



COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON, D.C. 20548

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B-167790

JUNE 18, 1979

RELEASED

The Honorable James R. Jones
House of Representatives

Dear Mr. Jones:

In August 1978 you requested that we examine allegations that Federal agencies providing disaster assistance had failed to collect moneys from victims' insurance policies. These allegations were made by Mr. John Johnson and Mr. Jack Mendenhall.

In our September 20, 1978, letter to you, we agreed to review the procedures Federal agencies use to insure the proper collection of funds due the Federal Government under Federal flood insurance policies or private insurance policies of victims assisted by these agencies.

RESULTS OF OUR REVIEW

We found that Federal and State agencies administering Federal disaster assistance programs are not required by existing procedures to review applicants' insurance coverage to insure that all available coverage is requested from their insurance companies. Current procedures require such agencies to insure only that Federal assistance provided does not duplicate insurance benefits received. Under present procedures, Federal agencies are relying on the insurance company to provide adequate proceeds from insurance policies. Insurance company adjusters have little incentive to provide full proceeds, especially when Federal assistance is provided for the same losses.

We believe that the Administrator, Federal Disaster Assistance Administration (FDAA), should take certain steps to insure that applicants for Federal assistance request and receive all available benefits under their insurance policies.

We could not estimate the potential cost savings from implementing such steps. As noted in our report, we attempted to compare private insurance coverage with a victim's total



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losses as documented in the files of the Small Business Administration (SBA). However, the cause of damage was not identified for specific items--private insurance covered only wind damage--and we could not determine whether the insureds were entitled to additional proceeds under their policies.

The following presents a detailed discussion of the results of our review.

INTRODUCTION

Under the Disaster Relief Act of 1974 (Public Law 93-288), the President can declare an area a major disaster. Upon designation, the Administrator, FDAA, appoints a Federal Coordinating Officer who coordinates all Federal disaster assistance programs in the disaster area. Several Federal programs exist that provide assistance to insured disaster victims for losses that could also be covered by insurance. For instance, the FDAA Administrator can provide temporary housing for disaster victims. This can be in the form of rented or purchased property, including mobile homes or readily fabricated dwellings. In lieu of such housing, owner-occupied private homes may be repaired or restored to a habitable condition if restoration can be done quickly with minimal repairs. This program is referred to as the minimal repair program. Prior to January 1979, the temporary housing function, including the minimal repair program, had been delegated to the Assistant Secretary for Housing, Federal Housing Commissioner in the Department of Housing and Urban Development. On January 28, 1979, FDAA withdrew the delegation and FDAA is now responsible for this function but is relying to a greater extent on those States that are willing and capable to administer this function.

Also, section 408 of the act authorizes FDAA to make grants to the States to allow the States to make grants--up to \$5,000--to meet disaster-related expenses of individuals or families under the individual and family grant program. Individuals or families are eligible for assistance not otherwise available to them through other disaster assistance programs or from other means, such as insurance.

In addition, SBA is authorized under its own legislation to provide disaster loans for the repair and replacement of homes and personal property. Victims are eligible for SBA loans for uninsured losses only.

In August 1978 Congressman James R. Jones and former Senator Dewey F. Bartlett asked us to examine allegations that Federal agencies providing assistance to disaster victims had failed to collect moneys under victims' insurance policies. These allegations were made by individuals who had sent a proposal to FDAA to assist in collecting these moneys. FDAA is responsible for coordinating all Federal disaster assistance programs and insuring that such assistance does not duplicate proceeds from insurance.

According to the allegations, one intent of the Disaster Relief Act of 1974 is to provide Federal disaster assistance to victims when their losses exceed their entitlements from private insurance. Federal agencies are relying on insurance adjusters' findings to determine the carriers' payments under the policies. Adjusters are employed to protect the economic interests of insurance companies. If Federal agencies employed qualified adjusters to act as advocates for disaster victims applying for Federal assistance, the Government would accrue substantial cost savings. By assuring that victims receive the full amounts available under their insurance policies, the Government would reduce the need for Federal disaster assistance.

