United Policyholders
Empowering the Insured

How the devastating Los Angeles fires could deepen California’s home insurance crisis

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- The fires across Los Angeles County are likely to be one of the most expensive natural disasters in U.S. history, with losses estimated at $50 billion or more.
- The losses threatened to deepen a crisis that has already left hundreds of thousands of Californians struggling to find and keep affordable homeowners insurance.

When raging wildfires tore through Pacific Palisades and other local communities this week, they not only left a path of destruction reminiscent of a World War II bombing campaign, but threatened to deepen a crisis that has already left hundreds of thousands of Californians struggling to find and keep affordable homeowners insurance.

The multiple fires from Los Angeles to the San Gabriel Valley that have burned thousands of structures since Tuesday — leading to losses that by one early estimate are well into the tens of billions of dollars — hit Southern California as insurers have been dropping customers statewide citing the increasing number and severity of wildfire-related losses.

The Palisades fire alone, which consumed more than 5,000 homes and structures, is being called the most destructive fire ever to hit the city, while the fires across the county are likely to be one of the most expensive natural disasters in U.S. history.

“It’s just an unmitigated disaster,” said Amy Bach, executive director of United Policyholders, a consumer advocacy group. “Wildfires in January? This just proves insurers’ point that the risk is so significantly increased due to climate change.”

State Farm, the state’s largest home insurer, announced in March it would not renew 72,000 property insurance policies, while Chubb and its subsidiaries stopped writing new high-value homes with higher wildfire risk — just to name two insurers that pulled back from the California market.

It's not clear how many homeowners in Pacific Palisades and elsewhere might not have had coverage, but at least some homeowners reported that insurers had not renewed their policies before the disaster struck. Actor James Woods, who lost his home in the Palisades fire, tweeted Tuesday that "one of the major insurances companies canceled all the policies in our neighborhood about four months ago."

State Farm last year told the Department of Insurance it would not renew 1,626 policies in Pacific Palisades when they expired, starting last July.

A spokesperson for State Farm declined to comment on the decision but said: "Our number one priority right now is the safety of our customers, agents and employees impacted by the fires and assisting our customers in the midst of this tragedy."

The situation has left many homeowners in neighborhoods at high wildfire risk with little choice but to seek relief from the California FAIR Plan, an insurer of last resort that sells policies with lesser coverage. The policies cover losses up to $3 million to a dwelling and its contents caused by certain hazards, such as fire, but do not include personal liability and other protection that are typically offered by private insurers.

The FAIR Plan has seen its policies grow from a little over 200,000 in September 2020 to more than 450,000 as of last September. That has roughly tripled its loss exposure to $458 billion over the same period. Pacific Palisades has one of the state's highest concentrations of FAIR Plan policy holders, with the insurer estimating its exposure in the neighborhood at $5.89 billion.

JP Morgan analysts estimate that total L.A. County losses could be close to $50 billion, while the losses insurers will have to pay could top $20 billion. Another estimate puts the losses even higher.

Such losses could cause insurers to exit the market completely, which Tokio Marine America Insurance Co. and Trans Pacific Insurance Co. said in April they would do in not renewing 12,556 homeowners.

The losses also could prompt insurers to further raise premiums, even though some insurers already have been granted big rate hikes, such as a 34% increase Allstate received last year.

Denise Rappmund, senior analyst at Moody's Ratings, said, "These events will continue to have widespread, negative impacts for the state's broader insurance market — increased recovery costs will likely drive up premiums and may reduce property insurance availability."

Should insurers further withdraw from the market, that would put additional pressure on the FAIR Plan, which is is backed by the state's licensed insurers, such as State Farm, who have to pay claims if they exceed the FAIR Plans reserves, reinsurance and catastrophe bonding. The insurers also can assess their own policyholders surcharges in the billions of dollars to bail out the plan under regulations put in place last year by Insurance Commissioner Ricardo Lara as part of his Sustainable Insurance Strategy to help the crippled market.

It's unclear whether the plan will be able to absorb the losses like it did after the 2018 Camp fire that destroyed the town of Paradise in North California. That conflagration was the single costliest natural disaster in the world that year with $12.5 billion in covered losses and $16.5 billion in total losses, according to the reinsurance firm, Munich RE.

"This further complicates an already complicated and hardened market," Lara said of the fires, in an interview with The Times.

Nonetheless, Lara's reforms seek to ensure the FAIR Plan remains solvent and to make it more attractive for insurers to write policies in fire risky neighborhoods now being absorbed by the program. He said the regulations should encourage insurers to write more homeowners policies, and if not, they can be adjusted. "I feel very confident," he said.

For the first time, California insurers can use so-called "catastrophe models" in setting their rates. Instead of largely relying on past claims data, the computer programs attempt to better refine an insurer's risk by taking into account a multitude of variables that affect a property's likelihood to suffer a loss.

The other major policy change allows insurers to charge California homeowners for the cost of reinsurance they buy from other insurers to limit their losses during huge catastrophes, such as wildfires and floods. This cost shift to policyholders is common elsewhere but a big change for California, where it will raise premiums.

In return for those concessions, insurers will have to write insurance in high-risk wildfire neighborhoods equivalent to 85% of their market share, meaning an insurer with a 10% statewide market share would have to cover 8.5% of the homes in such neighborhoods — a target they have at least two years to reach. Lara's plan has been blasted by the Los Angeles group, Consumer Watchdog, which says the regulations lack teeth in actually requiring insurers to meet the coverage goals.

"The Sustainable Insurance Strategy is not a magic wand. It's a set of incentives," Bach said. "At the end of the day, insurers are always still going to analyze, 'Are we going to make money here or not?'"

How much this week's fires will disrupt the already troubled insurance market depends, of course, on how big a disaster they are — but all indications are that insurers will have to absorb billions of dollars of claims given the number of homes destroyed, especially in the wealthy enclave of Pacific Palisades, where the average home is valued at about $3.5 million by Zillow.

Insurance industry experts say a clearer picture on the estimated losses will only come after adjusters have time to review submitted claims.

"I think it's going to be 45 days before we know what the true damage is," said Max Gilman, president of California personal lines at the brokerage HUB International.

Whatever the final cost, Gilman noted that the fires came after a couple of relatively light fire seasons — though in November the Mountain fire in Ventura County scorched more than some 20,640 acres and destroyed more than 130 homes amid parched conditions. That made it at the time the third most destructive fire in Southern California in a decade.

"I think what's currently transpiring is going to be of grave concern for the future," he said. "I feel like we we took three steps forward to take five steps back."

Denne Ritter, a vice president with the American Property Casualty Insurance Assn. trade group, said it is too early to assess the impact of the fires on Lara's reforms, especially given how they are just being put in place. Only one catastrophe model has been submitted for review to regulators, while the reinsurance regulation released last month still awaits final approval by the Office of Administrative Law.

"What the insurance industry wants is a healthy market in California where we can compete for business, as we have historically. And the number one priority right now is helping our customers get the resources they need to rebuild their lives and restore their property," she said.

However, she noted that Mercury Insurance — which recently announced it started writing insurance again in Paradise — and Farmers Insurance, which said last month it is increasing the number of new home policies it will write, have "certainly made moves indicating a more bullish approach on the market."

Allstate also has said it will resume writing new policies once Lara's reforms are in place and it can get rates that fully cover its costs.

But all those pronouncements came before this week's catastrophic fires.