Assembly Insurance Committee

Informational Hearing

California's Homeowners' Insurance Market:
A Report by the FAIR Plan
Assemblymember Tom Daly, Chair

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ASSEMBLYMEMBER, SIXTY-NINTH DISTRICT

Informational Hearing

California's Homeowners' Insurance Market:
A Report by the FAIR Plan
Assembly Insurance Committee
Assemblymember Tom Daly, Chair

Wednesday August 21, 2019
10:00 a.m. – 12 p.m.
State Capitol, Room 437
Sacramento, California

Panel 1 – FAIR Plan and Surplus Lines Coverage

Anneliese Jivan, President -- *California FAIR Plan*

Cliston Brown, Vice President -- *Surplus Line Association of California*

Panel 2 -- Department of Insurance

Joel Laucher, Special Consultant – *Department of Insurance*

Panel 3 -- Consumer Perspectives

Randy Fletcher, Supervisor, District 5 – *Yuba County*

Amy Bach, Executive Director – *United Policyholders*

Panel 4 -- Insurer Perspectives

Rex Frazier, President - *Personal Insurance Federation of California*

Mark Sektnan, Vice President - *American Property Casualty Insurance Association*

Public Comment

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SECTION ONE

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Introduction

In recent years, California has experienced a massive increase in the loss of life and property caused by wildfires. Beginning in 2015 with a spate of fires in Lake County, wildfires have devastated communities around the state including enormous fires in Butte, Shasta, Sonoma, Napa, Ventura, Santa Barbara and Los Angeles Counties. Among the many consequences of the losses caused by these fires are significant changes in the homeowner's insurance market in high fire risk areas.

A study of the homeowner's insurance market released in 2018 as part of the Governor's Fourth Climate Assessment found that insured losses through 2017 wiped out the entire underwriting profit insurers earned since 2000. The 2018 fires continued with another round of enormous losses. These losses have triggered rate filings by many property insurers, which have generally been approved by the Department of Insurance (DOI). The DOI's approval of these rate applications has increased rates (and therefore premiums for most policyholders – see discussion of "rate" vs "premium" below). These rates also generally reflect the widely recognized "new normal" of increased wildfire risks in many areas of the state by focusing the price increases in high risk areas.

In addition to increasing rates, insurers are re-evaluating whether they have an overconcentration of policies in high risk areas. This has resulted in many homeowners in these communities receiving a notice of non-renewal from their insurance company. Homeowners searching for new coverage invariably find it significantly more expensive than their prior policy. In some high risk counties, significant numbers of homeowners do not find a new policy from an admitted insurer, and therefore turn to either the FAIR Plan (California's "insurer of last resort") or a policy in the surplus lines market.

The combination of this process of *selective* non-renewal (see data from the FAIR Plan, below, that shows that California is not witnessing a wholesale withdrawal from the market) and premium increases has created significant stress among homeowners in high-risk areas. Some of this stress is likely temporary as some insurers reduce their exposure while other insurers take up policies in these high risk areas, with the FAIR Plan and surplus lines providing coverage for the remainder. Absent another event that significantly increases the projected risks in these high risk areas, the results of this market adjustment, once complete, are likely to remain stable for some time. However, it is reasonable to expect continued increases in premiums in high-risk areas so long as we continue to see major loss wildfire events associated with the "new normal."

Homeowners Insurance Basics

A typical homeowner's policy will protect against a variety of property and casualty losses, with each type of loss typically having a separate coverage limit. Dwelling coverage (referred to as "Coverage A") pays for damage to or destruction of the dwelling itself. Damage to or destruction of other structures on the property, such as fences and freestanding garages (referred to as "Coverage B"), is considered separately from the dwelling loss. Damage or destruction to personal property such as furniture, clothes, appliances, and electronics (referred to as "Coverage C") is also separated out from dwelling coverage. Standard policies also cover additional living expenses (referred to as "ALE"), such as temporary housing, while a home is replaced or repaired. A homeowners' insurance policy also typically covers losses due to theft or vandalism, as well as providing liability protection in the event the homeowner is sued as a result of an event associated with the property. Some risks, such as earthquake and flood, are not covered by a standard homeowner's policy (separate coverages are available for those risks). To the extent that a policyholder has not selected coverage limits sufficient to rebuild or repair the home, the homeowner is responsible for the remaining expense.

There are a few basic types of homeowner's insurance policies available in the market:

- **Actual Cash Value** – This type of policy provides for the cost to repair or replace the home (less depreciation) and caps the coverage based on the estimated normal cost of rebuilding.
- **Replacement Cost** – This type of policy provides for the cost to repair or replace the home (without depreciation) and caps the coverage provided based on the estimated normal cost of replacement.
- **Extended Replacement Cost** – Like the replacement cost policy, this type of policy provides for the cost to repair or replace the home (without depreciation) up to the estimated replacement cost, but provides additional coverage should the cost of replacement exceed the dwelling limit. This additional coverage typically increases the dwelling coverage limit by 25% - 50%.
- **Guaranteed Replacement Cost** – This type of policy does not have a limit on the dwelling coverage (although premium is charged based on the estimated normal replacement cost). Very few insurers sell this type of policy, as the open-ended expense

due to "demand surge"[1] in the aftermath of a major catastrophe is highly volatile and unpredictable.
- **Stated Value** – This type of policy provides coverage for a predetermined amount in the event of a loss. Stated value policies are commonly used to cover mobilehomes.

Most policies require a deductible, which is an amount the insured is responsible for before coverage applies. Limits, deductibles, and exclusions are ways to define both the scope of coverage provided by the policy and the risk borne by the homeowner (sometimes referred to as "risk retention" or "self-insurance"). Risk retention provisions are included to eliminate/reduce small value claims for losses easily borne by the homeowner, and to provide a financial incentive to the homeowner to take responsibility for protecting the property. The less risk transferred to the insurer (higher deductibles and lower limits), the lower the premium charged for the policy. However, lower premium (and the associated reduced coverage) increases what the homeowner may have to pay out-of-pocket.

Usually, Coverage A establishes the baseline for calculating other limits. The chart below describes the various coverages and common limits for those coverages.

Coverage	Description	Common Limit
A. Dwelling	Pays for damages to the house and attached structures.	Consumer selects
B. Other Structures	Pays for damages to fences, tool sheds, freestanding garages, etc.	10% of Coverage A
C. Personal Property	Reimbursement for the value of lost possessions such as furniture, clothing, appliances, and other personal property items.	50% of Coverage A
D. Additional Living Expense (ALE)	Reimbursement for living expenses while the home is repaired or rebuilt, and therefore uninhabitable.	20% of Coverage A
E. Personal Liability	Pays for financial losses arising from some forms of legal liability.	Consumer selects
F. Medical Payments	Pays for medical expenses for people injured on the property.	Consumer Selects

Policies may also provide code upgrade coverage (typically with an additional premium charged) to pay for costs of rebuilding based on updated building codes that have been adopted since the home was originally built. One expert notes that code upgrades for a home built before the early 2000s can drive up construction costs by as much as 20%.

Some insurers offer to increase the limit annually based on inflation and/or the increased cost of rebuilding. The premium charged will reflect the increased coverage. These mechanisms are

[1] "Demand surge" is the polite term that many observers would replace with "price gouging."

designed to prevent the value of the Coverage A limit from eroding over time, but these increases may not suffice when the cost of rebuilding increases dramatically after a catastrophe.

The FAIR Plan Structure and Purpose

The California FAIR Plan – "Fair Access to Insurance Requirements" – is an "association" of all admitted (licensed) insurance companies that sell property insurance in California. It was created by statute[2] in the 1960's, following urban disturbances, notably the Watts Riots in Los Angeles. Similar associations were created in other states for the same reasons. The purpose of the FAIR Plan was to ensure that urban property owners, mostly businesses, would have "access" ("fair access") to the property insurance necessary to continue to operate in a market that insurers viewed as too risky to cover. That risk evaluation resulted in a substantial market withdrawal by insurers from the urban property market. Despite its initial creation as an urban/business "insurer of last resort," the FAIR Plan expanded to provide coverage in "designated" brush fire regions of the state. It operated fairly well in this manner until the mid-1990's, when, as a consequence of the genuine homeowners' insurance crisis that followed the Northridge earthquake in 1994, the entire state was designated as the appropriate FAIR Plan coverage region.

The enabling statute provides, in part, that the purpose of the FAIR Plan is to "provide for the equitable distribution among admitted insurers of the responsibility for insuring qualified property for which *basic* property insurance *cannot be obtained* through the normal insurance market." (Emphasis added.)

In a broad sense, the purpose of the FAIR Plan is to be the insurer of last resort for "basic" property insurance in the event of a market failure. At inception, that was essentially urban commercial property. Ultimately, it has expanded to include homeowners' insurance anywhere in the state, provided that the insurance "cannot be obtained" in the normal manner in the market.

There appears to be some sentiment in the market that a FAIR Plan policy is not "real" insurance or is, in some way, inferior to private market insurance. While it is true that, by statute, the FAIR Plan policy is not as broad as traditional homeowners' policies, it is nonetheless a fully sound and guaranteed policy that satisfies lenders' security requirements and protects the property against the primary risk factor faced by homeowners in the Wildland Urban Interface (WUI) – fire. Other coverages are readily available in the market (typically through the purchase of a "difference-in-conditions" or "DIC" policy), which provides wraparound coverage that, coupled with a FAIR Plan policy, results in the same protection provided by a standard homeowner's policy. Because the FAIR plan's role is to provide coverage when the regular market won't, it is not the role of the FAIR Plan to provide DIC policies when there is a healthy market for those policies.

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[2] Technically, the statute does not "create" the FAIR Plan. Rather, it directs the insurers to establish, subject to approval by the Insurance Commissioner of a plan of operations, the Plan which is governed by a "governing committee" comprised of representatives of members insurers.

Market Withdrawal – Insurance After the Northridge Earthquake

The current role of the FAIR Plan is largely a result of the aftermath to the 1994 Northridge earthquake. A brief review of California's experience in the mid-1990's in comparison with today's current market conditions is helpful in evaluating the extent of the current problems and the efficacy of *existing* solutions.

Just as the past 3 or 4 years of wildfire losses has shaken the insurance industry's confidence in its prior assessment of the scale of wildfire risk, the Northridge earthquake generated a comparable re-evaluation with respect to earthquake risk in California. The market response was predictable. As long as state law mandated insurers to write earthquake insurance for any homeowners' insurance policyholder who chose to buy it, insurers would simply not write new homeowners' policies.

In the absence of a statewide coverage area for the FAIR Plan, the homeowners' insurance market for new policies virtually collapsed, and there was a serious and immediate risk of widespread non-renewals of existing policies. Escrows on home sales were failing for lack of available insurance (not merely insurance that prospective buyers found to be more expensive than had historically been the case). There was a complete lack of availability of homeowners' insurance to be purchased at any price.

