

**CALIFORNIA EARTHQUAKE AUTHORITY
GOVERNING BOARD MEETING
MINUTES**

**Thursday, June 25, 2009
1:00 p.m.**

Location: Joe Serna Jr. Cal/EPA Headquarters Building
1001 I Street, Sierra Hearing Room
Sacramento, California

Members of the Governing Board in attendance:

Anne Sheehan, designee of Governor Arnold Schwarzenegger, Chairperson
Bruce Patton, designee of Insurance Commissioner Steve Poizner
Reid McClaran, designee of Insurance Commissioner Steve Poizner
Grant Boyken, designee of State Treasurer Bill Lockyer
Pedro Reyes, designee of Speaker of the Assembly Karen Bass
Dietrich Stroeh, designee of Chair of the Senate Rules Committee Darrell Steinberg

Members of the CEA Staff in attendance:

Glenn Pomeroy, Chief Executive Officer
Tim Richison, Chief Financial Officer
Bob Stewart, Chief Operations Officer
Chris Nance, Director of Communications and External Affairs
Joe Zuber, Senior Counsel
Susan Pitton, Governing Board and Advisory Panel Liaison
Danny Marshall, General Counsel

Also Present:

Dr. Ned Field, United States Geological Survey
Dr. Thomas Jordan, Southern California Earthquake Center, University of Southern California

- 1. The meeting was called to order at 1:00 p.m. A quorum was established.**
- 2. Consideration and approval of the minutes of the April 30, 2009, Governing Board meeting.**
 - Ms. Sheehan noted that the Assembly Bill referred to at the top of page 4 as AB 2280 is actually AB 280.

MOTION: Mr. Boyken moved approval of the April 30, 2009, Governing Board minutes as amended; Mr. Patton seconded the motion. Motion carried unanimously.

3. Executive Report by Chief Executive Officer Glenn Pomeroy, assisted by CEA executive staff. Mr. Pomeroy's report will include an update for the Board on federal and state legislative activities of interest to the CEA.

- Mr. Pomeroy noted that U.S. Senate Bill 886 has been introduced by the two Florida Senators, Bill Nelson and Mel Martinez. Known as the Catastrophic Obligation Guaranty Act (COGA), it would allow state catastrophe insurance entities that qualify to secure their post-event borrowing with a committed federal guarantee. It has not been scheduled for a hearing.
- Florida Congressman Ron Klein has introduced a similar measure in the House of Representatives, H.R.2555 – the Homeowners Defense Act of 2009.
- CEA has begun discussions with the insurance industry on the implications of the bills, including meetings with trade groups and insurance companies.
- In the California Legislature, Assemblyman Sam Blakeslee's AB 43, which would create a CEA Chief Mitigation Officer position and remove the CEA's staffing cap (currently 25 full-time employees), while retaining the overall spending cap of three percent of premium. AB 43 moved through the Assembly unanimously and was heard in the Senate Banking, Finance & Insurance Committee earlier this week, where it passed on a vote of 8–3. It is now with the Senate Appropriations Committee.
- AB 280 is now in the suspense file and likely will not move.

4. Chief Financial Officer Tim Richison will present a financial report.

- Mr. Richison reported that CEA's claim-paying capacity as of March 2009 is almost \$9.5 billion, which translates to a 1-in-545-year claim-paying capacity. There are approximately 780,000 policies in force. According to data from the California Department of Insurance, CEA writes 69 percent (by premium) of the residential earthquake insurance sold in California.
- The overall return on investment for the first quarter of 2009 was approximately 2.4 percent.
- The third principal payment on the 2006 issue of \$315 million of revenue bonds will be paid July 1, which will reduce the remaining outstanding bond balance to \$221.5 million.
- 2008 was the third-highest year for catastrophe losses worldwide, with insured losses of \$52 billion. By comparison, 2007 saw insured losses of \$28 billion, and in 2006 it was \$17 billion. Although the 2008 catastrophes occurred outside California and mostly outside the U.S., the result is potentially significant to CEA because catastrophes that generate insured losses reduce the amount of reinsurance capacity available for the CEA.

5. Mr. Richison will present and request Board approval of revised CEA reinsurance guidelines and a proposed CEA financial structure for 2010.

