

**MONTANA UNIVERSITY SYSTEM -
WORKERS' COMPENSATION PROGRAM**

**AUDITED FINANCIAL STATEMENTS
With Supplemental Information**

June 30, 2017

**MONTANA UNIVERSITY SYSTEM -
WORKERS' COMPENSATION PROGRAM**

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INDEPENDENT AUDITORS' REPORT

Board of Regents - Montana University System Self-Funded
Workers' Compensation Management Committee
Helena, Montana

Report on the Financial Statements

We have audited the accompanying financial statements of the Montana University System - Workers' Compensation Program, an enterprise fund of the State of Montana, which comprise the statement of net position as of June 30, 2017, and the related statement of revenues, expenses and changes in net position, and cash flows for the year then ended, and the related notes to the 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 includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' 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 control relevant to the entity'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 entity's internal control. 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 evaluating the overall presentation of the financial statements.

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 Montana University System - Workers' Compensation Program (an enterprise fund of the State of Montana) as of June 30, 2017, and the changes in its financial position, and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 1 to the financial statements, the financial statements present only the Montana University System - Workers' Compensation Program and do not purport to, and do not, present fairly the financial position of the State of Montana as of June 30, 2017, and the changes in its financial position, or, where applicable, its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 4 through 7 and the schedule of claims development information on pages 23 and 24 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 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.

Report Issued in Accordance with *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated October 17, 2017, on our consideration of Montana University System - Workers' Compensation Program's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, 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 the internal control over financial reporting or on compliance. The report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Montana University System - Workers' Compensation Program's internal control over financial reporting and compliance.

Junkermier, Clark, Campanella, Stevens, P.C.

Helena, Montana
October 17, 2017

MANAGEMENT'S DISCUSSION AND ANALYSIS

Management of the Montana University System Workers' Compensation Program (Program) provides this *Management's Discussion and Analysis* of the Program's financial statements. This narrative overview and analysis of the financial activities of the Program should be read in conjunction with the Program's financial statements and accompanying notes for the fiscal year ended June 30, 2017.

OVERVIEW OF THE FINANCIAL STATEMENTS

The financial statements provide a broad view of the Program's short-term and long-term operations and financial position. These statements were prepared using the accrual basis of accounting with revenues recognized when earned and expenses recognized when incurred, regardless of the related cash flow timing. The financial statements include:

- *Statement of Net Position* - presents the Program's assets and liabilities, with the difference between the two reported as "net position."
- *Statement of Revenues, Expenses and Changes in Net Position* - presents changes to the Program's net position during the fiscal year.
- *Statement of Cash Flows* - shows how changes in balance sheet accounts and income affect cash and cash equivalents, and breaks the analysis down to operating, investing, and financing activities. The cash flow statement reflects the flow of cash in and cash out of the Program.
- *Notes to the Financial Statements* - provide additional information that is essential to a full understanding of the data provided in the financial statements.

Financial Position and Results of Operation

Revenue

Fiscal year (FY) 2017 total revenues were just under \$4.0 million with premiums paid by campuses contributing \$3.84 million and interest earnings contributing the balance of \$157 thousand. The Program utilizes an actuarial analysis to establish annual premium needs and corresponding composite premium rate to meet this need when applied to campus payroll. The MUS Work Comp Committee (Committee), then divides the composite rate into two separate rates that correspond to the National Council on Compensation Insurance (NCCI) risk classes for higher education.

The FY17 rates applied to payroll were approximately 10% less than the FY16 rates, while Montana University System (MUS) payroll increased approximately 5% during that same period. The result was approximately \$500 thousand (9%) less premium revenue in FY17 than in FY16.

The Program earns interest on funds deposited with the Montana Board of Investments' (MBOI) Short Term Investment Pool (STIP) and Trust Fund Investment Pool (TFIP) and from interest bearing bank accounts used to pay claim costs. Total interest revenue was nearly \$157 thousand for the fiscal year ending June 30, 2017, an approximate 14% increase over FY16 interest earnings.

Expenses

Total Program expenses for FY17 were \$2.79 million. Claim payments, ceded insurance premiums, SafetySmart awards and claims administration costs combine for approximately 84% of the Program's expenditures.

- The Program made claim payments of \$1.73 million during FY17 which was up significantly (25%) from FY16 when the claim expense was one of the lowest in the Program's history.
- FY17 ceded insurance premiums totaled \$314 thousand which was nearly unchanged from the prior fiscal year. The Department of Labor and Industry (DLI) mandates all self-insured workers' compensation programs carry excess insurance. Additionally, the Program purchases an "other states" workers' compensation policy to ensure coverage for MUS employees who are living and working outside Montana on a more than temporary basis.

- The Committee authorized \$300 thousand in SafetySmart awards during FY17 with \$285 thousand of the awarded funds spent within the fiscal year, both of which mirror FY16 Safety Smart amounts. SafetySmart was initiated in FY12 as a mechanism for reducing Program net position in a controlled manner consistent with its mission and goals. When authorized, SafetySmart funds are awarded to campuses specifically to enhance workers' safety and to reduce claim frequency and claim severity.
- The Program utilizes a Third Party Administrator (TPA) to managing the Program's claims. The claim administration expense in FY17 was \$187 thousand. The FY17 TPA contract limits annual claims administration cost adjustments to a Consumer Price Index (CPI), but in no event more than 4% per year. A very slight cost adjustment allowed increased TPA expenses between FY16 and FY17; however, due to invoicing/payment timing, the recorded claim adjusting expense was higher in FY16 than FY17.

Net Position

Net position at fiscal year-end was \$14.06 million; an increase of approximately \$1.21 million (9%) over net position at the end of the preceding fiscal year. The increase is largely attributable to \$581 (10%) reduction in long-term (non-current) claim liabilities along with increasing investment returns. Insurance programs acknowledge that it is entirely possible for a given year's losses to exceed premium revenues collected in that year and that equity built through positive results achieved most years can offset larger than expected losses in exceptional years.

