

**REGULAR MEETING OF THE
MONTANA BOARD OF INVESTMENTS
DEPARTMENT OF COMMERCE**

**2401 Colonial Drive, 3rd Floor
Helena, Montana**

Thursday, August 18, 2005

AGENDA

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| I. CALL TO ORDER | 12:00 p.m. |
| A. Roll Call | |
| B. Approval of the June 24, 2005 Regular Meeting Minutes | |
| C. Public Comment on Board Related Items | |
| D. Administrative Business | |
| 1. Board Member Report on Conferences Attended | |
| 2. Human Resource Committee Report | |
| 3. Audit Committee Report | |
| 4. Loan Committee Report | |
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| II. PRESENTATION – State Street Securities Lending | 1:00 p.m. |
| Mr. Jeff Trencher and Mr. Steven Meier | |
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| III. EXECUTIVE DIRECTOR REPORTS – Carroll South | 1:45 p.m. |
| A. Budgeting & Fee Setting Process Report | |
| B. Value-Added Loan Policy Revisions | |
| C. Legislative Update | |
| D. Budget Status Report | |
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| IV. BOND PROGRAM – Louise Welsh | 2:30 p.m. |
| A. INTERCAP | |
| 1. Activity Report | |
| 2. Staff Approved Loans Report | |
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| V. CHIEF INVESTMENT OFFICER REPORTS – Bob Bugni, CFA | 2:45 p.m. |
| A. Asset Allocation Review | |
| B. Investment Overview and Outlook | |
| C. Fiscal Year End Performance Report | |
| D. Educational Opportunities/Conferences/Seminars | |
| | |
| VI. MONTANA LOAN PROGRAM – Delrene Rasmussen | 3:15 p.m. |
| A. Residential Mortgage Loan Policy Revisions | |
| B. Coal Tax Loan Program Activity Report | |
| C. Pension Mortgage Program Activity Report | |

VII. INVESTMENT ACTIVITY – Equity

3:30 p.m.

- A. Domestic Equities (Montcomp) – Rande Muffick, CFA
 - 1. Strategy
- B. Montana Private Equity Pool (MPEP) – Ed Kelly
 - 1. Oak Hill Capital Partnership Fund II (OHCP II)
- C. Montana International Equity Pool (MTIP) – Rich Cooley, CFA
 - 1. MTIP Overview

VIII. INVESTMENT ACTIVITY – Fixed Income

- A. Intermediate Funds – Rich Cooley, CFA
 - 1. Strategy
- B. Long Term Funds – Rich Cooley, CFA and Bob Bugni, CFA
 - 1. Non-Investment Grade Holdings Report
 - 2. Strategy
- C. Short-Term Investment Pool – Ed Kelly
 - 1. Strategy

X. ADJOURNMENT

5:00 p.m.

The Board of Investments makes reasonable accommodations for any known disability that may interfere with a person's ability to participate in public meetings. Persons needing an accommodations must notify the Board (call 444-0001) or write to P.O. Box 200126, Helena, Montana 59620) no later than three days prior to the meeting to allow adequate time to make needed arrangements.

**MONTANA BOARD OF INVESTMENTS
DEPARTMENT OF COMMERCE**

**2401 Colonial Drive, 3rd Floor
Helena, Montana
August 18, 2005**

MINUTES

BOARD MEMBERS PRESENT:

Terry Moore, Chairman
Elouise Cobell
Teresa Cohea
Karen Fagg
Maureen Fleming
John Paull
Jack Prothero
Jim Turcotte
Calvin Wilson

BOARD MEMBERS ABSENT:

STAFF PRESENT:

Robert T. Bugni, CFA, Chief Investment Officer - Interim
Geri Burton, Deputy Director
Richard Cooley, CFA, Senior Investment Officer
Kimberly Dallas, Program Assistant
Bobbie Ecklund, Research Manager – Interim
Edward Kelly, Assistant Investment Officer
Herbert Kulow, Senior Portfolio Manager
Rande Muffick, CFA, Assistant Investment Officer
Delrene Rasmussen, Assistant Investment Officer
Carroll V. South, Executive Director
Steve Strong, Investment Analyst
Louise Welsh, Bond Program Officer

GUESTS:

Gordon Hoven, Piper Jaffray
Bruce Brensdaahl, Board of Housing
Mr. Jeff Trencher, State Street Securities Lending
Mr. Steven Meier, State Street Securities Lending

CALL TO ORDER

Chairman Moore called the regular meeting of the Board of Investments (Board) to order at 12:15 p.m. in the conference room at 2401 Colonial Drive, 3rd Floor, Helena, Montana. As noted above, the meeting convened with 9 members of the Board present.

