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Date: June 1, 2020

TO: MEMBERS, BOARD OF DIRECTORS

I. AGENDA ITEM # AND TITLE:	Open Agenda Item 5 – Financial Report: 1Q 2020
II. NAME AND PROGRAM:	Vernon Steiner, President and CEO and Peter Guastamachio, Chief Financial Officer
III. ACTIVITY:	<input checked="" type="checkbox"/> Informational <input type="checkbox"/> Request for Direction <input type="checkbox"/> Action Proposed <input type="checkbox"/> Exploratory
IV. JUSTIFICATION:	<input checked="" type="checkbox"/> Standard/Required Item <input type="checkbox"/> Board Request – New Item <input type="checkbox"/> New Topic from Staff

V. EXECUTIVE SUMMARY:

- Net premiums earned of \$228 million were 20.7% lower than prior year because State Fund filed a rate decrease of 10% and reduction of estimated audit premium bills
- Combined ratio of 130.8% was 4.5 points lower than prior year mainly due to losses and loss adjustment expenses (LAE) declining faster than premiums.
- Net income of \$79 million was \$23 million higher than prior year.
- Policyholders' surplus decreased by \$204 million since December 31, 2019, driven by a decrease of \$237 million in unrealized capital gains mainly due to negative impact from the COVID-19 pandemic, a drop in oil prices and a looming recession, partially offset by net income.

VI. ANALYSIS /BACKGROUND:

- Statutory financial results are filed with the California Department of Insurance and the National Association of Insurance Commissioners on a quarterly basis.
- Highlights are also shared with the Board on a quarterly basis.

STATE COMPENSATION INSURANCE FUND
Report on Statutory Financial Results
Three Months Ended March 31, 2020

The following summarizes our statutory financial results for the three months ended March 31, 2020. Our results reflect a decrease in premiums earned and policyholders' surplus.

- Underwriting results
 - Due to the nature of our business, our underwriting results are significantly impacted by the dynamics that affect California business including economic conditions, market pricing as well as the effects of the underwriting cycle.
 - Net premiums earned of \$228 million were 20.7% lower than prior year because State Fund filed a rate decrease of 10% and reduction of estimated audit premium bills of \$45M in March 2020.
 - Loss and loss adjustment expenses (LAE) ratio of 93.2% were 6.6 points lower than prior year. The decrease can be attributed from both industry wide improvements and several internal initiatives to improve claims outcomes, including a sharp focus on reduction in opioids, outcome-based Medical Provider Network launched in 2016, and claims specialization-model launched in 2017 that has led to improved closure rates.
 - Underwriting expense ratio of 37.6% was 2.1 points higher than prior year due to the decline in premiums written.
- The combined ratio of 130.8% was 4.5 points lower than prior year.
- Investment and other non-underwriting results
 - Net investment income of \$ 157 million was \$3 million lower than prior year.
 - Realized capital gains of \$13 million were \$14 million lower than prior year. This is due to the profit we made from stock disposition in the first quarter last year, the same did not repeat this year because of the stock market crash caused by the spread of COVID-19 pandemic, oil price drops and looming recession.
 - Other expenses, mostly representing charge-offs of uncollectible premiums were \$27 million higher in the prior year than this year. The decrease is attributable to the implementation of AB 2883 which resulted in unusually high audited premium billings in 2018, part of which were charged off in 2019.
- Net income and policyholders' surplus
 - Net income of \$79 million was \$23 million higher than the prior year mainly due to the \$27 million decrease in charge-offs of uncollectible premiums this year.
 - Policyholders' Surplus went down by \$204 million since December 31, 2019. This is due to the significant decrease of \$237 million in unrealized capital gains as a result of COVID-19 pandemic, oil price drops and a looming recession, reclassification of \$42 million of restricted surplus to recognize State Fund's share of Other Post Employment Benefit (OPEB), and a decrease in non-admitted assets, offset by the net income of \$79 million.

STATE COMPENSATION INSURANCE FUND
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Three Months Ended March 31, 2020

Financial Results (\$ millions)	2019 Actual	2020 Actual	Actual vs. Prior Year \$ Diff	Actual vs. Prior Year % Diff
Net premiums earned (NPE)	288	228	(60)	-20.7%
Losses	201	160	(42)	-20.7%
Loss adjustment expenses (LAE)	86	53	(33)	-38.3%
Underwriting (UW) expenses	104	106	2	2.2%
Underwriting results	(103)	(90)	13	12.3%
Net investment income	160	157	(3)	-1.6%
Realized capital gain (loss)	27	13	(14)	-52.9%
Other income (expense)	(27)	(0)	27	99.4%
Income before dividends to policyholders	56	79	23	41.1%
Dividends to policyholders (credits)	0	(0)	(0)	n/a
Net income (loss)	56	79	23	41.1%
Standard Industry Ratios				
Loss ratio	70.0%	70.0%		-
LAE ratio	29.8%	23.2%		-6.6%
Loss and LAE ratio	99.8%	93.2%		-6.6%
UW expense ratio	35.5%	37.6%		2.1%
Combined ratio	135.3%	130.8%		-4.5%

Numbers or ratios may not foot due to rounding.

Dash (-) represents a null value.

Zero (0) represents a calculated zero or number which rounds to zero

Green represents better than plan and prior year.

Red represents worse than plan and prior year.