A Report to the Montana Legislature

Financial-Compliance Audit

Montana State Fund

For the Fiscal Year Ended June 30, 2015

December 2015

Legislative Audit Division

14-05B

Financial-Compliance Audits

Financial-compliance audits are conducted by the Legislative Audit Division to determine whether an agency's financial operations are properly conducted, the financial reports are presented fairly, and the agency has complied with applicable laws and regulations. In performing the audit work, the audit staff uses standards set forth by the American Institute of Certified Public Accountants and the United States Government Accountability Office. Financial-compliance audit staff members hold degrees with an emphasis in accounting. Most staff members hold Certified Public Accountant (CPA) licenses.

The Single Audit Act Amendments of 1996 and OMB Circular A-133 require the auditor to issue certain financial, internal control, and compliance reports in addition to those reports required by Government Auditing Standards. This individual agency audit report is not intended to comply with these reporting requirements and is therefore not intended for distribution to federal grantor agencies. The Legislative Audit Division issues a statewide biennial Single Audit Report which complies with the above reporting requirements. The Single Audit Report for the two fiscal years ended June 30, 2013, was issued March 28, 2014. The Single Audit Report for the two fiscal years ended June 30, 2015, will be issued by March 31, 2016. Copies of the Single Audit Report can be obtained by contacting:

Single Audit Coordinator
Office of Budget and Program Planning
Room 277, State Capitol
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Helena, MT 59620-0802

Legislative Audit Division
Room 160, State Capitol
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Reports can be found in electronic format at:
http://leg.mt.gov/audit

LEGISLATIVE AUDIT DIVISION

Tori Hunthausen, Legislative Auditor
Deborah F. Butler, Legal Counsel

Deputy Legislative Auditors:
Cindy Jorgenson
Angus Maciver

December 2015

The Legislative Audit Committee
of the Montana State Legislature:

This is our financial-compliance audit report of the Montana State Fund, a component unit of the state of Montana, for the fiscal year ended June 30, 2015. This report does not include any audit recommendations. On page A-1, you will find the Independent Auditor's Report. We issued an unmodified opinion on the financial statements, which means the reader can rely on the information presented.

Montana State Fund's response to our audit is on page C-1. We thank the Montana State Fund President/CEO and his staff for their cooperation and assistance during the audit.

Respectfully submitted,

/s/ Tori Hunthausen

Tori Hunthausen, CPA
Legislative Auditor

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Phone (406) 444-3122 • FAX (406) 444-9784 • E-Mail lad@mt.gov

Table of Contents

Appointed and Administrative Officials

Montana State Fund	Laurence Hubbard, President/CEO	
	Mark Barry, Vice President, Corporate Support	
	Richard Duane, Vice President, Human Resources	
	Julie Jenkinson, Vice President, Insurance Operations	
	Peter Strauss, Vice President, Insurance Operations Support	
	Nancy Butler, General Counsel	
	Al Parisian, Chief Information Officer	
		Term Expires
State Fund Board of Directors	Lance Zanto, Chair	2017
	Joe Brenneman (through November 12, 2015)	2015
	Jack Edward Owens (as of November 12, 2015)	2019
	Wayne Dykstra (through October 19, 2015)	2015
	Matthew C. Mohr (as of October 19, 2015)	2019
	Bruce Mihelish	2017
	Richard Miltenberger	2017
	Lynda Moss	2017
	Jan VanRiper	2019
	Laurence Hubbard, President/CEO - ex officio nonvoting member	

For additional information concerning the Montana State Fund, contact:

Laurence Hubbard, President/CEO
855 Front Street
Helena, MT 59604
(406) 495-5015

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Montana Legislative Audit Division

Financial-Compliance Audit
Montana State Fund
For the Fiscal Year Ended June 30, 2015

December 2015 | 14-05B | Report Summary

Montana State Fund will be transitioning to a calendar year reporting basis, and after fiscal year 2015 will no longer report on a fiscal year ending June 30th. Per Chapter 320, Laws of 2015, (SB123), MSF will be under the regulatory authority of the Insurance Commissioner and will operate on a calendar-year basis beginning January 1, 2016. In order to comply with these new requirements State Fund will have a six-month reporting year ending December 31, 2015, and issue financial statements for the period July 1, 2015, to December 31, 2015.

Context

Montana State Fund (MSF) is established by Title 39, Chapter 71 of the Montana Code Annotated. MSF is governed by a seven-member board of directors appointed by the governor. The MSF board of directors appoints the President/CEO who oversees MSF day to day operations.

Operating as a nonprofit, independent public corporation, MSF provides a fair and equitable system of workers' compensation insurance. MSF functions like a private insurance carrier in a competitive marketplace which guarantees coverage to all employers in Montana.

MSF does not receive funding from the General Fund. Instead, revenue for MSF comes primarily from insurance premiums and investment income. Revenues from insurance premiums and investment income were \$164.6 million and \$42.5 million, respectively in fiscal year 2015. Expenses for MSF are primarily for workers' claims. Benefits and claims expenses were \$89.2 million in fiscal year 2015.

Results

We performed work over MSF internal controls and business processes related to the payment of claim expenses and the reserves for future claims, the collection of insurance premium revenue, investment activity, reinsurance activity, and compliance with selected laws and regulations. We also considered the overall reasonableness of the financial statement presentation.

We issued an unmodified opinion on the financial statements and this report does not contain any recommendations. The prior report also did not contain recommendations to MSF.

For a complete copy of the report (14-05B) or for further information, contact the Legislative Audit Division at 406-444-3122; e-mail to **lad@mt.gov**; or check the web site at **http://leg.mt.gov/audit**
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Call toll-free 1-800-222-4446, or e-mail **ladhotline@mt.gov**.

Chapter I – Introduction

Introduction

We performed a financial-compliance audit of the Montana State Fund (MSF) for the fiscal year ended June 30, 2015.

The objectives of this audit were to:

1. Determine whether the MSF's financial statements present fairly the financial position, results of operations, and cash flows for the fiscal year ended June 30, 2015.
2. Obtain an understanding of the MSF's control systems to the extent necessary to support our audit of MSF's financial statements, and if appropriate, make recommendations for improvement.
3. Determine whether MSF complied with selected applicable laws and regulations.

Our audit work included testing of MSF internal controls and business processes related to:

- Payment of claim expenses and reservations for future claims.
- Assessment and collection of policy premiums.
- Investment activity.
- Reinsurance activity.
- Compliance with selected laws and regulations.
- Overall reasonableness of the financial statement presentation, including note disclosures.

MSF personnel prepared the financial statements based on accounting information from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) with adjustments. Adjustments are made to present financial activity in accordance with Generally Accepted Accounting Principles (GAAP), such as adjusting the estimated claims liability based on an actuary report and board approval. This report contains no recommendations.

Background

MSF is a nonprofit, independent public corporation that provides Montana employers with an option for workers' compensation and occupational disease insurance, and guarantees available coverage for all employers in Montana. MSF is governed by a seven-member board of directors appointed by the Governor.

MSF management must set premium rates for claims incurred after July 1, 1990, at amounts sufficient, when invested, to carry the estimated cost of all claims to maturity, to meet the reasonable expenses of conducting the business of MSF, and to maintain a surplus over a calculated amount based on the National Association of Insurance Commissioners' risk-based capital requirements for a casualty insurer. The investments of the MSF, per state law, are managed by the Montana Board of Investments and invested in accordance with the prudent expert principle.

Per Chapter 320, Laws of 2015, (SB123), Montana State Fund will be under the regulatory authority of the Insurance Commissioner under the State Auditor's Office, and the reporting period will change from a fiscal year-basis ending June 30 to a calendar-year basis ending December 31. The act is effective January 1, 2016. Under the new law, by March 1 of each year, Montana State Fund is required to submit financial statements in a regulatory format to the Insurance Commissioner. Financial statements, completed in accordance with GAAP, will also continue to be prepared by Montana State Fund. The audit of GAAP financial statements remains a requirement per §39-71-2361, MCA, and will continue to be audited by our office in support of the audit of the state's basic financial statements.

Independent Auditor's Report

LEGISLATIVE AUDIT DIVISION

Tori Hunthausen, Legislative Auditor
Deborah F. Butler, Legal Counsel

Deputy Legislative Auditors:
Cindy Jorgenson
Angus Maciver

Independent Auditor's Report

The Legislative Audit Committee
of the Montana State Legislature:

Introduction

We have audited the accompanying Statement of Net Position of the Montana State Fund as of June 30, 2015, the related Statement of Revenues, Expenses and Changes in Net Position, and the Statement of Cash Flows for the fiscal year then ended, and the related notes which collectively comprise the Montana State Fund's basic financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this responsibility includes designing, implementing, and maintaining internal controls relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal controls relevant to the Montana State Fund's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Montana State Fund's internal control, and accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as the overall presentation of the financial statements.

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We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Montana State Fund as of June 30, 2015, and the changes in net position and cash flows for the fiscal year then ended in conformity with accounting principles generally accepted in the United States of America.

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Management Discussion and Analysis on page A-5 and the Required Supplementary Information on page A-39 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated December 2, 2015, on our consideration of the Montana State Fund's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the State Fund's internal control over financial reporting and compliance.

Respectfully submitted,

/s/ Cindy Jorgenson

Cindy Jorgenson, CPA
Deputy Legislative Auditor
Helena, MT

December 2, 2015

Montana State Fund Financial Statements

Montana State Fund
(A Component Unit of the State of Montana)
Management Discussion and Analysis
June 30, 2015 and 2014

Montana State Fund (MSF) is a self-sufficient, not-for-profit workers' compensation insurance carrier. Our statutory purpose is to act as a competitive insurance carrier, providing an available market and thereby guaranteeing coverage to all employers in Montana. Operating on the premium dollars paid by the insured employers and the net proceeds from our investments, MSF is not funded by the State general fund for primary business operations. We function like a private insurance carrier in a competitive marketplace and, as provided by law, perform all the functions and exercise all the powers of a private insurance carrier that are necessary, appropriate or convenient for the administration of the Montana State Fund.

