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MONTANA STATE FUND
SPECIAL BOARD OF DIRECTORS MEETING
March 21, 2017

The Montana State Fund (MSF) Board of Directors special meeting was held March 21, 2017 in Montana State Fund's Board Room at 855 Front Street, Helena, Montana 59601.

Directors Attending

Lance Zanto, Chair, Helena
Bruce Mihelish, Lolo
Jan VanRiper, Helena
Richard Miltenberger, Helena
Lynda Moss, Billings (by telephone)
Jack Owens, Missoula (by telephone)

State Fund Staff Attending

Laurence Hubbard, President/CEO
Verna Boucher, Special Asst to Pres/CEO
Kevin Braun, General Counsel
Mark Barry, Corporate Support VP
Julie Jenkinson, Ops Vice President
Al Parisian, CIO
Rick Duane, HR Vice President
Sam Heigh, Ops Support Vice President
Dan Gengler, Internal Actuary
Curt Larsen, Assistant General Counsel
Mary Boyle, Communications Specialist
Peter Strauss, Compliance Officer
Erika Ayers, IT Enterprise Apps Director
Sandy Leyva, Select Team Leader

Others Attending

Bob Biskupiak, SAO
Kerri Emmons, IAIA
Nancy Butler, SAO
Russ Ehman, SAO
Don Judge, MTLA/LMAC
Quinton Nyman, MPEA
Sonia Powell, OBPP
Kelly Taft, Metropoulos Law Firm
Bruce Hockman, Pinehurst Strategic Partners (telephonically)

I. Meeting Preliminaries

A. Call to Order

Chair Zanto called the meeting to order at 1:33 pm. He thanked those present for taking the time to attend and explained that this special Board Meeting was called to discuss LC993. He noted that two Board members were participating by phone: Jack Owens and Lynda Moss. He read the names of the entries from the sign-in sheet so Board members participating by phone would know who was in attendance. He also notified attendees that Bruce Hockman was participating telephonically as well and invited President Hubbard to provide an introduction.

President Hubbard explained that Mr. Hockman of Pinehurst Strategic Partners will be providing MSF some consultative support. He was a principal at JLT Re prior to Pinehurst and had been invited to listen in to the discussion and provide some insight and advice on the dimensions of these proposals. He told the Board Mr. Hockman was available for questions and has experience as a regulator for the Pennsylvania Department of Insurance and many years of experience in the insurance industry with an emphasis in workers' compensation insurance.

II. Legislation – Laurence Hubbard, President/CEO

A. Discussion Regarding Legislation (LC993) vs. Convert MSF to a Mutual Insurer

Mr. Hubbard noted this meeting contained one agenda item; to discuss and determine the Board's position on LC993. He explained that LC993 was a legislative draft requested by Senator Fred Thomas who asked for assistance from MSF staff in preparing the draft language. Kevin Braun, General Counsel; Mark Barry, Chief Financial Officer; and President Hubbard, as well as other staff assisted in preparation of this bill. Jameson Walker, Attorney with the Legislative Services Division, drafted the final version of LC993. This is an alternative to LC144 which the Board has already adopted a position to oppose. He said neither bill had actually been introduced so the language that was received from the sponsors and was supplied to Board members may change which could result in another special Board meeting.

President Hubbard explained that LC993 intends to convert MSF to a domestic mutual insurance company by December 2019. The bill calls for the Board and management to develop a transition plan by January 2018 with certain requirements. Importantly; MSF, as the mutual company, would continue to serve as the guaranteed market for Montana businesses. He explained that other states have proposed and created similar mutual insurers; most prominently the state of Maine in 1993. Maine Employers Mutual was created as a domestic mutual insurer, subject to all the laws and regulations of an insurance company, yet remaining the guaranteed market. This model has worked very successfully and has expanded into workers' compensation insurance subsidiaries into other New England states. LC993 attempts to move Montana in the direction of that model. He noted there are exemptions in current Montana insurance laws, specifically because MSF is the guaranteed market and regulated under Title 33 by the Insurance Commissioner. LC993 calls for MSF to become like a private insurance company which would subject it to premium taxes, Federal and state income taxes, as well as punitive damages and bad faith lawsuits. He said that since the legislature would be converting MSF to a domestic mutual, the standard formation requirements in Title 33 would not be applicable and that exception is included in the LC993 language. Current language, due to MSF's position as the guaranteed market, denies CSI the ability to suspend or revoke MSF's certificate of authority to do business and that provision would continue to apply. MSF would also not be required to participate in the guarantee association. He said much of MSF's current structure and regulatory framework would continue to exist for the domestic mutual. He added that payment of premium tax would become effective January 1, 2018 and would be earmarked and dedicated for payment of the liabilities in the Old Fund. The general fund currently receives about $100 million per year of premium tax from all lines of insurance, not just workers' compensation. He noted that the legislature could pass legislation now that would earmark collected premium tax to pay the Old Fund liabilities; however, they have not taken that position to date.

