

**CALIFORNIA EARTHQUAKE AUTHORITY
GOVERNING BOARD MEETING
MINUTES**

**Thursday, October 25, 2012
1:00 p.m.**

Location: CalSTRS Headquarters Building
Board Room – Lobby, E-124
100 Waterfront Place
West Sacramento, California

Members of the CEA Governing Board in attendance:

Pedro Reyes, designee of Governor Jerry Brown
Grant Boyken, designee of State Treasurer Bill Lockyer
Chris Shultz, designee of Insurance Commissioner Dave Jones
Dietrich Stroeh, designee of Chair of the Senate Rules Committee Darrell Steinberg

Members of the CEA staff in attendance:

Glenn Pomeroy, Chief Executive Officer
Tim Richison, Chief Financial Officer
Bob Stewart, Chief Operations Officer
Chris Nance, Chief Communications Officer
Janiele Maffei, Chief Mitigation Officer
Shawna Ackerman, Chief Actuary
Susan Pitton, Governing Board and Advisory Panel Liaison
Marc Keller, Legal Office Assistant
Danny Marshall, General Counsel

Also present:

Dr. Lucile M. Jones, United States Geological Survey
Kapil Bhatia, Raymond James & Associates, Inc.
Rick Patterson, Raymond James & Associates, Inc.

- 1. The meeting was called to order at 1:04 p.m. A quorum was established.**
- 2. Consideration and approval of the minutes of the August 23, 2012 Governing Board meeting.**

MOTION: Mr. Boyken moved approval of the August 23, 2012, Governing Board meeting minutes; seconded by Mr. Shultz. Motion passed unanimously.

3. Executive Report by Chief Executive Officer Glenn Pomeroy, assisted by CEA executive staff. Mr. Pomeroy's report will include an update for the Board on federal and state legislative activities of interest to the CEA. Mr. Pomeroy will introduce Dr. Lucile Jones, Science Advisor for Risk Reduction, United States Geological Survey (USGS).

- A devastating and fatal earthquake in Italy a few years ago has resulted in some recent criminal convictions: Six scientists and a public official were claimed to have failed to communicate properly the risk of impending earthquake to residents of the earthquake-affected region. An Italian court this week handed down sentences: the scientists and government official were each sentenced to six years in prison. The allegations and sentences sparked uproar within scientific and disaster-preparedness communities throughout the world.
- The case has underscored what the CEA is well aware of: This is a serious business. The State of California has benefited from relatively low seismic activity for about a decade and a half. But we know that is not always going to be the case. That is why everything the CEA does is designed to help more Californians better prepare to survive and recover from the next damaging earthquake.
- CEA efforts to make earthquake insurance more affordable continue in Washington, D.C. Support within Congress has grown since the August 2012 Board meeting. Additional cities, counties, and chambers of commerce have endorsed the Earthquake Insurance Affordability Act, and the CEA is very grateful for this support.
- The CEA has added about 60,000 policyholders in the last four years. There are a number of reasons for this growth, such as the occurrence of major earthquakes around the world, and the addition of a new Participating Insurer, Nationwide. Furthermore, a significant portion of this growth is due to new and creative CEA marketing initiatives.
- One example of this innovative outreach: During the San Francisco Giants' playoff run, a CEA radio announcement was played between innings, and during the post-game analysis show, the radio broadcasters continued to publicize the CEA by designating a "CEA Ground Shaking Play of the Day"[A recording of the material was played in the meeting room.]
- The CEA received a letter from Harold Brooks, CEO of the San Francisco Chapter of the American Red Cross, expressing the Red Cross's appreciation for the CEA's collaborative work with them.

Mr. Pomeroy then introduced Dr. Lucile M. Jones of the USGS. Dr. Jones is a co-founder of the "Great ShakeOut" drills.

- Dr. Jones thanked the CEA for its support of the ShakeOut, and noted that the ShakeOut drill had grown markedly since its inception five years ago. Participation in 2012 exceeded 19 million people in California, Washington D.C., Japan, Chile, Turkey, and New Zealand.

