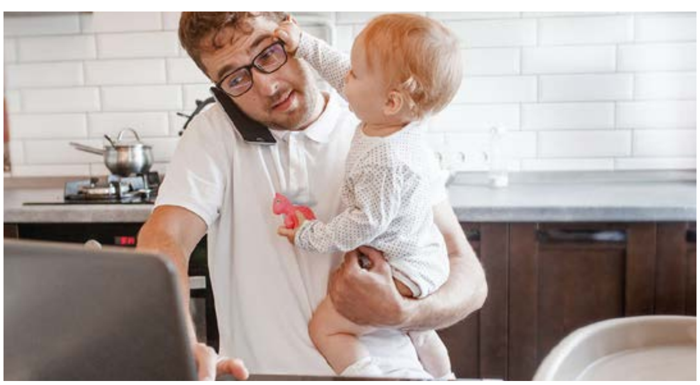
Unchanged:

A commitment to work and workers in Montana.



2021 GUIDE

TO WORKERS' COMPENSATION

Montana State Fund

safemt.com

OUR MISSION

We partner with employers and their employees to care for those injured on the job and we champion a culture of workplace safety for our fellow Montanans. At Montana State Fund (MSF) we work every day to help Montanans stay safe, healthy and productive on the job. When injuries occur, we provide medical and wage loss benefits and help injured workers get back to work. Our efforts contribute to business growth and to a more prosperous Montana.

HOW DOES WORKERS' COMPENSATION DIFFER FROM OTHER TYPES OF INSURANCE?

All workers' compensation insurance providers including self-insurance, private insurance companies and MSF must follow the same laws. For workers' compensation insurance, premiums are established long before the number, severity, duration or cost of claims can be known. Loss reserves are established as claims occur, but the ultimate cost of those claims is not known for many years. Catastrophic and/or unanticipated events may also occur, resulting in losses that can greatly exceed a policyholder's annual premium. Workers' compensation premium is paid wholly by the employer; employees do not share in covering the cost of the premium. In addition, when an accident occurs to an employee the insurer pays all the costs of that claim.

WHY IS THERE A MONTANA STATE FUND?

In most states, including Montana, workers' compensation is mandatory and employers must purchase insurance coverage or be subject to penalties and exposure to lawsuits by employees. With enactment of state workers' compensation laws, the need for workers' compensation insurance created other issues. Employers feared they would be forced out of business if refused coverage by insurance companies. They also worried that insurance carriers might impose excessive premium rates that would be a financial burden. In response, state legislatures provided for a guaranteed market for workers' compensation insurance by implementing one of three models:

1. Assigned risk plan
2. State monopoly
3. A competitive state fund

ASSIGNED RISK PLAN

There are a number of states where private insurance carriers or the state fund (if one exists) can reject both small and large businesses for workers' compensation insurance. When employers cannot get coverage, they are put into the assigned risk plan and are "assigned" to an insurance company. Assigned-risk plans generally have rates that are higher than the voluntary market because of the higher level of risk of the employers and the industries that are placed in the assigned risk plans.

STATE MONOPOLY

In monopoly states, all coverage is provided by a state agency (State Fund). There are no private insurers and no competition. This is the system in use by the states of Washington, Wyoming, North Dakota and Ohio.

A COMPETITIVE STATE FUND

The system that has basically been in place in Montana since 1915 gives employers three options for purchasing their insurance:

- Develop a self–insurance program. (Plan 1)
- Purchase from a private company. (Plan 2)
- Purchase from MSF. (Plan 3)

This system provides the most options and flexibility for employers. It also protects the interests of the majority of Montana businesses by fostering a competitive marketplace – resulting in premiums that can be as low as prudently possible. As the guaranteed market insurer, MSF cannot refuse to insure an employer except when the employer defaults on an obligation to MSF. Unlike MSF, private carriers have the ability to move in and out of the state based on opportunity and profit and can choose who they will and will not insure. MSF offers employers a stable, locally controlled, reliable and competitively priced source for workers' compensation insurance, regardless of the size or risk of the business.

Timeline of key events related to workers' compensation issues (1987–2020)

July 1, 1987

- *Payroll tax of 0.3% placed on employers because of the unfunded liability in the State Fund (Old Fund).*

1989 regular legislative session

- *Creation of State Compensation Insurance Fund as a domestic mutual insurance company with regulation by the Insurance Commissioner.*

1989 June special session

- *HB 56–Transfer of $20 million from the General Fund to workers' compensation tax account.*

MSF OPERATIONS

By law, MSF is a nonprofit independent public corporation governed by a Board of Directors. The governor appoints the seven members of MSF's Board, based on statutory eligibility requirements. Board members serve a four-year term on a staggered basis.

Montana law states that the management and control of MSF is vested solely with the Board of Directors, which is to operate MSF as an insurance company. The board's specific responsibilities include:

- Adopting rates to be filed with the State Auditor's Office Commissioner of Securities & Insurance (SAO).
- Declaring dividends.
- Adopting the annual business plan.
- Establishing the annual operating budget.
- Determining appropriate policyholder equity levels.
- Approving the annual financial report.
- Hire the CEO.

MSF is established to be neither more nor less than self-supporting from premium and investment revenue and is **not funded by taxpayer appropriated dollars**. MSF was created by the Legislature to function as an independent insurance company conducting business in a competitive market. MSF's Board of Directors is attached to the Department of Administration for administrative purposes only.

Montana comprises only one-half of 1 percent (0.5%) of the national workers' compensation market.

