

These minutes were approved by the Board on November 6, 2007

**MONTANA BOARD OF INVESTMENTS
DEPARTMENT OF COMMERCE**

**Zoot Enterprises
555 Zoot Enterprises Lane
Bozeman, MT.
August 21 & 22, 2007**

MINUTES

BOARD MEMBERS PRESENT:

Terry Moore, Chairman
Teresa Cohea
Karl Englund
John Paull
Jack Prothero
Jon Satre
Jim Turcotte

BOARD MEMBERS ABSENT:

Elouise Cobell – August 21, 2007
Maureen Fleming – August 21 & 22, 2007

STAFF PRESENT:

Jason Brent, Investment Analyst	Herb Kulow, Portfolio Manager
Robert T. Bugni, CFA, Portfolio Manager	Rande Muffick, CFA, Portfolio Manager
Geri Burton, Deputy Director	Clifford A. Sheets, CFA, Chief Investment Officer
Anna Collins, Bond Program Assistant	Carroll South, Executive Director
Richard Cooley, CFA, Portfolio Manager	Steve Strong, Investment Analyst
Kim Dallas, Program Assistant/Board Secretary	Louise Welsh, Bond Program Officer
Tim House, Chief of Investment Operations	Dan Zarling, CFA, Director of Research
Ed Kelley, Portfolio Manager	

GUESTS:

Dennis Byrne, Vice President, Client Serve Manager, Goldman Sachs Asset Management
Kyle Sommer, Vice President, Quantitative Equity Team, Goldman Sachs Asset Management
Chris Marx, Senior Portfolio Manager, Global Value Equities, Alliance Bernstein (via conference call)
James Thyne, Director, Western US, Alliance Bernstein
Trevor Graham, CFA, Vice President Research, Hansberger Global Investments
Evelyn Orley, Senior Vice President Marketing, Hansberger Global Investments
Russ Kuhns, R.V. Kuhns and Associates
Becky Gratsinger, R.V. Kuhns and Associates
Peter Madsen, R.V. Kuhns and Associates
Mark Berry, State Fund
Tom Neukranz, ING Investments

CALL TO ORDER

Chairman Moore called the regular meeting of the Board of Investments (Board) to order at 1:00 p.m. in the conference room of Zoot Enterprises, 555 Zoot Enterprises Lane, Bozeman, Montana. As noted above, the meeting convened with seven members of the Board present. Member Fleming and Member Cobell were absent.

Motion: Member Jack Prothero motioned for approval of the May 8 & 9, 2007 minutes; Member John Paull seconded the motion and the motion was unanimously approved 7-0.

EXTERNAL MANAGER PRESENTATIONS

Goldman Sachs Asset Management

Mr. Cliff Sheets introduced Mr. Dennis Byrne and Mr. Kyle Sommer, Goldman Sachs Asset Management (Goldman Sachs). Goldman Sachs manages an Enhanced Index portfolio in the Domestic Equity Pool. Mr. Byrne and Mr. Sommer reviewed their firm and management strategy.

Alliance Bernstein

Mr. Cliff Sheets introduced Mr. James Thyne and Mr. Chris Marx (via conference call), Alliance Bernstein. Alliance Bernstein manages an International Large Cap Value portfolio in the International Equity Pool. Mr. Thyne and Mr. Marx reviewed their firm and management strategy.

Hansberger Global Investments

Mr. Cliff Sheets introduced Ms. Evelyn Orley and Mr. Trevor Graham, Hansberger Global Investments (Hansberger). Hansberger manages an International Large Cap Growth portfolio in the International Equity Pool. Ms. Orley and Mr. Graham reviewed their firm and management strategy.

ADMINISTRATIVE BUSINESS

Chairman Moore presented the following Administrative Business:

Loan Committee Report

Member Prothero, Chairperson of the Loan Committee, stated that a recap of Loan Activity will take place during the INTERCAP agenda item.

Human Resources Committee Report

Member Cohea, Chairperson of the Human Resource Committee, reported that the HR Committee met earlier in the day and Mr. South gave an update on the reorganization of the staff equity positions. The reorganization went very well. At this time there is not a position description for two positions, the Asset Class Manager and the Research Director. These position descriptions are being drafted and will be presented to the HR Committee at an October meeting. Personnel evaluations of the exempt staff will also be reviewed during the October HR Committee meeting. The evaluations will be presented to the Board in November.

