Connecticut Debate Association
February 1st, 2025
Coginchaug High School and Fitch High School

THBT the US Federal Government should provide a national financial support program for property insurance risk.

Insurance

From Wikipedia, the free encyclopedia

Insurance is a means of protection from financial loss in which, in exchange for a fee, a party agrees to compensate another party in the event of a certain loss, damage, or injury. It is a form of risk management, primarily used to protect against the risk of a contingent or uncertain loss.

Insurability

Insurability can mean either whether a particular type of loss (risk) can be insured in theory,[1] or whether a particular client is insurable for by a particular company because of particular circumstance and the quality assigned by an insurance provider pertaining to the risk that a given client would have.[2]

Characteristics of insurable risks

Risks that can be insured by private companies typically share seven common characteristics.[4]

1. Large number of similar exposure units. Since insurance operates through pooling resources, the majority of insurance policies are provided for individual members of large classes, allowing insurers to benefit from the law of large numbers in which predicted losses are similar to the actual losses…
2. Definite Loss. The loss takes place at a known time, in a known place, and from a known cause.
3. Accidental Loss. The event that constitutes the trigger of a claim should be fortuitous, or at least outside the control of the beneficiary of the insurance…
4. Large Loss. The size of the loss must be meaningful from the perspective of the insured. Insurance premiums need to cover both the expected cost of losses, plus the cost of issuing and administering the policy, adjusting losses, and supplying the capital needed to reasonably assure that the insurer will be able to pay claims…
5. Affordable Premium. If the likelihood of an insured event is so high, or the cost of the event so large, that the resulting premium is large relative to the amount of protection offered, it is not likely that anyone will buy insurance, even if on offer…
6. Calculable Loss. There are two elements that must be at least estimable, if not formally calculable: the probability of loss, and the attendant cost. Probability of loss is generally an empirical exercise, while cost has more to do with the ability of a reasonable person in possession of a copy of the insurance policy and a proof of loss associated with a claim presented under that policy to make a reasonably definite and objective evaluation of the amount of the loss recoverable as a result of the claim.
7. Limited risk of catastrophically large losses. Insurable losses are ideally independent and non-catastrophic, meaning that the losses do not happen all at once and individual losses are not severe enough to bankrupt the insurer; insurers may prefer to limit their exposure to a loss from a single event to some small portion of their capital base, on the order of 5 percent. Capital constrains insurers' ability to sell earthquake insurance as well as wind insurance in hurricane zones. In the U.S., flood risk is insured by the federal government.

Hurricanes Milton and Helene showed the problem of insurance and moral hazard. Here's how to fix it

Quartz, By Peter Green, October 14, 2024 (Abridged for concision.)

At some point the feds must stop bailing out people who build homes and factories in the path of disasters.

Hurricane Milton has blown through and the worst is over for Florida. But it’s not over for everyone. Meteorologists warn we’ll get stronger and more frequent tropical storms in the coming years, as the oceans warm and sea levels rise thanks to climate change.

Let’s talk about one reason these storms keep causing so much damage — and how we might solve the problem.

Moral hazard

There’s a term that economists like to use: moral hazard. It refers to the practice of creating financial incentives that promote risky behavior. Last week, those incentives for risky economic behavior were on full view as Hurricane Helene and then Hurricane Milton slammed into the southern U.S. Surging tides and 120-mile-an-hour winds ripped the roofs off homes and businesses (and even the Tampa Bay Rays baseball stadium), flooding everything within

range of the coast and racking up damage estimated to be well over $100 billion.
It's not the first time coastal Florida has been devastated by violent storms, and meteorologists, climate scientists, and insurance risk advisors say it's a dead certainty that it will happen again — and with increasing frequency. So why are residents and businesses rebuilding, time after time, in the same places that were destroyed the last time around?