The administrative/legislative response was essentially two-fold. Administratively, the FAIR Plan was expanded to statewide, thereby ensuring access to essential coverage so that the state's real estate market would not collapse. Legislatively, the California Earthquake Authority (CEA) was established to address earthquake insurance in a manner that would enable a recovery of the basic homeowners' insurance market. Both of these efforts succeeded. [3]

There are several lessons to be drawn from the 1990's crisis:

1) The extent of the crisis was widespread, affecting all regions of the state, and severe in the sense of direct threats to an otherwise healthy statewide real estate market. We have not seen the current wildfire-driven market dislocations expand to the magnitude of the 1990's crisis.

2) It is very difficult to mandate that insurers write policies that their risk analysis shows to be unmanageable. This remains true either because the aggregate risk posed is too great or because existing rate structures do not permit insurers to charge adequate premium based on the risk created by issuing the policies.

3) There was credible evidence that insurers were delaying a more drastic market withdrawal across the state, absent administrative/legislative action to address the crisis.

[3] It bears mentioning that for the portion of the market that did not join the CEA, earthquake insurance rates increased shortly after the Northridge quake in excess of 50% across the state – and higher in high risk regions. Part of the 1990's "new normal" with respect to earthquake insurance was significantly higher costs for consumers.

4) The primary administrative tool (expansion of the FAIR Plan statewide) both served its immediate purpose, and in the years since, has not been tested in any sort of market crisis.

The challenges in the current insurance market caused by wildfire, and the FAIR Plan's effectiveness in answering these challenges, is discussed in more detail below.

Insurance pricing in the WUI (and elsewhere)

Recent media reports have described homeowners in the WUI facing insurance rate increases of double and triple what they have historically been paying. There have also been reports of homeowners being "unable" to obtain insurance, and of home sales that have failed because the prospective buyer could not afford the quoted premium to insure the home. Each of these "reports" deserves thoughtful consideration in light of market reality which is substantially driven California's rate regulation system and the premium structures it creates.

There is a difference between insurance "rates" and the "premium" a particular homeowner pays to their insurer. In insurance regulatory parlance, "rate" means the average price to be paid by customers that will generate an adequate amount of money required to cover the insurer's anticipated expenses and make a reasonable rate of return.[4] The "premium" that any particular homeowner pays is the result of the approved "rating plan" or "class plan" that uses a series of positive and negative factors to determine that actual price paid. This class plan spreads the cost required to cover insurer's losses, expenses, and return (all defined by DOI regulations) among the insurer's policyholders based on a set of factors also approved by DOI. Allocating premium within these rules is essentially a zero-sum game where a factor that reduces the premium charged in one area must be offset by a factor that increases the premium charged in another area. When those factors result in an insurer charging premium inadequate to pay the losses associated with a category of homes, that gap must be filled by higher premiums charged for categories of homes with lower losses.

As an example, the FAIR Plan recently was granted (after filing a lawsuit against the DOI) a 20% rate increase and a new rating plan to reflect changes in the risk exposure presented by homes in the WUI. That 20% increase translates into premium reductions of as much as 20% for policyholders in low risk areas and premium increases of 50-60% for policyholders in high risk areas. This new rating plan authorized for the FAIR Plan is in recognition of the fact that homeowners in the WUI have historically been significantly *subsidized* by homeowners in low-risk regions of the state, who have paid higher premiums so that WUI premiums could be lower.

Pooling risks through insurance mechanisms creates the possibility, in fact a likelihood of, creating subsidies. In its most basic operation, insurance literally "subsidizes" those with losses with the premiums paid by those without losses. That is not the sense in which the term is used here. Rather, it is used in a broader sense. Determining how risk will be priced and how groups

[4] Pursuant to Proposition 103, and the current regulations adopted by the Department of Insurance, an admitted insurer cannot charge a rate before it has been approved by the Insurance Commissioner, and that rate is set at the constitutionally minimum that can be imposed without resulting in a "taking" that would violate the United States constitution's "Takings Clause".

of insureds will be assembled to share that risk will create some financial incentives and disincentives. Financial incentives and disincentives are not determinative of individual behavior, but they do influence behavior that is not limited only to the insurance market. Thoughtful consideration of how the incentives/disincentives are created by the rules imposed for pricing risk (rating) and for assembling insureds (underwriting) create subsidies and those subsidies can either support or undermine the insurance market, as well as broad public policy goals. To the extent that subsidies are created on purpose, to serve identified public policy goals, those decisions ought to be made by policymakers with eyes wide open to the facts and consequences of the decision to create the subsidy.

In the private admitted market, this subsidy factor is even more pronounced than it has been with respect to the FAIR Plan, and as a result, homeowners in the WUI are not merely experiencing a "new normal" but also losing a long-term discounted price that was far below the actual cost of providing insurance in the WUI. This point needs to be clearly understood, *the premiums historically paid by homeowners in the WUI have already been substantially subsidized by low-risk policyholders*. Actions to reduce this subsidy will cause WUI premiums to rise independent of any consideration of the "new normal" and the billions of dollars in recent losses. Each of these factors will inflate property insurance cost in the coming years for all homeowners, but the increases born by homeowners in lower risk areas would be reduced to the degree that the current subsidy to the WUI is reduced.

Insurers point to two current regulations adopted by the Department of Insurance, that Commissioner Lara has the authority to change, as contributing to the underpricing of policies in WUI.[5] First, and most surprising, the rate regulation system *precludes* counting actual and proven reinsurance expenses as legitimate costs that can be built into the rate base.[6] It is widely accepted that insurers need to buy reinsurance to guard against catastrophic losses that may exceed expected losses. This is, now, especially true with respect to policies that cover homes in the WUI, and reinsurance prices have been rising in the face of substantial losses reinsurers have experienced in recent years. Thus insurers are bearing increasing reinsurance costs without being able to recover those costs through premium. Insurers argue that the current rate regulation system inherently underprices premiums in high risk areas. Second, the rate regulation rules *prohibit* the use of even the most sophisticated forward-looking risk modelling tools.[7] Rather, the rules require a retrospective look at historical losses. Insurers argue that if, in fact, we are facing a "new normal" with wildfires, limiting rate regulation analysis to historical losses inherently underestimates the risk, and results in underpricing. It is an unpopular and uncomfortable truth that price and availability go hand in hand. If insurers are facing underpriced premiums in high risk areas, their willingness to issue or renew policies in these areas will be low or non-existent.

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[5] The Legislature does not have the authority to direct the Insurance Commissioner to make these two changes, as the rate regulation system adopted by initiative statute specifically delegates that role to the commissioner.
[6] See California Code of Regulations, Title 10, Section 2644.25.
[7] See California Code of Regulations, Title 10, Section 2644.4, subdivision (e).

In addition to potential pricing concerns, large market share companies are also reconsidering the mix of risks presented by their current policyholders. The losses in recent years and the reality that this likely represents a "new normal" does require most insurers (particularly those with a large piece of the market) to reconsider if their policyholders are over-concentrated in high risk areas. Concentration of risk is an essential consideration when selling homeowner's insurance. The insurance community was reminded of this last year when a small insurer (Merced Casualty Insurance Company) became insolvent following the Camp fire. While large California insurers are backed by immense financial resources, it would be foolish for any company not to re-evaluate its current risks through the lens of the "new normal."

While the homeowner's insurance market is generally quite competitive (dozens of insurers offer homeowner's policies in California), there is commonly a wide variation in the premium charged by different insurers for the same home. That variation has a number of causes. As noted above, rates are primarily based on the losses that the insurer is likely to bear among the homes it insures. If the insurer has a riskier group of homes, its rates will be higher. Each insurer also develops its own class plan based in part on the mix of homes it insures. Lastly, while homeowner's insurance is a fairly standard product, policy design choices made by individual insurers do have a cost impact. Some insurers offer more generous coverage for contents or ALE than others and that generosity comes at a cost.

One consequence of California's rate regulation system is that many of the large market share insurers tend to have lower prices than small market share companies simply because few small market share companies' rate applications are challenged by interveners. Interveners exert pressure to reduce requested increases (or even turn requested increases into rate reduction orders) from large market share companies. Since many of the non-renewals in the WUI are from larger market-share insurers, when homeowners in the WUI find coverage from another admitted company they are likely get that coverage from a smaller market share company with higher rates.[8]

California Insurance Cost

As a general matter, Californians have had very low premiums for homeowner's insurance. A recent comparison of costs conducted by Insurance.com found that the average premium in California for a $200,000 replacement cost policy was 37th among the 50 states. The national average premium for that policy was $1288 and the average cost in California was $793 (35% lower than the national average.) For comparison purposes, the highest cost state was Florida with the same coverage costing $3575. West Virginia was the mid-point with $1288 and Hawaii was the lowest at $337.

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[8] It may also be possible that homeowners are experiencing the effect of getting new rebuild estimates. There has been heightened scrutiny on the rebuilding estimates that are used to establish the Coverage A limit in a homeowner's policy. As most homeowners do not shop for insurance very often, many may not have adjusted their Coverage A limits for years or decades and their new policy may reflect a higher Coverage A limit and the price that comes with it.

While the sample limits used to generate those figures are certainly well below typical values in California, the study does highlight that California has been a low cost state for homeowner's insurance. We should expect that premium cost will increase across the state in response to the massive losses experienced in recent years, and the recognition of the "new normal" associated with Climate Change. However, California homeowners will continue to enjoy lower rates than many states despite these expected rate increases.

FAIR Plan Market Activity

The FAIR Plan recently provided the Committee with data regarding its issuance of new policies throughout the state in the past 12 months (June 2018 – June 2019). The Committee sought this data as an indicator of conditions in the homeowner's insurance market. We would expect to see increases in new FAIR Plan policies in areas where insurers are issuing non-renewal notices in substantial numbers.

There is not a one-to-one correspondence between newly issued FAIR Plan policies and non-renewals because homeowners[9] are required to conduct a diligent search of the private market for new coverage before resorting to the FAIR Plan. After receiving a non-renewal notice, some homeowners will find coverage from the private market in the course of that diligent search -- information provided by the FAIR Plan supports the inference that coverage from the regular market is available in many areas. However, where there are significant increases in FAIR Plan policy counts, it is a sound assumption that there has been an increase in the number of non-renewal notices sent to homeowners.

The data show that there has been significant increases in the number of new policies issued by the FAIR Plan in a number of counties in the Sierra foothills, indicating a substantial increase in non-renewal activity in those communities. New policy issuance in the most affected counties accelerated strongly beginning in December 2018, and that pattern continued in the ensuing months. Counties that have seen the greatest increases include Amador, Calaveras, El Dorado, Mariposa, Nevada, Trinity and Tuolumne, while counties such as Butte, Lake, Lassen, Mendocino, Mono, Placer, Plumas, San Bernardino, Shasta, and Sierra have seen smaller, but still significant, increases. In the most affected counties, there has been as much as a ten-fold increase in the number of policies issued on a monthly basis. Individual communities within these counties have seen even more dramatic increases in the proportion of homeowners obtaining coverage from the FAIR Plan.

It is also notable that counties substantially (or entirely) outside of high-risk fire areas did not see meaningful increases in new FAIR plan policies. This data indicates that insurers are largely limiting non-renewal activity to high-risk fire areas, and insurers are not broadly withdrawing from the homeowner's insurance market. The FAIR Plan reports issuing over 43,000 new policies in the past 12 months. To put that number in perspective, the Department of Finance estimates that there are over 8 million single-family/detached homes in California which means

[9] Or, more specifically, the homeowner's insurance agent or broker.

that the overwhelming majority of homeowners in California have access to insurance in the regular market.