MSF OVERSIGHT

MSF is subject to oversight and regulation by:

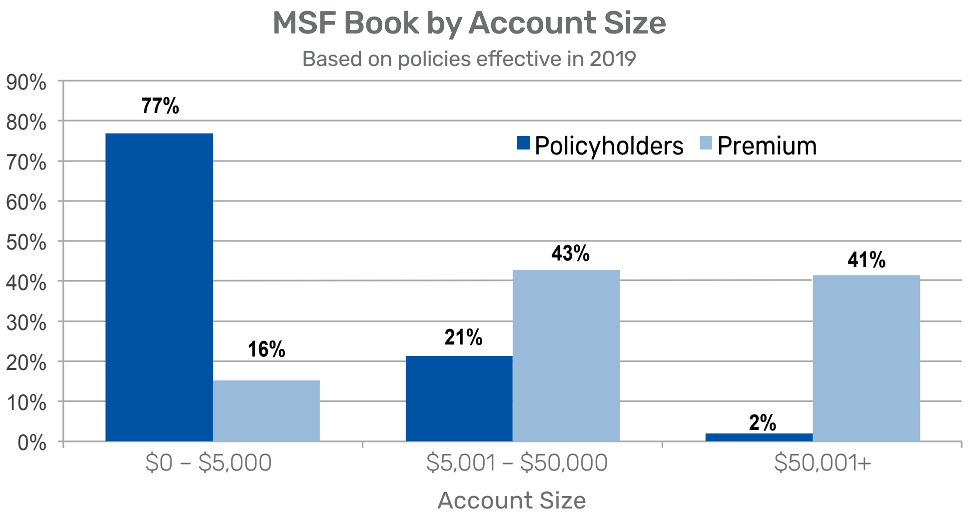
- State Auditor's Office
- Department of Labor and Industry
- Montana Legislature

STATE AUDITOR'S OFFICE (SAO)

Beginning in 2016, MSF is required to file quarterly and annual financial reports with SAO.

In addition, as the Commissioner of Insurance, SAO has regulatory responsibilities over MSF similar to that of other insurance companies. Those responsibilities include:

- Market Conduct Examinations.
- Financial Examinations.
- Solvency and Financial Monitoring.
- Rate Review / Approval.
- Form Approval.
- Policyholder Complaint Reporting.



MSF predominantly serves small businesses in Montana that would not otherwise have access to affordable workers' compensation insurance. However, MSF's role as a competitive guaranteed market allows MSF to maintain lower and more stable rates as well as a high level of customer service for all policyholders. The premium volume from medium and large account employers who choose to insure with MSF creates economies of scale and reduces financial variability, benefiting all Montana employers regardless of size.

- *Payroll tax on employers modified to 0.28%.*
- *Liability of State Fund separated into claims that occurred before July 1, 1990 (Old Fund), and claims that occurred on or after July 1, 1990 (New Fund — now Montana State Fund).*
- *The Old Fund became funded by the payroll tax. MSF would administer the Old Fund on behalf of the Legislature, but have no liability or funding responsibilities.*
- *MSF received $12 million startup and then became funded solely by insurance premiums and investment income from premiums.*
- *Any dividends declared by MSF were required to be transferred to the Old Fund.*
- *Legislative oversight was increased and regulation by the State Auditor's Office ended June 30, 1990.*

1990 May special session

Under the insurance laws of Montana, **premium rates filed by an insurer cannot be excessive, inadequate or unfairly discriminatory.** The insurance commissioner has the ability to reject a rate filing if he or she believes the rates do not meet these standards. MSF is required to follow these laws for SAO approval of MSF filed rates.

MSF is also required in law to set rates in consultation with an independent actuary in good standing with the American Academy of Actuaries.

DEPARTMENT OF LABOR AND INDUSTRY (DOLI)

As with all workers' compensation insurers, the Department of Labor and Industry is the regulator for matters related to workers' compensation claims.

MONTANA LEGISLATURE

The legislative auditor conducts annual financial and compliance audits. In addition, the Legislature monitors MSF through the Economic Affairs Interim Committee (EAIC), which appoints two legislative liaisons to attend the MSF Board of Directors meetings. The EAIC receives an annual report on MSF's Board-approved budget. MSF provides legislators a copy of the annual report every year.

THE LEGISLATURE'S ROLE IN CREATING THE OLD FUND AND MSF

BACKGROUND

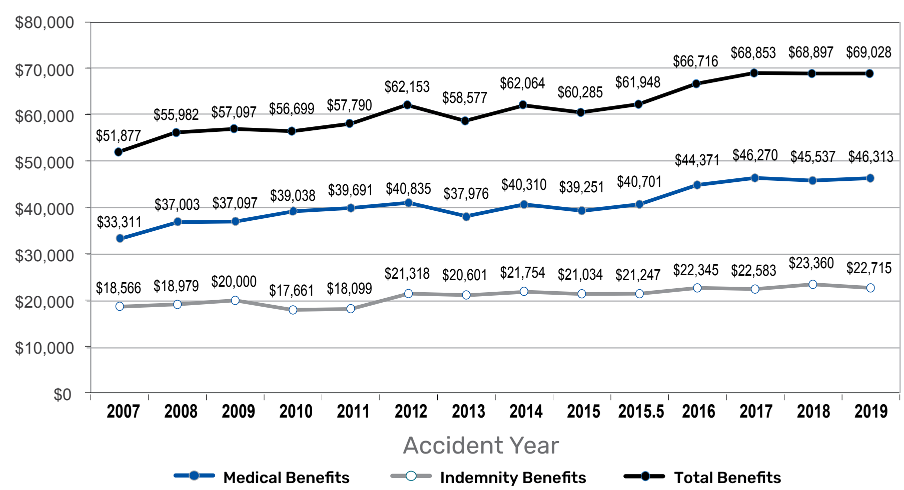
Between 1987 and 1993 the Legislature made major changes to the state's workers' compensation system to deal with an estimated unfunded claim liability of more than $500 million.