Member Prothero motioned for approval of the June 24, 2005 minutes; Member Wilson seconded the motion and the motion was passed 9-0.

Chairman Moore called for Public Comment of Board-Related Items. *No Public Comment was made.*

ADMINISTRATIVE BUSINESS

Chairman Moore presented the following Administrative Business:

1. Board Member Report – Conferences Attended
 - Member Wilson reported that he had recently attending the IFE International Investing Conference, in Vancouver, BC. Member Wilson stated that the conference was very good and very interesting.
2. Human Resources Committee Report
 - Member Fleming, Chairperson of the Human Resource Committee, reported to the Board the activities that took place at the HR Committee Meeting.
 - i. Review of the Committee minutes for the meeting dated August 15, 2005.
 - ii. The Committee discussed the Exempt Pay Plan. Three minor changes were made to the draft. 1) Page 1 – Titled “Establishment of Pay Ranges”, “... survey of peer organizations should be conducted every even numbered year to obtain...” will be changed to, “... survey of peer organizations should be conducted periodically to obtain...”; 2) Page 2 – Titled “Establishment of Individual Pay Rates” the last sentence “Under certain circumstances, the Board may at its discretion set salaries, grant raises, bonuses, or make other adjustments using other procedures.” was added; and 3) Page 3 – “C. Experience and Skill” the sentence “Additives granted by this factor are temporary...” was removed and the language “of up to one year” was added to proceed “... performance appraisal period...”

Member Wilson motioned for approval of the Exempt Staff Pay Plan as presented by Member Fleming; Member Prothero seconded the motion and the motion was passed 9-0.

Member Fleming also presented the Committee recommendation for a salary increase of 3.5% increase in October for the exempt staff. Member Fleming motioned for approval of this recommendation; Member Wilson seconded the motion and the motion was passed 9-0.

3. Audit Committee Report
 - Member Fagg, Chairperson of the Audit Committee, reported to the Board the activities that took place at the Audit Committee Meeting.
 - i. A formal entrance conference was held with the Legislative Audit Division (LAD). The LAD will begin the audit on October 3, 2005. Member Fagg discussed the tremendous amount of work that the accounting staff will need to complete in order for the LAD to begin on schedule.

- ii. The Retainer Consultant RFP has been issued. The Committee will review the responses of the Respondents to the RFP and a board meeting will be scheduled to hear the presentations of the finalists. Independent Fiduciary Services will be advising the Audit Committee during this process.

4. Loan Committee Report

- Member Prothero, Chairperson of the Loan Committee, reported that the Committee held an informal loan committee meeting to approve an INTERCAP Loan Request.

Borrower: City of Kalispell
Board Loan Amount: \$1.1 million
Term: 10 Years
Purpose: To purchase the Wells Fargo Bank building. The building will be used to relocate various City offices.

The Loan Committee authorized staff to proceed with processing and closing this loan using the Board’s standard Bond Program Office procedures:

EXECUTIVE DIRECTOR REPORTS

Value-Added Loan Policy Revisions

Mr. Carroll South presented the Value-Added Loan Policy to the Board for approval of revisions to the Policy.

Mr. South explained to the Board that these revisions apply to the Ethanol Bill approved during the last Legislative Session. This bill amended the Value-Added law and the concern stems from the financiers who would be financing the proposed ethanol plants. The financiers are investing in an opportunity to receive dividends, and the original bill stated that a borrower could not receive dividends. The revision to the Value-Added Loan Policy applies only to Ethanol Plants. Member Fleming moved for approval of the change as recommended; Member Prothero seconded the motion and the motion was passed 9-0.

Budget Status Report

Executive Director Carroll South presented this report for the period Fiscal Year Ending 2005.

Chairman Moore asked Mr. South to update the Board on the recent activities taking place between the Board of Investments, the two Retirement Boards and the Governor’s Office.

Mr. South reported that during the last session two bills were approved to be introduced. Both of these bills increased employer contributions in the state pension plans because the last actuary determined they were dramatically under funded. Both bills were initiated in the House and passed the House. The bills were tabled in the Senate Finance and Claims Committee as it is considered that any increase in employer contribution is considered a tax increase. The Governor has been very pro-active in resolving these issues.

Mr. South also stated that a special session will take place in December and this topic will be a priority.

