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MONTANA STATE FUND
BOARD OF DIRECTORS MEETING
March 10, 2017

The Montana State Fund (MSF) Board of Directors meeting was held March 10, 2017 in Montana State Fund's Board Room at 855 Front Street, Helena, Montana 59601.

Directors Attending

Lance Zanto, Chair, Helena
Bruce Mihelish, Lolo
Jack Owens, Missoula
Jan VanRiper, Helena
Richard Miltenberger, Helena
Lynda Moss, Billings
Matthew Mohr, Big Sky

State Fund Staff Attending

Laurence Hubbard, President/CEO
Verna Boucher, Special Asst to Pres/CEO
Kevin Braun, General Counsel
Mark Barry, Chief Financial Officer
Julie Jenkinson, Ops Vice President
Rick Duane, HR Vice President
Sam Heigh, Ops Support Vice President
Ethan Heverly, Dir., Gov. and Community Relations
Patti Grosfield, Internal Auditor
Lynn Mogstad, Business Unit Director
Darcy Dunlap, Actuarial Analyst
Hester Davies, Underwriting Services Specialist
Mary Boyle, Communications Specialist
Dan Gengler, Internal Actuary
Rene Martello, Controller
Christy Weikart, Underwriting Services Leader
Shannon Copps, Director, IT Plans & Controls
Al Parisian, CIO
Peter Strauss, Compliance Officer
Wayne Bunch, Business Unit Director
Nick Hopkins, Business Unit Director
Tammy Lynn, Safety Services Director
John Wilkins, Financial Analyst

Others Attending

Mari Kindberg, State Auditor's Office
Brenda Miller, Liberty Northwest
Les Vernon, Willis Towers Watson
Jeannie Keller, State Auditor's Office
Josh Porter, JLT Re
Bob Biskupiak, State Auditor's Office
Peter Van Nice, DLI-ERD
Pat Murdo, Legislative Services Division
Pete Burwell, Montana Chamber of Commerce

I. Meeting Preliminaries

A. Call to Order

Chair Zanto called the meeting to order at 8:33 am. He welcomed all attendees and thanked the Board and attendees for their attendance. He noted that due to weather and road conditions, Jan VanRiper and Lynda Moss were participating telephonically.

B. Approval of December 16, 2016 Minutes.

Chair Zanto called for a motion.

Richard Miltenberger made a motion to approve the December 16, 2016 minutes. The motion was seconded by Bruce Mihelish. Chair Zanto called for discussion from the Board, MSF staff and members of the public. Seeing none, he called for the vote and the motion passed unanimously.

C. Amended Motion on Consideration of Approval of the Construction Industry Premium Credit Program of Credit Percentages for Montana State Fund.

President Hubbard took a moment to introduce Josh Porter from JLT Re, MSF's reinsurance intermediary and noted that Mr. Porter has been working behind the scenes for many years supporting MSF's reinsurance programs.

He told the Board that it was necessary to amend a motion that was made at the December 16, 2016 Board meeting. A motion was made to adopt the construction credit plan; however, the drafting of the motion was in error and he apologized for the mistake that had been made. The draft motion read that the approval would be for "new and renewal policies with effective dates in Calendar Year 2017"; however, it should have read "with effective dates of July 1, 2017 to July 1, 2018." He asked the Board for action to amend the motion.

Chair Zanto made a motion the Board adopt the plan of credit percentages for Montana State Fund's Construction Industry Premium Credit Program, for new or renewal policies, with effective dates of July 1, 2017 to July 1, 2018, as proposed by Montana State Fund Management. Mr. Mihelish seconded the motion. Chair Zanto called for questions or discussion from those present. Seeing none, he called for the vote and the motion passed unanimously.

II. Ratemaking Decisions for July 1, 2017 to July 1, 2018

A. Overview of Rate Filing Process – Dan Gengler, Internal Actuary

Mr. Gengler provided an overview of the rate making process, explaining what a loss cost multiplier is and how MSF's current rates relate to the National Council on Compensation Insurance (NCCI) filing made this year. He also provided information on how MSF's rates benchmark to the market and reviewed the Board's key decision points in setting MSF's rates. He explained that the loss cost is the cost of benefits and claims management or loss adjustment expenses (LAE). In a loss cost state such as Montana, each carrier can evaluate what it thinks its loss costs are for the specific book of business they write and currently MSF estimates those costs to be about 3 percent lower than NCCI's stated loss cost. Also added to this calculation is an additional amount per hundred which represents the general overhead expense, acquisition or commission expense, profit and contingencies and offsets for underwriting programs and investment income on underwriting cash flow.

Mr. Gengler said MSF has five rate tiers which vary in percentage relationship to the NCCI loss cost; hence the five various loss cost multipliers. He said there are approximately 400 private carriers that hold filings in Montana to write workers' compensation business though only about 200 do so. He said their books of business vary from several million to tens of thousands of dollars. On average, MSF's filed rates are about eight percent lower than the average for all private carrier filed rates. Actual premiums employers pay may differ from these filed rates due to underwriting programs. He said the Board will be establishing the rate tiers for the coming rate year for business effective July 1, 2017.

Mr. Gengler said the key Board decisions will be: 1) the Board formally adopting the NCCI loss costs as the basis for MSF's rates, 2) establishing MSF's tiered rating plan 3) establish the loss cost multiplier for MSF's five rate tiers and 4) decision regarding various other rating programs.

Chair Zanto called for questions. There were none.

B. NCCI Montana Loss Costs Filing Update Effective July 1, 2017 – Dan Gengler, Internal Actuary

Mr. Gengler noted that the first step in the rate setting process is to formally adopt the NCCI loss costs as the basis for MSF's manual rates. He explained that Title 33 requires the use of approved

NCCI loss cost filings for private carriers and MSF. Montana's Commissioner of Securities and Insurance (CSI) has approved the NCCI loss cost filing for use in Montana for July 1, 2017.

Mr. Gengler said for July 1, 2017, NCCI has decreased their estimate of the cost of benefits and claims handling by an average of 7.8%. He said changes by individual class codes will vary, which means some will increase and others will decrease. He explained the statewide changes in loss-costs by industry and the maximum and minimum changes for individual class codes in each industry and noted that individual class codes generally decreased as much as 34% or increased as much as 20%.

C. *Adopt NCCI Filings/Loss-Costs Filing Effective July 1, 2017 – Dan Gengler, Internal Actuary*
Mr. Gengler said management's recommendation is to approve the NCCI loss costs as the basis for MSF's rates.

Chair Zanto called for questions from the Board and the public. There were none.

Mr. Mihelish made a motion for the Board to adopt the NCCI filed loss costs for rates applicable to new and renewal policies effective July 1, 2017 to July 1, 2018 for Montana State Fund classification codes. Matt Mohr seconded the motion. Chair Zanto called for further discussion from the Board and the audience; there was none and the motion passed unanimously.

