BofA SECURITIES

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Call for Contributions in Support of Study on New Models and Approaches to Complement or Replace the Wildfire Fund

BofA Securities, Inc.
One Bryant Park, 12th Floor
New York, NY 10036
Nathaniel Johnson, *Director*
nathaniel.e.johnson@bofa.com
321-527-7818

Abstract: California State Reinsurance Authority

The insurance sector in the State of California is addressing one of the most challenging periods in recent history. From discussions with professionals within the industry, we believe one of the headwinds contributing to constraints within the insurance marketplace is the inability to adequately address certain risks, including catastrophic risk from a range of perils, such as wildfire. Risk transfer programs for both the voluntary and residual market carriers have relied on traditional reinsurance policies and Insurance-Linked Securities ("ILS") offerings to address a portion of the risk within the policies they write. The market for these risk transfer opportunities can be volatile on a year-by-year basis, for both market capacity and cost. Implementing a state-created reinsurance authority could help stabilize the homeowner's insurance market by ensuring all carriers in the State (including the FAIR Plan) would have access to a solution that addresses exposure to catastrophic perils. A public sector, state-managed reinsurance authority would complement what is currently done in traditional markets, by adding capacity and creating competition for risk transfer solutions. Precedent exists in the United States for a similar solution addressing insurance challenges. Funded from reinsurance premiums and with assessment authority for unfunded losses, this entity could be developed to help stabilize the California insurance market while insulating the State of California from any potential losses by isolating these risks to the newly created California State Reinsurance Authority.

Addressing an Insurance Market Crisis: A State-Backed Reinsurance Authority for Wildfire Perils

California's homeowners insurance market is in profound crisis. As of late 2025, driven by escalating wildfire losses amplified by climate change and other factors, major insurers have reduced their exposures in the State by either non-renewing policies or exiting high-risk areas entirely. The California FAIR Plan, a barometer of the health of the insurance market, has ballooned to over 646,000 policies with more than $696 billion in total exposure[1], yet it, like the voluntary market, relies on expensive private risk-transfer solutions with uncertain availability and cost (and often with high retentions). This ad-hoc structure leaves the market fragile: private risk transfer/reinsurance capacity for wildfire is limited and costly, while the FAIR Plan endures significant strain during catastrophe events.

Florida faced a similar existential threat after Hurricane Andrew in 1992 devastated its insurance market. In response, the state created the **Florida Hurricane Catastrophe Fund ("FHCF")** in 1993 — a tax-exempt, state-administered reinsurance entity that has stabilized residential property insurance for over three decades. The FHCF provides mandatory reinsurance policies to all insurers writing residential coverage in Florida at highly competitive rates and lower attachment points, addressing their exposure to catastrophic hurricane losses and preventing mass hurricane driven insurer withdrawals. California could adapt this proven model by establishing a **California State Reinsurance Authority ("CSRA")** — a state-created reinsurance entity focused on wildfire perils. Such an entity could address the insurance sector crisis through providing guaranteed access to risk transfer needs, lowering reinsurance costs, helping retain private insurers, reducing FAIR Plan dependency; ultimately protecting the affordability and availability of homeowners insurance and providing greater stability to the housing market statewide.

Illustrating the need for additional risk transfer solutions, in December 2025, the California FAIR Plan completed the largest ever wildfire Catastrophe Bond / ILS offering, which provided $750 million of reinsurance to the FAIR Plan, but at a cost of nearly 10% rates.[2] This $750 million of successful risk transfer is a positive indication of growth in what historically has been a limited market for wildfire reinsurance solutions (historical wildfire ILS issuance has totaled only $1.2 billion in aggregate) but is quite small compared to the estimate insured losses of $35-45 billion from 2025 California wildfires[3] or the $696 billion of aggregate FAIR Plan exposure.

How the Florida Hurricane Catastrophe Fund Operates

The FHCF functions as a public reinsurance layer sitting above primary insurers' retention of initial losses from tropical events. Key features include:

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[1] Source: California FAIR Plan: Key Statistics & Data - The California FAIR Plan
[2] Source: Artemis.com
[3] Source: McKinsey: Resetting California's homeowners insurance market | McKinsey

Mandatory Participation: All insurers writing residential property coverage (including Citizens Property Insurance Corporation, Florida's residual market provider) must purchase FHCF coverage through annual reimbursement contracts.

