JLK Rosenberger
Certified Public Accountants

CALIFORNIA EARTHQUAKE AUTHORITY

Financial Statements and
Independent Auditors' Report

December 31, 2012 and 2011

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Independent Auditors' Report

To the Governing Board
California Earthquake Authority

Report on the Financial Statements

We have audited the accompanying balance sheets of California Earthquake Authority (CEA) as of December 31, 2012 and 2011, and the related statements of revenues, expenses, and changes in net position and cash flows for the years then ended, and the related notes to financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence that we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the financial position of California Earthquake Authority as of December 31, 2012 and 2011, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3 through 10 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audits were conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying schedules of participating insurer capital contributions, participating insurer premiums written, participating insurer unearned premiums, participating insurer commissions and participating insurer operating costs, on pages 30 to 34, are presented for purposes of additional analysis and are not a required part of the basic financial statements. The schedules of participating insurer capital contributions, participating insurer premiums written, participating insurer unearned premiums, participating insurer commissions and participating insurer operating costs are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

JLK Rosenberger, LLP

Glendale, California
August 20, 2013

CALIFORNIA EARTHQUAKE AUTHORITY

Management's Discussion and Analysis

History and Financing

This discussion provides an assessment by management of the financial position, revenues, expenses, changes in net position, cash flows and liquidity of California Earthquake Authority (CEA). Readers are encouraged to consider the information presented in conjunction with the financial statements as a whole, which follow Management's Discussion and Analysis.

Following the unprecedented losses from the 1994 Northridge earthquake, many insurance companies either stopped or severely restricted selling new homeowners' insurance policies in California. The insurer response was largely due to state law that requires insurers to offer earthquake insurance when selling or renewing residential property insurance.

In September 1996, legislation to create CEA was approved by the California State Legislature. On November 26, 1996, the State of California Insurance Commissioner certified that all statutory conditions necessary for CEA to become operational had been met, and CEA began writing earthquake policies on December 1, 1996. CEA is overseen by a three member Governing Board consisting of the Governor, the Treasurer, and the Insurance Commissioner or their designees. The Speaker of the Assembly and the Chairperson of the Senate Rules Committee or their designees serve on the Governing Board as nonvoting members. The Governing Board establishes premium rates, subject to the prior approval of the Insurance Commissioner. The Governing Board is advised by an 11 member advisory panel, consisting of members of the public, consumers and insurance industry representatives.

CEA uses its available capital (net position) to leverage approximately $10.2 billion in claims-paying capacity at December 31, 2012. CEA's claims-paying capacity is determined from CEA's available capital, risk-transfer coverage, available letters of credit, debt, and post-event prospective participating insurance company assessments. CEA derives its capital from participating insurer capital contributions and from increases in net position generated from the sale of earthquake insurance policies. CEA is exempt from federal income tax and from state insurance-premium tax. California Insurance Code section 10089.44 provides, in pertinent part, that "… premiums collected by the authority shall be exempt from collection of the state's insurance premium tax, and the amount of tax foregone by the state shall be considered for all purposes a contribution by the state and its citizens to the capital and operating revenues of the authority."

CEA has approximately 842,000 policyholders at December 31, 2012, most of whom insure single-family dwellings through CEA. CEA offers a basic residential earthquake policy to homeowners, which includes coverage for the insured dwelling and limited coverage for contents and loss-of-use if the residence is uninhabitable due to an earthquake. CEA also offers policies to condominium unit owners and renters. For an additional premium, CEA policyholders can significantly increase insured limits on contents and for loss-of-use, and homeowners can lower their CEA policy deductible from 15 percent to 10 percent.

CEA employs contract employees and employees subject to civil-service provisions. By law, the number of employees subject to civil-service provisions is limited to 25. On June 28, 2013 legislation was signed that eliminated this staffing cap.

Using the Report

While CEA is an instrumentality of the state, the State of California's General Fund is not liable for CEA claims, losses, or other liabilities. However, CEA meets the definition of a governmental organization, as defined by accounting principles generally accepted in the United States of America. CEA's financial statements for the years ended December 31, 2012 and 2011 have been prepared using accounting standards applicable to governmental entities. This financial report consists of three financial statements with accompanying notes. The balance sheets, prepared on the accrual basis of accounting, include all assets, liabilities and net position of CEA. The statements of revenues, expenses, and changes in net position, also prepared on the accrual basis, take into account all revenues and expenses for CEA regardless of when cash is received or paid. The statements of cash flows reflect the actual cash receipts and disbursements for a specified period of time.

Condensed Balance Sheets

CEA's assets, liabilities and net position as of December 31 are summarized as follows:

	2012	2011	2010
Assets			
Cash and investments	$ 4,804,687,807	$ 4,508,924,403	$ 4,273,041,274
Premium receivable, net	42,878,950	41,893,958	49,595,737
Unearned ceded premiums	1,325,001	-	-
Deferred policy acquisition costs	39,031,916	41,619,480	40,674,396
Other current assets	18,285,153	100,880,639	17,283,960
Total current assets	4,906,208,827	4,693,318,480	4,380,595,367
Reinsurance deposit	14,634,112	5,029,836	-
Capital assets	458,543	499,468	1,413,255
Total assets	$ 4,921,301,482	$ 4,698,847,784	$ 4,382,008,622
Liabilities and Net Position			
Unearned premiums	$ 290,632,289	$ 309,899,331	$ 302,862,221
Other current liabilities	47,571,589	42,317,010	39,616,100
Total current liabilities	338,203,878	352,216,341	342,478,321
Revenue bonds payable, noncurrent portion	94,500,000	126,000,000	157,500,000
Compensated absences, noncurrent portion	559,767	96,041	91,694
Total liabilities	433,263,645	478,312,382	500,070,015
Net position:			
Invested in capital assets, net of related debt	458,543	499,468	1,413,225
Restricted, expendable	237,918,554	205,889,564	168,559,583
Unrestricted	4,249,660,740	4,014,146,370	3,711,965,799
Total net position	4,488,037,837	4,220,535,402	3,881,938,607
Total liabilities and net position	$ 4,921,301,482	$ 4,698,847,784	$ 4,382,008,622

Condensed Balance Sheets (Continued)

Assets

Total assets grew $222.5 million (5%) in 2012 and $316.8 million (7%) in 2011. The 2012 and 2011 increases were primarily due to an increase in net position of $267.5 million and $338.6 million, respectively. Cash and investments grew $295.8 million (7%) and $235.9 million (6%), in 2012 and 2011, respectively. Investments are managed by external managers under the guidance of CEA. U.S. Treasuries, short-term investments and cash-equivalent securities comprise 100% of CEA's investment portfolio.

Premium receivable balances increased $1.0 million (2%) and decreased $7.7 million (16%) in 2012 and 2011, respectively. The 2012 increase in premium receivables was due to a significant reduction in the allowance for doubtful accounts at year end. The 2011 decrease in premium receivables was due to CEA receiving a larger portion of weekly premiums remitted by CEA participating insurers in the last week of the year than in the last week of the previous year.

Deferred policy acquisition costs, consisting of unearned participating insurer commissions and operating costs, are deferred and amortized ratably over the terms of the underlying policies. Deferred policy acquisition costs decreased $2.6 million (6%) in 2012, which corresponds with the decrease in policies that were unearned at the end of 2012. Deferred policy acquisition costs increased $0.9 million (2%) in 2011, which corresponds with the increase in policies that were unearned at the end of 2011. The operating cost reimbursement rate during 2012 was 3.09% and 2011 was 3.43%.

The 2012 decrease in other current assets of $82.6 million (82%) was primarily due to a combination of no security receivable at year end, which was a reduction of $68.5 million, and no capital contributions receivable at year end, which was a reduction of $17.3 million. The 2011 increase in other current assets of $83.6 million (484%) was primarily due to a combination of a security receivable of $68.5 million, and an increase in the capital contributions receivable of $14.1 million. The security receivable was from an investment that matured on Saturday, December 31, 2011. The proceeds from the matured investment were received on Monday, January 2, 2012, when the bond-market opened.

Reinsurance deposit increased $9.6 million in 2012 and $5.0 million in 2011. The 2012 increase was due to CEA entering into two new reinsurance agreements that required a deposit during the year. The 2011 increase was due to CEA entering into the 1st reinsurance agreement that required a deposit.