D. *Multiple Rating Tiers and Certification – Dan Gengler, Internal Actuary*
Mr. Gengler presented management's request for the approval of MSF's Tiered Rating plan for the July 1, 2017 renewal process. He stated that this plan works in conjunction with the NCCI experience rating plan so that together they formulate the pricing mechanisms to put policyholders in the correct rate given their risk profile. The rating plan also creates appropriate safety incentives. The tiered rating plan must be actuarially sound and Willis Tower Watson (WTW) has provided a certification letter to the Board which concludes that MSF's tiered rating structure effective July 1, 2017 results in rates that are neither inadequate, excessive nor unfairly discriminatory. CSI has also offered an opinion on the MSF tiered rating plan for the past four years and has found it to be reasonable and not unfairly discriminatory.

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.

* No change from current tiered rating plan factors

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He said the tiered rating plan is based on three variables, 1) three-year claim frequency, 2) account size and 3) claim-free tenure. He explained the requirements for meeting these three criteria. Mr. Gengler provided the Board with specifics regarding the make-up of MSF's tiers and the manner in which policy placement is determined. He noted that the recommended table of factors (depicted on the previous page) contains no change from the prior year's table.

Mr. Mihelish asked how the tiered rating process would slot a new business?

Mr. Gengler clarified if the business was new to MSF, loss runs would be requested from the prior carrier and that information would be applied to the rating process to determine the correct tier. If the business is newly beginning, there are variables that take that into account. He said if there is insufficient claim history, there is a variable for that. He said new businesses tend to have a higher loss rate than well established, long-term businesses.

Mr. Gengler said management's recommendation is to approve the tiered rating criteria as presented and noted that Board members had been provided the Willis Tower Watson certification letter.

Chair Zanto called for questions from the Board. Chair Zanto called for a motion to approve the use of the multiple rating tiers and factors.

Mr. Mohr made a motion that the Board approve, for new and renewal policies effective July 1, 2017 to July 1, 2018, the Tiered Rating plan which consists of five rating tiers and that policies be assigned to the tiers based on the factors as presented by management. Jack Owens seconded the motion. Chair Zanto called for questions or discussion from the Board and the public; seeing none, he called for the vote. The motion passed unanimously.

E. 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. It is not inclusive of all expenses; just those common to renewing or writing a new policy. The current expense constant level is $175 and management's recommendation is to increase that amount to $180.

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 explained how the expense constant and the minimum loss based premium are calculated and clarified MSF would be applying a proration used for cancellations as specified in Title 33. He said management is requesting approval of an expense constant of $180 to be charged to all new and renewal accounts effective July 1, 2017 and a loss base minimum premium of $240 for a total minimum premium of $420.

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

Chair Zanto made a motion that the Board approve an expense constant of $180 for all new and renewal policies effective July 1, 2017 to July 1, 2018. In additional Chair Zanto moved the Board approve the amount of $240 for the loss-based portion of the Minimum Premium so the total Minimum Premium is $420 for new and renewal policies effective July 1, 2017 to July 1, 2018. The motion was seconded by Mr. Mihelish.. Chair Zanto called for discussion.

Mr. Miltenberger sought clarification on the need to have an expense constant. Mr. Barry and Mr. Gengler provided additional information that explained the process by which the expense constant was valued and applied.

Mr. Mihelish added that the expense constant MSF charges is lower than that of any other carrier in the industry. He also added that new businesses typically end up in the Tier 5 category and he said he would prefer to see a way to make that work better and attract new business into MSF's book of business.

Chair Zanto said he wondered if the fact that new accounts are immediately placed in Tier 5 generates some of the general theory out there that MSF's rates are too high?

Mr. Barry clarified that an account being placed in Tier 5 is based on the data that the new account provides. Tier 5 placement is not automatic; it is based on analytics derived from the provided data.

Chair Zanto called for further questions or discussion from the Board and the public. Seeing none, he called for the vote and the motion passed unanimously.

F. *Additional Ratemaking Decisions – Christy Weikart, Underwriting Service Leader*

Ms. Weikart noted there were a number of additional ratemaking decisions the Board would be addressing.

1. Scheduled Rating

Ms. Weikart explained that the scheduled rating plan is to allow modification of an insured's premium to reflect the characteristics of the risk that are not reflected in its experience. Seven categories are considered when determining any credit or debit and they are: 1) premises, 2) classification peculiarities, 3) medical facilities, 4) safety devices, 5) employees – selection, training, supervision, 6) management – cooperation with insurance carrier and 7) management – safety organization. NCCI has filed a plan in Montana that provides for a maximum modification of plus or minus 25 percent. CSI approves a maximum modification in Montana of 40 percent. As the guaranteed carrier in a competitive market, MSF management recommends a maximum modification of plus or minus 40 percent.

The NCCI plan also contains ranges of modifications by category based on the rate filed plus or minus 25 percent. In order to accommodate the plus or minus 40%, MSF has doubled the level of credit/debit for each category.

Category	Maximum Credit	Maximum Debit
Premises	-20%	+20%
Classification Peculiarities	-20%	+20%
Medical Facilities	-10%	+10%
Safety Devices	-10%	+10%
Employees-Selection, Training, Supervision	-20%	+20%
Management-Cooperation with Insurance Carrier	-10%	+10%
Management-Safety Organization	-10%	+10%

A policy must have $15,000 or more in annual premium at manual rates in order to be eligible for this program. Should the Board approve, MSF will file a maximum modification of plus or minus 40 percent and double the modification by category in accordance with the table.

Ms. Weikart requested that one inclusive motion be proposed unless Board members had specific issues with individual items that needed to be addressed separately.

2. Employer's Liability

Ms. Weikart explained that employer's liability coverage is included on all MSF workers' compensation policies. NCCI publishes many different limits of liability that can be chosen by an employer with specific premium charges and minimum premiums applicable to each set of limits of liability. She said that MSF recommends basic limits continue to be included on all MSF workers' compensation policies for no additional premium or minimum premium. She also recommended that two levels of increased limits of liability be available to be chosen by MSF insureds. She reported that these are the same limits that have been available and have fulfilled the needs of MSF customers for many years.

Bodily Injury by Accident – Each Accident	Bodily Injury by Disease – Each Employee	Bodily Injury by Disease – Policy Limit	Premium Charge based on Manual Premium	Minimum Premium
$100,000	$100,000	$500,000	None	None
$500,000	$500,000	$500,000	0.8%	$75
$1,000,000	$1,000,000	$1,000,000	1.1%	$120

3. Deposit

Ms. Weikart said that NCCI publishes a rule about crediting a deposit premium to the final earned premium or to the renewal policy subject to the approval of the insurance regulatory authority. The rule is not mandatory. MSF's current practice is to keep a deposit premium from year to year with appropriate adjustments. The deposit premium is only applied to an outstanding balance after policy cancellation. This specific issue was included in the MSF transition plan submitted to CSI and if the Board concurs, MSF will file this information with CSI.

4. Short Rate Premium

She said as filed by NCCI, if a policy is cancelled by the insured (except when retiring from the business) the premium for the cancelled policy must be calculated using a "short-rate percentage or short-rate factor". Short Rate Cancellation applies a penalty for cancelling a policy. MSF has never used a short rate cancellation and management does not recommend adopting this usage. Instead, MSF will file with CSI a pro-rata method of cancellation that does not include any penalties.

