California Homeowners Insurance Crisis

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Crisis –Defined

California Homeowners Insurance Marketplace Crisis

- The California homeowners insurance market is in the grips of an urgent crisis as major insurers **cancel** existing policies, **refuse to write** new policies and, in some cases, **abandon** the state's insurance market entirely.
- Frequent news stories indicate California's leaders are now scrambling to find solutions. There has been a misguided approach to market interventions in the form of **price caps** and **over-regulation**.
- California must fix its regulatory approach and **remove barriers** to a well-functioning insurance market.
- TWELVE insurance companies cover 85% of all California homeowners policies. That is until the past couple of years, when SEVEN of them announced the are limiting or stopping the writing of policies in California.

How Did We Get Here

Overview

- An important reminder is that – unlike public utilities – insurance companies can limit **where** they write policies.
- Tens of thousands of California homeowners, especially those who live in areas at risk of wildfires, have lost their insurance. Those that haven't, are faced with higher premiums.
- As one after another major insurer began pulling out of the state, most cited the cost of claims. For those that remain, even with the recent rate hikes, almost all are **NOT** writing new policies.
- The current system is broken because government regulators have been too slow to react to the changing insurance market conditions.

How Did We Get Here

Overview and History

- Wildfires in California are a big concern for insurers, but fortunately the message hasn't been "**California is not insurable**."
- Insurers are saying that clearing regulatory hurdles will be enough to make it profitable to write homeowners insurance in the state. Many of the proposed changes indicate a **growing interest in changing Prop. 103**, the voter-approved law that requires prior approval from the CA DOI before implementing rate changes.
- The American Property Casualty Insurance Association has favored changing Prop 103 for years. The insurers want <u>adequate rates</u> in a <u>timely manner</u>. Streamlining approvals of rate filings is the key to addressing the insurance crisis in California.
- Data sources show California insurers **paying out $1.13 for every $1 taken in** over the **last decade** to insure homeowners.

How Did We Get Here

Overview and History

- California is and has been a LOW-COST state for insurance, but the low premiums did not accurately **reflect the risk** insurers faced. The devastating wildfires of 2017 and 2020 proved this.
- In 2017 and 2020, the fires **wiped out decades of insurer California profits** and shed critical light on what rate adequacy really looks like. The cheap insurance premiums were a result of Prop.103, which has been acting as a price control…which always leads to shortages. It proved to be a barrier to its original goal of "ensuring insurance is available to all Californians."
- **Nobody is served by cheap policies they can't get**. Prices match actual risk or there will be no policies at all. The higher premiums will be painful at first, but should stabilize when the insurance market opens back and eventually becomes competitive again.

How Did We Get Here

Overview and History

- Since early 2024, the "double-digit quickly-approved rate hikes", most 20% to 30% on current policies has simply **bought some time**. Insurance companies have **temporarily agreed** to stay in California. In years past, there were no expedited rate increases and none over 6.9%, based on the limitations in Prop 103 passed by voters in 1988.
- The insurance companies that stayed in California, **renewing policies at the higher premiums**, aren't fully committed to staying and almost **none are writing new policies**.
- Bold and immediate action from the Governor and Insurance Commissioner is needed to help open the markets back up. Insurers need to **feel confident** writing insurance in California and a robust market is needed that gives consumers more options for protecting their home, especially against the peril of fire.

How Did We Get Here

Overview and History

- Since 2017, 10 million forest acres and 39,000 homes have been destroyed in California due to wildfires.
- Eight of the ten largest wildfires in California have occurred since 2017.
- The largest wildfire in California history is the 2020 August Complex Wildfire in which 1,032,648 acres burned.
- Losses incurred by California insurance companies show a staggering increase. In **2016,** wildfire losses were $**4 billion.**
- Never again, were they this low, as wildfire losses in **2017** were $**15 billion**, followed by **$13 billion** in **2018** and now total over **$70 billion** for the past decade.
- Northern California accounts for more than 90% of the $70 billion in losses.

