

**STATE COMPENSATION INSURANCE FUND
BOARD OF DIRECTORS**

MINUTES OF OPEN SESSION MEETING

December 10 and 11, 2015

The Board of Directors of the State Compensation Insurance Fund met on December 10-11, 2015 at the State Fund Corporate Office, 333 Bush Street, San Francisco, CA.

December 10, 2015

AGENDA ITEM 1: CALL TO ORDER AND ROLL CALL

The meeting was called to order at 2:00 p.m.

Ms. Chalupa requested Ms. Padua to call roll. The following were present: Sheryl A. Chalupa (Chair); Christine Baker (non-voting member); Robin L. Baker; Daniel M. Curtin; Marvin P. Kropke; Sen. Michael J. Machado (Ret.); Lawrence E. Mulryan; Jack L. Neureuter; Steven L. Rank; Thomas E. Rankin; Scott K. Reid; and William M. Zachry.

There was a quorum.

Also present: President & CEO Vernon L. Steiner; General Counsel and Corporate Secretary Margie R. Lariviere; Board Liaison and Assistant Corporate Secretary Hilda B. Padua; Counsel and Assistant Corporate Secretary Judith D. Sapper; and Randall Keen of Manatt, Phelps & Phillips, LLP.

Ms. Chalupa acknowledged the presence of selected individuals from the Emerging Leader Program in the audience. Ms. Chalupa noted that the Emerging Leader Program was created to recruit and develop future leaders in order to build up State Fund's leadership talent pool. In this development program, participants will have the opportunity to attend industry-leading training; work on real-life business projects and make meaningful contributions; and demonstrate their ability to achieve top results on a variety of business projects and assignments. Ms. Chalupa also noted that the Board had an opportunity to interact with the selected participants in between Committee sessions.

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 August 18 and 20, 2015 Open Meeting Minutes**
- 3b. Board Member Educational Opportunities and Approval of Planned Board Member Education and Expense Reimbursement**
- 3c. Ratification of Appointment of Chief Claims Operations Officer**
- 3d. Authorization to Secure a Renewal Workers' Compensation Program effective January 1, 2016**
- 3e. Approval of 2016 Board and Committee Meeting Schedule and Location**

State Fund combined Loss and Loss Adjustment Expense ratios totaled 106.4% through September, 2015 which was 5 points lower than the same period in the prior year and slightly above budgeted target of 106%. This is due to State Fund increasing its reserves on its Workers' Compensation self-insurance program in June, 2015 by \$6M.

The Underwriting Expense Ratio of 22.8% was 0.6% higher than the same period in the prior year. This was attributed to higher variable expenses, primarily commissions and timing differences for group administrative fees. State Fund ended 3Q 2015 with a Combined Ratio of 129.2% and an Underwriting Loss of \$352M which were 5 points and \$30M lower than the prior year. Offsetting the underwriting loss, the net investment income for 3Q 2015 was \$484M with realized capital gains of \$59M. This resulted in net income of \$181M for the quarter which is \$1M lower than the prior year. There was an increase in policyholders' surplus of \$24M since December 31, 2014.

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

AGENDA ITEM 6: PRESIDENT'S REPORT

President and CEO Vern Steiner reported on the following activities:

Medical Provider Network (MPN):

Mr. Steiner noted that State Fund has had the same Medical Provider Network (MPN) since its initial MPN filing. In 2015, State Fund underwent a major effort, working with Harbor Health to create a new outcome-based network designed to choose physicians who achieve the best outcomes for injured workers for inclusion in the State Fund network. This quarter Harbor Health submitted the network to the Division of Workers' Compensation (DWC) for approval. The transition to the new network is expected to occur in 1Q 2016.

In addition, Mr. Steiner reported that State Fund created a pharmacy benefit network and expanded its MPN to include physical therapy, translation, and transportation services. This is an important and responsible step in utilizing the tools the legislature created to help manage medical costs and ensure that the system can both provide injured workers with appropriate benefits and allow employers to operate their businesses in California. Mr. Steiner reported that State Fund received several letters from various associations questioning State Fund's authority to take these steps. It is anticipated that some service providers who either have not elected to participate with State Fund's network partners or have not been selected based on the outcomes criteria will challenge State Fund's decisions. Mr. Steiner noted that State Fund is prepared for challenges from service providers who either have not elected to participate with State Fund's network partners or have not been selected based on outcomes criteria.

