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CHAIRWOMAN

United States House of Representatives
Committee on Financial Services
2129 Rayburn House Office Building
Washington, D.C. 20515

PATRICK MCHENRY, NC
RANKING MEMBER

September 19, 2022

Memorandum

To: Members, Committee on Financial Services
From: FSC Majority Staff
Subject: September 22, Housing, Community Development, and Insurance Subcommittee Hearing entitled, "State of Emergency: Examining the Impact of Growing Wildfire Risk on the Insurance Market"

The Subcommittee on Housing, Community Development, and Insurance will hold a hearing entitled, "State of Emergency: Examining the Impact of Growing Wildfire Risk on the Insurance Market" on September 22 at 9:00 am in room 2128 of the Rayburn House Office Building and on the Webex platform. The following witnesses will testify:

- Matthew Auer, Dean of the School of Public and International Affairs, University of Georgia
- Amy Bach, Executive Director, United Policyholders
- Ricardo Lara, California Insurance Commissioner
- Roy Wright, President & CEO of the Insurance Institute for Business & Home Safety
- Rex Frazier, President, Personal Insurance Federation of California

Overview

In the U.S., wildfires have grown in reach and severity in recent years as a result of several factors including: climate change, which has created warmer and drier conditions that help fuel longer and more severe wildfire seasons; reduced land management practices; and the increasing number of people living in the area of transition between wilderness and human development, known as the wildland-urban interface (WUI).[1] Since federal wildland fire agencies began reporting official wildfire data using current reporting processes in 1983, the number of acres burned by wildfires has increased substantially.[2] By 2021, the five-year average of acres burned by wildfires has roughly doubled from what it was in the early 1990s (see figure 1).[3] According to nationwide data compiled by the National Interagency Coordination Center (NICC), in 2021 alone, 58,985 wildfires burned 7,125,643 acres.[4] 2021 was a particularly active year in Northern California, the Northern Rockies, and in the Northwest and Eastern areas of the country,[5] where wildfire activity exploded across the western U.S., as the country grappled with record-breaking heat and historic drought conditions.[6] According to a 2021 analysis, of the insured wildfire losses paid by the insurance industry since 1950, 70% have occurred since 2015.[7] In 2017 and 2018 combined, home insurers' underwriting losses in California reached an estimated $20 billion, more than double their profits from that line of business since the late 1990s.[8]

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[1] FEMA, *Wildland Urban Interface: A Look at Issues and Resolutions* (Jun. 2022).
[2] National Interagency Fire Center, *Wildfires and Acres* (Accessed Sept. 2022).
[3] Congressional Budget Office, *Wildfires* (Jun. 2022).
[4] National Interagency Coordination Center, *Wildland Fire Summary and Statistics Annual Report 2021* (Dec. 2021).
[5] *Id.*
[6] NOAA, *U.S. West Hit with Extreme Heat, Drought and Unrelenting Wildfires in July* (Aug. 9, 2021).
[7] AON, *Wildfire Risk in the United States: How Climate Change and Other Variables are Enhancing the Risk* (2021).
[8] Milliman, *Trial by Wildfire: Will Efforts to Fix Home Insurance in California Stand the Test of Time?* (Sep. 29, 2020).

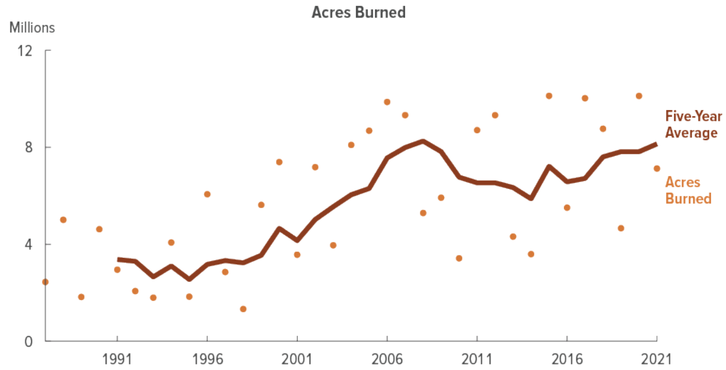

Figure 1: Number of Acres Burned, 1987 to 2021. Source: [Congressional Budget Office](#)