Audit Committee Report

Member Turcotte, Chairperson of the Audit Committee, reported that the Audit Committee met earlier in the day as well. At that meeting the Audit Committee discussed in length the IFS recommendations and implementation of those recommendations.

The report included numerous recommendations which for the purpose of the progress report are aggregated into 73 substantive recommendations. Several of the recommendations are no longer applicable since the internally managed domestic equity pool has been liquidated and the dedicated personnel redeployed to other duties.

The Committee limited their discussion to those that were to be implemented at the Boards discretion and those which staff recommends no implementation.

Recommendations to be implemented at Board discretion:

1. Budget Committee – Committee recommends not to be implemented;
2. Policy and Asset Allocation Committees – Committee recommends not to be implemented;
3. Proxy Voting Committee – Committee recommends not to be implemented;
4. Meeting Minutes – Committee recommends: (1) that a draft of the minutes be e-mailed to each board member within a reasonable time (7-10 days) after the meeting. This will allow the board the opportunity to review the minutes for accuracy rather than waiting until the next regular scheduled quarterly meeting. The minutes will still require a vote of approval at the next regular scheduled meeting. (2) Once the minutes have been approved in draft format, they will be posted to the BOI website as a draft document, pending approval by the full Board. (3) Staff recommendations on which the Board acts at the meeting will be linked to the minutes on the web site.
5. Resolution No. 199 – Committee recommends no changes be made at this time.
6. Board/Staff Educational Opportunities – Committee recommends (1) that staff present or conduct trainings and orientations for Board members as the need arises; (2) RVK assist in conducting training opportunities for Board and Staff; (3) Board conference opportunities continue to be shared by staff; and (4) Staff and Board members may consider attending annual meetings offered by Managers.

Staff recommends no implementation:

Legal Counsel:

- Staff does not believe it is necessary for the Board’s contracted legal counsel to attend Board meetings and review meeting minutes. Board staff at all levels is in continuous communications with legal counsel on a variety of issues. Legal counsel reviews and signs all contracts and limited partner agreements.
- If staff believes there are legal issues that may be addressed during a specific meeting, legal counsel is invited to attend.

Executive Session Minutes:

- The Board operates under the “open meeting” laws of Montana and can only close meetings (go into Executive Session) to discuss personnel issues when the demands of individual privacy clearly exceed the merits of public disclosure or in the case of litigation involving a non state agency the strategy discussion which if divulged would be detrimental to the Board. Minutes taken in these sessions would have to be made public to the detriment of the Board and its staff.

Board Membership:

- This recommendation would require legislation to codify any such arrangement for non-voting members. The law creating the Board is very specific relative to membership and the Board has no independent authority to change its makeup. Current law requires that two of the nine Board members also be members of the two pension Boards. All Board meetings are open to the public and contain an agenda item called “public comment” at which time any member of the public, including members of the retirement systems may comment.

Board Appointment Authority:

- The Board has no control over the appointment process. Any change in the process would require legislation that would ultimately have to be signed by the Governor. In the absence of legislation any change in the process would be at the Governor's discretion.

Budget Setting Authority:

- It is doubtful that the legislature will ever grant the Board the authority to set its budget without legislative oversight and concurrence. The Board essentially operates a "monopoly" of sorts because state agencies cannot invest their funds with any other entity. The Board's investment function is one of many services provided by state agencies to other state agencies. The legislature will likely always ensure that state agencies who receive "monopoly" type services will not be overcharged.

Exempt All Board Staff:

- The Board currently has eight of 34 staff exempt from the state's pay plan which is set by the legislature. A blanket exemption will likely not happen because the legislature will continue to review and approve the fees that the Board can charge a "captive" audience. The fees cannot be controlled if there is a blanket exemption for 34 staff salaries.

Political Contributions:

- This recommendation is not relevant to the Board's operations. Unlike many public investment boards, there are no elected officials on the Board or are there Montana elected officials that could in any way influence the Board's selection of providers. While Board members are appointed by the Governor they do not serve at the pleasure of the Governor but rather serve out their term unless they are removed for "cause." Board staff who ultimately select the providers serve at the pleasure of the Board and are not subject to political pressure.