The Program tracks numerous benchmarks to evaluate adequacy of its equity or net position. In the Program's experience, the least restrictive benchmark is Risk Based Capital--an insurance industry measure; a more restrictive measure has been DLI's Equity:SIR ratio of 10:1, where the SIR is the Self-Insured Retention (\$750,000) on the Program's excess insurance policy.

The Program's net position exceeds the conservative Equity:SIR benchmark of \$7.5 million. Starting in FY12 and continuing through the present, the Program has taken actions to stem the Program's net position growth. Efforts to reduce net position have been counteracted by a significant reduction in actuarial estimates of prior-year claim liabilities and a trend toward reduced claim frequency and reduced claim severity. Workers' compensation is a long-tailed liability insurance; therefore, actuaries rely on many years of historical data to formulate anticipated losses and revenue needs. As MUS generates more self-funding data, the actuaries rely less on prior insurers' experience and tailor ultimate loss estimates and premium needs more specifically to the self-funded Program data.

Investments

The Program's FY17 total assets (primarily cash and investments) were \$21.50 million, an increase of 3% over prior year, which is a more modest asset growth than the 8% increase from FY15 to FY16. The Program's assets are managed by the MBOI as required by state statute. At FY17 close, approximately 75% of the Program's assets were invested in STIP and 25% in TFIP. Though the Committee's Investment Policy Statement allows up to 35% of Program assets to be invested in TFIP, the Committee's currently approved maximum TFIP investment is capped at \$5 million. TFIP is expected to earn higher yields than STIP, though this higher yield bears higher risks, including loss of principal potential and duration risk. Loss of principal can occur when interest rates go up and duration risk is the loss of immediate access to invested funds. TFIP invested funds are expected to be committed for 3-5 years; however, in the event of need, access to the funds is approximately 60-90 days. STIP funds are typically available within 3 days.

Claim Liabilities

The Program carried total liabilities of \$7.44 million at the close of FY17, a reduction of \$525 thousand (7%) compared to FY16. Estimated claim liabilities account for \$7.30 million (98%) of the total liabilities and were comprised of \$2.16 million current claim liability and \$5.14 million non-current claim liability, also known as Incurred but not Reported (IBNR).

The MUS Program utilizes a Third Party Administrator (TPA) with experienced, senior staff to manage claims and an actuary experienced in workers' compensation to calculate its claim liability and to ensure adequate rate setting and reserving for the liability.

The Program and its actuary will continue to incorporate Montana University System claim data, trends and experience into the estimate of current and non-current claim liability and make adjustments accordingly.

Current Year Financial and Budget Results

	FY 2017 Actual	2017 Budget	Variance
REVENUE Premiums + Non-Op. income	3,995,258	4,065,000	69,742
OPERATING EXPENSES			
Personal services	98,956	100,706	1,750
Operational expenses	666,262	721,920	55,658
Benefits & Claims	1,734,932	3,000,000	1,265,068
OPERATING EXPENSE SUBTOTAL	2,500,150	3,822,626	1,322,476
OTHER EXPENSE - Safety Smart Awards	285,000	300,000	15,000
TOTAL EXPENSES	2,785,150	4,122,626	1,337,476
CHANGE IN NET POSITION	1,210,108	-57,626	1,267,734

Budget Variance FY17

The variations between budget and actual amounts are principally due to the necessary reliance on estimates of system payroll for revenue and estimates of claim costs for expenses prior to the start of the fiscal year.

The Committee adopted a FY17 budget of \$4.07 million. The Program received just under \$4.0 million in revenue through premiums. Because premiums are based on a rate applied to payroll, some variation between anticipated/budgeted revenues and actual revenue is expected.

The most significant line-item variance between budget and actual is with claims and benefits expense. The budgeted benefits and claims expense is an estimate of *ultimate losses* for claims occurring during the policy year, including IBNR, whereas the benefit and claims amount recorded for the fiscal year reflects only those payments made *within* the fiscal year (per accounting rules), so the potential for significant variance is well-recognized. The variance between the budgeted change in net position and the actual change in net position at the close of FY17 is considerably less than the FY16 variance when the claim expense was exceptionally low.

The Committee authorized \$300,000 in FY17 SafetySmart funds but not all authorized funds were spent within the fiscal year.

DLI Benchmarks

Annually, the DLI Self-Insurers' Regulatory Department conducts an analysis and determination of the Program's financial ability to meet its obligations. The Program is meeting all DLI benchmarks.

Currently Known Facts, Decisions or Conditions

Currently known facts, decisions, or conditions that are expected to have an impact on the Program's financial position or on the results of operations are summarized below:

- The Committee initially adopted an FY18 composite premium rate of \$0.82/\$100 payroll with the expectation of generating approximately \$3.78 million in FY18 revenue. In October 2017, the Committee adopted a premium rate holiday for FY18 with no further premiums being owed and those already paid to be returned. The Program intends to access its fund balance to meet operational costs during the fiscal year and thereby reduce its net position.
- \$500,000 in Safety Smart funds were authorized for distribution to campuses during FY18.

- The Program will continue to receive reimbursements on a FY09 claim that has pierced the SIR and is expected to remain open for the foreseeable future. A second claim was reported to the excess carrier in FY13; however, those costs are limited to statutory survivor benefits and are not expected to exceed the excess \$500,000 SIR until 2028. (Note: SIR was raised from \$500,000 to \$750,000 starting in FY14).
- The building in which the Office of Commissioner of Higher Education (OCHE) leases office space and had a lease agreement through FY19 has been sold. OCHE may relocate office space within Helena prior to December 2018 and lease rates for the Program may change.
- The Program underwent a review and selection of TPA services through a Request for Proposal (RFP) process coordinated by the Department of Administration (DOA). The incumbent, Intermountain Claims, Inc., was selected as the Program's TPA and entered a new contract, with the initial term running July 1, 2017 through June 30, 2020. The contract may be renewed through FY2024.
- DLI has initiated a review of their financial benchmarks for all public self-insured entities. Expectations are for DLI to implement a more stringent self-funding financial threshold. The Program anticipates the impact will be minimal as it currently exceeds the threshold benchmark.
- Several of the MUS campuses have experienced declining enrollments that have led to reductions in personnel; thus far potential impacts on premium revenue have been neutralized by growth on several other campuses. The Program is monitoring the situation to ensure it is planning appropriately for both work comp claim exposures and revenue adequacy.

