

MONTANA STATE FUND STUDY COMMITTEE

October 25, 2002

Elkhorn Room - Holiday Inn Downtown

The second Montana State Fund Study Committee Meeting was held on October 25, 2002 at the Holiday Inn Downtown, 22 North Last Chance Gulch, Helena, Montana.

Committee Members Attending

Rep. Rick Laible	Sen. Walter McNutt
Rep. Joe McKenney	Jerry Driscoll
Rep. Gary Matthews	Larry Jones
Sen. Vicki Cocchiarella	George Wood
Sen. Dale Mahlum	Angela Huschka

Others Attending

Thomas Schneider, MPEA
Jeane Carstensen-Garrett, Legislative Audit Division
Mari Gray, State Auditor
Curtis Larsen, Montana State Fund
Joe Mazurek, Crowley Law Firm
Aidan Myhre, Montana Chamber
Chuck Swysgood, Governor's Office
Kelly Jenkins, PER Board
Roger McGlenn, IIAM
Jack Morgenstern, Century Companies, Inc.
Jim Ahrens, Montana Hospital Association
Susan Knedler, Hi Heat Industries
Jill Gerdrum, State Auditor
Betsy Griffing, State Auditor
John McEwen, Dept. of Administration
Loretta Lynde, Loretta Lynde Consultant
Keith Olson, Montana Logging Association
Jason Todhunter, Montana Logging Association
Tom Horn, Montana State Fund Board
Carl Kochman, Wendt Kochman
Greg Petesch, Legislative Services Division
Pete Aspinwell, IBM
Eddie McClure, Legislative Services
Daniel Edwards, Montana Insurance Guaranty Association
Bob Biskupiak, Payne Financial Group
Shawn Bubb, Montana School Board Association
Larry Kibbee, Alliance of American Insurers
Bill Stevens, MFDA
Stuart Doggett, Lobbyist

Jacqueline Lenmark, American Insurance Association
Stacey Bird, MPEA
Jerry Keck, Dept. of Labor and Industry
Steve Bender, Department of Administration
Carl Swanson, Montana State Fund
Nancy Butler, Montana State Fund
Mark Barry, Montana State Fund
Matthew Cohn, Montana State Fund
Joanne Shydian, Montana State Fund
Kathy Gowen, Montana State Fund

Chairman Walter McNutt called the meeting to order at 10:04 a.m. There were no agenda changes and the minutes from the September 23, 2002 meeting were approved as presented.

Carl Swanson, President/CEO of Montana State Fund (MSF) provided an introduction and clarification of Montana State Fund's proposed legislation. Mr. Swanson spoke about an assigned risk pool analysis, which was completed by MSF, and referenced the summary on page 10. Montana represents 4/10ths of 1% of the market share in the nation. Montana is not a key market. Typically, when times get tough for private carriers, they retrench to protect key markets. This has been seen in Montana in the last couple of years. There are five or six carriers that were doing business here 2 years ago, that are no longer doing business. They are not doing business in Montana because of decisions made by those companies based upon regional or national reasons. There would likely be an increase in minimum premium, and prices for a large number of businesses would rise, in some cases as much as 260%, with an assigned risk pool vehicle. As an example, MSF has approximately 7,000 minimum premium customers who pay \$275 a year for their policy. In looking at assigned risk pool states, many of them are in the \$700 range. There would also be a negative impact on business and economic development in Montana. This would send the wrong signal to start up companies looking to relocate in Montana. It would also likely be a negative signal to other insurance carriers from entering our marketplace. The American Insurance Association indicated at our last meeting that those companies that are a member of the association are not in favor of an assigned risk pool vehicle in Montana. Typically, there is a stigma associated with being in a residual market mechanism or assigned risk pool. MSF estimates, based upon the National Council on Compensation Insurance (NCCI) data, that over 80% of the businesses that MSF currently insures would end up in an assigned risk pool vehicle. It would be disruptive for injured employees and policyholders because of long-term relationships that have been forged. It would also be a loss of a stabilizing force in the marketplace if MSF ceased to exist. Historically, some consider assigned risk pool mechanisms to be pass-through vehicles. There is typically a servicing carrier. The servicing carrier receives so many cents of the premium dollar for issuing the policies and settling and servicing the claims, and there is no strong incentive to provide loss control, safety, and high-quality claim management. There is not much incentive in an assigned risk pool state to provide safety workshops, such as MSF does throughout the state of Montana, free of charge.

NCCI has tried to address this issue through quality assurance, measurements and audits of companies that are servicing carriers.

Mr. Swanson also addressed MSF's top priorities for its legislative proposal. Certainly protecting the integrity of MSF's surplus or contingent liability fund is a key, number one priority. If the surplus were accessed, it would compromise MSF's ability to deal with catastrophes, and would impact bottom line pricing. There is a great deal of uncertainty in the worker's compensation business. MSF's surplus is benchmarked against industry practices. Montana needs a competitive state fund to serve the guaranteed market. However, MSF needs a structure that will allow it to manage and operate the business in an entrepreneurial and business-like fashion. There are significant inefficiencies that compromise MSF's effectiveness in servicing customers.

MSF wishes to be regulated in a manner comparable to other insurance companies, with certain exceptions, in recognition of the fact that MSF is the guaranteed market within Montana. The Insurance Department expressed that they need teeth in the statute if they are to regulate MSF. MSF agrees, and believes that the bill addresses that. The Insurance Department, as presented in the bill, would have the ability to conduct audits of the state fund, just as if it were a private carrier. The Insurance Department would have the ability to put MSF into rehabilitation if its performance was unsatisfactory, or take it under supervision. The Insurance Department could even go to a court of appropriate jurisdiction and have MSF declared insolvent if that were the case. The Insurance Department cannot dissolve MSF. That is the legislature's prerogative, because at the same time they would have to form an assigned risk pool vehicle. The other issue for the Insurance Department is that they would definitely need resources if they were to regulate another large insurance company within Montana. MSF believes this sends a positive signal to the marketplace, which goes back to MSF's vision statement. MSF is looking to do good for Montana. Within MSF, this is referred to as level three thinking. This is a positive signal to send to the marketplace.

MSF's employee's interests and status are secure within the bill. This is a prime concern. The current proposal is that MSF's employees retain access to the state pension or benefits - health, retirement, etc. MSF has done a lot of work and has had input from the retirement division. There is a concern that if existing employees were grandfathered into the defined benefit plan, and new hires went to a defined contribution plan, there could be legal issues with having disparate benefits for two groups of employees within the same company. They have also expressed that there would be a financial hardship within the state retirement plan if MSF were to take that approach. MSF's conclusion is that its employees should remain members of the retirement plan. This will eliminate the uncertainty for employees.

The needs and interests of Montana businesses are recognized by a state fund that is properly positioned to meet the challenges of the 21st century. Mr. Swanson stressed that MSF's number one priority is to be able to operate the Montana State Fund to the benefit of all customers and injured employees in an entrepreneurial and businesslike fashion, outside of the state agency requirements under which MSF currently operates.

Within that same priority is strengthening the language and protecting the surplus from being accessed. Other components of the bill, which will be discussed today, are there because MSF believes they are level three, and send a positive signal to the marketplace. Mr. Swanson stated that he is very interested in committee feedback on each of those components, although some may fall by the wayside. What MSF hopes to accomplish coming out of the study committee is priority one - non-state agency status so MSF can realize efficiencies and improve the effectiveness of its operations, and operate the way an insurance company needs to operate, as well as protection of the surplus. Mr. Swanson gave a few examples of other state funds. While what occurs with other state funds may not be meaningful in terms of a Montana solution, it is interesting to note that other states have progressed with their state funds in recognizing that they are a unique activity for state government and they need to be run like a business. As an example, there is a survey (provided to committee members) of 16 competitive state funds (monopolistic state funds were excluded). Of the sixteen state funds, several did not respond. In 12 of the state funds, employees are not state employees. 13 of the state funds are not on the state records retention plan. Nine of the state funds participate in state retirement programs. The vast majority of the remaining state funds not participating in the state retirement program were created in the early 1990s, so they started from scratch. Nine participate in state retirement programs, even though 12 have employees who are not considered state employees. Thirteen are not under state contracts purchasing. Fifteen are not part of the state telephone or communication systems, and 15 are not part of the state computer system and network. The reason is that it is a recognition that state funds are not funded by taxpayer dollars - solely by revenues; premiums received by customers who choose to insure with them. The insurance business is very competitive and is a service industry. That is the reason behind recognition that state funds are typically not considered state agencies and their employees are not state employees. State funds need to be efficient and effective.

Larry Jones asked about the figure on page 10, the 260% increase, and if it was based on the assumption that the minimum premium in an assigned risk pool would be \$750. Mr. Swanson replied that it would be somewhere in the \$700 range. Mr. Jones asked if there was any independent analysis done to show that the figure would really be applicable to Montana employers. Mr. Swanson replied that the figure was based on what is typically found in other assigned risk pool states. MSF looked specifically at two states that Mr. Jones or Larry Kibbee mentioned in the last study committee meeting. Typically, as you look across assigned risk pool states, it is double what would be found here in Montana. Mr. Jones stated that there is no factual basis to make that assumption in this state; in other words, no independent analysis. Mr. Swanson agreed that was correct.

Rep. Laible asked Mr. Swanson a question regarding the priority list, specifically regulation and oversight of the Insurance Commissioner with exceptions, and asked him to briefly explain why MSF wants exclusions of certain items, and how important they are as part of the priority. Mr. Swanson replied that the number 1 priority is non-state status to allow for the efficiencies and improve effectiveness and protect surplus. All the

other components, are lower priorities. MSF would be very interested in committee feedback. One exception is that the Board of Directors would continue to have ratemaking authority. The reason for this is that MSF cannot say no. Private carriers have the ability to exit the state if they consider rates to be inadequate - if there were political rate suppression. If there were political rate suppression in Montana, MSF would be forced to write business, by statute, as the guaranteed market, and would be creating another unfunded liability. The Board of Directors has a fiduciary responsibility to ensure that rates are adequate. There is also a provision in the bill that is above and beyond what the insurance regulator would do for a private carrier. They would issue an annual report evaluating the adequacy of MSF's rates, whether they are inadequate, excessive, or unfairly discriminatory. They would send a copy of that report to the legislative audit division, the Governor, and the MSF Board of Directors.

George Wood asked how the exception giving the Board of Directors ratemaking authority differs from the private insurance company's board submitting their rates to the Insurance Commissioner. Why the exception for the State Fund? Mr. Swanson stated that in the late 1980's and early 1990's there was political rate suppression within the United States. A number of Insurance Commissioners were not allowing filed rates to be utilized. Montana is a file and use state, but if the Insurance Department has issue with the rates, they can keep a dialogue going back and forth, where a carrier would not be able to utilize those rates. In the late 1980's there was political rate suppression and private carriers exited many states. That is the reason there were 6 or 7 new state funds created in the early 1990's. Those states decided the assigned risk pool vehicle was not viable for their state in the long term, and they created very competitive state funds in their place. MSF cannot say no. If that ever occurred in Montana, MSF would have to write risk, inadequately priced, and build an old fund fiasco all over again, which would send a negative message to the marketplace. Mr. Wood asked in the event that the Insurance Commissioner does not approve the rates for any one insurance company, what is their remedy? Can they appeal? Mr. Swanson replied that there is probably always an appeal process, but what occurred in the US in the late 1980's and early 1990's was in fact political rate suppression by insurance regulators. Carriers exited a number of states because they were not able to get adequate profit.

Jerry Driscoll stated that in the 1980's the Insurance Commissioner had nothing to say about rates, and the Director of Worker's Comp was appointed by the Commissioner of Labor, with the permission of the Governor. The Insurance Commissioner did not oversee rates in the 1980's in Montana. The fix was whenever election year came. Mr. Swanson agreed that Montana was unique, but there were at least three occasions when there was political rate suppression in Montana. The legislature changed the structure of the State Fund when it created the new fund in July of 1990 and put some checks and balances in. The bill proposes coming under Insurance Department regulation, which MSF believes further adds another check and balance. The Board today has the fiduciary responsibility of setting rates. What is being added to that is the insurance regulator will look at those rates annually, and issue a report to the legislature. They can raise a red flag if they feel the rates are not where they need to be. This is currently being done in Montana when the legislative audit division hires an

outside independent actuary who looks at MSF's actuary's analysis, so in effect MSF has two outside independent actuaries' input on rates.

