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Date: June 28, 2010

AGENDA ITEM 10

TO: MEMBERS OF THE BOARD OF DIRECTORS

- I. SUBJECT: Update on Governance, Ethics and Compliance**
- II. PROGRAM: Executive Office**
- III. RECOMMENDATION: Information**

Please find attached a copy of the Point Power.

JAMES F. NEARY
Executive Vice President

GOVERNANCE COMMITTEE MEETING (OPEN)

AGENDA ITEM 10

ATTACHMENT 10-I

UPDATE on GOVERNANCE, COMPLIANCE and ETHICS INITIATIVES

PRESENTED BY: Jim Neary

July 8, 2010

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***Update on Governance, Compliance, and
Ethics Initiatives***

Governance Committee Item#10

July 8, 2010

Jim Neary

- **A few updates were made to the Governance Framework.** (refer to appendix)

- **Barbara Simmons is coordinating a comprehensive review and update of all of our Corporate Policies.**
 - 4 policies have been completed
 - Development & Approval of Corporate Guidelines
 - Records & Information Management
 - Travel and Related Expenses
 - Client Related Business Expense Reimbursement
 - 6 policies are in draft form
 - 7 policies have been identified as obsolete and eliminated

Barbara Simmons is also working on a Governance Guide designed to document the division of authority and responsibility among State Fund's management team.

- A 1st draft of the introduction, overview of corporate governance, overview of the guide, management organization chart, and entries for the Board of Directors and company officers is out to other managers for review.
- In the 3rd quarter she expects to complete entries for Presidents of Claims and Field Operations, Senior Vice Presidents, Chief and Assistant Chief Counsels, the Vice Presidents of Government Relations and Communications, as well as duties common to regional vice presidents, program managers and attorneys-in-charge.

State Fund MAR Project Status

In 2009 (a pre-compliance year)

- 210 Key Controls identified
- 107 of these were tested and confirmed working

In 2010 we commenced a 2nd cycle of testing

- On-line MAR training program introduced in June.
- 187 Key Controls Identified (implementation of IT controls reduced the number of required overall controls by 23).
 - ❑ 3 Controls need further documentation
 - ❑ 184 Key Controls Documented
 - ❑ 29 Controls awaiting final documentation approval
 - ❑ 133 Controls ready for testing
 - ❑ 1 Control tested successfully
 - ❑ 21 Controls in remediation
- The project is on schedule and we expect to be able to make the appropriate certifications when due in early 2011.

MEDICARE REPORTING STATUS

- WC carriers must report their claims on Medicare eligible claimants to Medicare so Medicare can check for duplicate coverage.
- Failure to report a claim is subject to a \$1,000/day/claim penalty.
- Medicare expects to release a final User Reporting Guide in July 2010 and has moved our mandatory reporting date to January 8, 2011 for “regular” claims and to February 15, 2011 for State Contract claims.
- State Fund is undertaking an extensive data clean up to make sure all the required fields have correct entries.
- We expect to send a test file to Medicare in early August to ensure successful data transmission before our “go live” date.
- We expect to meet reporting deadlines.

Division of Workers Compensation - *Profile Audit Reviews (PAR audits)*

- DWC has completed PAR audits of our San Diego and San Jose offices so far this year. Both offices met minimum standards and no fines or penalties were assessed. (Adjusters however are required to pay any identified unpaid comp, with the applicable self-imposed penalty, and send any benefit notices that were found to be missing or deficient.)
- DWC does a Utilization Review audit concurrently with PAR audits. Both offices passed the UR audit. However, San Diego was assessed a \$1,350 fine for a delayed response to a treatment request on 1 claim.
- An audit of the Commerce Office is underway.
- DWC has scheduled PAR audits for 4 additional offices in 2010; those audits haven't started yet.

Conflict of Interest Disclosure

- 5,517 of our employees are required to file disclosures of their personal interests (2,762 of these are “new” filers under our expanded 3/21/10 policy).
 - “Old” filers were required to file their disclosures by April 1st; and as of June 24, 96% of their disclosures were in.
 - “New Filers” had until April 21st to file; and as of June 24, 91% of their disclosures were in.
- The new policy also requires consultants to file disclosures of their personal interests. We are in the process of identifying any potential for conflicts of interest and notifying the consultants of the scope of their required disclosure of personal interests.

Regulatory Compliance Inventory

It is considered a governance best practice to have an inventory of all the laws and regulations which a business is subject to. The Ethics, Compliance and Privacy Program has begun compiling such an inventory for the Fund. Obvious sources are the requirements of the Insurance, Labor and Government Codes, and the regulations of the Department of Insurance, Division of Workers Comp, Workers Compensation Insurance Rating Bureau and Department of Personnel Administration. We expect to complete the inventory in the 3rd Q of 2010.

MANDATORY TRAINING IN 2010

- Employees and Consultants becoming Form 700 Conflict of Interest filers for the first time must complete required training by September 20, 2010.
- Non-supervisory employees will complete Sexual Harassment Prevention training in 2010 (managers and supervisors completed similar training in 2009).
- Employees administering workers comp policies and claims must receive annual in-service anti-fraud training. This is planned for the 3rd Q.
- All employees with access to IT systems will receive annual security training in the 4th Q.

