Why all California homeowners could be on the hook for LA County wildfire costs

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Insurance providers could charge policyholders a "supplemental fee" if the state's insurer of last resort runs out of money.

Once debris from the Los Angeles County wildfires is cleared and rebuilding begins, attention will likely shift to the financial health of a small, but growing California fire insurance provider.

The California FAIR Plan has an outsized share of the state's riskiest policies because it is the insurer of last resort for home and building owners who can't get coverage elsewhere.

If the FAIR Plan is unable to pay all of its claims, virtually every insured homeowner in the state could end up paying a portion of the LA County fire losses.

The nonprofit "Fair Access to Insurance Requirements" Plan is a private insurance pool created by the state, but operated jointly by fully licensed property and casualty insurance providers in the state. It provides insurance for fire damage only. Homeowners must seek additional liability, theft and other homeowner coverage from separate "wraparound" policies from private insurers.

Last week, the FAIR Plan disclosed that it covers about 22% of structures in the Palisades Fire zone and 12% of structures in the Eaton Fire area.

Potential exposure in the Palisades fire totals more than $4 billion, the FAIR Plan reported in an update Friday, Jan. 17. Its potential exposure in the Eaton fire is $775 million.

The FAIR Plan must pay the first $900 million in claims before tapping into back-up plans from "re-insurance" companies — essentially insurance for insurers. Re-insurance would pay the bulk of the next

$4.9 billion in claims, leaving the FAIR Plan responsible for all losses over $5.78 billion.

A spokesperson for the FAIR Plan declined to say how much money it has in reserves, nor would she confirm the New York Times' report that U.S. Sen. Alex Padilla's office said the plan had just $377 million as of Jan. 10.

"Data on the FAIR Plan's surplus is not publicly available," the spokeswoman said in an email. The FAIR Plan's "financial situation evolves daily. We continually monitor our financial position and whether we will need to tap into available payment mechanisms."

But if its reserves and re-insurance money are insufficient to cover all its claims, the state's licensed insurance companies must pitch in to cover the gap, each paying an amount based on its market share from two years ago. Those private insurers, in turn, would seek state approval to pass on those costs to their policyholders in the form of a "supplemental fee."

What is the likelihood of that happening?

"We just don't have the information yet because the FAIR Plan is still gathering information," said Rex Frazier, president of the Personal Insurance Federation of California.

It will be months, if not years, before the FAIR Plan must start paying claims for reconstruction, during which it will continue collecting monthly payments from policyholders, he said.

"So, the question is, how much money will they have when they start having significant outflows to pay for rebuilding, and would they run out?" Frazier said. "That's just a complicated calculation."

Amy Bach, executive director of the insurance consumer group, United Policyholders, worries that the need for a bailout, or an "assessment," could slow the FAIR Plan's payment process to fire victims.

"I am anxiously awaiting an announcement from the FAIR Plan about whether they're going to make an assessment and in what amount?" Bach said.

Another question on everybody's mind, Bach added, is will the carriers request approval to pass on their bailout costs to consumers and will the state insurance commissioner grant it.

If so, “what will that mean for their policyholders?” she asked.

Under new insurance regulations implemented last summer, home and building owners will be on the hook for half of the first $2 billion in bailout money — $500 million for damages to homes and $500 million for damages to commercial structures like restaurants, supermarkets and office buildings .

Should bailout costs go even higher, consumers would be on the hook for “all amounts” private insurers pay over $2 billion.

Such financial rescues are rare. The last time the FAIR Plan ran out of money was after the 1994 Northridge earthquake.

Meanwhile, in Sacramento two Southern Californian legislators introduced a bill that could avert such a bailout. Assembly Bill 226, introduced two days after the fires began, would allow the FAIR Plan to seek bonds to increase its “liquidity and claims-paying capacity.”

“The loss in Southern California is inconceivable,” Assemblymember Lisa Calderon, D-Whittier, said in a statement. “AB 226 will alleviate some of the uncertainty that FAIR Plan policyholders may encounter as a result of this tragedy.”

Exposure does not equal loss, the FAIR Plan update said. History shows that current claims have averaged about 31% of total exposure.

“Some fires are substantially higher or substantially lower than this historical benchmark,” the update said.

But the toll is rising.

On Thursday, Irvine-based data firm CoreLogic upgraded its estimate of losses from the Los Angeles wildfires to $35 billion to $45 billion.

“The situation is ongoing and remains fluid,” the FAIR Plan said.

The FAIR Plan accounts for only about 3% of all policies in the state, but its share has been mushrooming in the past few years as private insurers began limiting their coverage and canceling homeowner policies in California.

Since September 2020, the FAIR Plan’s total exposure tripled to $458 billion, according to the organization’s website.

In the two main ZIP codes covering the Palisades fire, the FAIR Plan’s exposure jumped 74% since September 2020 to 3,416 policies, FAIR Plan figures show.

In the ZIP code covering Altadena, the number of policies rose 42% to 963 policies in the past four years.

CoreLogic’s loss estimates include smoke and fire damage for both residential and commercial properties, as well as increased rebuilding costs caused by demand surge, debris removal, clean up and temporary living expenses, the company said in a statement.

The majority of losses are to residential properties. Many of the potentially affected properties are high value homes, CoreLogic’s statement said.

“The destruction caused by these fires is anticipated to be the most expensive in the state’s history, with effects on the insurance industry that will persist into the future,” said Tom Larsen, Senior Director of CoreLogic Insurance Solutions.