2020 Annual Report

to the California Catastrophe Response Council and the Legislature on Wildfire Fund Operations

CEA CALIFORNIA EARTHQUAKE AUTHORITY™ | Wildfire Fund Administrator

July 23, 2020

Pursuant to California Public Utilities Code section 3283, this annual report on Wildfire Fund operations has been prepared by the California Earthquake Authority in its capacity as the Wildfire Fund Administrator, approved by the California Catastrophe Response Council, and is hereby presented to the following committees of the California State Legislature:

Senate Energy, Utilities and Communications Committee
The Honorable Ben Hueso, Chair
California State Senate
State Capitol, Room 4035
Sacramento, California 95814

Assembly Utilities and Energy Committee
The Honorable Chris R. Holden, Chair
California State Assembly
State Capitol, Room 5132
Sacramento, California 95814

California Catastrophe Response Council Members
Gavin Newsom, Governor, Chair
Richard Gordon, appointee of the Speaker of the Assembly, Vice Chair
Fiona Ma, State Treasurer
Ricardo Lara, Insurance Commissioner
Wade Crowfoot, Secretary of Natural Resources
Paul Rosenstiel, Public Member
Rhoda Rossman, Public Member
Catherine Bando, Public Member
Michael Wara, appointee of the Senate Rules Committee

WILDFIRE FUND ADMINISTRATOR

ANNUAL REPORT to the
CALIFORNIA CATASTROPHE RESPONSE COUNCIL
and the
LEGISLATURE on WILDFIRE FUND OPERATIONS

Report Period: July 12, 2019 – July 11, 2020
(Pursuant to Public Utilities Code section 3283)

Date of Report: July 23, 2020

Pursuant to Public Utilities Code section 3283, this annual report on Wildfire Fund operations ("Annual Report") was prepared by the Wildfire Fund Administrator ("Administrator") and is presented to the Legislature at the direction of the California Catastrophe Response Council ("Council").[1] In accordance with that statute, this Annual Report includes information on Wildfire Fund ("Fund") assets, projections for the durability of the Fund, the success of the Fund, and whether or not the Fund is serving its purpose.

The information in this first Annual Report covers the one-year period of July 12, 2019—the effective date of Assembly Bill ("AB") 1054 (Holden, Burke & Mayes, Chapter 79, Statutes of 2019) and AB 111 (Committee on Budget, Chapter 81, Statutes of 2019), and thus the creation date of the Wildfire Fund—through July 11, 2020.

[1] The Annual Report satisfies the Council's and Administrator's statutory duty to annually report to the Legislature on the Wildfire Fund's "Plan of Operations" as specified in Public Utilities Code section 3283.

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Executive Summary

On July 12, 2019, Governor Gavin Newsom signed Assembly Bill ("AB") 1054 and AB 111 (collectively, the "2019 Wildfire Legislation").[2] The 2019 Wildfire Legislation enacts a broad set of reforms and programs related to utility-caused wildfires in California, including establishing the Wildfire Fund ("Fund").

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

Oversight of the administration of the Fund is the responsibility of the California Catastrophe Response Council ("Council"), created under AB 111. The Council has nine members, consisting of the Governor, the Insurance Commissioner, the Treasurer, and the Secretary for Natural Resources, each of whom may appoint designees to attend Council meetings in their place, as well as one member appointed by the Senate Committee on Rules, one member appointed by the Speaker of the Assembly, and three members of the public appointed by the Governor.

I. Fund Assets

The 2019 Wildfire Legislation created a capitalization structure that establishes multiple revenue streams flowing into the Fund to provide approximately $21 billion in claim-paying capacity to cover claims arising from covered wildfires. The $21 billion in claim-paying capacity is split between contributions from the Fund's participating investor-owned utility companies ("IOUs")—San Diego Gas & Electric Company ("SDG&E"), Southern California Edison ("SCE") and Pacific Gas & Electric Company ("PG&E") (collectively, "the IOUs")—and surcharges on the IOUs' non-exempt ratepayers, which are also referred to as Wildfire Nonbypassable Charges ("NBCs"). The contributions from the IOUs are not passed through to their ratepayers, so are effectively funded by the stockholders of those publicly traded IOUs. The 2019 Wildfire Legislation also required that the Fund be initially capitalized in the form of a short-term $2 billion loan from the State of California's Surplus Money Investment Fund ("SMIF"), a fund within the State's Pooled Money Investment Account. As of July 11, 2020, SDG&E, SCE, and PG&E have all provided their initial and first annual financial contributions. The IOU contributions combined with the SMIF loan total $9.8 billion. In addition, California Public Utilities Commission ("CPUC") Decision 19-10-056 operationalized the collection of the NBCs. Should the Fund need additional capitalization to meet needs arising from eligible claims resulting from covered wildfires, the Fund can issue additional debt backed by the NBCs. Additional detail regarding the Fund's contributions as of July 11, 2020, and audited financials as of December 31, 2019, can be found in Section I: Fund Assets on page 4.

