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Glossary of Terms

Net Earned Premium

Premium is earned over the term of the policy. This number represents the proportionate amount earned (exclusive of reinsurance) within the fiscal year.

Investment Income

Investment returns (including realized capital gains) minus investment expenses.

Net Operating Income (NOI)

Net earned premium + net investment income + other income/expense minus losses and expenses. If a dividend is declared, it is subtracted from the NOI.

Underwriting Income

Income resulting from insurance operations. Net earned premium minus losses and expenses incurred.

Fiscal Year Loss Ratio

Accident Year incurred losses divided by net earned premium. Expressed as:

$$\frac{\text{Paid dollars} + \text{reserve amounts} + \text{any changes to incurred losses in prior accident year periods}}{\text{net earned premium}}$$

Expense Ratio

Fiscal year expenses divided by net earned premium. A higher ratio indicates less operating efficiency as more premium dollars are used for underwriting activities and claims administration. Expressed as:

$$\frac{\text{Allocated loss adjustment expense (ALAE)} + \text{Unallocated loss adjustment expense (ULAE)} + \text{Acquisition expense (commissions and incentives)} + \text{General expenses}}{\text{Net earned premium}}$$



From the President . . .



The adage that there is no “I” in Team is especially relevant at Montana State Fund. In fact, our entire business philosophy and vision are modeled on employees working in an environment of teamwork, creativity and trust. Our strategic planning process is no different.

To be a winning team, you can’t just go out on the field and play ball. It takes months of practice and conditioning to develop a cohesive game plan which ultimately leads to victory. Our leadership team used this approach in formulating our FY07 Strategic Business Plan. Through months of calculated planning, discipline and open, honest discussion, we have created a strategic plan that is not only realistic and measurable, but also challenges each of our employees to stretch his/her talents and performance level for the benefit of our customers. Our initiatives establish a benchmark that ensures Montana State Fund offers the highest quality workers’ compensation insurance to Montana businesses at competitive prices and instills pride in our staff members.

The priorities laid out in our FY07 Strategic Plan build upon our consistent, sustained performance of the past with an eye towards the future. Several initiatives retain continuity with prior year plans and build upon our long-term efforts. This year’s Strategic Plan challenges us to enhance external and internal customer service as well as capitalize on our investment in efficient, cost-effective, claim management. In addition, we will be initiating improvements to our data warehouse to provide management reporting capability on critical business metrics. In all, these initiatives will strengthen our organization and position us to meet our ever-changing business climate.

I am confident that the financial targets that we have set forth in this plan are realistic and attainable, and will provide winning results. We fully realize that we must have you, our stakeholders, on our team in order to achieve our goals. My staff and I look forward to working with all of you in the coming year, and appreciate your ongoing support of our organization as we continue to provide unmatched workers’ compensation insurance for the people of Montana.

Sincerely,

A handwritten signature in cursive script that reads "Laurence Hubbard".

Laurence Hubbard
President and Chief Executive Officer

Executive Summary

Montana State Fund continues to operate in a very dynamic and competitive environment. Our future success is dependent upon our ability to anticipate changing market conditions and to react in an appropriate manner. We will utilize all the resources at our disposal to build upon past successes to maintain a strong, viable and stable workers' compensation market for Montana businesses.

The strategic objectives outlined in this plan focus on those elements that enhance the satisfaction level of all the customers we serve and, at the same time, allow us to deliver our services in the most efficient and cost-effective manner. Furthermore, we have established specific financial targets that quantify the results of our efforts in a very tangible and meaningful way. The strategic priorities identified in our new plan build upon the foundation we have laid out in previous plans. We are focusing on operational improvements that will boost our efficiency and enhance customer service, as well as targeting specific financial success measures. Together, these initiatives will serve to strengthen our organization, and will position us to meet the challenges that lie ahead.

Our Enterprise-Wide Initiatives for FY 2007 are:

1) Focus on Employee Satisfaction

Create and nurture an environment where employees are recognized as our most valuable asset.

2) Focus on Customer Satisfaction

Address the needs, wants and expectations of all customers by providing superior service in every area of our organization.

