

**CALIFORNIA EARTHQUAKE AUTHORITY
GOVERNING BOARD MEETING
MINUTES**

**Thursday, October 28, 2010
1:03 P.M.**

Location: State Capitol
Room 447
Sacramento, California

Members of the Governing Board in attendance:

Anne Sheehan, designee of Governor Arnold Schwarzenegger
Grant Boyken, designee of State Treasurer Bill Lockyer
Bruce Patton, designee of Insurance Commissioner Steve Poizner
Deborah Doty, designee of Speaker of the Assembly John Pérez
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, Communications and External Affairs
Susan Pitton, Governing Board and Advisory Panel Liaison
Danny Marshall, General Counsel

Also Present:

John Forney, Raymond James, Inc.

- 1. The meeting was called to order at 1:03 p.m. A quorum was established.**
- 2. Consideration and approval of the Minutes of the August 26, 2010, Governing Board Meeting.**

MOTION: Mr. Patton moved approval of the August 26, 2010, Governing Board minutes; seconded by Mr. Boyken. Motion passed 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 reported that since the last Board meeting, Congress has been in a campaign mode so there is very little to report. Still, there is some possibility that the concepts CEA has been working on in Washington, D.C., may be taken up in the final days of this Congressional session.
- The California Legislature passed, and the Governor signed, AB 2746, a bill that authorizes the Board to hire a Chief Mitigation Officer.
- Mr. Pomeroy said he had had the opportunity to meet in New York with the rating agencies that deal with CEA credit issues; the visits went well again this year.
- Our Chief Actuary, Shawna Ackerman, is working on an analysis regarding steps CEA might consider undertaking to position itself with certainty for a second-event capability.
- This year was the second annual statewide Great California ShakeOut, and it was a tremendous success, with a record 7.9 million people signed up to participate.

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

- Mr. Richison stated that the CEA has more than \$4.1 billion in cash and reserves and more than \$3.6 billion available to pay claims.
- At the next Board meeting, Mr. Richison told the Board, he will bring forward a recommendation that the Board approve an additional amount of CEA claim-paying capacity in the form of reinsurance.
- CEA is heavily invested in long-term U.S. Treasuries but maintains some short-term U.S. Treasuries and U.S. Agencies as well.

5. John Forney of Raymond James, Inc., the CEA's independent financial advisor, will brief the Board on the current state of the financial markets.

- Mr. Forney made the following observations:
 - Activities in the financial markets are at the very core of what the CEA does.
 - In the last eight months, the stock market has gone up, and interest rates have gone down. The recession is over, but unemployment is still high and consumer confidence is still low and housing markets remain troubled, keeping financial markets jittery.

- Our country's appetite for leverage is low now, and the factors that are driving underlying growth in the economy are weak.
 - The municipal-debt markets remain functional and stable.
 - Insurance markets also have recovered nicely from the financial crisis and have stabilized to a large degree.
 - In the housing market, of the 52 million mortgages in the U.S. almost 8 million are in delinquency—extreme delinquency or in foreclosure.
 - Total debt in the United States as a percentage of GDP has quadrupled; for every dollar of income we produce, we have four dollars of debt.
 - The Federal Reserve Bank has over \$2.3 trillion in assets; there are only two banks in the U.S. that have \$2 trillion in assets, J.P. Morgan/Chase and Bank of America.
 - Equity markets have experienced robust growth, but going forward, six or seven percent a year as opposed to historical 10 or 12 percent probably is realistic, which may be a problem many of pension funds across the country.
 - Rates in the Treasuries market have come down to almost zero and stayed there, making borrowing cheap now. Last year was a record year for issuance in the corporate-debt market.
 - Top-line insurance-premium revenues have been down three years in a row for the first time ever in the history of our country, and this has affected the insurance industry in a negative way.
 - All in all, however, the reinsurance industry has recovered well from the crisis and is in good shape.
- Mr. Forney recommended that CEA maintain its conservative risk-transfer policy, but given the fundamental change in “the world as we know it,” the CEA should continue to press for ways to find more certainty in its capital structure and produce more value for consumers. He said that people want financial partners they can trust and value they can feel, and CEA's financial structure can support both.
 - Mr. Forney noted that when the CEA considers its \$4 billion of money invested, it wants to “spread out” to minimize systemic risk within the portfolio.
 - If and when passed, the COGA initiative that was endorsed and advanced by CEA would be a good example of how CEA can obtain a needed increase in certainty

in its capital structure; for that and other reasons, CEA should continue to pursue the COGA program.

Mr. Patton asked Mr. Forney his opinion of catastrophe bonds.

Mr. Forney replied that cat bonds are attractive an investor standpoint because it's a non-correlated asset based on the value of the underlying risk, not on a correlation with other economic investments, at least in theory. He added that cat bonds could become a useful part of the CEA's risk-transfer portfolio, but that amounts available historically in the financial markets would mean that it would not or could not replace reinsurance; still, from a diversity standpoint cat bonds would have their place.

Ms. Sheehan asked Mr. Forney to describe the "greatest risk" for CEA moving forward, with the exception of an earthquake?

Mr. Forney responded that, with the exception of an earthquake, the greatest risk to the CEA is probably a major disaster in the world that wreaks havoc on the reinsurance industry.