Senator Cocchiarella asked how long MSF has operated without this kind of oversight. Mr. Swanson replied that he believes that MSF was under the Insurance Department for approximately 6 months when the State Fund was initially created in July of 1990, but because of the serious financial issues existing with the state fund, the legislature brought it back in a special session. Senator Cocchiarella stated that she felt that MSF is a legislatively created entity, and she feels it is the legislature's responsibility to make sure that it works for employers and employees in Montana. She questioned why the auditor should be involved in rate-making. Why is MSF putting this on their list as a request? Also, why isn't legislative oversight enough? Mr. Swanson replied that the Insurance Department is in the business of regulating insurance carriers. Private carriers look at the fact that MSF is not regulated by the same entity as they are. MSF believes that it will send a positive signal for MSF to be regulated by the same entity that private carriers are regulated by, except for the few exceptions because of MSF's role as the guaranteed market. MSF believes that all the components of the bill are positive signals to the marketplace. However, if the study committee and the legislature decides that they do not want to go in that direction on a number of the components of the bill, priority one is that MSF needs the tools to serve Montanans, priority one is dealing with the state agency status and coming under the requirements of state agencies, and protecting the surplus. In looking at the survey data, it is a rare exception that a state fund is not regulated by the insurance department. Senator Cocchiarella asked if there were ever any complaints by insureds, employee claimants or legislators about lack of oversight or regulation by the Insurance Department. Mr. Swanson replied that he does not believe so; primarily input has come from others regarding what private carriers have said. MSF is looking at positive signals to the marketplace, and would like to attract insurance companies into the marketplace to give more options to businesses.

Mr. Jones stated that the Board of Directors is appointed by the Governor, and yet Mr. Swanson seems to suggest that somehow they are insulated from political pressure on suppression of rates. Secondly, even though the Board members have a fiduciary duty, they have no personal liability if they violate that duty, so how is that a check against political suppression of rates? Mr. Swanson stated that four members of the seven member Board of Directors have to be policyholders by law. As a fiduciary responsibility, which is basically in law, they are required to ensure rates are adequate. It is working now. It did not work during the old fund days, when the President was appointed by the Governor. Also, the legislative audit division audits MSF and brings in outside actuaries. There are business people on the MSF Board, with a fiduciary responsibility and a strong memory of the old fund fiasco, which Mr. Swanson believes is a further protection against political rate suppression.

Mr. Driscoll asked if the Governor appoints the Board, and if so, can the Governor remove them? Mr. Swanson replied that it would have to be for cause. Mr. Driscoll asked if a court would have to do that, or if the Governor could remove them. Ms.

Butler replied that the Governor could probably do it by negotiation or agreement, or something less than litigation.

Senator Cocchiarella asked Mr. Swanson if the surveyed states which are under the Insurance Commissioner also have legislative audit. Mr. Swanson replied that some do, but the majority are under insurance department regulation and not legislative audit division requirement.

Senator McNutt asked about when the new State Fund was under the Insurance Auditor's review for approximately six months, and why that was changed. Mr. Swanson replied that when the new State Fund was created in July 1990, the legislature envisioned it structured similarly to what MSF is proposing today. There were significant financial issues with the old fund, including a need for double digit rate increases. Mr. Swanson stated that he believed that those considerations, in view of other financial difficulties that the state was facing then, ended up having the State Fund pulled back in as a state agency.

Mr. Driscoll stated that as he remembers it, Andy Bennett was the Commissioner of Insurance, and when the legislature started up the State Fund there was only \$12 million for start up money, and there was something in insurance regulations or law that the State Fund had to have a certain amount in reserves. At that time, the Insurance Commissioner had the authority to shut the State Fund down. She wrote a letter to the legislature saying that something had to be done, so the legislature came to a special session and created the new State Fund.

Angela Huschka introduced Dave Edwards, of the Montana Guaranty Association, which is located in Denver, Colorado. Mr. Edwards stated that Montana has banded together with five other states, and has a non-profit company called Western Guaranty Fund Services, which is an association of associations, providing administrative duties for six different state guaranty associations, including Montana. A guaranty association is made up of all companies that are licensed to do business in the state, and is not voluntary. If a company is going to write business in a state it will be a member of the guaranty association. The primary duty of a guaranty association is to pay claims of companies that become insolvent. The guaranty association assesses funds from member insurers to pay claims that result from an insolvency. The guaranty association is governed by a board of directors, not less than seven members, and not more than nine. Two members are from the public at large, and are appointed by the commissioner, and the remaining members are selected by member companies, subject to the approval of the commissioner. As an operational entity, the guaranty association takes no position concerning the Montana State Fund, and whether or not it should be a member, but Mr. Edwards stated that he had no authority to speak for member insurers. Mr. Edwards explained how the Guaranty Association could be impacted by the inclusion of a company the size of MSF. The Guaranty Association is a post-insolvency assessment organization, which means that funds are not assessed until after a member company has become insolvent. The Association then determines how much money it thinks will be needed to pay claims for that particular liquidation;

then the member companies are assessed based on how much money will be needed. In many cases, this information comes from the reserves that are set by the company. This post-assessment is different from the banking industry, where the FDIC members contribute money prior to an insolvency. The Guaranty Association is allowed to assess up to 2% of a company's annual premium to satisfy any obligations to pay claims. Member companies are assessed in proportion to the ratio of their net direct written premiums in the preceding year compared to the net direct written premiums of all member companies. Whatever percentage of the business that they've written in that state is how their contribution level will be determined.

Montana is a one account state, meaning that all insurers who write any kind of covered line will all contribute in the event of an insolvency of any member company. Some states have several different accounts, so for example, the only companies that contribute to an insolvent auto liability insurer, are other companies that write that same kind of business. In 2001, the total net direct written premium was a little over \$913 million; therefore, the maximum assessment that could be made based on that premium in the event of a large insolvency would be a little over \$18 million. In the history of the Guaranty Association from the early 1970's through today, total assessments on the Montana Guaranty Association have been just under \$29 million. It is not often that the Association would be required to assess the maximum amount for claims within the state. Of that \$29 million that has been assessed in the past, the Association has been able to refund approximately \$7 million, based on collections from the liquidation of the estates of insolvent companies. The information Mr. Edwards was given shows that in 2001, MSF wrote a little over \$80 million in premium. If a company the size of MSF were to be added to the association, there would be a total premium base of \$994 million. This means that if those same ratios were to continue into the future, and any member company other than a company the size of MSF became insolvent, and an assessment had to be made, a company the size of MSF would be responsible for paying approximately 8 to 9 % of any assessment that would be made. On the other hand, if a company the size of MSF were to become insolvent, it would create a huge obligation for the remaining member companies. According to Best's reports at the end of 2001, MSF's reserves were almost \$326 million. An insolvency could conceivably shift the responsibility for payment of those reserves to the Guaranty Association. When workers' compensation insurers become insolvent, the Guaranty Association pays those claims in full, with no deductibles and no maximums. In some liability lines, there are certain caps that apply, and in some cases those might be less than policy limits. If a company the size of MSF became insolvent, and that \$326 million had to be paid by the Guaranty Association, it would take around 18 years to pay off that debt.

Senator Mahlum asked what is done with the interest earned from the fund. Mr. Edwards replied that money is not assessed unless there is a liquidation. Senator Mahlum asked if there is a current fund. Mr. Edwards replied that there is a fund based on funds collected in the past from prior liquidations. The board does have the authority to invest money, which is done through an investment committee. Senator Mahlum asked if those investment funds stay within that fund. Mr. Edwards replied that the board has the authority to decide what's done with that money. Basically, the

Association assesses for any given liquidation; then, when the monies are assessed and the claims are paid, if there is any money left there will be money in that fund. The board of directors determines if that money should be returned to member companies. Senator Mahlum asked if the Association is known as a reinsurer of last resort. Mr. Edwards replied that that is correct. Because the Association is funded by the industry, there are statutes providing that people who have claims that would be covered by the Guaranty Association, and have any other insurance, that other insurance applies before the Guaranty Association becomes involved. That is not much of an issue in workers' compensation.

Mr. Driscoll asked about Montana being a one account state. If, for example, a life insurance company went under, and the State Fund was in the guaranty fund, would the State Fund have to share in the loss? For example, Life of Montana went under in the 1980's. If MSF was in the guaranty fund at that point, would they have had to share in that? Mr. Edwards replied that no, they would not have, but only because Life of Montana was a life insurance company. The Guaranty Association that Mr. Edwards represents is a casualty and property guaranty association. Had that been a member of the Association and had the State Fund been a member, then they would have been assessed. Mr. Driscoll asked if it was a car insurance company, then would the State Fund have to share in the loss? Mr. Edwards replied that yes it would have to share in the loss. By the same token, if a company that writes only workers' compensation coverage becomes insolvent, then the auto insurers would also have to contribute.

Rep. Laible asked if there is an annual fee for the operation of the Association. Mr. Edwards replied that the operating expenses are included in the 2%. Rep. Laible asked for clarification regarding the Montana State Insurance Guaranty Association. Mr. Edwards replied that the Montana State Insurance Guaranty Association has banded together with six other guaranty associations to have their administration provided by Western Guaranty Fund Services. Rep. Laible asked if the guaranty fund is a separate entity within the group. Angela Huschka provided clarification that Montana has, in statute, a Montana Property and Casualty Guaranty Association, and every property/casualty carrier that writes in Montana belongs to that Association. That Association has grouped together with other similar states' associations and has the Western Guaranty Association oversee those associations. MSF does not currently belong to the Guaranty Association of Montana because they are not a private insurance carrier. Rep. Laible asked Mr. Edwards if those members that are currently members of the Guaranty Fund have a right of refusal of another company that wants to come in, for example, MSF. Mr. Edwards replied that he believes that the decision of whether MSF, or any other company would become a member, would be made by the Insurance Department, probably after receiving input from their member companies. Ms. Huschka replied that the statute says that if a company is going to write insurance in Montana, that company is a member. This is unique in that MSF is becoming more like an insurance company, but they aren't proposing to be an insurance company, to become a private carrier like everyone else. No other carrier has the opportunity to decline to belong because they only write one line, and only in Montana. For example, Valor only wrote workers' comp and only wrote in Montana, but they had to belong to

the Guaranty Fund. Rep. Laible asked a question to clarify that a company writing insurance has to belong to the Guaranty Fund, and the members have to accept any new company that starts to write insurance in the state. Mr. Edwards agreed that was correct.

Mr. Jones asked if the 2% cap applies to workers' compensation carriers. Mr. Edwards replied that it does apply to workers' compensation carriers. Mr. Jones asked a question regarding the possibility of the State Fund becoming insolvent. Would the \$18 million per year be paid over 18 years? Mr. Edwards replied that this would create a huge problem for the Guaranty Fund, because they would have a very large obligation to pay. In the event that the Guaranty Fund would not have enough money from assessments to continue to pay claims on an ongoing basis, statute does give the board the authority to seek loans to pay for that. With workers' compensation, for the most part, the claimants are paid over a period of time, so reserve figures may show that there are much bigger obligations than the fund is allowed to assess, but it could be possible to pay it without seeking loans. Mr. Jones asked if there were any other state funds in the Western Guaranty Association. Mr. Edwards replied that to his knowledge there are none.

Mr. Woods made a comment regarding the compulsory aspect of membership in the Montana Insurance Guaranty Fund and the fact that this is limited to licensed insurers. The State Fund's duty and authority to write in Montana is not by license, but by legislative action, therefore they are not compelled to belong to the Association. Mr. Edwards replied that it is his understanding that that is true. Mr. Woods clarified that they would become subject to membership only if required to be licensed as a private insurance company.

Sen. Cocchiarella asked Ms. Butler to clarify the information provided on the other state funds survey, regarding the guaranty fund. Ms. Butler replied that because state funds are statutory creatures, almost all either say that the state fund is subject to all the requirements of that state's insurance code, which by default puts the state fund in the guaranty fund, or they say that the state fund is in the insurance code of that state, then list exceptions. Several states have statutory exceptions that say the state fund is not to be a member of the guaranty fund. In Texas, the guaranty fund assumed the liability from a specific date forward. The guaranty fund would assume the liability when they were running more independently, like an insurance company, and there was more confidence that they would be run appropriately. There are also a couple of state funds that will become a member of the guaranty fund at future dates, based on contingencies such as adequate surplus.

Senator Cocchiarella asked Mr. Edwards who he meant by "The Commissioner". Mr. Edwards replied that he meant the Insurance Commissioner of the state. The Western Guaranty Fund administers each state separately. Senator Cocchiarella asked how often companies fail. Mr. Edwards replied that it seems to go in cycles. In the mid 1980's the Western Guaranty Fund set up liquidations for about 13 companies in 1988 and 1989. Then there was a cycle where liquidations were not prevalent. In the last

two years there have been close to 10 insolvencies, including the Reliance Insurance Company, which is the largest company to ever become insolvent. Senator Cocchiarella asked if Mr. Edwards was aware of any state funds that had become insolvent, which a guaranty fund had to take care of. Mr. Edwards replied that he was not aware of any. Senator Cocchiarella asked Mr. Edwards if it would be more risky for the association to have the State Fund or would it be better? Mr. Edwards replied that for the Guaranty Association as an operational entity, it would be good to have a strong company that could contribute close to 10% on any assessments, but it would be a horrible thing if that company failed. Mr. Edwards was not able to give the opinions of member companies.