MSF has undergone a number of changes since our creation in 1990. We have transitioned from a traditional organizational structure to one that is more adapted to the demands of the information age. Our operational structure includes multifunctional teams that are aligned with specific groups of employers and agents that allow us to work more closely with our policyholders and their injured employees. We continue to strive to improve efficiencies in all operational areas and have made a major investment in our safety management services as we work diligently with Montana employers in developing accident prevention programs. MSF has invested more resources for medical management and provider relations to improve our focus on managing medical costs as medical benefit costs are over half of total claim costs. As our state's economic structure continues to evolve, we stand ready to fulfill our critical role as the guaranteed workers' compensation market for all Montana employers.

MSF also administers and manages the claims remaining in the Old Fund for the State of Montana. The assets of the Old Fund were completely liquidated in 2011 and benefit payments and administrative costs for claims occurring before July 1st, 1990 are fully supported by General Fund resources as required under state law (Section 39-71-2352, MCA). Therefore, the Old Fund is considered to be part of the Primary Government for financial reporting purposes and is not included in the accompanying financial statements.

Overview of the Financial Statements

This overview is an introduction to Montana State Fund financial statements. The financial statements consist of two components: (1) basic financial statements, and (2) notes to the basic financial statements.

The Statement of Net Position presents information regarding all of MSF's assets, deferred outflows of resources, liabilities, deferred inflow of resources, and total net position.

The Statement of Revenues, Expenses, and Changes in Fund Net Position presents the financial results of operations for MSF for the fiscal year. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of the cash flows. Thus, revenues and expenses are reported in this statement for some items that will result in cash flows in future fiscal periods.

The Statement of Cash Flows details the cash used and provided by the various activities of MSF during the fiscal year. However, this statement does not consider unpaid responsibilities which have been established by contract or other underlying events during the fiscal year.

Financial Highlights

MSF continues to deliver high quality services to Montana businesses at the lowest possible cost consistent with sound insurance principles. MSF fosters and supports a competitive insurance market in Montana, offering a competitively priced product based upon actuarially sound rates while still fulfilling our role as the guaranteed market. The Board of Directors approved that there be no change in rates effective July 1, 2014 for policy year 2015.

MSF dividends return to employers a portion of premiums paid to MSF. It is a way for MSF to share our strong financial results with those employers who help make it possible by lowering workplace injuries. Total dividends of $20 million, the largest amount ever, were paid to qualifying policyholders in fiscal year 2015. The Board of Directors, based on analysis of policyholder surplus adequacy and financial results, approves the amount of dividends to be declared. MSF has declared and paid dividends for sixteen consecutive years.

The 2015 legislature passed legislation to move Montana State Fund under regulation by the State Auditor's Office and Title 33, Montana Insurance Code, effective January 1, 2016. The regulation implementation will require significant efforts to prepare for the operational and oversight change. MSF financial reporting will convert from a fiscal year ending June 30th to a calendar year of January 1st to December 31st. The first calendar year period will begin on January 1, 2016 and must be coordinated with State of Montana agencies and processes that remain on the existing fiscal year structure.

MSF continues to monitor the impact of House Bill (HB) 334, a state law that put into place significant changes to the workers' compensation system in Montana. Medical staff and services are utilized to ensure that the appropriate medical treatment protocols are applied and to facilitate more timely scheduling of doctor appointments and medical treatment for our injured employees. MSF looks forward to realizing the improvements intended by HB 334 and the positive benefit it can bring to workers' compensation.

Analysis of Financial Position and Results of Operations

The following analysis presents comparative condensed financial data for MSF.

Net Position (in thousands)

		6/30/2015		6/30/2014
Current and Other Assets	$	244,722	$	314,308
Capital Assets (Net)		29,328		29,764
Investments		1,421,359		1,380,202
Total Assets		1,695,409		1,724,274
Total Deferred Outflows of Resources		1,614		-
Current Liabilities		284,870		336,988
Long-term Liabilities		870,815		887,178
Total Liabilities		1,155,685		1,224,166
Total Deferred Inflows of Resources		4,357		-
Net Position:				
Net Investment in Capital Assets		29,328		29,764
Unrestricted		507,652		470,344
Total Net Position	$	536,980	$	500,108

MSF's overall net position increased during fiscal year 2015 as compared to the end of 2014 in large part because of a reduction in the amount of reserve strengthening contained in MSF's estimated unpaid claims liability. The reserve strengthening is an amount of loss reserves previously approved by the Board above the consulting actuary's central estimates. Reserve strengthening is established to protect MSF against loss development as a result of retroactive court decisions removing provisions of benefit reforms established in law in 2011 as well as the potential for general loss development above the actuary's estimates. MSF experienced \$5.8M of prior year loss development during fiscal year 2015. The MSF Board of directors approved a reduction of \$32.1M at its September 2015 meeting, thereby increasing total net position. The remaining amount in reserve strengthening is \$32.1 million.

During FY15, MSF total net position was also affected by the implementation of GASB Statement 68, *Accounting and Financial Reporting for Pensions*. This statement required MSF to record its allocated share of the State of Montana's unfunded pension liability, and restate beginning net position for the effects of that change that occurred prior to FY15. This restatement of (\$20.3M) significantly reduced the change in net position of \$57.2M shown below. Despite this change in accounting guidance, MSF's net position remains strong. With around \$1.7B in combined assets and deferred outflows of resources to meet \$1.2B of liabilities and deferred inflows of resources, MSF has a net position commensurate with prudent insurance operations.

The largest component of MSF's assets is its investments, which continued to grow in fiscal year 2015. Despite an overall unrealized loss for the fiscal year, due mostly to decreases in bond prices, MSF's portfolio increased about $40.9M. The change in value is summarized in the following display (in thousands):

	2015	2014
Prior Year Market Value	$ 1,380,202	$ 1,278,671
Purchases at Cost	222,306	253,312
Sales	(182,696)	(191,375)
Net Realized Gains	9,310	14,280
Net Accretion of Bonds	(383)	(370)
Unrealized Gain (Loss)	(7,379)	25,684
Current Year Market Value	$ 1,421,359	$ 1,380,202

The most significant MSF liability is estimated claims payable, which decreased from FY14 to FY15 by $29.1M, due to the significant reduction in reserve strengthening discussed above. This liability is increased as new claims for the year are added and decreased as claim payments are made. Additionally, changes to the estimates for prior years can increase or decrease the liability. The changes are summarized in the following display (in thousands):

	2015	2014
Estimated Claims Payable - Beginning	924,598	902,848
Incurred Claims Payable	89,197	132,320
Claim Payments	(118,252)	(110,570)
Estimated Claims Payable - Ending	895,543	924,598

Towers Watson, an independent actuarial firm, prepares an annual actuarial study used to estimate claims liabilities for MSF and provides a range of potential costs associated with claims. MSF management proposed a selected estimate within that range as the estimated claims payable, consisting of unpaid claims, reserve strengthening and claim adjustment expenses. The Board of Directors approved a reserve strengthening reduction of $32.1M in their evaluation of the preliminary year-end financial results.

Changes in Net Position (in thousands)

	6/30/2015	6/30/2014
Operating Revenues:		
Net Premium Earned	$ 164,557	$ 165,272
Total Operating Revenue	164,557	165,272
Operating Expenses:		
Benefits and Claims	89,197	132,320
Personal Services	25,657	23,996
Other Operating Expense	16,695	11,964
Total Operating Expense	131,549	168,280
Net Operating Income (Loss)	33,008	(3,008)
Nonoperating Revenue (Expense):		
Investment Income	42,487	80,878
Other Nonoperating Revenue	1,731	1,548
Dividend Expense	(20,005)	(12,003)
Total Nonoperating Revenue (Expense)	24,213	70,423
Change in Net Position	57,221	67,415
Prior Period Adjustment	(20,349)	-
Beginning Net Position	500,108	432,693
Total Net Position	$ 536,980	$ 500,108

As noted above, MSF's results for FY15 yielded a change in net position of $57.2M after returning $20.0M in dividends to eligible policyholders. Net premium income for both FY15 and FY14 was relatively consistent. The amount of premium written in FY15 was slightly higher than that of FY14, but more of that premium was ceded to reinsurers than in the prior year, resulting in a roughly similar net amount. Premium retention, or the amount of premium that was retained from the prior year, was approximately 90% in FY15.

The FY15 accident year ultimate loss, which is the expected ultimate cost of all claims incurred during the year, was lower than the prior year ultimate loss and resulted in lower benefits and claims expenses in FY15. In addition, the reserve strengthening component of the estimated claims liability was reduced from $64.2M in FY14 to $32.1M in FY15, which caused a substantial decrease in benefits and claims expenses.

Personal services and other operating expenses increased in FY15 as compared to FY14 due to both a general uptick in expense amounts and a significant year-to-year decrease in contingent commission related to MSF's reinsurance program, which increases operating expenses.

The final contributing factor in the $57.2M change in net position is MSF's investment income. While the investment markets did not yield the same overall growth in FY15 that they did in FY14, MSF still recorded $42.5M in investment income due mostly to the earnings on its bond portfolio.

Operating income of $33M coupled with investment income and a $20M dividend resulted in a change in net position of $57.2M. As indicated above, this amount was offset by the one-time prior period adjustment of ($20.3M) to record the historical impact of the defined benefit pension liability.