6. Director of Communications and External Affairs Chris Nance will seek Board approval to permit the CEA to enter a joint powers agreement with the California Emergency Management Agency (known as "CalEMA")

- Ongoing discussions between the CEA and CalEMA regarding a JPA are going well.
- The CEA currently has more than \$20 million set aside to help consumers, and CEA staff is looking at a program that would enable CEA to make available financial incentives for retrofits; being a part of and supporting this JPA would provide that opportunity.
- The CEA has established its residential retrofit programming in California's State Hazard Mitigation Plan, which was adopted by FEMA a few weeks ago.
- CEA staff worked to implement the first statewide building code for seismic retrofitting of residential structures.
- The Authority recently issued an RFQ to identify candidates interested in administering a statewide retrofit program, probably through the proposed JPA.
- A JPA offers an important benefit to its member, importantly the JPA's debts and obligations are not the responsibility of the members or any of them. And from a funding perspective, particularly if federal funds are available, those funds could be received directly and then spent by an entity separate from the CEA.

- The CEA would likely make voluntary contributions to a JPA, more or less on a “pay-as-you-go” basis.
- JPA staffing would be handled by contract, primarily through the private sector, with oversight by both the JPA board as well as the respective boards of the JPA members.
- The overall goals are to increase residential retrofitting and decrease residential earthquake damage, while serving as an example to other states.

In response to a question from Mr. Patton, General Counsel Marshall stated that two things that CEA staff and consultants are working on diligently are (1) the insulation of CEA assets from the liabilities or actions of the JPA of which CEA might become a member, and (2) to make sure that when the JPA is formed, the CEA’s tax status is not affected.

7. Director of Communications and External Affairs Chris Nance will report on the second statewide Great California ShakeOut and will seek Board approval to use remaining budgeted funds.

- Mr. Nance reported that on October 21st at 10.21 a.m. 7.9 million people participated in the Great California ShakeOut by dropping, covering, and holding on.
- CEA sought to take advantage of the opportunity offered by ShakeOut participation to enhance statewide awareness of the CEA and promote the purchase of earthquake insurance. In fact, just one week into CEA Great ShakeOut programming, there was a 650 percent increase in consumer (weekend) traffic on the CEA Web site.
- The CEA surveyed participating agents, and nearly 40 percent said that the ShakeOut media campaign generated requests for additional information and premium quotes, and policy sales. More than 93 percent of agents surveyed said they would like to participate in future campaigns and would recommend this type of programming to their colleagues.
- The greatest improvement for the CEA was in earned media. The CEA fashioned press conferences that had participation from FEMA, CalEMA, USGS, CGS, the American Red Cross, and local emergency and response agencies.
- The Board is now being asked to approve use of the approximately \$550,000 in funds remaining from the ShakeOut budget for next year’s communications programming, to cover the costs of producing a CEA-branded television ad, purchasing additional TV advertising, updating the CEA logo, and streamlining the *Putting Down Roots* publication.

MOTION: Mr. Boyken moved to approve the use of remaining budgeted funds of approximately \$550,000 from the ShakeOut budget to fulfill the needs stated in the staff memo; seconded by Mr. Patton. Motion passed unanimously.

8. Chief Operations Officer Bob Stewart will present for Board consideration and approval the application of Metropolitan Direct Property and Casualty Insurance Company (known as “MetDirect”), to become a CEA participating insurer.

- Mr. Stewart asked for Board approval of the application of Metropolitan Direct Property and Casualty Insurance Company (known as “MetDirect”) to become a CEA participating insurer.
- In addition, he said staff recommends the Board’s approval include a condition to granting the application for participation: based on staff’s analysis of data provided by Metropolitan, the company should be required under applicable law to pay risk-capital surcharges.

MOTION: Mr. Boyken moved to approve the resolution to approve the application and authorize continued negotiations with MetDirect; seconded by Mr. Patton. Motion passed unanimously.

9. Mr. Richison will seek Board approval to contract with additional investment managers selected in a competitive procurement and execute the resulting contracts with Dwight Asset Management Company, BlackRock, State Street Global Advisors, Longfellow Investment Management Co., Income Research & Management and Cypress Management.

- Mr. Richison stated that each of the proposed contracts would be for a five-year term, with an option for a single two-year extension at CEA’s sole discretion.

MOTION: Mr. Patton moved to approve the staff recommendation of the addition of State Street Global Advisors, Cypress Management, Longfellow Investment Management Co., and Income Research & Management as CEA primary fund investment managers and Dwight Asset Management company and BlackRock as CEA liquidity fund investment managers; and to authorize CEO Glenn Pomeroy to proceed with negotiations and execute the contracts on behalf of the CEA; seconded by Mr. Boyken. Motion passed unanimously.

10. Staff will present for Board consideration and approval a proposed 2011 Governing Board meeting calendar.

MOTION: Mr. Patton moved to approve the proposed calendar; seconded by Mr. Boyken. Motion passed unanimously.

11. The Board will meet in Closed Session to discuss personnel and litigation matters, as permitted by California Government Code Section 11126, subdivisions (a) and (e), respectively.

- The Board entered closed session at 2:29 p.m. and resumed its proceedings in open session at 2:54 p.m. Ms. Sheehan reported that the Board exercised its discretion under the appropriate Government Code provisions to take advice from counsel on litigation matters. The Board had nothing to report.

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

There was no public comment.

13. Adjournment.

The meeting was adjourned at 2:54 p.m.