Clearly some communities (primarily in the Sierra foothills) are experiencing a major market adjustment. However, that adjustment is likely a one-time phenomenon as homeowner's policies are generally renewed on an annual basis, and insurers are likely to reduce their risk exposure over one or two renewal cycles. The FAIR Plan has also experienced a notable volume of new policyholders cancelling their policies within months of issuance (17% of policies issued in October 2018 have been cancelled by the policyholder). Because insurance is not optional for a homeowner with a mortgage, these policyholders have found other coverage that is most likely in the regular insurance market. Some of this activity likely reflects that these homeowners are becoming more sophisticated consumers. The majority of homeowner's policies in California are issued by a relatively small number of insurers that work through "captive" agents (who are essentially limited to selling coverage from a single company) which means that most homeowners have not experienced interacting with an independent insurance agent. When these large market share companies issue a non-renewal notice, homeowners are most likely to find coverage with a smaller market share company, and those companies generally work through independent agents who sell policies from many insurers.

Increasing Fire Risk and the Insurance Market

A recent study sponsored by the California Natural Resources Agency and published by the RAND Corporation compared the insurance market in certain areas of the Sierra Foothills and San Bernardino County. The study also looked at the potential impact of climate change on that market based on recent trends. Although the study only looked at two areas in California, the findings are useful for all Californians who live in or near similar forested areas. That study made several findings pertinent to any conversation on high-risk areas and the insurance market.[10] The study found that:

- The average acres burned annually in the Sierra Foothills will double by midcentury and likely double again by the end of the 21st century.
- Homeowners in high-risk areas purchase less coverage relative to structure value, meaning that these homeowners, facing increased expenses, appear to have chosen to be underinsured.
- Climate change could substantially affect the insurance market in some parts of the Sierra Foothills. In some of the highest fire risk, by 2055 the rate per $1,000 of coverage in the admitted market is projected to rise by 18%, the insurance-to-value ratio is expected to drop by 6.5% (homeowners will be even more underinsured), and deductibles will increase by $121.

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[10] Lloyd Dixon, Flavia Tsang, and Gary Fitts, *The Impact of Changing Wildfire Risk on California's Residential Insurance Market*, RAND Corporation and GreenwareTech (Aug. 2018), p. 47, available at https://www.rand.org/content/dam/rand/pubs/external_publications/EP60000/EP67670/RAND_EP67670.pdf.

The study also discusses the recent catastrophic loss on insurers underwriting profits. Underwriting profit represents that portion of the premium that is set aside to pay claims but is not used for that purpose. What is not used one year, may be reserved and used in future years. The authors examined the underwriting profits in the homeowners multiple peril line (policies that cover a variety of damage types) and noted that they were highly negative in 2017. Many insurers lost money, and a good portion of those losses were due to wildfire. Those losses were paid for by profits from prior years. The study notes:

> The underwriting experience between 2001 and 2017 illustrates that an extended period of underwriting profits can be wiped out by a very large wildfire or other catastrophic event (a fire following an earthquake, for example). Underwriting profits in the Homeowners Multiple Peril and Fire lines totaled $12.1 billion from 2001 through 2016 combined, and were almost completely wiped out by the results for 2017. Insurers may not believe that the return is adequate to justify the risk, even once investment returns are included. [11]

Recent Legislative Actions

There appears to be some sentiment that the Legislature must "do something" despite the fact that existing law mechanisms are in fact performing as planned in the face of the current market response to wildfires. It bears recalling that last Session, the Legislature passed and the Governor signed a broad scope of insurance market reforms specifically targeted at addressing a number of problems that the recent wildfires highlighted. Many of these 2018 bills included a delayed effective date to allow either the Department of Insurance or the insurers' time to implement the changes in law. Thus, a number of the 2018 reforms are just now, or in the immediate future, being implemented. Further Legislative action prior to an evaluation of the efficacy of the 2018 reforms may be premature. These insurance bills include:

SB 30 (Lara), Chapter 614, Statutes of 2018, requires the Insurance Commissioner to convene a working group to assess new and innovative investments in natural infrastructure and insurance products in light of California's worsening fire vulnerability due to climate change.

SB 824 (Lara), Chapter 616, Statutes of 2018, prohibits an insurer from canceling or refusing to renew a homeowners' insurance policy for one year from the date of a declaration of a state of emergency, as specified; and requires admitted insurers with at least $10 million in written premiums in California to biennially report to the California Department of Insurance specified fire risk information on residential property policies.

SB 894 (Dodd), Chapter 618, Statutes of 2018, requires insurers to renew a residential insurance policy for at least two renewal periods (24 months); requires an insurer to grant an additional 12-month extension for a total of 36 months for additional living expense if an insured acting in good faith encounters a delay in the reconstruction process, subject to policy limits; allows an insured to combine payments for actual losses up to the policy limits for the primary dwelling and other structures, limited to the amount necessary to rebuild or replace the home if the policy

[11] *Id.* at 55.

limits for the dwelling are insufficient; and specifies that the payments for losses under this provision shall be full replacement value without requiring the replacement of the other structures.

SB 917 (Jackson), Chapter 620, Statutes of 2018, provides that if loss or damage results from a combination of perils, one of which is a landslide, mudslide, mudflow, or debris flow, an insurer shall provide coverage if an insured peril is the efficient proximate cause of the loss or damage and coverage would otherwise be provided for the insured peril; provides that this is declaratory of existing law.

AB 1772 (Aguiar-Curry), Chapter 627, Statutes of 2018, extends the minimum time limit for an insured to collect the full replacement cost of a loss related to a state of emergency to 36 months; requires an insurer to provide additional extensions of 6 months if the insured, acting in good faith and with due diligence, encounters a delay or delays in approvals or reconstruction of the home; and requires all policy forms issued or renewed by an insurer to be in compliance with these changes on or after July 1, 2019.

AB 1797 (Levine), Chapter 205, Statutes of 2018, requires an insurer that provides replacement cost residential property insurance to provide to the policyholder, every other year at the time of the offer to renew the policy, an estimate of the cost necessary to rebuild or replace the insured structure, with certain exceptions as specified; and takes effect on July 1, 2019.

AB 1799 (Levine), Chapter 69, Statutes of 2018, requires the complete copy of a residential insurance policy provided to an insured after a loss to include the full insurance policy, any endorsements to the policy, and the policy declarations page; and provides that if the request for a copy of the policy is a result of a loss in a state of emergency, the insurer may, upon the request of the insured, provide an electronic copy of the entire policy, as specified.

AB 1800 (Levine), Chapter 628, Statutes of 2018, prohibits, in the event of a total loss, a residential property insurance policy from containing a provision that limits or denies payment of building code upgrade cost or replacement cost, including extended replacement cost, to the extent those costs are otherwise covered under the policy, based on the fact the insured has chosen to rebuild or purchase a home at a new location.

AB 1875 (Wood), Chapter 629, Statutes of 2019, establishes the California Home Insurance Finder that will connect consumers who need residential property insurance with agents and brokers to help ensure they obtain plans and coverage that suit their specific needs and requires insurers to annually report the amount of extended replacement cost coverage to the Department of Insurance as specified.

AB 2229 (Wood), Chapter 75, Statutes of 2018, requires a residential property insurer to disclose any fire safety discounts it offers upon offer or renewal of a homeowner's insurance policy on or after January 1, 2020.

AB 2594 (Friedman), Chapter 639, Statutes of 2018, revises the standard form fire insurance policy to extend the statute of limitations to bring suit to 24 months after the inception of the loss if the loss is related to a state of emergency, as defined.

Concluding Thoughts

There is no "right" answer to the problem of how to provide homeowners with financial protection from catastrophic wildfire losses. Wildfires wreak tremendous personal and financial havoc on many Californians. The grim truth is that these losses will occur and the losses will be spread in varying amounts to insurers, government, homeowners generally, or individual homeowners who suffered losses. Much of that spreading will be driven by decisions we collectively arrive at regarding how insurance is priced (rate regulation) and what rules insurers must follow when deciding to offer coverage (underwriting). There is a virtually infinite number of combinations of rate making and underwriting rules, and each combination will spread these costs (both previous and future costs) differently.

To the degree we adopt policies to subsidize homeowners in high risk areas through insurance, that subsidy will be paid for by homeowners outside the high risk areas. This subsidy for homeowners in the WUI will act as any other subsidy will by tilting (ever so slightly) the economics in favor of those living in the WUI. The question of whether that subsidy is desirable and, if so, whether providing that subsidy through the mechanism of insurance is most likely to be effective, are both questions that should considered when making policy in this area.

Finding the balance between individual responsibility (i.e., paying higher premiums and buying more insurance in high risk areas) and collective protection (i.e., spreading costs and raising premiums in low fire risk areas) is an inherently subjective endeavor. Any balance found is likely to clash with other difficult and important public policy issues, such as the availability and affordability of housing, planning and land use policy, protection of property rights, environmental protection, and climate change. Legislating in an area so interconnected greatly increases the likelihood of any policy change to generate unintended consequences – for example, retaining or increasing subsidies for homeowners in high risk areas of the state will encourage continued development in places many environmentalists argue are not appropriate for this sort of development.

Policies that shift these losses, and the cost of bearing the risk of future losses, would create incentives that sometimes support and sometimes impinge on policies being pursued to address these other issues. For example, spreading the losses widely across homeowner's insurance policies and suppressing the cost of insurance in high fire-risk areas will reduce the cost of homeownership in those high risk areas, but increase it in low risk areas. While insurance is a relatively small portion of the total cost of owning a home, for those on the margins[12] an added insurance cost may be the difference between affording a home or not. Assessing how strong an incentive this might present and how it interacts with other policies being pursued regarding further development in the WUI, and the absolute need to build more housing units is a complex

[12] Recent media reports have identified anecdotally home purchase transactions that have "failed" due to unexpected insurance costs. For those prospective purchasers who have "maxed out" their borrowing ratios on the premise of historical insurance costs, some may discover that they no longer qualify for a loan at the desired purchase price. However, most buyers will face a personal choice – do I "want" to buy in the WUI in light of the reality of current cost structures.

and nuanced task. By the same token, pursuing a policy that focuses insurance costs more strongly in high fire risk areas creates the opposite incentives with no less complex and nuanced implications. Any significant policy proposal in this area is based (implicitly or explicitly) on a series of value judgments regarding the relative priority of competing policy priorities and conceptions of fairness. It must also contend with the structural limitations imposed on the Legislature by Proposition 103, which effectively precludes passing bills governing rate setting for property/casualty insurance. There is great risk that legislating extensive new rules for underwriting alone (without compensating changes in rate making) would significantly disrupt a homeowners' insurance market that is effectively serving the great majority of California homeowners.