Montana State Fund
Statement of Net Position
Montana State Fund is a component unit of the State of Montana

	June 30, 2015
ASSETS	
Current Assets	
Cash and Cash Equivalents	$ 33,942,555
Receivables, Net	63,940,256
Securities Lending Collateral	90,946,591
Other Assets	1,211,090
Total Current Assets	190,040,492
Noncurrent Assets	
Investments	1,421,358,984
Reinsurance Receivables	54,681,758
Capital Assets:	
Land	1,139,460
Other Capital Assets, Net of Depreciation	28,188,424
Total Capital Assets	29,327,884
Total Noncurrent Assets	1,505,368,626
Total Assets	1,695,409,118
DEFERRED OUTFLOWS OF RESOURCES	
Deferred Pension Outflows	1,614,023
LIABILITIES	
Current Liabilities	
Accounts Payable	13,362,985
Estimated Claims Payable	125,271,222
Unearned Premium	50,735,660
Securities Lending Liability	90,946,591
Compensated Absences	1,997,464
Policyholder Deposits	2,556,489
Total Current Liabilities	284,870,411
Noncurrent Liabilities	
Estimated Claims Payable	770,272,021
Reinsurance Funds Withheld	77,719,992
Net Pension Liability	16,863,200
Other Post Employment Benefits	5,135,382
Compensated Absences	824,552
Total Noncurrent Liabilities	870,815,147
Total Liabilities	1,155,685,558
DEFERRED INFLOWS OF RESOURCES	
Deferred Pension Inflows	4,357,173
NET POSITION	
Net Investment in Capital Assets	29,327,884
Unrestricted	507,652,526
Total Net Position	$ 536,980,410

The notes to the financial statements are an integral part of this statement.

Montana State Fund
Statement of Revenues, Expenses, and Changes in Fund Net Position
Montana State Fund is a component unit of the State of Montana

	For the Year Ended June 30, 2015
Net Premiums Earned	$ 164,556,709
Operating Expenses	
Benefits and Claims	89,197,465
Personal Services	25,657,005
Contractual Services	6,752,404
Supplies and Materials	597,329
Communications	1,109,787
Travel	205,184
Rent and Utilities	657,711
Repair and Maintenance	1,436,461
Depreciation and Amortization	1,265,771
Other Operating Expenses	4,669,187
Total Operating Expenses	131,548,304
Operating Income (Loss)	33,008,405
Nonoperating Revenue (Expenses)	
Investment Income	42,486,624
Securities Lending Income	505,004
Securities Lending Expenses	(107,299)
Penalties and Interest	60,001
Loss on Retirement of Assets	(19,350)
Dividend Expense	(20,004,917)
Other Income	478,051
Payment From State of Montana	814,922
Total Nonoperating Revenue (Expenses)	24,213,036
Change in Net Position	57,221,441
Total Net Position - Beginning (As Previously Reported)	500,107,581
Prior Period Adjustment	(20,348,612)
Total Net Position - Beginning (As Restated)	479,758,969
Total Net Position - Ending	$ 536,980,410

The notes to the financial statements are an integral part of this statement.

Montana State Fund
Statement of Cash Flows
Montana State Fund is a component unit of the State of Montana

YEAR ENDED JUNE 30,	2015
Cash Flows from Operating Activities	
Receipts for Premiums	169,333,205
Payments to Suppliers for Goods and Services	(15,414,743)
Payments to Employees	(25,216,418)
Payments for Claims	(117,674,429)
Other Operating Receipts	897,221
Net Cash Provided by (Used for) Operating Activities	11,924,836
Cash Flows from Noncapital Financial Activities	
Payment of Dividends to Policyholders	(20,004,917)
Net Cash Provided by (Used for) Noncapital Financing Activities	(20,004,917)
Cash Flows from Capital and Related Financing Activities	
Acquisition of Fixed Assets	(890,423)
Proceeds from Sale of Fixed Assets	47,626
Net Cash Used for Capital and Related Financing Activities	(842,797)
Cash Flows from Investing Activities	
Purchase of Investments	(218,927,287)
Proceeds from Sales or Maturities of Investments	182,313,775
Proceeds from Securities Lending Transactions	505,004
Payments of Security Lending Costs	(101,605)
Interest and Dividends on Investments	41,403,695
Net Cash Provided by (Used For) Investing Activities	5,193,582
Net Increase (Decrease) in Cash and Cash Equivalents	(3,729,296)
Cash and Cash Equivalents - July 1	37,671,851
Cash and Cash Equivalents - June 30	33,942,555

The notes to the financial statements are an integral part of this statement.

Montana State Fund
Statement of Cash Flows
Montana State Fund is a component unit of the State of Montana

YEAR ENDED JUNE 30,	2015
Reconciliation of Change in Net Position to Net Cash Provided by (Used for) Operating Activities	
Change in Net Position	57,221,442
Adjustments to Reconcile Change in Net Position to Net Cash Provided by (Used for) Operating Activities	
Depreciation	973,738
Amortization	292,034
Security Lending Costs	107,299
Security Lending Income	(505,004)
Income on Investments	(42,486,623)
Pension Offsets	(742,261)
Payments of Dividends to Policyholders	20,004,917
Decrease (Increase) in	
Accounts Receivable	(1,326,994)
Due from Component Units of the State of Montana	
Due from Primary Government	
Notes Receivable	
Other Assets	37,941
Increase (Decrease) in	
Accounts Payable	1,999,963
Unearned Premium	2,654,729
Property Held in Trust	(73,828)
Reinsurance Funds Withheld	2,247,000
Estimated Claims Payable	(29,054,337)
OPEB Liability	572,153
Compensated Absences	2,667
Total Adjustments	(45,296,606)
Net Cash Provided by (Used for) Operating Activities	11,924,836

The notes to the financial statements are an integral part of this statement.

Montana State Fund
(A Component Unit of the State of Montana)
Notes to Financial Statements
June 30, 2015

1. Summary of Significant Accounting Policies

Description of Business

The Montana State Fund (MSF) is a nonprofit, independent public corporation established under Title 39, chapter 71 of the Montana Code Annotated (MCA). MSF provides Montana employers with an option for workers' compensation and occupational disease insurance and guarantees available coverage for all employers in Montana. MSF is a discretely presented component unit of the State of Montana and results are included in the State's Comprehensive Annual Financial Report. MSF's results are included in the State of Montana's financial reports because of the significance of MSF's financial relationship with the State. MSF is governed by a seven member Board of Directors appointed by the Governor. The Board has full power, authority, and jurisdiction in the administration of MSF. MSF's Board is allocated to the State of Montana, Department of Administration for administrative purposes only.

During the 1990 Montana Special Legislative Session, legislation passed establishing separate funding and accounts for claims of injuries resulting from accidents occurring before July 1, 1990, referred to as the Old Fund, and claims occurring on or after July 1, 1990, referred to as the New Fund. Hereafter, any reference to MSF refers to the New Fund or those claims occurring after July 1, 1990.

MSF functions as an autonomous insurance entity supported solely from its own revenues. All assets, debts, and obligations of MSF are separate and distinct from assets, debts, and obligations of the State of Montana. If MSF is dissolved by an act of law, the assets held by MSF are subject to the disposition provided by the legislature enacting the dissolution with due regard given to obligations incurred and existing (Section 39-71-2322, MCA). MSF administers and manages the claims remaining in the Old Fund for the State of Montana and is the administering entity for recording the financial activity related to receipt and disbursement of funds and assets held by the Old Fund. Other than the administrative fees paid for the management of the Old Fund claims, no State of Montana General Fund money is used for MSF operations.

Prior Period Adjustment

During fiscal year 2015, MSF implemented GASB Statement 68, *Accounting and Financial Reporting for Pensions,* which requires that MSF record an allocated portion of the State of Montana's unfunded pension liability as well as other amounts related to the pension plan. As part of this implementation, MSF restated its beginning net position in order to record the effects related to prior fiscal years, including an amount for deferred outflows of resources. The net impact of this adjustment was ($20.3M).

Basis of Accounting

MSF uses the accrual basis of accounting, as defined by generally accepted accounting principles, for their workers' compensation insurance operations. Under the accrual basis, revenues are recorded in the accounting period earned, if measurable, and expenses are recorded in the period incurred, if measurable.

Cash and Cash Equivalents

Cash balances include demand deposits with the State Treasury. Cash equivalents are short-term, highly-liquid investments that are both readily convertible to known amounts of cash and so near their maturity that they present insignificant risk of changes in value. MSF participates in the Montana Board of Investments Short Term Investment Pool (STIP). STIP balances are highly-liquid investments with maturities of 397 days or less with the exception of securities having rate reset dates. The STIP portfolio is carried at amortized cost. MSF's STIP balance as of June 30, 2015 was $27.8M.

The STIP investments' credit risk is measured by investment grade ratings given individual securities. The Montana Board of Investment's (BOI) policy requires that STIP investments have the highest rating in the short-term category by one of any Nationally Recognized Statistical Rating Organizations (NRSRO).

Investments

In addition to STIP investments, the BOI invests in long-term securities. Under the provisions of the state constitution, MSF invested assets are managed by the BOI. Securities are stated at fair value as defined and required by GASB Statement 31, "Accounting and Financial Reporting for Certain Investments and for External Investment Pools". Premiums and discounts are amortized using the scientific method over the life of the securities. Net unrealized gains or losses on securities are included in net income in accordance with GASB 31.

The BOI follows the provisions of GASB Statement No. 40 – Deposit and Investment Risk Disclosures. The investment risk disclosures are described in the following paragraphs.