Workers' compensation insurance premium rates were influenced by the political process during the 1980s even as the cost of claims increased beyond the premiums charged. The unfunded liability grew, jeopardizing the entire system and, as a result, forced private carriers to leave the state because they could not profitably write coverage compared to the insufficient rate levels charged by the old state fund. Their departures meant that Montana businesses had fewer options for their workers' compensation insurance and placed a greater burden of a flawed system on the old state fund.

Once it became clear that the structure was no longer workable, the Legislature found it necessary to intervene. During the 1987 session, Montana's legislators made the difficult and unpopular decision to enact a 0.3 percent payroll tax on employers to raise revenues.

The average wage-loss claim currently costs an estimated $69,000, although the most catastrophic of claims can cost several million dollars. About 70% of workers' compensation claim costs are for medical services, which is a fast-growing driver of Montana claim costs. Wage replacement (indemnity) costs have been relatively constant over the past 10 years. Workers' compensation medical costs were rising 6% per year prior to 2012, but are currently rising about 2.5% per year after HB334 benefit reforms were enacted in 2011.

Average Cost Per Wage-Loss Claim



1993 regular legislative session

- *Payroll tax on employers increased to 0.5%.*
- *Payroll tax of 0.2% placed on employees, sole proprietors, partners, subchapter S corporation shareholders, and members or managers of LLCs.*

September 14, 1996

- *MSF board meeting: dividend returns money to state. The $103 million dividend repays $12 million initial funding and pays down Old Fund bonds.*

1997 regular legislative session

- *MSF repaid $20 million received by the Old Fund under HB 56 to the General Fund.*
- *SB 67 ended the requirement that dividends must be paid to the Old Fund and set up the test under which the payroll tax could terminate. MSF transfers $63.8 million to the Old Fund.*

December 31, 1998

- *Payroll tax terminated as Old Fund meets the criteria to be considered "adequately funded."*

However, further measures were needed to stabilize the state's workers' compensation system and in 1989 the Legislature created a new entity: the State Compensation Mutual Insurance Fund. This entity was structured to operate as a domestic mutual insurance company, and as such, function independently of state agency requirements.

Rather than addressing the underlying issue that rates were inadequate to fund the workers' compensation liabilities going forward, in 1989 the Legislature appropriated $20 million of the state's General Fund to the old state fund (those funds were later repaid). However, the unfunded liabilities continued to grow and the rates needed dramatic increases, which would be devastating to existing and new businesses in Montana. Since the required rate increases were simply unacceptable, an innovative solution needed to be found to resolve the crisis once and for all.

In the special legislative session in May 1990, the Legislature separated the liability into claims occurring before and after July 1, 1990. Claims occurring before this date became known as Old Fund. Any claims after this date became the responsibility of MSF. In doing this, the Legislature determined that the Old Fund liabilities would be funded by an increased payroll tax on employers and employees. Bonds were sold to cover the unfunded liability and were serviced by proceeds from the payroll tax. MSF administers the Old Fund on behalf of the Legislature (MSF is reimbursed for the cost of administering the claims but has no liability or funding responsibilities).

Old Fund liability of $500 million was financed through a combination of payroll tax collections (68 percent) and monies transferred from MSF (32 percent). The key events are:

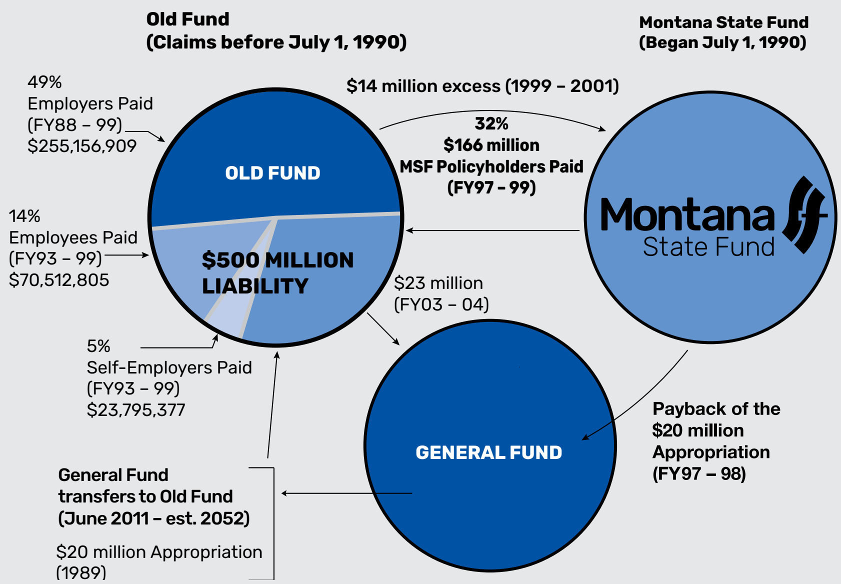
1989
$20 million appropriation of General Fund money to the Old Fund.

1987 – 1998
$349 million in payroll tax collections.

1996 – 1998
$166 million paid by Montana State Fund to eliminate the Old Fund liability and allow for payments of dividends to policyholders. In recognition of the payment, the state Legislature allowed for any excess beyond actuarial projection in Old Fund to be transferred back to MSF.

