

# MARYLAND

**2005 REPORT OF THE  
MARYLAND INSURANCE  
ADMINISTRATION  
ON THE EXPERIENCE  
OF MARYLAND CITIZENS  
WITH THE NATIONAL FLOOD  
INSURANCE PROGRAM  
IN THE AFTERMATH  
OF HURRICANE ISABEL**



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## ***EXECUTIVE SUMMARY***

Hurricane Isabel resulted in unprecedented damage to property along the waters of the Chesapeake Bay. Through its outreach efforts, the Maryland Insurance Administration (the "Administration") had the unique opportunity to hear first hand the frustration of those consumers whose attempts to rebuild were made even more difficult by the challenges of dealing with their insurance companies and the National Flood Insurance Program ("NFIP").

Maryland Insurance Commissioner, Alfred W. Redmer, Jr., distributed preliminary findings of the Administration to the Maryland Congressional Delegation on March 4, 2004 (the "Delegation Report"). The Delegation Report may be found on the Administration's website at [www.mdinsurance.state.md.us](http://www.mdinsurance.state.md.us). On June 30, 2004, President George W. Bush signed legislation that requires the Comptroller General of the United States to perform or conduct a comprehensive review of various aspects of the NFIP. Concurrently, the Administration continued its efforts and conducted an additional review of the complaints filed with the Administration and of the methodology used to process flood claims.

The Administration's investigation addressed the operations of several major Write Your Own ("WYO") carriers and their employees, as well as third party adjusters and a detailed evaluation of the complaint information received from Maryland consumers. WYO carriers offer flood insurance to eligible persons under an arrangement with the Federal Emergency Management Agency ("FEMA"). Additionally, the Administration interviewed representatives from various software companies who provide the adjusting software commonly used to adjust flood claims. Based on the review findings, the Administration reached the following conclusions:

- Because of differences between homeowners and flood policies, many consumers are surprised to learn that certain items and repairs are not covered under their flood policy;
- There is no clear process or procedure for amending the terms of a policy if it is determined that the property is over insured;
- Multiple layers of bureaucracy provide numerous opportunities for claims to be delayed;
- There is confusion among flood adjusters as to the appropriate use and role of the NFIP pricing guidelines;
- Many pricing anomalies are a result of adjusters' errors including, but not limited to, improper use of the adjusting software, hesitation to deviate from the NFIP published pricing guidelines and inadequate training or understanding of the flood program;

- Consumers often receive inaccurate or conflicting information from adjusters, producers, WYO carriers and FEMA representatives regarding the flood program;
- Claim estimates are not uniform and vary in their terms and format, resulting in inconsistency and consumer confusion.

## ***INTRODUCTION***

On September 18 and 19, 2003, Hurricane Isabel impacted numerous states along the East Coast, including Maryland. The devastating effect Isabel had on property along the Chesapeake Bay was unprecedented.<sup>1</sup> The Administration spent the weeks and months following the hurricane staffing the 15 Disaster Recovery Centers which were established expressly to assist storm victims.<sup>2</sup> In addition, the Administration assisted in the coordination of community meetings throughout the affected areas of the state. These meetings were held in conjunction with briefings with local government officials to facilitate communication between victims, local governments and the federal government. The Administration's role in the case of an emergency that involves insurance is to help citizens by informing them of their rights and coverage under their insurance policies and to assist them when they have problems with their claims. Also, the Administration created a special intake system to handle storm-related questions, concerns and complaints of Maryland consumers. A detailed outline of the Administration's actions to assist Maryland victims of Hurricane Isabel from the days just prior to the storm through September 2004 is found as Exhibit 1.

In addition to providing direct assistance to Maryland consumers, Insurance Commissioner Redmer also met with the Federal Insurance Administrator and the Maryland Congressional Delegation to discuss his findings and recommendations. A copy of the report provided to the Maryland Congressional Delegation is attached as Exhibit 2.

On March 23, 2004, Commissioner Redmer and representatives of the Federal Insurance and Mitigation Administration held a focus group meeting which allowed the officials to hear first hand the problems the citizens had encountered getting their flood insurance claims paid. The Administration also provided copies of intakes and complaints to the NFIP so that they could be reviewed to determine what changes in the procedures and policy were

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<sup>1</sup> For a detailed description of the impact Hurricane Isabel had on Maryland, see *Lessons Learned from Tropical Storm Isabel, Improving Disaster Management in Maryland* available on the Maryland Department of Planning's web site at [www.mdp.state.md.us](http://www.mdp.state.md.us).

<sup>2</sup> Historically, the Administration's efforts following a flood have been limited to manning disaster recovery centers. In the past, the Administration has received complaints regarding the Federal Flood Program, however, those complainants were advised that the Administration did not have jurisdiction over the Federal Flood Program and the complaints were forwarded to the NFIP for handling.

appropriate. Due to the ongoing complaints and concerns regarding the flood insurance settlements, the Commissioner requested the NFIP to reevaluate the claims of Isabel flood victims. After this meeting and as a result of the concerns expressed by federal and state government officials, including the Commissioner, the NFIP announced that it would reevaluate all flood claims from Hurricane Isabel to determine whether additional payments should be made.

In response to continued widespread complaints of low or insufficient claim settlements, the Administration conducted an additional review into the process by which claims submitted to the NFIP were being handled. Although the Administration does not have jurisdiction over the Federal Government's flood program, it decided nevertheless to conduct a review of the program to determine if there were areas where the program could be improved for the consumers who utilize it. During this review, the Administration interviewed various WYO carriers, contractors, flood program claims adjusters and software companies that provide flood claims adjusting software.<sup>3</sup>

As of April 5, 2005 the Administration had processed 1,418 intake files and 508 formal complaints relating to Isabel. Of that total, 636 intakes and 137 complaints were directly related to the NFIP. On a national level, the NFIP has paid out \$441,676,488 on 19,344 losses as a result of Hurricane Isabel.<sup>4</sup> That makes Isabel the third most costly flood event between 1978 and October 30, 2004 based on losses paid by the NFIP. Only Tropical Storm Allison in 2001 (\$1,094,461,572 in paid losses) and the Louisiana Flood of 1995 (\$584,140,014) were more costly.<sup>5</sup>

## ***BACKGROUND***

### ***History***

The NFIP was initially created by Congress in 1968 to provide insurance coverage for residential and commercial properties for flood damage because coverage was generally not offered by the private insurance industry as it was not profitable. Congress enacted the National Flood Insurance Act of 1968 in response to increasing costs of taxpayer funded disaster relief for flood victims and the increasing amount of damage caused by floods.

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<sup>3</sup> It should be noted that various adjusters refused to be interviewed by the Administration. Therefore, the findings contained in this report are drawn from those individuals and organizations that agreed to be interviewed.

<sup>4</sup> *Significant Flood Events, 1978 – October 31, 2004*, last updated Tuesday, 07-Dec-2004. FEMA Website.

<sup>5</sup> Id.

The 1968 Act made federally subsidized flood insurance available to owners of improved real estate or mobile homes located in a floodplain if their community participated in the NFIP. From 1968 until the adoption of the Flood Disaster Protection Act of 1973, the purchase of flood insurance was voluntary.

The 1968 Act was significantly amended by the 1973 Act by adding mandatory purchase requirements for properties in flood prone areas where the purchaser sought either a mortgage from a federally regulated lending institution or federal assistance. The 1973 Act mandated flood insurance coverage for many properties in flood prone areas that were not covered under the voluntary program. For the first time, regulated lending institutions could not make, increase, extend, or renew any loan secured by improved real estate located in a Special Flood Hazard Area ("SFHA") in a participating community unless the building and any personal property securing the loan had flood coverage for the term of the loan.

The 1973 revisions were necessary because, after major flooding disasters, it became evident that relatively few individuals in eligible communities who sustained flood damage had purchased flood insurance. Flooding in the Midwest in the summer of 1993 resulting in multi-billion dollar flood losses prompted further amendments because only an estimated 20% of households in those flood zones had coverage.

In 1994 the Congress enacted the Riegle Community Development and Regulatory Improvement Act which revised the NFIP by putting new obligations on federally regulated lenders, their servicers and secondary market purchasers. The 1994 provisions included mandatory escrow requirements for flood insurance and provisions for forced-placement of flood insurance if the policy lapsed or was cancelled.

### *Federal Preemption*

Federal law expressly preempts state law when a statute or regulation contains explicit language that federal law governs the matter. With regard to claim payments, the application of state law to federal flood insurance claims is expressly preempted by federal regulation. With regard to the handling of claims, express preemption also exists as to all policies issued after December 31, 2000. This is the date that a new FEMA regulation took effect that amended the Standard Flood Insurance Policy to add the provision: "all disputes arising from the handling of any claim under the policy are governed exclusively by the flood insurance regulation issued by FEMA, the National Flood Insurance Act of 1968, as amended (42 U.S.C. §4001, et seq.) and Federal common law" For policies issued before January 1, 2001, preemption of state law exists because, as the overwhelming majority of courts considering the issue have held, state

regulation of claims handling in this area would frustrate and obstruct the objectives of the federal program and, thus, conflict with federal law.

In the case of C.E.R. 1988, Inc. v. The Aetna Casualty and Surety Company (2004), the United States Court of Appeals for the Third Circuit reviewed the relevant case law and statutes on the issue of federal preemption of state law when a flood insurance policy holder files a tort claim for the mishandling of the flood loss claim. 386 F.3d 263 (3<sup>rd</sup> Cir. 2004). In its 2004 opinion, The Court held that state law is preempted based on conflict preemption stating: “we conclude that the application of state tort law would impede Congress’s objectives. Indisputably a central purpose of the Program is to reduce fiscal pressure on federal flood relief efforts . . . State tort suits against WYO companies, which are usually expensive, undermine this goal.” 386 F.3d at 270.

Insurance companies are authorized to write insurance in Maryland by issuance of a certificate of authority by the Insurance Commissioner. The Maryland laws found in the Insurance Article regulate these insurers and the insurance policies issued by them. The flood insurance policies issued by a Maryland authorized insurer that is also a WYO company are a clear exception to the authority of the Insurance Commissioner over insurers, the policies they issue and their handling of claims and other matters.

The Insurance Article imposes a variety of obligations on insurers that do business in the State. Those obligations include laws that direct the manner in which claims made under policies issued by those insurers must be processed and paid. See Ins. Art. §§27-303 and 27-304. An insurer that fails to comply with those legislative directives may be ordered to pay the claim and is subject to administrative action ranging from the revocation of its certificate of authority to the imposition of a monetary penalty, not to exceed \$125,000 per incident.

