



Frequently Asked Questions about the Montana State Fund legislative initiative

What is the purpose and reason behind this initiative?

When the 1989 legislature initially structured the Montana State Fund it envisioned that we would be structured as a self supporting, nonprofit, independent corporation of the state of Montana to provide employers a competitive option for workers' compensation insurance coverage. The financial issues facing the state fund in 1990 resulted in legislative modifications intended to address those issues. Over the past decade, MSF has focused its energies and resources to create a strong and stable workers' compensation system in Montana, providing businesses with a reasonable alternative for this mandatory coverage. We are now approaching the legislature and asking them to recognize that the operation of a competitive state fund is a unique activity for state government and that a public corporate structure, rather than that of a state agency, will best enable the Montana State Fund to be managed and operated in an entrepreneurial and business-like manner, assuring long term financial and operational stability. The benefits derived will include:

- ❑ Operational flexibility to allow MSF to respond to the needs of Montana businesses.
- ❑ Having MSF regulated in a manner consistent with other insurance carriers, creating a more level playing field.
- ❑ Bolstering the state's economic development plan by creating a structure that can respond quickly to changing market conditions and the needs of Montana's existing or prospective employers.
- ❑ Ensuring that operational reserves will be protected for the benefit of employers and employees in the state.

Over the past 15 years, 9 states have established independent state funds, similar to what we are proposing. A number of other states have made changes to the more traditional state funds giving them the tools necessary to operate in this dynamic milieu. Montana State Fund is different from other state agencies in that we are not funded by taxpayer dollars, and we are an insurance company conducting business in a very competitive market. We are seeking authority to operate accordingly in the best interest of Montana.

Why is there a Montana State Fund?

Nationally, state legislatures have provided for a guaranteed market for workers' compensation insurance (which is a mandatory line of coverage) as follows:

State Monopoly: All coverage is provided by a state agency (State Fund). There are no private underwriters and no competition. This is the system in use by the states of Washington, Wyoming, North Dakota, Ohio, and West Virginia.

Assigned Risk: There are a number of instances in which insurances carriers for a variety of reasons reject both small and large businesses for workers' compensation coverage. When an employer cannot get coverage, they are put into the assigned risk pool and they



are assigned to an insurance company. Assigned risk pools are generally unpopular with private sector carriers. During the last workers' compensation crisis in the U.S. (late 1980s-early 90s) legislatures in a number of states determined that the assigned risk approach was not viable due to private carriers leaving the market. To take their place, they created competitive State Funds that operate like domestic mutual insurance companies and not as state agencies.

A competitive state fund: This is the system in use in a number of states, including Montana, which gives employers three options for purchasing their insurance:

- ❑ From a private company
- ❑ Develop a self insurance program
- ❑ From Montana State Fund

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 pricing that can be as low as prudently possible. While MSF does not pay taxes, we must serve as the guaranteed market for Montana businesses and cannot refuse to insure except for non-payment of premium. We cannot leave the state when there are adverse market conditions or write other lines of commercial coverage's allowing us to spread out our risks. Our presence in the marketplace serves as a check on prices. A strong Montana State Fund protects the businesses in our state, both small and large, by providing stability and options in this mandatory line of insurance.

Unlike 1989, there is no crisis with workers' compensation in Montana. Why do we need to do this now?

It is imprudent to wait for a crisis to occur before making structural improvements. A well-run organization is constantly fine tuning itself, responding to the current and anticipated market environment. Among those states that have a state fund, most have taken the step to create or restructure their state fund to meet the challenges of the 21st century. Montana needs to be properly positioned to maintain our competitiveness in the marketplace.

What tie is there to this legislation and the Governor's economic development plan?

A viable, competitive and dynamic state fund facilitates a competitive market for workers' compensation insurance. This is a benefit to any employer doing business in Montana and ultimately to the economic competitiveness of the state. Our proposal fits within the scope of the Governor's economic development initiative to streamline the public sector, becoming more responsive and partnership oriented.