Passive Index Investment Guidelines:

- These investments have been significantly reduced since this report was written and will comprise a very small portion of the public equity portfolios. Staff believes their time would be better spent managing the active managers hired since the date of this report. As a practical matter, when the Board invests in commingled fund such as these it must accept the guidelines in place for all other participants in the fund

International Passive Investment Guidelines:

- The Pacific Basin passive portfolio has been liquidated and the European passive portfolio has been significantly reduced to the level necessary to balance the remaining active Pacific Basin portfolio. The European passive portfolio will only be used as long as the Board maintains some specific regional exposure in the MTIP. As a commingled fund, the Board does not have any influence on specific guidelines. When the international equity pool was restructured last fall, the new active managers were all given specific limits on their management of currency risk. The guidelines for each of them requires that currency hedging be limited to 15% of portfolio value and is expected to be primarily for defensive purposes. Each managers guidelines vary, but derivative instruments are addressed by most of the managers that utilize these as a portfolio tool. In certain cases these are constrained, but generally are not limited. Given the variety of markets and instruments available to international equity managers, and the challenges of buying local shares in some countries due to onerous custodial ownership rules, derivatives are often necessary as an indirect means of obtaining market exposure to some countries and companies.

Unaudited Statements:

- Staff does not believe this exercise is necessary and would result in an additional staff workload. The custodial bank provides the Board's official book of record and those records are reconciled with investment managers. Monthly reports are run from the custodial bank that includes the Board's entire

portfolio by account and asset class and all transactions for the previous month. These reports are posted on the Board's website and are available to all Board staff.

Motion: Member Turcotte motioned that the board is in concurrence with the recommendations submitted by staff; Member Paull seconded the motion and the motion was unanimously approved 7-0.

Member Turcotte publicly acknowledged Carroll South and Geri Burton for the work that was put in to the report presented to the Board.

Public Comment

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

ADJOURNED

The meeting adjourned for the day at 4:45 p.m.

CALL TO ORDER

The meeting was reconvened Wednesday, August 22, 2007 at 8:30 a.m. with eight members of the Board present. Member Fleming was absent.

ADMINISTRATIVE BUSINESS

Future Meeting Dates

Chairman Moore presented the following Administrative Business:

The next regularly scheduled meeting of the Board will take place on November 6 & 7, 2007. Staff will determine availability of the Board for a tentative future meeting date of February 12 & 13, 2008.

EXECUTIVE DIRECTOR REPORTS

State Fund Building Lease Rate - Decision

At the May 8, 2007 Board of Investments Board meeting, the Board authorized staff to proceed with the purchase of property and the planning/design of the State Fund Building. The approval also included the language "Staff will work with the State Fund staff to establish a "fair market" lease rate for the building and bring the recommended lease rate to the Board for approval at its August meeting."

The State Fund Board (Fund) and the Board of Investments (BOI) have authorized the construction of an office building to house the entire operation of the Fund that are now housed in three separate buildings. Opinions issued by legal counsels representing the Fund, the BOI, and the Legislature confirm that the Fund is legally empowered to hold an office building in its investment portfolio. The Fund has authorized both the holding of the building in its investment portfolio and the expenditure of operating funds to pay the lease.

BOI has the constitutional responsibility to manage the Fund's investment portfolio and is required to approve a real estate component in the Fund's portfolio. State law (39-71-2320, MCA, requires the State Fund to enter into an investment agreement with the Board of Investments. The required agreement was entered into on May 9, 2003.

Board of Investments staff recommends the following:

1. The lease rate for the new State Fund building be set at a 6.0 percent Cap Rate based on the total cost of the building.
2. The lease contain a 2.0 percent annual escalator.
3. The State Fund assume all responsibilities for building maintenance/operations.
4. That the Board of Investments assume all responsibilities for capital improvements on the building and manage the buildings as an investment portfolio asset.

Motion: Member Jack Prothero motioned for approval of the staff recommendations as presented; Member Jim Turcotte seconded the motion and the motion was unanimously approved 8-0.

IFS Recommendation Implementations – Informational

On September 21, 2004, the Board hired Independent Fiduciary Services (IFS) to conduct a thorough review of the Board’s operations and investment processes. The final report was issued on February 28, 2005, contained observations of Board procedures, staffing, and other important issues. The report included numerous recommendations which for the purpose of this progress report are aggregated into 73 substantive recommendations. Several of the recommendations are no longer applicable since the internally managed domestic equity pool has been liquidated and the dedicated personnel redeployed to other duties.

