

**STATE COMPENSATION INSURANCE FUND
BOARD OF DIRECTORS**

MINUTES OF OPEN SESSION MEETING

August 15 and 17, 2018

The Board of Directors of the State Compensation Insurance Fund met on August 15, 2018 at the State Fund San Francisco Office, 333 Bush Street (Board room), and on August 17, 2018 at the Omni Hotel, 500 California Street (Union Square room), San Francisco, California.

August 15, 2018

The Board of Directors of the State Compensation Insurance Fund met on August 15, 2018 at the State Fund San Francisco Office, 333 Bush Street (Board room).

AGENDA ITEM 1: CALL TO ORDER AND ROLL CALL

The meeting was called to order at 1:40 p.m.

Ms. Chalupa requested Ms. Padua to call roll. The following were present: Sheryl A. Chalupa (Chair); Robin L. Baker; Marvin P. Kropke; Sen. Michael J. Machado (Ret.); Lawrence E. Mulryan; Jack L. Neureuter; Steven L. Rank; Thomas E. Rankin; Scott K. Reid; William M. Zachry; and David Lanier (non-voting member).

Absent by prior arrangement: Daniel M. Curtin.

There was a quorum.

Also present: President and CEO Vernon L. Steiner; General Counsel and Corporate Secretary Margie R. Lariviere; Chief Financial Officer Peter Guastamachio; Board Liaison and Assistant Corporate Secretary Hilda B. Padua; and Counsel and Assistant Corporate Secretary Judith D. Sapper.

AGENDA ITEM 2: ANTITRUST ADMONITION

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

AGENDA ITEM 3: CONSENT CALENDAR

- 3a. Approval of May 24-25, 2018 Open Meeting Minutes**
- 3b. Board Member Educational Opportunities and Approval of Planned Board Member Education and Expense Reimbursement**
- 3c. Authorization to Secure Renewal of the Property and Casualty Insurance Program**
- 3d. Approval of Investment Policy Statement and Guidelines**
- 3e. Approval of Retirement Resolutions**
- 3f. Ratification of President's Deferred Compensation Plan**

Ms. Chalupa asked whether any Board member had any other comments on the items on the Consent Calendar of which there were none. Ms. Chalupa called for a Motion.

MOTION: Mr. Zachry

SECOND: Mr. Kropke

To approve the Consent Calendar as presented.

Ms. Chalupa requested public comment of which there was none. Ms. Chalupa called for the vote.

YES: 10

NO: 0

Abstain: 0

Motion carried.

AGENDA ITEM 4: STAFFING UPDATE

Executive Vice President and Chief Administrative Officer Andreas Acker presented an update on staffing. Mr. Acker reported that State Fund ended the second quarter of 2018 with 4,324 employees, 111 separations, 147 new hires, and 322 promotions. Of the 111 separations, 52 or 46.8% were retirements, 26 were resignations, 19 were transfers, and 14 were others (death or dismissal). The overall separation rate for the second quarter of 2018 was 2.6% and the primary driver was retirements. By the end of the year, the employee headcount will be smaller and the number of retirements will increase.

Mr. Acker reported as of June 30, 2018 there was a decrease of 13% in the number of hours over the 640 hour cap and a 5% decrease in the number of employees over the cap. The key driver for the decreased number of leave hours over the 640 cap is the cash-out of 60,000 leave hours offered by the State of California in June 2018. It is anticipated that leave hours will further decrease as employees continue to take vacation through the summer months and during the holidays in the fourth quarter.

Ms. Chalupa requested public comment, of which there was none.

AGENDA ITEM 5: FINANCIAL UPDATE – 2ND QUARTER 2018

Chief Financial Officer Peter Guastamachio reported on the 2Q 2018 financial results.