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[2] AB 1054 was subsequently amended by AB 1513 (Holden, Chapter 396, Statutes of 2019).

II. Projections for the Durability of the Fund

Durability is a probability measure expressing the likelihood that the Fund will have sufficient funds to pay eligible claims each year, over a number of years. The Administrator relies on catastrophe-loss model output from the AIR Worldwide Touchstone 7 model as a starting point for measuring the distribution of eligible claims to the Fund. The California Earthquake Authority ("CEA"), as Administrator, has engaged both Filsinger Energy Partners ("Filsinger") and Guy Carpenter & Company ("Guy Carpenter"), a global reinsurance broker, and has worked with them to make further refinements to the models to aid CEA in monitoring Fund durability and exposure to losses. The Administrator also uses the historical total losses to create an alternate "high risk" view. Additional detail regarding the test scenarios and durability analysis can be found in Section II: Projections for the Durability of the Fund on page 6.

III. The Success of the Fund

Assessing the success of the Fund during its first full year in existence requires examination of (1) the start-up process undertaken to operationalize and capitalize the Fund; (2) the establishment of the required infrastructure for administration and oversight of the Fund; and (3) whether the Fund had sufficient claim-paying capacity to cover any incurred or anticipated claims from the 2019 wildfire season.

(1) Start-up and Operationalization of the Fund

The Council and Administrator have taken all necessary actions to establish and operationalize the Fund. Immediately upon the effective date of the 2019 Wildfire Legislation, CEA was designated as the Interim Administrator of the Fund. Prior to the activation of the Council, the duties and responsibilities of the Council to oversee CEA's activities were vested in CEA's Governing Board (consisting of the Governor, the Insurance Commissioner, and the Treasurer, with ex officio members appointed by the Speaker of the Assembly and the Chair of the Senate Rules Committee). As Interim Administrator, CEA quickly established the required financial infrastructure (e.g., trust accounts, investment advisors, investment policies, asset managers, and financial and accounting systems) to allow for receipt of the more than $4.6 billion transferred to the Fund only weeks after the 2019 Wildfire Legislation was signed into law. The CEA Governing Board also approved CEA's activities to procure a reinsurance intermediary for risk transfer services, and to develop and implement risk transfer guidelines and a risk transfer strategy to protect the Fund during the looming 2019 wildfire season. It is important to note that the Fund was "on risk" immediately upon the Governor's signature of AB 1054.

(2) Establishment of the Council and Appointment of the Administrator

The Council was successfully activated in October 2019 and currently has a full roster of active members. The Council met twice during the report period: January 16, 2020, and April 23, 2020. The Council is scheduled to meet on

July 23, 2020, and October 22, 2020. Details of these future meetings will be included in the second Annual Report. All publicly noticed meeting agendas and materials, along with past meeting materials, are available at this website: cawildfirefund.com/council.

(3) Claims Summary
During the report period, no claims were made by any of the IOUs on the Fund. However, see below in Section IV on page 13 of this report, for a summary of the 2019 Kincade fire, which still has the potential to give rise to a claim on the Fund.

IV. Whether or Not the Fund Is Serving Its Purpose

During its first year of existence, the Fund furthered its statutorily defined goals to benefit ratepayers by its impact on IOUs' credit ratings, the participation of PG&E in the Fund, and the Administrator's experience with the 2019 wildfire season and associated impacts on the Fund.

- **IOU Credit Ratings**
  Since the formation of the Fund, and the receipt of initial financial contributions from SCE and SDG&E, both IOUs have experienced rating stabilizations. Though the actual ratings have not changed, both IOUs' ratings outlooks have moved in a positive direction.

- **Participation of PG&E in the Fund**
  On July 1, 2020, PG&E made its initial and first annual financial contribution to the Fund. This satisfied the final remaining statutory requirement for PG&E to be included in and protected by the Fund. As we enter the 2020 wildfire season, the Fund is available to respond to covered wildfires caused by any of the three large IOUs—PG&E, SDG&E, and SCE.

