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MONTANA STATE FUND
BOARD OF DIRECTORS MEETING
May 1, 2015

The Montana State Fund (MSF) Board of Directors meeting was held May 1, 2015 in the Board Room of Montana State Fund, 855 Front Street, Helena MT 59601.

Directors Attending

Elizabeth Best, Great Falls
Joe Brenneman, Kalispell
Wayne Dykstra, Billings
Bruce Mihelish, Lolo
Richard Miltenberger, Helena
Lance Zanto, Helena
Lynda Moss, Billings

State Fund Staff Attending

Laurence Hubbard, President/CEO
Verna Boucher, Special Asst to Pres/CEO
Nancy Butler, General Counsel
Mark Barry, Corporate Support VP
Rick Duane, Human Resources, VP
Peter Strauss, Operations Support VP
Dan Gengler, Internal Actuary
Rene Martello, Controller
Patti Grosfield, Internal Auditor
Christy Weikart, Underwriting Services Leader
Shannon Copps, Director, IT Plans & Controls
Mary Boyle, Communications Specialist
Sam Heigh, Director, Insurance Applications
Darcie Dunlap, Actuarial Analyst
Pat McCullough, Medical Team Leader
Pam Byers, Strategic Claim Leader

Others Attending

Russell Greig, Towers Watson
Mari Kindberg, SAO
Sen. Jim Keane
Pat Murdo, Leg. Services
Sonia Powell, OBPP
Bob Biskupiak, IIAM
Brenda Miller, Liberty Mutual
Glen Oppel, Montana Chamber
Carol Roy, SAO
Bill Wheeler, DOLI

I. Meeting Preliminaries

A. *Call to Order*
Elizabeth Best, Chair, called the meeting to order at 8:30 a.m. and welcomed attendees and specifically Senator Jim Keane from Butte. She noted that the Board welcomes and encourages comments and questions from the public and staff throughout the meeting and encouraged active participation.

B. *Approval of January 30, 2015 Board Meeting Minutes*
Chair Best called for a motion to approve the January 30, 2015 minutes.

Richard Miltenberger made a motion to approve the January 30, 2015 minutes as presented. The motion was seconded by Bruce Mihelish. Chair Best asked for any questions or comments from those present. There being none, she called for the vote and the motion was unanimously approved.

Corporate Support

A. *FY2015 Third Quarter Budget – Rene Martello, Controller*

Ms. Martello provided a review of the third quarter budget variance report, the Old Fund funding estimate and the third quarter financials. She reviewed the categories of the operational expenditures and explained the variances between actual budget and current budget projections. She noted that some categories (claim payments and ALAE) were over budget while others were under, which resulted in the overall budget being 3.9 percent over.

MSF Budget Status FY 2015

As of March 31, 2015	Budget	Projection	Variance from Budget (over) /under	Percent of Budget Expended
Operational Expenditures				
Personal Services	$26,608,599	$25,614,837	$993,762	96.3%
Operating Expenses	21,410,770	20,974,637	436,133	98.0%
Equipment & Intangible Assets	1,116,999	861,877	255,122	77.2%
ALAE	2,712,955	2,959,758	(246,803)	109.1%
Total Operational Expenditures	$51,849,323	$50,411,109	$1,438,214	97.2%
Claim Payments				
MSF Indemnity	$39,122,516	$37,509,973	$1,612,543	95.9%
MSF Medical	69,196,297	78,783,056	(9,586,759)	113.9%
Other States Coverage (Ind & M	1,276,293	1,112,349	163,944	87.2%
Total Claim Payments	$109,595,106	$117,405,377	($7,810,271)	107.1%
Total MSF Expenditures	**$161,444,429**	**$167,816,486**	**($6,372,057)**	**103.9%**

She provided further clarification of the variance to the medical benefits paid which was due to increased activity in that category beginning about the end of November 2014. Medical settlement practices increased in December resulting in a $9.6 million budget overage. Disputed and undisputed medical settlements have been occurring at greater frequency than was originally anticipated resulting in MSF management's request that the Board approve an $8 million increase to the budget.

B. *FY2015 Budget Amendment – Rene Martello, Controller and Pam Byers, Strategic Claim Leader*

Ms. Martello introduced Pam Byers, Strategic Claim Leader to explain the claim settlement process and changes.

Ms. Byers reported that prior to the changes of House Bill 334 (HB334) on July 1, 2011, future medical benefits could only be settled if a dispute existed. HB334 permits settlement of disputed and undisputed benefits as long as there is mutual agreement of the parties and the settlement is in the best interest of the parties; neither party can force a settlement to occur. The best interest of the injured employee is specifically outlined in the settlement documents that are submitted to the Employment Relations Division. The petition is very clear that the settlement includes unexpected worsening of the current condition and also any unknown conditions which may occur in the future; eliminating entitlement to future medical benefits. A recent medical report outlining the expected medical treatment is also required for submission with the petition.

Settlements offer a variety of benefits for the different parties; for instance the injured employee has control over his or her medical treatment and independence from the workers' compensation system. For MSF and its policyholders, future liabilities are capped and claim inventory is reduced.

Ms. Byers clarified that not all claims are appropriate for settlement, particularly when medical treatment is not known with enough specificity to accurately evaluate the settlement value. She said there are also injured employees not capable of managing the financial aspects of a claim themselves and it is not appropriate to settle those claims.

She explained that MSF has developed an enhanced process that focuses on applying consistency, fairness and oversight of settlement determinations on all claims. This new process has increased the number of settlements by about 18 percent for FY15.

Chair Best called for questions.

Mr. Miltenberger asked if the injured employees were typically represented by an attorney.

Ms. Byers explained that MSF has not been distinguishing between a represented status or not. Each claim is reviewed on its own merits and then negotiated either with the injured worker's attorney or directly with the injured worker (based on the injured worker's preference for representation or not).

Mr. Miltenberger also sought clarification about what constituted an injured worker not being in a position to manage their own settlement and how that determination was made without the injured employee having representation.

Ms. Byers provided an example of a past situation in which the injured employee had suffered a traumatic brain injury and was not represented by counsel. MSF was concerned about the employee's ability to manage the process and recommended that he proceed through the Employment Relations Division (ERD) mediation route so that the courts could weigh in and provide a third-party review to assure the appropriate action was taken for the injured employee. She said MSF takes a cautious approach when proceeding with settlements to assure that the injured employee's future best interests are considered.

Lynda Moss asked if there was a process in place for an evaluation of each settlement after they are finalized so there is feedback to assist MSF in assuring the system is working well for all the parties.

Ms. Byers reported that at the end of each month, she reviews every settlement payment, the evaluations that were completed and the settlement documentation as well as any feedback received. Her reviews are provided to the Claim Managers who follow up with the claims examiners. Additionally, ERD has taken a very active role in the settlement process and often ask questions about specific medical treatments to assure that MSF has included that consideration in its evaluations. A recent medical report is included in the submission to ERD so they can weigh in on the overall evaluation and settlement.

Ms. Moss asked if there was a process for the injured employee to provide follow up about the system.

Ms. Byers said that in settlement discussions with the injured employees, MSF is very candid and transparent about how the settlement evaluation was determined, including prior treatment costs, their physician's future treatment recommendations, or any potential surgeries.

Mr. Mihelish referenced the budget amendment that the Board would be voting on and asked why management decided to step up the claim settlement process yet failed to anticipate that increase when building the budget. He also asked if that consideration would be included in budget calculations going forward to avoid future budget amendments for this purpose.

President Hubbard explained that when the budget was presented in June 2014, the new Claims Manager positions/functions were included in the budget proposal; however, that had not been completely developed. After budget approval, MSF realized the potential that position offered for claims settlement and developed a process for reviewing files for that possible activity. He noted this settlement process provides MSF with an opportunity to close liability around the long term cost of claims. He said he believes it is something that MSF, organizationally, needs to better utilize. Even when the process was completed, it was still too difficult to anticipate what the settlement activity would look like. The process included claim examiner training to better identify files appropriate for settlement, which did not occur until the fall.

He noted that over the years, budget amendment requests have typically been the result of medical inflation costs running in double digits. These current liabilities are mandatory and Mr. Hubbard assured staff that he would approach the Board about a budget amendment rather than stop claim settlement activity because he supports this process. He said that if settling a claim can resolve future liability, containing the ultimate cost for MSF while still meeting the benefits and interests of the injured worker, then he feels strongly that this process should continue.

Joe Brenneman expressed concern that this will open MSF up to lawsuits from injured workers who settle then decide they did not receive a fair settlement and hire counsel to return for more compensation. He asked if there have been any lawsuits over the settlements in the short time they have been occurring and asked Nancy Butler, General Counsel to provide input on this question.

Ms. Byers said there have been no challenges to the settlements completed since November 1, 2014.

Ms. Butler said she believed the law was well thought out and developed through a process that began with input from a variety of interested parties at the Labor Management Advisory Council (LMAC) and was well vetted before it was introduced at the legislative level. She said the "best interest" language and the required documentation support defensible settlements.

Mr. Brenneman asked if Russell Greig the consulting actuary from Towers Watson was incorporating liability exposure in the rate calculation projections as well as considering possible follow-up lawsuits.

Mr. Greig said he will be looking at the increased settlement activity and building those considerations into his calculations; however, he would not be building in possible lawsuit considerations.

Chair Best said she believed any lawsuit would likely be a constitutional challenge to the entire system itself as to whether this continues to be a valid quid pro quo. She said workers' rights and the trade-off between what they give up and what they are getting back continues to erode.

Mr. Hubbard clarified that an injured worker and MSF agreeing to a settlement does not preclude the injured worker from filing a subsequent claim if they return to work and injure a different body part. He added that suing after a settlement approved by the Department of Labor and Industry (DOLI) would only be allowable if there were a mutual mistake of the law as opposed to a mutual mistake of fact. Injured workers returning after settlement due to a depletion of funds is common now and MSF routinely defends against those reopening requests based on current legal standards.

Lance Zanto asked if MSF has looked into annuity options provided through MSF for injured workers receiving large settlements that may need assistance managing their workers' compensation-related medical issues monetarily.

Ms. Byers said that annuities are occasionally utilized, however, those annuities are arranged by the injured employee's attorney. MSF is looking in to the process necessary to contract with an annuity vendor to provide that service to injured workers following the settlement process.

Wayne Dykstra provided an anecdote in which an injured employee opted to negotiate a settlement with MSF after an injury that precluded him from continuing his 15 year career, yet did not render him bed ridden or completely unable to work. He used the lump sum to pay for retraining and upon completion of his schooling started a small business which has been quite successful. Mr. Dykstra said he had not considered the implications of what people can do and/or why they would choose to consider a lump sum settlement.

Chair Best called for additional questions or comments; there were none.

Ms. Martello concluded her presentation with a request to the Board to approve the proposed budget amendment. She pointed out that when the annual budget was approved, the total budget amount of $161.4 million was submitted to the State Budget Office establishing MSF's spending authority within the state's accounting system. She explained that if MSF's spending in any category exceeds the current spending authority, nothing further will be paid out, including injured worker benefits. She noted that consideration of the amendment amount is developed patterning various amounts while keeping the request conservatively reasonable. She said the amendment request is for $8 million; however, if that amount is not necessary to continue operations, the additional budget funds will not be spent out just to deplete the amendment funds.

