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Date: May 20, 2010

AGENDA ITEM 11

TO: MEMBERS OF THE GOVERNANCE COMMITTEE

FROM: Carol R. Newman, General Counsel

I. Subject: Charter Amendments for Audit and Governance Committee

II. Program: Corporate Secretary

III. Analysis

Attached is the Enterprise Risk Management Resolution that the Board of Directors passed at their March 19, 2010 Board meeting and to be adopted unless amended as part of the Minutes during the May 19, 2010 Board meeting. Based on this resolution, the proposed Governance and Audit Committee Charters have been amended to reflect the Committees respective roles for Enterprise Risk Management. In addition, the Audit Committee will be evaluating their Charter as it aligns with the Governance Committee Charter.

GOVERNANCE COMMITTEE MEETING (OPEN)

AGENDA ITEM 11

ATTACHMENT 11-I

AMENDMENT to GOVERNANCE and AUDIT COMMITTEE CHARTERS

PRESENTED BY: Jeanne Cain and Carol Newman

May 20, 2010

RESOLUTION APPROVING AMENDMENT of CHARTERS of
STATE COMPENSATION INSURANCE FUND
BOARD OF DIRECTORS
AUDIT and GOVERNANCE COMMITTEES in accordance with
ENTERPRISE RISK MANAGEMENT BEST PRACTICE

WHEREAS, Enterprise Risk Management (“ERM”) is an emerging best practice in the insurance industry; and

WHEREAS, one of State Fund’s exempt positions is a Chief Risk Officer whose duties include a focus on ERM; and

WHEREAS, State Fund has established a Risk Committee whose mission includes a focus on ERM; and

WHEREAS, Governance Committee discussions have identified the importance of each Board committee developing different perspectives; and

WHEREAS, it is appropriate for the Governance Committee to have oversight on the identification of key risks, the likelihood and impact of those risks if they would occur, and mitigation plans for those risks; and

WHEREAS, it is appropriate for the Audit Committee to have oversight of testing of the processes and controls in place to mitigate risk;

Now therefore, be it RESOLVED:

State Fund management is directed to work with the chair of the Audit Committee and the chair of the Governance Committee to amend the charters of those committees to include ERM within those committees’ Mission/Purpose and Duties and Responsibilities, consistent with the Board’s findings above.

I, Carol R. Newman, Corporate Secretary for 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 March 19, 2010.

Carol R. Newman, Corporate Secretary

Date

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**STATE COMPENSATION INSURANCE FUND
Corporate Governance Committee Charter
(Amended May 20, 2010)**

Mission/Purpose

The Governance Committee (the "Committee") shall assist the Board of Directors (the "Board") of State Compensation Insurance Fund ("State Fund") in shaping corporate governance policies and practices including (1) overseeing that State Fund operates in a legal, ethical, and socially responsible manner; (2) overseeing Enterprise Risk Management ("ERM") issues which may have a material impact on State Fund; (3) advising and updating the Board on corporate governance trends and issues within the industry; (4) recommending to the Board, Corporate Governance Guidelines (the "Guidelines") which, along with State Fund's By-laws, State Fund's Code of Business Conduct and Ethics ("Code of Ethics"), the charters of the various Board committees, Insurance Code Section 11770 et seq., as amended pursuant to AB 1874, and Government Code Sections 6251 et seq. (Public Records Act) and 11120 et seq. (Bagley-Keene Open Meeting Act), provide the framework for the governance of State Fund; and (5) monitoring and evaluating State Fund's compliance with the Guidelines.

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Organization

The Committee is a standing committee of the Board composed of not less than three (3) Directors and shall include a Chair of the Committee who shall serve until resignation, removal or a successor has been appointed pursuant to the provisions of State Fund's By-laws.

Meetings

The Committee shall hold regular meetings in accordance with the provisions of the Bagley-Keene Open Meeting Act ("Bagley-Keene") and no less than four times a year. The Committee shall hold regular meetings on the same day as, or within one day of, the regular meetings of the Board. The Committee may hold additional meetings at the request of any Committee member, in compliance with the provisions of Bagley-Keene and State Fund's By-laws.

- a. The Committee may, at its discretion, invite members of management and/or other Directors to attend the Committee's meetings where necessary to further the business of the Committee. Notwithstanding the foregoing, the total number of members of the Board (including Committee members) attending the Committee's meeting at any one time shall not equal or exceed a majority of the number of members of the Board.