3) Establish Standards as “Best in the Industry” Relative to Claim Handling and Resolution

Improving claim handling will result in better outcomes for employers and their employees and help to reduce costs system wide.

4) Provide the Appropriate Infrastructure to Realize the Montana State Fund Vision

Ensure that Montana State Fund employees have the necessary tools available to do their job efficiently and effectively.

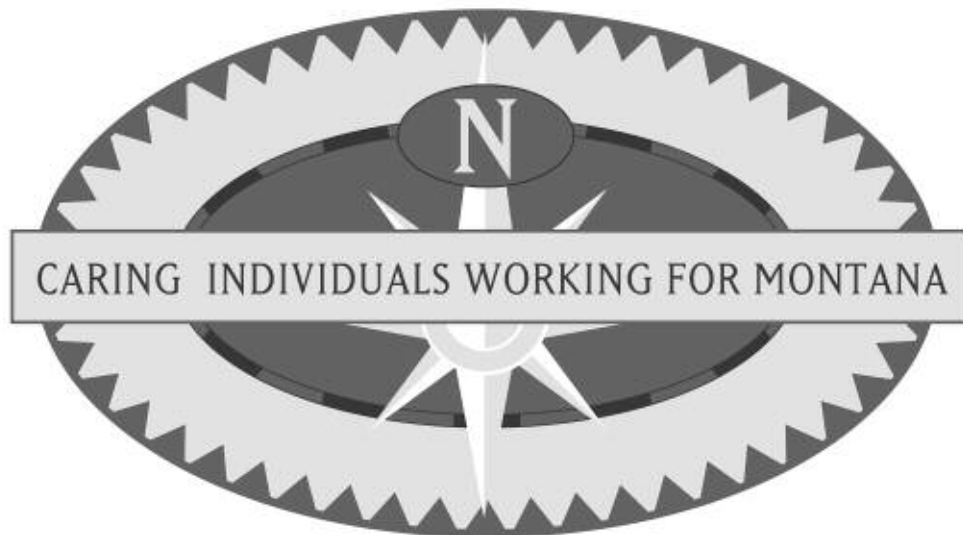
Mission

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**.

Strategic Framework



Guiding Principles

Integrity and Ethical Conduct

In the course of providing superior service to our policyholders, their injured employees, and insurance producers, we will conduct ourselves ethically and with the highest degree of integrity.

Customer Focus

Enhance and maintain a partnership with stakeholders in the true spirit of cooperation and collaboration. Enter into strategic partnerships where and when they provide value added to the service and products we offer our customers.

Strong Financial Position

Set adequate rate levels to maintain financial strength and stability, ensuring 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. MSF functions 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 within a continually improving work atmosphere that is conducive to the personal and professional growth and development of our employees. Promote a customer-focused, team-oriented, high-performance environment that empowers, challenges, rewards and satisfies our employees.

Strategic Framework/Key Success Measures

FY 2007 Key Success Measures

Key Success Measures are the goals/objectives established for fiscal year 2007. They represent **S-M-A-R-T** goals in that they are **S**pecific, **M**easurable, **A**ttainable, **R**ealistic and **T**imely.

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

- 1) Achieve targeted FY Net Operating Income before dividend of \$12.8 million
- 2) Achieve total Net Earned Premium of \$214.4 million
- 3) Achieve Fiscal Year Loss Ratio of 87.6%
- 4) Maintain Expense Ratio of 25.8% or less
- 5) Achieve Investment Income of \$35.5 million
- 6) Achieve Enterprise-Wide Initiatives



Enterprise-Wide Initiatives

Enterprise-wide initiatives are a critical element for the continued and sustained success of Montana State Fund. They are supported by a number of multi-functional efforts (most often initiative-based) comprised of key performance indicators that are measurable, ensuring the accomplishment of our stated goals/objectives.

1) Focus on Employee Satisfaction

Assemble a singularly focused group of individuals that embody the Montana State Fund Vision/Mission. Through their dedication and by their efforts, they will challenge themselves and their colleagues to be the best, personally and professionally, and be recognized and rewarded for doing so.