CONCLUSION

The Montana University System Workers' Compensation Program has a strong financial position with good liquidity. The Program has worked carefully to slow the growth of its net position over the last several years and implemented more aggressively steps in FY18 to better align its net position with adequacy measures for meeting its obligations. The Program and its actuary will continue to monitor the fiscal health of the Program and refine revenues to align with its specific experience as a self-insured entity.

**MONTANA UNIVERSITY SYSTEM -
WORKERS' COMPENSATION PROGRAM
STATEMENT OF NET POSITION
AS OF JUNE 30, 2017**

ASSETS

Current Assets

Cash and cash equivalents	\$ 16,515,394
Interest receivable	25,702
Reinsurance receivable	2,785
Short-term securities lending collateral	<u>38,576</u>

Total current assets	<u>16,582,457</u>
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Noncurrent Assets

Long-term investments	<u>4,915,098</u>
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Total assets	<u><u>\$ 21,497,555</u></u>
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LIABILITIES

Current Liabilities

Vouchers payable	\$ 79,858
Current portion of compensated absences liability	6,506
Current securities lending liability	38,576
Current portion of estimated claims liability	<u>2,155,934</u>

Total current liabilities	<u>2,280,874</u>
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Noncurrent Liabilities

Compensated absences liability - net of current portion	1,732
Estimated claims liability - net of current portion	5,141,125
Estimated liability - OPEB	<u>17,887</u>

Total noncurrent liabilities	<u>5,160,744</u>
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Total liabilities	<u><u>\$ 7,441,618</u></u>
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NET POSITION

Unrestricted	<u><u>\$ 14,055,937</u></u>
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See the notes to financial statements.

**MONTANA UNIVERSITY SYSTEM -
WORKERS' COMPENSATION PROGRAM
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION
FOR THE YEAR ENDED JUNE 30, 2017**

OPERATING REVENUES	
Premiums	<u>\$ 3,837,897</u>
OPERATING EXPENSES	
Claims administration	186,636
Actuary fees	19,100
Insurance and reinsurance expense	314,279
Audit fees	12,120
Dues	2,940
Department of Labor assessment	95,115
Rent	6,462
Travel	325
Supplies and materials	604
Personal services	98,956
Communications	252
Other operating expenses	28,429
Safety Smart awards	285,000
Benefits and claims	<u>1,734,932</u>
Total operating expenses	<u>2,785,150</u>
OPERATING INCOME	<u>1,052,747</u>
NONOPERATING REVENUES (EXPENSES)	
Interest and investment earnings	156,192
STIP security lending income	1,927
STIP security lending expenses	<u>(758)</u>
Total nonoperating revenues	<u>157,361</u>
CHANGE IN NET POSITION	1,210,108
NET POSITION BEGINNING OF YEAR	<u>12,845,829</u>
NET POSITION END OF YEAR	<u><u>\$ 14,055,937</u></u>

See the notes to financial statements.

**MONTANA UNIVERSITY SYSTEM -
WORKERS' COMPENSATION PROGRAM
STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED JUNE 30, 2017**

CASH FLOWS FROM OPERATING ACTIVITIES

Cash received from premiums	\$ 3,837,897
Benefits and claims	(2,141,902)
Cash payments for insurance and reinsurance expense	(314,279)
Cash payments for employees	(98,891)
Cash payments for administrative expenses	(309,615)
Cash payments for other operating expenses	<u>(319,914)</u>

Net cash provided by operating activities 653,296

CASH FLOWS FROM INVESTING ACTIVITIES

TFIP net purchases	(1,870,576)
STIP security lending income received	1,927
STIP security lending expenses paid	(758)
Interest received	<u>145,752</u>

Net cash used by investing activities (1,723,655)

Net change in cash (1,070,359)

CASH AND CASH EQUIVALENTS BEGINNING OF YEAR 17,585,753

CASH AND CASH EQUIVALENTS END OF YEAR \$ 16,515,394

**RECONCILIATION OF OPERATING INCOME TO NET CASH
PROVIDED BY OPERATING ACTIVITIES
FOR THE YEAR ENDED JUNE 30, 2017**

Operating income \$ 1,052,747

Adjustments to reconcile operating income to net cash provided by operating activities:

Decrease in reinsurance receivables	59,202
Increase in vouchers payable	6,296
Increase in compensated absences liability	65
Increase in estimated liability - OPEB	1,157
Decrease in estimated claims liability	<u>(466,171)</u>

(399,451)

Net cash provided by operating activities \$ 653,296

See the notes to financial statements.

**MONTANA UNIVERSITY SYSTEM -
WORKERS' COMPENSATION PROGRAM
NOTES TO FINANCIAL STATEMENTS
June 30, 2017**

NOTE 1 -- SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization and Description of Program:

The Montana University System - Workers' Compensation Program (the Program) was organized to provide self-insured workers' compensation coverage for employees of the Montana University System. The Montana University System Board of Regents elected to provide workers' compensation coverage under the Compensation Plan Number One (39-71-2101, MCA) as of July 1, 2003. Prior to that date, the Montana University System obtained its workers' compensation coverage through participation in the Montana State Fund. Each member of the Program is jointly and severally liable for the full amount of any and all known or unknown claims of each member arising during the member's participation in the program.

