



ANNUAL BUSINESS PLAN

January 1, 2016 through December 31, 2016



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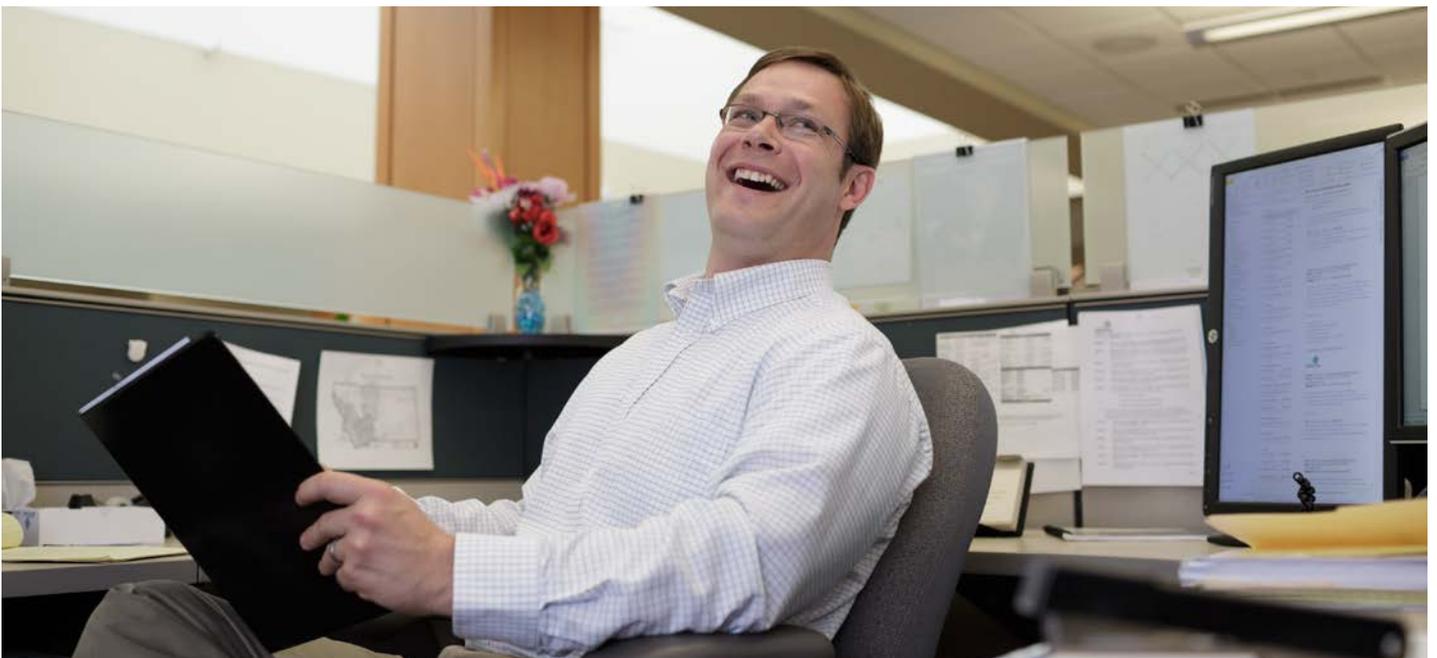
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FROM THE PRESIDENT ...

Effective January 1, 2016 Montana State Fund evolves from legislative oversight to regulation under Title 33, Montana Insurance Code. This puts Montana State Fund substantially in line with other insurance carriers in Montana, and will increase confidence in our stakeholders and the legislature in the conduct of Montana State Fund insurance operations and functions.

The regulation implementation is a significant undertaking for the company and requires technical and operational resources. I am pleased at the progress we have made the past six months. A cooperative effort between Montana State Fund and State Auditor's Office has helped establish expectations and a positive working relationship. We have completed both business process and system changes necessary to meet the January 1, 2016 effective date and we will continue additional transition activities throughout the year.

The Title 33, Montana Insurance Code implementation is organized into four projects; ensuring we manage related activities to successful completion through a team of internal experts and consulting resources where required. The Executive Team will continue to receive regular insight into overall progress through our established project management oversight process. It is my commitment that our internal and external stakeholders will be kept up to date on developments and that Montana State Fund minimizes any inconvenience to customers.