### Lenders

When the National Flood Insurance Act of 1968 was amended in 1973 by the Flood Disaster Protection Act of 1973, Congress added the mandatory purchase requirements for properties in flood prone areas. Under these provisions the purchaser who sought either a mortgage from a federally regulated lending institution or received federal assistance was subject to the regulations. The mandatory purchase laws require the federal agencies regulating federal lending institutions and Government Sponsored Enterprises (GSEs), Federal National Mortgage Association (Fannie Mae) and Federal Home Loan Mortgage Corporation (Freddie Mac), to adopt regulations requiring lenders to require borrowers to purchase flood insurance if the subject property is in a flood zone.

In 1994, Congress enacted the Riegle Community Development and Regulatory Improvement Act which revised the NFIP by putting new obligations on federally regulated lenders, their servicers and GSEs.. The federal agencies that regulate lenders were charged with implementing the stricter mandatory flood insurance purchase requirements. The 1994 Act newly imposed flood insurance escrow requirements and requirements for forced placement of flood insurance. Also, it is a prerequisite that a designated loan have flood insurance as a condition of closing. If a borrower will not voluntarily obtain coverage and a lender is unable to force place coverage, the lender must deny the loan or exercise the sanction provisions of the loan document if the loan has already been made. Additionally, flood insurance is required to be maintained during the term of the loan.

The 1994 Act requires Federal agency lender regulators to develop regulations to direct their federally regulated lenders not to make, increase, extend, or renew any loan on applicable property unless flood insurance is purchased. The proposed regulations were jointly issued by the federal agencies in October 18, 1995. It is significant to note that the 1994 Act's directives and prohibitions are applicable to federally regulated primary lenders and to secondary market entities involved in mortgage loan transactions. The flood insurance requirements do not apply to lenders or servicers that are not federally regulated and that do not sell loans to Fannie Mae and Freddie Mac or other GSEs.

FEMA's primary means of communicating the flood insurance requirements to lenders, the federal agencies regulating lenders and GSEs is through a publication entitled, "Mandatory Purchase of Flood Insurance Guidelines". Following the enactment of the 1994 Act, the Guidelines were revised and reformatted and republished in September 1999. Apart from the Guidelines, FEMA provides education on the requirements through workshops or articles in trade publications.

The Guidelines advise lenders that they should use the same general business practice used for calculating hazard insurance when calculating flood insurance coverage, and that the lender should take into account "the extent of recovery allowed under the NFIP policy forms."

Under the Federal laws, the key requirement for flood insurance covering improvements to property in flood areas is the lesser of "an amount at least equal to the outstanding principal balance of the loan" or \$250,000, the maximum amount currently available under federal law. This formula represents a floor and it is not reflected in the actual coverage provided by FEMA through the Standard Flood Insurance Policy Dwelling Form for residential property. The



Loss Settlement provisions of the Standard Policy favor insureds who have purchased flood insurance that is at least 80% of the full replacement cost immediately before the loss. The secondary mortgage market has incorporated the 80% of replacement cost into their requirements and use that amount of insurance as a minimum.

### ***RECENT LEGISLATION***

The NFIP required congressional reauthorization before June 30, 2004, when the program was scheduled to expire and flood insurance would no longer be available to new homeowners. On June 30, 2004, President George W. Bush signed into law the Flood Insurance Reform Act of 2004 (FIRA). The main purposes of the FIRA are: 1) to reauthorize the National Flood Insurance Program through September 30, 2008; 2) to establish a pilot program aimed at mitigating the damage and costs associated with repairing properties with severe repetitive flood losses; and 3) to improve consumer understanding and rights of NFIP policyholders.

Subsequent to the Administration's investigation, but prior to the issuance of this report, the United States Congress passed legislation that will require, among other things, the Comptroller General of the United States to conduct a study to review:

- the adequacy of payment to flood victims;
- the adequacy of the scope of coverage provided under flood policies;
- the practices of FEMA and insurance adjusters in adjusting losses incurred as a result of a flood; and
- how such practices affect the adequacy of payment to flood victims.

The Comptroller General is required to submit a report to Congress regarding the results of this study within one (1) year after the effective date of the legislation. The Comptroller General's report will no doubt be an in-depth review of the NFIP and the Administration looks forward to reviewing it. President George W. Bush signed the bill into law on June 30, 2004. Many of the areas recommended for review in the federal legislation were also addressed in the Commissioner's March 4, 2004 report to the Maryland Congressional Delegation (attached as Exhibit 2).

In addition, during the 2004 legislative session, the Maryland General Assembly passed legislation requiring that agents who sell flood insurance take continuing education courses on flood insurance (Exhibit 3). Although not insurance related, HB3 of the Acts of 2004, provided a means for Maryland residents who sustained damage due to the hurricane to obtain low interest loans to rebuild their homes.

In the interim, it is hoped the Administration's observations of how the NFIP worked in Maryland in the aftermath of Hurricane Isabel can serve as a starting point for a discussion about the adequacy of the claims procedures of the NFIP. These observations warrant recognition now while the memory of the disaster is still fresh and, unfortunately, while some people have yet to be fully compensated for their losses.

### ***WRITE YOUR OWN PROGRAM***

The NFIP initially made flood coverage available only through insurance agents who dealt directly with the Federal Insurance Administration ("FIA"). The coverage was serviced by private insurers for the first 10 years of the program. In 1978, the policy and claims operations were turned over to a private contractor supervised by the FIA. In 1979, the FIA was placed under the Federal FEMA, and within a few years the "direct" policy program was supplemented with the WYO program.

Under the WYO program, a pool of private insurance companies issue a policy that must mirror the terms and conditions of the Standard Flood Insurance Policy. In addition, the WYO companies adjust flood claims as well as settle, pay and defend all claims arising from the flood policies. The premium charged by the private insurer is the same as that charged by the Federal Government through the direct program. Nearly all of the flood policies issued today are written by WYO companies.

A private insurer becomes a WYO company by entering into a contract, the "Financial Assistance/Subsidy Arrangement" (the "Arrangement"), with the Federal Insurance Administration. Under the Arrangement, private insurers agree to issue flood policies in their own name and take certain responsibilities, such as marketing, claim processing, and general policy administration. The federal law authorizes WYO companies to issue the Standard Policy in the name of the company issuing the policy, and to substitute the company's name where the terms "FEMA" or "FIA" appear in the Standard Policy.

For the private insurers, the WYO program carries little or no risk. The companies collect the flood insurance premiums and retain about 30% as an administrative fee. From this premium the company must pay administrative expenses associated with issuing the policy (such as agent commissions) and state premium taxes. The actual amount of premium retained is determined by a formula contained in the Arrangement. The premium collected that is not retained by the WYO company is deposited in the National Flood Insurance Fund in the United States Treasury.

The WYO company is reimbursed by the federal government for loss adjustment expenses (the direct and indirect expenses associated with settling claims). These reimbursements are in addition to the premium retained. The company is allowed to keep an amount equal to 3.3% of losses paid, and is reimbursed for the services provided by claims adjusters according to a fee schedule.

Federal regulations require that all claims are processed in accordance with, on the one hand, all the WYO carriers' insurance procedures and, on the other hand, with the Financial Control Plan prepared by the NFIP.<sup>6</sup> The purpose of the Financial Control Plan is to "account for and ensure appropriate spending of any taxpayer funds." This accounting occurs by way of audits that occur biennially or "for cause." The audit reviews, among other factors, whether the carrier used unit prices that were within the established NFIP guidelines for the event.

### ***FLOOD INSURANCE CLAIMS***

If a policyholder has suffered damage due to flooding, the loss should be reported to the agent or insurer who provided the coverage, or to the NFIP if the policy was purchased directly through the NFIP. The adjuster assigned to the loss is required by the NFIP to "inspect the property within 48 hours of receiving the loss assignment for these losses of a critical nature and to inspect other losses as soon as possible within one week of receiving the loss assignment" (Claims manual, p II-4).

Once the risk has been inspected, the adjuster completes a Preliminary Damage Assessment form for all risks with substantial damage, which is then faxed to the NFIP's Bureau and Statistical Agent's Claims Department. Next, the adjuster prepares a preliminary scope of damage report, which along with the worksheets and the proof of loss, becomes the basis for the figures contained in his final report of loss. The insured must complete a proof of loss, containing the valuation of the claimed damages, which the adjuster may have furnished to assist in the settlement of the claim. The adjuster also must provide an itemized estimate of the scope of damage along with his or her worksheets. The adjuster is expected to be familiar with Standard Flood Insurance Policy ("SFIP") provisions, including coverage interpretations issued by FEMA, and to adjust the losses in accordance with those provisions. The insured is then required to sign the proof of loss, have it witnessed, and submit it within 60 days of the date of loss.

If the insured and adjuster agree with the figures contained on the proof of loss, the insured signs the proof of loss and returns it to the adjuster. The

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<sup>6</sup> See 44 CFR §62.24

adjuster will complete a final report of the loss and any other required forms (narrative report, elevation certificate, etc.) and forward all documentation to the WYO carrier or NFIP's Bureau & Statistical Agent (if directly written) for payment to the insured.

If the insured's property has been substantially damaged, the insured must obtain proof of this loss in writing from the local government officials. Once the certification is received by the insured and forwarded to the adjuster, a proof of loss for the increased cost of compliance ("ICC") coverage must be prepared and signed by the insured. The insured has 60 days from the date of loss to proffer this proof of loss, as well. Thus, unless FEMA waives the 60 day reporting requirement, all flood insurance claims should be adjusted and submitted for payment within 60 days of the date of the loss. Then, in accordance with the provisions of the policy, the loss will be payable within 60 days after the WYO carrier or NFIP, if written directly, receives the proof of loss, or within 90 days after the adjuster files an adjuster's report signed and sworn to by the insured (in lieu of a proof of loss) and the WYO carrier, or NFIP, has reached an agreement with the insured.

If the insured disagrees with the scope of loss or the amounts offered as compensation for certain items, the cause for disagreement should first be addressed with the flood adjuster. Any pertinent documentation the insured has acquired, such as estimates from contractors, also should be provided to the adjuster for consideration and review.

If the insured is still not satisfied with the adjuster's settlement offer after reconsideration, the insured may request that a General Adjuster from the NFIP re-inspect and re-evaluate the loss and the initial adjuster's determination.

If a General Adjuster is asked to re-inspect the loss, and supplemental payments are authorized, a new proof of loss must be signed and sworn to by the insured. If the insured is still not satisfied, an appraisal can be requested, but only if there is a dispute as to the amounts being offered and not the scope of damage. The specifics of the appraisal process are detailed in the flood policy and are as follows:

"If you and we fail to agree on the actual cash value or, if applicable, replacement cost of your damaged property to settle upon the amount of loss, then either may demand an appraisal of the loss. In this event, you and we will each choose a competent and impartial appraiser within 20 days after receiving a written request from the other. The two appraisers will choose an umpire. If they cannot agree upon an umpire within 15 days, you or we may request that the choice be made by a judge of a court of

record in the State where the covered property is located. The appraisers will separately state the actual cash value, the replacement cost, and the amount of loss to each item. If the appraisers submit a written report of agreement to us, the amount agreed upon will be the amount of loss. If they fail to agree, they will submit their differences to the umpire. A decision agreed to by any two will set the amount of actual cash value and loss, or if it applies, the replacement cost and loss.”