Greg Petesch, Director of the Legal Services Office of the Legislative Services Division, provided a legal opinion on the following questions: whether the State Fund could be legislatively established as a non-state agency entity and whether the State Fund could then be a mutual insurer or whether the State Fund could be legislatively established as a public corporation and operate as if it were a domestic mutual insurer. Mr. Petesch determined that there were four constitutional provisions that apply to those questions. Two of the provisions deal with special legislation, one of which is the general rule that the legislature can't enact special legislation where a general law can be made applicable. One is an arcane provision in the constitution, which provides that corporate charters can only be granted or dissolved pursuant to general law. The third constitutional provision provides that special franchises and privileges can't be granted, and the fourth provision deals with the investment of public funds. Mr. Petesch looked at a decision decided under the old, 1889 Montana constitution, *Normile v. Cooney*, which is one of only two cases in Montana that address the grant of special franchises and privileges. Both of those provisions were carried forward from the 1889 constitution. The constitutional convention transcripts are of little or no use in trying to determine the meaning of those provisions. Mr. Petesch concluded, based on the *Cooney* case and the Missouri decision, that the legislature could create the State Fund as a public corporation and direct them to operate as though they were a domestic mutual insurer. Mr. Petesch stated that the constitution is a document of limitation, not a document of a grant of authority. The legislature is free to do whatever it chooses in enacting laws, unless the constitution restricts what they can do. Because the State Fund is constitutionally addressed, and its funds are specifically enumerated as public funds, the legislature would be precluded from allowing it to be completely privatized. It is a constitutionally recognized entity whose funds are public funds. There is a caveat, which Mr. Petesch did not address in his opinion. The State Fund could not do all of the things that a domestic mutual insurer can do. For example, it could not choose to voluntarily dissolve. Mr. Petesch stated that the State Fund could probably not be liquidated by the Insurance Commissioner. It could be true that the State Fund could be declared insolvent, however, if the State Fund were following the law and being audited properly, that would be unlikely to happen. If there were a danger of that, the legislature would act to amend the statutes to prevent that. There has been some experience with that with the Old Fund, when the legislature enacted payroll taxes to resolve the insolvency. Being an insurer of last resort is a public purpose for which the State Fund was established, and that is why tax money could be used in the event of an insolvency.

Mr. Petesch stated that there was a lot of discussion about the State Fund being a non-agency. He stated that the constitution provides some restrictions. In the *Cooney* case, it was decided that they were a public corporation, therefore a state agency. Mr. Petesch believes that the State Fund, as a creature of statute and a state entity, has to be part of the executive branch of state government. It would not properly belong to either the judicial branch or the legislative branch because of the functions it performs, which are executive branch functions. The constitution does explicitly provide that the executive branch is limited to no more than 20 agencies and that every board, bureau, commission or instrumentality of government has to be attached to one of those agencies. Whether the State Fund wants to be a state agency or not, they are a public entity because the constitution requires them to be so, by recognizing that their funds are public funds. What aspects of law that are applicable to all other executive branch agencies that the legislature would choose to exempt the State Fund from, are policy choices to be made by the legislature. When the legislature makes those choices, it must have a rational basis for doing it, because it will be creating classifications. Under the equal protection clause, the rational basis standard is the one that would apply to those policy choices. Mr. Petesch commented on some of the statements about the State Fund's money not being public funds. He stated that a large portion of the premiums received by the State Fund are indeed public funds; that they are tax dollars passed through agencies to the State Fund for workers' compensation insurance coverage. That is because statute requires that all state governmental entities, other than the university system, procure their insurance through the State Fund. Public monies are going to the State Fund, and once the State Fund possesses those funds, they are still public funds. There are certainly restrictions that can be applied to those funds. For example, the public school fund is constitutionally restricted to the support of the public elementary and secondary schools in the state. The RIT fund is constitutionally restricted to certain purposes. Statutorily, every special revenue account the legislature creates is restricted to a purpose. With the State Fund there is an additional consideration - the state fund sells policies of insurance to private business, which is a contractual arrangement. Those contracts are protected from impairment by both the federal and state constitution. The legislature can no more impair state contracts than it can impair private contracts. The impairment of contracts provision applies to all public contracts. An example of how the contract protections works is as follows: One of the few instances in which the legislature directly appropriates coal severance tax money is to the Natural Resources Defense Litigation Fund. Those are direct appropriations of the trust fund to the Department of Justice to be used in litigation. The loans cannot be made by the Board of Investments to the Department until there is a contract in place, guaranteeing the repayment of the trust fund from any amounts recovered. This is an example of where a contract can be used to restrict the ability of the legislature to do things after the fact.

Joe Mazurek, of the Crowley Law Firm, presented his legal opinion on whether the legislature can establish the State Fund as an independent public corporation, structured or operating as a domestic mutual insurance company. Mr. Mazurek reached the same result, by and large, as Mr. Petesch. Mr. Mazurek stated that it is important to focus on the Missouri decision, because it involved a virtually identical state

constitution and the rationale it used to determine whether or not a legislature could create a corporation by what some might characterize as a special law. The court carefully analyzed and went through a number of steps in determining why it was appropriate to establish a public corporation for a legitimate public purpose. That goes back in part, to what the Montana Supreme Court has said, most recently in the *Grossman* decision. The legislature passed the water funding bonds, backed by the coal tax. The bonds were initially challenged because the money was going to several specific communities around the state - it was a question of whether it was a special or local law. There are limitations on the ability of the legislature to pass special or local laws, and in that instance the Court acknowledged that it was a special law, but because it served such a broad public purpose, the legislature had the authority to create a special law. When the state of Missouri looked at legislation similar to the State Fund's proposal, it focused on several key points that demonstrated the public character of the corporation. First, it was created by the legislature and was still publicly controlled. In that instance, the Board was appointed by the Governor and had to report to the Governor and the legislature annually. It was required to be the insurer of last resort, and could not elect to go out of business. It could only be abolished or repealed by an act of the legislature. It focused on the very important nature of the public purpose requirement - it was created for a very specific purpose and it performed an important public service function. About the time the decision was handed down in 1997, there were a number of states that had gone through the same exercise. This was the first decision that found a way around the provision that a corporation could only be created by general law as opposed to special law. Mr. Mazurek stated that in his memo he lists at least nine states that have gone through the same process, and none of them have been successfully challenged as being outside the authority of the legislature to create a public corporation.

Mr. Mazurek also addressed the state agency issue. In statute, an agency is very broadly defined, but in the context of being a department or fitting into a division, the State Fund is not an agency in the organizational sense. The legislature has the authority to impose requirements on the State Fund, or it can set it up with any structure the legislature likes, as long as it remains in the executive branch, and as long as it is done on a rational basis. The legislature has in fact demonstrated that. The State Fund has its own pay plan and was given the authority in the last session to establish its own leave policy. There are a number of requirements that apply to departments generally, which do not apply to the State Fund now. The legislature has the ability to carry that as far as they are willing to go, as long as there are reasons consistent with the public purpose for creating the entity. Mr. Mazurek agreed with Mr. Petesch that the State Fund couldn't be structured as a wholly private entity. When the workers' compensation fund was in trouble, one of the options that was considered was to take it wholly private; to sell the company. In order to do that, it would have to have been sold off lock, stock and barrel. However, the fund was recreated and bailed out with the payroll tax, which in the long run was best for employers in the state.

Mr. Mazurek also looked at the issue of restructuring the State Fund and using the name Montana Mutual Insurance Company. In most other states, state funds are set up

free from most restrictions applicable to state agencies, and function as domestic mutuals. Mr. Mazurek feels that the legislature has wide latitude in naming the entity, as long as it does not mischaracterize what it is. However, because of the language in the constitution, the legislature would have to be clear that the new entity is the successor to the State Compensation Insurance Fund, so the language tracks from the constitution. So long as the entity continues as the successor to the current State Compensation Insurance Fund, as its described in state law, the name is the legislature's choice, as long as it's not misleading and complies with the name requirements from the Montana Business Corporation Act.

Rep. Laible asked why the name needs to be changed, and if there is a legal requirement for this. Mr. Mazurek responded that the issue was whether the legislature has the authority to change the name. He believes that the objective is to convey the notion that the entity functions more like an insurance company, and it is a message to the marketplace. Rep. Laible asked about the reference made to "authority will be for workers' compensation and related coverages". He asked what Mr. Mazurek's legal opinion would be on the limitations to "related coverages". Mr. Mazurek responded that for example, there are currently some related coverages allowed by law, including occupational disease coverage and employers' liability coverage. It would be the authority of the legislature to decide how far that would go.

Senator Cocchiarella asked Mr. Petesch to respond to the name issue, and stated that she was a little concerned about Montana Mutual Insurance. She also asked what would be the test to know if that would pass the criteria of not being misleading. Mr. Petesch replied that the entity could be named anything the legislature chooses, although it should not be designed to mislead. There would be a presumption of validity attached to the name because it would be done by statute, which is important to bear in mind. Statutes have a presumption of constitutionality. Something that would indicate that they are an insurer authorized to issue workers' compensation insurance would be appropriate.

Senator Cocchiarella asked Mr. Petesch about MSF's policy jackets, and if he thinks the surplus could be protected by inserting language into the contract between the insurer and the policyholder to guarantee that their policy premium dollars are not spent in any other way. Mr. Petesch replied that he thinks that once the contract exists, the legislature cannot impair it. Certainly, it could be written that premium paid under this contract is to be used for providing payments to injured workers in compliance with the schedules provided by law, to pay for the administrative cost of the entity administering the contract, and for statutorily required reserves or statutorily required solvency provisions (meaning the actuarially required amounts). Then depending on the timing of each contract and how often they are renewed, the statutorily required reserves could be in effect on a certain time period, because the legislature would be able to change the amounts of reserves over time if they thought they were being unnecessarily accumulated. The legislature would not be able to apply that new requirement to those contracts remaining in effect. There would have to be an applicability provision put in that legislation that would not have the impact of impairing those contracts, or the

legislation would be susceptible to challenge and would be invalid. Senator Cocchiarella asked if this would be a more definite or secure position for the State Fund and its policyholders to be in, rather than to be subject to change in statute every other year, and if this would be a greater protection of premium dollars to have contract language that can't be breached. Mr. Petesch agreed that it would be more protective because the legislature is prohibited by federal and state constitutions from impairing contracts, and there are a number of cases that say that prohibition on impairment of contracts applies to contracts by state entities and between state entities to the same degree as it applies to contracts between private citizens. Senator Cocchiarella asked if the State Fund could put that language in their contract without the legislature doing anything. Mr. Petesch replied that they could, as long as they recognize the statutorily required provisions. What they can't do is put anything in their contract that could be interpreted as violating statute. Because they are a creature of statute, there are more restrictions imposed upon them than between private citizens. The State Fund, for example, would have to ensure that the statutorily required dividend provision was reflected in the contract, so they would have to analyze the statutes specifically to see which requirements that they wrote into the contract would not be violative of statute.

Mr. Wood asked for clarification of Mr. Petesch's conclusion that the State Fund would remain a state agency in the executive department. Mr. Petesch replied that it is required to remain a public entity with the executive branch. Mr. Petesch stated that the issue of state agency vs. public entity is semantical.

Mr. Driscoll asked if to meet that requirement they would need to insert the words "Montana Mutual is attached to "x" for administrative purposes only." Mr. Petesch replied that to use the phrase "for administrative purposes only" has a definition, so that would need to be analyzed to see if there are provisions that would need to be exempted. Mr. Driscoll replied that the entity would need to be attached to something. Mr. Petesch replied that under his interpretation of the constitution, that is correct.

Mr. Wood asked if the committee could grant to Montana Mutual the exceptions (protection of surplus, relief from hiring and firing requirements) by exception under the present statute. Mr. Petesch responded that it could be done to some degree, however, they could not be exempted from wrongful discharge laws in Montana. Mr. Woods replied that for example, the State Fund could be exempted from hiring freezes, etc. Mr. Petesch agreed.

Mr. Jones asked if the protection provided by the contract would be only for the life of the contract. Mr. Petesch replied that it would only be for the life of the contract, because once the contract is expired, it couldn't be impaired. Mr. Jones asked if only the policyholder would have standing to enforce it. Mr. Petesch replied yes, but he believes that a class could also be formed to enforce it. Mr. Jones asked if employees, as third-party beneficiaries, could bring claims against the State Fund if they thought the money was being mismanaged. Mr. Petesch replied that there is currently a Fraud, Waste and Abuse hotline in the legislative auditor's office which employees use. Mr. Jones clarified that he meant the third party suit would be against the State Fund for

mismanagement, then asked Mr. Petesch if in his opinion, claimants, individually or as a class, could bring third party suits against the State Fund in District Court. Mr. Petesch replied that he would have to analyze how the Montana State Tort Claims Act applied to that, because as a public entity, the State Fund has the protection of that Act, and limited liability under the Act.

