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MONTANA STATE FUND
BOARD MEETING
September 18, 2015

The Montana State Fund (MSF) Board Compensation Committee meeting was held September 18, 2015 at Montana State Fund, 855 Front Street, Helena, Montana.

Directors Attending

Richard Miltenberger, Helena
Wayne Dykstra, Billings
Bruce Mihelish, Lolo
Joe Brenneman, Kalispell
Lance Zanto, Helena (via telephone)
Jan VanRiper, Helena

MSF Staff Attending

Laurence Hubbard, President/CEO
Verna Boucher, Special Asst to Pres/CEO
Nancy Butler, General Counsel
Mark Barry, Corporate Support VP
Peter Strauss, Insurance Ops Support VP
Rick Duane, Human Resources VP
Mary Boyle, Communications Specialist
Shannon Copps, Team Leader
Patti Grosfield, Internal Auditor
Rene Martello, Controller
Dan Gengler, Internal Actuary
Sandy Leyva, Dir of Enterprise Applications

Others Attending

Russell Greig, Towers Watson
Neville Kenning, Kenning Consulting
Bill Wheeler, DOLI
Senator Gordon Vance, (Leg. Liaison)
Glenn Oppel, Montana Chamber
Pat Murdo, LSD
Les Vernon, Towers Watson
Jesse Laslovich, CSI
Sonja Powell, OBPP
Shelly Vance, Bozeman
Paul O'Loughlin, LAD

I. Meeting Preliminaries

A. *Call to Order*

Chair Lance Zanto attended this meeting via teleconference and requested that Richard Miltenberger serve as Acting Chair in his absence. Chair Miltenberger called the meeting to order at 8:30 a.m. He welcomed the Board members, MSF staff and honored guests; in particular Economic Affairs Interim Committee (EAIC) Legislative Liaison Senator Gordon Vance from Bozeman and General Counsel and Acting Deputy Commissioner Jesse Laslovich from the Commissioner of Securities and Insurance office (CSI). He noted that Board members Bruce Mihelish and Lynda Moss were absent.

B. *Approval of June 19, 2015 Board Meeting Minutes*

Chair Miltenberger noted that the first order of business was the approval of the Board meeting minutes for June 19, 2015.

Mr. Dykstra made a motion to approve the June 19, 2015 minutes. The motion was seconded by Mr. Brenneman. Chair Miltenberger called for discussion from the Board, MSF staff and members of the public. There being none, he called for the vote and the motion was unanimously approved.

II. Miscellaneous – Laurence Hubbard, President/CEO

A. Miscellaneous – Laurence Hubbard, President/CEO

President Hubbard also welcomed the attendees and thanked Mr. Laslovich for attending the meeting to present to the Board.

He welcomed new Board member Jan VanRiper and thanked Joe Brenneman and Wayne Dykstra for attending while their reappointment or replacement on the Board is pending. He thanked them for their years of service to MSF and their commitment and support to management and staff during their tenure.

He provided a status update on the implementation of Senate Bill (SB) 123 which transfers regulatory oversight of MSF from the legislature to CSI. He explained that there are four sub-projects that were approved by the Board at the June meeting to prepare and implement the regulatory change effective January 1, 2016 for rates effective July 1, 2016. The threshold for MSF is January 2016 and there are two important aspects that must be complied with by then. A transition plan must be submitted to CSI for approval and MSF completed and submitted that plan on July 31, 2015. The transition plan is primarily composed of exhibits indicating how MSF will come into compliance with the National Council on Compensation Insurance (NCCI) basic manual rules and class codes. MSF has requested two exceptions: class code treatment of domestic workers and relief from adherence to the Anniversary Rating Date (ARD) requirement and process. MSF's policy system is not equipped to apply a per capita premium charge for domestic workers and upgrading the current system would require 1,000 hours of technology and business time. MSF has not previously utilized the ARD application and NCCI has recently announced a national filing to remove the ARD requirement effective May 2017.

He said the other significant requirement is the issuance of a Certificate of Authority (COA) for MSF to do business. Though SB123 requires CSI to issue the certificate, MSF must provide the same materials and applications that a private insurance company is required to submit. Those materials were submitted to CSI on September 1 and contain affidavits from Board members, executive staff and a detailed biography of MSF's organizational structure. MSF has also prepared a trial rate filing using the last rate year's data and actuarial support for the current rates effective July 2015 for review by CSI's chief actuary to assure that MSF is correctly submitting the expected documents for rate filing. Four sets of forms have been submitted to CSI for approval, all of which have been approved. The endorsements that we use for special coverage are ready to go for use effective July 1, 2016 for new and renewal policies.

A major initiative currently being undertaken is the conversion to a calendar year for fiscal reporting. MSF is currently operating under a six month fiscal year that began July 1, 2015 and will end December 31, 2015. MSF will then adopt a calendar year reporting period which is unprecedented for state government accounting and requires substantial changes on the state side to be able to accommodate closing the financial statements. The investment reporting will also have to convert from a fiscal to a calendar reporting period.

The final project is change management to communicate with and guide MSF employees through the changes they too will be experiencing, such as obtaining producer licenses for our Customer Service Specialists. President Hubbard reported that over 40 staff members had already taken the producer licensing exam and the vast majority have passed.

Chair Miltenberger called for questions; there were none.

President Hubbard asked Board members to review the proposed meeting dates for 2016 and the proposed changes to the 2015 schedule. He asked that Board members review the dates and contact Ms. Boucher with any conflicts that may create attendance issues.

Chair Miltenberger welcomed Jesse Laslovich.

B. *Update from State Auditor's Office – Jesse Laslovich, Chief Counsel and Acting Deputy State Auditor*

Mr. Laslovich thanked Mr. Hubbard and his team for accommodating his request to address the Board, noting that he had heard of Mr. Hubbard's updates to the Board but wanted to be sure and personally address the Board. He stated that negotiating the final language for SB123 was not an easy process and CSI and MSF disagreed on various issues throughout the negotiations. He complimented the Board and the Executive Team for the proactive and communicative approach they adopted regarding the issues that needed addressing. He candidly shared that he did not like everything in the bill; however, noted that legislating is compromise and cited this collaborative effort as a great example and model for future legislative developments in Montana and nationally. He provided an update on the status of the transition and noted that CSI has been surprised by MSF's early submittal of items for consideration, such as the transition plan.

Mr. Laslovich said that the exception request regarding implementing usage of the ARD will be accommodated and CSI will provide a formal written response. He said CSI still has a few questions regarding the per capita exception request; however, CSI will try to be reasonable and work with MSF in this regard. He emphasized that CSI's primary consideration is to maintain a level playing field for the marketplace. Based on that consideration, exception requests are first looked at with an eye to determining the effect it will have on the market and if granting the request would give MSF a competitive advantage. He noted that it is inevitable that there will be times throughout the CSI/MSF relationship where both sides will not agree. He also stated that CSI recognizes that MSF is the guaranteed market and realizes that everything is not simply the same. SB123 also contemplates that caveat and has language exceptions based on that; some of which CSI agrees with, some that they do not. He said that CSI ultimately supported SB123 because they thought it was the right thing to do.

He said the form review has been very seamless and they are anticipating future CSI form reviews to be the same. The review of the mock rate filing has not been completed yet because the actuary has questions and perhaps, concerns. He noted that it is better to address this process early rather than next year when the rates proposal has to be announced by July 1, 2016. He said CSI salutes the MSF staff for stepping up in the producer licensing process and commended the team for the resounding passage rate by the MSF staff.

Mr. Laslovich addressed the COA application that MSF submitted. He remarked that under SB123 the COA issuance is automatic; however, CSI had some angst regarding that because they feel it is the best way to learn about a company. MSF agreed to submit the application. He said he has reviewed it and appreciated the narrative about MSF and learned a lot that he did not know. CSI has received most of the affidavits and understands the concern of one of the Board members and will attempt to work through that. He said that Mr. Hubbard has raised the concern regarding the issuance of an NAIC number which, in order to obtain, requires the COA. He said he has investigated if there is anything CSI can do to accommodate MSF getting the NAIC number. He announced that CSI will make it happen whether it is CSI actually giving MSF a COA or whether it is CSI working with the NAIC to get MSF an NAIC number. These efforts will mean MSF does not have to wait until January 1 to receive the COA and get the NAIC number. He said he would verify that in writing once completed.

He said CSI will complete a financial examination of MSF earlier rather than later so that CSI can have a starting point. Based on CSI's interaction with MSF since the passage of SB123, CSI is confident that though there may be some issues, CSI and MSF will work through them. He said CSI is not out to get MSF, they are there to help. The financial exam concentrates on solvency and the Board and MSF's management team have done a very good job on that. The market conduct exam will be a work in progress; however, he committed to the Board that CSI will work with MSF on both exams.

Mr. Laslovich said the one issue that he wanted to raise to the Board that he believes needs to be worked out with an eye toward the long term is the prosecution of MSF's fraud referrals. He said a senator offered an amendment to SB123 to have MSF pay for an attorney at CSI beginning in January 2016 as well as a market conduct examiner to begin in July 2016. CSI appreciates the resources; however Mr. Laslovich said this needs to be figured out. He said CSI prosecutes for the private carriers in all the markets; however, MSF has an exception to that and pays the Department of Justice (DOJ) to prosecute its fraud referrals. He said DOJ is doing an excellent job however it is not about doing a good job it is about consistency. MSF is paying two units of government for resources that should be funded and obtainable through the legislature for consistent operations. He said that is something CSI will be focusing on going forward. Though that is important it is not as important as the other issues that CSI will be addressing.