How Did We Get Here

Overview and History

- Here are the 10 largest wildfires in California *(Note: The Park Fire currently burning is currently the 4th largest wildfire in California history)*

Year	Fire Name	Acres Burned
2020	August Complex	1,032,648
2021	Dixie Fire	963,309
2018	Mendocino Complex	459,123
2020	SCU Lightning Complex	396,625
2020	Creek Fire	379,895
2020	LNU Lightning Complex	363,220
2020	North Complex	318,935
2017	Thomas Fire	281,893
2003	Cedar Fire	273,246
2012	Rush Fire	271,911

Where We Are At Now

New Regulations Needed

- Under current state law, insurers who file for a rate increase of 7% or more must be approved by the CA DOI. In justifying a rate hike, they're only allowed to use the past 20 years of data. Because 8 of the 10 largest wildfires have occurred since 2017, looking back 20 years to predict future losses and set premiums is absurd.
- Insurers want the CA DOI to let them use forward-looking so-called 'catastrophe' modeling. California is the **only state** that does not allow this.
- The insurers are not willing to continue writing policies in California unless a new set of regulations permitting them to use catastrophic modeling in ratemaking to ensure they can more accurately and fairly allocate risk of loss.
- Every other state permits cat models in rating and their strong homeowners **insurance marketplace** and **policy premiums** reflect this.

Where We Are At Now

Profits / Expected Losses / No New Policies

- Insurance Companies are not merely raising premiums to maximize profits. The mounting catastrophic losses, particularly 2017 and 2018 in which insurers paid close to **$30 billion** demonstrates how vulnerable California insurers are.
- Data from a New York University study of profit margins in various industries in the nation, found that that as of January 2024, the **national net profit margin** of for property and casualty insurance is **only 5 percent**.
- With expected losses EXCEEDING approved premiums, insurers predictably started **withdrawing** from the California market…entirely by the end of 2023.
- The largest homeowners multi-peril writers in California stopped writing new policies, starting with State Farm in May 2023. Soon after, Farmers, CSAA, Liberty Mutual and Allstate followed.

Where We Are At Now

No New Policies / Non-Renewals of Policies

- While the five major insurers stopped writing policies in 2023, most of the other insurance companies had already ceased writing homeowners insurance in California much sooner.
- In early 2020, **two of the five** luxury home/high net worth insurers stopping writing new policies: AIG in January and Nationwide (Crestbrook) Private Client in March.
- Not long after, various other smaller admitted preferred insurers followed, stating there is a moratorium on new business in California. This trend continued until early 2024 when the remaining insurers either stopped completely or gave agents an allotment of 1 or 2 new policies per month….but with very stringent guidelines: no high fire or earthquake hazard areas, no losses, proof of updates, etc. This **minimal allotment of new policies** allowed by a few insurance companies remains currently.

Where We Are At Now

Non-Renewals of Policies

- Sadly, from 2020 to the present not only did insurance companies **stop writing** new policies they began **non-renewing** policies.
- The first to go were the policyholders with a “fire score too high”. Not extreme but homes in some areas of San Rafael, Mill Valley and San Anselmo, for example. Essentially homes a **little further away** from the town or freeway. Next were those with **prior losses** and **other characteristics** the insurer took issue with.
- In 2023 and 2024 everything changed with non-renewals – suddenly many insurance companies ceased to do business in California and others non-renewed **any** policyholder with a home in or near an area believed to have too high of a wildfire exposure. In addition, homes deemed (by a drone or aerial internet maps) to have algae or moss on the roof, a tree limb too close to the roof or some other concern by an underwriter received a non-renewal.

Where We Are At Now

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Non-Renewals of Policies

- Currently there are an estimated **100,000 policies** being non-renewed for properties deemed too close to a wildfire hazard area.
- State Farm policies account for 72,000 of these non-renewals. The remainder of non-renewals are primarily coming from Farmers, CSAA and Allstate.
- A number of Liberty Mutual, Travelers, USAA and other insurers, with a smaller share of policies, are sending non-renewals as well. In addition, there are non-renewals from insurers who are leaving California completely, primarily Nationwide Private Client.

