



UNITED STATES
CIVILIAN BOARD OF CONTRACT APPEALS

December 11, 2017

CBCA 5457-FEMA

In the Matter of ORLEANS PARISH SCHOOL BOARD AND LOUISIANA
RECOVERY SCHOOL DISTRICT

Brent B. Barriere and Degan Skylar Rosenbloom of Fishman Haygood LLP, New Orleans, LA; Earnest B. Abbott of Baker, Donelson, Bearman, Caldwell & Berkowitz, PC, Washington, DC; and Wendy Huff Ellard of Baker, Donelson, Bearman, Caldwell & Berkowitz, PC, Jackson, MS, counsel for Applicants.

Mark S. Riley, Deputy Director, Carla Richard, Appeals Manager, and Danielle Aymond, Executive Counsel, Governor's Office of Homeland Security and Emergency Preparedness, Baton Rouge, LA, appearing for Grantee.

Charles Schexnaildre, Office of Chief Counsel, Federal Emergency Management Agency, Department of Homeland Security, Baton Rouge, LA; and John Ebersole and Brock Pierson, Office of Chief Counsel, Federal Emergency Management Agency, Department of Homeland Security, Washington, DC, counsel for Federal Emergency Management Agency.

Before the Arbitration Panel consisting of Board Judges **KULLBERG**, **CHADWICK**, and **O'ROURKE**.

This matter, CBCA 5457-FEMA, is a request for arbitration by the applicants, the Orleans Parish School Board (OPSB or applicant) and the Louisiana Recovery School District (RSD or applicant) regarding public assistance from the Federal Emergency

Management Agency (FEMA) for damage caused by Hurricane Katrina (Katrina).¹ At issue is the extent to which the applicants received proceeds from insurance settlements that duplicated eligible public assistance for Katrina-related damage. This matter is before the panel under authority of section 601 of the American Recovery and Reinvestment Act of 2009 (ARRA), Pub. L. No. 111-5, 123 Stat. 115, 164, and section 206.209 of title 44 of the Code of Federal Regulations. The grantee, the Governor's Office of Homeland Security and Emergency Preparedness (GOHSEP), supports the applicants' position in this matter.

Katrina struck the city of New Orleans, Louisiana, on August 29, 2005, and flooding occurred throughout much of the city. In addition to flooding, wind and wind-driven rain (collectively referred to as "wind") caused or contributed to property damage. The New Orleans school system suffered a similar level of devastation. More than 400 school buildings were damaged. FEMA determined that 271 of those school buildings would need to be replaced and provided roughly \$2.1 billion in funding. Such funding included both emergency work and permanent repairs to existing buildings as well as construction of new buildings. FEMA issued numerous project worksheets (PWs) for that work.

When Katrina struck, the OPSB had a commercial insurance policy in the amount of \$50 million with the Lexington Insurance Company (Lexington) for the period from May 1, 2005, to May 1, 2006.² The OPSB's policy with Lexington provided coverage for "all risks of direct physical loss or damage, including flood and earthquake." The policy contained language that provided coverage for "real [and] personal property (BPP), business income [(BI)], and extra expense [(EE)] including rents." In addition to the OPSB's insurance coverage with Lexington, there were also three successive layers of excess coverage with other insurers, which comprised the "Lexington tower." The first layer of excess coverage was divided between two insurers, Clarendon America Insurance Company and Essex Insurance Company (Clarendon/Essex),³ in the amount of \$25 million; the second layer of coverage was with Westchester Surplus Lines Insurance Company (Westchester) in the

¹ Both the OPSB and RSD managed schools within the New Orleans school system after Katrina. The applicants have represented that the Board "can treat OPSB/RSD as one entity with common interests."

² The Lexington policy provided for flood coverage up to \$2.5 million. OPSB also had insurance on its school buses and additional flood insurance under other policies.

³ The \$25 million in coverage by Essex/Clarendon was divided between the two companies, with Essex providing coverage up to \$15 million and Clarendon providing coverage up to \$10 million.

amount of \$25 million; and the third layer was with RSUI Indemnity Company (RSUI) in the amount of \$100 million.