Wildfires have devastating impacts on communities and households, leading to loss of life and billions of dollars in damages. More than 46 million homes—with an estimated value of $1.3 trillion—are now at risk from the impacts of wildfire.[9] California, Florida, Texas, Colorado, and New Mexico, among others, are included in the highest risk states for the number of single-family residences with wildfire risk.[10] Wildfires have the most destructive impact in the WUI. From 1990 to 2010, the size of the WUI grew by over 33% to 190 million acres, and the number of homes on these lands expanded by more than 41%.[11] Most of the large fires with significant property damage have occurred in California, where some of the fastest developing counties are in the WUI.[12] Between January 2005 and June 2022, wildfires destroyed more than 97,000 structures in the United States, including homes and businesses.[13] The U.S. has had 20 wildfire events that *each* caused more than $1 billion in damage between 1980 and 2021 with 16 of those occurring after the year 2000.[14] The California wildfires that occurred in 2018 alone caused an estimated $27.8 billion in damages and resulted in the deaths of 106 people.[15]

Property insurance is an important financial resource for recovering from wildfire damage and can encourage wildfire-related risk mitigation.[16] Primarily regulated by states, insurance policies, such as homeowner, renter, and commercial policies covering wildfire risk can provide financial protection to homeowners, renters, and commercial business, reducing economic hardship after a catastrophic event. Insurance coverage can also expedite the rebuilding and recovery process by providing liquidity to policyholders soon after a wildfire. By offering insurance incentives to policyholders for mitigation actions, either at the individual or community level, insurance can also help promote wildfire risk reduction efforts.[17]

In response to growing risk exposure and a significant spike in losses in recent years, some insurers have begun to increase rates or exit regions where a large volume of wildfire claims have occurred in recent years.[18] The Federal Insurance Office (FIO) within the Department of Treasury has observed that U.S. insurance consumers are increasingly unable to find affordable and available property insurance coverage in certain insurance markets affected by wildfires.[19] In the past, when other catastrophic disasters, such as hurricanes and terrorist attacks, have resulted in a lack of affordable insurance coverage, both states and the federal government have intervened in the insurance market to protect consumers and encourage the supply of insurance.[20]

[9] FEMA, *Wildland Urban Interface: A Look at Issues and Resolutions* (Jun. 2022).
[10] CoreLogic, *Four Western States and Florida Are at Most Risk for Wildfire Damages in 2022* (Sept. 8, 2022).
[11] *Id.*
[12] Insurance Information Institute, *2021 Insurance Fact Book* (2021).
[13] Headwaters Economics, *Wildfires Destroy Thousands of Structures Each Year* (Nov. 2020).
[14] NOAA, *Billion-Dollar Weather and Climate Disasters* (Accessed Sep. 7, 2022).
[15] *Id.*
[16] FIO, *Annual Report on the Insurance Industry* (Sep. 2021).
[17] National Fire Protection Association, *USAA Recognizes the Value of Firewise USA Program to Help Protect Neighbors* (Jul. 27, 2020).
[18] CBO, *Wildfires* (Jun. 2022).
[19] FIO, *Annual Report on the Insurance Industry* (Sep. 2021).
[20] *See* infra *Residual Insurance Market* section; *See also* Terrorism Risk Insurance Act, Pub. L. No. 107-297 (2002); California Department of Insurance, *Mandatory One Year Moratorium on Non-Renewals* (Accessed Sep. 14, 2022).

Homeowners Insurance

Homeowners insurance pays for losses and damage to a property in the case of covered events.[21] Most mortgage lenders require a homeowner to have insurance as long as they have a mortgage.[22] Roughly 95% of homeowners carry homeowners insurance, representing some 70 million policies across the country.[23] Destruction and damage caused by wildfire is typically, but not always, included in homeowner insurance policies.[24] However, because of the increasing risk of wildfires, many homeowners living in communities at high-risk of wildfires are facing steep increases in the cost of their homeowners insurance policies if they can find coverage that includes wildfire risks at all.