Based on the complaints and intakes received by the Administration, it appears that very few individuals requested an appraisal. The Administration believes that is due to the fact that most disputes revolved around scope of coverage and value of loss. As noted above, scope of loss is not subject to the appraisal process. In light of the fact that the policy holders are not satisfied with the amount offered, bearing the cost of an appraisal during this difficult time may prove too great a burden for the insured.

During its review, the Administration found inconsistencies between adjusters and WYO carriers in the speed and manner in which claims were processed. The recently enacted Federal Legislation requires the Director of FEMA to develop a flood insurance handbook which contains:

- a description of the procedures to be followed to file a claim under the flood program;
- a description of how to file supplementary claims, proof of loss and any other information relating to the filing of a claim under the flood program; and
- detailed information regarding the appeals process.

The Administration anticipates that the new handbook will promote greater consistency among WYO carriers and the claims handling which will, hopefully, reduce confusion and complaints for any future events.

### ***STANDARD FLOOD INSURANCE POLICY V. HOMEOWNERS INSURANCE POLICIES***

In most cases, WYO carriers also write homeowner’s coverage in the state of Maryland. In reviewing Isabel complaints filed with the Administration, the examiners found that some of the trends associated with flood complaints did not correspond to complaint trends for traditional homeowner’s coverage. Since many policy provisions are unique to the SFIP, victims making a claim against their flood policies for the first time may be surprised to find that they would not be made whole, even if building and personal property coverage had been

purchased and the amounts offered conformed with industry standards, due to the provisions in the policy.

There are many differences between a Standard Flood Insurance Policy and an Insurance Services Office HO-3 Homeowners Policy (“HOP”).<sup>7</sup> First, an SFIP covers one peril, flood, while an HOP covers all causes of direct physical loss unless otherwise excluded. When purchasing an SFIP, an insured must specifically request coverage for contents, whereas the HOP automatically includes contents coverage for specifically named perils. Under a SFIP, two separate deductibles would be applied for the flood damage to the building and for the flood damage to the contents, while only one deductible would be applied under the HOP if both the dwelling and the contents were damaged by a covered peril.

Under the SFIP, a basement is any area of a building, including any sunken room or sunken portion of a room, having its floor below ground level (subgrade) on all sides. It is important to understand this because the SFIP limits coverage for basements and the contents contained therein, unlike a HOP, which does not make any such distinctions.

The following language from the SFIP explains exactly what is covered in a basement under the building property coverage:

8. Items of property in a **building** enclosure below the lowest elevated floor of an **elevated post-FIRM building** located in Zones A1-A30, AE, AH, AR, AR/A, AR/AE, AR/AH, AR/A1-A3C, V1-V30, or VE, or in a **basement**, regardless of the zone. Coverage is limited to the following:
  - a. Any of the following items, if installed in their functioning locations and, if necessary for operation, connected to a power source:
    - (1) Central air conditioners;
    - (2) Cisterns and the water in them;
    - (3) Drywall for walls and ceilings in a **basement** and the cost of labor to nail it, unfinished and unfloated and not taped, to the framing;
    - (4) Electrical junction and circuit breaker boxes;
    - (5) Electrical outlets and switches;

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<sup>7</sup> A comparison between the two types of policies can be difficult as there are many different homeowner policy forms depending on carrier and type of coverage while there is only one SFIP Dwelling Form. The HO-3 is the most commonly used form and is therefore used for comparison purposes in this report.

- (6) Elevators, dumbwaiters, and related equipment, except for related equipment installed below the **base flood** elevation after September 30, 1987;
- (7) Fuel tanks and the fuel in them;
- (8) Furnaces and hot water heaters;
- (9) Heat pumps;
- (10) Nonflammable insulation in a **basement**;
- (11) Pumps and tanks used in solar energy systems;
- (12) Stairways and staircases attached to the **building**, not separated from it by elevated walkways;
- (13) Sump pumps;
- (14) Water softeners and the chemicals in them, water filters, and faucets installed as an integral part of the plumbing system;
- (15) Well water tanks and pumps;
- (16) Required utility connections for any item in this list; and
- (17) Footings, foundations, posts, pilings, piers or other foundation walls and anchorage systems required to support a **building**.

b. Clean-up.

Additionally, if an insured purchased contents coverage under the SFIP, the following policy language sets out what personal property is covered in a basement:

- 3. Coverage for items of property in a **building** enclosure below the lowest elevated floor of an **elevated post-FIRM building** located in Zones A1-A30, AE, AH, AR, AR/A, AR/AE, AR/AH, AR/A1-A3C, V1-V30, or VE, or in a **basement**, regardless of the zone is limited to the following items, if installed in their functioning locations and, if necessary for operation, connected to a power source:
  - a. Air conditioning units, portable or window type;
  - b. Clothes washers and dryers; and
  - c. Food freezers, other than walk-in, and food in any freezer.

Under a HOP, any damage caused by a covered peril to the building or contents would be covered, and would be reimbursed at replacement cost. All covered personal property damaged by flooding is reimbursed at actual cash value, which is computed as replacement cost less depreciation. So, there is minimal coverage for personal property items contained in the basement pursuant to a SFIP. A summary of some of the major coverage differences between an SFIP and HOP have been highlighted in the chart on page 14.

### Coverage Comparison Between a Homeowners Policy and a Standard Flood Insurance Dwelling Policy

ITEM	SFIP DWELLING FORM	HOMEOWNERS
1. Additional Living Expenses	NO	YES; limit of at least 20% of Coverage A limit
2. Appurtenant Structures	YES; 10% of limit of liability can be applied to detached garage at described location	YES; additional limit of at least 10% of Coverage A
3. Awnings	ACV, if attached to building	YES, RCV
4. Building Fixtures	Listed	YES, RCV
5. Carpeting	ACV; no overhead and profit	YES, RCV
6. Construction Before Walled & Roofed	YES; two times the deductible	YES, RCV
7. Debris Removal	YES	YES
8. Decks	NO; limit of 16 sq. feet	YES, RCV
9. Deductible	Applied separately to building and contents	Applied only once, if cause of loss damages both building and contents
10. Emergency Mitigation	Limited coverage, \$1,000	N/A
11. Exterior Paint	YES	YES
12. Fences	NO	YES, RCV
13. Hot Tubs & Spas	YES, only if they are bathroom fixtures	YES, RCV no matter where they are located
14. Ordinance or Law	YES, subject to Exclusion A.6.	YES, unlimited coverage if law and ordinance endorsement is purchased
15. Pollutants	YES	NO
16. Replacement Cost, Building	YES, if insured to 80% of RC and insured lived at risk 80% of previous 365 days	YES; if insured to value and replacement cost is purchased, Coverage A limit of liability is increased
17. Replacement Cost, Personal Property	NO	YES; for contents located anywhere in the world
18. Screened Porches	YES, unless below elevated floor (Post-FIRM)	YES, RCV
19. Storage Sheds	NO	YES, RCV up to 10% of Coverage A limit of liability
20. Stove & Refrigerator	Building ACV, if tenant's contents	YES, RCV
21. Swimming Pools/Hot Tubs	NO	YES, RCV
22. Temporary Repairs	NO	YES; actual amount spent
23. Trees	NO	Yes; up to coverage limit stated in policy
24. Venetian Blinds	Building ACV	YES, RCV



## ***Complaint Analysis***

The Administration conducted a detailed analysis of the complaints it had received and the information contained in those complaints. This information included the location of loss, the original proof of loss and in some instances the amended proof of loss or estimate after a re-review by NFIP.

The charts below reflect the following information compiled by the Administration:

- Federal Flood Intakes by county;
- Federal Flood Complaints and the amount of additional recoveries associated with those complaints by county;
- Federal Flood Complaints and the amount of additional recoveries associated with those complaints by carrier, including NFIP.

### **Federal Flood Intakes by County**

<b>County</b>	<b>No. of Intakes</b>
Anne Arundel	119
Baltimore City	6
Baltimore County	219
Calvert	18
Cecil	8
Charles	2
Dorchester	144
Harford	2
Kent	26
Montgomery/Prince George's	1
Queen Anne's	54
Somerset	5
St. Mary's	19
Talbot	12
Wicomico	1
<b>TOTAL</b>	<b>636</b>

**Federal Flood Complaints and the Amount  
of Additional Recoveries Associated With Those Complaints by County**

<b>County</b>	<b>No. of Complaints</b>	<b>Recovery Amount</b>
Anne Arundel	27	\$310,511.87
Baltimore City	1	0.00
Baltimore County	58	298,040.71
Calvert	1	0.00
Cecil	1	0.00
Charles	1	0.00
Dorchester	14	44,537.72
Harford	4	42,112.00
Howard	1	0.00
Kent	6	10,335.51
Montgomery	1	0.00
Queen Anne's	7	9,967.13
St. Mary's	7	0.00
Talbot	8	251,909.22
<b>TOTAL</b>	<b>137</b>	<b>\$967,414.16</b>

**Federal Flood Complaints and the Amount of Additional Recoveries  
Associated With Those Complaints by Carrier, Including NFIP**

<b>Insurance Company</b>	<b>No. of Complaints</b>	<b>Recovery Amount</b>
Allstate Ins. Co.	28	\$187,647.10
Brethren Mutual Ins. Co.	1	0.00
Farmers New Century Ins. Co.	1	0.00
Fidelity and Guaranty Ins. Co.	1	0.00
Fidelity National Ins. Co.	1	0.00
First Community Ins. Co.	1	0.00
Harleysville Mutual Ins. Co.	7	157,189.58
Hartford Fire Ins. Co.	7	27,608.59
Hartford Underwriters Ins. Co.	3	0.00
Liberty Mutual Ins. Co.	1	0.00
National Flood Insurance Program	16	52,694.98
National Grange Mutual Ins. Co.	1	0.00
Nationwide Mutual Fire Ins. Co.	15	67,000.00
Nationwide Mutual Ins. Co.	1	0.00
Omaha Property and Casualty Ins. Co.	5	180,793.88
Prudential Property and Casualty Ins. Co.	1	0.00
Selective Ins. Co. of America	20	188,657.77
South Carolina Ins. Co.	2	7,666.67
Standard Fire Ins. Co.	1	0.00
State Farm Fire and Casualty Co.	8	9,158.00
Travelers Property and Casualty Group	6	0.00
United Services Automobile Association	2	0.00
Unknown at time complaint was filed	8	88,997.59
<b>TOTAL</b>	<b>137</b>	<b>\$967,414.16</b>

The Administration conducted a further review of the complaints received, which included information regarding the NFIP re-review. These complaints included the original proof of loss settlement offer and the revised settlement offer/estimate after the re-review process. In conducting the evaluation, the Administration was seeking to identify those areas that may have been overlooked during the initial review or areas where unit prices were substantially increased for materials. Following are examples of the Administration's findings:

- The pricing for plywood was increased on re-evaluation to \$2.12/square foot from \$1.79/square foot;
- The initial estimate failed to include payment for scaffolding rental, mildicide and removal of fill dirt totaling \$9,289.40. Payment was allowed on re-evaluation;
- The removal and replacement of a condenser air-conditioning unit was increased from \$1,074.31 to \$2,653.80;
- Premium Grade tile flooring was adjusted from \$11.38/square foot to \$15.83/square foot;
- The initial estimate failed to include payment for removal and replacement of 47 square yards of indoor/outdoor carpeting totaling \$922.81. Payment was allowed on re-evaluation.