Credit Risk

Credit risk is defined as the risk that an issuer or other counterparty to an investment will not fulfill its obligation. With the exception of the U.S. government securities, the Montana State Fund fixed income instruments have credit risk as measured by major credit rating services. This risk is that the issuer of a fixed income security may default in making timely principal and interest payments. The Board of Investments' policy requires fixed income investments, at the time of purchase, to be rated investment grade as defined either by Moody's or by Standard & Poor's (S&P) rating services. MSF's investment policy, revised in April 2015, states "the maximum fixed income credit risk will be limited to 2% of the total securities portfolio in any one name". The U.S. government securities are guaranteed directly or indirectly by the U.S. government. Obligations of the U.S. government or obligations explicitly guaranteed by the U.S. government are not considered to have credit risk and do not require disclosure of credit quality. The credit ratings presented in the following table are provided by S&P's rating services. If an S&P rating is not available, a Moody's rating has been used.

Custodial Credit Risk

Custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, MSF may not be able to recover the value of the investment or collateral securities that are in the possession of an outside party. As of June 30, 2015, all the public securities as well as securities held by the separate public equity account managers were registered in the nominee name for the Montana Board of Investments and held in the possession of the BOI's custodial bank, State Street Bank. The Equity Index funds and real estate investments were purchased and recorded in the BOI's name.

Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the magnitude of any single investment per issuer name. The Montana State Fund Investment Policy requires credit risk to be limited to 2 percent in any one corporate name and 3 percent portfolio limit in non-agency Mortgage Pass-through (MBS) securities. Investments issued or explicitly guaranteed by the U.S. government are excluded from the concentration of credit risk requirement.

In October 2008, the U.S. government extended the explicit guarantee to certain government agencies such as Federal National Mortgage Association (Fannie Mae) and Federal Home Loan Mortgage Corporation (FHLMC-Freddie Mac). Given the explicit guarantee extension, Montana State Fund had no concentration of credit risk exposure to Fannie Mae and Freddie Mac.

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The Montana State Fund investment policy sets an average portfolio duration range of 2-5 years for fixed income securities except in extraordinary circumstances where a shorter duration may be advisable. In accordance with GASB Statement No. 40, the BOI uses effective duration as a measure of interest rate risk. The BOI's analytics software uses an option-adjusted measure of a bond's (or portfolio's) sensitivity to changes in interest rates. Duration is the average percentage change in a bond's price for a given change in interest rates. Prices move inversely to interest rates. The effective duration method incorporates the effect of the embedded options for bonds and changes in prepayments for mortgage-backed securities (including pass-throughs, CMOs and ARMs).

The fixed coupon holdings in the bond portfolio pay a fixed rate of interest until maturity while floating rate securities pay a variable rate of interest until maturity. As of June 30, 2015, the Montana State Fund portfolio held two variable-rate corporate and U.S. government agency bonds. Interest payments on these securities are based on an underlying reference rate, e.g.

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LIBOR (London Interbank Offered Rate).

Montana State Fund investments are categorized below to disclose credit and interest rate risk as of June 30, 2015. Credit risk reflects the bond quality rating, by investment type, as of the June 30 report date. Interest rate risk is disclosed using effective duration. If a bond investment type is unrated, the quality type is indicated by NR (not rated). The credit quality ratings have been calculated excluding non-rated investment types.

State Fund - MU26
Credit Quality Rating and Effective Duration as of June 30, 2015

Security Investment Type*	Fair Value	Credit Quality Rating	Effective Duration
Treasuries	196,639,435	AA+	4.37
Agency/Government Related	282,144,928	AA+	4.03
Asset Backed Securities	54,916,486	AAA	2.18
Mortgage Backed Securities	5,238,166	AA+	2.23
Commercial Mortgage Backed Securities	-		
Financial-Corporate	319,250,698	A	3.58
Industrial-Corporate	267,120,110	A	3.75
Utility-Corporate	45,856,689	BBB+	4.63
Short Term Investment Pool (STIP)**	27,998,663	NR	0.14
Total Fixed Income Investments	$ 1,199,165,175	AA-	3.83
Direct Investments			
Equity Index Fund-Domestic	146,276,741		
Equity Index Fund-International	19,085,192		
Total Equity Index Funds	$ 165,361,933		
Core Real Estate	84,590,118		
Total Direct Investments	$ 249,952,051		
Total Investments	$ 1,449,117,226		
Securities Lending Collateral Investment Pool	$ 90,946,591	NR	0.08***

*For June 30, 2015 the Security Investment Type categories were changed to more acurately reflect the categories reported to the BOI's Board of Directors

**The STIP portfolio is reported at amortized cost in the Fair Value column.

***Previously the Securities Lending Collateral Investment Pool was comprised of the Securities Lending Quality Trust Liquidity Pool and the Securities Lending Duration Pool. In March 2015 all holdings in the Securities Lending Duration Pool were sold.

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Legal and Credit Risk

As of June 30, 2015, the Federal National Mortgage Association and Federal Home Loan Mortgage Corp. remain in conservatorship from September 7, 2008.

On September 14, 2008, Lehman Brothers filed for Chapter 11 bankruptcy. Montana State Fund held two positions of Lehman Brothers Holdings, Inc., $5 million par, 0.0%, 05/25/2010 and $4 million par, 5%, 01/14/2011. During fiscal year 2009, the BOI wrote down the par value of these bonds. As of June 30, 2011, these securities, due to write downs, reported a book value of 20% of their original par value. The BOI sold the $4 million position in Lehman Brothers Holdings, Inc. 5% rate, January 14, 2011 maturity at a price of $26 on December 6, 2011. Because the bonds were previously written down to a price of $20, this sale generated a gain of $257,840. For the remaining $5 million position in Lehman Brothers Holdings, Inc. the BOI applied $259,560 in principal from the October 2013 bankruptcy payment resulting in a book value of $1 as of June 30, 2014. During FY15, payments of $231,782 and $159,392 were received in October 2014 and April 2015, respectively, and were recorded to gain.

In August 2011, S&P downgraded the U.S. AAA bond rating to AA+.

MSF is allowed by Montana Constitution to invest in equity securities, with the restriction that equity securities cannot exceed 25% of total investment book value. The BOI policy for MSF maintains equities in the 8% to 12% range. As of June 30, 2015, the value of equity securities in MSF's portfolio was $75.3M at cost, increased by $90.1M in market value appreciation.

MSF's Investment Policy Statement allows for investment in core real estate, with a targeted allocation of 5% of the total portfolio market value and an acceptable range of 3% to 7%. As of June 30, 2015, the value of core real estate in MSF's portfolio was $75.0M at cost, increased by $9.6M in market value appreciation. Additional investment information can be found in Note 2.

Securities Lending

MSF participates in a securities lending program through the BOI. The BOI is authorized by law to lend its securities and has contracted with the custodial bank, State Street Bank and Trust, "the Bank", to lend the BOI's securities to broker-dealers and other entities with a simultaneous agreement to return the collateral for the same securities in the future. The Bank is required to maintain collateral equal to 102 percent of the fair value of domestic securities and 105 percent of the fair value of international securities while the securities are on loan. On any day, including June 30th, the markets may move in a positive or negative direction resulting in under or over collateralization. The Bank compensates for market movement by recalculating on the following business day to meet the collateralization requirements. The BOI and the Bank split the earnings, 80/20% respectively, on security lending activities. The BOI retains all rights and risks of ownership during the loan period.

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During fiscal year 2015, the Bank lent the BOI public securities and received as collateral: U.S. dollar cash; U.S. Government and government sponsored agency securities; U.S. corporate debt securities and structured securities rated AA-/Aa3 or higher; sovereign debt securities of the G10 nations; and debt securities issued by certain supranational agencies. The Bank does not have the ability to sell collateral securities unless the borrower defaults.

The BOI imposed no restrictions on the amount of securities available to lend during fiscal year 2015. There were no failures by any borrowers to return loaned securities or pay distributions thereon during the period that resulted in a declaration and notice of Default of the Borrower. There were no losses during fiscal year 2015 resulting from a borrower default.

The following table presents the market values of the securities on loan and the total collateral held for fiscal year ended June 30, 2015:

	2015
Securities on loan - market value	$ 164,289,753
Collateral Cash	90,946,591
Collateral Securities	76,802,930
Collateral Total	167,749,521
% of Fair Value	102%

During fiscal year 2015, the BOI and the borrowers maintained the right to terminate all securities lending transactions on notice. The cash collateral received for each loan was invested, together with the cash collateral of other qualified plan lenders, in the Security Lending Quality Trust. The Trust is comprised of a liquidity pool and a duration pool. In March 2015, the BOI sold all of the holding within the duration pool of the Security Lending Quality Trust, which resulted in a loss of $26 thousand. Security lending income offset the entire amount of the loss. Because the securities lending transactions were terminable at will, their duration did not generally match the duration of the investments made with the cash collateral received from the borrower. At year-end 2015, State Street Bank indemnified the BOI's credit risk exposure to borrowers. The average duration and average weighted final maturity for the investment fund is as follows:

	Security Lending Quality Trust
Liquidity Pool	2015
Average Duration	30 days
Average Weighted Final Maturity	115 days

Income earned related to securities on loan for MSF for the fiscal year ended June 30, 2015

$505K (thousand). Expenses related to securities on loan for MSF for the fiscal year ended June 30, 2015 were $107K.

Receivables

At June 30, 2015, MSF had a net receivable balance of $63.9M. The gross receivables for billed premium and claim benefits overpayments are $8.4M, which are then reduced by the estimated uncollectible receivables reported as an allowance for doubtful accounts of $2.0M. Other receivables include $43.4M in unbilled premium, $9.1M in investment income due, $78K in retrospective premium and $197K in notes receivable, all of which are short term. Accounts receivable also includes $4.8M at June 30, 2015 for premium that has been earned but unbilled (EBUB).