Premiums

The past two years, State Fund continued to see a decline in new and renewal business. However, this quarter State Fund started to see an uptick in the new business. The Estimated Annual Premium (EAP) in new business was \$114M for the first half of the year versus \$112M last year and the EAP on renewal business was \$481M, down from \$512M last year, which is attributed to a filed rate decrease of 8% in September 2017. As for the net premiums earned, it was up slightly at \$694M versus \$692M last year, mainly due to increased capacity to do audits. The audited premium was \$157M this year versus \$59M last year. This year, State Fund wrote about 63,000 policies, which was 4.7% lower than the prior year. State Fund has about 108,000 policies-in-force or 4.4% less than prior year (113,000).

Losses and Loss Adjustment Expense (LAE)

State Fund had \$499M in Losses and an LAE of \$189M this year versus \$512M and \$184M from the prior year. For the 2Q 2018, the Loss and LAE ratios were 72% and 27.3% and overall combined Loss and Loss Adjustment Expense Ratio of 99.3% was 1.3 points lower than the prior year.

The underwriting expense ratio of 33.2% was 1.7 points higher than the same period last year. The Underwriting expenses were up by \$10M from last year primarily from increases in salary and benefits.

The combined ratio for 2Q 2018 was 132.5%, and underwriting loss was \$224M. The combined ratio and underwriting loss for the same period last year were 132.1% and \$223M. Offsetting the underwriting loss, net investment income was \$310M plus realized gains of \$15M. Overall this resulted in net income of \$72M, which was \$94M lower than the last year. The policyholders' surplus grew by \$38M since year-end.

Ms. Chalupa requested public comment, of which there was none.

AGENDA ITEM 6: PRESIDENT'S REPORT

President and CEO Vernon Steiner provided the following updates:

The California insurance market continues to be soft with insurance carriers filing for further rate decreases. California employers continue to have ongoing savings as carriers are charging rates lower than what was filed by the Workers' Compensation Rating Bureau (WCIRB). The WCIRB proposes another rate decrease for January 1, 2019.

Mr. Steiner noted that the driver behind the increase in new business and stabilization is that State Fund is engaging the market in a way that embraces the purpose of State Fund. State Fund is here to be helpful and to serve Californians and be the California workers' compensation carrier of choice. The strategy is to continue to deliver helpful services to policyholders, charge a fair price for coverage, and position State Fund in preparation for an inevitable market change.

Claims restructuring took place with One Process and through resolution specialization, investigations, and disability management the number of legacy claims decreased in the first half of this year. In 2000, State Fund grew tremendously within a short period of time. As a result, 40% of open inventory were claims from 2002-2008. Since 2017, Claims achieved a 15.8% reduction of open inventory for legacy claims with a 10.5% reduction in the first half of 2018. Currently, legacy claims dated 2002-2005 account for 24% of open inventory. There have been 6,231 closed claims with 12% of all closures being legacy claims. The reduction in inventory will free up resources to handle incoming claims and State Fund will not need to add staff if it has to increase market share.

Lastly, Mr. Steiner reported that there was good feedback from employees at the Town Hall meeting in Redding. Mr. Steiner, Mr. Hunckler and Mr. Acker visited the 150 employees in Redding after the wildfire. About 50 of those employees had to evacuate their homes during the fire and one employee lost her home. State Fund managers opened up the office in case evacuees needed a place to stay. Although none of the employees ended up staying at the office it was important that the consideration and care for State employees was there. Mr. Steiner stated that the only way to be of service to California is to create an environment where employees feel valued and in turn they can make customers feel valued.

AGENDA ITEM 7: REPORTS BY THE CHAIRS OF COMMITTEE ACTIVITIES

7a: GOVERNANCE COMMITTEE

7ai: GOVERNANCE, COMPLIANCE AND PRIVACY UPDATE

Governance Chair Mr. Mulryan reported on the following:

New Legislation – AB 375 (Chau and Hertzberg) – California Consumer Privacy Act of 2018

Effective January 1, 2020, the bill provides consumers with additional privacy rights to access, delete, and make opt-in and opt-out choices about use of their personal information (PI). There is a limited private right of action against a business to recover damages from \$100 to \$750 per incident and seek injunctive, declaratory, or other relief for a data breach.