After Katrina, the OPSB filed a claim under its policy with Lexington. In a letter dated May 18, 2006, the OPSB took issue with Lexington's offered payment of \$25 million. The OPSB contended that wind damage was approximately \$68 million, which exceeded the value of the policy. With regard to flood damage, the OPSB took issue with Lexington's position that such damage was limited to \$2.5 million under the policy. Instead, the OPSB interpreted the policy as providing \$2.5 million in coverage "at each location where damages are sustained." The record, however, does not indicate that the OPSB sought any recovery for flood damage under the Lexington tower policies after sending that letter. Finally, the OPSB asserted that the policy also covered business interruption losses, which included EE and BI losses, but the amount of such losses was not set forth in that letter.

On August 9, 2006, the OPSB filed suit against Lexington in the District Court for the Parish of New Orleans (district court). In its pleading, the OPSB alleged that Lexington had offered payment of \$25 million, but its losses far exceeded the \$50 million limit of its policy. Additionally, the OPSB stated that its property loss was in excess of \$800 million. Also, the OPSB represented that it had other losses, which included EE and BI, but no dollar amount was alleged for those losses. In an amended pleading, the OPSB included the other insurers in the Lexington tower as defendants, and the RSD intervened in the suit. A lengthy period of litigation ensued.

On June 5, 2009, the OPSB and Lexington executed a settlement agreement that resulted in payment of \$50 million, the full amount of the policy, less a payment of \$439,827 to a third party for the cost of leasing modular buildings. The RSD joined in the settlement. The settlement agreement did not identify the type of loss or damage for which the applicants were receiving compensation under the terms of the settlement.

For roughly four years after Katrina, the applicants still had not completed a proof of loss for wind damage. During 2010, a lawyers consortium acting on behalf of the OPSB hired Adjusters International (AI) to determine the amount of wind damage. Initially, AI determined that wind damage to buildings alone totaled \$1,073,057,163.08. The Lexington tower insurers employed Unified Building Services (UBS) for the same purpose. The task of determining the amount of wind damage took several years.⁴

⁴ The documentary evidence of AI's findings include a letter from UBS, which was dated May 29, 2013, and a letter from the OPSB's counsel, which was dated July 13, 2015.

In July of 2010, the OPSB filed a motion for partial summary judgment against the remaining Lexington tower insurers regarding its claim for EE and BI loss. On August 18, 2011, the district court granted the OPSB's motion. *Orleans Parish School Board v. Lexington Insurance Co.*, No. 2006-7342 (Aug. 18, 2011). The court ruled that the Lexington policy and the other policies in the Lexington tower, which were "follow-form policies," provided blanket coverage for EE and BI loss up to the dollar amount of those policies.

After the district court issued its decision, Clarendon/Essex reached a settlement with the applicants in the amount of \$22.5 million. An order dismissing the action against Clarendon/Essex was issued on February 1, 2012. The settlement agreement with Clarendon/Essex was silent as to what types of losses or damage were contained in the amount of the settlement.

With only two of the four insurers in the Lexington tower remaining that had not reached settlements with the applicants, the task of determining the amount of the applicants' losses continued. On March 13, 2012, AI submitted to UBS a revised report on wind damage, which did not include building contents, in the amount of \$216,338,009.83. The OPSB submitted to its insurers on March 25, 2012, a proof of loss statement for its combined BI loss and EE in the amount of \$194,838,142.19. That amount included a BI loss of \$41 million, which was the result of a decline in revenue compared to expenses for the period from 2006 to 2008. In addition, the OPSB claimed EE in the amount of \$153.8 million, which included expenses such as construction management, leasing of temporary facilities, settlements, and legal fees.