Liabilities

Unearned premiums represent the pro rata portion of the premiums written related to the remaining term of policies in force. Unearned premiums decreased $19.3 million (6%) and increased $7.0 million (2%) in 2012 and 2011, respectively. The 2012 decrease was due to the decrease in premiums written caused by a rate reduction that became effective January 1, 2012. The 2011 increase was due to the increase in premiums written by the end of 2011.

Other current liabilities include loss and loss adjustment expense reserves, which are not significant since California has not suffered a major earthquake during CEA's existence. Other current liabilities increased $5.3 million (12%) in 2012 largely due to an increase in accrued reinsurance premium expense of $4.3 million related to new reinsurance contracts. Other current liabilities increased $2.7 million (7%) in 2011 largely due to an accrued reinsurance premium expense of $1.7 million.

Condensed Balance Sheets (Continued)

Liabilities (Continued)

Revenue bonds payable decreased by $31.5 million (25%) in 2012 resulting from the annual 10% principal reduction payment. The bonds were initially issued in June 2006, totaling $315 million. The revenue bonds bear interest at a fixed rate of 6.196% and mature in 2016 requiring annual 10% principal reduction payments.

Compensated absences – noncurrent increased by $0.5 million (483%) in 2012 due to recognizing civil service leave as part of this balance. Prior to 2012 civil service leave was not included in the financial statements due to the fact that the liability was only payable by CEA if an employee left civil service, which was not a common occurrence since CEA's inception. However, due to employees leaving civil service in 2012, it is deemed appropriate to recognize this liability in addition to the contract employees that was already recognized. As such, the entire balance is treated as a current year addition to CEA.

Net Position

CEA classifies its net position into three components, invested in capital assets, net of related debt; restricted-expendable and unrestricted. Invested in capital assets, net of related debt consists of equipment and leasehold improvements, and there is no debt related to the purchase of these assets. Restricted net position includes the net position of the Earthquake Loss Mitigation Fund (Mitigation Fund), unspent bond proceeds restricted for payment of claims as defined in the debt agreements offset by underlying debt, funds held for debt service by the revenue bond trustee, and investment income earned on the bond proceeds restricted as pledged revenue for debt service. The Mitigation Fund was created by statute and related funds must be used solely for the establishment and operation of earthquake mitigation programs. The remaining net position of CEA is classified as unrestricted. CEA's net position grew $267.5 million (6%) and $338.6 million (9%) in 2012 and 2011, respectively. The 2012 increase was comprised of the underwriting profit of $243.8 million, premium tax contributions from the State of California of $13.1 million, and net investment income of $18.4 million. The 2011 increase was comprised of the underwriting profit of $282.7 million, premium tax contributions from the State of California of $14.4 million, and the increase in contributed capital of $20.8 million.

Condensed Statements of Revenue, Expenses, and Changes in Net Position

CEA's operating results are presented in the following table:

	2012	%	2011	%	2010	%
Underwriting income:						
Premium written	$ 569,235,337	100%	$ 612,830,953	100%	$ 603,127,689	100%
Less premium ceded – Reinsurance	(222,817,695)		(200,622,675)		(221,788,128)	
Net premium written	346,417,642	61%	412,208,278	67%	381,339,561	63%
Change in net unearned Premiums	19,267,042		(7,037,110)		(3,867,476)	
Net premium earned	365,684,684	64%	405,171,168	66%	377,472,085	63%
Expenses:						
Loss and loss adjustment expenses	649,221		299,164		75,036	
Other underwriting expenses	121,284,705		122,142,585		118,816,262	
Total expenses	121,933,926	21%	122,441,749	20%	118,891,298	20%
Underwriting profit	243,750,758	43%	282,729,419	46%	258,580,787	43%
Non-operating income and expenses:						
Net investment income	18,435,449		27,893,141		22,486,654	
Other non-operating income	13,564,995		14,935,389		14,447,146	
Other non-operating expenses	(8,248,767)		(7,733,154)		(9,286,272)	
Total non-operating income and expenses	23,751,677	4%	35,095,376	6%	27,647,528	5%
Capital contributions	-		20,772,000		5,470,000	
Increase in net position	267,502,435	47%	338,596,795	55%	291,698,315	48%
Net position, beginning of year	4,220,535,402		3,881,938,607		3,590,240,292	
Net position, end of year	$ 4,488,037,837		$ 4,220,535,402		$ 3,881,938,607	

The increase in net position was $267.5 million in 2012, which resulted in a net profit margin of 47%, and $338.6 million in 2011, which resulted in a net profit margin of 55%. Net investment income decreased $9.5 million (34%) in 2012. The decrease was largely due to a $4.2 million decrease in the change of unrealized investment gains on U.S. Treasuries and a decrease of $7.1 million in investment income. Net investment income increased $5.4 million (24%) in 2011. The increase was largely due to a $13.7 million increase in the change of unrealized investment gains on U.S. Treasuries and a decrease of $8.9 million in investment income. CEA's net premiums written decreased $65.8 million (16%) in 2012 and increased $30.8 million (8%) in 2011. The 2012 decrease is due to a $43.6 million reduction in written premiums and an increase in premiums ceded of $22.2 million. The 2011 increase is due to a $9.7 million growth in written premiums and a decrease in premiums ceded of $21.2 million.

Condensed Statements of Revenue, Expenses, and Changes in Net Position (Continued)

The variance of the change in unearned premiums increased $26.3 million and decreased $3.2 million in 2012 and 2011, respectively. The 2012 variance is due to a decrease in unearned premium caused by a decrease in premiums for policies not effective at the end of 2012. The 2011 variance is due to an increase in unearned premium was caused by a slight increase in premiums for policies not effective at the end of 2011.

In 2012 and 2011, CEA's loss and loss adjustment expenses were essentially zero due to California not experiencing any significant earthquakes.

In 2012, the decrease in other underwriting expense of $0.9 million was largely due to a $4.3 million decrease in participating insurer commissions and operating expense, a $1.3 million decrease in pro forma premium taxes, $4.1 million increase in marketing services and $0.7 million increase in compensated absences expense. In 2011, the increase in other underwriting expense of $3.3 million was largely due to a $0.9 million increase in participating insurer commissions and operating expense, a $0.5 million increase in pro forma premium taxes, and a $1.9 million total increase in various underwriting expenses.

Other non-operating income decreased $1.4 million in 2012 and increased $0.5 million in 2011 primarily due to the change in the State of California premium tax contribution. Other non-operating expenses increased $0.5 million in 2012 due primarily to the contribution to the California Residential Mitigation Program. The 2011 decrease of $1.6 million is due primarily to a reduction in net financing expenses.

Capital contributions decreased $20.8 million in 2012 and increased $15.3 million in 2011. The 2012 decrease was due to no capital contributions necessary in the current year. The 2011 increase was due to Nationwide Insurance Company joining CEA as a participating insurer as of November 2011.

Condensed Statements of Cash Flows

Primary sources of cash included cash flows from operations and capital contributions received from participating insurers. The primary use of cash was for operating expenses, repayment of debt, and the purchase of short-term and long-term investment securities.

The cash flows of CEA are summarized as follows:

	2012	2011	2010
Net cash provided by operating activities	$ 234,419,608	$ 308,461,371	$ 277,639,512
Net cash used in noncapital financing activities	(21,991,315)	(32,719,584)	(37,229,465)
Net cash used in capital and related financing activities	(316,030)	(80,424)	(774,371)
Net cash used in investing activities	(43,888,910)	(211,457,391)	(198,332,217)
Net increase in cash and cash equivalents	168,223,353	64,203,972	41,303,459
Cash and cash equivalents, beginning of year	160,660,834	96,456,862	55,153,403
Cash and cash equivalents, end of year	$ 328,884,187	$ 160,660,834	$ 96,456,862

Cash from operating activities decreased $74.0 million (24%) in 2012 and increased $30.8 million (11%) in 2011. The 2012 decrease resulted from a decrease in cash received from premiums of $54.0 million and an increase in payments for reinsurance of $23.7 million. The 2011 increase resulted from an increase in cash received from premiums of $15.9 million and a decrease in payments for reinsurance of $15.3 million.

