



**GOVERNING BOARD MEETING
WEDNESDAY, AUGUST 7, 2019
1:00 P.M.**

**California Department of Food and Agriculture
1220 N Street
Auditorium, Room 131
Sacramento, California 95814**



Date of Notice: Friday, July 26, 2019

AMENDED* PUBLIC NOTICE

*** Additional telephonic audio instructions**

**A PUBLIC MEETING OF THE GOVERNING BOARD OF THE CALIFORNIA WILDFIRE FUND
(The California Earthquake Authority Governing Board,
Exercising the Powers of the California Catastrophe Response Council
pursuant to California Gov't Code §8899.70 and
Ins. Code §10089.7(c)(13).)**

NOTICE IS HEREBY GIVEN that the Governing Board of the California Earthquake Authority ("CEA"), acting in an interim capacity on behalf of, and exercising the authorities, duties and powers of, the California Catastrophe Response Council, will meet in Sacramento, California. Pursuant to California Insurance Code §10089.7(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.

LOCATION: California Department of Food and Agriculture *
Auditorium, Room 131
1220 N Street
Sacramento, California

DATE: Wednesday, August 7, 2019

TIME: 1:00 p.m.

This meeting of the Governing Board will be available for audio. Please wait until the official start time of the meeting before clicking the icon:



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*** Because of facility limitations at this location, this Governing Board meeting will not be available as streaming video on the Internet, but can be listened to remotely as noted above. Please note that Public Participation will be available only at the meeting location.**

AGENDA:

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. Executive Report: Report by CEA Executive Staff regarding CEA's responsibilities and actions as Interim Administrator of the California Wildfire Fund under recently enacted AB 1054 and AB 111.
3. Wildfire Fund Setup and Capitalization: Discussion and approval of all administrative steps undertaken or to be undertaken by CEA to implement and operationalize the California Wildfire Fund, and to prepare for initial capitalization of the Fund. Consideration and adoption of a resolution or resolutions as follows:
- a. Approving, adopting and/or ratifying agreements by CEA, as Interim Administrator of and on behalf of the Wildfire Fund, for Custodial Banking and Demand Deposit Accounts, Asset-Management Services, and Investment Consulting;
 - b. Authorizing CEA to undertake expedited procurement and engagement of additional Asset Managers in anticipation of additional capitalization;
 - c. Approving and adopting Investment Policies for the Wildfire Fund;
 - d. Authorizing CEA to exercise and carry out such of the duties specified in Public Utilities Code § 3281 as CEA determines necessary to the start-up and initial capitalization of the Wildfire Fund; and
 - e. Authorizing CEA staff to develop, document and implement a cost allocation methodology to allocate all CEA administration expenses arising from or related to the Wildfire Fund for payment by the Wildfire Fund consistent with Ins. Code § 10089.6(d)(11).
4. Wildfire Fund Risk Transfer Issues: Discussion and approval of CEA's activities to procure reinsurance intermediary and risk transfer services. Consideration and adoption of a resolution or resolutions authorizing CEA to contract for reinsurance and risk transfer advisory services, and to develop and implement risk transfer guidelines and a risk transfer strategy to protect the Wildfire Fund.
5. Administrator's Plan of Operations: Discussion of the development of a Plan of Operations for the Wildfire Fund pursuant to Public Utilities Code § 3282.
6. 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.
7. Adjournment.

For further information about this notice or its contents:

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To view this notice on the CEA website, 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 Shannon McEuen by telephone, toll free, at (877) 797-4300 or by email at CEABoardLiaison@calquake.com.

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

August 7, 2019

Agenda Item 2: Report by CEA Executive Staff

Recommended Action: No action required—information only

CEA Executive Staff will report on CEA’s responsibilities and actions as Interim Administrator of the California Wildfire Fund under AB 1054 and AB 111.



Governing Board Memorandum

August 7, 2019

Agenda Item 3: Wildfire Fund Setup and Capitalization: Discussion and approval of all administrative steps undertaken or to be undertaken by CEA to implement and operationalize the California Wildfire Fund, and to prepare for initial capitalization of the Fund.

Recommended Action: Consideration and adoption of a resolution or resolutions as follows:

- a) Approving, adopting and/or ratifying agreements by CEA, as Interim Administrator of and on behalf of the Wildfire Fund, for Custodial Banking and Demand Deposit Accounts, Asset-Management Services, and Investment Consulting;
- b) Authorizing CEA to undertake expedited procurement and engagement of additional Asset Managers in anticipation of additional capitalization;
- c) Approving and adopting Investment Policies for the Wildfire Fund; and
- d) Authorizing CEA staff to develop, document and implement a cost allocation methodology to allocate all CEA administration expenses arising from or related to the Wildfire Fund for payment by the Wildfire Fund consistent with Pub. Utilities Code § 3294 and Ins. Code § 10089.6(d)(11).

Background

2019 Wildfire Legislation. On Friday, July 12, 2019, Governor Newsom signed into law AB 1054 (Holden, Burke & Mayes) and AB 111 (Committee on Budget) (the "2019 Wildfire Legislation"). The 2019 Wildfire Legislation enacts a broad set of reforms and programs related to utility-caused wildfires in California. The 2019 Wildfire Legislation, which took immediate effect upon the Governor's signature, establishes the California Wildfire Fund.

The purpose of the Wildfire Fund is to provide a source of money to pay or reimburse eligible claims arising from a covered wildfire caused by a utility company which participates in the Wildfire Fund by assisting in capitalizing the Fund, and undertaking certain other obligations specified in the law.

Wildfire Fund Capitalization. In general terms, the 2019 Wildfire Legislation creates a capitalization structure that will result in a total of \$21 billion flowing into the Wildfire Fund to provide claim-paying capacity after utility-caused wildfires. The \$21 billion in funding is split (roughly in half) between surcharges on utility ratepayers and contributions from the three large investor-owned utility companies in California. The following shows a high-level summary of the capitalization structure:¹

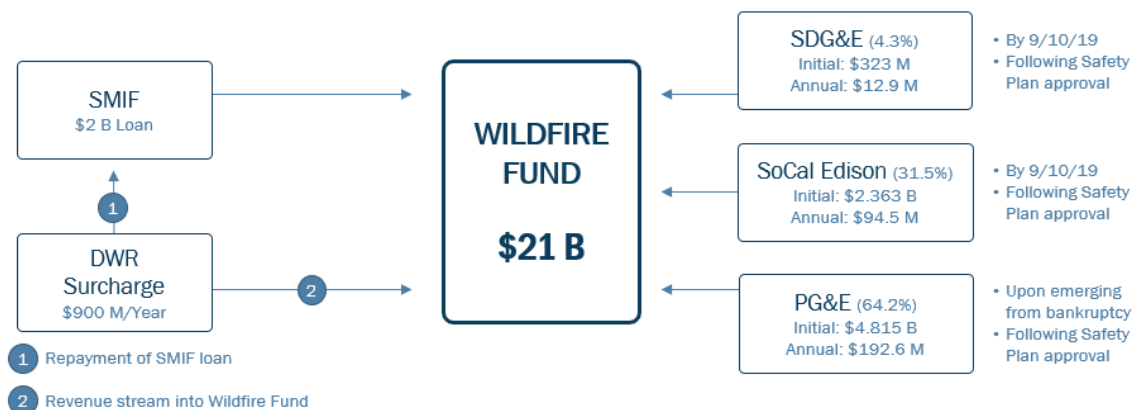
Ratepayers \$10.5 B

- Initial SMIF Loan: \$2 B
- Annual Revenue Stream from DWR Surcharge: ~\$900 M/year

+

Utilities \$10.5 B

- Initial Contribution: \$7.5 B
- Annual Contribution: \$300 M (\$3 B total)



Governance. Governance of the Wildfire Fund is the responsibility of the newly-created California Catastrophe Response Council (“Council”). 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. However, the Council does not become active and empowered until there is a quorum of members appointed, which has not yet occurred. Once activated, the Council is charged with appointing an “Administrator” for the Wildfire Fund.

¹ The contribution numbers in this chart are approximate figures for illustration purposes only.



Until such time as the Council is activated, and the Administrator is appointed, the legislation provides for CEA to act as the Interim Administrator, and for CEA's Governing Board to have all the powers granted to the Council related to the Wildfire Fund. Thus, this meeting of the Governing Board is specifically and solely related to the Wildfire Fund, and the Governing Board is exercising the powers of the Council to consider, discuss and approve the several agreements described below related to the set-up and initial capitalization of the Wildfire Fund.

Initialization and Capitalization of the Wildfire Fund. As noted above, the 2019 Wildfire Legislation requires that the Wildfire Fund be established and initially capitalized in the form of a short term \$2 billion loan from the Treasurer's Surplus Money Investment Fund (SMIF), a fund within the State's Pooled Money Investment Account. The SMIF loan will be repaid in 2020 from the proceeds of Department of Water Resources revenue bonds, which bonds will in turn be repaid from small monthly surcharges on utility ratepayer invoices. The Governor's Finance Director, Treasurer's Office and Controller's Office are actively working together to ensure funding on August 15, 2019 of the \$2 billion loan from the SMIF.

Thus, the first order of business for CEA, as the Interim Administrator, and the Governing Board, exercising the power and authority of the Council, is to establish immediately an administrative infrastructure to receive and invest the \$2 billion in the Wildfire Fund. Drawing on its more than 20 years of experience administering and investing a multi-billion-dollar fund (the Earthquake Authority Fund), CEA was able to quickly negotiate and finalize agreements with (i) U.S. Bank, for establishment of a Custodial Trust Account and a Demand Deposit Account (i.e., a checking account), (ii) with four asset management firms for asset management/investment services (one of these firms is a minority-owned firm), and (iii) with Raymond James & Associates, Inc. for investment consulting services (the lead advisor will be Kapil Bhatia, CEA's long-standing investment and financial advisor). Collectively these agreements will allow CEA to operationalize and commence receipt and investment of the \$2 billion initial capitalization on an accelerated timeline consistent with the 2019 Wildfire Legislation. Upon approval of these arrangements by the Board, the initial \$2 billion in capitalization is scheduled to be received by the Wildfire Fund on August 15, 2019.

These banking, advisory and asset management agreements will also prepare the Wildfire Fund to receive, over time, the additional \$7.5 billion in initial capitalization from the three large investor-owned utility companies. On or around September 10, 2019, the Wildfire Fund expects to receive approximately \$2.68 billion from the two utilities that are not in



bankruptcy (SDG&E and SoCal Edison), with the balance of approximately \$4.82 billion coming from PG&E after it confirms a plan of reorganization and emerges from its current bankruptcy proceeding. In preparation for the receipt and investment of those additional funds, CEA has undertaken an expedited procurement process to obtain services from additional asset managers to manage the capital deposited by the utility companies. CEA is seeking authority to execute additional asset management agreements with qualified firms that provide competitive responses to this procurement process.

Contracting Process and Vendor Selection

Process. In undertaking the identification of vendors to provide these initial banking and investment services to the Wildfire Fund, CEA engaged in a thorough diligence process to ensure that the vendors were suitable and reliable, and offered highly competitive economic terms to the Wildfire Fund. The 2019 Wildfire Legislation expressly provides that the Wildfire Fund is a fund “outside” the state treasury. Notwithstanding the short-term loan from the SMIF, as noted above, the Wildfire Fund is *privately funded* through a combination of utility payments and electric ratepayer surcharges. As such, the Wildfire Fund is not an “public agency” subject to Department of General Services procurement processes or to the Public Contracts Code. Importantly, given the interim status of the Governing Board and CEA relative to the Wildfire Fund, all agreements were negotiated with initial contract durations of just one year, with authority to terminate without cause on just 30 days’ notice. Accordingly, if the Council or the Administrator subsequently decide to undertake a new procurement process for these services, they will be free to do so.

Selected Vendors. The process described above resulted in the selection of several vendors to provide banking, asset management investment advisory services.