Another important initiative in our business plan is the first phase of a multi-year project to replace our Policyholder System (PHS). While PHS has served us well since 1997 it is built on aging technology and presents integration challenges with modern systems. Replacement of this core application was not a hasty decision. In fact, we completed initial market research in 2014 and have talked about this need as a team for several years. As we are now faced with new business requirements based on regulation compliance this is an appropriate time to begin the project.

The immediate effort to implement regulation under Title 33, Montana Insurance Code in no way overshadows our focus on workplace safety. Montana State Fund provides a multifaceted approach to accident prevention including policyholder visits from Safety Management Consultants, Worksafe Champions program, free safety workshops, return to work resources, and our safetmt.com and nojack.net (young worker specific) websites. Decreasing accident frequency in Montana remains a priority goal for Montana State Fund. These resources provide Montana businesses with informative and practical safety education and working together we can help meet that goal.

Much work is ahead of us – yet this organization has been here before. We have successfully navigated change be it economic, legislative, legal, or organizational many times in the past. I believe our employees are creative, committed, and proud of the purpose we serve. There is no doubt in my mind this team will tackle the challenges head on, embrace the opportunity regulation provides, and successfully evolve Montana State Fund to this new environment.

Sincerely,
Laurence A. Hubbard
President / CEO

“Decreasing accident frequency in Montana remains a priority goal for Montana State Fund. These resources provide Montana businesses with informative and practical safety education and working together we can help meet that goal.”

EXECUTIVE SUMMARY

In calendar year 2016 Montana State Fund (MSF) continues implementing changes to business process and systems, as well as monitoring accuracy of the work already completed to effectively meet regulation requirements under Title 33, Montana Insurance Code.

Four projects organize this work. Preparation for financial and market conduct exams begins in earnest in calendar year 2016 and work continues on process changes not required for January 1, 2016 implementation. A second project will monitor and ensure accurate reporting based on the changes completed in December, 2015 to move financial reporting and related business processes from a July 1-June 30 period to a January 1-December 31 period. A third project coordinates activities for compliance with specific areas of Title 33, Montana Insurance Code such as timely rate filing, eliminating class code differences, approval of MSF forms not approved by December, 2015, and implementing transition plan required portions of the NCCI basic manual in our systems. The MSF Executive Team is committed to consistent and regular communication regarding the changes this new regulatory environment brings for all employees and stakeholders. The last project ensures change is managed with effective communication and support to our employees, our customers, and other stakeholders during the first year under Title 33, Montana Insurance Code.

The final business plan project is phase one of a multi-year effort to replace our 1997 Policyholder System (PHS) application. Year one work includes developing high-level requirements and completing the RFP process for application and vendor selection.



ENTERPRISE-WIDE INITIATIVES:

1) Customer Service

- We continue the first phase of a multi-year project to replace our legacy policy handling and billing system. The new systems will provide easy access to modern workers' compensation insurance policy products and features as well as accommodate regulatory environment requirements.

2) Infrastructure

- Montana State Fund continues implementing requirements of regulation under Title 33, Montana Insurance Code effective January 1, 2016. Projects to change business processes and systems continue in calendar year 2016 to ensure we effectively meet regulatory oversight requirements.

STRATEGIC FRAMEWORK

MISSION – *Montana State Fund is Montana's insurance carrier of choice and industry leader in service.*

VISION – *Montana State Fund is committed to the **health and economic prosperity** of Montana through **superior service, leadership and caring individuals** working in an environment of **teamwork, creativity and trust.***

GUIDING PRINCIPLES

Integrity and Ethical Conduct

In the course of providing superior service to our policyholders, their injured employees, and insurance producers, we conduct ourselves with honesty, consistency, and transparency.

Customer Focus

Enhance and maintain a partnership with stakeholders in the true spirit of cooperation and collaboration. Enter into strategic partnerships where appropriate to enhance the service and products we provide our customers. Educate stakeholders on the economic and human impacts of the Montana workers' compensation system.

Financial Strength

Set adequate rate levels to maintain financial strength and stability. Operate to ensure long-term viability and financial solvency.

