Date of Notice: Friday, July 5, 2019

PUBLIC NOTICE

A PUBLIC MEETING OF THE GOVERNING BOARD OF THE CALIFORNIA EARTHQUAKE AUTHORITY

NOTICE IS HEREBY GIVEN that the Governing Board of the California Earthquake Authority ("CEA") will meet in Sacramento, California, and in a secondary location in Lakewood, California, that will be telephonically connected to the meeting location in Sacramento. Pursuant to California Insurance Code §10089.7, subdivision (j), the Bagley-Keene Open Meeting Act applies generally to meetings of the Board, and the meeting is open to the public—public participation, comments, and questions will be welcome for each agenda item. All items are appropriate for action if the Governing Board wishes to take action. Agenda items may be taken out of order.

LOCATIONS: California Earthquake Authority
Main Conference Room
801K Street, Suite 1000
Sacramento, California

Lakewood City Hall
Pan American Room
5050 Clark Avenue
Lakewood, CA 90712

DATE: Monday, July 15, 2019

TIME: 9:00 a.m.

This CEA Governing Board meeting will be broadcast <u>live</u> on the internet. Please wait until the official start time of the meeting before clicking on this icon:

Video (with audio)

If you are unable to view and hear the meeting, please call CEA directly at (916) 661-5001 for assistance.

AGENDA:

Preliminary Matters

1. Call to order and member roll call:

   Governor
   Treasurer
   Insurance Commissioner
   Speaker of the Assembly
   Chair of the Senate Rules Committee

   Establishment of a quorum

2. Chief Executive Officer Glenn Pomeroy, assisted by CEA staff, will update the Board regarding the July 4th magnitude 6.4 earthquake, and subsequent aftershocks, near Ridgecrest, California.

3. Mr. Pomeroy and General Counsel Tom Welsh will update the Governing Board on legislative activities of interest to the CEA in order to receive Governing Board directives, by way of Resolution, as to any formal positions the CEA should or may take on pending legislation.

4. Mr. Pomeroy will recommend adoption of a resolution authorizing a modification to the CEA Brace + Bolt program, to expand the eligibility requirements for this program while remaining within the original authorized budget as approved at the July 9, 2018 Governing Board meeting.

5. Public comment on matters that do not appear on this agenda and requests by the public that those matters be placed on a future agenda.

6. Adjournment.

For further information about this notice or its contents:

General Information:

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To view this notice on the CEA website or to learn more about CEA, please visit www.EarthquakeAuthority.com.

Persons with disabilities may request special accommodations at this or any future Governing Board meeting or may request the accommodation necessary to receive agendas or materials CEA prepares for its Board meetings. Please contact Colby Tunick by telephone, toll free, at (877) 797-4300 or by email at CEABoardLiaison@calquake.com. We would appreciate hearing from you at least five days before the meeting date to best allow us to meet your needs.

NOTE: If in the future you do not wish to receive public notices pertaining to CEA, please send your request by email to CEABoardLiaison@calquake.com.

Governing Board Memorandum

15 July 2019

Agenda Item 2:	Chief Executive Officer Glenn Pomeroy with update the Board on the July 4 & 5 Ridgecrest earthquakes.
Recommended Action:	No action required—information only

Chief Executive Officer Glenn Pomeroy will provide an update to the Board regarding the July 4th magnitude 6.4 and the July 5th magnitude 7.1 earthquakes, and subsequent aftershocks near Ridgecrest, California.

Governing Board Memorandum

July 15, 2019

Agenda Item 3:	Glenn Pomeroy (CEO) and Mr. Welsh (General Counsel) will provide a briefing on the legislation signed by the Governor on July 12, 2019, which creates the California Wildfire Fund and designates CEA as *Interim* Wildfire Fund Administrator, and on CEA's Implementation Plan for the Wildfire Fund
Recommended Action:	No Action Required – Information and Discussion

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Background

The California Constitution imposes strict liability on a utility company when the company's energy infrastructure causes a wildfire that damages private property. This liability is commonly referred to as "inverse condemnation." In brief, utility companies have the power under our State Constitution to condemn private property to establish access easements for purposes of installing energy infrastructure to distribute electricity to property owners; and the inverse of that condemnation authority is accepting liability when that infrastructure causes damage to private property.