Basis of Accounting:

The accompanying financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America as applied to governmental units, specifically standards applicable to public entity risk pools. The Governmental Accounting Standards Board is the accepted standard setting body for establishing governmental accounting and reporting principles.

Professional standards require resources to be classified for accounting and reporting purposes into the following three net position categories:

- *Net investment in capital assets:* Capital assets, net of accumulated depreciation, reduced by the outstanding balances of debt and deferred inflows of resources related to the acquisition, construction, or improvement of those assets.
- *Restricted:* Restricted assets reduced by liabilities and deferred inflows of resources related to those assets.
- *Unrestricted:* Amounts not required to be reported in the other components of net position.

When both restricted and unrestricted resources are available for use, it is the Program's policy to use restricted first, then unrestricted resources as they are needed.

Reporting Entity:

In accordance with governmental accounting and financial reporting standards, there are no component units to be included with the Montana University System - Workers' Compensation Program as a reporting agency.

Fund Accounting:

The Program is considered a public entity risk pool and is classified as an enterprise fund of the State of Montana; that is, a fund that is financed and operated in a manner similar to private business enterprises, where the intent of the Program is that the expenses of meeting its organizational purpose be financed or recovered primarily through user charges and investment earnings, and the periodic determination of revenue earned and expense incurred as appropriate for capital maintenance, public policy, management control, accountability and other purposes. The Program maintains its records on the accrual basis of accounting with revenues recorded when earned and expenses recorded when the obligation is incurred. Operating revenues and expenses generally arise from providing insurance coverage. All other revenues and expenses are classified as non-operating.

**MONTANA UNIVERSITY SYSTEM -
WORKERS' COMPENSATION PROGRAM
NOTES TO FINANCIAL STATEMENTS (Continued)
June 30, 2017**

NOTE 1 -- SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Administration of Claim Payments:

The Program contracts directly with Intermountain Claims, Inc. for claims administration services.

Allowance for Doubtful Accounts:

Management of the Program considers all premium receivables to be fully collectible, therefore, an allowance for uncollectible premiums is not deemed necessary.

Cash and Cash Equivalents:

Cash and cash equivalents consist of cash in checking and savings accounts and specific investments held on behalf of the Program in pooled accounts with the Montana Board of Investments Short-Term Investment Program (STIP). The Program considers all highly-liquid investments with maturity of three months or less when purchased to be cash equivalents.

Estimates:

The preparation of the financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosures of contingent assets and liabilities, and the reported amounts of revenue and expenses. The major estimates are unpaid claims liabilities, and due to their prospective nature, actual results may differ from those estimates.

Premium Revenue:

Premium rates for all members are established by the Program's Committee based on anticipated premiums needed as determined by the actuary. Premium rates are adjusted annually based on inflation, claims experience, and other factors. Premiums are recorded as revenue in the period for which coverage is provided. Members may be subject to supplemental assessments in the event of deficiencies and in the event of increased costs due to changes in law or excessive claims costs. The Program considers anticipated investment income in determining if a premium deficiency exists.

Unpaid Claims Liabilities and Expenses:

The Program establishes claim liabilities (loss reserves) for unpaid claims liabilities based on actuarial estimates of the ultimate cost of claims (including future allocated claim adjustment expenses) that have been reported but not paid or settled and that have been incurred but not reported. The liability includes the unallocated claims adjustment expense. The liabilities are based on the estimated ultimate cost of settling the reported and unreported claims, and claims reserve development including the effects of inflation and other societal and economic factors. Estimated amounts of subrogation and reinsurance recoverable on unpaid claims are deducted from the liability for unpaid claims. Estimated claims liabilities are recomputed periodically based on current reviews of claims information, experience with similar claims and other factors. Adjustments to estimated claims liabilities are charged or credited to expense in the periods in which they are made.

**MONTANA UNIVERSITY SYSTEM -
WORKERS' COMPENSATION PROGRAM
NOTES TO FINANCIAL STATEMENTS (Continued)
June 30, 2017**

NOTE 2 -- CASH, CASH EQUIVALENT, AND INVESTMENTS

Cash and cash equivalents at June 30, 2017 consist of the following:

Cash with fiscal agent	\$ 371,771
Cash in bank	961,580
Short Term Investment Program (STIP)	<u>15,182,043</u>
Total	<u>\$ 16,515,394</u>

All of the cash on deposit in operating, savings and claims accounts at June 30, 2017 are held at US Bank which is covered up to the limits imposed by Federal Depository Insurance Corporation (FDIC). Cash in bank represents the cash held in the State of Montana Treasury and STIP is invested and managed by the Montana Board of Investments (MBOI).

Short Term Investment Pool (STIP) – This investment program is managed and administered under the direction of the MBOI as authorized by the Unified Investment Program. Funds may be invested for one or more days and provides a 24-hour liquidity for state agency participants. It is a commingled pool for investment purposes and requested redemptions from the pool are redeemed the next business day. The fair values of the investments in this category have been determined using the Net Asset Value (NAV) per share (or its equivalent) of the investment.

The STIP portfolio may include asset-backed securities, commercial paper, corporate, U.S. Government direct obligations, U.S. Government agency securities, repurchase agreements, institutional money market funds, certificates of deposit, and variable-rate (floating-rate) instruments. Investments must have a maximum maturity of 397 days or less unless they are a variable rate security.

Trust Fund Investment Pool (TFIP) – TFIP is an external investment pool managed and administered under the direction of the MBOI as statutorily authorized by the Unified Investment Program. It is a commingled external investment pool and participants may request for redemption on a monthly basis. The fair values of the investments in this category have been determined using the NAV per share (or its equivalent) of the investment.

The TFIP fixed income portfolio includes U.S. Treasury securities, U.S. agency and government-related securities, asset-backed securities, mortgage-backed securities, commercial mortgage-backed securities, and corporate securities categorized as financial, industrial or utility. This portfolio may include variable-rate (floating rate) instruments with the interest rate tied to a specific rate such as LIBOR (London Interbank Offered Rate). Variable rate securities pay a variable rate of interest until maturity.

