

**STATE COMPENSATION INSURANCE FUND
BOARD OF DIRECTORS**

MINUTES OF OPEN SESSION MEETING

May 23 and 24, 2019

The Board of Directors of the State Compensation Insurance Fund met on May 23-24, 2019 at the State Fund Pleasanton Office, 5890 Owens Drive (Atlantic and Pacific conference rooms), Pleasanton, California.

May 23, 2019

AGENDA ITEM 1: CALL TO ORDER AND ROLL CALL

The meeting was called to order on May 23, 2019 at 1:30 p.m.

Mr. Lanier requested Ms. Padua to call roll. The following were present: David M. Lanier (Chair); Robin L. Baker; Sen. Thomas C. Berryhill (Ret.); Daniel M. Curtin (joined during item 6); Marvin P. Kropke; Sen. Michael J. Machado (Ret.); Jack L. Neureuter; Arthur H. Pulaski; Thomas E. Rankin; Angela Tate; and William M. Zachry.

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

Mr. Lanier 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 February 14-15, 2019 Open Meeting Minutes**
- 3b. Board Member Educational Opportunities and Approval of Planned Board Member Education and Expense Reimbursement**
- 3c. Annual Review and Approval of State Fund By-Laws**
- 3d. Annual Review and Approval of Board Education and Travel Expense Reimbursement Policy**
- 3e. Annual Review and Approval of Committee Charters**
- 3f. Review and Approval of Revised Board Committee Assignments for 2019**
- 3g. Approval of Retirement Resolutions**

Ms. Padua noted that the Governance Committee had a discussion regarding the 2019 Board Committee Assignment and approval was deferred to the Board level as part of the Consent Calendar.

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

MOTION: Mr. Kropke SECOND: Mr. Rankin

To approve the Consent Calendar as presented.

Mr. Lanier requested public comment of which there was none. Mr. Lanier called for the vote.

YES: 10 NO: 0 Abstain: 0 Motion carried.

Mr. Curtin was not present when the vote was taken.

AGENDA ITEM 4: STATEMENT OF ACTUARIAL OPINION

Mr. Guy Avagliano, FCAS, MAAA of Milliman, State Fund's Appointed Actuary, reviewed the Loss and Loss Adjustment Expense reserves as of December 31, 2018. He reported State Fund's booked loss reserves for Statutory Claim and Claim Adjustment Expense Reserves were: unpaid losses (including direct and assumed) at \$10B and unpaid loss adjustment expense (including direct and assumed) at \$2.5B. Milliman provided a clean Actuarial opinion, noting the reserves set were consistent with California State standards; consistent with Actuarial standards; and reasonable provisions were made for unpaid loss and loss adjustment expense obligations.

AGENDA ITEM 5: STAFFING UPDATE

Executive Vice President and Chief Administrative Officer Andreas Acker presented an update on staffing. Mr. Acker reported that State Fund ended 1Q 2019 with 4,280 employees, 56 separations, 80 new hires, and 78 promotions. Of the 56 separations, 24 or 42.8% were due to retirements, 13 were resignations, 9 were transfers to other agencies, and 10 were others (death or dismissals). Mr. Acker noted that the new hires exceeded the number of separations. This is a normal trend and separations will increase by the 4Q. The overall separation rate was 5.3% and the primary driver was retirements.

Mr. Acker noted that included in the Board materials was a report on age and state service as of December 31, 2018. The report showed that 660 Employees (15.5%) were over 55 and have 20 or more years of service and 1,269 employees (29.8%) were over 55 and have 10 or more years of service.

Mr. Acker reported as of March 31, 2019 there was an increase in the number of hours over the 640 hour cap and an increase in the number of employees over the cap. Mr. Acker noted that many employees don't take vacation during the 1Q. Mr. Acker also noted that this year employees can cash out up to 80 hours of vacation, which will help reduce the leave hours over the 640 cap. In addition, State Fund required employees over the cap to have a plan to reduce their leave hours. This is a liability which is important to State Fund to monitor and maintain.

Mr. Lanier requested public comment, of which there was none.

AGENDA ITEM 6: FINANCIAL AND PRESIDENT'S REPORT

Mr. Curtin joined the meeting.