### ***AREAS OF CONCERN***

As a result of the complaint analysis, the Administration also conducted further inquiry into the allegations of slow processing, handling and payment of claims and low offers to settle covered losses. The additional investigation included interviews with adjusters, WYO carriers, contractors, scoring modelers and testing of the most common software applications utilized in adjusting flood losses. The interviews and subsequent investigation identified the following areas of concern:

#### ***Adjusters***

Adjusters are individuals who assist the WYO carriers and FEMA in reviewing the loss location to determine the scope of damage and the amount of payment the insured is entitled to receive. Adjusters are often hired by independent adjusting firms which are, in turn, hired by the WYO carriers. Certain WYO carriers contract directly with adjusters, while others utilize their employee adjusters rather than hiring outside staff. The NFIP sets forth minimum qualifications for adjusters; however, WYO carriers are free to hire any qualified adjuster they wish. The Administration's observations from interviewing various adjusters and adjusting firms revealed that adjusted losses resulting from Hurricane Isabel focused on three key issues.

First, as a result of Hurricane Isabel, more than 6,323 claims from Maryland were filed with the Federal flood program. As with any natural disaster, losses are not spread out over time. The magnitude of the damage and number of policyholders affected was simply greater than the number of experienced adjusters available to adjust losses. In an attempt to meet the demands of policyholders, adjusters were flown in from across the country to adjust losses. As a result, the knowledge, experience and expertise of each adjuster varied widely.

Second, the pay scale for adjusters has not increased for seven (7) years. Many of the adjusters interviewed indicated that the lack of a pay increase discourages new adjusters from applying. Additionally, independent third party adjusting firms collect between 30 – 40% of the fee, leaving the individual adjuster with approximately 60% of a fee that has not increased in seven (7) years.

Third, confusion occurred over what areas of the property were or were not covered by the NFIP. The NFIP, itself, has reversed its position as to what is properly covered by the Federal flood program. This position resulted in inconsistency and confusion about these claims. Additionally, despite FEMA's statements regarding coverage and expansion of coverage, NFIP's contractor, Consumer Services Corporation ("CSC"), has failed to consistently implement and adopt these changes and has continued to enforce more restrictive interpretations.

### Software

Like most tasks, the adjusting of claims has entered the computer era and adjusters are increasingly utilizing various software applications to prepare estimates and "proofs of loss" that are submitted to the WYO carriers. The Administration spoke with virtually all of the major software companies providing flood claims processing applications and learned how the software is used to input, adjust and output data. A number of observations were made from these conversations and the Administration's own experience with the software.

Software is simply a mechanism by which one can access and use pricing data. However, the accuracy of the estimates depends on the skill, knowledge and experience of the adjuster using the software. Adjusters are responsible for knowing the terms and limitations of coverage and entering the correct information in the software for pricing. Therefore, if an adjuster omits a portion of a loss, the software is unable to calculate for that loss.

In general, adjusters are responsible for maintaining the most up-to-date pricing data in the software used for adjusting losses. While this information can often be easily downloaded directly from the Internet, there is no requirement or method of verification to ensure that the most current data is being used when the claim is adjusted. The Administration, through its review, determined that some adjusters were using older pricing data at the time of the loss.

When the most recent databases were used, the Administration determined that prices among the various software programs were similar. The Administration also verified that each program compensated for additional costs associated with repair and reconstruction and allowed the adjuster the freedom to alter the unit price or time required for each job item on the loss.

One of the differences among the various software applications was that there is no uniformity as to the terms used to adequately describe a loss nor is there a uniform format for the estimate provided with the "proof of loss". These differences promote confusion among policyholders regarding the scope of an estimate and make comparison between two estimates difficult.

Eventually while each software program tested could identify item costs that were manually overridden by an adjuster, this information was generally not reflected on the final estimate provided to the consumer, the WYO carrier or the NFIP. The adjuster has the ability to determine what information will be provided on the final printout, resulting in estimates, that while similar, appear different.

### Claims Processing

Because of the amount of paperwork involved, adjusters believe that they have little flexibility to work with the policyholder when adjusting a flood claim. The nature of flood losses, the coordination between WYO carriers and the Federal flood program and certain claim submission requirements does, in fact, result in significantly more paperwork for a flood claim than for a traditional homeowner's insurance claim. Adjusters indicated that, because of the additional paperwork, flood claims take significantly longer to process for less compensation. Most adjusters estimated they could complete three (3) homeowner's claims in the time it takes to complete one (1) flood claim.

Another requirement that causes delays is the mandatory affidavit necessary to receive compensation for overhead and profit associated with repair work. A policyholder must provide an affidavit with the name of the contractor performing the work. Due to the magnitude and remote location of the damage left in the wake of Hurricane Isabel, the amount of repair work needed exceeded the number of available contractors. Therefore, while it was evident that the

scope of damage required a contractor in order to facilitate the repairs, many policyholders were unable to promptly secure a contractor for repair; therefore, they could not be compensated for overhead and profit until such time as they could produce an affidavit.

### Pricing Guide

On May 7, 2004, FEMA issued a memorandum about Flood Insurance Claims Guidance. In that memorandum, FEMA stated that it expects repair estimates to be based on current local prices and that price guidelines are to be used "with discretion and flexibility." Unfortunately, the Administration found that the guidelines in place after Hurricane Isabel were not necessarily used with "discretion and flexibility."

CSC, the entity contracted with FEMA to administer the Federal flood program, released a Pricing Guide to adjusters and WYO carriers to be used when adjusting flood claims. The Pricing Guide applies to all of Maryland and provides recommended pricing for some of the most common items, such as plywood. Adjusters acknowledged it was common practice for FEMA or its contractor to release a Pricing Guide unique to the specific disaster and location.

CSC states that the Pricing Guide is to be used only as a guide and that estimates should be based on the circumstances surrounding the individual loss. However, the National Flood Insurance Program – Financial Control Plan Requirement and Procedures (the "FCPRP") states that biennial claims audits shall "verify that the unit prices were within the established NFIP guidelines for the event."<sup>8</sup>

FEMA re-inspects approximately 10% of the claims. If FEMA determines there are errors in the estimates, or the prices offered were too high, the costs of any repayment are passed onto the adjuster who priced the claim. Additionally, if an adjuster is found to be consistently high in his/her quotes, he/she may lose future flood business. Certain adjusters acknowledged a hesitancy to stray from the Pricing Guide for fear they would be charged with any overages identified during an audit.

While carriers are required to process claims consistent with their own internal procedures used for homeowner's claims, they also are expected to comply with the FCPRP. Frequently the two procedures differ and the resulting conflict appears to create confusion for those adjusters employed by WYO carriers who also adjust losses other than flood claims.

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<sup>8</sup> National Flood Insurance Program. The Write Your Own Program Financial Control Plan Requirements and Procedures, Fifth Printing – December 1, 1999, p. 1-5.

Also during this period, due to high demand and limited supply, the price of plywood rose faster than expected. Adjusters and carriers acknowledged that the price for plywood contained in the Pricing Guideline was low. In order for the price of plywood to accurately reflect market conditions, it would have been necessary for the adjuster to consistently override the price of all repairs involving plywood.

### Over Insurance

As a result of the devastating effects of Isabel, many Maryland citizens found their homes to be a total loss. That is, the structure was damaged beyond repair and total reconstruction of the structure was required. Unfortunately, many insureds found that they purchased higher coverage limits than they were eligible for, even in the event of a total loss. Under the Federal Flood Insurance Policy, policyholders are limited to the replacement cost of their property; the land is not insurable. During its discussions with victims of Isabel, the Administration heard many complaints that the insured was required to purchase a specific amount of coverage by their lenders. During a review of complaints, the Administration concluded that determinations of replacement cost were dictated by the lender requirements, not FEMA procedures.

The Administration also identified a number of inconsistencies within various FEMA manuals that may have contributed to the confusion. For example, the basic agent training tutorial, in reference to completing a Flood Insurance Application, states:

“Enter the estimated replacement cost value for single family principal residential condominium buildings, and all V zone buildings. Include the cost of the building foundation when determining replacement cost.”

The *Policy Forms* section of the same manual states:

“When determining the full replacement cost of the building insured under the Dwelling Policy Form, exclude the costs for excavations; underground wiring and drains; brick, stone and concrete foundations; piers and other supports which are below the under surface of the lowest **basement** floor or where there is no basement, which are below the surface of the ground inside the foundation walls.”



Page APP4 of the Flood Insurance Manual contains the following statement:

“• Estimated replacement cost

Using normal company practice, estimate the replacement cost value and enter the value in the space provided. Include the cost of the building foundation when determining the replacement cost value.”

Page 23 of the Mandatory Purchase of Flood Insurance Guidelines, which applies to lenders, includes a section devoted to calculating appropriate coverage limits. To summarize, the section states that land is not insurable, and the lender should determine the amount of coverage required in relation to the portion of the loan associated with the improvements on the land and require this amount, or policy limits, whichever is less. This section includes the following quote that appears to address the issue of over insurance:

“When the lender does not take into account separate valuations of land, which is not insurable under the NFIP, and improvements, which are insurable, the insured may be paying for coverage that exceeds the amount the NFIP will pay in the event of a loss. Lenders should avoid creating such a situation”

However, this statement conflicts with instructions provided on page 25 of the same manual. Page 25 addresses the issue of insuring a low value building on high-valued property. It should be noted that this is what occurred in many areas of Baltimore County affected by Isabel. If the value of the land is more than enough to secure the value of the loan, the lender must still require flood insurance if the property is in a Special Flood Hazard Area (“SFHA”). The section provides:

“...the insurable value of the building and its improvements will govern the amount that can be required. The amount of required flood insurance coverage is the lesser of the principal balance of the loan(s) or the maximum coverage available under the NFIP. The NFIP policy does not provide coverage for losses in excess of the value of the insurable building.”

There is no clear definition of replacement cost or of how to appropriately calculate replacement cost. Additionally, the following information is found in the endorsement section of FEMA's Flood Insurance Manual.