The bill requires businesses to inform consumers about the use of PI, disclose if it will be sold, and prohibit specific uses without consumer notice. It also prohibits businesses from discriminating against consumers for exercising their rights under the bill.

State Fund does not meet the definition of a business as outlined in the statute. State Fund may choose to comply with the requirements of the statute.

2018 Corporate Governance Annual Disclosure (CGAD)

The confidential CGAD provides information about governance activities at State Fund. State Fund submitted its annual CGAD report, attested by the CEO and General Counsel/Corporate Secretary, to the California Department of Insurance on May 29, 2018. Reports are due annually by June 1.

2018 Biennial Insurer Supplier Diversity Survey

California admitted insurers with premiums in California of \$100 million or more must report biennially to the Department of Insurance about their efforts to obtain services from diverse suppliers. Insurer surveys are public information. State Fund submitted its *Supplier Diversity Survey* to the Department of Insurance on June 30, 2018 as required. State Fund's diverse spend was 12.24% during the reporting period, spread amongst 23 unique suppliers.

California Whistleblower Protection Act Annual Notification

The annual Whistleblower communication and brochure about the State Auditor's Whistleblower Program was sent by email to all employees on July 11, 2018. The 2018 whistleblower posters were displayed in State Fund locations where other employee notices are maintained. Attestation of distribution was sent to the State Auditor on July 13, 2018.

Ethics and Privacy Reported Issues

The total number of hotline reports increased by 27% (22 Q2 vs. 16 Q1). There was a slight decline in hotline reporting in Q1 because of the new hotline vendor. In Q2, State Fund employees became more aware of the new hotline and reporting increased. Compared to the first half of last year, the total number of hotline reports increased by 21% (242 in 2017 to 306 in 2018).

Human Resources-related issues continue to be the most reported category. For Q2 2018, HR issues represent 65% of total incidents; 35% of incidents include privacy incidents, falsifying records, issues related to corporate policies and procedures, and claims, policy and legal practices.

7b: AUDIT COMMITTEE

7bi: UPDATE ON COMPLETED CLOSED AUDITS

Audit Chair Mr. Reid reported on the following activities:

Completed Closed Audits

Mr. Reid reported that eight projects were reported in the first quarter of 2018 in the Closed Session in May 2018. There are no non-proprietary projects to report in Open Session.

In addition, Mr. Reid reported that the California Department of Insurance (CDI) completed its financial examination of State Compensation Insurance Fund's financial statements for the period January 1, 2013 through December 31 2016. There were no adjustments made to the financial statements as a result of the examination. The final report was published on April 20, 2018.

7c: INVESTMENT and RISK COMMITTEE

7ci: BOND TRANSACTIONS AND COMPLIANCE REPORT

Investment Chair Senator Machado (Ret.) reported on the following:

Sen. Machado reported that the Investment and Risk Committee received an update on the status of State Fund's Information Security Plan. State Fund exceeds the industry's security best practices as far as the plan to address its security gap analysis and developing an overarching plan for security.

Sen. Machado proudly announced that Chief Investment Officer Stephanie Chan has passed the second of three Chartered Financial Analyst Exams, measuring knowledge of ethical and professional standards, investment tools, asset classes and portfolio management.

The investment transactions and compliance reports for the periods of April 1, 2018 to June 30, 2018 were approved by the Investment & Risk Committee pursuant to its delegated authority. Sen. Machado also reported the Investment & Risk Committee heard a report from staff on portfolio performance.

7d: AD HOC SAFETY AND LOSS PREVENTION COMMITTEE

Chair Robin Baker reported that the Ad Hoc Safety and Loss Prevention Committee has been working with staff to develop an enhanced plan for loss prevention activities which will be presented to the Board at the Strategic meeting in Closed Session.

AGENDA ITEM 8: CHAIRWOMAN'S REPORT

Ms. Chalupa reported that she attended President Steiner's Town Hall meetings at the State Fund Bakersfield office July 12, 2018. The discussion included overviews of market and pricing trends, the roles of reserves and surplus, combined ratio and expense ratio, and North Star progress. In addition to the discussion topics, both groups had good questions on a variety of subjects, and Ms. Chalupa was encouraged by the amount of participation and engagement. In the afternoon after the Town Hall, a group of executives hosted an ice cream social and served ice cream to all employees.