As noted above, it is an unpopular and uncomfortable truth that property insurance costs in California are going to rise, and this is especially true in the WUI. It follows that as the impact of this reality moves through the market, there will be disruptions and discomfort. However, until the volatility of the current market has had an opportunity to settle, it would be perilous to propose major "reforms" to a market where it is yet unclear where and to what extent it may be failing.

SECTION TWO

The California FAIR Plan and Property Insurance Availability

Anneliese Jivan
President
California FAIR Plan

August 21, 2019

CA FAIR Plan was created by statute in 1968 to:

(1) assure **stability** in the property insurance market

(2) assure the **availability** of **basic property insurance** as defined in the Plan

(3) **encourage the maximum use**, in obtaining basic property insurance, **of the normal insurance market**

(4) ...insuring qualified property for which basic property insurance **cannot be obtained** through the **normal insurance market**

The FAIR Plan is not a state agency

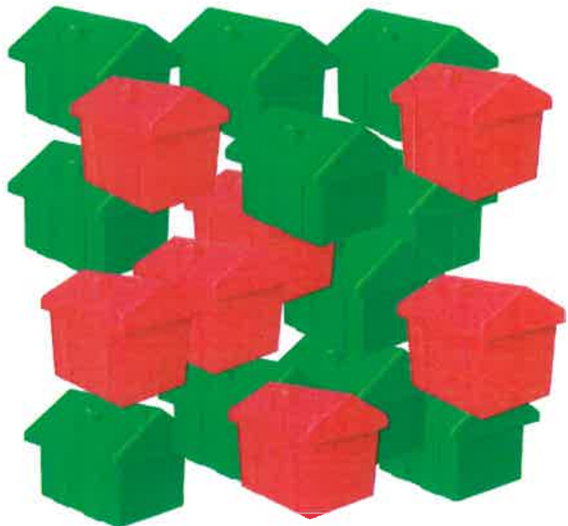
- **Private Association** comprised of all insurers licensed to write property insurance in California
- FAIR Plan has the **ability to assess the insurers** if funds are needed, and this is done on a market share basis adjusted for write-out credits
- There is no public funding, or taxpayer monies involved
- Small organization of less than 60 employees specializing in fire coverage and claims

Where does FAIR Plan write?

- **Any location** in California subject to limited underwriting guidelines including:
  - Home must be in insurable condition
  - Home cannot be vacant for more than a year
  - No illegal activities can take place at property
- The FAIR Plan will insure a property **regardless of its exposure to brush/wildfire**

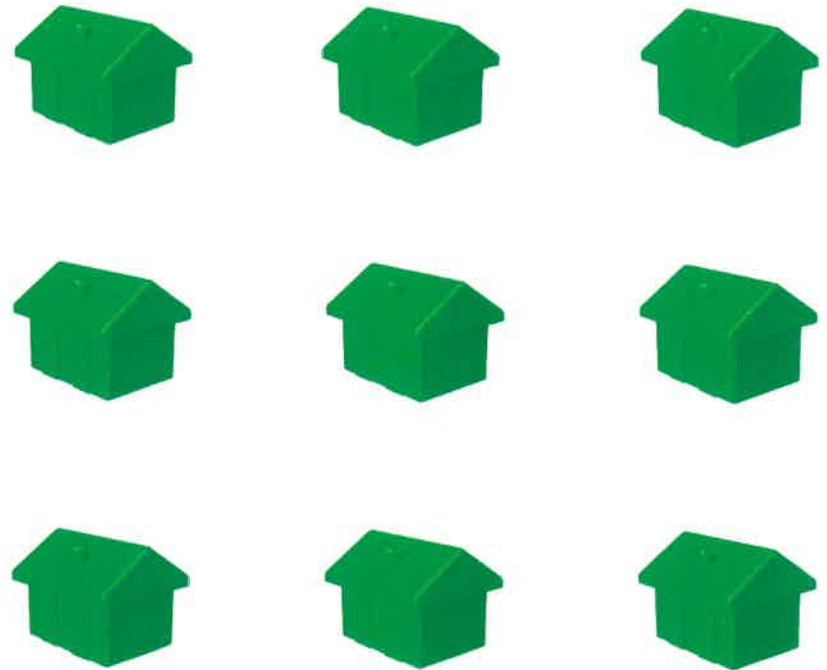
Where does FAIR Plan write?

All properties, including high-risk properties, regardless of concentrations



VS

Managed concentration and lower risk properties = Fewer losses



FAIR Plan stats

- **61%** of FAIR Plan Dwelling policies are Urban policies

- FAIR Plan insures **2.7%** of housing units in CA in the High and Extreme wildfire risk category

- FAIR Plan has grown **22,101** Dwelling policies in the last 12 months

- **18%** of the policies written in November were no longer with the FAIR Plan by July

What the FAIR Plan writes

What the normal insurance market will not

FAIR Plan
Dwelling Policy

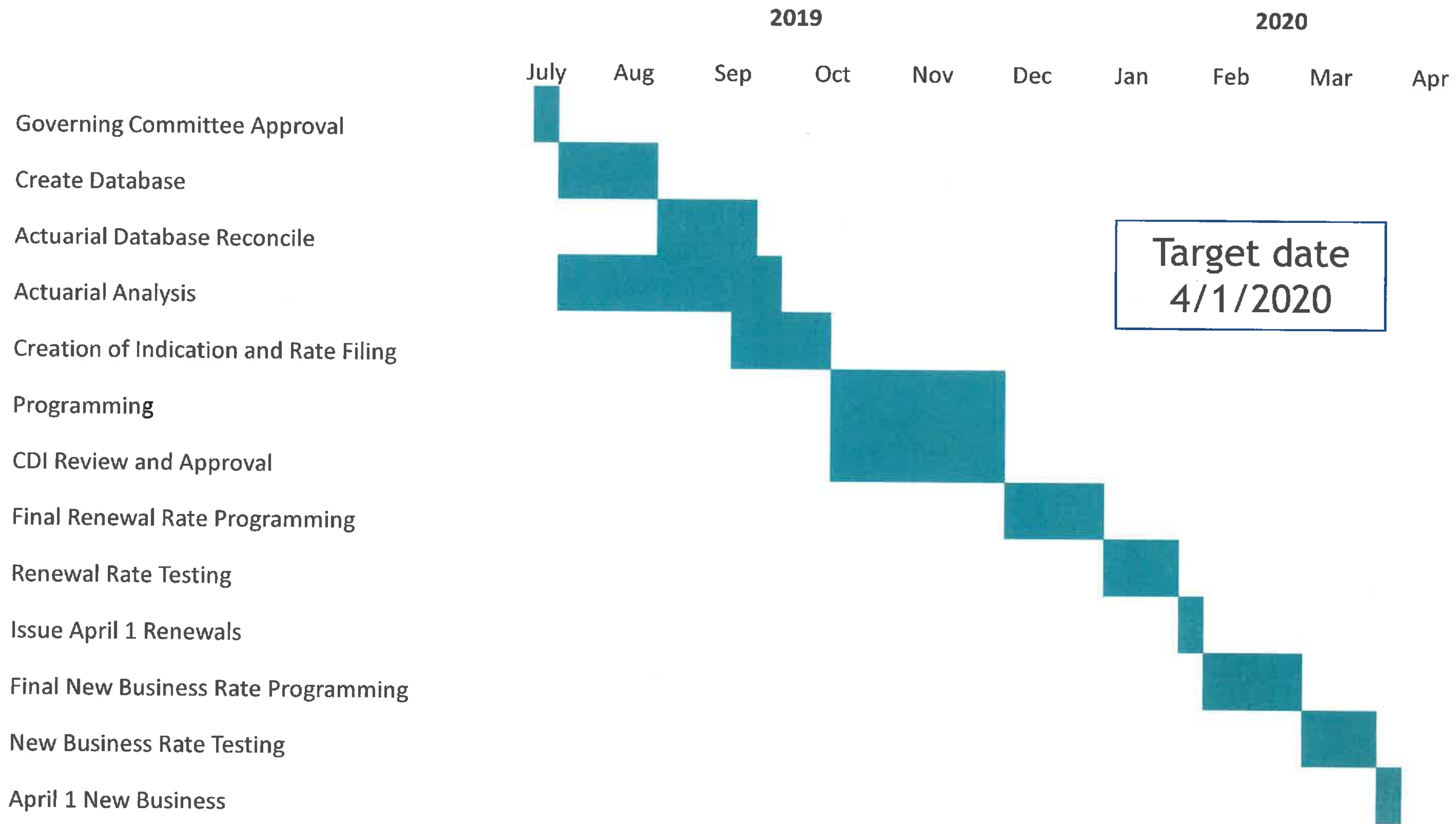
- Brush/wildfire exposed
- Older homes
- No fire protection
- Knob and tube wiring

What the Normal Insurance Market writes

Difference in Condition (DIC) Policy

Combined with a FAIR Plan policy = **Homeowners Policy**

Dwelling limit increase from $1.5M to $3M Timeline



Testimony of Cliston Brown

Vice President, Communications and Government Relations
Surplus Line Association of California

Presented to the California State Assembly Committee on Insurance

Sacramento, California
August 21, 2019

Good morning. My name is Cliston Brown, and I am the vice president for communications and government relations with the Surplus Line Association of California.

I would like to thank the chair, Assembly Member Daly; the vice chair, Assembly Member Mayes; and the members of the committee for this opportunity to brief you today regarding the state of the homeowners' insurance market and the surplus lines industry's role in that market.

First, I would like to provide some brief background on who we are and what we do. The Surplus Line Association was created in 1937, and it was appointed in 1994 as the California Department of Insurance's surplus lines advisory organization. In this role, we review every surplus lines policy filed in the state of California to ensure compliance with all pertinent laws and regulations. Our 5,500 licensed brokers placed 687,743 policies with a total premium of $7.6 billion in 2018.

It is important to note up front that state law requires our members to perform a diligent search for an admitted carrier that will cover a risk before placing that policy in the surplus lines market. *[California Insurance Code Section 1763 (a)].* The code considers three declinations from admitted carriers to be prima facie evidence that a diligent search has taken place. *[California Insurance Code Section 1763 (b)].* In some instances, admitted insurers will make a business decision not to cover a particular risk or class of risks. These are usually in cases of distressed, new, complex, or high-capacity risks.

In the homeowners' market, there are many reasons why an admitted carrier may reduce its insured concentration. For instance, it might find that it is too concentrated in a particular area, or the risk profile might have changed due to forces beyond its control, such as climate change or government action. In these cases, consumers need options, or they will be left without the insurance coverage they need. They can either go to the FAIR plan or seek coverage in the surplus lines market, or both.

The overwhelming majority of risks that go into the surplus lines market are commercial risks. Very little personal lines business goes into the surplus lines market. In the last five calendar years, homeowners' insurance has consistently accounted for between 1.4% and 1.8% of all surplus lines premiums collected in California. However, we have seen increases in recent years in the total premium and number of policies in the surplus lines homeowners market as admitted carriers have pulled back in certain areas.

- Surplus lines homeowners premiums increased from more than $110 million in 2017 to more than $122 million in 2018.
- Surplus lines homeowners policies increased from 44,986 in 2017 to 49,281 in 2018.