- **The 2019 Wildfire Season**
  The work the Administrator and Council have performed over the past year to operationalize the Fund puts the Administrator in a ready position to be able to discharge its statutory duties related to paying claims for covered wildfires. And while, to date, no IOU has made any claims on the Fund, the Administrator is aware that on July 16, 2020, the California Department of Forestry and Fire Protection (CAL FIRE) determined that the Kincade fire was caused by electrical transmission lines owned and operated by PG&E. Should PG&E in the future seek reimbursement from the Fund for claims incurred during the 2019 wildfire season, including as a result of the Kincade fire, the Administrator will reimburse those claims consistent with Public Utilities Code section 3292(e) and will report to the Legislature in a future Annual Report.

2020 Annual Report

I. Fund Assets

Public Utilities Code section 3280 defines “Wildfire Fund assets” as “the sum of all moneys and invested assets held in the fund which shall include, without limitation, any loans or other investments made by the state to the fund, all interest or other income from the investment of money held in the fund, any other funds specifically designated for the fund by applicable law, and the proceeds of any special charge (or continuation of existing charge) allocated to and deposited into the fund, reinsurance, and the proceeds of any bonds issue for the benefit of the fund.”

As the Administrator, CEA is custodian of the Fund’s cash and investments. This requires CEA to report those held assets as a segregated custodial fund in CEA’s financial statements. Detailed information relevant to the Fund can be found in CEA’s 2019 audited financial statements, available at this website: EarthquakeAuthority.com/About-CEA/Financials/Financial-Statements. Following are excerpts of that financial information, which covers calendar year 2019, along with supplemental unaudited information related to the Fund’s contributions received through July 11, 2020.

CALIFORNIA EARTHQUAKE AUTHORITY
Statement of Fiduciary Net Position – Fiduciary Funds of California Wildfire Fund
As of December 31, 2019

	Custodial Funds
Assets	
Cash and investments:	
Cash and cash equivalents	$ 170,912,277
Investments	4,599,954,544
Total assets	$ 4,770,866,821
Liabilities and Net Position	
Liabilities	
Securities payable	$447,511
Net position:	
Restricted for CWF	4,770,419,310
Total liabilities and net position	$ 4,770,866,821

CALIFORNIA EARTHQUAKE AUTHORITY

Statement of Changes in Fiduciary Net Position –
Fiduciary Funds of California Wildfire Fund

For the Period from Inception of July 12, 2019 to December 31, 2019

	Custodial Funds
Additions:	
Deposits from CWF	$ 4,789,829,741
Deductions:	
Withdrawals by CWF	19,410,431
Increase in net position	4,770,419,310
Net position, at inception	–
Net position, end of year	$ 4,770,419,310

The 2019 Wildfire Legislation created a capitalization structure that ultimately will result in a total claim-paying capacity for the Fund of approximately $21 billion. As noted above, the approximately $21 billion in claim-paying capacity is generated from two revenue streams: surcharges on ratepayers of IOUs and contributions from the equity base of the IOUs. The 2019 Wildfire Legislation also required that the Fund be initially capitalized in the form of a short-term $2 billion loan from the SMIF, a fund within the State's Pooled Money Investment Account.

The 2019 Wildfire Legislation authorizes the Department of Water Resources ("DWR") to receive from the IOUs collections by the IOUs from their non-exempt ratepayers of NBCs to support the Fund. The 2019 Wildfire Legislation also authorized DWR to issue revenue bonds ("Wildfire Revenue Bonds") after the legacy Power Supply Revenue Bonds have been paid or defeased in full to support the Fund. The NBCs are to be imposed by the CPUC on approximately 11.5 million customers in the service areas of the participating IOUs.

CPUC Decision 19-10-056 adopted the Rate Agreement between DWR and the CPUC, established an "irrevocable financing order" under the CPUC code, and calculated the annual revenue requirement of $902.4 million to be collected through NBCs that shall remain in effect until January 1, 2036. NBCs will be used to secure Wildfire Revenue Bonds; NBCs in excess of those required to pay the Wildfire Revenue Bonds, replenish any bond-related reserves, and pay DWR administrative and operating expenses will be deposited in the Fund. Once deposited in the Fund, NBCs are no longer available to pay debt service on the Wildfire Revenue Bonds. The NBCs build upon the long and successful history of the collection of similar bond charges under the DWR Power Supply Revenue Bond Program through several economic cycles and two PG&E bankruptcies dating back to 2002.