With regard to banking services, the 2019 Wildfire Legislation requires that those service be provided by a nationally chartered bank. The selected vendor, U.S. Bank National Association (USB), is one of the leading national banks dedicated to offering governmental custodial services. USB was extraordinarily responsive to CEA’s requests for information, provided competitive pricing similar to pricing CEA has negotiated over its history, and devoted extensive resources to negotiating an agreement for custodial services on terms acceptable to CEA. CEA staff is highly confident that USB will meet and exceed all services required by the Wildfire Fund.



With respect to consulting services, Raymond James & Associates, Inc. (Raymond James) is the long-standing financial and investment advisor to CEA, and to a number of similar catastrophe insurance funds throughout the United States. CEA also has similar and unqualified confidence in the expertise of Raymond James to provide investment advisory services to the Wildfire Fund and to ensure that investments are prudently managed consistent with the statutory guidance set forth in the 2019 Wildfire Legislation.

Finally, the four asset managers that CEA is recommending to the Governing Board to provide initial asset management and investment services to the Wildfire Fund (Eaton Vance Management, PFM Asset Management, RBC Global Asset Management and Smith Graham & Co) are currently under contract with CEA to provide services for the Earthquake Authority Fund. CEA procured those services through a competitive process that assessed both service quality and competitiveness of pricing. The pricing, in particular, that CEA has negotiated with its stable of asset managers is clearly “best in class” (i.e., lowest available), and these asset management firms are matching that low pricing for the Wildfire Fund. In short, although it is brand new, the Wildfire Fund is a beneficiary of negotiated relationships that CEA has forged over many years. With regard to the ongoing process to contract with additional asset managers, the Wildfire Fund also benefits from CEA’s well-established ability to conduct efficient, transparent and fair procurements to obtain service from highly qualified vendors on appropriate and reasonable commercial terms.

Agreements and Wildfire Fund Investment Policies

The following agreements have been negotiated and are either executed or ready for execution by the parties upon authorization of the Governing Board:

A. Agreements

1. Banking Arrangements with U.S. Bank. Arrangements have been negotiated with U.S. Bank for both a custodial trust account and a demand deposit account (i.e., an account for routine banking services). The core agreement is the *Governmental Custody Agreement*, by and between U.S. Bank National Association, a national banking association organized under the laws of the United States (USB), and CEA, in its capacity as Interim Administrator of the Wildfire Fund. In order for USB to open and activate the accounts for the Wildfire Fund in adequate time to receive funding of the \$2 billion SMIF loan, this agreement was signed by CEA on July 17, 2019, subject to approval, adoption and ratification of the Governing Board.



2. Investment Advisory Agreement with Raymond James. CEA has negotiated its standard form of agreement with Raymond James – Agreement to Provide Investment Consultant and Risk Transfer Advisory Services (Advisory Agreement). The Advisory Agreement has fundamentally the same terms as the Raymond James agreement with CEA for its work for CEA and the Earthquake Authority Fund. The fact that California is currently in the early period of the “wildfire season” dictates that the Wildfire Fund have immediate access to seasoned catastrophe risk transfer advice. For all practical purposes, the Wildfire Fund is currently exposed to financial risk from a utility-caused wildfire. Those risk must be managed and mitigated through the development and implementation of risk transfer strategies.
3. Asset Management Agreements: Agreements with the following four investment management firms were negotiated to provide for investment of assets in the Wildfire Fund, in a manner consistent with the investment policies and guidelines of the Wildfire Fund described in Section B below:
 - a. Eaton Vance Management
 - b. PFM Asset Management, LLC
 - c. RBC, Global Asset Management
 - d. Smith Graham & Co, Investment Advisors, L.P.

The forms of these agreements are substantially the same as the agreements these firms entered into with CEA for asset management for the Earthquake Authority Fund, with the same highly favorable pricing. The agreements have an initial term of one-year, and are all subject to termination on 30 days’ notice.

B. Investment Policies of the Wildfire Fund

The 2019 Wildfire Legislation authorizes the Administrator, and thus CEA as Interim Administrator, to invest assets in the Wildfire Funds in investments qualified under Government Code section 16430 and/or vehicles that are within the guidelines and policies approved by the Council (or the Governing Board exercising the powers of the Council). CEA has generated written Investment Policies for the Wildfire Fund (one for the Primary Account and one for the Claim-Paying Account) modeled on the Investment Policies that govern investments of the Earthquake Authority Fund. The need for separate Policies for the Primary Account and the Claim-Paying



Account is based on differences in the liquidity needs of the two accounts, and thus the applicable investment durations.

While the Investment Policies are fundamentally the same as the policies governing the investment of CEA's Earthquake Fund, one small but important addition to the Investment Policies for the Wildfire Fund is authorization to utilize daily money market sweeps that will ensure that any uninvested funds in the Wildfire Fund can be moved into interest bearing money market funds that are invested solely in US Treasuries. The addition of this important and beneficial authorization is enabled by flexibility and discretion that the Legislature granted to the Governing Board/Council in the 2019 Wildfire Legislation. This authorization to utilize daily sweeps will prevent uninvested funds from sitting, even overnight, in non-interest earning cash accounts.

In addition to being developed and tested by CEA, the proposed Wildfire Fund Investment Policies have also been informally reviewed and evaluated by Raymond James, the proposed Investment Advisory firm for the Wildfire Fund. Raymond James has concluded that the investment policies are consistent with the purpose and prudence dictated by Government Code § 16430. A copy of the proposed Wildfire Fund Investment Policies is attached as Attachment A.

Authorization to Perform Duties of the Wildfire Fund Administrator.

The 2019 Wildfire Legislation enacts several new code sections that, collectively, create the statutory role of the Administrator of the Wildfire Fund, designates CEA as the Interim Administrator, authorizes the Governing Board to exercise the powers and duties of the Catastrophe Response Council, and instructs CEA to "carry out the duties" of the Administrator "subject to the oversight" of the Governing Board. In particular, Public Utilities Code § 3281 enumerates several duties that CEA, as Interim Administrator, is empowered to undertake. Subdivision (h) of Section 3281 states a broad authorization for CEA to "undertake such other activities as are related to the operations, management, and administration of the [Wildfire Fund], as approved by the council."

It is clear that as CEA undertakes the expedited and complicated process of setting up the Wildfire Fund and establishing the systems, controls, policies, procedures, staffing and vendor relationships that are required for the prudent and efficient management of the Wildfire Fund, CEA will be required to exercise some or all of the ministerial administrative powers set forth in Section 3281. For example, Section 3281 provides that the



Administrator may, among other things, hire staff, advisors and experts, enter into contracts related to the administration of the fund, and pay the costs and expenses of administering the Wildfire Fund from the Fund's assets. Given that this section specifically provides that the powers must be exercised with the oversight and approval of the Governing Board, CEA recommends and requests that the Governing Board discuss and adopt a narrowly tailored, and relatively short-duration Resolution that grants the required approval and authorizes CEA to exercise and carry out such of the duties specified in Public Utilities Code 3281 as CEA determines necessary to the start-up and initial capitalization of the Wildfire Fund. This short-duration Resolution will prevent any delays or avoidable impediments to the start-up of the Wildfire Fund. The Resolution will provide that it may be rescinded at any time by the Governing Board or the Council, and will only operate during the initial phase of the Wildfire Fund. As will be discussed under Agenda Item No. 5 of this meeting (Development of the required Plan of Operations for the Wildfire Fund), the long term governance and oversight rules for the Administrator will be memorialized in the Plan of Operations to be presented to the Governing Board or Council, after which there should be no need for this type of "omnibus" resolution.

Authorization to Develop and Implement Cost Allocation Methodology.

The 2019 Wildfire Legislation also requires that all costs and expenses related to the administration and operation of the Wildfire Fund be paid from the assets of the Wildfire Fund. (Pub. Utilities Code § 3294; Ins. Code § 10089.6(d)(11).) Because CEA is now obligated to administer two separate and segregated funds – the Earthquake Authority Fund and the Wildfire Fund – and is using its operating assets and employees for the benefit of both funds, CEA is required to develop and implement a cost allocation methodology to ensure that each of these two funds bear their own expenses. CEA is developing a methodology and systems to accomplish a fair and fully auditable allocation of expenses between the two funds, and requests that the Governing Board adopt a



resolution that authorizes the immediate implementation of the final cost allocation methodology that is developed.

Recommendations:

CEA, in its capacity as Interim Administrator of the Wildfire Fund, recommends that the Governing Board adopt one or more resolutions to accomplish the following:²

- a) Approving, adopting and/or ratifying agreements by CEA, as Interim Administrator of and on behalf of the Wildfire Fund, for Custodial Banking and Demand Deposit Accounts, Asset-Management Services, and Investment Consulting;
- b) Authorizing CEA to undertake expedited procurement and engagement of additional Asset Managers in anticipation of additional capitalization;
- c) Approving and adopting Investment Policies for the Wildfire Fund; and
- d) Authorizing CEA staff to develop, document and implement a cost allocation methodology to allocate all CEA administration expenses arising from or related to the Wildfire Fund for payment by the Wildfire Fund consistent with Pub. Utilities Code § 3294 and Ins. Code § 10089.6(d)(11).

² The Public Notice and Agenda for this Governing Board Meeting included one sub-item (Agenda Item 3.d) that CEA has determined is not required or necessary for CEA to complete the start-up and initial capitalization of the Wildfire Fund, so that item is not included in CEA's recommended resolutions.



California Wildfire Fund – Primary Fund

Investment Policy (DRAFT 7/25)

Adopted: August [7], 2019

DEFINITIONS

“Applicable Laws and Regulations” or “Legal Restrictions” means Public Utilities Code section 3281, subdivision (C) and section 3284 subdivision (e) for un-invested monies, California Government Code section 16430, Wildfire Fund section 3284 (e), as well as any amendments or successor provisions to those sections.

“Business Day” or “Business Days” means a day or days other than Saturdays, Sundays, or state holidays.

“California Wildfire Fund” means the Wildfire Fund created pursuant to Section 3284 for California Wildfire Fund

“Covered Wildfire” means any wildfire ignited on or after effective January 1, 2019 caused by an electrical corporation as determined by the governmental agency responsible for determining causation

“Daily” refers to Business Days.

“Fund” means a fund within the Wildfire Fund such as, but not by way of limitation, the Wildfire Fund’s Primary Fund and Claims-Paying Fund.

“Investment Consultant” means a firm contracted by the Wildfire Fund to provide as needed investment analysis for the Fund and to provide services related to selection and oversight of the Fund’s Investment Managers.

“Investment Manager” means a firm contracted by the Wildfire Fund to invest monies on its behalf, in accordance with all Applicable Laws and Regulations and the Wildfire Fund’s Investment Policies.

“Investment” refers to a Security purchased for, and owned by, the Wildfire Fund.

“Modified Duration” is the average length of time to receive the present value of bond cash flows.

A “Security” is a financial instrument before it is purchased for, or owned by, the California Wildfire Fund.

“Wildfire Fund Portfolio” or “Portfolio” means the entirety of all the individual Funds of the Wildfire Fund collectively, i.e., the Primary Fund and the Claims-Paying Fund or any other created by the Wildfire Fund.

BACKGROUND

The California Wildfire Fund (“CWF” or “Wildfire Fund”) is a statutory fund segregated from and independent of the California Treasury, and was created under California Public Utilities Code section 3284 in July 2019. The California Earthquake Authority, a governmental instrumentality for the State of California in its statutory capacity is the acting Interim Administrator for the Wildfire Fund. The Wildfire Fund will hold dedicated accounts, separate from the California Earthquake Authority’s accounts. This investment policy pertains to the Wildfire Fund’s Primary Fund.

PHILOSOPHY

The CWF is a legislatively created Fund to provide third party damage claims resulting from Covered Wildfire Losses. The interim administrator has set forth the following prioritized goals:

- 1) Safety and preservation of principal;
- 2) Liquidity, so that claims can be paid in a timely manner; and
- 3) Competitive returns (yield).

