

## Assembly Bill No. 3232

### CHAPTER 969

An act to amend Sections 10089.23, 10089.29, and 10089.40 of, and to add Section 10089.54 to, the Insurance Code, relating to earthquake insurance.

[Approved by Governor September 26, 1996. Filed with Secretary of State September 27, 1996.]

#### LEGISLATIVE COUNSEL'S DIGEST

AB 3232, Knowles. Earthquake insurance: California Earthquake Authority.

Existing law creates the California Earthquake Authority, which is authorized to become operational and issue policies of basic residential earthquake insurance, as defined, under certain conditions.

This bill would:

(1) Revise the amount of the aggregate assessment of participating insurers authorized under existing law, as specified.

(2) Require a notice to policyholders of the right to cancel or nonrenew an earthquake policy if a policy issued by the authority includes a premium surcharge.

(3) Provide that scientific information shall be used by the authority to set earthquake insurance rates only if the information, assumptions, and methodology used are consistent with the available geophysical data and the state of the art of scientific knowledge within the scientific community, as specified, and would further provide that this information shall not be conclusive to support the establishment of different rates between the most populous rating territories in the state unless there is a clear showing of higher risk of earthquake frequency, severity, or loss between those most populous rating territories to support those differences, as specified.

(4) Require the authority to cease writing new earthquake insurance policies 180 days after implementation by both the Federal National Mortgage Association ("Fannie Mae") and the Federal Home Loan Mortgage Association ("Freddie Mac") of policies to require earthquake insurance for any single-family residential structure, other than a condominium unit or townhome, as a condition of purchasing a mortgage or trust deed secured by that structure, except as specified.

The bill would also provide that it shall not become operative unless AB 2086 and SB 1993 are also enacted and become operative. It would declare the intent of the Legislature that certain provisions



in this bill shall supersede and prevail over conflicting provisions in those other bills.

*The people of the State of California do enact as follows:*

SECTION 1. Section 10089.23 of the Insurance Code, as amended by Senate Bill 1993 of the 1995–96 Regular Session, as amended July 7, 1996, is amended to read:

10089.23. (a) (1) If at any time following the payment of earthquake losses the authority's available capital is reduced to less than three hundred fifty million dollars (\$350,000,000), or if at any time the authority's available capital is insufficient to pay benefits and continue operations, the authority shall have the power to assess participating insurance companies subject to the maximum limits as set forth in this section and Section 10089.30. The assessment shall be limited to the amount necessary to pay the outstanding or expected claims of the authority and to return the authority's available capital to three hundred fifty million dollars (\$350,000,000), as determined by the board, subject to approval by the commissioner.

(2) Each participating insurer's assessment shall be determined by multiplying its residential earthquake insurance market share, as of December 31 of the immediately preceding year or the most recent year for which premium data not more than one year old are available, by the amount of the total assessment sought by the authority.

(3) Maximum permissible insurer assessments pursuant to this section and Section 10089.30, maximum permissible earthquake policyholder assessments pursuant to Section 10089.29, and maximum permissible bond issuances or other debt financing issued or secured by the Treasurer pursuant to Section 10089.29 shall be reduced uniformly by multiplication of the maximum assessments and other amounts provided in those sections by the percentage of the total residential property insurance market share participation attained by the authority upon its commencement, as described in Section 10089.15. The total amount of all assessments levied on participating insurance companies by the authority pursuant to this section shall not exceed three billion dollars (\$3,000,000,000), regardless of the frequency or severity of earthquake losses at any and all times subsequent to the creation of the authority. Once a participating insurer has paid amounts equal to its residential earthquake insurance market share multiplied by three billion dollars (\$3,000,000,000) pursuant to this section, the authority's power to assess that insurer under this section shall cease and the authority shall be prohibited from levying additional assessments on that insurer pursuant to this section.

(4) Beginning December 31 of the first year of operations, and each December 31 thereafter, the board shall adjust the maximum



permissible insurer assessments pursuant to this section and Section 10089.30, the maximum permissible authority policyholder assessment pursuant to Section 10089.29, and the maximum permissible bond issuances or other debt financing issued or secured by the Treasurer pursuant to Section 10089.29 to reflect the market share of new insurers entering into the authority as authorized by Sections 10089.15 and 10089.16 and participating insurers withdrawing from the authority as authorized by Section 10089.19. The adjustments shall be made in the same manner as authorized by paragraph (3).