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- b. Unless the Committee determines otherwise, the Committee shall hold a closed session at each regularly scheduled meeting. During a portion of this closed session, the President or the General Counsel, or both, will be present. Closed sessions of the Committee may be held at any meeting pursuant to the provisions of Bagley-Keene and California Government Code section 11120 et seq., as may be amended.
- c. A majority of the Committee shall constitute a quorum. Each member of the Committee will have one vote and actions at the meeting shall be approved by a majority of the members present.
- d. Minutes shall be prepared at each meeting and filed with the minutes of State Fund's Board.
- e. The Committee Chairperson or the Chair's designee shall give a full report on the Committee's actions at the earliest scheduled Board meeting.

Duties and Responsibilities

In discharging its duties and responsibilities to shape corporate governance policies and practices, the Committee shall:

1. **Oversee**

- a. Oversee that State Fund operates in a legal, ethical, and socially responsible manner and that all directors, officers, and employees support State Fund's Code of Business Conduct and Ethics which is designed to promote (1) honest and ethical conduct; (2) full, fair, accurate, timely, and understandable disclosures in the periodic reports required to be filed by State Fund; and (3) compliance with applicable laws, rules, and regulations.
- b. Oversee the orientation and continuing education of the members of the Board. In this regard, the Committee shall, from time to time, recommend educational programs for the full Board, any Committee or any individual Director as the Committee may determine is necessary or appropriate.
- c. Assist in developing criteria for the assessment of the performance of the Board and management and take the lead in overseeing the evaluation of the Board and State Fund's management on no less than an annual basis.
- d. Oversee the Enterprise Portfolio Management Office's ("EPMO") material projects recommended by State Fund's management which relate to corporate governance.
- e. Work with State Fund's Chief Risk Officer and Risk Committee in overseeing the identification, assessment, and where appropriate, the development of mitigation plans for risks within State Fund.

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2. Recommend

- a. Recommend to the Board, director nominees for appointment to the Committee or any sub-committee in compliance with the procedures outlined in State Fund's By-laws.
- b. Recommend the establishment, charter, and membership of the various committees of the Board.
- c. Recommend corporate governance guidelines for State Fund.
- d. Recommend appropriate changes to corporate governance documents such as by-laws, Code of Ethics, and as requested, the charters of the other committees' charters.
- e. Review the qualifications of members suggested to be Chairperson, and Directors of the Board, and make recommendations to the appointing authority concerning these members.
- f. Recommend changes to the charters of other State Fund Board committees.
- g. On an ad hoc basis and upon the request of the Board, a review of specific operational segments of State Fund that may pose unusual, significant risks that could have a material impact on the risk profile of State Fund.

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3. Advise

- a. Advise the Board on matters related to governance as deemed appropriate by the Board.
- b. Advise the Board on corporate governance trends and issues within the industry.
- c. Advise the Board with respect to Board procedures including the frequency and structure of the Board meetings.
- d. Advise the Board on qualifications for leadership positions within State Fund.
- e. Advise and assist the Board in its responsibilities relating to succession planning, particularly with respect to the President and Chief Operating Officer and other identified executive positions.

4. Evaluate

- a. Conduct a self-evaluation, on an annual basis, of the performance of the Committee and deliver to the Board a written report setting forth the results of its evaluation which shall be discussed with the full Board and acted upon as appropriate.
- b. Evaluate, at least annually, the overall performance of the Board as a whole and in consultation with all Board members, conduct an assessment of individual Board members.
- c. Evaluate on an annual basis whether the committees of the Board are functioning effectively and within the guidelines as set forth in their respective charters.
- d. Evaluate, at least annually, the quality, sufficiency and currency of information furnished by management to the Directors in connection with Board and committee meetings and other activities of the Directors.

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Powers

The Committee shall have the following powers:

- a. To obtain advice and assistance from internal or external legal, accounting or other advisors and to have direct access to advisors without the presence of any officer of State Fund.
- b. To interview and meet with any employee of State Fund without the presence of any officer of State Fund.
- c. To form and delegate authority to subcommittees.
- d. To amend or repeal the Charter or any provisions of the Charter as appropriate due to new laws or regulations and recommend any changes to the Board.
- e. Such other powers as may be necessary and appropriate to fulfill the Committee's purposes.
- f. To perform such other functions as assigned by State Fund's charter, bylaws, or the Board.