PRIVACY

- The Ethics, Compliance and Privacy Department has launched a new Privacy Initiative.
- A Privacy Policy has been drafted and is going through final approval. (The State of California is also developing a Privacy Policy which will be taken into account in finalizing State Fund's policy.)
- A Corporate Privacy Response Team has been established; the team will work in concert with I.T. Security Response Team.
- Single reporting/tracking system has been developed for both IT and non-IT related incidents.

WHISTLE BLOWER HOTLINES

Annual required Notices Sent Out in 1st Quarter:

- Integrity In Action for ethical concerns.
- Bureau of State Audits for the California Whistleblower Act.
- CHP Task Force for issues related to management misconduct.

- Approval by the Fair Political Practices Commission of our updated Conflict of Interest Code in March of this year was an important ethics milestone. The vast majority of our employees and consultants now have to disclose (in a Form 700 filing) any personal interests that might conflict with their State Fund responsibilities.
- Work continues on the drafting and approval process of a comprehensive employee Code of Conduct. The Code of Conduct will incorporate a list of activities identified as incompatible with State Fund responsibilities, as well as our business ethics policies.

ETHICS TRAINING

- A 45 minute on-line ethics course was launched in May 2010.
 - The program focuses on Ethical Decision Making and the core values of Fairness, Honesty, Integrity and Respect.
 - 1,778 Users Completed Course through June 15th.
- Follow-Up classroom training is being developed for late 2010, focusing on Ethics 24/7.

IN CONCLUSION

We continue to build upon the initiatives begun in 2008 to enhance State Fund's governance, compliance, ethics and transparency. These initiatives are a work in process. Our goal is to be recognized by our customers, regulators, and the insurance industry as the gold standard of workers compensation carriers.

APPENDIX

- GOVERNANCE FRAMEWORK

GOVERNANCE FRAMEWORK

Board of Directors	Compliance & Regulatory Matters	Ethics	Investigations and Fraud Reporting	Managing Risks	Monitoring Activities
Directors are independent of management	Creation of an Ethics, Compliance & Privacy Department	Creation of an Ethics, Compliance & Privacy Department	Insurance Fraud Policy established and provided to all new hires as part of orientation	Addition of CFO, Chief Risk Officer and Chief Investment Officer positions	Creation of a Program Management Office to oversee IT project management
Board has established Governance, Audit & Investment Committees	Model Audit Rule documentation & testing	Employee Handbooks	Email and telephone hotlines established to allow confidential reporting	Promotion of candid/open discussions of risk at Executive level	Internal Audit does an annual risk based audit plan
Board subcommittee charters Established	Analysis of new regulations that impact company	Conflict of Interest Disclosure (FPPC 700) for designated filers	Independent investigations performed under attorney-client privilege	Quarterly Senior Management Business Updates	Management follow-up of issues raised in the Auditors Management Letter
Independent Reporting by External & Internal Auditors and General Counsel to Board	Required postings in all company locations	Ethics Policy in place for Mgrs & Supervisors	Internal Audit investigation of controls where suspected wrongdoing has occurred	ERM linked to annual planning process	Management follow-up of whistleblower reports
Director continuing education on Governance	Sexual harassment training every 2 yrs	HR policies and procedures	Identified fraud or other criminal activity always reported to law enforcement	Business Continuity/IT disaster recovery plans in place	Internal Audit follow-up on audit findings and corrective actions
Periodic evaluation of management	Annual insurance fraud training for customer contact employees	Performance appraisal process		An Enterprise Risk Analysis Completed	Financial results, trend analysis, forecasted cash flow reports
Board Assimilation Process in place	Corporate Policy Initiative established for sustained management of policy review and development	Hotline in place for employee whistle blowing		Appropriate risk transference through contractual clauses and 3 rd party insurance	Investment Activity Reports
Periodic review of "Tone at the Top" in each governance area	Internal Affairs Division established	Required pre-employment screening		Fleet Safety Program for drivers	

GOVERNANCE FRAMEWORK

Board of Directors	Compliance & Regulatory Matters	Ethics	Investigations & Fraud Reporting	Managing Risks	Monitoring Activities
Audit Committee review of financial statements	Internal Audit Charter	Orientation program for new hires		Leadership succession plans developed	
Board selects external auditors	Bi-annual Ethics Training for FPPC filers	Incompatible Activities Statement adopted		Creation of a Risk Committee at the Executive Level	
Board Conflict of Interest policy & a Code of Conduct	Annual Hotline notice to employees	Ethics related hotline established		Creation of a Governance, Risk & Compliance Committee at a middle management level	
Audit Committee Oversight of whistleblower reports	Initiation of a Privacy Policy initiative	Mandatory ethics training		Purchase of appropriate catastrophe reinsurance	
Board discussion of Enterprise Risk Management				Annual Strategic Planning	
Independent Appointed Actuary reports to Board on reserves					
Board reviews and adopts By-Laws					
Delegated Authorities by Board resolution					
Governance Guide being developed					
Audit Committee oversight of Internal Affairs					