Insurance

The answer, people who have studied the problem say, is insurance. Even as private insurers flee hurricane zones or raise premiums and lower coverage limits, the federal government, and to a lesser degree the state of Florida, remain as the insurers of last resort — paying out claims to people whose homes were washed away and businesses that were flooded out. Programs like the National Flood Insurance Program, managed by the much-maligned Federal Emergency Management Agency, the Small Business Administration, and numerous other government programs hand out cash. The federal departments of Transportation, Housing and Urban Development, and Interior, as well as organizations like the Army Corps of Engineers and the federal Highway Trust Fund, along with state and local government, help to rebuild devastated infrastructure…

A possible solution

Some insurance experts and climate watchers do see a way out of the problem: Create a federally-backed national fund to insure against climate disasters of every kind, and carefully manage the risks it underwrites.
It's not that the market has failed, forcing government to step in, it's that private insurers are doing what they should be doing: If they can't sell insurance at the rates they need to accommodate risk, they pull out of markets.
Cliff Rossi, a former head of global consumer risk management risk at Citi, is a leading advocate for a national climate risk insurer that would be chartered by the federal government — much like mortgage insurers Fannie Mae and Freddie Mac, which are known as government-sponsored entities, or GSEs.
Rossi, now Director of the Smith Enterprise Risk Consortium at the University of Maryland's business school, said that anyone whose mortgage is guaranteed through Freddie or Fannie is already required to have flood insurance if their property is in a designated flood plain.
The current system, Rossi said, is flawed. "It does incentivize folks to continue to reside in these very critical areas that are increasingly exposed to [severe] storms," he said. "We have to rethink the approach to who is allowed to have insurance."
Denying government-backed insurance to second homes, requiring adherence to strict building codes, and limiting the amount of money that can be paid out on any one claim would limit both the damage and the cost of cleaning up and rebuilding.
State-funded insurance programs aimed at disaster recovery, like Florida's Citizens insurance, a not-for-profit insurer of last resort with 1.26 million policies in force, have been running out of cash, Rossi noted. "If you're concentrating on just homeowners in the state of Florida, you've concentrated risk to such a level that it makes it extremely expensive," he said.

A national natural hazard insurance company?

That's where Rossi's Federal Natural Hazard Insurance Corporation comes in. As a GSE, the insurer would package its credit risk, much like Fannie and Freddie package their mortgage risk, and resell it on the private market. His plan would absorb FEMA's National Flood Insurance Program, too.
"It would be part of this new federal agency that would be staffed with actuaries and scientists who are better able to qualify and price out the risk associated with all kinds of climate risk, including drought, wildfires, earthquakes as well as storms and flooding," Rossi said. The company would then repackage its risk and sell it.
This would solve the problem of private insurers backing away from climate-related risk because of the uncertainty involved in estimating that risk. But by having an entity dedicated to the task of pricing climate risk and insuring against it, and having the federal government — backed by the U.S. Treasury — as the ultimate guarantor, the risk would be reduced to the point that businesses could rely on the insurance to be affordable and comprehensive. And the stricter qualifying requirements for the insurance would reduce the incentives for locating or rebuilding in the wrong spot.
Rossi has spent time with large insurance companies, state governments, and federal officials developing his plan. All the players seem enthusiastic, he said, but there's only one problem: Congress. A new GSE would need Congress to approve its charter, and in a divided government that's unlikely to happen.
"It's going to take more of those back-to-back category 4 or 5 storms coming through," Rossi said. "And at some point that will be the catalyst for some sort of major intervention."

Home insurance rates are rising due to climate change. What could break that cycle?

NPR, July 23, 2024

Home ownership can be daunting, but there is an order that things tend to follow:

1. If you're the average American looking to buy a home, you need a mortgage.
2. And in order to get a mortgage, you need homeowners' insurance.

But what happens to homeowners if an insurance company decides it doesn't want to do business where they live anymore? For Beth Pratt, who lives outside Yosemite National Park in California, that question has become a reality.

"I just got a letter, not even a 'Hey, we want these things done.' It was, 'We're not renewing you,'" she told NPR last year

Her insurer of 31 years said the fire risk in her area was too great, and simply declined to cover her anymore.