President Hubbard outlined the essential features of LC993 that would remain the same and those that would change. He said that since MSF was originally created by statute, under this bill, MSF would need to be created under the domestic mutual laws and would become a private entity. MSF's assets would be held in trust under 39-71-2316, 2320 and 2322 for payment of obligations and administration of expenses of all liabilities incurred by MSF post July 1, 1990. The policyholders would become the owners of the company; and, as a domestic mutual, the successor company could file to write other lines of insurance, not just workers' compensation. The successor company would be regulated by the Insurance Commissioner as MSF is now and would continue to be subject to financial and market conduct examinations. Currently, MSF's Board of Directors are appointed by the Governor and confirmed by the Senate and the Board then hires the President. Under a domestic mutual structure, the policyholders would elect a Board of Directors who would then appoint management. MSF employees participate in the Public Employee Retirement System (PERS) but would not be eligible to continue in that program if MSF becomes a domestic mutual which would necessitate a transition plan for current and new employees. Medical coverage for employees, treasury functions and other services currently provided by the State of Montana would have to be secured by other services or brought in house. He said this is perhaps the most complicated aspect of conversion of MSF to a domestic mutual.

Mr. Hubbard illustrated the practices that are current and would remain if MSF were to become a domestic mutual, such as: rates would continue to be filed with CSI and would be:

- Subject to approval or rejection by the insurance department if the rates are inadequate, excessive or unfairly discriminatory,
- Annual statements completed according to statutory accounting principles would continue to be filed with NAIC,
- Declaration of dividends payable to policyholders would also continue,
- Services for fraud detection and prosecution is currently administered for MSF by the Department of Justice; however that would no longer apply should MSF become a domestic mutual,
- The domestic mutual would no longer be subject to legislative audits; and
- MSF is not a member of the guaranteed fund in the event of insolvency and would not become a member as a domestic mutual as long as it continued to serve as the guaranteed market.

Chair Zanto called for a motion which he hoped would encourage Board discussion on LC993 in its current form.

Jan VanRiper moved the Board approve taking a formal position in opposition to LC993 before the Montana Legislature and to direct President Hubbard to engage lobbying efforts in opposition to LC993. Chair Zanto called for a second; there was not a second and the motion failed.

Chair Zanto moved the Board approve taking no position on LC993 and to direct President Hubbard to engage lobbying efforts to provide informational testimony on LC993 before the Legislature. Bruce Mihelish seconded the motion.

Chair Zanto called for discussion.

Ms. Van Riper stated that she was not opposed to the motion but did have a worry. She said that just as President Trump realized that the health insurance market is complicated, she thinks that the workers' compensation insurance market is also complicated and she is concerned that if the Board just takes an informational stance, the bill may become law and she said she thought it was too soon. She said she is not opposed to mutualizing; however, thinks a longer research and review period than this bill provides is necessary.

Mr. Mihelish said he concurred with Ms. VanRiper's comment. He said this is a big step and the legislature is in its eleventh hour this session and he said he believes there needs to be a lot more work done and a lot more thought put into something that is this complex. He said to introduce this at this time in the session does not make sense to him.

Chair Zanto said he agreed.