He said some at CSI, and he believed some at MSF, had great trepidation about what this is going to mean. This is new for CSI and certainly for MSF as well and it will take time to learn how to "dance together"; however he believes that is happening. He credited Mr. Hubbard and team for making that happen. He said he approached this process very skeptically and while in the legislature had concerns about MSF. He said there were things that he said that he should not have. He has learned more about MSF over the last couple of years and is impressed with the staff and the company. He acknowledged the extraordinary work of the MSF team in effectuating SB123, and equally importantly, implementing the transition in a seamless manner. He said MSF has made it very easy on CSI thus far and could not overemphasize how grateful CSI staff are for that and the continued open dialog that has been fostered.

Chair Miltenberger called for questions.

Mr. Dykstra thanked Mr. Laslovich for addressing the Board and thanked Mr. Hubbard and the MSF staff for the efforts, transparency and communication provided to Board members regarding the implementation of SB123. He asked Mr. Laslovich what Board members could anticipate, in the future, regarding the oversight transition.

Mr. Laslovich provided an overview of issues that CSI views as the biggest concerns, the largest being the rating process. MSF addressed rate setting under Administrative Rules, which under SB123 will go away. There will be differences in how MSF's rates are set and that review is going to be a big deal for CSI which is why he appreciates the mock review that is being conducted. He said the examinations will also be a big part of the regulatory authority. The Board will proceed as normal; however, there will now be a regulator so MSF will file its rates, be subjected to a market conduct exam and a financial examination which will indicate from CSI's perspective, the concerns or not about how MSF is operating.

Mr. Dykstra asked for further clarification regarding rate setting and whether CSI will be responsible for establishing the rate base or a range of rates or will that decision remain with the Board.

Mr. Laslovich said that decision will remain with the Board as each insurance company does now. CSI will review the rates to determine if they are excessive, inadequate or unfairly discriminatory. He explained that there is a standard in the rating statute that CSI had to address with MSF with regard to excessiveness. He said there is a measurement under the law that determines that if the market is deemed to be competitive, then rates are presumed to not be excessive. That analysis excludes MSF because, if included, the market would not be deemed to be competitive so a definition of excessive was included to address MSF's rates.

Mr. Dykstra asked Mr. Laslovich to describe MSF's obligation to remain under the supervision and direction of the legislature as opposed to falling under the regulatory agenda and umbrella of CSI. Specifically, he indicated concerns regarding legislators' continuing efforts to strip MSF money and assets for use for unrelated expenses and costs. He asked if that ability by the legislators will continue or is that something CSI will be able to stop.

Mr. Laslovich said the legislators could still make those attempts because MSF is still an entity of state government. The benefit of this legislation is that MSF now has an experienced insurance company regulator that will have, by 2017, a year of regulating MSF and will be able to take a seat at the table to provide assurances regarding MSF's solvency or express concerns regarding proposed asset grabs. He noted that perception indicates to some that insurance companies are overcapitalized with too much surplus and that needs to be addressed; however, CSI is concerned that MSF be able to play claims and not repeat the past financial insolvency history. He said he thinks being under CSI's regulation will help MSF and CSI will be vocal if they have concerns about proposed legislation. He said the ultimate reason CSI supported SB123 is because they do not believe the legislature should be the regulator. As a part time entity, they cannot adequately regulate MSF and the legislative auditor is not an insurance regulator. He said he might be overestimating CSI's influence; however, he is hopeful that it will be considered when legislators are determining support of or opposition to proposed legislation that affects MSF.

Jan VanRiper asked if the workers' compensation claim dispute process would change under SB123.

Mr. Laslovich said the dispute resolution process will still be handled by the Department of Labor and Industry (DOLI). He said CSI anticipates receiving more phone calls; however, they are already prepared to address the increase as they do now with similar dispute calls received regarding private carriers.

Mr. Brenneman said that Mr. Laslovich indicated during his term in the legislature that he had concerns regarding MSF and Mr. Brenneman believes that exemplifies the Board's repeated experience with legislators. He said people seem to think the Board and MSF are up to something and must be investigated, hence the number of legislatively required audits. MSF now has auditors auditing auditors, which provides no real value to the Board and is a further indicator that MSF is overregulated. He asked Mr. Laslovich if there was any chance, under the new oversight structure, to streamline the number of required audits to just one.

Mr. Laslovich said he thinks it is better than just a chance. He also shared that some at CSI would say that MSF is not regulated at all; auditing is one thing but regulation is another. Now that MSF has an entity that regulates the insurance industry involved in all aspects of MSF's business, MSF will have CSI as a point of information to the legislature which can only help MSF. He said that having that reference point from CSI and Legislative Liaison Senator Vance will help MSF at the legislative level. He noted that he believed that having a full time regulator will help CSI address the "lack of trust" of MSF in the legislature and may reduce some of the redundant auditing requirements.

Chair Miltenberger called for additional questions or input and invited Senator Vance to offer his insights. There were no questions and Senator Vance declined to comment at this time.

C. Report of the Internal Auditor, Patti Grosfield, Internal Auditor

Ms. Grosfield reported that MSF is experiencing internal and external audit activity.

She said the Legislative Audit Division (LAD) is currently on-site conducting the annual fiscal year review for approximately five weeks. She introduced Legislative Auditor, Paul O'Loughlin, and provided some background on his tenure in auditing MSF. She reported that this will be the final fiscal year audit; however, the audits will not be eliminated, they will now be based on the calendar year reporting.

She said the Eide Bailly statutory auditors are off-site gathering information and will be on-site the first part of October. MSF's statutory financial statements and Eide Bailly's audit use NAIC based insurance accounting principles which will assist MSF in preparing for the regulatory action and authority of CSI. Additionally, this year, the auditors will be reviewing the IT systems, controls and accesses in greater depth.

Ms. Grosfield said the audit of the annual merit pay adjustment review process was completed and the adjustments have been implemented. The adjustments are based on employee performance during the last fiscal year and this year there are five levels of achievement ranging from zero up to six percent.

Chair Miltenberger called for questions. There were none.

President Hubbard requested a moment to address a couple of additional items.

He announced that current Operations Support Vice President, Peter Strauss, has graciously agreed to become the Compliance Officer for MSF with CSI. He will now be the primary contact between MSF and CSI with regard to regulation and compliance and will now report to General Counsel.

He also announced that Nancy Butler, General Counsel, will be retiring in January of 2016. He said she will stay to see MSF through the transition to oversight under CSI. He said she has been remarkable as a colleague and mentor and noted that she will be sorely missed by everyone in the organization.

He then thanked Mr. Laslovich for his observations. He shared his views that the lack of trust by legislators is not only based on confusion regarding rate setting but also the items that are unnatural for public entities such as the MSF building, employee salaries, incentive plans and the sources and responsibility for MSF's monetary assets. The fact that CSI is regulating MSF like an insurance company is a significant step to public perception that MSF is, first and foremost, an insurance company.

Chair Miltenberger thanked Mr. Strauss for stepping into the Compliance Officer position and asked Ms. VanRiper to share her history with Ms. Butler.

Ms. VanRiper shared that she was in a position quasi-related to Mr. Hubbard's position now and she was the one who hired Ms. Butler.

Chair Miltenberger commented that he was remiss in not introducing Ms. VanRiper at the beginning of the meeting. He welcomed her to the Board and shared that she served capably in workers' compensation and also at the state auditor's office.

D. *Succession Planning Update on Prior Projects – Rick Duane, VP Human Resources*

Mr. Duane provided the update requested by the Board regarding MSF's succession planning. He explained the planning approaches utilized and stressed that proper management of the succession plan is critical for building bench strength in a competitive labor market and is essential to sustaining organizational success. He said three key areas of concern were CEO succession, claims examiner development and leadership readiness and succession.

To address those concerns, the FY2013 Business Plan called for improved recruitment results, identification of short and long term needs or challenges through the Critical Position Review (CPR) and the building of strategies and resources to address the organization needs. To achieve these goals, MSF hired an internal recruiter versed in social media recruiting methods to attract both active and passive candidates with the skillsets and experience needed. The Caliper Corporation's personality assessment tool was utilized during the hiring process for most positions and MSF worked with Caliper Corporation to develop enhanced Calipers for claims examiners, medical case managers and customer service specialists. An employee engagement survey was conducted to gather organizational insight and confirm pockets of expected turnover. An Organizational Development Professional (OD) was hired in mid-2012 to develop an effective workforce development strategy for MSF based on organizational input and needs. The Leadership Development Program (LDP) was created to develop future leaders within MSF.

