California FAIR Plan could be on the hook for up to $24 billion in L.A. fire losses

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Experts have predicted that the fires blazing through several parts of Los Angeles County could easily become the most costly wildfire event in the U.S. One insurer alone faces potential losses of up to $24 billion: the California FAIR Plan.

The FAIR Plan is a state-created but privately run insurer of last resort, providing fire insurance for residents and businesses unable to secure a policy on the private market. The FAIR Plan is not funded or financially backed by the government — instead, if the FAIR Plan runs out of money to pay claims, it's private insurers and their customers who end up with the bill.

Experts worry that if the FAIR Plan is overwhelmed, it could both financially strain policyholders across the state and their insurance companies, which could motivate more companies to rethink doing business in California.

But there are several steps before that would happen.

First, the FAIR Plan would have to blow through all of its reserves — a possibility that seems increasingly likely as strong winds continue to spread the uncontrolled fires. Over the summer, FAIR Plan President Victoria Roach disclosed to the Chronicle that the insurer only had about $385 million in unreserved funds available to pay claims.

The large fires of 2024 largely hit areas where the FAIR Plan had relatively small amounts of exposure.

But Los Angeles County is one of the FAIR Plan's largest areas of exposure in the state. A Chronicle analysis of the insurer's data found it covers more than $24 billion worth of residential and commercial property within the ZIP codes in and around the fire perimeters as of Thursday afternoon.

The FAIR Plan would only end up paying that amount if every single property it insures inside those ZIP codes ends up totally destroyed.

Long before it reached that amount, the FAIR Plan would turn to reinsurance — insurance for insurance companies to tap into during catastrophic events such as massive wildfires. The FAIR Plan has not publicly disclosed how much reinsurance it purchases. But a spokesperson told the Chronicle on Wednesday regarding the L.A. event: "The FAIR Plan has payment mechanisms in place, including reinsurance, to ensure all covered claims are paid."

Were the losses from the fire to be so large that it would overwhelm even the FAIR Plan's reinsurance, then the insurer would tap into its third source of money: private insurance companies and their policyholders.

When the FAIR Plan runs out of money to pay claims, it's allowed to split its remaining costs amongst all of the licensed insurers in the state, with costs allocated according to each company's market share. The last time that happened was in 1994, when the devastating Northridge earthquake caused an estimated $32 billion in insured property damage adjusted for inflation.

The process is similar to what happens if a private insurance company goes insolvent during a wildfire, namely that an organization created by the legislature would compel other insurers to help pay its claims.

Once insurance companies get charged, they would be able to pass on those costs to their customers — but only to a certain degree. In July, Insurance Commissioner Ricardo Lara announced a new plan for how to handle an event in which the FAIR Plan asked insurers for financial help.

For the first $1 billion each of residential and commercial claims, insurers would be required to pay half themselves, with the option of passing on the other half to their customers.

With the fires still burning, it's still too early to tell how many claims the FAIR Plan might get, the spokesperson for the plan said.

Michael Wara, director of the Climate and Energy Policy Program at Stanford University, said whether the FAIR Plan charges the industry will be a major indication that these fires will deeply disrupt California's already-fragile insurance market.

By its nature, a FAIR Plan assessment would hit insurers just as they’re dealing with large financial losses of their own, worsening the problem.

“If the FAIR Plan runs through its reserves and private insurers are required to pay an assessment… I don’t know how that’s going to affect the continued appetite to do business here,” said Amy Bach, founder of the consumer advocacy group United Policyholders.