Senator Cocchiarella asked Mr. Mazurek if in his opinion, with his experience in the legislature, it would be better to create the State Fund in statute as a public corporation for the purposes of protecting their surplus, or would it be better for them to have contractual language that protects the premium dollars from being taken by the legislature. Mr. Mazurek responded that clearly, they have to be a public corporation, and that he has not analyzed the contractual issue very much. Clearly, one of the things the State Fund is most concerned about is protecting the surplus. He believes that the contractual issue is attractive, but there may be pitfalls. There are a number of states with provisions which prevent the legislature from taking the surplus, and in a number of states legislatures have nevertheless tried to take those funds. When the state fund has stood up to them, they have been successful in not letting that happen. Senator Cocchiarella asked if as Attorney General, did Mr. Mazurek feel comfortable that the money borrowed for the Natural Resource Defense Litigation would be repaid. Mr. Mazurek replied that the money was repaid, and that the first step was the bill being introduced and getting the three-quarters vote and providing the framework for the contract between the Department of Justice and Natural Resources Damages Litigation Program. Mr. Mazurek stated that the contract language may work, but he has not explored the additional issues that may be created.

Mr. Driscoll asked a question about the other states where the legislature tried to take their surplus. Did those other states have the language "held in trust", and did they repeal that before they took the money? Mr. Mazurek replied that he was not sure, but he assumes that because of the language "held in trust" they were successful. Mr. Driscoll stated that Mr. Mazurek was there when they put the .28% payroll tax on employers, and promised that they would never raise it without 2/3 vote of the legislature. Then in 1993, the legislature repealed that and raised it to .5%. Mr. Mazurek replied that no sitting legislature can bind a future legislature. Mr. Driscoll stated that it might be unwise to repeal the law and take the money, but it could happen very easily. Mr. Mazurek responded that employers could make an argument that the money was paid in under one statutory scheme, which placed the money in trust.

Mr. Driscoll asked Mr. Petesch if the legislature could repeal the law that says the money is held in trust, and then take any of the \$510 million. Mr. Petesch replied that the law could be repealed, but whether the money could be taken is a separate issue. He believes that there are cases that say that public contracts incorporate the statutory scheme in place when the contract was entered into, because public entities can only do what statutes authorize them to do. Because the statute at the time imposed a fiduciary duty on the state as trustee, a very strong case could be made that the legislature would not have free access to all of those funds. However, because state government is required to be a party to the contracts with the State Fund, a separate

analysis could be made for the monies paid by state agencies from the monies paid by private parties. The legislature is free to regulate all state entities, and the legislature could say that they determined this fiduciary responsibility overrides another fiduciary responsibility. Mr. Petesch concluded that the legislature could repeal the statute, but could probably not raid the money, at least not the amount attributable to private entities. Mr. Jones asked where the money would go. Mr. Petesch replied that it would go wherever the legislature decided it went. Currently, everything the State Fund does is under contract, and there is a specific provision that says in the event the legislature repeals the State Fund, the law providing for the repeal shall provide for the disposition of the funds in existence at the time of repeal. Mr. Jones asked if the State Fund were dissolved, could the legislature move any or all of that money into the general fund? Mr. Petesch replied that under the current statutes, they could.

There was some discussion about the date for the next meeting. Rep. Laible had a conflict with November 7th. It was decided to hold the next meeting on November 12, 2002 at the Holiday Inn Downtown.

Nancy Butler, General Counsel for the Montana State Fund, presented the legislative proposal in order of priority. The number one priority is to be an independent corporation, not subject to state agency requirements and with a new name, and the second part of that is to strengthen the language regarding surplus. There have been four different attempts to take new fund premium dollars for other purposes. The law is clear today, and says that the money is to be held in trust for the purpose for which it was collected. The premiums are collected to pay claims to injured workers, set aside reserves, pay operational expenses and have adequate surplus. The state funds that have had their legislatures try to appropriate their funds brought legal action, and have prevailed. The courts looked at the statutory structure, and the "held in trust" language. Therefore, the statutory language needs to be as strong as it can possibly be. Extra insurance is making sure that the contract of insurance has appropriate language. MSF will need to thoroughly analyze this issue, to make sure that nothing is put into the contract that will have an unexpected impact. This will be done before the next meeting. Other state funds have been concerned about their surplus as well. Colorado and Texas have both recently dealt with this and put express language into statute that the state itself agreed that it would not borrow, appropriate or direct payments for any other purpose.

Ms. Butler spoke about the priority that MSF be able to operate in as efficient a way as possible, and that it have the flexibility to meet its customers' needs. The legislature has been very good to work with in recognizing the things that need to be strengthened, but they only meet every two years. Therefore, MSF is asking for a declaration that it is not a state agency, and not subject to state agency requirements. MSF has received authorization for a number of things in the past, which has made a big difference in MSF's ability to function appropriately. Other state agencies, primarily the Department of Administration, provide MSF services or are in charge of regulations on MSF. For example due to Senate Bill 131, all information technology projects must be approved by the Department of Administration. It is proposed that MSF would not be subject to

these requirements as of July 1, 2003. However, there would be a transition period, and this time frame may need to be extended a little bit. There are two areas that continue to need some work. First, is whether or not MSF is a component unit of the state for financial reporting, or is in footnote disclosure status. In footnote disclosure status, there is less connection needed for financial reporting. MSF has asked for a GASB opinion, which will hopefully be received before the next meeting. The other area is that MSF has proposed to not purchase insurance (liability, property/casualty) from tort claims. MSF would also not have protection from punitive damages or the limits on liability, which is tied to being regulated by the Insurance Commissioner. After talking with Tort Claims, if there is a cut-off point where they are no longer responsible for MSF's claims, they are still handling things that occurred when they were responsible for MSF. Tort Claims has a different funding mechanism. They look back each year and decide what a state entity should pay them for the next year. MSF does not want to leave them with liabilities, but no funding, so MSF will need to work out a transition plan. MSF will continue to have the Board of Investments invest its assets and the Legislative Audit Division will still audit MSF's financials on an annual basis. The fraud program is currently at the Department of Justice. MSF had planned on moving that program to the Insurance Commissioner's office, but after discussions with the Attorney General's Office and the Insurance Commissioner's office, MSF looked at what was being paid at the Department of Justice. The Insurance Department did not feel like they could absorb that cost under the funding scheme in place today. Therefore, as a public entity, it is probably best to keep the fraud investigation and prosecution effort at the Department of Justice. The last issue is office space. The MSF office building was built for the Division of Workers' Compensation and bonds were sold. The Department of Labor moved out of the building in 1990 and the State Fund took over the payments. Premium dollars have contributed to about 73% of the cost of building the building, which is paid for today. The bill provides for the ability to approach the landlord to buy the building, which would be held in MSF's name and be in the financials. The money from the purchase would go to the general fund. As an alternative, it seems appropriate to continue to rent the building from the Department of Administration.

Ms. Butler spoke about MSF employees. Currently, MSF has 251 employees, and under the proposed language in the bill they would be public employees. For collective bargaining purposes, the statute defines a public employer as a public corporation, so MSF is comfortable that the language of the law today concurs with MSF's intent to leave its employees with the ability to have a collective bargaining arrangement. MSF explored providing insurance, group benefits and retirement benefits independently. To duplicate and administer the insurance benefits would cost at least an additional \$500,00 per year. MSF's recommendation is to have employees stay in the insurance and group benefits plans. MSF also looked at the retirement plan. To duplicate those benefits, even for current employees, would cost \$15 million. In further discussion with PERS, there are legal and actuarial concerns, so MSF recommends that the employees stay in the state retirement plan. MSF also looked at how the employees would be impacted by not being state employees. Since the employees would still be public employees, many things would not change. The things that would be impacted would be things like leave and pay classification plans, from which MSF is already exempt.

MSF is not anticipating disruption or negative impacts on its employees, and is actually hoping for a positive impact.

Mr. Jones asked Ms. Butler about the “held in trust language”. He stated that in the Workers’ Compensation Act it says it’s held in trust except for the section which expressly says that there can be transfers to the general fund. Mr. Jones asked her if she wouldn’t agree that as the State Fund is now set up, it is not an absolute, unconditional trust, and instead the legislature has retained the authority to transfer money from the State Fund into the general fund. Ms. Butler disagreed strongly. In 1989, the Old Fund received \$20 million from the general fund. At that period of time the State Fund was not allowed to make dividend payments to its policyholders until the Old Fund liability was paid off. If the State Fund declared a dividend, by law it was to go to the Old Fund instead of the policyholders. A dividend of about \$102 million was declared which went to the Old Fund; then, through Senate Bill 67 there was an additional \$68 million transferred to the Old Fund. At the same time, \$20 million was returned to the general fund to pay off the original \$20 million. It is a totally different circumstance. Mr. Jones asked if the State Fund’s position is that the current statutory language is sufficient to protect the surplus. Ms. Butler replied that MSF wants to strengthen the statutory language.

Mr. Driscoll stated that on page 4 of the bill it says “Montana Mutual is exempt from laws that generally apply to state agencies, unless included in this part or in the specific law by name”, and that he could not find collective bargaining in the draft. Ms. Butler replied that Title 39 provides that public employers are in collective bargaining. A public corporation is considered a public employer, and MSF did not exempt itself from status as a public employer. Mr. Driscoll stated that it says MSF is exempt from laws that apply to public agencies, governmental entities or agencies, institution, board, political subdivision or agency. Ms. Butler replied that she was relying on the definition of public employer, which is how an agency gets into the collective bargaining act. Ms. Butler stated that MSF would be open to adding some clarification of this matter.

Mr. Jones asked if the surplus became high enough so the State Fund could and did engage in predatory pricing, would the legislature have the authority to come in and prevent predatory pricing. Ms. Butler replied that it would not have the authority until the next session, just as it is today. There are a number of statutes that lay out the responsibilities of the Board to set appropriate rates, set aside reserves and set aside appropriate surplus. If they follow the statutes and there are audits every year, things should work like they are supposed to. If they didn’t, the legislature would have the option of stepping in.

Mr. Driscoll asked about the section of the bill stating that MSF would rent the building at standard Department of Administration rent. He was told that their agency was subsidized by the capitol land grant at \$1 a foot. Does MSF intend to get that rent? Mark Barry, MSF VP of Corporate Support stated that they are proposing \$6.32 a square foot. Mr. Driscoll stated that the only reason he brought it up is that for all the other agencies, it is just tax money. In this situation, it is a little bit different because it is

premium dollars. If the state is subsidizing the rent, the other insurance companies will probably want a subsidy too. Ms. Butler replied that the building is paid for, and the rent should cover the cost of maintaining the building. MSF currently maintains the building and pays utilities in lieu of paying rent. Mr. Swanson stated that the intent is to pay fair market value. Mr. Driscoll asked if he meant fair market value on rent or purchase. Mr. Swanson replied that it would be fair market value for rent or purchase.

Sen. Cocchiarella asked if MSF was asking to go from paying \$1 to rent the building and paying its own maintenance to paying \$6.50 to lease the building and still do maintenance, or would Department of Administration do the maintenance? Ms. Butler replied that maintenance should be part of the rent. Sen. Cocchiarella asked if MSF wanted to give up their responsibility and lease the building and get the services back, like a state building rented to any other state agency. Ms. Butler replied that what is being done today seems very appropriate, and that MSF has substantially contributed to paying for the building. MSF would like to reflect the cost of the building on its financial statements as an asset, and the general fund would gain some funding through the purchase of the building. However, MSF needed a backup plan in case the purchase did not work out.

Mr. Wood asked if MSF intends to pay \$6 million dollars for the right to take care of maintenance. Ms. Butler replied that MSF would be able to reflect the building on its financial statements. Mr. Wood asked if the building is reflected on MSF's financial statements now, and Ms. Butler replied that it is not. Mr. Wood asked where MSF would get the \$6 million. Ms. Butler replied that it would come from the surplus. Mr. Wood replied that this would be giving up the ability to use the cash, for a building that would have to be sold if that asset was needed.

Rep. Laible asked about who would pay the cost of any improvements in the future, if the building were leased. Ms. Butler replied that an arrangement could probably be worked out whereby MSF takes care of anything that is taken care of today, so premium dollars would take care of the building, or if rent was paid, that would take care of utilities, maintenance, etc. Anything out of the ordinary would probably need to be paid by MSF. Rep. Laible asked if this would be a typical rent, like a triple net. Would MSF pay property taxes? Mr. Barry replied that MSF pays service fees that are assessable, but not property taxes. Mr. Laible stated that this situation would be almost like a triple net, but is not really a triple net because MSF would not pay utilities. Ms. Butler stated that if MSF was paying Department of Administration rent, utilities are usually included.