- Mr. Richison told the Board that CEA staff analyzed 172 financial structures. Those brought to the Board representing four different financing concepts. One of those financial concepts is the current financial structure, which uses reinsurance as the only means of risk transfer. A series of dynamic financial analysis (DFA) model projections were made, going out five years.
- The four financial structure options considered were:

Option 1 - Reinsurance only (the existing structure)

Option 2 - Reinsurance and issue additional revenue bonds

Option 3 - Post-event borrowing only

Option 4 - Post-event borrowing and reinsurance

Mr. Richison discussed pros and cons of each option and concluded with the staff recommendation: continue with the existing structure (Option 1). He recommended that the Board direct staff to:

1. Proceed with obtaining a proposed 2010 reinsurance-program option of \$2.9 billion, as outlined in financial structure Option 1;
2. Approve using the proposed guidelines for source of claim-paying capacity, revised as suggested in this meeting's Board memorandum, for obtaining the 2010 reinsurance program;
3. Bring to the Board at the August 2009 meeting a formal, complete recommendation for the CEA's 2010 reinsurance program.

Ms. Sheehan asked if anyone from the public would like to ask questions or address the Board on this issue. Seeing no response, she asked for the motion.

MOTION: Mr. Boyken moved approval of the three staff recommendations listed above. Mr. Patton seconded the motion. Motion carried unanimously.

6. CEA Advisory Panel member Jonathan Leong will provide a summary of the proceedings at the May 21, 2009 Panel meeting.

- Mr. Leong congratulated CFO Richison for his outstanding work.
- He remarked that Fitch and Moody's issuance of A ratings on the '06 revenue bonds was good news.
- He said he had attended a focus group put on by the CEA where various mitigation issues were discussed. He said that that 35 million people live within

20 miles of active earthquake faults, and of those, only a small percentage have retrofitted their homes in anticipation of a quake.

- Mr. Leong confirmed that the Panel supports the CEA's participation in the PBS earthquake-awareness programs.
- Mr. Leong said Wayne Coulon had been nominated again as Advisory Panel chair, with Mark Simmonds as vice chair. The Panel unanimously approved each selection.

7. General Counsel Danny Marshall will present and request Board approval of a proposed new CEA Investment Compliance Program.

- Mr. Marshall remarked that PricewaterhouseCoopers was used in a consulting role during development of the proposed Program, which is designed to optimize CEA's resources by having a good alignment between the business and compliance sides. Once established as a program, people will be able to look at what CEA is doing in investment compliance and say "yes, you are doing due diligence."
- He concluded by recommending two steps: first, the creation of the role of an independent investment compliance manager, and second, the creation of an investment committee.

MOTION: Mr. Boyken moved to approve the implementation of the proposed new CEA Investment Compliance Program. Mr. Patton seconded the motion. Motion carried unanimously.

8. Director of Communications and External Affairs Chris Nance will seek Board approval of a contract with Ogilvy Public Relations Worldwide for communications services.

- Mr. Nance stated that the CEA had been working with a new public relations firm since an agreement was executed with Ogilvy Public Relations Worldwide on May 22, 2009. The firm was a finalist under the most recent Request for Qualifications issued to the public, seeking such firms.
- Two projects have been identified and are now underway:
 1. A study of branding, which the CEA has never accomplished. A string of activities and actions, including focus groups throughout the state, will establish the CEA brand. As an example, a branding process result will inform production of a marketing kit that agents and producers can use to help tell a compelling story about CEA products—rather than talk price alone, those selling CEA products can associate values with them. Cost of the study is estimated at \$144,000, which is within budget and consistent with the Business Implementation Plan.

2. A market research study, to be conducted using what's called a "conjoint" design, will seek to survey consumer attitudes in a mechanism that will simulate the insurance-policy-purchase decision. The survey will be done online so consumers can easily see all options for which information and opinions are sought. Estimated cost for this study is \$92,800.

Both studies will be conducted in consultation with Ogilvy Public Relations Worldwide and will involve the use of highly qualified subcontractors.

- Mr. Nance concluded with the staff recommendations—approve the two projects with Ogilvy and authorize the expenditure levels set forth and direct relevant CEA staff to secure and accomplish all requisite documentation for audit, legal, and other compliance-related purposes.

MOTION: Mr. Patton moved approval of the staff recommendations. Mr. Boyken seconded the motion. Motion carried unanimously.

9. Mr. Pomeroy will introduce Thomas H. Jordan, Ph.D., Director, Southern California Earthquake Center, University of Southern California; and Ned Field, Ph.D., United States Geological Survey, who will make a presentation to the Board in support of a proposed seismic science research project (UCERF3) intended to provide direct and indirect benefits to the CEA. Mr. Pomeroy will request Board approval of the project, which is targeted for commencement in 2009.