To evaluate the Board’s progress in implementing the recommendations, they have been separated into five categories of implementation:

1. Fully Implemented or No Longer Applicable	35
2. Partially Implemented	13
3. Not yet Implemented	9
4. To be Implemented at the Board’s Discretion	6
5. Staff recommends no Implementation	<u>10</u>
Total	<u>73</u>

A detailed analysis of each recommendation and the progress to date is included in a report written by Carroll South, Executive Director and is kept with the official documents of this board meeting.

Board Governance/Ethics Policy – Decision

Mr. Carroll South presented a proposed Governance Manual for Board review and consideration. The Manual is designed to be a comprehensive guiding document containing the previously approved Committee Charters, Class Action Litigation Policy, and Functional Organization Chart as well as a proposed Code of Ethics for Board members and staff.

One of the purposes of a public investment board Governance Policy (Policy) is to clearly spell out the fiduciary responsibilities of the Montana Board of Investments (Board) as an entity and how those responsibilities, if any, are delegated to staff to carry out the Board’s mission on a day to day basis. State law assigns to Board members the fiduciary responsibility of managing the Unified Investment Program and gives the Board the authority to hire staff as it deems necessary. Because the fiduciary responsibility ultimately lies with the Board it is important that the authority and roles of the Board as an entity and Board staff be clearly defined. Board staff has only those powers specifically delegated to them by the Board as specified in this Policy. This Policy shall be published on the Board’s web site and may only be revised by the Board at a public meeting. Staff may update Board membership rosters as necessary.

State law regarding the standards of conduct for public officers and employees defines both Montana Board of Investments (Board) members and staff as public employees and includes them within the state's Code of Ethics (Ethics Code). The Board finds that the state Ethics Code is subject to differing interpretations and may not adequately address the fiduciary responsibilities of Board members and staff. Therefore, the Board adopts this Code of Ethics tailored specifically for its members and staff who have the fiduciary responsibility of managing billions of dollars in state and local government funds. The Board's Code of Ethics, while derived from and conforming to state law, establishes standards for Board members and staff conduct that specifically relate to the Board's responsibilities, mission, and potential for conflicts of interest. The state Ethics Code contains four major provisions that are applicable to the Board's investment and operations activities.

- Monetary Provisions
- Relationship Provisions
- Time and Facilities Provisions
- Dual Salary Provisions

Decision: This is a comprehensive document that may be too lengthy and complex to both review and approve at the August meeting. The Board will submit their comments to Mr. South during the month of September and the Board Governance/Ethics Policy will be placed on the November agenda for further discussion and a decision.

Custodial Bank Selection Update

Mr. Carroll South presented an update of the Request for Proposals of Custodial Bank services. The RFP was issued on June 11, 2007 with a response due date of July 13, 2007. Three responses were received, J.P. Morgan, Northern Trust and the current custodian State Street Bank. Interviews and demonstrations took place on July 31, August 1 and August 2. Follow-up questions were sent to the respondents on August 6 with a response due date of August 9.

Currently staff is reviewing the latest responses and will likely schedule one more demonstration of the respondents' accounting systems. Staff had planned to make a recommendation at the August meeting but the process is taking longer than anticipated. The current custodial contract expires October 31, 2007. Staff is requesting a Board teleconference call board meeting in September to consider and act on a staff recommendation.

A conference call board meeting will be scheduled in September when staff is ready to present a recommendation to the Board.

BOND PROGRAM

New Staff Person

Ms. Louise Welsh introduced Ms. Anna Collins. Ms. Collins is the new Bond Program Assistant for the Bond Program.

Activity Report

The Board reviewed this report for the period ending June 30, 2007.

Loan Committee Approvals and Recommendations

Member Prothero, Chairperson of the Loan Committee, reported that the Committee reviewed and approved the following INTERCAP Loan Requests via email during the period of June 1 – August 14,

2007. The Loan Committee authorized staff to proceed with processing and closing these loans using the Board's standard Bond Program Office procedures.