Loss Prevention:

Mr. Steiner noted that in early 2015 State Fund focused on its purpose of helping make workplaces safer. To that end, State Fund has taken several steps, including a recent training at the University of Iron in Benicia where State Fund Loss Prevention personnel attended along with Cal-OSHA staff. Mr. Steiner reported that he had the opportunity to participate in the training kick-off. The facility was truly impressive and the expertise State Fund staff gained will be critical in helping make California workplaces safer. In addition, Mr. Steiner noted that traditionally State Fund has provided training, education, and resources to policyholders. State Fund will continue to support these efforts focusing on the impact a good safety program could have on employees' well-being and the success of the business. Mr. Steiner shared some success stories and the Loss Prevention personnel involved.

Stephen Hunckler, New Chief Claims Operations Officer:

Mr. Steiner reported that Stephen Hunckler has joined State Fund as its new Chief Claims Operations Officer. In just over two months, Mr. Hunckler has visited many offices and started getting to know the people in Claims and Workers' Compensation Legal.

AGENDA ITEM 7: REPORTS BY THE CHAIRS OF COMMITTEE ACTIVITIES

7a: GOVERNANCE COMMITTEE

7ai: GOVERNANCE, COMPLIANCE AND PRIVACY UPDATE

Mr. Mulryan reported on the following activities:

New Legislation (AB 553 – Daly) – Corporate Governance Annual Disclosure:

AB 553 was signed as an urgency bill and is now in effect. The bill requires California insurers to annually summarize their corporate governance framework and align with the National Association of Insurance Commissioners' (NAIC) Model Regulation. The Annual Disclosure report requires certification by either the President and CEO or Corporate Secretary and is exempt from California Public Records Act. The first report is due on June 30, 2016. Reports submitted after the due date are subject to late fees.

New Legislation (SB 570 – Jackson/AB 964 – Chau) – Privacy Data Breach:

The bill is effective January 1, 2016. The bill defines "encrypted" to mean information which is transformed to be indecipherable and unreadable to an unauthorized person. It also creates a model security breach notification form with specific titles and headings, which will be considered in compliance with the law.

Revised Incompatible Activities Corporate Policy:

The Incompatible Activities Corporate Policy was revised to incorporate the Close Personal Relationships policy; and it clarifies engagement in certain activities contrary to the interests of State Fund does not affect employee rights under collective bargaining agreements. Mr. Mulryan noted the Board is required to approve changes to this corporate policy. Ms. Chalupa requested a Motion.

MOTION: Sen. Machado

SECOND: Ms. Robin Baker

To approve the Revised Incompatible Activities Corporate Policy as presented.

Ms. Chalupa requested public comment of which there was none. Ms. Chalupa called for the vote.

YES: 11

NO: 0

Abstain: 0

Motion carried.

Ethics and Privacy Reports:

There is a significant increase in internal referrals other than Management, including concerns raised through AskHR and Corporate HR Investigations, accounting for 42% of the referrals. HR-related matters account for 75% of all reported concerns (Performance 38%; EEO/Conflicts of Interest 23%; Inappropriate Behavior 20%). Privacy incidents

decreased. Sixteen percent of all concerns were reported via State Fund's independent hotlines.

7b: AUDIT COMMITTEE

7bi: UPDATE ON COMPLETED CLOSED AUDITS

Ms. Chalupa reported on the following activities:

Completed Closed Audits – There were eight completed closed audits. At the December 9, 2015 Audit Committee Meeting, Mr. Robinson reported on the four non-proprietary completed closed audits: Claims Legal Operations, Claims Operations Combined (2014), Claims Operations Site Visit and File Review – Redding, and Corporate Communications Distribution List Consulting Engagement. The other four projects are deemed to be proprietary.

All of the closed audits are correctible in the normal course of business and do not represent significant risk to State Fund. Management has provided their corrective action plans and Internal Audit monitors the completion of the corrective action plans.

Whistleblower Hotline – All reports made through the Ethics Hotline are investigated. During 3Q 2015 there were 41 reports: 1 Management referral and 22 referrals from the Privacy Office. There were 64 new allegations received and 61 investigations completed. From the 61 completed investigations, there were 35 substantiated allegations and 26 unsubstantiated. Of the 35 substantiated allegations, 34 were referred to Manager Services for action and one involved an employee who separated or retired from State Fund.

State Fund continues to educate its employees on the importance of protecting Personally Identifiable Information (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 July 1, 2015 to September 30, 2015 were approved by the Investment Committee pursuant to its delegated authority, which included the purchase of 63 bonds totaling \$692.7M and sale of 3 bonds for \$33.7M. In the equity portfolio \$89.4M were purchased and \$57.8M were sold for rebalancing. The total net gain from the entire portfolio was \$16.1M. The aggregate book value of all the investments was \$19.2B. There were 2 bonds no longer in compliance with State Fund's Investment Policy.