As a public instrumentality, created by act of the California state government, the Wildfire Fund discloses much of its operations and investment activity. The integrity of the Wildfire Fund’s investment activities should be above that of private sector organizations conducting comparable business operations. Therefore, the Wildfire Fund has the social and ethical obligation to require that Investments made on its behalf and held in its accounts be in corporations and entities that meet a high standard of conduct in their operations. Still, the investment of the Wildfire Fund’s assets should appropriately reflect sound judgment that each Investment will produce an attractive rate of return, within the bounds of all Applicable Laws and Regulations and these Investment Policies.

PRINCIPLES

After the primary goals of safety and preservation of principal and attention to appropriate liquidity requirements are met, rate of return must be considered. Safe and prudent investment management will be the primary and underlying criterion for the selection of Securities and retention and disposition of Investments.

Non-economic factors will supplement profit factors in making investment decisions. Non-economic factors are defined as those considerations not directly related to providing for the

safety of principal, maintaining adequate liquidity, and maximizing income, but which seek to ensure that in making or holding its Investments, the Wildfire Fund does not, either through action or inaction, promote, condone, or facilitate social or environmental injury.

Social or environmental injury may be said to exist when the activities of a corporation serve to undermine basic human rights and dignities, or when the Wildfire Fund perceives that the practices of a corporation result in undesirable side effects for others and that those side effects are substantial in nature. Side effects that may be deemed undesirable and substantial include, but are not limited to, the following:

- A. Subject to current federal, state, and local law, any practice that is known to endanger, directly or indirectly, human health or the environment:
- B. Practices that result in the suppression of human rights, including:
 - 1) The sale of weapons and technology to governments known to engage in the systematic suppression of human rights; and
 - 2) The sale of goods to, or the purchase of goods from, countries known to employ forced labor.
- C. Practices that endanger human health, including:
 - 1) The sale and distribution of known contaminated products;
 - 2) The sale and distribution of dangerous drugs; and
 - 3) The sale of goods to, or the purchase of goods from, companies known to disregard worker safety.

Investments shall not be selected or rejected based solely on non-economic factors. In general, non-economic factors, to the extent known after reasonable investigation, should be considered after all relevant financial criteria and Legal Restrictions have been satisfied.

The Wildfire Fund Portfolio will be managed to ensure the safety of the Portfolio and the Funds by investing in high-quality fixed-income Securities with limited durations.

PRUDENT INVESTOR STANDARD

In addition to complying with the Investment Policies and all Applicable Laws and Regulations, all Wildfire Fund Investments and evaluation of such Investments shall be made with regard to the “prudent investor” standard of care, that is, with the care, skill, prudence, and diligence under the circumstances then prevailing, that persons of prudence, discretion, and intelligence exercise in the professional management of their business affairs, not for speculation, but for investment, considering the probable safety of their capital, including liquidity of the Investment, as well as the probable income to be derived.

ETHICS, AVOIDANCE OF CONFLICT OF INTERESTS, AND COMPLIANCE WITH INVESTMENT ADVISERS ACT OF 1940

No officer or employee of the Wildfire Fund, or of any firm contracted with the Wildfire Fund involved in the investment of Wildfire Fund funds, shall engage in any personal or business activity that may conflict with proper execution of the Wildfire Fund's investment program or that may impair his or her ability to make impartial investment decisions for the Wildfire Fund. Any personal investments in entities that do business with the Wildfire Fund, either by contract or where the Wildfire Fund has Investments with that entity, shall be disclosed as required in regulations of the Fair Political Practice Commission (using its Form 700, which shall be filed according to law) and the Wildfire Fund's Conflict of Interest Code.

The Wildfire Fund's Investment Consultant and Investment Managers shall ensure that they are registered with, and comply with the rules, advice, rulings, and regulations of, the Securities and Exchange Commission as an investment adviser under the Investment Advisers Act of 1940 that is licensed to choose investments for clients. The CWF's Investment Consultant and Investment Managers shall procure and fully and currently maintain the permits and licenses, if any, necessary to advise the Wildfire Fund on investments and to make investments on the Wildfire Fund's behalf.

PERMISSIBLE INVESTMENTS

In accordance with Division 1 of the Public Utilities Code Section 3281 subdivision (c), and Section 3284 subdivision (2), paragraph (e), for un-invested monies.

Investments made by the investment managers on behalf of the Wildfire Fund shall be made in compliance with California Government Code section 16430, as section 16430 is in effect at the time the Investment is made. California Government Code section 16430 may be amended from time to time, and the Wildfire Fund's Investment Managers shall be responsible for being aware and informed of any amendments to section 16430 and to all Applicable Laws and Regulations. As of January 1, 2017, California Government Code section 16430 is provided in its entirety in Exhibit A.

The Wildfire Fund's Primary Fund will be invested only in Treasury securities and any un-invested moneys in the Fund may be held un-invested pending cash investment, distribution, resolution of a dispute, or for other operational reasons and may be deposited in the associated sweep account prior to the Fed wire cutoff time. Any remaining un-invested monies after the Fed wire cutoff time will be invested in the Wildfire Fund's designated account by the custodian, or in such other account as designated by the Fund in future.

COMPLIANCE

The Investment Policies, and all Applicable Laws and Regulations, shall be observed by the Wildfire Fund's Independent Investment Consultant and acted on by all Investment

Managers in the course of their administering Wildfire Funds. The Investment Policies are subject to continual monitoring and review by the Interim Administrator for the CWF.

A trade executed for the Wildfire Fund's Portfolio shall be deemed to be in compliance with the Investment Policies if, as of the trade date, the trade met both (A) the requirements of the Investment Policies and (B) all Applicable Laws and Regulations. Notwithstanding, however, the deemed trade-day compliance of any individual trade, if at the close of any day any fund maturity or duration exceeds the limit stated in the Investment Policies, the Investment Manager must, within one business day, consult with the Interim Administrator for the CWF in order that the CWF in its sole discretion, may provide a directive to correct maturity or duration limit; if the interim administrator (or his or her designee) provides no such directive, the Investment Manager must bring the exceeded maturity or duration limit back into compliance with the Investment Policies as soon as reasonably possible.

The Wildfire Fund will perform Daily quality-assurance checks of the Portfolio and of each Fund (or portion of a Fund in the case where an Investment Manager is managing a defined portion of a Fund) to ensure compliance with the Investment Policies and with all Applicable Laws and Regulations. If the Wildfire Fund becomes aware of any noncompliance with the Investment Policies, the Wildfire Fund will contact the Investment Manager immediately to discuss the situation so that the Wildfire Fund may determine the appropriate actions to be taken by the Investment Manager and Wildfire Fund to bring the Fund into compliance; if an Investment Manager or the Investment Consultant becomes aware of any noncompliance with any Investment Policies, it shall contact the Wildfire Fund immediately to discuss the situation so that the Wildfire Fund may determine the appropriate actions to be taken by the Investment Manager and Wildfire Fund to bring the Fund into compliance.

The performance by Wildfire Fund of a Daily quality-assurance check does not relieve any Wildfire Fund Investment Manager of its respective independent duties to ensure that all Investments made and held for the Wildfire Fund comply with the Investment Policies and all Applicable Laws and Regulations at all times. Wildfire Fund's failure to discover, or failure to report the discovery to the Wildfire Fund's Investment Consultant or Investment Managers (or any of them), any noncompliance, does not constitute (A) Wildfire Fund's acceptance or ratification of that noncompliance or (B) any waiver by Wildfire Fund of its right to require compliance by Investment Managers with the Investment Policies and all Applicable Laws and Regulations.

THE WILDFIRE FUND PORTFOLIO

For the purposes of the Investment Policies, the "Wildfire Fund Portfolio" consists of the following Funds:

- Claims-Paying Fund
 - This fund consists of a number of custody accounts, which are funded by contributions from Utility Companies
- Primary Fund

- This fund consists of a number of custody accounts, which are funded by contributions from ratepayers

MATURITY & DURATION

The Investments made in the Primary Fund Portfolio shall have a maximum Modified Duration of no greater than 3.0 years. To minimize the risk of portfolio market value decline due to a change in market conditions, each Investment Manager managing Investments with maturity dates greater than 365 days shall spread the maturities of those Investments to avoid having 10% or more of the market value of the Investment Manager's Fund of Investments maturing on a single date.

The "maximum maturity" requirement listed in the table in the Permitted Investments section is defined as the number of days from trade date to maturity date, including the trade date but excluding the maturity date.

CUSTODY

All Wildfire Fund Investments shall be secured or held at all times by a custody bank.

PRIMARY DEALER

All treasury trades must be executed with eligible brokers registered as Primary Dealers. The list of eligible brokers are listed on Federal Reserve Bank of New York Website.

UNINVESTED CASH

Each Investment Manager shall seek to minimize the amount of cash remaining at the end of a Business Day that is not invested in a manner consistent with the Investment Policies.

Any un-invested moneys in the Fund may be held un-invested pending cash investment, distribution, resolution of a dispute, or for other operational reasons and may be deposited in the associated sweep account prior to the Fed wire cut off time. Any remaining un-invested monies after the Fed wire cutoff time will be invested in the CWF's designated account by the custodian, or in such other account as designated by the Fund in the future.

NEGATIVE YIELDS

The Investment Managers are encouraged to hold cash until an allowable Security with a positive yield becomes available. The Investment Managers must notify the Wildfire Fund when yields are negative.

MINIMUM TRADE RETURN

Subject to guidance from the Wildfire Fund, Investment Managers should not execute a trade if the expected return is less than the cost of executing the trade. If any Investment Manager believes that circumstances warrant making such a trade, it must contact the Interim Administrator for the CWF.

INVESTMENT GOALS

Consistent with the Wildfire Fund's published Investment Philosophy, and in order of priority, the Wildfire Fund's investment goals are:

- 1) **Portfolio Safety**
Under this Investment Policy, the Portfolio shall contain a sufficient number with multiple maturity dates of treasury securities so that a reasonable portion of the Portfolio can be readily converted to cash at a price closely approximating amortized cost.
- 2) **Liquidity**
The Portfolio shall be managed to ensure that the Wildfire Fund's usual cash needs to pay eligible claims can be met; if unforeseen cash needs arise, the Wildfire Fund's Administrator or another individual designated by the Wildfire Fund will work with individual Managers to plan to meet liquidity requirements.
- 3) **Rate of Return**
Investments shall be made in such a way as to realize the maximum return consistent with the principles of prudence expressed in the Wildfire Fund's Investment Philosophy and these Guidelines.

Investments in the Portfolio may be sold to:

- Provide liquidity, and
- Purchase an Investment that better meets the current needs of the Portfolio, after notification to and consultation with the CWF.

REPORTING

Each Investment Manager shall report to the Wildfire Fund, via email by 9:00 a.m. Pacific Time each Business Day, the previous day's holdings in the Fund, or a portion of the Fund, under its management.

For each Investment it makes, the Investment Manager shall transmit to the Wildfire Fund, via email sent by 9:00 a.m. Pacific Time on the trade date, a copy of the trade ticket generated for that Investment transaction. Wildfire Fund will use this trade ticket in the Daily quality assurance process and to update Wildfire Fund's investment accounting system and other

trade-related information as requested by the Wildfire Fund's Administrator, or another individual designated by the Wildfire Fund.

Each Investment Manager shall compile a monthly report of the Fund, or a portion of the Fund, managed by the Investment Manager and deliver the report electronically to the Wildfire Fund on or by the fifth Business Day of the following month. The report shall contain information as requested by the Wildfire Fund's interim administrator (or his or her designee).

PRIMARY FUND PERMITTED INVESTMENTS

Treasury Securities with maximum maturity of five (5) years.

Any un-invested moneys in the Fund may be held un-invested pending cash investment, distribution, resolution of a dispute, or for other operational reasons and may be deposited in the associated sweep account prior to the Fed wire cut off time. Any remaining un-invested monies after the Fed wire cutoff time will be invested in the California Wildfire Fund's designated account by the custodian, or in such other account as designated by the Fund in the future.