President and CEO Vernon Steiner provided the following updates:

Underwriting results

Mr. Steiner noted that due to the nature of State Fund business, the underwriting results are significantly impacted by the dynamics that affect California business including economic conditions, market pricing as well as the effects of the insurance profitability cycle. State Fund net premiums earned of \$288 million were 19.3% lower than the prior year which can be attributed to an ongoing competitive environment; State Fund's filed rate decrease of 10% effective January 2019, and lower audited premium compared to last year. The most significant factor is actually the lower audited premium as last year audit premium was unusually high due to delays in 2017 that arose from the implementation of AB 2883.

The State Fund's Loss and loss adjustment expenses (LAE) ratio of 99.8% were 0.5 points higher than prior year. The underwriting expense ratio of 35.5% was 6 points higher than prior year due to lower net premiums written. Overall, the underwriting loss of \$103 million was flat compared to last year. The combined ratio of 135.3% was 7 points higher than prior year.

Investment and other non-underwriting results

Mr. Steiner reported that the net investment income of \$160 million was \$4 million higher than prior year. The realized capital gains of \$27 million were \$17 million higher than prior year due to sales of stocks during favorable market conditions. Other expenses, mostly representing charge-offs of uncollectible premiums, were \$11 million higher than prior year. This increase was also attributable to the unusually high audited premium in 2018. Overall State Fund ended the 1Q 2019 with net income of \$56 million, which was \$8 million higher than prior year. The policyholders' surplus grew by \$153 million since December 31, 2018.

Operational Update

Mr. Steiner highlighted the following 2018 operational achievements:

Core Values

Mr. Steiner reported that State Fund recently updated its Core Values. Mr. Steiner discussed what are Core Values as follows: 1) they are guiding principles that a business uses to manage its internal affairs as well as its relationship with customers; 2) they are basically beliefs about right and wrong; 3) they should be used to guide recruitment, hiring, training, recognition and awards; and 4) leaders should consider whether business decisions are consistent with its core values.

Mr. Steiner then explained the reasons why State Fund Core Values were updated. The previous core values (Adaptability, Integrity, Honesty, Collaboration, Accountability) represented important concepts, but the way they were presented was vague and not unique. On their own, they could mean different things to different people. Mr. Steiner also noted that he wanted employees to be able to connect emotionally to State Fund's values. State Fund's core values support the North Star, guiding employees in decision-making and in their interactions with each other and customers. In pursuit of State Fund vision, the core values were updated to make them more actionable, meaningful, and reflective of who State Fund is and its purpose. The new core values are as follows: 1) Respect everyone; 2) Be innovative; 3) Do what's right; and 4) Show we care.

Ms. Padua showed the new Core Values video.

Mr. Lanier acknowledged and thanked the staff who worked on the new Core Values video. The Board was impressed with the result.

Mr. Steiner further noted that to support the launch, Communications posted the video and a Core Values Page on Worksite and launched the annual townhalls to discuss values with employees. In addition, Communications will send out posters to all offices and materials to support unit and department meetings designed to help identify how these values show up in their work and opportunities to do more; update the employee recognition platform (RAVE), to reflect the new values; and expand the scope of Worksite "Everyday Hero" stories to spotlight employees living the Core Values.

Mr. Lanier requested public comment, of which there was none.

AGENDA ITEM 7: REPORTS BY THE CHAIRS OF COMMITTEE ACTIVITIES

7a: GOVERNANCE COMMITTEE

7ai: GOVERNANCE, COMPLIANCE AND PRIVACY UPDATE

Governance Chair Mr. Rankin reported on the following:

Effective Training, Communication and Awareness

State Fund had a 98.88% compliance rate for the annual filing of the Statement of Economic Interest forms.

The 2019 Mandatory Compliance Training Schedule has been provided to all employees, featuring material on security awareness, privacy, Code of Conduct, preventing workplace harassment, and anti-fraud.

Ethics and Privacy Reported Issues

Ethics reported issues for the first quarter of 2019 increased 33% from the fourth quarter of 2018. Human Resources (HR) related issues remain the highest reported category (78%, 28 of 36); Equal Employment Opportunity (12 of 28) and Inappropriate/Offensive Behavior issues (8 of 28) were the most reported HR related issues in that category.

7b: AUDIT COMMITTEE

7bi: UPDATE ON COMPLETED CLOSED AUDITS

Audit Chair Mr. Zachry reported on the following activities:

Completed Closed Audits

Mr. Zachry reported that twenty projects were reported in the fourth quarter of 2018 in the Closed Session in February 2019, of which eighteen new issues identified were added to the issue track database. Internal Audit Department continues to monitor Management's progress in addressing these issues until Management implements an action plan to mitigate the risk identified.

All the completed project reports were deemed to be proprietary. There were no non-proprietary projects to report in Open Session.