Condensed Statements of Cash Flows (Continued)

The $10.7 million (33%) change in cash used in noncapital financing activities for 2012 was a result of $10.7 million increase in capital contribution installments received from Nationwide Insurance Company, and the change in interest paid and interest income on revenue bond proceeds in 2012 compared to 2011. The $4.5 million (12%) change in cash used by noncapital financing activities for 2011 was a result of $4.0 million in capital contribution installments received from Nationwide Insurance Company and the change in interest paid and interest income on revenue bond proceeds in 2011 compared to 2010.

The change in cash used in investing activities for 2012 was $167.6 million (79%) and $13.1 million (7%) for 2012 and 2011, respectively, and reflects CEA's decision, fully implemented in 2012, to continue to prudently extend the duration of its portfolio as a result of the lagging economy, continued all-time low Treasury rates, and the Federal Reserve's postponement of any monetary tightening through the remainder of 2013.

Liquidity

CEA maintains a highly liquid investment portfolio in order to be able to quickly pay claims in the event of a large earthquake. As of December 31, 2012, 21.06% of the portfolio was scheduled to mature in 90 days or less, securities maturing between 91 days and one year accounted for 25.96% of the portfolio, while securities maturing between one to five years accounted for the remaining 52.98% of the portfolio, with a total portfolio modified duration of approximately one and half years. Based on earthquake modelers' results of analyzing the CEA's portfolio, management believes CEA has sufficient liquidity to meet its obligations as they become due resulting from an earthquake or series of earthquakes. The probability of an earthquake or series of earthquakes occurring that would deplete CEA's liquidity and the associated claims-paying capacity is estimated to be 0.19% in any one year. CEA pays policyholder claims from its claims-paying capacity. The following depicts CEA's claims-paying capacity in effect as of December 31, 2012, in millions of dollars:

CEA capital available for claims	$	4,250
Risk transfer financial products		3,557
Revenue bonds		314
Post-earthquake industry assessments (2nd Layer)		1,558
Post-earthquake industry assessments (New Layer)		500
Total	$	10,179

Additionally, CEA is able to recover amounts under risk transfer contracts when policyholder claims reach certain levels.

Capital Assets and Debt Activity

Capital Assets

CEA's investment in capital assets as of December 31, 2012 was $458,543 (net of accumulated depreciation). No major capital asset purchases were made in the current year and none are expected in the coming year.

Debt Administration

At December 31, 2012, CEA had total long-term debt obligations of $126,000,000 in the form of revenue bonds. During the year, no additional debt was acquired while $31,500,000 of revenue bonds was retired. Additional information on CEA's long-term debt can be found in Note 3 in the Notes to the Financial Statements.

Capital Assets and Debt Activity (Continued)

Current Economic Factors and Conditions

If the current California unemployment conditions continue, CEA could see in the near future a reduction of Californians purchasing earthquake insurance.

Requests for Information

This financial report is designed to provide a general overview of CEA's finances for all those interested. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to California Earthquake Authority, 801 K Street, Suite 1000, Sacramento, CA 95814.

CALIFORNIA EARTHQUAKE AUTHORITY

Balance Sheets
As of December 31, 2012 and 2011

	2012	2011
Assets		
Current assets:		
Cash and investments:		
Cash and cash equivalents	$ 276,406,016	$ 111,091,346
Restricted cash	52,478,171	49,569,488
Restricted investments	314,130,654	310,862,316
Investments	4,161,672,966	4,037,401,253
Total cash and investments	4,804,687,807	4,508,924,403
Premiums receivable, net of allowance for doubtful accounts of $6,801,039 and $10,561,115	42,878,950	41,893,958
Capital contributions receivable	-	17,310,000
Interest receivable	14,806,316	12,035,424
Securities receivable	-	68,858,008
Prepaid reinsurance premiums	1,325,001	-
Prepaid transformer maintenance premium	3,365,306	2,546,102
Deferred policy acquisition costs	39,031,916	41,619,480
Other current assets	113,531	131,105
Total current assets	4,906,208,827	4,693,318,480
Transformer reinsurance premium deposit	14,634,112	5,029,836
Capital assets, net	458,543	499,468
Total assets	$ 4,921,301,482	$ 4,698,847,784
Liabilities and Net Position		
Current liabilities:		
Unearned premiums	$ 290,632,289	$ 309,899,331
Accounts payable and accrued expenses	5,849,676	3,370,720
Reinsurance premium payable	6,068,468	1,676,612
Loss and loss adjustment expense reserves	12,909	-
Compensated absences, current	254,066	40,167
Securities payable	-	871,423
Revenue bond payable, current	31,500,000	31,500,000
Revenue bond interest payable	3,886,470	4,858,088
Total current liabilities	338,203,878	352,216,341
Revenue bond payable, noncurrent	94,500,000	126,000,000
Compensated absences, noncurrent	559,767	96,041
Total liabilities	433,263,645	478,312,382
Net Position:		
Invested in capital assets, net of related debt	458,543	499,468
Restricted, expendable	237,918,554	205,889,564
Unrestricted	4,249,660,740	4,014,146,370
Total net position	4,488,037,837	4,220,535,402
Total liabilities and net position	$ 4,921,301,482	$ 4,698,847,784

See accompanying notes to financial statements.

CALIFORNIA EARTHQUAKE AUTHORITY

Statements of Revenues, Expenses, and Changes in Net Position
For the Years Ended December 31, 2012 and 2011

	2012	2011
Underwriting income:		
Premiums written	$ 569,235,337	$ 612,830,953
Less premiums ceded	(222,817,695)	(200,622,675)
Net premiums written	346,417,642	412,208,278
Change in unearned premiums	19,267,042	(7,037,110)
Net premiums earned	365,684,684	405,171,168
Operating expenses:		
Loss and loss adjustment expense	649,221	299,164
Participating insurer commissions	58,867,335	60,623,577
Participating insurer operating costs	18,237,966	20,776,606
Reinsurance broker commissions	4,800,000	4,800,000
Pro forma premium taxes	13,120,011	14,446,598
Other underwriting expenses	26,259,393	21,495,804
Total operating expenses	121,933,926	122,441,749
Underwriting profit	243,750,758	282,729,419
Non-operating income and expenses:		
Net investment income	18,435,449	27,893,141
Other income	444,984	488,791
Financing expenses, net	(7,274,681)	(7,389,584)
Mitigation fund expenses	(474,086)	(343,570)
California Residential Mitigation Program contribution	(500,000)	-
State of California premium tax contribution	13,120,011	14,446,598
Total non-operating income	23,751,677	35,095,376
Contributed capital	-	20,772,000
Increase in net position	267,502,435	338,596,795
Net position, beginning of year	4,220,535,402	3,881,938,607
Net position, end of year	$ 4,488,037,837	$ 4,220,535,402

See accompanying notes to financial statements.

CALIFORNIA EARTHQUAKE AUTHORITY

Statements of Cash Flows
For the Years Ended December 31, 2012 and 2011

	2012	2011
Cash Flows from Operating Activities:		
Cash received from premiums	$ 568,250,345	$ 622,232,732
Cash payments for premiums ceded - reinsurance	(230,174,320)	(206,522,001)
Cash payments for operating expenses	(92,603,150)	(98,997,304)
Cash payments to employees for service	(11,053,267)	(8,252,056)
Net cash provided by operating activities	234,419,608	308,461,371
Cash Flows from Noncapital Financing Activities:		
Capital contributions received from participating insurers	17,310,000	6,652,830
Repayment of revenue bonds	(31,500,000)	(31,500,000)
Interest paid on revenue bonds	(10,049,349)	(11,981,989)
Interest income on revenue bonds proceeds	1,803,050	3,620,784
Other income	444,984	488,791
Net cash used in noncapital financing activities	(21,991,315)	(32,719,584)
Cash Flows from Capital and Related Financing Activities:		
Acquisition of equipment	(316,030)	(80,424)
Net cash used in capital and related financing activities	(316,030)	(80,424)
Cash Flows from Investing Activities:		
Proceeds from maturities of investments	4,026,369,413	3,692,317,795
Purchases of investments	(4,120,992,295)	(3,951,135,195)
Investment income	52,816,706	49,263,651
Investment expense	(2,082,734)	(1,903,642)
Net cash used in investing activities	(43,888,910)	(211,457,391)
Net increase in cash and cash equivalents	168,223,353	64,203,972
Cash and cash equivalents, beginning of year	160,660,834	96,456,862
Cash and cash equivalents, end of year	$ 328,884,187	$ 160,660,834
Reconciliation to Balance Sheets:		
Cash and cash equivalent	$ 276,406,016	$ 111,091,346
Restricted cash	52,478,171	49,569,488
Cash and cash equivalents, end of year	$ 328,884,187	$ 160,660,834

See accompanying notes to financial statements.