Availability of Wildfire Insurance Coverage

As wildfire risk continues to increase, some homeowners in wildfire prone areas of the United States have reported negative pressures on the availability of homeowner's insurance.[25] For example, from 2010 to 2018 consumer complaints on issues of renewals filed with the California Department of Insurance within counties having the greatest risk of wildfire increased by 573%.[26] Supporting data collected from insurance companies by the State of California found that from the end of 2018 to the end of 2019, residential non-renewals by insurance companies increased statewide by 31% and a 203% increase in non-renewals for homes in the top 10 counties with the highest wildfire exposure.[27] Following declared states of emergencies, in 2019, 2020, 2021 and 2022 the State of California instituted several one-year moratoriums on insurance non-renewals in zip codes within or adjacent to specified fire incident perimeters.[28]

Affordability of Wildfire Insurance Coverage

Studies have also found that insurance rates have increased substantially with growing wildfire risk and have been increasing more rapidly in recent years,[29] likely because insurance pricing is typically proportional to the risk that is being transferred.[30] To calibrate prices according to risks, insurers review and analyze available data when developing guidelines for rating wildfire risk and underwriting policies.[31] As opposed to simply using historical loss data, insurance companies are increasingly relying on risk modeling solutions to better gauge where wildfire risk lies and determine premiums.[32] These models can be controversial[33] and, for example, the state of California has disallowed their use in the past.[34] New proposed rules in California would specifically require wildfire risk models be provided to the Department as part of the rate approval process and be made available for public inspection.[35] In some instances, the California Department of Insurance documented complaints where homeowners paid an annual premium

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[21] CFPB, *What is Homeowner's Insurance? Why is Homeowner's Insurance Required?* (Sep. 9, 2020).
[22] National Association of Insurance Commissioners, *A Consumer's Guide to Home Insurance* (2010).
[23] National Fire Protection Association, *The Influence of Insurance* (Accessed Sep. 8, 2022).
[24] Progressive, *Does Homeowners Insurance Cover Wildfires?* (Accessed Sep. 8, 2022). There is no national data showing how many homeowners insurance policies exclude this coverage and how that is changing over time. Unless homeowners are carefully reading the fine print in their insurance contracts, many may be surprised to find that wildfire damage is excluded from their policies.
[25] NY Times, *As Wildfires Get Worse, Insurers Pull Back from Riskiest Areas* (Aug. 20, 2019).
[26] California Department of Insurance, *December 2017 Availability Affordability Report* (Revised Feb. 2019).
[27] California Department of Insurance, *Data on Insurance Non-Renewals, FAIR Plan, and Surplus Lines (2015-2019)* (Oct. 19, 2020).
[28] California Department of Insurance, *Mandatory One Year Moratorium on Non-Renewals* (Accessed Sep. 8, 2022).
[29] RAND Corporation, *California Wildfires: Can Insurance Markets Handle the Risk?* (2020).
[30] Society of Actuaries, *Actuarial Toolkit* (Sep. 2022).
[31] Headwaters Economics, *Do Insurance Policies and Rates Influence Home Development on Fire-Prone Lands?* (Jun. 2016).
[32] Milliman, *Wildfire Catastrophe Models Could Spark the Changes California Needs* (Oct. 28, 2019). However, some states do not allow for the use of forward-looking models, including California.
[33] Voice of San Diego, *Insurance Companies Say They're Not Allowed to Plan for the 'New Normal' of Intense Wildfires* (Jun. 24, 2019).
[34] NY Times, *Wildfires Hasten Another Climate Crisis: Homeowners Who Can't Get Insurance* (Sep. 10, 2020).
[35] California Department of Insurance, *Commissioner Lara announces new regulations to improve wildfire safety and drive down cost of insurance* (Feb. 25, 2022).