Coverage Structure: Insurers select attachment levels (e.g., 45%, 75%, or 90% reimbursement of losses above a retention level). The FHCF has a statutory cap on its annual capacity of $17 billion, limiting its maximum loss in any year.

Funding Mechanism: FHCF was created to be self-funded and self-supporting, with the primary revenue for FHCF coming from risk-based premiums paid by participating insurers (all admitted carriers in the state) which is passed through to policyholders as part of the annual ratemaking formula. FHCF is also funded through the investment earnings on accumulated reserves.

- Following a catastrophic event, if reserves are exhausted, FHCF has the authority to implement assessments on nearly all property-casualty policies statewide (excluding workers' comp, medical malpractice, and limited others)
- Those assessments can be used to secure "post-event" tax-exempt revenue bonds issued to fund any excess losses, if needed
- With affordability being a primary concern, this assessment has been used infrequently over the past two decades and has historically been in the range of 1% of insurance premiums for Property & Casualty ("P&C") insurance in the state.

This design makes FHCF reinsurance considerably more affordable than private markets because the state spreads the risk of losses exceeding premium revenue across all P&C policyholders statewide and accesses the municipal bond market at lower tax-exempt borrowing rates. The state created FHCF also avoids the need to provide a profit/return on investment like a private reinsurance companies would, thereby also lowering the implied premium costs to primary carriers.

Parallels and Application in California

California's wildfire risk mirrors Florida's hurricane exposure in scale and unpredictability: both are climate-intensified, geographically concentrated perils with the potential of causing multi-billion-dollar insured losses. Recent significant events (and related losses) of the 2017-2018 fires seasons and 2025 Los Angeles fires have eroded private capacity much like Hurricane Andrew did in Florida.

California has yet to address many of the underpinnings of the insurance crisis. The FAIR Plan acts as a residual market safety net but is still subject to the private reinsurance market for catastrophe risk transfer, at uncertain rates and capacity. A state created public reinsurance solution would flip this dynamic: mandatory and affordable reinsurance would incentivize private carriers to remain or expand in wildfire-prone areas, once there is a demonstrated way to address that peril and adequacy of rates for the risks insurers are taking.

Potential for A Multi-Peril California Reinsurance Authority: Combining Wildfire and Earthquake Risk into a Single State Reinsurance Entity

The core tenet behind Florida's Hurricane Catastrophe Fund is that a public sector entity is best positioned to address truly catastrophic, low-frequency perils that private reinsurance markets either price prohibitively or are unable to write at scale. California faces not one but two such perils—wildfire and earthquake—that are largely uncorrelated with each other and with other risks throughout the U.S. insurance market. Combining both perils into the single California Multi-Peril Reinsurance Authority ("CMPRA") could create the deepest, most diversified state-level risk pool in the nation, lowering costs and increasing capacity beyond what two separate funds could achieve.

Benefits of a Multi-peril Authority

Diversification Benefit - Major earthquakes and mega-wildfires almost never occur in the same policy year at catastrophic scale. The last earthquake causing $20 billion in residential damage was in 1994[4]; the last $25+ billion wildfire season was 2017–2018[5] (and potentially 2025). This negative correlation means the combined fund can spread risk and losses from the two perils across a consolidated business, allowing premium revenue from one risk to support the other.

Operational Efficiency – Having a single governance, staff, contracting process, annual reimbursement contract, and post-event assessment mechanism would capture economies of scale for both operations and costs, when compared with duplicating each aspect for separate wildfire and earthquake funds.

Primary Market Improvements – a multi-peril reinsurance entity could simultaneously address two concerns.

