



CITY COUNCIL STAFF REPORT

DATE: May 16, 2012

CONSENT

SUBJECT: SUPPORT FEDERAL EARTHQUAKE INSURANCE AFFORDABILITY ACT
AND AUTHORIZE DELIVERY OF A LETTER IN SUPPORT

FROM: David H. Ready, City Manager

BY: Douglas Holland, City Attorney

SUMMARY

Congress is currently reviewing legislation that would allow the federal government to guarantee bonds issued through state catastrophe insurance programs. It is estimated that this approach, codified in the Earthquake Insurance Affordability Act, could lower earthquake insurance rates for California property owners and expand coverage across the state. The proposed legislation enjoys bi-partisan support; Senator Feinstein (D) is a co-author of the legislation in the Senate and Congressman Campbell (R) is a co-author in the House of Representatives.

RECOMMENDATION:

Authorize the Mayor to execute and deliver a letter to appropriate representatives in Congress supporting passage of the Earthquake Insurance Affordability Act.

ANALYSIS:

Prior to the 1994 Northridge earthquake, many insurers offered relatively inexpensive earthquake insurance to property owners in California. At the time of the earthquake, state law required insurers to provide earthquake insurance with home insurance policies. The \$20 billion in damage resulting from the Northridge earthquake caused many insurers to leave the state. Homeowners and prospective purchasers were unable to purchase home insurance policies at affordable rates. The state subsequently created the California Earthquake Authority, a nonprofit entity, to offer earthquake insurance policies and eliminated the requirement for private home insurers to provide earthquake insurance.

In order to provide policies without risking major loss, the California Earthquake Authority invests in reinsurance policies from multiple private insurers. The high cost of reinsurance results in the Authority offering policies with significantly higher rates than were in place prior to the Northridge quake and deductibles as high as 10 percent of the property's replacement value. The result is only 10% of homeowners in California maintain earthquake insurance.

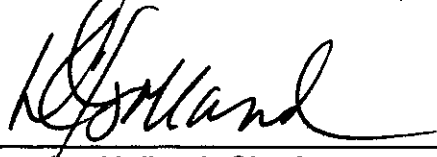
ITEM NO. 82

Earthquake Insurance Affordability Act

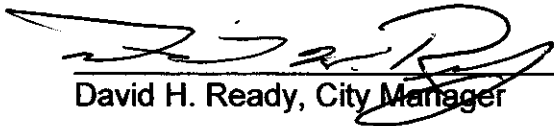
The proposed Earthquake Insurance Affordability act would provide up to \$5 billion in federal guarantees for loans issued by private lenders for state catastrophe insurance programs. The federal loan protection guarantee would eliminate the California Earthquake Authority's need for costly private reinsurance.

The Congressional Budget Office found that the approach will have no cost to the taxpayers. The federal guarantee will simply back private loans in the event of an earthquake. The Authority will have the ability through its insurance premiums to pay back the loans over time without risk to the federal treasury. The Authority estimates that upon passage of the Act it will be able to immediately eliminate reinsurance costs and reduce consumer rates by as much as 20 percent.

FISCAL IMPACT: No fiscal impact.



Douglas Holland, City Attorney



David H. Ready, City Manager

Attachments:

1. Earthquake Insurance Affordability Act
2. Draft Letter to Congress

Letter to:

Honorable Diane Feinstein
Honorable John Campbell

Re: Earthquake Insurance Affordability Act (S. 637; HR 3125)

Dear Senator Feinstein:

On behalf of the City Council of the City of Palm Springs, I am pleased to inform you of our support of the Earthquake Insurance Affordability Act.

Recent catastrophic earthquakes in Japan, Haiti, and Mexico have served as painful reminders of California's vulnerability to the devastation wrought from earthquakes. No part of our great state is immune from earthquakes. Experts agree that a major earthquake within the next 30 years is a virtual certainty for our state. Although 80% of Californians currently reside on or near a fault, fewer than 10% of California households are covered by earthquake insurance.

Palm Springs property owners, as well as all Californians, need greater access to affordable earthquake insurance. This Council believes that the Earthquake Insurance Affordability Act is a fiscally sound solution that will enable homeowners to acquire reasonably affordable earthquake insurance. Increasing the number of insured homeowners should reduce the risk to all taxpayers who may otherwise bear substantial costs in the aftermath of a catastrophic earthquake. Insurance is key to a faster recovery from a disaster and important to rebuilding our communities after a natural disaster. As you have both noted, preliminary estimates from the nonpartisan Congressional Budget Office shows that the cost of the Earthquake Insurance Affordability Act to the federal government and taxpayers is zero.