Westchester and RSUI appealed the district court's decision, and on August 22, 2012, the Court of Appeal of Louisiana, Fourth Circuit (fourth circuit) reversed the district court's decision. *Orleans Parish School Board v. Lexington Insurance Co.*, 99 So.3d 723 (La. Ct. App. 2012). The fourth circuit held that the district court "erred in concluding that the excess insurance policies provide blanket coverage for business income and extra expense, when both policies limited any coverage to items listed and values stated on the Statement of Values filed with the Excess Insurers." *Id.* at 726-27. The fourth circuit remanded the case to the district court on the issue of coverage for EE and BI loss. *Id.* at 729. Westchester executed a settlement agreement with the OPSB and RSD in the amount of \$17 million on October 25, 2012. The applicants' agreement with Westchester was also silent as to what types of losses or damage were contained in that agreement.

On February 12, 2013, AI again revised the amount of wind damage to \$204,955,690.92. In its letter dated May 29, 2013, UBS criticized AI's findings and determined that the amount of wind damage was the considerably lesser amount of

\$42,538,676.51. UBS, however, recognized that AI had gathered over several years a substantial documentary record in support of its findings, which included twelve million PDF files.

Almost one year after the fourth circuit issued its first decision, that court issued its second decision and held that the Westchester and RSUI policies only provided coverage for EE in the amount of \$5 million and no coverage for BI loss. *Orleans Parish School Board v. Lexington Insurance Co.*, No. 2013-C-0511 (La. Ct. App. Aug. 14, 2013). On October 15, 2013, RSUI executed a settlement agreement with the applicants in the amount of \$37.5 million. As was the case with the previous Lexington tower settlements, the RSUI settlement agreement did not break down the amount of those settlements in terms of the types of damages or losses included in the amount paid. Having reached settlements with all of the Lexington tower insurers, the applicants received a total of \$126,560,172.

The record shows that AI made a final determination as to wind damage to both property and building contents, which is documented in a July 13, 2015, letter from the OPSB's legal counsel. That letter represented that wind damage to real property totaled \$174,511,537, and damage to building contents totaled \$57,669,153. The OPSB's counsel also represented that UBS had hired Stoner & Company to determine building contents losses, which amounted to \$9,684,106, and FEMA made a separate determination of building contents loss, which was \$33,036,416. The OPSB's counsel took the position that the dollar amount for wind damage should be computed by averaging AI's and UBS' findings, which would amount to \$108,525,122. Additionally, the OPSB's counsel contended that the dollar amount for building contents damage should be the amount determined by FEMA, as that amount was roughly an average between the amounts determined by AI and UBS.

In anticipation of the applicants' receipt of insurance proceeds from the Lexington tower, FEMA withheld a portion of public funding until a determination could be made as to what portion of those proceeds amounted to a duplication of benefits. FEMA and the applicants spent a considerable amount of time discussing how to apportion the Lexington tower settlement between eligible expenses, which duplicated public funding and would be retained by FEMA, and ineligible expenses, which did not duplicate public funding and would be released to the applicants. By letter dated April 14, 2016, the applicants proposed to FEMA an apportionment of the Lexington tower settlement that consisted of 59.79% eligible expenses and 40.21% ineligible expenses. In computing that apportionment, the applicants represented that the total of their eligible and ineligible expenses exceeded the Lexington tower settlement. The applicants contended that their eligible expenses for wind damage to buildings and building contents amounted to \$141,121,755.59, and their ineligible

expenses totaled \$94,922,623.35. Their ineligible expenses included EE, \$20 million; BI loss, \$57,979,634; and a recovery for bad faith in its settlement with RSUI, \$15 million.⁵

By letter dated July 27, 2016, FEMA determined that the apportionment ratio for the Lexington tower settlement was 85.22% eligible expenses, which amounted to \$90,155,413.80 in duplication of benefits, and 14.78% ineligible expenses. FEMA held that the applicants' ineligible expenses included only \$20 million for EE, which represented coverage of \$5 million for each policy in the Lexington tower, and found no coverage for BI loss. The apportionment ratio was computed using the total of the Lexington tower settlement, which was eligible expenses, and the recovery for EE, which was ineligible expenses. Additionally, FEMA determined that the applicants had not established that any portion of the RSUI settlement included a recovery for bad faith.