The Goal of Succession for 2014 was to increase the number of quality candidates, decrease the time to fill and increase the quality of the hire. He reported that the time to fill has been reduced from 90+ days to generally 45-60 days. Social media accounts for 46 percent of MSF's new hires in 2014 and 2015, many of which were not actively looking for a job. MSF held its first Career Open House to expose the local market to the positions and culture at MSF. The Employee Referral Program was enhanced and 12 people have been hired based on that program. Management utilized the engagement survey to identify turnover risks and employee development and growth desires and needs. MSF sought to provide challenging development opportunities, identify key positions and high potential employees, and formalize the succession processes to ensure a sustainable and proactive approach to workforce development. A High Potential Assessment process was designed and implemented as was the Leadership Competency Dictionary and enhanced Caliper profiles for leadership positions. A leadership On-Boarding Guide and a coaching and mentoring training program were developed. The Board approved 14 FTE to support the succession work to be used for bench strength, knowledge transfer, improved injured employee outcomes and succession support for critical institutional knowledge transfer.

Mr. Duane noted that MSF's Organizational Development Specialist has created an impressive program that is attracting attention from other organizations and industry leaders. He said these developments have had an impact on attracting and keeping critical talent and MSF intends to continue moving forward with cutting edge programs and proposals that enhance employee development and growth. He stressed the need for continued Board support to maintain the market based compensation component as well as enhancing MSF as a desirable place to work.

Chair Miltenberger thanked Mr. Duane for the report and said he was encouraged by the additional trainings/opportunities provided for employees to move upward within MSF. He called for additional questions.

Mr. Brenneman commented that he was encouraged to see the continued emphasis on claims examiner and claims management personnel due to their key role within the organization.

Mr. Dykstra stated that he was pleased with the programs that MSF has built to address the succession issues and concerns. He said he is very impressed with MSF's accomplishments in the development of various resources and opportunities to address these by identifying new hires that fit the requirements of the MSF careers.

Chair Miltenberger called for questions from the public; there were none and he thanked Mr. Duane for his report and moved to the next agenda item.

III. Reserve and Financial Reports – New Fund

A. *Introduction – Laurence Hubbard, President/CEO*

Mr. Hubbard introduced Russell Greig, consulting actuary from Towers Watson, to present the reserve report on the FY 2015 ultimate liabilities, reserve report and loss adjustment expense reserve.

B. *Montana State Fund FY15 Reserve Report – Russell Greig, Director, Towers Watson*

Mr. Greig introduced his colleague Les Vernon, a credentialed actuary from Towers Watson's Atlanta office. He explained the objectives of the Towers Watson analysis, which were to estimate the aggregate amount of unpaid claims benefits providing a range of estimates and including a provision for loss adjustment expenses (LAE) or claims administration expenses. He said for the New Fund, the analysis encompassed injuries occurring between July 1, 1990 and June 30, 2015 and explained the application of Towers Watson's methodologies. He noted that regulators as well as many stakeholders want assurances that MSF will have tangible assets and has set aside enough assets to pay out the claims incurred through June 30, 2015. He said the financial condition of any property casualty insurance company cannot be properly evaluated without sound loss reserve estimates.

He said over the last six months, the ultimate losses were $2.6 million or 0.1 percent above projections which essentially means that MSF's loss experience has stabilized. Actual payment activity over the past six months was $100 thousand more than expected for indemnity and $800 thousand more than expected for medical.

Periods of favorable development and periods of adverse development tend to run in cycles and those developments have stabilized in the last four to five years. The aggregate amount of unpaid claims benefits is an estimate so there are several contingencies that can impact future analysis: 1) medical costs may increase more than expected due to medical technology, utilization or higher frequency of severe diagnosis, 2) trends can swing between frequency and severity, 3) benefit changes, 4) litigation or attorney involvement, 5) court cases that retroactively change benefits, 6) economic cycles and social trends and 7) the duration of an injury.

Mr. Greig noted that the medical development patterns have continued to stabilize after several years of lengthening and over the last four or five evaluation dates, his confidence has increased that that trend will continue allowing for the eventual use an unadjusted reported development medical projection.

He stated that for the unpaid loss benefits for medical, his actuarial central estimate is $611.8 million and for indemnity $168.8 million making the total $780.6 million. He quantified the range of uncertainty around the actuarial central estimate.

	Low Estimate	Actuarial Central Estimate	High Estimate
Unpaid Loss at June 30, 2015	$703.3 M	$780.6 M	$888.3 M

Mr. Greig said that MSF's equity provides a substantial cushion which is required to support the continued growth of MSF and to minimize the impact of unexpected events on MSF's financials.

He explained that MSF equity could be significantly impacted in the case of a sustained change in expected trends. He said if medical inflation rates were running two percentage points higher than those embedded in his models over the next ten years, it could mean the ultimate losses would need to be $79 million higher which would have to be funded by policyholder equity.

Chair Miltenberger asked what the long range inflationary expectation embedded in Towers Watson's projection was.

Mr. Greig responded that over the latest three or four years for medical severity he has assumed two percent after a spike encountered in 2012. The average across all of those years is five to six percent.

President Hubbard asked Mr. Greig to provide his probability confidence level of the central estimate versus the high and low ranges of that estimate.

Mr. Greig said the actuarial central estimate is supposed to be the middle of the road and at the 50 percent confidence level which would mean there is a 50 percent chance the liabilities will pay out higher and a 50 percent chance they will pay out lower. A key issue throughout the process is that the actuary is exercising judgement in selecting parameters that are an unbiased estimate. He also pointed out that the range around his actuarial central estimate is not symmetrical because there is a higher probability that there will be a bigger pay out loss relative to a smaller loss because the loss distribution is skewed. He explained that there is a low end cap of zero on how good things could be in terms of a claim; however, occasionally, a younger worker is severely injured and becomes permanently and totally disabled which means the insurance carrier will be paying out wage replacement for 40 or more years and in addition to a lifetime of 24 hour health care. That scenario would mean costs to the insurance carrier of $10 to $20 million. Workers' compensation benefits are not capped and that is the only line of business where that is the case.

Mr. Greig noted that there is an expectation that MSF will receive some recovery from its reinsurers and he forecast the amount based on excess reinsurance only at approximately $18 million. The total estimated recoveries based on the aggregate was $22.3 million making the actuarial central estimate $40.2 million. The recoverable range is $26 to $66.6 million.

Mr. Greig went on to discuss claim administration expense and Towers Watson's methodology of examining recent relationships between claim payments and claim administration expense. The selected reserve provision of 14.2 percent of future loss payments recognizes that a significant portion of LAE occurs when a claim is first reported.

Towers Watson's overall conclusion as of June 30, 2015

Unpaid claims benefits – Actuarial Central Estimate

Medical	$611.8 million
Indemnity	$168.8
Unpaid claims administration expense	$110.8
Total gross unpaid benefits & administration	$891.4 million
Reinsurance Recoverable	(40.2)
Total net unpaid benefits & administration	$851.2 million

Considerable uncertainty is associated with projections of unpaid claims

Low estimate, $736.6 million

High estimate, $988.5 million

Chair Miltenberger questions or comments from the Board.

Mr. Dykstra noted that he had questioned Mr. Greig in the past about the potential impact and liability associated with the asbestos challenges facing MSF. He asked if enough data has been collected to give the actuary a solid footing to develop a projected trend regarding asbestos claims behaviors and expectancies.

Mr. Greig remarked that as stated in the past, he still lacks the necessary asbestos expertise to provide a knowledgeable projection. Mr. Greig mentioned that at a recent casualty loss reserve seminar he learned that claims examiners could be using subrogation to address asbestos claims payouts by tapping into the trusts that have been set up as a result of decades of litigation. He reiterated that when MSF needs to address a projected strategy for asbestos claims, he will have to reach out to an expert in asbestos from Towers Watson.

Ms. VanRiper asked if MSF is looking at subrogation on asbestos claims.

President Hubbard noted that he was not familiar with the utilization of the subrogation trust given the "made whole" law in Montana that has made subrogation so difficult in the past. He said he has not engaged probability or opportunity discussions with legal counsel regarding this issue. He noted that MSF has a team of attorneys and examiners that handle all of the emergent asbestos claims and said the average claim settlement activity has been anywhere from $100 to $150 thousand dollars on average. That experience has not matriculated through the data yet to impact Mr. Greig's analysis; however, MSF is at least operationally aware of them and handling those as a special type of circumstance. He noted that he will need a discussion with General Counsel to clarify their perspective on the subrogation possibilities.

Mr. Hubbard asked Mr. Greig to explain to the Board why Tower Watson's and management's recommendations do not contain discounts for projected medical liabilities. He asked Mr. Greig to provide some reasoning detail and why he believed it was appropriate for the Board to continue to not apply a discount assumption to the unpaid liabilities.

Mr. Greig said it really boils down to accounting not actuarial determination. He said insurance companies are governed by statutory accounting principles which are based on solvency and determining immediate liquidation of an enterprise. By definition, statutory accounting principles are much more conservative than GAAP accounting principles. GAAP strives to show the economic reality and focuses on looking at a company as a going concern and therefore finds it reasonable to discount reserves. Statutory accounting does not discount reserves in order to be as conservative as possible because the discount amount serves as a risk margin. He also stated that he was not aware of any other operating state funds that are discounting reserves. Workers' compensation carriers across the United States do not discount reserves. He clarified that he has seen companies that are in rehabilitation or under supervision from the insurance department discount reserves just so they can pay out the claims.