Offer Quality and Competitive Insurance Products

Deliver high quality products to Montana businesses at the lowest possible cost consistent with sound insurance principles. Foster and support a competitive insurance market in Montana. Function like a private insurer, offering a competitively priced product based upon actuarially sound rates while still fulfilling our role as the guaranteed market.

Employee Growth and Development

Provide a performance-driven culture that is conducive to the growth and development of our employees. Promote a customer-focused, team oriented, high performance environment that empowers, challenges, and rewards our employees.

Continuous Improvement

Dedicate ourselves to identify and implement new and better ways to efficiently and effectively operate and improve customer service.



KEY SUCCESS MEASURES

CY 2016 Key Success Measures

The following objectives represent the corporate level success measures that allow us to gauge our financial and enterprise progress. We have incorporated five financial measures and one multi-faceted qualitative measure that, combined, define success for Montana State Fund.



- 1) Achieve targeted Net Operating Income before dividend of \$27.3 M
- 2) Achieve total Net Earned Premium of \$162.0 M
- 3) Achieve Loss Ratio of 78.6%
- 4) Maintain Expense Ratio of 28.6% or less
- 5) Achieve Investment Income (including realized gains on investments) of \$44.1 M
- 6) Achieve Enterprise-Wide Initiatives

ENTERPRISE-WIDE INITIATIVES

Enterprise-wide initiatives are critical elements for the continued success of Montana State Fund. They are supported by a number of multifunctional efforts composed of key performance indicators and success measures to ensure we accomplish our objective. In addition, they support our Mission, Vision and Guiding Principles.

1. CUSTOMER SERVICE

We continuously look for ways to enhance our service as part of our commitment to our policyholders, their employees, and workers' compensation system stakeholders.

KEY PERFORMANCE INDICATORS

Policy and Billing System Replacement – Engage stakeholders in this first phase to produce high level requirements based on improved understanding of the regulatory environment and other relevant system decisions. Release the request for proposal for systems replacement.

Success Measures:

Policy and Billing System Replacement

1. Release request for proposal for policy and billing system replacement by September 30, 2016.

2. INFRASTRUCTURE

January 1, 2016 Montana State Fund begins regulation under Title 33, Montana Insurance Code - the same as all other insurance companies licensed to conduct business in Montana. This change ensures MSF is structured to best serve Montana businesses and their employees into the future under sound insurance principles.

Four projects coordinate the regulation implementation work.

KEY PERFORMANCE INDICATORS

Regulation – This project includes the activities to ensure our quarterly financial reports are successfully completed under the new regulatory structure as well as the training and preparation for financial and market conduct examinations expected to begin in 2017.

Success Measures:

Regulation

1. Complete quarterly financial report filings by May 15, 2016, August 15, 2016, and November 15, 2016.
2. Contract with regulation and/or examination consultants for training to occur through June 30, 2017.