PRESENTATION

State Street Securities Lending

Mr. Jeff Trencher and Mr. Steven Meier presented to the Board the annual Performance Review for the Montana Board of Investments.

BOND PROGRAM

Activity Report

The Board reviewed this report for the period ending July 31, 2005.

Staff Approved Loans Report

Ms. Louise Welsh reported that:

Borrower:	Tri-City Interlocal Equipment Pool (Cut Bank)
Purpose:	To purchase an asphalt zipper and sewer camera.
Staff Approval Date	June 6, 2005
Board Loan Amount:	\$120,000
Term:	3 years

Borrower:	Stanford School District #12
Purpose:	To finance costs associated with repairing the gymnasium roof and floor and storage shed construction.
Staff Approval Date	June 16, 2005
Board Loan Amount:	\$200,000
Term:	5 years

Borrower:	Paradise School District #8
Purpose:	To finance costs associated with constructing storage buildings for food service dry and frozen foods/maintenance equipment/supplies.
Staff Approval Date	June 16, 2005
Board Loan Amount:	\$24,000
Term:	5 years

Borrower:	Beaverhead County
Purpose:	To finance costs associated with fairground restroom facility improvements.
Staff Approval Date	July 6, 2005
Board Loan Amount:	\$85,000
Term:	10 years

Borrower:	Sheridan School District #5
Purpose:	To replace the boiler/heating systems in the schools.
Staff Approval Date	July 13, 2005
Board Loan Amount:	\$131,852
Term:	5 years

Borrower:	Elliston Rural Fire District
Purpose:	To construct a new fire hall.
Staff Approval Date	July 14, 2005
Board Loan Amount:	\$100,000
Term:	10 years

Borrower:	Town of Sunburst
Purpose:	To finance costs associated with a refuse truck overhaul.
Staff Approval Date	July 15, 2005
Board Loan Amount:	\$15,000
Term:	5 years

Borrower:	Independent School District#52 (Billings)
Purpose:	To finance costs associated with building an addition for the Special Education program.
Staff Approval Date	July 19, 2005
Board Loan Amount:	\$185,000
Term:	5 years

Borrower:	Wilderness Plateau Water & Sewer District (Troy)
Purpose:	To finance costs associated with a preliminary engineering report.
Staff Approval Date	July 21, 2005
Board Loan Amount:	\$10,000
Term:	3 years

Borrower:	Cayuse Prairie School District #10 (Kalispell)
Purpose:	To finance costs associated with purchasing a 25 unit wireless computer lab.
Staff Approval Date	July 22, 2005
Board Loan Amount:	\$24,761
Term:	3 years

Borrower:	Town of Sheridan
Purpose:	To purchase land for Main Street parking.
Staff Approval Date	July 22, 2005
Board Loan Amount:	\$43,000
Term:	10 years

Borrower:	Town of Culbertson
Purpose:	To purchase a new refuse truck.
Staff Approval Date	July 25, 2005
Board Loan Amount:	\$75,758
Term:	7 years

Borrower:	City of Harlem
Purpose:	To purchase a law enforcement vehicle.
Staff Approval Date	July 28, 2005
Board Loan Amount:	\$34,504
Term:	4 years

has been approved by staff.

CHIEF INVESTMENT OFFICER REPORTS

Asset Allocation Review

Mr. Bob Bugni, Chief Investment Officer - Interim, presented the Asset Allocation report for the period ending June 30, 2005.

Quarterly Investment Performance Report

Mr. Bugni presented the Montana Board of Investments Quarterly Board Performance Report for the Fiscal Year ending June 30, 2005.

LOAN PROGRAMS

Residential Mortgage Loan Program Policy Revisions

Mr. Herb Kulow presented staff recommendation to the Board for the following changes to the Residential Mortgage Loan Program.