Over the past several years, utility-caused wildfires (fueled or exacerbated by climate change) have caused tens of billions of dollars in damage to private property. As a result of its liability for wildfires during the 2017 and 2018 wildfire seasons, on January 29, 2019, PG&E (the State's largest investor-owned utility) and its parent company filed voluntary petitions under Chapter 11 of the U.S. Bankruptcy Code in the United States Bankruptcy Court for the Northern District of California. These bankruptcy petitions were filed to avail PG&E of the opportunity to restructure the massive liabilities it incurred by causing catastrophic wildfires during 2017 and 2018 wildfire seasons.

Even prior to the filing of PG&E's bankruptcy petition, the California Legislature was taking action to begin to address the serious and complex issues presented by utility-cause wildfires. In the 2018 session, the Legislature enacted and Governor Brown signed SB 901 (Dodd), which created the *California Commission on Catastrophic Wildfire Cost and Recovery*. During the latter part of 2018 and into 2019, the Commission conducted hearings and undertook research into these issues, and on June 18, 2019, issued its

Report to the Legislature making certain recommendations to assist the Legislature in remediating the challenges of utility-cause wildfires.

Immediately after PG&E's bankruptcy filing, newly-elected Governor Newsom appointed a "Strike Force" within the Governor's Office to develop actionable recommendations for the Legislature regarding steps the state should take to reduce the incidence and severity of wildfires caused by utility infrastructure, and to attempt to ameliorate the impact of those wildfires on the operations of the utilities and on utility ratepayers. On April12, 2019, the Governor's Strike Force issued its report entitled *Wildfires and Climate Change: California's Energy Future*. In the Governor's Strike Force Report, the administration identified several concepts for consideration by the Legislature, including the creation of a Wildfire Fund, similar in some respects to the California Earthquake Authority Fund, to provide utilities with a liquidity facility to loan money to fund inverse condemnation payments, and/or to act as an catastrophic insurance fund to address the utility companies' exposure to liability from wildfires.

These collective efforts by the Governor and the Legislature resulted in the enactment of a package of related bills during the 2019 session that passed through the Legislature prior to the Legislature's Summer Recess, all of which were signed into law by the Governor on this past Friday, July 12, 2019.

Summary of 2019 Wildfire Fund Legislation Related to CEA

The package of bills signed by the Governor on Friday include the following:

> **AB 1054 (Holden, Burke & Mayes)** –The most significant piece of legislation is AB 1054, which includes numerous provisions related to addressing wildfires caused by utility company infrastructure. The bill bolsters safety oversight and regulatory processes, initiates reforms to the process under which utilities may seek to recover wildfire related costs from utility ratepayers, and of most significance to CEA, establishes the California Wildfire Fund to provide a source of funds to allow for the payment of eligible claims arising from a covered wildfire.
>
> AB 1054 provides for the joint capitalization of the Wildfire Fund from a (1) utility ratepayers (in the form of a re-reauthorization and 15-year extension of an existing surcharge on ratepayers, which surcharge was initially authorized to facilitate the State's recovery from the energy crisis of the early 2000s), and (2) contributions from investor-owned utilities that desire to participate in and draw benefits from the Wildfire Fund. The bill establishes a metric for allocating the contributions among the three large utility companies in California – PG&E

(~64.2%), Southern California Edison (~31.4%) and San Diego Gas & Electric (~4.3%). The total initial capitalization from the utility companies, if they elect to participate in and be protected by the Wildfire Fund, is $7.5 billion, with annual additional contributions of $300 million (also allocated according the Wildfire Fund Allocation Metric).

In order to implement immediately the operation of the Wildfire Fund, AB 1054 provides for initial capitalization in the amount of $2 billion, in the form of a loan to the Wildfire Fund from the State's Surplus Money Investment Fund (SMIF). The short-term loan from SMIF is to be repaid when revenue bonds are issued in 2020 to securitize some portion of the ratepayer surcharges that are extended under the bill. Of significance to CEA is the expectation of the Governor's Office that the Wildfire Fund will be implemented and operationalized immediately so that it can receive the initial $2 billion in capitalization on or around July 26, 2019 – less than two weeks from today.