1997 – 1998
MSF paid back the 1989 appropriation of $20 million to the General Fund.

1999 – 2001
$14 million in excess returned to MSF.



2003 – 2004
$23 million transferred as Legislature determined that all existing contingency reserves and any excess from the Old Fund should go to the General Fund.

June 2011 – est. 2052
By law, when Old Fund assets are inadequate to pay claims, transfers are to be made from the General Fund to the Old Fund. Between 2011 and June 30, 2020, the General Fund has expended more than $84 million to support the Old Fund.

- *SB 19 transferred $4 million of Old Fund excess to General Fund and set up study committee to report to the 58th Legislature on the structure of Montana State Fund.*

2002 special session

- *HB 363 removed the reserve requirements from the Old Fund and transferred $18.2 million, as well as any future excess, to the General Fund from the Old Fund.*
- *SB 304 created an interim committee to study the structure and role of MSF, and if it would be in the best interest of the state to sell either the Old Fund or the New Fund. The committee was tasked with making recommendations to the 2005 Legislature.*
- *SB 360 stipulated that the Legislature cannot transfer monies from Montana State Fund to be used for other funds or other programs.*
- *$800,000 of Old Fund excess transferred to General Fund for a total of $23 million.*

2003 regular legislative session

OLD FUND STATUS

There are approximately 495 open claims remaining in the Old Fund. As of June 30, 2020, the actuarial estimates for the remaining obligations range from a low of $36 million to a high of $61 million. The actuarial central or best estimate of $48.3 million will not be completely paid out until 2050. All Old Fund assets were depleted by June 2011 and, as required by law, the state General Fund is used to pay the remaining Old Fund liabilities. Actuarial estimates indicate the funding requirement for the Old Fund in Fiscal Years 2021 and 2022 will total approximately $16 million.

FINANCIAL CONDITION OF MSF

The Montana Legislature intended that MSF be run in a businesslike manner, solely funded through insurance premiums and investment income. MSF receives no taxpayer appropriated dollars.

Over the 31 years of its existence, MSF has built a financially strong organization serving Montana business and has provided a stable insurance market over this period as reflected in overall rate levels and the return of dividends to businesses insured with MSF.

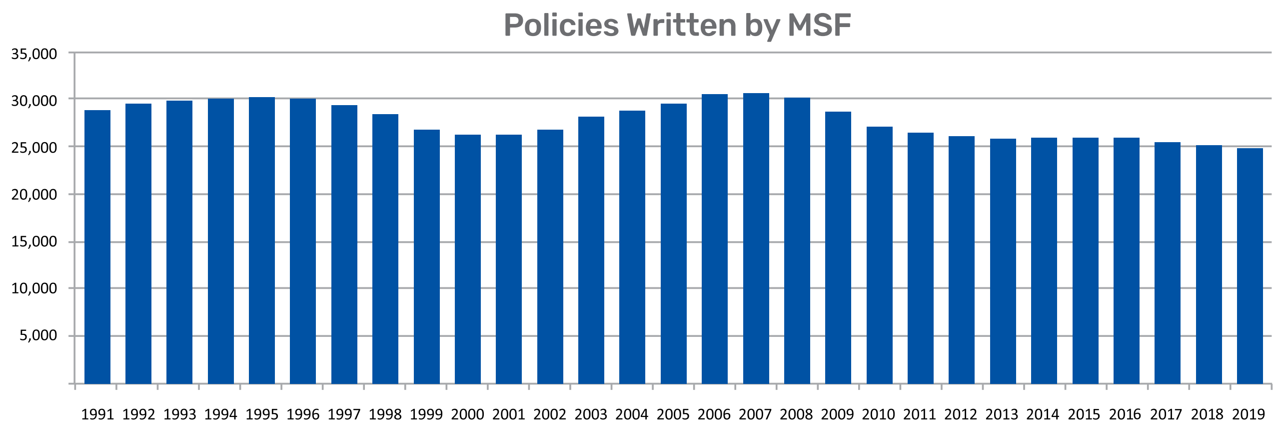
MSF has not raised its rates since the policy period that began July 1, 2006. Since that time, the MSF Board of Directors has approved rate reductions so that rates are 47% below the level in 2006.

Most recently, the MSF Board approved an 8.6% rate decrease effective July 1, 2019, and held rates steady for policies effective July 1, 2020.

MSF RATES

Current rates (effective July 1, 2020) are at their lowest level in the history of the current State Fund – dating back to July 1990. MSF's objectives in setting the price for workers' compensation insurance includes the following:

- To generate funding needed to meet the cost of providing indemnity and medical benefits to injured employees and cost-effective services to Montana businesses.
- To provide risk transfer for losses equitably among employers, keeping in mind that the risk of injury to employees varies by industry.



Since the inception of the Montana State Fund in 1990, private carriers have variously expanded and contracted their written workers' compensation insurance volumes in Montana, depending on the business conditions at the time. General economic conditions also affect the number of insured employers. As the guaranteed market MSF insures any Montana business, offering employers a stable, locally controlled, reliable, and competitively priced source for workers' compensation insurance.

2005 regular legislative session

- *SB 61 created legislative liaisons to the MSF board. In response, two legislators were appointed as nonvoting liaisons to the board; they attend all meetings and receive all board materials. The SB 304 committee determined there would be no sale of MSF and therefore maintained the current structure of MSF as an independent public nonprofit and competitive state fund with the responsibility of being the guaranteed market for Montana businesses.*

June 2011

- *The Old Fund assets were depleted and, as required by law, the General Fund began transfer of funds to pay Old Fund claims and administration costs.*

2011

- *MSF Board of Directors adopted a 20% average decrease in rates due to the passage of HB 334 by the 2011 Legislature.*

2013 / 2014

- *The EAIC studies the workers' compensation system.*

- To provide incentive to employers to maintain safe working environments to reduce injuries.
- To ensure a stable insurance market and pricing structure for employers.