The Administrator is working with DWR, the State Treasurer's Office, the Department of Finance, the CPUC, municipal advisors, underwriters, and law firms to prepare for the issuance of bonds by DWR, backed by a pledge of the NBCs as described above.

During 2019, the Fund received $2,792,400,000 in contributions from two of the IOUs—SCE and SDG&E. And, in early July 2020, the Fund received a contribution from PG&E following its emergence from bankruptcy. As the table below shows, as of July 11, 2020, the Fund had received $9.8 billion in capitalization. Should the Fund need additional capitalization to meet needs arising from eligible claims resulting from covered wildfires, the Fund can issue additional debt backed by the NBCs.

CALIFORNIA WILDFIRE FUND
Contributions received schedule
from inception through 07/11/2020

	Description	Date Received	Amount
1.	SMIF Loan Proceeds	8/15/2019	$ 2,000,000,000
2.	SDG&E initial capital contribution	9/9/2019	322,500,000
3.	SCE initial capital contribution	9/9/2019	2,362,500,000
4.	SDG&E 2019 annual contribution	12/19/2019	12,900,000
5.	SCE 2019 annual contribution	12/27/2019	94,500,000
6.	PG&E initial capital contribution	7/1/2020	4,815,000,000
7.	PG&E 2019 annual contribution	7/1/2020	192,600,000
			$ 9,800,000,000

The 2019 Wildfire Legislation also requires that all costs and expenses related to the administration and operation of the Fund be paid from the assets of the Fund. 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 developed and implemented a cost-allocation methodology to ensure that each of those funds bears its own administration expenses.

II. Projections for the Durability of the Fund

The stated legislative intent and language of the 2019 Wildfire Legislation requires that the Fund be administered to maximize its durability so that it provides protection and claim-paying resources to the IOUs while they continue to invest in safety measures designed to reduce the frequency and severity of utility-caused wildfires. For example, Public Utilities Code section 3281(e) authorizes the Administrator, subject to the oversight of the Council, to "buy insurance or take other actions to maximize the claims paying resources of the fund." Additionally, the Council and Administrator are specifically required to report at least annually to the Legislature on the projected durability of the Fund.

"Durability" Defined

Durability is a probability measure expressing the likelihood that the Fund will have sufficient funds to pay eligible claims each year, over a number of years. For example, if Fund durability is 90% at 2035, that would mean there would be a 90% probability that the Fund will have endured to 2035, while paying eligible claims as and when they arise. Conversely, there would be a 10% chance that the Fund would not have had sufficient funds to pay all eligible claims arising during that time period. Durability is a cumulative measure and is expected to decline over any specific number of years as money is periodically drawn from the Fund to pay eligible claims.

Dependencies/Key Factors Influencing Durability

At its simplest, durability depends on the amount of losses flowing to the Fund and the amount of money the Fund has, or will have, to pay eligible losses. Larger, more frequent losses potentially exhaust the Fund more quickly. The larger the amount of available Fund resources to pay losses (initial capital; investment income; risk transfer, if any; and available ratepayer funds), the longer the Fund will remain in a position to pay losses.

The key factors influencing durability are:

- The dollar amount of wildfire losses;
- A determination of prudency;
- The subrogation settlement rate;
- Successful mitigation measures;
- Climate change;
- Exposure growth, which is the increase in the value of the property at risk for wildfire damage; and
- Funding.

Estimating Fund Losses — Catastrophe-Loss Models

Using catastrophe-loss models to assess the loss potential from hurricanes and earthquakes has been commonplace in the insurance industry for underwriting risk and understanding loss potential since the early 1990s. Catastrophe-loss models are also used for assessing risk at the local, state, and national levels and for emergency planning scenarios. In contrast, catastrophe-loss models for wildfire risk are relatively new, have not been widely tested in the market, and have significant differences in the approaches used and the modeled results from one model to the next. Nevertheless, the models can be useful in developing a range of potential wildfire losses. The Administrator relies on catastrophe-loss model output from the AIR Worldwide Touchstone 7 model as a starting point for measuring the potential distribution of eligible claims to the Fund. The Administrator also considers historical losses potentially attributable to IOUs in assessing durability.