In the event, however, that any requirement on the following page may appear to be inconsistent with any of the Applicable Laws and Regulations, the Applicable Laws and Regulations shall be followed, and the Investment Manager shall immediately notify the Wildfire Fund of any such inconsistency. If there is any question regarding any permissible Investment described in the table, the Investment Manager shall contact the Wildfire Fund's interim administrator (or his or her designee) for clarification.

Wildfire Fund staff may issue interpretive memorandum for the intended purpose to further enhance understanding of the Investment Policies or provide guidance for matters not covered by the Investment Policies.

Primary Fund

Investment	U.S. Treasury	Federal Agency	Banker's Acceptance (BA)	Certificate of Deposit (CDs)	Commercial Paper (CP)	Corporate Bond / Note
Maximum Maturity	5 years	Not Permitted	Not Permitted	Not Permitted	Not Permitted	Not Permitted
Maximum Par Value, total Portfolio	None	Not Applicable	Not Applicable	Not Applicable	Not Applicable	Not Applicable
Maximum Par Value Per Name	None	Not Applicable	Not Applicable	Not Applicable	Not Applicable	Not Applicable
Maximum Par Value Per Maturity	None	Not Applicable	Not Applicable	Not Applicable	Not Applicable	Not Applicable
Credit	Full faith and credit of the Federal Government	Not Applicable	Not Applicable	Not Applicable	Not Applicable	Not Applicable
Other Requirements	Exclude: <ul style="list-style-type: none"> • Treasury Inflation Protect Security (TIPS) • Separate Trading of Registered Interest and Principal of Securities (STRIPS) 	Not Applicable	Not Applicable	Not Applicable	Not Applicable	Not Applicable

California Government Code, Statute 16430

“Eligible securities for the investment of surplus moneys shall be any of the following:

“(a) Bonds or interest-bearing notes or obligations of the United States, or those for which the faith and credit of the United States are pledged for the payment of principal and interest.

“(b) Bonds or interest-bearing notes on obligations that are guaranteed as to principal and interest by a federal agency of the United States.

“(c) Bonds, notes, and warrants of this state, or those for which the faith and credit of this state are pledged for the payment of principal and interest.

“(d) Bonds or warrants, including, but not limited to, revenue warrants, of any county, city, metropolitan water district, California water district, California water storage district, irrigation district in the state, municipal utility district, or school district of this state.

“(e) Any of the following:

“(1) Bonds, consolidated bonds, collateral trust debentures, consolidated debentures, or other obligations issued by federal land banks or federal intermediate credit banks established under the Federal Farm Loan Act, as amended (12 U.S.C. Sec. 2001 et seq.).

“(2) Debentures and consolidated debentures issued by the Central Bank for Cooperatives and banks for cooperatives established under the Farm Credit Act of 1933, as amended (12 U.S.C. Sec. 2001 et seq.).

“(3) Bonds or debentures of the Federal Home Loan Bank Board established under the Federal Home Loan Bank Act (12 U.S.C. Sec. 1421 et seq.).

“(4) Stocks, bonds, debentures, and other obligations of the Federal National Mortgage Association established under the National Housing Act, as amended (12 U.S.C. Sec. 1701 et seq.).

“(5) Bonds of any federal home loan bank established under that act.

“(6) Obligations of the Federal Home Loan Mortgage Corporation.

“(7) Bonds, notes, and other obligations issued by the Tennessee Valley Authority under the Tennessee Valley Authority Act, as amended (16 U.S.C. Sec. 831 et seq.).

“(8) Other obligations guaranteed by the Commodity Credit Corporation for the export of California agricultural products under the Commodity Credit Corporation Charter Act, as amended (15 U.S.C. Sec. 714 et seq.).

“(f)(1) Commercial paper of “prime” quality as defined by a nationally recognized organization that rates these securities, if the commercial paper is issued by a federally or state-chartered bank or a state-licensed branch of a foreign bank, corporation, trust, or limited liability company that is approved by the Pooled Money Investment Board as meeting the conditions specified in either subparagraph (A) or subparagraph (B):

“(A) Both of the following conditions:

“(i) Organized and operating within the United States.

“(ii) Having total assets in excess of five hundred million dollars (\$500,000,000).

“(B) Both of the following conditions:

“(i) Organized within the United States as a federally or state-chartered bank or a state-licensed branch of a foreign bank, special purpose corporation, trust, or limited liability company.

“(ii) Having programwide credit enhancements including, but not limited to, overcollateralization, letters of credit, or surety bond.

“(2) A purchase of eligible commercial paper may not do any of the following:

“(A) Exceed 270 days maturity.

“(B) Represent more than 10 percent of the outstanding paper of an issuing federally or state-chartered bank or a state-licensed branch of a foreign bank, corporation, trust, or limited liability company.

“(C) Exceed 30 percent of the resources of an investment program.

“(3) At the request of the Pooled Money Investment Board, an investment made pursuant to this subdivision shall be secured by the issuer by depositing with the Treasurer securities authorized by Section 53651 of a market value at least 10 percent in excess of the amount of the state's investment.

“(g) Bills of exchange or time drafts drawn on and accepted by a commercial bank, otherwise known as bankers acceptances, that are eligible for purchase by the Federal Reserve System.

“(h) Negotiable certificates of deposits issued by a federally or state-chartered bank or savings and loan association, a state-licensed branch of a foreign bank, or a federally or state-chartered credit union. For the purposes of this section, negotiable certificates of deposits are not subject to Chapter 4 (commencing with Section 16500) and Chapter 4.5 (commencing with Section 16600).

“(i) The portion of bank loans and obligations guaranteed by the United States Small Business Administration or the United States Farmers Home Administration.

“(j) Bank loans and obligations guaranteed by the Export-Import Bank of the United States.

“(k) Student loan notes insured under the Guaranteed Student Loan Program established pursuant to the Higher Education Act of 1965, as amended (20 U.S.C. Sec. 1001 et seq.) and eligible for resale to the Student Loan Marketing Association established pursuant to Section 133 of the Education Amendments of 1972, as amended (20 U.S.C. Sec. 1087-2).

“(l) Obligations issued, assumed, or guaranteed by the International Bank for Reconstruction and Development, the Inter-American Development Bank, the Asian Development Bank, the African Development Bank, the International Finance Corporation, or the Government Development Bank of Puerto Rico.

“(m) Bonds, debentures, and notes issued by corporations organized and operating within the United States. Securities eligible for investment under this subdivision shall be within the top three ratings of a nationally recognized rating service.

“(n) Negotiable Order of Withdrawal Accounts (NOW Accounts), invested in accordance with Chapter 4 (commencing with Section 16500).”



California Wildfire Fund – Claims-Paying Fund

Investment Policy (DRAFT 7/25)

Adopted: August [7], 2019

DEFINITIONS

“Applicable Laws and Regulations” or “Legal Restrictions” means Public Utilities Code section 3281, subdivision (C) and section 3284 subdivision (e) for un-invested monies, California Government Code section 16430, Wildfire Fund section 3284 (e), as well as any amendments or successor provisions to those sections.

“Business Day” or “Business Days” means a day or days other than Saturdays, Sundays, or state holidays.

“California Wildfire Fund” means the Wildfire Fund created pursuant to Section 3284 for California Wildfire Fund

“Covered Wildfire” means any wildfire ignited on or after effective January 1, 2019 caused by an electrical corporation as determined by the governmental agency responsible for determining causation

“Daily” refers to Business Days.

“Fund” means a fund within the Wildfire Fund such as, but not by way of limitation, the Wildfire Fund’s Primary Fund and Claims-Paying Fund.

“Investment Consultant” means a firm contracted by the Wildfire Fund to provide as needed investment analysis for the Fund and to provide services related to selection and oversight of the Fund’s Investment Managers.

“Investment Manager” means a firm contracted by the Wildfire Fund to invest monies on its behalf, in accordance with all Applicable Laws and Regulations and the Wildfire Fund’s Investment Policies.

“Investment” refers to a Security purchased for, and owned by, the Wildfire Fund.

“Modified Duration” is the average length of time to receive the present value of bond cash flows.

A “Security” is a financial instrument before it is purchased for, or owned by, the California Wildfire Fund.

“Wildfire Fund Portfolio” or “Portfolio” means the entirety of all the individual Funds of the Wildfire Fund collectively, i.e., the Primary Fund and the Claims-Paying Fund or any other created by the Wildfire Fund.

BACKGROUND

The California Wildfire Fund (“CWF” or “Wildfire Fund”) is a statutory fund segregated from and independent of the California Treasury, and was created under California Public Utilities Code section 3284 in July 2019. The California Earthquake Authority, a governmental instrumentality for the State of California in its statutory capacity is the acting Interim Administrator for the Wildfire Fund. The Wildfire Fund will hold dedicated accounts, separate from the California Earthquake Authority’s accounts. This Investment Policy pertains to the Wildfire Fund’s Claims-Paying Fund.

PHILOSOPHY

The CWF is a legislatively created Fund to provide third party damage claims resulting from Covered Wildfire Losses. The interim administrator has set forth the following prioritized goals:

- 1) Safety and preservation of principal;
- 2) Liquidity, so that claims can be paid in a timely manner; and
- 3) Competitive returns (yield).

As a public instrumentality, created by act of the California state government, the Wildfire Fund discloses much of its operations and investment activity. The integrity of the Wildfire Fund’s investment activities should be above that of private sector organizations conducting comparable business operations. Therefore, the Wildfire Fund has the social and ethical obligation to require that Investments made on its behalf and held in its accounts be in corporations and entities that meet a high standard of conduct in their operations. Still, the investment of the Wildfire Fund’s assets should appropriately reflect sound judgment that each Investment will produce an attractive rate of return, within the bounds of all Applicable Laws and Regulations and these Investment Policies.

PRINCIPLES

After the primary goals of safety and preservation of principal and attention to appropriate liquidity requirements are met, rate of return must be considered. Safe and prudent investment management will be the primary and underlying criterion for the selection of Securities and retention and disposition of Investments.

Non-economic factors will supplement profit factors in making investment decisions. Non-economic factors are defined as those considerations not directly related to providing for the

safety of principal, maintaining adequate liquidity, and maximizing income, but which seek to ensure that in making or holding its Investments, the Wildfire Fund does not, either through action or inaction, promote, condone, or facilitate social or environmental injury.

Social or environmental injury may be said to exist when the activities of a corporation serve to undermine basic human rights and dignities, or when the Wildfire Fund perceives that the practices of a corporation result in undesirable side effects for others and that those side effects are substantial in nature. Side effects that may be deemed undesirable and substantial include, but are not limited to, the following:

- A. Subject to current federal, state, and local law, any practice that is known to endanger, directly or indirectly, human health or the environment:
- B. Practices that result in the suppression of human rights, including:
 - 1) The sale of weapons and technology to governments known to engage in the systematic suppression of human rights; and
 - 2) The sale of goods to, or the purchase of goods from, countries known to employ forced labor.
- C. Practices that endanger human health, including:
 - 1) The sale and distribution of known contaminated products;
 - 2) The sale and distribution of dangerous drugs; and
 - 3) The sale of goods to, or the purchase of goods from, companies known to disregard worker safety.

Investments shall not be selected or rejected based solely on non-economic factors. In general, non-economic factors, to the extent known after reasonable investigation, should be considered after all relevant financial criteria and Legal Restrictions have been satisfied.

The Wildfire Fund Portfolio will be managed to ensure the safety of the Portfolio and the Funds by investing in high-quality fixed-income Securities with limited durations.

PRUDENT INVESTOR STANDARD

In addition to complying with the Investment Policies and all Applicable Laws and Regulations, all Wildfire Fund Investments and evaluation of such Investments shall be made with regard to the “prudent investor” standard of care, that is, with the care, skill, prudence, and diligence under the circumstances then prevailing, that persons of prudence, discretion, and intelligence exercise in the professional management of their business affairs, not for speculation, but for investment, considering the probable safety of their capital, including liquidity of the Investment, as well as the probable income to be derived.

