development and some of its policy determinations for spending CDBG-DR funds.²⁹

On January 29, 2013, Congress made \$16 billion of CDBG-DR funds available to states, including New York, to cover damages caused, in part, by Sandy.³⁰ As a CDBG-DR grantee, New York was required to

23. See generally Disaster Relief Appropriations Act, 2013 Pub. L. No. 113-2, 127 Stat. 4 (Jan. 29, 2013).

24. Note, however, that BIB applicants may also have the option to sell their Sandy-damaged properties to the state. Interested applicants are transferred from BIB to NY Rising. See *Acquisition for Redevelopment Program*, N.Y.C. RECOVERY, <http://www.nyc.gov/html/recovery/html/homeowners/acquisition-for-redevelopment.shtml> (last visited Nov. 23, 2014).

25. Requirements for Grantees Receiving Community Development Block Grant (CDBG) Disaster Recovery Funds in Response to Hurricane Sandy, 78 Fed. Reg. 14,329-48 (effective Mar. 11, 2013) [hereinafter Requirements for Grantees Receiving CDBG].

26. *Id.* at 14,330.

27. See *supra* text accompanying notes 21-22.

28. See *infra* text accompanying note 35.

29. For more information on BIB, see the BIB website, which contains excellent resources and publications that explain the program and eligibility criteria. See *Welcome to NYC Recovery*, NY RISING, <http://www.nyc.gov/recovery> (last visited Nov. 23, 2014).

30. See generally Disaster Relief Appropriations Act, 2013 Pub. L. No. 113-2, 127 Stat. 4 (Jan. 29, 2013). CDBG funds are available to distressed areas resulting from a major disaster

submit an action plan that described its proposed use of funds, and it released its initial action plan on March 12, 2013.³¹ HUD approved New York's plan on April 25, 2013, and, since then, New York published six subsequent amendments.³² In total, \$3,810,960,000 is available to New York, excluding New York City, for disaster recovery and victims' unmet needs.³³ More money may be on the way. Yet, CDBG-DR funds come from the same payor as the NFIP—the federal government.

NY Rising is spending these funds for the provision of assistance to Sandy victims, among other storm victims, for: repairs; reimbursement; elevation; "optional resiliency" measures; and interim mortgage assistance.³⁴ To receive assistance, however, victims must establish their eligibility under the program. In addition to other eligibility criteria, such as a primary residency at the time of damage requirement, homeowners who reside in certain flood-prone areas and who receive financial assistance from NY Rising *must*, under federal law, obtain flood insurance under the NFIP.³⁵ Moreover, and also according to federal law, "anyone that previously received Federal assistance following a disaster and was required to get flood insurance, but did not, is *ineligible* for CDBG-DR assistance."³⁶ This requirement has serious implications.

declared pursuant to the Robert T. Stafford Disaster Relief and Emergency Assistance Act of 1974, 42 U.S.C. §§ 5121–5207 (2012). *See also* Requirements for Grantees Receiving CDBG, *supra* note 25.

31. *See generally* N.Y. STATE HOMES AND CMY. RENEWAL, STATE OF NEW YORK ACTION PLAN FOR COMMUNITY DEVELOPMENT BLOCK GRANT PROGRAM DISASTER RECOVERY (2013), available at <http://www.ny.gov/assets/documents/CDBGActionPlan.pdf>.

32. *Action Plan and Amendments*, N.Y. STORM RECOVERY RESOURCES CTR., <http://stormrecovery.ny.gov/action-plans-and-amendments> (last visited Nov. 23, 2014).

33. GOVERNOR'S OFFICE OF STORM RECOVERY, STATE OF NEW YORK ACTION PLAN AMENDMENT NUMBER 6 TO THE ACTION PLAN FOR COMMUNITY DEVELOPMENT BLOCK GRANT DISASTER RECOVERY 2 (2014), available at http://www.stormrecovery.ny.gov/sites/default/files/documents/second_allocation_apa_final_clean_20140220v3.pdf.

34. NY RISING HOUSING RECOVERY PROGRAM, HOMEOWNER GUIDEBOOK 2-4 (2014), available at http://stormrecovery.ny.gov/sites/default/files/uploads/homeowner_guidebook_040814.pdf.

35. *Id.* at 5-6; *see also* 42 U.S.C. § 5154a(a) (2006). The statute states:

[N]o Federal disaster relief assistance made available in a flood disaster area may be used to make a payment (including any loan assistance payment) to a person for repair, replacement, or restoration for damage to any personal, residential, or commercial property if that person at any time has received flood disaster assistance that was conditional on the person first having obtained flood insurance under applicable Federal law and subsequently having failed to obtain and maintain flood insurance as required under applicable Federal law on such property.

§ 5154a(a).