When the legislature created a workers' compensation system in 1915, the goal was to ensure that all Montana workers were insured against on-the-job injuries. Today, MSF is still the only guarantor of that promise. Without MSF, many businesses with employees in



high-risk fields, new start-up businesses, and many small businesses would be saddled with exorbitant workers' compensation insurance costs. Some businesses would cease to exist, simply because they couldn't find insurance at any price. Such an environment would threaten existing businesses and stifle the creation of new ones.

In the early 1990s Montana businesses paid high premiums for workers' compensation coverage because MSF was not yet in the position to offer competitive rates. A stable, financially strong state fund has been an important factor over the years in reducing rates. While premiums will fluctuate due to economic and market conditions, MSF's sole purpose is to provide a stable source of insurance coverage, thus protecting employers from market uncertainties.

MSF reports a surplus in its financial statement. Why shouldn't those funds be returned to the state?

When an insurer reports a surplus, they are not talking about unneeded or excess funds. A surplus is in actuality a contingent liability fund, and is intended to assure that the insurer will be able to fulfill its obligations to policyholders and injured employees. These funds should only be spent for the purposes for which they were collected. In the insurance business, premiums are established long before the number, severity, duration, or cost of claims can be known. Case and actuarial reserves are established as claims occur, but the ultimate cost of those claims is not known for many years, sometimes taking as long as 35 to 40 years. Catastrophic and/or unanticipated events may also occur which are not covered by annual premiums. Because of this, insurance is quite different from all other goods and services where the price is established after most costs of production and delivery are known. A surplus that is based on sound industry standards helps to stabilize costs to business, thereby fostering regional economic competitiveness for Montana employers. MSF's surplus exists to protect against normal financial variations, loss development and unanticipated events. **The investment return on surplus is a key factor in the pricing of insurance policies for businesses in Montana. Any reduction in surplus translates to an increase in pricing for insured businesses.** The tragic events of 9/11 make it painfully clear that catastrophic losses can occur at any time, resulting in significant claims. A responsible insurance carrier needs to be prepared for any eventuality. When reserves are adequate and results are positive, an insurance company can declare a dividend to return unneeded funds to their customers. In the past 4 years, MSF has returned over \$28 million to our policyholders, resulting in a positive impact on the Montana economy

What is a public corporation, and why should the Montana State Fund be given this status?

A public corporation is an entity that serves a public need identified by the legislature. It is a non-profit corporation that is "owned" by the state. When Montana State Fund was restructured by the 1989 legislature, it was envisioned that it would be organized along these lines. MSF has now reached a point in its evolution where it is appropriate to move



in this direction to assure longevity, with a structure and regulatory requirements that match those of other insurance companies.

MSF operates in an entrepreneurial environment. Traditional governmental regulatory structures are cumbersome for functioning in the competitive insurance industry, which require flexibility and rapid response to ever changing market conditions. We are not a regulatory agency, but an insurance company. Currently, each time MSF needs authority to more fully function as an insurance company, we need to seek legislative approval. The benefit of these changes flows directly to our policyholders. Private carriers can act based on market realities, putting us at a considerable competitive disadvantage. Operating as a public corporation, MSF would best be able to serve the people of Montana and fulfill our obligations.

What will happen to legislative oversight of MSF if this bill passes?

The legislature maintains ultimate control over MSF. We were created in statute and could be restructured or repealed if the legislature felt it was appropriate. There is no change in this regard. Our proposal requires MSF to provide the legislative and executive branch with the same information, on a regular basis, like we do today. We are asking that the Insurance Commissioner handle the authority for oversight for insurance related matters. This would put MSF in line with all the other insurance carriers that operate in our state.

Will there be an increase in rates because of these changes?

Currently all other insurance companies operating in Montana pay the premium tax into the general fund. Our proposal would make MSF similar to other carriers in this regard. We estimate the cost to businesses insured will increase by 2.75%. Nothing else in the proposal should result in increased rates.

Why should MSF be able to own its building?

Purchasing the building from the state for fair market value creates a win-win situation. For MSF policyholders, we would create an asset that further strengthens our financial stability and diversity. For the state, an estimated \$6 million would be generated for the general fund that could be used, as the legislature deems appropriate. We are asking that current law be amended to allow for the State Land Board to sell property to a public corporation if they deem it appropriate and in the best interest of the state.