Ms. Butler spoke about MSF's second priority, which is regulation and oversight by the Insurance Commissioner. It is proposed on two basic grounds, which are creation of a more level playing field and utilization of insurance expertise. MSF will never be on a level playing field with private companies, because MSF is the guaranteed market. MSF's intent is to move in those areas, where possible, to create a more level playing field in Montana. The Insurance Commissioner's office raised questions regarding enforcement ability and resources. The Insurance Commissioner's role will be very similar to what the legislative role is today. Legislative Audit Division audits MSF and

contracts with an independent actuary to review rates each year. The difference is that the Insurance Commissioner would have more authority to examine insurance related issues, and MSF would be treated more like the private companies. MSF would function as a domestic mutual under the insurance code. Chapter 1 has the examination of affairs, transactions, accounts, records and assets as often as the Commissioner considers advisable, which MSF would be subject to. The Insurance Commissioner is also responsible for approval of forms. MSF would not be under the Insurance Fraud protection. Chapter 2 deals with the regulation of insurance companies. MSF would receive a Certificate of Authority, but the issue is being able to revoke the Certificate of Authority. As the guaranteed market, MSF could not have its Certificate revoked. MSF would follow the assets and liabilities requirements in the insurance code, and would pay all the deposits that private carriers pay. MSF would be subject to supervision and rehabilitation, but could not be declared dissolved or liquidated. MSF would need to be exempt from the statute regarding mutual insurers, because that is typically an organization chapter. All of MSF's organization is taken care of in the enabling statute. Insure investments is a minor exception, but it talks about the Board of Director's responsibility for investments. In MSF's situation the Board of Investments has that responsibility by the constitution, not the Board of Directors, so it needed to be clarified that there would not be a conflict. MSF will follow any necessary insurance contract provisions. MSF is proposing that the Board of Directors, with the help of an independent actuary, will set the rates each year. Currently, there is no approval or disapproval process, however there is oversight by the Legislative Audit Division, which hires an independent actuary to review the rates and issue a report. MSF is not required to follow NCCI rates or classifications, which MSF intends to continue. MSF does use NCCI rates to a large extent, but because of being the guaranteed market, there are some exceptions that need to be addressed. There is a chapter on insurance producers, which MSF's producers currently follow. MSF would simply be reporting who it contracts with under that chapter. MSF also proposes to be subject to the unfair trade practices chapter. MSF is currently subject to common law bad faith. If the bill goes through with the Insurance Commissioner regulation, the protection of surplus and the exemption from state agency status, then MSF would also agree to be subject to punitive damages like private carriers.

Senator Mahlum asked Ms. Butler if the premium tax would create an increase in premium for businesses. Ms. Butler replied that it would, in order for MSF to meet that obligation.

Senator Cocchiarella asked if Ms. Butler knew how much the Insurance Commissioner would charge for the oversight provided for in the bill. Ms. Butler replied that it might be similar to what is paid today for the Legislative Audit Division to contract out for an actuary, which was \$10,500 this year. MSF would still have to pay for the financial audit, as well as any financial examinations. Senator Cocchiarella asked if there could be an estimate from the Insurance Commissioner's office available at the next meeting. Ms. Huschka responded that she would try to do that.

Mr. Jones asked some questions about the market of last resort. Mr. Jones stated that as he reads the statute, it says that the State Fund has to set premiums that are neither more nor less than self-supporting. He asked if it was true for the market of last resort, and if the State Fund has to write them at a loss. Ms. Butler replied that MSF is not forced to write them at a loss. Mr. Jones asked if MSF is required to write them so they cover their cost. Ms. Butler replied that MSF looks at the overall and does not make a distinction on the market of last resort, but instead looks at exposures as a total. Mr. Jones asked if Ms. Butler agreed that it is the conduct of the insurance adjuster, and not the employer that exposes a workers' compensation insurer to a bad faith suit. Ms. Butler agreed that in a claim situation, it is typically the claim adjuster making decisions on benefits, and if there is considered to be a decision made in bad faith, then it is the insurance company that the adjuster works for who is responsible. Mr. Jones asked if Ms. Butler agreed that the fact that MSF writes the market of last resort does not in and of itself create a liability for punitive damages for claim adjusters. Ms. Butler agreed.

Mr. Wood asked for the name of the state agency operational requirements, which MSF wants to be exempt from. Ms. Butler replied that MSF would be exempt from laws that generally apply to a state agency. The laws are not consolidated in one place, and different definitions are used, so in order to catch everything, MSF had to put a laundry list in the bill. Mr. Wood asked if it was acceptable to put the laundry list in. Ms. Butler replied that she believes it helps, otherwise MSF could say it is not a state agency for one thing, but in another area it might just say the word "agency". Mr. Wood stated that he understood that MSF was going to accept the responsibility for paying premium tax, but now there seems to be some equivocation. Ms. Butler replied that MSF did propose that and has not withdrawn that proposal. Mr. Wood asked if it is paid by private insurance companies. Ms. Butler replied that insurance companies pay it today, and among state funds it seems to be a matter of preference.

Matthew Cohn, MSF Communications Team Leader, spoke about priority number 5, which is to purchase the office building, and made it clear that MSF's goal is to actually purchase the building. That is taken care of in the bill, which amends in that a public corporation has the ability to approach the land board. As an illustration of how the collection of the premium tax would increase premiums; if a policyholder paid \$5,000 a year, with the premium tax it would be \$5,137.50.

Mr. Cohn also spoke about MSF continuing as the sole insurer for state agencies. Current law has MSF as the sole insurer for state agencies, with the exception of the university system. That process began in the 1930's, in which insurance for some industries, such as mining and logging, was not available. It was written into statute for the State Fund to write insurance for that, and in return they received the ability to write to state agencies and contractors for state agencies. Insurance is subject to significant market swings, and currently there is a return of a hard market. MSF is experiencing a rapid growth in premium volume, in some cases due to private carriers leaving the state. Fluctuations in the market cause a myriad of operational challenges in terms of providing service, having adequate staffing and performing all the functions necessary to be a solvent insurance carrier while serving the role as the guaranteed market in the

state. Retaining the state agencies supports a stable and predictable base of premium and aids in supporting a more financially stable and operationally sound State Fund, which is a benefit to all Montanans. Therefore, MSF proposes to keep the current status.

Mr. Jones stated that at the last state Chamber board meeting, Nancy Butler was asked what the total agency premium was, and she estimated about \$6 million. Mr. Cohn replied that it is actually estimated at \$8.5 to \$9 million. Mr. Jones asked if MSF opposed allowing the university to have private carriers insure for the same reasons that they oppose allowing agencies to do that. Mr. Cohn replied yes.

Mark Barry, MSF Vice President of Corporate Support spoke about MSF's surplus level and how surplus levels are set. Surplus is not excess or unneeded funds, but is there to ensure that the insurance carrier will be able to pay their obligations for the claims that are filed by injured employees. It is important to note that when rate levels are set each year, MSF will not know the actual cost of that coverage for 20-30 years in the future. Based on that, MSF needs to have strong surplus to ensure that it is covering the potential for adverse development. MSF writes only one line of business and can't diversify into other lines. MSF only writes in one state, so it is subject to whatever happens in this state, such as legislation on benefits, Supreme Court decisions or catastrophes within the state, so it needs strong surplus. Also, unlike a private company, MSF is not able to go out to the market and raise capital should there be adverse development. For example, after September 11th, MSF's reinsurance costs increased over 300%. When MSF received its quotes on coverage, it was actually in excess of 500%. MSF had to modify its reinsurance program so that it was able to meet its budget. This means that the surplus has been exposed by an additional \$47 million. Senator Cocchiarella asked Mr. Barry if MSF set its reinsurance limits higher and took on more of the risk. Mr. Barry replied that MSF initially attached at \$3 million, and went up to \$115 million in reinsurance coverage and were covered 100% at each layer. Now MSF is exposed for the first \$5 million of loss, and has not taken 100% of the layer in each layer, in order to meet the budget. The bottom line is that MSF has exposed its surplus more than in the past.

Mr. Barry stated that premiums are set at a target level of 1.5 to 2, reserve to surplus ratio. Mr. Wood asked Mr. Barry to explain the 1.5 to 2 by using the \$346 million in reserve. Mr. Barry replied that it would be in the range of \$217 million to \$185 million in surplus.

Senator Cocchiarella asked Mr. Barry what the State Fund does to have accurate reserving. Is there any quality assurance or a certainty about how good the reserves are? Mr. Barry replied that on a case-by-case basis, claims are reserved individually. MSF has an automated reserving system called MIRA, which is only used as a guideline. MSF adjusters review what MIRA has set as reserves to determine if they agree with it. If a claim is over \$250,000 in reserves, MSF requires its adjusters to manually reserve that claim. MSF has a quality assurance process where each quarter, each adjuster has a number of claims that are reviewed by QA staff. In addition to that,

MSF adds Incurred But Not Reported (IBNR), which is where the consulting actuary and internal actuary staff determine how much additional development will be made on those claims on an aggregate basis, to get to the actuarial ultimate losses. Senator Cocchiarella stated that she has a concern about appropriate reserving, and she remembers that in the past, reserving was not very good. She stated that if the committee is going to look at what MSF has in surplus and it is based on what is reserved, then that number needs to be very accurate, and closely monitored and checked on. The self-insured people have to go through a process to make sure their reserving is up to speed. The committee needs to have some security in that reserve number. Mr. Barry replied that MSF has one of the top consulting actuaries in the nation, Bob Conger of Tillinghast Towers Perrin, and MSF is very satisfied with the work he and his staff are doing. In addition, MSF has two internal actuaries and one actuarial assistant. MSF is continually looking at its reserves, because it is also concerned about the level of reserves.

Mr. Wood asked Mr. Barry if the State Fund can determine the changes in reserves from year to year. Mr. Swanson replied that last year, MSF saw \$9 million of adverse development. That means that as you look at each accident year, the actuary looks back and says that we estimated losses at x , now it's $x + 1$, in the aggregate it was \$9 million of adverse development. That is occurring nationally in workers' comp. MSF also has another outside independent actuary looking at Tillinghast Towers Perrin. The Legislative Audit Division hires another actuary that looks at the adequacy of MSF's reserves. MSF has two outside independent actuaries, which is way beyond what most property/casualty insurance companies in the United States have, because the person who determines the ultimate liability for almost 70% of national P & C carriers is the internal chief actuary. In addition, MSF follows an industry best practice of not discounting its reserves. If the actuary says MSF needs to put \$100 million in the bank for a particular year, that is what's being set aside.

Mr. Wood asked if the final determination of the reserve is based on the actuaries doing an audit per claim. Mr. Barry responded that the consulting actuary relies on MSF's numbers. Mr. Swanson stated that there are seven tests that actuaries apply on reported claims and paid claims. However, as Mr. Barry said, actuaries are only right on the best estimate projection about half the time, so that is why MSF does not discount its reserves.

Mr. Driscoll asked what is done with the interest that is made on the \$350 million. Mr. Barry stated that when MSF sets its rates each year, it is required by law to consider the investment income on the premiums collected. The dollars that are collected in premium are 80% of the ultimate cost of that accident year. Some of that investment income goes to offset that difference. The rest of it goes to MSF's net income and surplus, and if it's available for dividend, it is dividended back to the customers. Mr. Driscoll asked if the \$9 million in adverse development was paid for out of investment income or increased rates. Mr. Barry replied that it came out of surplus, but it could be the case that the net income covered it. In the past year, that was the case. Mr. Driscoll stated that MSF has about \$350 million in reserves and asked if MSF was

making 6%. Supposing there was \$17 million in investment income, when it is put in the bottom line does MSF figure rates or leave it in the reserve for losses column? Mr. Barry replied that MSF does not consider what has happened in the past when setting rates. MSF sets rates based on the accident year under review, so that it will be actuarially sound each accident year. Mr. Driscoll asked if MSF estimates that it needs premium dollars of \$80 million, but got \$17 million in investment income, could MSF charge only \$63 million. Mr. Barry replied that if MSF needs \$80 million to ultimately cover claims, that amount is discounted and MSF collects only about \$64 million. If losses become \$80 million, then MSF has to take that that \$16 million of investment income and offset it on the financial statements. MSF is undiscounted on losses, but not on rates. MSF is required by law to consider the investment income that will be earned over time on that accident year.

Mr. Barry spoke about the segmentation of MSF's book of business. Looking at the array of each accident year, the total book of business is tightly compacted. This demonstrates the stability of MSF's entire book of business. When there is that kind of stability, MSF is able to estimate what the costs are going to be on those years. As the premium segment gets smaller, there is more volatility. If MSF were to try to price out that book of business alone, MSF would have to assess at the higher end of the rate to make sure that MSF is covered for that volatility. However, because there is a broader base of premium and a more balanced book of business, MSF is able to share that volatility risk in the small book across the entire book, and establish a stable rate. Mr. Wood asked if MSF can live with the 120% combined loss ratio indefinitely. Mr. Barry replied that the break even point is approximately 120%.

Mr. Jones asked why MSF didn't go back to 1990 with the chart. Mr. Barry responded that the information from the last five years was readily available. Mr. Jones asked if the other information was available. Mr. Barry responded that it would have to be created. Mr. Jones asked about the combined loss ratio of 1.54 in 2000, and if that meant that for every dollar of premium taken in for that account size, MSF paid out \$1.54. Mr. Barry replied that was correct - MSF paid out \$1.54 in losses and expenses on that segment of business.

Rep. Laible asked a question regarding pricing. He asked if all businesses, no matter their size, have the same rate for classification. Mr. Barry responded that on a rate base, that is correct. They are assessed on their payroll times their class rate. Rep. Laible asked if the larger ratepayers are in essence subsidizing the smaller. Mr. Barry responded that in looking at the results of the smaller group in 2001, the smaller group had a combined ratio of 110%, but in the same year the \$5000 and over group had a combined ratio of closer to 130%. From year to year, the small account could be profitable or unprofitable, but there is volatility in that book. MSF tries to balance that with a balanced book of business.