AGENDA ITEM 9: BOARD MEMBER REPORTS

Ms. Chalupa requested any Board member reports, of which there were none.

AGENDA ITEM 10: PUBLIC COMMENT ON APPROPRIATENESS OF CLOSED SESSION FOR ITEMS 13 THROUGH 20

Ms. Chalupa requested public comment on the appropriateness of Closed Session for agenda items 13 through 20, of which there was none.

AGENDA ITEM 11: PUBLIC COMMENT

Ms. Chalupa requested public comment, of which there was none.

ADJOURNMENT

There being no further business, Ms. Chalupa adjourned the meeting at 2:05 p.m. to immediately reconvene in Closed Session.

August 17, 2018

AGENDA ITEM 21: CALL TO ORDER AND ROLL CALL

The meeting reconvened at 10:40 a.m. at the Omni Hotel, 500 California Street (Union Square room), San Francisco, California following the conclusion of the Board Closed Session and the following Members were present: Sheryl A. Chalupa (Chair); Robin L. Baker; Sen. Michael J. Machado (Ret.); Lawrence E. Mulryan; Jack L. Neureuter; Steven L. Rank; Scott K. Reid; William Zachry; and David Lanier (non-voting member).

Absent by prior arrangement: Daniel M. Curtin and Marvin P. Kropke.

There was a quorum.

Also present: President and CEO Vernon L. Steiner; General Counsel and Corporate Secretary Margie R. Lariviere; Chief Financial Officer Peter Guastamachio; Board Liaison and Assistant Corporate Secretary Hilda B. Padua; and Counsel and Assistant Corporate Secretary Judith D. Sapper.

AGENDA ITEM 22: APPROVAL OF EXECUTIVE COMPENSATION AND LONG-TERM INCENTIVE PLAN

RESOLUTION No. 2171 - APPROVING INTERIM INCREASE TO 2018 COMPENSATION OF THE CHIEF INVESTMENT OFFICER

Ms. Chalupa reported that Stephanie K. Chan, the Chief Investment Officer, is working toward her credential as a Chartered Financial Analyst. This is the highest distinction in the investment management profession and a globally recognized standard for measuring the competence and integrity of financial analysts. Ms. Chalupa proudly announced that Ms. Chan has passed the second of three Chartered Financial Analyst Exams, measuring knowledge of ethical and professional standards, investment tools, asset classes and portfolio management.

In recognition of Ms. Chan's achievement the Board requested to increase Ms. Chan's 2018 base salary.

Ms. Chalupa noted that copies of Resolution No. 2171 are available at the front table outside.

Ms. Chalupa requested a Motion and Second.

MOTION: Sen. Machado

SECOND: Mr. Zachry

To approve the Interim Increase to 2018 Compensation of the Chief Investment Officer to \$175,000.

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

YES: 9

NO: 0

Abstain: 0

Resolution carried.

Mr. Kropke had left the meeting before the vote was taken and Mr. Curtin was absent.

The certified Resolution No. 2171 is attached hereto.

RESOLUTION No. 2170 - APPROVAL OF LONG-TERM INCENTIVE PLAN (LTIP) FOR EXEMPT EMPLOYEES AND CAREER EXECUTIVE ASSIGNMENT POSITIONS

Ms. Chalupa noted that as discussed at the May 2018 meeting, the Board decided to establish President Vern Steiner's long-term and deferred compensation options before addressing a Long-Term Incentive Program (LTIP) for the executives and selected leaders. The Board requested Mr. Steiner to present the new LTIP at the August 2018 Board meeting. This LTIP is intended to assist State Fund in attracting, retaining and motivating leadership talent and to provide competitive pay opportunities for management employees. The LTIP recognizes these key employees for their performance, accomplishments, and meaningful contributions over multiple years to the efficiency, productivity, and financial performance of State Fund and the achievement of its long-term strategic objectives.