## Endorsement Rules

### A. Coverage Endorsements

#### 2. Reduction of Insurance

A reduction in the amount of *building* insurance *cannot* be made unless part of the building has been removed, which reduces the building's value to less than the amount of the building insurance. (See Example 6 at the end of this section.)

A reduction in the amount of *contents* insurance *cannot* be made unless some of the contents have been sold or removed, which reduces the contents' value to less than the amount of the contents insurance.

#### 3. Removal of a Coverage

There is no return premium for the removal of building or contents coverage unless the property is no longer at the described location or the property of the policyholder. (See Example 5 at the end of this section.) (emphasis in the original).

Based on this information, there does not appear to be any method to reduce coverage during the term of the policy if it is determined that the property is over insured. It appears that an insured would have to cancel the policy and purchase a new one, or wait until renewal and have the policy re-written. So, while a policy can be reformed to allow for an increase in premium, there is no apparent method for amending or endorsing a policy to allow for a refund if the property is over insured.

The Administration also noted that none of the replacement cost estimators used to calculate coverage are designed for the NFIP. These estimators are designed to calculate coverage under the terms and conditions of a traditional homeowners policy and therefore take into consideration items which may not be covered under a flood policy.

## ***RECOMMENDATIONS***

### A. Consumer Education

The Administration recommends that steps be taken to educate consumers as to the benefits and limitations of the National Flood Insurance Program. The particular recommendations of the Administration are outlined below, in conjunction with the problem the action is intended to alleviate.

Problem: Because of the differences between homeowners and flood policies, many consumers are surprised to learn that certain items and repairs are not covered under the flood policy.

Recommendation:

- 1) Consumers must be educated to understand the benefits and limitations of the NFIP. Specifically, the Administration believes the consumers must be educated as to the differences between the NFIP and traditional homeowners insurance. The Administration has drafted an educational packet entitled "*Why You Should Consider Purchasing Flood Insurance*", as an educational tool and has distributed the packet at statewide events such as fairs, conventions and tradeshow where the Administration's Consumer Education and Advocacy Unit customarily distributes literature and answers inquiries.
- 2) During the 2004 legislative session, the Maryland General Assembly passed legislation proposed by the Insurance Administration requiring that, as a part of their continuing education requirements, producers selling flood insurance take a course on flood insurance during their every two year licensing cycle. This will allow producers to better explain the differences between homeowners insurance and flood insurance.

### B. National Flood Insurance Program

The Administration recommends that FEMA, through the NFIP, consider the following recommendations. The particular actions suggested by the Administration are listed below, in conjunction with the problems the action is intended to alleviate.

Problem: Because of the difference between homeowners and flood policies, many consumers find that they have purchased higher coverage limits for flood insurance coverage than they are eligible to receive payment for under the terms of their policy, even in the event of a total loss.

Recommendation:

- 1) Correct the Lenders Manual and The Flood Insurance Manual to remove any inconsistencies in how to calculate replacement cost.
- 2) Develop a replacement cost estimator specifically designed for the coverage provided in the Flood Insurance Program in conjunction with a company such as Marshall & Swift/Boeckh.
- 3) Develop a clear process or procedure for amending the terms of a policy if it is determined that the property is over insured.
- 4) Include a guideline for auditing coverage amounts to make certain that properties are adequately insured.

Problem: Shortage of experienced certified adjusters

Recommendation:

- 1) Re-evaluate the training, certification and pay scale and methodology for flood adjusters. Consideration should be given to the role of adjusting firms and the costs associated therewith.
- 2) Consider increasing the number of certified flood adjusters so there are a sufficient number of trained and qualified adjusters to handle catastrophic losses. Efforts to maintain long term, highly qualified adjusters should be instituted.
- 3) The Administration recently introduced legislation which was adopted by the General Assembly and signed by the Governor requiring producer education for those producers selling flood insurance. Likewise, NFIP should require minimal training to be a certified adjuster and require certification to be renewed annually or bi-annually with a condition that adjusters satisfy a minimum continuing education course.

Problem: Multiple layers of bureaucracy provide numerous opportunities for claims to be delayed

Recommendation:

- 1) Consult with adjusters and WYO carriers to identify paperwork that is unique to the flood program. Consideration should be given to eliminate any unnecessary or ineffective paperwork.
- 2) Review the use of the affidavit for overhead and profit to determine its value when adjusting a catastrophic loss.
- 3) Communication between NFIP and its contractor, CSC, needs to be improved to ensure that policy decisions regarding coverage are consistently implemented and adopted by CSC.

Problem: Claims estimates are not uniform and vary in their terms and formats

Recommendation

Establish a uniform estimate/"proof of loss" format. Each software company indicated that incorporating a standard format, as prescribed by FEMA, could be easily accomplished. The format should include:

- a) Uniform use of terms;
- b) Indication of which prices were manually adjusted or overridden by the adjuster;
- c) Override explanation: when a price is overridden, the software needs to provide a field for an explanation and it must be mandatory that the field be completed by the adjuster; and
- d) Notation as to which pricing database was used at the time the claim was adjusted.

Problem: Confusion over the use of Pricing Guidelines

Recommendation:

Eliminate the use of the Pricing Guidelines or alternatively the FCPRP must be clarified to indicate that the Pricing Guidelines are not used for auditing purposes. This change will allow adjusters more liberty to adjust the costs of materials to reflect increased prices that almost always occur after a flood event.

Problem: Oversight over the administration of the Federal Flood Program

Recommendation:

FEMA needs to review the findings of the GAO audit and conduct a thorough self-evaluation to determine why so many consumers were dissatisfied with the claims process. Additionally, FEMA should consider allowing states to have more regulatory oversight of the flood program.

### ***CONCLUSION***

Over the last eighteen months, the Maryland Insurance Administration has assisted hundreds of Marylanders who filed complaints stating that they received insufficient funds or inappropriate settlements in accordance with the terms of their flood insurance policies. In many cases, these allegations have been substantiated through the re-review process as additional sums have been paid to consumers. However, there are still individuals and families displaced in FEMA trailers, unable to re-build their homes and move forward with their lives.

Many factors caused these conditions to occur: inadequate consumer education, inconsistencies in pricing guidelines and claims estimates, a shortage of trained adjusters, and a confusing and complicated bureaucracy that is difficult for the average consumer to navigate. The result is that consumers have been offered insufficient settlement amounts from the NFIP. For those Maryland citizens who are still displaced, the NFIP should take steps to review the claims again in an effort to ensure consistency and fair value in accordance with our recommendations. For future natural disasters, Congress should take the appropriate legislative action necessary to reform the NFIP by considering and implementing the recommendations contained in the Administration's report, as well as those offered as a result of the pending GAO audit.

EXHIBIT 1

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GOVERNOR

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COMMISSIONER

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## **MARYLAND INSURANCE ADMINISTRATION PREPAREDNESS AND RESPONSE TO HURRICANE ISABEL**

- On September 15, 2003, in advance of the Hurricane, the MIA began contacting Property & Casualty insurers licensed in Maryland to ensure that each company had their storm centers and catastrophe teams ready to respond in Maryland.
- From September 16 through September 20, 2003, the MIA provided two staff members at the MEMA headquarters for a combined total of 98.5 hours. The MIA was present in order to facilitate responses to any insurance concerns.
- On September 16, 2003, the MIA created a Hurricane Isabel page on its web site, [www.mdinsurance.state.md.us](http://www.mdinsurance.state.md.us) to provide pre-storm information including tips on what people need to know before the storm and what to do if they incurred storm damage. The web site continued to be updated on a regular basis and a news release was distributed statewide telling consumers about the information on the web site.
- On September 19 and 21, 2003, Commissioner Redmer was at MEMA headquarters in Baltimore County for meetings with Governor Ehrlich and other state representatives regarding the ongoing state response to Hurricane Isabel.
- On September 22, 2003, Commissioner Redmer participated in two briefings to discuss plans to address damages resulting from the hurricane. The first briefing was held in Baltimore City with Mayor O'Malley and the second was held in Towson with County Executive Smith, congressional representatives, and various legislators.
- On September 22, 2003, MIA staff reported to the first three Disaster Recovery Centers (DRCs) which were opened in Annapolis, Baltimore City and Baltimore County. MIA employees continued to staff those centers, as well as the other DRCs which were opened throughout the state, seven (7) days a week until each DRC was closed by FEMA.



- On September 23, 2003, Commissioner Redmer gave an interview on WBAL-TV to inform Maryland citizens of their rights as policyholders, including the right to seek assistance from the Maryland Insurance Administration.
- On September 25, 2003, the Commissioner participated in two town hall meetings in the hardest hit communities of Baltimore County; one in Bowley's Quarters (Middle River) attended by more than 200 people and the other in Sparrows Point with more than 500 people in attendance.
- On September 28, 2003, Commissioner Redmer appeared on three (3) local TV stations to announce that he had arranged for two (2) community meetings to be held in Baltimore County to address residents' concerns about their damages and insurance claims. The purpose of the meetings were to provide an opportunity for citizens to meet with insurance company representatives. The first meeting occurred on September 29<sup>th</sup> at the Bowley's Quarters Fire Hall and the second meeting occurred on September 30<sup>th</sup> at Sparrows Point High School; both were attended by approximately 200 people who had an opportunity to meet with representatives of their insurance company.
- Commissioner Redmer and the MIA staff received training from the regional manager of the National Flood Insurance Program. This training was designed to inform the Commissioner and his staff on ways to better assist citizens as they file claims under their federal flood policies.
- In early October, Commissioner Redmer sent an email to all members of the Maryland General Assembly expressing his willingness to meet with them and their constituents at any time to help them through storm-related problems.
- On October 2, 2003, the MIA briefed the Senate Budget and Taxation Committee and the Baltimore County Executive at Sollers Point Technical High School regarding the MIA's efforts before, during, and after the storm.
- On October 3, 2003, the MIA staff attended a FEMA/NFIP (National Flood Insurance Plan) briefing on issues raised by the recent flooding.
- On October 6, 2003, the MIA briefed the Anne Arundel County delegation in Annapolis on events and issues relating to the hurricane.
- On October 7, 2003, Commissioner Redmer and members of the MIA staff participated in an evening town hall meeting at the Kent Island Library sponsored by Delegate Dick Sossi. The MIA arranged for representatives from FEMA, SBA, and NFIP to be at the meeting. The purpose of the town hall meeting was to provide citizens with information on the National Flood Insurance Plan and other related issues.

