California's Housing Crisis Meets California's Insurance Crisis

By Josh Stephens on July 8, 2024

Housing, Infill, Insurance, Wildfire

For decades, housing advocates, and some policymakers, have stressed the dire need to develop new housing in infill areas and — for a host of reasons — leave open space alone. These advocates now have an ally, albeit it an unwelcome one, in the form of the insurance industry.

Recently, property insurers in California have curtailed the number of types of policies that are willing to write in parts of the state determined to be prone to wildfires—and to the potentially massive property loses that they can cause, especially when research indicates that climate change has exacerbated frequency and severity of wildfires.

At least seven major insurers—State Farm, Allstate, Farmers, USAA, Travelers, Nationwide and Chubb— have reduced their coverage in California. They've been pressured not only by losses but also by inflation and rising reinsurance rates. Most of all, they have been hemmed in by Prop. 103, the 1988 ballot measure that requires the state to approve rate increases and prevents carriers from using future projections to estimate losses and set rates. The trend may affect future development significantly if insurance companies decline to write new policies.

Many of the properties that have been abandoned by insurers are located in areas on the urban fringe, in small towns surrounded by forests or chaparral, or in entirely rural areas.

These areas are particularly susceptible to wildfires, which have grown particularly intense, numerous, and destructive in recent years. The proximate cause of this trend goes back to 2017, when over 1.5 million acres burned — up from less than 1 million in each of the previous eight years. Further perilous, expensive years followed. (This year over 118,000 acres have already burned.)

A recent study by Next 10 estimates that 4.5 million homes are located in the wildlands-urban interface (WUI) and, of them, 1.5 million face high fire risk. Areas considered at risk by the Dept. of Insurance encompass hundreds of ZIP codes and are located in the vast majority of the state's 58 counties. They are concentrated especially heavily on the western slope of the Sierra Nevada Mountains, many inland portions of coastal counties, and nearly the entire state north of Redding.

Even though the insurance trend may inadvertently support the state's goal of limiting development in WUI, it could undermine efforts of exurban and semi-rural counties to meet their housing targets under the Regional Housing Needs Allocation system. Rural counties have low RHNA targets but exurban counties on the metropolitan fringe– many of which are located in high fire risk areas – have higher numbers.

"It's certainly stifling development," said Staci Heaton, Senior Policy Advocate for the Rural County Representatives of California. "We are having trouble meeting our low-income development numbers for the state because we're finding that new developments cannot get insured."

At the same, state insurance regulators realize that there's a crisis and they're working on a way to keep insurance companies writing or renewing policies in areas of high wildfire risk – which could, of course, increase development in vulnerable, and usually car-dependent, areas.

The proposed "Sustainable Insurance Strategy" would give insurance carriers concessions on premiums and forward-looking models in exchange for their pledge to cover "distressed" areas—with "distressed" correlating roughly with high wildfire hazard severity zones and/or areas with relatively low insurance coverage — at 85% of their respective levels of coverage in fire-safe areas. (Among other things, Prop. 103 permits only backward-looking models to be used in calculating insurance rates – an approach that may not take climate change into account.)

But future development may not fare so well, at least unless and until the Sustainable Insurance Strategy is adopted.

Rex Frazier, president of the Personal Insurance Federation of California, said that developers are having particular difficulty getting blanket insurance to cover master-planned developments.

"I have never spoken with so many builders and real estate professionals as I have in the last three years," Frazier said. "Insurance is starting to be a major feature of a real estate transaction or of a homebuilding project in a way that it shouldn't and has on very few occasions in the past."

The current insurance crisis arguably reflects land-use policy just as much as it does insurance policy. Many decades of development, at least since the end of World War II, on the urban fringe has, critics say, put an inordinate number of homes in harm's way

"A lot of times the development goes to areas of the least community opposition," said Frazier. "But, look at where you're building: high brush, very dry, lots of hills. If people are going to be building there, we have to start having some consensus on what hazards need to be identified, observed, and hopefully mitigated."

Simultaneously, state and local policies that complicated infill development have prevented developers from building more housing in relatively fire-safe center cities.

"The state's inability to loosen the tourniquet on infill housing development in cities is going to come and bite it in the form of this insurance problem in remote, fire-prone, flood-prone areas," said Matthew Lewis, director of communications for California YIMBY.

The insurance peril is not necessarily limited to rural areas. In at least one instance, insurer Liberty Mutual balked at insuring property in an urban area "where the dwellings are considered to be too densely concentrated," according to the *San Francisco Chronicle*. Liberty Mutual did not publicly share a reason for non-renewal. Its concerns for density could refer to the dangers that fire could travel easily from one dwelling to another or that the company had too many policies in one area and felt overexposed to a localized risk, such as an earthquake.

A map published by the *Chronicle* reveals a higher non-renewal rate for some areas of San Francisco – up to 2.2% -- than for neighboring cities or for comparably dense areas of the City of Los Angeles, where non-renewal rates are effectively 0%.

The current crisis thus presents a paradox: it may limit development in the WUI, but for the wrong reasons. And, it stands to reduce development in

problematic places without doing anything to promote development in places where many planners and many recent state policies want to promote development. At its most extreme, a more extensive collapse of the property insurance industry could even lead to higher premiums in fire-safe locations.

"Six months ago, I would have said this was not a statewide problem. Then State Farm said they're not writing new business in the state of California," said Frazier.

State Farm's California subsidiary has hinted that it might go out of business entirely. It recently requested state approval for substantial rate hikes statewide: 30% for homeowners, 52% for renters, and 36% for condominium owners.

Whatever happens with insurance policy, this crisis gives planners and builders ever more impetus to implement measures to protect homes and communities from wildfire.

"I think planners should also do the work to understand local communities' roles, planning agencies' roles, the development community's role in reducing risk," said de Kok. "If we're going to balance meeting our housing needs with our climate goals, this needs to be discussed."

"The push for affordable housing is pushing us into more and more risky areas," said Carmen Balber, executive director of Consumer Watchdog, the successor to the organization that originally sponsored Prop. 103. "We do think there needs to be a statewide entity, whether it's a board or a commission, that has a hand in that decision-making."

New developments have to be constricted according to Chapter 7A of the California Building Code which is, "arguably the most stringent building requirements for building in wildfire prone areas," according to Steve Hawks, Senior Director for Wildfire at the Insurance Institute for Business & Home Safety.

The prospects of hardening and mitigation, though, can do only so much. Only a small percentage of properties in [fire areas] are newly developed and, therefore, subject to the most aggressive building regulations. Carriers are still looking at countless existing properties that could burn.

"We do have better codes and standards, and strong evidence that that's working," said de Kok. "But we also have many legacy developments and land use developments over the past 100 years that were not built to those standards."

"Fire is a lot more complicated than wind. You can do everything right on your parcel, but there are things bigger than you that determine whether your house burns," said Frazier.

Importantly, older and poorly maintained properties can endanger their neighbors.

If insurers are going to adopt forward-looking risk models, said Heaton, they should account for recent advanced and investments in wildfire mitigation and prevention.

"They're not necessarily taking into account literally billions of dollars that residents and communities and counties are leveraging on wildfire mitigations," said Heaton. "We need to get that balanced out so that the insurers will look at these mitigations and account for them appropriately."

In a worst-case scenario, though, reluctant insurers may cause communities in the WUI to rethink their futures.

"We are facing the reality of managed retreat…. from places we can no longer defend from fire," said Lewis.

Contacts & Resources

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