



Everything we do, does more.



2018 Annual Report

Montana 
State Fund

montanastatefund.com | safemt.com

Letter from Leadership

Do what's right

It was the culmination of a year, but on April 30, 2018, Montana State Fund (MSF) kicked off its brand refresh celebration. This event ushered in a renewed mission, vision, guiding values, and logo. MSF employees updated the new mission, vision, and guiding values. MSF's renewed mission states, *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.* As you read MSF's 2018 annual report, you will see how the mission, vision and values are reflected in the work MSF has done and will continue to do moving forward.

Focus on what matters

The safety of Montana's future workforce is crucial. This belief is clearly pursued through two programs in MSF's Growing a Safer Montana initiative. MSF's High School Safety Equipment Grants Program supplies essential safety gear for students in the industrial trade classrooms. Last year, 2,000 students in 22 classrooms received the gear. MSF's Academic Scholarships Program awarded \$3,000 scholarships to 11 higher education students in the trades or safety and health fields, to assist with their education and the financial burden of working towards a college degree.

Deliver with heart

As a collaborative partner of businesses and their employees, insurance agents, medical providers, and others throughout Montana, MSF believes it is its duty to support projects that enhance safety and community well-being. MSF's Assisting Charitable Endeavors (ACE) program is the mechanism to do just that. Last year MSF awarded safety-related grants to 11 Montana non-profit organizations

Succeed together

MSF's dividend program illustrates a true partnership between MSF and employers to enhance safety and the prosperity of MSF policyholders. For the nineteenth year, MSF was pleased to disburse another dividend to MSF's safety-conscious policyholders. Last year, 23,000 employers shared a \$40 million dividend. Since 1999, MSF has returned \$256 million in dividends to policyholders.

Find a better way

To meet evolving employer needs and expectations, MSF is moving closer to replacing its policyholder and billing system. This long-term investment will improve the online functionality that MSF's customers can use be more responsive to their myriad of specific business needs.

Take the long view

In closing, we would like to thank MSF's board members, who diligently ensure that MSF operates to the benefit of its customers and all Montanans. Their work, and the work of our 292 employees, extends our renewed vision as an indispensable partner in achieving a safer, healthier, and more prosperous Montana.

Thank you for your support and partnership in creating a culture of safety across the great state of Montana.

Laurence Hubbard & *Lance Zanto*
President / CEO *Board Chair*

Executive Team & Board Members



Left to right: Sam Heigh, Vice President, Insurance Operations Support; Kevin Braun, General Counsel; Laurence Hubbard, President/CEO; Al Parisian, Chief Information Officer; Rick Duane, Vice President, Human Resources; Julie Jenkinson, Vice President, Insurance Operations and Mark Barry, Vice President, Corporate Support



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2018 Highlights



- We launched an employee-driven effort to refresh our mission, vision, values and logo.
- Over 23,000 safety-minded policyholders shared a \$40 million dividend. Since 1999 we have returned \$256 million of total dividends to our safety conscience policyholders.
- Last year our safety service team hosted 35 safety workshops that touched 575 Montana workers.
- Our WorkSafe Champions onsite program graduated 75 employees from nine policyholder businesses. Our centralized classes graduated 15 people. Since the program's inception in 2008, 568 employees representing 288 unique policyholders have graduated from the program.
- We highlighted Community Closet in Livingston, MT as our 2018 WorkSafe Champion spotlight.
- We have produced 15 safety educational videos that can be viewed on our safety focused website safemt.com. Employers from around the world have accessed and viewed these videos.
- Nearly 2,000 students from 22 Montana high school construction trade and industry classrooms received safety equipment through our Growing a Safer Montana Initiative. In addition, 11 college students studying Occupational Safety and Health / Industrial Hygiene or Construction Trade and Industry each received a \$3,000 academic scholarship. This amount was doubled from our \$1,500 scholarship award in 2017.
- Over 200 medical providers and workers' compensation professionals from across Montana attended our 18th annual medical education conference *Evidence-Based Medicine: New Opportunities to Improve Outcomes*.
- We contracted with Rising Medical Solutions (RMS) to review and process our medical bill payments. MSF processes 145,000 medical bills every year for injured workers.
- We awarded \$23,869 to 14 deserving nonprofit organizations through our ACE (Assisting Charitable Endeavors) program.
- Our college scholarship program, which aids the children and spouses of workers who were fatally injured in a work-related accident, awarded a total of \$6,000 in scholarship money to six individuals in 2018.
- Our employees contributed \$36,881 to the State Employee Charitable Giving Campaign (SECGC). This is the fourth-highest contribution among the 30 state agencies involved. This amount was \$3,936 more in employee contributions than our 2017 contributions. In addition, employees contributed \$2,030 to the Helena Food Share Turkey Challenge.
- MSF received three communications awards from AASCIF (American Association of State Compensation Insurance Funds). These include: 1st place for our Protect Your Parts: Young Worker Social media campaign. And two 3rd place awards for our Work Hard. Be Safe. Head Home statewide media campaign and our Work Hard. Be Safe. Head Home radio/TV ads.