Ms. Chalupa noted that the LTIP will have an effective date of January 1, 2018. The Board of Directors will establish the performance measures and set the performance targets each year and any award payouts will occur over a three-year period.

Ms. Chalupa noted that copies of Resolution No. 2170 are available at the front table outside.

Ms. Chalupa requested a Motion and Second.

MOTION: Mr. Mulryan

SECOND: Mr. Rankin

To approve the Long-Term Incentive Plan for Exempt Employees and Career Executive Assignment Positions, Resolution No. 2170 as presented.

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

YES: 9

NO: 0

Abstain: 0

Resolution carried.

Mr. Kropke had left the meeting before the vote was taken and Mr. Curtin was absent.

The certified Resolution No. 2170 is attached hereto.

AGENDA ITEM 23: PROPOSALS AND SUGGESTIONS FOR NOVEMBER 15-16, 2018
AGENDA

Ms. Chalupa requested suggestions for agenda items for the November 15-16, 2018 Board meeting. Ms. Padua noted that the proposed agenda items are for Closed Session.

Ms. Chalupa requested public comment, of which there was none, and she noted that the next Board meeting is scheduled for November 15-16, 2018 at the State Compensation Insurance Fund Office, Pleasanton, California unless noticed for a new date and time.

Ms. Chalupa adjourned the meeting at 10:45 a.m.

Respectfully submitted,

Hilda B. Padua
Board Liaison and Assistant Corporate Secretary



**RESOLUTION APPROVING INTERIM INCREASE TO 2018
COMPENSATION OF THE CHIEF INVESTMENT OFFICER**

WHEREAS, Insurance Code section 11785(a) authorizes the Board of Directors (“Board”) of State Compensation Insurance Fund to appoint and set the salary for certain exempt officer positions including a Chief Investment Officer; and

WHEREAS, the Board approved the appointment of Stephanie K. Chan to serve as the Chief Investment Officer effective April 1, 2018 at a base annual salary of \$150,000; and

WHEREAS, the State Fund Board of Directors is vested with full power, authority and jurisdiction over State Fund and may perform all acts necessary or convenient in the exercise of any power, authority or jurisdiction over State Fund, as fully and completely as the governing body of a private insurance carrier; and

WHEREAS, Stephanie K. Chan, the Chief Investment Officer, is working toward her credential as a Chartered Financial Analyst, the highest distinction in the investment management profession and a globally recognized standard for measuring the competence and integrity of financial analysts, and has passed the second of three Chartered Financial Analyst Exams, measuring knowledge of ethical and professional standards, investment tools, asset classes and portfolio management; and

WHEREAS, in recognition of Stephanie K. Chan’s achievement the Board seeks to increase her 2018 base salary.

NOW, THEREFORE,

IT IS RESOLVED, that the Board of Directors hereby approves a \$25,000 increase in the base annual salary for Stephanie K. Chan for a base annual salary of \$175,000 effective as of September 1, 2018.

PASSED AND ADOPTED at the meeting of the Board of Directors of the State Compensation Insurance Fund held on this 17th day of August, 2018 by the following vote:

State Compensation Insurance Fund
Board of Directors – August 17, 2018
Open Agenda Item 22 –Executive Compensation—Approval of Interim Increase in Compensation of Chief Investment Officer (Resolution)

PASSED AND ADOPTED at the meeting of the Board of Directors of the State Compensation Insurance Fund held on this 17th day of August, 2018 by the following vote:

<u>MEMBER</u>	<u>VOTE</u>
Sheryl A. Chalupa, Chair	Yes
Robin L. Baker	Yes
Daniel M. Curtin	Absent
Marvin P. Kropke	Not present
Sen. Michael J. Machado (Ret.)	Yes
Lawrence E. Mulryan	Yes
Jack L. Neureuter	Yes
Steven L. Rank	Yes
Thomas E. Rankin	Yes
Scott K. Reid	Yes
William M. Zachry	Yes

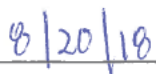
BOARD of DIRECTORS of the STATE COMPENSATION INSURANCE FUND

Certification by Assistant Corporate Secretary

I, Hilda B. Padua, Assistant Corporate Secretary for the State Compensation Insurance Fund Board of Directors, hereby certify that the foregoing resolution was adopted by the Board of Directors at their regular meeting held August 17, 2018.