ETHICS, AVOIDANCE OF CONFLICT OF INTERESTS, AND COMPLIANCE WITH INVESTMENT ADVISERS ACT OF 1940

No officer or employee of the Wildfire Fund, or of any firm contracted with the Wildfire Fund involved in the investment of Wildfire Fund funds, shall engage in any personal or business activity that may conflict with proper execution of the Wildfire Fund's investment program or that may impair his or her ability to make impartial investment decisions for the Wildfire Fund. Any personal investments in entities that do business with the Wildfire Fund, either by contract or where the Wildfire Fund has Investments with that entity, shall be disclosed as required in regulations of the Fair Political Practice Commission (using its Form 700, which shall be filed according to law) and the Wildfire Fund's Conflict of Interest Code.

The Wildfire Fund's Investment Consultant and Investment Managers shall ensure that they are registered with, and comply with the rules, advice, rulings, and regulations of, the Securities and Exchange Commission as an investment adviser under the Investment Advisers Act of 1940 that is licensed to choose investments for clients. The CWF's Investment Consultant and Investment Managers shall procure and fully and currently maintain the permits and licenses, if any, necessary to advise the Wildfire Fund on investments and to make investments on the Wildfire Fund's behalf.

PERMISSIBLE INVESTMENTS

In accordance with Division 1 of the Public Utilities Code Section 3281 subdivision (c), and Section 3284 subdivision (2), paragraph (e), for un-invested monies.

Investments made by the investment managers on behalf of the Wildfire Fund shall be made in compliance with California Government Code section 16430, as section 16430 is in effect at the time the Investment is made. California Government Code section 16430 may be amended from time to time, and the Wildfire Fund's Investment Managers shall be responsible for being aware and informed of any amendments to section 16430 and to all Applicable Laws and Regulations. As of January 1, 2017, California Government Code section 16430 is provided in its entirety in Exhibit A.

The Wildfire Fund's Primary Fund will be invested only in Treasury securities and any un-invested moneys in the Fund may be held un-invested pending cash investment, distribution, resolution of a dispute, or for other operational reasons and may be deposited in the associated sweep account prior to the Fed wire cutoff time. Any remaining un-invested monies after the Fed wire cutoff time will be invested in the Wildfire Fund's designated account by the custodian, or in such other account as designated by the Fund in future.

COMPLIANCE

The Investment Policies, and all Applicable Laws and Regulations, shall be observed by the Wildfire Fund's Independent Investment Consultant and acted on by all Investment

Managers in the course of their administering Wildfire Funds. The Investment Policies are subject to continual monitoring and review by the Interim Administrator for the CWF.

A trade executed for the Wildfire Fund's Portfolio shall be deemed to be in compliance with the Investment Policies if, as of the trade date, the trade met both (A) the requirements of the Investment Policies and (B) all Applicable Laws and Regulations. Notwithstanding, however, the deemed trade-day compliance of any individual trade, if at the close of any day any fund maturity or duration exceeds the limit stated in the Investment Policies, the Investment Manager must, within one business day, consult with the Interim Administrator for the CWF in order that the CWF in its sole discretion, may provide a directive to correct maturity or duration limit; if the interim administrator (or his or her designee) provides no such directive, the Investment Manager must bring the exceeded maturity or duration limit back into compliance with the Investment Policies as soon as reasonably possible.

The Wildfire Fund will perform Daily quality-assurance checks of the Portfolio and of each Fund (or portion of a Fund in the case where an Investment Manager is managing a defined portion of a Fund) to ensure compliance with the Investment Policies and with all Applicable Laws and Regulations. If the Wildfire Fund becomes aware of any noncompliance with the Investment Policies, the Wildfire Fund will contact the Investment Manager immediately to discuss the situation so that the Wildfire Fund may determine the appropriate actions to be taken by the Investment Manager and Wildfire Fund to bring the Fund into compliance; if an Investment Manager or the Investment Consultant becomes aware of any noncompliance with any Investment Policies, it shall contact the Wildfire Fund immediately to discuss the situation so that the Wildfire Fund may determine the appropriate actions to be taken by the Investment Manager and Wildfire Fund to bring the Fund into compliance.

The performance by Wildfire Fund of a Daily quality-assurance check does not relieve any Wildfire Fund Investment Manager of its respective independent duties to ensure that all Investments made and held for the Wildfire Fund comply with the Investment Policies and all Applicable Laws and Regulations at all times. Wildfire Fund's failure to discover, or failure to report the discovery to the Wildfire Fund's Investment Consultant or Investment Managers (or any of them), any noncompliance, does not constitute (A) Wildfire Fund's acceptance or ratification of that noncompliance or (B) any waiver by Wildfire Fund of its right to require compliance by Investment Managers with the Investment Policies and all Applicable Laws and Regulations.

THE WILDFIRE FUND PORTFOLIO

For the purposes of the Investment Policies, the "Wildfire Fund Portfolio" consists of the following Funds:

- Claims-Paying Fund
 - This fund consists of a number of custody accounts, which are funded by contributions from Utility Companies
- Primary Fund

- This fund consists of a number of custody accounts, which are funded by contributions from ratepayers

MATURITY & DURATION

The Investments made in the Claims-Paying Fund Portfolio shall have a maximum Modified Duration of no greater than 3.0 years. To minimize the risk of portfolio market value decline due to a change in market conditions, each Investment Manager managing Investments with maturity dates greater than 365 days shall spread the maturities of those Investments to avoid having 10% or more of the market value of the Investment Manager's Fund of Investments maturing on a single date.

The "maximum maturity" requirement listed in the table in the Permitted Investments section is defined as the number of days from trade date to maturity date, including the trade date but excluding the maturity date.

CUSTODY

All Wildfire Fund Investments shall be secured or held at all times by a custody bank.

PRIMARY DEALER

All trades must be executed with eligible brokers registered as Primary Dealers. The list of eligible brokers are listed on Federal Reserve Bank of New York Website.

UNINVESTED CASH

Each Investment Manager shall seek to minimize the amount of cash remaining at the end of a Business Day that is not invested in a manner consistent with the Investment Policies.

Any un-invested moneys in the Fund may be held un-invested pending cash investment, distribution, resolution of a dispute, or for other operational reasons and may be deposited in the associated sweep account prior to the Fed wire cut off time. Any remaining un-invested monies after the Fed wire cutoff time will be invested in the CWF's designated account by the custodian, or in such other account as designated by the Fund in the future.

NEGATIVE YIELDS

The Investment Managers are encouraged to hold cash until an allowable Security with a positive yield becomes available. The Investment Managers must notify the Wildfire Fund when yields are negative.

MINIMUM TRADE RETURN

Subject to guidance from the Wildfire Fund, Investment Managers should not execute a trade if the expected return is less than the cost of executing the trade. If any Investment Manager believes that circumstances warrant making such a trade, it must contact the Interim Administrator for the CWF.

INVESTMENT GOALS

Consistent with the Wildfire Fund's published Investment Philosophy, and in order of priority, the Wildfire Fund's investment goals are:

- 1) **Portfolio Safety**
Under this Investment Policy, the Portfolio shall contain a sufficient number with multiple maturity dates of securities so that a reasonable portion of the Portfolio can be readily converted to cash at a price closely approximating amortized cost.
- 2) **Liquidity**
The Portfolio shall be managed to ensure that the Wildfire Fund's usual cash needs to pay eligible claims can be met; if unforeseen cash needs arise, the Wildfire Fund's Administrator or another individual designated by the Wildfire Fund will work with individual Managers to plan to meet liquidity requirements.
- 3) **Rate of Return**
Investments shall be made in such a way as to realize the maximum return consistent with the principles of prudence expressed in the Wildfire Fund's Investment Philosophy and these Guidelines.

Investments in the Portfolio may be sold to:

- Provide liquidity, and
- Purchase an Investment that better meets the current needs of the Portfolio, after notification to and consultation with the CWF.

REPORTING

Each Investment Manager shall report to the Wildfire Fund, via email by 9:00 a.m. Pacific Time each Business Day, the previous day's holdings in the Fund, or a portion of the Fund, under its management.

For each Investment it makes, the Investment Manager shall transmit to the Wildfire Fund, via email sent by 9:00 a.m. Pacific Time on the trade date, a copy of the trade ticket generated for that Investment transaction. Wildfire Fund will use this trade ticket in the Daily quality assurance process and to update Wildfire Fund's investment accounting system and other

trade-related information as requested by the Wildfire Fund's Administrator, or another individual designated by the Wildfire Fund.

Each Investment Manager shall compile a monthly report of the Fund, or a portion of the Fund, managed by the Investment Manager and deliver the report electronically to the Wildfire Fund on or by the fifth Business Day of the following month. The report shall contain information as requested by the Wildfire Fund's interim administrator (or his or her designee).

CLAIMS-PAYING FUND PERMITTED INVESTMENTS

As shown in the table on the following page, the permissible investment types for the Claims-Paying Fund includes Treasury securities with a maximum maturity of up to 5 years and Federal Agency securities, Commercial Paper, Certificates of Deposit, Bankers Acceptances and Corporate Bonds/Notes with maximum maturities of up to 181 days, which complies with both Applicable Laws and Regulations and the CWF's Investment Policies.

Any un-invested moneys in the Fund may be held un-invested pending cash investment, distribution, resolution of a dispute, or for other operational reasons and may be deposited in the associated sweep account prior to the Fed wire cut off time. Any remaining un-invested monies after the Fed wire cutoff time will be invested in the California Wildfire Fund's designated account by the custodian, or in such other account as designated by the Fund in the future.

In the event, however, that any requirement on the following page may appear to be inconsistent with any of the Applicable Laws and Regulations, the Applicable Laws and Regulations shall be followed, and the Investment Manager shall immediately notify the Wildfire Fund of any such inconsistency. If there is any question regarding any permissible Investment described in the table, the Investment Manager shall contact the Wildfire Fund's interim administrator (or his or her designee) for clarification.

Wildfire Fund staff may issue interpretive memorandum for the intended purpose to further enhance understanding of the Investment Policies or provide guidance for matters not covered by the Investment Policies.

Claims-Paying Fund

Investment	U.S. Treasury	Federal Agency	Banker's Acceptance (BA)	Certificate of Deposit (CDs)	Commercial Paper (CP)	Corporate Bond / Note
Maximum Maturity	5 years	181 days	181 days	181 days	180 days	180 days
Maximum Par Value, total Portfolio	None	50%	25%	25%	25%	25%
Maximum Par Value Per Name	None	25%	5%	5%	5%	5%
Credit	Full faith and credit of the Federal Government	Implied government guarantee - credit analysis of certain agencies	Long-term debt ratings of at least "A" by Standard & Poor's or "A2" by Moody's or "A" by Fitch OR short-term debt ratings of "A-1" by Standard & Poor's or "P-1" by Moody's or "F-1+" by Fitch			
Other Requirements	Exclude: <ul style="list-style-type: none"> Treasury Inflation Protect Security (TIPS) Separate Trading of Registered Interest and Principal of Securities (STRIPS) 	Exclude: Federal Home Loan Bank notes	Must be purchased directly from the issuer and are eligible for purchase by the Federal Reserve System	Must be purchased directly from the issuer	<ul style="list-style-type: none"> Organized in U.S. Total assets must be >\$500M On Pooled Money Investment Board's approved list <10% of the outstanding paper of the issuer If >15% of the fund is in CP, the dollar weighted average maturity of the fund cannot exceed 31 days 	Organized in U.S.

California Government Code, Statute 16430

“Eligible securities for the investment of surplus moneys shall be any of the following:

“(a) Bonds or interest-bearing notes or obligations of the United States, or those for which the faith and credit of the United States are pledged for the payment of principal and interest.

“(b) Bonds or interest-bearing notes on obligations that are guaranteed as to principal and interest by a federal agency of the United States.

“(c) Bonds, notes, and warrants of this state, or those for which the faith and credit of this state are pledged for the payment of principal and interest.