Ms. Moss said she did not find any indication in the draft legislation that this approach would have anything to do with improving MSF or benefiting Montana businesses. She said she just saw it as a thinly veiled effort by a private company and lobbyists. She commented that she had seen efforts like this before such as the deregulation of Montana Power. She added that she has attended a lot of the workers safety programs in Billings and said she is always impressed with the diversity of business owners and those people are always very supportive of MSF; some are policyholders, some are not. MSF has a great retention rate, hovering around 90 percent, and a decline in accidents rates. She said she believes MSF is doing an excellent job in its current structure and having legislation proposed this late in the session on a very complex issues is very unfortunate and she said she was very concerned about it.

Chair Zanto sought clarification as to whether Ms. Moss's comments were referring to LC144.

Ms. Moss said her comments applied to both LC144 and LC993 as well.

Chair Zanto reported that he spoke with Matt Mohr who was unable to attend; however he asked that his comments be shared. Chair Zanto said that Mr. Mohr expressed concern for the employees of MSF and what the impact of this legislation would be on them. Chair Zanto said there is an obvious impact either way and that Mr. Mohr's issue is that the message that is being sent to the employees right now is not a good message; essentially, that they are being questioned on their ability to manage claims or to manage this business. He said Mr. Mohr is very concerned about that and what mutulization impacts would be in LC993. Chair Zanto said Mr. Mohr is also very concerned about the impacts to employers and the rate implications that might be shouldered by those employers. Lastly, Chair Zanto said Mr. Mohr was concerned about the Old Fund implications because LC993 calls for dedicated funding to the Old Fund through an earmarked premium tax. Chair Zanto noted that the available language for LC993 is not the final bill and said he had concerns as to what would ultimately flush out with regard to the Old Fund.

Chair Zanto shared his own comments and noted that he has gone back and forth regarding opposition of LC993 in its current form or whether to take a neutral positon. He said the Board does not know what this legislation is going to be and the responses today are based on "draft" language. He stated that if the final language, expected out later that week, were substantially different, the Board would have to have another discussion. He said due to that uncertainty, he was reserved in his decision and felt it was important for the Board to know what the final impact is going to be once there is final bill language. He said he believed the safest position to take at this time is to not take a position on the bill in case there is a substantive change to the current language. If necessary, he offered the Board the options of a phone discussion or holding another public meeting when the final language is available.

President Hubbard commented that it is difficult to determine the best position to take on draft language that changes by the minute which is often the legislative process of negotiations and changes throughout the drafting phase to assure passage. He said he concurred with all of the Board member's comments and echoed Mr. Mihelish's previous meeting position that "If it ain't broke, why are we trying to fix it?" He said MSF is not broke and he wanted to be clear that the proposal to become a domestic mutual emanated from the bill draft to eliminate MSF from existence and take its assets, essentially creating a New Old Fund. The sponsor, Senator Thomas attempted to craft legislation that would respect the current structure of MSF as an independent public corporation while addressing the public pressure to compete with neighboring states' workers' compensation insurance rates. He reminded the Board members that when the New Fund was created, it was structured as a domestic mutual; however that was reversed in a special session due to the rate impact it would have had on MSF's customers. He encouraged the Board to take, at a minimum, an informational position on LC993 so that MSF can be good informers and educators about how MSF operates and be available to answer questions that may arise at the hearing which would allow MSF to establish itself as a reliable source of credible information.

He said he could see potential difficulties in opposing the plan to mutualize MSF; in particular, opposing that and the proposal to eliminate MSF would leave no fallback position. He said he believed that would not serve MSF's employees, injured workers or insureds well at all. He told the Board that it would be possible to wait until the bill is introduced to determine the Board's preferred approach; however, discussions with legislators are indicating that both bills are considered too much, too late in the session; assertions he agreed with. He indicated that he felt it was more appropriate to encourage legislators to take the time during the biennium to determine what would be best for Montana businesses, injured workers and MSF employees. He said in his 27 years at MSF, there have been three studies of MSF reviewing various approaches and each time the assigned study committees concluded that it was not in the best interest of Montana business and injured workers to make changes. He said circumstances have changed over the years. Economic health changes as well as MSF's financial health were, and are, considerations in each study. President Hubbard said he thought the Board could be very proud of MSF as it operates today and said members had good reason to have trepidation about anything that would disrupt a system that is working.