June 21, 2007 - Loan Committee approved the following loans via e-mail:

Borrower:	Department of Transportation
Purpose:	To finance vehicle purchases for its Motor Pool
Board Loan Amount:	Two loans totaling \$1,006,494 (\$949,151 & \$57,343)
Terms:	6 & 7 years

Borrower:	City of Malta
Purpose:	Interim loan in anticipation of USDA Rural Development (RD) long term financing for wastewater system improvements.
Board Loan Amount:	\$3,606,000
Term:	2 years

August 6, 2007 - Loan Committee approved the following loans via e-mail:

Borrower:	Town of Columbus - increase
Purpose:	Increase to February 15, 2007 staff approved \$800,000 loan to finance costs associated with a storm sewer project.
Board Loan Amount:	\$368,278 increase; \$1,168,278 total loan
Term:	10 years

Borrower:	City of Whitefish
Purpose:	Interim loan in anticipation of issuing long term general obligation bonds to purchase property adjacent to Whitefish City beach.
Board Loan Amount:	\$3,148,530
Term:	1 year

Borrower:	Petroleum Tank Release Compensation Board (PTRCB)
Purpose:	To reimburse owners and operators for clean up costs over the course of the 2009 biennium.
Board Loan Amount:	\$2,500,000
Term:	10 years

INTERCAP Loan Request

Member Prothero presented the following INTERCAP Loan Request to the Board. This loan request was reviewed and approved by the Loan Committee on August 13, 2007. The total loan request is in excess of \$5 million dollars and requires a vote by the full Board.

Borrower:	Department of Justice – term extensions & loan increase
Purpose:	To finance costs associated with the Montana Enhanced Registration and Licensing Information Network (MERLIN) Project.
Board Loan Amount:	Loan #1054 - \$6 million increase; \$24 million total loan
Term:	Loan #824 extended to June 15, 2016 Loan #1054 extended to June 15, 2018

Motion: Member Prothero motioned for approval of this loan request as recommended; Member Satre seconded the motion and the motion was unanimously approved 8-0.

Staff Approved Loans Report

Ms. Louise Welsh reported that the following loan requests have been approved by staff and staff will process and close these loans using the Board’s standard Bond Program Office procedures:

Borrower:	Toole County
Purpose:	To finance the purchase of a new Magnetic Resonance Imaging (MRI) unit for the Marias Medical Center.
Staff Approval Date	April 2, 2007
Board Loan Amount:	\$240,000
Term:	5 years

Borrower:	Highwood Elem. School Dist. #28 & High School Dist. #4
Purpose:	To finance the costs associated with remodeling its superintendent housing.
Staff Approval Date	April 11, 2007
Board Loan Amount:	\$125,000 total; two separate loans \$68,750 and \$56,250
Term:	10 years

Borrower:	Flathead County
Purpose:	To finance costs associated with Rural Improvement District No. 142 sewer collection system improvements.
Staff Approval Date	April 17, 2007
Board Loan Amount:	\$200,000
Term:	10 years

Borrower:	Fort Ellis Fire Service Area (Bozeman)
Purpose:	To purchase a new fire rescue vehicle.
Staff Approval Date	May 3, 2007
Board Loan Amount:	\$190,000
Term:	10 years

Borrower:	York Fire Service Area (Helena)
Purpose:	To finance costs associated with constructing a fire station.
Staff Approval Date	May 3, 2007
Board Loan Amount:	\$70,000
Term:	10 years

Borrower:	Missouri River Medical Center (Fort Benton)
Purpose:	To finance costs associated with purchasing adjacent property for a parking lot.
Staff Approval Date	May 4, 2007
Board Loan Amount:	\$38,000
Term:	10 years

Borrower:	Powell County
Purpose:	To finance costs associated with multiple bridge maintenance/replacement projects throughout the County.
Staff Approval Date	May 10, 2007
Board Loan Amount:	\$250,000
Term:	7 years

Borrower:	East Helena
Purpose:	To finance costs associated with constructing a new shop building.
Staff Approval Date	May 10, 2007
Board Loan Amount:	\$177,208
Term:	10 years

Borrower:	Eureka Elementary & Lincoln High School
Purpose:	to finance costs associated with the purchase and installation of a central wood-fired (biomass) heating plant and distribution lines for all its school buildings.
Staff Approval Date	May 11, 2007
Board Loan Amount:	\$566,480 total; to separate loans the same amount \$283,240 and the same term
Term:	10 years

Borrower:	City of Havre
Purpose:	Changing two city hall buildings from a flat to a pitch roof
Staff Approval Date	May 14, 2007
Board Loan Amount:	\$455,800 total; to separate loans \$280,000 over a 15-year term and \$175,800 over 10-year term
Term:	15 & 10 years

Borrower:	Fergus County
Purpose:	To finance capitol improvements to the County Fairgrounds.
Staff Approval Date	May 15, 2007
Board Loan Amount:	\$998,000
Term:	10 years