We applaud your bipartisan support of this vital legislation and your efforts to work cooperatively to help the residents of this state to anticipate and prepare for the next major earthquake that will certainly impact our state.

Sincerely

Stephen Pougnet
Mayor

.....
(Original Signature of Member)

112TH CONGRESS
1ST SESSION

H. R. _____

To establish a program to provide guarantees for debt issued by or on behalf of State catastrophe insurance programs to assist in the financial recovery from earthquakes, earthquake-induced landslides, volcanic eruptions, and tsunamis.

IN THE HOUSE OF REPRESENTATIVES

Mr. CAMPBELL introduced the following bill; which was referred to the Committee on _____

A BILL

To establish a program to provide guarantees for debt issued by or on behalf of State catastrophe insurance programs to assist in the financial recovery from earthquakes, earthquake-induced landslides, volcanic eruptions, and tsunamis.

1 *Be it enacted by the Senate and House of Representa-*
2 *tives of the United States of America in Congress assembled,*

3 **SECTION 1. SHORT TITLE; TABLE OF CONTENTS.**

4 (a) **SHORT TITLE.**—This Act may be cited as the
5 “Earthquake Insurance Affordability Act”.

1 (b) TABLE OF CONTENTS.—The table of contents for
2 this Act is as follows:

- Sec. 1. Short title; table of contents.
- Sec. 2. Findings and purposes.
- Sec. 3. Definitions.
- Sec. 4. Eligible State programs.
- Sec. 5. Establishment of debt-guarantee program.
- Sec. 6. Effect of guarantee.
- Sec. 7. Assessment at time of guarantee.
- Sec. 8. Payment of losses.
- Sec. 9. Full faith and credit.
- Sec. 10. Budgetary impact; costs.
- Sec. 11. Regulations.

3 **SEC. 2. FINDINGS AND PURPOSES.**

4 (a) FINDINGS.—Congress finds the following:

5 (1) Major earthquakes are likely in the United
6 States. For example, the United States Geological
7 Survey predicts that there is a 99.7 percent chance
8 that a magnitude 6.7 earthquake will strike in Cali-
9 fornia in the next 30 years and that there is a 46
10 percent chance that a magnitude 7.5 earthquake will
11 strike in California in the next 30 years. Earth-
12 quakes can be caused by volcanic or tectonic events
13 and result in destructive shaking of the earth, fires,
14 landslides, volcanic eruptions, and tsunamis.

15 (2) Despite the known risk of earthquakes, rel-
16 atively few homeowners have earthquake insurance.
17 For example, in California, 88 percent of homes in-
18 sured for fire do not have earthquake insurance. In
19 the event of a catastrophic earthquake, the lack of
20 homeowner earthquake-insurance coverage will slow

1 recovery, create economic hardship, and increase the
2 risk of mortgage and other credit defaults and ad-
3 versely affect the Nation's banking system.

4 (3) It is important that States improve the af-
5 fordability, availability, and quality of earthquake in-
6 surance so that more homeowners will purchase cov-
7 erage. For example, California has created the Cali-
8 fornia Earthquake Authority to provide earthquake
9 insurance to homeowners through private-sector in-
10 surers.

11 (4) It is a proper role of the Federal Govern-
12 ment to help prepare and protect its citizens from
13 catastrophes such as earthquakes and to facilitate
14 consumer protection, victim assistance, and indi-
15 vidual and community recovery, including financial
16 recovery.

17 (b) PURPOSES.—The purposes of this Act are to es-
18 tablish a program—

19 (1) to promote the availability of private capital
20 to provide liquidity and capacity to State earthquake
21 insurance programs; and

22 (2) to expedite the payment of claims under
23 State earthquake insurance programs and better as-
24 sist the financial recovery from significant earth-

1 quakes by authorizing the Secretary of the Treasury
2 to guarantee debt for such purposes.

3 **SEC. 3. DEFINITIONS.**

4 In this Act, the following definitions shall apply:

5 (1) **COMMITMENT TO GUARANTEE.**—The term
6 “commitment to guarantee” means a commitment to
7 make debt guarantees to an eligible State program
8 pursuant to section 5.

9 (2) **ELIGIBLE STATE PROGRAM.**—The term “eli-
10 gible State program” means a State program that,
11 pursuant to section 4, is eligible to receive a debt
12 guarantee under this Act.

13 (3) **INSURED LOSS.**—The term “insured loss”
14 means any loss resulting from an earthquake, an
15 earthquake-related event, or fire following an earth-
16 quake that is determined by an eligible State pro-
17 gram as being covered by insurance made available
18 under that eligible State program.