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

C. *Montana State Fund FY15 Reserve Recommendations – Laurence Hubbard, President/CEO*
President Hubbard thanked Mr. Greig for his presentation. He then provided management's recommendation to the Board of Directors for purposes of adopting a net loss and loss adjustment reserve for the New Fund. He provided the graph depicted below which shows a summary of the recommendation and the differences between Towers Watson's recommendation and management's. He noted that the primary differences between Towers Watson and MSF appear in the reinsurance recoverables reserve and reserve strengthening.

Recommended Losses and LAE

As of June 30, 2015 (In Millions)		
	Towers Watson	MSF
Unpaid Losses	780.6	780.6
LAE	110.8	110.8
Gross Losses and LAE	891.4	891.4
Adjustments:		
Reinsurance	(40.2)	(35.6)
Reserve Strengthening		64.2
Other States/EL		3.0
Additional LAE		9.3
Net Unpaid Losses and LAE	$ 851.2	$ 932.2

Total MSF Recommended Losses and LAE	$ 813.0
	$ 119.2

He said management recommended a slightly more conservative estimated recoverable at $35.6 million which has the effect of carrying slightly more loss reserves than was recommended in Mr. Greig's analysis. Third party contracts contain substantial credit risk. MSF has been fortunate regarding those contracts but has experienced the downside of reassuming the liabilities of a commutation agreement with a reinsurer and experiencing adverse development for a particular accident year. Based on the inherent risks in the reinsurance contracts, management recommends a slightly more conservative estimate for the recoverables. He said management also recommended the Board maintain the $62.4 million hedge against additional loss development. That provides the Board with time should the HB334 savings not be realized and the Board needs to strengthen reserves for additional liabilities. Mr. Hubbard also noted that the recommendation includes $3 million for other states excess of loss and $9.3 million additional LAE for a total of $932.2 million.

Chair Miltenberger called for questions from the Board.

Mr. Brenneman asked Mr. Greig if reserve strengthening was ever a component in his calculations.

Mr. Greig replied that it was not and explained that his job was to provide an unbiased estimate. He said it was up to the individual insurance company to determine if they will book his recommendation. He said when he has to provide a reserve opinion, he simply indicates whether he feels the reserves are adequate and within a reasonable range of his estimate. A reasonable range initially runs minus five to ten percent around his actuarial central estimate and that is without doing sensitivity testing.

Mr. Brenneman asked if MSF were under-capitalized, would Mr. Greig have a number in his recommendation?

Mr. Greig said MSF's level of capitalization does not affect his formal reserve opinion or his reserve recommendations.

Chair Miltenberger called for additional questions.

Mr. Dykstra said he had been operating under the impression that the asbestos issue was not being directly dealt with by companies and was not aware that there were available trust monies out there. He requested that MSF staff research the current asbestos reality and provide a brief summary at the next Board meeting. He specifically wanted to know if there were trust monies available that MSF could potentially go utilize and what was MSF's legal position and ability to pursue subrogation. He expressed concern that this liability could be in the billions as is reported nationally.

President Hubbard said that Dan Gengler, Nancy Butler, Mark Barry and Julie Jenkinson will prepare a report for the next Board meeting. He assured Mr. Dykstra that MSF's liability would not be in the billions but could quite possibly be in the millions which has not been anticipated in prior rate levels.

Ms. Van Riper sought clarification regarding management's recommendation. She asked if the Board went with the $932.2 million would that add $81 million to the $780 which is the central estimate and gets us up within $20 million of the high estimate.

Mr. Hubbard said that if considering just the unpaid losses and maintaining the reserve strengthening already in play, that is added to the $780.6 million which were established by prior Board decisions. He clarified that Towers Watson's central estimate of $891.4 million compared to management's recommendation of $932.2 million constitutes 4.6 percent more in booked liabilities and LAE than Towers Watson's central estimate.

Chair Miltenberger called on Mr. Zanto for questions.

Mr. Zanto indicated that he did not have any questions, he was just trying to process the recommendation.

Chair Miltenberger called for a break and upon calling the meeting back to order asked Mark Barry, Vice President of Corporate Support to present.

D. FY15 Preliminary Financial Report – Mark Barry, V.P. Corporate Support

Mr. Barry pointed out that the low estimate of the actuarial range is $736.6 million and the high estimate is $988.5 million. He explained that the reason for the range is to provide Board members with the low and high estimates for loss reserves and reinsurance recoverable. He noted that management's recommendation of $932 million is approximately $55 million below that high end of the actuaries estimate.

He provided a comparison between last year's loss reserve of $924.6 million and this year's loss reserve of $932.2 million which was a total projected loss increase of $7.6 million or .82 percent from FY2014. He provided a condensed balance sheet and explained how investments, assets and liabilities and equity have performed to date for the fiscal year.

FY15 Balance Sheet

Condensed Balance Sheet			
	FY 2015	FY 2014	Variance
ADMITTED ASSETS			
Bonds	1,132,699,368	1,083,973,027	48,726,341
Equity Securities	165,361,933	167,515,006	(2,153,073)
Real Estate Investments	26,375,740	26,908,775	(533,035)
Cash and Short-term Investment	34,182,977	38,011,790	(3,828,813)
Other Invested Assets	85,920,568	74,841,190	11,079,378
Securities Lending Collateral	90,946,591	166,416,008	(75,469,417)
Total Investments and Cash	1,535,487,177	1,557,665,796	(22,178,619)
Other Admitted Assets	124,160,059	113,444,450	10,715,609
Total Admitted Assets	1,659,647,236	1,671,110,246	(11,463,010)
LIABILITIES AND EQUITY			
Reserve for Unpaid Losses	813,008,940	805,717,546	7,291,394
Reserve for Unpaid Loss Adjustment Exp.	119,192,503	118,880,034	312,469
Securities Lending Liability	90,946,591	166,416,008	(75,469,417)
Other Liabilities	156,252,542	136,244,064	20,008,478
Total Liabilities	1,179,400,576	1,227,257,652	(47,857,076)
Policyholders' Equity	480,246,660	443,852,594	36,394,066

He provided historical information on loss and LAE, reinsurance recoverable and policyholder equity and also provided an illustration of investment asset distribution. He noted that changes in policyholder equity have been erratic primarily due to unrealized gains in the investment markets principally on the equities side. The 2015 change dipped to 8.2% growth and much of that was from the $20M dividend and investment markets not being as robust as in previous years.

He said the Reserve to Equity ratio for the year was 1.94 to 1 which was an improvement from 2.08 to 1 from last year. The causes for the improvement would include: stabilized premium, stabilized loss reserves and management of claims, expense management and investment market returns.

Mr. Barry provided a review of Risk Based Capital (RBC) which is a formula driven calculation evaluating the **minimum** amount of capital or surplus a company needs based on their exposure to various risks. Risk areas include: underwriting, invested assets, credit and other things like off balance sheet, contingencies or guarantees. He explained that the RBC triggers are at the Company Action Level (CAL), Regulatory Action Level (RAL) or Authorized Control Level (ACL). For the CAL, the company must prepare a plan that identifies the conditions that caused the CAL trigger and propose corrective actions to be taken. The RAL requires the insurer to prepare and submit a plan to the Insurance Commissioner who examines and analyses the assets, liabilities and operations of the company and issues an order requiring corrective actions. The ACL is when the Insurance Commissioner takes the actions under the RAL criteria or if the commissioner considered it to be in the best interest of the policyholders and the public, places the company under regulatory control under Title 33, Chapter 2, part 13. He described the action levels depicted in the graph below and explained that as established in SB123 the action level criteria that will be applied to MSF are higher than for private carriers.

Risk Based Capital (RBC)

	Title 33 Private Insurance Carriers (As Percent of ACL)	SB 123 Criteria to Apply to MSF
Company Action Level (CAL)	200%	400%
Regulatory Action Level (RAL)	150%	300%
Authorized Control Level (ACL)	100%	100%
Mandatory Control Level (MCL)	70%	70%

Mr. Barry provided an overview of the FY15 income statement depicted below

FY15 Income Statement

Condensed Income Statement	FY2015	FY2014	Variance
Net Premium Earned	164,556,709	165,271,880	(715,171)
Losses Incurred	121,643,987	127,812,156	(6,168,169)
Loss Expenses Incurred	16,933,056	15,538,264	1,394,792
Underwriting Expenses Incurred	25,841,900	20,538,085	5,303,815
Net Underwriting Gain/(Loss)	137,767	1,383,375	(1,245,608)
Net Investment Income Earned	41,398,973	42,457,728	(1,058,755)
Net Realized Capital Gains (Losses)	9,309,050	14,279,687	(4,970,637)
Net Income after Dividends	26,776,753	41,742,579	(14,965,826)
Prior Year End Policyholders' Equity	443,852,594	372,277,435	71,575,159
Net Unrealized Gains (Losses) on Inv.	9,016,970	28,036,023	(19,019,053)
Change in Non-admitted Assets	600,343	646,364	(46,021)
Other Adjustments - Pension Liability	-	1,150,193	(1,150,193)
End of Period Equity	480,246,660	443,852,594	36,394,066
Combined Ratio	99.9%	99.2%	0.8%
Expense Ratio	26.0%	21.8%	4.2%
Loss Ratio	73.9%	77.3%	(3.4%)
Operating Ratio	74.8%	73.5%	1.3%

He provided a premium history and noted that MSF payroll is growing despite a zero percent rate change; however, net earned premium has had a slight decrease due to the estimated amount of return premium being lower than projected and reinsurance ceded $929 thousand higher than planned.

