Date: March 16, 2022

To: Honorable Susan Rubio, Chair
Honorable Brian W. Jones, Vice Chair
Members, Senate Insurance Committee

From: Rex D. Frazier, President
Seren Taylor, Senior Legislative Advocate
Allison Adey, Legislative Advocate

RE: Senate Insurance Committee Informational Hearing:
WILDFIRE RESILIENCE: INNOVATION IN MITIGATION

Dear Senator Rubio (Chair) and Members,

The Personal Insurance Federation of California (PIFC) offers the following comments regarding initiatives and innovations aimed at increasing resiliency to wildfire and growing the availability of homeowners' insurance in high wildfire-risk regions.

Of the 20 most destructive wildfires in California's recorded history, 13 have occurred since 2017. Together, these 13 fires caused tremendous damage, destroying nearly 40,000 structures, taking 148 lives, and charring millions of acres. In particular, the 2017 and 2018 wildfire seasons were the most destructive and costly in California history. It is estimated that the 2017 and 2018 wildfire seasons wiped out about two times the combined underwriting profits for California homeowners' insurers for the prior 26 years.[1]

Several factors have led to the increase in wildfire events over the past few years. Climate change along with population shift toward the wildland-urban interface (WUI) areas have contributed to an increase in the impacts of wildfires. More focus is being placed on ways that consumers can prevent or mitigate damages to their homes when these events occur. Mitigation and prevention measures, both on an individual and community basis, have been shown to reduce wildfire risk substantially.

The speed and pace of advancement in mitigation science and the development of sophisticated wildfire risk models is striking. Prior to 2017-18, wildfires were not typically considered to be catastrophic risks that required the complex predictive modeling techniques that are used for primary perils like hurricanes. Similarly, while the science of hurricane protection evolved significantly from 1996-2005, the study of wildfire mitigation for homes and communities has only recently become a top priority for the public and private sectors.

<u>Science-based Mitigation Actions</u>

On February 14, 2022, Insurance Commissioner Ricardo Lara and emergency

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Eric Xu, Cody Webb, David D. Evans. Wildfire catastrophe models could spark the chances California needs. *Milliman (2019).*

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management leaders in Governor Gavin Newsom's Administration announced "Safer from Wildfires," a new insurance framework that provides a list of mitigation actions to reduce risk for property owners, including community-wide safety recommendations to prevent the spread of wildfire to other properties. We are appreciative that this inter-agency workgroup met with PIFC and the Insurance Institute for Business & Home Safety (IBHS), among other stakeholders, to incorporate broad expertise for the new framework.

Although there are some notable differences, the "Safer from Wildfires" framework seems largely consistent with the recent research by IBHS, which is reflected in their new *Wildfire Prepared Home*™ program. This IBHS program incorporates available wildfire science, building performance characteristics, data analytics insights, and contributions from a diverse group of wildfire leaders to address wildfire risk with the latest science.

Taken together as a set of requirements, these clearly defined mitigation actions will allow the wildfire resilience of a property to be meaningfully distinguished from unmitigated or partially mitigated properties and can result in a *Wildfire Prepared Home* designation. It is important to note that, given the dynamic nature of vegetation, terrain, and other fuels on properties and surrounding areas, some mitigation elements will require consistent and recurring maintenance to ensure risk remains reduced.

Some differences exist between the "Safer from Wildfires" framework and the IBHS' *Wildfire Prepared Home*. For example, while the framework includes clearing the underdeck of debris, it does not require enclosing the underdeck (as required by *Wildfire Prepared Home*). In some cases, the *Wildfire Prepared Home* requirements on defensible space may go beyond the framework.

Another important feature of the IBHS program is that it will provide homeowners with a pathway to meet and maintain a three-year designation recognizing their commitment to reducing wildfire risk. The designation process will include an independent inspection and assessment to give homeowners, policymakers, and insurers peace of mind that, based on the latest science, a *Wildfire Prepared Home* designation indicates a home actually has a lower wildfire risk than unmitigated properties.

<u>Fighting Wildfires with Innovation</u>

California is the largest insurance market by premium volume in the United States — and one of the largest in the world. Insurers have a strong economic incentive to offer coverage to households and businesses in the state. As destructive wildfires increasingly become more common in California, it is to the insurance industry's advantage to encourage at-risk communities to be more wildfire resilient and to develop innovative products that help better measure and transfer risk.

In response to the increasing risk to life and property caused by California wildfires, the rate filings insurers submit to the California Department of Insurance (CDI) are beginning to reflect wildfire mitigation at the parcel and community level. This includes a growing number of admitted market insurers offering premium reductions or more favorable eligibility for homes that meet specified wildfire mitigation standards.

According to the CDI, there are 13 insurance companies (including PIFC member companies Allstate, State Farm, CHUBB, Mercury and Progressive/ASI) representing 40 percent of the insurance marketplace already offering discounts for safer homes and communities, with more companies interested. The amount of interest from insurance companies to offer mitigation discounts has grown from just 7 percent of the market three years ago.