FEMA made its determination for the apportionment of the Lexington tower settlement in accordance with Disaster Assistance Fact Sheet DAP9580.3 (fact sheet). That fact sheet, which was issued in 2008, was not in effect when Katrina struck New Orleans, but FEMA relied on it in order to provide the maximum benefit for the applicants.⁶ The fact sheet stated in pertinent part the following:

Where eligible and ineligible damage is insured in one policy, how will the insurance settlement proceeds be apportioned?

- If the Applicant's insurance policy specifies the amount of coverage for each type of loss, the proceeds will be apportioned according to the policy limits.
- If the insurer provides a Statement of Loss that specifies the amount of proceeds per type of loss, that will be used to determine the proceeds for eligible damage.
- If the Applicant's insurance covers eligible and ineligible damage (for example, property damage and business interruption losses respectively) without specifying limits for each type of loss, the proceeds will be apportioned based on the ratio of the Applicant's

⁵ The applicants acknowledged that the amount of their BI loss, which had been \$117,455,688, was reduced as the result of the forgiveness of a Special Community Disaster Loan.

⁶ FEMA's Brief at 6.

eligible to ineligible damage. For example, if the Applicant's total losses are 60 percent property damage and 40 percent business interruption, then 60 percent of the insurance proceeds would be applied to offset the eligible damage, since business interruption losses are not eligible for reimbursement under the [public assistance] Program.

In response to FEMA's July 27, 2016, determination, the applicants requested an arbitration before the Board in which they alleged that they were entitled to the release of additional public funding in the amount of \$29,706,637.53. A three-day hearing followed. The panel issued a detailed order subsequent to the hearing that requested that the parties address the standard of review and burden of proof in light of the issues presented in this matter. Both parties submitted briefs after the hearing as directed by the Board.

The question of whether public funding received by an applicant is duplicated by other funds received by that applicant is addressed by the Stafford Act, 42 U.S.C. §§ 5121-5207 (2012), which provides, in pertinent part, the following:

The President, in consultation with the head of each Federal agency administering any program providing financial assistance to persons, business concerns, or other entities suffering losses as a result of a major disaster or emergency, shall assure that no such person, business concern, or other entity will receive such assistance with respect to any part of such loss as to which he has received financial assistance under any other program or from insurance or any other source.

Id. § 5155(a). Additionally, “[a] person receiving Federal assistance for a major disaster or emergency shall be liable to the United States to the extent that such assistance duplicates benefits available to the person for the same purpose from another source.” *Id.* § 5155(c). Regulation provides that “[a]ctual and anticipated insurance recoveries shall be deducted from otherwise eligible costs, in accordance with this subpart.” 44 CFR 206.250(c) (2015).

The issue before the panel is what amount of eligible expenses were actually received or available to the applicants under the Lexington tower settlement. It has been established that “[42 U.S.C.] § 5155(c) requires disaster aid recipients to reimburse FEMA the duplicative benefits that they actually received and also requires the recipients to reimburse any additional benefits that they would have received had they acted in a commercially reasonable manner.” *Hawaii v. Federal Emergency Management Agency*, 294 F.3d 1152, 1165 (9th Cir. 2002). The Ninth Circuit stated additionally that duplicative benefits included

not only those received by an applicant, but also “any duplicative relief that was available to it, whether that relief was received or not.” *Id.* at 1160.

Both parties’ briefs addressed the cost of wind damage to the applicants’ property. There is no dispute that the Lexington tower policies covered wind damage up to the value of those policies. The applicants alleged in their brief that wind damage, including buildings and building contents, was only \$57 million and cited the testimony of one of FEMA’s witnesses, Neil Cason, in support of that finding.⁷ That amount for wind damage asserted by the applicants was considerably less than the amount that they had asserted before their request for arbitration. Previous to their request for arbitration, they had asserted that wind damage was in excess of \$141 million. In contrast, FEMA’s brief noted that the applicants’ witness, Robert Kutcher, testified that wind damage was roughly \$200 million.⁸ Additionally, FEMA has relied upon documentary evidence provided by the applicants in order to determine the amount of wind damage.