Mr. Jones asked if there is anything in the law or in MSF's ability to operate that would prevent it from writing a book of business, for example 2002, 0-\$1,000, at a premium rate that would cover their risk. Mr. Barry replied that MSF does not try to write that

book at an unprofitable basis. It is difficult to price that book of business because of its volatility. For example, an account paying less than \$1,000 a year in premium could go ten years without a loss. If it has one loss at \$20,000, it will wipe out 20 years of profit on that business. MSF makes every attempt to price that book of business correctly. Senator Cocchiarella asked if what Mr. Jones was describing is how an assigned risk pool would be priced. Mr. Barry stated that if it were to be priced it on its own, MSF would have to price it at the higher end of that experience. Senator Cocchiarella asked if that is what would happen to the small businesses in Montana if there were an assigned risk pool - would they be charged what they cost? Mr. Barry responded that they would be charged based on their experience in order to cover that type of volatility. Senator Cocchiarella stated that if you look at the 0-\$1,000 account size, there are 7,000 minimum premium payers, and in the state of Montana 80% of our businesses are minimum premium payers, and that what Mr. Jones was saying is not appealing.

Mr. Driscoll asked what general and acquisition expenses are. Mr. Barry replied that acquisition expense is the cost of writing the policy - underwriting, agent commission, etc. General is general overhead. Mr. Driscoll stated that in 1998 it was \$6 million and in 2002 it was \$15. Mr. Barry responded that in 1998, MSF began writing business with independent insurance agents, and costs increased. MSF compares its operating expense ratio as a percentage of its premium to other insurers, and MSF closed its year with a 30% operating expense ratio; compared to other competitors that run anywhere from 40-50%.

Rep. Laible stated that the reserves are really a basis of the actuarial review of all the losses MSF has. That is just a function of what's happening within MSF's clients. The surplus tends to be as a ratio in direct relationship to MSF's premiums that were written. He asked if there is a percentage of where the surplus should be so that actuarially, MSF would be in a good financial position, and can there be a benchmark on the surplus, so that the amounts over that surplus would then become either reductions in premium costs or dividends to the ratepayers. Mr. Barry replied that there are a number of ways to look at this issue. Because it is the guaranteed market, MSF chooses to look at a reserve to surplus ratio, and has a target of 1.5 to 2, reserve to surplus. Once MSF reaches that range, then it will have sufficient surplus. Rep. Laible asked if MSF's reserves stay on track with the premiums that MSF has written, and do they stay in the same ratio to one another all the time, within reason. Mr. Barry replied that MSF sets rates so that they are within a range, so that there is a small contingency for a small contribution to surplus. However, as Mr. Swanson mentioned, there was a \$9 million adverse development this past year on prior years. MSF sets rates, but it does not know what the ultimate costs will be. Each year MSF tries to set the target so that it can cover losses, expenses, and have a small contribution to surplus. Rep. Laible stated that even though MSF had an adverse effect of \$9 million last year, in reverse MSF could have had \$9 million to the plus side. Mr. Barry agreed and stated that in the mid 1990's, in one year, the consulting actuary lowered MSF's ultimate loss estimates by \$100 million. If that should occur in today's market, it would go to the surplus and if available for dividend, would go back to the policyholders as a dividend. Rep. Laible asked if MSF could control the actuarial amounts, which in effect would control the

surplus. Mr. Barry responded that MSF does not control what the independent actuary tells them, but considering that over time, prior accident years are being paid down, at some point when the State Fund is mature enough, theoretically, the new reserves will offset the reductions in reserves on prior years.

Rep. McKenney asked for clarification of the reserves. His understanding is that the reserves are there to cover the known liabilities, and the surplus is a ratio of the reserves to cover potential, unknown liabilities and also investment income. Mr. Barry replied that the surplus is there to cover unknown events, such as catastrophic events or adverse development. Rep. McKenney stated that based on the ratios that MSF is suggested to follow, it appears to him that the surplus is short of where it needs to be. Mr. Barry replied that MSF has been making improvements toward the target, and that the actuary has advised that MSF can gradually move in that direction. Mr. McKenney stated that the surplus isn't really a surplus, because MSF has not reached its target amount to have a safe reserve and a safe surplus to cover the unexpected liabilities. Mr. Barry stated that MSF does not feel that there is excess surplus.

Senator Cocchiarella asked what loss adjustment expense is. Mr. Barry replied that it is the estimated cost of managing the claims. Mr. Wood asked what it currently runs. Mr. Barry replied that it runs about 12%. Senator Mahlum asked if the 12% is part of the 30%. Mr. Barry replied that it's 12% of the loss. Senator Cocchiarella asked if the general expense includes other overhead, including management expense, salaries, and benefits. Mr. Barry replied that yes it does.

Mr. Barry spoke about the inefficiencies of being part of state government. MSF is a competitive organization, competing for a balanced book of business, which makes it different than other state agencies. MSF does not have any regulatory responsibilities, does not charge fees for licenses, or collect taxes. MSF is governed by a Board of Directors, which sets MSF's direction and establishes its budget each year. MSF makes its presentations to the Board of Directors and obtains their approval of its recommendations. An example of where MSF utilizes additional resources as a result of being a state agency is that MSF has seen additional requirements for getting approval for technology needs. MSF spends a great deal of internal time, analyzing and determining options and costs, then presenting them to the Board of Directors for approval. Once the Board's approval has been obtained, MSF must go to ITSD and further obtain their approval, then submit an IT plan. Being attached to the state's network services system causes problems with moving forward with an e-strategy vision. This has to do with providing security and bandwidth. MSF's vision is to provide on-line services to its customers, including the ability to transact business over the web, or for them to view their losses and experience over the web. This requires securities, because there needs to be limits to what can be seen. A recent survey indicates that 87% of MSF policyholders have access to the web at work, which is a 20% increase over two years ago. 46% of MSF's customers were interested in doing business over the internet. MSF estimates that there are potentially 30,000 potential users of these services, and MSF would be competing with other state agencies for bandwidth and security services. MSF would like to control that within MSF. MSF also envisions

providing training services over the internet, especially to small policyholders that MSF cannot otherwise efficiently service. This would provide visual or audio training over the internet for loss-control and safety services.

The Board of Directors approves and has full authority over MSF's budget, yet MSF is required bi-annually to submit a budget to OBPP, which is included in the Governor's budget book. This is a budget that is not approved by the Board of Directors, and which will probably change when MSF goes to the Board for budget approval. MSF also finds that SABHRS does not provide the accounting that MSF needs as an insurance organization. MSF prepares its financial statements on an insurance accounting basis using spreadsheets, which is extremely manual. MSF also finds that when there are changes in accounting requirements, approval must be obtained for new account codes in order to utilize the SABHRS system. MSF's primary concern is the ability to act quickly with changes in the marketplace, and prepare itself for the trends in the market. MSF finds itself in an area where it needs to get approvals, and there are delays in getting those approvals, therefore MSF's request is that it be removed from those requirements, because MSF is a unique entity - a competitive insurer in a state government setting.

Senator Mahlum asked if MSF's competitors provide e-business. Mr. Barry responded that currently, a number of insurance companies provide e-business. Senator Mahlum asked Mr. Jones if Liberty Northwest has e-business. Mr. Jones replied that Liberty has internet access where certain size accounts can apply on-line. Senator McNutt asked Mr. Jones to clarify the size of accounts that have internet access. Mr. Jones replied that he is not sure, but can provide that information at the next meeting. Senator McNutt asked if Mr. Jones is talking about premium dollars. Mr. Jones replied that yes, that is what he meant. Liberty is a direct writer, and does not have agents. There is a certain account level at which a person would be referred to another resource other than an account executive. Senator Mahlum asked if the account executives receive commissions. Mr. Jones replied that he does not believe Liberty's people work on commissions, but he will find out.

Senator Cocchiarella asked Mr. Barry if there are any disadvantages to the separation. For example, there was a time when there was a sharing of information between State Fund and Department of Labor. Mr. Barry responded that there would not be a problem with that, and that it is done on a RJE transmission. MSF does not currently have access to their system, nor do other insurers.

Mr. Wood asked if the inefficiencies would be done away with if MSF was given an exception to the state agency operational requirements. Mr. Barry replied that the biggest impediment has to do with information technology, and MSF would like more flexibility in that area. If MSF is considered a component unit of the state of Montana, as it currently is, the Department of Administration accounting division will dictate that MSF must be on SABHRS, so MSF will probably not be able to move away from that. MSF has a request into the Department of Administration who is forwarding the request to the Governmental Accounting Standards Board for a ruling on whether or not MSF is

a component unit. Mr. Woods asked if the exceptions need to be listed individually in the legislation, or if it could be done as a group. Ms. Butler replied that it could be done as a group, but a lot of terms would need to be used, or it could be done by going into each section.

Senator Cocchiarella expressed a concern about any agency going off on their own and doing purchasing and developing, given what's happened with the Department of Revenue. Now the state is in a situation where it has spent millions. She stated that she hoped MSF would not give up some help or oversight that might protect them from bad decisions. Although, MSF seems to feel confident that they will make the right decisions, it could put the state back in a big black hole with the State Fund if it goes the wrong way with those kind of investments. Mr. Barry replied that the Department of Revenue may have made some inappropriate decisions, but businesses do make inappropriate decisions. Everyone runs the risk of making bad decisions.

Mr. Barry spoke about the Old Fund. At the end of FY02, the Old Fund has total invested assets of \$131 million, with total assets of \$134 million. Loss and loss adjustment expenses discounted at 5.5% are \$90.9 million. The surplus on the year is \$24.8 million. From that, MSF calculates what is available for transfer to the State Fund, but \$4 million will go back to the general fund under Senate Bill 19. MSF calculates that there is \$13.2 million available to be transferred. MSF is proposing that the rest of that goes back to the general fund each and every year. What that means is that MSF will have \$9 million dollars of the 10% contingency remaining on the books. There were some questions at the last meeting about what could be done with the Old Fund. Mr. Barry stated that he has been working with Bruce Hockman, on both an annuity and a loss portfolio transfer, which is a reinsurance mechanism. On a discounted basis, there is \$90.9 million. Losses are \$79.7 million; loss adjustment expenses are \$11.2 million. The actuarial range of estimates goes from a low of \$117 million to a high of \$141 million. A reinsurer looks at this information and determines what the best estimate is, and what the low and high is in the range. MSF is using the \$128.9 million discounted at 5.5% to get \$90.9 million. A reinsurer would look at a number of risk areas. First, they look at the investment return risk, then they look at the payout patterns, and whether they feel the payout patterns will be different than expected, and they also try to determine whether they believe the actual payout will exceed the best estimate. MSF obtained a quote on an annuity situation on loss only. Old Fund losses on the financial statements are discounted, and that amount is \$79.7 million. The quote on the losses is \$85 million. Under this scenario, \$5 million of surplus would be used in order to fund the liability. An annuity is only another funding mechanism, and would cost money. This would not include loss adjustment expense, and MSF would still have to pay for the cost of adjusting those claims for the remainder of their life. The annuity company would not adjust those claims, and the state would not be able to remove the liability from its financial statements. If the annuity company went bankrupt, the state would still have to pay the losses. MSF has already set aside assets to take care of the Old Fund.

A loss portfolio transfer is more of a sure thing. Mr. Hockman has been trying to maintain the \$24 million surplus, and has not been able to get anyone to give him a bid on paying the losses at \$90.9 million. The problem is that the losses have already been discounted, so the reinsurer cannot make any money on it. MSF does not believe that it is a good idea to look at either of these options now. MSF manages the assets for the Old Fund, and if those claims develop positively, towards the low end of the range, then that money would go to the benefit of the state. Mr. Barry mentioned that MSF's administration of the Old Fund includes claims management, financial reporting, actuarial reviews and auditing. Mr. Driscoll suggested that MSF should not charge the premium tax and should administer the claims for free.