Borrower:	Toole County
Purpose:	To finance the purchase of a new search and rescue boat.
Staff Approval Date	June 6, 2007
Board Loan Amount:	\$60,000
Term:	10 years

Borrower:	Gardiner Rural Fire District
Purpose:	To finance a replacement fire engine.
Staff Approval Date	June 6, 2007
Board Loan Amount:	\$44,000
Term:	5 years

Borrower:	Fort Benton
Purpose:	To finance the purchase of road material and a patching machine.
Staff Approval Date	June 6, 2007
Board Loan Amount:	\$97,500
Term:	8 years

Borrower:	Gallatin County
Purpose:	To finance a building purchase and costs associated with moving County departments into the building.
Staff Approval Date	June 14, 2007
Board Loan Amount:	\$999,000
Term:	10 years

Borrower:	Beaverhead County
Purpose:	To purchase state land road easements.
Staff Approval Date	June 18, 2007
Board Loan Amount:	\$120,000
Term:	10 years

Borrower:	Stillwater County
Purpose:	To finance two motor graders and one loader.
Staff Approval Date	June 21, 2007
Board Loan Amount:	\$360,610
Term:	6 years

Borrower:	Town of Hobson
Purpose:	To finance costs associated with chip sealing the streets.
Staff Approval Date	June 27, 2007
Board Loan Amount:	\$85,000
Term:	10 years

Borrower:	Paradise Valley Fire Service Area (Emigrant)
Purpose:	To purchase and convert a building into a fire station.
Staff Approval Date	June 27, 2007
Board Loan Amount:	\$60,000
Term:	10 years

Borrower:	Lockwood School District#26 (Billings)
Purpose:	To finance capitol improvements to the Lockwood School Campus
Staff Approval Date	July 3, 2007
Board Loan Amount:	\$540,000
Term:	3 years

Borrower:	Golden Valley County
Purpose:	To purchase and equip a patrol pickup for its Sheriff's Department.

Staff Approval Date	July 6, 2007
Board Loan Amount:	\$42,285
Term:	7 years

MONTANA LOAN PROGRAMS

Loan Committee Approvals and Recommendations

Member Prothero, Chairperson of the Loan Committee, reported that the Committee reviewed and approved the following Montana Loan Program Loan Requests via email during the period of June 1 – August 14, 2007. The Loan Committee authorized staff to proceed with processing and closing these loans using the Board’s standard Montana Loan Program Office procedures.

June 12, 2007 - Loan Committee approved the following loans via e-mail:

Borrower:	Purdy-Hatzenbeller Investments
Lender:	First Interstate Bank, Great Falls
Purpose:	Real estate holding company for a Tony Roma’s franchise restaurant.
Total Loan Amount:	\$1,875,000
BOI Participation:	\$1,500,000 – 80%

July 25, 2007 - Loan Committee approved the following loans via e-mail:

Borrower:	JST Properties
Lender:	First Interstate Bank, Billings
Purpose:	Real estate holding company for a Hardware Hank retail hardware store.
Total Loan Amount:	\$1,464,484
BOI Participation:	\$1,171,587 – 80%

Commercial and Residential Portfolios Report

Mr. Herb Kulow presented and the Board reviewed this report for the period ending June 30, 2007.

QUARTERLY PERFORMANCE REPORTS

The Quarterly Performance Report for the period ending June 30, 2007 was presented.

INVESTMENT ACTIVITY

State Street Performance Report by Manager

Mr. Cliff Sheets presented the Summary of External Active Managers (Net of fees) Report for the period ending June 30, 2007.

Retirement System Asset Allocation Report

Mr. Cliff Sheets presented the Retirement Systems Asset Allocation Report as of June 30, 2007.

Private Equity (MPEP)

Mr. Cliff Sheets presented the Private Edge Portfolio Holdings Performance Report, MPEP Activity Summary of the fund investments and investment briefs for the Montana Private Equity Portfolio for commitments made since the last Board meeting, as shown below.

<u>Fund Name</u>	<u>Vintage</u>	<u>Subclass</u>	<u>Amount</u>	<u>Date</u>
Avenue Special Situations Fund V	2007	Distressed (Non-Control)	\$35M	7/18/2007
OCM Opportunities Fund VII B	2008	Distressed (Non-Control)	\$25M	7/18/2007
Siguler Guff Small Buyout Opportunities Fund	2007	Buyout	\$25M	7/25/2007
Total New Commitments			\$85M	

Real Estate (MTRP)

Mr. Cliff Sheets presented the real estate fund commitments made to date, with the MTRP Activity Summary, and investment briefs for the Montana Real Estate Pool Portfolio for commitments made since the last Board meeting, as shown below.

