

**STATE COMPENSATION INSURANCE FUND
AUDIT COMMITTEE**

MINUTES OF OPEN SESSION MEETING

February 19, 2014

The Audit Committee met on February 19, 2014 at the State Fund Corporate Office, 333 Bush Street, San Francisco, California.

AGENDA ITEM 1: CALL TO ORDER AND ROLL CALL

The meeting was called to order at 2:05 p.m. and the following Members were present: Sheryl A. Chalupa (Chair); Robin Baker; Jack Neureuter; Steven L. Rank, and William M. Zachry.

There was a quorum.

Also present: Acting President and CEO Carol R. Newman; Acting Chief Financial Officer and Chief Investment Officer Peter Guastamachio; Chief of Internal Affairs Dante Robinson; Board Liaison and Interim Corporate Secretary Hilda B. Padua; and Randall Keen of Manatt, Phelps and Phillips.

AGENDA ITEM 2: ANTITRUST ADMONITION

Ms. Chalupa called attention to and requested confirmation that the Audit Committee members read State Fund's Antitrust Admonition, which is included in each Committee member's meeting materials.

AGENDA ITEM 3: APPROVAL OF NOVEMBER 13, 2013 OPEN MEETING MINUTES

MOTION: Mr. Zachry

SECOND: Mr. Rank

To approve the minutes of the November 13, 2013 Open Meeting of the Audit Committee as presented.

Ms. Chalupa asked for public comment of which there was none, and called for the vote.

YES: 3

NO: 0

Abstain: 2

Motion carried.

Mr. Neureuter and Ms. Baker were not present at the November 2013 Audit meeting and thus did not vote on the approval.

AGENDA ITEM 4: COMPLETED CLOSED AUDITS

Chief of Internal Affairs, Mr. Robinson reported on the completed report on the two closed audits, the Statement of Economic Interests – Form 700 Compliance and Dummy Test Check Copies Incident. He also noted all of the closed audits are correctible in the normal course of business and do not represent significant risk to State Fund. Management has provided their corrective action plans and Internal Audit monitors the completion of the corrective action plans. Closed

issues are validated on a sample basis to ensure management's corrective actions are functioning as intended.

AGENDA ITEM 5: WHISTLEBLOWER HOTLINE

Mr. Robinson reported all Ethics Hotline reports are investigated. Mr. Acker introduced Patrick Gage, Program Manager of Ethics & Labor Relations. During 4Q 2013 there were 60 reports from all sources (Ethics Hotline - 23; Management referral – 4; Privacy – 33).

Management works with Human Resources and the Privacy Office to implement corrective actions and to execute disciplinary action. Management will continue to educate State Fund Workforce of their responsibility for preventing the improper disclosure or use of private/confidential information.

AGENDA ITEM 6: CYBER RISK

Chief Risk Officer Ken Van Laar noted that given the recent events surrounding Target, et. al. the Audit Committee requested an industry perspective of this growing risk. Staying on top of the most recent developments in this area is critical to proper risk mitigation.

Willis Senior Vice President of National Resource E&O and E-risk Chris Keegan provided Willis' outlook on managing cyber risks for financial institutions and other organizations. Mr. Keegan discussed legal and regulatory changes, risk exposure, and loss trends in the new privacy environment. The greatest financial exposure is from disclosure of Personally Identifiable Information (PII). The financial impact of a privacy breach can exceed \$100M. The cost of Cyber insurance has decreased and there is broader coverage with more claims being paid. Insurance is focused on services to decrease risk and address risks.

Mr. Keegan also reported that the number of breaches has increased significantly from 83,870 in 2012 to 383,000 in 2013. Large companies in the Financial area have the greatest number of breaches. The highest incidence of breaches by industry group is Accommodation and Food Services followed by Retail Trade. The potential high cost of a data breach is associated with notification to consumers/employees, credit monitoring costs, costs of restoring data, and public relations. Other major costs associated with a data breach include civil penalties and fines, class action suits, legal costs (defense costs, counsel), and business interruption costs.

Discussion ensued on insurance companies as soft targets for cyber risk. Mr. Keegan noted that large financial institutions are the most secure with large IT departments and funds invested in security, followed by insurance companies, retailers and health care. Mr. Keegan noted that the frequency and severity of cyber breaches has not improved with increased security spending and regulation due to the evolving nature of technology. The National Institute of Standards and Technology (NIST) in Washington DC involved the input of 16 critical industries to develop a Cyber security framework that was released on February 12, 2014. This framework provides a structure that organizations, regulators and customers can use to improve cyber security programs to protect their information from Cyber-attack. It is voluntary and there are no regulations set at this time.

AGENDA ITEM 7 PUBLIC COMMENT ON APPROPRIATENESS OF CLOSED SESSION FOR ITEMS 10 THROUGH 16

Ms. Chalupa requested public comment on the appropriateness of Closed Session Agenda Items 10-16, of which there was none.

AGENDA ITEM 8: PUBLIC COMMENT

Ms. Chalupa requested other public comment, of which there was none. The Audit Committee immediately convened into Closed Session at 2:45 p.m.

AGENDA ITEM 17: CALL TO ORDER AND ROLL CALL

The meeting reconvened at 5:30 p.m. following the conclusion of the Closed Session and the following Members were present: Sheryl A. Chalupa (Chair); Robin Baker; Jack Neureuter; Steven L. Rank, and William M. Zachry.

Also present: Acting President and CEO Carol Newman; Acting Chief Financial Officer and Chief Investment Officer Peter Guastamachio; Chief of Internal Affairs Dante Robinson; Board Liaison and Interim Corporate Secretary Hilda B. Padua; and Randall Keen of Manatt, Phelps and Phillips.

There was a quorum.

AGENDA ITEM 18: COMMITTEE MEMBER PRESENTATIONS

Ms. Chalupa requested presentations from the Committee members of which there were none.

AGENDA ITEM 19: PROPOSALS AND SUGGESTIONS FOR MAY 14, 2014 AGENDA

Ms. Chalupa requested suggestions for agenda items for the May 14, 2014 Audit Committee meeting other than the standing agenda items, of which there were none.

Ms. Chalupa requested public comment, of which there was none, and she noted that the next Audit Committee meeting is scheduled for May 14, 2014 at the State Fund's corporate office, 333 Bush Street, San Francisco, California unless noticed for a new date and time.

ADJOURNMENT

There being no further business before the Audit Committee, the meeting adjourned at 5:35 p.m.

Respectfully submitted,

Hilda B. Padua
Board Liaison and Interim Corporate Secretary