- Comparing the first six months of this year to the first six months of 2018, surplus lines homeowners premiums have increased from over $51 million in first half 2018 to almost $111 million in first half 2019.
- Comparing the first six months of this year to the first six months of 2018, the surplus lines homeowners market grew from 22,564 policies in first half 2018 to 39,210 policies in first half 2019.

However, even with these increases, homeowners' insurance still accounts for less than 2.5% of the entire surplus lines marketplace in California. And based on the most recent figures available on the California Department of Insurance's website, only about 1.7% of the entire homeowners' insurance market in the state went into surplus lines in 2017, though it is probable, based on the growth we have seen, that this percentage has surpassed 2% in the last 19 months.

Although we do not have data on the value of homes insured in the surplus lines marketplace, it is our sense that most such homes are high-end homes with owners who need more coverage than the FAIR Plan can provide.

In these cases, the surplus lines industry is filling a role that is no longer being served by the admitted market, which is exactly the role that the State of California has envisioned for our industry. Our purpose is not to supplant the admitted market. Rather, we are here to provide options to consumers who otherwise might not be able to obtain the level of insurance they want during a market dislocation like the one we are seeing now.

In closing, the surplus lines industry plays a vital role in ensuring that California consumers who cannot obtain insurance coverage in the admitted market have options to insure property against potential losses. Our mission is to ensure a responsive and lawful surplus line insurance market exists in California.

At this time, I would be glad to take any questions you may have. Thank you for the opportunity to testify here today about our industry's role in ensuring a healthy, fair and competitive insurance market for California consumers.

SECTION THREE

CALIFORNIA DEPARTMENT OF INSURANCE
Number of New, Renewed, and Non-Renewed Residential Dwelling Policies in Moderate to Very High Fire Risk ZIP Codes Based on CalFire's State Responsibility Area Map

California FAIR Plan

	TOTAL (New + Renewed)				New			Renewed			Non-Renewed (Insured Initiated)				Non-Renewed (Insurer Initiated)			
Calendar Year	Non-State Responsibility Area	State Responsibility Area (SRA[1])	YoY Percent Change in SRA	SRA Percentage to Total	Non-State Responsibility Area	State Responsibility Area (SRA[1])	SRA Percentage to Total	Non-State Responsibility Area	State Responsibility Area (SRA[1])	SRA Percentage to Total	Non-State Responsibility Area	State Responsibility Area (SRA[1])	YoY Percent Change in SRA	SRA Percentage to Total	Non-State Responsibility Area	State Responsibility Area (SRA[1])	YoY Percent Change in SRA	SRA Percentage to Total
2018	90,331	48,891	7.4%	35.1%	9,495	12,353	56.5%	80,836	36,538	31.1%	9,896	7,061	11.7%	41.6%	2,902	2,270	11.7%	43.9%
2017	94,801	45,511	8.1%	32.4%	10,187	11,830	53.7%	84,614	33,681	28.5%	10,444	6,322	10.4%	37.7%	2,942	2,032	-9.1%	40.9%
2016	99,075	42,117	8.0%	29.8%	11,679	10,964	48.4%	87,396	31.153	26.3%	10,785	5,729	19.2%	34.7%	3,229	2,236	1.7%	40.9%
2015	102,376	39,015		27.6%	11,990	10,750	47.3%	90,386	28,265	23.8%	10,489	4,805		31.4%	3,452	2,198		38.9%

Surplus Lines

	TOTAL (New + Renewed)				New			Renewed		
Calendar Year	Non-State Responsibility Area	State Responsibility Area (SRA[1])	YoY Percent Change in SRA	SRA to State Percentage	Non-State Responsibility Area	State Responsibility Area (SRA[1])	SRA to State Percentage	Non-State Responsibility Area	State Responsibility Area (SRA[1])	SRA to State Percentage
2018	4,120	15,636	13.9%	79.1%	1,726	6,502	79.0%	2,394	9,134	79.2%
2017	3,955	13,726	9.3%	77.6%	1,521	5,136	77.2%	2,434	8,590	77.9%
2016	4,047	12,560	19.4%	75.6%	1,620	5,798	78.2%	2,427	6,762	73.6%
2015	3,791	10,521		73.5%	1,590	4,886	75.4%	2,201	5,635	71.9%
2014	11,179	7,895		70.6%	5,114	3,736	73.1%	6,065	4,159	68.6%
2013	9,525	6,373		66.9%	5,284	3,762	71.2%	4,241	2,611	61.6%
2012	6,386	3,951		61.9%	2,885	1,874	65.0%	3,501	2,077	59.3%

Voluntary Market

	TOTAL (New + Renewed)				New			Renewed			Non-Renewed (Insured Initiated)				Non-Renewed (Insurer Initiated)			
Calendar Year	Non-State Responsibility Area	State Responsibility Area (SRA[1])	YoY Percent Change in SRA	SRA Percentage to Total	Non-State Responsibility Area	State Responsibility Area (SRA[1])	SRA Percentage to Total	Non-State Responsibility Area	State Responsibility Area (SRA[1])	SRA Percentage to Total	Non-State Responsibility Area	State Responsibility Area (SRA[1])	YoY Percent Change in SRA	SRA Percentage to Total	Non-State Responsibility Area	State Responsibility Area (SRA[1])	YoY Percent Change in SRA	SRA Percentage to Total
2018	4,240,392	4,302,128	-0.1%	50.4%	470,595	501,214	51.6%	3,769,797	3,800,914	50.2%	356,272	375,388	-1.4%	51.3%	79,383	88,187	5.5%	52.6%
2017	4,240,015	4,305,414	0.4%	50.4%	484,090	502,946	51.0%	3,755,925	3,802,468	50.3%	368,747	380,723	2.8%	50.8%	78,497	83,551	-3.8%	51.6%
2016	4,214,126	4,286,163	1.1%	50.4%	477,244	497,356	51.0%	3,736,882	3,788,807	50.3%	356,935	370,215	2.7%	50.9%	80,552	86,807	-3.1%	51.9%
2015	4,162,906	4,238,488		50.4%	471,578	483,109	50.6%	3,691,328	3,755,379	50.4%	358,165	360,398		50.2%	84,774	89,571		51.4%

DEMOGRAPHICS. Estimate Total Households [2]

Calendar Year	Non-State Responsibility Area	State Responsibility Area (SRA[1])	YoY Percent Change in non-SRA	YoY Percent Change in SRA
2018	7,664,665	5,671,402	0.6%	0.5%
2017	7,621,141	5,642,963	1.8%	1.9%
2016	7,489,086	5,540,200	1.0%	0.4%
2015	7,412,658	5,519,808		

[1] State Responsibility Area (SRA): CalFire created a fire map depicting moderate to very high fire hazard severity zones in California that was adopted on November 7, 2007. We were able to conjoin the fire zones with ZIP codes to identify the ZIP codes affected. However, we have no means to determine to which extent.

[2] A household is composed of one or more people who occupy a housing unit. Keep in mind that these housing units also include apartment complexes which are normally insured under a commercial policy.

CALIFORNIA DEPARTMENT OF INSURANCE

Number of New, Renewed, and Non-Renewed Residential Dwelling Policies

in ZIP Codes Affected by 2015 and 2017 Wildfires

California FAIR Plan

	TOTAL (New + Renewed)				New			Renewed			Non-Renewed (Insured Initiated)				Non-Renewed (Insurer Initiated)			
Calendar Year	State	ZIP Codes Affected by Recent Wildfires (WF[1])	YoY Percent Change in WF	WF to State Percentage	State	ZIP Codes Affected by Recent Wildfires (WF[1])	YoY Percent Change in WF	State	ZIP Codes Affected by Recent Wildfires (WF[1])	YoY Percent Change in WF	State	ZIP Codes Affected by Recent Wildfires (WF[1])	YoY Percent Change in WF	WF to State Percentage	State	ZIP Codes Affected by Recent Wildfires (WF[1])	YoY Percent Change in WF	WF to State Percentage
2018	139,222	8,734	1.7%	6.3%	21,848	1,487	9.4%	117,374	7,247	0.3%	16,957	1,077	2.4%	6.4%	5,172	274	39.8%	5.3%
2017	140,312	8,587	0.4%	6.1%	22,017	1,359	0.9%	118,295	7,228	0.3%	16,766	1,052	4.2%	6.3%	4,974	196	-19.0%	3.9%
2016	141,192	8,553	0.8%	6.1%	22,643	1,347	-0.8%	118,549	7,206	1.1%	16,514	1,010	9.0%	6.1%	5,465	242	5.7%	4.4%
2015	141,391	8,483		6.0%	22,740	1,358		118,651	7,125		15,294	927		6.1%	5,650	229		4.1%

Voluntary Market

	TOTAL (New + Renewed)				New			Renewed			Non-Renewed (Insured Initiated)				Non-Renewed (Insurer Initiated)			
Calendar Year	State	ZIP Codes Affected by Recent Wildfires (WF[1])	YoY Percent Change in WF	WF to State Percentage	State	ZIP Codes Affected by Recent Wildfires (WF[1])	YoY Percent Change in WF	State	ZIP Codes Affected by Recent Wildfires (WF[1])	YoY Percent Change in WF	State	ZIP Codes Affected by Recent Wildfires (WF[1])	YoY Percent Change in WF	WF to State Percentage	State	ZIP Codes Affected by Recent Wildfires (WF[1])	YoY Percent Change in WF	WF to State Percentage
2018	8,542,520	397,784	-0.2%	4.7%	971,809	43,549	2.0%	7,570,711	354,235	-0.5%	731,660	33,092	2.0%	4.5%	167,570	8,751	9.6%	5.2%
2017	8,545,429	398,633	0.0%	4.7%	987,036	42,681	-0.1%	7,558,393	355,952	0.0%	749,470	32,434	1.7%	4.3%	162,048	7,981	0.7%	4.9%
2016	8,500,289	398,629	0.8%	4.7%	974,600	42,742	3.1%	7,525,689	355,887	0.6%	727,150	31,884	3.5%	4.4%	167,359	7,922	-1.8%	4.7%
2015	8,401,394	395,300		4.7%	954,687	41,452		7,446,707	353,848		718,563	30,815		4.3%	174,345	8,066		4.6%

[1] ZIP codes hit with wildfires in 2015 and 2017. Including Butte and Valley fires in 2015 and fires in October 2017, December 2017, and the Montecito mudslide that occurred January 2018.

[2] ZIP codes hit by the 2018 wildfires are not included.