Chair Best called for questions or comments.

Mr. Dykstra asked that staff provide a bi-monthly (every sixty days) settlement report to the Board members so that they can monitor how the process is trending and see the dollar amounts.

President Hubbard said MSF could and would provide a report in the aggregate on activity during that period with any injured worker personal information redacted.

Chair Best called for questions from the Board, public and staff; there were none.

Mr. Zanto made a motion to approve an amendment to the Fiscal Year 2015 budget, of an increase of $8.0 million. Ms. Moss seconded the motion.

Mr. Brenneman said he would vote in favor of the motion but hoped that next fiscal year's budget projections could be closer than 13 percent off.

Chair Best called for questions or comments; seeing none, she called for the vote and the motion passed unanimously.

Ms. Martello provided an update on annual expenditure projections for the Old Fund compared to the funding estimate that was provided to the Department of Administration at the beginning of the year. The projections of total Old Fund expenses are just slightly under budget for the year. The claims reserve review requested by the Economic Affairs Interim Committee (EAIC) that was completed by Deloitte cost $48 thousand which was not originally in the budget projections. The allocated loss adjustment expenses are over budget in relation to costs for the Medicare set aside evaluations. Despite those added costs, the Old Fund funding status is still slightly under projections.

Chair Best called for questions or comments from the Board.

Mr. Dykstra asked for clarification on the demographics of the claimants in the Old Fund to try to determine the possible duration of the Old Fund liability.

Mr. Hubbard explained that Towers Watson analysis indicates that the Old Fund liabilities, based on current payment patterns, are projected to run until approximately 2054.

Mr. Dykstra requested that staff provide a two or three page executive summary of the profile of the Old Fund liabilities.

President Hubbard responded that the report would be prepared by staff and delivered to Board Members before the close of the Board meeting.

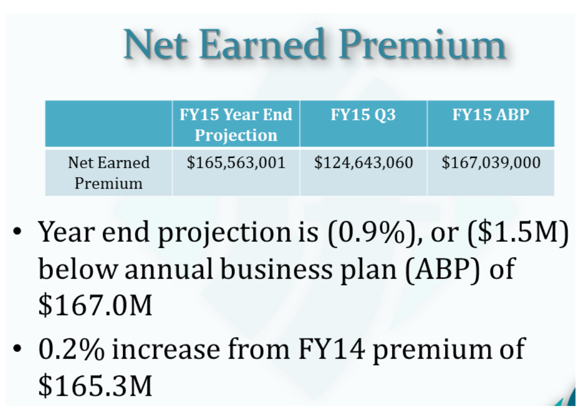
Mr. Zanto sought clarification about the differences observed between MSF's and LAD's actuarial estimates of the Old Fund ultimate liability.

Dan Gengler, Internal Actuary, reported that LAD contracted with AMI to estimate the Old Fund liabilities. He indicated he was operating from memory but could provide the approximate figures to the Board. Their estimation was about $120 million of unpaid liabilities as of June 30, 2014. Financial Risk Analysts (FRA), under contract with the Commissioner of Securities and Insurance (CSI), central estimation ranged in the mid $70 to $80 million. Towers Watson's estimation was $45 million.

Chair Best called for additional questions or comments.

C. *FY2015 Financial Report – Rene Martello, Controller*

Ms. Martello provided a FY2015 third quarter financial summary and emphasized that the net earned premium and projections as depicted in the slide shown below are under the year end projection by 0.9 percent.



She said there was $1.1 million of adverse development on prior years and it decreased recoverables in the reinsurance program by about $1.8 million. Loss expenses were projected at $16.5 million which was lower than the business plan of $21.2 million. Underwriting expenses were slightly above plan due to higher contingent commissions associated with the reinsurance program at third quarter. Investment income was projected to be $49.1 million, including about $7.2 million of realized gains, which is very close to projected. The net income was projected to be $44.8 million before dividend, compared to the annual business plan target of $40 million. After the $20 million dividend was applied, the projected net income was $24.8 million.

Ms. Martello provided an overview of the income statement summary projected for year end.

Income Statement Summary

Condensed Income Statement			
	FY2015 Proj.	FY2014	Variance
Net Premium Earned	165,563,001	165,271,880	291,121
Losses Incurred	122,546,303	127,812,156	(5,265,853)
Loss Expenses Incurred	16,510,511	15,538,264	972,247
Underwriting Expenses Incurred	26,792,171	20,538,085	6,254,086
Net Underwriting Gain/(Loss)	(285,983)	1,383,375	(1,669,358)
Net Investment Income Earned	41,908,942	42,457,728	(548,786)
Net Realized Capital Gains (Losses)	7,220,136	14,279,687	(7,059,551)
Net Income after Dividends	24,836,356	41,742,579	(16,906,223)
Prior Year End Policyholders' Equity	443,852,594	372,277,435	71,575,159
Net Unrealized Gains (Losses) on Inv.	6,936,806	28,036,023	(21,099,217)
Change in Non-admitted Assets	536,475	646,364	(109,889)
Other Adjustments - Pension Liability	(40,000,000)	1,150,193	(41,150,193)
End of Period Equity	436,162,231	443,852,594	(7,690,363)

-- GASB 68 requires MSF to record its proportionate share of the unfunded pension liability. An estimate of $40M was used for the year-end projection.

She then provided a refresher regarding the net pension liability and explained that it was the difference between the total pension liability and the market value of the assets on the measurement date. The old accounting standards called for only the employers share or MSF's contribution to be booked. The employers share was booked as an expense and there was no liability shown. Under the new standard effective at year end, MSF, as well as other state agencies, must show the proportionate share of its total statewide liability. As of June 30, 2014, PERS had their actuarial evaluation completed which determined there was a $1.6 billion unfunded liability for the entire PERS program. The employer share schedules and disclosure data should be available by June 2015. As an employer participating in the PERS cost sharing plan, MSF will use the data based on the June 30, 2014 evaluation for its fiscal year ending June 30, 2015 to record the proportionate share of the unfunded pension liability and expense.

Mr. Dykstra asked if MSF had the ability to control, fund and administer its own retirement program to alleviate MSF's reliance upon the state's retirement system and the unfunded liability.

Ms. Martello said it is not as simple as just receiving a bill for the pension amount. If MSF looked to create its own pension program, the unfunded liability would become due immediately, like an entire mortgage that suddenly became totally payable. She explained that it is not truly due at this point. PERS is considering all of the funds that would be needed to pay current employees, inactive employees and retirees and based on investment values at a point in time, what that liability would be. Over time, there could be adjustments that occur such as a higher contribution or plan changes to reduce benefits; however, there is a great deal of uncertainty and addressing the issues now would be shortsighted.

Mr. Dykstra noted that Illinois's pension fund has an unfunded pension liability of $18 or $19 billion based on an assumption of 18 percent return on their investment portfolio. He asked if MSF would be able to segregate its investments from the PERS assumptions if the Board felt the assumed investment return was not appropriate.

Ms. Martello said there was not a lot of flexibility to change the program; however, input from the MSF Board could be submitted to the board of the pension program. She noted that their assumptions are more reasonable than those of Illinois's and that a key disadvantage at this time is that the measurements are being taken from data completed on June 30, 2014. More recently investments have had greater returns and if the June 30, 2015 amounts were the measurement, MSF's unfunded liability would be even less.

Mr. Dykstra said when he reviewed his materials and saw the $40 million liability for MSF, he was very concerned at that amount and that it could go higher. He requested an Executive Summary covering the assumptions and processes used by the pension board so that he could have the opportunity to voice his concerns before the decisions are made and affect MSF's balance sheet.

President Hubbard said he was concerned about the effect of this liability on the balance sheet as well and asked Ms. Martello if the amount changes either up or down, how will any changes be reflected in the financial statements in future periods? Is it simply an adjustment to ending balance equity or will it be reflected in the income statement as there are changes in that amount?

Ms. Martello explained that it will be reflected as an expense on the income statement and show as a liability on the balance sheet. She also noted that the MPERA website contains some very useful information and summaries as well as frequently asked questions in relation to GASB 67 and 68. She said MPERA is also struggling to understand these new accounting standards and the guidelines and information manuals are voluminous and time consuming to review. It is expected that once the next set of analysis from the actuaries are received, the summaries will be issued and more information of that allocation will roll out to all of the agencies and local governments.

Mr. Dykstra asked that a representative from the pension board be invited to an MSF Board meeting to provide an overview and answer Board questions.

Mr. Hubbard assured Mr. Dykstra that MSF would extend an invitation to MPERA.

Chair Best called for additional questions or comments, there were none.

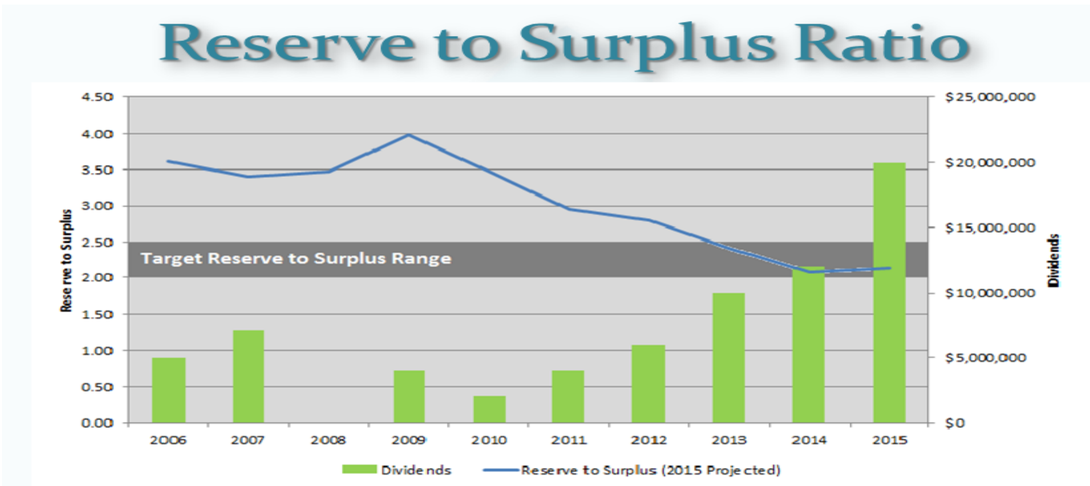
Balance Sheet Summary

Condensed Balance Sheet

	FY 2015 Q3	FY 2014	Variance
ADMITTED ASSETS			
Bonds	1,117,809,188	1,083,973,027	33,836,161
Equity Securities	167,704,746	167,515,006	189,740
Real Estate Investments	26,508,999	26,908,775	(399,776)
Cash and Short-term Investment	36,240,041	38,011,790	(1,771,749)
Other Invested Assets	82,720,090	74,841,190	7,878,900
Securities Lending Collateral	91,632,743	166,416,008	(74,783,265)
Total Investments and Cash	1,522,615,806	1,557,665,796	(35,049,990)
Other Admitted Assets	133,987,764	113,444,450	20,543,314
Total Admitted Assets	1,656,603,570	1,671,110,246	(14,506,676)
LIABILITIES AND EQUITY			
Reserve for Unpaid Losses	813,402,019	805,717,546	7,684,473
Reserve for Unpaid Loss Adjustment Exp.	119,342,246	118,880,034	462,212
Securities Lending Liability	91,632,743	166,416,008	(74,783,265)
Other Liabilities	161,337,339	136,244,064	25,093,275
Total Liabilities	1,185,714,347	1,227,257,652	(41,543,305)
Policyholders' Equity	470,889,223	443,852,594	27,036,629

-- Year-end Policyholders' Equity is projected to be $436.2M assuming a $40M pension liability is recorded as of June 30, 2015.