Modeling wildfire risk is a complex process. The AIR model considers such factors as ignition, fuel and fuel characteristics, terrain, wind, land use and land cover, wildland-urban interface, and building and construction materials. The output from Touchstone 7 includes individual event scenario losses that can be accumulated and ranked to form a distribution of loss by size of loss. Losses from the AIR model are specific to insurable property losses only. Additionally, the AIR model does not consider who is responsible for causing a wildfire. Therefore, modeled losses are attributed to the IOU as part of the financial modeling, which is described below. Modeled losses are also scaled up as needed to reflect total wildfire losses. There are multiple sources of uncertainty in assessing the amount and frequency of eligible claims flowing to the Fund. It must be recognized that actual losses to the Fund will vary, perhaps significantly, from the modeled losses.

Financial Models

Because the Fund is a complex mechanism dependent on largely uncertain events, a typical best-case/worst-case/expected-case type of pro-forma analysis is not sufficient to understand the potential range of outcomes. Using the catastrophe-loss models and the Fund's financial status as the starting point, a stochastic financial model is built to project the Fund's durability probability through 2035. The financial model used by the Administrator is similar to those developed when the Fund's structure and mechanics were established. Specifically, the Governor's Office engaged a team of experts, including Filsinger and Guy Carpenter, to develop financial models of the Fund to assess durability during the development of the 2019 Wildfire Legislation. CEA, as Administrator, has engaged both Filsinger and Guy Carpenter and has worked with them to make further refinements to the models to aid CEA in monitoring Fund durability and exposure to losses. The key differences in the two financial models are the wildfire losses used and the incident rate or attribution to the IOUs. These differences are discussed in turn.

Wildfire Losses

Guy Carpenter relies on the AIR model and increases its projections by a factor of 1.5 to approximate total loss. Filsinger considers two views of losses. In the first view Filsinger, too, looks at the AIR model output. For the second view, Filsinger relies on historical total losses potentially attributable to the IOUs.

Attribution

Filsinger uses the loss allocation percentages in the 2019 Wildfire Legislation to attribute losses to each IOU. Guy Carpenter attributes the loss to each IOU in a two-step process. First, the modeled loss is assigned to a specific IOU based on the location of the ignition and the IOU service area. Second, the loss is attributed to the specific IOU based on size and the probability that the modeled loss was caused by an IOU. The probability is based on a review of available data for total fire ignitions from 2001 to 2019.

The Administrator relies upon the loss and attribution rate methodology from Guy Carpenter to develop potential wildfire losses. The Administrator also uses the historical total losses to create an alternate "high risk" view. The financial model provides a multi-year view of the Fund starting with the actual financial position of the Fund for the most recent year-end.

As noted above, there are multiple sources of uncertainty in assessing the amount and frequency of eligible claims flowing to the Fund. Scenario testing provides an opportunity to measure the relative impact of key factors. A summary of the test scenarios and results are displayed in the table below.

Scenario	Current Year
1. Base - 60% & 40% settlement rate - 10% mitigation credit - 100% prudency	99.9%
2. Phased Mitigation - 40% settlement rate - Mitigation credits postponed to 2024 - 100% prudency - Base risk	99.9%
3. High Settlement Rate - 70% settlement rate - 10% mitigation credit - 100% prudency - Base risk	99.9%
4. High Risk - 40% settlement rate - No mitigation credits - 100% prudency	99.9%

Base — 1

The Base scenario is the current view of risk considering subrogation settlement rates from 40% to 60%.[3] Because a higher settlement rate means more losses are paid from the Fund, the 60% settlement rate is associated with a slightly lower durability estimate in the current year. However, the difference is negligible because the probability associated with a modeled loss large enough to exhaust all sources of claim-paying capacity is remote. Over a longer projection period, the higher settlement rate has a compounding negative effect on Fund durability.

[3]The term "subrogation settlement rate" refers to settlements between an IOU that caused a covered wildfire, and the insurance companies that initially paid insured losses from the fire, and later seek reimbursement of some or all of their aggregate claim payments from the IOU by way of "subrogation claims." Historically, the insurance companies and IOUs negotiate aggregated settlements for a percentage of the amounts paid out by the insurers.

In the Base scenario, modeled losses are adjusted for a 10% mitigation credit to reflect the Administrator's estimate of mitigation effects based on a review of the IOU mitigation plans and the estimates contained therein along with State mitigation activities. For all scenarios, prudency is assumed to be 100% throughout the projection period. This assumption is done for two specific reasons. First, there is no historical basis upon which to estimate the likelihood that a particular wildfire caused by an IOU would have been deemed to be imprudent. The concept of, and criteria for, imprudence is created by the 2019 Wildfire Legislation and depends on the CPUC's prudency review. Second, assuming 100% prudency presents a more conservative view of durability. If the CPUC's prudency review determines that the IOU was not prudent, the IOU must reimburse the Fund, subject to statutory limits, and there is less loss to the Fund. While this is not a desirable result—better that the IOUs act prudently—the effect is that the Fund has more resources and higher durability when prudency is low.