Key Performance Indicators/Functional Support

Career Development
Employee Opinion Survey Follow-Up
Succession Planning
Training

2) Focus on Customer Satisfaction

Listen to our customers and understand their needs. By fulfilling these needs, transform our customer base from users of our products and services into advocates for Montana State Fund, thereby, solidifying our position as **insurance carrier of choice** for Montana businesses.

Key Performance Indicators/Functional Support

Customer Focus Recognition/Reward
Customer Service Training
Young Workers Safety Awareness Program (safetyrocks.us)

3) Establish Standards as “Best in the Industry” Relative to Claim Handling and Resolution

Apply a compartmentalized, multi-disciplined approach to the claim resolution process, allowing for an unbiased, fact-based appraisal of our current state capabilities and performance, identifying areas for improvement.

Key Performance Indicators/Functional Support

Claim Center Upgrade
Legal/Legislative Involvement
Performance Metrics
Training

Enterprise-Wide Initiatives

4) Provide the Appropriate Infrastructure to Realize the Montana State Fund Vision

Provide the appropriate working environment and the necessary technology and tools that will allow the employees of Montana State Fund to service their customers effectively and efficiently.

Key Performance Indicators/Functional Support

Administrative Support Systems

Business Intelligence

Physical Plant



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 taken 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, increasing employee empowerment, allowing 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 management services, working diligently with Montana employers in developing accident prevention programs. As our state's economic structure continues to evolve, we stand ready to continue filling our critical role as the guaranteed workers' compensation market for all Montana employers.



Financial Projections

PROJECTED RESULTS OF OPERATIONS MONTANA STATE FUND

Statutory Basis (\$000)

Operating Statement	Actual	Estimate	Plan	Projection	
	2005	2006	2007	2008	2009
Premium Income	\$189,379	\$211,888	\$214,400	\$223,359	\$234,119
Investment Income	29,125	31,640	35,500	40,172	45,301
Other Income	(298)	(2,218)	(2,353)	(2,451)	(2,569)
Total Losses & Expenses	194,370	222,978	234,696	239,375	247,434
Policyholder Dividend	5,004	5,000	TBD	TBD	TBD
Net Income	\$18,832	\$13,332	\$12,851	\$21,705	\$29,417

TBD - Future dividends to be determined by Board of Directors

Premium to Surplus Ratio (X:I)*	1.23	1.21	1.14	1.03	0.92
Loss Reserve to Surplus Ratio (X:I)*	3.34	3.30	3.42	3.24	3.00
FY Combined Ratio (Loss+LAE+U/W)	102.64%	105.23%	109.47%	107.17%	105.69%
Dividend to Premium Ratio	2.64%	2.36%	TBD	TBD	TBD

* - Ratios prior to any dividend declaration

Balance Sheet

Total Assets	\$801,824	\$869,119	\$953,296	\$1,042,412	\$1,138,037
Unpaid Loss and Loss Adj. Exp.	511,558	578,942	644,079	703,822	761,568
Other Liabilities	141,912	119,645	120,818	121,558	122,471
Total Liabilities	\$653,470	\$698,587	\$764,897	\$825,380	\$884,039
Surplus	\$148,354	\$170,532	\$188,399	\$217,032	\$253,998
Total Liabilities and Surplus	\$801,824	\$869,119	\$953,296	\$1,042,412	\$1,138,037

Montana State Fund Board of Directors

Ed Henrich, Chairman
Fairmont

Mardi Madsen
Billings

Jane DeBruycker
Dutton

James Swanson
Glendive

Joe Dwyer
Billings

Lawrence Zanto
Helena

Ken Johnson
Missoula



iBurn
Unless I'm always thinking about workplace safety

Register to win an iPod @ safetyrocks.us

STATEFUND

The advertisement features a silhouette of a person in a hard hat holding a flaming object. The background is dark grey.



iSlip
Unless I'm always thinking about workplace safety

Register to win an iPod @ safetyrocks.us

STATEFUND

The advertisement features a silhouette of a person slipping on a banana peel. The background is dark grey.



iCrash
Unless I'm always thinking about workplace safety

Register to win an iPod @ safetyrocks.us

STATEFUND

The advertisement features a silhouette of a person crashing into a steering wheel. The background is dark grey.