CALIFORNIA EARTHQUAKE AUTHORITY

Statements of Cash Flows (Continued)
For the Years Ended December 31, 2012 and 2011

	2012	2011
Reconciliation of operating income to net cash provided by operating activities:		
Underwriting profit	$ 243,750,758	$ 282,729,419
Adjustments to reconcile underwriting profit to net cash provided by operating activities:		
Depreciation on equipment	356,955	994,212
Pro forma premium tax expense	13,120,011	14,446,598
Contribution to California Residential Mitigation Program	(500,000)	-
Mitigation Fund Expenses	(474,086)	(343,566)
Changes in operating assets and liabilities:		
Premiums receivable	(984,992)	7,701,779
Risk capital surcharge receivable	-	1,700,000
Deposit with reinsurer	(9,604,276)	(5,029,836)
Prepaid transformer maintenance premium	(819,204)	(2,546,102)
Deferred policy acquisition costs	2,587,564	(945,084)
Other assets	17,574	(88,610)
Unearned ceded premiums	(1,325,001)	-
Unearned premiums	(19,267,042)	7,037,110
Loss and loss adjustment expense reserves	12,909	-
Reinsurance premium payable	4,391,856	1,676,612
Compensated absences payable	677,625	44,514
Accounts payable and accrued expenses	2,478,957	1,084,325
Net cash provided by operating activities	$ 234,419,608	$ 308,461,371

Non-cash Investing, Capital and Financing Activities

The change in the fair value of investments, which is included as a component of net investment income in the Statements of Revenues, Expenses and Changes in Net Position, was $(2.5) million and $1.7 million in 2012 and 2011, respectively. Premium tax contributed by the State of California and recognized as a component of expense in the Statements of Revenues, Expenses, and Changes in Net Position was $13.1 million and $14.4 million in 2012 and 2011, respectively.

See accompanying notes to financial statements.

1. Reporting Entity and Summary of Significant Accounting Policies

Reporting Entity

The California Earthquake Authority (CEA) is a privately financed, publicly managed authority that provides insurance coverage for earthquake damage to residential property owners, condominium owners, mobile homeowners, and renters in the state of California. In September 1996, legislation to create CEA was approved by the California State Legislature. On November 26, 1996, the State of California Insurance Commissioner certified that all statutory conditions necessary for CEA to become operational had been met, and CEA began writing earthquake policies on December 1, 1996. CEA is overseen by a three member Governing Board consisting of the Governor, the Treasurer, and the Insurance Commissioner or their designees. The Speaker of the Assembly and the Chairperson of the Senate Rules Committee or their designees serve on the Governing Board as nonvoting members. The Governing Board is advised by an 11 member advisory panel, consisting of members of the public, consumers and insurance industry representatives.

CEA policies are sold to policyholders by participating insurers of CEA. Insurance companies admitted to write residential property insurance in California and who elected to become participating members of CEA sign Insurer Participation Agreements with the Insurance Commissioner and CEA. Under these agreements, participating insurers act as independent contractor agents on behalf of CEA by performing policy and claims services which include policy issuance, premium collection, and claims adjustment. Under the agreements, CEA reimburses participating insurers for non-claims related costs incurred by these companies in servicing CEA policies. The operating cost reimbursement is 3.09% of written premium. The producer commission is equal to 10% of written premium of all new and renewal CEA policies. Additionally, participating insurers receive reimbursement for expenses associated with servicing CEA claims equal to 9% of paid claims. As of December 31, 2012, there are 21 participating insurers of which 16 insurers are writing CEA policies. Four participating insurers account for 73% of CEA’s written premiums.

CEA has eligibility requirements that compel CEA to issue and renew policies if the insured structure has no pre-existing, non-cosmetic earthquake damage and the policyholder has a companion policy of residential property insurance from a participating insurer.

In the event that a natural disaster program is enacted by Congress, the Advisory Panel is required to prepare a plan to dissolve CEA or to conform the sections of the California Insurance Code regarding CEA to the federal program and recommend an action plan to the CEA Governing Board and the California State Legislature.

Basis of Accounting

While CEA is an instrumentality of the state, the State of California's General Fund is not liable for CEA claims, losses, or other liabilities. However, CEA meets the definition of a governmental organization, as defined by accounting principles generally accepted in the United States of America.

1. Reporting Entity and Summary of Significant Accounting Policies (Continued)

Basis of Accounting (Continued)

CEA is accounted for as an enterprise fund and is financed and operated in a manner similar to that of a private business enterprise. CEA uses the economic resources measurement focus and the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America. Under this method, revenues are recorded when earned and expenses are recorded when incurred. In preparing the financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the balance sheet and revenue and expenses for the period, as well as the disclosure of contingent assets and liabilities. Actual results could differ from those estimates applied in the preparation of the accompanying financial statements.

Operating revenues are those revenues that are generated from providing earthquake insurance policies. All other revenues are reported as non-operating revenues. Operating expenses are those costs related to providing those earthquake insurance policies. All other expenses are reported as non-operating expenses.

Revenue Recognition

Premiums are recognized as earned on a pro rata basis over the policy contract period. All premium rates charged by CEA must be approved by the State of California Insurance Commissioner before use. Unearned premiums represent amounts written which relate to coverage in future periods.

Premiums paid or accrued by CEA under reinsurance agreements are accounted for as a reduction in the related premium revenue earned and amortized over the remaining reinsurance contract period. Unearned ceded premium is the pro rata portion of premiums ceded applicable to the unexpired period of reinsurance coverage.

Use of Restricted/Unrestricted Net Position

When an expense is incurred for purposes for which both restricted and unrestricted net position is available, CEA's policy is to apply unrestricted net position before applying any restricted net position available.

CEA's policy could change if California experiences a major earthquake event.

Cash and Cash Equivalents

For purposes of the statement of cash flows, CEA considers investments in certificates of deposit, U.S. treasuries, commercial paper, corporate bonds, and bankers' acceptances with original maturities of three months or less, to be cash equivalents. Restricted cash and cash equivalents are comprised of unspent bond proceeds, debt service sinking funds and monies transferred to the Earthquake Loss Mitigation Fund (Mitigation Fund).

1. Reporting Entity and Summary of Significant Accounting Policies (Continued)

Investments

Investments consist primarily of certificates of deposit, U.S. treasuries, commercial paper, corporate bonds, and bankers' acceptances, as authorized by California Insurance Code (Code) section 10089.6. All investments are reported at fair value in the balance sheets. Fair value is the amount at which a financial instrument could be exchanged in a current transaction between willing parties, and is determined from published data provided by the exchanges, computerized pricing sources, securities custodians, and other authoritative sources. CEA is permitted to invest in securities eligible in California Government Code section 16430. Restricted investments are comprised of unspent bond proceeds and monies transferred to the Mitigation Fund. CEA intends to hold all investments to maturity unless there is an earthquake or series of earthquakes causing significant damage in California warranting CEA's need to liquidate securities to pay policyholder claims.

Capital Assets

Capital assets are stated at historical cost. The capitalization threshold for assets with a useful life beyond one year is $500. Depreciation is computed using the straight-line method over the useful lives as follows:

Leasehold improvements	Shorter of useful life or remaining lease term
Computer equipment and software	3 years
Furniture and other equipment	5 years
Capital leases	Shorter of useful life or remaining lease term

Risk-Capital Surcharge

Under California Insurance Code sec. 10089.16(d), effective July 1, 2008, the CEA Governing Board must calculate a risk-capital surcharge one year after the date that a new participating insurer first places or renews business into CEA. The law provides that each annual risk-capital surcharge must equal CEA's increased cost of providing or securing capacity to insure the new participant's excess earthquake-insurance risk.