Ms. Martello provided a review of the balance sheet. She said total investments and cash decreased by $35 million due to a $75 million decrease in the securities lending program which frequently changes contingent upon how much is held as collateral. That category is directly offset by the liability for the same amount. Other admitted assets increased $20.5 million due to receiving unearned premium receivables. Reserves for unpaid losses and loss adjustment expenses were up by $8.1 million; a result of $91.9 million in the current accident year, $1.1 million of adverse development and $83.4 million in paids. As of third quarter policyholder equity was projected to be $436.2 million assuming a $40 million pension liability.



	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Rate Changes	3.0%	2.4%	-1.0%	-3.0%	0.0%	-4.0%	-20.0%	0.0%	-6.0%	0.0%

Ms. Martello reviewed the reserve to surplus ratio graph that provided a review of the measures management and the Board have taken to achieve the target to reserve surplus. The target reserve range is 2 to 2.5 to one. The blue line on the graph is the reserve to equity ratio and the green bars reflect dividends paid. Rate changes are reflected at the bottom of the graph by year. As the target range was achieved the business was able to increase dividend amounts and consider rate reductions.

Chair Best called for questions or comments. Seeing none she moved to the next agenda item.

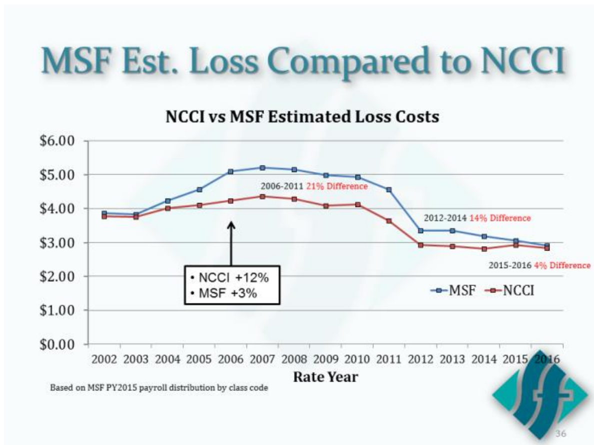
D. Overview of Montana State Fund Class Rating Process – Dan Gengler, Internal Actuary

Mr. Gengler provided an overview of the class rate making process. He explained how carrier rates relate to the NCCI loss cost filing and how current MSF rates compare or benchmark to the market. He also addressed the key decision points for the Board in setting the rates and provided insight into how those decision points are likely to change due to the passage of SB123.

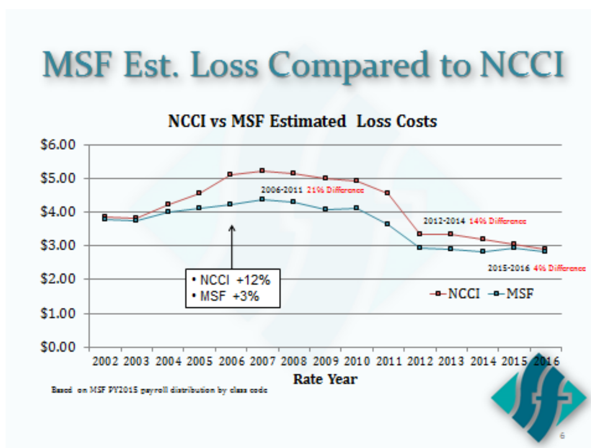
Mr. Gengler said MSF establishes about 2,100 rates, utilizes 425 class codes and five rate tiers but that can be reduced to a broad average for the sake of making comparisons. NCCI estimates the rate for each class code necessary to cover the lifetime benefit cost of all the claims incurred and the lifetime cost of the claims administration. The rates established by a carrier begin with the loss cost but also include an additional amount to cover the costs of general overhead expenses, commissions, profits and contingencies, offsets for investment income and underwriting off balances. He provided an overview of how MSF's loss costs are established in comparison to NCCI's and explained that this provides a mechanism by which carrier rates can be compared to one another.

Mr. Gengler presented the slide below and noted that the slide was incorrect and should reflect that MSF is depicted by the red line, and NCCI by the blue line. [Note: The corrected slide is also included in these minutes.]

Incorrect Slide



Corrected Slide



Mr. Gengler explained that in the early 2000s, NCCI's and MSF's loss cost estimations were approximately the same but from 2006 until about 2011 the differences were as high as 21 percent. In 2012 the gap narrowed and has continued to close further with NCCI's 2016 loss cost only four percent above MSF.

He said that the key board decisions begin with formally adopting the NCCI loss costs as a basis for MSF's rates. He noted that this decision point will become moot under SB123 because under regulation with CSI, we will be required to use NCCI's loss cost. The second decision point is to approve exceptions to the NCCI loss costs and MSF has 14 special class codes such as the agricultural and state agencies class codes. Those class codes were recently adopted by the Montana Classification and Rating Committee for use in Montana so adoption of these exceptions will not be necessary in future years. However, the Board must approve them for the coming rate year. He noted that there were no deviations for this year. He said MSF's independent consulting actuary reviews and certifies to the Board that the loss costs are not inadequate, excessive or unfairly discriminatory.

Mr. Gengler said the third decision point is the tiered rating plan which provides price differentiation for MSF customers by offering five different rate levels. The Board approves the criteria for assignment of policies and the consulting actuary also reviews and certifies the tiered rating plan. The final decision is approval of the lost cost multipliers for the five rate tiers which includes consideration of the level of expenses and contingencies as well as contribution to equity and assumed investment yield.

Chair Best called for questions or comments.

Senator Keane provided some handouts before addressing the Board. He noted that he had attended MSF Board meetings in the past when he was the liaison from the House of Representatives. He said he has been working on issues regarding MSF for a number of years because he is very concerned about the equity that has accumulated. As the ultimate decision makers for MSF, he felt it would be appropriate for him to review some things with the Board while they are discussing setting rates. He said he believes the rates have been set too high for a number of years and thinks MSF should decrease its rates by 15 percent or $25 million. He said that according to Montana statute, MSF is to be no more or no less than self-supporting and when the premium rates are set, that code is to be taken into consideration. He said that when setting rates, MSF has built into the premiums contribution amounts to its equity and he wanted to show the Board why that should not have been done. He said MSF should have been returning part of the investment income to the people who pay the premiums over the past number of years. He said that the policyholders receiving dividends have to pay a tax on those dividends so lowering the premium would be a better benefit. He said by lowering the premiums it would reduce the company’s costs and the companies could use that to provide health benefits or address other issues. He said he believes it is very important to reduce rates especially if MSF is still able to cover its costs. He reviewed portions of MSF’s financials, information he received during the legislative session, and noted that as of December 31, 2014, MSF had $1.7 billion at the Board of Investments. After further review, his bottom line was that by mid-July MSF’s equity will be at just about half a billion dollars. He said that was substantially above what the State of Montana has and the State spends $10 billion a year. He asked how that benefits the policyholder. He said that each year from 2012 MSF has been contributing $1.9 million to the equity and accumulating all that money and he believes it is time to take a look at that. Does MSF need half a billion dollars? He said he knows that MSF is trying to get to the ratio line and he knows that the actuary will tell the Board what is needed to achieve that but he is very concerned that the policyholders are not getting the break that they deserve. He does think that 15 percent, $25 million put over into premiums would help every small business that MSF insures in the state of Montana. He said he would bet his boots that the Board could return in November and still declare a $25 million dividend and not hurt equity. He believes the Board are the ultimate decision makers at MSF and they need to start taking a hard look at the increase in equity. He said he knows that MSF will come up with every excuse because he has heard them all but he wanted the Board to think of the policyholder and the worker out there. He said if the Board lowers these premiums, that frees up an amount of money that those people have to pay that allows at least a worker to be able to get a raise or maybe get something in retirement. He said he cannot in his good conscience, see why MSF has to accumulate more than the state of Montana in equity. He encouraged the Board to take a hard look at the numbers on the sheet he provided and help out every business in the State of Montana. He said the Board needed to take a look at that $50 million out of $500 million, even if they take $40 million – “let’s say you take $100 million off, count the 40 and another 50 is 90, you are still at $400 million in equity.” He said he thought there was some way this Board should review increases in equity and how it relates to premium in all the future dealings.

Chair Best thanked Senator Keane.

Mr. Dykstra thanked Senator Keane and explained that when he joined MSF, he came to his position with concerns about how MSF was administered and concerns about his rates. He said he also had the experience of having paid the surcharge for the Old Fund. He noted that the Old Fund went bankrupt because people who did not know how to run a workers' compensation insurance company were the ones establishing the rates. He said in his four years serving on the Board he has really focused on the equity and loss reserves. He said there are three different actuarial analytics completed on MSF's reserves and equity each year and he has watched the number increase each year. He said he is a small businessman with 40 employees and his company does $3.5 million a year. In comparison, MSF is almost a $2 billion enterprise with 300 employees. He said it puts him in a difficult position as a Board member because the equity amount is getting close to $500 million - $500 million just sitting in a piggy bank. On the other side of the coin, the actuaries report there is a 30 - 50 year tail of liabilities out there that is over a billion dollars. There are also the unknown consequences of HB334. He said he believed it is Senator Keane's opinion that there is too much money but that Mr. Dykstra has a fiduciary obligation as a Board member to try to make sure that just as the statute reads, there is not too much, not too little, it is just right and he believes in the science associated with looking at the future value. He said the feel good response would be to agree with the Senator and vote to give back a substantial sum but based on actuarial analytics and the previous history of state fund, he was extremely reluctant to do something that is adverse to the recommendations of MSF's independent actuary. He noted there are two other actuarial examinations that are completed under the cover of other elements of state government. He asked Senator Keane if he has some basis other than his personal opinion for taking that kind of action.

Senator Keane thanked Mr. Dykstra for the question and noted that he was one of the people who was actually working to pay off the Old Fund liability. He said that is the argument that is used to debate him that "we don't want to go back to that Old Fund liability", he said "we are so far back from the Old Fund liability it's unbelievable right now." He said his recommendation was not just his opinion, it is the opinion of the numbers and they speak for themselves. He said the Board has an obligation under its fiduciary responsibility to say what the number should be and he told the Board that $500 million is too much. He said it was not his intent to have the Board just throw money away, he thinks this needs to be done prudently. He said $25 million out of $500 million is a small step to try to get your hand around the deal between premiums and equity. "I think you, as a responsible board member and all the board members have to address that issue. Why should the businesses of Montana be paying more than they should. That's what the code says, that's your [the Board's] responsibility."