5. Payroll Versus Per Capita for Domestic Workers

NCCI uses classification codes for domestic workers that base premium on a per capita basis. MSF uses classification code #9015 for domestic workers and bases premium on payroll. MSF's current policyholder system is not capable of basing premium on a per capita basis. This item was also included in MSF's transition plan that was submitted to CSI. CSI granted an exception to MSF to continue use of the payroll-based classification for domestic workers with the stipulation that a new policyholder system must provide for per capita capability for policies issued or renewed on and after July 1, 2019.

6. Volume Discount

MSF provides a volume discount based on the premium size of a policy and recommends no change to the current volume discount program utilized. If the Board concurs, the following Volume Discount will be filed with CSI.

Standard Premium	Discount
$0 - $12,000	0%
$12,001 - $150,000	5%
$150,001 - $750,000	7%
$750,001 & Over	9%

7. Retrospective Rating Plan Factors – Dan Gengler, Internal Actuary

Mr. Gengler continued the presentation and explained that the retrospective rating plan was an option for larger, more sophisticated employers. By mutual agreement, this plan is offered to an insured risk who pays the premium upfront while agreeing to take the risk of later paying more than that amount if losses are high. They also could share in the reward of paying less if losses are low. After the end of the policy period, a look-back at actual losses incurred determines if either a charge or return of premium is warranted. This rating option is attractive to employers that are confident in their ability to control losses. He shared the parameters with the Board and noted that they are applicable to individual policies and group association plans.

Chair Zanto called for questions. There were none and he called for a motion.

Jack Owens moved the Board to adopt management's recommendations for the following additional ratemaking decisions to apply to new and renewal policies effective July 1, 2017 to June 30, 2018, as follows:

- *a. Schedule Rating*
- *b. Employer's Liability*
- *c. Deposit*
- *d. Short Rate Premium*
- *e. Payroll versus Per Capita for Domestic Workers*
- *f. Volume Discount*
- *g. Retrospective Rating*

Ms. VanRiper seconded the motion. Chair Zanto called for further discussion and questions. There were none. He called for the vote and the motion passed unanimously.

III. Actuarial Report – Leslie Vernon, Senior Consulting Actuary – Willis Towers Watson

Mr. Vernon summarized WTW's analysis in support of MSF's management and Board selections of loss cost multipliers for policies incepting from July 1, 2017 to June 30, 2018. 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 to policyholder equity and provision for adverse deviation and indicated loss cost multipliers. Mr. Vernon walked the Board members through the analysis process utilized by the actuaries. He said MSF's indicated loss cost multipliers assume an investment yield on underwriting cash flow of 2.75 percent and management recommended target contribution to equity is 0.0 percent of earned premium again this year.

Chair Zanto called for questions or discussion from the Board and the public; there were none.

IV. Ratemaking Decisions for July 1, 2017 to July 1, 2018 – Laurence Hubbard, President/CEO

A. Rate level Recommendation and Contribution to Equity - Laurence Hubbard, President/CEO

President Hubbard said there are two requirements for the Board and management to consider when setting rates; one is legal and the other is philosophical. Rates set by the Board must not be inadequate, excessive or unfairly discriminatory which is the legal standard enforced by the Insurance Commissioner for all insurance companies. The actuaries have an obligation to ensure that legal principle is met. There is also another principle that requires the Board to establish rates that are no more or less than self-supporting of this organization and its obligations over the decades. The premium rates are MSF's only ability to raise capital. There is also a statute enacted by the legislature that when an expense or cost is uncertain or unknown, the Board is to select a provision that is more than likely to cover the cost other than less than likely. There is an inherent statutory requirement that the Board behave more conservatively to assure there is rate or cost adequacy over time.

He said the philosophical piece enters when you consider that MSF is a significant player in the economy of Montana. MSF's rate level and the actions the Board and management take affect the economy, particularly since MSF carries approximately 60 percent of the workers' compensation insurance market. He noted that since he has been CEO and this management team has been in place their philosophy of recommendations to the Board of Directors provide relative stability in rate setting, avoiding the inevitable peaks and valleys that are going to occur because this industry is cyclic and the actuary science is imperfect. He said management recognizes that policyholders want their rates to be kept as low as possible but rate setting must be done prudently to protect the economic environment.

Chair Zanto called for questions.

Mr. Mihelish noted that HB334 resulted in a 20 percent decrease on 2011 and asked if there was any solid data to date that would prove or disprove that that rate reduction has shown a benefit.

Mr. Hubbard said he believed that the data is beginning to support the 20 percent rate reduction as a positive step, though future court decisions could determine certain provisions are unconstitutional. He said over half of the 20 percent reductions, 12.1 percent, was based on the provisions that called for the termination of medical benefits for most permanent partial cases at five years. HB334 passed in 2011; however, it wasn't until 2016 that MSF began seeing the five year closure date for claims become effective and there is already a court case challenging that provision which. Regardless of the court case challenges, the data is indicating positive trends which are reflected in the analysis that the actuary just completed on the recommended rate actions for this meeting.

Mr. Gengler said the data shows increasingly solid evidence that MSF's losses are coming in consistent with the reductions that were taken; however, it cannot be strongly established that was due to the provisions of HB334. He said other factors such as operational improvements made by MSF or general positive impacts in the environment, such as reduced use of opioid narcotics could also be key contributing factors. He said he believed the reduction of losses is a combination of all those factors. He added that only six months of data is available for claims that can be closed under the five year closure provision; however, very few of those claims are having the medical closures specifically due to that provision. Many of the claims that would have remained opened after 60 months have already closed due to medical settlements, not necessarily the 60 month closure deadline.

President Hubbard said there are three key decisions the Board will need to feel comfortable with: 1) Is a zero percent contribution to equity target for the rate level this year appropriate? 2) Is a 2.75 percent assumed return on underwriting cash flow appropriate given the current economic environment and projecting that well into the future? 3) Is a 2.5 percent provision for adverse deviation appropriate? He explained that steps taken in past years to address adverse development levels and expected increased income on cash flow were key in the development of management's recommendation to the Board to adopt a minus five percent manual rate level change, on average, for MSF customers for the policy year beginning July 1, 2017.

Chair Zanto asked Mr. Gengler to walk the Board members through the recommendations.

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

Mr. Gengler provided an additional perspective on the loss cost multipliers and their components. He explained how the loss cost multipliers were derived and offered clarification regarding the availability of the investment income in MSF's financials and explained how that interplayed with the rates. Mr. Gengler presented the proposed lost cost multipliers based on a five percent rate reduction from current rates. 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% Rate Change

Analysis of LCM Components

	Tier1	Tier2	Tier3	Tier4	Tier5
Loss & LAE	0.754	0.905	1.005	1.206	1.458
Offsets for UW Programs	0.101	0.121	0.135	0.162	0.196
Genl & Acquisition Expense	0.159	0.190	0.211	0.254	0.307
Profit & Contingency	-0.081	-0.098	-0.109	-0.130	-0.157
Loss-Cost Multiplier	**0.932**	**1.119**	**1.243**	**1.492**	**1.802**

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

C. *Adopt Loss Cost Multipliers for new and renewal policies effective July 1, 2017 to July 1, 2018*

Mr. Mihelish moved the Board to adopt loss-cost multipliers as recommended by management to reflect a -5.0% overall change 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, 2017 to July 1, 2018 as follows:

For Tier 1, a loss-cost multiplier of 0.932
For Tier 2, a loss-cost multiplier of 1.119
For Tier 3, a loss-cost multiplier of 1.243
For Tier 4, a loss-cost multiplier of 1.492, and
For Tier 5, a loss-cost multiplier of 1.802.