- On October 9, 2003, the MIA staff participated in a town hall meeting sponsored by Anne Arundel County Executive Janet Owens at the Annapolis Middle School. The MIA facilitated the scheduling of representatives from FEMA, SBA, and the NFIP for the purpose of providing citizens with information on the National Flood Insurance Plan and other hurricane related concerns.
- On October 10, 2003, Commissioner Redmer toured the four Eastern Shore Disaster Recovery Centers in Crisfield in Somerset County, Cambridge in Dorchester County, Easton in Talbot County, and Rock Hall in Kent County.
- On October 14, 2003, Commissioner Redmer and the MIA staff participated in a town hall meeting at Sollers Point Technical High School sponsored by Baltimore County Councilman John Olszweski. The MIA arranged for representatives of FEMA, SBA, and the NFIP to be present for the purpose of providing citizens with information on the National Flood Insurance Plan and other hurricane related concerns.
- On October 15, 2003, the MIA participated in an evening community meeting at Bayside Beach in Anne Arundel County sponsored by Senator Philip Jimeno. The MIA arranged representatives of FEMA, SBA, and the NFIP to attend for the purpose of providing citizens with information on the National Flood Insurance Plan and other hurricane related concerns.
- On October 16, 2003, Commissioner Redmer and the MIA participated in a town hall meeting at Prince George's Community College sponsored by the Prince George's County Executive and the County Emergency Management Office. The MIA arranged for representatives of FEMA, SBA, and the NFIP for the purpose of providing citizens with information on the National Flood Insurance Plan and other hurricane related concerns.
- On October 21, 2003, two press releases were issued by Commissioner Redmer concerning the hurricane. The first provided the upcoming filing deadlines for FEMA, SBA, and the NFIP and the second explained Maryland's homeowner's insurance weather-related claims law.
- On October 25, 2003, the MIA staff participated in a community meeting in Venice on the Bay in Anne Arundel County sponsored by Senator Philip Jimeno. The MIA arranged for representatives of FEMA, SBA, and the NFIP for the purpose of providing citizens with information on the National Flood Insurance Plan and other hurricane related concerns.
- On October 25, 2003, the MIA staff participated in a community meeting south of Cambridge in Dorchester County sponsored by Delegate Addie Eckardt for the purpose of providing citizens with information on the National Flood Insurance Plan and other hurricane related concerns.

- On October 28, 2003, Commissioner Redmer met with MIA staff for the purpose of discussing what actions had been taken by the MIA with respect to Hurricane Isabel and what future actions would be taken by the MIA.
- On November 10, 2003, the 7<sup>th</sup> District Delegation sponsored a community meeting at Bowley's Quarters Fire Hall in which the MIA participated.
- On November 13, 2003, the MIA participated in a meeting sponsored by the community association in Bowley's Quarters for the purpose of discussing hurricane related concerns.
- On November 14, 2003, the MIA brought in sixteen (16) employees from other state agencies to assist citizens who either did not have insurance or whose insurance coverage was insufficient to pay for damages from Hurricane Isabel. These employees continue to work with citizens to obtain assistance from other governmental agencies or local volunteer organizations to address the citizens' unmet needs.
- On November 18, 2003, Commissioner Redmer and his staff met for three (3) hours with representatives of the Victims of Isabel Citizens Group. The purpose of this meeting was to facilitate discussions with representatives of FEMA and NFIP, who were also in attendance at this meeting.
- On November 24 and 25, 182 Maryland insurance producers participated in training sessions initiated by the MIA and sponsored by the National Flood Insurance Program. The purpose of the training was to educate the agents and brokers who sell the NFIP insurance about the program.
- On December 6 and 7, 2003, the MIA placed approximately seven hundred (700) telephone calls to citizens to remind them of the upcoming deadline for putting FEMA on notice of an intention to make a claim.
- On January 6 and 7, 2004, the MIA participated in all-day community meetings in Bowley's Quarters and Dundalk in Baltimore County sponsored by United States Senator Barbara Mikulski.
- On January 26 and 27, 2004, the MIA participated in all-day community meetings on Hoopers Island in Dorchester County sponsored by United States Senator Barbara Mikulski.
- On January 27, 2004, Commissioner Al Redmer spoke at a community meeting in Crisfield.
- February 5, 2004, MIA staff participated in a community Help Fair in Shady Side in Anne Arundel County sponsored by the County Executive.

- On March 4, 2004, Commissioner Redmer meet with the Maryland Congressional Delegation and separately with Anthony Lowe, Federal Insurance Administrator and director of FEMA's Mitigation Division, to discuss the MIA report outlining observations and suggestions for the National Flood Insurance Program and other Federal programs.
- On March 12, 2004, Commissioner Redmer began providing Anthony Lowe with copies of complaints and intakes filed by Maryland citizens pertaining to problems they have encountered with the settlement of their claims under the National Flood Insurance Program.
- On March 23, 2004, Commissioner Redmer and Anthony Lowe co-sponsored a focus group meeting with 11 victims of Hurricane Isabel at the State House. The purpose of the meeting was to allow FEMA representatives the opportunity to hear first-hand the consumer experiences with the NFIP.
- On March 25 and 26, 2004, Commissioner Redmer and a member of his staff attended the Mid-Atlantic NFIP Summit. The purpose of the Summit was to identify issues consumers had regarding their flood insurance policies and to discuss what, if any, changes are needed in the flood insurance program.
- During the months of March and April, MIA representative, Tom Henry, staffed weekly community opportunities for assistance in Edgemere on Tuesdays and in Essex on Thursdays.
- MIA scheduled community opportunities for assistance in Hooper's Island, Rock Hall, and Leonardtown on March 29, March 30, and April 2, 2004 respectively.
- On April 6, 2004, the MIA sent letters to approximately 1,400 citizens who had come to the MIA for assistance reminding them to discuss the coverage of unoccupied properties with their agents and provided information on housing loans available through HB3.
- On April 7, 2004, Commissioner Redmer participated in a MEMA news conference announcing the reevaluation of flood claims.
- On April 8, 2004, Commissioner Redmer participated in a FEMA news conference announcing the reevaluation of flood claims.
- Starting on April 8, 2004, MIA staff began participating in all the FEMA Open Houses being scheduled around the state.
  - 4-8 Bowley's Quarters (Baltimore County)
  - 4-14 Hughesville (Charles County)
  - 4-20 Hooper Island (Dorchester County)
  - 4-21 Baltimore City
  - 4-27 Rock Hall (Kent County)

- 4-28 Chester (Queen Anne's County)
  - 4-29 Edgewater (Anne Arundel County)
  - 4-30 Prince Frederick (Calvert County)
  - 5-3 Hollywood (St. Mary's County)
  - 5-4 Easton (Talbot County)
  - 5-5 Turner's Station (Baltimore County)
  - 5-6 Lakes & Straits (Dorchester County)
- On April 19, MIA staff received additional training on the National Flood Insurance Program.
  - On April 22, Associate Commissioner Joy Hatchette participated in a panel discussion on the NFIP at the 19<sup>th</sup> Annual Severe Storm Awareness Conference at the State Emergency Operations Center at Camp Fretterd.
  - On April 26, MIA staff participated in a meeting in Bowleys Quarters in Baltimore County sponsored by the Department of Housing and Community Development (DHCD) where DHCD staff explained the various loan programs available through HB 3.
  - On May 17, Associate Commissioner Hatchette participated in a panel discussion on the effects of Hurricane Isabel on Baltimore County sponsored by Leadership Baltimore County.
  - On June 14, 2004, Commissioner Redmer issued a message urging the importance of understanding flood insurance.
  - On June 17, 2004, MIA participated in MEMA conference at Camp Fretterd. The purpose of the conference was to discuss ideas and measures needed to improve response to, and management of, natural disasters such as Hurricane Isabel.
  - On August 5, 2004, Commissioner Redmer issued a message urging consumers to contact their agents or company and ask whether they should consider purchasing flood insurance.
  - On August 23, 2004, Commissioner Redmer and members of his staff held a meeting with many of the individuals that attended the March 23, 2004 focus group meeting. The purpose of this meeting was to allow the Commissioner to gather additional information on the review process and the status of the flood claims.
  - In September 2004, an article was published in the Daily Record explaining the benefits of purchasing flood insurance.
  - As of April 5, 2005
    - 1418 intakes done by MIA staff
    - 508 formal complaints filed against insurance companies

496 closed complaints

\*\*\*\*\*

MIA staff members were present to assist citizens at all 15 of the Disaster Recovery Centers and all of the FEMA Open Houses scheduled throughout the State, during every hour that each location was open. In total, more than 50 MIA employees participated in this response.

EXHIBIT 2



A REPORT TO  
THE MARYLAND CONGRESSIONAL DELEGATION  
ON HURRICANE ISABEL

MARYLAND INSURANCE ADMINISTRATION

MARCH 4, 2004

Alfred W. Redmer, Jr.  
Insurance Commissioner  
State of Maryland



## **Introduction**

The devastation Maryland experienced on September 18 and 19, 2003 as a result of Hurricane Isabel included unprecedented damage to property along the waters of the Chesapeake Bay. We have seen first-hand the loss of homes, cars, personal possessions and commercial properties. And, we have heard and shared the frustration of those whose attempts to rebuild their lives have been made even more challenging because of difficulties in dealing with their insurance companies -- and with the National Flood Insurance Program (NFIP).

The Maryland Insurance Administration (MIA)'s role in the case of an emergency that involves insurance is to help citizens by informing them of their rights and coverages under their insurance policies and to assist them when they have problems with their claims.

In the weeks and months following the storm, the MIA's outreach efforts focused on staffing each of the 15 Disaster Recovery Centers (DRC) that opened around the State and coordinating and co-sponsoring nine public meetings within affected communities. In order to speed up the existing formal Complaints process, which can take months to achieve a resolution, an Intake system was created. As a result of that effort, MIA staff opened Intake files on 1,321 storm victims they met face-to-face at the DRCs, at community meetings or when they called into the MIA. Policyholder's insurance company were immediately called by a member of the MIA staff in an effort to resolve the insured's concerns. In some cases, claimants' questions and concerns were satisfied with a couple of telephone calls. In other cases, resolution took longer and was more involved. Out of the total 1,321 Intakes, only 280 became formal Complaints and of those, 195 were closed by February 28.

Closing such a high number of Intakes before they became formal Complaints shows how successful the Intake process was. Putting these numbers into perspective, in 2003 there were 20,000 complaints for other Property and Casualty issues. Each Complaint could take several weeks to several months to investigate. Being able to intercede before the Isabel problems became formal Complaints and being able to deal with those problems so quickly, meant that literally hundreds of people were assisted in a very short time.

While many of the issues raised by citizens in the Intake process centered on homeowners insurance questions, the vast majority of problems concerned the NFIP policies and coverage.

To put Hurricane Isabel into perspective with other Federal flood claims from Maryland in the past 25 years, flood claims usually totaled fewer than 500. There were more than 1,000 claims in only two of those years (1979 with 1,067 claims and in 1996 there were 1,370 claims). Total claims pay-outs topped \$1 million in only in eight of those 25 years (1979-\$8.9 million, 1984- \$2.89 million, 1985- \$5.75 million, 1989-\$1.45 million, 1992-\$4.57 million, 1996-\$12 million, 1998-\$2.6 million, 1999-\$4.6 million). In

2003, a total of 6,323 claims have so far topped \$102,258,000 in payments to policyholders. Hurricane Isabel claims account for just about one-half of all claims to the Federal flood program since 1975, (6,323 for Isabel, 13,009 total claims since 1975).

