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Testimony of Rex Frazier, Personal Insurance Federation of California
before
SB 901 Wildfire Cost and Recovery Commission,
March 13, 2019 – Redding, California

Commissioners,

My name is Rex Frazier. I'm the President of the Personal Insurance Federation of California, representing admitted market insurers on residential property insurance issues. The admitted market, which means insurers voluntarily writing insurance after receiving a customer application, is presently insuring over 98% of the approximately 11.5 million insured structures in California.

The admitted market also provides a financial back-stop for high-risk properties, known as the California FAIR Plan. The FAIR Plan provides property owners guaranteed access to fire insurance. All admitted homeowners' insurers are required to be members of the FAIR Plan as a condition of doing business in California, and the FAIR Plan operates without any state financial support. If the FAIR Plan is short of funds, it will assess admitted insurers, as required. Of the 123,000 properties insured by the FAIR Plan, only 34,000 are located in brush areas with medium- or extreme-brush exposure.

The 18,000 homes not served by admitted insurers (either directly or through the FAIR Plan) are served by the non-admitted market.

These three elements, the admitted market, FAIR Plan and non-admitted market, collectively, comprise the private property insurance system in California. Following a major fire, this system executes a massive claims response – which typically involves bringing hundreds of people from across the country who are willing to move to California for months, and sometimes in excess of a year, to serve people impacted by the fires.

When a fire is caused by a third party, property insurers begin the claims-payment process as well as the subrogation process. Subrogation is a common process where both private and government payors answer the call of people to whom they owe a duty, and then seek to recover those payments from the party causing the damage. This happens every day in the auto insurance industry, where a customer makes claim with his or her collision insurer and then that insurer seeks to recover from the at-fault driver's liability insurer. The Medi-Cal program does this every day, paying for indigent health care and then seeking recovery from those who caused the harm (often times an insured driver).

This subrogation process applies equally on the rare occasion that a utility causes a fire. Wildfire plaintiffs, including subrogating insurers, have repeatedly settled claims arising from utility-caused fires. This practice had never received significant public attention until late 2017, after the California Public Utilities Commission found that San Diego Gas & Electric did not reasonably operate its facilities prior to its 2007 wildfires and, as a result, denied SDG&E's application to socialize across its ratepayers the remaining fire costs that exceeded its commercial insurance recoveries.

While the 2018 legislative session prominently featured a debate about whether the Takings Clause should apply to investor owned utilities, that debate obscured the real problem facing the IOUs, which is how the 2017 PUC decision disrupted the widely-held market assumption that all excess liabilities of an IOU would automatically be socialized across the ratepayer base – particularly when that PUC decision was so close in time to the massive potential liabilities accruing after the Tubbs Fire in Santa Rosa. For the first time, investors realized that a California IOU could face a large unfunded liability if the PUC determined, after the fact, that an IOU imprudently caused the damages. This risk exists whether or not plaintiffs sue using their constitutional rights to an inverse condemnation claim, or more traditional causes of action, such as negligence.

In 2018, we urged parties to focus on developing “brighter line” PUC standards for when, and how, an IOU should be permitted to socialize its unfunded liabilities. Every regulated company deserves a clear legal standard for evaluating its conduct. Such standards allow managers to develop proper goals and supervise towards achieving them. The standards applied to SDG&E in 2017 left them claiming unfair surprise, and this surprise rippled across the investor community. While SB 901 included changes to the process for determining prudent behavior, it retained much more ambiguity than is present in a more traditional negligence analysis.

An additional concept on how to better socialize utility wildfire liabilities is the emerging consideration of a utility excess liability fund. We encourage serious deliberation of such a funding mechanism. While there are many details to such an approach, the concept is straightforward: after determining, first, a utility’s self-insured retention (meaning the fire risk it retains) and, second, the preconditions necessary for claiming to a catastrophe pool (such as compliance with a wildfire mitigation plan), a utility could tap pooled funds to pay for catastrophic liabilities it causes. There are many options for how to capitalize such a fund, and many conversations occurring outside of this forum. We remain committed to being an active participant in these discussions and responding to the Governor’s challenge to develop the framework for a solution in the very near future.

Thank you for this opportunity to participate.