Mr. Mohr seconded the motion. Chair Zanto called for questions or discussion from the Board.

Ms. VanRiper clarified for the audience that the Board has an opportunity in advance of the Board meeting to review the information and ask questions regarding management's recommendations. She said that it may appear that the Board is not engaged or asking questions; however, the reality is that management provides the information in advance and meets with Board members to answer questions and provide any requested additional information.

Chair Zanto confirmed Ms. VanRiper's comments and stated that it felt good to be able to give a rate reduction. He said he believed this rate reduction sends several messages, one being a rebuttal to the perception that MSF's rates are too high. He said he thinks the five percent rate reduction sends a clear message that MSF is being managed very well and its financial position is such that we are able to take this action. He noted that setting rates appropriately will enable the Board to declare a dividend in the future should the accident year performance prove to be better than expected.

Mr. Mihelish noted that during his Board tenure he thought this was the first time he had participated in a rate reduction which he said was a testament to good management and a strong safety culture growing in the state of Montana as well as the other programs and campaigns MSF has led with.

President Hubbard said that MSF's average rates have decreased about 42 percent since 2007 due to actions the Board has taken as well as the effects of HB334. He noted that manual rates are as low as they were in 1994 despite wage and medical inflation which is a testament to the discipline exhibited by the Board of Directors that have served throughout MSF's existence, recognizing that stability matters to MSF policyholders. At times, these decisions have been difficult, particularly when the Board has had to vote to increase rates.

Chair Zanto called on members of the public to provide any comments or questions. He took a moment to congratulate Mr. Bob Biskupiak on his appointment as Deputy Insurance Commissioner at CSI.

Jeannie Keller, Insurance Services Bureau Chief at CSI commented that she believed MSF moving under regulation by the Insurance Commissioner will further help to dispel claims that MSF's rates are excessive.

Chair Zanto called for additional discussion from the Board and comments from the public. Seeing none, he called for the vote and the motion passed unanimously.

V. Reserve and Financial Reports – Montana State Fund – Mark Barry, VP Corporate Support

A. Loss Reserve Year-End Reconciliation and Calendar Year 2016 Financial Report Update

Mr. Barry reported that MSF had filed its Calendar Year 2016 financial statement with CSI before the deadline of March 1, 2017. He said that submission included a required filing of a statement of actuarial opinion from WTW that certified MSF's loss reserves. He said WTW presented the loss estimates for the first three quarters of 2016 at the December Board meeting and this report covers the final quarter and WTW has provided an addendum to their report. The addendum included their review and changes. He reminded the Board that they had approved the loss reserves as presented; however, that approval was subject to change based on the actual losses as of year-end and adjustments were expected.

He reported that the actual loss reserves reported in the financials increased by $2.8 million driven primarily by paid loss estimates coming in lower than expected by $2.3 million which is a .3 percent change. The payments were lower than expected which causes the loss reserves to be higher. He said that WTW has certified that MSF's loss reserves are reasonable.

Mr. Barry said the balance sheet indicates MSF has policyholder equity of $526 million which was estimated in December to be at $517 million. He said overall admitted assets have not changed appreciably from those reported in December 2015; however, unpaid losses have changed by about $20 million and other liabilities include $75 million of reinsurance held in our aggregate stop loss program. The change is driven primarily by reported premium of $170 million when the initial estimated was $167 million and unrealized gains were about $1 million more than expected.

He provided a comparison of the Annual Business Plan projections and the actual results noting that premium was up by 4.7 percent and losses were lower than plan by $1 million. Total expenses are $1.9 million better than anticipated which results in the business plan underwriting results coming in at $10.3 million better than was planned. With investment income higher than the plan by $6.9 million and other expenses lower than expected by $1 million, net income was higher than planned by $18.5 million.

He then provided an overview of the next steps. He noted that the annual statement had been filed with CSI by the March 1 deadline as required by statute. The statutory audit by Eide Bailly is being finalized and the Legislative Audit Division will be on-site to begin the governmental financial statements audit. He said supplementary information will be filed with CSI on April 1 and the audited statutory financial statements will be filed by June 1.

President Hubbard said that legislators and elected officials often comment on the amount of capital that MSF holds and noted that the income statement clearly indicates that if not for MSF's investment income, MSF would have operated at a loss on operations alone for 2016. He said everyone has experienced the upturn in the markets and investment results have been favorable. He added that it is not the rate levels that are driving the bettered financial results, it is the investment income results.

Chair Zanto noted that the Board has experienced two years of zero contribution to equity. He asked how much control or input the management team had in the investment strategy.

Mr. Barry responded that management meets with the Board of Investments staff quarterly to review investments and options going forward and said management does work with BOI on those strategies.

Mr. Miltenberger offered kudos to the management team on the terrific work they had done. He said this was very good news, but good financial results during a time when the legislature is dealing with funding shortfalls is bad timing; however, if the Board believes it is not prudent to increase policyholder equity, they can address that with a dividend declaration. He then said that management and the Board should not be embarrassed, these results reflect good work and the Board is equipped to take the right action at the right time to address any concerns.

Mr. Barry clarified that though the investment income is driving these results, he noted that Julie Jenkinson, Vice President, Operations deserved credit for changes she has implemented to claim management focus that have also added positive results.

Mr. Mihelish said it is very common in the insurance industry for investment income to drive the positive results seen on financial statements. Though it may appear MSF is cutting edge with this approach, he assured the Board it was not and that most carriers depend on investment income.

Chair Zanto called for questions or comments from the Board; there were none. He called for public comment; there was none.

VI. Public Meeting on Calendar Year 2016 Annual Business Plan

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

Ms. Copps presented the summary of the results of the Calendar Year 2016 business plan, beginning with a report of the Key Success Measures (KSM) depicted below.

Key Success Measures

KSM	CY16 Plan	CY16 Result
Net Earned Premium	$162.0M	$169.7M
Fiscal Year Loss Ratio	78.6%	74.4%
Expense Ratio	28.6%	26.4%
Investment Income	$44.1M	$51.0M
Net Operating Income (before dividend)	$27.3M	$45.8M

Ms. Copps said net earned premium was $7.7 million over target due mainly to wage growth on payroll that was above the estimated target. Net operating income was targeted at $27.3 million before dividend and achieved 45.8 million; the major drivers of the increase were the increased $7 million in investment and $8 million more in premium than planned.

Chair Zanto called for questions; there were none.

She provided a review of the Enterprise-Wide Initiatives which were focused in two main areas: 1) Customer Service and 2) Infrastructure. Customer Service includes a Policy and Billing System Replacement project that has been partially met and is multi-year. Phase one sought to engage the stakeholders to produce high level requirements and establish an estimated schedule and budget based on improved understanding of the regulatory environment and other relevant system decisions. This project was delayed two months to allow for other project completion and to accommodate the policy renewal timeframe. The Infrastructure project is a multi-year coordination effort with the Insurance Commissioner to lay the groundwork for implementing regulation of MSF. This project includes Regulation, Calendar Year Conversion, Rates and Rate Filing and Change Management and Communication. Ms. Copps provided a review of the projects and noted that all Infrastructure Projects have been completed.