SCOPE OF REVIEW

At the time we received the congressional requests, we were beginning a review of Federal assistance provided to disaster victims in eight Massachusetts coastal counties declared eligible for assistance by the President in February 1978. As a part of that review, we examined Federal agencies' procedures to insure that proper payments were received by insured disaster victims under their private homeowners policies or their flood insurance policies under the national flood insurance program administered by the Federal Insurance Administration.

The overall objective of our review of Federal disaster assistance provided in Massachusetts was to evaluate the effectiveness of the various Federal programs available to assist disaster victims. We selected 32 individuals from those who had applied for an SBA home repair loan and 2 or more other types of Federal assistance. During our review, we interviewed each individual and contacted his or her insurance agent concerning insurance coverage and any proceeds received as a result of the February flooding. We received

copies of the homeowners' policies and proof of loss statements, including lists of damaged items and amounts supporting the proceeds paid. We also received from the Federal Insurance Administration similar information for those individuals with national flood insurance policies.

NO EVALUATION OF INSURANCE
COVERAGE UNDER FEDERAL DISASTER
ASSISTANCE PROGRAMS

Section 315(b) of the Disaster Relief Act of 1974 (42 U.S.C. 5155) requires the President to assure that Federal assistance is not provided for losses or partial losses, suffered as the result of a major disaster, that are compensated by insurance or any other source. Through delegations of authority, the FDAA Administrator is authorized to administer this portion of the act.

In implementing section 315(b), the Administrator has issued regulations in temporary housing functions (including the minimal repair program) and the individual and family grant program. These regulations require that program officials avoid duplication of assistance with insurance proceeds. For example, FDAA regulations require that an insured individual or family receiving temporary housing must agree to repay the program that portion of insurance proceeds received for such housing up to an amount equivalent to the fair market value of the assistance provided.

In the case of the minimal repair program, FDAA regulations require recipients to repay that portion of the cost of any repairs or replacements by the program which are compensated by insurance.

SBA's standard operating procedures for processing disaster loan applications require loan officers to deduct insurance proceeds from the total loss to determine what SBA assistance the victim is entitled to receive. A victim's total loss is determined by an SBA loss verifier who makes an onsite inspection of the damaged property.

The primary emphasis of all Federal programs providing disaster assistance, including the State-administered individual and family grant program, is to avoid providing victims assistance that duplicate what they received from insurance proceeds. However, FDAA regulations do not require a Federal or State agency to compare the coverage available under insurance policies with the assistance provided by the program

to insure that all available coverage has been requested from the insurance company.

We found that Federal and State agencies that provided Federal assistance in Massachusetts did not review information on insurance coverage. Information requested from insurance agents or companies was used to identify duplicate benefits.

Review of proceeds paid
by insurance companies

In our review we attempted to evaluate the adequacy of the insurance proceeds paid to victims in our sample by determining why SBA assistance was necessary where proceeds were less than total coverage under an insurance policy(ies).

Damages in the Massachusetts disaster occurred primarily from coastal flooding which is not covered under a standard homeowners insurance policy. However, wind, which is covered under a homeowners policy, also caused damage to homes in the Massachusetts disaster.

Eleven of the 32 individuals selected had flood insurance policies under the national flood insurance program. Six of the 11 received almost all of the face value of their policies. In the other five cases, the insureds received less than face value amounts of their policies. In four of the five cases, the individuals received SBA loans; the other individual refused an SBA loan after he had applied for it.

In the four SBA loan cases, we reviewed those items SBA covered to determine if the items should have been covered by flood insurance. It appeared that the Federal Insurance Administration paid all of the claims properly and that the items not covered by it and picked up by SBA were related to depreciation or the appropriate deductibles or were items specifically not covered under the policy. Items not covered were generally those located outside the insured structure (i.e., sea wall, landscaping, patio, etc.).