- This year all of the media participation was been arranged by the CEA, while the USGS worked on the science and the American Red Cross worked on disaster response. With the formation of the Earthquake Country Alliance, all of the organizations made the commitment to speak with one voice, giving a coherent message.
 - Mr. Stroeh commented that his firm participated in the ShakeOut drill.
 - Mr. Reyes noted that he would like to see Mexico and Italy added to the list of participants, as those countries are clearly impacted by earthquakes.

4. Chief Communications Officer Chris Nance will provide the Board with an update on the CEA’s Marketing Value Program (MVP) and the fifth annual ShakeOut drill.

- Mr. Nance reported that the CEA communications team worked under budget and offered these accomplishments:
 - Doubled television network participation, adding ABC and NBC to CBS and Fox.
 - Added two additional designated market areas—Monterey and Santa Barbara—to Sacramento, San Francisco, Los Angeles, and San Diego.
 - The insurance agent base was just under the goal of 5,000 agents, with approximately 4,200 registrations in the direct-mail program. Efforts were focused on non-CEA-policyholders.
- Combining forces with the American Red Cross (“ARC”) was a “great match” of expertise and resources. Two programs were executed through what CEA and ARC call their “joined-forces programming”:
 - The auction in spring 2012, which achieved great success.
 - The Traveling Red Table™, a symbol of what people get under when the ground shakes. It traveled statewide, engaging interest from many celebrities, many of whom have signed the table, as have public officials. An interesting celebrity who participated with the Table in a “drop, cover, and hold on” moment was the orca Shamu from Sea World in San Diego.
- Mr. Nance introduced Michael Preacher, representing Clear Channel Media and Entertainment, which assisted the CEA with developing a Web site through which the spring 2012 auction was implemented.
- The CEA team had worked with direct mail on brochures for homeowners, renters, and condo owners. They co-branded direct mail pieces with the ARC to CEA policyholders. In addition to English-language pieces, direct-mail pieces were also made available in Chinese and Spanish.
- The team’s strategy for using the online space involves two types of implementation: general preparedness and earthquake-insurance-specific programming. For the latter,

there are four online campaigns, entitled by CEA “Blueprint,” “Lifeline,” “What Moves You,” and “House of Cards.” For example, pop-up ads on Web sites allow users to select a house and then watch it shake at various levels of earthquake intensity, view the damage, “rebuild” the house, read factoids, and finally click through to a “landing page” to read about earthquake insurance.

- The two landing pages are the interim steps that people who see the ads take before they land on the CEA premium calculator. So far, through the online marketing strategy alone, consumers have spent 500,000 minutes considering earthquake insurance.
- For the first time, more consumers are visiting the CEA web site than insurance agents.

5. Chief Financial Officer Tim Richison will present the periodic CEA financial report.

- At the end of August 2012, the available capital to pay claims was a little over \$4.1 billion. The CEA’s capital, risk-transfer, revenue bond proceeds, and available participating-insurer assessment capability amount together to more than \$10 billion.
- Mr. Richison reviewed the status and characteristics of the CEA’s risk-transfer programs.
- Through the end of August 2012, CEA policy writings have increased almost 1.4%. The increase in renters policy count, almost 4%, surpasses any other year.
- With the increase in policies, the CEA must have sufficient risk-transfer in place to maintain the proper capacity and financial security.
- Mr. Richison presented a graph showing the average insured value of all of the coverages on a CEA policy and the average premium—the lines have converged, in large part due to CEA rate decreases taking effect this year and even though the insured value of all coverages on a CEA policy is increasing.

6. Mr. Richison will present for Board approval the CEA’s 2013 risk-transfer program, effective January 1, 2013.

Mr. Richison had reported at the August 2012 Board meeting that the CEA had split its risk-transfer program into different pieces. At virtually every Board meeting, it seems, a portion of CEA’s overall risk-transfer program is presented to the Board for its consideration.

The January 2012 risk-transfer program is scheduled to expire on December 31, 2012, and must be replaced. Mr. Richison described the new program plan.

- The CEA will need risk-transfer of just over \$3.5 billion on January 1, 2013, to maintain the level of security that the Governing Board and staff have tried to maintain for policyholders.
- CEA’s risk-transfer has been split into many different contracts that start at different times during the year, with terms for contracts being one or three years.