"These are not luxury items for myself or others," Pratt said. "You have to have insurance. So I think that policies and how we insure people probably has to change."

Increasing premiums

Even if private insurance companies stop short of pulling out of a high-risk region, they're often raising premiums. In many instances, they say that's to cover the increasing losses from weather-related property damage.

Nationwide, home insurance costs are up 21% since 2015, according to a 2021 LexisNexis trend report.

It's even more in areas like hurricane-prone Florida, where insurance costs more than 3.5 times the national average last year. Costs aren't projected to go down anytime soon either: climate change is making storms and wildfires more intense, and more destructive.

Last year, the U.S. had a record 28 disasters that cost more than a billion dollars in damage.

In a Senate Budget Committee hearing last month, chairman Sheldon Whitehouse (D-RI), compared the state of home insurance today to another recent housing market disaster.

"This all sounds eerily reminiscent of the run-up to the mortgage meltdown of 2008," he said.

Addressing the future

This month, the U.S. Department of Housing and Urban development held a summit to address the spike in home insurance costs.

Acting HUD Secretary Adrianne Todman spoke with *Consider This* host Ari Shapiro about what her department can do to resolve this crisis. Todman says that her main concern lies in how these changing rates will impact housing stability for all types of people.

"We have first-time homeowners who are unable to purchase a home because of the unexpected cost of insurance. We have some of our existing affordable housing providers seeing their insurance costs go up by levels they've never seen before," Todman said. "And they're having to make some financial decisions about what they invest in."

That leaves some affordable housing providers considering whether they can make necessary repairs or keep their existing staff, she said, adding: "None of that is ever good for tenants."

And while there is now increased risk for insurance providers, Todman says that the rates that premiums have increased don't seem to add up.

"It is rather curious, the level of the increase that happens even year over year. Something else that's rather curious is where the increases are occurring. I'm hearing ... from some of our affordable housing providers that some of the insurance increase may be happening in certain types of their housing portfolio, but not all part of their housing portfolio."

So, could this be another case of companies taking advantage of climate inflation to gouge prices? Todman says it's possible, but there isn't enough existing data to say so definitively.

"We don't have the data holistically — or at the micro level, at the neighborhood level — to know, are insurers doing that? Some people will say, 'Yes, that's exactly what they're doing,' but we don't have the data yet to suggest that," she said, adding that gathering that data is one purpose for this month's summit

This episode was produced by Kathryn Fink and Rebecca Hersher. It was edited by Patrick Jarenwattananon and Neela Banerjee. Our executive producer is Sami Yenigun.

We Have to Stop Underwriting People Who Move to Climate Danger Zones

New York Times, By Parinitha R. Sastry and Ishita Sen, January 16, 2025

Fires are still raging across Los Angeles in what is shaping up to be one of the most expensive calamities on American soil, with estimates of the economic damage and losses running as high as $275 billion. Thousands of residents have lost their homes, which are often their most valuable asset.

Yet there are few signs that policymakers and regulators are grappling with the decisions that brought so many people into high- risk areas to begin with. Their refusal to do so sets the stage for an even bigger, and potentially deadlier and even more expensive disaster down the line.

Financial markets, if left to their own devices, would naturally force Americans to confront the ugly realities of our changing climate and deter them from flocking to places where human habitation is increasingly untenable.

Unfortunately, this basic system of supply and demand has been stymied by regional and federal policies — policies supported by both Democratic and Republican lawmakers in both blue and red states who buckle under the short-term political pressure to keep home insurance premiums artificially low.

The result is highly unfair and distorts the market. It endangers our economy by sending scarce resources into the path of natural disasters and will likely devastate still more lives.

In theory, insurance prices quantify the risks of living in a certain place. Of course it should be more expensive to insure a home in an area buffeted by disaster. But in practice, states vary widely in their willingness to allow insurance premiums to increase, with some making it far harder than others for insurers to raise prices. California is one of the most resistant, and until recently refused to let insurers raise premiums or reflect climate-catastrophe risks in their pricing.