CALIFORNIA DEPARTMENT OF INSURANCE

Number of New, Renewed, and Non-Renewed Homeowners' Policies

		Voluntary Market				California FAIR Plan	
				Number of Non-renewed Policies			
County	Year	Number of New Policies	Number of Renewed Policies	Insured-Initiated	Insurer-Initiated	Number of New Policies	Number of Renewed Policies
State	**2018**	**971,809**	**7,570,711**	**731,660**	**167,570**	**21,848**	**117,374**
	2017	**987,036**	**7,558,393**	**749,470**	**162,048**	**22,017**	**118,295**
	2016	**974,600**	**7,525,689**	**727,150**	**167,359**	**22,643**	**118,549**
	2015	**954,687**	**7,446,707**	**718,563**	**174,345**	**22,740**	**118,651**
ALAMEDA	2018	36,202	316,806	29,088	4,809	275	1,865
	2017	36,396	316,739	28,811	4,772	274	1,955
	2016	35,897	313,912	27,672	5,136	260	2,081
	2015	35,794	310,866	27,941	5,151	298	2,201
ALPINE	2018	61	567	45	11	8	22
	2017	64	570	51	11	13	13
	2016	42	587	35	15	9	9
	2015	52	578	37	13	8	3
AMADOR	2018	1,587	11,786	1,092	327	85	142
	2017	1,199	12,214	1,016	328	92	86
	2016	1,180	12,588	1,071	453	67	53
	2015	1,145	12,951	1,138	397	46	31
BUTTE	2018	7,511	57,183	5,945	1,488	198	239
	2017	7,221	57,620	5,777	1,481	135	164
	2016	7,461	57,882	5,455	1,647	127	94
	2015	6,877	58,201	5,463	1,618	88	42
CALAVERAS	2018	2,407	19,168	1,910	518	309	323
	2017	2,092	19,936	1,886	590	256	166
	2016	2,037	20,414	1,796	663	113	101
	2015	1,976	21,002	1,934	648	66	66
COLUSA	2018	564	4,335	418	119	2	8
	2017	576	4,389	445	125	1	8
	2016	550	4,415	420	148	5	5
	2015	559	4,414	420	147	-	5
CONTRA COSTA	2018	32,271	268,268	25,871	4,265	160	701
	2017	33,071	268,122	25,923	4,374	129	745
	2016	32,765	265,547	24,824	4,416	156	763
	2015	32,443	262,119	24,876	4,718	138	819
DEL NORTE	2018	831	6,368	593	202	8	13
	2017	830	6,444	600	234	9	12
	2016	851	6,387	567	175	5	13
	2015	785	6,437	602	244	7	8
EL DORADO	2018	8,612	61,712	6,155	1,594	400	568
	2017	7,790	63,236	6,125	1,417	351	380
	2016	7,614	63,511	5,974	1,567	217	299
	2015	7,165	63,843	5,797	1,820	205	197
FRESNO	2018	27,889	189,788	20,998	4,233	170	668
	2017	27,699	189,703	21,116	4,484	139	641
	2016	26,225	188,554	19,391	4,540	120	645
	2015	25,537	185,341	18,967	4,685	130	641
GLENN	2018	747	5,889	544	138	-	8
	2017	696	5,951	538	173	-	10
	2016	753	5,892	561	135	-	10
	2015	739	5,895	560	156	-	11
HUMBOLDT	2018	3,777	35,847	2,886	797	65	107
	2017	3,614	36,162	2,873	744	65	82
	2016	3,513	36,219	2,807	774	51	58
	2015	3,508	36,189	2,700	788	28	48
IMPERIAL	2018	3,415	28,515	2,589	885	54	231
	2017	3,718	28,345	2,702	856	27	238

County	Year	Voluntary Market: Number of New Policies	Voluntary Market: Number of Renewed Policies	Voluntary Market: Number of Non-renewed Policies, Insured-Initiated	Voluntary Market: Number of Non-renewed Policies, Insurer-Initiated	California FAIR Plan: Number of New Policies	California FAIR Plan: Number of Renewed Policies
State	**2018**	**971,809**	**7,570,711**	**731,660**	**167,570**	**21,848**	**117,374**
	2017	**987,036**	**7,558,393**	**749,470**	**162,048**	**22,017**	**118,295**
	2016	**974,600**	**7,525,689**	**727,150**	**167,359**	**22,643**	**118,549**
	2015	**954,687**	**7,446,707**	**718,563**	**174,345**	**22,740**	**118,651**
	2016	3,595	28,464	2,513	904	58	243
	2015	3,487	28,306	2,458	928	67	227
INYO	2018	568	5,290	385	131	7	30
	2017	559	5,291	407	121	7	30
	2016	510	5,338	366	117	11	27
	2015	474	5,368	346	103	8	24
KERN	2018	29,619	184,673	20,838	6,005	572	1,913
	2017	30,135	183,112	21,617	6,052	611	1,866
	2016	29,877	180,194	20,310	6,203	523	1,769
	2015	27,446	170,644	18,517	6,139	514	1,722
KINGS	2018	3,685	25,928	2,608	658	10	22
	2017	3,518	25,912	2,602	644	8	23
	2016	3,684	25,436	2,361	715	12	21
	2015	3,691	24,822	2,370	673	3	22
LAKE	2018	3,129	20,541	2,103	846	104	187
	2017	3,124	20,971	2,262	941	119	156
	2016	2,962	21,508	2,412	979	135	105
	2015	2,899	21,865	2,297	799	83	66
LASSEN	2018	1,184	9,465	924	285	21	37
	2017	1,138	9,716	934	322	20	28
	2016	1,156	9,767	849	329	13	22
	2015	1,093	9,847	918	285	12	14
LOS ANGELES	2018	179,871	1,550,466	132,697	34,921	9,584	84,014
	2017	186,428	1,543,497	137,225	32,627	10,420	87,909
	2016	186,629	1,537,094	136,210	32,261	11,774	90,641
	2015	186,464	1,522,187	137,770	35,424	12,356	93,519
MADERA	2018	4,637	31,316	3,171	881	97	146
	2017	4,376	31,770	3,486	814	84	106
	2016	4,342	31,920	3,291	867	56	92
	2015	3,842	32,058	3,098	1,000	76	56
MARIN	2018	5,992	64,483	4,716	1,106	75	361
	2017	6,142	64,749	4,681	1,108	69	356
	2016	6,581	63,913	4,368	1,063	71	359
	2015	6,598	63,336	4,797	1,216	69	333
MARIPOSA	2018	468	4,786	338	145	91	123
	2017	426	4,918	335	153	69	91
	2016	464	5,044	361	155	47	71
	2015	408	5,203	435	166	46	52
MENDOCINO	2018	2,560	22,723	1,862	640	108	125
	2017	2,458	22,987	1,892	626	79	84
	2016	2,483	23,243	1,838	659	64	49
	2015	2,749	23,021	1,988	546	29	42
MERCED	2018	7,982	52,282	5,555	1,174	12	45
	2017	7,814	51,749	5,834	1,222	10	50
	2016	7,513	51,481	5,563	1,312	22	40
	2015	6,959	50,811	5,411	1,291	25	37
MODOC	2018	271	2,255	199	66	10	16
	2017	240	2,268	219	86	8	12
	2016	218	2,328	162	61	3	10
	2015	222	2,335	224	73	2	9

County	Year	Voluntary Market				California FAIR Plan	
		Number of New Policies	Number of Renewed Policies	Number of Non-renewed Policies		Number of New Policies	Number of Renewed Policies
				Insured-Initiated	Insurer-Initiated		
State	**2018**	**971,809**	**7,570,711**	**731,660**	**167,570**	**21,848**	**117,374**
	2017	**987,036**	**7,558,393**	**749,470**	**162,048**	**22,017**	**118,295**
	2016	**974,600**	**7,525,689**	**727,150**	**167,359**	**22,643**	**118,549**
	2015	**954,687**	**7,446,707**	**718,563**	**174,345**	**22,740**	**118,651**
MONO	2018	346	4,441	268	84	56	102
	2017	395	4,444	332	104	38	82
	2016	383	4,526	324	87	37	58
	2015	322	4,596	322	92	22	45
MONTEREY	2018	8,484	79,587	6,489	1,466	137	234
	2017	8,607	79,840	6,664	1,442	135	179
	2016	8,961	79,156	6,475	1,479	104	138
	2015	8,535	78,431	6,347	1,575	85	95
NAPA	2018	3,922	35,592	3,229	667	32	74
	2017	3,889	35,785	3,001	599	28	64
	2016	3,774	35,841	2,904	597	41	46
	2015	3,812	35,557	3,011	648	41	31
NEVADA	2018	3,752	36,651	3,099	1,071	235	269
	2017	3,507	37,940	3,068	776	176	168
	2016	3,884	38,155	3,037	918	110	125
	2015	3,825	38,725	3,282	1,118	92	85
ORANGE	2018	68,836	547,407	51,838	10,491	597	2,013
	2017	69,641	543,960	53,063	9,853	644	1,907
	2016	70,016	540,159	53,258	9,980	680	1,789
	2015	67,955	535,314	52,008	10,749	654	1,619
PLACER	2018	17,398	116,675	13,334	2,199	196	247
	2017	17,213	116,895	13,535	2,128	154	164
	2016	16,633	115,676	13,029	2,146	108	125
	2015	16,301	113,935	12,676	2,550	91	74
PLUMAS	2018	892	7,484	672	213	35	57
	2017	795	7,752	704	221	31	44
	2016	743	7,903	664	237	26	29
	2015	742	8,070	670	218	19	15
RIVERSIDE	2018	88,922	520,707	64,787	15,209	1,385	3,518
	2017	91,840	514,704	66,657	14,464	1,471	3,126
	2016	90,634	510,613	65,627	15,681	1,534	2,780
	2015	86,363	503,821	61,998	15,434	1,394	2,436
SACRAMENTO	2018	53,731	353,355	41,778	7,807	126	375
	2017	54,490	352,746	43,044	8,217	106	392
	2016	53,424	350,177	40,895	8,420	92	429
	2015	51,670	345,308	39,324	8,865	101	474
SAN BENITO	2018	1,934	12,429	1,166	224	5	8
	2017	1,781	12,126	1,101	237	3	8
	2016	1,533	11,882	1,028	217	10	5
	2015	1,507	11,628	1,101	204	3	3
SAN BERNARDINO	2018	66,732	437,222	47,393	13,048	3,754	9,263
	2017	68,598	434,223	49,736	12,710	3,557	8,213
	2016	65,850	434,857	48,914	12,745	3,453	7,209
	2015	63,541	432,433	48,017	12,962	3,342	6,038
SAN DIEGO	2018	73,624	610,612	54,644	14,225	1,127	4,258
	2017	75,934	610,318	57,874	12,441	1,109	4,062
	2016	75,429	609,195	56,543	13,511	1,131	3,838
	2015	73,881	603,621	55,003	13,670	1,242	3,429
SAN FRANCISCO	2018	10,083	117,637	8,366	1,329	51	408
	2017	10,674	117,731	8,912	1,384	55	424