“(d) Bonds or warrants, including, but not limited to, revenue warrants, of any county, city, metropolitan water district, California water district, California water storage district, irrigation district in the state, municipal utility district, or school district of this state.

“(e) Any of the following:

“(1) Bonds, consolidated bonds, collateral trust debentures, consolidated debentures, or other obligations issued by federal land banks or federal intermediate credit banks established under the Federal Farm Loan Act, as amended (12 U.S.C. Sec. 2001 et seq.).

“(2) Debentures and consolidated debentures issued by the Central Bank for Cooperatives and banks for cooperatives established under the Farm Credit Act of 1933, as amended (12 U.S.C. Sec. 2001 et seq.).

“(3) Bonds or debentures of the Federal Home Loan Bank Board established under the Federal Home Loan Bank Act (12 U.S.C. Sec. 1421 et seq.).

“(4) Stocks, bonds, debentures, and other obligations of the Federal National Mortgage Association established under the National Housing Act, as amended (12 U.S.C. Sec. 1701 et seq.).

“(5) Bonds of any federal home loan bank established under that act.

“(6) Obligations of the Federal Home Loan Mortgage Corporation.

“(7) Bonds, notes, and other obligations issued by the Tennessee Valley Authority under the Tennessee Valley Authority Act, as amended (16 U.S.C. Sec. 831 et seq.).

“(8) Other obligations guaranteed by the Commodity Credit Corporation for the export of California agricultural products under the Commodity Credit Corporation Charter Act, as amended (15 U.S.C. Sec. 714 et seq.).

“(f)(1) Commercial paper of “prime” quality as defined by a nationally recognized organization that rates these securities, if the commercial paper is issued by a federally or state-chartered bank or a state-licensed branch of a foreign bank, corporation, trust, or limited liability company that is approved by the Pooled Money Investment Board as meeting the conditions specified in either subparagraph (A) or subparagraph (B):

“(A) Both of the following conditions:

“(i) Organized and operating within the United States.

“(ii) Having total assets in excess of five hundred million dollars (\$500,000,000).

“(B) Both of the following conditions:

“(i) Organized within the United States as a federally or state-chartered bank or a state-licensed branch of a foreign bank, special purpose corporation, trust, or limited liability company.

“(ii) Having programwide credit enhancements including, but not limited to, overcollateralization, letters of credit, or surety bond.

“(2) A purchase of eligible commercial paper may not do any of the following:

“(A) Exceed 270 days maturity.

“(B) Represent more than 10 percent of the outstanding paper of an issuing federally or state-chartered bank or a state-licensed branch of a foreign bank, corporation, trust, or limited liability company.

“(C) Exceed 30 percent of the resources of an investment program.

“(3) At the request of the Pooled Money Investment Board, an investment made pursuant to this subdivision shall be secured by the issuer by depositing with the Treasurer securities authorized by Section 53651 of a market value at least 10 percent in excess of the amount of the state's investment.

“(g) Bills of exchange or time drafts drawn on and accepted by a commercial bank, otherwise known as bankers acceptances, that are eligible for purchase by the Federal Reserve System.

“(h) Negotiable certificates of deposits issued by a federally or state-chartered bank or savings and loan association, a state-licensed branch of a foreign bank, or a federally or state-chartered credit union. For the purposes of this section, negotiable certificates of deposits are not subject to Chapter 4 (commencing with Section 16500) and Chapter 4.5 (commencing with Section 16600).

“(i) The portion of bank loans and obligations guaranteed by the United States Small Business Administration or the United States Farmers Home Administration.

“(j) Bank loans and obligations guaranteed by the Export-Import Bank of the United States.

“(k) Student loan notes insured under the Guaranteed Student Loan Program established pursuant to the Higher Education Act of 1965, as amended (20 U.S.C. Sec. 1001 et seq.) and eligible for resale to the Student Loan Marketing Association established pursuant to Section 133 of the Education Amendments of 1972, as amended (20 U.S.C. Sec. 1087-2).

“(l) Obligations issued, assumed, or guaranteed by the International Bank for Reconstruction and Development, the Inter-American Development Bank, the Asian Development Bank, the African Development Bank, the International Finance Corporation, or the Government Development Bank of Puerto Rico.

“(m) Bonds, debentures, and notes issued by corporations organized and operating within the United States. Securities eligible for investment under this subdivision shall be within the top three ratings of a nationally recognized rating service.

“(n) Negotiable Order of Withdrawal Accounts (NOW Accounts), invested in accordance with Chapter 4 (commencing with Section 16500).”



Governing Board Memorandum

August 7, 2019

Agenda Item 4

Wildfire Fund Risk Transfer Issues: Discussion and approval of CEA's activities to procure reinsurance intermediary and risk transfer services. Consideration and adoption of a resolution or resolutions authorizing CEA to contract for reinsurance and risk transfer advisory services, and to develop and implement risk transfer guidelines and a risk transfer strategy to protect the Wildfire Fund.

Recommended Action:

Consideration and adoption of a resolution or resolutions as follows:

- a) Authorizing CEA, as Interim Administrator of and on behalf of the Wildfire Fund, to enter into a contract for reinsurance intermediary and advisory services;
- b) Approving and adopting Risk Transfer Guidelines for the Wildfire Fund; and
- c) Authorizing CEA, as Interim Administrator of and on behalf of the Wildfire Fund, to purchase insurance, reinsurance and other forms of risk transfer to protect the Wildfire Fund and increase the durability and claim-paying capacity of the Wildfire Fund.

Background

The background of the 2019 Wildfire Legislation and the capitalization of the Wildfire Fund is set forth in detail in the Governing Board Memorandum regarding Agenda Item 3 (Wildfire Fund Set-up and Initial Capitalization). Importantly, while the initial capitalization of the Wildfire Fund has not yet been received, **the Wildfire Fund is "on risk"** for the wildfire season that has already started. The Wildfire Fund is currently exposed to incurring liabilities in the event of a utility-caused wildfire.



The 2019 Wildfire Fund Legislation states that among the duties of CEA, as the Interim Administrator of the Wildfire Fund and with the oversight and approval of the Governing Board, is to “buy insurance or take other actions to maximize the claims paying resources of the fund.” (Pub. Utilities Code § 3284(e)). Protection of the Wildfire Fund through implementation of a prudent risk transfer strategy is essential to increasing the claim-paying capacity and durability of the Wildfire Fund.

Consistent with the dictates of the 2019 Wildfire Legislation, CEA has (i) commenced a process of procuring a reinsurance intermediary/broker firm, and (ii) developed Risk Transfer Guidelines to articulate the policies that will govern the procurement of insurance, reinsurance or other forms of risk transfer contracts to protect the Wildfire Fund.

Based on CEA’s reinsurance market experience and expertise, and its work to date on the Wildfire Fund, CEA is seeking Governing Board authorization to contract with a qualified reinsurance intermediary/broker to work for the Wildfire Fund on procuring risk transfer contracts. CEA is also seeking approval and adoption of proposed Risk Transfer Guidelines that will govern CEA’s decisions regarding the binding of risk transfer contracts for the Wildfire Fund. Finally, given that the Wildfire Fund is currently exposed to risk of liability and loss during the current wildfire season, CEA seeks authorization to commence the prompt procurement of risk transfer contracts, if available from the market on reasonable economic terms.

Reinsurance Intermediary/Broker Procurement.

Process. There are a limited number of internationally recognized reinsurance intermediary firms with the market reach, reputation and expertise required to implement a risk transfer strategy for the Wildfire Fund. Still fewer have developed a particular expertise related to wildfires and public utilities. CEA met with three globally recognized reinsurance firms with which CEA has existing relationships and extensive knowledge of their capabilities. The purpose was to assess their specific capabilities with respect to the peril of wildfires, and to obtain proposed financial terms for providing intermediary and brokerage services to CEA for the Wildfire Fund. The assessment process included in-person meetings at CEA’s offices, and detailed discussions regarding market strategy and fee structures.



CEA is in the final stages of its assessment, and will be prepared to execute a contract with the firm that is best qualified to undertake the immediate work to procure risk transfer contracts for the Wildfire Fund, based on a reasonable fee structure.

Wildfire Fund Risk Transfer Guidelines

The Wildfire Fund's risk profile and exposure to catastrophe losses from utility-caused wildfires is decidedly different from the earthquake risks that face the CEA Earthquake Fund, but the markets that are willing to provide catastrophe risk transfer for these perils are very similar. Moreover, the strategies for negotiating and purchasing risk transfer from these markets is also similar between earthquake and wildfire. Accordingly, CEA has modeled its proposed Risk Transfer Guidelines for the Wildfire Fund on CEA's earthquake Risk Transfer Guidelines, with necessary confirming changes to maximize CEA's access to the markets.

The proposed Risk Transfer Guidelines set forth general guidelines and standards for purchasing risk transfer contracts. The Policy does not mandate any particular purchases or prices. CEA believes the proposed Risk Transfer Guidelines are reasonable and appropriate, and will greatly assist in guiding CEA in the implementation of a reasonable risk transfer strategy to protect the Wildfire Fund. A copy of the proposed Wildfire Fund Risk Transfer Guidelines is attached as Attachment A.

Authorization to Purchase Insurance, Reinsurance or other forms of Risk Transfer.

As noted above, the Wildfire Fund is presently at risk, and will remain at risk for the duration of the current wildfire season. CEA believes it is essential to the long term durability of the Wildfire Fund and the enhancement of its claim-paying capacity that CEA enter immediately the international reinsurance markets to begin the process of purchasing risk transfer agreements, provided that contracts can be negotiated and structured on reasonable terms.

Given the complex and competitive aspects of these sophisticated financial markets, the open and public discussion with the Governing Board of specific pricing or structuring strategies would potentially harm CEA's market position, to the detriment of the Wildfire Fund and its California beneficiaries. Given the circumstances, a broad grant of authority to CEA to execute a risk transfer strategy and purchases, consistent with the written Risk Transfer Guidelines, is warranted and appropriate.



Recommendations:

CEA, in its capacity as Interim Administrator of the Wildfire Fund, recommends that the Governing Board adopt one or more resolutions as follows:

- a) Authorizing CEA, as Interim Administrator of and on behalf of the Wildfire Fund, to enter into a contract for reinsurance intermediary and advisory services;
- b) Approving and adopting Risk Transfer Guidelines for the Wildfire Fund; and
- c) Authorizing CEA, as Interim Administrator of and on behalf of the Wildfire Fund, to purchase insurance, reinsurance and other forms of risk transfer to protect the Wildfire Fund and increase the durability and claim-paying capacity of the Wildfire Fund.

CALIFORNIA WILDFIRE FUND

GUIDELINES FOR SECURING RISK TRANSFER: TRADITIONAL REINSURANCE AND ALTERNATIVE RISK TRANSFER

ADOPTED/APPROVED BY THE CEA GOVERNING BOARD, AS INTERIM ADMINISTRATOR OF AND ON BEHALF OF THE WILDFIRE FUND ON AUGUST 7, 2019

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INTRODUCTION

These *Guidelines for Securing Risk Transfer: Traditional Reinsurance and Alternative Risk Transfer* (referred to as the “Guidelines”) are intended to identify and set out the best practices of the California Wildfire Fund (“CWF”) for accessing and purchasing risk transfer products—not only traditional reinsurance market but also alternative risk transfer markets (including risk transfer products funded by the sale of catastrophe bonds, collateralized reinsurance issued by institutional investors that are not traditional reinsurers, and other related products).

By adopting these Guidelines, the CWF recognizes the evolution of risk transfer markets and reaffirms its commitment to stable and efficient risk transfer, whether in the traditional or alternative markets. These Guidelines may be further updated or modified periodically by the CWF in its discretion, including to respond to changing conditions in the reinsurance and broader financial markets, as well in response to as business, legal, and regulatory developments.