Chair Best called for additional questions.

Mr. Mihelish thanked Senator Keane for the perspective regarding taxing dividends and said he did not take that into account. He also thought Senator Keane's comments should be listened to because as a businessman in Montana for 35 years, he believes in Montana and the Montana economy. He said the economy struggles and one of the reasons is the high expense of workers' compensation. He said if the Board can prudently make a move to reduce rates in some way that is advice that should be taken into account because he has looked at businesses attracted to the state of Montana and upon review of our workers' compensation rates compared to our neighboring states, it is not good. He acknowledged that benefits are paid at different levels in the neighboring states but felt that if the Board can make it a goal to prudently reduce rates, he thought that would be good for Montana.

Mr. Miltenberger said he thought it would be very easy for the Board to push off a strategic decision like this onto the actuaries and thought a better measure would be to monitor the Risk Based Capital benchmark that would provide a singular percentage that the Board could discuss and then render a decision based on that level.

Mr. Brenneman read from the Montana Code Annotated that Senator Keane provided to the Board members and highlighted the portion that read: "In determining premium rates, the state fund shall make every effort to adequately predict future costs. When costs are not clear and difficult to predict the state fund shall use the prediction calculated to be more likely to cover these costs rather than be less likely to cover those costs." He said as a Board member he has struggled with determining the correct response to this test because scenarios exist in which a great deal of money might be needed requiring enormous premium rate increases. He also noted that he has attended interim legislative committee meetings and at one, the committee compared the MSF Board members to the directors of Enron and other massively failed and catastrophic companies. He explained that he too is a policyholder and rate payer and has every incentive to arbitrarily vote for lower rates because there have been years when he has struggled to make that payment as a small business person. He said he believes that as Board members in a more or less voluntary position, there is every incentive to make these rates as low as possible and the fact that the Board sets them based on the information provided speaks pretty strongly to the fact that there must be a fair amount of logic that the Board listens to in order to do this.

Mr. Dykstra said his workers' compensation premium is the second biggest expense he has behind payroll and he does not take an adversarial position regarding the discussion about equity. He said he would prefer to wait until MSF is under the regulation of CSI to get a better understanding of what their rate analytics would require.

Chair Best thanked Senator Keane for attending this Board meeting and told him she hoped he would continue to come to the meetings. She said she believed the Senator has probably seen that this Board vigorously debates these issues and honestly wrestles with the decision and challenges MSF management all the way to Mr. Hubbard who welcomes the debate and the vigor. However, she said she was not an expert on rates, and does not pretend to be, but she does listen hard and she listened to the Senator. She said she is not convinced, frankly, that workers are getting a square deal legislatively. She said she believed Montana is balancing rates on workers who are losing on their end of the deal.

Mr. Zanto said he thought Senator Keane's point regarding the tax impact to employers receiving a dividend was an important one and a rate reduction would benefit all policyholders, whereas with a dividend, only qualifying customers receive that payment.

Mr. Grieg noted that during dividend discussions in November, when he will address the level of policyholder equity and the potential dividend that the Board can safely declare, the NAIC RBC threshold is taken into account. That threshold is approximately $100 million for MSF. The issue with the RBC is that it is primarily used to identify the companies that are in a weak position and MSF does not want to get back to being in a weak position. He said he would agree with the Senator that if everything goes as planned, $500 million of policyholder equity would be too much but the purpose of the policyholder equity is to cover unexpected scenarios that have significant financial impacts. There was a financial catastrophe in 2008 where stocks dropped by approximately 50 percent and bonds dropped by 10 percent, which hit policyholder equity by about

$94 million. He said in November, Towers Watson also does an economic capital model analysis that also supports that as long as everything is going fine, MSF policyholder equity is enough but what happens when the market hardens and MSF's market share grows to 75 or 80 percent and there are several years of adverse medical development? He said policyholder equity is there for worst case scenarios.

Mr. Brenneman added that the dividends being taxed is a non-issue because if the rates were lower, the policyholder would have to pay the taxes on the income that was not charged for premium so there is no actual loss.

Ms. Moss took a moment to greet her Senatorial colleague and thanked him for his attention to this issue. She said the Board members are stewards of public resources, whether working on the investment portfolio or the lives of the workers and making sure they are safe and have good working environments. She said she truly respects the information and analysis that occurs and the decision making at the MSF Board. She said the questions the Senator raised about keeping the workers in mind and safe are ones that the Board should always keep in mind while balancing that with making sure that MSF has the resources are needed for future expenses. She said it is very complicated and unpredictable but it is something that is the Board's responsibility to do.

President Hubbard thanked Senator Keane for attending and said he hoped the Senator would stay for the remainder of the meeting when the decisions would be made. He told the Senator they were going to have to agree to disagree. He said Senator Keane is a politician elected by his constituency and Mr. Hubbard is the CEO of an insurance company. He started with MSF in 1989 just when the fallout from the Old Fund was palpable and deep and a half billion dollar unfunded liability existed. He said he was part of the team that worked to dig State Fund out of the hole with the help of a great legislative body that recognized that political decision making does not work for an insurance company. He said with all due respect to Senator Keane, he believed the Senator's approach matches the ones taken then. He said it seems to be the kind of thinking when just the numbers on a page are reviewed because they are large numbers and the conclusion is drawn that they are the wrong numbers or that some unfairness or injustice is being worked against the policyholders or the injured workers of the state of Montana. He noted that no other insurance company that he was aware of conducts its decision making in an open forum but he believed this method enhances the transparency and quality of discussion. He said that Senator Keane remarked that some of the investment income needs to go back to the policyholders, and Mr. Hubbard noted that it does. By law, the Board must assume investment income and reduce the rate in anticipation of that. He said the Senator's discussion was really about balance sheet management and the largest number on the balance sheet is the $937 million of liability. He also noted that no state entity has unknown expenses that can last and unfold for decades. State government entities close their balance sheet at the end of the fiscal year and LAD reviews and closes all the costs associated with its operations. MSF does not have that luxury. He said it is more difficult to run a workers' compensation insurance company than state government or a manufacturing company. He said he agrees that MSF should be no more nor less than self-supporting but it is important to pay attention to both sides of those equations. When HB334 was passed, MSF took a 20 percent rate reduction and bet that those savings would actually be realized; however, that was based on termination of medical benefits five years from the date of injury on most permanent/partial disability cases and the first claim hitting that threshold will not occur until July 1, 2016. That is a tremendous amount of uncertainty on whether those savings will come to fruition. If they do not, surplus will have to be used to stabilize the impact to customers. The financial strength of MSF is good for Montana businesses particularly because of the stability offered should a bad year occur. The Board would not necessarily have to address the situation with a rate increase just to weather the storm. Mr. Hubbard said he does not disagree with Senator Keane's premise, however, any actions that require

MSF to disgorge $100 million of assets without any actuarial support are irresponsible. As an insurance company executive it would be irresponsible and he would not make such a recommendation to the Board of Directors. The Board is required by law to use an independent consulting actuary in making its decisions which is their fiduciary obligation. The legislature does not have that fiduciary obligation so he said his advice would be to listen to the consulting actuary. He added that he believed that questioning management's recommendations is absolutely appropriate and debate on these decisions and issues is important. He also encourages any and all legislators to attend these board meetings and weigh in on the issues but also asked that people who are opining and passing judgement on the management of this body take the time to learn about the challenges and the decision-making pressure points that this Board faces. He said it is good to listen but it is also important to recognize that the Board and the MSF management team are ultimately accountable.

Senator Keane said he was thrilled that the actuary actually said that $500 million may be too much. He also clarified that he never said $100 million, he said look at $25 million. He said he thinks a $25 million reduction in rates to the people is not unfair for MSF to do at this time. The Board will look at dividends later knowing how the money comes in. MSF has more money than the State of Montana and he thinks that having that amount of money, more than the state of Montana, which has a lot more exposure in a lot of different ways, he just cannot wrap his mind around that. He said he has never questioned the reserves because they actually help generate interest and protect those claims; however, the increase in equity has to be addressed. He added that he does run an insurance company, he runs this insurance company (State Fund) that is a state agency and he runs this agency so Mr. Hubbard is not the only one. He said he is elected to run this agency and that is why he brought this up.

Mr. Miltenberger posed a number of questions to Mr. Greig regarding MSF's RBC level and seeking help in establishing a level that the Board could use as a threshold to determine if the equity level is too high or too low. He was hopeful that if the Board sat down for an hour or two and spent time digesting the RBC requirements and establishing a level that they felt appropriate, that could be used by the Board members to determine rate levels and dividend declarations.

President Hubbard said that the RBC level for MSF is addressed in SB123 with a Company Action Level (CAL) of 400 percent. He noted that a private carrier's RBC CAL is typically 200 percent; however, during the legislative process for SB123, legislators were concerned that MSF did not have a financial backstop other than the people of Montana and wanted an early warning mechanism for insolvency.

Mr. Barry clarified that currently, for MSF, at June 30, 2014, a 400 percent RBC would be about $227 million, and MSF is at $430 million.

Mr. Dykstra said he was delighted that Senator Keane attended this Board meeting and hoped he was planning to attend every meeting, particularly the rates and dividends meetings. He said that Senator Keane notified the Board and President Hubbard that he was elected to run MSF and Mr. Dykstra said he gets very frustrated that there is an entire building of people elected by their constituents to run MSF yet other than the legislative liaisons from the Economic Affairs Interim Committee (EAIC) he has never seen another legislator at any of these meetings. He said Senator Keane was the first legislator, to his knowledge, who has shown up in the four years he has been on the Board. He sincerely thanks Senator Keane for taking the time to attend this meeting.

Chair Best called for additional comments or questions; there were none.

III. Ratemaking Decisions for Fiscal Year 2016

A. Volume Discount – Peter Strauss, VP-Operations Support
Chair Best called the meeting back to order after a brief break.

Mr. Strauss thanked Ms. Byers and her staff for providing the Old Fund statistics that were requested earlier in the meeting.

Mr. Strauss said Administrative Rule 2.55.403 permits MSF to provide a volume discount program based on premium levels. He said every year MSF reviews its premium programs to assure they are performing as expected. To properly respond to changing costs and losses generated by policies, MSF surveys the competition to determine that market changes have not inadvertently been missed. As a result of that effort, management is again asking the Board to maintain the volume discount at the same level as last year. Most competitors, though not all, have a volume discount program. Mr. Strauss asked the Board to approve the proposal to maintain the current volume discount program for Fiscal Year 2015.

FY2016 Recommended Volume Discount Program

No change from FY15

Layer	CURRENT Threshold	Discount
1	$ 0 - $12,000	0%
2	$ 12,001 - $150,000	5%
3	$ 150,001 - $750,000	7%
4	> $750,000	9%

Chair Best called for questions from the Board, public and staff; there were none.

Mr. Dykstra moved the Board approve for new and renewal policies in effective July 2, 2015 to July 1, 2016, the volume discount table for modified standard premium as recommended by Montana State Fund management. Mr. Brenneman seconded the motion. Chair Best asked for any questions or comments from those present. There being none, she called for the vote and the motion passed unanimously.