Public Comment

Larry Kibbee, Regional Vice President of the Alliance of American Insurers offered public comment. He stated that MSF has not taken a look at what businesses may or may not be assigned risk material in their book of business. In terms of putting some objectivity into the 260% increase and 80% population, he asked his home office to take a look at what's going on in the assigned risk plan population around the country. Mr. Kibbee handed out an NCCI table entitled "Comparison of NCCI-Reported Direct Workers Compensation Premiums to Residual Market Premiums for Calendar Years 2000 and 2001" (available on the NCCI website) to the committee members. In the 28 assigned risk plans that NCCI looks after, the highest premium percentage, or highest percentage of business in an assigned risk plan is 16.3%. He gave the example that in Alaska 16.3% of the written premium in a calendar year ended up in an assigned risk plan, which was the top percentage. The first page of the handout breaks out the actual premium, and Mr. Kibbee clarified that some of it is assigned risk premium and some of it is reinsurance premium, but it is residual market premium as a percentage of direct written premium. Therefore, Mr. Kibbee challenged that fact that all of the \$1,000 to \$5,000 risks would automatically end up in an assigned risk plan. First, assigned risk plans in the states in the handout are overseen by the state Insurance Commissioner. Assigned risk plans have the same kind of regulatory oversight that the regular market does. They have to operate with rates that are actuarially sound. Some assigned risk plans have two or three tiers. Mr. Kibbee suggested that an assigned risk pool would not necessarily be calamitous for Montana employers, and that the committee should take a further look at the operational characteristics of assigned risk plans by states that actually do that. Mr. Kibbee also spoke about the guaranty fund. His concerns that were expressed at the last meeting are still the same. From the guaranty fund's standpoint, in section 4 (2) of the proposal, the Insurance Commissioner is required to offer a Certificate of Authority to the State Fund. By that very action, under current law, they would be a part of the guaranty fund, unless the legislature made an exception. Given the special regulatory considerations that the State Fund is also seeking; the freedom to set their own rates, and the freedom to not have the Insurance Commissioner disallow rates, Mr. Kibbee believes that it would be irresponsible for private carriers to welcome that kind of company into a guaranty fund. Mr. Kibbee hopes that if the State Fund goes ahead with its proposal as it exists, the committee will give serious consideration as to whether or not it should be in the guaranty fund. Finally, Mr. Kibbee spoke about messages to the marketplace and the fact that the

State Fund would like to send a positive message to the marketplace. Based on what he has heard today, if in fact the proposal was adopted as it stands today, the message would be that the 800 pound gorilla is alive and well, and will probably be 900 pounds soon.

Jim Ahrens of the Montana Hospital Association (MHA) stated that for 15 years hospitals have subsidized a lot of what is going on in the State Fund by taking substantial discounts. The MHA does not have a position on privatization. The subsidies started in 1987 as a temporary fix, and became law in 1991 as a permanent fix. In 1997 the MHA worked with Senator Harp to get their payment rate at 69% of charges, which are different than costs. At that time, the MHA was subsidizing the State Fund at about \$12 million per year. That is a built in factor, and the hospitals take the discounts. The MHA thinks it is time for a reasonable payment rate for hospitals, which provide a substantial amount of care to injured workers. Mr. Ahrens would like the committee to think about this, and if it's not part of this consideration, it will be part of the MHA's legislative initiative.

Steve Bender, Deputy Director of the Department of Administration stated that his agency is in the business of providing services to state government. It is of concern to them because for a budget cycle, they need to plan on the services they are expected to provide and the volume of those services so they can be priced appropriately. The fact that MSF may or may not consume some of those services provides a certain amount of risk to the Department of Administration and possibly some other agencies. Mr. Bender stated that MSF has been more than willing to work with his agency to mitigate the impact on his and other agencies. The Department of Administration can work with MSF going forward to 2005 and beyond to fine tune the plans and appropriately resource itself and price its services appropriately.

Senator Cocchiarella asked how much lead time the Department of Administration needs to determine its budget and also asked him to address those services MSF wants or does not want. Mr. Bender replied that the Department was required to set its rates last May. The Department looks forward three years, so there is a tremendous amount of uncertainty. They figure out what their average cost is and provide that to the Budget Office. The awkward part is rate budgets. They are built into every agency's budget, and it is very difficult and time-consuming to change them. If the bill passed and the Budget Office wanted to shift costs to other agencies, that would ultimately be done in the free conference committee of House Bill 2. Rates can be adjusted in the legislative process. It is very unusual, but it can be done. The Department has agreed with MSF in principle on how they are going to mitigate costs. Mr. Driscoll asked if the Department of Administration has discussed rent with MSF. Mr. Bender responded that it is his understanding that MSF's \$1 per year lease is up very soon. Normally, the Department would be in the position of charging the normal state agency rental rate, which is about \$6.25. There are tremendous space needs for state government, and the state leases about 40% of its space. Scott Darkenwald suggested that MSF pay a market rate, which is about \$10.50.

Senator Cocchiarella asked why it takes so long to get new software approved through Department of Administration. Mr. Bender replied that when Senate Bill 131 passed, it created the position of Chief Information Officer, and that law also has many requirements. The CIO, Brian Wolf, is from the private sector. He is insistent that before he commits any state funds to a project, the planning has been done up front and a business case has been made to convince him that the project is worthwhile. He has also been personally charged by the budget office to look for redundancies. That adds another element of review.

Senator Cocchiarella asked Jim Ahrens to clarify to the committee that he is talking about hospital rates and fee schedules, which apply to Plan 1, Plan 2 and Plan 3 companies. Mr. Ahrens replied that he would assume that it does.

Mr. Swanson stated that he needed to follow up on Mr. Kibbee's comments. He is right in his comment that on a percentage basis, in the information he handed out, it is a relatively small percentage. However, Mr. Swanson stated that he was also using NCCI data, and his comments this morning were on number of businesses in Montana. On page 6 of the assigned risk document, there are 85% of the businesses in the assigned risk group for NCCI that are less than \$5,000 in premium. \$5,000 and under is 23,000 of MSF's 26,000 customers. Mr. Swanson stated that Mr. Kibbee is right on a premium basis, but the number of businesses in Montana that might fall into an assigned risk pool, according to NCCI information, would be over 80%.

Jacqueline Lenmark of the American Insurance Association provided public comment. The AIA is not yet able to give wholehearted support to the proposal as presented. The AIA is strongly in support of Priority Number 1, especially the strengthening of the language regarding surplus. Ms. Lenmark also brought some additional suggested language from Texas and Maine.

The AIA strongly supports Priority Number 2, which is regulation and oversight by the Insurance Commissioner. The exceptions within Priority Number 2 are still problematic for the AIA, most particularly the fact that MSF would be operating on a different rate making basis, and that the Insurance Commissioner would not have oversight of that ratemaking process. In the last meeting, Senator Cocchiarella asked Ms. Lenmark about measures that Montana's legislature had taken that either discouraged or invited participation in the market. Ms. Lenmark stated that one measure she neglected to mention in the last meeting was the fact that the legislature enacted a competitive rating law that has substantially improved the marketplace as far as private carriers are concerned. The way that law operates is for NCCI to file loss costs with the Insurance Commissioner from which all insurance carriers must then build their rates by adding the expense component. The Insurance Commissioner can then disapprove the rates if they are excessive, inadequate, or unfairly discriminatory. The AIA sees no reason why MSF should make their rates in a different manner, and advocates that MSF should use the same class codes and rating mechanism. Ms. Lenmark stressed that she acknowledges the serious problem that rate suppression presents to a state, to companies and to the stability of a system. The AIA believes that with the competitive

rating law, other safeguards, and audit functions, that will bring a more competitive and uniform atmosphere or marketplace. The AIA advocates fewer exceptions.

Regarding Priority Number 4, continuing as sole insurer for state agencies, the AIA has historically taken the position that as the stability of MSF has been enhanced, MSF should continue to have access to some of those exclusive markets. Ms. Lenmark stated that some people at the meeting would recall testimony from the State Fund that at some point that exclusive market should be taken away, and that they should compete in the marketplace along with the rest of the companies, while still continuing to operate as the market of last resort. The AIA would support that objective, and believes that if MSF is going to be in the marketplace, then they should compete in the market in the same manner as other carriers. The AIA has supported going slowly in the past. The changes that are being contemplated in the proposal are significant enough that the exclusive market should be looked at phasing out or taking out altogether.

The AIA has no objection to the purchase or lease of the office building, but it should be done at fair market value.

The AIA supports Priority Number 6, which is collection of premium tax. That is assuming that their book of business is appropriately priced and that they are going to operate in the market on the same basis as other companies.

The AIA absolutely opposes the participation of MSF in the guaranty fund. MSF writes one line of insurance in one state, and it has a very significant portion of the market share. It is in a very strong fiscal position right now. Should another company go insolvent, and the members of the guaranty fund be assessed, then MSF would be assessed for a significant portion of other member companies' insolvencies, further jeopardizing its stability. Because it writes only one line of insurance in one state, the AIA believes that it is more vulnerable. If it is not operating under the same rating laws and the same regulation as other companies, it is potentially more susceptible to insolvency. Ms. Lenmark acknowledged that MSF makes a very strong argument about its financial strength, oversight, and management that is in place right now. She stated that on an individual basis, she does not think that better auditors or management could be found. However, the AIA's position is based on a much longer view. Because MSF is a creation of statute, the statutory scheme needs to acknowledge any level of management or inadequacies in management that might come in the future. For those reasons, the AIA would advocate that the Insurance Commissioner have full regulatory authority. If that does not happen, the AIA would not welcome MSF into the guaranty fund.

At the last meeting, Senator McNutt asked Ms. Lenmark about the market share of the 410 companies Ms. Lenmark represents, and how often they have come and gone in the market. Ms. Lenmark provided a copy of a market share report dated November 2001 from the American Insurance Association. It provides the total market share of AIA member companies, and the individual market share of the top ten AIA writers and

the top ten writers in the market, including MSF. Ms. Lenmark stated that she is not able to provide details on when an individual company came and left the market. With some significant effort, such a detailed report could possibly be developed. Senator McNutt responded that he was just trying to get an idea of how many have come and gone, and stated that this report would probably be sufficient.

Ms. Lenmark handed out a paper entitled "Elements of State Fund Legislation", which are elements that the AIA would look for or support in any state that is contemplating maintaining a state fund. The AIA is in support of the three-way system, and therefore cannot support the creation of an assigned risk pool. The AIA feels that it is not to the advantage of employers, and if the committee is contemplating an assigned risk pool, that also contemplates eliminating the State Fund. The handout gives the committee the fifteen most important issues or elements that the AIA would look for and support in any state fund legislation, many of which are already in place in Montana, or in the proposed legislation.

Jack Morgenstern, who appeared as an individual/employer from Lewistown, stated that he is passionate about the workers' compensation system, because in the early 1990's his business was threatened with double-digit escalation in workers' comp. Subsequently, he became a part of a group that organized a self-funded group for his industry, and then served a term on the State Fund Board of Directors. Mr. Morgenstern stated that he appreciated the committee and all of the material that the committee has to process, so he would like to take a more global look at the system and express his support for the State Fund's proposal. If MSF's competitors agree on one thing, it would be that the insurance business is competitive. The State Fund needs the freedom to compete to the greatest degree of efficiency. Years ago, the legislature took a bold step to allow the State Fund to operate like a business. If MSF is to operate like a business, MSF needs to be given the proper tools. The downside to these priorities seems very minimal and reversible. There are other states to lean on. Certainly the goals are to protect the long term integrity and financial position of MSF, and to protect its surplus ratios from future attack. Secondly, the business needs to operate efficiently. Mr. Morgenstern asked the committee to think about the more intangible things that have to do with business. He stated that he thinks name means everything. The fiduciary responsibility for MSF lies with the Board of Directors, who are serious, competent, business-oriented directors. Mr. Morgenstern encouraged the committee to give MSF's priorities serious consideration.

Senator Cocchiarella asked Mr. Morgenstern if he is currently on the Board of Directors. Mr. Morgenstern replied that he is not. Senator Cocchiarella asked if he was self-insured at the time he was a Board member or if he was insured with MSF. Mr. Morgenstern replied that he has two companies, one of which is self-insured and the other of which is insured with MSF.

Senator McNutt stated that the committee needs to look at the priorities, and discuss what elements the committee can agree upon.

Murray Steinman, facilitator, stated that the committee will mostly be working with Priority 1. He stated that he took MSF's handout and broke it down into a couple of components, then added one or two things that he believes are intrinsically related. The goal is to find out if these are items the committee wants to even consider. The following elements were placed on the board:

- MSF would be a public corporation
- Exempt from state's operating requirements
- Protect surplus
- Name change
- Employees

Mr. Steinman suggested that the committee start the discussion with the above listed points, then move on to the other points.

Senator Cocchiarella stated that the group needs to decide whether or not to consider an assigned risk pool, which means getting rid of the State Fund and/or selling the State Fund, and see if there is a consensus about not selling the State Fund and not having an assigned risk pool. Mr. Steinman suggested starting with the assigned risk pool and asked if there were any strong feelings about having an assigned risk pool. Mr. Jones replied that an assigned risk pool and a state fund are not mutually exclusive options. He also stated that during the first meeting he made a proposal considering the sale of MSF and getting information developed for that, and there was a general agreement not to do that. Therefore the committee does not have that information available on the technicalities or legalities of selling MSF. Mr. Steinman asked if Senator Cocchiarella was trying to eliminate the selling of MSF. Senator Cocchiarella replied that she wanted to bring the subjects up, because she believes they either need to be taken off the table or explored further. Mr. Steinman asked if there was any strong feeling about selling MSF. There was a consensus that the committee did not want to sell MSF. Mr. Jones asked a question clarifying that if it is off the table, it is not for consideration by the committee. The committee agreed. The recommendation of the majority was to not sell MSF.

Mr. Steinman asked if there was any interest in pursuing an assigned risk pool. Ms. Huschka asked for clarifications on what type of recommendations would be coming out of the committee. Mr. Wood responded that his understanding of the charge was that the committee is not going to recommend for or against, but is going to put through a bill that is acceptable to the group, but not mention any of those things that aren't acceptable. For example, the committee is not going to take a stand against selling MSF, but is just not going to consider it as part of the bill. Mr. Steinman stated that it was his understanding that the committee would reach consensus on the recommendations that were put forth by MSF and that in the end there would be a report that stated what the committee did and the conclusions that were reached.