Deferred Policy Acquisition Costs

Acquisition costs, consisting of participating insurer commissions and operating costs, are deferred and amortized over the terms of the underlying policies. Deferred acquisition costs are limited to the estimated recoverable value of such costs. The determination of estimated recoverable value gives effect to the premium to be earned, losses and loss adjustment expenses incurred, investment income to be earned, and certain other costs expected to be incurred as the premium is earned.

1. Reporting Entity and Summary of Significant Accounting Policies (Continued)

Losses and Loss Adjustment Expenses

Reserves for insurance losses and loss adjustment expenses include the accumulation of case estimates for claims reported, claims incurred but not reported, and estimates of expenses for investigating and adjusting all incurred claims. The reserve is established at a level that management estimates to be sufficient to satisfy those claims. Estimates are revised as more information becomes available. Since CEA's inception, there has not been a major earthquake. If a major California earthquake were to occur, there would be a significant increase in the reserve for claims and claim adjustment expenses. CEA does not have any significant unpaid claims reported as of December 31, 2012.

If CEA's Governing Board determines that CEA's net position, bond proceeds, additional participating insurer capital contributions and reinsurance proceeds are exhausted and that no source of additional funds is available to CEA to pay policyholder claims, the Governing Board is required to develop a plan for approval by the State of California Insurance Commissioner to pay policyholder claims on a pro rata or installment basis. In such circumstances, the insurance code states that the commissioner shall order CEA to cease renewing or accepting new earthquake insurance policies.

Participating Insurer Capital Contributions

Each insurer that elected to participate in CEA during its first year of operations was required to contribute as its share of CEA's initial operating capital, an amount equal to $1,000,000,000 multiplied by the percentage representing that insurer's residential earthquake insurance market share as of January 1, 1994. Insurers that elect to participate in CEA after December 1, 1996, are required to make an initial capital contribution calculated using their residential earthquake insurance market share as of January 1, 1994, or the latest date for which such market share information is available to CEA, whichever contribution amount is greater. As of December 31, 2012, participating insurer capital contributions totaled $777 million and were 100% funded.

Participating Insurer Assessments

The California Insurance Code (Code) states that, subject to certain maximum limits as set forth in the Code, CEA has the power to make additional assessments of participating insurers in the event of a major California earthquake, subject to the approval of the State of California Insurance Commissioner. CEA's ability to make certain additional assessments for the 1st industry assessment layer pertaining to the participating insurers expired December 1, 2008. However, during 2007 CEA worked with the state legislature and participating insurers to establish a new industry assessment layer, which commenced on December 1, 2008. The maximum assessment amount of the new industry assessment layer as of December 31, 2012, was $500 million. CEA continued to retain its 2nd industry assessment layer of $1.558 billion.

As of December 31, 2012, participating insurers have a cumulative residential property insurance market share of approximately 81% of the total residential property insurance market in California based on written premium. If participating insurers withdraw their participation in CEA such that the cumulative residential property insurance market share is less than 65%, the Insurance Commissioner is required by law to make recommendations to the California Legislature for the continuation or termination of CEA.

1. Reporting Entity and Summary of Significant Accounting Policies (Continued)

Net Position

CEA classifies its net position into three components, net position invested in capital assets, net of related debt; restricted-expendable and unrestricted net position. There is no debt related to capital assets, so the balance of net position invested in capital assets consists only of the capital assets balance. Restricted net position includes the net position of the Mitigation Fund, unspent bond proceeds restricted for payment of claims as defined in the debt agreements and funds held for debt service by the revenue bond trustee offset by underlying debt, and investment income earned on the bond proceeds restricted as pledged revenue for debt service.

Income Taxes

In a private letter ruling dated November 8, 1996, the Internal Revenue Service determined CEA to be an integral part of the State of California for federal income tax purposes. As such, CEA is exempt from federal income tax.

State of California Premium Tax

California Insurance Code section 10089.44 provides that "Notwithstanding any other provision of law, premiums collected by the authority shall be exempt from collection of the state's insurance premium tax, and the amount of tax foregone by the state shall be considered for all purposes a contribution by the state and its citizens to the capital and operating revenues of the authority." As a result, CEA is exempt from remitting state premium tax. State premium tax contributions were $13,120,011 and $14,446,598 for the years ended December 31, 2012 and 2011, respectively.

Compensated Absences

Employees accrue vacation, holiday and sick leave benefits. However, unused sick leave is not included in compensated absences because they do not vest to employees. CEA contract employees are paid at the time of termination from CEA employment. CEA civil-service employees are paid at the time of termination only for employees that have left civil service employment. CEA civil-service employees that retain employment within civil service are removed as a liability for CEA, without a payout, as CEA is no longer responsible for the vested balance of these employees.

2. Cash and Investments

As of December 31, 2012 and 2011, CEA had the following cash and investments:

	December 31, 2012					
	Investment Maturities (in Years)					
	Less than 1	1-2	2-3	3-4	4-5	Total
U.S. Treasuries	$ 1,759,586,447	$ 746,862,483	$ 942,547,239	$ 600,917,964	$ 236,599,477	$4,286,513,610
U.S. agencies	406,477,430	-	-	-	-	406,477,430
U.S. Gov't money market funds	27,874,662	-	-	-	-	27,874,662
Cash	7,043,183	-	-	-	-	7,043,183
Commercial paper	76,778,922	-	-	-	-	76,778,922
Total	$ 2,277,760,644	$ 746,862,483	$ 942,547,239	$ 600,917,964	$ 236,599,477	$ 4,804,687,807

	December 31, 2011					
	Investment Maturities (in Years)					
	Less than 1	1-2	2-3	3-4	4-5	Total
U.S. Treasuries	$ 2,305,085,737	$ 907,398,231	$ 293,038,782	$ 271,924,587	$ 202,472,254	$ 3,979,919,591
U.S. agencies	387,678,169	-	-	-	-	387,678,169
U.S. Gov't money market funds	25,590,837	-	-	-	-	25,590,837
Cash	2,921,259	-	-	-	-	2,921,259
Commercial paper	112,814,547	-	-	-	-	112,814,547
Total	$ 2,834,090,549	$ 907,398,231	$ 293,038,782	$ 271,924,587	$ 202,472,254	$ 4,508,924,403

The table below identifies the investment types that are authorized for CEA by the California Government Code or CEA's investment policy, where more restrictive. The table also identifies certain provisions of CEA's investment policy that address interest rate risk, credit risk, and concentration risk.

Liquidity Fund:

Authorized Investment Type	Maximum Maturity	Maximum Percentage of Portfolio	Maximum Investment In One Issuer
U.S. Treasury Securities	180 days	None	None
Federal Agency Securities	180 days	50%	25%
Bankers Acceptances (BA)	180 days	25%	5%
Certificates of Deposit	180 days	25%	5%
Commercial Paper	179 days	25%	5%
Corporate Bonds/Notes	180 days	25%	5%

2. Cash and Investments (Continued)

Primary Reserve Fund:

Authorized Investment Type	Maximum Maturity	Maximum Percentage of Portfolio	Maximum Investment In One Issuer
U.S. Treasury Securities	5 years	None	None
Federal Agency Securities	N/A	None	None
Bankers Acceptances (BA)	N/A	None	None
Certificates of Deposit	N/A	None	None
Commercial Paper	N/A	None	None
Corporate Bonds/Notes	N/A	None	None

Mitigation Fund:

Authorized Investment Type	Maximum Maturity	Maximum Percentage of Portfolio	Maximum Investment In One Issuer
U.S. Treasury Securities	90 days	None	None
Federal Agency Securities	90 days	50%	25%
Bankers Acceptances (BA)	90 days	25%	5%
Certificates of Deposit	90 days	25%	5%
Commercial Paper	90 days	25%	5%
Corporate Bonds/Notes	90 days	25%	5%

Claims Paying Fund:

Authorized Investment Type	Maximum Maturity	Maximum Percentage of Portfolio	Maximum Investment In One Issuer
U.S. Treasury Securities	5 years	None	None
Federal Agency Securities	180 days	50%	25%
Bankers Acceptances (BA)	180 days	25%	5%
Certificates of Deposit	180 days	25%	5%
Commercial Paper	179 days	25%	5%
Corporate Bonds/Notes	180 days	25%	5%

Cash Deposits

The only contractual provision that CEA has in regards to cash deposits is that CEA is required, by the CEA Revenue Bond Indenture, to set-aside into a trust account, written premium on a monthly basis of $3.625 million to cover interest and principle payment amounts in case of default.