Reinsurance Receivables

As part of the aggregate stop loss reinsurance program, MSF records a receivable for each contract year's funds withheld amount until the loss performance for that contract year is known. The receivable is increased as interest accrues and decreased with the development of recoverable or in the event of a commutation. The reinsurance receivables were $54.7M at June 30, 2015.

Equipment, Accumulated Depreciation and Intangible Assets

Equipment and intangible assets are capitalized if the actual or estimated historical cost exceeds $5K and $100K, respectively. Depreciation expense is computed on a straight-line basis for equipment over a period of three to ten years and amortization of intangible assets is computed on a straight-line basis over four years. Amortization of intangible assets is recorded directly to the asset balance. All fixed assets are shown net of depreciation.

Other Assets

Other assets include advances and prepaid expenses.

Land and Buildings

For the fiscal year ended June 30, 2015, MSF financial statements include $1.1M in land and $25.2M in buildings, net of depreciation. Buildings are depreciated on a straight-line basis over a period of 50 years.

Accounts Payable

Accounts payable is a short term liability account reflecting amounts owed for goods and services received by MSF.

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Estimated Claims Payable

The estimated claims payable, also called loss reserves, is established to provide for the estimated ultimate settlement cost of all claims incurred. Estimated claims payable is based on reported aggregate claim cost estimates combined with estimates for future development of such claim costs and estimates of incurred but not reported (IBNR) claims. Towers Watson, an external actuarial firm, prepares an actuarial study that provides a range of potential costs associated with reported claims, the future development of those claims and IBNR. The MSF Board of Directors approved estimates within that range as the estimated claims payable for MSF. For additional disclosure related to the estimated claims payable, refer to Note 4.

Unearned Premium

Unearned premium reflects premium that has been written but not yet earned. The unearned premium was $50.7M at June 30, 2015.

Policyholder Deposits

Policyholder deposits consist of security deposits required for deposit-type policies and secure the policy with cash, letter of credit or certificate of deposit.

Reinsurance Funds Withheld

Reinsurance funds withheld represents the reinsurance funds held on behalf of the reinsurer, a requirement of MSF's aggregate stop loss reinsurance contract. Additional information regarding the funds withheld account can be found in Note 3.

Net Position

Net Position consists of the net excess or deficit of assets plus deferred outflows of resources over liabilities plus deferred inflows of resources. Net Position as of June 30, 2015 was $537.0M.

Premiums

The MSF Board of Directors approves premium rates annually. Generally, policies are effective for the term of the policy period not to exceed 12 months. Premium revenue is recognized over the term of the fiscal year, which runs from July 1 through June 30, as it is earned or when MSF is liable for coverage.

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Policyholders are contractually obligated to pay certain premiums to MSF in advance of the period the premiums are earned. Premium advances are refundable when the policyholder's coverage is canceled and all earned premiums have been credited by MSF.

Basis of Presentation

The financial statements are presented in accordance with generally accepted accounting principles as prescribed by the GASB. MSF insurance operations are classified as an enterprise fund, proprietary fund type. MSF comprises only a part of the State of Montana's enterprise funds. The financial statements in this report reflect the financial position and results of operations and cash flows of MSF.

An enterprise fund is used to account for operations: (a) financed and operated in a manner similar to private business enterprises, where the legislature intends that the entity finance or recover costs primarily through user charges; (b) where the legislature has decided that periodic determination of revenues earned, expenses incurred or net income is appropriate; (c) where the activity is financed solely by a pledge of the net revenues from fees and charges of the activity; or (d) when laws or regulations require that the activities' costs of providing services be recovered with fees and charges rather than with taxes or similar revenues.

Investments are presented in accordance to GASB Statement Number 31, "Accounting and Financial Reporting for Certain Investments and External Investment Pools." STIP is considered an external investment pool, which is defined as an arrangement that pools the monies of more than one legally separate entity and invests, on the participant's behalf, in an investment portfolio. STIP is also classified as a "2a7-like" pool. A 2a7-like pool is an external investment pool that is not registered with the Securities and Exchange Commission (SEC) as an investment company but operates in a manner consistent with the SEC's Rule 2a7 of the Investment Company Act of 1940. If certain conditions are met, 2a7-like pools are allowed to use amortized cost rather than fair value to report net position to compute unit values. The BOI has adopted a policy to treat STIP as a 2a7-like pool. See Note 1, Basis of Accounting – Investments and Note 2 for further discussions of the effect of GASB 31.

2. Investments

MSF has the following recurring fair value measurements as of June 30, 2015:

The amortized cost and market value of MSF's fixed maturity and equity securities as of June 30, 2015, is as follows:

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June 30, 2015	Amortized Cost	Gross Unrealized Gain	Gross Unrealized Loss	Market Value
Government Direct-Indirect	$ 462,276,571	$ 17,128,759	$ 620,967	$ 478,784,363
Government Mortgage-Backed	4,883,959	354,207	-	5,238,166
Corporate Securities Asset-Backed	52,632,158	671,931	134,345	53,169,744
Other Corporate Securities	612,906,681	22,650,400	1,582,842	633,974,238
Other Securities	240,422	-	-	240,422
Equity Securities	75,261,419	90,100,514	-	165,361,933
Core Real Estate	75,000,000	9,590,118	-	84,590,118
STIP *	27,758,241	-	-	27,758,241
Total	$ 1,310,959,451	$ 140,495,929	$ 2,338,155	$ 1,449,117,225

**The STIP portfolio is recorded at amortized cost in the Market Value column.*

The amortized cost and estimated market value of MSF's fixed maturity securities as of June 30, 2015 are shown below at contractual maturity. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

June 30, 2015	**Amortized Cost**	**Market Value**
Due one year or less	$ 91,036,675	$ 92,840,513
Due after one year through five years	619,228,989	643,000,696
Due after five years through ten years	415,434,382	427,697,892
Due after ten years	34,997,986	35,626,072
Total	$ 1,160,698,032	$ 1,199,165,174

During the fiscal year ending June 30, 2015, MSF realized gross gains from sales of securities of $9.5M and gross realized losses of ($157K).

As discussed in Note 1, GASB 31 requires governmental entities to report their investments at fair value. Fair value is defined as the amount at which an investment could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. The adjustment to fair value is reflected as an increase or decrease in investment income.

During the fiscal year ended June 30, 2015, investment income for MSF was $42.5M, which includes an unrealized loss on investments in the amount of $7.4M.

3. Reinsurance

For the fiscal year ended June 30, 2015, MSF ceded premiums to reinsurance companies to

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limit the exposure arising from large losses. These arrangements consist of excess of loss contracts that protect against individual occurrences over stipulated amounts and an aggregate stop loss contract which protects MSF against the potential that aggregate losses will exceed expected levels expressed as a percentage of premiums.

The excess of loss contract provides coverage up to $100 million with a MSF retention of $5 million on the first layer of coverage. The excess of loss protection applies to an individual occurrence with a maximum of $5 million on any one life. The coverage for fiscal year 2015 is as follows:

Contract Period	Reinsurance Coverage
2015	Workers' compensation accidents of up to $5M in excess of $5M, maximum of $5M per any one claimant.
	Workers' compensation accidents of up to $20M in excess of $10M, maximum of $5M per any one claimant.
	Workers' compensation accidents of up to $70M in excess of $30M, maximum of $5M per any one claimant.

The term of the current aggregate stop loss contract is July 1, 2014 through December 31, 2016. The contract provides coverage based on MSF's premium levels, not to exceed 15% of the subject net earned premium. In the event reinsurers are unable to meet their obligations under either the excess of loss contracts or aggregate stop loss contract, MSF would remain liable for all losses, as the reinsurance agreements do not discharge MSF from its primary liability to the policyholders.

Premium revenue is reduced by premiums paid for reinsurance coverage of $11.3M in fiscal year 2015. The aggregate stop loss contract requires that MSF maintain a funds withheld liability account which represents the basic premium portion of the total premium paid for aggregate stop loss coverage. The funds withheld liability account at June 30, 2015 is $77.7M for contracts in place from July 1, 2002 to June 30, 2015. Interest must be accrued on the funds withheld account which resulted in accrued interest of $3.8M for fiscal year 2015.

Estimated claim reserves were reduced by $13.3M for fiscal year 2015, for the amount of reinsurance estimated to be ultimately recoverable on incurred losses due to the excess of loss reinsurance contracts. In fiscal year 2015 the estimated claim reserves were reduced by an additional $22.3M for the amount of reinsurance estimated to be ultimately recoverable on incurred losses due to the aggregate stop loss contract.

As part of the aggregate stop loss reinsurance program, MSF records a reinsurance receivable for each contract year's funds withheld amount until the loss performance for that contract year is known. The receivable is increased as interest accrues and decreased with the development of the recoverable or in the event of a commutation. The reinsurance receivables were $54.7M at June 30, 2015.

MSF also has assumed reinsurance relationships with Zurich American Insurance Company and Argonaut Insurance Company related to Other States Coverage (OSC). MSF assumes risk related to Montana domiciled businesses with operations in other states, which are then covered under MSF's ceded reinsurance contract. Assumed premium is $2.6M for fiscal year 2015. The incurred losses from OSC benefits were $1.3M for fiscal year 2015 and the assumed liability for OSC claims is $2.8M at June 30, 2015.

4. Risk Management

MSF provides liability coverage to employers for injured employees that are insured under the Workers' Compensation and Occupational Disease Acts of Montana. Workers' compensation claims occurring on or after July 1, 1990, are reported in the MSF financials. At June 30, 2015, approximately 24,400 active policies were insured by MSF.

