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Alternative Options for Resolution of Property and Casualty Claims Arising out of Natural Disasters

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ALTERNATIVE OPTIONS FOR RESOLUTION OF PROPERTY AND CASUALTY CLAIMS ARISING OUT OF NATURAL DISASTERS

By: Kimberly Taylor†

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I. INTRODUCTION

At the time of this Article, at least twelve large wildfires are burning in California across more than 1,000 square miles, having damaged or destroyed over 2,000 structures, according to the California Department of Forestry and Fire Protection (CAL FIRE).¹ At least eight people have lost their lives.² The Kilauea volcano continues to erupt in Hawaii, having destroyed 600 homes.³ The 2018 hurricane season is in full swing, and while there have been no catastrophic events to date, residents in Houston, Florida, Puerto Rico, and elsewhere are still recovering from the devastating winds and rains wrought by Harvey, Maria, and Irma last year. Those hurricanes are estimated to have caused more than \$200 billion in damages, making the 2017 hurricane season the costliest in U.S. history.⁴ Around the world, natural disasters such as deadly heat waves, flooding, mudslides, hurricanes, and

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1. *California Statewide Fire Map*, CAL FIRE, http://www.fire.ca.gov/general/fire_maps (last visited Aug. 16, 2018).

2. Gabby Ferreira & Don Sweeney, *California Wildfires: How Many Fires Are Burning and Where Are They?*, SACRAMENTO BEE (July 30, 2018, 8:30 AM), <https://www.sacbee.com/latest-news/article215746875.html> (updated Sept. 1, 2018, 1:57 PM).

3. Doug Stanglin, *Lava from Hawaii Volcano Has Destroyed 600 Big Island Homes, Mayor Says*, USA TODAY (June 8, 2018, 9:40 AM), <https://www.usatoday.com/story/news/nation/2018/06/08/lava-hawaii-volcano-has-destroyed-600-homes-mayor-says/684158002/> [<https://perma.cc/XE9P-QWER>].

4. Willie Drye, *2017 Hurricane Season Was the Most Expensive in U.S. History*, NAT'L GEOGRAPHIC (Nov. 30, 2017), <https://news.nationalgeographic.com/2017/11/2017-hurricane-season-most-expensive-us-history-spd/> [<https://perma.cc/5UXP-3W33>].

tornadoes will cause untold losses as temperatures across the globe are rising.⁵

After the smoke clears, the ash settles, the waters subside, and initial recovery efforts restore basic functions like the delivery of food, water, and electricity, survivors face the task of rebuilding. Inevitably, property and business owners either look to their insurance carriers for relief or initiate tort actions against alleged wrongdoers. In 2007, more than 2,000 law suits were filed against San Diego Gas & Electric following a series of wildfires that engulfed San Diego County in California, where faulty power lines were blamed for some of the fires. Dozens of cases have been filed in Ventura and Santa Barbara counties in California relating to the deadly Thomas Fire and related devastating mudslides that killed twenty people and destroyed hundreds of homes late last year.⁶

Traditional litigation used to resolve these disputes has the potential to overwhelm the courts, consume limited resources of insurance carriers and others, and be unduly burdensome to survivors. Alternative dispute resolution (“ADR”) mechanisms such as mediation can offer significant relief to the parties, permitting them to negotiate a resolution in a less formal setting than the courthouse, and usually within a shorter time frame than typical litigation would require. In situations where a mass disaster does not easily lend itself to individual mediations, however, providers can customize the process to ensure that all parties—those parties that have suffered losses, insurance carriers, and potentially responsible parties—experience a fair, economic, and efficient resolution. National ADR providers such as JAMS and the American Arbitration Association offer comprehensive, customized processes that can be tailored to meet the needs of the parties and the unique requirements of each case. Individual mediators around the country routinely provide assistance with ADR process design for complex, multi-party matters. Some examples follow.

II. POST DISASTER NEUTRAL REVIEW PROCESSES

A. Hurricane

Superstorm Sandy bore down on the East Coast of the United States on October 29, 2012. It caused billions of dollars in damage across several states. In New York alone, there was an estimated \$19 billion in damage. According to a report issued by the City of New

5. Chelsea Harvey, *Scientists Can Now Blame Individual Natural Disasters on Climate Change*, SCI. AM. (Jan. 2, 2018), <https://www.scientificamerican.com/article/scientists-can-now-blame-individual-natural-disasters-on-climate-change/> [https://perma.cc/ET5W-WKN2].

