

Montana State Fund Restructuring Options – No Change to Limited Change to Complete Privatization

QUESTION: SHOULD MONTANA STATE FUND BE FULLY TREATED IN LAW AS A PRIVATE INSURER?

Status Quo Option

Retain Montana State Fund as it is.

Retained as is means:

- o Rate review and financial audit by Legislative Auditor who contracts with an independent actuary to determine if rates are discriminatory, adequate, not excessive. Actuary also reviews adequacy of reserves. Audit has no direct authority to require change. State Auditor also does a review of the actuary's review.
- o High legislative involvement in some years.
- o Budget reviews by Legislative Finance Committee. Both statutory and GAAP budget reports are provided.
- o Agency monitoring by EAIC, which assigns legislative liaisons to Montana State Fund

State Entity Regulated Mostly Like Other Insurers

Regulate under the State Auditor's Office

Regulated by State Auditor means:

- Insurance commissioner has authority for form filing, rate review, market conduct exams, review to determine financial solvency.
- Insurance Commissioner may rehabilitate, liquidate, and dissolve insolvent insurers.

Regulation under the Insurance Commissioner means choices must be made to determine degree of regulation. These are in Box 1.

Almost Private Option

Regulate under the State Auditor's Office but the remove all state agency-related costs and benefits except for having the Board of Investments handle its investments.

This would mean:

- no vote would be needed to win passage of a constitutional amendment regarding investments of MSF assets.
- a cost to the Public Employees Retirement System for loss of projected participants (not offset until future years by nonparticipation in the system by future MSF employees).
- resolving questions in Box 1.
- other costs to state agencies. See Box 2.

Fully Privatized

Regulated by State Auditor's Office and no longer a state entity.

This would mean:

- a policy determination and most likely a judicial determination of whether State Fund's liabilities and assets are those of the state.
- a constitutional amendment to remove reference to investment of the state compensation insurance fund's assets.
- resolving all questions in Boxes 1, 2, and 3 and Notes listed below.

BOX 1: Under the State Auditor's Office would Montana State Fund:

- A) Continue to serve as a guaranteed market? YES__ NO__ (If No, see Note 1. If Yes, options B, C, D, E, F, G, and H are related.)
- B) Continue to be eligible for federal income tax exemption? See Note 2. YES__ NO__
- C) Be statutorily immune from dissolution by the State Auditor? YES__ NO__ (If No, option D is required to retain the federal income tax exemption per B, above.)
- D) Be subject by statute to its assets (and liabilities?) diverting to the state in case of dissolution? YES__ NO__ (If D is No, then option C should be yes.)

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BOX 1, continued: Under the State Auditor's Office:

- E) If subject to dissolution (no in option C), should participation be required in the Guaranty Association (which covers liabilities if the Montana State Fund is dissolved)? YES__ NO__
- F) If immune from dissolution (yes in option C), should there be an early trigger (e.g. 400% of risk-based capital requirements) to start State Auditor rehabilitation? YES__ NO__
- G) Should there be adverse risk development coverage (in addition to or in lieu of Guaranty Association)? *In addition to?* YES__ NO__ -- OR -- *in lieu of?* YES__ NO__
- H) Should there be offsets/benefits for serving as a guaranteed market? YES__ NO__ [See Options I(a) and I(b)]
- I(a) Should Montana State Fund pay zero __ limited __ or full __ premiums tax?
- I(b) Should MT State Fund be sole provider of state agencies' workers' comp? YES__ NO__
- J) Should Montana State Fund be treated the same as other insurers for punitive damages purposes? YES__ NO__ (If Yes, should both be exempt from punitive damages? YES__ NO__)
- K) Should Montana State Fund be under the fraud and prosecution unit of the State Auditor's Office instead of under the Dept. of Justice? YES__ NO__
- L) Should Montana State Fund have a calendar (not fiscal) budget year? YES__ NO__
- M) Should Montana State Fund have tiered rating allowed in statute? YES__ NO__
- N) Should Montana State Fund (& all insurers) use a higher experience-rating trigger YES__ NO__ and all have same Code Classification Options? YES__ NO__
- O) Should there be a revision in board of directors appointments? YES__ NO__
- P) Should Montana State Fund statutes be in Title 33, not Title 39? YES__ NO__
- Q) Should Montana State Fund get an automatic certificate of approval? YES__ NO__
- R) If Q is NO, should certificate of authority be based on filing, other criteria? YES__ NO__
- S) Should the determination of market concentration include MT State Fund? Yes__ NO__
- T) Should Montana State Fund be allowed discretion for assumed business name? Yes No

BOX 2: As an entity only tied to the state through very limited connections? (Almost Private Option):