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**STATE COMPENSATION INSURANCE FUND
Audit Committee Charter
(Amended May 20, 2010)**

Mission/Purpose

The Audit Committee (the "Committee") shall assist the Board of Directors (the "Board") of State Compensation Insurance Fund ("State Fund") in fulfilling its responsibility for oversight of (1) the quality and integrity of State Fund's accounting, auditing and financial reporting practices and the management of State Fund's financial risks; (2) the independent public accounting firm's qualifications, performance, and independence; (3) the performance of State Fund's internal audit function; (4) State Fund's compliance with legal, ethical and regulatory requirements; and (5) evaluating the effectiveness of State Fund's Enterprise Risk Management ("ERM") initiatives.

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Organization

The Committee is a standing committee of the Board and shall be composed of not less than three (3) members. All members should have general knowledge of financial and auditing matters and the Board shall have, at all times, a member with an auditing background for the purposes of fulfilling the responsibility of the Chair of the audit committee pursuant to Insurance Code 11770(b)(1) as may be amended.

Meetings

The Committee shall hold regular meetings, in accordance with the provisions of the Bagley-Keene Open Meeting Act ("Bagley-Keene") and no less than four (4) times a year. The Committee shall hold regular meetings on the same day as, or within one day of, the regular meetings of the Board. The Committee may hold additional meetings at the request of any Committee member in compliance with the provisions of Bagley-Keene and State Fund's By-laws.

- a. The Committee is expected to maintain free and open communications with the independent auditor, internal audit manager, internal finance staff and management in compliance with Bagley-Keene.
- b. The Committee may, at its discretion, invite members of management or other Board members to attend the Committee's meetings where necessary to further the business of the Committee. Notwithstanding the foregoing, the total number of members of the Board (including committee members) attending the Committee's meeting at any one time shall not equal or exceed a majority of the number of members of the Board.
- c. The Committee shall create an agenda for each meeting pursuant to the requirements of Bagley-Keene.

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- d. Unless the Committee determines otherwise, the Committee shall hold separate closed sessions to meet with management, the internal auditors and independent auditors. Closed sessions of the Committee may be held at any meeting pursuant to the provisions of Bagley-Keene and California Government Code section 11120 et seq., as may be amended.
- e. A majority of the Committee shall constitute a quorum. Each member of the Committee will have one vote and actions at the meeting shall be approved by a majority of the members present.
- f. Minutes shall be prepared at each meeting and shall be filed with the minutes of State Fund's Board.
- g. The Committee Chairperson or the Chairperson's designee shall give a full report on the Committee's actions at the earliest scheduled Board meeting.

Duties and Responsibilities

In discharging its duties and responsibilities, the Committee shall:

1. **Financial Reporting**
 - a. Review with management and the external auditor, State Fund's financial statements on an annual basis and discuss State Fund's financial reports filed with the Department of Insurance and the California State Controller's Office and solicit the external auditor's opinion with respect to the financial statement in the reports.
 - b. Review with management and the head of Internal Audit, any interim financial reports that may be issued throughout the year.
 - c. Review with management and the external auditor any significant changes or other issues regarding accounting principles, judgments and the quality of financial reporting.
 - d. Review with management and the external auditor, State Fund's accounting practices, policies and compliance with accounting standards.
 - e. Review with management, external and internal auditors, the integrity of State Fund's financial reporting processes and controls, any significant financial risk exposures, and State Fund's policies, guidelines and steps management has taken to monitor, control and report such risk exposures.
 - f. Review significant findings prepared by the independent auditors and the internal auditing department together with management's responses.
 - g. Review and assess all matters related to audits, examinations, investigations or inquiries of the State Auditor and other appropriate State and Federal agencies.

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- h. Review the report issued by the external auditor and discuss with the external auditor all critical accounting policies and practices to be used and alternative treatments of financial information within statutory accounting principles ("SAP") that have been discussed with management, ramifications of the use of alternative disclosures and treatments, the treatment preferred by the external auditor, and any other material written communications between the external auditor and State Fund's management.
- i. Create an agenda for the ensuing year or review and approve the agenda submitted by the head of Internal Audit
- j. Oversee the preparation of, or prepare, an audit committee annual report.

2. External Audit

- a. Have responsibility for the appointment, retention, compensation, termination and oversight of the independent, external auditors' work, scope and terms including the coordination of the audit effort with internal audit. The Committee will recommend to the Board approval of all audit engagement fees. The external auditor reports directly to the Committee, and the Chairperson of the Committee or a Committee member will sign the engagement letter with the auditor. The standards for selections of the independent auditors will comply with all State and Federal laws and regulations.
- b. Discuss with the external auditor any disclosed relationships or services that may impact the auditor's objectivity and independence.
- c. Review and confirm the independence of the external auditors by obtaining statements from the auditors of relationships between the auditors and State Fund including non-audit services.
- d. At least annually, the Committee will obtain and review a report either in writing or orally by the external auditors describing the external auditor's internal quality control procedures; material issued raised by recent internal quality control reviews of the firm, and any investigations by governmental or professional authorities concerning independent audits conducted by the firm for the last five years.
- e. Monitor and ensure the external audit partner in charge is rotated as required by law or regulation.
- f. Review the scope and results of the audit and any disagreements the external audit partner may have had with management and any problems encountered by the external audit partner in performing the audit(s).
- g. Review any questions, comments or suggestions the auditor may have relative to the internal controls and accounting practices and procedures of State Fund.