He said the expense ratio is up slightly from last year at 26 percent compared to 22 percent for FY14 and 24 percent for FY13. He provided a depiction of expense ratios for private carriers which illustrated that MSF is very competitive on the expense side.

Mr. Barry said that in 2016, MSF took a five percent rate decrease which eliminates any profit coming in on its rates. The volatility in the investment markets and decreasing investment yield are also concerns with regard to the gains that have been seen in prior years and any hope of repeating that surplus growth. He said the $64 million in additional reserves is tied to the concern that we do not realize the HB334 savings that were projected. He said those are some of the headwinds that the Board needs to be aware of and keep in mind.

He provided the reconciliation of statutory accounting requirements to the GASB reporting and noted that MSF had sought a legal interpretation from the Crowley Fleck law firm on the treatment of pension accounting for statutory purposes. Crowley Fleck's legal determination indicated that MSF does not have to report the unfunded liability, thus MSF will not record the $19.6 million unfunded liability on its statutory statements

FY15 Loss Reserves Request for Board Approval

Loss and LAE Reserves	FY 2015
Net Unpaid Loss Reserves (Towers-Watson)	780,521,872
MSF Adjustments:	
Estimated Reinsurance Recoverable	(34,715,653)
Reserve Strengthening	64,200,000
OSC and EL	3,002,721
Total Unpaid Losses	813,008,940
Loss Adjustment Expenses Reserves	119,192,503
Total Unpaid Loss and LAE	932,201,443

Mr. Barry requested Board approval for the unpaid loss reserves and loss Adjustment Expense reserves based on the recommendation depicted on the previous page for a total of $932.2 million.

Chair Miltenberger thanked Mr. Barry for his presentation and called for questions from the Board.

Mr. Brenneman stated that he had a motion to suggest prior to the main motion.

Mr. Brenneman made a motion that the reserve strengthening be changed to $24.2 million.

Chair Miltenberger pointed out that he believed with the LAE there was a multiplicative effect and asked if Mr. Brenneman wanted to include that in his motion.

Mr. Brenneman agreed there would be a multiplicative effect but remarked that there were mathematicians sitting amongst them who could quickly come up with that.

Chair Miltenberger called for a second.

Ms. VanRiper seconded the motion. Chair Miltenberger called for discussion.

Mr. Dykstra asked Mr. Brenneman where he got that number?

Mr. Brenneman said he pulled it out of the air just like the $64.2 million that he believed came out of the air. He qualified that remark by saying that in listening to Mr. Barry's presentation, there was no indication that there has been even more than the $8 million that was required last year above what had been allocated or somewhere around there for additional losses.

Mr. Barry noted that last year the Board voted to increase the reserve strengthening by $10 million, making the amount $64.2 million.

Mr. Brenneman said the reserves exist to pay the expenses that are incurred this year and all the expenses that happen from now until forever.

Mr. Barry explained that the loss reserves, as estimated by Towers Watson, include an estimate for a decreased benefit level as a result of HB334 which means reserves have been reduced by 22 percent per year for four years. The $64.2 million exists in case savings that are projected under HB334 are not realized. He said if there is litigation that removes the five year cut-off on claims, the reserves afford MSF a financial cushion to address those unexpected costs rather than having to immediately tap into surplus to pay the bills.

Mr. Brenneman said he understood that.

President Hubbard encouraged the Board not to adopt the proposed motion. He said he understood and appreciated the reasoning for the proposed motion, specifically the pressure from legislators who testify to the Board that MSF is overcapitalized and the appearance of actuarial reports that indicate that MSF is financially healthy. He said there is still substantial risk exposure for MSF which is one of the reasons he asked Mr. Greig to clarify the central estimate. He had hoped to not give the Board an over-abundance of confidence that the central estimate is anything more than an actuarial 50/50. He said $64 million on $900 million or 4.6 percent more than the central estimate, is a very small percentage hedge toward having a greater degree of confidence that MSF's financial solvency will come closer to the ultimate liabilities of the New Fund. He said inadequate reserves is the largest and most volatile potential risk to MSF's assets and financial health as an organization which he believes calls for maintaining a more conservative reserve estimate. There is a second opportunity to revisit this full context in November with regard to a dividend declaration. The discussion about the reserve position maintained by MSF would be very germane and relevant to dividend declaration discussion because the Board will be considering the risk to equity in that discussion. HB334 savings have not been realized yet and the Board will need to determine to what degree MSF reserves are sufficient to safely declare back to customers. He said that though he recognized the concerns, he believed that pulling a number out of the air is not wise though he respected the honesty. He said the analytics that went into making those recommendations to hedge against the central estimate still remain valid and sound and he encouraged the Board to not adopt the motion.

Chair Miltenberger thanked Mr. Hubbard and commented that he thought Mr. Barry's analysis of MSF's finances was pretty thorough. He asked Mr. Barry what the annual fee for Mr. Grieg's services was and if management continued to have confidence in Mr. Greig and his actuarial advice.

Mr. Barry said the fee was about $270,000 per year which included this report, a rate level report and a report that will be heard at the November Board meeting.

He also pointed out that the consulting actuaries contracted by CSI and LAD to review MSF's financials and the work of Towers Watson, have concluded that MSF's loss reserves are acceptable based on the level of reserve strengthening that has been executed to date. Both actuaries have indicated that they would estimate higher loss reserves which is based primarily on the methodologies utilized to make the determination. Towers Watson also employs an understanding, of MSF's operations and applies those judgments to its recommendations. Tower Watsons recommendations are lower than the other actuaries recommendations based on their judgment.

Chair Miltenberger asked if MSF's internal actuary completed a comparison analysis that would justify the additional $64 million recommendation.

Mr. Barry said yes, the internal actuary does prepare a comparison and calculates the potential development on accident years. He said there are two concerns; unrealized savings from HB334, as well as a general analysis of pressure to higher losses on prior years. A review of the summary of the actuaries' report will illustrate that there is negative IBNR on some of the older New Fund years which indicate potential development on those years and is being given some weight. MSF's analysis this year indicated additional amounts of $10 or $11 million that could have been recommended for reserve strengthening; however, staff recalled the Board's concerns during last year's discussion regarding the reserve strengthening levels. Those concerns are why staff did not recommend the additional reserves. The amounts were primarily derived from considerations adding one more year under HB334 benefits.

Chair Miltenberger thanked Mr. Barry and said he would offer further comment then leave the discussion open for further questions by the Board and the public. He said his last comment would simply be that looking at the finances, he thought MSF seems to be doing well without any reference to legislative or executive pressure upon the organization. He said that he recognizes that MSF's primary duty is to be there for injured workers so that in the event of a worst case scenario there are sufficient dollars to fulfill MSF's obligations to the workers of Montana. He said he would be supportive of Mr. Brenneman's motion but that was his personal opinion. He encouraged Ms. VanRiper or Mr. Zanto to share their thoughts on this issue or a counter recommendation if appropriate.

Mr. Zanto commented that last year at this meeting the Board discussed the impacts regarding future changes in reserve strengthening and what the ultimate reaction would be when discussing rate setting and dividend declaration. He said with regard to Mr. Miltenberger's comments and establishing a solid foundation in which MSF is still able to pay benefits to injured workers, he is also interested in the impacts to employers. He expressed concern that if no adjustments are made now, during rate setting, the Board may be setting themselves up for a decision that requires rate increases or a smaller dividend in the future. He asked President Hubbard if the Board accepted the recommendation to take a more conservative approach with reserve strengthening what would be the ultimate impact when determining rates? He asked if the Board faced the potential of having to increase rates or readjust reserve strengthening, would they be locked into this decision now?

President Hubbard thanked Mr. Zanto for the question. He said with regard to the rate itself, the rate level decision the Board makes is essentially about the expected loss costs in the future. So the case reserves or financial reserves that the Board has already established support already incurred claims and the potential that those claim liabilities will develop upward. He explained that the Board should think of the $64 million as a slightly more conservative estimate of past liabilities that are already incurred. That obligation already exists, regardless of whatever the medical bill or the permanent partial or permanent total status is. MSF has the burden to pay those claims and that is what that number represents. The Board's rate level discussion is whether or not the rates need to include a contribution to equity which is a significant decision on the Board's part with regard to maintaining the right equity level. In that discussion, the Board will need to ask if it feels comfortable that the equity level could absorb any kind of material change in the long term liabilities of State Fund. He said the rate is not designed that way, nor would he recommend that the Board made a decision to book lower ultimate liabilities that would then cause the Board to have to implement a rate level increase.