### **The NFIP and the Jurisdictional Issue**

Congress established the National Flood Insurance Program (NFIP) under the National Flood Insurance Act of 1968 in order to make flood insurance available, on reasonable terms and conditions, to those in need of such protection in any part of the United States. As a Federal program, it is under the jurisdiction of Congress and regulations promulgated by the Federal Emergency Management Agency (FEMA).

Both in response to complaints filed in 1999 after Hurricane Floyd and to complaints filed in 2003 after Hurricane Isabel, the MIA has consistently taken the position that it does not have jurisdiction over claims submitted by Maryland policyholders under policies issued under the NFIP's Write Your Own (WYO) program.

First, Federal statutory law and regulation, as well as Federal case law, expressly provides that Federal law governs Federal flood insurance policies. Thus, all actions on such policies must be brought in Federal courts, which apply Federal law to the construction of policy terms and conditions. Second, it is well recognized that Federal law preempts the application of any state law or action against a WYO carrier in connection with the handling or payment of a Federal flood claim. FEMA actually revised its regulations effective December 31, 2000 in order to clarify that any matters "relating to and arising out of claims handling" are "governed exclusively by Federal law."

An exception to the general preemption rule does exist with regard to misrepresentation. The MIA may take regulatory action against insurance producers and insurance carriers with regard to misrepresentations made at the time that the policy was sold. Such cases, however, are very difficult to prove, particularly when the policy was sold many years before and documents may no longer be available or memory may be unclear.

Recognizing that the MIA's knowledge of the Federal program was limited, Commissioner Redmer scheduled a training session for key members of his staff 10 days after the Hurricane. The NFIP Regional III Manager led the training session on a Sunday afternoon to review the program, explaining what it covers and what it does not. The Commissioner was clear from the outset that the MIA would be the entry point for any insurance questions or concerns, whether or not the MIA had authority to regulate the handling and payment of the claims.

In addition, MIA employees from various internal Units voluntarily "transferred" to the Consumer Complaints Unit to help staff the Agency's response growing out of the storm. Some employees worked at the 15 DRCs (sites were open seven days a week for an extended period of time) and some filled positions internally for those who were out in

the field. In all, more than 70 people out of a total Agency population of 300 directly participated in the effort to assist Maryland citizens. Everyone who worked at a DRC was trained in the Federal program so they would be able to help citizens sort out their insurance problems.

Although hampered in its ability to step in to help solve NFIP claims issues directly because of Federal preemption, the MIA still went out of its way to develop a relationship with NFIP staff to help facilitate closure of claims for Maryland citizens. This new relationship has meant repeat appraisals for some policyholders and increased insurance pay-outs for others. The MIA is appreciative of the response of the NFIP in these cases.

### **What Needs to Happen Next**

Maryland's recent experience has shown that greater attention by both the State and Federal government needs to be shown to the flood insurance program -- how it is marketed and sold, what training the sellers should have before being able to sell the product, what coverage should be provided by the policy, how the claims process is handled, and what recourse policyholders have if they are dissatisfied with the outcome.

Moreover, the issue of NFIP policy compliance in relation to mortgage loans must be addressed. In as much as Congress has declared that everyone in a floodplain has to have flood insurance, it is not acceptable for there to be even one Isabel-damaged property that should have had flood insurance and did not. Nor should there be a homeowner without an adequate amount of coverage because the mortgage company didn't know what was required. Unfortunately, there were many of both. Greater lender education and involvement is critical to the success of the program and to the insurance security concerns of Marylanders.

In order to also cover property owners who, for one reason or another, have no mortgage, there needs to be a requirement that property owners in a floodplain are notified of the flood insurance requirement. Notification could be handled at the local level through tax assessment notices, but the Federal program should required that this happen.

In addition, when FEMA changes a flood zone, all property owners in affected zones need to be notified by certified letter from FEMA. Currently, the burden falls on the property owner to know if the property is in a flood zone. If at the time of sale of the property the site is not in a flood zone, but subsequently FEMA places it in a flood zone, the owner has no way of knowing. FEMA could notify local jurisdictions who would then be required to send the status change with property tax bills. Also, this information must be readily available at the time of a title search.

The MIA recommends that Federal officials work more closely with the Banking and Mortgage industry concerning the amount of flood insurance required in relation to the amount of the mortgage. Specifically, while mortgage lenders require flood insurance

to cover the value of the mortgage, which includes the value of the structure AND the land, the NFIP policy only covers damage to the structure. So, although a policyholder may be required to pay for an insurance policy based on the full value of a mortgage, that policyholder can never recover the full value of the policy because some of it covers the value of land which is not covered under the policy. In the case of Hurricane Isabel, we have discovered that some people were "over insured" and paying for an amount of coverage they could never recover under any circumstances.

The Maryland Insurance Administration has, and will continue, to work with storm victims to help resolve their individual problems with their insurance companies, FEMA, and the NFIP. While the MIA can act as an advocate on behalf of individuals in their specific cases, this experience has revealed that there are broader, systemic problems that must be addressed in order to protect our citizens in the event of future disasters.

Given our current experience with the NFIP, a list of recommendations has been developed.

The Maryland Insurance Administration suggests FEMA, through the NFIP should:

At the time of the sale of the policy,

- Require Write Your Own (WYO) companies to audit policies at the time they are purchased to make certain appropriate rating and classification criteria (such as flood zone designation) have been applied and appropriate premium has been charged. Failure to perform the audit would preclude the company from charging additional premium at the time a claim is made.
- Assure that there is full disclosure of the difference between contents and structural coverage by requiring the signature of the insured on the application or other documents that explain and waive contents coverage.
- Assure that consumers understand how the Increased Cost of Compliance (ICC) coverage works. At the time of sale, there needs to be a written document given to the purchaser that explains what ICC includes (whether it includes stairs, garage doors, flood vents, steel beams, etc.), that the ICC payments will be paid out in increments not all at once if there is a claim, that the ICC coverage is not a flat \$30,000 guaranteed payment for compliance costs but could be deemed to be less, etc.
- Provide to policyholders at time of sale, a Frequently Asked Questions ("FAQ") booklet or another easy to understand document that explains what is and what is not covered by the flood policy and how claims will be handled and paid under the policy. There should be a place on the document the purchaser signs where there is also a sign-off that the FAQ and ICC materials were given.

- Explain that a 30-day underwriting waiting period exists before the coverage becomes effective, unless the property is newly purchased and the policy must be procured in accordance with federal lending requirements.
- Assure that policyholders understand how the depreciation system works, i.e. that full replacement cost will not be paid until repair or rebuilding work is completed. This could cause a cash flow problem for the policyholder if damage is incurred.

In addressing the coverage currently provided by the policy,

- Conduct an exhaustive review of the terms and conditions of the policy in light of the types of properties located in the flood zones, (i.e. those with oil tanks located on the outside of the dwelling), the value of the properties and the coverage provided (i.e. no coverage for contents in basement or lowest level). The review should include an analysis of the items that are currently covered and excluded.
- Reassess the requirement that in order to get a Small Business Administration (SBA) loan, an NFIP policyholder who did not previously have contents coverage may be required to purchase a contents policy even if the structure is not currently inhabitable and there is no contents to insure at that point.
- Conduct a review of the policy provision that allows the insurance company to delay the settlement of a claim relating to the loss of contents pending the resolution of a claim relating to damage to the insured structure.
- Add in the cost of the sales tax required to pay for items when determining the total payment. Currently, the policy only pays for the actual cash value of replacement materials. When the policyholder or contractor purchase materials to rebuild, they have to pay the sales tax over and above what payment the policyholder has been given. This is a critical difference for people who are already strapped for cash.
- Consider amending the portion of the policy which states that repair or rebuilding of damaged or lost property will be made with material of "like kind and quality or its functional equivalent" by deleting the "functional equivalent" statement. It is unreasonable to expect that when people make an investment to upgrade their property and are paying added insurance to cover the value of that upgrade (and more of a mortgage), that they will not be compensated accordingly if there is a loss. An example is a kitchen with granite countertops which is valued by the appraiser for the value of Formica countertops. Both are functional equivalents, but while they may be "like kind," they are certainly not "like quality."

In review of the claims process,

- Establish a time deadline for inspection of damage and for the settlement of claims. The MIA received numerous inquiries and complaints because of the time it took adjusters to conduct initial inspections of properties, the time it took for adjusters to return with a proof of loss statement, the time it took for an offer of settlement to be made, and the time it has taken for a final check to be issued.
- Require the Single Adjuster Program to prevent consumers' confusion in dealing with multiple adjusters and to assure consistency in the claims handling process.
- Require that, when a claim is made, companies immediately provide the claimant with a document that explains in clear and simple language the claims adjustment process, including how the claimant can challenge the decision of the original adjuster.
- Create a formal appeals process for policyholders. Tell policyholders *in all printed materials* that they are entitled to ask for a General Adjuster to review the insurance company's adjuster's decision. Currently there is NO formal appeals process for policyholders who do not agree with the decision of the insurance company adjuster. There is no way for citizens to voice their dissatisfaction with the process, no way to see if their claim was received, no way to find out at where in the adjudication process their claim is, or no way to determine when they can expect to get an answer on the claim. In fact, the NFIP policy itself has neither a telephone number to call nor address to write directly to NFIP for inquiries.
- Require that claim denial letters give clear and specific explanations of the basis for the denial and include instructions for contesting the denial.
- Consider changing the depreciation portion of the policy so the policyholder is not caught short because payment for replacement value is a depreciated amount. In most cases, policyholders cannot pay contractors the difference (replacement cost minus depreciation cost) as they wait for their work to be completed and NFIP to pay the depreciation amount that has been held back.
- Consider changing the Proof of Loss timeframes. There also needs to be greater detail given concerning the parameters of the limits and the procedure for getting extensions of those limits.
  - Currently, a victim has 60 days from the time an offer of settlement is made to sign a Proof of Loss statement. Depending on the time of the year, the location of the property, the volume of damaged properties in an area, etc., a policyholder may not be able to get a contractor to come out and give an estimate of the cost of repair or replacement of a structure within 60 days.

Given the rural setting of some of the Hurricane Isabel damaged properties, the 60-day limitation was impossible.