Report of Leadership



The Leadership of the Montana State Fund (MSF) is responsible for the results and stewardship of the resources entrusted to it which is reflected in its financial statements and all other information presented in the Annual Report. MSF governance, culture, values, and system of internal controls are designed to provide reasonable assurance that resources are used appropriately, assets are safeguarded against loss, and that transactions are executed and recorded promptly and accurately in accordance with Leadership's direction, authorization, and State of Montana statutes. These functions, attributes, and tools include the organizational structure and corporate governance practices, selection and training of personnel, communication and enforcement of policies and procedures, strategic and financial planning and budgeting, enterprise risk management, monitoring, and ongoing internal and external audit programs. The effectiveness of these systems, controls, and tools are continually being evaluated by Leadership.

MSF's financial statements are presented on its website. for the year ending December 31, 2018, and include financial results and balances, based on the best estimates and judgment of MSF Leadership. These results are presented on a statutory basis which is consistent with insurance industry financial statement presentation. Inasmuch as MSF, which is domiciled in the State of Montana, is subject to the auspices of the Montana State Auditor, it compiles and reports its financial results according to Statutory Accounting Principles (SAP), which are the principles and standards required by the Montana State Auditor's Office.

The financial overview and results included in this Annual Report should not be considered MSF's audited financial statements. The results presented herein are summarized from the audited financial statements produced by the independent public accounting firm, Eide Bailly, LLP, for the year ending December 31, 2018. Eide Bailly issued a "clean" auditor's opinion, which means that MSF financial statements fairly represent results and balances and there were no material misstatements identified. MSF's complete audited financial statements, including the accompanying notes, are available on MSF's website. Furthermore, inasmuch as MSF is a component unit of the State of Montana, it is required by statute that the State of Montana's Legislative Audit Division (LAD) conduct an audit of MSF's financial statements in accordance with generally accepted accounting principles (GAAP) as prescribed by the Governmental Accounting Standards Board (GASB). The governmental financial statements and the related audit opinion for the year ending December 31, 2018, will be available on the State of Montana Legislative Audit Division's website once they have been presented and approved by the Legislative Audit Committee. Due to reporting differences between SAP and GASB, it should be noted that the statutory financial results differ from the GASB results. Therefore, a financial reconciliation of policyholder equity between the GASB financial statements and the SAP financial statements follows:

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Report of Leadership (continued)



A Comparison of Statutory Policyholders' Equity to GASB Net Assets

For the year ended December 31, 2018

Statutory policyholder equity (SAP)	\$512,475,039
Adjustments to get GASB Net Position	
Non-admitted assets ¹	14,368,607
Change in investment value of bonds to fair market value ²	(15,696,307)
Change in investment lot inventory method ³	2,001,572
Change in investment value of other invested assets to equity method ⁴	(1,468,909)
Change in allowance for doubtful accounts ⁵	(2,666,868)
Effect of differences in pension accounting standards ⁶	(24,752,692)
Effect of differences in OPEB accounting standards ⁷	(1,031,150)
Rounding differences	(1)
GASB net position (subject to audit)	\$483,229,284

Quick Facts as of December 31, 2018

Net earned premium	\$161,258,975
Number of policies serviced	26,527
Number of new claims processed	9,030
Investment income earned	\$57,344,354
Policyholder dividends	\$39,997,664
Loss and loss adjustment expense reserves	\$941,637,695
Statutory equity	\$512,475,039
Reserves to Equity Ratio (after dividend)	1.84
Premium to Equity Ratio (after dividend)	0.31

Transparency in Government

As part of the corporate governance practices of MSF, the following is the list of the top five compensated executives / employees in the organization as well as their compensation for the year.