As of June 30, 2017 the fair value of the TFIP investment was \$4,915,098.

Fair Value Measurement:

The MBOI categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles as follows:

- Level 1 - Quoted prices for identical assets or liabilities in active markets.
- Level 2 - Prices determined using inputs, other than quoted prices included within Level 1, that are observable for an asset or liability, either directly or indirectly.
- Level 3 - Prices are determined using unobservable inputs.

**MONTANA UNIVERSITY SYSTEM -
WORKERS' COMPENSATION PROGRAM
NOTES TO FINANCIAL STATEMENTS (Continued)
June 30, 2017**

NOTE 2 -- CASH, CASH EQUIVALENT, AND INVESTMENTS (Continued)

Refer to the fair value measurement note disclosures within the MBOI's annual financial statements for the underlying investments within the fair value hierarchy.

The MBOI annual financial information is available from the MBOI at 2401 Colonial Drive 3rd Floor, PO Box 200126, Helena, MT 59620-0126 or by calling 406-444-0001. The annual financial statements are located on the MBOI's website, www.investmentmt.com.

The investment risk disclosures are described in the following paragraphs.

Credit Risk:

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligation. With the exception of U.S. Government securities, the pools' fixed income instruments have credit risk as measured by major credit rating services. For all retirement Pools, only approved cash investment vehicles are permitted. These include the custodian's STIF vehicle, STIP, or any SEC-registered money market fund, all of which specifically address credit risk in their respective investment guidelines. The MBOI's policy requires TFIP fixed income investments to be invested in investment grade securities (Baa3/BBB- or higher) with the exception of non-rated securities issued or guaranteed by agencies or instrumentalities of the US Government. The MBOI's STIP investment policy specifies that STIP securities have a minimum of two separate credit ratings as provided by Standard and Poor's, Moody's, or Fitch that meet the minimum as stated in the STIP investment policy depending on the type of investment. The U.S. Government guarantees the U.S. Government securities directly or indirectly. 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 per GASB Statement No. 40.

Custodial Credit Risk:

Custodial credit risk is the risk that, in the event of the failure of the counterparty to a transaction, the MBOI will not be able to recover the value of the investment or collateral securities that are in the possession of an outside party. Per policy, the MBOI's custodial institution must hold short-term and long-term credit rating by at least one Nationally Recognized Statistical Rating Organization with a minimum requirement of A1/P1 (short term) and A3/A-1 (long-term).

Concentration of Credit Risk:

Concentration of credit risk is the risk of loss attributable to the magnitude of any single investment per issuer name. Investments explicitly guaranteed by the U.S. Government are excluded from the concentration of credit risk requirement. 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, the MBOI had no concentration of credit risk exposure to Fannie Mae and Freddie Mac in either the TFIP or STIP.

The TFIP Investment Policy Statements provide for a 2% portfolio limit for dollar denominated debt obligations of domestic and foreign corporations (Yankee bonds) and a 3% portfolio limit in non-agency Mortgage Pass-through (MBS) securities. The four RFBP external managers are limited to debt obligations of domestic and foreign corporations up to 3% of portfolio assets per issuer.

**MONTANA UNIVERSITY SYSTEM -
WORKERS' COMPENSATION PROGRAM
NOTES TO FINANCIAL STATEMENTS (Continued)
June 30, 2017**

NOTE 2 -- CASH, CASH EQUIVALENT, AND INVESTMENTS (Continued)

The STIP Investment Policy limits concentration of credit risk exposure by limiting portfolio investment types to 3% in any issuer with the exception of US Treasury and US Agency securities as well as any repurchase agreements with a financial institution. Concentration risk was within the policy as set by the MBOI.

Interest Rate Risk:

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. In accordance with GASB Statement No. 40, the MBOI uses effective duration as a measure of interest rate risk for the Bond Pool portfolio. Duration is the average percentage change in a bond's price for a given change in interest rates. Prices move inversely to interest rates. Per policy, the TFIP's duration is to remain within 20% of the established Index duration.

According to the STIP investment policy "the STIP portfolio will minimize interest rate risk by:

1. structuring the investment portfolio so securities mature to meet cash requirements for ongoing operations thereby normally avoiding the need to sell securities on the open market prior to maturity;
2. maintaining a dollar-weighted average portfolio maturity (WAM) of 60 days or less (for this purpose, the date to the next coupon reset date will be used for all floating or variable rate securities; and
3. STIP will maintain a reserve account."

Although the STIP investments have been rated by investment security type, STIP, as an external investment pool, has not been rated.

NOTE 3 -- SECURITIES LENDING

The MBOI has authorized the use of securities lending transactions - loans of debt or equity securities to broker-dealer and other entities for collateral with a corresponding agreement for the MBOI to return the collateral for the same securities in the future. The MBOI has contracted with the custodial bank, State Street Bank and Trust (the Bank). The Bank is required to maintain collateral equal to 102 percent of the fair value of domestic securities while the securities are on loan. The MBOI and the Bank split the earnings on security lending activities. The MBOI retains all rights and risks of ownership during the loan period. Information regarding the STIP securities lending transactions is available in the MBOI's comprehensive annual financial report.

NOTE 4 -- RELATED PARTIES

Certain employees of the campuses of the university system provide services to the Program at no charge. The value of such services has not been determined.

