



The Role of Surplus

Ultimately, surplus is intended to assure that Montana State Fund will be able to fulfill its obligations to policyholders and injured employees. It is not excess, un-needed funds. It should be viewed as policyholder's equity. Workers' Compensation insurance differs from virtually all other goods and services in that:

- ⇒ Premiums are set before the number, severity, duration, or cost of claims can be known. Actuaries are trying to predict the future based on the past when rates are set
- ⇒ The ultimate cost of claims is not known for many years.
- ⇒ Unanticipated risks (i.e. the tragic events of 9/11) can have a dramatic impact that cannot be fully funded in each year's premium.
- ⇒ Assets that are held in support of the obligations vary in value over time

The amount of surplus that an insurance company needs is based on sound industry standards and conservative accounting practices. For a workers' compensation carrier like MSF, there are several characteristics that have the potential for a greater volatility of results and require a stronger than average surplus to address these issues. These include:

- ⇒ Extremely long-term obligations associated with claims
- ⇒ MSF writes only one type of insurance in one state
- ⇒ MSF provides the guaranteed market
- ⇒ Unlike a stockholder-owned insurance company, MSF cannot access additional capital to cover adverse financial results

MSF's long-range target is to have a reserve to surplus ratio of 1.5~2.0. A strong surplus, along with adequate loss reserves, protects injured employees, policyholders, and allows Montana State Fund to continue to operate as a strong and viable insurance carrier, committed to the businesses in Montana.

Many of the problems associated with the Old Fund in the 1980s were the result of inadequate pricing and reserves. At that time private sector insurers left Montana because of these unsound practices. It took a number of years and millions of dollars to repair the damage that was done. The Montana State Fund has worked hand in hand with subsequent legislatures to ensure that this will never be repeated.