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Where We Are At Now

A Look at State Farm

- State Farm, the insurer with the largest market share in California is understandably the insurer struggling the most. This is evident, based not just not on the massive number of non-renewals, but a 2024 downgrade by AM Best of their financial rating to “B” fair from “A” excellent.
- The biggest impact to California homeowners insured by State Farm, might not be the non-renewal of policies or not writing new policies.
- It might be the **State Farm rate hike filed in July of more than 50%.** An estimated 1.2 million homeowners would be affected. State Farm states the rate increase will help shore up its financial situation following massive losses from wildfires and other natural catastrophes. Two previous rate increases were approved and implemented, a 20% rate increase in December 2022 and a 6.9% rate increase in January 2023.
- State Farm is “working toward its long-term sustainability in California” according to a statement from the company.

Where We Are At Now

The Current Marketplace

- With the California insurance marketplace currently in a crisis, due to the lack of availability of new policies it's important to know what options there are for homeowners.
- Because almost all insurers have stopped accepting new customers, regardless of where their home is located, it has significantly and adversely affected **new homebuyers**. Of course, **existing homeowners** who have been non-renewed, are struggling to find replacement policies.

Where We Are At Now

The Current Marketplace

- Lets first look at the **THREE LEVELS**, so to speak, of homeowners insurance companies:

Level One – Preferred/Admitted Insurers:

- These are the insurance companies offering the **best policies** in terms of coverage, limits and premium. They also have the **strictest guidelines** of trying to qualify for a new policy.
- In addition, these are the companies who are primarily **non-renewing policies** due to wildfire concerns. They are also **non-renewing policies** for concerns about roofs and other home/premises characteristics.
- The most well-known of these insurers are Allstate, Amica, Chubb, Cincinnati, CSAA, Farmers, GEICO, Liberty Mutual, Mercury, Nationwide, Progressive, Pure, Safeco, State Farm, Travelers and USAA.

Where We Are At Now

The Current Marketplace

Level Two – Non-Preferred/Non-Admitted Insurers:

- These are the insurance companies offering policies that provide **less coverage**, **fewer endorsement** options, **lower limits** and **higher premiums**. These companies are often considered the "secondary market" and are not approved or backed by the State of California.
- They are not likely to be in compliance with the state's insurance laws and regulations. If the policyholder files a claim and it can't be paid because the insurance company became insolvent, the claim simply won't be paid.
- The most well-known of these insurers are American Modern, American Western Home, AZGUARD, Evanston, Great Lakes SE, Kinsale, KW Specialty, Lloyd's of London, MSI/Spinnaker, Private Client Select, Scottsdale and Vault E&S.

Where We Are At Now

The Current Marketplace

<u>Level Two – Non-Preferred/Non-Admitted Insurers</u>:

- For reference, the **Level One preferred/admitted** insurance companies **must follow state regulations** regarding how much they can charge and what risks they can (or can't) cover.
- **Non-preferred/non-admitted** insurers **do not have to follow** these regulations, which allows them to take on higher risks. Being <u>non-preferred/non-admitted</u> doesn't affect the validity of their policies or that they aren't regulated to some extent. The regulations are just different from those that govern <u>preferred/admitted</u> insurance companies.

Where We Are At Now

The Current Marketplace

Level Three – California FAIR Plan:

- The California FAIR Plan is deemed the last resort for homeowners who have been declined by every insurer and are unable to purchase a policy. Essentially, it is a fire insurance program for high-risk properties. The policy primarily covers **fire, smoke, lightening and internal explosion**. However, additional coverage is offered for windstorm and hail.
- The lack of traditional policy options has pushed many people to the California FAIR Plan, an insurer that is morphing into the fastest-growing policy writer in the state. This is a disaster waiting to happen.

Where We Are At Now

The Current Marketplace

Level Three – California FAIR Plan:

- The California FAIR Plan is writing the highest-risk policies in California, but is woefully **underfunded**, with only a **few billion** in assets and **several hundred billion** in liabilities.
- A **single catastrophic loss event** in an area dense with FAIR Plan policies **would bankrupt** the entity quickly. The insurance industry is the **backstop** for the FAIR Plan, meaning they would be liable for paying out excess FAIR Plan claim in proportion to the amount of business they write in California. This is regardless of the fact they are not receiving **any premium** for those policies and would also pay out for **losses** on their own policies.
- The lose-lose scenario is another reason why insurers are shrinking their California footprint, to avoid FAIR Plan financial liability. The state leaders must provide a mechanism for the FAIR Plan to remain solvent without uncapped industry exposure. Creating a reinsurance program specifically for the FAIR Plan could be a solution.