Mr. Mihelish said he respectfully disagreed with President Hubbard. Harkening back to the adage, "If it ain't broke, don't fix it" he said he was concerned that taking a neutral position would send the wrong message to the legislature. He said he wanted to be on the record saying that "It ain't broke." He said he opposes any change to MSF in its current state because it is run well, run by good people and he did not see what advantage mutualization would bring to the state of Montana - the policyholders and business people - other than higher rates. He said he could not understand why this was being done and asked what motivated Senator Thomas to propose this bill? He asked if this was a compromise because it was thought that MSF was going to be privatized and said he was not in a mood to compromise right now. He said he agreed that MSF could be informational but said he believed the Board needs to take a stronger position.

Mr. Miltenbeger, said with all due respect to Mr. Mihelish and Mr. Mohr, in his review of the events of the past 30 days, particularly with LC144, he is having difficulty squaring the two situations. He said he has been in Montana for 17 years and this is the second time there has been a run on MSF. How on earth is it not broken that we can have the state look at the relative success of this organization and view it as a piggy back in a bad year and say it's not broken. He said MSF is a well-run organization that has succeeded for the injured workers and the small employers of Montana and in that sense, no it is not broken. He said what is broken is that policyholders and injured workers are under continuing peril. Every two years when the State of Montana has a bad year, heads turn to MSF to see if money can be taken from this company. He recommended that the general movement towards the Maine model would remove MSF from the claws of the state but maintain the role of the organization as being committed to Montana - not something that can be sold to AIG for a profit in five years but something that is committed to workers' compensation. Being a mutual company, staying in the state of Montana, remaining as the carrier for all comers, to Mr. Miltenberger would be an ideal world. He said he did not know how that process would work and therefore completely agreed with the concept to ask the legislature to slow down a little bit. He then addressed Mr. Mohr's point regarding the employees of MSF. He said when the employees of this organization who have tenure or are even just starting out on their career at MSF, see that the rug can be pulled out from under their career path every 24 months by the whims of the legislature, that indicates to him that it is broken. He said it is broken for the employees of MSF, the employers and for the injured workers because of the uncertain future that is held out. He said that is why he believes it is important to try to move towards some better status, whether or not it is a mutual or some other hybrid, whether it 2019 or 2020. He stated the current system does not provide financial guarantees because today, MSF is completely vulnerable.

Mr. Mihelish commented that every organization is subject to corporate governance. MSF is currently governed, somewhat by the legislature; however, if mutualized, MSF will still be governed by somebody who could come up with some crazy idea to divest assets. He said that concern doesn't go away just by eliminating the legislature's interest in MSF; there will still be somebody who will have to guide MSF.

Mr. Owens asked President Hubbard to clarify the different treatments of MSF's current assets based on the specifications of each approach, becoming a mutual or being dissolved.

President Hubbard stated that the current assets of MSF are already held in trust, as required by law, for the payment of MSF's obligations for injuries post July 1, 1990. He said he believed that even under any proposed new legislation, only assets subsequent to an effective date of that legislation would be subject to that law change. He explained that under a mutual company the assets are protected in a similar fashion on behalf of the policyholders.

Chair Zanto called for additional comments or questions.

Ms. Van Riper said whatever the Board choses to adopt regarding LC993 should reference it in its current form. She said her position, provisionally, would be that the Board does not believe the state fund is broken; however, would be open to the possibility that mutualizing MSF could be better for the effected entities given the changes in the market, changes in working employment and so forth. She said if the Board supports an interim study, they would recognize that would delay any action another couple of years and allow for input from effected parties to explore the benefits and costs of the mutualization with an eye to, if it is a potentially positive alternative, having a group draft that bill prior to the next session.

Chair Zanto called for public comment.

Quint Nyman, Executive Director of the Montana Public Employees Association and Vice President of Montana AFL-CIO, stated that their position is to oppose privatization as a whole which comes out of a perspective that there was a reason government took up these services and they believe that reason still exists today. On behalf of the employees, privatization creates a level of uncertainty that MPEA just cannot support and move forward with. He noted that he appreciated the conversation by the Board regarding the stability of the employees who work here and how important that is to the Board members. He thanked the Board and promised to convey those conversations with the MSF employees.