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3. Internal Audit Function

- a. Review with management and the internal audit manager the charter, budget, activities, staffing and organizational structure of the internal audit function, internal audit's compliance with applicable standard and guidelines, and any recommendations with respect to the performance or strengthening of that function.
- b. Review and recommend approval of the annual audit plan, all major changes to the plan and the annual update of the biennial plan.
- c. Review with the manager of internal audit and management the adequacy and effectiveness of State Fund's internal controls, the reliability of its financial reporting as well as the external auditor's assessment of the adequacy of such controls and systems and management's response to any material weakness in State Fund's internal controls.
- d. Review and evaluate the performance of the internal audit function including a review of the performance of the manager of internal auditing and, if appropriate, recommend the selection of a new manager.
- e. Review with the internal auditor any difficulties including restriction on scope of work, access to required information, and any other issues the Committee deems appropriate.

4. Ethics and Legal Compliance

- a. Review with management, the finance staff, the internal auditors and external auditors, as applicable, on at least a quarterly basis, the adequacy and effectiveness of State Fund's systems and controls for monitoring and managing legal and regulatory compliance, including State Fund's disclosure procedures and controls.
- b. Establish procedures for the receipt, retention and treatment of complaints received from the California State Auditor regarding improper governmental activity, theft, conflict of interest, gross misconduct, inefficiencies or incompetence of State Fund's employees, accounting, internal accounting controls or auditing matters.
- c. Establish procedures for the confidential, anonymous submission of complaints and tips by State Fund's employees as mandated by the Board or by law.
- d. Establish procedures for the receipt, retention, and treatment of reports of investigations and audits conducted of State Fund by the California State Auditor.
- e. Formulate and recommend to the Board any changes to the Code of Ethics or Code of Conduct and/or other compliance policies and

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guidelines that relate to financial reporting, and monitor compliance with these Codes.

- f. Recommend to the Board, as appropriate, any other compliance policies and guidelines that the Committee deems appropriate to ensure compliance with applicable laws and regulations.
- g. Conduct a review of all related-party transactions, as necessary, and recommend to the Board, as appropriate, whether to approve such transactions.
- h. Approve State Fund's compliance plan, make and approve changes as needed and ensure that compliance functions are performed with independence and in accordance with professional standards.
- i. Obtain regular updates from State Fund's management and State Fund's legal counsel regarding compliance matters.
- j. Review with management, State Fund's policies and procedures with respect to officers and key employees' expense accounts and perks, including excess benefit transactions, and review the results of any audit of these areas by the internal or external auditors.

5. Enterprise Risk Management

- a. Work with State Fund's Chief Risk Officer and Risk Committee on overseeing the testing of processes and controls in place to mitigate certain risks identified by the Board that could have a material impact on State Fund.
- b. Evaluate the effectiveness of State Fund's Enterprise Risk Management system including the design and function of the processes; effectiveness and efficiency of risk responses and control activities; and completeness and accuracy of risk management reporting.

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Powers

The Committee shall have the following powers:

- a. To form and delegate authority to subcommittees.
- b. To hire appropriate experts as it deems necessary, including but not limited to outside counsel and investigators, to carry out its responsibilities and have other responsibilities and authority as designated from time to time by resolution of the Board.
- c. To amend or repeal the Charter or any provisions of the Charter as appropriate due to new laws or regulations and recommend any changes to the Board.

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- d. To have unrestricted access to management, State Fund personnel, and the external auditors as is appropriate for the proper performance of its function.
- e. To oversee all contracted reviews, assessments and examinations required by the Board or requested by the Committee including, but not limited to, compliance with audit-related laws, rules, regulations, Board policies, internal controls, management operating procedures, and industry best practices.
- f. Such other powers as may be necessary and appropriate to fulfill the Committee's purposes.
- g. The Committee will evaluate its performance on an annual basis, either separately or in conjunction with an annual evaluation of the full Board.
- h. To perform such other functions as assigned by State Fund's charter or bylaws, or the Board.