Insurers doing business in such heavily regulated states, finding themselves unable to raise premiums when needed, wind up shifting some of the costs to homeowners who happen to live in states that are more accommodating to premium increases. That is, in part, how middle-class communities, such as Enid, Okla., can end up subsidizing the owners of million-dollar houses in Malibu. And under our current regulatory regime, that dynamic is only expected to strengthen, as climate losses continue to cut into insurance companies' bottom line.

The voices loudly criticizing California for its rigid control of insurance pricing are ignoring numerous similar examples from the rest of the country. In 2023, after the federal flood insurance program began to adjust its premiums to better reflect climate realities, 10 states across the political spectrum — including reliably red Louisiana, Florida and Texas and moderate blue Virginia — sued the program. And California isn't the only state that failed to raise premiums to properly fund its FAIR plan, the state-sponsored insurer of last resort often relied on by those living in climate-vulnerable areas; Florida did as well.

Home insurance is just one way our financial system encourages Americans to move to flood-prone sections of Florida or parched, air-conditioning-dependent Arizona. The government mortgage giants Fannie Mae and Freddie Mac, which guarantee about 70 percent of mortgages on single-family homes, charge the same fees regardless of climate risk. Nobody intends to move into harm's way. Many people settle in places like Texas because housing is generally more affordable. But that affordability is a mirage: Their mortgage and insurance risks are being subsidized by everyone else. This system, and the continually building in risky areas, portends ever-rising disaster losses.

We get why change is hard. Losing one's home can be economically and emotionally devastating. Rising insurance premiums can stress homeowners who are already struggling. For households that have their entire life savings tied to their home, hefty premiums combined with lower home values tied to the cost of insurance could even lead them to default on their mortgage.

That may explain why a growing number of households living in imperiled areas are not only taking on more debt to pay for higher premiums, they are reducing coverage altogether, leaving them dangerously exposed to disasters.

Regulators can and should monitor insurers so they don't use their market power to charge excessive rates. But we are at the other extreme in many high-risk areas: At some point, regulators will have to allow prices to go up so insurers remain solvent and private insurance stays available, even in places hard hit by climate change. The longer they delay, the larger and more disruptive the price increases will be.

Premiums in Florida nearly doubled from 2018 to 2023. And by the time premiums catch up to risks, more households will have moved to dangerous areas, lured by artificially low prices that mask the true cost, and sunk their life savings into their homes. It is pain now versus even more pain later. But eventually, once prices reflect risks, incentives will rebalance, and people will be discouraged from migrating to and building in disaster-prone areas.

For state and federal policymakers, the question they must face is not whether we should move to insurance pricing that reflects risks, but how.

The federal flood insurance program can point to an approach. From 2021 to 2023, the program phased in risk-based pricing. Policies for new customers were adjusted first. Existing customers in high-risk areas have a much longer adjustment period. This gives households information and time to adjust to the new pricing regime.

If climate change creates more frequent, intense and correlated disasters, insurers may continue to leave high-risk areas, even with risk-based pricing. If so, the government could step in, by creating, say, a federal reinsurance backstop. If policymakers choose to go in this direction, it is paramount for this coverage to be priced correctly. Otherwise, we risk adding yet another implicit subsidy for disaster-prone areas.

We don't have to live this way. Our policies were designed for a world where the gap between high- and low-risk areas was smaller and less persistent. But these gaps have been growing rapidly. And the longer we wait, the more we, and our society, will suffer.

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'Bluelining' leaves climate vulnerable communities without home insurance

Counterpunch, by Jessica Garcia May 20, 2024

In an era of climate disasters, Americans in vulnerable regions will need to rely more than ever on their home insurance. But as floods, wildfires and severe storms become more common, a troubling practice known as "bluelining" threatens to leave many communities unable to afford insurance — or obtain it at any price.

Bluelining is an insidious practice with similarities to redlining — the notorious government-sanctioned practice of financial institutions denying mortgages and credit to Black and brown communities, which were often marked by red lines on maps.

