MONTANA BOARD OF INVESTMENTS
CLARK FORK RESTORATION FUND (MU3H) (FUND 08221)
INVESTMENT POLICY STATEMENT

INTRODUCTION

The purpose of this investment policy statement is to outline the account objectives, permissible investments, and constraints that will guide the management of the portfolio. The policy is designed to give the investment manager flexibility to achieve in a prudent manner the investment objectives of the client, the Department of Justice (DOJ), to implement the remedial action ("the Remedy") on the Clark Fork River Restoration in accordance with the ARCO Settlement Consent Decree.

BACKGROUND INFORMATION

In August 2008, a Consent Decree was entered between the State of Montana and Atlantic Richfield Company (ARCO), in order to settle certain litigation and to provide for the funding of the restoration action at the Clark Fork River (CFR) Operable Unit. The settlement involves, among other things, payment by ARCO of $26.7 million plus accrued interest from April 1, 2006. Those funds and the earnings from the investment of those funds are to be used by the State for the purpose of restoration of the CFR over an estimated ten to twelve year period.

Major construction is projected to begin during calendar year 2009 and end during calendar year 2019.

The project being financed through this fund is the restoration of the Clark Fork River and associated riparian areas from Warm Springs Ponds to Milltown Reservoir and related projects. The nature of restoration work includes the potential for cost overruns and unexpected expenses. DOJ will use its best efforts to inform the Board of Investments of any expected overruns or changes in the cash draw schedule and will attempt to provide notice of such changes as much in advance as possible.

OBJECTIVES

Risk and Return:
Earnings alone will not be sufficient to fund expected expenditures nor will the principle provided by the settlement be sufficient. A combination of current income, total return, and use of principle will be necessary to fund the expected expenditures. It will require a return in excess of the assumed risk free rate to fund current projected expenditures, as well as possible future cost over runs. This account has an average ability to assume interest rate risk. Some risk of loss of principal must be taken to provide a return sufficient to fund objectives. An allocation to the Trust Funds Bond Pool (TFBP) will be made to obtain exposure to a diversified fixed income portfolio. An allocation to U.S. Treasuries, U.S. Agencies and Corporate securities may be made to provide a greater certainty of cash flows from maturities. Risk tolerance will decline if long-term investments have to be liquidated earlier than estimated to meet the cash draw down schedule.

There was $26.8 million in the account as of December 31, 2008, invested solely in the Short-term Investment Pool (STIP). The risk and return factors along with other considerations result in the expected asset allocation shown below.

FIXED INCOME	Range
U.S. Treasury Bonds	0-10%
U.S. Agency Bonds	0-30%
Corporate Bonds	0-10%
Trust Fund Bond Pool (TFBP)	40-80%
Short-term Investment Pool (STIP)	0-25%
Total Fixed Income	100%

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OTHER CONSIDERATIONS

Liquidity Needs:
Material annual expenditures are projected in each year through 2019 in the initial cash draw down schedule provided by DOJ. The timing of expenditures within the calendar year will be somewhat uncertain, thus necessitating a significant cash balance be available to meet these needs without forcing an inordinate amount of TFBP sales in any one year. There will be significant seasonality in the pattern of expenditures. Liquidity needs will be met with a combination of cash on hand, earnings, maturities and sales of investments. The minimum Short Term Investment Pool (STIP) balance will be the expected next one year of expenditures less expected maturities of individual securities prior to any adjustment to reflect funding needs.

Maturity Horizon:
The maturity horizon of the investments utilized is designed to meet the liabilities of the client with income, maturities and a reasonable amount of sales of securities and TFBP units. The liabilities are the cash needs for restoration expenditures as provided by the DOJ at the outset of the account and as modifications are made in ensuring years. At this time expenditures are expected to occur commencing immediately and each year through 2019, with the majority occurring during years 2012 - 2019.

Investment Limits:
1. To reduce the risk of loss on individual corporate bonds, investment purchases in any one credit will be limited to 1% of the market value of the fund at the date of purchase or 2% of the lowest projected fund balance before the securities mature, which ever is lower.
2. Corporate bond sector (Industrial, Finance, and Utility) exposure shall be constrained to no more than a 4% exposure at the time of purchase, or 6% at any time over the future projected fund balance.
3. The quality rating of any corporate bond shall be in the top of the single-A rating classification or better at the time of purchase. (e.g., A1/A+ or higher), and have at least two ratings.
4. Exposure to the securities of any one U.S. Agency are limited to 5%, and in no event will an agency security be purchased if it carries a rating that is less than top-rated (AAA) at the time of purchase.

Legal Considerations:
This fund is governed by state regulations, specifically, the "prudent expert principle" which requires the Board of Investments to: (a) discharge the duties with the care, skill, prudence, and diligence, under the circumstances then prevailing, that a prudent person acting in a like capacity with the same resources and familiar with like matters exercises in the conduct of an enterprise of a like character with like aims; (b) diversify the holdings of each fund within the unified investment program to minimize the risk of loss and to maximize the rate of return unless, under the circumstances, it is solely prudent not to do so; and (c) discharge the duties solely in the interest of and for the benefit of the funds forming the unified investment program.

The Montana Constitution does not allow equity type investments in non-retirement funds.

ADMINISTATIVE

Securities Lending:
Section 17-1-113, MCA, authorizes the Board to lend securities held by the state. The Board may lend its publicly traded securities held in the investment pools, through an agent, to other market participants in return for compensation. Currently, through an explicit contract, State Street Bank and Trust, the state's custodial bank, manages the state's securities lending program. The Board seeks to assess the risks, such as counterparty and reinvestment risk, associated with each aspect of its securities lending

MONTANA BOARD OF INVESTMENTS
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INVESTMENT POLICY STATEMENT

program. The Board requires borrowers to maintain collateral at 102 percent for domestic securities and 105 percent for international securities. To ensure that the collateral ratio is maintained, securities on loan are marked to market daily and the borrower must provide additional collateral if the value of the securities on loan increases. In addition to the strict collateral requirements imposed by the Board, the credit quality of approved borrowers is monitored continuously by the contractor. From time to time, Staff or the investment manager may restrict a security from the loan program upon notification to State Street Bank. Staff will monitor the securities lending program, and the CIO will periodically report to the Board on the status of the program.

Cash Investments

Cash investments held at the pool level, any managed account within it, or any separate account entail an element of credit risk. Thus, 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.