DIVIDENDS

Since 1999 MSF has successfully and safely returned a portion of the premiums paid by employers through our dividend program. Although dividends cannot be guaranteed, the payment of policyholder dividends rewards businesses that demonstrate safety. The amount of the dividend depends on the financial position and health of MSF, economic conditions that warrant a return of premium and the prospects for a continued stable operating environment. Dividends are distributed to policyholders based on their losses incurred and premium paid for the dividend year.

- MSF has returned $306 million in total dividends issued since FY 1999.

Section 39-71-2311, MCA requires MSF to establish premium rates using conservative estimates. It states,

Premium rates must be set at least annually at a level sufficient to ensure the adequate funding of the insurance program, including the costs of administration, benefits, and adequate reserves, during and at the end of the period for which the rates will be in effect. In determining premium rates, the state fund shall make every effort to adequately predict future costs. When the costs of a factor influencing rates are unclear and difficult to predict, the state fund shall use a prediction to be more than likely to cover those costs rather than less than likely to cover those costs.

- The Board of Directors declared a $20 million dividend in September 2020.
- In the last four years MSF has returned over $130 million to customers through the general dividend process.
- In the last four years alone, MSF has reduced premium rates by 20%.

WHY NOT JUST LOWER RATES?

Why doesn't MSF just decrease premium rates each year so dividends wouldn't be necessary? Actually, MSF has reduced rates while still distributing dividends. MSF has not raised rates in the last 14 years, since 2006, and the Board of Directors has reduced rates by a total of 47% over that same period. Current rates are at the lowest level in the 31-year history of MSF — all while distributing record dividends to deserving policyholders.

MSF objectives include maintaining stable rates for Montana employers who need to reliably anticipate their costs of doing business. MSF works to keep rate volatility from causing disruption to Montana businesses. MSF has a strong track record of reducing rates when they can be safely lowered due to fewer workplace accidents or improved return to work.

MSF premium rates are set based on several assumptions including:

- The number of policies expected to be written.
- The types of businesses and industries insured.
- The number of claims expected to occur.
- And most important: The estimated cost of the claims.

MSF cautiously evaluates these assumptions in setting premium rates.

MSF dividends are funded as a result of favorable operating results, which include the investment returns on funds set aside for past claims. When operating results are better than expected and investment income exceeds what is needed to pay claims, as well as provide a strong level of policyholder equity, these funds can be shared with insured employers in a dividend. Because investment returns can vary widely from year to year reducing MSF rates in lieu of a dividend would

2015 regular legislative session
- *SB 123 transferred regulatory oversight of MSF from the Legislature to the State Auditor's Office (SAO).*

January 1, 2016
- *MSF converts to calendar year reporting basis.*

July 1, 2016
- *SAO begins review and approval of MSF rates.*

November 1, 2017
- *SAO completes the first financial examination of the MSF 2016 Annual Financial Statement.*

2017 special legislative session
- *Legislature passes SB 4 instructing the Montana Board of Investments to transfer up to $30 million ($15 million each year) of MSF assets to the state's Fire Suppression Fund to be transferred by April 2018 and by April 2019.*

2018
- *The EAIC completes review of the workers' compensation system and MSF under SJR 27.*

cause MSF rates to be volatile, which is detrimental to the Montana economy.

In addition, the general dividend allows MSF to reward those customers that have demonstrated a focus on safety and have managed their results. Remember, MSF is the guaranteed market insurance carrier; MSF is not able to refuse to write a policy even though that policy may be in a highly hazardous industry or may have poor safety records and higher losses. Recent history demonstrates the value MSF provides to businesses in Montana by both rate reductions and dividend payments.

POLICYHOLDER EQUITY – HOW MUCH IS ENOUGH?

Policyholder equity (equity) protects insurance companies from unanticipated costs above those normally anticipated when setting premium rates. Equity also protects employers from swings in rate changes from year to year as a result of the impacts of catastrophic events, adverse court rulings, financial crises, or economic downturns, among others.

There is no single formula for the right level of equity. There are minimum regulatory requirements and several actuarial methods that assist insurers and regulators in ensuring financial solvency and health of insurance companies.

An important measure of the level of equity appropriate to support MSF's long-term solvency is the reserve-to-equity ratio that measures the amount of equity required to support changes in unpaid liabilities (reserves). The MSF Board of Directors consults with its independent actuary to evaluate the level of equity required to support unpaid liabilities. Based on the projected financial statements for 2020, MSF will have a reserve-to-equity ratio of 1.67 to 1 (for every $1.67 of reserve there is $1.00 of equity). MSF's level of equity is similar to but not as strong as that of the insurance industry generally or other state funds.

- Private workers' compensation companies average: 1.3 to 1 (2019).
- State funds rated A or A- by AM Best average: 1 to 1 (2017).