Laurence Hubbard	President / CEO	\$358,842
Albert Parisian	Chief Information Officer	\$242,845
Julie Jenkinson	VP – Insurance Operations	\$236,009
Mark Barry	VP – Corporate Support	\$223,040
Kevin Braun	General Counsel	\$201,350

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Report of Leadership (continued)



- ¹ **Non-admitted assets** – Under Statutory accounting standards, assets that are not readily convertible into cash and cannot be used to fulfill policyholder obligations are categorized as “non-admitted assets” and removed from the balance sheet via a direct charge to policyholders’ equity. Under GASB standards, these assets are recognized on the balance sheet subject to certain valuation allowances.
- ² **Change in investment value of bonds to fair market value** – Statutory accounting standards require investment valuation practices that differ from those required by governmental accounting standards.
- ³ **Change in investment lot inventory method** – Statutory accounting standards require investment valuation practices that differ from those required by governmental accounting standards.
- ⁴ **Change in investment value of other invested assets to equity method** – Statutory accounting standards require investment valuation practices that differ from those required by governmental accounting standards.
- ⁵ **Change in allowance for doubtful accounts** – Governmental accounting standards regarding accounts receivable require an assessment of collectability and the establishment of an allowance for doubtful accounts on the balance sheet. Statutory accounting standards require doubtful accounts to be charged directly against the income statement.
- ⁶ **Effect of differences in pension accounting standards on income and policyholders’ equity** – Governmental pension accounting standards (GASB 68) require recognition of an allocation of the state’s unfunded retirement plan liability at the agency level. Under SAP, the recording of a portion of the unfunded liability is not required for a reporting entity who participates in a plan sponsored by another entity, but is not directly liable for the obligations under the plan (SSAP No. 102 paragraph 86); however, the amounts contributed to the plan by MSF are recorded as expense in the current period.
- ⁷ **Effect of differences in OPEB accounting standards on income and policyholders’ equity** – Governmental postemployment benefit accounting standards (GASB 75) require recognition of an allocation of the state’s Other Post-Employment Benefit liability at the agency level. Under SAP, the recording of a portion of the liability is not required for a reporting entity who participates in a plan sponsored by another entity, but is not directly liable for the obligations under the plan (SSAP No. 92 paragraph 100).