Interest Rate Risk

As a means of limiting its exposure to fair value losses resulting from rising interest rates, CEA's investment policy limits all securities purchased to a maximum maturity duration of 181 days, except for U.S. Treasuries. U.S. Treasuries are allowed to have maturities of up to 5 years as long as CEA's combined portfolio does not exceed a maximum modified duration of 1.75 years. As of December 31, 2012, CEA's combined portfolio had a maximum modified duration of 1.5 years.

2. Cash and Investments (Continued)

Credit Risk

CEA investment policy limits investments in banker's acceptances and commercial paper to issuers with the highest rating category by all rating agencies that rate the issuer. The policy limits investments in corporate bonds to the top three ratings issued by nationally recognized rating services. As of December 31, 2012, 90% of the portfolio consisted of U.S. Treasuries and 10% of the portfolio consisted of U.S. Agencies, U.S. Government money market funds that invest exclusively in obligations of the U.S. Treasury, cash and commercial paper.

CEA's investments are rated as follows:

Security Type	Moody's	Standard & Poors
US Treasury	Aaa	AA+
Federal Home Loan Mortgage Corporation	Aaa	AA+
Federal National Mortgage Association	Aaa	AA+
Commercial Paper:		
General Electric Capital Corporation	A1	AA+
JP Morgan Chase & Co.	A1	A
Toyota Motor Credit Corporation	Aa3	AA-

Concentration of Credit Risk

There is no concentration of investments in any one non U. S. Governmental issuer, which is not explicitly guaranteed, that represents 5% or more of total investments.

Custodial Credit Risk

Custodial credit risk for deposits is the risk that, in the event of failure of a depository financial institution, CEA will not be able to recover its deposits or will not be able to recover collateral securities that are in the possession of an outside party. CEA has no policy that would limit the exposure to custodial credit risk for deposits. As of December 31, 2012 and 2011 all CEA deposits were covered by federal depository insurance (FDIC).

Investment Income

Total investment income is comprised of interest, realized gains and losses, and unrealized gains and losses due to changes in the fair value of investments held at year end. Investment income earned on unspent bond proceeds are offset against related interest expense and classified as financing expenses, net on the statements of revenues, expenses, and changes in net position.

2. Cash and Investments (Continued)

Investment income for the years ended December 31, 2012 and 2011 are as follows:

	2012	2011
U.S. agency securities and government money market accounts	$ 473,196	$ 634,357
U.S. Treasuries	24,079,425	30,942,605
Other short-term investments	233,416	129,948
Interest income	24,786,037	31,706,910
Change in fair value of investments	(2,464,804)	1,710,656
Less investment expenses	(2,082,734)	(1,903,642)
Total investment income	$ 20,238,499	$ 31,513,924

The following is a reconciliation of investment income to the statements of revenues, expenses, and changes in net position:

	2012	2011
Investment income included in financing expenses	$ 1,803,050	$ 3,620,783
Net investment income	18,435,449	27,893,141
Total investment income	$ 20,238,499	$ 31,513,924

The change in fair value of investments for the years ended December 31, 2012 and 2011 are calculated as follows:

	2012	2011
Fair value of investments at the end of year	$ 4,475,803,620	$ 4,348,263,569
Add: Proceeds of investments matured	3,957,511,405	3,761,175,803
Add: Amortization of premium and discount	32,724,193	20,862,314
Less: Change in realized gain/loss	(119,581)	-
Less: Cost of investments purchased	(4,120,120,872)	(3,952,006,618)
Less: Fair value of investments at the beginning of year	(4,348,263,569)	(4,176,584,412)
Change in fair value of investments	$ (2,464,804)	$ 1,710,656

Fair Value of Financial Instruments

The recorded value of other receivables and payables which are financial instruments approximates fair value due to the short-term nature of these assets and liabilities.

3. Long-Term Liabilities

The following is a summary of long-term liabilities as of December 31, 2012:

	Balance January 1, 2012	Additions	Retirements	Balance December 31, 2012	Due within One Year
Revenue Bond	$ 157,500,000	$ -	$ (31,500,000)	$ 126,000,000	$ 31,500,000
Compensated Absences	136,208	752,833	(75,208)	813,833	254,066
Total	$ 157,636,208	$ 752,833	$ (31,575,208)	$ 126,813,833	$ 31,754,066

CEA issued its first long-term debt of $315 million in fixed rate revenue bonds on July 20, 2006 to enhance claims paying capacity. The net proceeds from the revenue bonds were deposited into the Claims Paying Account and were used to purchase investments according to CEA's investment policy. The proceeds will only be used for future payments of earthquake policyholder claims and related loss adjustment expenses and may not be used to repay principal and interest of the debt. Revenue bond proceeds may be used for payment of claims after CEA exhausts its capital available for claims and any capacity made available by reinsurance contracts. Repayment of debt does not affect the level of the Claims Paying Account.

The bonds are payable from future pledged policyholder premiums. The bonds bear interest at 6.169% and are federally taxable. Interest is payable semi-annually, beginning January 1, 2007. The bonds are due July 1, 2016, but are subject to annual mandatory sinking-fund payments as indicated below. The bonds are subject to optional redemptions at any time prior to maturity, in whole or in part, at the option of CEA. CEA is subject to certain bond covenants, the most restrictive of which requires a debt service coverage ratio of 3:1.

Future scheduled debt service payments, including mandatory sinking-fund payments, for CEA's long-term debt are as follows as of December 31, 2012:

	Principal	Interest	Total
2013	$ 31,500,000	$ 6,801,323	$ 38,301,323
2014	31,500,000	4,858,088	36,358,088
2015	31,500,000	2,914,853	34,414,853
2016	31,500,000	971,617	32,471,617
Total requirements	$ 126,000,000	$ 15,545,881	$ 141,545,881

Interest paid during the year was $8,744,558 and $10,687,793 for 2012 and 2011, respectively.

4. Net Position

As described in note 1, net position includes restricted and unrestricted portions. The following table details the components of net position as it relates to restricted and unrestricted:

	2012	2011
Restricted:		
Mitigation Fund	$ 25,801,060	$ 25,537,617
Claims Paying Account (bonds)	212,117,494	180,351,947
Total restricted net position	$ 237,918,554	$ 205,889,564
Unrestricted:		
Contributed capital	$ 777,384,796	$ 777,384,796
Premium tax contribution	182,170,089	169,050,078
Other unrestricted	3,290,105,855	3,067,711,496
Total unrestricted net position	$ 4,249,660,740	$ 4,014,146,370

5. Risk Transfer

CEA cedes risk to reinsurers under catastrophe excess-of-loss reinsurance contracts for purposes of limiting its maximum exposure. All contracts provide coverage for losses as well as allocated loss adjustment expenses. Although the ceding of risk does not discharge CEA from its primary responsibility to its policyholders, the insurance company that assumes the coverage assumes responsibility to reimburse CEA for the related liability. Management believes that its reinsurers are and will continue to be able to satisfy their obligations under the reinsurance agreements. To date, losses have been recovered only under the supplemental coverages reinsurance contracts. In the event that legislation is enacted by the State of California that has the effect of increasing a reinsurer's exposure to loss under the reinsurance contract, a reinsurer has the right to cancel the reinsurance contract.