MSF is a self-supporting, competitive state fund and functions as the guaranteed market insurer for employers since workers' compensation insurance is mandatory in Montana. Employers may obtain coverage through private carriers, through MSF, or through self-insurance if they meet certain criteria. Public entities may self-insure or insure through MSF.

Unpaid claims and claim adjustment expenses are estimated based on the ultimate cost of settling the claims including the effects of inflation and other social and economic factors. Towers Watson, an external actuarial firm, prepares an actuarial study used to estimate liabilities and the ultimate cost of settling claims reported but not settled and claims incurred but not reported (IBNR) for MSF as of June 30, 2015. Because actual claim costs depend on such complex factors such as inflation and changes in the law, claim liabilities are recomputed periodically using a variety of actuarial and statistical techniques to produce current estimates that reflect recent settlements, claim frequency, and other economic and social factors. A provision for inflation is implicit in the calculation of estimated future claim costs because reliance is placed both on actual historical data that reflects past inflation and on other factors that are considered to be appropriate modifiers of past experience.

Towers Watson provides a range of potential costs associated with reported claims, the future development of those claims and IBNR. MSF management has selected a central estimate within that range as the estimated claims payable, consisting of unpaid claims and claim adjustment expenses, for fiscal year 2015. The MSF estimated unpaid claims and claims adjustment expenses payable presented at face value, net of estimated reinsurance recoverable were $895.5M, as of June 30, 2015. The estimated claims payable decreased $29M from 2014 to 2015 due to the Board of Directors approval of a $32.1M reduction of

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management reserve estimates. The Statement of Net Position displays this total separated as current and noncurrent estimated claims payable.

State law (Section 39-71-2311, MCA) requires MSF to set premiums at least annually at a level sufficient to ensure adequate funding of the insurance program during the period the rates will be in effect. Anticipated investment income is considered when computing premium rate levels. State law also requires the MSF Board of Directors to establish surplus above risk based capital requirements to secure MSF against risks inherent in the business of insurance.

Changes in Claims Liabilities for the Past Two Years

The following table presents changes in the aggregate liabilities for MSF, net of estimated reinsurance recoverable. The information presented has not been discounted.

	2015
Unpaid claims and claim adjustment expenses at beginning of year	$ 924,597,580
Incurred claims and claim adjustment expenses:	
Provision for insured events of the current year	135,111,395
Increase(Decrease) in provision for events in prior years	(45,913,930)
Total incurred claims and claim adjustment expenses	89,197,465
Payments:	
Claims and claim adjustment expenses attributable to insured events of CY	(24,150,099)
Claims and claim adjustment expenses attributable to insured events of PY	(94,101,703)
Total payment	(118,251,802)
Total unpaid claims and claim adjustment expenses at end of the year	$ 895,543,243

5. Administrative Cost Allocation

State law (Section 39-71-2352, MCA) requires MSF to separately determine and account for administrative expenses and benefit payments for claims for injuries resulting from accidents occurring before July 1, 1990 (Old Fund) from those occurring on or after July 1, 1990 (MSF). The law also limits annual administrative costs of claims associated with the Old Fund to $1.25M. MSF allocated $815K in administration costs to the Old Fund in fiscal year 2015. The administration costs are recorded in non-operating revenue as a payment from the State of

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Montana. Beginning in June 2011, the State of Montana General Fund began making transfers to cover the cost of administering and paying the Old Fund claim benefits.

6. MSF Distributions

During the fiscal year ended June 30, 2015, the MSF Board of Directors authorized a dividend to policyholders. MSF paid dividends to eligible policyholders in the amount of $20.0M for the policy year 2012.

7. Compensated Absences

MSF supports two leave programs, the State of Montana Leave Program, (Traditional Plan) and the MSF Personal Leave Program, implemented in January 2002. The State of Montana Leave Program covers union represented employees who have elected to remain in the plan. These employees accumulate both annual leave and sick leave and MSF pays employees 100% of unused annual leave and 25% of unused sick leave upon termination. MSF also pays 100% of unused compensatory leave credits upon termination to non-exempt employees in the Traditional Plan. The MSF Personal Leave Program covers all non-union employees, union employees hired before July 26, 2006 who have elected to adopt the plan, and all employees hired after July 25, 2007. Employees in the Personal Leave Program accumulate personal leave and extended leave. MSF pays employees for 100% of unused personal leave upon termination but extended leave has no cash value at the time of termination.

The total MSF compensated absences liability is $2.8M as of June 30, 2015.

8. Retirement Plans

MSF and its employees contribute to the Public Employees' Retirement System (PERS), which offers two types of retirement plans administered by the Public Employees' Retirement Board (PERB), a defined benefit retirement plan (PERS-DBRP) and a defined contribution retirement plan (PERS-DCRP).

<u>Defined Benefit Retirement Plan</u>

Benefits provided. The PERS-DBRP is a multiple-employer, cost-sharing plan that provides retirement, disability and death benefits to plan members and their beneficiaries. Benefits are established in state law and may only be amended by the State of Montana Legislature. Members are vested after five years of membership service, which entitles the member to an accrued normal retirement benefit payable at age 60 (or age 65 if hired after June 30, 2011). A member may receive a refund of accumulated contributions in lieu of a pension, thereby forfeiting the right to a monthly benefit. A description of the benefits and eligibility rules for the plan are shown in the following table:

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Member's highest average compensation (HAC)

Hired prior to July 1, 2011 - highest average compensation during any consecutive 36 months;
Hired on or after July 1, 2011 - highest average compensation during any consecutive 60 months;
Hired on or after July 1, 2013 - 110% annual cap on compensation considered as part of a member's highest average compensation.

Eligibility for benefit

Service retirement:

Hired prior to July 1, 2011:	Age 60, 5 years of membership service; Age 65, regardless of membership service; or Any age, 30 years of membership service.
Hired on or after July 1, 2011:	Age 65, 5 years of membership service; Age 70, regardless of membership service.

Early retirement, actuarially reduced:

Hired prior to July 1, 2011:	Age 50, 5 years of membership service; or Any age, 25 years of membership service.
Hired on or after July 1, 2011:	Age 55, 5 years of membership service.

Vesting

5 years of membership service

Monthly benefit formula

Members hired prior to July 1, 2011:

Less than 25 years of membership service: 1.785% of HAC per year of service credit;
25 years of membership service or more: 2% of HAC per year of service credit.

Members hired on or after July 1, 2011:

Less than 10 years of membership service: 1.5% of HAC per year of service credit;
10 years or more, but less than 30 years of membership service: 1.785% of HAC per year of service credit;
30 years or more of membership service: 2% of HAC per year of service credit.

Guaranteed Annual Benefit Adjustment (GABA)

After the member has completed 12 full months of retirement, the member's benefit increases by the applicable percentage each January, inclusive of all other adjustments to the member's benefit.

-- 3% for members hired prior to July 1, 2007
-- 1.5% for members hired on or after July 1, 2007

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Contributions. Contribution requirements for the plan are established in Montana Code Annotated Title 19, Chapter 3, Part 3, and can only be amended by the State of Montana Legislature. All members contribute 7.9% of their compensation. This is a temporary 1% increase for members hired prior to July 1, 2011 and remains the same for members hired on or after July 1, 2011. Interest is credited to member accounts at the rates determined by the PERB. All member contributions will be decreased to 6.9% on January 1 following the actuarial valuation results that project the amortization period to drop below 25 years and remain below following the termination of the 1% additional member contribution rate.

MSF contributes 8.27% of each member's compensation. This was increased from 6.9% to 7.035% on July 1, 2007, 7.17% on July 1, 2009, and to 8.17% on July 1, 2013. The rate will continue to increase .1% each year until 2024. These increased contributions will terminate on January 1 following the actuarial valuation results that project the amortization period to drop below 25 years and remain below following the termination of the additional employer contribution rates. Effective July 1, 2013, contributions are also made to the plan from the Coal Severance Tax Fund. The plan recognized $1,351,735 in MSF (employer) contributions during FY15.

Further information regarding description of the plan is available Montana Public Employees Retirement Administration website: http://mpera.mt.gov/docs/2014CAFR.pdf

Actuarial assumptions. The plan costs and liabilities in the June 30, 2013 actuarial valuation were determined using the following assumptions:

Rate of Investment Return	7.75% (net of investment expenses)
Rate of Wage Inflation	4.00%
Interest on Member Contributions	3.50%
Rate of Increase in Total Payroll	4.00%

Mortality rates were based on the RP-200 Combined Employee and Annuitant Mortality tables, with adjustments for mortality improvements using scale AA. These actuarial assumptions are based on the most recent experience study of the plan, which was completed in 2010.

Discount rate. The discount rate used to measure the total pension liability was 7.75%, which is the assumed long-term expected rate of return on plan assets. The projection of cash flows used to determine the discount rate assumes contractual contribution rates. Based on those assumptions, the pension plan's fiduciary net position is projected to be sufficient to make all projected future benefit payments of current active and inactive employees. Accordingly, the long-term expected rate of return on pension investments was applied to all periods of projected benefit payments to determine the liability.

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The 7.75% long-term expected rate of return on plan investments was determined by considering information from various sources, including historical rates of return, rate of return assumptions adopted by similar public sector systems, and by using a building-block method in which best-estimate ranges of expected future real rates of return are developed for each major asset class. The target allocation and best estimates of arithmetic real rate of return for the asset classes are shown in the following table:

Asset Class	Target Allocation	Expected Rate of Return
Cash Equivalents	2.0%	-0.25%
Domestic Equity	36.0%	4.80%
Foreign Equity	18.0%	6.05%
Fixed Income	24.0%	1.68%
Private Equity	12.0%	8.50%
Real Estate	8.0%	4.50%

The following table displays MSF's proportionate share of the net pension liability using the 7.75% discount rate as well as the proportionate share using 6.75% and 8.75%, a decrease of 1% and an increase of 1%, respectively.

