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Date: May 5, 2017

**TO: MEMBERS, BOARD OF DIRECTORS**

<b>I. AGENDA ITEM # AND TITLE :</b>	Open Agenda Item 5 – Financial Update: 1 <sup>st</sup> Quarter 2017
<b>II. NAME AND PROGRAM:</b>	Peter Guastamachio, Chief Financial Officer
<b>III. ACTIVITY:</b>	<input checked="" type="checkbox"/> Informational <input type="checkbox"/> Request for Direction <input type="checkbox"/> Action Proposed <input type="checkbox"/> Exploratory
<b>IV. JUSTIFICATION:</b>	<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 \$354 million were 3.7% less than the prior year.
- Combined ratio of 132.6% was higher than the same period last year which resulted in underwriting loss of \$116 million.
- Net income of \$127 million was \$60 million more than the same period in the prior year.
- Policyholders’ surplus grew by \$57 million since December 31, 2016.

**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 shared with the Board of Directors on a quarterly basis.

**STATE COMPENSATION INSURANCE FUND**  
**Report on Statutory Financial Results**  
**Three Months Ended March 31, 2017**

The following summarizes our statutory financial results for the three months ended March 31, 2017. Our results reflect a slight decline in premiums earned and continued growth in 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, unemployment, market pricing as well as the effects of the insurance profitability cycle.
  - Net premiums earned of \$354 million were 3.7% lower than the prior year.
  - Our loss and loss adjustment expenses (LAE) ratio of 100.6% were 6 points lower than prior year.
  - Underwriting expense ratio of 32.0% was 10 points higher than the same period last year.
  - Combined ratio of 132.6% was 4 points higher than the same period last year due to the net effect of the increase in our underwriting expense ratio and decrease in our LAE ratio. With the enhanced capabilities of tracking expenses at more granular level, State Fund improved its insurance functional allocation methodology effective beginning of the year which resulted to shifting expenses from LAE to Underwriting.
- Investment and other non-underwriting results
  - Net investment income of \$159 million was \$3 million lower than the same period in prior year.
  - Realized capital gains of \$93 million were \$71 million higher than the same period in prior year. This is the result of the liquidation of holdings from the termination of an equity portfolio manager.
  - Other expenses, mostly representing charge-offs of uncollectible premiums, were \$4 million higher than the same period in the prior year.
- Net income and policyholders' surplus
  - Net income of \$127 million was \$60 million higher than the same period in the prior year mainly due to realized capital gains from liquidation of equity holdings.
  - Policyholders' surplus grew by \$57 million since December 31, 2016.

**STATE COMPENSATION INSURANCE FUND**  
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**Three Months Ended March 31, 2017**

Financial Results (\$ millions)	2016 Actual	2016 Actual Proforma*	2017 Actual	Actual vs. Prior Year \$ Diff	Actual vs. Prior Year % Diff
Net premiums earned (NPE)	368	368	354	(13)	-3.7%
Losses	272	272	262	(10)	-3.7%
Loss adjustment expenses	119	94	94	(25)	-20.7%
UW expenses	88	110	114	26	29.5%
Underwriting results	(111)	(109)	(116)	(5)	-4.4%
Net investment income	162	160	159	(3)	-1.8%
Realized capital gain (loss)	21	21	93	71	332.9%
Other income (expense)	(5)	(5)	(9)	(4)	-90.3%
Income before dividends to policyholders	67	67	127	60	88.2%
Dividends to policyholders (credits)	-	-	0	0	n/a
Net income (loss)	67	67	127	60	88.2%
<b>Standard Industry Ratios</b>					
Loss ratio	74.0%	74.0%	74.0%		0.0%
LAE ratio	32.3%	25.6%	26.6%		-5.7%
Loss and LAE ratio	106.3%	99.6%	100.6%		-5.7%
UW expense ratio	22.3%	28.0%	32.0%		9.7%
Combined ratio	128.6%	127.6%	132.6%		4.0%

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 prior year.

Red represents worse than prior year.

\* New insurance functional allocation methodology applied