		Voluntary Market				California FAIR Plan	
				Number of Non-renewed Policies			
County	Year	Number of New Policies	Number of Renewed Policies	Insured-Initiated	Insurer-Initiated	Number of New Policies	Number of Renewed Policies
State	**2018**	**971,809**	**7,570,711**	**731,660**	**167,570**	**21,848**	**117,374**
	2017	**987,036**	**7,558,393**	**749,470**	**162,048**	**22,017**	**118,295**
	2016	**974,600**	**7,525,689**	**727,150**	**167,359**	**22,643**	**118,549**
	2015	**954,687**	**7,446,707**	**718,563**	**174,345**	**22,740**	**118,651**
	2016	10,606	117,059	8,423	1,406	51	447
	2015	10,949	115,979	8,972	1,565	41	473
SAN JOAQUIN	2018	24,807	157,907	18,427	4,006	42	447
	2017	24,966	156,940	19,296	4,116	74	475
	2016	24,485	155,927	18,395	4,384	63	488
	2015	23,735	153,034	17,400	4,473	77	505
SAN LUIS OBISPO	2018	8,883	78,245	6,565	1,519	68	180
	2017	8,892	78,178	6,800	1,330	74	145
	2016	9,131	77,853	6,694	1,511	48	118
	2015	9,296	76,463	6,477	1,654	50	103
SAN MATEO	2018	13,737	153,339	11,406	1,677	65	164
	2017	14,180	153,939	11,627	1,844	76	137
	2016	14,221	152,771	11,002	1,896	60	119
	2015	14,459	151,728	11,544	1,954	58	104
SANTA BARBARA	2018	9,375	85,785	6,831	1,741	88	420
	2017	9,460	85,367	6,937	1,462	67	462
	2016	9,486	85,182	6,798	1,701	88	472
	2015	9,437	83,941	6,714	1,802	91	462
SANTA CLARA	2018	38,049	353,073	31,284	4,940	122	671
	2017	39,033	353,595	31,342	5,087	91	685
	2016	37,506	352,550	29,665	5,185	95	726
	2015	38,913	349,149	30,998	5,358	96	763
SANTA CRUZ	2018	6,328	69,088	5,118	1,167	159	275
	2017	6,446	69,255	5,076	1,237	119	241
	2016	6,560	69,033	4,976	1,308	104	213
	2015	7,060	68,486	5,260	1,326	139	163
SHASTA	2018	8,549	52,788	6,382	1,485	122	204
	2017	7,671	53,627	5,731	1,442	110	145
	2016	7,095	54,196	5,265	1,607	77	116
	2015	6,764	54,020	5,152	1,342	91	70
SIERRA	2018	136	1,196	100	28	8	21
	2017	89	1,255	63	34	7	18
	2016	123	1,251	84	36	11	13
	2015	100	1,292	126	36	4	11
SISKIYOU	2018	1,919	13,886	1,330	462	49	118
	2017	1,748	14,148	1,322	476	53	83
	2016	1,586	14,255	1,238	509	46	60
	2015	1,548	14,304	1,202	430	43	47
SOLANO	2018	13,279	108,388	10,539	1,620	31	121
	2017	13,338	108,349	10,489	1,709	28	123
	2016	13,580	107,264	10,070	1,934	41	129
	2015	13,301	105,393	9,867	1,948	34	134
SONOMA	2018	14,996	130,250	12,511	2,323	121	189
	2017	14,412	131,087	11,203	2,440	85	152
	2016	13,947	130,841	10,828	2,232	85	118
	2015	13,998	129,912	10,938	2,382	74	90
STANISLAUS	2018	17,496	119,995	13,414	2,851	35	52
	2017	17,917	120,081	14,555	2,851	33	43
	2016	17,050	120,102	13,467	3,027	40	38
	2015	16,869	118,783	13,102	3,160	25	32

CALIFORNIA DEPARTMENT OF INSURANCE
Number of New, Renewed, and Non-Renewed Homeowners' Policies

County	Year	Voluntary Market				California FAIR Plan	
		Number of New Policies	Number of Renewed Policies	Number of Non-renewed Policies: Insured-Initiated	Number of Non-renewed Policies: Insurer-Initiated	Number of New Policies	Number of Renewed Policies
State	**2018**	**971,809**	**7,570,711**	**731,660**	**167,570**	**21,848**	**117,374**
	2017	**987,036**	**7,558,393**	**749,470**	**162,048**	**22,017**	**118,295**
	2016	**974,600**	**7,525,689**	**727,150**	**167,359**	**22,643**	**118,549**
	2015	**954,687**	**7,446,707**	**718,563**	**174,345**	**22,740**	**118,651**
SUTTER	2018	3,165	21,448	2,645	536	2	7
	2017	3,310	21,423	2,533	545	6	4
	2016	3,116	21,478	2,335	575	2	5
	2015	2,809	21,372	2,192	494	3	4
TEHAMA	2018	1,907	13,234	1,306	412	17	31
	2017	1,847	13,201	1,363	504	18	21
	2016	1,729	13,389	1,229	569	15	14
	2015	1,691	13,493	1,254	499	6	13
TRINITY	2018	359	4,072	264	120	89	90
	2017	371	4,200	282	156	67	62
	2016	356	4,310	323	133	43	47
	2015	349	4,369	336	109	52	26
TULARE	2018	13,297	91,093	9,450	2,878	130	335
	2017	13,340	91,224	9,634	2,733	160	259
	2016	12,858	90,911	8,855	2,986	107	201
	2015	12,123	89,457	8,508	2,878	73	167
TUOLUMNE	2018	1,862	17,888	1,440	653	185	244
	2017	1,464	19,152	1,411	570	137	168
	2016	1,955	19,563	1,482	627	84	131
	2015	1,558	20,805	1,576	1,076	94	76
VENTURA	2018	21,010	177,840	15,914	3,470	306	987
	2017	21,541	177,762	16,403	3,280	278	964
	2016	20,932	177,435	16,095	3,035	304	903
	2015	20,604	175,856	15,623	3,404	276	838
YOLO	2018	5,190	44,299	4,070	805	11	30
	2017	5,511	44,079	4,210	823	3	32
	2016	5,500	43,684	4,149	809	14	19
	2015	5,212	43,130	4,067	829	4	16
YUBA	2018	2,966	16,398	2,047	594	37	47
	2017	2,805	16,358	2,115	521	29	31
	2016	2,603	16,462	1,856	564	20	19
	2015	2,538	16,313	1,866	507	19	13

It includes aggregated counts on the following: homeowners coverage forms similar to HO-2, HO-3, HO-5 & HO-8, etc., dwelling fire forms (excluding dwelling fire contents only coverage), landlord business owner policies (residential policies of 4 units or less), and mobile homes, representing 98.3% of the homeowners market. It excludes HO-4 and HO-6 data.

SECTION FOUR

United Policyholders

Roadmap to Preparedness Program

Dropped by your Insurer in California? What to do...

If you are one of the many Californians whose insurance company had notified you they will not be renewing a policy on your home, don't panic, but start shopping ASAP. By law they have to give you 45 days notice, and you may need that much time to find a replacement policy you can afford.

In most parts of the state, you still have buying options and insurance companies are still competing for your business. But if you live in a brush-heavy or forested area that's been hit by recent wildfires, it may be hard to find a company willing to insure your home. When you find a replacement policy, it will probably cost more but provide less protection than your old policy. It may be through a "non-admitted" insurer.[1] These types of companies are picking up customers that "admitted" (well-known brand) insurers are dropping.

United Policyholders is here to help you shop and deal with this unfortunate situation, and we are working on initiatives to fix it. To learn more about the reasons why so many insurance companies are reducing the number of homes they're insuring in parts of California, visit the Advocacy and Action section of uphelp.org.

1) TRY AND GET YOUR INSURER TO CHANGE COURSE AND AGREE TO RENEW YOU[2]

Contact your current insurance company and ask them if there are improvements you can make to your home that will qualify you for a renewal. Give them your best arguments for keeping you as a customer. If you bought your expiring policy through an agent, ask him/her to go to bat for you with the company.

Contact your local fire department, Fire Safe Council or elected officials and find out if there is an inspection, fire risk reduction certification or brush clearing assistance program available in your area.

NOTE: If your insurer did not give you 45 days notice, or their reasons for dropping you seem unfair, seek help from the California Department of Insurance (CDI) at 1-800-927-HELP, www.insurance.ca.gov.

Limited circumstances where an insurer must renew your policy:

1. You have a policy with a guaranteed renewal provision. A few companies offer this. Some AARP members who bought through The Hartford have this protection.

2. You lost your home in a declared disaster within the past two years: CA Insurance Code at section 675.1 gives disaster victims the right to one or two renewals when their policy comes up for renewal.

3. Your home was damaged in a declared disaster with the past two years

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[1] "Admitted" insurers are fully regulated by the CA Department of Insurance and their customers are protected by CIGA, the CA Insurance Guarantee Association if their insurer becomes insolvent (runs out of money). "Non-admitted" insurers are not.

[2] With a few exceptions, your insurance company can drop (non-renew) you as long as they give you written notice at least 45 days prior to the date your old policy will expire, and as long as they are following their own guidelines and not discriminating against you. Their guidelines must be objective, have a substantial relationship to the risk of loss, and be applied consistently. Common reasons include wildfire risk, the age or condition of the property, lack of defensible space, type of roof or construction. The 45-day notice must contain the reason or reasons for the nonrenewal, the telephone number of the insurer's representatives that handle consumer inquiries or complaints, and a statement that you can have the insurer's nonrenewal decision reviewed by the CDI.

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2) **DON'T PANIC, START SHOPPING**

Contact the insurance agent you've been using, or ask trusted sources for recommendations to an "independent" insurance agent. Independent agents have relationships with multiple insurance companies. A "captive" agent that sells for companies like State Farm, Farmers or Allstate probably can't help you, as they're limited to only one insurance company.

Visit UP's website, www.uphelp.org and click on the "Insurance Finder" link on the right side of our home page. Try using the Match UP Insurance Finder.

Try the California Department of Insurance's shopping tools. They offer a list of CA home insurance companies with toll-free phone numbers, and a list of companies that sell "DIC" ("Difference in Conditions") policies that fill gaps in Fair Plan policies. www.insurance.ca.gov

If your best coverage and price option is through a "non-admitted" (also called "surplus lines") insurance company, check their financial strength rating with Demotech, A.M. Best, or another agency before you buy. This is important. If a non-admitted insurer runs out of money to pay claims, (becomes "insolvent") their customers are not protected by the same safety net[3] that "admitted" well-known brands have under them, and the CA Dept. of Insurance has less oversight power over them.

3) **SHOP SMART**

Your policy should cover what it would likely cost to rebuild your home in compliance with current building codes if it were to be completely destroyed by a natural or manmade disaster of any kind. But many policies don't. Don't blindly trust that your agent or insurer is selling you a policy that will fully protect your assets. UP surveys show that 2/3 of U.S. homes are underinsured. Shop for a policy that will adequately insure your dwelling for a total loss fire, (including building code upgrades) then add coverage for flood and quake protection if you can afford it. Ask the right questions and take good notes while shopping.

- Aim to insure your property for Replacement Cost Value, not depreciated Actual Cash Value.

- Coverage for building code upgrades and an extended replacement cost rider are worth paying for.

- Your dwelling coverage limit should match local construction costs (per square foot) for a home of similar style, age and quality, plus an "extended replacement cost" feature for extra protection.

-Choose the highest deductible you feel comfortable with to keep the cost of your coverage manageable

4) **THE FAIR PLAN IS A LAST RESORT**

If you strike out in the "normal" marketplace, you can buy home insurance through the California Fair Plan. Call them at (800) 339-4099). https://www.cfpnet.com/ The CA FAIR Plan is a state-run home insurance program for people who can't find a better option. Fair Plan policies provide only basic fire protection (no liability or theft) and cost more than a traditional policy. If you end up having to buy a Fair Plan policy, we recommend two things: Shop again in 6 months. New options may be available. And, if you can afford to, add supplemental coverage for what a Fair Plan policy excludes. Not all insurance agents are familiar with these options, so visit https://www.insurance.ca.gov/01-consumers/105-type/5-residential/carriersDICpolicies.cfm for more info.