Regarding the use of dividend declaration, he offered an example of the Board being confident in Mr. Greig's analytics and adopting a loss exposure of $803 million which is the low end of the range and would mean a higher level of risk. He said all of that money would flow to the equity side and the Board would then need to discuss that they expect liabilities to come in at the low end level and determine whether or not MSF could withstand any potential adverse catastrophic risk or exposure to establish a safe dividend level. He noted that good and bad development run in cycles and when he first became CEO, MSF had to book $35 million of adverse development. He said MSF has enjoyed a period of relative stability with regard to development; however, that stability has been coming down and he was trying to convey the magnitude of this decision.

Chair Miltenberger called for additional questions or comments on the motion.

Mr. Dykstra stated that he has been considering the impacts of not realizing the savings assumed under HB334 for some years now. Though he assumes there will be litigation regarding the five year cut off, he did not have an opinion on how severe the affects could be.
He asked if MSF does experience some adverse rulings against HB334 what is the time interval or timeline the Board would have to smooth out the impacts of that. He said he would really like to lower that number as well and wondered if that would be imprudent assuming there were a number of years to smooth out the impact.

President Hubbard remarked that the numbers make people think that this is simply a matter of math; however, there is a whole lot of judgement that goes in this decision. The law requires this Board and management to pick a number that is more than likely to meet the obligations of state fund not less than likely when an exposure, a risk and expense is uncertain and not readily calculable. He said that is his mandate as the CEO, to make sure that he and staff are providing recommendations that are more than likely to meet future obligations and keep the state fund solvent, rather than less likely. He said that about half of the savings of HB334 are embedded in the termination of medical benefits after five years of the date of injury. He asked Dan Gengler, MSF Internal Actuary, if it were challenged and ultimately determined to be unconstitutional, how much money would MSF have been undercharging in terms of liability, year over year?

Mr. Gengler stated that if only approximately half of the savings of HB334 are realized and half of the savings that we have been counting on do not materialize, by the time, seven to eight years later, that were realized that, MSF would be somewhere between $170 to $200 million under water. That is because there would be the accumulation of seven to eight years' worth of savings that are currently being assumed, yet no hard evidence that they are actually going to be there.

President Hubbard said decisions that affect the constitutionality of laws in Montana are retroactive by the Supreme Court's own mandate so if the law changes, any open claims would have a retrospective liability.

Mr. Greig responded to Mr. Dykstra's question and added that in order to manage the increase in liabilities, the Board would need to immediately book the $200 million of unpaid losses or otherwise risk getting in trouble with the insurance department. Secondly, since a 22 percent rate level decrease has been embedded, rates would have to be increased by more than 22 percent, about 26 percent because HB334 is no longer valid.

Chair Miltenberger called for other comments or questions; there were none. He pointed out that MSF apparently currently has $259 million in surplus above the 400 percent of the required amount under SB123. Under the Department of Insurance scrutiny, we have to maintain 400 percent of our authorized control or Risk Based Capital. We are at $260 million above that 400 percent at this point, so in terms of context, while there could be a booking of $200 million that would not put us into a danger zone immediately. He said that though it is something we ought to be contemplating, he thinks it is something we need to be seriously thoughtful about but that does not change his perspective that at this point we are in a good position to protect the injured workers. He said it is his opinion that increasing the reserves above the central estimate by $24 million is prudent.

Mr. Brenneman said "I realize that I engage in a profession that the risks are insanely present all of the time so perhaps my perspective isn't the best one to take when you actually have resources that you can allocate for this." He said the fact is, that should or when the first case comes around regarding HB334, MSF has an entire room full of competent attorneys who will be able to assess at that point what is the likely liability for MSF for this particular case and subsequent cases coming. He said the cases will not just appear all of a sudden; the proceedings will take years and at which time our attorneys will be advising about needed reserves. He said he did not believe it was quite the fearsome terrible boogey man that it might be portrayed by those of us who we pay to make us aware of those risks. He added that he has been telling legislators since his appointment to the Board that MSF needs to do some reserve strengthening and capital building and here is where we need to get. He said we have gotten there and if we continue to say, well, we weren't quite where we thought and there are some other reasons to consider, we start to lose credibility with our story at that point.

President Hubbard asked the Chair if he could engage in a small discussion on that issue with Mr. Brenneman?

Chair Miltenberger consented to just a brief one.

President Hubbard said he thought Mr. Brenneman was going to withdraw his motion because he was validating that the risk is the same and is still there which is the reason for the reserve strengthening in the first place. He noted that the Board and MSF staff have been consistent with what has been told to the legislature. The last rate year had zero contribution to equity included in the rate level in recognition of that fact that we achieved our objectives to be in the target range of reserve to equity. He said the Board was credible on that point because they took it to the bank for policyholders by not including any contribution to equity in rates. Last November, the Board declared the largest dividend in the history of the MSF of $20 million. That also delivered on the message that the reserve to equity ratio target was achieved. Board members will have another opportunity to do that in November as well.

Chair Miltenberger thanked President Hubbard and called for any more comments from the Board before opening it up to the public.

Ms. VanRiper stated that she was not sure of the protocol; however, wanted to move to amend the motion. Chair Miltenberger encouraged her to proceed.

Ms. Van Riper made a motion to amend calling for a $32.1 reserve strengthening figure which is half of what the State Fund requested. Mr. Dykstra seconded the motion.

Chair Miltenberger acknowledged that the motion had been seconded and asked if it was necessary to call on Mr. Brenneman to accept that amendment.

President Hubbard said it was not, the Board would simply need to debate the motion.

Chair Miltenberger called for discussion.

Ms. VanRiper explained that she proposed that amount because it was half of what management recommended. She said her proposal was probably partially emotional because she was at State Fund back when they were settling permanent total disability cases at a market rate discount when an unexpected Supreme Court opinion stated that the discount could not be applied. She said state fund was not in a good position to absorb that so she recognizes that some crazy things can happen. She said she is both sympathetic to the notion of not adding to the reserves more than is really prudent but also thinks that the Board should heed the state fund experts who have really analyzed all of this. She said she thought the Board needed to come into this a little bit closer to management's recommendation.

Chair Miltenberger called for additional discussion. There was none. He then invited members of the public to comment or ask questions and in particular Senator Vance. There was no public comment.

Chair Miltenberger clarified that the amended motion was $32.1 million and then a percentage of that for the loss adjustment expense.

Chair Miltenberger called for the vote: Mr. Brenneman, Ms. VanRiper, Mr. Zanto and the Chair voted yes, Mr. Dykstra voted no. The motion passed.

Mr. Brenneman pointed out that the Board still needed to vote on the motion of whether or not to change the surplus.

Mr. Barry provided an estimate of the updated amounts for the motion.

A clarification discussion regarding the next motion to be voted on was held. Mr. Brenneman stated that the Board needed to vote on whether or not the Board wanted to change the reserve strengthening from 64 to 32.1. He said if that motion fails then Board will need to go back to determining whether to use the suggested motion or not. He said the Board needed to vote on his motion which was amended.

Chair Miltenberger called for the vote. Mr. Brenneman, Ms. VanRiper, Mr. Zanto and the Chair voted yes, Mr. Dykstra voted no. The motion passed.

Mr. Dykstra offered an editorial comment while waiting for the correct amounts to be placed into the motion. He said that he was not sure that he was opposed to his colleagues, he really wished that he had a day or two to consider this action.

President Hubbard reiterated that management's recommendation involved a lot of judgement and he hoped that the Board felt that he had given them a credible reserve strengthening recommendation. He noted it is the Board's decision as to how much is carried over. He added that the financials will change; the equity level will be higher than it would have been otherwise and staff will prepare and have audited those financial statements based on this Board's decision. He stated that the auditors will review to assure the numbers are correct and the Board will see the resulting product at the November meeting when the Board considers how much equity and surplus is necessary.

Mr. Barry provided the corrected numbers to the Board: losses become $781,808,940, and the LAE became $114,634,303 for a total of $896,443,243.

E. Adoption of Montana State Fund FY15 Unpaid Loss and Loss Adjustment Expenses Reserve Estimate – Laurence Hubbard, President/CEO

Chair Miltenberger asked Board members if there were questions or if they were prepared to take action.

Mr. Brenneman made a motion that based on the actuary's best estimate of unpaid losses and loss adjustment expenses, adjusted for reinsurance recoverable and for the Board's recommendation for loss reserves for Other States coverage, Employers' Liability, and reserve strengthening, undiscounted as of June 30, 2015, I move we adopt $781,808,940 as unpaid loss reserves and $114,634,303 as the unpaid loss adjustment or if those numbers need to be adjusted slightly by the auditor, expense reserve estimates for the financial statements of the Montana State Fund for the fiscal year ending on June 30, 2015. Mr. Dykstra seconded the motion. Chair Miltenberger called for discussion, questions or comments from the Board and the public.

There were no comments or questions from the public or the Board; however Mr. Barry asked that if staff determined during the lunch break that the numbers were incorrect this issue could be revisited when the meeting reconvened.

Chair Miltenberger said yes, the Board would redo the motion.

Mr. Brenneman said he tried to include that contingency to make slight allocation changes in his motion.

Chair Miltenberger adjourned the meeting for the lunch break.