Chair Zanto called for questions; there were none.

VII. Miscellaneous – Laurence Hubbard, President/CEO

A. Miscellaneous (Legislative Update

President Hubbard provided a brief update on the progression of the 2017 Legislative Session and invited Kevin Braun, General Counsel to address the Board on any bills he thought the Board may be interested in.

Mr. Braun mentioned the presumptive illness legislation for fire fighters had passed the Senate and was heard in the House Business and Labor Committee earlier in the week. He confirmed with Pat Murdo, legislative staff for that committee, that no executive action had yet been taken.

Mr. Hubbard noted that presumptive illness for fire fighters is an issue nationally as well and there has been proposed legislation during a number of legislative sessions. He said the proposed legislation this session seeks to provide the funding through the fire tax.

President Hubbard addressed the Board regarding proposed legislation that has not yet been introduced. The bill is currently LC144, once introduced it will have a bill number. He said this bill will have significant consequences to the businesses of Montana, MSF and MSF employees and for those reasons, he sought the guidance of the Board for handling this legislation. He said because this bill directly affects how MSF functions and if it functions, it is important that the Board take a position. He said the copy of the proposed language that he currently has may not be what the final bill reflects. He said Senator Moore from Miles City will be introducing the bill and the essence of this legislation it to eliminate Montana State Fund as a Plan 3 insurer and the guaranteed market for Montana. He commented that the "Whereas" statements at the beginning of the bill did not fairly represent the nature of MSF in the past or as it exists today. MSF has served as the market of last resort for employers in Montana since 1915. He shared the varied approaches that were taken to address concerns and issues throughout the years.

He said in the late 80s when MSF was an arm of DOLI, the workers' compensation system was in a financial crisis due to inadequate rates. Legislators, during the 1989 legislative session, created the State Compensation Mutual Insurance Fund as a domestic mutual company. A Board of Directors was appointed to the mutualized company and it was to be regulated by the Insurance Department and function like an insurance company. The first Board of Directors realized that the new state fund was grossly under-capitalized because rates were extremely inadequate so there were not enough assets to support the liabilities. The first Board of Directors was faced with an immediate and substantial rate increase on policyholders in excess of double digits and was considering issuing bonds to fund liabilities and to manage the capitalization requirements of insurance department commissioner. Both options were politically untenable so the Legislature held a special session in May, 1990 and created the current State Fund with a separation of the unfunded liabilities of the Old Fund from the State Fund. At that time, they withdrew the "mutual" status of State Fund and restored it as a public, independent corporation and provided for more legislative oversite thereafter.

President Hubbard said that is the point when Montana State Fund began in its current form, January 1, 1990 for all liabilities that were incurred after July 1, 1990. Montana State Fund has tried to rebuild its capital and tried to maintain the financial strength necessary to not be a burden on the taxpayers in the future like the Old Fund liabilities. This ensured that MSF served as a ready and competitive market for Montana businesses so that they could get the lowest reasonable rates that they possibly could. Most importantly, it was run like a domestic mutual insurance company and not as a state agency, which is exactly what the law requires the Board of Directors to do. He said there has been criticism of MSF's assets and equity levels established by the Board, which he believes is a direct cause of legislation like LC144. He said MSF has served, and continues to serve, an important public role.

He then outlined the nature of the bill which would eliminate MSF as a plan three insurer. A residual market mechanism would be established and all of MSF's 26,000 policies would be redistributed, with the help of the DOLI, to the remaining carriers that are writing insurance in Montana. The assumption is that there will be plenty of carriers in the voluntary market lined up to write the business that would no longer be provided by MSF. The assigned risk pool which operates in other states, would be placed in the DOLI for regulation which is highly unusual. Typically the residual market is administered by the insurance departments. He said he believed LC144 is written this way because the original bill in 1989 that mutualized MSF had placed the oversite of the residual market in DOLI. At that time, the system was quite different than it is now. This draft bill also states that if a Plan Two insurer refuses to cover an account, the insurance commissioners may revoke its license. All of MSF's current claims would be transferred to DOLI for run off and the $900 million worth of liabilities would be handled for many decades in the future. The assets of MSF would be converted into two trusts, Trust A and Trust B. Trust A would consist of all currently booked actuarially established reserves plus 20 percent more and would be for payment of claims. Half the remaining surplus would go to the General Fund, approximately $250 million and the rest would be placed in Trust B which would then be available to feed Trust A just in case there were not enough. The interest earnings off Trust B would be subject to disposition as the legislature chooses. This bill is effective on passage and approval which means as soon as the governor signs this bill or it is enrolled, MSF ceases to exist.

MSF management is taking a strong position in opposing this despite the uncertainty of the final bill draft language. He said there are a lot of employees at MSF who are doing a good service to the people of Montana who are aware of the service level that exists at MSF. He noted that the Montana Public Employees Association (MPEA) represent 3/4 of MSF employees and he asked that Quinton Nyman's letter be attached to the record.

He provided a summary of Mr. Nyman's letter is that the MPEA, on behalf of its membership, will unequivocally oppose LC144 as it is in current concept and any privatization efforts toward MSF. He read one passage "Privatization through LC144 or any future proposed legislation would have nothing less than a detrimental effect on all involved." Mr. Nyman has requested the support of the Board of Directors and commitment to opposing this and any other privatization measures on behalf of the members of the MPEA.

President Hubbard asked for a discussion and guidance from the Board of Directors and indicated that he hoped the Board would chose to unequivocally oppose LC144 and authorize management to take all necessary measures to oppose.

Chair Zanto called for discussion on this issue.

Mr. Mihelish asked what was the underlying motive for this bill? He asked if it was a money raiser for the state coffers or are private carriers thinking there is unfair competition?

Mr. Miltenberger said that on an unsolicited basis, he received a phone call from a friend, John Metropolis, who is an attorney and a lobbyist. Mr. Metropolis requested a meeting six weeks ago. Mr. Miltenberger said he met with Mr. Metropolis and another lobbyist who explained the essence of this bill to Mr. Miltenberger. At that time, they mentioned to Mr. Miltenberger as well as others including the Board of the Montana Chamber of Commerce, that all of the lobbyists working for the passage of this bill have been retained by Victory Insurance. He said a private insurance company has hired lobbyists to eliminate State Fund and he said, one can imagine that they have a selfish interest at heart. He said, at the same time, knowing the owner of Victory, he probably has mixed motivations and genuinely believes that this will invite a lot of competition into the market and believes that there are a number of insurance companies who are just standing on the sidelines afraid to sneak into Montana because MSF is so powerful. He said their take is that this will help the consumers and employers because more competition will come in to take MSF's place. He said he has been advising insurance trusts that are not insurance companies for a lot of years and it has been encouraging to him to see three different trusts that he has advised vote themselves out of business because they realized that their usefulness was over and under the Affordable Care Act, they could not add value to their members anymore. Rather than cling onto the organization just for self-preservation, they voted to disband themselves. He said the Board members of MSF should be open to the idea, if convinced that this was in the best interest of the policyholders and employees that they ought to be willing to say "for the greater good" the Board will encourage the effort of the legislature to dissolve State Fund. He said that being said, he was convinced that this approach was an absolutely horrible idea. He said there are 400 registered insurance companies with 200 writing workers' compensation insurance in Montana and at least a dozen very actively writing business, getting the business they want right now. The employers that have their business with State Fund do not have the attractive experience that other companies want to write. He said most policyholders are here because MSF provides a good product and a good price. MSF's current clients have a choice today and they chose to be with MSF. He said removing MSF's policyholder surplus from the Montana marketplace will simply end up causing higher prices for the smaller accounts and less options for everybody. As bad as it might be the next two or three years, he said the real problem is the next hard market. The next time there is scarcity and overseas insurance producers decide to pull out of the U.S. market, there "will be a huge sucking sound of capital out of the workers' comp market" and prices will rise which will hit the little states and the rural areas the worst. At that point, there will be small employers who simply cannot get coverage despite the residual market or will end up with very, very high rates.