of $800-$1,000 but, upon renewal, reported increases to as high as $2,500-$5,000.[36] Trends in California mirror concerns about rising premium increases in several other states.[37] Increased insurance premiums for properties at risk of wildfire has the potential to make policies unaffordable for many, particularly low-income families who disproportionately impacted by wildfires.[38]

Underinsurance

Many consumers are "underinsured"—carrying insurance policies which do not include adequate coverage to compensate the policyholder for the full extent of fire related losses. Underinsurance occurs when there is a gap between available insurance benefits and the actual cost of repair or replacement. Underinsurance may stem from a number of causes. A property can be underinsured due to insurance limits that are too low, gaps due to policy exclusions, or high deductibles.[39] Consumers may opt for insurance that is the most affordable but provides coverage that is inadequate to cover the cost of repair or replacement to the home.[40] Insurers estimate that two out of every three homes in America are underinsured with an average uninsurance amount of about 22% and some homes underinsured by 60% or more.[41] These nationwide estimates are similar to real world experience. The 2021 "Marshall Fire" in Colorado damaged approximately 6,000 acres and destroyed 1,084 residential structures in what was the most financially destructive wildfire in Colorado's history.[42] According to data from the Colorado Division of Insurance, as many as two-thirds of those who lost their homes in the Marshall fire were underinsured.[43] Several Marshall Fire victims report believing they were adequately covered but face estimated coverage gaps exceeding six-figures.[44]

Problems due to underinsurance may be exacerbated if insurers seek to modify policies to restrict investigations into the scope of damage, narrow policy benefits, and increase hurdles for homeowners seeking payment for claims in response to increased wildfire losses, actions that research has found may occur.[45] Federal disaster assistance may be able to fill insurance gaps or provide resources to Americans who are uninsured or underinsured in limited cases but is typically not an adequate replacement for homeowners being fully insured.[46]

Residual Insurance Markets

To make basic coverage more readily available to consumers who want or need insurance, state regulators have worked with the insurance industry to established special insurance plans, known as residual, shared or involuntary markets.[47] Known as "markets of last resort,"[48] residual insurance markets exist to provide insurance to high-risk policyholders who may have difficulty obtaining coverage from the private market, including homeowners unable to obtain wildfire coverage.[49] These markets are subsidized by private insurers and taxpayers collectively pooling the risk.[50] However, the insurance provided in

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[36] *Id.*
[37] National Association of Insurance Commissioners, *Application of Wildfire Mitigation to Insured Property Exposure* (Nov. 15, 2020).
[38] USDA, *Innovating Wildfire Insurance* (Aug. 3, 2021); Matthew Auer and Benjamin Hexamer, *Income and Insurability as Factors in Wildfire Risk* (Jul. 18, 2022).
[39] United Policyholders, *A Guide to Underinsurance* (Accessed Sep. 9, 2022).
[40] *Id.*
[41] Nationwide, *Underinsurance: Is Your Home Covered for All It's Worth?* (Accessed Sep. 9, 2022).
[42] Boulder County, *Boulder County Releases Updated List of Structures Damaged and Destroyed in the Marshall Fire* (Jan. 6, 2022).
[43] Colorado Division of Insurance, *Division of Insurance Releases Initial Estimates of Underinsurance for Homes in the Marshall Fire* (Apr. 26, 2022).
[44] The Denver Post, *"It's a Gut Punch": Marshall Fire Survivors Fear Their Were Underinsured and They Can't Afford to Rebuild* (Feb. 18, 2022).
[45] Consumer Watchdog, *Up in Smoke: How Insurance Companies and the Insurance Commissioner Burned Wildfire Victims* (Jul. 2022).
[46] FEMA, *Wildfire Survivors Can Apply for Federal Aid Even if Insured* (Oct.15, 2020).
[47] Insurance Information Institute, *Residual Markets* (Dec. 2006).
[48] Insurance Information Institute, *Residual Market Property Plans: From Markets of Last Resort to Markets of First Choice* (May 2016).
[49] Insurance Information Institute, *Residual Markets* (Dec. 2006).
[50] Insurance Business Magazine, *What are FAIR Insurance Plans?* (Jul. 12, 2019).