During the disaster homeowners insurance policies were in effect for 30 of the 32 disaster victims in our sample. At the time of the review, 18 had received some reimbursement under their policies, 2 had claims still pending, and 10 had not received reimbursement and did not have claims pending.

We attempted to evaluate the propriety of insurance proceeds paid or the nonpayment of proceeds by insurance companies under the homeowners policies. We reviewed SBA's documentation of the victims' total loss amounts developed by SBA loss verifiers. However, the documentation did not identify what caused damage to specific items because loss verifiers did not attempt to identify causes. It was not possible for us to identify which items were damaged by flood and which were damaged by wind. Therefore, we could not determine the reasonableness of insurance proceeds paid under the homeowners policies.

In the 10 cases where no proceeds were paid by the insurance companies, we could not determine whether some coverage should have been paid, again due to a lack of documentation as to cause of damage. In our discussion with the insureds and their agents, some information suggests that some insurance agents may not be reimbursing the insureds for the losses that are covered by their policies.

In our discussion with the 10 insured victims who received no proceeds under their homeowners policies, 5 told us they had contacted their agents but were told that their policies did not cover flood damages. Neither an agent nor an adjuster was sent to inspect the property to determine if any wind damage had occurred. Two of the five specifically requested that an adjuster inspect the property, but the agent refused. In these two cases, the agents told us that the properties were in areas that received flood damage and, therefore, no adjusters were sent. These two insureds and one other believed that their property had received some wind damage. Only one believed the damages (i.e., roof blown off) were significant. However, none of the five filed a formal claim with the insurance company. Also, of the 10 victims, another 3 indicated they did not have wind damage and did not contact their agent or file claims.

In our contacts with insurance agents in the five cases where the insureds were told they had no coverage for flood damages, one agent told us that the insured did not file a claim and, therefore, no adjuster was sent out. Another agent said that the insured would have filed a claim if he had wind damage, yet the insured told us that the agent had told him he had not received wind damage.

We noted on page 5 of this letter that two individuals had claims still pending with their insurance companies. In one of these cases, the insured was initially offered about

\$5,000 to cover wind damage to his home. The insured refused to accept the offer. In our latest contact, the insured had received \$12,000 from his insurance company in a final settlement.

In the other pending case, the insurance company had initially determined that the insured incurred no wind damage and, therefore, refused any coverage under his homeowners policy. The insured hired a public adjuster who is now negotiating with the company. The company has offered \$7,500 on the claim.

The above suggests that insurance agents and companies may not be providing proceeds in accordance with the coverage purchased by the insured. This point was recently addressed in a study 1/ performed by consultants for FDAA. As noted in the study:

"* * * adjusters have a strong economic incentive to avoid proper insurance compensation to insured parties struck by a disaster whenever government funds have already been or will be expended for the same damage covered by an insurance policy. The adjuster is motivated to lower claims to gain favor with the insurance company. Low adjustments will result in an unauthorized subsidy from the taxpayers whenever federal funds replace valid claims on policies and legal claims are either not made or are not paid in full, regardless of the reason."

New combined application process
for disaster assistance

FDAA is now evaluating a new combined application form process for temporary housing, including the minimal repair program, disaster home loans, and individual and family grants. Presently, each program has its own separate application form and performs its own verification of application data (including insurance) and residential damages. Under the new process,

1/Howard A. Cohen and Steven R. Gretenstein, "Review of Federal Government Disaster Relief Programs and Analysis of the Unsolicited Proposal on Duplication of Benefits," March 21, 1979.

the Federal Coordinating Officer will perform these functions and provide this information to each agency for its determination as to the applicant's eligibility. FDAA has developed application and verification procedures and forms for the new process and is currently field-testing the new process in a recent disaster in the State of Arkansas.