Sen. Machado also reported the Investment Committee heard a report on Portfolio Performance results.

AGENDA ITEM 8: CHAIRWOMAN'S REPORT

Ms. Chalupa reported on the following activities:

Presentation at the California Golden Empire CPCU Chapter:

Ms. Chalupa was the key speaker at the California Golden Empire CPCU Chapter on September 17, 2015 in Bakersfield. There were 40 attendees. Ms. Chalupa shared why Workers' Compensation is personal as it has a huge impact on Goodwill's mission. Ms. Chalupa also discussed the workers' compensation market; State Fund's purpose and role in the market; Workers' Compensation post-SB 863; political landscape in workers' compensation and the type of legislation that may be introduced in the next session; and what State Fund is doing to manage workers' compensation effectively for injured workers and employers, specifically to educate doctors about the dangers of using opioids to treat minor injuries; and the plans to roll out the new outcome-based MPN.

National Association of Corporate Directors (NACD) Conference - September 26-29, 2015 in Washington, D.C.:

Board members Marvin Kropke, Lawrence Mulryan, Sen. Michael Machado (Ret.), Scott Reid, Steve Rank, William Zachry, and Sheryl Chalupa attended the conference. Other attendees included Vernon Steiner, Peter Guastamachio, Marjorie Hutchings, and Margie Lariviere.

The Board members attended a Diversity Symposium where topics included Unconscious Bias and The 21st Century Board; forums which included Audit, Strategy and Risk, Compensation, and Governance; heard from keynote speakers on a wide-ranging set of topics including: Value Creation; the Intersection of Sustainability and Risk; The Future of Digital Currencies; Cyber Disclosure, Liability and Reputation Risk; The Economics of IT; Navigating Enterprise Risk; Reputation, Crisis, and Transparency in the Age of Social Media; and many others.

Business Review Meetings – October 28-29, 2015 in Santa Ana:

Sheryl Chalupa and Lawrence Mulryan attended the Business Review Meetings in Santa Ana and heard reports from Claims, Legal, Field Operations/Policy, Customer Service Center, and Customer Processing Center. Ms. Chalupa was impressed with the ability of the various units to talk about the business results, what's working and what's not working, about successes and about lessons learned. Some of the highlights included the report on the Claims Innovation Camp pilot at the Pleasanton campus, the improved quote turnaround times, and the continued progress in the Customer Service Center and Claims Processing Center to improve quality and service.

Lastly, Ms. Chalupa wished everyone a safe and happy holiday season. Ms. Chalupa requested public comment of which there was none.

AGENDA ITEM 9: BOARD MEMBER REPORTS

Ms. Chalupa requested any Board member reports.

Mr. Zachry noted that Board members have acquired the NACD Fellow designation and the additional training received from the NACD conference was a good experience.

Mr. Mulryan noted that when he attended the Business Review meetings, he was impressed by the employees' dedication to details, and liked their open discussions and willingness to challenge each other.

AGENDA ITEM 10: PUBLIC COMMENT ON APPROPRIATENESS OF CLOSED SESSION FOR ITEMS 13-23

Ms. Chalupa requested public comment on the appropriateness of closed session for items 13-23 of which there was none.

AGENDA ITEM 11: PUBLIC COMMENT

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

ADJOURNMENT

There being no further business, Ms. Chalupa adjourned the meeting at 2:40 p.m. to immediately reconvene in Closed Session.

December 11, 2015

AGENDA ITEM 24: CALL TO ORDER AND ROLL CALL

The meeting reconvened at the State Fund Corporate Office, 333 Bush Street, San Francisco, CA, following the conclusion of the Board Closed Session and the following Members were present: Sheryl A. Chalupa (Chair); Robin L. Baker; Daniel M. Curtin; Marvin P. Kropke; Sen. Michael J. Machado (Ret.); Lawrence E. Mulryan; Jack L. Neureuter; Thomas E. Rankin; Scott K. Reid; and William Zachry.

Absent by prior arrangement: Steven L. Rank and Christine Baker (non-voting member).

There was a quorum.

Also present: President & 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; Counsel and Assistant Corporate Secretary Judith D. Sapper; and Randall Keen of Manatt, Phelps & Phillips, LLP.

AGENDA ITEM 25: PROPOSALS AND SUGGESTIONS FOR FEBRUARY 18-19, 2015
AGENDA

Ms. Chalupa requested other agenda items 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 February 18, 2016 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 11:45 a.m.

Respectfully submitted,

Hilda B. Padua
Board Liaison and Assistant Corporate Secretary