- AA)** Explicitly provide in statute that the state's full faith and credit does/ does not back Montana State Fund? YES__ NO__
- BB)** Should all Montana State Fund employees continue as state employees? YES__ NO__ (If YES, skip Options CC through EE.)
- CC)** Should Montana State Fund new employees no longer be part of the Public Employees Retirement System? YES__ NO__
- DD)** Should Montana State Fund employees no longer participate in the state's health insurance plan? YES__ NO__
- EE)** Should Montana State Fund pay to PERS an offset of the cost of removing existing/future employees from PERS? YES__ NO__ (If No, should the general fund pay that cost? YES__ NO__)
- FF)** Should Montana State Fund be under Title 5 Legislative Audit statutes (yearly/biennial financial compliance audits as a component unit of state government)? YES__ NO__
- GG)** Should Montana State Fund get authority to lease, etc. Y__ N__
- HH)** Should Montana State Fund be exempt from state services like e-mail, tort, property-casualty insurance, etc.? YES__ NO__

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BOX 3: Moving Montana State Fund toward Privatization (requires recognition of certain components in Boxes 1 and 2):

A-1) -- Amend Montana Constitution to remove Montana State Fund references within the public investment sections ([Article VIII, Section 13](#)). This requires a vote by the people, presumably on a referendum passed by the Legislature. Requires a contingent enactment date only upon positive vote.

A-2) – Determine whether assets are those of Montana State Fund or of the state, or a combination of both, and the associated value.

A-3) -- If the assets are considered assets of Montana State Fund, then determine a timeline to remove Montana State Fund assets from being invested under the Board of Investments. The timing would have to allow for transfer of assets to the financial direction of and investment by Montana State Fund. (The Montana State Fund building in Helena is considered an asset of the Montana State Fund and it was completely paid for by Montana State Fund with no bond outstanding.) The Board of Investments will need time to account for a \$1.3 billion or so loss in its portfolio.

A-4) –Determine if Montana State Fund is to pay for cost of removing Montana State Fund employees from the Public Employees Retirement System if no longer considered state employees. (Requires an actuarial determination using a formula similar to that developed to allow employees to transfer to a defined contribution plan in [19-3-2114, MCA](#)).

A-5) Other?

Note 1: Because Montana requires workers' compensation coverage of most employees (except those that are exempt), some sort of back-stop generally is considered necessary to make sure that workers' compensation coverage is available to the hardest to insure. That back-stop has been the State Fund since workers' compensation first went into effect in 1915. Back-stops typically are either one entity serving as the guaranteed market or a risk pool in which all workers' compensation insurers would participate, except perhaps self-insurers.

Note 2: Certain requirements are necessary to be eligible for a federal income tax exemption. These require: 1) the entity be created and operate by state law exclusively to provide workers' compensation insurance but may provide work comp-related insurance; 2) the state must provide either start-up costs or backing with the state's full faith and credit; 3) the entity serves as a guaranteed workers' compensation provider (which does not mean they provide cheap coverage, just that they must offer coverage); 4) the assets of the entity revert to the state upon dissolution or state law must prevent dissolution of the entity; and 5) the entity has a majority of its board of directors appointed by the governor or the legislature. The law is: 26 USC 501 <http://codes.lp.findlaw.com/uscode/26/A/1/F/I/501> (27 (B) Any organization (including a mutual insurance company) if – (i) such organization is created by State law and is organized and operated under State law exclusively to – (I) provide workmen's compensation insurance which is required by State law or with respect to which State law provides significant disincentives if such insurance is not purchased by an employer, and (II) provide related coverage which is incidental to workmen's compensation insurance, (ii) such organization must provide workmen's compensation insurance to any employer in the State (for employees in the State or temporarily assigned out-of-State) which seeks such insurance and meets other reasonable requirements relating thereto, (iii)(I) the State makes a financial commitment with respect to such organization either by extending the full faith and credit of the State to the initial debt of such organization or by providing the initial operating capital of such organization, and (II) in the case of periods after the date of enactment of this subparagraph, the assets of such organization revert to the State upon dissolution or State law does not permit the dissolution of such organization, and (iv) the majority of the board of directors or oversight body of such organization are appointed by the chief executive officer or other executive branch official of the State, by the State legislature, or by both.

Note 3: The State Auditor is required under [33-16-1020, MCA](#), to determine if the workers' compensation market is competitive. Currently only private insurers, which have a minority market share, are evaluated and Plan 3, the State Fund, is not considered. If a market is not competitive, the State Auditor has authority to delay rates and may find rates are excessive.

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Timeline and Potential Continuum regarding State Fund

