Insurance Companies Say They're Not Allowed to Plan for the 'New Normal' of Intense Wildfires

Voice of San Diego

Insurance companies says state regulators aren't letting them plan for climate change and the so-called "new normal" of intense wildfires. They warn of price spikes and more people being denied coverage. Regulators worry the industry's models aren't credible, and could be manipulated to overcharge consumers.

Last year, the California insurance industry began to get cranky.

Pacific Gas & Electric's equipment had recently started or been suspected of starting several major wildfires, causing billions in damage and killing dozens of people. Afterward, the company argued the catastrophes were the result of climate change and were simply the "new normal."

Faced with overwhelming liabilities, PG&E began to float the idea of a bailout.

The bailout didn't happen and PG&E filed for bankruptcy. But, across the state, many people accepted PG&E's basic version of events: The world had changed, of course disaster is to be expected.

When Gov. Gavin Newsom announced a plan last week to help utilities cope with the losses triggered by the fires they help cause, he said climate change is the "new reality," so it's not a question of if but when there will be more fires.

But, so far, the insurance industry has felt left out and says state insurance regulators aren't letting them plan for climate change and the so-called "new normal." They warn of price spikes and more people being denied coverage.

Near the top of the industry's wish list is a wonky request: Let insurers set premiums based on the risk of fires that could burn someday soon.

Insurance is about sharing risk, of course, but also about collecting money now to pay for things that may happen in the future. Right now, insurance companies say they can't do that because of restrictions on how they set rates.

California home insurers are required to predict future losses based on losses that happened in the past, usually over the past 20 years. When the climate is changing, that doesn't make sense, the industry argues. If catastrophes become more frequent, the past will no longer tell us much about what will happen in the future.

"Are we in the new normal or not?" said Rex Frazier, the head of the Personal Insurance Federation of California, an industry trade group.

Since 10 of California's 20 biggest fires have happened in the past five years, rates are already rising quickly. But if there are going to be more costly fires, insurance companies and their customers will have trouble keeping up if fires keep getting worse.

The industry's solution is not new. Since the 1980s, insurers have used increasingly sophisticated computer models to prepare for hurricanes and earthquakes. The California Earthquake Authority, a government-run insurer, uses catastrophe models to set rates, as does a similar effort in Florida to provide hurricane insurance.

Private insurance companies already use models to make some decisions about where to write policies and whether some customers should pay more than others, but they can't use catastrophe models to set their overall rates.

Allison Castro, a spokeswoman for the state's Department of Insurance, said there hasn't been an instance yet where an insurer tried to use a model and was denied, but the department has a litany of concerns. Regulators worry the models aren't credible, and that they're a "black box" and could be used to overcharge consumers.

At their worst, the models could be used to manipulate the market to increase rates based on catastrophes that never happen.

Amy Bach, the executive director of United Policyholders, an industry watchdog, recently warned a state commission investigating wildfire risks that such insurance models were "vulnerable to having the dials shift to desired outcomes."

Harvey Rosenfield, the attorney who led the effort to pass Proposition 103, which reformed the insurance industry in the late-1980s, has the same worry.

"They want to go to a system where they hire a company nobody has ever heard of to crunch all the numbers in secret and then spit out a rate increase," he said.

At their best, the models could actually prevent rate spikes by allowing insurers to plan for disasters without clear precedent.

"In principle, the price charged for insurance the day after a catastrophe should not change, because the event was already included," one prominent catastrophe modeler, Robert Muir-Wood, wrote in a book on the insurance industry, "The Cure For Catastrophe."

While the California insurance industry sometimes calls catastrophe models "climate change modeling," the models don't try to predict future climate change, said Roger Grenier, the vice president of global resilience at AIR, one of the leading catastrophe modeling firms.

The company's models use historical weather data and look at what would happen if a fire strikes in a place where it hasn't happened in recent years. Because conditions for fire may be different now than in the past, the models account for a changing climate. But the main factor is actually people who live now in places they didn't use. Over 1 million homes are now in high-risk fire areas.

"You need a way to account for fires in areas where historically people haven't been living," Grenier said.

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