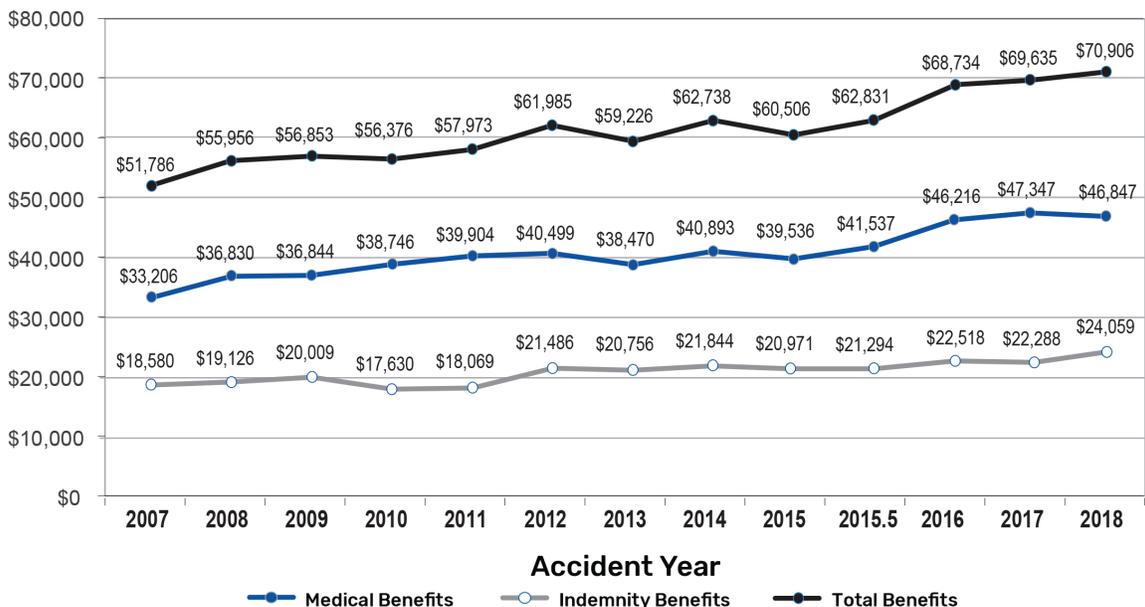
Financials



Being regulated by the Montana State Auditor's Office (SAO) Commissioner of Securities and Insurance (CSI), MSF annually files audited financial statements and all other required reports and documentation and had a financial examination completed by SAO. The MSF Board of Directors (Board) approved rate reductions of 8% for policies effective July 1, 2018, and further reductions of 8.6% were approved by the MSF Board, which were effective July 1, 2019. During 2018, the Board of Directors declared that a \$40 million dividend be returned to 95% of policyholders. Since 1999, MSF has returned a total of \$256 million to policyholders through dividends. During the 2017 Special Legislative session, Senate Bill 4 was passed and signed into law, which required MSF to transfer \$28.3 million of MSF equity in two transfers – \$14.7 million and \$13.6 million in 2017 and 2018, respectively, to the State of Montana Fire Suppression Fund. After issuance of the dividend and accounting for the 2018 transfer, MSF recorded a net loss of (\$5.97) million for 2018. A group of MSF policyholders has brought suit against the State of Montana arguing the legislation is in violation of state law and contract. This legal action has not yet been decided by the courts. Despite decreasing claim benefit costs and continued strong investment market returns, MSF policyholder equity decreased to \$512.5 million. MSF's strong financial condition enhances the financial performance of many Montana businesses; its admirable financial condition strength allows MSF to offer efficacious safety programs and training, stable year-to-year costs for their workers' compensation coverage, and dividends rewarding policyholders for safe workplaces.

Average Cost Per Wage-Loss Claim

MSF Appointed Consulting Actuary, Willis Towers Watson has found that the average wage-loss claim currently costs an estimated \$71,000, although the most catastrophic of claims can cost several million dollars. Approximately 70% of workers' compensation claim costs are for medical services, which are 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 3% per year after HB334 benefit reforms were enacted in 2012.

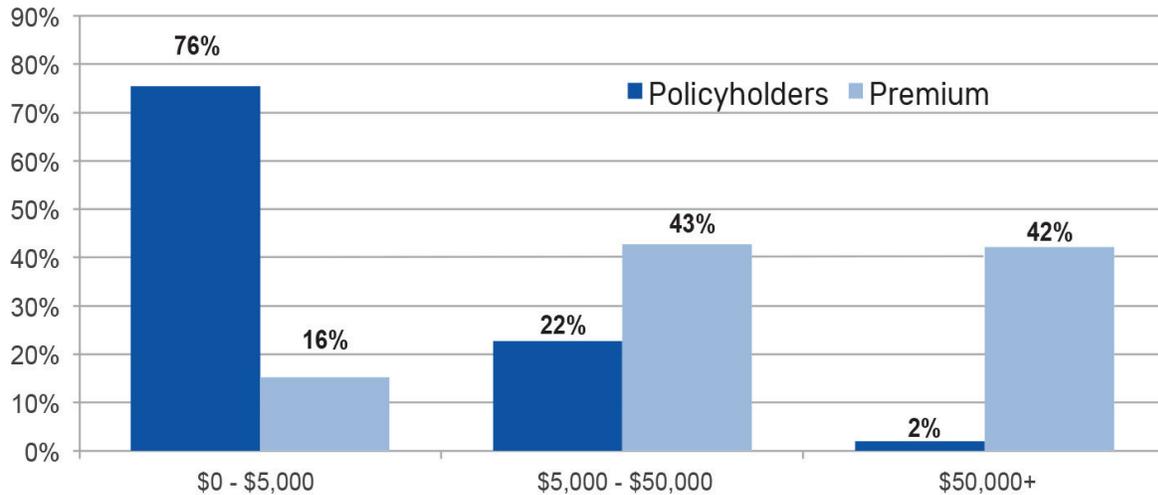


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Financials (continued)