6. James Rainey, *Montecito Homeowners Sue Utilities, Alleging Negligence Before Deadly Mudslide*, NBC NEWS (Jan. 16, 2008, 6:57 PM), <https://www.nbcnews.com/news/us-news/montecito-homeowners-sue-utilities-alleging-negligence-deadly-mudslide-n838171> [https://perma.cc/A8BQ-2CS6].

York, *Sandy and its Impacts*,⁷ it was the costliest storm in history following Hurricane Andrew in 1992 and Hurricane Katrina in 2005. Forty-three people died and thousands of structures were damaged or destroyed, either by wind or flood waters or both. Predictably, within the following year, those affected by the hurricanes filed hundreds of lawsuits in state and federal courts in New York and New Jersey involving claims against insurance companies and claims under the National Flood Insurance Program (“NFIP”). In the Eastern District of New York (“EDNY”) alone, over 1,400 cases were filed, leading the court to create a specialized mediation program to accommodate the influx. That program, which was managed by a committee of three magistrate judges and involved input from liaison counsel on global issues, is a useful model for other court programs, and information about its structure and implementation is available on the EDNY’s website.

Not every homeowner availed themselves of the courts, however, and many submitted claims through the NFIP, which FEMA administers. Most homeowner’s insurance policies do not cover flood damage, making separate NFIP coverage the primary recourse for property owners suffering losses directly attributable to flooding. FEMA’s website states the following:

The National Flood Insurance Program aims to reduce the impact of flooding on private and public structures. It does so by providing affordable insurance to property owners, renters and businesses and by encouraging communities to adopt and enforce floodplain management regulations. These efforts help mitigate the effects of flooding on new and improved structures. Overall, the program reduces the socio-economic impact of disasters by promoting the purchase and retention of general risk insurance, but also of flood insurance, specifically.

By early 2015, more than two years after Superstorm Sandy, and partly in response to claims of fraud surrounding engineering consultants retained by private insurance companies that issued NFIP policies through FEMA’s Write Your Own program,⁸ FEMA created a Claims Review program that permitted nearly 144,000 NFIP policyholders who previously filed Hurricane Sandy claims to have their claims re-reviewed. According to a February 27, 2018, “Fact Sheet” produced by FEMA,⁹ the agency received 19,467 requests from poli-

7. CITY OF NEW YORK, *A STRONGER, MORE RESILIENT NEW YORK* 12 (2013), http://www.nyc.gov/html/sirr/downloads/pdf/final_report/Ch_1_SandyImpacts_FINAL_singles.pdf [<https://perma.cc/N5EL-C6TK>].

8. *What Is the Write Your Own Program?*, FEMA (Aug. 24, 2018), <https://www.fema.gov/what-write-your-own-program> [<https://perma.cc/W7ZH-CVAJ>].

9. *Fact Sheet: Sandy Claims Review Division Update*, FED. EMERGENCY MGMT. AGENCY (Feb. 1, 2018), https://www.fema.gov/media-library-data/1518101164216-73461746bb31f62a38ff95a90962093f/Updated_Feb1_Final_Fact_Sheet_Sandy_Claims_Review_Division.pdf [<https://perma.cc/7TQY-J3VB>].

cyholders to have their claims re-reviewed. Following FEMA's review, the policyholder had the option of either accepting FEMA's determination of money owed under the NFIP or requesting a Third-Party Neutral Review.

FEMA's Neutral Review program was neither a *mediation*, where each side to a dispute comes together with a neutral facilitator and negotiates a resolution of a claim, nor an *arbitration* or court process, where a neutral fact-finder receives and considers evidence and then renders a final (binding) decision. FEMA's Neutral Review process was unique. FEMA contracted with private ADR provider JAMS to establish a panel of former judges and attorneys (whose practices focused almost entirely on private dispute resolution and who are commonly referred to as "neutrals") to review entire claims files (often consisting of thousands of pages of documents and photographs); conduct a telephonic conference—if requested—with the policyholder, adjusters, and FEMA representatives; and issue a recommendation to FEMA concerning any additional payments that might be owed. Because JAMS and its neutrals were contractors of the government, they were not in a position to direct payments or bind FEMA to any particular result requiring the payment of government or taxpayer funds. Instead, FEMA would review the neutral's recommendation to determine whether it complied with agency regulations and policy and then determine whether to adopt the recommendation.¹⁰ According to statistics published by FEMA in early 2018, 2,454 files were submitted for neutral review, 2,082 files were completely processed, and in approximately 90% of the files, FEMA concurred with the neutral reviewer's recommendation. FEMA paid more than \$44 million in additional compensation to policyholders under this program, which concluded in early 2018.¹¹