<u>Fund Name</u>	<u>Vintage</u>	<u>Subclass</u>	<u>Amount</u>	<u>Date</u>
Carlyle Europe Real Estate Partners Fund III	2007	Opportunistic	\$30M	7/16/2007
DRA Growth and Income Fund VI	2007	Value Added	\$35M	7/16/2007
Macquarie Global Property Fund III (Asia)	2007	Opportunistic	\$30M	7/16/2007
Total New Commitments			\$95M	

Domestic Equity (MDEP)

Mr. Cliff Sheets presented the Montana Domestic Equity Pool Report as of June 30, 2007 and a summary of the pool manager changes and recent market trends as prepared by Rande Muffick.

Summary of Large Cap Transition

Mr. Rande Muffick presented a memo summarizing two recent transactions which took place in the domestic equity pool.

Since the last Board meeting there were two transitions that effected the large cap equity allocation. First, in May a portion of the internal equity pool totaling \$225 million was transitioned to the enhanced portion of the large cap allocation. The objective was to further diversify and lower tracking error within large caps. Three of the four enhanced managers received additional investment. T Rowe Price and Western Asset management received \$80 million each and Enhanced Investment Technologies received \$65 million.

State Street Global Markets (SSGM) was selected as the transition manager based upon a lower cost per trade estimate. The trades implemented in the transition took place on May 23rd and the enhanced managers assumed responsibility for the funds on May 31st. The composition of total trades was 34% in-kind transfers, 25% crossed in trading networks, 22% market trading, and 19% cash and equity futures trading. The cost of the transition or "Total Implementation Shortfall" was -6.3 basis points or a transition gain of \$141, 757. The net gain occurred due to a favorable movement of the legacy portfolio relative to the target portfolio on the trade date.

The second transition took place in July. The objective was to diversify from the remaining internally managed portfolio into five large cap long-only managers. Three growth managers (Columbus Circle Investors, Rainier Investment Management, and Renaissance Investment Management) and two value managers (Barrow Hanley Mewhinney & Strauss, and Quantitative Management Associates) received

their initial investments. Additionally, the BGI 500 Index portfolio was chosen to receive residual proceeds beyond the amount of the allocation directed to the large cap long-only style category. A total of \$856 million was transitioned in the following amounts: \$150 million each to Columbus, Rainier, and Quantitative, \$220 million to Barrow Hanley, \$154 million to Renaissance, and \$32 million to the BGI 500 Index fund.

State Street Global Markets (SSGM) was selected as the transition manager based upon a much lower dollar commission cost estimate. The transition took place on July 31st with the managers assuming responsibility for the respective funds on August 7th. The composition of total trades was 40% in-kind transfers, 39% crossed in trading networks, 17% market trading, and 4% cash and equity futures. The cost of the transition or "Total Implementation Shortfall" was 33 basis points or \$2,864,057. This was a much higher cost than expected due to a very volatile market on the trade date and an adverse move in the legacy portfolio relative to the target portfolio.

Update on Large Cap US Equity Search (130/30)

Mr. Cliff Sheets presented a verbal update on the Large Cap US Equity search, also referred to as the 130/30 managers. The RFP Process was completed in June and on schedule. Four managers were selected: Analytic Investors, State Street Global Advisors, Martingale and JP Morgan.

Staff plans to target an initial 15% allocation within the large cap US equity holdings, or approximately 13% of the total domestic equity pool. This is an approximate dollar amount of \$450 million.

Staff preference is to set each manager up in a separate account as opposed to using their commingled funds. Separate accounts will provide better transparency which is important given the relatively new strategies. A necessary step to enabling separate account manager is to hire a prime broker. The prime broker will facilitate the borrowing of stock for purposes of short – selling and the financing of additional long positions that are the crux of a 130/30 strategy. A Request for Information has been prepared by R.V. Kuhns and will be issued on August 30, 2007. The deadline for submissions will be October 5, 2007. Staff hopes to make a selection and enter into a contract by late November, at which time the transition into the new managers will occur. Prior to funding the new managers, staff will obtain and review up-to-date performance data to confirm confidence in the selections made. All contracts with selected managers must be finalized by this time. Staff intends to complete the process by calendar year end.