Phased Mitigation — 2

This scenario is the same as Base scenario 1 with the mitigation credit postponed. The intent of this scenario is not to imply that mitigation efforts have been or will be postponed; it is intended to provide a means to compare the results of this scenario to Base scenario 1 and demonstrate the beneficial effects of mitigation on Fund durability. This scenario also assumes 100% prudency and likewise presents a more conservative view of durability. The results are shown using a 40% subrogation settlement rate.

High Settlement Rate — 3

This scenario is provided to further explore the effects of settlement rates on Fund durability. This scenario is the same as Base scenario 1 with the settlement rate at 70%. A 70% settlement rate is associated with a slightly lower durability estimate in the current year. However, as noted above, the difference is negligible because the probability associated with a modeled loss large enough to exhaust all sources of claim-paying capacity is remote. Over a longer projection period, the higher settlement rate has a compounding negative effect on Fund durability.

High Risk — 4

The High Risk scenario uses the recent historical losses attributed to the IOUs over the past several years to create an alternate view of potential total losses where large losses are more frequent than those used in the Base scenario. Like the Base scenario, this scenario assumes 100% prudency for the same reasons as noted above, as well as for the purpose of isolating the difference to the alternate view of potential future losses. However, it should be noted that assuming 100% prudency in this scenario presents a significantly more conservative view of durability. The results are shown using a 40% subrogation settlement rate.

Frequency of Review

The financial models are updated each year to reflect the most recent year-end financial status of the Fund, including any claim activity, change in the risk transfer program, or change in key assumptions, such as growth and mitigation impacts. The financial models can also be used and updated throughout the year to measure the impact of anticipated or actual changes. Additionally, the models may be used throughout the year as a planning tool to test alternative strategies and what-if scenarios.

Enhancing Durability Using Risk Transfer

- **2019 Risk Transfer Program**
  During its August 7, 2019, meeting, the CEA Governing Board, acting as the Interim Council, granted the Administrator broad authority to execute a risk transfer strategy and purchase, consistent with the written Risk Transfer Policy, insurance protection for the Fund. This risk transfer protection was for nearly nine months and went into effect in September 2019, just two months after enactment of the 2019 Wildfire Legislation and the creation of the Fund. The 2019 risk transfer protection covered liabilities arising from the 2019 wildfire season, related to the two IOUs that had joined the Fund at that time, SDG&E and SCE.

- **2020 Risk Transfer Program**
  In June 2020, the Administrator once again engaged the reinsurance market regarding the potential for a risk transfer program for the 2020 wildfire season. After considerable analysis and great consideration, including Zoom-enabled reinsurer marketing presentations to more than 200 individuals representing more than 50 reinsurers located in the U.S. and elsewhere in the Americas, Bermuda, London, Europe, and Asia, Administrator staff determined that the pricing and structure did not sufficiently meet the goal of enhancing the Fund's durability. Administrator staff continue to evaluate and analyze the risk, pricing, and structural alternatives to enhance the claim-paying capacity and durability of the Fund and may engage the market if a program later developed can achieve the durability goals of the Fund. If the Administrator does engage in a 2020 risk transfer program, details will be provided in a future annual report.

Plan for Winding up the Fund

Current projections do not demonstrate that the Fund will be exhausted within the next three years. Accordingly, this Annual Report does not include a plan for winding up the Fund.

Comparison to Prior Year

Changes from prior-year results, models, and methodologies will be discussed in this section in subsequent reports.

III. The Success of the Fund

The Council and Administrator have taken all necessary actions to establish and operationalize the Fund. As Interim Administrator, CEA quickly established the required financial infrastructure (e.g., trust accounts, investment advisors, investment policies, asset managers, and financial and accounting systems) to allow receipt of the more than $4.6 billion transferred to the Fund only weeks after the 2019 Wildfire Legislation was signed into law. From a Fund governance perspective, the Council was successfully activated in October 2019 with the appointment of a majority of its members, and it currently has a full roster of nine active members.

This section provides a brief summary of the Council's public meetings during this reporting period, includes information on the investments of moneys in the Fund as authorized by Public Utilities Code section 3281(c), and provides a summary of incurred claims.