B. *Fire*

In 2007, several wildfires erupted in San Diego County, eventually leading to more than 2,000 law suits filed against San Diego Gas & Electric by more than 5,000 plaintiffs and involving multiple insurance carriers, underwriters, and government agencies. Such massive litigation had the potential of completely overwhelming the court system and delaying much-needed compensation to victims. All stakeholders were interested in finding a more efficient method to resolve the disputes, and they worked together to craft a sophisticated mediation program where 98% of the cases ultimately settled for total recovery of more than \$800 million.¹²

10. *Id.*

11. *Id.*

12. John Pardun, *How ADR Can be Used to Resolve Mass Disaster and Insurance Claims*, INT'L IN-HOUSE COUNS. J., Spring 2013; See also Henry Meier, *Neutrals Cre-*

The parties spent approximately sixty days negotiating the protocols for exchange of documents, property inspections, hearings, damages, pre-judgment interest, valuation of crops, and reasonable rebuild costs. The stakeholders created timelines and adhered to them, grouped cases with similar issues together so that patterns relating to damages and other issues were treated in similar fashion, and quickly moved the cases along. According to retired Fourth District California Court of Appeals Justice John Trotter, who orchestrated the creation of the mediation program, “When there’s a massive number [of cases] it [i]s much more productive to use something like this. You need a structured, disciplined, agreed-upon approach.”¹³ And as noted by JAMS mediator Viggo Boserup, who participated in the mediations and served as Special Master, the process may be duplicated in other matters such as products liability or pharmaceutical cases, or any situation with multiple claimants dealing with a single, similar event. A system like this can be used in product cases, pharmaceutical cases, and automobile cases. Similar mediations worked in World Trade Center cases and Virginia Tech shooting cases. It’s ideal for situations when multiple claimants arise out of a single, similar circumstance.”¹⁴

III. COMPENSATION FUNDS

Most Americans are familiar with the establishment of the 9/11 Victim Compensation Fund, which was created by Congress to provide compensation for those who suffered physical harm or death as a result of the terrorist attacks of September 11, 2001. In his book, *Who Gets What: Fair Compensation After Tragedy and Financial Upheaval*, Kenneth Feinberg described the process by which, as Special Master of the Fund, he distributed more than \$7 billion to approximately 5,500 individuals. The process was complex, essentially bypassed the tort system entirely, and according to Mr. Feinberg, is not likely to establish a precedent because of the unique circumstances surrounding its creation.¹⁵

Yet other private contributions from individual donors have established compensation funds, such as the following: Hokie Spirit Memorial Fund in the wake of the 2007 Virginia Tech mass shooting, totaling over \$7 million;¹⁶ and One Fund Boston, which distributed approxi-

ate Streamlined Process for Resolving Natural Disaster Cases, L.A. DAILY J., Mar. 15, 2013, at 1.

13. *Id.*

14. *Id.*

15. Feinberg, Kenneth, *Who Gets What: Fair Compensation After Tragedy and Financial Upheaval*, PublicAffairs, New York, 2012, p. 57.

16. *Id.*

mately \$61 million to survivors and families of victims of the Boston Marathon bombings.¹⁷

Not all compensation funds relate to terrorist attacks or mass shootings, and the model can be applied to both man-made and natural disasters. Following the 2010 Deepwater Horizon oil rig explosion—which killed eleven people, injured scores of others, and discharged millions of gallons of raw oil into the Gulf of Mexico—British Petroleum agreed to create a compensation fund of \$20 billion (Gulf Coast Compensation Fund) to reimburse individuals and businesses that suffered economic harm as a result of the disaster. Individuals filed over one million claims, and the Gulf Coast Compensation Fund distributed more than \$6 billion.¹⁸

In 2012, another application of the compensation fund concept occurred when a life insurance company under receivership since the early 1990s entered into a state-supervised liquidation and restructuring. As a consequence of the liquidation, approximately 1,500 persons were anticipated to have annuity benefits reduced, in some cases significantly. The total uncovered amount following the liquidation was estimated to be approximately \$900 million. Many of these people purchased annuities in the early 1980s after settling catastrophic injury and death cases. Some annuitants were gravely disabled, and a reduction in benefits would have a profoundly negative impact on their daily lives.

Although not required to do so under the law or any liquidation order, a consortium of life insurance companies voluntarily committed to establishing a \$100 million “Hardship Fund” to assist those people most affected by the liquidation. Despite this distribution of largesse, the total uncovered amount following the liquidation was estimated to be approximately \$900 million, leaving a substantial gap in benefit payments. Unlike a traditional settlement fund following the resolution of a mass tort claim, eligibility would have to be determined based on relative hardship and need.

