MONTANA BOARD OF INVESTMENTS
CLARK FORK SITE RESPONSE ACTION FUND (MU3A) (FUND 08212)
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 Environmental Quality (DEQ), to implement the remedial action ("the Remedy") on the Clark Fork Site in accordance with the Clark Fork Site Consent Decree and the Site Specific Memorandum of Agreement (SMOA) between the United States and the State of Montana.

BACKGROUND INFORMATION

In August 2008, a Consent Decree was entered between the State of Montana, the United States and Atlantic Richfield Company (ARCO), in order to settle certain litigation and to provide for the funding of the remedial action at the Clark Fork River (CFR) Operable Unit. The settlement involves, among other things, payment by ARCO of $83.3 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 with oversight, input and approval from the United States EPA for the purpose of remediating the CFR over an estimated ten to twelve year period. Any funds left over after clean up will be transferred to the Clark Fork State Restoration Account (established under the same Consent Decree). In October of 2008 ARCO paid the entire Remedy settlement amount of $96.2 million to the State of Montana.

Major construction is projected to begin during calendar year 2009 and end during calendar year 2019. At that time, a small fund balance will be needed to fund Operations and Maintenance going forward and the remaining balance with EPA approval will be transferred to the Clark Fork State Restoration Account. The fund balance at that time is expected to be mostly Trust Funds Bond Pool (TFBP) units.

The project being financed through this fund is the remediation of environmental contamination at one operable unit of a federal Superfund site. The nature of construction/remediation work includes the potential for cost overruns and unexpected expenses. DEQ 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, possible future cost over runs, and leave residual funds for future expenses such as operation and maintenance. 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. A large allocation to the TFBP will be made to obtain exposure to a diversified fixed income portfolio return while reducing idiosyncratic risk. 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.

The risk and return factors along with other considerations result in the expected asset allocation shown on the following page.

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ASSET ALLOCATION

FIXED INCOME	Range
U.S. Treasury Bonds	0-10%
U.S. Agency Bonds	0-10%
Corporate Bonds	0-10%
Trust Funds Bond Pool (TFBP)	50-95%
Short-term Investment Pool (STIP)	0-25%
Total Fixed Income	100.0%

OTHER CONSIDERATIONS

Liquidity Needs:
Material annual expenditures are projected in each year through 2024 in the initial cash draw down schedule provided by DEQ. 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 remediation expenditures as provided by the DEQ 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 2024, 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.

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

ADMINISTRATIVE

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 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.