(b) In the case of any insurer assessment, the authority shall cause to be sent to each participating insurer a notice of that insurer's assessment, and full payment shall be due within 30 days and shall be overdue after 30 days. Penalties and interest shall be assessed for late payments in the same manner as provided for late payments of the insurer gross premium tax pursuant to Section 12258 of the Revenue and Taxation Code. The board may waive the penalties and interest for good cause shown. The board shall make every effort to assess insurers only for funds reasonably anticipated to be necessary for claims payments and to return the authority's available capital to three hundred fifty million dollars (\$350,000,000).

(c) Notwithstanding the other provisions of this section, the aggregate assessment authorized by this section shall be reduced to zero 12 years following the commencement of authority operations.

SEC. 2. Section 10089.29 of the Insurance Code, as amended by Assembly Bill 2086 of the 1995-96 Regular Session, as amended July 7, 1996, is amended to read:

10089.29. (a) If benefits paid by the authority following an earthquake event exhaust the total of (1) the authority's available capital, (2) the maximum amount of all insurer capital contributions and assessments pursuant to Sections 10089.15 and 10089.23, (3) all reinsurance actually available and under contract to the authority, and (4) all capital committed and actually available by contract to the authority from private capital markets, the Treasurer, as agent for sale of bonds for the authority, may sell investment grade revenue bonds or issue or secure other debt financing of the authority or any combination of the revenue bonds or debt financing in an amount up to one billion dollars (\$1,000,000,000), in an amount determined by the board pursuant to Section 10089.32. The Treasurer shall make available the net proceeds of the revenue bonds or debt financing as funding for the authority. These funds shall not be used to replenish the fund. Failure of the authority to obtain such funding for any reason shall not obligate the State of California to provide or arrange replacement funding for the authority. The Treasurer may sell revenue bonds for the purpose of refunding the revenue bonds or other debt financing when authorized to do so by the board, and the



surcharge authorized by this section may be used to repay that refunding.

(b) (1) In the event of a revenue bond sale or debt financing arrangement pursuant to this section, the authority shall have the power annually to surcharge all authority policies to secure funds solely to repay the bonded indebtedness or other debt. The net surcharge collected shall not exceed the sum calculated pursuant to paragraph (3) of subdivision (a) of Section 10089.23, and in no event exceed one billion dollars (\$1,000,000,000), plus costs of issuance and sale of those revenue bonds or other debt and amounts paid or payable to bond issuers and providers of credit support and letters of credit for and interest on those revenue bonds or other debt. In no event shall the surcharge on any authority policy exceed 20 percent of the annual basic residential earthquake insurance premium in any one year for the policy.

(2) If a policy issued by the authority includes a premium surcharge pursuant to this subdivision, the participating insurer shall provide the insured a notice in a stand-alone document stating that the policyholder may cancel or nonrenew the earthquake policy. The notice shall specify that cancellation or nonrenewal of the earthquake policy will not affect the underlying residential property insurance policy. The statement shall be provided with the premium billing and shall include the following statement in 14-point boldface type:

**NOTICE OF SURCHARGE ON CEA EARTHQUAKE  
INSURANCE POLICY AND RIGHT TO CANCEL**

**A SURCHARGE HAS BEEN INCLUDED IN THE PREMIUM FOR YOUR CEA EARTHQUAKE INSURANCE POLICY. YOU MAY CHOOSE TO RENEW THIS POLICY AT THE NEW RATE OR YOU MAY CANCEL OR NONRENEW YOUR CEA EARTHQUAKE INSURANCE POLICY. CANCELLATION OR NONRENEWAL OF YOUR CEA POLICY WILL HAVE NO AFFECT ON YOUR HOMEOWNERS' OR FIRE INSURANCE POLICY. HOWEVER, IF YOU WANT EARTHQUAKE INSURANCE TO BE PROVIDED BY THE CEA, YOU MUST PAY THE FULL PREMIUM FOR THE CEA POLICY, INCLUDING THE SURCHARGE.**

(c) The total amount of indebtedness and policy surcharges authorized under this section shall not exceed the sum calculated pursuant to paragraph (3) of subdivision (a) of Section 10089.23, and in no event exceed one billion dollars (\$1,000,000,000) plus costs of issuance and sale of those revenue bonds or other debt and amounts paid or payable to bond issuers and providers of credit support and



letters of credit for, and interest on, those revenue bonds or other debt, regardless of the frequency or severity of earthquake losses at any and all times subsequent to the creation of the authority. Once the authority has levied policy surcharges in an amount equal to the sum calculated pursuant to paragraph (3) of subdivision (a) of Section 10089.23, and in no event more than one billion dollars (\$1,000,000,000) plus costs of issuance and sale of those revenue bonds or other debt and amounts paid or payable to bond issuers and providers of credit support and letters of credit for, and interest on, those revenue bonds or other debt, the authority's power to surcharge policies shall cease and the authority shall be prohibited from levying additional surcharges pursuant to this section.