1. Conforming Conventional Automated Underwriting Requirement. All conforming conventional loans submitted to the Board must use Automated Underwriting through Freddie Mac or Fannie Mae with credit approval of at least Accept or Approve Eligible. The Accept or Approve Eligible designation is considered to be "A" paper, the highest quality credit available. This approval will be subject to review by Board staff of the appraisal to ensure that it is satisfactory property. Presently the Board also accepts applications that are manually underwritten. Manually underwritten loans will no longer be eligible for purchase.
2. FHA insured and VA guaranteed loans. FHA/VA loans will continue to be accepted with approved insurance or guarantee. BOH also accepts insured FHA and guaranteed VA loans with their programs and will use the Board criteria for the applications.
3. Investor Loans. Investor Loans will not be eligible. Under the current policy, the Board allows manual underwriting applications for investor property but will not accept Investor Property loans using Automated Underwriting. The Board has received very few applications for investor property and staff does not feel that the market will be affected.
4. Seasoned Loans. Staff recommends elimination of the seasoned loan provision, since there have been no requests for purchase of seasoned loans in the last eight years.
5. Jumbo Loans. Jumbo loans exceeding Freddie Mac's conforming loan limit (currently \$359,650) will not be eligible for purchase by the Board. Automated Underwriting does not consider loans exceeding the conforming loan limit.
6. Reservation extensions for construction loans. The revised policy states that the Board will adjust to the higher of the original reservation rate or the prevailing interest rate at the time of the request.
7. Partial Release of secured party. The revised policy states that the Board will not assume any costs associated with the release.
8. Lender on Line. Lenders will have access to "Lender on Line" through the BOH program. The lender will input the credit information needed for a reservation through the internet. The process will be more efficient and will eliminate manual processing of most of the reservation and commitment letters currently processed by the Board office staff. Most of the lenders are using Lender on Line with BOH and should be able to engage in the new process readily.
9. Remedies.
10. A new component has been added in the policy under Section XVI. Section 13.1 of the Board's residential service agreement outlines conditions when the Approved Lender will be required to repurchase a loan sold to the Board. Part C (iv) in the residential service agreement states that the lender must repurchase a loan if there is a violation of the

Board Mortgage Loan Policy. The remedies outlined in the new policy state clearly the circumstances when the Board will require the lender to re-purchase a loan.

11. It is prudent to have the Participant certify that the mortgage loan documents are true and accurate copies of the respective original documents.
12. The policy will also clarify that the Board review of the documents does not constitute a waiver of any warranty, representation or term thereof.

Board staff has met with BOH to discuss having BOH manage the reservation and commitment process of residential loan requests. It is staff's goal to simplify the process to allow BOH to operationally support the program. In order to prepare for that transition, staff recommends the above residential mortgage policy changes:

Staff recommends that the policies of the Board's program be modified so that BOH staff will be able to process the Board's conventional loan applications with the aide of Automated Underwriting.

Member Prothero moved for approval of staff recommendations as presented; Member Turcotte seconded the motion and the motion was passed 9-0.

Coal Tax Loan Program Activity Report

The Board reviewed this report for the period ending July 30, 2005.

Pension Mortgage Program Activity Report

The Board reviewed this report for the period ending July 30, 2005.

INVESTMENT ACTIVITY - Equity

Domestic Equities (Montcomp)

Mr. Rande Muffick presented the current investment strategy. Member Wilson moved for approval of the Montcomp strategy as presented; Member Fagg seconded the motion and the motion was passed 9-0.

Montana International Equity Pool (MTIP)

Mr. Rich Cooley presented the MTIP overview for the period ending June 30, 2005.

Montana Private Equity Pool (MPEP)

Mr. Ed Kelly presented the MPEP overview for the period ending June 30, 2005.

In addition, Mr. Kelly presented to the Board an Investment Brief for Oak Hill Capital Partnership Fund II. A due-diligence review by Staff has been completed and in compliance with the authority delegated and following the due diligence requirements outlined in the MPEP Investment Policy Statement, a commitment for \$25 million (US\$) has been made to Oak Hill Partner, Fund II.

INVESTMENT ACTIVITY – Fixed Income

Intermediate Funds

Mr. Rich Cooley presented the current investment strategy. Member Fleming moved for approval of the Montcomp strategy as presented; Member Cohea seconded the motion and the motion was passed 9-0.

Long Term Funds

Mr. Rich Cooley presented the current investment strategy. Member Fleming moved for approval of the Montcomp strategy as presented; Member Cobell seconded the motion and the motion was passed 9-0.

In addition, Mr. Cooley presented the Non-Investment Grade Holdings Report for the period ending June 30, 2005.

Short-Term Investment Pool (STIP)

Mr. Ed Kelly presented the current investment strategy. Member Fleming moved for approval of the Montcomp strategy as presented; Member Prothero seconded the motion and the motion was passed 9-0.

ADJOURNMENT

There being no further business, the meeting was adjourned at 5:00 p.m.

BOARD OF INVESTMENTS

APPROVE: _____
Terry Moore, Chairman

ATTEST: _____
Carroll South, Executive Director

DATE: _____