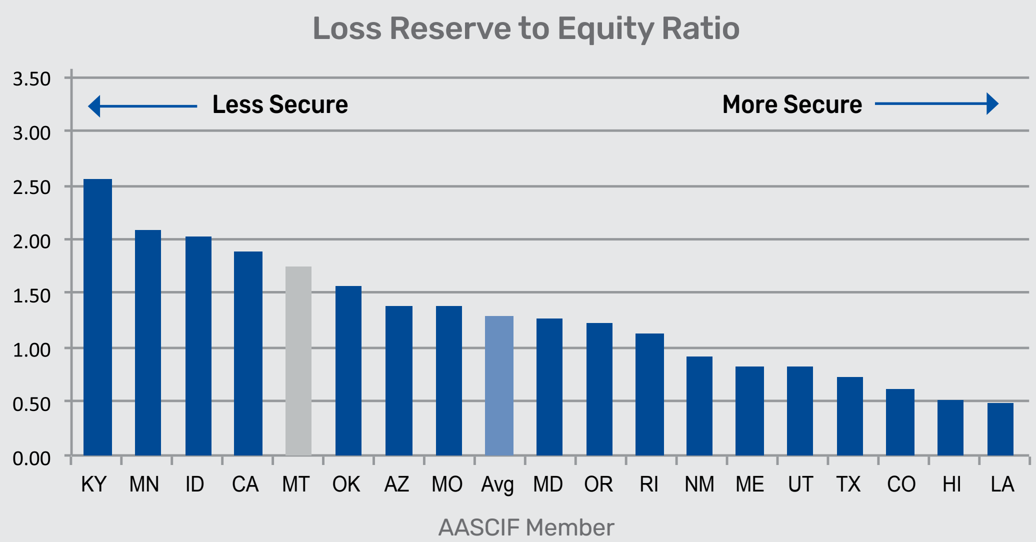
The laws applicable to private insurance companies, as well as to MSF, recognize that insurance companies must maintain adequate levels of equity.

Workers' compensation insurance is different than most other types of insurance because of the long-term nature of the losses that occur. Risks inherent to MSF include but are not limited to:

- Significant long-term obligations associated with workers' compensation claims where the premiums assessed for providing the coverage are established before the actual costs are known.
- MSF provides a guaranteed market and cannot refuse to write coverage.
- Court challenges to HB 334 benefit level changes.

Every insurer, including state funds, must maintain adequate equity in order to safely operate. Without adequate equity, a state fund would be in danger of becoming insolvent and could potentially lead to a taxpayer bailout – which was exactly what happened in Montana with the "Old Fund." The current MSF was created and charged with operating in a manner consistent with best practices in the insurance industry so that it could fulfill its role in providing a guaranteed source of workers' compensation

The ratio of loss reserves to policyholder equity is one of several metrics used to evaluate the financial stability and strength of an insurance operation. The higher the ratio, the greater the risk of insolvency due to fluctuations in asset values and/or liabilities. The lower the ratio, the greater the financial strength to withstand unexpected adverse conditions. Very low ratios may indicate overcapitalization. Among 18 members of the American Association of State Compensation Insurance Funds (AASCIF) that file financial statements with the NAIC, MSF compares favorably. MSF's long-term goal is a ratio of loss reserves to equity in the range of 2.5 to 1.5, which is a somewhat lower equity level than most reporting AASCIF members.



insurance to Montana businesses at reasonable rates while remaining financially sound for the long term.

Maintaining adequate equity is not only a good business practice for the MSF, it is required in state law. The equity held by MSF serves several important functions:

- MSF's equity provides a high level of financial security to insured employers and injured employees in Montana to ensure benefits will be paid.
- MSF's equity contributes to economic development by supporting a stable workers' compensation market, competitive yet stable pricing, and service options for Montana employers.
- MSF's equity minimizes the risk of insolvency and provides a buffer against financial variation from underwriting, loss development, and investment experience.

MSF must meet and exceed Montana's legal requirements for equity that apply to the private insurance market. MSF must be particularly careful to maintain strong equity because of the risks inherent in serving as the guaranteed market – while also writing only one line of insurance in only one state.

According to MSF's independent consulting actuary, MSF has a low likelihood of insolvency at the current level of equity.

In addition, based on a recent comparison of MSF with other competitive state funds, MSF's loss reserve to equity ratio is near the middle of the pack. The lower the ratio of loss reserves to equity, the lower the likelihood that MSF's assets will be exhausted by future claim payments. Compared to other competitive state funds, the level held by MSF is neither the most secure nor the least secure.

BUILDING A SAFER MONTANA

SAFETY. IT'S GOOD FOR BUSINESS.

Our vision is to be an indispensable partner in achieving a safer, healthier and more prosperous Montana. Notice where that starts – safety. Montana's workplace injury rate has long been higher than national averages. While we've improved over the past decade, we're helping business get even better. Here are a few ways we support a culture of safety for every workplace in Montana.

SAFETY MANAGEMENT CONSULTANTS

Our professional team of Safety Management Consultants (SMCs) offer one-on-one safety support for our policyholders. The SMCs provide our customers with customized solutions to develop and implement a solid workplace safety culture.

SITES ON SAFETY

Our complete safety-focused website, safemt.com, offers a comprehensive set of practical safety tips, videos, interactive safety games, useful resources and convenient forms employers and employees can access to create a culture of safety. See https://safemt.com/safety-education/safety-videos/#casestudies for safety stories.

SAFETY WORKSHOPS

We designed our safety workshops to give Montana's employers and employees the tools they need to create and fine-tune their safety programs.

These free seminars cover a variety of important and timely issues. The workshops are open to anyone, even if they are not insured through Montana State Fund. Workshop details and registration can be accessed online at safemt.com.