B. Terrorism & Catastrophe Rate – Peter Strauss, VP-Operations Support
Mr. Strauss reminded the Board that last year Congress failed to enact an extension of the terrorism reinsurance act before the end of the year. He noted that at the MSF Board meeting held in December, the Board authorized MSF to continue to collect the one cent per $100 of payroll for the terrorism coverage rate and the one cent per $100 of payroll for the catastrophe rate to assure those exposures were still covered. Congress enacted a new law to extend the terrorism risk insurance act from December 31 of 2014 through the end of 2020. There were some changes to the program; however, the passage of this program assures MSF that there is a Federal backstop for terrorism losses. NCCI has filed with CSI a two cent per $100 of payroll rate to cover terrorism and catastrophe and MSF management asked that the Board approve those rate charges for policies effective July 1, 2015 through July 1, 2016.

Chair Best called for questions from the Board.

In response to the Terrorism Risk Insurance Act of 2002, as renewed, amended and extended by an act of Congress in December 2005, and extended under the Terrorism Risk Insurance Program Reauthorization Act (TRIPRA) through December 30, 2014, and as extended in January 2015, Mr.

Brenneman moved the Board adopt the NCCI lost cost filing for Terrorism and Catastrophe of 2 cents per $100 of payroll for new and renewal policies effective July 1, 2015 to July 1, 2016. Mr. Zanto seconded the motion. Chair Best asked for any questions or comments from those present. There being none, she called for the vote and the motion passed unanimously.

C. *Multiple Rating Tier Program Modifications – Dan Gengler, Internal Actuary and Russell Greig, Director-Towers Watson*

Mr. Gengler explained that many insurance companies, including MSF, maintain several rate levels and said it is important for MSF to maintain this pricing function to remain competitive and still serve as the guaranteed market. He said there have been some friction points for current stakeholders that MSF asked the consulting actuary to review and provide, if possible adjustments to the program that could address these concerns. He said that Phase 1 of this project was designed to implement recommended parameter changes only for July 1, 2015 and in Phase 2, explore additional structural changes for a possible future project. He noted that the proposed process must be actuarially sound so it can be certified by Towers Watson and meet the regulatory review of CSI.

Mr. Gengler outlined the stakeholder concerns and provided a review of the changes that could be instituted. The concerns were that the e-mod and hazard code variables were counterintuitive, there was rate volatility for small accounts and there was a real desire to reduce the range in the loss cost multipliers (LCM). Rate tier assignments were also difficult for agents to calculate or anticipate and there was a desire to increase the ratable claim threshold and have the rate tier assignments strictly correlate with the experience modifier.

Mr. Gengler said MSF was able to address the e-mod and hazard code variable by removing them from the process and was able to do so without loss of predictive power to the process. Rate volatility was partially mitigated by reducing the range in LCMs. There are approaches under consideration and development to address the agent's concerns with the difficulty in accurately calculating the rate tier assignments. He said the increase in the ratable claim threshold was not recommended by Towers Watson because about 40 percent of MSF's non-zero loss claims are under $500 so the process is currently ignoring 40 percent of our claims experience and is only built on 60 percent. Increasing the ratable claim threshold would compromise too much of the predictive power of the process. He also said it simply was not possible to always have rate tier correlated with the e-mod because there are exceptions where the e-mod is frequency driven vs. severity driven.

Mr. Gengler introduced Russell Greig, Consulting Actuary, Towers Watson.

Mr. Greig provided an overview of the background that it took to develop the tiered rating process. He said establishing the price of workers' compensation based only on the class code can lead to inequities because the spread of business in a class code is very broad and quite heterogeneous. The NCCI experience rating goes a long way to reduce the inequities and provide incentives for safety, but still leaves room for improvement because it is based on older data than that used in the tiered rating process and is not specific to MSF. Tier rating reflects the variability in risk that is not captured in the experience modification or classification codes and therefore improves the equity reflective of a risk that has a lower likelihood of loss or a higher likelihood of loss. MSF slots its insurers into five rating tiers which have been, and continue to be, effective in supporting the equitable and objective treatment of MSF's policyholders.

He explained that predictive modeling has greatly improved the traditional insurance pricing techniques. It is an advanced application of statistics, data mining and economic theory to better understand the true drivers of risk. Traditional techniques are based on analysis of the impact of a single rating factor on an observed event in isolation and do not consider the correlations and interactions in the data. He said with predictive modeling the data can be finely split while still maintaining statistical credibility.

Mr. Greig explained that Towers Watson was engaged to recommend revisions to MSF's rating tier structure and parameters to mitigate the stakeholders' concerns while maintaining actuarial integrity. He provided a review of the process that was used to complete the analysis and develop the recommended changes. He said the proposed/revised structure enhances price equity while more directly tying tier assignment to historical experience. The stability of the proposed structure is similar to that of the current structure and improves the prediction of future propensity to incur or not incur loses.

Chair Best called for questions or comments from those present.

Mr. Dykstra asked a number of questions about the number of workers' compensation insurers he worked with and his experience with dealing with multiple tiered rating systems. He also asked Mr. Hubbard, based on his experience with American Association of State Compensation Insurance Funds (AASCIF) how many state funds and private insurers use a tier rating system.

Mr. Greig said Towers Watson works with a lot of workers compensation insurers and provided an overview of his experience in that industry. He said he has five large workers compensation insurance clients and does a lot of large self-insureds. He said workers' compensation is approximately 99 percent of the work he does. He noted that of the four workers' compensation clients that he does analysis for, two have tiered rating programs.

President Hubbard said he was not able to provide an exact number of state funds utilizing tiered rating but added that for the state fund population, most of his colleagues do file multiple rating tiers. He said some state funds, such as CopperPoint in Arizona, have mutualized and become fully private so are now exploring multiple lines. Carriers often have carrier groupings and customers are determined eligible for a rate and placed in that particular company. Mr. Hubbard said MSF's customer placement in the tiered rating program is much more transparent than just receiving a quote from a private carrier.

Mr. Greig clarified that a workers' compensation insurer writing across a group of states or a region and writing more than $75 million of workers' compensation premium a year, is more likely than not to have a tiered rating structure as well as one based on predictive modeling.
Mr. Dykstra asked if it was safe to say that the tiered rating system is industry best practice.

Mr. Greig said yes.

Chair Best called for questions from the Board.

D. *Multiple Rating Tiers/Actuarial Certification – Dan Gengler – Internal Actuary*
Mr. Gengler said that management requests the approval of Tiered Rating 2.2 for the July 1, 2015 renewal process. He reiterated that 2.2 eliminated the experience modifier and hazard code as rate variables in the tier rating process. He reviewed the changes with the Board and explained the major shifts. He asked that the Board approve the tiered rating criteria as proposed and noted that Board members had received the certification letter from the consulting actuary that this process results in rates that are not unfairly discriminatory and improves the equity in pricing for MSF policyholders.

Tiered Rating 2.2 - Table of Factors

Claim Frequency Value	Factor
No History	1.100
0.00-0.00	1.000
0.01-0.10	1.020
0.10-0.15	1.060
0.15-0.20	1.090
0.20-0.25	1.110
0.25-0.30	1.130
0.30-0.35	1.170
0.35-0.40	1.190
0.40-0.45	1.210
0.45-0.50	1.240
0.50-0.55	1.260
0.55-0.60	1.290
0.60-0.70	1.320
0.70-0.80	1.360
0.80-0.90	1.420
0.90-1.00	1.460
1.00-1.25	1.520
1.25+	1.560

Claim-Free Tenure Value	Factor
New	1.100
0	1.100
1	0.980
2	0.950
3	0.920
4	0.885
5	0.850
6	0.815
7	0.780
8	0.740
9	0.700
10+	0.660

Account Size Value	Factor
<$1,500	1.600
$1,500-$2,500	1.500
$2,500-$5,000	1.400
$5,000-$8,000	1.300
$8,000-$12,000	1.150
$12,000+	0.950

Rate Tier	Lower	Upper	Relativity
Tier1	0.000	0.870	0.750
Tier2	0.870	1.100	0.900
Tier3	1.100	1.250	1.000
Tier4	1.250	1.600	1.200
Tier5	1.600	& Above	1.450

Two-Tier Swing Limit

Renewal policies shall be limited to a maximum change of two rate tiers from one policy period to another.

Chair Best called for questions.

Mr. Mihelish thanked MSF for listening to the concerns that he brought to management regarding the tiered rating process. He noted that he was not a huge proponent of the five factor tier rating system because he believed it was too complex and heard from many customers and agents that agreed with him. He said he believed it has been made less complicated; however, questioned the cases that “fall through the cracks” where it does not appear fair. He wanted to know if the underwriters at MSF had the authority to change the placement if they did not believe it was appropriate.

Mr. Hubbard explained that MSF does not underwrite polices that are under $12,000 estimated annual premium so placement would rely on the rate tier modeling. He noted that there will always be someone who feels their pricing is not fair and there is no way to eliminate that and still maintain any pricing distinction in the tier rating process. He said the underwriters do not have the authority to apply judgmental pricing tools on small accounts where the experience volatility is tremendous. Typically smaller accounts do not have, and cannot afford to establish, safety programs to mitigate the tremendous losses that could result from one severe accident turning a $1,500 account into a loss for five or ten years.

Mr. Gengler added that with regard to rate tier assignment the rules and criteria must be established in advance and MSF must rigidly follow those rules and thus would not be allowed to judgmentally move an account from one rate tier to another. The LAD reviewed MSF’s pricing practices and recommended that there should be no kind of judgmental override and MSF has complied with that recommendation. MSF will also be subject to that same notion under regulation by CSI.

Chair Best called for additional comments or questions; there were none.

Mr. Zanto moved the Board approve, for new and renewal policies effective July 1, 2015 to July 1, 2016, the Tiered Rating plan which consists of 5 Rating Tiers, and that policies be assigned to the tiers based on the factors as presented by management. Mr. Miltenberger seconded the motion. Chair Best called for discussion and public comment. There were none, so she called for the vote and the motion passed unanimously.

E. *NCCI FY 2015 Montana Loss Costs Filing Update – Dan Gengler, Internal Actuary*

Mr. Gengler explained that the NCCI loss cost filing is the basis for MSF’s rates that must be formally adopted by the Board under administrative rules. The administrative rules offer the choice of using the new filing to be effective July 1, 2015 or to use the old filing effective last July 1. The circumstances by which management would recommend not using the prospective filing are extremely narrow: therefore, this item was on standing approval for many years. Converting MSF from a fiscal year to a calendar year creates a bit of an issue as far as how that standing approval motion was worded so management asked the Board to take a motion and vote on this particular item even though it is relatively pro forma.

F. *Adopt NCCI Filings/Loss Costs Filing Effective July 1, 2015- Dan Gengler, Internal Actuary*
Mr. Gengler said with respect to the NCCI loss cost filing, a decrease is reflected in NCCI's previously filed loss cost of 4.8 percent on average. This varies widely by individual class code. Individual class codes can decrease as much as 31 percent or increase as much as 21 percent but the overall average is 4.8 percent which also varies by NCCI's industry groupings. He said management's recommendation is to use the most recently filed NCCI loss cost filing as the basis for MSF's rates. This issue will become moot next year because under SB123 MSF will be required to use the NCCI loss cost filing.