AB 111 & SB 111 (Committee on Budget) – Separate budget trailer bills – AB 111 and SB 111, which are identical – contain provisions related to the governance of the Wildfire Fund created under AB 1054. The budget trailer bills create the California Catastrophe Response Council ("Council") to oversee the Wildfire Fund, and to oversee any activity of CEA related to the administration of the Wildfire Fund. The Council has 9-members, consisting of (1) the Governor; (2) the Insurance Commissioner, (3) the Treasurer, (4) the Secretary of Natural Resources, (5&6) two members appointed by the Senate and the Assembly, and (7, 8 & 9) three members of the public appointed by the Governor.

The Council is vested with authority to administer, govern and direct the activities of the Wildfire Fund. However, until a majority of the Council is appointed, the powers and obligation of the Council are vested in the CEA Governing Board (Governor, Treasurer and Insurance Commissioner). These bills also authorize the Council to appoint an Administrator of the Wildfire Fund. Until the Administrator is appointed, the CEA is designated as the Interim Administrator of the Wildfire Fund. After appointment of the Administrator by the Council, CEA is authorized to contract with the Council or the Administrator to undertake some of all of the operational requirements of the Wildfire Fund, such as accounting, banking, investment management, governance liaison service, and other general administrative services required to operate the Wildfire Fund.

These bills expressly provide for CEA to undertake to ensure, among other things, that the Wildfire Fund is established and remains entirely segregated from the

CEA Fund, and the administrative expenses of the Wildfire Fund are borne solely by the Wildfire Fund, and the expenses of the CEA Fund are, in turn, borne solely by the CEA Fund.

As a practical matter, these provisions require that the CEA undertake the immediate responsibility to implement and operationalize the Wildfire Fund. In the short term, this requires the establishment of an administrative infrastructure to ensure that the Wildfire Fund can receive its initial capitalization loan from the SMIF within the next two weeks.

Status of CEA Activities Related to the Wildfire Fund

Even before the Governor signed these bills into law, CEA staff had undertaken the development of the features of an Implementation Plan for the operationalization of the Wildfire Fund. These activities fall into two primary categories: (1) tasks related to the activation and capitalization of the Wildfire Fund; and (2) tasks related to the administration and governance of the Wildfire Fund.

1. Activation & Capitalization of Wildfire Fund: The steps necessary to implement the Wildfire Fund's ability to receive capitalization deposits require the following key administrative steps, all of which are currently being undertaken or initiated by CEA staff:

    a. Obtaining State and Federal Tax ID numbers

    b. Establishing Agreements for Custodial Trust Accounts at National Bank (as required by AB 1054)

    c. Negotiating Loan Agreement between the Wildfire Fund and the SMIF related to the initial $2 billion loan to the Wildfire Fund

    d. Establishing Operating Bank Accounts (i.e., Demand Deposit Account to facilitate receipts to and payments by the Wildfire Fund)

    e. Contracting with Asset Managers to invest the initial $2 billion in capitalization immediately upon receipt by the Wildfire Fund

    f. Establishment of Investment Guidelines for the Wildfire Fund

    g. Engagement of an Investment Consultant and Independent Financial Consultant to the Wildfire Fund

2. General Administration Requirements: In addition to the banking and financial activities described above, the Wildfire Fund also requires implementation of a number of basic operational functions, which CEA staff is beginning to address, including:

    a. Accounting Functions: General Ledger, Chart of Accounts and Reports

    b. Independent Auditor: Retention of Independent Financial Auditor

    c. Back-Office Staffing: Retention of temporary employees pending the appointment of the Administrator of the Wildfire Fund, and/or assign duties to existing CEA staff

    d. Cost Allocation Agreement – Develop an agreement and allocation methodology to spread administrative costs appropriately between the Wildfire Fund and CEA Fund