These days, financial institutions are now drawing "blue lines" around many of these same communities, restricting services such as insurance based on environmental risks. Even worse, many of those same institutions are bankrolling those risks by funding and insuring the fossil fuel industry.

Originally, bluelining referred to blue-water flood risks, but it now includes other climate-related disasters such as wildfires, hurricanes and severe thunderstorms, all of which are driving private-sector decisions. (Severe thunderstorms, in fact, were responsible for about 61% of insured natural catastrophe losses in 2023.)

In the case of property insurance, we're already seeing insurers pull out of entire states such as California and Florida. The financial impacts of these decisions are considerable for everyone they affect, and often fall hardest on those in low-income and historically disadvantaged communities.

A Redfin study from 2021 illustrated that areas previously affected by redlining are now also those prone to flooding and higher temperatures, a problem compounded by poor infrastructure that fails to mitigate these risks. This overlap is not a coincidence but a further consequence of systemic discrimination and disinvestment.

This financial problem exists no matter where you live. In 2024, the national average home insurance cost rose about 23% above the cost of similar coverage last year. Homeowners across more and more states are left grappling with soaring premiums or no insurance options at all. And the lack of federal oversight means there is little uniformity or coordination in addressing these retreats.

This situation will demand a radical rethink of how we approach investing in our communities based on climate risks. For one thing, financial institutions must pivot from funding fossil fuel expansion to investing in renewable energy, natural climate solutions and climate resilience, including infrastructure upgrades.

What about communities in especially vulnerable areas?

One strategy is community-driven relocation and managed retreat. By relocating communities to low-risk areas, we not only safeguard them against immediate physical dangers but also against ensuing financial hardships.

Additionally, preventing development in known high-risk areas can significantly decrease financial instability and economic losses from future disasters.

As part of this strategic shift, financial policies must be realigned. We need regulations that compel financial institutions to manage and mitigate financial risk to the system and to consumers. We also need them to invest in affordable housing development that is energy-efficient, climate-resilient and located in areas less susceptible to climate change in the mid- to long-term.

Meanwhile, green infrastructure and stricter energy efficiency and other resilience-related building codes can serve as bulwarks against extreme temperatures and weather events.

The challenge of bluelining offers us an opportunity to forge a path toward a more resilient and equitable society. We owe it to the future generations to do more than just adapt to climate change. We also need to confront and overhaul the systems that harm our climate. The communities most exposed to climate change deserve no less.

Jessica Garcia is a senior policy analyst for climate finance at Americans for Financial Reform Education Fund. This was originally published and distributed by OtherWords.org and is reprinted with permission.

The World Is Getting Riskier. Americans Don't Want to Pay for It.

The Wall Street Journal, Greg Ip, Jan. 19, 2025

Insurance is one of finance's great gifts to mankind. Through the statistical magic of risk pooling, an individual can obtain peace of mind and protection against devastating loss.

This remarkable invention shows signs of breaking down. As risks from illness and old age to natural and financial disaster grow, so does Americans' resistance to paying to insure against them.

The latest example is California. Earlier this month, JPMorgan estimated the fires around Los Angeles had inflicted $50 billion in losses, of which only $20 billion were insured.

One reason for the gap: State regulators have prevented insurers from charging premiums commensurate with rising property values, construction costs and wildfire risk exacerbated by a warming climate. Many thus stopped renewing policies.

Hundreds of thousands of homeowners shifted to California's state-run backstop, the Fair Plan, whose exposure has tripled since 2020 to $458 billion. It has only $2.5 billion in reinsurance and $200 million in cash.

If the Fair Plan runs out of money, it can impose an assessment on private insurers to be partly passed on to all policyholders. In other words, the costs of the disaster will be socialized.

California is a microcosm of what happens when insurance breaks down: Either households face potential ruin or the public is handed a financial time bomb.