Chair Best moved the board adopt the NCCI filed loss costs for rates applicable to new and renewal policies effective July 1, 2015 to July 1, 2016 for Montana State Fund classification codes, except those loss costs for classification codes approved as exceptions by the board. Mr. Dykstra seconded the motion. Chair Best called for discussion, comments or questions. There was none.

G. *Adopt Loss Cost Exception Analysis/Actuarial Certification – Dan Gengler, Internal Actuary* –Mr.
Mr. Gengler said there are a small number of modifications that MSF makes to the NCCI loss cost filing; MSF special classifications and any necessary deviations. This will be the last year this will be required because the agricultural code and state agencies and other governmental entities will be contained in the NCCI loss cost filings. There are no deviations from the NCCI loss costs this year; however, adoption of the MSF special class codes will still have to be addressed. He noted that Towers Watson provided a certification of the loss costs and requested that the Board approve the loss cost exceptions.

Chair Best called for questions or comments. Seeing none, she called for a motion.
Ms. Moss moved the Board to adopt the recommended modified loss-costs for the classification codes identified by management. She moved the Board to accept the consulting actuary's certification of the loss-costs proposed by Montana State Fund management. The loss-costs will apply for rates applicable to new and renewal policies effective July 1, 2015 to July 1, 2016. Mr. Dykstra seconded the motion. Chair Best called for questions, comments or discussion; there were none. She called for the vote and the motion passed unanimously.

H. *Minimum Premium and Expense Constant – Mark Barry, VP Corporate Support*
Mr. Barry explained that management was requesting approval on the expense constant and loss based minimum premium for small accounts for the year. Expense constant is the charge to every account, regardless of size, for the costs expected to be incurred for issuing a policy and is not inclusive of all expenses; just those common to renewing or writing a new policy. The current expense constant level is $170.

The minimum premium or loss base premium is primarily charged to small accounts (those with little or no payroll) to cover the loss based portion of their exposure that they might have from medical and wage loss. The current level is $235.

Mr. Barry said management is requesting approval of an expense constant of $170 to be charged to all new and renewal accounts effective July 1, 2015 and a loss base minimum premium of $235.

Chair Best called for questions or comments from the Board; there were none.

Mr. Mihelish moved the Board approve an expense constant of $170 for all new and renewal policies effective July 1, 2015 to July 1, 2016. In addition, he moved the Board approve the amount of $235 for the loss based portion of the Minimum Premium so that the total Minimum Premium is $405 for new and renewal policies effective July 1, 2015 to July 1, 2016. Mr. Brenneman seconded the motion. Chair Best called for discussion; there was none so she called for the vote. The motion passed unanimously.

IV. Actuarial Report – Russell Greig, Consulting Actuary – Towers Watson

Chair Best welcomed Mr. Greig back to the podium.

Mr. Greig summarized Towers Watson's analysis in support of MSF's management and Board selections of loss cost multipliers for policies incepting from July 1, 2015 to June 30, 2016. The recommended loss cost multipliers cover the expected losses and expenses and generate a reasonable contribution to policyholder equity to cover the risk that is assumed by MSF from the individual policyholders. He included in his presentation an overview of their methodology, key management decisions, an estimation of historical ultimate losses of the premium, expenses, and management's recommendations on investment income on cash flow, contribution of policyholder equity and provision for adverse deviation and indicated loss cost multipliers.

Indicated Loss Cost Multipliers

Assumed Investment Yield on U/W Cash Flow: 2.50%

Management Recommended Target Contribution to Equity: 0.0% of Earned Premium

Projected Loss Experience	Indicated Loss Cost Multipliers				
	Tier 1	Tier 2	Tier 3	Tier 4	Tier 5
Low	0.826	0.992	1.102	1.322	1.598
Actuarial Central	0.887	1.064	1.182	1.419	1.714
High	0.958	1.150	1.277	1.533	1.852

Alternative Scenarios +/- Actuarial Central Estimate LCM	
-1.0% Contribution to Policyholder Equity	(0.01)
1.0% Contribution to Policyholder Equity	0.01
2.25% Assumed Investment Yield	0.01
2.75% Assumed Investment Yield	(0.01)

Mr. Dykstra asked if moving under the regulatory umbrella of the CSI would have any impact on rates and reserves.

Mr. Greig said it would not. He said MSF sets actuarially sound rates and reserves and carries a policyholder equity that reflects strength versus weakness. Over the years of the fund, MSF has relied on actuarial principles and said he believes the insurance department wants MSF to continue to be run based on actuarial principles. That means that MSF is going to be regulated like any other insurance company. Regulators want adequate rates, they want adequate reserves.

Mr. Dykstra asked if the state insurance commission would be ordering a fourth actuarial analysis or will they be using one of the three that were currently generated.

Mr. Hubbard responded that the implementation of SB123 provides the authority of the insurance commissioner to conduct financial examinations of MSF which would include rate reviews. Rates above NCCI's loss cost are considered file and use; however, a rate or loss cost multiplier below NCCI's LCM would be subject to review because there is concern that it would be inadequate. CSI's reviews will address whether rates are excessive, inadequate or unfairly discriminatory.

Mr. Miltenberger asked for clarification from Mr. Greig that a recommendation for a contribution to policyholder equity was not being recommended for this year.

Mr. Greig said that was correct.

Mr. Miltenberger had additional questions regarding use of the RBC as the standard for the Board to use in determining financial strength of MSF and setting the bar at the 400 percent described as the measure for review in SB123.

Mr. Greig said he does not recommend targeting to the RBC. That measure is typically used to identify weak companies. He said a better target is the level of policyholder equity comparable to private carriers and a comparable reflection of MSF's financial strength. He said 99 percent of insurance companies are above that minimum RBC threshold and those above are not targeting the RBC level because it would mean reducing rather than building financial strength. Mr. Greig said he would provide additional information in November regarding policyholder equity for consideration during the dividend discussion. He noted that his report will include a comparison to risk based capital which for MSF is a non-issue. He also compares several leverage ratios from other state funds, the premium to equity ratio, a look at gross leverage and net leverage. He said the most important ratio is the reserve to equity ratio which is the basis for MSF's target; the 2 to 2.5 to one ratio of reserves to equity. He said that means if the reserves are increasing, more equity is needed to absorb the variability in the reserves. If reserves are decreasing, the amount of policyholder equity can also decrease because that target ratio has been met. The recommended range looks at reserves relative to equity which is based off the economic capital model that Towers Watson completes to determine if there is enough to continue to run as planned. This model also quantifies what happens if MSF has a significant number of years of adverse development or a financial catastrophe. This provides a feel for the probability of insolvency given a certain level of equity. Towers Watson has determined that the 2 to 2.5 to one reserve to equity ratio provides the Board with a small probability of insolvency.

Chair Best called for additional comments. There were none and she called on President Hubbard for his presentation.

V. Ratemaking Decisions – Laurence Hubbard, President/CEO

A. *Recommendation on Contribution to Equity*

Mr. Hubbard said the recommendation of management was to not add a contribution to equity into the rates this year. The three key decisions that the Board makes regarding rate level are the amount of contribution to equity that the Board seeks to obtain through the upcoming rate year, the amount of discount to be applied to reduce the rate level based on expected return on invested assets from the underwriting results for the year and a provision for adverse deviation from the actuaries' estimates. Management believes, in consultation with Mr. Greig, that MSF's rate level this year can contain zero contribution to equity. That means there is no profit component built into this rate: however, there is still a five percent provision for adverse deviation in the rate level. That deviation is necessary because there is still prior year adverse development. In the third quarter it is estimated to be $1.1 million but in 2003 when he became the CEO, it was $32 million in one year and since then has averaged about $20 million per year. That presented a pattern of absorbing prior year adverse development while trying to build to the level of the target reserve to equity range that the

Board had established. MSF is well within the targeted range which is certified by the consulting actuary and management recommends a zero percent contribution to equity in the rate level. He said with that the resulting manual rate change, on average, would be a minus five percent for our customers.

Chair Best welcomed Mr. Gengler back to the podium.

B. Loss Cost Multipliers and Components – Dan Gengler, Internal Actuary

Mr. Gengler provided additional perspective on the loss cost multipliers and their components. He provided a clarification regarding the availability of the investment income in MSF's financials and explained how that interplayed with the rates. He said MSF discounts its rates, charging 85 cents on the dollar. The other 15 cents is generated from future investment income over many decades while MSF continues to pay out claims. Reserves are put up on an undiscounted basis therefore chewing up a big chunk of generated investment income. He said if MSF generated $40 million in investment income, about $15 million of that would be attributed to closing the discounted rate gap. That reduces what is potentially available every year for dividends; in this example it would be around $25 to $30 million.

Mr. Gengler presented the proposed lost cost multipliers based on a minus five percent rate change. He explained that each of the rate tiers begins with a comparison to the NCCI loss costs. Then provisions for offsets to underwriting programs, general and acquisition expenses, and profit and contingency are added. Profit and contingency is a negative number because it is offset by investment income.

Proposed Loss Cost Multipliers

-5.0% Rate Change

Analysis of LCM Components

	Tier1	Tier2	Tier3	Tier4	Tier5
Loss & LAE	0.716	0.860	0.955	1.146	1.385
Offsets for UW Programs	0.073	0.087	0.097	0.116	0.140
Genl & Acquisition Expense	0.149	0.179	0.199	0.239	0.289
Profit & Contingency	-0.052	-0.062	-0.069	-0.083	-0.100
Loss-Cost Multiplier	**0.887**	**1.064**	**1.182**	**1.419**	**1.714**

Mr. Gengler said the proposed loss cost multipliers depicted above are management's recommended loss cost multipliers

Chair Best called for questions or comments.

Mr. Brenneman asked if he was correct in believing that if rates were kept the same, MSF would make money next year, if rates were reduced by five percent, MSF would break even. He also wondered if the rates were reduced by 10 percent would some equity have to be used to cover the loss.

President Hubbard said Mr. Brenneman was correct and if rates were reduced by 10 percent, MSF would be underpricing. He provided clarification that income generated by decisions that the Board is charged with making is unknown for quite some time due to the uncertainly surrounding ultimate liabilities that remain with MSF. A contribution to equity in any given rate level recognizes the inherent risk that rates may not be adequate. That, he said, reflects the portion of the statute that says when the cost of a factor is uncertain, the Board must take a projection that is more than likely as opposed to less than likely to cover those expenses. He emphasized that preserving MSF's assets and equity is imperative due to the uncertainty of future events and maintaining the requirement that the Board have time and opportunity to respond appropriately stabilizes the cost of workers compensation insurance for Montana businesses by eliminating radical ups and downs. He noted that his belief that MSF's assets remain stable is the primary reason he disagrees with Senator Keane's recommendations. He added that since 2007 with this proposed rated reduction, the MSF Board has reduced rates by 39 percent which is significant when considering there have been increasing costs in wage inflation and medical inflation.