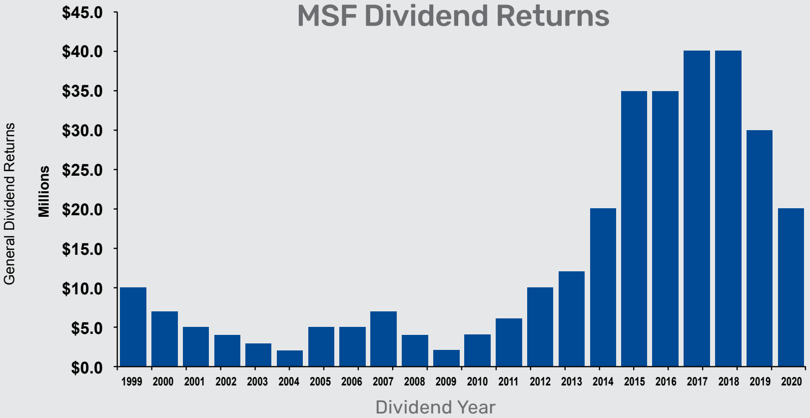
WORKSAFE CHAMPIONS

Our intensive WorkSafe Champions safety education program trains selected employers and employees to become safety advocates to help build a culture of safety in their workplaces. Participants dedicate themselves to learning the nuts and bolts of safety education, communication and implementation.

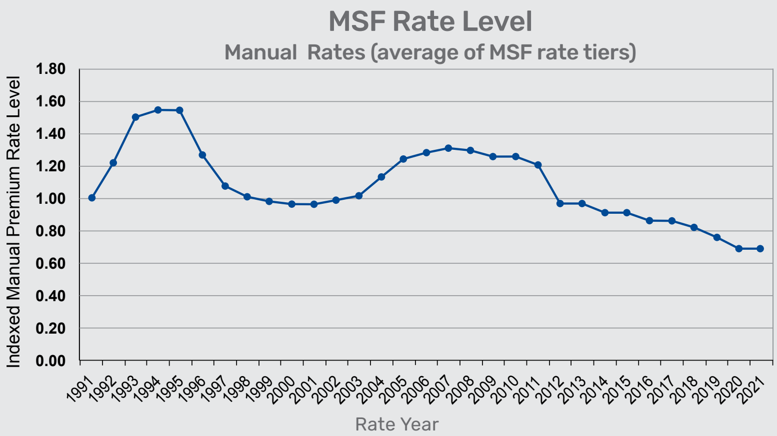
GROWING A SAFER MONTANA

In 2017 MSF launched our Growing a Safer Montana initiative. Within the initiative we established two programs. The first is the high school safety equipment grant program where we award safety gear to eligible Montana high school industry and trade classrooms. The second project is our academic scholarships for college students studying either Occupational Safety and Health / Industrial Hygiene or Construction Trade and Industry. This initiative reflects our commitment to change the safety culture for the next generation of Montana workers.

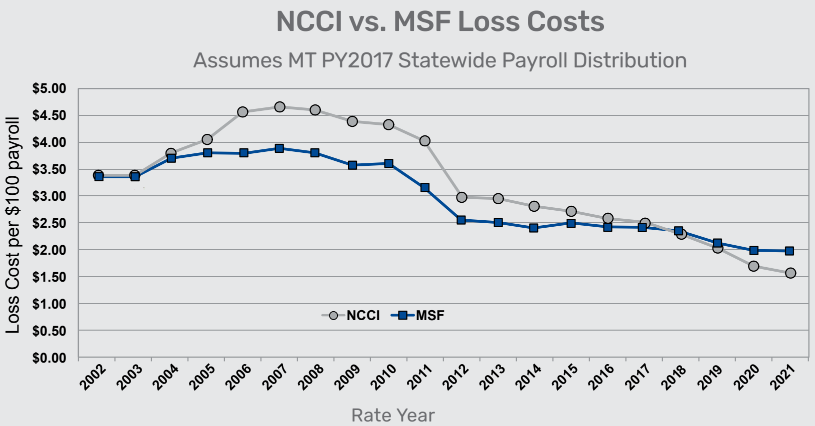
MSF invests approximately $3 million each year to provide safety services to Montana employers and their employees.



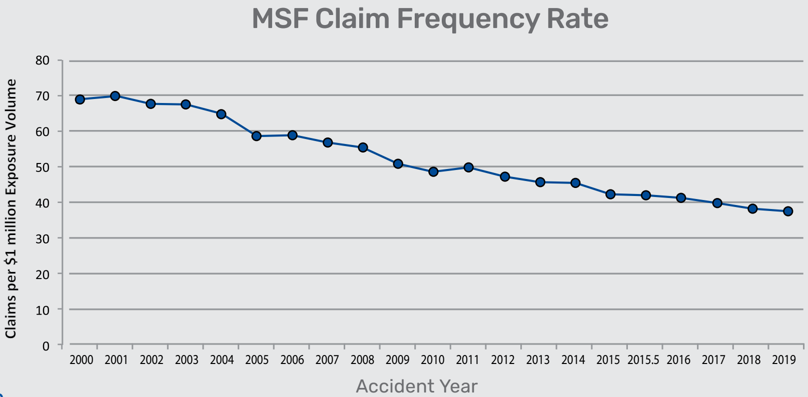
Since 1999 when MSF began returning general dividends to its policyholders, MSF has returned a total of $306 million to policyholders through its general dividend program. Primarily as a result of interest income and stock market gains, MSF's last five dividend returns have averaged $33 million per year. MSF's dividend program helps stabilize rates by distributing excess capital when conditions are favorable as opposed to having rates increase and decrease in unpredictable ways depending on the whims of financial markets. About 95% of MSF policyholders receive a dividend each year. Dividends are an effective incentive in favor of workplace safety that is noticed by policyholders when they receive a reward for having no or few employee injuries that year.



