

**Assembly Joint Resolution**

**No. 6**

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**Introduced by Assembly Member Cooley**

February 24, 2015

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Assembly Joint Resolution No. 6—Relative to earthquake insurance.

LEGISLATIVE COUNSEL'S DIGEST

AJR 6, as introduced, Cooley. California Earthquake Authority: postearthquake financing.

This measure would recognize a need for federal legislation that would establish guarantees of postearthquake financing for prequalified, actuarially sound state earthquake insurance programs, including the California Earthquake Authority, and would urge the President and Congress of the United States to enact that legislation.

Fiscal committee: no.

1 WHEREAS, Over the last 30 years, California has experienced  
2 1,451 earthquakes of magnitude 4.0 or greater, ranging from 16  
3 to 168 per year; and  
4 WHEREAS, Most Californians live within 20 miles of a major  
5 earthquake fault capable of producing damaging earthquakes; and  
6 WHEREAS, On the morning of August 24, 2014, many residents  
7 of Napa discovered they lived closer to such a fault than they  
8 believed. A magnitude 6.0 earthquake struck American Canyon,  
9 south of Napa, at 3:20 a.m., leading to one death and many injuries.  
10 The earthquake seriously damaged nearly 100 homes, as well as  
11 many historic downtown buildings. It cost local wineries millions  
12 of dollars in spilled wine and damaged equipment, and numerous  
13 people were injured. The overall damage and effects of the

1 earthquake demonstrated how even a moderate-sized earthquake  
2 can have a large impact on a community; and

3 WHEREAS, In June 2014, the Los Angeles Times reported that  
4 the first five months of the year were marked by five earthquakes  
5 larger than magnitude 4.0, after what had been a relatively quiet  
6 period of seismic activity for the Los Angeles area. That number  
7 of earthquakes at that magnitude had not occurred in a year since  
8 1994, the year of the Northridge earthquake; and

9 WHEREAS, Faced with the certainty of its peril from  
10 earthquakes, over the last three decades California has repeatedly  
11 shown that smart public policy choices can help Californians  
12 prepare for a catastrophic earthquake. Milestone innovations across  
13 this era include the following:

14 (a) In the year following the 1983 Coalinga earthquake,  
15 California passed the Earthquake Insurance Act, requiring  
16 residential property insurers to offer homeowners earthquake  
17 coverage, to ensure homeowners considered the possibility of  
18 protecting their home from earthquake damage.

19 (b) In the year after the 1989 Loma Prieta earthquake, California  
20 began examining how a state-based financial pool might be  
21 constructed to improve protection for homeowners. This effort,  
22 the California Residential Earthquake Recovery Fund (CRERF),  
23 was intended to cover the cost of earthquake insurance deductibles.  
24 While this plan was repealed in 1992 as potentially actuarially  
25 unsound, it pointed the way to further innovations.

26 (c) Since 1996, the multipart funding mechanism of the  
27 California Earthquake Authority (CEA), a public instrumentality  
28 of the State of California, has succeeded as the primary source of  
29 earthquake insurance for California homeowners seeking to protect  
30 their homes from earthquakes; and

31 WHEREAS, Despite the growing successes of the CEA since  
32 its 1996 formation, how it can be improved has become clear.  
33 Almost every news story about California earthquake insurance  
34 and the CEA notes that residential earthquake insurance is costly  
35 for homeowners and the deductibles are high. The high cost and  
36 high deductibles are seen as a key factor behind why only 12  
37 percent of Californians who buy homeowners' insurance also buy  
38 earthquake insurance; and

39 WHEREAS, There is no better way to prepare California for  
40 the inevitability of disastrous earthquakes than to make earthquake

1 insurance work better for its residents. The limitations of the  
2 existing system are well-known. Now is the time for the next key  
3 step in policy innovation to make the state’s earthquake insurance  
4 system work better for renters and homeowners; and

5 WHEREAS, As the CEA approaches two decades of operation,  
6 it has become clear that the CEA has pushed the envelope on how  
7 a single state-based pool can materially assist in catastrophe  
8 readiness. But by law, the CEA’s rates must be actuarially sound  
9 and based on the best available scientific information for assessing  
10 earthquake frequency, severity, and loss; these sensible conditions  
11 also temper the CEA’s ability to cut the cost of earthquake  
12 insurance; and

13 WHEREAS, As a public instrumentality of the state, the CEA  
14 must cover all its risks, including the possibility that at any time,  
15 a truly catastrophic earthquake might hit the state; and

16 WHEREAS, The CEA’s need, as a stand-alone, risk-bearing  
17 public instrumentality of the state, to always have a plan to cover  
18 the chance of a catastrophic earthquake is what, under the current  
19 system, keeps the price of earthquake insurance high. For the level  
20 of total exposure the policies represent, the rates yield sufficient  
21 premiums to pay for a backstop of reinsurance sufficient to offset  
22 expected CEA losses in all but the most catastrophic earthquake;  
23 and

24 WHEREAS, A federal policy of certain access to federal debt  
25 guarantees for postevent financing would strengthen the  
26 risk-bearing capacity of actuarially sound state-based disaster  
27 programs like the CEA and reduce the preevent expense of  
28 providing that insurance. In recent sessions of the United States  
29 Congress, a proposed federal partnership limited to prequalified,  
30 actuarially sound state earthquake insurance programs has been  
31 estimated to expose the federal government to a 10-year cost of  
32 only \$25 million; and

33 WHEREAS, A state and federal partnership to enhance the  
34 ability of prequalified, actuarially sound state earthquake funds to  
35 access postdisaster borrowing would enable California and other  
36 states using actuarially sound programs to manage risk with a  
37 dramatically better tool; and

38 WHEREAS, The CEA’s certain access to a federal guarantee  
39 of its postearthquake borrowing would ensure access to the private  
40 capital markets at reasonable rates, enhancing the claims-paying

1 capacity for a catastrophic earthquake. That lower-cost capacity,  
2 in turn, would permit the CEA to adjust its annual purchase of  
3 earthquake reinsurance and lower expenses, thus speeding  
4 long-term capital accumulation to help CEA modulate its cost of  
5 providing basic earthquake insurance across the state; now,  
6 therefore, be it

7 *Resolved by the Assembly and the Senate of the State of*  
8 *California, jointly,* That the Legislature urges the President and  
9 the Congress of the United States to enact legislation to establish  
10 guarantees by the federal government to support the responsible  
11 sale of postearthquake bonds by financially sound  
12 residential-earthquake-insurance programs operated by any of the  
13 several states on an actuarially sound basis; and be it further

14 *Resolved,* That the Chief Clerk of the Assembly transmit copies  
15 of this resolution to the President and Vice President of the United  
16 States, to the Speaker of the House of Representatives, to the  
17 Majority Leader of the Senate, and to each Senator and  
18 Representative from the State of California in the Congress of the  
19 United States.