Where We Are At Now

The Current Marketplace

Level Three – California FAIR Plan:

- When purchasing a California FAIR Plan policy, it's important that an additional policy be purchased. This **companion policy** is called a DIC (Difference in Conditions) policy.
- A DIC policy provides coverage for common perils, such as theft and water damage. In addition, liability and medical payments can be added to the DIC policy.
- Note that all DIC policies are not created equal and the agent writing the policy should be knowledgeable about how to **tailor the policy** to best meet the needs of the insured.
- Also note that that DIC policies are typically written through the same **non-preferred/non-admitted** insurers offering policies in high wildfire prone areas.

Where We Are At Now

Steps Homeowners Can Take

- It's important to mention that there are things a homeowner can do to **prevent** their insurance company from **issuing a non-renewal** of their policy. Insurers are now completing frequent inspections, both in-person and aerial inspections, of homes.
- In addition, if a homeowner receives a non-renewal and needs to purchase a new policy, there is a possibility **no policy** will be found (except the last resort California FAIR Plan) if the **condition** and/or **updates** to the home are unacceptable to new insurers.
- Some of the best actions that can be taken, to keep a home insurable, are as follows:
- Maintain the condition of the roof. If a roof has debris, algae or moss on it, has deterioration or discoloration or other signs it's not well maintained or past its lifespan, this will trigger non-renewal.

Where We Are At Now

Steps Homeowners Can Take

- Unlike in years past, there is little chance an insurance company will reverse the notice of non-renewal. Often times no second chance is given in allowing time for the roof to be cleaned, have repairs made or have it replaced. The notices of non-renewal are not being rescinded, regardless of the action. In addition, a new insurance company will not write a policy for a home with a roof in poor condition.
- Trim tree limbs so that they are not hanging over the roof of the home
- Be certain there is clearance of at least 100 feet from the home for all unmanaged vegetation
- Install ember-resistant vents
- Enclose eaves with non-combustible materials

Where We Are At Now

Steps Homeowners Can Take

- Replace wood decking with fire-resistant decking
- Replace wood siding with non-flammable siding
- Update the following:
- **Electrical** (service panel/breaker box) cannot be more than 25 years old (no exceptions). In addition, for very old homes, there can be no knob & tube wiring remaining.
- **Plumbing** (pipes, lines, fittings, connectors, valves, drains and hoses in visible areas) will need to have been updated in the last 25 years and the water heater in the last 15 years
- **Heating System**: It can be no more than 25 years old, regardless of regular maintenance and the opinion of a service professional that it is in good condition.

Where We Are At Now

Steps Homeowners Can Take

- **Roof**: As already stated, the condition of the roof is important, it must be free of debris, algae, moss, etc.
- The **age of a roof** is also important. The maximum age of a roof allowable is 25 years, with the exception of a tile or metal roof. Typically, an insurer will allow longer for these roof types, up to 35 years for a tile roof or metal roof. A lot depends on the condition of the roof.
- It is recommended that any **roof older than 20 years** be inspected by a licensed roofer. The report from the inspection should be retained and be available to send to the insurance company showing no repairs or replacement needed.

Where We Are At Now

Steps Homeowners Can Take

- Finally, while not really a **maintenance** or **fire prevention** recommendation, this step is very important to mention:
- Don't file ANY water damage claims.
- Also don't file more than ONE claim (regardless of the **amount** of the claim or **type** of claim) in a five-year period.
- Filing a **water damage claim** or **two claims** likely will result in a notice of non-renewal. Finding a new policy, with a prior claim filed in an already challenging marketplace, will be very difficult.

Thank you!

For any questions related to the California Homeowners Insurance Crisis, please feel to reach out.

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