**MONTANA UNIVERSITY SYSTEM -
WORKERS' COMPENSATION PROGRAM
NOTES TO FINANCIAL STATEMENTS (Continued)
June 30, 2017**

NOTE 5 -- PUBLIC EMPLOYEES' RETIREMENT SYSTEM

Funding Policy

The State of Montana's Public Employees' Retirement Board (Retirement Board) was authorized by 19-3-2102, MCA, to establish with the Public Employees' Retirement System (PERS) a defined contribution plan (Plan) in accordance with Montana law in July 2002. The Plan was established as a pension plan for the exclusive benefit of members and their beneficiaries and as a "qualified plan" pursuant to section 401(a) of the Internal Revenue Code and its implementing regulations. The assets of the Plan are held in a trust, with the Retirement Board acting as a trustee. The Retirement Board has the powers and shall perform the duties regarding the Plan as provided in 19-3-2104, and 19-2-403, MCA as applicable and may also exercise the powers and shall perform the duties provided in Title 19, Chapter 3, MCA. A Plan participant is vested in 100% of the participant's employee contribution account at all times and is vested 100% in the participant's employer contribution account upon completion of five years of membership service. Normal retirement age under the Plan is age 65. Upon a participant's attainment of normal retirement age and completion of five years of membership service, the participant has a nonforfeitable right to the employer contribution account. Any non-vested amounts shall be forfeited upon termination of service. Any amount forfeited will be held in a separate plan account and used to pay administrative expenses of the Plan.

The employer contribution rate per 19-3-316, MCA is calculated as follows: 6.9% and an additional contribution of 1.27% beginning on July 1, 2013, increasing .10% each fiscal year and continuing until the additional contributions terminate pursuant to 19-3-316, MCA; less the plan choice rate determined under 19-3-2117 and 19-3-212, MCA; less the education fund rate and less the long term disability fund rate under 19-3-2117, MCA. Employee plan contributions per 19-3-315(2), MCA are 7.9% of compensation. The total contribution to the participant's individual account is 16.37%.

	<u>*Employer</u>	<u>Employee</u>	<u>Total</u>
2017	8.13%	7.9%	16.37%
2016	4.19%	7.9%	12.09%
2015	4.19%	7.9%	12.09%

*Total Employer Contributions (8.47%) less required disbursements (0.34%) = Allocation to Employee Account (8.13%) in 2017.

The amount contributed by the Program to the Plan during the year ended June 30, 2017 was \$6,261.

Further information regarding the plan may be obtained by contacting:

Public Employees' Retirement System
100 N Park Avenue, Suite 200
P.O. Box 200131
Helena, MT 59620-0131
(406) 444-3154

**MONTANA UNIVERSITY SYSTEM -
WORKERS' COMPENSATION PROGRAM
NOTES TO FINANCIAL STATEMENTS (Continued)
June 30, 2017**

NOTE 6 -- LEASE AND RENT EXPENSE

The Program as part of the Office of the Commissioner of Higher Education entered into a ten year lease agreement with Student Assistance Foundation of Montana to lease a portion of office space at the building located on 2500 Broadway, Helena, Montana. The commencement date of the lease was January 1, 2009. During the year ended June 30, 2017, the Program paid rent of \$6,462.

The following is a schedule by year of minimum future lease payments for the years ended June 30:

2018	\$ 5,094
2019	<u>2,547</u>
 Total minimum future lease payments	 <u><u>\$ 7,641</u></u>

NOTE 7 -- UNPAID CLAIMS LIABILITIES

As discussed in Note 1, the Program establishes actuarial estimated unpaid claims liabilities (undiscounted basis). The estimated unpaid claims incurred but not reported and loss development liability have been adjusted to reflect the actuarial best estimates of the ultimate costs of claims for 2017.

The following represents changes in the aggregate unpaid claims liabilities for the Program for 2017:

Total present value of estimated unpaid claim losses at beginning of year	<u>\$ 7,763,231</u>
Changes in the estimated unpaid claim losses:	
Provision for insured events of the current year	3,096,000
Decrease in provision for insured events of prior years	<u>(1,368,093)</u>
Total incurred claims	<u>1,727,907</u>
Payments (including claims legal defense):	
Claims paid attributable to insured events of current year	940,066
Claims paid attributable to insured events of prior years	<u>1,254,013</u>
Total payments	<u>2,194,079</u>
Total present value of estimated unpaid claim losses at end of year	<u><u>\$ 7,297,059</u></u>

The estimated liability for workers' compensation claims as of June 30, 2017, consist of the following:

Estimated claims reported but unpaid	\$ 2,155,934
Estimated claims incurred but not reported and loss development	<u>5,141,125</u>
	<u><u>\$ 7,297,059</u></u>

**MONTANA UNIVERSITY SYSTEM -
WORKERS' COMPENSATION PROGRAM
NOTES TO FINANCIAL STATEMENTS (Continued)
June 30, 2017**

NOTE 8 -- OTHER POST-EMPLOYMENT BENEFITS

A retiree may continue coverage with the Montana University System Employee Group Benefits Plan (Benefits Plan) if the retiree is eligible to receive a State Retirement Benefit from Teacher Retirement System (TRS) or the Public Employee Retirement System (PERS) at the time they leave their employment with the Montana University System.

An eligible retiree must make arrangements with the Human Resources/Benefits Office to continue coverage as a retiree on a self-pay basis within 63 days of retirement.

Plan Description

The Benefits Plan is considered a multiple employer agent plan. The Benefits Plan allows retirees to participate, as a group, at a rate that does not cover all of the related costs. This results in the reporting of an "implied rate" subsidy in the related financial statements and footnotes. While this liability is disclosed for financial statement purposes, it does not represent a legal liability of the Program. The Benefits Plan is reported as an agency fund. There are no assets or liabilities as only contributions collected and distributions made are reflected in the fund. See the funding policy that follows.

The Benefits Plan does not issue a standalone financial report, but is subject to audit as part of the State of Montana's Comprehensive Annual Financial Report (CAFR). A copy of the most recent CAFR can be obtained online at <http://accounting.mt.gov/cafr/default.mcp> or by contacting the Montana Department of Administration, P.O. Box 200102, Helena, MT 59620-0102.

As of June 30, 2017, the number of Montana University System - Workers' Compensation Program active participants in the Benefits Plan was 1.

