Glimmers of Hope

Reforming insurance regulation amid ever-expanding California FAIR Plan exposures

C A R Strategic Planning Forum
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Disclaimer

Nothing in this presentation is intended, or should be relied upon, as legal advice.

All statutes and bill texts are available at: https://leginfo.legislature.ca.gov/

"Quick Bill Search," or "Quick Code Search," on home page

Or use tabs for "Bill Information" or "California Law." Mind the legislative session when using the "Bill Information" tab. Current default is 2025-26.

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The worst availability crisis most independent agents and brokers have ever experienced.

More than $40 billion in insured losses between 2017-24.

Global warming and worsening draught, forest mismanagement, utility negligence, growth in WUI, inflationary and supply chain problems.

Delays of up to two years to get rate approvals from CDI

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California property/casualty insurers require political approval to increase rates

Prop. 103 required premium refunds, made the job of Insurance Commissioner an elected position, and imposed a “prior approval” system that ultimately was designed (post-*Calfarm*) to suppress rates and delay rate increases.

Insurers learned to live with the regulations because property insurance has historically been highly consistent, predictable and profitable. The only catastrophic losses California has experienced with regularity in the past (EQ and Flood) are expressly excluded from most property policies.

Regulators and legislators were unwilling to admit, or unable to recognize, the property insurance market was constricting.

Insurers and their trade associations were reluctant to publicly criticize the Insurance Commissioner, because he holds plenary authority and unfettered discretion over their rates.

Two years ago+, Commissioner Lara continued to deny there were any availability problems. Then State Farm announced it wasn't writing any new policies—which captured international media attention and made Lara's continued denial untenable.

A politically influential coalition led by IIABCal and CAR was formed.

IIABCal came to the California Association of Realtors, the California Building Industries, the California Farm Bureau, mortgage lenders, as well as organizations representing condominium assoications and apartment owners—the actual consumers of insurance—to enlist the support of Governor Newsom and legislative leaders, including the chairs of the two insurance committees—to pressure Lara to either solve this crisis, or get out of the way while others did.

Possible legislative solution to the ongoing availability crisis in California property insurance.

Negotiations in early August 2023 involving the Governor, Insurance Commissioner, Legislative leaders, representatives of our coalition including CAR, as well as insurance industry stakeholders, including IIABCal, produced a detailed conceptual plan for restoring competitive health to the property insurance marketplace.

Opposition in the Legislature, and the imminent end of the session, combined to kill the plan before it could be amended into a bill or voted upon.

On 9/21/23, the Governor declared a state of emergency, and the Commissioner announced his Sustainable Insurance Strategy.

- Crediting insurers for reinsurance costs attributable to California exposures.
- Permiting insurers to use prospective risk modelling for catastrophic loss exposure, rather than solely historic actual loss costs.
- Speeding prior approval process by requiring CDI to comply with existing “deemer” provisions.
- Reining in paid intervenors
- Strengthening FAIR Plan financial strength, and permitting recoupment of assessments

Insurers must agree to resume writing and renewing property insurance risks in distressed areas.

To take advantage of the new rating rules, insurers must agree to maintain or increase their book of business in "distressed areas," or remove risks from the FAIR Plan. One method is to agree to write at least 85% of an insurer's current book of business in non-distressed areas in zip codes determined to be "underserved." Insurers have other options, permitting them to ask the Commissioner to waive or modify that requirement.

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There is still no "immediate fix."

While the Commissioner submitted his final set of proposed regulations (on net cost of reinsurance) in the closing working hours of 2024, every insurer wishing to use the new regulatory tools will be required to file, and receive CDI approval to use, detailed new rating plans.

Those applications are subject to prior approval—and paid intervenor—requirements. Assuming (1) that none of the Commissioner's regulations are judicially challenged, and (2) that the Legislature avoids sabotaging or second-guessing the reforms, it will likely take many months before insurers can avail themselves of the new tools.

The California FAIR Plan

The Fair Access to Insurance Requirements Plan is a private association comprised of all insurers licensed to write property insurance in California and is funded primarily through the policies it sells to customers. The FAIR Plan is not a state agency and is not funded by the state or other public agencies.

