

**STATE COMPENSATION INSURANCE FUND
BOARD OF DIRECTORS**

MINUTES OF OPEN SESSION MEETING

September 23 and 26, 2014

The Board of Directors of the State Compensation Insurance Fund met on September 23 and 26, 2014 at the Hyatt Regency Hotel, 1 Old Golf Course Road, Monterey, CA 93940.

September 23, 2014

AGENDA ITEM 1: CALL TO ORDER AND ROLL CALL

The meeting was called to order on September 23, 2014 at 3:05 p.m.

Ms. Chalupa requested Ms. Padua to call roll. The following were present: Sheryl A. Chalupa (Chair); Robin Baker (joined at item 4); Daniel M. Curtin (joined at item 4); Marvin Kropke; Sen. Michael J. Machado (Ret.); Lawrence E. Mulryan; Jack Neureuter; Steven L. Rank; Thomas E. Rankin; and Scott Reid.

Absent by prior arrangement: Christine Baker (non-voting member) and William Zachry.

There was a quorum.

Also present: President and CEO Vernon L. Steiner; Chief Financial Officer Peter Guastamachio; Board Liaison and Interim Corporate Secretary Hilda B. Padua; Counsel and Assistant Corporate Secretary Judith D. Sapper; and Randall Keen of Manatt, Phelps & Phillips, LLP.

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 15-16, 2014; May 22-23, 2014; and July 8-9, 2014 Open Meeting Minutes**
- 3b. Board Member Educational Opportunities and Approval of Planned Board Member Education and Expense Reimbursement**
- 3c. Ratification of President's Official Bond for Vernon L. Steiner**
- 3d. Legislative Update**
- 3e. Approval of Retirement Resolutions**

Ms. Chalupa noted that there is no approval of an action for item 3d, "Legislative Update."

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

MOTION: Mr. Kropke

SECOND: Mr. Mulryan

To approve the Consent Calendar as presented.

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

YES: 8

NO: 0

Motion carried.

AGENDA ITEM 4: STAFFING UPDATE

Executive Vice President of Human Resources and Chief Administrative Officer Andreas Acker presented an update on staffing. Mr. Acker reported that State Fund permanent staffing levels continue to decline with 4,151 permanent employees at the end of August 2014. There were 180 employees that separated through July, which represented a 7.1% annualized separation rate. The 7.5% annualized separation rate as of August was lower than last year's 8.1%. It is projected that at the end the year, the retirement rate will be 8.5% and the overall separation rate will be 8%.

In addition, Mr. Acker reported that as of July 30, 2014 there was a 5% reduction in both the hours and employees over the 640 cap. This was due to higher usage and participation in a voluntary 20-hour leave cash out for managers and supervisors authorized by the administration. There were 362 supervisors and managers who cashed out some 7,239 hours (\$276,183). State Fund supports further cash out opportunities.

AGENDA ITEM 5: FINANCIAL UPDATE – 2nd QUARTER 2014

Chief Financial Officer Peter Guastamachio reported on the 2nd quarter financial results for 2014. State Fund's financial results are significantly impacted by economic conditions, including unemployment and market pricing. State Fund continues to maintain disciplined pricing and wrote approximately 74,000 policies, which were 4% more than budget and 7% more than the same period in the prior year. Estimated annual premiums were 5% less than budget and 31% more than same period in the prior year. The strong growth in premiums in 2014 is due to a continued hardening market. The loss and loss adjustment expenses (LAE) ratio of 111.4% was 9 points higher than budget and 14 points higher than the same period in the prior year. This reflects a strengthening of LAE reserves by \$50 million in the 1st quarter for Medical Cost Containment and an increase of \$18M in prior year loss adjustment expenses due to an increase in the liability for State Fund's self-insured insurance program.

The combined ratio of 133.6% was 4 points higher than budget and 3 points higher than the same period in the prior year. The increase in the combined ratio is primarily attributed to the increases in LAE. The related underwriting loss for the quarter was \$242M. The net investment income of \$331M was 2% higher than budget. The net income of \$135M was \$5M more than budget. Policyholders' surplus grew by \$113M since December 31, 2013. Ms. Chalupa requested public comment of which there was none.

AGENDA ITEM 6: PRESIDENT'S REPORT

Ms. Chalupa welcomed Vern Steiner officially as the President and CEO of State Fund. Ms. Chalupa noted that Mr. Steiner is a seasoned insurance executive with 24 years of industry experience, the majority of it in workers' compensation. Ms. Chalupa noted that with Mr. Steiner's strong track record of building effective senior teams and strong capabilities in the organizations he has led, the Board is confident that Mr. Steiner will lead State Fund in building a competitive company with a resourceful, creative workforce that delivers on State Fund's purpose of providing

fair prices and excellent service. Ms. Chalupa added that she is impressed with the considerable amount of time Mr. Steiner has devoted to getting out into the offices around the state and meeting with employees and other State Fund stakeholders.