Funding Policy

The Benefits Plan funds the post employment benefits on a pay-as-you-go basis from premiums from campuses, which are paid by retirees. Montana Code Annotated, Title 20, Chapter 25, Part 13 gives authority for establishing the group benefits plans.

The Benefits Plan's administratively established self-insured retiree medical premiums vary between \$387 and \$1272 per month and are revised annually. The Benefits Plan provides different coinsurance amounts depending on whether members use in-network or out-of-network providers. After an annual \$750 in-network deductible for most non-Medicare-eligible retirees, the Benefits Plan reimburses 75% in medical claims until the in-network out of pocket maximum of \$4,000 has been reached. After the in-network out of pocket maximum is reached, the Benefits Plan reimburses covered medical claims at 100% for the remainder of the Benefits Plan year. For out-of-network services, after an annual \$750 deductible (which is separate from the in-network deductible), the Benefits Plan reimburses 65% in allowed medical claim charges until the out-of-network out of pocket maximum of \$6,000 is reached. The Benefits Plan automatically reduces claim reimbursement for members eligible for Medicare, even if the member is not enrolled in Medicare.

Annual Other Post-employment Benefit Cost and Contributions

The Program's annual other post-employment benefit (OPEB) cost (expense) is calculated based on the annual required contribution (ARC) of the employer, an amount actuarially determined in accordance with GASB Statement No. 45. The calculated ARC represents an amount that, if funded, would cover normal cost each year and amortize any unfunded actuarial liability over a period not to exceed 30 years. For the fiscal year ended June 30, 2017, the Program's annual OPEB cost (expense) of \$1,736 was equal to the ARC. The actuarial determination was based on plan information as of July 1, 2015.

There are no long-term contracts for contributions to the OPEB plan. Contributions refer to contributions made in relation to ARC.

**MONTANA UNIVERSITY SYSTEM -
WORKERS' COMPENSATION PROGRAM
NOTES TO FINANCIAL STATEMENTS (Continued)
June 30, 2017**

NOTE 8 -- OTHER POST-EMPLOYMENT BENEFITS (Continued)

The following table presents the Workers' Compensation Program OPEB cost for the fiscal year ended June 30, 2017, the amount contributed, and changes in the Workers' Compensation Program OPEB plan for fiscal year 2017:

Annual required contribution/OPEB cost	\$ 1,563
Interest on net OPEB obligation	802
Amortization	<u>(629)</u>
Annual OPEB cost	1,736
Contributions made	<u>(579)</u>
Increase in net OPEB obligation	1,157
Net OPEB obligation - beginning of year	<u>16,730</u>
 Net OPEB obligation - end of year	 <u><u>\$ 17,887</u></u>

Actuarial Methods and Assumptions

The projected unit credit funding method was used to determine the cost of the Benefits Plan. This method's objective is to fund each participant's benefits under the Benefits Plan as they accrue. The total benefit to which each participant is expected to become entitled at retirement is categorized into units, each associated with a year of past or future credited service.

The actuarial assumptions included, in addition to marital status at retirement, mortality rates and retirement age:

Interest/Discount Rate	4.25%
Payroll Growth Rate	2.50%
Participation	50% of future retirees are assumed to elect medical coverage, 60% of the future retirees who elect coverage and are married are assumed to elect spousal coverage as well
Healthcare Cost Trend Rate-Medical	7.50%
Healthcare Cost Trend Rate-Prescription drugs	7.50%

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Actuarially determined amounts are subject to continual review and revision as actual results are compared with past expectations, and new estimates are made about the future.

NOTE 9 -- SUBSEQUENT EVENTS

Management has evaluated subsequent events through October 17, 2017, the date on which the financial statements were available to be issued.

REQUIRED SUPPLEMENTARY INFORMATION

**MONTANA UNIVERSITY SYSTEM -
WORKERS' COMPENSATION PROGRAM
CLAIMS DEVELOPMENT INFORMATION**

The table on the following pages illustrates how the Program's earned revenues (net of excess loss coverage) and investment income compare to related costs of loss (net of loss assumed by excess loss coverage insurers) and other expenses assumed by the Program as of the end of each of the previous twelve years. The rows of the table are defined as follows:

1. This line shows the total of each fiscal year's gross earned contribution revenue and investment revenue.
2. This line shows each fiscal year's other operating costs of the Program including overhead and claims expense not allocable to individual claims.
3. This line shows the Program's gross incurred claims and allocated claim adjustment expenses and net incurred claims and allocated adjustment expense (both paid and accrued) as originally reported at the end of the first year in which the event that triggered coverage under the contract occurred (called *policy* year).
4. This section of rows shows the cumulative net amounts paid as of the end of successive years for each policy year.
5. This line shows the latest reestimated amount of claims assumed by reinsurers as of the end of the current year for each accident year.
6. This section of rows shows how each policy year's net incurred claims increased or decreased as of the end of successive years. (This annual reestimation results from new information received on known claims, reevaluation of existing information on known claims, and emergence of new claims not previously known.
7. This line compares the latest reestimated net incurred claims amount to the amount originally established (line 3) and shows whether this latest estimate of net claims cost is greater or less than originally thought. As data for individual policy years mature, the correlation between original estimates and reestimated amounts commonly is used to evaluate the accuracy of net incurred claims currently recognized in less mature policy years. The columns of the table show data for successive policy years.