The task of the panel comes down to a very basic question of the dollar amount of wind damage with regard to the Lexington tower settlement. Putting aside the testimony of Mr. Cason and Mr. Kutcher, AI, apparently, generated a voluminous record that would show wind damage to buildings and building contents well in excess of \$200 million. UBS, which represented the insurers, contended that wind damage to buildings and contents was a considerably lesser amount. The applicants have advanced a wide range of dollar amounts for wind damage at various points before and after the hearing of this matter without a sound basis to explain those changes in their position. UBS’ correspondence and correspondence from the applicants’ counsel indicates a substantial record in support of a finding that wind damage was likely in excess of the Lexington tower settlement. Moreover, the applicants asserted in their April 14, 2016, submissions to FEMA that wind damage was in excess of \$141 million, which exceeded the total Lexington tower settlement. Using the information available from the applicants, FEMA would have been well within its authority under the Stafford Act to have deemed the entire amount of the Lexington tower settlement to have been duplicative of public funding. Consequently, FEMA’s apportionment of the Lexington tower settlement in accordance with the fact sheet allowed a release of more funds to the applicants than was required under the Stafford Act. The majority of the panel does not deem it necessary to disturb that result.

⁷ Applicants’ Brief at 6. Mr. Cason testified that total property damage due to wind was \$62 million. Transcript at 677.

⁸ FEMA’s Brief at 22. Mr. Kutcher testified that wind damage constituted ten percent of the \$2 billion in total damage to the applicants’ school property. Transcript at 156.

The panel notes the applicants' proposed findings that EE and BI loss were extensive and that a significant portion of the Lexington tower settlement should be attributed to those losses. However, the threshold issue of wind damage was never addressed satisfactorily by the applicants, which makes any effort at apportionment of eligible and ineligible expenses all but futile. As discussed above, the Stafford Act allowed FEMA to recover duplicative benefits actually received or that were available, and there was no requirement for FEMA to follow the fact sheet retroactively to apportion eligible and ineligible expenses.

Decision

The applicants' request for an increase of public funding is denied.

H. CHUCK KULLBERG
Board Judge

KYLE CHADWICK
Board Judge

I respectfully dissent from the majority's opinion. There is no dispute that the Lexington Tower insurance policies contained coverage for losses that were considered eligible *and* ineligible for public disaster assistance grants. Nor is there any dispute that losses covered by FEMA grants *and* insurance policies constitute a duplication of benefits under section 5155(c) of the Stafford Act—a result that is understandably prohibited by the statute. Where I take issue with the majority's opinion is its affirmation of FEMA's apportionment of the insurance proceeds when the evidence favors the applicants' position.

FEMA's demand for the majority of the applicants' insurance money must be supported by a determination that the funds duplicate public assistance grants. In the absence of regulations governing this determination, a reasonable approach would entail an analysis of the insurance policies and the settlement agreements to discern where the benefits overlap. What complicates this task is the fact that each of the four settlement agreements was silent as to how the proceeds were allocated in terms of coverage type.¹ This predicament, however, does not excuse the determination of duplicate benefits mandated by section 5155(c).² The record contains sufficient information about the insurance policies and the settlement negotiations to support the applicants' apportionment of the insurance money.

Beginning with the policies themselves, it is undeniable that the applicants' understanding of their own insurance policies and the resulting settlements is superior to FEMA's. The applicants purchased the insurance policies, paid the premiums, and litigated against their insurers for *eight* years in order to receive the benefits thereunder. FEMA, on the other hand, declined to participate in the litigation or settlement discussions. The applicants, therefore, cannot be less informed than FEMA as to the nature of their agreements. The parties' presentations at the hearing reflect this disparity.

