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.

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.) (continued next page)

Almost Private Option

Regulate under the State Auditor's Office but the remove all state agencyrelated 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.

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

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

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

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 (<u>Article VIII, Section 13</u>). 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 https://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 or

Note 3: The State Auditor is required under <u>33-16-1020, MCA</u>, 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.

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

Timeline and Potential Continuum regarding State Fund

1915 1975 1989 1990 Today

1915 – Industrial Accident Board provides workers' compensation as the state "Plan 3"

provider.

1975 -Legislature designates Division of Workers' Compensation within the Department of Labor and Industry in place of Industrial **Accident Board** as the Plan 3 provider and trustee of the industrial accident account.

1989 - Duties of "state fund" became the duties of a state compensation mutual insurance fund, a nonprofit, independent public corporation established for the purpose of allowing an option for employers to insure their liability for workers' compensation and occupational disease coverage ...". (39-71-2313) The state fund operates as a domestic mutual insurer as defined in Title 33. the Insurance Code. Also is subject to Title 33.

1990 (Special Session) – Status Quo Option

The Legislature dropped the reference to State Fund being a domestic mutual insurer under Title 33, although the name remained the "State Compensation Mutual Insurance Fund", with the same description as in 1989 of a nonprofit, independent public corporation, etc. The 1993 Legislature directed dropping the term "mutual" from the name.

State Fund is subject to laws applying to state agencies unless specifically mentioned in law as exempt. 39-71-2314, NOTE A: State Fund no longer an "insurer" subject to Title 33.

NOTE B: Liabilities of "old fund" and "new fund" separated for injuries before/on and after July 1, 1990.

Farther along the continuum tomorrow? Three main possible options:

DATE TBD – Option 1:
"Limited Regulation by
Insurance Commissioner
Option"

"State fund' remains a state agency with continuation of most current state obligations and benefits (see Box 3, next page) but regulation is under the Insurance Commissioner. By remaining a state agency

remaining a state agency with regulation by the insurance commissioner, certain exemptions from insurance law would have to be included, such as preventing the Insurance Commissioner from dissolving the State Fund. (That is only a legislative prerogative.) Other options are: does the State Fund still serve as a guaranteed market or pay the premium tax?

DATE TBD – Option 2: "All But Private Option"

"State fund' remains a state agency only for the purpose of using the **Board of Investments** and being exempt from federal tax. The latter exemption includes the requirements to provide a guaranteed market for workers' compensation, dissolution limited to action by the Legislature, and appointment of a board of directors by the governor. NOTE C: A constitutional

amendment would not be required. NOTE D: State Fund employees may or may not be state employees

not be state employees, having a cost impact on the public pension system.

DATE TBD – Option 3: "Privatization Option"

The Legislature provides a timeline to separate "State Fund' as a state agency. The timeline must allow for a public statewide vote asking to remove the State Fund reference in the Montana Constitution related to investments. Decisions would include whether to create a risk pool so that all insurers rotate in providing work comp coverage to those unable to get coverage elsewhere. The new entity would not: be exempt from federal tax, have a politically appointed board, or be exempt from the premium tax. NOTE E: Would the state be

NOTE E: Would the state be liable for pre-separation work comp claims?

Note F: Are there constitutional issues with state agency assets going to a private company?