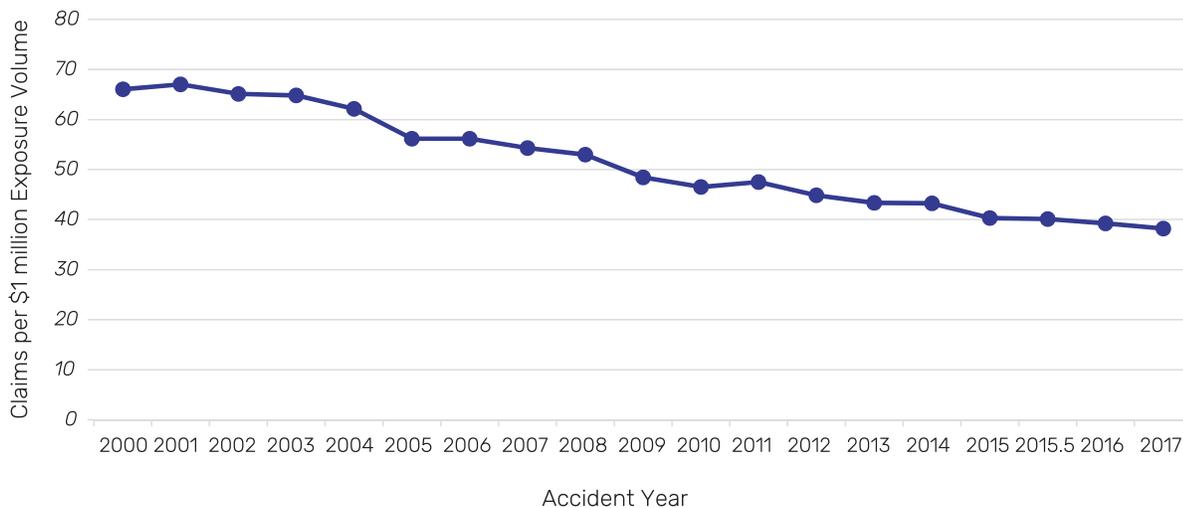
MSF Book by Account Size

MSF predominately serves small employers in Montana which often do not 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 large account employers that choose to insure with MSF, creates economies of scale and reduces financial variability, benefiting all Montana employers regardless of size).



MSF Claim Frequency Rate

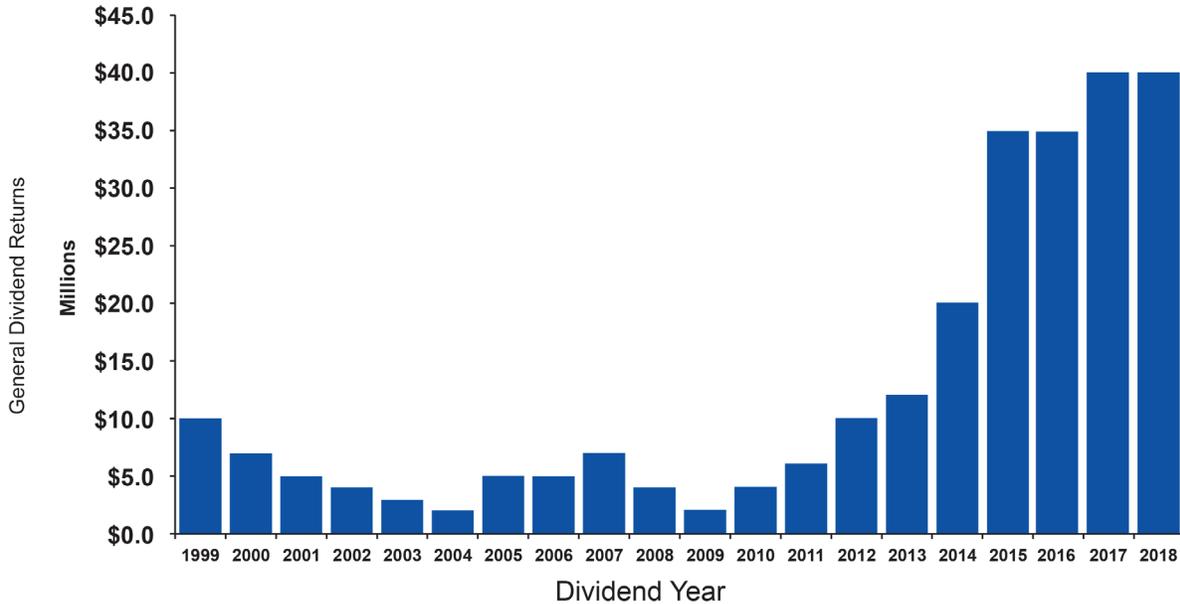
MSF total claim frequency has declined by 3% per year over the past decade. The National Council on Compensation Insurance (NCCI) has found a general pattern of declining workers' compensation claim frequency throughout the country. NCCI research suggests that innovations which improve labor productivity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



Financials (continued)