MSF's manual rate levels rose in the early 2000s due to increasing medical costs, and statutory and judicial benefit expansions. Rate levels have decreased since 2006, particularly as a result of legislative benefit-level reforms enacted with HB334 in 2011. MSF rates effective July 1, 2020, are now 47% below the 2006 level and are the lowest rates ever in the history of the Montana State Fund.



"Loss costs" refers to the amount estimated to cover the cost of workers' compensation benefits and claim administration. Loss costs currently represent 83% of MSF premium rates. In a competitive rating state like Montana, carriers use the NCCI loss cost as the starting point in establishing their rates but may adjust the level for the book of business they write. Throughout the mid-2000s, NCCI's estimated loss costs were an average 21% higher than MSF's estimates. MSF's independent consulting actuary determined that MSF did not need to charge as much as estimated by NCCI. NCCI's loss costs have been coming down to the level assumed in MSF rates over the past several rate years. In recent years, NCCI's estimate of the loss costs have been declining at an accelerating downward trend. MSF's estimate has also been declining but by not quite as much as estimated by NCCI.



Claim frequency is measured in claims per exposure volume written in order to account for changes in business volume and rate level. MSF total claim frequency has declined by 3% per year over the past decade. NCCI finds a general pattern of declining workers' compensation claim frequency throughout the country. NCCI research suggests that innovations that improve labor productivity in the economy tend to have secondary impacts on workplace injury rates. Reductions in claim frequency have helped offset increases in medical costs.

GLOSSARY OF WORKERS' COMPENSATION TERMS

Classification Codes: The classification system groups employers so the rates reflect common exposures. The class code assigned best describes the business and includes all types of labor. The business is classified – not the separate employments or occupations. Policyholders report payroll and pay a premium based on the classification codes assigned to their policies.

Exclusive Remedy: The premise on which the workers' compensation system is based: Workers give up the right to sue their employers in exchange for wage loss and medical benefits for their injuries and occupational diseases.

Experience Rating: A mandatory program that modifies an employer's premium based on a comparison of its experience with the expected experience of an average employer using the same class code(s). The experience modification factor either increases or decreases premium.

Impairment Rating: A medical term that is sometimes confused with disability. An impairment rating is a medical determination wherein the medical provider assigns a numerical rating for whatever type of bodily function has been lost, based on the AMA Guides to the Evaluation of Permanent Impairment.

Incurred Losses: The total of the reserves and paid amounts for claims.

Indemnity Benefits: Payments to a worker with an injury or occupational disease representing wage-loss benefits.

Independent Medical Examination (IME): An examination by a physician, psychologist or panel to obtain an independent evaluation of the employee.

Loss Cost: The amount estimated to cover the cost of workers' compensation benefits and claim administration.

Manual Premium: Payroll, divided by 100, multiplied by the manual rate for the classification code(s) assigned a business.

Maximum Medical Healing (Medical Stability or Maximum Healing): A term used by the medical provider to indicate when further material improvement in the healing process would not be expected by a worker with an injury or OD.

Medical-only Claims (MO): Claims with only medical bills and no indemnity benefits owed or paid.

National Council on Compensation Insurance, Inc. (NCCI): National Council on Compensation Insurance, Inc., manages the nation's largest database of workers' compensation insurance information. NCCI analyzes industry trends, prepares workers' compensation insurance rate recommendations, determines the cost of proposed legislation, and provides a variety of services and tools to maintain a healthy workers' compensation system.

Occupational Disease (OD): A medical condition resulting from employment-related activities that occur over a period of time and not from a single traumatic event on a single day.

Old Fund: Claims occurring before July 1, 1990, and, by law, the financial responsibility of the state of Montana.

Permanent Partial Disability (PPD): A condition in which the worker is able to return to work, but has wage loss and a permanent impairment.

Permanent Total Disability (PTD): A condition in which the worker is not able to perform regular employment.

Policyholder Equity: A retained earnings account intended to assure that the insurer will be able to fulfill its obligations to policyholders and injured employees. When an insurer reports a surplus, it is not talking about unneeded or excess funds.

Premium Rates: Includes loss costs plus general and acquisition expenses, offsets for underwriting programs, offsets for investment income, profit and contingency, taxes (as applicable) and other necessary adjustments.

Rehabilitation Benefits: Benefits provided to a disabled worker who has a permanent impairment, job limitations and an actual wage loss, or a worker with an impairment rating of 15 percent or greater. To assist the worker in returning to work following a work-related injury or OD.

Reserves: The estimated value of the benefits and claim costs expected over the life of a claim. Paid amounts are not included in the reserve.

State Average Weekly Wage: Established annually by the Department of Labor and Industry, it is the basis for determining maximum weekly benefits under the Workers' Compensation Act.

Social Security Disability Benefits (SSDI): SSDI benefits are payable to disabled individuals through the federal Social Security Administration.

Temporary Partial Disability (TPD): A worker prior to maximum healing who can temporarily return to work in a modified or alternative employment, but suffers a partial wage loss, can receive this wage-loss benefit.

Temporary Total Disability (TTD): A physical condition resulting from an injury or occupational disease that results in total loss of wages and exists until the worker reaches maximum medical healing.

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Montana State Fund

P.O. Box 4759, Helena, MT 59604-4759
800-332-6102 | 406-495-5000
TDD-TTY 406-495-5030
Fax 406-495-5020
montanastatefund.com | safemt.com