Mr. Brenneman said that rates have been reduced in anticipation of savings projected in HB334 and if that uncertainty were not looming he would push for a bigger decrease in the rates. However, because of that uncertainty, he will support the minus five percent rate recommendation.

President Hubbard encouraged the Board to consider rates in terms of accidents yet-to-happen at costs yet to be determined with actuarial guesses regarding medical inflation, the cost of claims, and claim frequency. Dividends are the Board's opportunity to take a look back and reward deserving customers who show an investment in safety with a return of their premium.

Mr. Brenneman said he did not think there was a business in Montana that would not rather pay lower rates than count on the dividend.

Mr. Hubbard told Mr. Brenneman he has had the fortunate pleasure of sitting on the Board when no rate increases have been required which is equally as difficult when necessary. He stressed the importance of assuring stability for MSF customers.

Board members questioned President Hubbard as to whether other percentage amounts were modeled. Mr. Hubbard said MSF had modeled minus five and below but nothing over that.

Mr. Barry provided a view of the proposed rate level with an emphasis on consideration for the unknown claims costs, MSF expenses and investment income for the coming year. He reminded Board members that this was a recommendation to decrease rates by five percent with a zero contribution to equity. He said every account wants lower rates rather than to wait for a dividend; however, if rates are lowered for every account that would mean that reduction goes to the good accounts that are developing income and to the bad accounts that are losing money.

Mr. Mihelish replied that Mr. Barry defines things differently than he does and he does not believe those are evil accounts. He said in his estimation, it is all about the economy, whether they are good accounts or bad accounts, they all need to buy workers' compensation and some have losses and some do not. He said he would like to think that MSF could pass some savings along in the form of rates and not dividends because that might attract more business which might enhance the economy of Montana. He said he would agree to disagree here but did not think there was evil and good here; this is all about small business trying to do business.

Ms. Butler provided an overview of how the statute addresses rate setting. She said it was very clear that the Board's responsibility is to set adequate rates based on the estimated exposure for future claims. She said statute also calls for reserves to be set aside and when surplus is not adequate, the Board must address that as well. The law is also very clear that when there are additional funds beyond what is needed to pay claims safely and have reserves and surplus then the Board is to declare dividends. According to the law, setting rates and declaring dividends are two separate items and they must be analyzed and addressed individually.

Senator Keane said this is exactly the kind of discussion the Board should be having. He said he agrees that setting rates and declaring dividends is the responsibility of the Board. He reiterated that employers have to pay taxes on dividends and not everyone gets a dividend; however if the Board lowers the rates, which the Board can do, everybody benefits. He believes there is a level there that should be given back and it is more than five percent but that is the Board's decision. He told the Board to at least do something and to take a look down the road instead of setting these rates which are increasing the contribution to equity at a phenomenal rate. He added that his recommendation is for one year and he does not believe MSF could get in trouble with $500 million in the bank. He said that includes the adverse things that could happen. He said he thought the Board should take a hard look at this and try to do something a little different. He said the front end people should get a break this time.

Mr. Zanto questioned staff about the possibility of lowering the rate further to minus six percent or minus six and a half percent.

President Hubbard said it is not management's recommendation to go lower than minus five percent. He noted that the Board has the authority to ignore the recommendation and management's counsel. The minus five percent recommendation is based on actuarial certification that it is a responsible level of change and it provides no contribution to equity. The target range of equity level is the discussion to have in the fall when looking at dividend declarations. He noted that if financial projections remain the same he will be asking staff to model an equity range of 2.3 to one, which would allow MSF to maintain an adequate equity level. The Board would be able to declare a fairly substantial dividend. He highlighted Ms. Butler's point that the Board must establish adequate rates. He said rate setting is not an economic stimulus package and if the legislature wanted a stimulus package, they would have funded an infrastructure bill. Setting rates at an adequate level is something that has to be done because MSF is an insurance company and Montana has a worse than average safety record. He said MSF plays a huge role in creating incentives to make sure employers invest in safety and one of those incentives is that an employer is not rewarded if they are not practicing good safety standards. MSF still has an obligation, by law, to assure rates are adequate and he said he does not believe going below minus five percent would be adequate.

Mr. Mihelish clarified that he felt minus five percent is a good thing and he would want to review the numbers and other modeling before considering other potential decrease increments. He added that he thinks that MSF has a great management team and the Board does entrust this to them and their recommendation should be given serious consideration. He requested that staff offer more options for consideration at future meetings so that Board members could see the varying impacts to the financials.

Mr. Brenneman applauded Mr. Mihelish's point and stressed that the Board really needs to have additional scenarios to consider. He said they do not really know what minus ten or minus fifteen actually look like or, for that matter, minus zero. He said in future considerations a range should be provided and management can then argue vehemently for their recommendation. The Board can then determine the best course of action; however, the Board really deserves to know what the implications are should they decide to take management's advice under advisement and do something else.

Mr. Hubbard directed Mr. Brenneman to the Towers Watson report and noted that on page seven, the ranges from no change to minus 5 percent were outlined there. He added that if the Board went with a minus ten percent rate, MSF would be offering rates below loss cost. Modeling it would show a negative number as the result so the rates would be inadequate in Mr. Hubbard's opinion.

Mr. Brenneman said the board has the authority to make that decision if we believe the equity is higher than it needs to be. He stated he did not think that but it seems the board should have the ability to say what things have changed, otherwise by that logic there is no way for the board to ever reduce equity.

Mr. Dykstra remarked that one of the goals the Board has been working to accomplish since he has been on the Board is getting the reserve to equity ratio to the target. This discussion is looking to undo that and slide that equity level back and he said he is reluctant to do that. He said he is concerned about the unknown implications of the constitutionality challenges to HB334; however, in 2016 when the Board has a better feel for how that will all shake out, he will be taking a closer look at that ratio. He urged the Board to go with management's recommendation and stay the course.

Chair Best called for comments or questions from the Board; seeing none, she called for comments or questions from the public or staff; there were none.

C. Adopt Loss-Cost Multipliers for FY2016

Mr. Dykstra moved the Board to adopt loss-cost multipliers as recommended by management to reflect a 5% overall decrease in rates and 0% contribution to surplus; to be applied to the loss-costs as approved by the Board, resulting in rates for new and renewal policies effective July 1, 2015 to July 1, 2016 as follows:

For Tier 1, a loss-cost multiplier of 0.887
For Tier 2, a loss-cost multiplier of 1.064
For Tier 3, a loss-cost multiplier of 1.182
For Tier 4, a loss-cost multiplier of 1.419, and
For Tier 5, a loss-cost multiplier of 1.714.

Mr. Brenneman seconded the motion.

Chair Best asked for any questions or comments from those present.

Mr. Miltenberger said he believed MSF was being a bit tone deaf to the outside concerns regarding the level of equity. The legislature tried to forcibly disgorge a significant amount of policyholder equity and he said he is concerned that MSF is pushing the envelope. He suggested that the rate decrease should be higher than minus five percent; that he recommends negative seven or eight percent to be the reduction range. He said he felt that range would be sensitive to keeping MSF's equity at a level that would be considered less than confiscatory.

Mr. Zanto said he agrees with Mr. Miltenberger and he feels that there is some room in the rates to provide some assistance to employers.

Chair Best said she agreed with Mr. Miltenberger and Mr. Zanto in principle but she has a great deal of respect for the management team and their conservative approach to the issues, which she believes is what has brought MSF to the financial position it is in now. She said from her perspective, which is always banging the drum of workers safety, because she really does not know anything about the rate information other than what she is learning, she would rather see some sort of an incentive on the dividend side rather than on the rate side.

Mr. Zanto clarified that his remarks were not intended to disparage MSF staff or the information provided but he would prefer to see additional options even if they are more than the recommended level.

President Hubbard asked if the Board does decide to go below the recommended rate levels, that the meeting breaks so that Mr. Gengler could recalculate so that the LCMs the Board votes on are reflective of a negative contribution to equity in the rate level. He said the Board was getting management's best recommendation and the actions that management has taken to date to achieve these levels have been deliberate and tempered. He recommends staying the course and does not recommend double digit changes because it creates volatility for our customers.

Ms. Moss said she appreciates the maturity of MSF and its transition into a wonderful organization that balances the intersection of a private organization and a public entity. She noted that she has indirectly heard other conversations similar to this and believes it is important to always be mindful of the independent consultants and the information provided to help make these decisions. She said she also believes that it is important for a governing board to have the discipline to look at the information and not to make decisions immediately. She said there is a healthy amount in the investment portfolio but that could change dramatically and that is one of the variables the Board needs to be aware of. With the transition to regulation under CSI and management structure changes she said she believes this is a conversation that will be very worthy in the fall discussions to be able to issue dividends that could encourage more worker safety. She said she respects the work of the management team and fully supported their recommendation.

Mr. Zanto called for the question

Chair Best called for the vote and the motion passed unanimously.

D. Retrospective Rating Plan Factors – Peter Strauss, VP Operations Support

Mr. Strauss said Administrative Rule 2.55.408 permits MSF to have a retrospective rating plan. A retrospective rating plan provides for individually priced coverage for policyholders who are willing to assume more of the risk. It is designed for the more sophisticated policyholders, who have full-time dedicated professional risk managers on staff. If losses are managed well and the costs are less than anticipated, the cost could be below that of guaranteed cost coverage. The trade-off is that if losses are greater than anticipated, the policyholder could pay significantly more. As applied to our group program, a return of premium is provided for years with better than expected results but there is no additional or retrospective premium increase for results that are worse than expected. As applied to individual policyholders, this plan is only for the largest and most sophisticated policyholders. Last year, MSF quoted 30 policies and wrote 12, which represented about $1.8 million in premium. MSF has provided about $330,000 in return premium for FY 2013 policy results. The policies are reviewed at 18 and 24 months to determine loss development. MSF has also collected about $129,000 in additional premium from some of those policyholders who did not do as well as expected. He noted management was recommending two changes to the retrospective rating plan factors this year. The first is an increase to the expense ratio from 10.8 to 11.3 percent representing the differential change from decreasing rates and stable expenses. The second recommendation is a decrease to the contribution to equity from no less than two percent to zero percent. He asked the Board to approve the retrospective rating plan, the individual components of the program to be applicable to individual retrospectively rated policies and group retention plans, and to permit the President to adjust the expense ratio to include costs of business acquisition and other specific costs not generally included in the expense ratio.

FY2016 Retrospective Rating Plan Factors

Maximum Premium Factor:	1.00 to 1.75
Expense Ratio:	11.3%
Contribution to Surplus:	0%
Loss Conversion Factor:	1.10 to 1.25
Premium Deferral:	up to 40%
Loss Limitation:	per NCCI Retrospective Rating Plan Manual
Tax Multiplier:	1.00
Minimum Premium Threshold:	$50,000

Chair Best called for questions from the Board, the public or staff; there were none.