Whistleblower Hotline

All Ethics Hotline reports are investigated. For the 1Q 2019, there were 36 new allegations received. Of the 36 new allegations, 15 did not require investigation and were referred to Manager Services and 21 were referred to the Internal Investigations Unit. Of the 21 allegations, 17 are currently still in progress and 4 have been closed as unsubstantiated. In addition, 7 investigations from prior quarters were closed.

This report is available to the public and posted on State Fund's website.

7c: INVESTMENT and RISK COMMITTEE

7ci: BOND TRANSACTIONS AND COMPLIANCE REPORT

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

The investment transactions and compliance reports for the periods of January 1, 2019 to March 31, 2019 were approved by the Investment and Risk Committee pursuant to its delegated authority. The Investment and Risk Committee Charter was also reviewed and approved. Sen. Machado also reported the Investment and Risk Committee heard a report from staff on portfolio performance.

Sen. Machado also noted that the Committee received a report from the Enterprise Risk Management (ERM) program and there were no significant changes in the overall risk position of State Fund over the 1Q 2019. The ERM program continues to progress in implementing changes to the framework and methodologies to improve alignment with State Fund's functional and enterprise objectives. The Committee also heard a report on the Board Cybersecurity Primer, which is being created to serve as an introduction and a resource on State Fund's security profile, responsibilities, and expectations.

7d: AD HOC SAFETY AND LOSS PREVENTION COMMITTEE

Chair Robin Baker noted there was nothing to report.

AGENDA ITEM 8: CHAIRPERSON'S'S REPORT

Mr. Lanier noted that upon advisory of the Board and Executive Committee members, he attended the April 2019 Business Review Meetings (BRM) held in Vacaville. Mr. Neureuter was also present. Mr. Lanier was impressed with the staff's presentation discussion, and recommendation.

Mr. Lanier also reported that he attended the New Employee Onboarding held in Vacaville. Again, he was impressed with the presenters and details of the onboarding program. Mr. Lanier commented that he would have mirrored and implemented the same program during the time he had oversight of state agencies.

AGENDA ITEM 9: BOARD MEMBER REPORTS

Mr. Lanier requested any Board member reports, of which there were none.

AGENDA ITEM 10: PUBLIC COMMENT ON APPROPRIATENESS OF CLOSED SESSION FOR ITEMS 13 THROUGH 25

Mr. Lanier requested public comment on the appropriateness of Closed Session for agenda items 13 through 25, of which there was none.

AGENDA ITEM 11: PUBLIC COMMENT

Mr. Lanier requested public comment, of which there was none.

ADJOURNMENT

There being no further business, Mr. Lanier adjourned the meeting at 1:55 p.m. to immediately reconvene in Closed Session.

May 24, 2019

AGENDA ITEM 26: CALL TO ORDER AND ROLL CALL

The meeting reconvened at 10:55 a.m. at the State Fund Pleasanton Office (Atlantic and Pacific conference rooms), Pleasanton, California and the following Members were present: David M. Lanier (Chair); Robin L. Baker; Sen. Thomas Berryhill (Ret.); Daniel M. Curtin; Marvin P. Kropke; Sen. Michael J. Machado (Ret.); Jack L. Neureuter; Arthur H. Pulaski; Thomas E. Rankin; Angela Tate; and William M. Zachry.

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 27: ANNUAL REVIEW AND APPROVAL OF BOARD DELEGATED AUTHORITY AND APPROVAL LEVELS

This item was deferred for the August Board meeting.

AGENDA ITEM 28: PROPOSALS AND SUGGESTIONS FOR AUGUST 20-22, 2019 AGENDA

Mr. Lanier requested suggestions for agenda items for the August 20-22, 2019 Board meeting. Ms. Padua noted that the proposed agenda items are for Closed Session.

Mr. Zachry requested to add on to a future Board agenda the following items: 1) Southern California fraud as an individual cost driver in CT claims and 2) increased cost trend for the Subsequent Injury Fund.

Mr. Lanier requested other agenda items, of which there were none.

Mr. Lanier requested public comment, of which there was none, and he noted that the next Board meeting is scheduled for August 20-22, 2019 at The Lodge at Sonoma Renaissance, Sonoma, California and the Board will also hold its Strategic meeting, unless noticed for a new date and time.

Mr. Lanier adjourned the meeting at 11:00 a.m.

Respectfully submitted,



Hilda B. Padua
Board Liaison and Assistant Corporate Secretary