    e. Information Technology support

    f. Office space and other FF&E needs

    g. Development of Risk Transfer Guidelines

    h. Tax compliance matters

3. Governance Requirements: Finally, the Wildfire Fund will need to establish a governance infrastructure similar to what exist for CEA's Governing Board, to ensure that the business of the Wildfire Fund is conducted with proper approval by and oversight of the Council (and prior to the Council's activation, by the CEA Governing Board, in its capacity as the Interim Council). These requirements include, among other things:

    a. Organizational Board Meeting – An initial Organizational Board meeting of the CEA Governing Board, in its capacity as the interim Council will be Noticed and conducted pursuant to the Bagley-Keene Act, to seek approval or ratification of, among other things:

        i. Bank Account Agreement (Trust and DDA)

        ii. Asset Manager Agreements

        iii. Investment Guidelines

iv. Cost Allocation Agreement

v. Investment Consultant Agreement

b. Council/Board Liaison Functions – The Wildfire Fund, in order to operate under the mandatory oversight of the Council, and in a manner consistent with the Bagley-Keene Act, with require staff to facilitate meetings as necessary to conduct the affairs of the Wildfire Fund. These functions are similar to the long-standing support that CEA staff has provided to the CEA Governing Board to allow it to meet its obligations under the CEA statute.

Recommendation:

This is a non-action item, for reporting and discussion purposes.

Governing Board Memorandum

July 15, 2019

Agenda Item 4:	Mr. Pomeroy will recommend adoption of a resolution authorizing a modification to the CEA Brace + Bolt (CEA BB) program, to expand the eligibility requirements for this program while remaining within the original authorized budget as approved at the July 9, 2018 Governing Board meeting.
Recommended Action:	Approve adjusting the CEA BB program parameters

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Background

At the July 19, 2018, Governing Board meeting, the Board approved the CEA BB program aimed at incentivizing certain CEA policyholders to reduce their earthquake risk by accepting our offer of a Brace + Bolt grant to seismically retrofit their vulnerable older home. As explained in last year's Board memo (7/19/18 memo attached) the plan was to reach targeted policyholders who met the following criteria:

- CEA policyholder for three or more consecutive years,
- Own a pre-1940 wood-frame construction home and otherwise eligible for our retrofit program (raised foundation, etc.), and
- Home located in a ZIP Code where policyholders will have a 15% or greater increase in premium (as a result of CEA's recent rate filing, effective July 1, 2019).

At that meeting the Board approved this new CEA BB program, which replaced a 2016 pilot program and reallocated the remaining pilot project budget to the new CEA BB program. The total approved budget is $11.5 million.

Based the program eligibility criteria above, CEA staff estimated that grants could be made available to approximately 12,000 CEA policyholders, with that number growing over time as more policyholders satisfied the 3 year persistency requirement. From that population of 12,000 policyholders, CEA initially reached out to 4,000 policyholders to offer CEA BB grants. That outreach produced very disappointing results. To date, only 76 policyholders (out of the 4,000 contacted) have expressed interest in the grant. Fourteen of the 76 retrofits have been completed, with 62 in progress.

<u>Expanding CEA BB program parameters</u>

Given the disappointing results of the first outreach, CEA is recommending a change to the CEA BB eligibility criteria to expand the pool of policyholders eligible for a mitigation grant. Expanding eligibility for a grant is particularly important at this time given the rollout of CEA's new insurance rates which went into effect on July 1, 2019.

The new rating plan approved by the Governing Board and CDI makes significant changes to CEA's rates based on new earthquake science and other underwriting factors. Overall, about 75% of CEA policyholders will see a premium *reduction*. However, the remaining 25% will see a rate increase, with some increases being modest (10% increase or less); others will experience a significant increase as a result of the application of best available science and the statutory mandate that CEA's rates be actuarially sound. Notably, approximately 44,000 CEA policyholders will receive a very significant premium increase of more than 50%.

Most of the policyholders hardest hit by these premium increases are not currently eligible for the CEA BB program according to our current program parameters, as their insured home was built after 1940. Given the low take-up from the 4,000 policyholders offered a grant under the current program, and the certainty that we will fall far short of our goal to retrofit 4,000 CEA policyholders under the current program, we propose expanding the eligibility criteria in order to capture a larger population of the CEA policyholders who can benefit the most from undertaking a retrofit.