- Currently, a victim has 180 days to get reimbursed by NFIP on "recoverable depreciation" (for work that has been completed). Again, depending on time of year, location, etc., work may not be completed in 180 days. People need to be told up-front that they can get an extension and how to do so.
- Require that people be told that even after they sign the proof of loss statement, they can reopen their claim if material and building costs go up. Policyholders can ask for a variance (with receipts for proof), even after construction has been completed, but many do not know this.
- Require that either the proof of loss statement or additional printed materials tell people to make copies of all paperwork before sending it back to NFIP or the insurance company. While it may seem like common sense to make copies of paperwork, people suffering the effects of a disaster may not be thinking clearly enough to do a seemingly simple thing such as this.
- Require the company to secure, at its own expense, an inspection of the property by a structural engineer when ICC coverage is at issue.

In review of the education requirements for sellers and buyers,

- Require that minimum educational standards be established for producers and adjusters working for all WYO companies participating in the program.
- Require that consumer education be provided by the producer at the inception of the policy, and Question and Answer documents, newsletters, etc. should be sent at renewal to the consumer. Flood damage mitigation and prevention tips should also be provided.

The MIA acknowledges that subsequent to the Hurricane, at the request of Commissioner Redmer, NFIP staff held five free training sessions for insurance producers at four locations around Maryland. At those training sessions, 182 producers completed the course. Additional sessions will be planned by NFIP and supported by the MIA.

In the body of the policy or on a printed attachment to the policy,

- Require specific instructions that explain what a policyholder's appeals rights are, including what legal action can and cannot be taken against the WYO, FEMA, or NFIP. While FEMA may believe the National Flood Insurance Act made clear that Congress intended lawsuits only on a disallowance of a claim and that by creating the WYO program they did not intend to expand the areas in which policyholders could bring suit, insureds do not understand the narrow interpretation of sovereign immunity in these cases.

- Require contact information, including a telephone number and email address that policyholders can use if they have questions concerning coverage or the appeals process. The lack of any contact information forces the policyholders to turn to their local regulators who don't have jurisdiction or the WYO companies who may or may not know how to answer their questions.

### **Other FEMA/NFIP/SBA Observations**

Because MIA personnel were at every location of the DRCs for every hour they were open, certain observations were made about the FEMA and the Small Business Administration (SBA) response. While we are grateful for the time the FEMA, NFIP, and SBA employees spent in our State trying to help citizens in this most critical time, inconsistencies in their messages only confuse people and may, in the long run, not get the right help to those who need it most.

The following are some of these observations, both positive and negative.

- In one DRC, the FEMA manager turned people away who had not yet called the toll-free telephone number to get a FEMA registration number. He would not let anyone use the telephone there. This was particularly difficult for those who had no home to call from and no cell phone to use. In another DRC, the FEMA manager let people use the telephone to call the toll-free telephone number and get registered.
- In one DRC, the FEMA manager held daily meetings at 8:30 a.m. (before the Center opened) for all of the participating staff, so everyone could share information with each other. In that way, each agency or program represented learned what the others were doing and how they would be able to help victims. The MIA staff person at that DRC thought it was very helpful.
- Some FEMA mitigation personnel volunteered information to victims about mold remediation, bringing it up even if the homeowner did not, while others did not seem to go out of their way to stress what help and information was available.
- At one DRC, the SBA representative was not aware of a program available to help people recover lost wages. A paper on the wall at the FEMA manager's desk explained what was available, the deadline, and where to call. The SBA representative said people had asked, but she hadn't known there was a program to tell them about. This was four weeks after the storm, after many victims had already been through the Center, and after many people had asked her for help which she was not able to give.
- There was no full-time NFIP representation at the DRCs. So, NFIP information and guidance was often provided by other FEMA representatives who may not



have had any flood insurance training. Given the nature of this event, specific, consistent NFIP information was critical to the victims.

- Several of the NFIP representatives at the DRCs were knowledgeable, but somewhat defensive, in their conversations with victims. They could quote regulations supporting an NFIP decision without explaining why those regulations were in place. In this sort of event, people need to understand why certain decisions are made, not be lectured to about regulations.
- There was a misunderstanding about qualifying for, applying for, and getting ICC funds through NFIP. Victims were told they had to get “substantial damage” certifications from their County governments. Unfortunately, few were told or knew where in County government to go to get what they needed. In this sort of event, FEMA should coordinate information with the local jurisdictions, so the FEMA personnel know where to direct victims.
- Victims have recognized that people who had flood insurance are getting less monetary assistance from FEMA than those people without flood insurance. People without flood insurance are getting up to \$5,000 for their lost possessions, while those with flood insurance and no contents coverage are getting nothing.
- Victims have recognized that no one is receiving the full \$25,000 amount FEMA representatives told them was available at public meetings and at the DRCs. Most victims in Baltimore County say they are getting no more than \$13,000 in assistance.
- SBA subtracts whatever amount a victim has been paid from FEMA. Those early payments went to cover daily living expenses, etc., but are being subtracted from the eventual rebuilding and rehabilitation loans. People need the full amount of the loans to cover their costs.
- The locations and times the DRCs were open were not sufficiently advertised after their initial opening announcements. Weeks after the storm, people were saying they didn’t know where to go or that there was even a place to go to get help.
- Sometimes, there was not enough coordination and communication between the Disaster Field Office (DFO) and the DRCs. In one instance, two mini-DRCs opened in lower Dorchester County on a Saturday and the FEMA manager at the main Dorchester DRC didn’t know until late that afternoon that they had opened. No other information, including location, was available.

## **Comments from the Insurance Industry**

In addition, the MIA has received the comments listed below which are recommendations from the insurance industry. These comments should be explored with representatives from industry and the NFIP to determine whether these changes would benefit the policyholders.

- NFIP education for claim adjusters and agents needs to be tailored to the different skill levels, abilities and experience of adjusters and agents. Current educational programming is general and does not serve the needs of all agents and adjusters. At a minimum, there should be two levels of claims adjuster training classes: a basic class covering policy fundamentals and an advanced class incorporating complex claim handling, litigation issues, and file examination & exception trends. The materials need to be updated and maintained as changes are made to the Flood Program. Simple job aids should also be created.
- NFIP should expand the Preliminary Report completed by the claims adjuster to capture more of the critical rating factors relevant to the damaged property to ensure consistency in property description (such as dimensions, elevation, number of vents, etc.).
- NFIP should increase its allowance for expenses (such as cost for photographs) to validate property descriptions at the time of initial policy underwriting/issuance.
- To assist insurers in the deployment of claim adjusters for large catastrophic events, NFIP should assemble and distribute actual industry and NFIP data regarding the location and severity of loss at the onset of a large event, rather than relying on computer models.
- Increase initial claims capacity by encouraging and coordinating the development of inside (telephone) claims handling (education of techniques, development of best practices, and establishing clear method of inspection limits).
- The approval process for payment of SALAE (supplemental allocated loss adjustment expense) should be more mechanized and timely.
- NFIP should work with the insurance industry to develop a process for electronic filing and storage of claim files and supporting documentation.
- NFIP response time to WYO company and flood vendor inquiries, whether via e-mail, mail, or phone, should be quicker.
- All flood program requirements, clarifications and expansions must be in writing.
- Flood program changes are often not provided with sufficient advance notice for insurers to comply; new rating information should be sent via a rate file rather than PDF.

- Communications from NFIP should be electronic, rather than regular mail.
- When flood zones change, insurers should be provided with a file identifying all policies for which the zones have changed. This will allow WYO companies to mechanically update policies at the following renewal.
- All flood program Rules/Requirements should be reviewed in their entirety and simplified where the complexity is not warranted.
- It is recommended that NFIP assess whether there is a continuing need for Submit for Rating.
- Agents should be required to be certified to write flood policies.

### **Conclusion**

The MIA has a rather unique perspective on the workings of the DRCs, because it staffed all of the DRCs at all times. It was MIA staff who gathered information at various locations about available programs and services, and then reported back to the MIA Associate Commissioner for Complaints in Baltimore. She then distributed the information, much of it not insurance related, back out to all of the MIA staff in the field. What became very clear early on, was that if the MIA didn't coordinate and distribute these messages to each of its staff members, important information would not have gotten to the people who needed help.

Because the FEMA employees work at one disaster after another around the country, it might be helpful if they received an orientation as a group when they are assigned to a new disaster location to help assure that their messages are uniform and appropriate for that disaster and jurisdiction. One would think the communication by FEMA/NFIP/SBA personnel would be consistent, but it was obvious that the level of training provided to such personnel (and thus the scope and accuracy of the information they could provide) varied greatly.

This report makes several suggestions that are intended to improve the Federal Emergency Management Agency's National Flood Insurance Program and its relationship with policyholders, producers, and the insurance companies that sell the Federal flood insurance product. The Maryland Insurance Administration stands ready to work with FEMA, the NFIP, and the Maryland Congressional Delegation to accomplish these goals. These policyholders and producers are our constituents. If this experience has taught us anything, it is that we must raise the awareness and understanding of flood zone property owners and educate the insurance industry on the policy and claims process.

***Respectfully submitted,  
Alfred W. Redmer, Jr., Maryland Insurance Commissioner  
March 4, 2004***

EXHIBIT 3

**SENATE BILL 584**

Unofficial Copy  
Session  
C4

2004 Regular

4lr2593  
CF HB 177

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By: **Senators Stone, Dyson, Grosfeld, Harris, Hughes, and Jacobs**  
Introduced and read first time: February 6, 2004  
Assigned to: Finance

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Committee Report: Favorable  
Senate action: Adopted  
Read second time: March 12, 2004

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CHAPTER \_\_\_\_\_

1 AN ACT concerning

2 **Insurance Producers - Continuing Education Requirements**

3 FOR the purpose of requiring certain insurance producers to receive continuing  
4 education on flood insurance under certain circumstances; requiring certain  
5 insurance producers to complete the continuing education requirements relating  
6 to flood insurance on or before a certain date; and generally relating to  
7 continuing education requirements for insurance producers.

8 BY adding to  
9 Article - Insurance  
10 Section 10-116(a)(4)(iii)  
11 Annotated Code of Maryland  
12 (2003 Replacement Volume)

13 SECTION 1. BE IT ENACTED BY THE GENERAL ASSEMBLY OF  
14 MARYLAND, That the Laws of Maryland read as follows:

15 **Article - Insurance**

16 10-116.

17 (a) (4) (III) EACH INSURANCE PRODUCER WHO POSSESSES A LICENSE  
18 TO  
19 SELL PROPERTY AND CASUALTY INSURANCE AND WHO SELLS FLOOD INSURANCE  
20 SHALL RECEIVE CONTINUING EDUCATION THAT DIRECTLY RELATES TO FLOOD  
INSURANCE.

**SENATE BILL 584**

1 SECTION 2. AND BE IT FURTHER ENACTED, That each insurance  
2 producer subject to this Act shall have completed the continuing education  
3 requirements related to flood insurance on or before September 30, 2006.

4 SECTION 3. AND BE IT FURTHER ENACTED, That this Act shall take  
5 effect October 1, 2004.