- Wildfire Driven Insurance Contraction
    - Affordable and consistently available CMPRA policies replace traditional reinsurance in the voluntary market and FAIR Plan's risk transfer programs
    - Private insurers can re-engage in high-risk areas because their maximum wildfire loss is better addressed
    - FAIR Plan exposure shrinks as insurers begin writing policies again
- Earthquake Considerations
    - Current California Earthquake Authority ("CEA") take-up rates hover around 10%[6] because earthquake premiums are a rising incremental cost and coverage is optional
    - By making basic earthquake coverage more affordable (through more efficiently priced reinsurance), effective take-up could rise significantly

[4] Source: CEA California Earthquake Authority's Story - Building Earthquake Resilience
[5] Source: Insurance Information Institute Archived Tables | III
[6] Source: FEMA Earthquake Insurance | FEMA.gov

Designing a California State Reinsurance Authority

Either a single peril CSRA or multi-peril CMPRA (going forward both referred to as the "CSRA") could be consolidated under the Department of Insurance or a newly created entity administered by an agency like the California Earthquake Authority (similar to the Wildfire Fund). Suggested key operational focuses could be:

1. **Scope and Participation**:

- Mandatory for all admitted homeowners/multi-peril insurers writing business in wildfire-prone districts (as defined by Cal Fire or DOI maps)
- Coverage would be for residential and small commercial lines; with the potential expansion to carriers writing larger commercial policies
- FAIR Plan would be a "participating insurer," also required to engage CSRA for wildfire reinsurance. This would serve to help cap FAIR Plans exposure to wildfire losses at a time when policy count and maximum exposure is at historical high levels

2. **Coverage Layers**: The CSRA would need to engage actuarial professionals to help determine coverage limits, but as an example:

- Reimbursement of a significant portion of losses above insurer-specific retention levels
- Annual capacity/maximum loses for CSRA could initially be phased in as claims paying resources build, starting at an illustrative $10 billion and building to $20 billion (examples only), after industry retention of $5-10 billion

3. **Funding and Loss Absorption**:

- The primary funding source for CSRA would be premium revenue collected from insurers. Premiums would be determined on an actuarially fair basis, but expected to be lower than private sector risk-transfer costs
- These premium revenues would allow CSRA to build reserves through accumulation and investment returns
- In the initial periods of CSRA operations, or after significant event driven losses, CSRA could rely on "pre-event" financing for liquidity, which are bonds issued prior to any covered event to provide CSRA with claims paying resources. CSRA's assessment authority would be sufficient to secure the pre-event bonds and assessments would not need to be implemented unless CSRA losses require them. Pre-event Bond debt service could be nearly satisfied from investment returns on the unused/invested bond proceeds
- Should a significant event occur that exceeds claims paying resources available to CSRA, broad-based assessments on all P&C lines (home, auto, commercial) could be implemented and CSRA could issue "post-event" bonds repaid by the assessments. The

proceeds from the post-event bonds would be used to supplement the existing resources CSRA has available for losses at the time of the event

There are several unique challenges that wildfire peril presents when compared to hurricane risks that would need to be considered. Wildfires differ from hurricanes in modeling and behavior, requiring adjustments to the approach hurricane solutions have relied on. Hurricane models are much more mature and have greater regulator acceptance, while wildfire modeling is still evolving. The CSRA would need ongoing third-party validation of a covered event to define triggers for carrier reimbursement. Hurricane triggers often rely on a criteria of "named events," or category/windspeed thresholds, which are determined by the National Hurricane Center. Identifying that peer entity for wildfires would be important in the creation of CSRA operations. However, despite these differences, wildfire losses remain insurable (and therefore reinsurable) at scale.

CSRA Benefits and Path Forward

A California State Reinsurance Authority would align with the objectives of SB 254 through:

- Reducing the reliance on volatile private reinsurance markets by providing stability and predictability to risk transfer program, while significantly reducing certain reinsurance costs, thereby lowering premiums and stabilizing rates
- Retaining private insurers in the State, helping reduce dependency on insurance policies from the FAIR plan.
- Spreading risk equitably with a goal of a heathier insurance sector and overall housing market, ***increasing the affordability and availability of homeowners insurance statewide***

The FHCF model proves that a public sector solution can address signature catastrophic perils and keep the private insurance market viable: with very few hurricane-specific insurer insolvencies, despite approximately 40 hurricanes and tropical events making landfall in Florida over the past 20 years.

A California State Reinsurance Authority concept could provide a proven approach to current insurance sector challenges and paired with California's Sustainable Insurance Strategy, it would mark the bold reform needed to change direction from the current insurance crisis.