In addition, the CDI has approved filings by Farmers Insurance and the California FAIR Plan Association (FAIR Plan) that include use of Zesty.ai's new technology, the Z-FIRE™ scoring model, which represents a new generation in wildfire risk prediction and accounts for the property-level factors that contribute to wildfire risk, such as building materials, vegetation density and ease of fire suppression.

Many modeling firms are developing innovative new wildfire risk models that will help insurers expand coverage opportunities for residences located in wildfire-risk areas by assessing individual wildfire risks to homes on a more granular basis while evaluating overall wildfire risk exposure in various parts of the state.

To help at-risk communities adapt to the new reality of catastrophic wildfires, insurers have been instrumental in leading resilience efforts in several ways:

- Educating policyholders and communities about wildfire risks and tactics to increase resilience;
- Working to help create resilient communities in high-risk areas; and
- Developing innovative insurance products and tools to help better underwrite, price and transfer wildfire risk.

CDI Mitigation in Rating Plans and Wildfire Risk Models Regulations

On February 25, 2022, CDI proposed new regulations that require insurers to incorporate the mitigation actions contained in the “Safer from Wildfire” framework in their rating plans and wildfire risk models. Insurers support the goal of these draft regulations, which are primarily to reduce risk and loss from wildfires by incentivizing individual and community mitigation and provide increased understanding for consumers regarding risk scores. However, we believe that, as drafted, there remain significant implementation issues in this regulation that must be addressed.

Insurers are eager to work with the Insurance Commissioner on the proposed regulations to ensure they embrace the latest science and technology and support increased access to comprehensive property coverage in wildfire zones without leading to unintended negative consequences for homeowners throughout the state.

It is critical to the future of the insurance market that insurers and regulators find ways to work together to appropriately price and assess this risk in order to provide an insurance market with stable rates, robust coverages, incentives to mitigate, and increased consumer choice.

Wildfire Catastrophe Models

Use of wildfire risk models to distinguish between different risks is allowed by the CDI but using these catastrophe models for pricing purposes at the statewide level is illegal under current California rules. Catastrophe models consider the impacts from mitigation measures and the effects of climate change, thus permitting an insurer to charge premiums that reflect the actual risk related to the homes that it insures

Catastrophe models have been successfully used and relied upon to model extreme events and have been accepted by regulatory authorities worldwide for almost 30 years. In fact, fortyseven other states allow the use of these models in rate-making, and in California, they have long been used to effectively evaluate earthquake and fire-following earthquake risk.

However, California regulations require insurers to estimate their future catastrophic fire losses using the average historic losses for at least the last 20 years. This is like driving a car using only the rear-view mirror. The experience method currently required under the CDI rate template exposes both insurers and consumers to rate shock, as evidenced by the availability and affordability challenges California has been experiencing. Catastrophe models introduce rate stability, the ability to plan ahead, and a better understanding of how wildfire risk is changing

Ultimately, a major flaw of the historical method is that it requires an insurer to ignore the actual location of the properties it insures when filing a rate application. It is inherently retrospective, whereas the first principle of ratemaking is that it is prospective. The historical method does not respond to changes in the underlying risk, and is subject to the randomness of the timing, location, and severity of wildfires that occur. These issues have led to fears of rate inadequacy in areas with substantial wildfire risk for many insurers and an insurance availability problem in high-fire threat areas of California. When catastrophe models help to determine the total statewide premiums that the CDI allows an insurer to collect, insurers can better work with the CDI to determine premium levels that will support more insurance sales in higher risk communities

Conclusion

As Benjamin Franklin once said, “out of adversity comes opportunity.”

Since catastrophic wildfire first emerged as a top tier peril in California just five years ago, there have been major advances in the science of wildfire mitigation and development of sophisticated catastrophe risk models that dramatically improve the ability of insurers to evaluate and price wildfire risk. This will help accomplish the dual goals of increased insurance availability and increased incentives for home hardening and community resiliency efforts.

The work of private and public sector leaders and stakeholders, including emergency/fire professionals, research institutions, modeling firms and the insurance industry, among others, has led to new technologies and innovations that will help us all adapt to a future with more frequent and ferocious wildfires.

Over that same time the Legislature, in partnership with the Insurance Commissioner, enacted more than a dozen insurance-related bills that support homeowners and communities impacted by wildfires including mandated homeowners’ insurance renewals, expanded insurance coverage and benefits, and new tools to help homeowners find insurance in their area.

As the CDI continues to challenge insurers to be creative and develop new approaches to better serve California homeowners, insurers have responded with filings that expand underwriting across the state and recognize the mitigation actions that homeowners implement. According to the most recent data, despite the continued growth in California wildfire activity, the number of non-renewals by insurance companies fell from 235,597 in 2019 to 212,727 in 2020 while the number of new and renewed homeowners’ policies issued by the voluntary market statewide increased from 8.62 million to 8.7 million.

PIFC greatly appreciates the opportunity to provide these comments as we continue to work collaboratively with the Legislature and the Insurance Commissioner to achieve a comprehensive solution that protects choice and insurance availability for all Californians.

Sincerely,

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Seren Taylor
Senior Legislative Advocate
Personal Insurance Federation of California