Good afternoon. My name is Benjamin McKay, and I am the Executive Director of the Surplus Line Association of California. Currently, I have more than 17 years of experience in the insurance industry, both on the legislative and the practitioner side. I would like to thank Committee Chair Roth, Vice Chair Gaines, and all the committee members and staff for the opportunity to testify at today’s hearing.

Our association is composed of nearly 5,200 licensed brokers who place more than half a million policies in the nonadmitted market each year on behalf of California consumers. Last year, our members placed 580,273 policies in the state.

The California Department of Insurance in 1994 appointed the SLA as its statutory surplus lines advisory organization. Our job as the CDI-appointed advisory organization is to ensure that all California-licensed brokers remain in compliance with all pertinent state laws and regulations, and we do this by examining every surplus line policy filed in the state.

We work with our members to ensure a healthy, fair and competitive surplus line market in the state of California that protects consumers and helps meet our goal of getting all Californians the coverage they need.

Here, I would like to address a concept which is widely held about the surplus lines industry, which is that it is largely unregulated. In fact, the industry is well and diligently regulated in California and also in the other states. Twenty-one sections of the California Insurance Code (1760 to 1780) relate directly to the surplus lines industry by requiring brokers to be licensed, monitored and directly responsible for compliance with all laws and regulations. On the carrier end, all carriers that issue surplus lines policies in the state of California are regulated by the insurance regulators in their states of domicile.

Surplus lines insurance is typically placed only in cases of unique, distressed or high-capacity risks, or new risks for which there is no loss history. If the admitted market will write a policy, the surplus lines market is forbidden from offering the same policy. Surplus line brokers can place policies with carriers who are licensed outside the state.
of California if and only if they cannot find an admitted carrier who will insure the risk. By law, a broker must receive at least three declinations in the admitted market before seeking to place a risk in the surplus lines market, unless the coverage has been previously deemed uninsurable by the California Department of Insurance and placed on the department’s Export List. Brokers must list these declinations in the policies they file with our association, or be referred to the department for failure to achieve compliance with state laws and regulations.

By placing surplus line policies, our brokers help consumers who could not otherwise get insurance to protect themselves against significant losses. Typically, our brokers place insurance for commercial interests, and the overwhelming majority of policies placed in the California surplus lines market are commercial policies. While it is true that the number of homeowners policies insured in the surplus lines market in California roughly doubled from 2012 to 2014, only a tiny fraction of the total number of homeowners policies placed in California are in surplus lines.1 The number of total homeowners’ policies is between 13,000 and 14,000, representing less than 2.5% of all surplus lines policies written in the state. The current total written premium for surplus lines homeowners’ insurance in California represents approximately 1.9% of all surplus lines premiums in the state.

In fact, the overwhelming majority of homeowners insurance in California is placed in the admitted market. According to U.S. Census Bureau estimates as of July 1, 2014, there were approximately 13.9 million housing units in the state of California.2 This means that only about one-tenth of one percent of all housing units in the state are insured in the surplus lines market.

We believe, based on the information we have, that the increase from roughly 6,000 surplus line homeowners policies placed in California in 2012 to the current total of more than 13,000 has been driven in large part by wildfires. While we do not specifically track the reasons that homeowners’ policies are issued, we have seen a number of factors that indicate some correlation between fires and the issuance of surplus homeowners policies. First, the higher the acreage burned per county correlates with the percent increase in policies.3 Second, the 2012 fire season was the third worst since 1960 in terms of area burned.4 Third, the number of fires per county correlates with the percentage increase in policies.5 Fourth, as the risk, or the perception of risk, increases, so does the number of policies filed.

Looking ahead, we think it is very possible, perhaps likely, that this trend will continue.

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1 2014 Annual Report to the Legislature and the California Insurance Commissioner on CEA Program Operations; California Earthquake Authority, available at: www.earthquakeauthority.com
2 Annual Estimates of Housing Units for the U.S.; U.S. Census Bureau, available at: www.factfinder.census.gov
3 Acreage burned available at: www.fire.ca.gov
4 Playing with Fire: How Climate Change and Development Patterns are Contributing to the Soaring Costs of Western Wildfires; Union of Concerned Scientists, available at: www.ucsusa.org
5 Number of fires available at: www.fire.ca.gov
a. From 1980 – 1989, there were approximately 140 wildfires.
b. From 1990 – 1999, there were approximately 160 wildfires.
c. From 2000 – 2012, there were approximately 250 wildfires\(^6\).

The 75 percent increase from 1980 to 2012 does not even take into account the large fires since then: notably the fires in Lassen County (2012), Tuolumne County (August 2013), Siskiyou County (August 2014) and Fresno County (July 2015) – all of which are included in the list of the top 20 largest California wildfires since 1932\(^7\).
d. The average length of wildfire season has increased substantially. In the early 1970s, it was five months. Today, it exceeds seven months\(^8\).
e. Since 1990, the average number of structures burned has more than tripled\(^9\).
f. Over the past 12 years, every state in the Western United States has experienced an increase in the average number of large wildfires per year compared to the annual average from 1980 – 2000.
g. The 2015 fire season set a new record for the number of acres burned in the United States: 68,151 wildfires, burning more than 10,125,149 acres nationwide\(^10\).
h. California is continually at high risk for wildfires.
   i. California’s 2015 total acres burned exceeded 900,000\(^11\).
   ii. California ranks as the number-one most wildfire-prone state, with 1.9 million households at high or extreme risk from wildfires, according to the 2010 U.S. Census\(^12\).
   iii. Of the Top 10 most costly wildland fires in the United States, seven were in California.
   iv. California saw 270 structures destroyed by wildfires in 2012, 713 in 2013 and 468 in 2014\(^13\).
   v. In 2015, the Valley fire alone burned 888 homes, and the Butte fire destroyed another 535 homes\(^14\).

I thank you again for the opportunity to testify here today, and I would be happy to take any questions that you might have.

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\(^6\) Western Wildfires & Climate Change; Infographic provided by Union of Concerned Scientists, available at www.ucsusa.org
\(^7\) Top 20 Largest California Wildfires; Cal Fire, available at: www.fire.ca.gov
\(^8\) Western Wildfires & Climate Change; Infographic provided by Union of Concerned Scientists, available at www.ucsusa.org
\(^10\) Statistics from the Insurance Information Institute; available at: http://www.iii.org/fact-statistic/wildfires
\(^12\) Statistics from the Insurance Information Institute, available at: http://www.iii.org/fact-statistic/wildfires
\(^13\) Statistics from Cal Fire; available at www.fire.ca.gov