CONCLUSION

In considering the new process, we believe that now is an appropriate time to establish procedures to evaluate the reasonableness of insurance proceeds paid by private insurance companies and the national flood insurance program. Such procedures, if adequately implemented, would insure that insurance companies are providing reasonable proceeds under existing insurance policies and thereby are minimizing the need for Federal assistance.

The Director of FDAA's Office of Individual Assistance ✓ stated that the act did not give the Federal Government the right to "audit" insurance settlements nor is the Federal Government responsible for insuring that insureds received all proceeds due them under their insurance policies.

We agree that the Federal Government is not responsible for auditing insurance settlements to protect the rights of the insured. However, the Federal Government has a direct financial interest in whether or not insureds receive adequate proceeds under their insurance policies when they apply and are eligible for Federal disaster assistance.

Under present procedures, Federal agencies are relying on insurance company adjusters to provide adequate proceeds to insured victims who request Federal assistance. Adjusters have little incentive to provide full proceeds to the insured, especially when the Federal Government is providing assistance for the same losses.

The present procedures also rely on insureds to make formal claims and collect all amounts due them under their insurance policies. However, if Federal assistance is provided or available, we question if insureds have any incentive to collect from the insurance company and reimburse the Federal agency, especially when Federal assistance is provided at no cost to insureds; for example, the minimal repair program and temporary housing. We believe that if insured victims have coverage for losses or costs for which Federal

assistance is requested, they should be required to make formal claims under appropriate policies.

RECOMMENDATIONS TO THE SECRETARY
OF HOUSING AND URBAN DEVELOPMENT

We recommend that the Secretary direct the FDAA Administrator to

- establish procedures to require the evaluation of insurance coverage under policies held by victims requesting disaster assistance,
- require loss verifiers to identify the causes of losses when victims have insurance coverage, and
- require victims to make formal claims under insurance policies that cover losses or costs for which Federal assistance is requested.

AGENCY COMMENTS

In January 1979 we informed the Director and staff members of FDAA's Office of Individual Assistance of our conclusions and recommendations. The Director agreed with the recommendations and stated that he would take corrective actions. He informed us at that time that FDAA had under development procedures for a Combined Application/Verification Process (CAVP) that would include the review of insurance coverage of disaster victims. On May 24, 1979, the FDAA Administrator informed us that the CAVP was being field-tested in the Arkansas disaster area. The procedures also incorporate our other two recommendations. In another 12 areas recently declared disasters, the FDAA Administrator has instructed the Federal Coordinating Officer to aggressively pursue the entire insurance question to insure that assisted victims receive the full benefits from their insurance policies.

In addition, the Administrator indicated that, in all Federal/State disaster assistance agreements, a stipulation has been included that the State Insurance Commissioner will insure that insurance companies make full payments of insurance benefits to disaster victims.

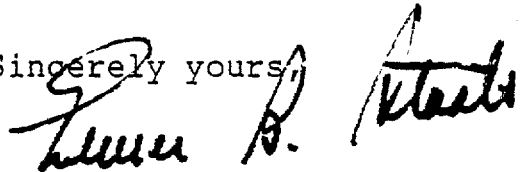
FDAA has developed an instructional brochure for insured disaster victims to inform them of

- how to deal with their insurance companies and adjusters,
- the types of coverage that may be available under their insurance policies, and
- their responsibilities to pursue and obtain the full benefits from their insurance policies.

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As requested by your office, we will send copies of this report 1 week after issuance to the House and Senate Committees on Appropriations; the House Committee on Government Operations; the Senate Committee on Governmental Affairs; the House Committee on Public Works and Transportation; and the Senate Committee on the Environment and Public Works. In addition, we will send copies to the Secretary of Housing and Urban Development; the Acting Director, Federal Emergency Management Agency; the Administrator, Federal Disaster Assistance Administration; and the Director, Office of Management and Budget.

Sincerely yours,

A handwritten signature in black ink, appearing to read "Glenn B. Stacks". The signature is written in a cursive style with a large initial "G" and "S".

Comptroller General
of the United States