International Equity (MTIP)

Mr. Cliff Sheets presented the Montana International Equity Pool Report for the period ending June 30, 2007, and discussed market trends during the quarter.

Fixed Income

Mr. Cliff Sheets presented the Fixed Income Overview and Strategy, the Below Investment Grade Holdings Report, the Short-Term Investment Pool, State Fund Insurance and Treasurer's Fund Portfolio Reports as prepared by the respective portfolio managers, Mr. Bob Bugni and Mr. Richard Cooley.

A question was raised with respect to the two bond pools regarding the significant difference in weighting of U.S. Treasury and Corporate Credit sectors between the portfolios and the benchmark, the Lehman Aggregate Index. Mr. Sheets responded that there have been internal discussions with staff and R.V. Kuhns as to whether the Lehman Aggregate is the appropriate benchmark for the pools and this was an ongoing consideration. He acknowledged that underweighting Treasuries and overweighting

credit has been a long-standing portfolio preference on the part of the portfolio manager over time. This has generally been successful, but does entail greater risk. The question of bond policy and further diversification across fixed income as an asset class is expected to be addressed in greater detail over coming months. At that time it is expected that tolerance bands regarding portfolio risk characteristics will be discussed further with the Board and the policy documents revised.

Mr. Bugni presented a staff recommendation to be given authority to invest in Agency hybrid securities. Agency hybrid securities are mortgaged-backed securities guaranteed by a U.S. Government Agency. Agency hybrid securities have the characteristics of both fixed-rate and adjustable rate mortgages thus the hybrid name. They have a fixed coupon for 3, 5, 7 or 10 years after which the mortgage becomes an adjustable rate resetting periodically. These securities were added to the Lehman Aggregate Bond Index in April and as of June 30, they comprise 3.82 percent of the benchmark. Staff has no plans to purchase these securities at this time, however if market conditions change the securities may be used to diversify or add value to the portfolio.

Motion: Member Prothero motioned for approval of this staff recommendation as presented; Member Paull seconded the motion and the motion was unanimously approved 8-0.

Investment Policy Statements

Mr. Bob Bugni presented five Investment Policy Statements. Three are new accounts requiring Board approval and two are existing accounts which have been modified and also require Board approval.

Big Sky Economic Development Fund – The 2005 Montana Legislature (HB 249) created the Big Sky Economic Development Fund as a separate subfund within the Permanent Coal Trust. The income produced by this subfund will be transferred to a separate income account called the economic development special revenue account. The Legislature directed that income be spent to provide financial assistance to local governments for qualified economic development projects and to provide financial assistance to certified regional development corporations and certain other economic development organizations. The Legislature also established a Big Sky Economic Development Program within the Department of Commerce to oversee this program.

Older Montanans Trust Fund – The 2007 Montana Legislature (SB 155) created the Older Montanans Trust Fund. The money in the fund may be used to create new, innovative services or to expand existing services for the benefit of Montana residents 60 years of age or older that will enable those Montanans to live an independent lifestyle in the least restrictive setting and will promote the dignity of and respect for those Montanans. The legislature provided for a transfer of funds from the Health and Medicaid Initiates account to this new trust fund.

Endowment for Children – The 2007 Montana Legislature (HB 608) created the Endowment for Children. The Montana Children's Trust Fund Board was established in 1985, consisting of seven members appointed by the Governor for 3-year terms. The purpose of the endowment is to provide a permanent source of funding to support the programs and services related to a broad range of child abuse and neglect, primary prevention activities, and family resource programs operated by nonprofit or public, community-based educational and service organizations.

Old Fund Insurance – Staff recommended various changes to the Old Fund Insurance Investment Policy Statement.

Trust & Legacy Fund – Staff recommended various changes to the Trust & Legacy Fund Investment Policy Statement.

Motion: Member Terry Cohea motioned for approval of the staff recommendations as presented; Member Englund seconded the motion and the motion was unanimously approved 8-0.

NEXT MEETING

The next regularly scheduled meeting of the Board will be November 6 & 7, 2007.

ADJOURNMENT

There being no further business, the meeting was adjourned at 1:15 p.m.

BOARD OF INVESTMENTS

APPROVE: _____
Terry Moore, Chairman

ATTEST: _____
Carroll South, Executive Director

DATE: _____