During 2012, Embarcadero Reinsurance Ltd. (Embarcadero Re), an independent Bermuda insurance company, completed two offering of catastrophe bonds to unrelated investors of $150 million and $300 million. In connection with the offerings, Embarcadero Re entered into two reinsurance agreements (covering a three year period) with CEA. The first agreement provides up to $150 million of reinsurance coverage defined at 50% of $300 million of losses in excess of a retention of $2.9 billion. The second agreement provides coverage up to $300 million in losses in excess of a retention of $6.2 billion. During 2011, Embarcadero Re completed an offering of catastrophe bonds to unrelated investors of $150 million. In connection with the offering, Embarcadero Re entered into a reinsurance agreement (covering a three year period) with CEA, providing reinsurance coverage up to $150 million of losses in excess of a retention of $3.4 billion. Under the terms of the agreements with Embarcadero Re, CEA is obligated to pay annual reinsurance premiums. These agreements are subject to adjustments of the retention at the beginning of the second and third annual contract periods based on exposure adjustments and losses. Reinsurance limits will be reduced by any amounts paid to CEA under the reinsurance agreement. These reinsurance agreements meet the requirements to be accounted for as reinsurance in accordance with the guidance for reinsurance contracts.

CEA has a deposit to ensure its performance under the terms of its agreements with Embarcadero Re. The deposit was $14,634,112 and 5,029,836 at December 31, 2012 and 2011, respectively.

5. Risk Transfer (Continued)

Certain aggregate excess reinsurance contracts allowed for an adjustment of premium, based on the average aggregate insurance in-force and the exposure adjustment limit, as defined in the contracts. As of December 31, 2012 in accordance with these terms, CEA did not have a premium adjustment expense against the contracts. During 2012, CEA continued to cede insurance to reinsurers under catastrophe excess-of-loss reinsurance contracts provided maximum limits of $3.405 billion at varying attachment points.

6. Statutory Compliance

The State of California Insurance Code limits CEA's "operating expenses" to 3% of its "premium income." In calculating this limitation, CEA has determined that its premium income is its reported premiums written and that its operating expenses do not include certain start-up expenses and certain credits and payments, including payments to reinsurers, payments to investment managers and advisors, payments to participating insurers, or payments of agent commissions. Operating expenses, as determined by CEA, totaled $15.0 million and $11.0 million for the years ended December 31, 2012 and 2011, respectively, and did not exceed 3% of premiums written.

7. Commitments and Contingencies

CEA is a defendant in various legal actions arising from the normal course of business. Management does not believe that the ultimate disposition of these actions will have a material adverse effect on CEA's financial position or results of operations.

CEA leases office facilities and equipment under various non-cancelable operating lease agreements that expire through December 2016. Rental expense associated with the lease agreements was $704,306 and $638,812 for the years ended December 31, 2012 and 2011, respectively. Future minimum rental payments under these agreements are as follows:

	Amount
2013	$ 722,190
2014	709,208
2015	711,446
2016	192,677
Total	$ 2,335,521

8. Mitigation Fund

California Insurance Code (Code) Section 10089.37 created the Earthquake Loss Mitigation Fund (Mitigation Fund) as a "sub-account of CEA". According to statute, the Mitigation Fund must be used solely for the establishment and operation of an earthquake loss mitigation program. The Code requires CEA to annually transfer an amount equal to the lesser of 5% of investment income or $5 million to the Mitigation Fund if deemed actuarially sound by a consulting actuary. The transfer and setting aside of those monies into the Mitigation Fund sub-account have been formally approved by the CEA Governing Board. It is the opinion of the general counsel of CEA and of CEA's outside counsel that the monies that reside in the Mitigation Fund sub-account within CEA are by statute not available to pay policyholder or other claims against CEA.

As of December 31, 2012 and 2011, the balance sheets include expendable restricted net position related to the Mitigation Fund totaling $25,801,060 and $25,537,617 respectively. The expendable restricted net position of the Mitigation Fund as of December 31, 2012 includes the potential annual transfer amount of $1,238,300, which is subject to actuarial review and formal approval of CEA's Governing Board as discussed in the previous paragraph.

9. Defined Benefit Pension Plan

All CEA civil-service employees participate in the California Public Employees' Retirement System (CalPERS), an agent multiple-employer public employee defined benefit pension plan. CalPERS provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. CalPERS acts as a common investment and administrative agent for participating public entities with the State of California. Benefit provisions and all other requirements are established by state statute. Copies of CalPERS' annual financial reports may be obtained from their Executive Office located at 400 P Street, Sacramento, California 95814.

Funding Policy

CEA has civil service employees that are members of the following bargaining units: Professional Administrative, Financial and Staff Service (Bargaining Unit 1); Attorneys and Hearing Officer (Bargaining Unit 2) and Professional Scientific (Bargaining Unit 10), which are required by bargaining unit agreements to contribute 8.0% to 9.0% of their annual covered salary. CEA is required to contribute remaining amounts necessary to fund the benefits for the actuarial members, using the actuarial basis recommended by CalPERS actuaries and actuarial consultants and adopted by CalPERS Board of Administration. For the fiscal year ended December 31, 2012 the employer contribution rate by plan was 20.503% for Tier 1 State Miscellaneous and 20.457% for Tier 2 State Miscellaneous. For the fiscal year ended December 31, 2011 the employer contribution rate by plan was 18.175% for Tier 1 State Miscellaneous and 17.025% for Tier 2 State Miscellaneous. CEA makes the contributions required of CEA civil service employees on their behalf and for their account. All of CEA's civil service employees are classified as members of the State Miscellaneous Plans.

9. Defined Benefit Pension Plan (Continued)

Annual Pension Cost

CEA's employee contributions in 2012 and 2011 were $192,348 or 8.3% of annual covered payroll and $165,756 or 8.2% of annual covered payroll, respectively. The employer's contributions in 2012 and 2011 were $422,532 or 21.6% of annual covered payroll and $321,152 or 16.4% of annual covered payroll, respectively.

Three-Year Trend Information for PERS

Fiscal Year Ended	Annual Pension Cost (APC)	Percentage of APC Contributed	Net Pension Obligation
12/31/12	$ 422,532	100%	--
12/31/11	321,152	100%	--
12/31/10	315,595	100%	--

The benefits are based on the highest 12 consecutive months compensation during their employment. The state's funding policy is to make the minimum annual contributions required by applicable regulations and charges CEA for its allocable share of such contributions based on a percentage of payroll. CEA has no legal obligation for benefits under this plan.

10. Defined Contribution Plan

CEA sponsors the California Earthquake Authority Retirement Plan (Plan), a 401(A) defined contribution savings plan for contract employees. The Plan is administered by UBS Financial Services. Employees contribute 5% of base compensation. CEA contributes 12.71% of the employee's base compensation. The maximum base compensation for 2012 and 2011 was $250,000 and $245,000, respectively. The contributions are funded semi-annually and allocated to CEA based on employee contributions.

Employees are fully vested in their account from beginning of employment. CEA has no legal obligation for benefits under this Plan. Only the CEA Board has the authority to amend the Plan provisions. Employee contributions in 2012 and 2011 were $60,967 and $47,344, respectively. CEA's contributions in 2012 and 2011 were $155,115 and $121,624, respectively.

11. Post-Employment Benefits

CEA has no obligations to former employees for benefits after their employment other than compensation related to earned vacation and severance. The liability for earned but untaken leave, such as vacation, personal leave days, or holiday credit, has been accrued to contract and civil service employees.

12. Risk Management

CEA is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. CEA has insurance policies with private insurance companies for the following policies:

Policy Type	Policy Limits
Workers Compensation	$ 1,000,000
Financial Institution Bond	$ 1,500,000
Business Liability	$ 5,000,000
Director and Officers Liability	$10,000,000

Management believes such coverage is sufficient to preclude any significant uninsured losses to CEA.

13. California Residential Mitigation Program

On August 16, 2011, CEA entered into a Joint Powers Agreement with the California Emergency Management Agency (Cal EMA) to create the California Residential Mitigation Program (CRMP) for the purpose of supplying grants, loans, and loan guarantees (and related assistance and incentives) to owners of dwellings in California. The CRMP Governing Board is comprised of two employees from each, CEA and Cal EMA. Previously, on December 10, 2011, CEA's Governing Board approved a $500,000 transfer from the CEA Mitigation Fund to the CRMP when certain conditions were met, mostly relating to the formation of the CRMP. In April 2012, those conditions were met and CEA transferred the funds to the CRMP.

14. Subsequent Events

Management has evaluated subsequent events through August 20, 2013, which is the date the financial statements were made available to be issued. No events, other than those disclosed below and elsewhere in these financial statements, have occurred subsequent to December 31, 2012 requiring recording or disclosure in these financial statements.

