

[Why Sandy Homeowners Were Left In The Lurch](#)

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Superstorm Sandy's storm surge was so strong when it hit Long Island in October 2012 that it lifted up Dan Stapleton's Long Beach home and then kicked in the corner of the foundation. It left a 30-foot hole around his house. Stapleton, unlike many Sandy victims, actually had flood insurance, and therefore hoped he could quickly fix his house and be reimbursed for it. But the engineer from the insurance company who came out to inspect the damage didn't quite see things the same way. He reported that the hole was only half as large, and the insurance company ended up offering Stapleton only \$98,000, less than half of what it cost to rebuild. So Stapleton sued. Federal judges wanted both sides to attempt mediation first to see if an agreeable settlement could be reached. But the company wouldn't budge. That was when his frustration with the flood insurance system grew even greater. "You think mediation, you have a puncher's chance," Stapleton laughed coldly. "But that wasn't the case." Stapleton was not the only one. At least 1,800 homeowners have sued their flood insurance companies and have similar stories. They say they were underpaid, and their attempts to strike a deal through mediation went nowhere. Insurance companies have claimed in the past that they do not have a reason to underpay flood claims. But an investigation by public radio stations WSHU in Fairfield, Connecticut and WNYC in New York City, found that over the past decade, the Federal Emergency Management Agency set up a system that gave insurance companies an incentive to underpay claims and even bring cases to trial rather than settle out of court. "Splitting the Baby" All of this became clear at a training seminar for federal mediators in July 2014. The training session was organized by federal judges in New Jersey. About 200 retired judges and lawyers came to be briefed on the nuances of the National Flood Insurance Program. "The feeling in the room was that we have to do something and we have to do it quickly," said Christopher Gerold, a lawyer representing about 160 Sandy victims, who was there. The aura of immediacy vanished as soon as a lawyer for the insurance companies took the stage. His name was William Treas, a prominent flood insurance lawyer from Louisiana. Neither he nor his law partners returned numerous messages. Treas, according to Gerold, said that insurance companies were willing to

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pay homeowners but did not want to risk being audited by FEMA. “He was very matter of fact about that,” Gerold said. Private insurance companies process claims and payments for the flood program, but the Federal Emergency Management Agency oversees — and funds — the program. The audits are FEMA’s way to double-check the work of the private insurance companies. If an audit reveals the insurance company underpaid a homeowner, the company simply uses FEMA’s checkbook to cut another check. But if the company overpaid the claim, that money came out of its own pocket. The mediators in the auditorium that day grew concerned when FEMA staffers stood up and confirmed that the agency would undertake audits even on settlements reached through mediations. “Essentially there was a lot of hushed whispers.” Gerold said, “Oh my God, how are we going to settle all these cases?” The answer was they weren’t, because FEMA’s rules discourage private insurance companies from settling. Gerold’s account is backed up by a memo that Treas, the insurance company lawyer, distributed to participants, which WSHU and WNYC obtained from another homeowners’ lawyer, Charles Mathis IV. In the memo, Treas said, “‘Splitting the baby’ just to make cases go away is not a part of the federal program. Candidly, it’s illegal.” (See William Treas memo on Flood Insurance.) History of FEMA’s Rules According to interviews with current and former insurance adjusters, FEMA began cracking down on overpayments by insurance companies to homeowners almost 10 years ago, after Hurricane Katrina. Then, around 2008, insurance companies really began to fear the audit. David Charles, a public adjuster who once worked for several insurance companies, said insurers “didn’t let us pay for things that we had always paid for and that we considered essential to the rebuilding process. And it was all out of fear of a FEMA audit that would make it look like they paid too much.” Charles remembers having a disagreement with his supervisor who was pushing to lower insurance payouts. “He said FEMA is auditing more aggressively, we’re not going to take any chances that we have to pay fines.” Charles said, “This is our new standard and you are going to do it this way. He was stern with me.” Data from FEMA shows that the audits and over-payment penalties had a big impact. In 2008, insurance companies overpaid policyholders some \$4 million. But that number dropped each year until finally reaching zero in 2013. Taxpayer-funded legal team With a strategy of underpaying, insurance companies could eliminate the risk of an audit. The only problem with reducing payments was that policyholders might sue. But insurance companies were covered there also, because FEMA reimburses insurance companies for all litigation costs, according to the program’s rules. “If you have free attorneys and free experts and your only downside is overpaying, then in theory every case should go to trial,” Gerold says. Once a judge makes a decision on the case, by FEMA’s own rules, the agency can’t audit the claim. On top of that, insurance companies even get a percentage of anything the judge adds to the payout. “It is a very good deal for insurance companies,” Gerold said. The vice president of the Property Casualty Insurers Association of America, Don Griffin,

agreed that in theory the best way to make money would be to underpay and then to litigate. But in practice, he said, insurance companies preferred to close claims as quickly as possible because open cases require employee time and hurt their image. "Because what happens when they do that is they lose a customer," Griffin said. "So the short-term gain is going to be a long-term loss for the company." Griffin also said that FEMA makes the rules and insurance companies follow them. But now, after months of criticism, FEMA has acknowledged those rules need to be fixed. "As a guy who is standing in the middle of the storm right now, this is not the program that can deliver the best service for our survivors, and we do everyone a service if we reform it now," Brad Kieserman, FEMA's new head of the National Flood Insurance Program, said in an interview. Kieserman explained that what happened with Sandy claims was the result of a slow accumulation of unchecked policies that created an incentive to shortchange homeowners. He added that FEMA's limited staff was insufficient to patrol the numerous insurance companies processing claims. "How do you oversee that with 75 employees out of Washington?" he asked. "How do you oversee 82 companies with thousands of employees each, with [only] 75 people?" Kieserman said he is considering sweeping reforms to the flood program. That could include reducing the number of insurance companies contracted by FEMA or even doing away with them altogether - whatever it takes to regain the trust of policyholders. But Dan Stapleton, the Long Beach homeowner, said he doubts he will ever trust the federal flood program again. "Just from what I've learned. It's been a front-row seat to the most ridiculous pony show I've ever seen in my life," he said. Right now, FEMA is gearing up to reopen as many as 144,000 Sandy claims. State and federal investigators are continuing to probe whether any laws were broken during the claims process. Now that FEMA has stepped in to oversee the ongoing lawsuit settlements, homeowners like Stapleton have started to get good news. Stapleton said the insurance company has reconsidered and will pay his full policy limit of \$200,000. But he is far from excited. He says Sandy victims have become too emotionally raw to care anymore.