As used in these Guidelines, the terms “reinsurance” or “reinsurer” may sometimes refer to aspects of the broader risk transfer market (including alternative or nontraditional risk transfer markets or providers, as well as primary insurers) rather than strictly to traditional reinsurance. References that are intended to apply solely to traditional reinsurance or traditional reinsurers will use those specific terms.

I. PRINCIPAL GOALS

These Guidelines seek to accomplish four principal goals, presented in order of priority, while mitigating the CWF’s potential legal or financial liabilities and ensuring regulatory compliance:

1. *Financial Strength*: To minimize the risk to the CWF that a provider might fail to timely pay reinsurance as a result of that provider’s financial condition.
2. *Stability*: To encourage the CWF to secure risk transfer capacity from providers and use products that, together, can endure all reasonably-foreseeable market conditions.
3. *Efficiency*: To enable the CWF to select the most efficient risk transfer capacity, including at rates-on-line that are competitive with other sources of risk transfer capacity.
4. *Flexibility*: To provide for reasonable flexibility by allowing for alternative products and stable sources of risk transfer capacity that are more cost-effective than competing sources.

II. GENERAL STRATEGY

A. APPROVAL OF RISK TRANSFER STRATEGY

Given the CWF's risk transfer needs, the CWF recognizes that it must be in a position to obtain the broadest reasonably-obtainable access to the entire global risk transfer market in order to meet its capacity needs, including, among other possible sources, through the purchase of traditional reinsurance and the use of alternative risk transfer structures. In order to most effectively accomplish the four principal goals outlined above, the CWF's administrator, in consultation with the CWF's Risk Transfer Advisory Committee (described below), must prepare and submit to the governing body of the CWF for its approval, on at least an annual basis, a comprehensive risk transfer strategy that sets forth the basic risk transfer goals and benchmarks for the ensuing year, including identifying potential capacity constraints and anticipated exposures to be transferred to the risk transfer markets.

B. RISK TRANSFER ADVISORY COMMITTEE

The CWF will establish a Risk Transfer Advisory Committee (hereinafter referred to as the "RTA Committee"), which will have primary responsibility for formulating, overseeing, and approving the CWF's risk transfer strategies and, as appropriate, any specific risk transfer transaction that materially vary in nature or structure from previous CWF risk transfer transactions.

The RTA Committee will be composed of a group of between three and seven persons (which may consist, during the CEA administration of the CWF, among others, the CEA CEO, CFO, General Counsel, Chief Actuary, and other CEA staff or officers (supplemented, as necessary, by outside experts) deemed appropriate by the RTA Committee) to oversee the development and approval the CWF's risk transfer strategies. The RTA Committee will operate through the consensus of its members. Formal meetings of the RTA Committee and approval of matters before the RTA Committee through formal voting procedures will not be required.

The RTA Committee should ensure that all CWF staff involved in risk transfer transactions periodically receive appropriate training regarding the legal and regulatory framework applicable to CWF risk transfer transactions, including traditional reinsurance transactions and insurance-linked securities and other forms of alternative risk transfer transactions.

The RTA Committee will convene on at least a quarterly basis to review, consider, advise the CWF on, and make any necessary modifications to:

- The CWF's general risk transfer needs, and its general plan for fulfilling those needs for the following quarter;
- The general plan for risk transfer purchases and transactions for the following quarter; and
- The CWF's structural standards, practices, and procedures for securing risk transfer.

In addition to convening on a quarterly basis, the RTA Committee will convene periodically, as needed, to evaluate any risk transfer transaction that the CWF may consider entering into for which the structure, terms, or nature of the transaction varies significantly and materially from existing or past CWF risk transfer transactions (such a transaction will be referred to herein as a "Nonstandard Transaction"). The

CWF will not enter into any Nonstandard Transaction unless the RTA Committee approves of the CWF entering into that Nonstandard Transaction in advance of its inception. In considering whether to approve a Nonstandard Transaction, the RTA Committee must determine that the Nonstandard Transaction satisfies all of the following criteria:

- The transaction is economically reasonable for the CWF in light of market conditions;
- The transaction furthers the CWF’s claim-paying capacity without subjecting the CWF to unreasonable exposure to market, legal or regulatory risk; and
- The transaction does not pose any undue risk of harm to the CWF’s stature or reputation.

In considering whether to approve a Nonstandard Transaction, the RTA Committee may consult independent third party advisors, such as the CWF’s reinsurance intermediaries and independent financial advisor, to analyze and discuss with the RTA Committee the benefits, risks and opportunities of any proposed Nonstandard Transaction. CWF staff should appropriately document discussions and decisions related to these topics.

III. TRADITIONAL REINSURANCE

The following section of the Guidelines will apply to all providers of *traditional* reinsurance and all *traditional* reinsurance contracts to which the CWF is a party.

A. STABILITY

To provide uninterrupted availability of capacity to fulfill its purpose of providing funds to cover utility wildfire losses, the CWF must endeavor to buy reinsurance only from providers that can endure all foreseeable market conditions.

To most effectively accomplish this goal, the CWF will take into account the following considerations:

1. When cost-effective and advantageous under the existing economic and market environment, the CWF will seek to enter into an appropriate percentage of its reinsurance commitments on multi-year terms.
2. The CWF will take steps to ensure that future markets into which CWF risk can be transferred will continue to be available and accessible.
3. To the extent practical and feasible, the CWF prefers to transact directly with entities that are the primary bearers of the ultimate risk (the “primary risk bearers”). The CWF will identify, and appropriately treat, primary and secondary market capacity, under the following terms:
 - a. The CWF distinguishes primary market capacity from secondary marked capacity as follows:
 - Primary market capacity offers direct contact between the CWF and the ultimate risk-bearer and, all other considerations being equal, is generally deemed by the CWF to be more stable than secondary capacity. Direct contact will generally permit a more thorough and effective exchange of knowledge between the CWF and the ultimate

risk bearer—this direct collaboration can mature into a long-term relationship that enhances uninterrupted access to risk capital, which is crucial to the CWF’s mission.

- Secondary market capacity means the entity executing the transaction with the CWF is not the ultimate risk bearer—instead, it may be a fronting entity that is a conduit of risk and premium to a retrocessionaire or bondholder (in secondary markets). In such a case, while the contracting counterparty is directly liable to the CWF under the terms of the reinsurance contract for the payment of claims, it is the secondary market that has accepted the ultimate risk of CWF loss.
- b. Because of certain general advantages of primary market capacity, the CWF prohibits any *specific retrocession* of CWF risk without the advance written permission of the CWF. In those cases where the CWF has approved the specific retrocession of CWF risk, the line risk should be applied against the maximum permitted line of *both* the direct reinsurer and each retrocessionaire, as described in the next section of these Guidelines.
- c. The CWF relies on input from reinsurance intermediaries and independent financial consultants to help the CWF evaluate the economic environment at the time of securing reinsurer participations, and to consider reinsurers that might occasionally (with CWF permission) use retrocessional reinsurance to manage risk.

5. Given the potential size of the CWF’s risk transfer program, the CWF will avoid relying entirely on a few entities or markets to provide all its reinsurance and claim-paying capacity. An inordinately large allocation to one reinsurer could disadvantage the CWF. (The CWF may, at its sole discretion, moderate this guideline in response to compelling and appropriate circumstances.)

B. FINANCIAL STRENGTH

A reinsurer’s financial strength and its ability to fulfill its promise of claim-paying obligations are the primary considerations in determining whether that reinsurer qualifies to do business with the CWF. Accordingly, in obtaining claim-paying capacity from traditional reinsurance sources, the CWF should apply the following criteria at inception of the reinsurance contact, but also should maintain the flexibility to take appropriate action, including by means of the credit enhancements described below, if these criteria are not satisfied.

In the sole judgment and discretion of the CWF, acting with the advice of staff and experts, the CWF may waive or modify any allocation guideline if to do so would bring substantial benefit to the CWF without compromising the basic goals of financial strength, stability, and efficiency.

1. General Requirements

To qualify as a CWF reinsurer, a reinsurer must meet both of the following requirements (all amounts in US dollars):

- A policyholders’ surplus (PHS) of at least \$150 million; and
- An A.M. Best financial strength rating of at least A-, or a Standard & Poor’s (S&P) financial strength rating of at least A-, or a Moody’s financial strength rating of at least A3.

The CWF will use the following criteria to allocate lines of reinsurance to reinsurers:

- The rating agencies A.M. Best, S&P, and Moody’s assign ratings to reinsurers that signify a reinsurer’s financial strength. Each rating agency analyzes key financial ratios to measure leverage, liquidity, asset quality, and other balance-sheet and income-statement indicators of financial strength. The rating agencies also assess management qualifications and take into account a reinsurer’s exposure to natural disasters. It is therefore appropriate that the rating that A.M. Best, S&P, or Moody’s assigns a reinsurer should influence the size of that reinsurer’s participation in CWF reinsurance contracts.
- “Economic mass” — a company’s policyholders’ surplus (“PHS”) — is an indicator of financial staying power and should directly influence the CWF participation allocation. No reinsurer should be allocated combined participating shares in CWF reinsurance contracts for a given contract period that would generate total liabilities (including exposures to reinstated, reset, or secondary limits, if any) of greater than 10% of that reinsurer’s PHS.

2. Lloyd’s Syndicates

The financial statements of syndicates at Lloyd’s do not state a policyholders’ surplus; therefore, unlike with non-Lloyd’s reinsurers, policyholders’ surplus cannot be used as an allocation criterion for Lloyd’s. The CWF must instead use a “policyholders’ surplus equivalent” in lieu of using policyholders’ surplus.

- a. The CWF will use one or more of the following, as specified below in this section, as policyholders’ surplus equivalents:
 - The syndicate’s premium receipts plus its reserves. This is commonly referred to as “Syndicate Level Assets.”
 - Any additional capital dedicated by a syndicate’s member(s) for the syndicate’s liabilities by a deposit of funds into any of three trust funds in which members’ assets may be held—the Lloyd’s deposit fund, the special reserve fund, or the personal reserve fund—each of which is available to meet cash calls made on the member with respect to syndicate needs. This is commonly referred to as “Members’ Funds at Lloyd’s.”
 - The syndicate’s volume of business measured in gross written premiums net of acquisition costs underwritten by a syndicate’s business plan accepted by Lloyd’s (Lloyd’s requires syndicates to have a stated amount of capital to support the amount of gross written premiums in the business plan). This is commonly referred to as the syndicate’s “stamp capacity.”
- b. For purposes of determining a syndicate’s maximum line allocation, the CWF will calculate the policyholders’ surplus equivalent as follows:
 - i. If the syndicate has disclosed to the CWF both its Syndicate Level Assets and its dedicated Members’ Funds at Lloyd’s, the combination of Syndicate Level Assets and dedicated Members’ Funds at Lloyd’s will be used as the policyholders’ surplus equivalent.
 - ii. If the syndicate has disclosed to the CWF its Syndicate Level Assets but not its dedicated Members’ Funds at Lloyd’s, the Syndicate Level Assets will be used as the policyholders’ surplus equivalent.

iii. If the syndicate has not disclosed to the CWF its Syndicate Level Assets, the syndicate's stamp capacity will be used as the policyholders' surplus equivalent.

3. ***Maximum Line Allocation:*** To properly scale a reinsurer's CWF participation level to its rating and PHS, the following guidelines will be used when allocating lines of reinsurance contracts:

Table 1

(For reinsurers with PHS greater than \$150 million)

Maximum Line (% of PHS)	A.M. Best Rating*	Standard & Poor's Rating*	Moody's Rating*
0% — 3.0%	A-	A-	A3
3.01% — 5.5%	A	A to A+	A1 to A2
5.6% — 8.0%	A+	AA- to AA	Aa3 - Aa2
8.01% — 10.0%	A++	AA+ to AAA	Aa1 to Aaa

** For a company that is rated by two or more of the rating agencies listed above, the appropriate rating to use for determining that company's maximum line allocation will be selected at the sole judgment and discretion of the CWF, in consultation with and acting with the approval of the RTA Committee.*

The maximum line allocation is calculated as follows: The sum of all the reinsurer's authorized lines on all CWF reinsurance contracts that are or will be in force during reinsurance contract period under consideration will be compared to the maximum permitted line from Table 1. As used herein, the "reinsurer's authorized lines" that will be used to determine the maximum permitted line will be deemed to be the aggregate of all lines of CWF risk assumed by that reinsurer that will be in effect during that period, regardless of whether any such lines are assumed as primary market capacity, as a fronting entity, as a retrocessionaire, or in any combination of these.