Subsequent to year end, legislation was passed that removed the staffing cap of a maximum 25 CEA employees subject to civil service provisions.

SUPPLEMENTARY INFORMATION

CALIFORNIA EARTHQUAKE AUTHORITY

Schedule of Participating Insurer Capital Contributions
From Inception through December 31, 2012

		2012
State Farm General Insurance Company	$	254,658,275
Allstate Insurance Company		145,612,517
The Fire Insurance Exchange (Farmers)		143,280,000
United Services Automobile Association[1]		58,992,512
Safeco Insurance Company of America[3]		46,500,000
California State Automobile Association Inter-Insurance Bureau[2]		39,013,494
Nationwide Insurance Company[6]		20,772,000
California FAIR Plan Association		15,029,487
Interinsurance Exchange of the Automobile Club		14,443,651
CNA/Continental[4]		13,924,611
Prudential[4]		11,531,455
Liberty Mutual Fire Insurance Company[5]		6,699,434
Foremost Property and Casualty Insurance Company		4,614,304
Mercury Casualty Company		1,406,238
Armed Forces Insurance Exchange		783,685
GuideOne (formerly Preferred Risk)[4]		123,133
Homesite Insurance Company of California		-
Pacific National Insurance[4]		-
Encompass Insurance Company		-
Glen Falls Insurance Company[4]		-
Commerce West Insurance Company		-
Total	$	777,384,796

[1] Includes Garrison Insurance Company

[2] Includes ACA Insurance Company

[3] Joined CEA as of December 1, 2008

[4] Not currently writing residential property insurance in California

[5] Includes Golden Eagle Insurance Company

[6] Joined CEA as of November 2011

CALIFORNIA EARTHQUAKE AUTHORITY

Schedules of Participating Insurer Premiums Written
For the Years Ended December 31, 2012 and 2011

	2012	2011
State Farm General Insurance Company	$ 192,595,510	$ 219,132,203
Allstate Insurance Company	80,720,903	92,430,246
The Fire Insurance Exchange (Farmers)	69,554,447	75,330,427
United Services Automobile Association[1]	72,504,343	81,720,225
Safeco Insurance Company of America[3]	32,437,920	32,306,958
California State Automobile Association Inter-Insurance Bureau[2]	25,881,034	27,304,761
Nationwide Insurance Company[6]	14,116,866	1,370,877
California FAIR Plan Association	4,528,078	4,715,894
Interinsurance Exchange of the Automobile Club	37,067,111	39,961,992
CNA/Continental[4]	-	-
Prudential[4]	-	-
Liberty Mutual Fire Insurance Company[5]	14,954,323	15,098,844
Foremost Property and Casualty Insurance Company	2,919,379	2,520,191
Mercury Casualty Company	16,838,211	15,506,120
Armed Forces Insurance Exchange	616,769	731,553
GuideOne (formerly Preferred Risk)[4]	-	-
Homesite Insurance Company of California	689,237	521,465
Pacific National Insurance[4]	-	-
Encompass Insurance Company	3,773,243	4,153,175
Glen Falls Insurance Company[4]	-	-
Commerce West Insurance Company	37,963	26,022
Total	$ 569,235,337	$ 612,830,953

[1] Includes Garrison Insurance Company

[2] Includes ACA Insurance Company

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[6] Joined CEA as of November 2011

CALIFORNIA EARTHQUAKE AUTHORITY

Schedules of Participating Insurer Unearned Premiums
As of December 31, 2012 and 2011

	2012	2011
State Farm General Insurance Company	$ 97,223,283	$ 108,836,524
Allstate Insurance Company	41,031,050	46,584,860
The Fire Insurance Exchange (Farmers)	34,388,911	37,155,208
United Services Automobile Association[1]	36,606,687	40,815,491
Safeco Insurance Company of America[3]	19,772,570	19,650,543
California State Automobile Association Inter-Insurance Bureau[2]	13,169,677	13,955,939
Nationwide Insurance Company[6]	7,211,421	1,284,332
California FAIR Plan Association	2,343,457	2,416,204
Interinsurance Exchange of the Automobile Club	18,456,072	19,563,131
CNA/Continental[4]	-	-
Prudential[4]	-	-
Liberty Mutual Fire Insurance Company[5]	8,280,790	8,111,551
Foremost Property and Casualty Insurance Company	1,518,157	1,336,556
Mercury Casualty Company	8,213,956	7,581,421
Armed Forces Insurance Exchange	318,059	388,394
GuideOne (formerly Preferred Risk)[4]	-	-
Homesite Insurance Company of California	280,657	233,683
Pacific National Insurance[4]	-	-
Encompass Insurance Company	1,807,096	1,977,670
Glen Falls Insurance Company[4]	-	-
Commerce West Insurance Company	10,446	7,824
Total	$ 290,632,289	$ 309,899,331

[1] Includes Garrison Insurance Company

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[6] Joined CEA as of November 2011

CALIFORNIA EARTHQUAKE AUTHORITY

Schedules of Participating Insurer Commissions
For the Years Ended December 31, 2012 and 2011

	2012	2011
State Farm General Insurance Company	$ 20,417,401	$ 21,603,880
Allstate Insurance Company	8,632,610	9,252,759
The Fire Insurance Exchange (Farmers)	7,236,527	7,754,381
United Services Automobile Association[1]	7,670,867	8,088,164
Safeco Insurance Company of America[3]	3,233,553	3,205,629
California State Automobile Association Inter-Insurance Bureau[2]	2,667,744	2,616,554
Nationwide Insurance Company[6]	820,224	8,728
California FAIR Plan Association	460,341	465,038
Interinsurance Exchange of the Automobile Club	3,820,228	3,936,319
CNA/Continental[4]	-	-
Prudential[4]	-	-
Liberty Mutual Fire Insurance Company[5]	1,478,410	1,430,181
Foremost Property and Casualty Insurance Company	277,005	237,014
Mercury Casualty Company	1,621,286	1,482,192
Armed Forces Insurance Exchange	68,770	73,417
GuideOne (formerly Preferred Risk)[4]	-	-
Homesite Insurance Company of California	64,286	49,570
Pacific National Insurance[4]	-	-
Encompass Insurance Company	394,549	417,460
Glen Falls Insurance Company[4]	-	-
Commerce West Insurance Company	3,534	2,291
Total	$ 58,867,335	$ 60,623,577

[1] Includes Garrison Insurance Company

[2] Includes ACA Insurance Company

[3] Joined CEA as of December 1, 2008

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[5] Includes Golden Eagle Insurance Company

[6] Joined CEA as of November 2011

CALIFORNIA EARTHQUAKE AUTHORITY

Schedules of Participating Insurer Operating Costs
(Net of Deferred Acquisition Costs)
For the Years Ended December 31, 2012 and 2011

	2012	2011
State Farm General Insurance Company	$ 6,340,859	$ 7,407,774
Allstate Insurance Company	2,681,598	3,172,508
The Fire Insurance Exchange (Farmers)	2,244,026	2,658,559
United Services Automobile Association[1]	2,382,150	2,773,506
Safeco Insurance Company of America[3]	995,829	1,090,284
California State Automobile Association Inter-Insurance Bureau[2]	826,887	896,465
Nationwide Insurance Company[6]	232,631	2,434
California FAIR Plan Association	142,454	159,132
Interinsurance Exchange of the Automobile Club	1,184,947	1,351,818
CNA/Continental[4]	-	-
Prudential[4]	-	-
Liberty Mutual Fire Insurance Company[5]	459,112	487,858
Foremost Property and Casualty Insurance Company	81,802	80,862
Mercury Casualty Company	500,144	508,943
Armed Forces Insurance Exchange	21,434	25,117
GuideOne (formerly Preferred Risk)[4]	-	-
Homesite Insurance Company of California	20,382	17,595
Pacific National Insurance[4]	-	-
Encompass Insurance Company	122,590	142,963
Glen Falls Insurance Company[4]	-	-
Commerce West Insurance Company	1,121	788
Total	$ 18,237,966	$ 20,776,606

[1] Includes Garrison Insurance Company

[2] Includes ACA Insurance Company

[3] Joined CEA as of December 1, 2008

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[5] Includes Golden Eagle Insurance Company

[6] Joined CEA as of November 2011