- Chief Operations Officer Bob Stewart introduced a project to accomplish the Uniform California Earthquake Rupture Forecast, Version 3 (UCERF3). UCERF2, completed in early 2008, delivered the first statewide uniform earthquake-rupture forecast based on the same science throughout the state, an important step. UCERF3 is the next step in the evolution of the UCERF model, and it will be a 30-month project.
- Dr. Jordan began by saying that earthquake loss estimation, fundamental to the CEA, comprises a number of pieces; but most fundamental is earthquake-rupture forecasting. From that, one gets probabilistic measures of shaking intensity and then can derive estimates of earthquake losses. The UCERF2 model was a groundbreaking step that now provides a uniform earthquake-rupture forecast for all of California with a comprehensive methodology.
- Dr. Field added that UCERF2 is a static earthquake model that does not account sufficiently for aftershocks. UCERF3 will be designed to monitor rate changes of seismicity in aftershocks and then use those changes to modify the probabilities of much larger earthquakes. It will be a dynamic earthquake forecast that can adapt to what is occurring on the ground.

- Dr. Jordan listed three major benefits of UCERF3:
 1. It will provide the best available science to account for fault-to-fault jumping, earthquake triggering and clustering, and several other improvements to the current UCERF2 model. This will allow CEA to incorporate triggering and clustering into its loss models, to reconsider aftershock-related provisions in earthquake insurance policies, and to rapidly assess the increases and decreases in regional risk that follow large earthquakes.
 2. It will provide new data and new scientific understanding to sharpen earthquake probabilities and refine uncertainties in earthquake risk, which will improve loss modeling and the science supporting the ratemaking process and financial analysis.
 3. It will build on CEA's successful partnership with USGS, the California Geological Survey, and SCEC, among the international leaders in earthquake science, with a proven ability to deliver consensus products. This will allow CEA to leverage investments it has already made in the UCERF framework, and to leverage new resources that will be committed to UCERF improvements by the three participating organizations.
- He concluded by saying that the bottom line is that CEA participation will ensure delivery of an improved and dynamic UCERF on a schedule that meets CEA's needs and helps it maintain its global leadership in the support and use of scientific earthquake forecasting.

MOTION: Mr. Patton moved approval of the recommendation to fund UCERF3. Mr. Boyken seconded the motion. Motion carried unanimously.

10. Mr. Pomeroy will present and seek Board approval of his appraisal of Mr. Stewart's performance under his performance-management plan and seek a minor amendment to Mr. Stewart's employment contract with the CEA.

- Mr. Pomeroy reported to the Board that Bob Stewart has performed in his position of chief operations officer at the highest level, and he noted Mr. Stewart's experience in the insurance industry and his professionalism, demonstrated daily in the CEA office to the benefit of CEA staff. Mr. Pomeroy said Mr. Stewart is a delight to work with, and that the CEA is fortunate to have Mr. Stewart on staff. He summed up his views of Mr. Stewart's performance by terming his overall appraisal "glowing," and he recommend extension of Mr. Stewart's employment contract, as follows.
- Mr. Pomeroy recommended a two-year contract extension with an opt-out, if needed. He also noted that Mr. Stewart had suggested he not take a salary increase, which Mr. Pomeroy had not requested but which he reluctantly supported; no COLA was warranted, on account of a slight decrease in the cost of living figures the CEA uses to compute executive-employment COLAs.

- Board members, in turn, praised Mr. Stewart's performance, calling his work "of the highest caliber" and uniformly expressing their appreciation.

MOTION: Mr. Patton moved approval to formally accept Mr. Pomeroy's performance appraisal of Mr. Stewart and to approve an extension of the Stewart employment-contract term by two years with a one-year opt out, if necessary, with appropriate documentation to be executed on behalf of the Board and provided to Mr. Stewart. Mr. Boyken seconded the motion. Motion carried unanimously.

11. Senior Counsel Joe Zuber will brief the Board on the renewal of the CEA's Directors & Officers and Employment Practices Liability Insurance coverages and request the Board's approval to pay the annual policy premium.

- Mr. Zuber noted that the premium amount for this insurance policy is the same as last year's, \$116,085. He stated staff's recommends binding the renewal coverage before the expiration date of the current coverage at the end of July 2009.

MOTION: Mr. Boyken moved approval of the staff recommendation to renew the policy and pay the annual policy premium. Mr. Patton seconded the motion. Motion carried unanimously.

12. The Board will meet in closed session to discuss personnel matters and litigation matters, as permitted by California Government Code section 11126, subdivisions (a) and (e), respectively.

- The Board entered closed session at 3:08 p.m. and resumed its proceedings in open session at 4:50 p.m. Ms. Sheehan stated that the Board had met to discuss confidential personnel matters, as well as to receive and discuss advice on litigation matters and to instruct counsel.

13. Public comment on items that do not appear on this agenda and public requests that those matters be placed on a future agenda.

- There were no questions or comments from the public.

14. Adjournment.

- The meeting was adjourned at 4:56 p.m.