19 (4) **QUALIFYING ASSETS.**—The term “quali-
20 fying assets” means the policyholder surplus of the
21 eligible State program as stated in the most recent
22 quarterly financial statement filed by the program
23 with the domiciliary regulator of the program in the
24 last quarter ending prior to an insured-loss trig-
25 gering event or events.

1 (5) RESIDENTIAL PROPERTY INSURANCE.—The
2 term “residential property insurance” means insur-
3 ance coverage for—

4 (A) individually owned residential struc-
5 tures of not more than 4 dwelling units, individ-
6 ually owned condominium units, or individually
7 owned mobile homes, and their contents, located
8 in a State and used exclusively for residential
9 purposes or a tenant’s policy written to include
10 personal contents of a residential unit located in
11 the State, but shall not include—

12 (i) insurance for real property or its
13 contents used for any commercial, indus-
14 trial, or business purpose, except a struc-
15 ture of not more than 4 dwelling units
16 rented for individual residential purposes;
17 or

18 (ii) a policy that does not include any
19 of the perils insured against in a standard
20 fire policy or any earthquake policy; or

21 (B) commercial residential property, which
22 includes property owned by a condominium as-
23 sociation or its members, property owned by a
24 cooperative association, or an apartment build-
25 ing.

1 (6) SECRETARY.—The term “Secretary” means
2 the Secretary of the Treasury.

3 (7) STATE.—The term “State” means each of
4 the several States of the United States, the District
5 of Columbia, the Commonwealth of Puerto Rico, the
6 Commonwealth of the Northern Mariana Islands,
7 Guam, the United States Virgin Islands, American
8 Samoa, and any other territory or possession of the
9 United States.

10 **SEC. 4. ELIGIBLE STATE PROGRAMS.**

11 (a) ELIGIBLE STATE PROGRAMS.—A State program
12 shall be considered an eligible State program for purposes
13 of this Act if the State program or other State entity au-
14 thorized to make such determinations certifies to the Sec-
15 retary, in accordance with the procedures established
16 under subsection (b), that the State program complies
17 with the following requirements:

18 (1) STATE PROGRAM DESIGN.—The State pro-
19 gram is established and authorized by State law as
20 an earthquake insurance program that offers resi-
21 dential property insurance coverage for insured
22 losses to property, contents, and additional living ex-
23 penses, and which is not a State program that re-
24 quires insurers to pool resources to provide property
25 insurance coverage for earthquakes.

1 (2) OPERATION.—The State program shall
2 meet the following requirements:

3 (A) A majority of the members of the gov-
4 erning body of the State program shall be pub-
5 lic officials or appointed by public officials.

6 (B) The State shall have a financial inter-
7 est in the State program.

8 (C) If the State has at any time appro-
9 priated amounts from the State program's
10 funds for any purpose other than payments for
11 losses insured under the State program, or pay-
12 ments made in connection with any of the State
13 program's authorized activities, the State shall
14 have returned such amounts to the State fund,
15 together with interest on such amounts.

16 (3) TAX STATUS.—The State program shall
17 have received from the Secretary (or the Secretary's
18 designee) a written determination, within the mean-
19 ing of section 6110(b) of the Internal Revenue Code
20 of 1986, that the State program either—

21 (A) constitutes an “integral part” of the
22 State that has created it; or

23 (B) is otherwise exempt from Federal in-
24 come taxation.

1 (4) EARNINGS.—The State program may not
2 provide for any distribution of any part of any net
3 profits of the State program to any insurer that par-
4 ticipates in the State program.

5 (5) LOSS PREVENTION AND MITIGATION.—

6 (A) MITIGATION OF LOSSES.—The State
7 program shall include provisions designed to en-
8 courage and support programs to mitigate
9 losses for which the State insurance program
10 was established to provide insurance.

11 (B) OPERATIONAL REQUIREMENTS.—The
12 State program shall operate in a State that—

13 (i) has in effect and enforces, or the
14 appropriate local governments within the
15 State have in effect and enforce, nationally
16 recognized building, seismic-design, and
17 safety codes and consensus-based stand-
18 ards; and

19 (ii) has taken actions to establish an
20 insurance rate structure that takes into ac-
21 count measures to mitigate insured losses.

22 (6) REQUIREMENTS REGARDING COVERAGE.—

23 The State program—

24 (A) may not, except for charges or assess-
25 ments related to post-event financing or bond-

1 ing, involve cross-subsidization between any
2 separate property-and-casualty insurance lines
3 offered under the State program pursuant to
4 paragraph (1);

5 (B) shall be subject to a requirement
6 under State law that for earthquake insurance
7 coverage made available under the State insur-
8 ance program the premium rates charged on
9 such insurance shall be actuarially sound; and

10 (C) shall make available to all qualifying
11 policyholders insurance coverage and mitigation
12 services on a basis that is not unfairly discrimi-
13 natory.