Overview of the Council's Public Meetings

Prior to the establishment of a quorum of the Council, the 2019 Wildfire Legislation designated the CEA Governing Board ("Governing Board") to exercise the powers and duties of the Council on an interim basis. The Governing Board met in that capacity once, on August 7, 2019, and approved administrative steps undertaken by CEA, as the interim administrator of the Fund, to implement and operationalize the Fund. The Governing Board approved, adopted, and/or ratified agreements by CEA for custodial banking and demand deposit accounts, asset-management services, and investment consulting; authorized CEA to undertake expedited procurement and engagement of additional asset managers in anticipation of additional capitalization; approved and adopted investment policies for the Fund; and authorized CEA to develop, document and implement a cost allocation methodology to allocate all CEA administration expenses arising from or related to the Fund for payment by the Fund consistent with Insurance Code section 10089.6(d)(11). During this meeting, the Governing Board also approved CEA's activities to procure a reinsurance intermediary for risk transfer services, and to develop and implement risk transfer guidelines and a risk transfer strategy to protect the Fund during the looming 2019 wildfire season. It is important to note that the Fund was "on risk" immediately upon the Governor's signature of AB 1054.

Once activated by the appointment of a majority of members, the Council held its first public meeting on January 16, 2020, and elected a Chair, Mark Ghilarducci (the Governor's designee and also Director of the Governor's Office of Emergency Services), and a Vice-Chair, Rich Gordon (the appointee of the Speaker of the Assembly). Among other matters, during this initial meeting, the Council authorized CEA to manage the Conflict-of-Interest Code adoption process pursuant to Government Code section 87300 and adopted a Statement of Incompatible Activities pursuant to Government Code section 19990. The Council also discussed key Fund issues, including the appointment of the Administrator, the development of an Annual Report, and the Administrator's procurement of consulting services to advise CEA on the development of policies and procedures for claims administration functions.

During its April 23, 2020, meeting, after careful deliberations and discussions about whether CEA had the core competencies to perform all required functions of the Administrator, and after making a specific factual finding that CEA did indeed possess those core competencies, the Council appointed CEA as the Administrator. The Council also adopted a slightly revised Statement of Incompatible Activities, which was amended at the request of the California Department of Human Resources. Finally, during this meeting, the Council and Administrator participated in a dialogue regarding the Fund's durability analysis and management, potential revisions to the Investment Policy for Fund Assets, and the status of the Administrator's procurement process for consulting services for claims administration functions.

The Council is scheduled to meet again on July 23 and October 22, 2020. Details of these future meetings will be included in the second Annual Report.

Summary of Investments as Authorized by Public Utilities Code Section 3281(c)

Public Utilities Code section 3281 enumerates the duties and powers of the Administrator of the Fund. Among the Administrator's duties is the responsibility to prudently invest Fund assets. In establishing investment parameters for the Fund, the Legislature incorporated by reference into Public Utilities Code Section 3281(c) the investment guidelines enumerated in Government Code section 16430, which lists permissible investments for the State's general fund moneys held in the Treasurer's SMIF. While Section 16430 was enacted solely for the purpose of guiding the investment of public funds, the Legislature's incorporation of Section 16430 into the 2019 Wildfire Legislation expresses a clear directive to the Administrator to be conservative and apply low risk investment policies that emphasize capital preservation. The written Investment Policies that the Council has approved establish authorized investments that remain within the confines of Government Code Section 16430.

Claims Summary

During the report period, no claims were made by any of the IOUs on the Fund. However, see below in Section IV of this report, a summary of the 2019 Kincade fire, which still has the potential to give rise to a claim on the Fund.

IV. Whether or Not the Fund Is Serving Its Purpose

The 2019 Wildfire Legislation's stated goals for the Fund are to benefit California ratepayers by:

- Reducing costs to ratepayers in addressing utility-caused catastrophic wildfires;
- Limiting the electrical corporations' exposure to financial liability resulting from wildfires that were caused by utility equipment;
- Increasing electrical corporations' access to capital to fund ongoing operations

and to make new investments to promote safety, reliability, and California's clean energy mandates; and

- Supporting electrical corporations' credit worthiness so they can attract capital for investments in safe, clean, and reliable power for California at a reasonable cost to ratepayers.

See AB 1054 (Holden, Burke & Mayes, Chapter 79, Statutes of 2019), Section 1.