Mr. Miltenberger said he thought this was a terrible piece of legislation and for the benefit of MSF's policyholders, he said he thought the Board should oppose it. He added that MSF had great employees who do a good job and this should be opposed for them as well.

Mr. Mihelish said Mr. Miltenberger covered everything that he was thinking and added "If the wheel ain't broke, don't fix it." And he said the wheel ain't broke. He said he could see this discussion occurring in 1989 but not now.

Mr. Mohr said upon review of this bill draft, he tried to determine the benefit this bill would have for the State of Montana, MSF's policyholders and injured workers and could see none. He added that he believed this would be devastating to the almost 300 employees of MSF. He said he believed the Board's job is to protect the policyholders, our injured workers in the State of Montana, and the MSF employees and therefore urged the Board to stand in opposition to this bill. He said he did not know if MSF employees were on the minds of the people making decisions on Capitol Hill but they are on the minds of the Board and the Board needs to protect them.

Ms. VanRiper said she was initially leaning in the direction to oppose; however, she generally prefers to not take a position until she has heard from both sides. She said she assumed there was no one at the meeting that could provide the input regarding why this would be such a great deal for policyholders and if at a later date someone is able to provide that information, she would be willing to reconsider. Barring that additional input, she said she was in full support of opposing this legislation.

Ms. Moss thanked Mr. Miltenberger for his comments. She said she had heard inklings of this for a while and views LC144 as a very hostile, adversarial piece of legislation. She said good policy happens when you bring stakeholders together and develop consensus to assure you are recognizing all of the different perspectives and LC144 does none of that. As a Board member, she said she does not support this in any form whether it is amended or not and she cautioned members of any amendments.

Mr. Owens commented that the legislature seems a little confused. He noted it was difficult to say if a lot of these legislators were there at the time the New Fund was created. He questioned how legislators could establish State Fund, hire the excellent employees that work here and then just abolish it and start over. He said he agreed with Mr. Mihelish's point that if it's not broke, don't fix it.

Mr. Mihelish added that this Board of Directors does not serve as a Board to pad its pockets. He said they are here basically as volunteers who receive travel expenses. He noted that the Board members do take on this job because they care about Montana and the employers of Montana as well as the employees of MSF.

Ms. Moss also added that as Board members they are serving in a voluntary capacity; however, Board members have a fiduciary responsibility to MSF.

Chair Zanto said that he has spent a lot of time reviewing this bill draft language and outlined his concerns. He said when he first received the language, he told management that the Board needed to be addressed regarding this bill and the Board would need to take a formal position to support management's opposition to this bill. He determined early on that it would be important for the Board to send a strong message regarding this proposal and was pleased to hear that all of the Board members were supportive of management's recommendation to oppose. He said this bill does nothing to protect the guaranteed market nor does it maintain a stabilized market in Montana. He said he felt it adversely affects employers, MSF employees and injured workers who upon passage of this bill would then be wondering "now what?" He added that the Board has a responsibility to properly and efficiently manage the policyholder dollars that are paid to MSF for the very purpose of administering this workers' compensation insurance company as well as taking care of the MSF employees. He said the position to oppose has the support of MPEA and he has spoken to other union representatives that also support opposition.

He added that there have been discussions regarding the potential of forming a domestic mutual insurance company out of MSF and talk that President Hubbard is pushing for that, which he is not. Chair Zanto stressed that point. He said there will definitely be a lot more discussion around all of the opinions and positions currently being addressed. He said he foresees a lot of effort coming forward in opposition simply because it is not a good bill and it seems very similar to deregulation. He concluded his comments by stating that he strongly opposed this proposed legislation as it exists and assured the Board that this opposition position will be carried forward.

B. *Legislative Proposal(s) Regarding Montana State Fund*

President Hubbard asked that the Board address adopt a formal position to direct Management and staff regarding the LC144.

Chair Zanto made a motion that the Board approve taking a formal position in opposition to LC144 before the Montana Legislature and to direct President Hubbard to engage efforts to oppose LC144 until the bill either dies or is amended to a form that is not detrimental to the Montana State Fund, its policyholders, its injured workers or its employees. Mr. Mohr seconded the motion. Chair Zanto called for further discussion.

Mr. Miltenberger commented that mutualizing the company had been mentioned as well as the origin of MSF as a mutual and wanted to touch on that stream of thought. He also added that Mr. Mihelish said if something is not broken, don't fix it. He said he believes that what is being dealt with today is a broken system. He said it is broken when a private entrepreneur can hire a lobbyist to put 300 people in Helena out of work. When a private entrepreneur, for mixed emotions, mixed reasons, can come after this fine organization and dangle an incentive in the form of policyholder money in front of the state, I think that is a broken system. I would like to see the motion amended so that somewhere near the tail end we include language along the lines of "and to request management to provide information to legislators and the governor's staff regarding the advantages and costs of converting Montana State Fund to an independent mutual insurance company." With the goal of establishing that MSF does work well, the system is not broken, just vulnerable to the legislature looking towards MSF as a piggy bank in a bad year. When it's a good year for MSF it makes MSF look that much more tempting for the legislature; however this is policyholder money and one way to stop the threats of taking it, is to convert MSF so that it is owned by the policyholders. He said it could be redesigned, theoretically, in a way that could keep MSF from being sold off and still remain the market of choice in Montana, remaining in Montana.

President Hubbard, in the spirit of full transparency, said that the subject of mutualizing has come up in several studies since 1989. We have represented the importance of the current role MSF serves as well as the efficiency and effectiveness of having an independent non-profit public corporation. MSF currently does not pay premium tax or have the other expenses that private insurers have which inures to the benefit of MSF policyholders in the form of lowest possible rates. He stressed that the current model is not the only way a state fund can serve the Montana market. Mutualizing has been successful for other states while helping to protect policyholders, workers and employees. He said he agreed with Mr. Miltenberger to not close the doors on an idea that would meet those three strategic goals.