Effective July 1, 2019, a policyholder who has completed a code-compliant retrofit qualifies for a Hazard Reduction Discount of up to 25% off their CEA earthquake insurance premium. This new, more generous Hazard Reduction Discount replaces CEA's previous rating plan that offered lower verified discounts and also allowed homeowners to receive a 5% discount for "self-verifying" that their home has undergone a retrofit.

The recommendation of CEA staff is to expand the criteria for qualifying for a retrofit grant, but without seeking to augment the previously approved budget for this risk reduction program. These changes will make the grant program available to more CEA policyholders who will be facing a significant rate increase this year. Provided the policyholder's home was constructed prior to 1980, and would otherwise be eligible for an EBB-type retrofit grant (raised foundation, etc.), staff recommends expanding the pool of eligible policyholders to include the following:

- All CEA policyholders who will receive a premium increase in excess of 50% (this would sweep in approximately 17,000 of the 44,000 CEA policyholders receiving a greater than 50% rate increase), and
- All CEA policyholders who will receive a premium increase of between 20% and 50%, provided they have been a CEA policyholder for two years or more—including those who are currently in their second year of persistency (approximately 13,000 additional eligible policyholders).

This would increase the total number of policyholders eligible for this CEA BB grant program from 12,000 to approximately 40,000.

The board has already approved sufficient funds to provide approximately 4,000 grants, or about 10% of the eligible pool of CEA policyholders. The grants would be made available on a first come, first-served basis. Based on our previous experience, staff believes it is highly unlikely that demand will outstrip authorized funds. In the unlikely, but welcome, event that the allocated funds are insufficient, the Board could consider approving additional funds for the program at a subsequent Board meeting.

Recommendation:

Staff recommends adjusting the CEA BB program parameters as outlined above to allow those policyholders most impacted by implementation of CEA's current rating program.

Governing Board Memorandum

July 19, 2018

Agenda Item 14:	Changes to pilot risk-reduction program and proposed [new] program to provide retrofit incentives to selected CEA policyholders
Recommended Action:	Approve phase-out of pilot risk-reduction program and approve budget allocation of $11.5 for new CEA risk-reduction program

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Background:

On January 1, 2016, the CEA began offering a 20% hazard-reduction premium discount to qualifying policyholders who live in pre-1940 wood-frame houses built on raised foundations (called in this memo, "target houses").

The 20% discount—four times larger than the minimum statutory retrofit discount of 5% the CEA had offered for many years—recognized that (1) retrofitting older houses according to the *California Existing Building Code* significantly reduces expected losses, and (2) policyholders who have retrofitted their houses should benefit from the reduced risk exposure.

On March 16, 2016, the Board approved the pilot-risk reduction program allocating $12 million to support mitigation within its policyholder base by providing a cash incentive to seismically retrofit from the CEA, paid to tenured policyholders in 10 ZIP codes in higher-risk areas who live in target houses. The program provides up to $3,000 for each verified seismic retrofit and was initially available to 3,200 CEA policyholders. Upon completion of a retrofit and submission of the Discount Verification Form to their participating insurer, an eligible policyholder would receive a 20% hazard-reduction premium discount.

In February 2018, CEA submitted a Rate and Form Filing (RFF) to the California Department of Insurance (CDI), regarding which CEA anticipates a response sometime later this year. The filing proposes to increase statewide average rates by 0.04%; provide an enhanced hazard-reduction discount to qualified CEA homeowners policies with a verified seismic retrofit; establish additional rating factors and additional rating territories; and publish new forms and other refinements to coverages, definitions, and policy language.

If the RFF is approved as submitted, about 20 percent of CEA's policyholders would see a rate increase of more than 10 percent. But many of those CEA policyholders with an increase of more than 10 percent also would be eligible for the enhanced hazard-reduction discount if their houses had a verified seismic retrofit.

Analysis:

CEA staff believes that policyholders receiving a 15% or greater premium increase, who reside in a CEA-insured house with defined characteristics, should be eligible to a new CEA brace and bolt (CEA BB) program. Completing a CEA BB retrofit would afford those policyholders a significant Hazard Reduction Discount on their CEA earthquake insurance premiums.