The CWF seeks to buy reinsurance from the global reinsurance community. Many of the CWF's reinsurers may not domiciled in the United States, and many of those reinsurers provide financial reports (including PHS) based on currencies other than U.S. dollars. Exchange rates fluctuate daily, and an exchange rate moving downward in relation to the U.S. dollar could result in diminished financial security for the CWF. To manage this risk, the CWF will use the following procedures to determine the financial status of a non-U.S.-domiciled reinsurer:

- In assigning reinsurance-contract participations, the CWF will calculate the non-U.S.-domiciled reinsurer's PHS based on its domicile's currency exchange rate against the U.S. dollar not more than 30 days before the date of binding that reinsurer's participation in a reinsurance contract. This is called the "Base Exchange Rate."
- If during the term of a reinsurance contract a reinsurer's domicile's currency exchange rate falls below the Base Exchange Rate, the CWF will reevaluate compliance with the Guidelines for any reinsurer based in that domicile.

The CWF requires that all its reinsurance contracts grant the CWF the right (but not the obligation) to reduce or terminate a reinsurer's participation share, before contract expiration, if the reinsurer's financial strength weakens, causing the reinsurer's existing participation allocation to exceed what the Guidelines would permit

4. Credit Enhancements

The CWF, at its sole discretion, may accept certain credit-enhancement tools in support of reinsurance-line allocations for reinsurers (including non-traditional reinsurers that may wish to participate in the CWF's traditional reinsurance placements) that do not meet the above financial strength criteria and would therefore ordinarily fall outside the financial strength requirements of these Guidelines. This provision, which permits the CWF certain flexibility in waiving or modifying allocation guidelines, is not intended to reserve or grant, and does not reserve or grant, any rights whatsoever to any person or entity other than the CWF. Credit enhancement may include, without limitation, any of the following:

- a. **Collateralization.** The CWF may allow reinsurers to provide the CWF with collateral, in a form acceptable to the CWF, to support an allocation of reinsurance limit outside the Guidelines. All such Collateral must be posted in a collateral account established in a U.S.-based bank with a long-term credit rating of at least "A-" from Standard & Poor's or "A-" from A.M. Best, using a form of collateral account control agreement approved by the CWF. The collateral account control agreement must require that collateral in the account be solely held in the form of specified types of permitted assets, consisting of one or more of the following:
 - i. Cash, in United States Dollars;
 - ii. Interests in money market mutual funds rated in the highest rating category by Moody's or Standard & Poor's and registered under the Investment Company Act of 1940 that invest solely in direct obligations of the U.S. Treasury and have a per share value of \$1.00 or more;
 - iii. Direct obligations of the U.S. Treasury, excluding Treasury "separate trading of registered interest and principal securities" zero coupon bonds (Treasury STRIPS) or Treasury Inflation Protected Securities (TIPS); or
 - iv. Other assets that the CWF may, at its option, permit upon a determination, in the sole judgment and discretion of the CWF acting with the approval of the RTA Committee and with, as needed the advice of staff and experts, that the assets provide levels of safety, security, and liquidity comparable to the categories of assets specified in subparagraphs (i) through (iii) immediately above.
- b. **Letters of Credit.** The CWF may allow reinsurers to provide one or more letters of credit, in a form acceptable to the CWF, to support an allocation of reinsurance limit outside the Guidelines. All letters of credit must meet appropriate format and security standards, which may include, without limitation, the following criteria:
 - i. The letter of credit is issued by a U.S.-based bank with a long-term credit rating of at least "A-" from Standard & Poor's or "A-" from A.M. Best.
 - ii. The letter of credit is a clean, irrevocable, unconditional direct pay letter of credit payable to the CWF and in form and substance satisfactory to the CWF.
 - iii. The letter of credit is issued for a term expiring no earlier than the termination date of the reinsurance contract for which the reinsurer is securing its line by the letter of credit, and includes an evergreen provision that automatically extends the term for at least one additional year beyond the expiration date unless the issuer of the letter of credit gives written notice of non-renewal to the CWF by certified mail

not less than 60 days prior to the expiration date, and in the event of such a non-renewal or other expiration of the letter of credit, the subscribing reinsurer agrees to obtain replacement letters of credit to the extent necessary to comply with its collateralization requirements.

- c. ***Parental Guarantees.*** A reinsurer that has exceptionally strong capitalization, or a company that is affiliated with a strongly capitalized parent that is willing to provide, and does provide, a written parental guarantee, may be acceptable even if it fails to meet the criteria in the above allocation guidelines. In deciding whether to accept a parental guarantee as a credit enhancement, the CWF will consider the following:
- i. A subsidiary of a quality parent typically enjoys superior liquidity and access to capital.
 - ii. A strong parent would likely not abandon a failed subsidiary and would fulfill the subsidiary's obligations because of the damage that abandonment would inflict on the parent's reputation. Parent companies that are not insurers, however, should be carefully examined for appropriate risk appetite and other desirable, relevant attributes.
 - iii. For a parent company, including a parent company that is itself an insurer or reinsurer, the amount of reinsurance for which a parental guarantee is provided will be deemed to be part of the authorized line of that parent company as well as of the subsidiary company, and thus will count toward the calculation of the maximum line allocations of both the parent and the subsidiary.

The CWF, in its discretion, may require a reinsurer to provide credit enhancements in support of the entire line allocated to the reinsurer, or only that portion of the reinsurer's allocated line that exceeds the amount of that would otherwise be permissible under these Guidelines.

C. EFFICIENCY

Because a competitive market environment benefits the CWF when it negotiates terms for traditional reinsurance, the CWF should:

- Work to place cost-effective alternatives to traditional reinsurance;
- Provide reinsurers detailed underwriting information through its intermediaries.

Appropriate use of capital market transactions can supplement traditional reinsurance capacity. This can include the use of alternative transactions such as catastrophe bonds and transformer reinsurance arrangements in which the participants are primarily or exclusively capital markets entities, as well as collateralized re transactions in which capital markets entities participate alongside traditional reinsurers. Certain negative attributes of some secondary capital market products (instability, inflexibility, and lack of claim-paying track record) may be counterbalanced by achieving the desirable attributes of lower cost, encouragement of competition among reinsurers, and diversification of sources of claim-paying capacity.

D. FLEXIBILITY

In the sole judgment and discretion of the CWF, acting with the advice of staff and experts, the CWF may waive or modify any allocation guideline if to do so would bring substantial benefit to the CWF without compromising the basic goals of financial strength, stability, and efficiency.

IV. ALTERNATIVE RISK TRANSFER

This section of the Guidelines applies to transactions that are not reinsurance transactions with traditional reinsurers, but rather, to all alternative risk transfer transactions in which the CWF is a party, including reinsurance funded by the proceeds of a catastrophe bond issued by a special purpose reinsurer and other transactions funded by insurance-linked securities (referred to collectively as “ILS Transactions”), collateralized reinsurance with institutional investors, such as hedge funds and pension plans, and other similar transactions. These transactions will be referred to in these Guidelines as “Alternative Transactions.”

The CWF, at its sole discretion, may enable the development of and utilize Alternative Transactions, which may bring greater efficiency and stability to the CWF’s claim-paying structure or diversify the CWF’s sources of claim-paying capacity, in order to, among other things:

- Attract capacity at more efficient terms;
- Attract capacity that is comparable with the pricing of traditional reinsurance markets; or
- Enable the development of alternative markets or alternative financial products, which may bring, without limitation, greater efficiency and stability to the CWF’s risk transfer structure or diversify the CWF’s sources of risk transfer capacity.

PRICING

The final pricing of any Alternative Transaction must be approved by the administrator and any other appropriate professionals at the CWF appointed by the RTA Committee to advise on pricing matters. The administrator should solicit the views of reasonably selected market professionals to assist the CWF in determining whether an Alternative Transaction is competitive from a pricing standpoint, taking into account the relative benefits of the transaction, with other forms of risk transfer, including but limited to with traditional reinsurance.

NEGOTIATION OF TERMS

It is recommended that the CWF’s internal and external counsel (if any) either draft or review the terms of any reinsurance agreement entered into by the CWF in connection with an Alternative Transaction to ensure that the terms are consistent with appropriate market standards and create effective risk transfer from the CWF’s perspective.

In connection with its procurement of reinsurance funded by the proceeds of a catastrophe bond or other insurance-linked securities issued by a special purpose reinsurer (referred to as an ILS Transaction), certain special terms must be included as part of the transaction, including, but not limited to, the following:

- The aggregate limit of the reinsurance agreement will be fully collateralized, up to the full aggregate limit of the agreement. The proceeds from the sale of the bonds must be deposited into a collateral account established in a U.S.-based bank with a long-term credit rating of at least “A-” from Standard & Poor’s or “A-” from A.M. Best, using a form of collateral account control agreement approved by the CWF. The collateral control agreement must require that collateral in the account be solely held in the form of specified types of permitted assets, consistent with those collateral categories stated above in the “Collateralization” requirements of the Traditional Reinsurance section of these Guidelines.

- The CWF will pay negotiated fees and expenses only upon successful completion of a risk-transfer transaction by the reinsurer. If the risk-transaction is not successfully completed by the reinsurer, the CWF will not be obligated to pay or reimburse any person or entity (including, without limitation, the reinsurer, the underwriter, or any service providers engaged by the reinsurer or underwriter) for any expenses and fees associated with the transaction.
- The CWF may only agree to indemnify the reinsurer or service providers for claims relating to inaccuracies in CWF subject business data, if any, used in the ILS Transaction. However, the CWF will not agree to provide any other indemnification for the transfer of the risk from the reinsurer into the capital markets, except through the procurement of an insurance policy where the risk of indemnification is not borne by the CWF.

OPERATING GUIDELINES

In connection with its procurement of reinsurance funded by the proceeds of a catastrophe bond and similar ILS Transactions, it is recommended that the CWF and its staff comply with the following operating guidelines.

- A. Underwriters.** While ultimate selection may be within the discretion of the reinsurer, the underwriters assisting the reinsurer in the effort of transferring the risk into the capital markets should be acceptable to the CWF from a reputation and experience perspective, including that:
- The lead underwriter has been in business for at least five years and has a satisfactory reputation in connection with insurance-linked securities offerings and the broader capital markets;
 - The underwriters are appropriately licensed as broker-dealers to perform the functions required of them under the purchase agreement with the reinsurer; and
 - The underwriters have appropriate experience in transferring insurance risk to the capital markets.
- B. Offering Materials.** All CWF information provided by the CWF to any party involved in an ILS Transaction and that may reasonably foreseeably be used in connection with the reinsurer's preparation of offering materials should be subject to the review and approval of appropriate personnel appointed by the RTA Committee in order to determine, at the time the information was provided, whether the information (i) is accurate in all material respects and (ii) does not omit to state a material fact necessary in order to make the statements contained therein, in the light of the circumstances under which they were made, not misleading
- C. Subject Business.** If any subject business data is provided by the CWF to the reinsurer, then internal procedures should be put in place to ensure that any such underlying subject business data, which in turn may be provided to a third party risk modeling firm, is accurate and constitutes the complete set of business that the CWF intends to be covered by the reinsurance agreement.



Governing Board Memorandum

August 7, 2019

Agenda Item 5: Administrator's Plan of Operations

Recommended Action: No action required—information and discussion only

CEA Executive Staff will discuss the statutory obligation to commence development of a Plan of Operations for the Wildfire Fund, pursuant to Public Utilities Code § 3283.