residual insurance markets may cost more than private insurance and offer less coverage.[51] For example, homeowners in California can access insurance coverage for wildfires through the state's Fair Access to Insurance Requirements (FAIR) plan, but typically this coverage is more expensive and less comprehensive than private insurance.[52]

Mitigation

Mitigation is risk management action taken to avoid, reduce, or transfer the long-term risk that threats and hazards present to people and their property.[53] Mitigation, both on an individual and community basis, has been shown to reduce wildfire risk.[54] Some insurance companies seek to inform homeowners as to available mitigation measures and, through price signals and financial incentives, to encourage consumers to invest in those measures.[55] Federal, state and local governments may also provide financial incentives, through grant programs and tax incentives, or impose regulations to support mitigation measures.[56] Wildfire risk mitigation strategies generally fall into two categories: 1) hardening a structure by using fire-resistant materials, and 2) reducing the intensity of a potential fire around a structure.[57] The National Mitigation Investment Strategy compliments other federal government initiatives for mitigation investment and calls for the federal government and nonfederal partners to work together to identify, prioritize, and implement community-wide mitigation strategies.[58]

The cost of mitigation measures and the inability of most homeowners to effectively assess wildfire risk may limit the ability of insurers to influence policyholder behavior.[59] Particularly for individual residents, mitigation and maintenance can be technically, physically, and financially challenging.[60] Consumers may also have a limited understanding of wildfire hazard and exposure, or of the actions required to minimize their vulnerability.[61] Few states require wildfire risk be disclosed to consumers during the homebuying process.[62] One study found that some homeowners will require accessible and persuasive information about wildfire risk as well as significant financial incentives to undertake private wildfire risk mitigation efforts.[63] Homeowners insurance companies may be able to expand or initiate education efforts regarding wildfire risk.[64] The State of California has proposed requiring insurance companies to recognize and reward wildfire safety and mitigation efforts in setting rates.[65]

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[51] Kiplinger, *How to Get Property Insurance in High-Risk Areas* (Sep. 15, 2020).
[52] Policygenius, *Homeowners in California see rate increases ahead of peak wildfire months* (Aug. 2, 2022).
[53] FEMA, *National Mitigation Framework* (Jun. 2016).
[54] American Academy of Actuaries, *Wildfire: Lessons Learned from the 2017 to 2021 Events* (Jan. 2022).
[55] FIO, *Report Providing an Assessment of the Current State of the Market for Natural Catastrophe Insurance in the United States* (Sep. 2015).
[56] *Id.*
[57] Insurance Institute for Business & Home Safety, *Suburban Wildfire Adaptation Roadmaps: A Path to Coexisting with Wildfires* (Nov. 2021).
[58] Department of Homeland Security, *National Mitigation Investment Strategy* (Aug. 2019).
[59] FIO, *Report Providing an Assessment of the Current State of the Market for Natural Catastrophe Insurance in the United States* (Sep. 2015).
[60] Zurich, *Building Resilience from the Ashes* (Dec. 2019).
[61] *Id.*
[62] National Public Radio, *Millions Are At Risk Of Wildfires, But It's Rarely Disclosed* (Oct. 21, 2020).
[63] International Journal of Disaster Risk Reduction, *Homeowners Willingness to Pay to Reduce Wildfire Risk in Wildland Urban Interface Areas: Implications for Targeting Financial Incentives* (Jan. 2022).
[64] National Association of Insurance Commissioners, *Application of Wildfire Mitigation to Insured Property Exposure* (Nov. 15, 2020).
[65] California Department of Insurance, *Commissioner Lara Submits First-In-Nation Wildfire Safety Regulation to Drive Down Cost of Insurance* (Sep. 7, 2022).

Appendix: Legislation

- **H.R. 8483, the "Wildfire Insurance Coverage Study Act of 2022," (Waters)** would require the Federal Emergency Management Agency (FEMA) and the Government Accountability Office (GAO) to conduct studies assessing the danger that wildfires increasingly pose to communities and how the market for homeowners' insurance is responding to this growing threat.