JAMS, in consultation with a specially-selected team of neutrals, an independent ethicist, and members of the structured settlement and life insurance industries, developed guidelines for review of applicants to ensure the funds were distributed to those most in need. The guidelines included: (1) an analysis of whether a reduction in annuities impaired the ability of payees to receive necessary medical care and/or cover basic living expenses; (2) the totality of the financial resources available for the benefit of payees, including among others: Social Security, Medicare, Medicaid, other benefit programs, private insurance,

17. See Mitchell Weiss, *Lessons Learned from Boston’s Experiment with the One Fund*, HARV. BUS. REV. (Jan. 22, 2016), <https://hbr.org/2016/01/lessons-from-bostons-experiment-with-the-one-fund> [<https://perma.cc/EF2X-ZW38>].

18. Feinberg, *Who Gets What: Fair Compensation After Tragedy and Financial Upheaval*, p. 175.

other sources of income, i.e., employment and pension payments; (3) the degree to which physical injuries suffered by payees affected their ability to provide for their own care and to provide financially for family and dependents; and (4) the degree to which reductions in the amount of annuity benefits would be expected to jeopardize payees' medical care and/or impair daily life functions, such as transportation, social activities, family interaction, or other similar activities.

Individuals could submit to the fund an application describing their financial status, medical history, and any other factors weighing on the issue of hardship and need. The neutral team was empaneled to review each application; conduct additional efforts to reach non-responding payees or request additional information; review objective factors such as the original annuity/settlement amount, current financial circumstances, and medical histories; and make a determination about the amount of financial support each payee should receive.

JAMS received approximately 835 unique applications and issued more than 300 monetary awards. The JAMS administrative team also investigated other sources of payment for impacted individuals, including contact with original defendants and/or their insurers, some of whom were obligated under the law to make up any shortfalls caused by the liquidation. JAMS verified coverage from this source for an additional 265 people.

Keeping in mind the overarching goal of the Hardship Fund—to assist those annuitants most affected by the liquidation—JAMS took great efforts to reduce the negative financial impact for those annuitants who demonstrated the greatest hardships and needs resulting from the demise of the insurance company. The application process and the rigorous review and oversight by a team of experienced former judges and attorneys were designed to provide objectivity and consistency to the allocations.

IV. CHALLENGES AND LESSONS LEARNED

ADR options for resolving claims resulting from natural disasters or other catastrophic events are not without challenges. Property valuations are relatively objective, but how does one value a human life? What proof is required to establish loss when homes are demolished beyond all recognition? What level of due process is realistic and manageable when thousands of individuals seek compensation from a finite fund? How should an administrator deal with individuals who are likely not represented by counsel and may have little understanding of how the process should work, complicated by the emotions and stress brought on by the disaster?

In the aftermath of Superstorm Sandy, disputes were resolved along multiple tracks—state and federal courthouses in several states, court-annexed mediation, and arbitration programs—through private ADR

providers and the Sandy Review process described previously. In an ideal world, and as a potential model for the future, coordination and information sharing among the dispute resolution professionals might have improved the outcomes. A mediated approach with input from all stakeholders in the design of specialized dispute resolution processes (as modeled in the San Diego fire cases) would likely lead to a more efficient process in the long run and would resolve unanticipated issues that might arise as programs are implemented.

Unfortunately, disasters and other mass tragedies are inevitable. As the current spate of fires in California are brought under control, it is expected that a Special Master will be appointed to deal with and likely mediate the 2017 fire claims consolidated in the San Francisco Superior Court. Such appointments are, in essence, illustrative of how the “a” in the ADR acronym is now becoming less of an alternative and more of the accepted manner to handle large-scale dispute resolution.

In summary, lessons can be learned from the programs described above, as well as other large-scale ADR programs that are managed in accordance with special rules, procedures, and protocols.¹⁹ It is important to note, however, that while ADR can yield better results than traditional processes, there is no “one size fits all” approach that works in every scenario or every dispute.

19. Among many other matters, for example, JAMS has allocated an \$80 million settlement to over 13,000 claimants in an oil refinery litigation, adjudicated the largest civil right settlements in U.S. history involving tens of thousands of claims, allocated billions of dollars to thousands of claimants in landmark pharmaceutical and medical device mass tort settlements, and resolved numerous claims arising from data breaches and other ‘single event’ instances yielding large numbers of telephonic and paper arbitrations.