36. NY RISING HOUSING RECOVERY PROGRAM, *supra* note 34, at 6 (emphasis added); *see also* § 5154a(a).

Consider the following common scenario: a Long Island homeowner, with no mortgage, lives in a neighborhood that had never flooded before. The homeowner is no longer working, and lives on a modest, fixed income. Purchasing flood insurance coverage, according to the homeowner, was an expenditure deemed unnecessary. In the summer of 2011, however, Irene caused flood damage to the home.

Like many disaster victims, the homeowner seeks assistance from the Federal Emergency Management Agency ("FEMA"), and is granted \$1000 for home repair assistance. Under federal law, the homeowner is now required to purchase flood insurance as a result of receipt of this assistance. But, when the homeowner contacts her insurance broker, the homeowner is quoted a price for the premium of an NFIP policy that the homeowner could not afford. Accordingly, the homeowner chooses not to purchase an NFIP policy after Irene.

Fast-forward to October 2012, and the arrival of Sandy. This time, a tremendous amount of flood damage is caused to that same home. Again, the homeowner applies for assistance from FEMA. However, because the homeowner did not purchase an NFIP policy despite receiving a FEMA grant after Irene, the homeowner will receive *nothing* from FEMA, and, in addition, will not be eligible for assistance under CDBG-DR funded programs like NY Rising.³⁷

By contrast, for homeowners who had no flood insurance coverage in place at the time of Sandy, but were not required to because they never received any federal assistance prior to Sandy, FEMA benefits and CDGB-DR funded programs, like NY Rising, *are* available. Let us consider the example of the homeowner who had no flood insurance in place at the time of Sandy, *but suffers "earth movement" flood damage*. NY Rising assists this homeowner with Sandy-related repairs. The homeowner, under NY Rising's guidelines and federal law, is now required to purchase flood insurance to mitigate against future storms.³⁸ This homeowner did purchase an NFIP policy. However, as previously discussed, earth movement is excluded from coverage under the NFIP.³⁹ If damage resulting from earth movement occurs in a future storm, the homeowner, who will have paid timely and repeatedly for "flood" coverage, will likely receive *nothing* from damage claims submitted under the NFIP policy. The homeowner has paid, in this scenario, for the false belief of insurance, and federal policy essentially forces homeowners to purchase an NFIP policy and buy-in to that program.

37. Requirements for Grantees Receiving CDBG, *supra* note 25, at 14,344-45.

38. See *supra* text accompanying notes 34-35.

39. See *supra* text accompanying notes 21-22.

But for CDBG-DR money, and programs like NY Rising and BIB, homeowners impacted by Sandy would have been left to fend for themselves to fill significant unmet needs and funding gaps due to, in large part, NFIP limitations. Unless the federal government envisions funding CDBG-DR programs following every natural disaster and flooding event, there will continue to be unmet financial needs because of NFIP shortcomings.

Moreover, eventually, homeowners will be expected to pay more for that false sense of security. In this scenario, which could apply to many homeowners, flood insurance under the NFIP, absent more homeowner-friendly revisions to the Policy, is a pecuniary charge imposed upon a homeowner to yield public revenue, or, in other words, a tax.⁴⁰

V. CONCLUSION

For better or worse, flood insurance under the NFIP is often the frontline, financial first responder for disaster recovery in flood-prone areas. The current model requires that, at some point, some portion of the financial burden of protection shifts to the homeowner. There is nothing controversial about requiring homeowners to bear some of that cost. However, to charge homeowners more for the same, deficient thing is unjust. If financing the NFIP is moving more towards the direction of applying market principles, then a market should be created.

The only real, material choice homeowners have in deciding what flood coverage to have in place is the dollar amount of coverage—"should I have \$50,000 worth of coverage, or \$250,000?" Instead, why not offer homeowners the opportunity to choose from multiple types of policies at varying costs, or negotiate more property-appropriate policies, rather than imposing upon them the current one-size-fits-all Policy?

The practical reality of the current model short-changes homeowners from recovering money under policies that *they thought* would fully protect their homes in the event of flood damage. This could be for a multitude of reasons, not least of which is the current form of the Policy. When recovery under the NFIP, administered by WYO carriers, has been exhausted, or when homeowners, who faced repeated delay and inaction understandably give up, the funding gap or unmet

40. BLACK'S LAW DICTIONARY 1594 (9th ed. 2009). A "tax" is defined as: "A [monetary] charge . . . imposed by the government on persons, entities, transactions, or property to yield public revenue." *Id.*

need is filled by CDBG-DR, state- and city-administered programs.⁴¹ CDGB-DR funds are supplied by the same source as the NFIP—the U.S. Treasury. While it remains to be seen how effective programs like NY Rising will be, why not get it right the first time? Why not provide homeowners, who have paid costly flood insurance premiums, and will be expected to pay more, with a competent, comprehensive, and fair NFIP? Not only would this accelerate disaster recovery, it would be the right thing to do.

41. *See supra* Part III.