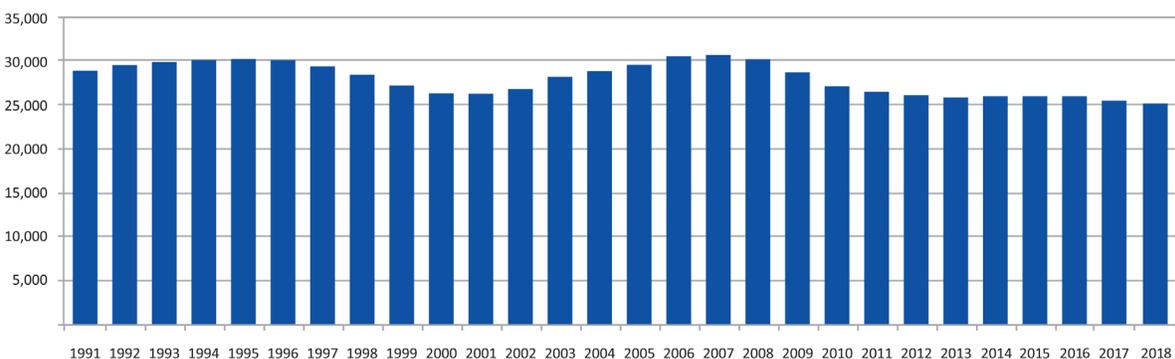
MSF Dividend and Premium Returns

MSF has returned a total of \$256 million to policyholders through dividends which have been declared and distributed every year since 1999. Primarily as a result of interest income and stock market gains, MSF recently declared a record \$40 million dividend to its customers who had policies in Policy Year 2016. 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. While dividends are not guaranteed, typically 95% of MSF policyholders have received a dividend. Dividends are an effective incentive for workplace safety.



MSF Policies Written

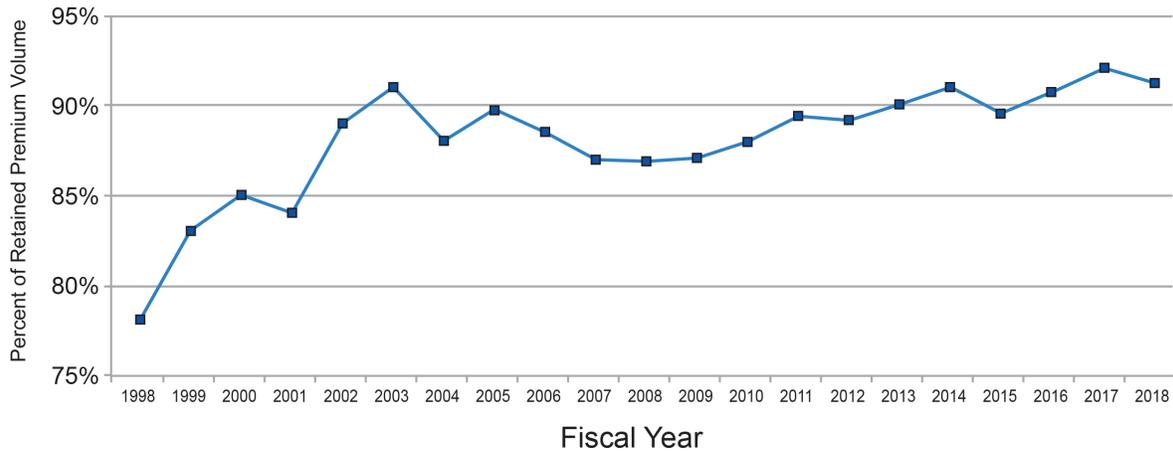
Since the inception of the Montana State Fund in 1990, private carriers have variously expanded and contracted their written workers' compensation insurance volumes in Montana, depending on the business conditions at the time. General economic conditions also affect the number of insured employers. As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



Financials (continued)

MSF Premium Retention Rate

In the “soft” market conditions of the late 1990s, MSF’s retention of written premium was relatively low by industry standards. However, in the last few years as market conditions have changed and MSF has established itself as the industry leader in service and as the carrier of choice in Montana, MSF’s retention of written premium has dramatically improved. In recent years, MSF has retained more than 90% of its policyholders from year-to-year, based on premium dollars.



MSF Rate Level

MSF manual rate levels rose in the early 2000s due to increasing medical costs and statutory and judicial benefit expansions. Rate levels have decreased since 2007, particularly as a result of legislative benefit level reforms enacted through HB334 in 2012. MSF rates effective July 1, 2019 are 47% below 2007 rates. Currently, MSF rates are the lowest rates ever in the history of the Montana State Fund.

