

Trends and Insights:

California Struggles to Fix Insurance Challenges

Even as California moves to [address regulatory obstacles](#) to fair, actuarially sound insurance underwriting and pricing, the state's risk profile continues to evolve in ways that impede progress.

Perhaps most notably, as of December 2024, the exposure of the California FAIR Plan – the state's property insurer of last resort – was \$529 billion, reflecting a 15 percent increase since September 2024 (the prior fiscal year end) and a 217 percent increase since fiscal year end 2021. In 2025, the Fair Plan will begin offering higher commercial coverage for larger homeowners, condominium associations, homebuilders and other businesses. The commercial plan will cover up to \$20 million per structure and a total of \$100 million per location per year.

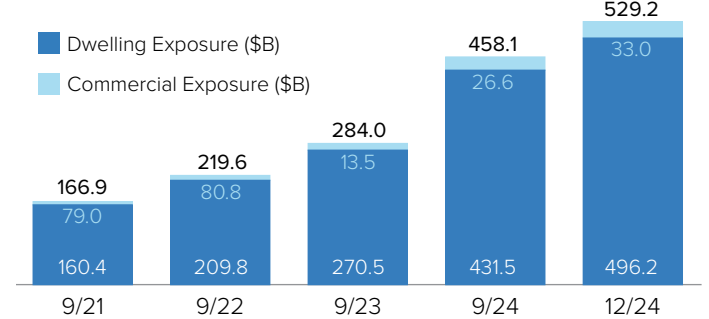
And, regardless of any moves regulators might take, one thing is clear: homeowners insurance premium rates will need to rise to reflect the state's changing risk profile.

As is happening elsewhere, homeowners and auto insurance rates in California have been rising. Some of this is due to replacement costs that skyrocketed during the pandemic and Russia's invasion of Ukraine. In California and other wildfire-prone states, construction trends in the wildland-urban interface also play a role by putting more property at risk.

More recently, uncertainty surrounding the Trump Administration's [imposition of tariffs](#) on U.S. trade partners has added more uncertainty.

But much of California's problem is related to regulators' application of a 1988 measure – [Proposition 103](#) – that constrains insurers' ability to profitably insure property in the state. The decades-old legislation, which predates the full recognition of climate-related risks and the development of modeling tools to help more accurately identify and price insurance to cover them, has become an obstacle to doing business in the state. As insurers have adjusted their risk appetite to reflect these constraints, more property owners have been pushed into the FAIR plan.

California FAIR Plan Exposure is on the Rise



Source: California FAIR Plan

Trouble with Proposition 103

State regulators' application of Proposition 103 caused several unintended consequences related to insurance availability and affordability:

- Insurers couldn't price catastrophe risk prospectively. Instead, regulators interpreted Proposition 103 in ways that required prices to be based on historical data alone.
- Accurate underwriting and pricing were inhibited by restrictions on incorporating reinsurance costs into pricing. If premiums can't reflect reinsurance – particularly in catastrophe-prone areas – insurers must pay for them from [policyholder surplus](#), reduce their market share in the state, or do both.
- Proposition 103 allowed consumer advocacy groups to intervene in the rate-approval process, making it hard for insurers to respond to changing market conditions and driving up administration costs.
- Intervenors also have been a force in resisting the use of catastrophe models.

Insurance Commissioner Ricardo Lara has implemented a [Sustainable Insurance Strategy](#) to alleviate these pressures. This has generated positive impacts, but it continues to meet resistance from legislators and consumer groups.

Losses exceed underwriting profits

Insurers' underwriting profitability is measured using a "combined ratio" that represents the difference between claims and expenses insurers pay and the premiums they collect. A ratio below 100 represents an underwriting profit, and one above 100 represents a loss.

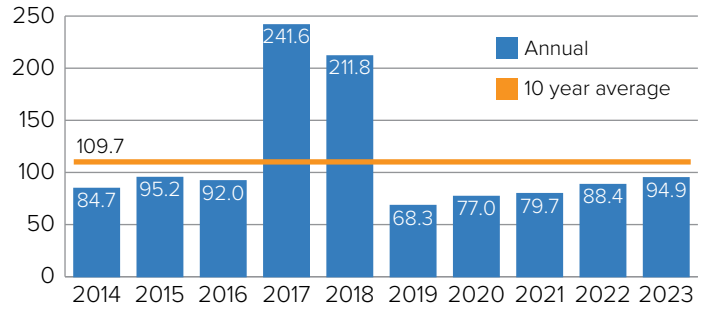
As the chart at right shows, insurers have earned healthy underwriting profits on their homeowners business in all but two of the 10 years between 2013 and 2022. However, the claims and expenses paid in 2017 and 2018 – due largely to wildfire-related losses – were so extreme that the average combined ratio for the period was 108.1.

Underwriting profitability matters because that is where the money comes from to maintain "policyholder surplus" – the funds insurers set aside to ensure that they can pay future claims. Integral to maintaining policyholder surplus is risk-based pricing, which means aligning underwriting and pricing with the cost of the risk.

Artificially lower-than-average premiums

Despite all these challenges – which need to be addressed – California homeowners actually enjoy below-average home and auto insurance rates as a percentage of median income.

California Homeowners Insurance Combined Ratio



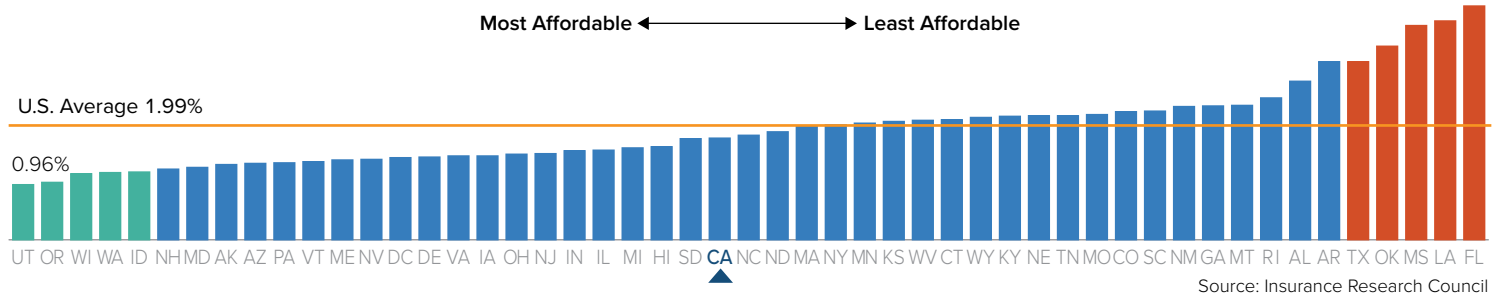
Source: Best's Market Share Reports, Homeowners Multi-peril

Insurance availability ultimately depends on insurers being able to charge rates that adequately reflect the full impact of increasing climate risk in the state.

"Higher rates and reduced regulatory restrictions will allow more carriers to expand their underwriting appetite, relieving the availability crisis and reliance on the FAIR plan," said Triple-I Chief Insurance Officer Dale Porfilio.

The reforms being implemented by the Department of Insurance are meeting legislative resistance, and costly events like January's devastating fires and frequent "atmospheric rivers" that bring floods and mudslides will continue to be an issue for the Golden State. Mitigating such risks and building resilience will require a collective effort at all levels, from state and local governments to the business community and individual property owners.

Homeowners Insurance Premiums as Percent of Median Income (2021)



Auto Insurance Expenditures as Percent of Median Income (2022)