To assess whether or not the Fund is serving its purpose, this section of the Annual Report examines the rating stability of the IOUs, the incentives AB 1054 creates for the IOUs to invest in mitigation, PG&E's emergence from bankruptcy, and potential future implications from the Kincade fire on the Fund.

Rating Stability of the IOUs

Prior to the Fund, the IOUs experienced increased pressure and, in some cases, action by the rating agencies. Since the formation of the Fund, and the receipt of initial financial contributions from SCE and SDG&E, both IOUs have experienced rating stabilizations. Though the actual ratings have not changed, both IOUs' ratings outlooks have moved in a positive direction. Standard & Poor's changed the outlook for SDG&E from negative to stable and removed SCE from credit watch negative and assigned a stable outlook. Moody's affirmed ratings but moved SDG&E's outlook from negative to positive, and SCE's from negative to stable.

AB 1054 Creates Incentives for the IOUs to Invest in Mitigation

Increased investments in electric utility grid hardening, situational awareness, and, in the near-term, the use of public safety power shutoffs may help to significantly reduce the risk of utility-caused catastrophic wildfires. AB 1054 requires $5 billion in the aggregate for utility wildfire safety investments with no return on equity for the utility. AB 1054 requires electrical corporations to annually file Wildfire Mitigation Plans with the CPUC. These Wildfire Mitigation Plans must cover at least a three-year period and describe a utility's plans to implement preventive strategies and programs to minimize the risk of its electrical lines and equipment causing catastrophic wildfires, including consideration of dynamic climate change risks. More information on PG&E, SCE, and SDG&E 2020 Wildfire Mitigation Plans and related documents is available at the CPUC's website: cpuc.ca.gov/wildfiremitigationplans.

In addition, AB 1054 creates incentives by way of cost recovery from the Fund, for IOUs to obtain and maintain safety certifications from the CPUC. Safety certifications encourage an IOU to invest in safety and improve safety culture to limit wildfire risks and reduce costs. During the report period, PG&E, SCE, and SDG&E all received their 2019 safety certifications from the CPUC. More information on these safety certificates is available at the CPUC's website: cpuc.ca.gov/wildfires.

The Fund & PG&E

On July 1, 2020, the Administrator received $5.008 billion (initial capitalization of $4.815 billion, plus $193 million for PG&E's share of the aggregate annual IOU contributions for 2019) in contributions from PG&E, qualifying it for coverage from the Fund. The Fund's asset managers have been able to invest all the PG&E contributions in a manner consistent with the Fund's Investment Policy.

PG&E's contributions satisfied the final remaining statutory requirement for PG&E to be included in and protected by the Fund. As we enter the 2020 wildfire season, the Fund is available to respond to covered wildfires caused by any of the IOUs.

The 2019 Wildfire Season and the Implications of the Kincade Fire on the Fund

The 2019 wildfire season caused less damage than the devastating 2017 and 2018 seasons. Detailed information about the 2019 wildfire season is available at CAL FIRE'S website: fire.ca.gov/incidents/2019. During the report period, there have been nine wildfires—Saddle Ridge fire (October 10, 2019), Cypress Complex fire (October 27, 2019), Milpitas fire (October 27, 2019), Pleasant fire north (October 27, 2019), Pleasant fire south (October 27, 2019), Forest fire (October 27, 2019), Easy fire (October 30, 2019), Maria fire (October 31, 2019), and Cambria fire (July 6, 2020)—that may have been caused by IOUs that have been reported to CAL FIRE or in the IOUs' CPUC incident records. There has been one wildfire, the Kincade fire (October 23, 2019) that CAL FIRE has determined was caused by PG&E. With the exceptions of the Saddle Ridge and Kincade fires, all these actual and potential IOU-caused fires resulted in minimal structural damage, with fewer than 5 structures damaged in each case. The Saddle Ridge fire resulted in the damage or destruction of 107 structures, while the Kincade fire resulted in the damage or destruction of as many as 434 structures.

While, to date, no IOU has made any claims on the Fund, the Administrator is aware that on July 16, 2020, CAL FIRE determined that the Kincade fire was caused by electrical transmission lines owned and operated by PG&E. Since it has been determined that PG&E was at fault, the fire will become a covered wildfire, and loss claims in excess of PG&E's $1 billion annual retention may be submitted to the Fund. Because PG&E was still in bankruptcy at the time the fire was ignited, the Fund's reimbursement obligation would be capped at 40% of the amount of eligible claims that would otherwise be reimbursable by the Fund. If the Kincade fire results in a claim, details will be included in a subsequent annual report.

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