	1% Decrease (6.75%)	Discount Rate (7.75%)	1% Increase (8.75%)
MSF's Proportionate Share of the Net Pension Liability	$ 26,827,610	$ 16,863,200	$ 8,459,198

Plan fiduciary net position. Detailed information about the plan's fiduciary net position is available in the separately issued PERB Comprehensive Annual Financial Report available at the following address: http://mpera.mt.gov/docs/2014CAFR.pdf

Pension liabilities, expense, and deferred inflows and outflows of resources. At June 30, 2015 MSF reported a liability for its proportionate share of the plan's total net pension liability in the amount of $16,863,200, representing a 1.353375% share of the total based on amount of contributions by each employer. The net pension liability was measured as of June 30, 2014, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of June 30, 2013, with updated procedures used to roll forward the liability to June 30, 2014. There were no significant events between the measurement date and reporting date that are expected to have an impact on MSF's proportionate share of the liability.

For the year ended June 30, 2015, MSF recognized pension expense of $1,295,317 and revenue of $455,753 for support provided by the Coal Severance Tax. At June 30, 2015 MSF reported

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deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Actual vs. Expected Experience	$ -	$ -
Changes of assumptions	-	-
Actual vs. Expected Investment Earnings	-	4,357,173
Changes in Proportionate Shares	-	-
Differences Between Actual Contributions and Proportionate Share Contributions	32,197	-
Contributions Subsequent to the Measurement Date	1,581,825	-
Total	$ 1,614,023	$ 4,357,173

The $1,581,825 reported as deferred outflows of resources related to pensions resulting from MSF contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ended June 30, 2016. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to pensions will be recognized in pension expense as follows:

Year ended June 30:	
2016	$ (1,078,561)
2017	(1,078,561)
2018	(1,078,561)
2019	(1,089,293)
2020	-
Thereafter	-

Defined Contribution Retirement Plan

The PERS-DCRP is a multiple-employer plan that provides retirement, disability and death benefits to plan members and their beneficiaries. Benefit terms are established in state law by the State of Montana Legislature. Those terms are as follows:

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Eligibility for benefit
Termination of Service

Vesting
Immediate for participant's contributions and attributable income;
5 years of membership service for the employer's contributions to individual accounts and attributable income.

Benefit
Depends upon eligibility and individual account balance;
Various payout options are available, including: taxable lump sums, periodic payments per participant direction and IRS permitted rollovers.

Member and employer contribution rates are established in state law by the State of Montana Legislature. The member contribution rate for FY15 was 7.9% of member compensation. The MSF contribution rate for FY15 was 8.27% of member compensation. Both the member and employer rates have been temporarily increased by the Legislature and will decrease to 6.9% on January 1 following actuarial valuation results that show the amortization period of the PERS-DBRP has dropped below 25 years and will remain below 25 years following the reduction of both the additional employer and additional member contribution rates.

Pension expense for the plan year was $1,295,317, of which none was outstanding at June 30, 2015.

Deferred Compensation Plan

MSF and its employees are eligible to participate in the State of Montana 457(b) Deferred Compensation Plan administered by the PERB. The Deferred Compensation plan is a voluntary, tax-deferred supplemental retirement plan sponsored by the Montana Public Employee Retirement Board and held in trust for the exclusive benefit of public employees and their beneficiaries. The Plan is authorized by IRC Section 457(b) and is subject to specific Internal Revenue Service's laws and requirements. It allows employees to voluntarily contribute a portion of their compensation on a pre-tax basis. The amount invested, plus interest credited on any fixed options and any gain on the variable options, is not taxable until withdrawn at a future date. MSF incurs no costs for this plan. A summary of eligibility and benefits is shown in the following table:

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Contribution

Voluntary, pre-tax deferral or designated Roth contribution.

Eligibility for benefit

Not available to participant until separation from service, retirement, death, or upon an unforeseeable emergency, while still employed, provided IRS-specified criteria are met.

Vesting

Participants are fully vested in their accounts immediately.

Benefit

Lump sum or periodic benefit payment, at the option of the participant. Based on individual account balances and plan provisions. IRS permitted rollovers are also possible.

9. Leases and Commitments

MSF leases office facilities outside of Helena under various operating leases that expire through February 2019.

MSF leases 350 parking spaces from the City of Helena in a parking garage adjacent to the MSF facility. The cost of the parking spaces is the same monthly rate as equivalent parking passes sold by the City and has the potential to change based on parking rates assigned by the Helena Parking Commission until the lease expires on June 30, 2040.

Rental expenses for FY15 of $439K include $365K for the parking garage lease, $56K for office facility leases and $18K for minor office equipment.

The future minimum rental payments for office and parking space are as follows:

Fiscal Year	Amount
2016	$ 345,599
2017	329,543
2018	318,442
2019	306,995
2020	289,800
Thereafter	5,796,000
	$ 7,386,379

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10. Other Post-Employment Benefits (OPEB)

Beginning with the fiscal year ending June 30, 2008, the State of Montana implemented Governmental Accounting Standards Board (GASB) Statement 45, Accounting and Financial Reporting by Employers for Post-employment Benefits Other Than Pensions. This statement requires the disclosure of employer liability for retiree medical subsidies and other post-employment benefits. The OPEB liability is $5.1M at June 30, 2015.

Post-employment Healthcare Plan Description:

MSF employees and dependents are eligible to receive health care through the State Group Benefits Plan administered by the Montana Department of Administration. In accordance with section 2-18-704, MCA, the State provides optional post-employment medical, vision and dental health care benefits to the following employees and dependents who elect to continue coverage and pay administratively established premiums: (1) employees and dependents who retire under applicable retirement provisions and (2) surviving dependents of deceased employees. For GASB 45 reporting, the State Group Benefits Plan is considered an agent multiple-employer plan and MSF is considered to be a separate employer participating in the plan.

In addition to the employee benefits described in Note 8 Retirement Plans, the following post-employment benefits are provided. Montana Department of Administration established retiree medical premiums vary between $371 and $1,345 per month depending on the medical plan selected, family coverage, and Medicare eligibility. Retirees pay 100 percent of the premiums for medical, dental, and vision. Administratively established monthly dental premiums vary between $22.00 and $68.50; monthly vision hardware premiums vary between $5.76 and $16.76; and both premiums vary depending on the coverage selected. Basic life insurance in the amount of $14,000 is provided until age 65 at a cost of $1.90 per month. The State Benefit Plans reimburse all validated medical claims net of member obligations (annual deductibles and coinsurance of the members' selected medical plan). Dental claims are reimbursed at 50% to 100% of the allowable charges, depending on the services provided. The State acts as secondary payer for retired Medicare-eligible claimants.

Benefits Not Included in the Actuarial Valuation:

The dental and vision benefits are fully-insured and retirees pay 100 percent of the cost for both dental and vision; therefore, no liability for these benefits is calculated in the actuarial valuation. Continuation of the life insurance benefit is not available as an employer-provided group insurance benefit for retirees; therefore, no liability for life insurance is calculated in this valuation.

Funding Policy:

The following estimates were prepared based on an actuarial evaluation prepared as of the year

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ending December 31, 2013 for the Department of Administration and the resulting State of Montana Actuarial Valuation of Other Post-Employment Benefits Plan (plan) contains the MSF data and is available through:

Montana Department of Administration
State Accounting Bureau
Room 255, Mitchell Bldg.
125 N Roberts St
PO Box 200102
Helena, MT 59620-0102

GASB 45 requires the plan's participants, including MSF, to report the annual required contribution (ARC), an amount actuarially determined in accordance with the parameters of GASB Statement 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year of retiree health care costs and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed thirty years. The 2015 ARC is calculated for all the State plan's participants and then allocated to individual participants. The MSF 2015 allocated portion of the ARC is estimated at $754K and is based on the plan's current ARC rate of 5.69% percent of participants' annual covered payroll. The MSF 2015 ARC is equal to an annual amount required each year to fully fund the liability over thirty years.

Actuarial Methods and Assumptions:

Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations. Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents information that shows the actuarial value of plan assets and liabilities. As of the January 1, 2013, actuarial valuation date, the projected unit cost funding method is used. The actuarial assumptions did not include an investment rate of return since no assets meet the definition of plan assets under GASB 43 or 45. Annual healthcare cost trend rates of 10 percent were used for both medical and prescription claims. The unfunded actuarial accrued liability is amortized following a 30-year level percent of pay amortization on an open basis, using a 4.25 percent discount rate and a 2.50 percent payroll growth rate assumption.

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The State finances claims on a pay-as-you-go basis and does not advance-fund the OPEB liability. While this liability is disclosed for financial statement purposes it does not represent a legal liability of the State of Montana or MSF.

Annual Other Post Employment Benefits (OPEB) Cost:

MSF's allocated annual OPEB cost was $797K for the year ending June 30, 2015. For the current year, the components of OPEB cost and changes in net OPEB obligation are as follows:

Annual required contribution	$ 753,759
Interest on net OPEB obligation	199,425
Adjustment to annual required contribution	(156,412)
Annual OPEB cost	796,772
Contributions made	(224,619)
Increase in net OPEB obligation	572,153
Net OPEB obligation - beginning of year	4,563,229
Net OPEB obligation - end of year	$ 5,135,382

The MSF annual OPEB cost, the percentage of annual OPEB cost contributed to the plan and the net OPEB obligation for 2015 and prior are as follows:

Fiscal Year Ended	Annual OPEB Cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation
6/30/2013	739,778	11.99%	3,930,710
6/30/2014	783,312	19.25%	4,563,229
6/30/2015	796,772	28.19%	5,135,382

Funded Status and Funding Progress:

The most recent actuarial valuation available that was completed by the State of Montana was as of January 1, 2013 for the year ending December 31, 2013. This actuarial evaluation is completed every two years with the next valuation to be completed as of January 1, 2015 for the year ending December 31, 2015.