“What we are seeing is a real disconnect,” said Carolyn Kousky, an economist specializing in risk and founder of the nonprofit Insurance For Good. “There are opposing views on insurance: Is it a private market good, or is it social protection, to make sure everyone has the resources to recover from disaster?”

A central feature of insurance is risk pooling: The combined contributions of the community cover the losses incurred by members of the community in a given year.

Another feature of private insurance is actuarial rate-making, that is, calibrating premiums to the customer’s risk. That’s to prevent “adverse selection,” in which only the riskiest people buy insurance, and moral hazard—the tendency to encourage risk by undercharging for it.

But some activities or individuals are so risky they could never obtain, or afford, private insurance. That’s when risk gets socialized. The federal government’s expansion since the 1930s has largely been through the provision of insurance: Social Security, unemployment insurance, health insurance for the elderly and poor, deposit, mortgage, and flood insurance and, after Sept. 11, 2001, terrorism insurance. Not for nothing is the federal government often called an insurance company with an army.

The Luigi Factor

Nowhere are feelings about insurance more conflicted than in health. Americans want neither the rationing that comes with government-run insurance, nor the risk-management that comes with private insurance. This became painfully apparent when the fatal shooting of Brian Thompson, chief executive of UnitedHealthcare, triggered an outpouring of fury not at the suspected killer, Luigi Mangione, but at insurers for limiting benefits, such as by requiring prior authorization for care.

In fact, long before that shooting, the Affordable Care Act had constrained insurers’ ability to base premiums on risk, by prohibiting them from charging more to people with pre-existing conditions or denying coverage altogether. The ACA also stipulated that insurers spend at least 80% to 85% (depending on the plan) of premiums on benefits. So while denials, deductibles and copays may, at the margin, affect profits, ultimately they serve to control premiums.

In finance, where risk supposedly goes hand in hand with reward, losses have been repeatedly socialized, most notably when major financial institutions were bailed out in 2008.

Deposit insurance, on paper, is capped at $250,000. Depositors with more are supposed to be careful where they keep their money. But in 2023, the Federal Deposit Insurance Corp. bailed out all the uninsured depositors of Silicon Valley Bank and Signature Bank. The costs are being socialized via a special assessment on other banks’ uninsured deposits.

What financial disaster was to the last era, natural disaster may be to the next. In a World Economic Forum survey, business, government and other leaders ranked extreme weather the most severe of 33 risks facing the world in the next 10 years. Major disasters pose a particular problem for insurers because claims occur all at once instead of randomly.

And as with financial disasters, the cost of natural disasters is being socialized. Numerous states have backstops for homeowners unable to get private insurance, and all struggle to charge premiums that reflect actual risk.

In a 2023 study for California insurers, Nancy Watkins, an actuary with Milliman, an insurance consultancy, found that plans in California, Washington, Louisiana and Florida, which had doubled in size between 2017 and 2022, all incurred more in losses and expense than they took in through premiums.

In Florida, frequent storms, flood-plain development, inflation, fraud and litigation have pushed home-insurance premiums to the highest in the country. Yet insurers were “discouraged from large rate hikes by public hearings, documentation requirements, and their own customers and agents,” Kousky and a co-author wrote last year. In years past, some insurers pulled back, or became insolvent.

As in California, Florida homeowners flocked to the government backstop, Citizens Property Insurance. Like California, Florida has taken steps to make its insurance market financially viable. It has cracked down on litigation and allowed Citizens to raise premiums. Nonetheless, Citizens last year said premiums are 22% below the actuarially sound level.

Kousky said in the event of a series of major storms, Florida’s three insurance backstops—Citizens; a reinsurance fund; and guaranty program for insolvent insurers—could struggle to borrow enough to pay claims, triggering demands for a state or federal rescue.

Taxpayers nationwide are also on the hook. Since 2020, Congress has appropriated an average of $46 billion per year for disaster relief, triple the average of the prior decade (in constant 2023 dollars). Late last year, Congress rushed through $100 billion in aid for disasters including hurricanes Helene and Milton.