He added that for any bills to mutualize MSF that may be proposed this legislative session, management would support the process without committing the Board inappropriately. Should something else come up, a special Board meeting would have to be called. President Hubbard added that to be clear, MSF converting to a mutual would cause increased costs: there would be premium taxes, Federal income taxes, bad-faith punitive damages in courts and the cost of separating from the Public Employees Retirement System (PERS) would take time and carry a hefty price tag. He said that during the last study session, HJ25 did address the issue of mutualizing MSF and PERS advised the Board and the study committee that it would cost $102 million to fully fund the retirement obligation. He said he supported Mr. Miltenberger's amendment because there are other discussion items that could arise that may serve the three key interests; employers, injured workers and MSF employees.

Mr. Moss said that she respectfully disagreed with President Hubbard and Mr. Miltenberger. She said she felt LC144 was so poorly drafted that she would be very wary of any type of amendment. She added that she is very cautious about mutualizing because of the changes it would mean for the policyholders. As a Board, she felt they should direct staff to research and review mutualizing and provide more detailed information to the Board. She also cautioned about backing complex legislation so late in the session because of the unintended consequences caused by things getting missed. She said she would prefer to just support the opposition of LC144 without the amendment.

Mr. Miltenberger thanked Ms. Moss and President Hubbard for their comments. He clarified that his suggested language was to request management to provide information to legislators regarding the advantages and costs of converting MSF to a mutual insurance company. He said he believed this would be best suited for an interim committee; however, not attached to LC144. He also addressed the issue of MSF pulling out of the PERS system and suggested it could be possible for the state to loan or lease the employees to the new independent company. Management staff could be fully assigned to the new company and the rank and file employees could remain as state employees which would eliminate the termination costs. That would also allow the Board and management to honor people, like Quint Nyman who has stuck his neck out here to support MSF in this effort.

Chair Zanto said that he approached the question of addressing only LC144 in his motion. He said he does not intend to shut the door to other potential alternatives should they be presented in the future. He encouraged the Board to make their message clear on LC144 and address a mutualization bill when and if that occurs. He said if one does arise, he will call a special Board meeting to address that issue at that time and asked the Board to take action that provides a clear stance on the opposition of LC144.

Mr. Mihelish agreed with Chair Zanto and Ms. Moss and reiterated that he believed the Board should issue a focused message to oppose LC144.

Ms. Van Riper said she generally agreed with the last line of thought; however, did not see any issue with adding language that would support working on a study in the future. She then asked if there was a policy regarding state agencies taking positions on bills. She clarified that she recalled either a statutory or regulatory prohibition on state agencies taking positions and that they could only provide informational testimony.

President Hubbard stated that there is no statutory prohibition on state agencies. He also added that MSF, as an independent public corporation, has the full authority as if a domestic mutual to take a position on proposed legislation. There is no statute that precludes a public agency from taking a position; however it could be gubernatorial policy in instructions from the administration to the various agencies attached to the administration, but there is not law. He asked for confirmation of that from General Counsel, Kevin Braun.

Mr. Braun said President Hubbard was correct. With regard to MSF there are no prohibitions against, statutorily or otherwise, MSF taking a position on legislation. He said when you are dealing directly with the state government agencies, there is a statute that declares the Governor the chief policymaking officer of the state so he can direct his various departments to take the position of his choosing. The departments do not have their own independent authority.

Chair Zanto called for further discussion on a proposed amendment regarding mutualziation.

Mr. Mohr expressed concern regarding the mutualization language because of the speed of this proposed legislation that liquidates MSF and then taking into consideration how mutualization would affect our policyholders and our employees at MSF. He said he supports the language as presented by Chair Zanto's original motion.

President Hubbard said the motion does not have to be perfectly drafted because the intent that he is hearing from the Board is to take a very focused position on LC144 or its progeny. He said he agreed with Ms. Moss that LC144 is not fixable. He reiterated that just opposing LC144 is sufficient guidance for management.

Mr. Mihelish stated that if the mutualization addendum were added, that would indicate that there is a second position MSF is willing to take and he does not believe there should be that negotiation at this point.

Chair Zanto asked Mr. Miltenberger if he wanted to propose a formal amendment to the motion. His amendment did not received a second so was not yet open to a vote.

Mr. Miltenberger said he did want to make a formal amendment and still does; however, after listening to the comments from other Board members did not feel the need to "go down in flames" so opted not to proceed.

Chair Zanto called for a second to Mr. Miltenberger's motion. There was no second. Chair Zanto called for further comments from the Board; hearing none, he called for comments from the public. There were no comments and he called for the vote; the motion passed unanimously.

Chair Zanto said this bill would continue to be watched as it progresses and Board members will be kept informed. If something else arises, the Board will be called to action.

C. *Renewal of Compensation Consultant Service Contract*

Chair Zanto asked Rick Duane, Vice President, Human Resources to explain the renewal request for the Compensation Consultant Service Contract for the Board's review of President Hubbard's performance. Mr. Duane explained that the contract for the Compensation Consultant to the Board of Directors must be extended in order to secure those services for the President/CEO performance review and compensation consideration in June, 2017. This proposal will extend the contract to the end of 2017 with no change in scope or fees. He provided some background information about the process to date and noted that the Board has decided to defer the compensation review until June, 2017. That delay requires an extension of the contract and he asked Board members to support that position.

Chair Zanto called for questions or discussion, then called for a motion.

Chair Zanto made a motion to approve the Amendment to the Contract for Compensation Consultant Services with Kenning Consulting as presented by management. Mr. Miltenberger seconded the motion. Chair Zanto called for questions or discussion from the Board and the public. Seeing none, he called for the vote and the motion passed unanimously.

D. *Actuarial Services*

President Hubbard noted that from time to time it is prudent for the Board of Directors to issue a call for actuarial services though the services from Willis Towers Watson have been wonderful. He asked Mr. Barry when the contract expires.

Mr. Barry explained that the current contract has been extended two years over the original seven year contract because MSF has a statutory exemption for actuary services when applying the seven year standard. He said the Board has been extending the contract as necessary.

President Hubbard stated that MSF must have a Request for Proposal (RFP) for actuary consulting services and would certainly encourage WTW to respond. This action will authorize management to proceed with an RFP for a competitive process for actuarial services before the expiration of the current contract.

Chair Zanto called for a motion

Mr. Owens made a motion the Board direct management to proceed with a Request for Proposal for Actuarial Services. Mr. Mihelish seconded the motion. Chair Zanto called for questions. There were none and he called for the vote. The motion passed unanimously.

Chair Zanto asked for any volunteers from the Board to serve on the selection committee. Mr. Miltenberger and Mr. Mihelish volunteered to serve. Chair Zanto reminded the Board that he had volunteered to serve on the pharmacy benefit manager RFP.

E. *Report of Internal Auditor – Patti Grosfield, Internal Auditor*

Ms. Grosfield reported that she recently completed the audit of the agency incentive plan that was calculated for accident year ending June 30, 2016. She explained that the agencies earn the incentive payments based on profitability or containment of losses and retention of book of business. The incentive table provides for payouts in a range of .1 percent up to 4.3 percent of the agencies earned premiums. The program is designed to reward supporting agencies for their overall superior results. She provided summary data and stated that almost $1.6 million was paid out with 16 out of 28 agencies receiving payments. The largest incentive earned was $867,343 and the smallest was $2,205. The overall payout target was 1.25 percent and the actual achieved was 1.26 percent. The profitability percent achieved was .96 percent versus target of 1.0 percent and the retention multiplier came in slightly higher at 1.3 percent versus targeted 1.25 percent.