Upon reconvening the meeting, Chair Miltenberger noted that there was a slight restatement of the numbers represented in the last motion. Mr. Barry shared the correct number with Chair Miltenberger and he read into the record that the motion that was passed unanimously should have read that the reserve for unpaid losses is $780,908,940 and the loss adjustment expenses have not changed and remain as they were stated in the record at $114,634,303. With no comments or objections those amount were added to the record.

Chair Miltenberger announced that Agenda Item VII, the President/CEO Compensation Update and discussion were being moved to this point in the meeting and introduced Mr. Neville Kenning.

VII. President/CEO Compensation

A. Compensation Update – Neville Kenning, Kenning Consulting

Mr. Kenning thanked the Board for the opportunity to present on the CEO compensation considerations. He stated that the purpose of his presentation was to provide context in the public setting for when the Board moved into the private setting to discuss the CEO's compensation.

He stated that in accordance with good governance practices, the Board of Directors of MSF adopted a formal approach to the review and setting of CEO compensation. He reminded Board members that MCA 39-71-2317 sets authority for the Board to appoint and set compensation for the CEO and the additional statute of MCA 2-18-103 exempts the president's position from the state's classification and compensation plan. The current plan for the CEO had its genesis back in 2000 when a policy was adopted by the Board to set the policy position at 95% of the national average of all Group A state funds. The reason it was set at 95% was the consideration of the Montana factor, which stated that the labor rate in Montana is not as high as the national average. The market target was revisited in 2004 and a regional cut of State Fund CEO's was taken into account.

Mr. Kenning said there is no longer an incentive compensation plan for the CEO position or for MSF employees. He noted that other state funds and private sector organizations, from which MSF competes for talent, still have employee incentive plans and on balance that will make MSF's compensation less competitive than those organizations.

He explained how Kenning Consulting's CEO compensation survey was conducted and the groupings which provide a same-company analysis to provide a clear reliable sense of how the market moves for similar companies. He noted that the data he shared with the Board excluded President Hubbard's salary information. He provided CEO salary increase and incentive payout data for FY2014 within the AASCIF-responding organizations and also a private sector comparison.

Mr. Kenning identified the considerations the Board would want to utilize when determining the MSF CEO salary. He noted that the primary factor for consideration is the performance of the incumbent against the performance objectives and measures for the period under review.

Chair Miltenberger called for questions from the Board.

VIII. President/CEO Compensation

Introduction – Notice of Closure of Meeting *Richard Miltenberger, Acting Chair of the Board*
Chair Miltenberger asked if Mr. Hubbard wished to waive his right of privacy for his individual performance review.

Mr. Hubbard stated that he did not wish to waive his right to privacy. He would however waive his right if the Board wished to consult with Mr. Kenning, Nancy Butler or Rick Duane.

Chair Miltenberger closed the meeting at this time, which was 1:30 p.m. to be reopened after the discussion of the President/CEO's individual performance review for action by the Board on the President/CEO's compensation.

IX. President/CEO Compensation – Closed Meeting

A. *Call to Order*
B. *President/CEO's Compensation/Incentive Plan Performance Review*

REOPEN Meeting

X. President/CEO Compensation

Chair Miltenberger called the meeting back to order.

A. *Introduction – Richard Miltenberger, Acting Chair of the Board*
Chair Miltenberger introduced the CEO compensation recommendation.

B. *President/CEO's Annual Compensation*
He called for action from the Board.

Mr. Dykstra made a motion that the annual base compensation of Laurence Hubbard, President and CEO of Montana State Fund, be set by the board at $305,000, effective September 5, 2015. Ms. VanRiper seconded the motion. Chair Miltenberger called for discussion; there was none. He called for comments from the public; seeing none he called for the vote and the motion passed unanimously.

Chair Miltenberger stated that the Board wished to express its thanks to Mr. Hubbard for his excellent service over the past year and were looking forward to many years to come and certainly this coming year.

President Hubbard thanked the Board.

C. *Budget Amendment for the Period of July 1, 2015 to June 30, 2016*

Ms. VanRiper moved that the budget for the period of July 1, 2015 to June 30, 2016 be amended to include the Board approved increase to the President/CEO's base compensation. Mr. Dykstra seconded the motion. Chair Miltenberger called for questions or comments; there being none, he called for the vote. The motion passed unanimously.

Chair Miltenberger also read into the record some of the administrative matters concerning the CEO performance review that will be adopted going forward. The executive compensation consultant will be the direct recipient of the Vice President's and Board member's performance evaluations of the CEO and will distribute those as necessary. Board consensus determined that as a best practice in this age of transparency, the Board Chair will locate an off-site repository for certain elements of the CEOs evaluation and file. Mr. Zanto will address that need upon his return to Montana.

IV. Reserve Report – Old Fund

A. Overview of Old Fund Statutes – Mark Barry, V.P. Corporate Support

Mark Barry noted that there are two statutes that require separation of the Old Fund claims and expenses from MSF claims and expenses. He advised the Board that Section 39-71-2351, MCA separates the Old Fund liability for funding of claims from New Fund liability. Section 39-71-2352, MCA calls for a separate payment source and structure for claims. The MSF independent actuary projects the unpaid claims liability of the Old Fund. "Adequately funded" means the present value of: (a) the total cost of future benefits remaining to be paid; and (b) the cost of administering the claims. If in any fiscal year the Old Fund is not adequately funded, any amount necessary to pay claims for injuries resulting from accidents that occurred before July 1, 1990, must be transferred from the General Fund.

Chair Miltenberger called for questions. There were none.

B. Old Fund FY15 Reserve Report – Russell Greig, Consulting Actuary, Towers Watson

Mr. Greig reported that Tower Watson's objective in the analysis of the Old Fund is to estimate the aggregate amount of unpaid future claims benefits with a range of estimates. It includes a provision for claim administration expenses, as well as a provision for future Department of Labor assessments. In addition, because Montana statute requires an estimate of the present value of unpaid liabilities for purposes of determining whether the Old Fund is adequately funded, it's necessary to forecast the timing of the payout. Mr. Greig noted that the Old Fund analysis encompasses all injuries occurring prior to July 1, 1990. He then reviewed the methodologies used to arrive at the aggregate amount of unpaid claims.

His indemnity observations are that in fiscal year 2015, payment activity has been slightly higher than expected. Towers Watson is projecting a continued decline in indemnity payment activity as the Old Fund claims continue to mature.

In recent fiscal years, actual medical payment activity has been above expectations. Towers Watson has been weighting this higher activity level into its projections and long-term development patterns are still given considerable weight in their selections.

Selected unpaid medical losses are significantly lower than the case reserve indications with the actuarial central estimate being $27.6 million. Mr. Greig stated that Towers Watson is projecting a less gradual decline in medical payment activity. He noted that development patterns are continuing to lengthen on the Old Fund. The medical payments have been declining as expected over recent fiscal years and as a result, the estimated unpaid losses have been increased.

Mr. Greig's overall conclusion as of June 30, 2015 for estimated unpaid losses and claims adjustment expenses is that the unpaid claim benefits for medical are $27.6 million and indemnity is $8.2 million for a total of $35.8 million for benefits. The unpaid claims administration expense is $4.7 million and the future DLI assessment is $1.1 million, making the undiscounted claim-related unpaid amounts $41.6 million.

Chair Miltenberger called for questions or comments from the Board and the public; there were none.

C. *Old Fund FY15 Reserve Recommendations – Laurence Hubbard, President/CEO*
President Hubbard stated that the Old Fund is essentially a run off fund that does not experience new incurred claims occurring however, there are some asbestos claims being originate that belong to Old Fund years. He said those new claims do not impact the Old Fund loss reserve recommendation.

Mr. Hubbard asked Mr. Greig to explain how the gap between the central estimate and the low range is much tighter and narrower and how can that be if it is supposed to be the central estimate?

Mr. Greig said that it is the same for the New Fund due to skewness in the loss distribution. In looking at the unpaid amounts, there is a higher probability that things could pay out a little bit higher, and compared to medical, substantially higher versus paying out lower. So there are more bad things that can happen versus good things and that is just part of the insurance business. When we get the question about a symmetrical distribution or the difference between the low and the actuarial central estimate and the difference and the actuarial central and the high, we are really thinking about a normal distribution and that goes back to statistics 101. Nothing in insurance represents a symmetric distribution. That is because insurance is in place for those small probability events that cost a whole lot of money. Because if it is a small loss you can retain it, you don't need insurance for it.

Mr. Hubbard recommended the Board adopt, on an undiscounted basis, the Towers Watson's best estimate of unpaid losses and LAE for FY15 in the amount of $41,596,811. He clarified that this amount did not contain any reserve strengthening.

D. *Adoption of Old Fund FY15 Unpaid Loss and Loss Adjustment Expense Reserve Estimate – Laurence Hubbard, President/CEO*

Ms. VanRiper made a motion that the Board adopt for the Old Fund, based on the actuary's best estimate of unpaid losses and loss adjustment expenses for Fiscal Year 2015, the amount of $41,596,811 undiscounted as of June 30, 2015. Mr. Dykstra seconded the motion. Chair Miltenberger called for questions or discussion from the board and the public, there being none, he called for the vote. The motion passed unanimously.