President Hubbard asked that when Board members craft a motion directing management's response to LC993 they provide enough guidance and allow some leeway at the same time so that management can carry out their wishes but still remain flexible in the response. He noted that approach would assist in avoiding the need to call another special Board meeting.

Mr. Mihelish said he suggested the Board oppose LC993 in its present form and await further draft. In the meantime, MSF should hold themselves available as informational on some sort of mutualization concept.

President Hubbard said the Board should take action on the current standing motion by either amending, passing or failing it.

Chair Zanto called for additional public comment to assure that the Board had received input from all interested parties. There was no additional public comment and Chair Zanto called for the vote.

Mr. Mihelish asked Chair Zanto to read the motion again.

Chair Zanto said "I move the Board approve taking no position on LC993 and to direct President Hubbard to engage lobbying efforts to provide informational testimony on LC993 before the legislature." A roll call vote was taken: Chair Zanto, Mr. Miltenberger and Mr. Owen voted aye, Ms. VanRiper, Mr. Mihelish and Miss Moss voted no. The motion failed.

Chair Zanto said the Board could choose to take no position on LC993 in its current form or oppose LC993 in its current form. Mr. Mihelish reported his preference was to oppose LC993 in its current form.

Ms. Van Riper made a motion that the Board oppose LC993 in its current form and the Board acknowledges with changes in the market and other relevant conditions in recent years, mutualization could be a positive alternative that the Board would support an amendment that would call for an interim study including input from interested parties providing a cost benefit analysis broadly construed and if mutualization appears to be a positive alternative, support efforts to draft a bill for the next session with input from interested parties. Mr. Mihelish seconded the motion.

Chair Zanto clarified that this motion would position the Board to oppose LC993 in its current form; however he expressed concern that the motion did not specify that the Board wants management to continue its lobbying efforts.

President Hubbard said he believes that motion instructs staff to support an interim study and if LC993 is passed calling for an interim study, staff would have the authority to support it.

Chair Zanto called for further discussion.

Ms. Moss amended the motion with a statement that the Board acknowledges that as Montana State Fund exists now, they recognize the excellent employees, the sound management, the fiscal integrity and oversight. She said she thinks it is important to share with MSF policyholders, MSF employees and the public that the Board believes the organization is well managed and has the willingness to look at all possibilities for the future.

Chair Zanto called for further discussion.

Ms. Van Riper expressed appreciation to the legislators who brought the study bill idea forward as an alternative to LC144. She said the position she encouraged the Board to take was not in any way to convey that the Board was unappreciative of their efforts.

Mr. Mihelish also noted that he had requested information from President Hubbard the day before the Special Board meeting which clearly indicated how well run MSF is and how the policyholders of this state have benefited from the management of MSF for the last 20 years or more. He said that since 2011 $122 million of dividends have been declared and returned to the policyholders of Montana. The Board has decreased rates by 40 percent since 2011: 2011 decreased by 4 percent, 2012 decreased by 20 percent, 2014 decreased by 6 percent, 2016 decreased by 5 percent and 2017 decreased by another 5 percent. He said "It ain't broke folks."

Chair Zanto called for further discussion, there was none. He called for public comment; there was none. Chair Zanto called for the vote and the amended motion passed unanimously.

III. Old Business/New Business

Chair Zanto called for old or new business.

President Hubbard provided an update on LC144. He noted there was a representative of the primary proponent creator of LC144 in the audience and asked that if he misspoke the representative would be willing to provide clarification for the record. He said LC144 is expected to be introduced by Senator Eric Moore of Miles City and the bill, in its current draft calls for the dissolution of MSF effective July 1, 2018. This is a change from the original language which called for the dissolution upon passage of the bill and this provides a year to achieve dissolution. The bill charges the Commissioner of the Department of Labor and Industry (DOLI) with the construction of a plan of operation for an assigned risk market mechanism. In that mechanism, employers would have to be declined three times by a voluntary market insurer in order to be able to apply for coverage under the assigned risk plan. The DOLI Commissioner approves the rates of the assigned risk pool which will be called Plan 4. Currently there is Plan 1 – self insurers, Plan 2 – private carriers, Plan 3 – Montana State Fund. Under this bill, Plan 3 will be eliminated and Plan 4 would be erected in its place. The Commissioner is instructed to provide for the orderly and efficient dissolution of the State Fund, transition of policies, risks and MSF's obligations, transition of MSF employees to either state or private employment or retirement in the State Employee Retirement System as required in MCA 19-2-1002. He said that code contains special statutory provisions with regard to elimination of state entities and displacement of public employees.