Socializing risk weakens one of the main benefits of insurance: Encouraging the insured to mitigate their risk so as to reduce premiums. Without that price signal, it usually takes direct intervention to modify behavior. After being bailed out in 2008-09, banks have had to submit to far more stringent safety and soundness rules.

The same may be true of natural disasters. If the risk is to be socialized, society has a right to demand the insured mitigate their risk, such as making homes more flood, wind and fire proof or staying out of disaster-prone areas entirely.

"It involves alignment of ordinances, building codes, enforcement, inspection, and finding resources for…communities and homeowners who really can't afford" such measures, Watkins said. "All that is politically difficult. But it's becoming increasingly obvious the old strategy, of denying the risk, has failed."

California's FAIR Plan, the home insurer of last resort, may need a bailout after the L.A. fires

Los Angeles Times, by Laurence Darmiento January 18, 2025 (Abridged for concission.)

- The huge costs of the historic Los Angeles fires could force a bailout of the state's insurer of last resort, which has just $377 million in reserves and additional reinsurance.
- To remain solvent, California's Fair Plan may turn to its member insurers for financial help and prompt them to levy surcharges on policyholders.

The California FAIR Plan Assn., the state's property insurer of last resort, was born of smoldering ashes — not of a wildfire, but of one of the worst urban disturbances in U.S. history.

The Watts riots in 1965 damaged or destroyed more than 600 buildings, causing insurers to flee and highlighting the need for a new type of carrier to step in.

Established by the Legislature to also cover communities at risk for wildfires, the plan has proved resilient, paying out billions of dollars over the decades, including after the 2018 Camp fire that destroyed the town of Paradise and cost insurers $12.5 billion.

Now, however, the FAIR Plan is facing its biggest crisis since the 1994 Northridge earthquake, when it was bailed out by the state's licensed property insurance companies, which operate the plan and provide it with a financial backstop.

The temblor caused some $15.3 billion in insured losses for the industry, or roughly $33 billion adjusted for inflation. But even after inflation, the Palisades and San Gabriel Valley's Eaton fires alone are expected to be costlier.

CoreLogic, a leading property data and analytics firm, estimates the losses of those fires at $35 billion to $45 billion, not including the other smaller blazes that broke out. The fires have damaged or destroyed more than 12,000 structures and killed at least 27 people. Many homeowners in the fire zones were on the FAIR Plan after insurers pulled back from California's troubled insurance market.

Forking over billions of dollars could wipe out the plan's $377 million in reserves, as well as $5.78 billion worth of reinsurance the FAIR Plan announced Friday it had. The reinsurance requires the plan to pay the first $900 million in claims and has other limitations…

It's unclear what the FAIR Plan's final bill will total, but its statewide exposure to financial losses has tripled to $458 billion over the last several years, according to the plan's website. During that time, hundreds of thousands of homeowners, especially in foothills and other neighborhoods at high risk for fires, have piled into the plan as insurers have pulled back from the market over growing wildfire losses.

Based on preliminary estimates released Friday, the plan said that it has insured 22% of the structures within the Palisades fire zone as defined by the state Department of Forestry and Fire Protection, giving it a potential loss exposure of more than $4 billion. And it has insured 12% of the structures in the Eaton fire zone, giving it a potential exposure there of more than $775 million…

Jewlz Fahn and her husband, Terry, signed up for the FAIR Plan last year after State Farm, which had insured them for more than a decade, did not renew the fire, personal property and loss-of-use coverage they had for their home on Fiske Street, which burned down near the heart of Pacific Palisades.

They were able to get similar coverage for their dwelling — a little under $2 million — but their personal property coverage was slashed from $1.55 million to $153,000 and their loss-of-use insurance, which will cover their living expenses while their home is rebuilt, also dropped sharply from $620,160 to $153,000. More frustrating, Fahn said, has been the inability to get a timely payment for living expenses.

"I just finally got a phone call Wednesday from my claims manager — eight days after the fire started. They are very overwhelmed. I was trying to keep my cool, and I was told that they are trying to give an advance of a six-month payment, which for us would be a total of $52,038," said Fahn, 52, who has been living in a Century City hotel with her husband.