14 (b) ANNUAL CERTIFICATION.—The Secretary shall
15 establish procedures for initial certification and annual re-
16 certification as an eligible State program.

17 **SEC. 5. ESTABLISHMENT OF DEBT-GUARANTEE PROGRAM.**

18 (a) AUTHORITY OF SECRETARY.—The Secretary is
19 authorized and shall have the powers and authorities nec-
20 essary—

21 (1) to guarantee, and to enter into commit-
22 ments to guarantee, holders of debt against loss of
23 principal or interest, or both, on any debt issued by
24 eligible State programs for purposes of this Act; and

1 (2) to certify and recertify State catastrophe in-
2 surance programs that cover earthquake peril to be-
3 come or remain eligible for the benefits of such a
4 debt-guarantee program.

5 (b) LIMIT ON OUTSTANDING DEBT GUARANTEE.—
6 The aggregate amount of debt covered by the Secretary's
7 guarantees and commitments to guarantee for all eligible
8 State programs outstanding at any time shall not exceed
9 \$5,000,000,000, including interest.

10 (c) FUNDING.—

11 (1) APPROPRIATION OF FEDERAL PAYMENTS.—
12 Subject to subsection (b), there are hereby appro-
13 priated, out of funds in the Treasury not otherwise
14 appropriated, such sums as may be necessary to sat-
15 isfy debt guarantee commitments extended to eligible
16 State programs under this Act.

17 (2) CERTIFICATION FEE.—Upon certification or
18 recertification as an eligible State program under
19 section 4(a) or 4(b), a State program shall be
20 charged a certification fee sufficient in the judge-
21 ment of the Secretary at the time of certification to
22 cover—

23 (A) applicable administrative costs arising
24 from each certification or recertification, includ-
25 ing all pre-certification costs and a proportional

1 share of the costs arising from the administra-
2 tion of the program established under this Act,
3 but in any event not to exceed one-half of 1
4 percent annum of the aggregate principal
5 amount of the debt for which the eligible State
6 program is issued a guarantee commitment;
7 and

8 (B) any probable losses on the aggregate
9 principal amount of the debt for which the eligi-
10 ble State program is issued a guarantee com-
11 mitment.

12 (3) RULE OF CONSTRUCTION.—Any funds ex-
13 pended or obligated by the Secretary for the pay-
14 ment of administrative expenses for conduct of the
15 debt-guarantee program authorized by this Act shall
16 be deemed appropriated at the time of such expendi-
17 ture or obligation from the certification and recer-
18 tification fees collected pursuant to paragraph (2).

19 (d) CONDITIONS FOR GUARANTEE ELIGIBILITY.—A
20 debt guarantee under this section may be made only if
21 the Secretary has issued a commitment to guarantee to
22 a certified, eligible State program. The commitment to
23 guarantee shall be in force for a period of 3 years from
24 its initial issuance and may be extended by the Secretary
25 for 1 year on each annual anniversary of the issuance of

1 the commitment to guarantee. The commitment to guar-
2 antee and each extension of such commitment may be
3 issued by the Secretary only if the following requirements
4 are satisfied:

5 (1) The eligible State program submits to the
6 Secretary a report setting forth, in such form and
7 including such information as the Secretary shall re-
8 quire, how the eligible State program plans to repay
9 guarantee-eligible debt it may incur.

10 (2) Based on the eligible State program's report
11 submitted pursuant to paragraph (1), the Secretary
12 determines there is reasonable assurance that the el-
13 igible State program can meet its repayment obliga-
14 tion under such debt.

15 (3) The eligible State program enters into an
16 agreement with the Secretary, as the Secretary shall
17 require, that the eligible State program will not use
18 Federal funds of any kind or from any Federal
19 source (including any disaster or other financial as-
20 sistance, loan proceeds, and any other assistance or
21 subsidy) to repay the debt.

22 (4) The commitment to guarantee shall specify
23 and require the payment of the fees for debt guar-
24 antee coverage.

1 (5) The maximum term of the debt specified in
2 a commitment issued under this section may not ex-
3 ceed 30 years.

4 (e) MANDATORY ASSISTANCE FOR ELIGIBLE STATE
5 PROGRAMS.—The Secretary shall upon the request of an
6 eligible State program and pursuant to a commitment to
7 guarantee issued under subsection (d), provide a guar-
8 antee under subsection (f) for such eligible State program
9 in the amount requested by such eligible State program,
10 subject to the limitation under subsection (f)(2).