MONTANA UNIVERSITY SYSTEM - WORKERS' COMPENSATION PROGRAM
CLAIMS DEVELOPMENT INFORMATION

	Fiscal and Policy Year Ended													
	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
1. Net earned (required contribution and investment revenues)	\$ 2,273,944	\$ 2,850,849	\$ 3,510,259	\$ 4,153,570	\$ 4,777,099	\$ 4,930,524	\$ 4,758,849	\$ 4,515,064	\$ 3,968,546	\$ 4,052,736	\$ 1,930,189	\$ 4,316,704	\$ 4,088,926	\$ 3,679,810
2. Unallocated expenses	227,267	279,716	263,904	259,412	386,512	460,508	441,977	426,068	883,006	701,688	1,002,129	985,418	739,829	735,938
3. Estimated incurred claims and expenses, end of policy year	2,174,000	2,366,000	2,453,000	2,600,000	2,693,000	2,922,000	2,959,000	3,115,000	3,158,000	3,399,000	3,329,000	3,417,000	3,157,000	3,096,000
4. Gross paid (cumulative) as of:														
End of policy year	551,749	382,154	390,972	367,913	469,399	640,717	572,486	742,041	709,651	891,252	1,010,989	701,427	597,999	940,066
One year later	1,019,751	1,001,996	910,335	932,787	1,099,932	1,764,405	1,446,724	1,608,465	1,185,473	1,803,450	1,647,393	1,440,073	1,366,109	
Two years later	1,123,504	1,227,600	1,254,242	1,092,644	1,286,205	2,997,006	1,835,851	1,900,333	1,277,606	2,282,882	1,870,557	1,767,555		
Three years later	1,147,508	1,526,088	1,351,046	1,157,520	1,440,632	3,275,598	2,071,374	1,961,168	1,317,629	2,536,294	1,887,113			
Four years later	1,165,362	1,554,903	1,386,285	1,203,059	1,497,940	3,450,482	2,190,713	2,078,996	1,322,131	2,644,417				
Five years later	1,210,361	1,660,121	1,393,297	1,227,284	1,563,146	3,630,194	2,354,356	2,086,650	1,322,350					
Six years later	1,251,309	1,691,861	1,401,236	1,238,378	1,571,929	3,672,828	2,393,894	2,097,773						
Seven years later	1,253,722	1,759,234	1,408,799	1,238,514	1,574,542	3,765,763	2,408,683							
Eight years later	1,257,246	1,769,993	1,410,797	1,238,514	1,574,542	3,785,533								
Nine years later	1,259,246	1,785,717	1,410,797	1,238,901	1,574,829									
Ten years later	1,261,093	1,793,068	1,410,756	1,239,026										
Eleven years later	1,263,925	1,800,068	1,410,756											
Twelve years later	1,266,174	1,800,068												
Thirteen years later	1,267,074													
5. Reestimated ceded claims and expenses	-	-	-	-	-	-	-	-	-	-	-	-	-	-
6. Reestimated net incurred claims and expenses														
End of policy year	2,174,000	2,366,000	2,453,000	2,600,000	2,693,000	2,922,000	2,959,000	3,115,000	3,158,000	3,399,000	3,329,000	3,417,000	3,157,000	3,096,000
One year later	2,174,000	2,565,000	2,267,356	2,293,413	2,686,541	3,046,000	3,017,000	3,428,000	3,364,000	3,693,000	3,317,000	2,999,000	3,048,000	
Two years later	2,037,000	2,459,000	2,510,000	2,412,000	2,630,000	3,977,000	3,000,000	3,396,000	2,650,000	3,712,000	2,979,000	2,636,000		
Three years later	1,830,000	2,602,000	2,471,000	2,131,000	2,391,000	4,199,000	3,078,000	3,032,000	2,140,000	3,729,000	2,596,000			
Four years later	1,570,000	2,622,000	2,069,000	1,804,000	2,335,000	3,987,000	2,923,000	2,725,000	1,598,000	3,558,000				
Five years later	1,499,000	2,312,000	1,512,000	1,779,000	1,754,000	3,657,000	2,926,000	2,367,000	1,502,000					
Six years later	1,327,000	1,965,000	1,511,000	1,412,000	1,769,000	3,318,000	2,691,000	2,325,000						
Seven years later	1,284,000	1,825,000	1,422,000	1,231,000	1,661,000	3,312,000	2,680,000							
Eight years later	1,288,000	1,825,000	1,388,000	1,232,000	1,638,000	3,319,000								
Nine years later	1,244,000	1,785,000	1,390,000	1,232,000	1,571,000									
Ten years later	1,246,000	1,805,000	1,390,000	1,232,000										
Eleven years later	1,248,000	1,914,000	1,390,000											
Twelve years later	1,334,000	1,798,000												
Thirteen years later	1,253,000													
7. Increase (decrease) in estimated net incurred claims and expenses from end of policy year	(921,000)	(568,000)	(1,063,000)	(1,368,000)	(1,122,000)	397,000	(279,000)	(790,000)	(1,656,000)	159,000	(733,000)	(781,000)	(109,000)	-

See the accompanying independent auditors' report.



INDEPENDENT AUDITORS' 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*

Board of Regents - Montana University System Self-Funded
Workers' Compensation Management Committee
Helena, Montana

We have audited, 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, the financial statements of the Montana University System - Workers' Compensation Program, (an enterprise fund of the State of Montana) which comprise the statement of net position as of June 30, 2017, and the related statement of revenue, expense and changes in net position and cash flows for the year then ended and the related notes to the financial statements, and have issued our report thereon dated October 17, 2017.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Montana University System - Workers' Compensation Program's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Montana University System - Workers' Compensation Program's internal control. Accordingly, we do not express an opinion on the effectiveness of the Montana University System - Workers' Compensation Program'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 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 control 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 over financial reporting 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 University System - Workers' Compensation Program's financial statements are free of 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 of 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*.

We noted certain other matters that we reported to management of the Montana University System - Workers' Compensation Program in a separate letter dated October 17, 2017.

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 the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Junkermier, Clark, Campanella, Stevens, P.C.

Helena, Montana
October 17, 2017

**MONTANA UNIVERSITY SYSTEM -
WORKERS' COMPENSATION PROGRAM
SCHEDULE OF FINDINGS AND RESPONSES**

The results of our tests disclosed no instances of noncompliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters or any internal control deficiencies considered to be significant deficiencies or material weaknesses, which were required to be reported under *Government Auditing Standards* as of June 30, 2017.