Personal Insurance Federation of California
California's Personal Lines Trade Association
REPRESENTING THE LEADING AUTOMOBILE AND HOMEOWNERS INSURERS
State Farm • Farmers • 21st Century Insurance Group • SAFECO • Progressive



**MEMORANDUM**

**Date:** April 10, 2003

**To:** Honorable Juan Vargas, Chair
Members, Assembly Insurance Committee

**From**: Dan C. Dunmoyer, President
G. Diane Colborn, Vice President of Legislative and Regulatory Affairs
Michael A. Gunning, Senior Legislative Advocate

**Re:** AB 1048 (Calderon): Earthquake
Assembly Insurance Committee Hearing: April 23, 2003
**PIFC Position: Support/ Sponsor**

---

The Personal Insurance Federation of California (PIFC), representing insurers who sell nearly 50% of the earthquake insurance written in the California Earthquake Authority (CEA), **supports AB 1048** by Assembly member Calderon.

Assembly Bill 1048 (Calderon) would amend the definition of "available capital" to clarify that available capital does not include "unearned premium", as well as require the CEA Governing Board to establish and maintain a reserve account that would hold an amount equal to policyholders unearned premium. To understand the benefit of this change, it is best to explain the difference between earned and unearned premium.

The money a policyholder pays to keep an insurance policy in force is called premium. "Earned Premium" is the portion of the total premium that applies to the amount of the policy that has already expired. "Unearned Premium" is the portion of the total premium that applies to the remaining portion or the unused amount of the policy period. For example, if Jane Consumer purchases a six-month policy for $300 that has been in effect two months, one-third or $100 of the total premium is said to be "earned" by the insurance company. Two-thirds or $200 of the total premium is said to be "unearned".

What should be noted is that on a traditional insurance company balance sheet, unearned premium is recorded as a liability. It is recorded as such because the insurer would be required to repay this balance to its policyholder should the policyholder elect to cancel the policy before the full term of coverage expires.

In contrast to this standard practice, current statute does not clearly restrict the CEA from recording unearned premium as available capital thereby risking the interests of the consumer and inflating the amount of available capital. AB 1048 would clarify CEA statute by removing unearned premium from the definition of available capital and requiring the CEA Governing Board to create an unearned premium reserve account that would hold an amount equal to policyholders unearned premium to

980 Ninth Street, Suite 2030 Sacramento, CA 95814
Phone (916) 442-6646 • Fax (916) 446-9548 • e-mail: pifc@pifc.org • Website: www.pifc.org

protect consumer interests and rights. In conclusion, changing the definition of available capital within the CEA to exclude unearned premium is not only standard insurance practice, it is appropriate policy to ensure that if a policyholder elects to cancel a policy there is money to provide for a refund. We believe this is an important incremental change that will allow the CEA to operate in a more business wise fashion.

For the reasons stated above the Personal Insurance Federation of California **supports AB 1048.** If you have any questions or concerns regarding the position taken in this letter, please contact Dan Dunmoyer at (916) 442-6646.

cc: Ann Richardson, Deputy Legislative Secretary, Governor's Office
Mike Mattoch, Assembly Insurance Committee
Kevin Hanley, Assembly Republican Caucus