Effective July 1, 2018, the bill creates a trust upon dissolution of MSF and the DOLI Commissioner is given the authority to declare dividends for policyholders under LC144. After a dividend declaration, the remainder of the assets/reserves would be placed in a single trust plus 20 percent of the remaining equity. The principal of the State Fund dissolution trust would be permanent and if the state fund dissolution trust is insufficient to pay current claim benefits and expenses, the DOLI Commissioner may authorize such funds as may be necessary to be withdrawn from the State Fund Dissolution Trust principal. Half of the investment income can be appropriated by the legislature and the remaining amount would be deposited in the trust. Each year on an annual basis the DOLI Commissioner is able to establish the necessary funding level required for the next year and make necessary adjustments, up or down, and any excess unnecessary principal (up to 50 percent) in the trust based on that evaluation may be appropriated by the legislature. After a complete run off of all claims, which would likely run decades into the future, the legislature may appropriate any part of the remaining state fund dissolution trust principal by a vote of 3/4s of each house of the legislature.

He said the first 14 pages of the bill called for the dissolution of State Fund, running off the liabilities through DOLI, which management believes is a serious conflict of interest because this bill makes DOLI the payer as well as the regulator of the benefit system in Montana. He added that there is old case law from 1989, *Sky Country vs. Montana State Fund*, which brought to light the conflict of interest between the State Fund being part of the DOLI Division of Workers' Compensation and the regulatory body of the benefits system, the Workers Compensation Court at DOLI. The court agreed with Sky Country that there is an inherent conflict of interest in the regulator also being the real party in interest. President Hubbard said his comments highlighted the differences between the first draft that he sent to the Board and the current LC144 language.

Chair Zanto called for comments.

Mr. Miltenberger commented that this language seemed to be an improved version over the first one as it allows more time for dissolution and less immediate taking of the policyholder surplus by the state. He said, nevertheless, he continues to think it is not wise for our policyholders, employees and the injured workers. He asked if it would be appropriate to consider opposition to the new version?

President Hubbard said a new motion is not necessary, the Board already authorized staff to express their opposition to this bill in whatever form it takes.

Chair Zanto said there was no need to take action unless one of the Board members thought it was necessary to reconsider the position to strongly oppose the bill that the Board established at the March 10 Board meeting. No Board members expressed a desire to reconsider their position.

IV. Public Comment

Chair Zanto called for public comment.

Mark Barry, Chief Financial Officer, Montana State Fund, expressed frustration with a study bill of MSF as previous studies have found the MSF structure best serves Montana businesses and the workers' compensation system in Montana. He said he agreed it could be studied but felt the question that really needed to be answered is how to develop the protection of MSF assets for the Montana businesses that are insured by MSF. In addition to developing such protection, the only other areas to evaluate would be mutualize MSF or leave it the same.

Chair Zanto asked if any Board members opposed the language he had suggested to "strongly oppose" LC144; no Board members expressed opposition to use of that language. He then asked the management team and Quint Nyman, as the union representative, to express to MSF employees that the Board strongly opposed LC144. He said they are not in any way behind that bill. He clarified that the Board has essentially stated that they oppose both bills and are going to continue to move forward in discussions around the potential for further discussions around a mutualization concept. Chair Zanto noted that based on his memory, this is the first time the Board has had to call a special meeting on an issue such as this and he thanked the Board members for committing their time to attend and participate as well as their review of the documentation necessary to discuss this issue. He also thanked the audience for their participation and called for any additional public comment; there was none.

Mr. Miltenberger made a motion to adjourn. Mr. Mihelish seconded the motion.

The meeting was adjourned at 2:40 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