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The MSF allocation of the plan as of the year ending December 31, 2013 was as follows:

Actuarial Accrued Liability (AAL)	$7,288,059
Actuarial Value of Plan Assets	$0
Unfunded Actuarial Accrued Liability (UAAL)	$7,288,059
Funded Ratio (Actuarial Value of Plan Assets/AAL)	0%
Covered Payroll (Active Plan Members)	$18,899,275
UAAL as a Percentage of Covered Payroll	38.56%

11. Contingencies

Susan Hensley v. Montana State Fund Montana State Fund received a Petition for Hearing that was filed before the Workers' Compensation Court in October, 2013. The matter is Susan Hensley vs. Montana State Fund, WCC No. 2013-3235. The matter is fully briefed and is submitted for a decision. Under HB 334, as passed by the legislature in 2011 and codified in 39-71-703 (2), MCA, when a claimant receives a Class I impairment, it is not payable unless the claimant has an actual wage loss as a result of the compensable injury or occupational disease. The law was effective July 1, 2011 and applicable to claims that occurred on or after that date. The petitioner in this matter is challenging the constitutionality of 39-71-703 (2), MCA. State Fund anticipates the chances are remote, but as with any litigated matter there is the possibility of an adverse decision. Should the statute be held unconstitutional, determined to be applicable to other claims and also determined to be retroactively applicable, potential liability is estimated to be at least $2.2 million per year, as based on NCCI initial pricing, and current estimated business volumes. However, based on experience, costs may be substantially higher than the estimate of $2.2 million per year.

Montana State Fund also is involved in a great deal of litigation in the areas of workers' compensation and disputes with policyholders. These are of a generally routine nature and there are no known matters at this time that will have a large and widespread financial impact.

12. Subsequent Events

Montana State Fund commuted two of its excess of loss reinsurance contracts with Canada Life during August 2015. In exchange for $855K, $1.2M of reinsurance recoverables was removed from the estimated claims payable liability.

The Montana State Fund Board of Directors declared a $35 million dividend at their November 20, 2015 board meeting. The dividend will be issued in January 2016 to eligible policy holders for the 2013 policy year.

REQUIRED SUPPLEMENTARY INFORMATION

Risk Management (Financial Statement Note 4)

The following table illustrates how the earned revenues of MSF plus investment income compare to related costs of loss and other expenses assumed by MSF for fiscal years 2006 through 2015. In addition, cumulative amounts related to estimated and actual paid claims are presented. The information allows for comparison of actual and estimated claims and is a basis for developing revenue and claims information. As data for individual policy years mature, the correlation between original estimates and re-estimated amounts is used to evaluate the accuracy of incurred claims currently recognized for less mature policy years.

Risk Management Trend Information

(In Thousands)	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
1. Premiums and Investment Revenue										
Earned	272,253	312,529	297,355	262,096	222,915	218,143	184,006	181,131	190,263	182,600
Ceded	13,618	14,856	14,676	13,702	13,224	11,286	11,501	8,459	9,460	11,310
Net Earned	258,635	297,673	282,679	248,394	209,690	206,857	172,505	172,671	180,804	171,291
2. Unallocated expenses including overhead	40,548	41,947	47,778	49,215	44,188	57,282	49,557	49,515	46,206	52,570
3. Estimated losses and expenses, end of accident year										
Incurred	155,057	170,652	177,100	159,229	137,507	142,989	118,066	128,522	139,145	124,831
Ceded	-	-	-	-	-	9,769	1,099	-	-	-
Net Incurred	155,057	170,652	177,100	159,229	137,507	133,220	116,967	128,522	139,145	124,831
4. Net paid (cumulative) as of:										
End of policy year	30,977	32,708	31,002	29,009	25,475	27,902	24,729	25,706	26,808	24,150
One year later	66,063	67,928	67,034	60,009	52,701	56,502	54,982	50,574	55,957	
Two years later	84,014	85,646	86,268	74,132	66,235	69,918	70,487	64,327		
Three years later	94,091	98,427	95,612	83,737	74,028	76,385	80,144			
Four years later	100,189	104,967	103,337	89,431	78,884	81,578				
Five years later	105,815	109,569	109,144	93,622	82,764					
Six years later	109,993	112,562	113,630	96,935						
Seven years later	113,366	115,195	118,024							
Eight years later	115,181	118,476								
Nine years later	117,877									
5. Re-estimated ceded losses and expenses	-	-	5,503	-	-	5,051	8,535	-	-	-
6. Re-Estimated net incurred losses and expense:										
End of policy year	155,057	170,652	177,100	159,229	137,507	133,220	116,967	128,522	139,145	124,831
One year later	157,711	171,783	174,279	152,886	139,554	134,175	130,507	123,912	125,597	
Two years later	163,433	170,786	173,808	151,738	135,833	133,652	130,281	115,233		
Three years later	164,358	172,038	172,888	151,303	135,253	133,796	117,062			
Four years later	165,313	171,987	172,570	150,212	134,681	133,885				
Five years later	164,613	170,997	167,166	149,230	132,232					
Six years later	164,248	169,555	166,367	147,576						
Seven years later	163,824	168,400	166,418							
Eight years later	162,406	166,588								
Nine years later	161,921									
7. Increase (decrease) in estimated net incurred losses and expenses from end of policy year	6,864	(4,064)	(10,682)	(11,653)	(5,275)	664	96	(13,289)	(13,547)	-

Retirement Plans (Financial Statement Note 8)

Schedule of MSF's Proportionate Share of the Net Pension Liability*

June 30:	2014
Proportionate Share of the Net Pension Liability	1.35%
Proportionate Share of the Net Pension Liability	$ 16,863,200
Defined Benefit Pensionable Payroll	15,132,665
Proportionate Share as % of Pensionable Payroll	111.44%
Plan Fiduciary Net Position as a % of Total Pension Liability	79.90%

Schedule of MSF Contributions*

June 30:	2014
Contractually Required Contributions	$ 1,351,735
Contributions in Relation to the Contractually Required Contributions	1,351,735
Contribution Deficiency (Excess)	-
Defined Benefit Pensionable Payroll	15,132,665
Proportionate Share as % of Pensionable Payroll	8.93%

*This schedule is intended to show ten years of data. Additional years will be presented as they become available.

Other Post-Employment Benefits (Financial Statement Note 10)

As of June 30, 2014, the most recent actuarial valuation available that was completed by the State of Montana was as of January 1, 2013 for the year ending December 31, 2013. This actuarial evaluation is completed every two years with the next valuation to be completed as of January 1, 2015 for the year ending December 31, 2015.

The State of Montana finances claims on a pay-as-you-go basis and does not advance-fund the OPEB liability. Therefore, the funded ratio remains at 0% at June 30, 2015.

Schedule of Funding Progress

Date	Actuarial Value of Assets (A)	Actuarial Accrued Liability (AAL) (B)	Unfunded AAL (UAAL) (B-A)	Funded Ratio (A/B)	Covered Payroll (C)	UAAL as a Percentage of Covered Payroll (B-A)/C)
1/1/2007	$0	$8,079,405	$8,079,405	0.00%	$16,805,676	48.08%
1/1/2009	$0	$6,985,326	$6,985,326	0.00%	$16,766,753	41.66%
1/1/2011	$0	$6,355,058	$6,355,058	0.00%	$19,544,196	32.52%
1/1/2013	$0	$7,288,059	$7,288,059	0.00%	$18,899,275	38.56%

Report on Internal Control and Compliance

LEGISLATIVE AUDIT DIVISION

Tori Hunthausen, Legislative Auditor
Deborah F. Butler, Legal Counsel

Deputy Legislative Auditors:
Cindy Jorgenson
Angus Maciver

Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

The Legislative Audit Committee
of the Montana State Legislature:

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to the financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the Montana State Fund, as of and for the year ended June 30, 2015, and the related notes to the financial statements, which collectively comprise the Montana State Fund's basic financial statements, and have issued our report thereon dated December 2, 2015.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered Montana State Fund's internal control over financial reporting to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Montana State Fund's internal control. Accordingly, we do not express an opinion on the effectiveness of Montana State Fund's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal controls was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Montana State Fund financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination on financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of Montana State Fund's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Montana State Fund's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Respectfully submitted,

/s/ Cindy Jorgenson

Cindy Jorgenson, CPA
Deputy Legislative Auditor
Helena, MT

December 2, 2015

State Fund Response

Montana State Fund

MONTANA
STATE FUND

P.O. Box 4759 • Helena, MT 59604-4759
Customer Service 1-800-332-6102
Fraud Hotline 1-888-682-7463 (888-MT-CRIME)

November 23, 2015

RECEIVED
DEC 0 4 2015
LEGISLATIVE AUDIT DIV.

Ms. Tori Hunthausen
Legislative Auditor
Legislative Audit Division
State Capitol Building, Room 106
Helena, Montana 59620-1705

Dear Ms. Hunthausen:

Montana State Fund (MSF) appreciates the professionalism of the Legislative Audit Division staff in completing the financial-compliance audit of our governmental financial statements. We are pleased with your issuance of an unmodified opinion with no recommendations.

The management and staff of MSF are very proud of our accomplishments and the high level of customer service we provide to Montana employers and employees. We value the Legislative Audit Division's assurance and assistance and value opportunities to improve our operations to ensure Montanans will benefit from a strong Montana State Fund many years into the future.

Sincerely,

Laurence A. Hubbard
President/CEO