Other internal audits recently completed included:

- The MSF Code of Conduct update was completed in January 2017. She said she works with HR to assure adherence to state laws and ethical considerations for MSF employees. This policy governs ethical conduct and discusses identifying and mitigating any potential ethical conflicts of interest. It also discusses appropriate versus inappropriate gifting situations from vendors and injured employees. This form also contains a whistleblower protection and no-retaliation provision and is reviewed and signed annually by all MSF employees. Any potential conflicts that are disclosed are investigated and addressed.

- The Data Confidentiality and Acceptable Use Policy was also reviewed and issued to employees. This policy reviews how MSF protects its data and how data requests from internal or outside sources are addressed. This policy also details acceptable use of MSF's computer systems and other electronic equipment.

- The Excess Leave Payouts were reviewed for accuracy. This policy keeps ultimate payouts down to the current level rather than paying out later at a higher level and disallows unlimited accruals of leave. The personal leave policy pays leave time exceeding two times the annual accrual. This year, 40 employees received payouts for a total of $161,414.

- Banked Holiday excess payout policy pays excess over 80 hours accrued of Banked Holiday time. This year, two employees received payouts for a total of $6,269.

She said she is currently in the process of auditing the performance based compensation adjustments which is an annual process in which employees are rated based on their achievement of predetermined goals. The pay adjustments are correspondingly earned based on the employee's performance. Ms. Grosfield said there are continual on-going and various internal controls reviewed daily and the top risks identified in Enterprises Risk Management are reviewed and the controls verified for the major risks.

She said externally:

- Staff has just completed the review of the draft reports from the CY16 statutory financial statement audit, Eide Bailly is finalizing the audit and copies of the final report will be distributed shortly. The audit will be presented at the June Board meeting and a request for approval will be sought then. She said MSF is expecting a clean unmodified audit opinion with no recommendations, no significant deficiencies and no material weaknesses noted.

- Fieldwork on the CY16 GASB (governmental) financial statements audit will begin on-site on Monday, March 13 and typically takes four to five weeks. There will be more information available at the June meeting.

- The final report on the current pharmacy benefit manager, Express Scripts, Inc. (ESI) was received the week of March 6, 2017 and staff is in the process of reviewing and drafting comments. She said the audit firm hired is Donn and Company and they presented a report of their initial findings in November 2016. After review and discussion by staff, MSF instructed Donn and Company to address all findings with ESI to sort through potential discrepancies and provide a finalized audit report and findings to MSF. The audit scope included the review of adherence with the comprehensive list of pricings, operational requirements, the itemized lists of program components, drug pricing, duplicate billings, formulary, preferred drug lists and other prior authorizations, edits, eligibility, early refills, step therapy, out-of-pocket reimbursements, Lockhart Liens and performance guarantees. Following the exchange of questions and responses, Donn and Company indicated that "Overall this audit process has confirmed a small number of isolated issues and no systematic or substantial overcharges or deviations from contractual terms." MSF's spend on pharmacy is over $8 million and the largest potential overcharge would be under $26,000. There were also program enhancement suggestions that MSF is considering going forward with the RFP for a pharmacy benefit manager.

Chair Zanto called for questions. There were none.

F. *Budget Variance Reports as of December 31, 2016 – Rene Martello, Controller*

Ms. Martello covered the budget variance report for MSF's first calendar year which was year 2016. The net earned premium had already been covered and had come in at $7.7 million over planned. Total MSF expenditures saw operational expenditures under budget by $3 million and claim benefit payments under by $5.8 million.

She provided information on expenditures compared to net earned premium and explained that payroll growth has continued to keep the premium level even and the increase in benefits displayed in her graph were a result of increased settlement activity. She said that 2017 saw an increase in both operational and benefit expenditures due to project work experienced on the operational expenditures and continued increased settlement activity. The expense ratio for 2017 is at 32.4 percent but was 30 percent for 2016. She said settlements are beginning to level out or remain more consistent and medical payments patterns are showing more of a variance. She said other states coverage expenditures also were lower than planned by $500,000. Operational expenses were under budget by $3 million primarily due to personal services and operating expenses coming in better than expected. She provided an overview of some of the larger operating expense variances such as the need for outside janitorial services, software licenses needed for the imaging system and a cost resulting from an audit done by Oracle and Adobe of the State Agency licensing contracts. She mentioned that the largest under-budget items were the Annual Business Plan and ESPM projects which were budgeted in anticipation of requiring consulting services to meet the requirements of moving under regulation; however, staff was able to complete the majority of this work on their own. She provided reports highlighting the below budget variances and explained the causes and reasons for the savings.

Chair Zanto called for questions; there were none.

Ms. Martello provided a budget variance review of the Old Fund. She noted that the Old Fund reports will remain on a fiscal year basis and this report was for the second quarter of the 2017 fiscal year. The funding for the Old Fund will continue to come from the General Fund. She said the Old Fund funding estimate was $9.8 million and the current projection is expected to come in at $9.5 million or $380,000 under. Benefit payments were estimated at $8.7 million and the current projection is expected to come in at $8.3 million due to less than expected in claim benefit payments, medical payments and medical settlements. She said the Old Fund seems to be performing as expected and management is not expecting to have to come to the Board to request a funding increase. She reported that there were 671 claims open at December 31, 2016 compared to the end of 2015 which had 724.

Chair Zanto called for questions; there were none.

VIII. Old Business/New Business

Chair Zanto called for old or new business. He said he missed his opportunity to ask if the formulary bill was still alive and asked Mr. Braun if he could provide some information on that.

Mr. Braun said the bill is still alive and is scheduled in the second chamber in the Business and Labor Committee for a hearing on March 21.

Chair Zanto explained that the Labor Management Advisory Council (LMAC), an advisory council developed by the Commissioner of DOLI on which both Chair Zanto and Mr. Braun serve, had requested a formulary drug management system into the workers' compensation arena in Montana. He said a formulary is a schedule of medications that are approved to be prescribed by a carrier. This is common practice in the healthcare industry; however, is just beginning to be used more in workers' compensation.

Mr. Mihelish asked what the Old Fund liability currently was?

President Hubbard said that as of June 30, 2016 the total was $38 million.

Mr. Mihelish said he has been using $50 million so he was a little over.

President Hubbard said that $38 million is the actuary's central estimate and there are also high and low estimates. The actuaries have opined that ultimate liabilities could be as low as $20 million and as high as $80 million.

Chair Zanto called for additional old or new business. There was none.

IX. Public Comment

Chair Zanto called for public comment. There was none.

Mr. Braun congratulated Mr. Mohr, Mr. Owens and Ms. VanRiper on being confirmed by the Senate the previous week.

The meeting was adjourned at 2:34 p.m. The next regularly scheduled Board meeting will be held on Friday, June 9, 2017 at Montana State Fund, 855 Front Street, Helena, Montana.

Respectfully submitted,

Verna Boucher
Special Assistant to the President/CEO