[Exclusive: Can California’s FAIR Plan handle a huge wildfire? Here’s what insurer’s president says]

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How much money does California’s FAIR Plan have available to pay insurance claims if a huge wildfire were to cause billions of dollars in damage to homes and businesses?

In an exclusive interview with the Chronicle, FAIR Plan President Victoria Roach for the first time disclosed the answer: about $385 million, as of June 30.

For the more than 400,000 California homeowners on the FAIR Plan, that figure may sound alarming. In Truckee alone, a massive wildfire could expose the FAIR Plan to more than $5 billion in losses, according to data from the plan. An additional fire in Grass Valley (Nevada County) or Nevada City could add more than $3 billion each on top of that.

As the “insurer of last resort,” the FAIR Plan has quickly become the only option in wildfire-prone areas where homeowners are unable to find insurance anywhere else. The plan was created by the state in 1968 but is privately run, with the backing of all licensed insurers in the state.

Homeowners who switch to the FAIR Plan often report paying thousands of dollars more per year for a policy that only covers damage from fire, smoke and lightning. To get coverage for other kinds of damage, liability and all other elements of standard homeowners insurance, FAIR Plan clients are required to buy an additional policy. At the same time, Roach has said that the FAIR Plan’s current rates still aren’t enough to cover its expenses.

The potential for financial instability for the FAIR Plan has caught the attention of both the private industry and public officials, who are searching for solutions for how to keep its financial issues from spilling over into a disruption of the entire market. Last month, Gov. Gavin Newsom released a statement saying that strengthening the FAIR Plan was a “key priority.”

If the FAIR Plan were to burn through its surplus, it has two backup options of where to get more cash.

First, like a typical insurer, the plan can tap into its reinsurance (insurance for insurers) in the event of a catastrophic event that wipes out its surplus in one go, according to Roach.

But too many losses, or too few, can result in the FAIR Plan being unable to use its reinsurance to cover the total amount. The FAIR Plan has a deductible that it must meet before it can access its reinsurance. But that deductible level may be higher than its surplus, which fluctuates as premium payments come in and claims payments go out.

So if a fire — or series of fires — causes losses that exceed the amount of the surplus, but not enough to hit the FAIR Plan’s deductible level, then the FAIR Plan would not be able to use its reinsurance. Another problem: if a fire were to cause so much damage that it exceeds a pre-set coverage amount, then reinsurance may not pay for all of it.

If the FAIR Plan comes up short and can’t cover the rest with reinsurance, its second option has the potential to affect every residential and commercial policyholder in the state. All licensed insurers in the state, also called admitted insurers, are required to financially back the FAIR Plan as a condition of doing business in California, and therefore are on the hook for extra losses through an assessment.

“Reinsurance in and of itself does not eliminate the risk of assessment to the admitted carriers,” Roach said. “It mitigates it, and hopefully makes that amount smaller, should we need to assess, but we could be in a position with multiple smaller catastrophic events across the state that would not hit reinsurance levels but that would put us in a position of potential assessments to the admitted market.”

Rex Frazier, president of the Personal Insurance Federation of California, an industry group, said that in a scenario where a huge wildfire goes beyond what reinsurance will pay for alone, the FAIR Plan’s reinsurance would pay for half the damage and the private industry would cover the bill for the other half.

“It doesn’t take a huge fire anymore for there to be the first assessment on insurance companies,”

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Frazier said.

“That’s been the scary thing,” he added. “When companies are already struggling to pay the losses that they know are on their own books from business they sold and for which they collected premium, then you can get an assessment out of left field from the FAIR Plan.”

Under a new agreement released late last month, Insurance Commissioner Ricardo Lara spelled out how an assessment could trickle down to everyday policyholders. For the first $1 billion in residential damage the industry would be asked to pay, companies would have to pay for half of it themselves, and then spread the cost of the other half — and all losses beyond that — among their residential policyholders. The same would happen on the commercial side.

In other words, customers of every licensed insurer in the state — from State Farm to Allstate to Travelers — would see a portion of the losses on their bill, though it would first need to be approved by the state Department of Insurance.

Amy Bach, executive director of the consumer advocacy group United Policyholders, noted that companies would be charged in proportion to their market share — meaning bigger companies would bear the lion’s share of the payment and split it up among their many policyholders.

Ultimately, the system guarantees that no FAIR Plan policyholder will ever lose their home to a wildfire and find themselves with nowhere to turn — an important goal, Frazier said, although one that adds uncertainty for the private insurers that could be on the hook.

As of the beginning of August — as the Park Fire reached 400,000 acres — Roach said the FAIR Plan did not anticipate running out of money anytime soon. But it remains a looming threat over an already unstable insurance market.

“The FAIR Plan is designed to provide stability in the market per statute,” Roach said. “Any kind of assessment undermines that stability in the market.”

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