The FAIR Plan offers basic property insurance for all Californians who cannot access coverage in the voluntary insurance marketplace. As an insurer of "last resort," the FAIR Plan was established by statute to provide a temporary safety net for consumers who need fire insurance until coverage through the voluntary market is available.

The California FAIR Plan

As of September 2024 (most recent FY-end), the FAIR Plan's total exposure is $458 billion, reflecting a 61.3% increase over the prior 12 months.since September 2023 (prior fiscal year-end). It has been processing 1,500 new applications—every day.

The FAIR Plan cannot refuse to insure properties because of their location or exposure to wildfire loss. No insurance commissioner in the elected era has obeyed the law requiring Plan rates to be "actuarially sound," leading to grossly inadequate rates in many areas. An increase in commercial coverage (up to $100 million) announced last September is still awaiting CDI rate approval, which is not expected until July.

Nevada City
Exposure - $3,756M
Grass Valley
Exposure - $3,965M
Truckee
Exposure - $5,213M
Berkeley
Exposure - $5,512M
Orinda
Exposure - $4,193M
CALIFORNIA REPUBLIC
Big Bear City
Exposure - $7,105M
Crestline
Exposure - $7,809M
Big Bear Lake
Exposure - $6,727M
Pacific Palisades
Exposure – $5,894M
Lake Arrowhead
Exposure - $9,144M
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The January Southern California catastrophes

Roughly 22% of the structures in the CAL FIRE incident map for the Pacific Palisades Fire, and 12% of the structures in the Eaton Fire incident map, are covered by the FAIR Plan. The FAIR Plan has total potential “exposure” of over $4 billion for the Pacific Palisades Fire, and over $775 million for the Eaton Fire.

“Exposure” does not mean “loss.” Exposure is the total amount of insurance for all insured properties in an area, and would equal losses only if every insured structure was totally destroyed.

Historically, losses typically equate about 30% of potential exposure.

Plan financial resources

The Plan reported $1.4 billion in reserves or other “cash on hand” as of last month to pay all initial covered claims.

It can access up to $5.78 billion in reinsurance proceeds after the first $900 million in claims are incurred. AB 226 introduced as urgency bill.

After reinsurance is exhausted, the Plan can request the Commissioner’s approval to assess all admitted insurers selling property insurance in California, based on their California market share from two years ago. No assessment has been requested in response to the SoCal fires—at least yet.

Potential recoupment of assessments

Last September, Commissioner Lara issued two orders—described in Bulletin 2024-8—which amended the FAIR Plan's plan of operation in several significant ways. Among other things, it required the Plan to increase commercial coverage limits, temporarily, to $20 million per insured building (rather than location), with $100 million in coverage in the aggregate. The orders also expressly authorized insurers, for the first time, to request permission from the Commissioner to "recoup" some or all of potential future assessments.

For assessments up to $1 billion in any calendar year, insurers can request permission to recoup 50% of assessment; for assessments over $1 billion, they can request permission to recoup 100%.

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Impact of SoCal Disaster on Sustainable Insurance Strategy

Only time will tell. But we are cautiously optimistic that the package of reforms the Commissioner has to-date announced have the potential to give insurers the opportunity to charge adequate rates and get faster decisions on rate change requests—two things sorely absent in California rate regulation for the last 30+ years, and keys to restoring competitive health to the property insurance market.

Impact of SoCal Disaster on Sustainable Insurance Strategy

As utterly horrible and unwelcome as the Pacific Palisades, Eaton and other fires have been, they do not come as any particular surprise to the insurance industry. Insurers have long understood the potential for devastating loss of life and destruction of property in those areas—which is exactly why so many insurers non-renewed risks and refused to write new policies in those areas long before the fires started, and why the FAIR Plan had to assume such concentrated loss exposures.

Impact of SoCal Disaster on Sustainable Insurance Strategy

But the voluntary insurance market, comprised of admitted and non-admitted insurers, has demonstrated the ability and even willingness to write policies, even in areas that present catastrophic loss exposures—IF they can charge rates that are actuarially adequate to the risks they are insuring, and if they can get timely regulatory approval to raise rates when needed.

When the Commissioner's reforms fully take effect, we are hopeful that the property insurance market will begin to recover. Somewhat paradoxically, insurers may find a powerful financial incentive to return to the market sooner than later, since the first companies to return will have their pick of FAIR Plan and other policies to underwrite.

For additional information

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