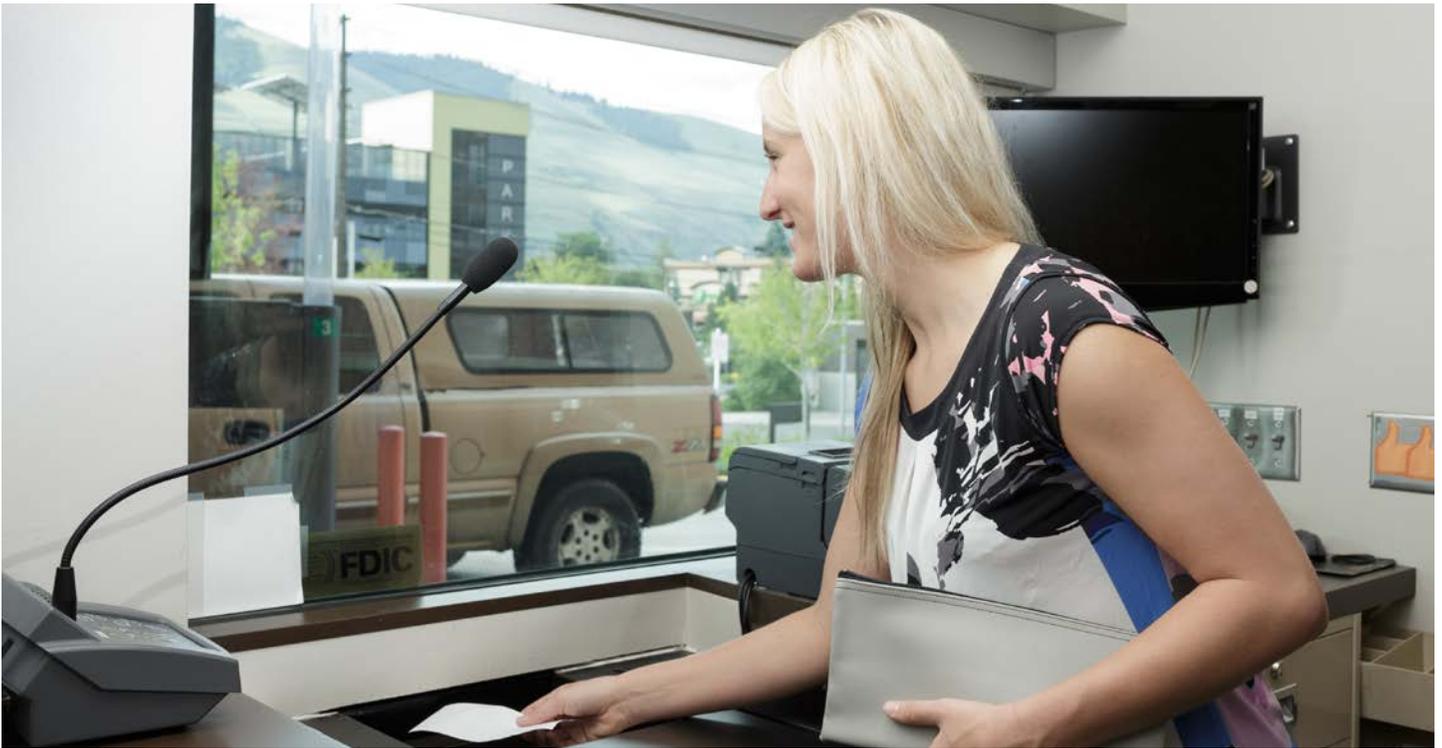


Calendar Year Conversion – This project implements changes to Montana State Fund systems, processes, contracts, and reports as well as changes to our interactions with several State agencies to effectively transition from a July 1-June 30 fiscal year reporting period to a January 1-December 31 calendar year reporting period to align with insurance regulation.

Success Measures:

Calendar Year Conversion

1. The Montana State Fund budget process is converted to a calendar year basis to track the approved calendar year budget and record financial and budget transactions on that basis beginning January 1, 2016.
2. The Montana State Fund financial reporting process is converted to allow financial reporting on the Governmental accounting basis and the Statutory accounting basis to meet financial reporting requirements beginning May 15, 2016 and to ensure preparation and completion of the annual financial statements as of December 31, 2016.



Rates and Rate Filing – This project ensures Montana State Fund is compliant with rate-related areas of the Montana Insurance Code and includes: eliminate classification code differences between MSF classification codes and the NCCI classification codes, implement transition plan specified provisions of the NCCI Basic Manual, prepare and submit MSF forms to State Auditor’s Office for approval, and comply with rate filing requirements.

Success Measures:

Rates and Rate Filing

1. Policy system changes, business rule changes, and necessary training to implement the transition plan are complete and implemented by March 31, 2016 for new and renewal policies effective July 1, 2016.
2. Additional forms required by State Auditor’s Office approved by April 30, 2016.
3. Montana State Fund rates and related rate filing requirements implemented for rates for new and renewal policies effective July 1, 2016.

Change Management and Communication – This project ensures internal and external stakeholders are informed of changes affecting them as Montana State Fund is regulated under Title 33, Montana Insurance Code.

Success Measures:

Change Management and Communication

1. Regular communications regarding transition to Title 33, Montana Insurance Code.
 - a. Montana State Fund employee communication plan:
 - i. Monthly communications through March, 2016
 - ii. Quarterly communications April – December, 2016
 - b. Montana State Fund external stakeholders communication plan:
 - i. Quarterly communications through March, 2016
 - ii. Communication at least once from April – December, 2016

ORGANIZATIONAL PROFILE

The state of Montana originally established the predecessor to Montana State Fund (MSF) in 1915 to function as a competitive workers' compensation insurance carrier. Since then MSF has operated under a number of different forms, with its current structure resulting from legislative actions implemented in 1990. At that time the Legislature separated the workers' compensation regulatory function (originally established in the Montana Department of Labor and Industry) from the day-to-day insurance operations responsibilities (which were vested in a separate, new entity known as Montana State Fund). A seven member Board of Directors, appointed by the Governor, governs the operations of Montana State Fund. The Board is also responsible for appointing the President/CEO.