Mr. Zanto moved the Board adopt the following factors for retrospective rating plans for new and renewal policies effective July 1, 2015 to July 1, 2016:

- *A maximum premium factor of 1.00 to 1.75,*
- *An expense ratio of 11.3%, or as approved by the President,*
- *A contribution to surplus of 0%,*
- *A loss conversion factor of 1.10 to 1.25,*
- *A premium deferral of up to 40%,*
- *The excess loss limitation factors as specified in the NCCI Retrospective Rating Plan Manual,*
- *A tax multiplier of 1.00,*
- *A minimum premium threshold of $50,000, and*
- *Loss development factors for each evaluation based upon actuarial analysis.*

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Mr. Brenneman seconded the motion. Chair Best asked for any questions or comments from those present; seeing none, she called for the vote and the motion passed unanimously.

E. Optional Deductible Plan Factors – Peter Strauss, VP Operations Support

Mr. Strauss said Administrative Rule 2.55.407 permits MSF to have an optional large deductible plan which is similar to the retrospective rating plan in that it is limited to policyholders who are willing and financially capable of accepting and managing their own risks. This type of policy provides a relatively large deductible amount, such as $50 thousand, $100 thousand or $250 thousand. These plans also call for the review of the financial capability of the policyholder. MSF did not quote or write any large deductible policies in FY15, but approval allows MSF the opportunity to provide policyholders a comparison of this type of policy should it be desired. As with the Retrospective Rating plan, there were two recommended changes: an increase the expense ratio from 10.8 to 11.3 percent and a decrease the contribution to surplus from no less than two percent last year to two percent this year.

FY2016 Optional Deductible Plan Factors

Aggregate Limit:	up to 175% of standard premium
Expense Ratio:	11.3%
Contribution to Surplus:	0%
Loss Conversion Factor:	1.10 to 1.25
Loss Limitation:	per NCCI Retrospective Rating Plan Manual
Tax Multiplier:	1.00
Minimum Premium Threshold:	$50,000

MSF is asking the Board to approve the optional large deductible plan, the individual components of the program and permit the President to adjust the expense ratio to include the costs of business acquisition and other account specific costs not generally included in the expense ratio.

Chair Best called for questions or comments from the Board; seeing none, she called for questions or comments from the public or staff. There were none.

Mr. Miltenberger moved the Board adopt the following factors for optional deductible plans for new and renewal policies effective July 1, 2015 to July 1, 2016:

- *An Aggregate Limit of up to 175% of standard premium,*
- *An expense ratio of 11.3%, or as approved by the President,*
- *A contribution to surplus of 0%,*
- *A loss conversion factor of 1.10 to 1.25,*
- *The excess loss limitation factors as specified in the NCCI Retrospective Rating Plan Manual,*
- *A tax multiplier of 1.00,*
- *A minimum premium threshold of $50,000, and*
- *Loss development factors for each evaluation based upon actuarial analysis.*

Mr. Mihelish seconded the motion. Chair Best asked for any questions or comments from those present. Seeing no questions, she called for the vote and the motion passed unanimously.

VI. Laurence Hubbard, President/CEO

A. Miscellaneous

President Hubbard asked Mr. Strauss to introduce Pat McCullough, Medical Team Leader.

Ms. McCullough addressed the Board and provided a brief history of her education and experience. She shared that based on her passion and nursing degree, her career path has focused primarily on building companies and programs that take care of employees in the workplace and building safety programs.

The Board members welcomed Ms. McCullough to MSF.

Mr. Hubbard said MSF is happy to have Ms. McCullough and the quality of leadership that she brings to the table.

He reminded the Board the Board terms of Chair Best, Mr. Brenneman and Mr. Dykstra technically ended on April 28, 2015; however, he asked them to remain in service until the Governor has an opportunity to replace or reappoint. He noted there has been no communication from the Governor's office regarding these appointments, which was probably due to finishing up legislative issues.

B. Internal Audit Update – Patti Grosfield, Internal Auditor

Ms. Grosfield provided an update on two items.

Externally

She provided a wrap up of the FY2014 annual mandatory governmental financial statement audit. She said the Legislative Audit Committee met on March 5, 2015 and the audit was

presented to the committee. Representatives from MSF attended and provided information and answered questions. She reported that it was a clean audit with an unmodified opinion which means the reader can rely on the information presented. The report did not contain any recommendations. The opinion states: "In our opinion, the financial statements referred to above present fairly, in all material respects, the net position of the MSF as of June 30, 2014, and 2013, and the changes in net position and cash flows for the fiscal years then ended in conformity with accounting principles generally accepted in the United States of America." (GAAP compliant).
She said the audit work included testing internal controls and business processes related to:

- Payment of claim expenses and reserves for future
- Assessment and collection of policy premiums
- Investment activity
- Compliance with selected laws and regulations
- Overall reasonableness of the financial statement presentation

She then provided an overview of the audit process and noted portions of the report that provided some valuable information: management discussion and analysis, MSF financial statements and notes to financial statements.

Ms. Grosfield said that due to the passage of SB123, MSF will be converting from a fiscal year to a calendar year and that will have an effect on when audits are scheduled. She provided the revised schedule.

Future External Audits

Fall 2015:

- FYE 6/30/15 LAD audit
- FYE 6/30/15 Statutory Statement audit

January, February 2016:

- Calendar year conversion audits to set 1/1/16 beginning balances
    - 7/1/15 – 12/31/15 LAD audit
    - 7/1/15 – 12/31/15 Statutory Statement audit

Future years:

- FYE 12/31 LAD audits
- FYE 12/31 Statutory Statement audits

Chair Best called for questions or comments from the Board.

Mr. Dykstra thanked Ms. Grosfield for the quality of the work she always presents to the Board and the clarity that she provides to the Board. He said MSF's audit group is first class and he finds the information to be very valuable. He also likes the fact that MSF always receives such clean audit reports.

Ms. Grosfield said kudos really go to the Finance Department and the entire staff at MSF. She said everyone works very hard to produce a quality product.

Chair Best called for additional questions or comments. There were none.

C. Legislative Update – Nancy Butler, General Counsel

Ms. Butler reported that the Montana House of Representatives and the Senate adjourned Sine Die on April 28, 2015, the 87th day of the 64th Regular Session. She provided a report on the bills that MSF had been following:

Senate Bill 123 (SB123) – Revised the regulatory authority of MSF to the Commissioner of Securities and Insurance (CSI), was passed by the legislature and was signed by the Governor on April 29, 2015. It is effective January 1, 2016; rate filing and review with rates will be effective July 1, 2016. There will be more information at the June MSF Board Meeting such as the changes to MSF Board meeting dates. She noted that the timing of the Board meetings will change because MSF will move to a calendar year and a meeting in December will be required to accommodate some of the decisions that need to be put in place for next year.

Senate Bill 379 (SB379) – Effective, April 28, 2015, SB379 requires MSF to report to the Economic Affairs Interim Committee (EAIC) on MSF's Board approved budget. Current law has MSF reporting to the EAIC on operations and other functions.

Senate Resolution 39 (SR39) – Confirmed the Governor's appointments to MSF's Board of Directors: Richard Miltenberger, Bruce Mihelish, Lynda Moss and Lance Zanto. It was confirmed by the Senate.

House Bill 538 (HB 538) – Provided extraterritoriality options for workers' compensation coverage in North Dakota (ND). If a worker is solely working in ND and ND coverage is in place, the worker is not considered a MT employee - commuting from MT to ND does not constitute work in MT. If job duties begin in MT prior to traveling to ND, then is covered in MT. The Department of Labor is to develop a verification of employment form for use by insurers and employers. It is effective July 1, 2015.

House Bill 503 (HB 503) – Clarified the provision of insurance loss-runs to employers in the Workers' Compensation Act. There is an added requirement to provide within 10 days of the request by an employer. Effective April 24, 2015.

Senate Bill 259 (SB 259) – Revised the Department of Labor (DOL) Workers' Compensation Administration Fund and Safety Administration Fund assessments. The assessment funds safety programs and the Workers' Compensation Court (among many other functions), used by insurers, employers and injured workers. The DOL budget is approved by the Legislature and the Old Fund will no longer be assessed a Safety assessment. Effective July 1, 2015.

Senate Bill 4 (SB 4) – This bill authorized the temporary appointment of a judge for the workers' compensation court in the instance of a vacancy or disability. The appointment is by the Supreme Court – of a retired District Court Judge, or from a list of interested attorneys. Effective October 1, 2015.

House Bill 90 (HB 90) – Department of Labor's "housekeeping" bill included: requiring notification to the claimant when there is a change in examiner, within 14 days. Treats receipt of paid leave, other than sick leave, like vacation leave – as not impacting eligibility for temporary total. Effective July 1, 2015.

Senate Bill 347 (SB 347) – Provided a workers' compensation coverage option for emergency medical technicians, working for an ambulance service or a non-transporting medical unit, unless otherwise required to be covered. This bill allows purchase of coverage for an all-volunteer unit serving the public, but coverage is not mandatory. Effective July 1, 2015.

Senate Bill 258 (SB 258) – This bill revised workers' compensation laws relating to coverage requirements for religious organizations. Agricultural services are only required to be covered if performed off their property. Effective October 1, 2015.

Senate Bill 254 (SB 254) – required the transfer of $50 million from MSF to the Old Fund. This bill died in process.

Senate Bill 398 (SB 398) – Required MSF to declare $100 million in dividends over the next two years without any actuarial analysis. This bill died in process.

Chair Best called for questions or comments from the Board, the public or staff; there were none.

D. Annual Business Plan Update – Shannon Copps, Director of Enterprise Strategy and Project Management

Key Success Measures

KSM	2015 BP	2015 Projected
Net Earned Premium	$167.0 M	$165.6 M
Fiscal Year Loss Ratio	74.7%	74.0%
Expense Ratio	27.2%	26.2%
Investment Income	$49.2 M	$49.1 M
Net Operating Income (before dividend)	$40.0 M	$44.8 M
Achieve Enterprise Wide Initiatives		

Ms. Copps provided an update on the Key Success Measures. Ms. Copps said that the Enterprise Wide Initiatives are in four main categories: Workforce, Engagement, Customer Service, Claim and Medical Management and Infrastructure. She reported that all initiatives are on track or completed with the exception of the engagement initiative, which was off track due to a slight decrease in overall engagement scores from the mini-survey. Management is developing a response to the concerns expressed by employees during this project.

Chair Best called for questions or comments; there were none.

VII. Old Business/New Business

There was no old or new business.

VIII. Public Comment

Chair Best called for further public comment.

President Hubbard announced that the MSF Communications and IT staff launched a new website that day at noon and offered the Board members a preview if they were interested.

Mr. Dykstra commented that he received the memo regarding the Old Fund status during the meeting and thanked staff for preparing that so quickly.

Mr. Zanto wanted to note that the discussion heard at this meeting was not unique just because Senator Keane was in attendance. He said he highly respects the MSF staff and he feels it is the Board's job to ask the tough questions.

Mary Boyle provided a preview of the new website and walked the Board members through some of the new features.

Chair Best called for additional questions or comments. There were none.

The meeting was adjourned at 2:05 pm. The next scheduled Board Meeting will be held on Friday, June 19, 2015 at 8:30 a.m. in the Board Room at Montana State Fund, 855 Front Street, Helena, Montana.

Respectfully submitted,

Verna M. Boucher
Special Assistant to the President/CEO