Hilda B. Padua, Assistant Corporate Secretary



Date



BOARD OF DIRECTORS

STATE COMPENSATION INSURANCE FUND

**RESOLUTION REGARDING LONG-TERM INCENTIVE PLAN FOR
EXEMPT EMPLOYEES AND CAREER EXECUTIVE ASSIGNMENT POSITIONS**

WHEREAS, the State Fund Board of Directors is vested with full power, authority and jurisdiction over State Fund and may perform all acts necessary or convenient in the exercise of any power, authority or jurisdiction over State Fund, as fully and completely as the governing body of a private insurance carrier; and

WHEREAS, the Board of Directors is vested with the authority to appoint and establish the compensation for exempt employees pursuant to California Insurance Code section 11785; and

WHEREAS, pursuant to Insurance Code section 11873, State Fund is not subject to Government Code section 19823, which authorizes the rewards programs established by the State of California for state employees; and

WHEREAS, private insurance carriers utilize long-term incentive programs to attract and retain executive employees; and

WHEREAS, the Board of Directors has approved a long-term incentive plan for the President and CEO; and

WHEREAS, a long-term incentive plan for exempt employees and certain Career Executive Assignment positions would provide State Fund with additional ability to attract and retain superior management and executive level employees, and provide an incentive to those employees to actively promote and further State Fund's strategic plans and objectives.

NOW, THEREFORE,

IT IS RESOLVED that the Board hereby approves and adopts the establishment of the Long-Term Incentive Program for the exempt employees appointed pursuant to California Insurance Code section 11785 and certain Career Executive Assignment Positions, with an effective date of January 1, 2018.

IT IS FURTHER RESOLVED that the Long-Term Incentive Program shall provide the Board with the discretion to establish annual target awards, if any, and the annual award pool, if any; that award payouts shall occur over a three-year period; and that awards shall be based on individual and/or enterprise performance goals; and

IT IS FURTHER RESOLVED that awards provided through the Long-Term Incentive Program shall not be considered compensation for calculation of retirement or benefits; and

IT IS FURTHER RESOLVED that the President of State Fund is hereby granted the authority to take all actions necessary, including the establishment of any necessary policies and procedures, to implement the Long-Term Incentive Program pursuant to this resolution; and

IT IS FURTHER RESOLVED that the Board hereby adopts and approves a 10% target award for 2018 for each eligible employee.


PASSED AND ADOPTED at the meeting of the Board of Directors of the State Compensation Insurance Fund held on this 17th day of August, 2018 by the following vote:

<u>MEMBER</u>	<u>VOTE</u>
Sheryl A. Chalupa, Chair	Yes
Robin L. Baker	Yes
Daniel M. Curtin	Absent
Marvin P. Kropke	Not present
Sen. Michael J. Machado (Ret.)	Yes
Lawrence E. Mulryan	Yes
Jack L. Neureuter	Yes
Steven L. Rank	Yes
Thomas E. Rankin	Yes
Scott K. Reid	Yes
William M. Zachry	Yes


BOARD of DIRECTORS of the STATE COMPENSATION INSURANCE FUND

Certification by the Assistant Corporate Secretary

I, Hilda B. Padua, Assistant Corporate Secretary for the State Compensation Insurance Fund Board of Directors, hereby certify that the foregoing resolution was adopted by the Board of Directors at their regular meeting held August 17, 2018.



Hilda B. Padua, Assistant Corporate Secretary



Date

State Compensation Insurance Fund
Board of Directors – August 17, 2018
Open Agenda Item 22 – Approval of Executive Compensation and Long-Term Incentive Plan (Resolution)