Montana State Fund is a self-sufficient, not for profit workers' compensation insurance carrier. Our statutory purpose is to act as a competitive insurance carrier, providing an available market and thereby guaranteeing coverage to all employers in Montana. We receive no taxpayer or general fund money, operating solely on the premium dollars paid by the insured employers and the net proceeds from our investments. We function like a private insurance carrier in a competitive marketplace and, as provided by law, perform all the functions and exercise all the powers of a private insurance carrier that are necessary, appropriate or convenient for the administration of the Montana State Fund.

MSF has undergone a number of changes since our creation in 1990. We have transitioned from a traditional organizational

structure to one that is more adapted to the demands of the information age. A comprehensive corporate re-design in 2000 enhanced our operational flexibility with the addition of multi-functional teams that are aligned with specific groups of employers. This change resulted in a "flatter" organization that increased employee empowerment and allows us to work more closely with our policyholders and their injured employees. We continue to strive to improve efficiencies in all operational areas and have made a major investment in our safety, nurse case management, and provider relations services. We work diligently with Montana employers to develop accident prevention programs yet recognize that accidents will still occur. When an injury does occur on the job, we have resources to assist with appointments, understand medical issues and treatment process, and work with provider offices to ensure ease of documentation.

The 2015 legislature passed legislation to move Montana State Fund under regulation by the State Auditor's Office and Title 33, Montana Insurance Code. We see this latest evolution in our oversight as continued opportunity to preserve our financial strength and remain a stable partner with Montana business.

As our state's economic structure continues to evolve, we stand ready to fulfill our critical role as the guaranteed workers' compensation market for all Montana employers.



CY 2016 FINANCIAL PROJECTIONS

Projected Results of Operations Montana State Fund

Statutory Basis (\$000)

OPERATING STATEMENT

	ACTUAL FY14	ACTUAL FY15	PROJ FY15.5	PLAN CY16	PROJ CY17	PROJ CY18
Premium Income	\$165,272	\$164,557	\$82,932	\$162,010	\$167,042	\$171,189
Investment Income	56,738	50,708	19,880	44,147	45,234	46,345
Other Income	(4,375)	(4,064)	(2,173)	(5,128)	(5,685)	(6,279)
Total Losses and Expenses	163,889	127,761	83,519	173,711	179,850	187,050
Policyholder Dividends	(12,003)	(20,005)	(35,000)	TBD	TBD	TBD
Net Income	\$41,743	\$63,435	(17,880)	\$27,319	\$26,741	\$24,206

TBD - Future dividends to be determined by Board of Directors

Premium to Surplus (X:1)*	0.37	0.32	0.17	0.30	0.30	0.29
Loss Reserves to Surplus (X:1)*	2.08	1.73	1.85	1.71	1.63	1.58
Combined Ratio	99.2%	77.6%	100.7%	107.2%	107.7%	109.3%
Dividend to Premium Ratio	7.3%	12.2%	42.2%	TBD	TBD	TBD
Operating Ratio	78.9%	62.0%	81.3%	86.2%	86.5%	87.7%

*Prior to dividend declaration

BALANCE SHEET

	ACTUAL FY14	ACTUAL FY15	PROJ FY15.5	PLAN CY16	PROJ CY17	PROJ CY18
Total Assets	\$1,671,110	\$1,659,647	\$1,590,392	\$1,676,390	\$1,728,074	\$1,778,998
Unpaid Loss and LAE	\$924,598	\$895,543	\$904,117	\$908,817	\$917,558	\$928,310
Other Liabilities	302,660	247,199	198,396	234,944	248,720	263,434
Total Liabilities	\$1,227,258	\$1,142,742	\$1,102,513	\$1,143,761	\$1,166,279	\$1,191,744
Surplus	\$443,852	\$516,905	\$487,879	\$532,629	\$561,796	\$587,255