Mr. Steiner then gave an update on his activities of the past three months. Mr. Steiner reported that he has been making field visits and listening to the employees and stakeholders of State Fund. Mr. Steiner has visited 11 offices and spoken with over 500 individuals. He will complete all his office visits by end of October 2014. It is important to Mr. Steiner to have an open dialogue about “what’s important to employees” and to re-empower leaders to solve problems. Mr. Steiner noted that after the leadership meeting he wants to follow-up on how things are going differently and wants to give more authority to supervisors to address issues locally. In addition, Mr. Steiner conveyed his appreciation of being part of several employee appreciation events, celebrating State Fund’s 100th year anniversary. Lastly, Mr. Steiner noted that he is becoming familiar with the broker community and obtaining insights on what it is like to work with State Fund.

AGENDA ITEM 7: REPORTS BY THE CHAIRS OF COMMITTEE ACTIVITIES

7a: GOVERNANCE COMMITTEE

7ai: GOVERNANCE AND COMPLIANCE UPDATE

Mr. Mulryan reported that the second quarter compliance reporting includes code of conduct targeted training and acknowledgement results, reported ethics and privacy related issues, and oversight resources. Privacy and Cyber Security was selected as the 2014 training topic to reinforce State Fund’s obligations and responsibilities for protecting data of State Fund’s stakeholders. Included with the training is the Annual Code of Conduct Certification. As of August 20, 2014, 99.6% of employees and 75% of consultants have completed the Code of Conduct certification.

Mr. Mulryan reported that Human Resources reporting volume for 2Q 2014 increased by a factor of 1.7 compared to the same period in 2013. The 2Q 2014 reports by category included 17% suspected conflict of interest/discrimination; 22% suspected misconduct; and 61% suspected misuse/theft of time or funds. Suspected privacy/security incident report volume declined 46% compared to the 2nd quarter of 2013. This is attributed to a decrease in volume of transmissions of private information for non-business purposes.

7b: AUDIT COMMITTEE

7bi: UPDATE ON COMPLETED CLOSED AUDITS

Ms. Chalupa reported on the following activities:

Completed Closed Audits – There were three completed closed audits: Corporate Communications Assessment, Business Services, and Claims Operations. These three engagements are considered non-proprietary.

Corporate Communications self-disclosed there was a lack of control to prevent or detect non-compliance with corporate policy. The Business Services audit identified five issues relating to improving control activities over vendor management including supply ordering, expense review and approvals, and mailroom access. The Claims’ site visits to Greater Bay Area Claims, Riverside, and Monterey Park identified four issues. These issues are timely liability decisions, balancing of disability payments on claims, no uniform standard for closing non-rated and non-litigated claims, and file maintenance

and documentation. All the findings were correctible and posed no significant risks to State Fund.

Whistleblower Hotline – All reports made through the Ethics Hotline are investigated.

During 2Q 2014 there were 106 reports from all sources (Ethics Hotline – 48; Management referral – 34; Privacy – 24). There were 30 substantiated allegations; 28 involved employees transmitting their own personal identifying information (PII) or of their family members, relatives, policyholders, and claimants to a non-State Fund e-mail account. None of the 28 substantiated privacy allegations were material to State Fund's financial statements. State Fund continues to educate its employees on the importance of protecting PII and proprietary information. This education is completed through various training courses including annual Code of Conduct training.

7c: INVESTMENT COMMITTEE

7ci: BOND TRANSACTIONS AND COMPLIANCE REPORT

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

The investment transactions and compliance reports for the period of April 1, 2014 to June 30, 2014 were approved by the Investment Committee pursuant to its delegated authority, which includes the purchase of 102 bonds totaling \$1.1B and sale of 23 bonds for \$302.3M. In the equity portfolio \$41.5M were purchased and \$45.2M were sold for rebalancing. The total net gain from the entire portfolio was \$40.1M as of June 30, 2014. The aggregate book value of all the investments was \$18.8B. There were two bonds no longer in compliance with State Fund's Investment Policy.

AGENDA ITEM 8: CHAIRWOMAN'S REPORT

Ms. Chalupa reported on the following activities:

Leadership Conference

Ms. Chalupa reported that she was very fortunate to have the opportunity to address all of State Fund's supervisors at the statewide supervisor conference. The conference's theme was "Unleash the Power" and it was designed to deepen leaders' connection to State Fund's purpose and goals as well as their connections to each other.