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[3] CIGA – the CA Insolvency Guarantee Association pays up to $500k per home if the insurer goes insolvent.

SECTION FIVE

STATE FARM

LIBERTY MUTUAL INSURANCE

PROGRESSIVE

MERCURY

NATIONWIDE

NAMIC

Testimony of Rex Frazier, Personal Insurance Federation of California
before
Assembly Insurance Committee
August 20, 2019 – Sacramento, California

Mr. Chair and Members,

My name is Rex Frazier. I'm President of the Personal Insurance Federation of California. Thank you for the opportunity to testify today about homeowners' insurance regulation and pricing. Issues with homeowners' insurance availability, which my colleague will discuss in greater depth, have their roots in several regulatory decisions. It is important to identify these policy choices, and acknowledge their direct consequences.

An insurer's ability to serve communities threatened by wildfire is directly related to its relationship with the California Department of Insurance, which has a dual role: on one hand, the Department is empowered to prevent excessive rates and can even order insurers to reduce previously-approved rates that it believes have become excessive over time; on the other hand, the Department must monitor solvency to ensure that insurers can pay claims. In this balancing act, if the Department restrains an insurer's rates too aggressively, it places financial pressure on that insurer, which will, then, reduce exposure to higher-risk areas.

The Department has approached rate regulation in a manner very different from the rest of the country. According to the National Association of Insurance Commissioners, as of 2016, California had the 32nd highest average homeowners' insurance premium in the country (and, when adjusted for average household income, this dropped to 43rd). This lower premium level was a stark change from several years earlier when, in 2009, California had the 14th highest average premium. During that period, the average homeowners' premium in the nation increased by 45%, while California's average only increased by 8.1%. During this same time period, California CPI grew 14%.

Hurricane-exposed states, such as Louisiana and Florida, now have average homeowners' insurance premiums almost double that of California.

While admitted market carriers have been concerned about rate inadequacy, local government officials and residents in high fire risk areas have voiced the opposite, with complaints about high prices. This is a disconnect worth significant consideration. While the Gulf Coast States have already had a climate-driven increase in insurance rates, California has not. California regulations, but not statute, continue to prohibit insurers from using climate change modeling in pricing – instead requiring insurers to predict future losses based upon the average of the last 20 years of losses. California's recognition of a "new normal" does not yet extend to insurance rates.

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This climate change restriction is on top of California's continued regulatory prohibition on allowing insurers to include their actual cost of reinsurance in insurance rates. As the world reinsurance market recognizes California's climate risk and seeks higher prices from California insurers, California rating rules continue the legal fiction that insurers do not buy reinsurance.

Perception of catastrophic wildfire risk as a secondary consideration has changed. S&P Global Ratings recently acknowledged this change by adding wildfire risk to the list of disasters that implicate insurer credit worthiness, which was limited in the past to include only tornados, hurricanes and earthquake risk. Reinsurers have had three years in a row of wildfire losses in excess of $10 billion, due to catastrophic fires in Canada in 2016 and such fires in California in 2017 and 2018. Not surprisingly, there is alarm among rating analysts, reinsurers and primary insurers about the adequacy of wildfire risk modeling, underwriting practices and rate levels. S&P recently predicted that reinsurance pricing for California wildfire risk could rise 30% - 70% between now and the January, 2020 renewals. If a California insurer maintains significant exposure to this catastrophic risk, they will be expected to pay significantly increased reinsurance premiums while California rules prevent that cost recovery. We urge this Committee to consider the situation that current California reinsurance regulations are creating.

Wildfire catastrophe models are improving and we expect continued improvement. As the science advances, the risk that insurers and reinsurers will underestimate fire risk will reduce, which will, in turn, reduce concerns about insurer creditworthiness. But, we have likely transitioned in our understanding of wildfire risk, which will no longer be considered a secondary risk moving forward.

Despite the lid on pricing in the last decade and the emergence of wildfire risk as a credit-impacting consideration, statewide availability numbers are relatively stable, with the Department's recent report showing, from 2015-2018:

- The number of new homeowners' insurance policies statewide has increased 1.8%;
- The number of policyholder-initiated non-renewals has increased 1.7%, while the number of insurer-initiated non-renewals has decreased 3.9%; and
- Of the policyholders non-renewed by their insurers, only 13% end up in the FAIR Plan.

These numbers exist despite efforts of insurers to evaluate their business and ensure they are not irresponsibly, over-concentrated to any single catastrophic risk area. This is a solvency risk of importance to insurers and the Department alike, with the most recent worst case scenario being Merced Property & Casualty's failure following a single fire.

I appreciate the opportunity to talk about regulation and pricing issues. I'll turn it over to my colleague who will provide additional information about availability issues. Thank you.

Testimony of Mark Sektnan, American Property Casualty Insurance Association

Before

Assembly Insurance Committee

August 21, 2019 – Sacramento, California

Good morning, chair and members of the Assembly Insurance Committee. My name is Mark Sektnan and I am vice president of state government relations for the American Property Casualty Insurance Association.

Thank you for the opportunity to talk about one of the most important issues related to homeowner's insurance and one of the most difficult questions to answer.

Insurance is key to protecting most people's key asset – their home. In many cases, insurance is required by the mortgage company. Sadly, we often see people drop their insurance coverage after they pay off their house but that is a conversation for another panel.

As highlighted by previous speakers, we need to be very careful not to confuse the affordability of insurance with the availability of insurance. I understand that the cost of insurance may have gone up in some areas but not wanting to pay the price is much different than not having the ability to buy insurance. The previous speaker also highlighted another issue. If an insurer cannot get adequate rate to appropriately cover the risks they are insuring, the only option may be to write less policies in some areas. Insurers may also have to adjust

their writings due to restrictions placed on them by reinsurers who may want to adjust their exposures.

Several years ago, Governor Brown created the Tree Morality Task Force. At the request of several rural elected officials, a subcommittee on insurance issues was created. The subcommittee was tasked at looking at several issues including availability. The subgroup struggled with the question of availability. We discovered there was no real data to answer the question of availability. We had plenty of anecdotes on both sides, but no one could determine what was going on.

The recent data call released by the California Department of Insurance provides us with data on the first part of the question – non-renewals but does not answer the second part of the question -- was the homeowner able to find insurance somewhere else.

The data reflects slight changes in where consumers are getting their insurance. From 2015 to 2018 the percentage of residential insurance policies in moderate to very high fire risk zip codes covered by the voluntary market declined from 98.8% to 98.5%, while Fair Plan increased from 0.91% to 1.12% and surplus lines increased from 0.25% to 0.36% over the same time period? On top of that, the voluntary markets actually wrote more new and renewal policies in the moderate to very high fire risk zip codes in 2018 than in 2015, but due to an increase in homes in these areas - the voluntary market's share of these higher risk homes declined VERY SLIGHTLY (again, from 98.9% to 98.5%).

Insurers are still increasing the number of policies they write in moderate to high fire risk areas overall where they feel they can get appropriate rate to compensate for the higher risk. The

rest is being picked up by Fair Plan and Surplus lines carriers who are both able to charge appropriate rates for the risks they are taking. Other sign that homeowners might not be able to find insurance would be an increase in insurance placed on policies by banks and other lending institutions. Insurance is a requirement of almost all mortgages and if the homeowner does not have insurance, the homeowner is in violation of the contract and will place insurance on the property. Typically, these policies are far more expensive and very limited in coverage. We are not hearing that this is a problem.

As pointed out in the staff briefing paper, companies need to be mindful of managing their risk to ensure these risks are not overly concentrated in one potentially risky area. The agent who sold 400 polices for one company in a mobile home park that later burned down was certainly efficient from his perspective but did the company no favors. As pointed out in the staff paper, companies are also being forced to reevaluate risk as conditions change. Areas we never thought were high risk are being destroyed by wildfires. The question is this. If company a decides to non-renew policies in an area, are there other companies that will step in and write the business?

One of the things we did discover was that the perceptions of whether insurance was available was often determined by how the consumer was purchasing insurance. In some cases, a policy is written by an agent who only works for one company. If that company adjusts their book of business, the consumer would believe that homeowners' insurance was not available. In some cases, the same thing might happen with a broker who represents a small number of companies. A friend of mine who lives near the Woosly fire called me earlier this year to say that his insurance had gone up 500%. He went out and shopped and found a better

policy for a lower rate. He knew where to shop but most consumers have not worked in the insurance industry for 40 years.

What we discovered is that the insurance market is somewhat inefficient because consumers do not have the information readily available to know all the companies who write in a particular area. The insurance subgroup created the first insurance finder pilot project in Placer county – the sierra insurance finder. The idea was that homeowners having problems finding insurance could place their information on a website and agents and companies selling in the area could connect. This was the genesis of the "California home insurance finder" that is going to be created by the department of insurance with the passage of AB 1875 (Levine.)

As you know, insurers are required to provide homeowners insurance either directly or through the California Fair Plan, which is an association of all companies that write property insurance in California. The fair plan is the "insurer of last resort" -- an option for those who have looked for and cannot find homeowners insurance. As referenced in the briefing paper, the fair plan can act as a "canary in the coal mine" and significant growth in the Fair Plan might be an indication of a market problem. However, these numbers need to be fully understood to make sure they are telling the right story. In March, the fair plan saw a bump in new policies. How much of this was agents pushing the product before the April rate increase? Another key number is how long do people stay with the fair plan. This could be an indication that homeowners are finding coverage in the regular market. As stated previously, the Fair Plan saw 17% of their policies leave after several months. Much remains to be answered on the question of whether insurance is available.

We can also look at the surplus lines market. Growth in the surplus market could signal problems in the admitted market. While Lloyds of London is an exotic example of a surplus lines company, many of the surplus lines' companies are owned by admitted carriers who use the surplus lines companies to write difficult risks. While we have seen some growth in surplus lines policies it remains a small percentage of the market.

Clearly the market is hardening, and companies are taking a close look at the risks and their book of business.

There is another tool mentioned in the staff briefing that can help more insurers write business and that is better use of modeling. As noted in the staff paper, insurers cannot use models to predict the future, rates must be based on loss history, so we are always looking backwards. When the environment is changing as fast as we are seeing in California, the past might not be good predictor of the future. There is a reason why the windshield of a car is bigger than the rear-view mirror. Better ability to understand the future can help companies better understand the current risk and better determine where they feel comfortable writing.

My association represents a broad cross section of large, medium and small carriers. In many cases the small and medium companies may use different underwriting tools and have more appetite to write in high risk areas when the big companies do not. I remember a particularly heated conversation during an insurance task force meeting where a captive agent was talking about an availability problem in grass valley. I have one of my members on the phone. She said not only was her company writing policies in that area, but they were losing policies to other companies.

In the interest of time, I will rest and take questions.