V. Corporate Support

A. *FY15 Final Budget Report – Rene Martello, Controller*
Ms. Martello provided the results of the fiscal year end 2015 budget variance report. She noted that this is the very last fiscal year variance report based on a June 30 year end for MSF. She said net earned premium for FY15 came in at $164.6 million which was $2.5 million below plan. Operational expenditures were under by $1.1 million and claim benefits payments were under by $3.2 million. She noted that the expenditures included the $8 million amendment that was approved by the Board in May 2015 and without the amendment, the budget would have been 2.2 percent or $3.7 million over for the year. Claim benefit payments were $3.2 million or 2.7 percent under planned.

She said operational expenditure variances were: personal services are under $1.2 million, operating expenses are $100 thousand below, equipment and tangible assets were $200 thousand below and allocated loss adjustment expenses were $400 thousand over. Total operations expenditures were $1.1 million under budget. She summarized that the MSF FY15 budget was 2.5% under the amended budget.

There were no questions on the New Fund variance report.

Ms. Martello went on to review the funding estimate for the Old Fund and noted that the Old Fund will remain on the June 30 fiscal year end date. She said the administrative costs were over by $21,598 due to increased costs for medical and legal review related to the asbestos claims. The DOLI assessment was on track; however, there was a claim liability review that was not originally planned for but was added as requested by the EAIC that cost $48,000. LAE was also over by $10 thousand from plan making total operational expenditures $71,884 over plan. Benefit payments were $77,370 under what was estimated putting the total funding at 99.99 percent of the funding estimate spent or $5,486 under budget.

Chair Miltenberger called for additional questions. There were none.

B. *Data Measurement Criteria for Premium & Incurred Losses for Potential Dividend Declaration – Rene Martello, Controller*

Ms. Martello explained that to prepare for the November Board meeting and the dividend discussion, there is a requirement under the administrative rules that the board must approve the data measurement criteria of when losses and premium will be valued. Management recommended and requested an approval to use June 30, 2015 as the date of measurement for losses of premium of policies with coverage in policy year 2013. This is consistent with the evaluation date that has been used for the past seven years and allows for a reasonable period of time to evaluate the premium and maturity of losses for those policies.

Chair Miltenberger called for questions, there were none.

Mr. Dykstra made a motion that the Board approve management's recommendation to utilize June 30, 2015 as the date to value premium and incurred losses on new and renewal policies from July 1, 2012 through June 30, 2013 for potential dividend calculation purposes. The motion was seconded by Ms. VanRiper. Chair Miltenberger called for questions or comments, there being none he called for the vote. The motion passed unanimously.

VI. Public Meeting on FY15 Strategic Business Plan Performance

A. *Presentation of Results – Shannon Copps, Director of Enterprise Strategy and Project Management*

Ms. Copps provided the results of the FY15 Strategic Business Plan which represented the time period beginning July 2014 to June of 2015. She reported that there are five success measures that are set each year which are key to gauging MSF's progress. She said the Key Success Measures were:

- Generate Net Earned premium of $167.0 million
    - Achieved $164.6 million

Ms. Copps noted that due to the action taken by the Board earlier in the meeting the loss ratio and expense ratio results were different than the slides originally prepared for this presentation which were based on management's recommendation.

- Achieve Fiscal Year Loss Ratio of 74.7 percent
    - Achieved 54.4 percent
- Achieve Expense Ratio of 27.2 percent or Less
    - Achieved 23.2 percent
- Attain Investment Income of $49.2 million
    - Achieved $50.7 million
- General Net Operating Income $40.0 million before dividend
    - Achieved $83.4 million before dividend

She noted that MSF statutorily reports the premium to equity ratio result, also based on the earlier Board action is now .32 to 1 compared to the .36 to 1 plan.

Chair Miltenberger asked when the Board will adopt the Business Plan for 2016.

Mr. Hubbard stated that the 2016 Business Plan was adopted in June; however, it will be redone in December to accommodate the switch to calendar year reporting.

Ms. Copps then reported on the Business Plan Initiatives.

Enterprise Wide Initiatives categories and Executive Sponsors are:

- **Workforce : Sponsors – Rick Duane, Nancy Butler and Al Parisian**
  The *Engagement Initiative* (partially met) was developed to implement engagement strategies identified in FY2014 to enhance organizational communication, organizational effectiveness, and employee perceptions regarding respect and fairness.
    - Conduct a follow up engagement survey to measure the effectiveness of implemented engagement strategies.
      Result: Consulting firm administered full engagement survey in June 2015.
    - Show statistically significant improvement in engagement scores from FY2013 survey in the areas of: communication, organizational effectiveness, respect and fairness
      Result:
    -

FY13 Survey	FY15 Survey
Communication: 3.15 out of 5	Communication: 3.09 out of 5
Org Effectiveness: 3.10 out of 5	Org Effectiveness: 2.95 out of 5
Respect/Fairness: 3.11 out of 5	Respect/Fairness: 3.02 out of 5

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in voluntary non-retirement turnover rate below 6 percent. Result: voluntary non-retirement turnover rate of 9.78 percent

Mr. Miltenberger asked how many of the employees took the survey and if there was any incentive offered to complete the survey.

Mr. Duane said that 89 percent of the MSF employees completed that survey and there was a television offered to encourage completion of the survey. He added that ICF International, the company that administered the survey, expressed amazement that MSF achieved such high numbers of survey participation. The surmised that part of the high completion rate was the TV incentive and the other part was a clear indication that MSF has employees with high engagement levels who feel they can share their input.

The *Succession Initiative* (completed) formalized a well-defined and documented succession process that includes the continuation and enhancement of the Leadership Development Program based on year one results and feedback.

- Modify the Leadership Development Program as appropriate based on learnings from FY2014 pilot by September 30, 2014.
  Result: Thirteen recommendations made by FY2014 participants and all incorporated in 2015 program by September, 2014.
- Identify high potential candidates for FY2015 Leadership Development Program by December 31, 2014.
  Result: Four candidates selected by Executive team for FY2015 Leadership Development program by December 19, 2014.
- Launch FY2015 Leadership Development Program with any approved and funded modifications from the FY2014 program by March 31, 2015.
  Result: FY2015 Leadership Development Program launched on February 9, 2015.

- **Customer Service: Sponsors – Julie Jenkinson and Peter Strauss**
  The *Stay at Work*/*Return-to-Work Initiative* (complete) improves stakeholders' understanding of stay-at-work and return-to-work opportunities through targeted education and communication.
  - Reduce Temporary Total Disability from FY2014 baseline by five percent June 30, 2015.
    Result: Reduction of 20.3 percent. The Temporary Total Disability baseline as of August 31, 2014 was 34.13 weeks and as of August 31, 2015 was 27.18 weeks.
  - Host quarterly stay-at-work education webinars and achieve at least an 80 percent attendee evaluation rating.
    Result: Four education webinars hosted. 86.8 percent of attendees very satisfied or satisfied with the presentations.
  - Expand the job description bank on the MSF safety website to add a minimum of 50 additional job descriptions by June 30, 2015.
    Result: 52 job descriptions added to safemt.com job description bank.

- **Claim and Medical Management: Sponsors – Al Parisian and Julie Jenkinson**
  Claim Center Upgrade Initiative (complete) will maintain currency of a core business processing system and take advantage of new performance and business features.
  - Complete configuration and integration development by October 31, 2014.
    Result: User front end screens, interface system code and majority of nightly batch processing complete by October 31, 2014.

- Complete all testing phases by February 28, 2015.
  Result: Developer system testing, quality assurance testing, and user testing complete by February 12, 2015.
- Implement Claim Center upgrade in production environment by March 31, 2015.
  Result: Claim Center 8 implemented in production on February 14, 2015.

- **Infrastructure: Sponsors – Nancy Butler and Mark Barry**
  Structure Review Initiative (complete) was a collaborative efforts to draft legislation to move MSF under Title 33, Montana Insurance Code regulation.
  Success Measures
  - MSF to continue to serve as the guaranteed market for employers seeking workers' compensation insurance coverage in Montana.
  - MSF will continue to meet federal tax exempt status.
  - MSF will continue to use the unique agricultural and public entity class codes.
  - Ensure MSF's ability to establish and file multiple rating tiers for its book of business.
  - MSF will avoid unnecessary duplicative regulatory oversight.

  Results
  Senate Bill 123 was introduced and passed by the 2015 legislature and signed by the Governor to evolve MSF from legislative oversight to regulation under Title 33, Montana Insurance Code, beginning effective January 1, 2016. MSF worked cooperatively with CSI, the EAIC and bill sponsor Senator Tutvedt and other interested parties to draft the bill language.

  Senate Bill 123 met all five of MSF's objectives.

Ms. Copps noted that with the exception of the engagement initiative all projects were completed as scheduled and delivered meaningful deliverables for MSF.

Chair Miltenberger called for questions; there were none.

XI. Old Business/New Business
Chair Miltenberger called for Old or New Business; there was none.

XII. Public Comment
There was no public comment.

Mr. Dykstra made a motion to adjourn the Board meeting.
The meeting was adjourned at 4:19 p.m. The next scheduled board meeting will be held on Friday, November 20, 2015 at Montana State Fund, 855 Front Street, Helena, Montana in the first floor Board Room.

Respectfully submitted,

Verna Boucher
Special Assistant to the President/CEO