- Mr. Richison said he will report to the Board in upcoming months how the CEA is in a “survivability mode.” That is, by implementing the risk-transfer program as suggested, the CEA can survive not only one major earthquake but another one on the very next day.
- For the reinsurance program to take effect on January 1, 2013, staff contacted 169 reinsurers in 25 countries, making the effort a global placement. CEA plans to have 39 reinsurers on the January 2013 and August 2013 programs. The January 2013 program has a 12-month maturity date, while the August 2013 program is a 7-month program.

There are three different contracts for the August 2013 program and one contract for the January 2013 program. The total amount of reinsurance limit being purchased is \$1.6 billion.

- Mr. Richison displayed a list of program reinsurers. Some have been on the CEA program for quite some time, while some are new. They are some of the biggest reinsurers in the world for catastrophe reinsurance, as well as Lloyd’s syndicates.
- Each of the four contracts (January 2013 and August 2013 programs) will become effective on January 1, 2013. At the February 2013 Board meeting, staff will recommend to the Board an additional 2013 risk-transfer program, because the April 2013 program expires March 31, 2013.
- Mr. Richison requested Board authorization to seek reinsurance commitments from the reinsurers listed in the relevant attachment in Board materials, on the terms and conditions described above and elaborated on in the written resolution.
- General Counsel Danny Marshall reviewed the resolution for the Board.

Mr. Reyes commented that much of this risk-transfer activity is driven by the number of policies the CEA acquires. He suggested that the CEA set up a policy to allow Mr. Richison to go and get reinsurance at a level needed for the 1-in-500-year event, so that he has some authority to take care of the risk-transfer requirements as the needs arise, rather than waiting until the Board meets.

Mr. Marshall responded that the topic has come up before; staff wants to make sure that to support this sort of initiative, there is a substantial compliance framework first in place. That framework will assure that if there is an overarching type of authorization provided by the Board, there is a comfort level that all will be accomplished within Board authorization and according to Board expectations.

Mr. Richison stated that he, Mr. Marshall, and their staffs have been working together to put a framework in place that would address these situations, to recommend a compliance perspective for the framework in place that meets appropriate conditions, going forward.

Mr. Reyes stated that the Board would like to make sure that staff has the latitude to conduct business, since the CEA’s needs are driven by its [increasing] exposure. When and if

exposure goes up, CEA should not have to wait for the next Board meeting to request approval and risk being out of compliance with the goal of a 1-in-500-year financial structure.

Mr. Marshall replied that he thought they could fold in the concept of a “blanket authorization” by the Board, as well. As the exposure growth dictates more risk-transfer or more financing capability in general, staff definitely wants to provide a compliant method to allow those Board authorizations to be given in a more general way.

MOTION: Mr. Shultz moved approval of the resolution as corrected; seconded by Mr. Boyken. Motion passed unanimously.

7. Kapil Bhatia, Director of Public Finance, and Rick Patterson, Managing Director of Public Finance, Raymond James & Associates, Inc., the CEA’s independent financial advisor, will present to the Board the annual report on the state of the economy.

Mr. Patterson stated that the CEA is widely considered to be “*the gold standard*” among state-supported, state-sponsored catastrophe insurers.

It has a debt-service coverage of over 12.5 times, as well as solid “A” ratings from multiple credit-rating agencies.

The financial market affects the CEA in a number of ways and was elaborated on in the presentation.

Mr. Bhatia and Mr. Patterson described the challenging times in the market and addressed issues such as:

- the Federal Reserve’s strategy,
- the United States deficit and budget issues,
- U.S. unemployment,
- the upcoming “fiscal cliff,”
- the European debt crisis, and
- the equities market.

Mr. Bhatia spoke about the insurance market.

- There is a significant amount of reinsurance capital in the marketplace. Currently, there is approximately \$480 billion of reinsurance capital available, almost 20% more than was available last year. And the reinsurance markets are stable.

The result is that CEA should be able to obtain better pricing and better capacity.

- The non-traditional risk-transfer capacity has significantly increased globally. In each year since 2003, the non-traditional portion of the reinsurance market has expanded.

That portion includes everything from insurance-linked securities to capital markets, risk-transfer, and catastrophe bonds, as well as collateralized reinsurance – everything but traditional reinsurance.