During the hearing, the applicants presented extensive information showing that the insurance policies collectively contained coverage in varying amounts for property loss, business interruption (BI), and extra expense (EE), and that coverage for losses of each type were fiercely litigated prior to settling with the individual insurers. The first insurer settled for the full value of its policy after the applicants validated wind damage of \$68 million (a FEMA-eligible loss). The second insurer settled after the applicants filed suit against their insurers in district court, and the court held that BI could be recovered up to the full value of the policy. The third and fourth insurers appealed, and the appellate court reversed and remanded the case to determine BI coverage based on the stated values of the policies. The third insurer then settled. The fourth insurer –and the largest of the four–settled only after the appellate court found no BI coverage in its policy and decided that the allegation of bad faith would go to a jury.

¹ In their brief, the applicants pointed out that “when insurance disputes are litigated, they are frequently settled in the manner of OPSB’s settlements: in a black box settlement in which the insurers make a lump sum payment in return for settlement of all claims and often, as is the case here, with the insurer disclaiming any liability for any losses.”

² It may be tempting to place the risk of this deficiency on the applicants, but such an approach must be balanced against the risk of foregoing immediate use of settlement money in order to pursue a precise allocation of insurance proceeds through continued litigation.

FEMA's apportionment ignores all but one fact in the settlement history of this case: that the last insurer's policy did not cover BI. Instead of accepting the scope of that ruling, FEMA interprets the holding to mean that BI was not covered in *any* of the policies, given the follow-form nature of the policies. FEMA asks that the panel speculate (as it did in calculating its apportionment) that had the first three insurance companies held out for eight years (like the fourth one did), the court would have found those policies to contain no BI coverage. Although FEMA supports speculation on this issue, it does not desire that the Board speculate on what might have happened had the issue of bad faith gone to a jury in Louisiana.

Despite the facts and circumstances surrounding the settlements, the contents of the policies, and the conclusions of expert reports, the majority reasons that because the applicants failed to establish the amount of wind damage, "any effort at apportionment of eligible and ineligible expenses [is] all but futile." I disagree. There are at least four different figures for wind damage in the majority's own opinion, two of which were raised by the applicants during the insurance litigation: \$68 million and \$57 million. It is far more reasonable, especially in this arbitration forum, to choose one of these numbers, or to average them, than to defer to FEMA's insurance expert, who could not articulate a reasonable basis for FEMA's position.

Furthermore, the majority acquiesces to FEMA's position *not* because it agrees with its apportionment, but because it interprets the word "available" as meaning "whatever is on the table" from insurers—in this case \$126.5 million. Construing "available" in this manner either omits the important step of finding the funds duplicative, or presumes them as such since the applicants suffered more than that amount in property loss. Whatever the case, we cannot turn a blind eye to insurance coverage that the applicants paid for, then fought to recover through years of litigation.

Had the insurance process worked as expected, the applicants would have been paid under their policies for various losses in each category, then FEMA could have supplemented the insurance proceeds with disaster assistance grants. Under that scenario, the applicants would have had the full spectrum of insurance benefits *and* disaster assistance grants available for recovery efforts. Because the money came in the reverse order, and the insurers claimed no liability in their settlements, the applicants are deprived of benefits that FEMA could not otherwise claim.

The fact that the applicants received substantial disaster assistance funding in the aftermath of Hurricane Katrina is of no import in the analysis of duplicative benefits. The Stafford Act is clear: recouped funds must be duplicative. The applicants have sufficiently demonstrated that coverage for ineligible losses and the specter of bad faith largely

contributed to the resulting \$126.5 million settlement. FEMA's apportionment, on the other hand, flies in the face of Congress' purpose for prohibiting duplicate benefits: to incentivize disaster victims to aggressively pursue insurance benefits and avoid creating a subsidy for insurers. Congress did not intend for disaster victims to give money back to the Government simply because it was *available*; Congress' intent was to avoid duplication, and it expected its representatives to find duplication—not presume it, especially in the face of evidence to the contrary.

KATHLEEN J. O'ROURKE
Board Judge