Ms. Chalupa appreciated the opportunity to speak to the importance of the work State Fund does for California, specifically how safety and claims services have positively impacted her organization, Goodwill, over the years. Ms. Chalupa noted that several employees informed her after the conference how much they appreciated her attendance and that they had never previously met or seen a Board member. Ms. Chalupa reported staff greatly appreciates Board visits and the opportunity to hear what is on Board members' minds. The overall feedback received about the conference was extremely positive. The supervisors and managers appreciated the opportunity to connect in person with their colleagues across the state, to hear from executives directly about the direction State Fund is going and especially to give feedback. Ms. Chalupa thanked everyone who put the conference together.

Board Development session in July

Ms. Chalupa reported that in July the Board of Directors came together for a continuing education session. Ms. Chalupa thanked all of the presenters for sharing their expertise and the State Fund team that put the training together. The Board Continuing Education covered a lot of important topics including: insurance regulation, financial reporting, enterprise risk management and reserving. This training is pertinent to the Board strategic planning process and generated positive feedback from the Board.

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 13-22

Ms. Chalupa requested public comment on the appropriateness of closed session for items 13-22, of which there was none.

AGENDA ITEM 11: PUBLIC COMMENT

Ms. Chalupa requested further public comment.

1. Executive Director of the Central Coast Builders Association Christie Cromeenes welcomed the Board and Executives to Monterey. Ms. Cromeenes expressed the value that State Fund's Group Program brings to her association and requested the opportunity to work with State Fund to develop a program to help everyone's industry.
2. Executive Director of the Roofing Contractors Association of California Marc Connerly stated the evaluation process for State Fund's Group Program lacked the State Fund core values of accountability and collaboration. Mr. Connerly requested the Board not to make any decisions on the staff proposal but to give an opportunity for the groups to work and collaborate with State Fund to create a better program. The Group Associations have been State Fund business partners for decades and seek an exchange of ideas and collaboration.
3. CEO of Sacramento Regional Builders Exchange Peter Tateishi echoed Mr. Connerly's comments and expressed the desire to work on creating a proposal together with State Fund. Mr. Tateishi noted that during the assessment phase, State Fund requested information from the groups but did not provide feedback. He was concerned that the Board is only seeing one-sided information. He is awaiting a response to his request for a meeting with State Fund. Mr. Tateishi values the safety programs and noted that State Fund has presented invaluable safety information including at the annual Sacramento Expo. He would like to work together with State Fund and provide input on the Group Program before the Board makes a final decision.
4. Executive Director of Bay Area Builders Exchange Scott Leary noted that the group safety programs have prevented or reduced injuries, brought workers back to work, and controlled costs for employers. Business with State Fund is an economical choice because there are limited options for small businesses. The State Fund Group Program provides safety programs for small employers. Mr. Leary would like to continue to leverage the associations' strengths and relationships for mutual benefit.
5. President and CEO of the North State Building Industry Association Michael Strech noted that there are 5,000 employers who are in his group. He is concerned with the future of

State Fund's Group Program. In the past, the Association Advisory Council which ran 2006-2010 allowed discussion with staff from actuarial, claim, and underwriting departments with the attendance of Executives and the President. Mr. Strech would like to resume the meetings. Mr. Strech noted currently there has been limited discussion with State Fund. He expressed doubts about the focus on tiered rates. Mr. Strech requested that the Board consider the consequences of their decision on this matter.

6. SEIU Local 1000 Vice President Margarita Maldonado presented organizational charts of State Fund executive teams and consultants. Ms. Maldonado voiced her concern about the number of State Fund consultants in influential leadership roles. She requested further information on the number and placement of consultants within the organization. Ms. Maldonado reported that SEIU made a formal request for information on September 11, 2014 in expectation of an October meeting with State Fund.

Ms. Maldonado stated that employees aren't afforded the opportunity to be part of the infrastructure for the future and that no true knowledge transfer process has been identified. She noted that there are over 100 vacancies in IT and questioned whether the salary structure that is currently in place is enough to attract the right talent to State Fund. Ms. Maldonado also noted that vacancies are posted for Vacaville while most IT consultants work in Pleasanton. SEIU has submitted different ideas to State Fund addressing salary, training, and incentives offered for opportunities available within State Fund. The apprenticeship program has not gone far enough and SEIU members have not seen desired salary opportunities. There is still the issue of ongoing reliance on consultants and USIS contractors. Ms. Maldonado indicated SEIU recently obtained from State Fund sources an internal report issued in January 2014 noting there would be a \$100M savings through eliminating this reliance on consultants. SEIU would like to partner with State Fund to find solutions on reducing the reliance on consultants. She is confident that a new salary structure and other benefits will attract the right talent to State Fund.

7. Executive Director of The Builders' Exchange of Stockton Michael Self shared that eight years ago he was a general contractor and personally saw the benefit of safety programs. Mr. Self expressed that the State Fund Group relationship is important to his group and requested collaboration with State Fund to create a win-win solution. He noted that there was a good history with State Fund and would like to move forward in a healthy and beneficial way.

