

**MONTANA BOARD OF INVESTMENTS  
INVESTMENT POLICY STATEMENT  
TREASURE STATE ENDOWMENT FUNDS (FUNDS 09040 & 09044)  
APRIL 2015**

## **INTRODUCTION**

The purpose of an investment policy statement is to give the investment manager guidance in developing an investment program to achieve the objectives agreed upon and enable the sponsor, Department of Revenue, to monitor the progress of the plan.

## **OBJECTIVES**

Return Requirement: To maximize the total rate of return through a broadly diversified portfolio of fixed income assets while exceeding the Salomon Broad Investment-Grade Bond Index and/or the Lehman Aggregate Bond Index over a five-year moving average.

Current income is important since the Legislature is transferring 100 percent of income earned to the treasure state endowment special revenue account to fund local government projects.

Risk Tolerance: This fund is being managed as a long-term, permanent fund; therefore, the fund has an above average ability to assume risk. The ability to tolerate volatility in value of the portfolio is larger than the ability to tolerate volatility in total spendable return.

## **CONSTRAINTS**

Liquidity: As a long-term constitutional trust fund, liquidity needs are low, except for investment purposes. There is no need to maintain any sizeable short-term holdings.

Time Horizon: The fund is considered a permanent long-term fund that has a time horizon well beyond normal market cycles.

Tax Considerations: This fund is tax-exempt; therefore, tax advantage investments will not be used.

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 manners 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 clearly 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.

### 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.

Unique Circumstance: None.

Client Preference: None

## TREASURE STATE ENDOWMENT FUNDS

### BACKGROUND INFORMATION

In 1992 the Treasure State Endowment Fund Program (TSEP) was passed by the January 1992 Special Legislative Session and submitted to the voters as a referendum in the June primary election. It was approved by the voters.

The TSEP is a state funded grant and is a program designed to assist cities, towns, and counties in financing infrastructure projects within their jurisdictions. Authorized projects include drinking water systems, waste water treatment facilities, sanitary and storm sewer systems, solid waste disposal systems, and bridges.

A separate sub fund, the Treasure State Endowment Fund (TSEF) was established within the Permanent Coal Trust (Trust) to generate ongoing funding for TSEP projects. As a sub fund of the Trust, the TSEF's principal is afforded the same constitutional protection as is principal in the Trust. The Montana constitution states, "The principal of the trust shall forever remain inviolate unless appropriated by vote of three-fourths of the members of each house of the legislature".

On July 1, 1993, \$10.0 million was transferred from the Trust to TSEF. The TSEF will receive 50 percent of the coal severance taxes constitutionally earmarked for the Trust during the next 20 years. The Department of Commerce staff estimates that by fiscal year 2014, principal in TSEF will reach \$190 million. Funds for TSEP grants and loans are generated by interest earnings on the principal of the TSEF and by loan repayments by local government loan receipts.

The state treasurer shall monthly transfer from the treasure state endowment fund to the treasurer state endowment special revenue account the amount of earnings, excluding unrealized gains and losses, required to meet the obligations of the state that are payable from the account for regional water systems under 90-6-710. Earnings not transferred to the treasure state endowment special revenue account must be retained in the treasure state endowment regional water system fund.

#### **MCA 17-5-703 (1999 Session)**

Beginning July 1, 1999, the tax allocation was increased from 50 percent to 75 percent.

#### **MCA 17-5-703**

Beginning July 1, 2003, the tax allocation was reduced from 75 percent to 50 percent thru June 30, 2016.

**TREASURE STATE ENDOWMENT FUNDS**

**CASH FLOW SUMMARY**  
(in millions)

<u>Fiscal Year</u>	<u>Additions to Fund</u>	<u>Book</u>	<u>Market</u>	<u>Total Inv. Income</u>	<u>Income Return</u>
7/01/93	\$10.0	\$10.0	\$10.0	--	--
1994	7.3	17.3	16.1	\$0.93	6.81%
1995	13.9	31.2	31.9	1.81	7.46
1996	7.3	38.5	38.4	2.92	8.37
1997	9.2	47.7	48.0	3.45	8.00
1998	8.7	56.4	58.9	4.25	8.17
1999	8.3	64.7	63.8	4.77	7.88
2000	9.5	77.0	73.3	5.12	7.47
2001	10.6	87.6	87.0	5.80	7.05
2002	11.7	99.3	99.7	6.80	7.28
2003	12.3	111.6	117.8	7.18	6.81
3/31/2004	5.0	116.6	121.8		

**ASSET ALLOCATION**  
(at market)

<u>FIXED INCOME</u>	<u>6-02</u>	<u>6-03</u>	<u>3-04</u>	<u>Ranges</u>
<b>Trust Funds Bond Pool (TFBP)</b>	80.0%	80.8%	86.8%	85-100%
<b>Montana Investments</b>	17.9	16.0	12.0	0-15
<b>Short-Term Investment Pool (STIP)</b>	<u>2.1</u>	<u>3.2</u>	<u>1.2</u>	<u>0-5</u>
<b>Total Fixed Income</b>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>