Senator McNutt stated that he thinks the goal today is to get some items on or off the table, and in the end the goal is to have a bill draft that the committee has consensus in.

Mr. Wood stated that he does not want an assigned risk pool.

Senator Cocchiarella stated that she does not think there should be a formal voting process or recommendation process. She thinks the committee needs to dispose of or do something with a topic before it can move on to the next one.

Rep. Laible stated that he is not in favor of the assigned risk pool and that he is in support of the status as public corporation. He also stated that MSF should have the same operating requirements as the competition. The surplus needs to be protected, i.e. something similar to what has been done in Texas. He is not in favor of changing the name, and he would like to keep the employees as recommended.

Rep. McKenney stated that he agrees with Rep. Laible, and would like to see all of that still on the table at the next meeting. He has no objection to the name change.

Mr. Driscoll stated that he thinks the laws about the employees should stay the same.

Senator Mahlum stated that he is concerned about the name. If the name is to be changed, he wants to make sure that the name includes workers' comp or state fund. He also is very interested in protecting the surplus, and feels that the employees are taken care of.

Mr. Jones asked if there needs to be further discussion of the Montana Insurance Guaranty Association. Mr. Driscoll responded that there is no good reason for MSF to be in it. Ms. Huschka stated that has been the opinion of the industry, and if the committee agrees, she also agrees. Rep. Matthews asked Mr. Swanson why MSF wants to be in the guaranty fund. Mr. Swanson replied that MSF felt it would be a positive signal. He is not aware of any state funds that have ever been bailed out by a guaranty fund, and it would remove any potential liability from the state. It also seems to be a trend in the industry. Mr. Swanson stated that he did not have a problem with it dropping off. Senator McNutt stated that it appears to him that the risk is more to MSF than to the rest of the industry. Mr. Swanson agreed. Senator McNutt stated that the committee needs to mitigate the increase in premiums as much as possible.

Mr. Wood asked if anyone else had an opinion on the assigned risk pool. Senator McNutt stated that he is not in favor of it. Mr. Driscoll stated that it should be noted in the minutes that there was discussion, and that no one spoke in favor of it. The consensus of the committee was that there was no interest in going forward with this issue.

Mr. Steinman asked the committee to consider the collection of a premium tax. Mr. Driscoll stated that the Governor would probably veto this, because she is not signing any tax bills. Senator Cocchiarella stated that she believes this is a package deal. MSF tried to come up with a package that was acceptable to as many people as possible, and she believes it needs to be approached that way. She stated that she looked at the

cost of business in Montana, which translates to either reductions in benefits to employees or something negative to them. If MSF were to adopt the guaranty fund, costs would go up. She asked why there needs to be a premium tax, which is a cost to business people. She believes that it is very important for the legislature to be responsible for MSF. She does not think the state agencies should be required to insure with MSF, and that they should be free to be self-insured or to be what some would call, "an opportunity for everyone to pursue as customers." She believes that self-insurance is the best kind of worker's comp insurance, and the state could save money. Some people do not like the fact that state agencies are still captive. State agencies need to be on their own as part of a package deal. MSF should still continue as the insurer of last resort. Senator Cocchiarella believes that MSF should be more like a public corporation and should be freed from some of the encumbrances of being a typical state agency. The employees should be left alone. She would like to talk more to the Department of Administration about letting MSF go off on its own regarding technology and check writing, because she feels there may be risks that nobody has uncovered yet.

Senator Mahlum asked Senator Cocchiarella about her suggestion to let all state agencies procure their own insurance. Who is going to give the final authority in the department? Mr. Wood and Senator Cocchiarella stated that all the agencies would have to be one group. Then, there would be a situation where private insurers and MSF could try to sell them insurance, or they could be self-insured. Senator Cocchiarella stated that the state should be pursuing self insurance, and pulling the university system along with it. Mr. Steinman asked who in the state would make the decision. Senator Cocchiarella and Ms. Huschka stated that it would be the same way that health insurance is done. Senator Cocchiarella stated that under the current law, if a company wants to be self insured it must apply to the Department of Labor, and be approved and prove that the company has the financial standing to be self insured.

Mr. Steinman asked if the committee would favor MSF purchasing the building. Senator Cocchiarella stated that she does not believe that state should sell MSF the building.

Mr. Wood agreed with most of the things Senator Cocchiarella said. He did disagree with her regarding the premium tax. He thinks that in the element of fairness, if they are going to be a competitive state fund, they should pay premium tax, which is in their proposal. Mr. Wood recommended amending the changes into the Workers' Compensation Act, rather than doing a new bill.

Mr. Steinman stated that there were five items to be left on the list for consideration. He asked if the committee felt that anything should be added to the list. Mr. Jones asked if Insurance Commissioner regulatory authority was included in the list. Mr. Steinman replied that it was not on the list at that point.

Mr. Driscoll stated that the committee needs to pursue the operating requirements issue. If they are so cumbersome on MSF, they must be cumbersome to other state

agencies, and some of them should probably be gotten rid of. He asked if MSF needs out, why don't the other agencies need out.

Rep. Laible asked about the operating requirements and stated that he thought that meant going back to the Insurance Commissioner. If the committee is trying to level the playing field, and MSF is going to become a public corporation and compete in the marketplace, it should have the same requirements that their competition has. He stated a concern about opening up the entire state government and taking it away from MSF, because it is the insurer of last resort. It is a balancing act to say that MSF is the insurer of last resort, and for that they are able to insure the state agencies. He stated a concern that MSF could become so aggressive in their marketing that instead of owning 50% of the marketplace, they could control 80% and there would be no interest in the other carriers.

Rep. McKenney stated that the committee is confusing itself by jumping from priority to priority without making decisions. He stated that he believes they need to consider the priorities in order.

Mr. Steinman suggested that the committee go through the priorities systematically.

Mr. Steinman asked the committee how it felt about Priority Number 2, oversight by the Insurance Commissioner. Ms. Huschka responded that since the committee has not even talked about oversight by the Insurance Department, it can't be off the table. The committee agreed to leave Priority Number 2 on the table.

Mr. Steinman asked the committee about Priority Number 4, continuing as the sole insurer for state agencies. Senator Cocchiarella stated that it needs to stay on the list, and that everything on the priority list needs to stay. Mr. Driscoll stated that the committee should take guaranty fund and premium tax off the list. Ms. Huschka stated that premium tax could not come off. Mr. Jones stated that he would like to see Priority Number 4, stay on the list. Rep. McKenney agreed that it should stay on the list. Senator McNutt also agreed that it should be on the list. He is not convinced that Priority Number 4 should be gotten rid of all at one time. He believes that he needs to weigh the responsibility of insurer of last resort against keeping a sound system. The committee agreed to keep Priority Number 4.

Regarding the purchase of the building, Mr. Driscoll suggested that MSF should rent it at full market value and not buy it. Rep. Laible stated that if the public corporation is still under the control of the legislature, so if the building is sold to MSF it would still be under the legislature. The committee should let MSF buy the building and do maintenance, repairs and pay utilities, and it would still belong to the state. Mr. Steinman stated that it was his understanding that it would transfer some funds to the general fund, and give MSF an asset on its balance sheet. Mr. Swanson stated that it is a win-win, which allows MSF to manage the building. Senator Mahlum stated that he thinks it is a win situation in one way, because of the fact that it is an asset. However, he does not like the idea of giving the money to the general fund, because it will go

someplace. Mr. Wood asked if MSF wouldn't just be replacing one surplus item with another on its balance sheet. Senator Mahlum stated that the money can come back again as surplus is earned. Mr. Driscoll stated that if MSF is still a state agency, and they buy the building, they have not really accomplished anything. It will still be the state's building, since MSF is still a state agency. Rep. McKenney stated that the building is an asset which will appreciate, and the issue needs further discussion. Senator McNutt would like to see this priority stay on the table, but stated that he still has some confusion about a state entity buying a building from the state.

The committee agreed that the issue of collection of premium tax needs to stay on the table.

The committee agreed to not consider MSF being a member of the guaranty fund.

Mr. Jones asked about the consumer protection issue of bringing MSF into the Unfair Trade Practices Act and subjecting them to punitive damages, from which they are currently immune. Ms. Huschka replied that part of that discussion is in the oversight of the Insurance Commissioner's office.

Mr. Wood asked Senator McNutt how many more meetings are contemplated. Mr. Wood stated that before the committee can approve anything, it will have to see the bill. He suggested planning on at least two more meetings.

Senator McNutt stated that for the next meeting the committee needs the language for the public corporation, specifically what MSF wants to opt out of from Department of Administration, and two or three alternatives for language to protect the surplus.

Mr. Steinman asked if there was anything that could be done with the name issue. Senator McNutt stated that Senator Mahlum had a good point on the name issue. He feels that Montana Mutual Insurance Company suggests that the company is selling something more than workers' compensation. He stated that MSF needs to come back to the committee with a name that denotes it is a mutual insurance company and a private corporation, but that it only sells workers' compensation. Rep. Laible stated that the proposed name implies that it could be something other than State Fund, and everyone in the state knows what State Fund does. Mr. Steinman asked if there was a consensus that if there is going to be a name change that it has to be with some kind of recognition of what MSF does. Mr. Swanson asked the committee to leave the issue on the table, and stated that MSF will go back and think on the suggestions that have been made. Senator Cocchiarella stated that it is important that people know where to find the State Fund to buy their workers' compensation insurance.

Senator Cocchiarella asked if the committee could just start working on the proposed bill. Ms. Butler stated that the bill has everything that was proposed, but that the difficulty would come if the committee wanted something less than what was proposed. She could prepare another version, if the committee could give her some idea of what it

wants. The first 14 sections are the primary changes, most of the rest of it is name changes.

Mr. Steinman asked if the committee could do anything further to clarify things. Ms. Butler stated that the biggest issue in drafting the bill is the Number 2 Priority, the Insurance Commissioner piece. Ms. Butler stated that she could work on the current bill, and also work on an alternate bill. Mr. Jones asked if the committee could get the final version. Ms. Butler stated that everything MSF has proposed is in the bill. Mr. Jones stated that on page 8 of the handout, there is a proposal to put MSF under the Unfair Trade Practices Act if they get certain things. Mr. Jones stated that these are the kinds of things that are outside of the bill, and the committee seems to have a moving target. The committee keeps coming back to options, so Mr. Jones proposed that the committee get one bill for the committee to consider at the last meeting. The committee could either vote on individual items or on the whole bill.

Mr. Swanson stated that everything MSF proposed is in the bill draft, and it is only a moving target as the committee makes decisions and MSF considers those decisions, for example, taking out the part about the guaranty fund. The punitive damage piece that Mr. Jones mentioned is in the bill. Mr. Jones asked if MSF would have any objection to putting just the bill before the committee for the committee to discuss. Senator McNutt stated that if the committee wants something out of the bill, it should be done now, so Ms. Butler can come back with a modified bill. Senator McNutt stated that Ms. Huschka has some concerns she would like to convey to the committee, which should probably be done at the beginning of the next meeting. Mr. Wood asked Senator McNutt if he would accept that the bill be written with alternatives. Senator McNutt stated that he does not think the bill needs to be written with alternatives because any decisions can be edited into the bill. Senator Mahlum stated that time is starting to become of the essence and that decisions need to be made at the next meeting.

Mr. Steinman stated that at the next meeting, Ms. Huschka will speak about her concerns at the beginning, then MSF will speak about the name, and then the committee will work on the bill text.

Mr. Swanson asked Senator McNutt if he would like MSF to offer a bill draft without the insurance regulation piece, which is a substantial part of the bill. Senator McNutt replied that his perception is that the committee is not ready to make that decision yet. Senator Cocchiarella stated that she thinks the committee has what it needs already, and that the committee needs to look at itself as a work group. Each member can read the bill and write their thoughts on the page, and use the bill as a working document. The committee should vote on the issues as they go through it and vote on it at the end.

Mr. Steinman suggested that MSF bring a laptop and video projector and edit as the committee works, so everyone can see what the changes are.

Mr. Jones stated that this is the second 100-page bill he has had to go through, and he does not want to have to go through another one. Senator McNutt stated that the current bill draft is the one that committee will be working with, with the guaranty fund edited out. Rep. Laible stated his concern that there are a lot of new sections in the bill, and a lot of new language, for example “the Montana Mutual Insurance Company is exempt from laws that generally apply to state agencies.” The question is going to be, what are those laws? Mr. Steinman stated that one of MSF’s assignments is to bring the specifics to the next meeting. Ms. Huschka stated that there are a lot of repealers, so the committee may need to have access to other code. Senator McNutt stated that some of those questions could be addressed to Eddy McClure.

The priorities left on the table were as follows:

- Public Corp (language)
- No Op requirements
- Protect Surplus
- Name
- Employees
- Oversight/Bad Faith/Punitive Damages
- Sole Insurer
- Buy Building
- Premium Tax

The meeting was adjourned at 5:05 p.m.