In contrast, she said, a friend received a $75,000 payment within days of the fire from her commercial carrier.

…
Consumer Watchdog — which wrote the 1988 ballot measure that provided for an elected insurance commissioner with the authority to review and turn down insurer rate requests — called the provision an industry bailout last year. The group said existing law did not allow for the surcharges. Lara maintained it did and said he was offering consumers some protection.
“For us, it’s pretty simple. Homeowners across the state should not be on the hook for the L.A. fires because insurance companies abandoned those neighborhoods and dumped homeowners on the FAIR Plan,” said Carmen Balber, executive director of the Los Angeles consumer group…
The idea that millions of Californians who live nowhere near the Los Angeles County fires could face surcharges on homeowner policies — that in some instances already have risen by hundreds or thousands of dollars over the last several years — has sent lawmakers in Sacramento scrambling for an alternative.
Just two days after the Palisades fire began, legislators introduced a bill that would allow the FAIR Plan to float bonds if the insurer faces “liquidity challenges.” The FAIR Plan said it supports the bill.
“The most important question for us right now is: ‘How can we help?’” Assembly Speaker Robert Rivas said in unveiling the legislation sponsored by two Southern California lawmakers.
A spokesperson for Gov. Gavin Newsom said, “The climate crisis has changed everything” and that the governor and insurance commissioner were still trying to assess the effects of the fires on the plan but would be “vigilant as the FAIR Plan explores the options they have to make sure impacted Californians have their claims paid.”
Jones, the former insurance commissioner, is dubious that floating potentially billions of dollars of tax-free bonds to pay claims will solve the crisis, although they would be very helpful in making sure there is money available to pay FAIR Plan claims.
“Bonds will help them pay off the claims as they come in, but they have got to be able to pay off the bonds. And the only way they’re going to be able to pay off the bonds is with an assessment if they run out of money,” he said. “Bonds are not a magic wand.”
Times staff writer Ben Poston contributed to this report.

Hurricanes, Flooded Homes, and Moral Hazard

Real Clear Policy, By Bruce Yandle, June 14, 2018 (Abridged for concission)

With heavy rainfall having brought severe flooding to Maryland and other areas along the Atlantic and Gulf Coasts and the 2018 hurricane season just getting underway, it’s a good time to remember that the United States suffers from more than just weather patterns. In some situations, our flood insurance system encourages people to live where the risk is greatest. The worst part of it? We know better.
Of those hurricanes that eventually make landfall, according to Yale University economist Robert Mendelsohn, only some 4 percent actually hit the United States.
How could that be? What is it about us that causes disproportionate damage in our otherwise-prosperous corner of the world? And why hasn’t our government fixed an obvious problem?
Put in insurance economics jargon, the problem is called “moral hazard.” This is a situation where the solution to a hazard can the problem worse. Fire insurance provides an easy illustration: If insurance companies wrote policies covering 100 percent of losses from fire, there would be a significant incentive for some people to buy a policy today and set fire to their home tomorrow.
Through centuries of experience, fire insurance companies have learned to require policy owners to bear part of the risk. Policies now commonly cover around 80 percent, and homeowners co-insure. Unfortunately, Uncle Sam has only partially taken this lesson to heart when trying to help homeowners in flood-prone areas.
Federal law requires anyone purchasing a home in a designated flood area using financing from a federally insured and regulated lender to buy flood plain insurance through the Federal Emergency Management Agency (FEMA). Instead of charging insurance premiums that cover the expected cost of floods, FEMA offers partly subsidized insurance; the government discount can be huge. Moral hazard knocks at the door. In 2015, there were 5.1 million policies in force….
Understandably, homeowners who hold highly subsidized insurance do all they can to keep it. That can mean avoiding selling a property or choosing to rebuild in the same place even after suffering severe damage from a storm. In short, it means some people have a strong incentive to continue to live in flood-prone areas.
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