- Increased capital has also resulted in additional capital-market risk-transfer capacity. And because of increased issuance, there is a high investor demand for the resulting products. Almost \$3.6 billion of new catastrophe bonds were issued in the first six months of 2012.
- For reinsurance and the P&C insurance industry outlook, everything is stable. The only challenge industry-wide is low investment yield.
- The reinsurance industry's trading value compared to equity price, and companies' book value, is improving to around 88%, on average. That improvement has led to higher stock prices for both reinsurance and primary-insurance sectors.

What does all this mean to the CEA?

- With interest rates low, the CEA may modify its investment policy to maximize yield.
- With risk-transfer mechanisms effectively diversified, there is more capacity available and more sustainability achieved.
- CEA should continue to look for alternative capital resources. And CEA should continue trying at the federal level to secure guarantees for post-event bonding, which can help to maximize capital resources.
- CEA could also employ selective use of revenue bonds, which can help achieve sustainability and survivability, too.

8. Chief Mitigation Officer Janiele Maffei will update the Board on the CEA's mitigation programming, including its participation in the California Residential Mitigation Program.

The CEA and the California Emergency Management Agency have joined forces in a joint powers authority, which manages the California Residential Mitigation Program. In all of the mitigation programs managed by the CEA, the goal is to reduce earthquake damage to single-family dwellings.

The problem they are working on is the structural vulnerability (e.g., soft or weak first stories) common in older houses. The rather simple fix is to install anchorage between the sill plate and the concrete, and install plywood on cripple walls.

To assure compliant implementation of an incentive program for that kind of retrofit, the CRMP has just issued RFQ for an independent financial auditor. CRMP anticipates posting an additional five RFQs in November 2012.

9. Ms. Maffei will present to the Board a summary of the building code-related Guidelines Development Workshop, which the CEA co-hosted with the Federal Emergency Management Agency (FEMA), on September 17, 2012 in Millbrae, California.

A key objective of the CEA's Mitigation Program is to develop comprehensive guidelines for the evaluation and retrofit of single-family dwellings. Those guidelines would cover buildings that cannot be retrofitted in existing programs, because they are unusual and there is no corresponding building-code provision.

The strategy was to develop guidelines with FEMA as the primary partner. The first step was a workshop in September 2012 that brought stakeholders together. The workshop was a success, with more than 70 attending, including engineers, building officials, contractors, residential building inspectors, researchers, and attorneys, as well as CEA Board designee Dietrich Stroeh. There were four presentations, with two breakout sessions to discuss and identify what should be in the guidelines.

The next day, staff met with the moderators to discuss next steps, recognizing that homeowners make retrofit decisions based on cost. For that reason, the new guidelines should expand current retrofit provisions so they can be used by contractors, without engineers involved – i.e., pre-engineered solutions where possible. And the guidelines should include cost-benefit information.

Staff will be moving into guideline development and coming back to the Board with a program process.

10. Staff will present for Board consideration and approval a proposed 2013 Governing Board meeting calendar.

Mr. Reyes asked the Board to consider meeting quarterly instead of every other month.

Mr. Boyken stated that he would feel most comfortable keeping all of the dates on the calendar while the Board discusses meeting quarterly—he said he wanted to ensure that CEA staff has the flexibility to accomplish what it needs to do.

Mr. Shultz agreed: Meeting quarterly makes sense, as long as the CEA risk-transfer program does not require action between the newly scheduled quarterly meetings. He agreed that the Board should keep the existing schedule while staff works to come up with a quarterly meeting process that also accomplishes the CEA's risk-transfer objectives.

Mr. Stroeh commented that the CEA staff has now stabilized the CEA to a point that the organization is moving well in the proper direction. He agreed with the idea of fewer meetings but keeping the calendar the way it is pending a new schedule.

Mr. Pomeroy stated that staff would work on the idea between now and December.

MOTION: Mr. Boyken moved approval of the calendar as proposed, with the recognition that it may be altered later; seconded by Mr. Shultz. Motion passed unanimously.

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

There was no closed session.

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

There was no public comment.

- 13. Adjournment.**

The meeting was adjourned at 2:32 p.m.