ADJOURNMENT

Ms. Chalupa noted that the Friday, September 26, 2014 Open Session is now scheduled to begin at 9:30 a.m. not 10:30 a.m. as originally Noticed, or upon adjournment of the Closed Session Strategic meeting. There being no further business, Ms. Chalupa adjourned the meeting at 3:50 p.m. to immediately reconvene in Closed Session.

September 26, 2014

AGENDA ITEM 23: CALL TO ORDER AND ROLL CALL

The meeting reconvened at 9:30 a.m. following the conclusion of the Closed Session and the following Members were present: Sheryl A. Chalupa (Chair); Robin Baker; Lawrence E. Mulryan; Jack Neureuter; Steven L. Rank; Thomas E. Rankin; and Scott Reid.

Absent by prior arrangement: Daniel M. Curtin; Marvin Kropke; Sen. Michael Machado; William Zachry; and Christine Baker (non-voting member).

There was a quorum.

Also present: President and CEO Vernon L. Steiner; Chief Financial Officer Peter Guastamachio; Board Liaison and Interim Corporate Secretary Hilda B. Padua; and Randall Keen of Manatt, Phelps & Phillips, LLP.

AGENDA ITEM 24: RATIFICATION OF APPOINTMENT OF CHIEF FINANCIAL OFFICER AND CHIEF OPERATING OFFICER

Ms. Chalupa reported that Peter Guastamachio has been named State Fund's Chief Financial Officer effective July 15, 2014. Mr. Guastamachio joined State Fund in 2009 as State Fund's Chief Investment Officer and has been an asset to the organization. During Mr. Guastamachio's five-year tenure with State Fund, he has stepped in to lead programs outside of his primary duties as investment officer, even briefly serving as Chief Information Officer. Mr. Guastamachio's financial strategy and leadership have continued to strengthen State Fund's financial position in the California workers' compensation market.

Ms. Chalupa requested a motion to ratify the Appointment of Peter Guastamachio as Chief Financial Officer effective July 15, 2014.

MOTION: Mr. Neureuter

SECOND: Mr. Rank

To ratify the appointment of Peter Guastamachio as Chief Financial Officer effective July 15, 2014 as presented on Resolution No. 2034 as attached hereto.

YES: 7

NO: 0

Motion carried.

AGENDA ITEM 25: PROPOSALS AND SUGGESTIONS FOR NOVEMBER 20, 2014 AGENDA

Ms. Chalupa requested additional items for the November 20, 2014 Board meeting of which there were none.

Ms. Chalupa requested public comment, of which there was none, and she noted that the next Board meeting is scheduled for November 20, 2014 at the State Fund Corporate Office, 333 Bush Street, San Francisco, California unless Noticed for a new date and time.

Ms. Chalupa adjourned the meeting at 9:35 a.m.

Respectfully submitted,

Hilda B. Padua
Board Liaison and Interim Corporate Secretary



**BOARD OF DIRECTORS
STATE COMPENSATION INSURANCE FUND**

**RESOLUTION of the BOARD of DIRECTORS of the
STATE COMPENSATION INSURANCE FUND
APPOINTING the CHIEF FINANCIAL OFFICER**

Adopted September 26, 2014

WHEREAS, the State Compensation Insurance Fund requires the services of a Chief Financial Officer; and

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

WHEREAS, the Board of Directors of the State Compensation Insurance Fund has delegated to the President of the State Compensation Insurance Fund, subject to conditions that the Board of Directors may from time to time prescribe, the powers, functions, and duties conferred by law on the Board of Directors in connection with the administration, management, and conduct of the business and affairs of the State Compensation Insurance Fund.

NOW, THEREFORE,

IT IS RESOLVED, that the Board of Directors hereby appoints Peter A. Guastamachio as Chief Financial Officer, effective as of July 15, 2014, at a base annual salary of \$320,000; a recruitment and retention differential of \$32,472 on an annual basis; and a potential at-risk compensation differential of up to 30% of annual salary, subject to approval by the Board, and based on the Chief Financial Officer's achievement of specifically defined metrics and performance goals; and

IT IS FURTHER RESOLVED, that the President of State Fund is hereby granted the authority to enter into an employment agreement with the Chief Financial Officer and any amendments that may be necessary from time to time except that any change in compensation must be presented to the Board of Directors for approval; and

IT IS FURTHER RESOLVED, that the Board of Directors hereby ratifies and approves all actions taken by the President of the State Compensation Insurance Fund as were necessary to appoint the Chief Financial Officer of the State Compensation Insurance Fund.

I, Hilda B. Padua, Interim 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 meeting held September 26, 2014 unless amended and approved by the Board of Directors at such time as minutes for the September 26, 2014 Board of Directors meeting are approved.

Hilda B. Padua, Interim Corporate Secretary

Date