(d) Consistent with the provisions of Section 676, the authority shall cancel the policy of basic residential earthquake insurance if the policyholder fails to pay the earthquake policy surcharge authorized by the authority, and the insurer shall cancel the policy of residential property insurance if the policyholder fails to pay the policy surcharge authorized by the authority.

SEC. 3. Section 10089.40 of the Insurance Code, as amended by AB 2086 of the 1995-96 Regular Session, as amended July 7, 1996, is amended to read:

10089.40. (a) Rates established by the authority shall be actuarially sound so as to not be excessive, inadequate, or unfairly discriminatory. Rates shall be established based on the best available scientific information for assessing the risk of earthquake frequency, severity, and loss. Rates shall be equivalent for equivalent risks. Factors the board shall consider in adopting rates include, but are not limited to, the following:

(1) Location of the insured property and its proximity to earthquake faults and to other geological factors that affect the risk of earthquake or damage from earthquake.

(2) The soil type on which the insured dwelling is built.

(3) Construction type and features of the insured dwelling.

(4) Age of the insured dwelling.

(5) The presence of earthquake hazard reduction factors, including those set forth in subdivision (a) of Section 10089.2.

(b) (1) If scientific information from geologists, seismologists, or similar experts that assesses the frequency or severity of risk of earthquake is considered in setting rates or in arriving at the modeling assumptions upon which those rates are based, the information may be used to establish differentials among risks only if the information, assumptions, and methodology used are consistent with the available geophysical data and the state of the art of scientific knowledge within the scientific community.

(2) Scientific information from geologists, seismologists, or similar experts shall not be conclusive to support the establishment of different rates between the most populous rating territories in the



northern and southern regions of the state unless that information, as analyzed by experts such as the United States Geological Survey, the California Division of Mines and Geology, and experts in the scientific or academic community, clearly shows a higher risk of earthquake frequency, severity, or loss between those most populous rating territories to support those differences.

(3) It is not the intent of the Legislature in adopting this subdivision to mandate a uniform statewide flat rate for California Earthquake Authority policies.

(c) The classification system established by the board shall not be adjusted or tempered in any way to provide rates lower than are justified for classifications that present a high risk of loss or higher than are justified for classifications that present a low risk of loss.

(d) Policyholders who have retrofitted their homes to withstand earthquake shake damage according to standards and to the extent set by the board shall enjoy a premium discount or credit of not less than 5 percent on the authority-issued policy of residential earthquake coverage, as long as the discount or credit is determined actuarially sound by the authority.

(e) All rates shall be approved by the commissioner prior to their use.

SEC. 4. Section 10089.54 is added to the Insurance Code, to read:

10089.54. (a) Unless authorized by a statute enacted subsequent to the effective date of this section, the authority shall cease writing new earthquake insurance policies 180 days after implementation by both the Federal National Mortgage Association (“Fannie Mae”) and the Federal Home Loan Mortgage Association (“Freddie Mac”) of policies to require earthquake insurance for any single-family residential structure, other than a condominium unit or townhome, as a condition of purchasing a mortgage or trust deed secured by that structure. Notwithstanding this restriction, the authority shall continue to renew its existing earthquake insurance policies and shall accept applications for earthquake insurance from residential property insurance policyholders of participating insurers in accordance with subdivision (b) of Section 10086.

(b) In the event that both the Federal National Mortgage Association (“Fannie Mae”) and the Federal Home Loan Mortgage Association (“Freddie Mac”) have proposed to implement policies to require earthquake insurance for any single-family residential structure, other than a condominium unit or townhome, as a condition of purchasing a mortgage or trust deed secured by that structure, it is the intent of the Legislature that the Legislature should convene to consider whether the authority should continue to write new earthquake insurance policies, with or without modification, or to cease writing new earthquake insurance policies.



SEC. 5. This act shall not become operative unless Assembly Bill 2086 and Senate Bill 1993 of the 1995–96 Regular Session are also enacted and become operative.

SEC. 6. It is the intent of the Legislature that Sections 10089.23 and 10089.40 of the Insurance Code, as amended by this act, shall supersede and prevail over any conflicting provisions in Assembly Bill 2086 and Senate Bill 1993 of the 1995–96 Regular Session, if either or both of those bills are enacted after this act.

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