CEA's pilot-risk reduction program now operates in 10 ZIP Codes—five in Northern California and five in Southern California. At the time of implementation there were approximately 3,200 target houses in those ZIP Codes, for which 89 verified seismic retrofits are complete; those policyholders have a CEA-policy retention rate of 92.1%, which is higher than CEA's overall book-of-business retention rate. An additional 14 policyholders have retrofits in process. While CEA staff expected more policyholders to participate in the pilot risk-reduction program, it has learned valuable lessons on engaging potential future participants, including additional outreach and individualized help through the process.

Analysis of CEA's book of business reveals that more than 10,000 policyholders would be eligible to participate in a new CEA BB program that is based on the following criteria:

- Three or more years tenure with the CEA;
- Pre-1940 wood-frame construction on a raised foundation, lacking adequate bolting or bracing (or lacking both); and
- Located in ZIP Codes where policyholders will have a 15% or greater increase in premium if the recent CEA RFF filing is approved.

Staff's initial analysis, from the August 26, 2015, Board meeting, shows that when policyholder retrofits improve the CEA's risk profile, then CEA risk-transfer capacity can be reduced. Based on the above-described experience, CEA staff now recommends that the current pilot-risk reduction program be phased-out—allowing the 14 policyholders in process to complete their retrofits—and that implementation of a new CEA BB program commence.

1. Close-out of Pilot-Risk Reduction Program

    - 89 seismic retrofits have been completed at a total cost of $426,000. Should the 14 retrofits currently in-process be completed, CEA would incur an additional estimated $42,000 in retrofit costs. Of the $12 million originally allocated for this program, approximately $11,500,000 would be available for reallocation.
    - The average total cost for the completed retrofits is $9,624, with a low of $2,999.96 (a bolt-only retrofit) and a high of $61,411(a fully engineered brace-and-bolt retrofit). Regardless of the costs incurred by the policyholder, CEA provides a grant of up to $3,000 to reimburse eligible seismic-retrofit costs.
    - The CRMP's other program, *Earthquake Brace + Bolt* (EBB), is available to the public, without regard to CEA-policyholder status. Only 40% of homeowners accepted for the program follow through to a completed retrofit.

It was reasonable, then, that fewer than 100% of the selected CEA policyholders would participate in the pilot risk-reduction program.

- Funding for a new CEA BB program would come from a reallocation of funds already approved and allocated to the original lpilot-risk reduction program.

2. CEA Brace & Bolt (CEA BB) Program

The new CEA BB program would leverage successful CRMP EBB techniques and use a similar approach, including a gradual roll-out of the program. Appropriate communication to potentially eligible CEA policyholders and dedicated staff to guide participants through the retrofit process are key. In addition, CEA will work closely with participating insurers and their agents to engage with eligible CEA policyholders and encourage their participation.

Staff recommends providing the same incentive as the pilot-risk reduction and Earthquake Brace + Bolt programs: a $3,000 incentive, paid upon completion of a qualifying retrofit.

The potential success of the CEA risk-reduction program must be a measured success, using program-success metrics, including:

- The number of policyholders who register for the program after receiving notice that they own a CEA-insured target house.
- The number of policyholders who secure a building permit for the retrofit work.
- Program participants' respective tenure as a CEA policyholder (this would include whether (and on what terms) the policyholder remains a CEA policyholder, post-retrofit).
- Cost per retrofit.

Recommendation:

1. Approve phase-out of the current CEA pilot-risk reduction program, in the manner described.

2. Approve, and authorize CEA staff to develop and implement, a new CEA BB program, with a goal of commencing implementation by third quarter 2018:
   - Phase-out pilot-risk reduction and re-allocate remaining funds to the new CEA BB program.
   - Support the following eligibility parameters for policyholders participating in the new CEA BB program:
     - three or more years tenure with the CEA;
     - pre-1940 wood-frame construction on a raised foundation, lacking adequate bolting or bracing (or lacking both); and

        - located in ZIP Codes where policyholders will have a 15% or greater increase in premium, based on the pending CEA RFF filing.
    - Direct staff to develop an implementation plan, to be reported to the Board, and program rules.