11 (f) CATASTROPHE DEBT GUARANTEE.—A debt guar-
12 antee under this subsection for an eligible State program
13 shall be subject to the following requirements:

14 (1) PRECONDITIONS.—The eligible State pro-
15 gram shows to the satisfaction of the Secretary that
16 insured losses to the eligible State program arising
17 from the event or events covered by the commitment
18 to guarantee are likely to exceed 80 percent of the
19 eligible State program's qualifying assets available to
20 pay claims, as calculated on the date of the event
21 and based on the eligible State program's most re-
22 cent quarterly financial statement filed with its
23 domiciliary regulator.

24 (2) USE OF FUNDS.—Proceeds of debt guaran-
25 teed under this section shall be used only to pay the

1 costs of issuing debt and of securing or providing
2 claim-payment capacity for paying the insured losses
3 and loss adjustment expenses incurred by an eligible
4 State program. Such amounts shall not be used for
5 any other purpose.

6 **SEC. 6. EFFECT OF GUARANTEE.**

7 The issuance of any guarantee by the Secretary
8 under this Act shall be conclusive evidence that—

- 9 (1) the guarantee has been properly obtained;
10 (2) the underlying debt qualified for such guar-
11 antee; and
12 (3) the guarantee is valid, legal, and enforce-
13 able.

14 **SEC. 7. ASSESSMENT AT TIME OF GUARANTEE.**

15 To extent not satisfied by the fees collected under sec-
16 tion 5(c)(2), the Secretary shall charge and collect fees
17 for each guarantee issued in amounts sufficient in the
18 judgement of the Secretary at the time of issuance of the
19 guarantee to cover applicable administrative costs and
20 probable losses on the guaranteed obligations.

21 **SEC. 8. PAYMENT OF LOSSES.**

22 (a) **IN GENERAL.**—The Secretary agrees to pay to
23 the duly appointed paying agent or trustee (in this section
24 referred to as the “Fiscal Agent”) for the eligible State
25 program that portion of the principal and interest on any

1 debt guaranteed under this Act that shall become due to
2 payment but shall be unpaid by the eligible State program
3 as a result of such program having provided insufficient
4 funds to the Fiscal Agent to make such payments. The
5 Secretary shall make such payments on the date such
6 principal or interest becomes due for payment or on the
7 business day next following the day on which the Secretary
8 shall receive notice of failure on the part of the eligible
9 State program to provide sufficient funds to the Fiscal
10 Agent to make such payments, whichever is later. Upon
11 making such payment, the Secretary shall be subrogated
12 to all the rights of the ultimate recipient of the payment.
13 The Secretary shall be entitled to recover from the eligible
14 State program the amount of any payments made pursu-
15 ant to any guarantee entered into under this Act.

16 (b) ROLE OF THE ATTORNEY GENERAL.—The Attor-
17 ney General shall take such action as may be appropriate
18 to enforce any right accruing, and to collect any and all
19 sums owing, to the United States as a result of the
20 issuance of any guarantee under this Act.

21 (c) RULE OF CONSTRUCTION.—Nothing in this sec-
22 tion shall be construed to preclude any forbearance for the
23 benefit of the eligible State program which may be agreed
24 upon by the parties to the guaranteed debt and approved
25 by the Secretary, provided that budget authority for any

1 resulting cost, as such term is defined under the Federal
2 Credit Reform Act of 1990, is available.

3 (d) RIGHT OF THE SECRETARY.—Notwithstanding
4 any other provision of law relating to the acquisition, han-
5 dling, or disposal of property by the United States, the
6 Secretary shall have the right in the discretion of the Sec-
7 retary to complete, recondition, reconstruct, renovate, re-
8 pair, maintain, operate, or sell any property acquired by
9 the Secretary pursuant to the provisions of this Act.

10 **SEC. 9. FULL FAITH AND CREDIT.**

11 The full faith and credit of the United States is
12 pledged to the payment of all guarantees issued under this
13 Act with respect to principal and interest.

14 **SEC. 10. BUDGETARY IMPACT; COSTS.**

15 For purposes of section 502(5) of the Federal Credit
16 Reform Act of 1990, the cost of guarantees to be issued
17 under this Act shall be calculated by adjusting the dis-
18 count rate in section 502(5)(E) of such Act for market
19 risk.

20 **SEC. 11. REGULATIONS.**

21 The Secretary shall issue any regulations necessary
22 to carry out the debt-guarantee program established under
23 this Act.