

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

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

**Special Conference Call Board Meeting
Friday, September 7, 2007**

AGENDA

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|-------------|---|------------------|
| I. | CALL TO ORDER | 9:00 a.m. |
| | A. Roll Call | |
| | B. Public Comment - <i>Public Comment on issues with Board Jurisdiction</i> | |
| II. | EXECUTIVE DIRECTOR REPORTS – Carroll South | 9:10 a.m. |
| | A. Custodial Bank Recommendation and Decision | |
| III. | ADJOURNMENT | 9:45 a.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.

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

**MONTANA BOARD OF INVESTMENTS
DEPARTMENT OF COMMERCE
SPECIAL CONFERENCE CALL BOARD MEETING**

**2401 Colonial Drive, 3rd Floor
Helena, Montana
Friday, September 07, 2007**

MINUTES

BOARD MEMBERS PRESENT: Terry Moore, Chairman
Karl Englund
John Paull
Jack Prothero
Jon Satre
Jim Turcotte

BOARD MEMBERS ABSENT: Elouise Cobell
Teresa Cohea
Maureen Fleming

STAFF PRESENT:

Polly Boutin, Accountant	Gayle Moon, Accounting Fiscal Manager
Geri Burton, Deputy Director	Mari Rohrig, Accountant
Kim Dallas, Program Assistant/Board Secretary	Coralie Sciuchetti, Accountant
Rachel Fairbank, Accountant	Clifford A. Sheets, CFA, Chief Investment Officer
Linda Hunter, Accountant	Carroll South, Executive Director

GUESTS: Jonathan Kowolik, R.V. Kuhns & Associates

CALL TO ORDER

Chairman Moore called the special conference call board meeting of the Board of Investments (Board) to order at 9:00 a.m. As noted above, the meeting convened with six members of the Board present. Member Elouise Cobell, Member Terry Cohea and Member Maureen Fleming were absent.

Public Comment

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

EXECUTIVE DIRECTOR REPORTS

Custodial Bank Recommendation and Decision

Mr. Carroll South presented staff recommendation that the Board approve the selection of State Street Bank as its custodial bank subject to successful contract negotiations.

State Street Bank, the current custodian, was first hired by the Board in December 1993 under a seven year contract. In 2000, the Board issued a Request for Proposal (RFP) for custodial banking services. State Street Bank was the only respondent and the Board entered into another seven year contract that expires October 31, 2007.

A RFP for custodial banking was issued through State Procurement on June 11, 2007 with a response due date of July 13, 2007. Responses were received from JP Morgan, Northern Trust and State Street Bank.

After reviewing the responses, staff sent a list of additional questions to each respondent and scheduled interviews and demonstrations at the Board's office on July 31, August 1, and August 2. Based on JP Morgan's responses to the RFP and the two sets of follow up questions the firm was eliminated from further consideration. Northern Trust and State Street Bank were interviewed and provided further demonstrations at the Board's offices on August 27 and 28.

Consensus scoring was conducted by Cliff Sheets, Gayle Moon, and Carroll South on August 31, 2007. That resulted in scores of 70 and 80 respectively for Northern Trust and State Street Bank. The scoring was then reviewed and approved by State Procurement.

Motion: Member Jim Turcotte motioned for approval of the staff recommendations as presented; Member Karl Englund seconded the motion and the motion was unanimously approved 6-0.

A copy of the memorandum written by Carroll South is attached to these minutes.

ADJOURNMENT

There being no further business, the meeting was adjourned at 9:45 a.m.

BOARD OF INVESTMENTS

APPROVE: _____
Terry Moore, Chairman

ATTEST: _____
Carroll South, Executive Director

DATE: _____

MEMORANDUM

Montana Board of Investments

Department of Commerce

2401 Colonial Drive, 3rd Floor

Helena, MT 59601 (406) 444-0001

To: Board Members

From: Carroll South, Executive Director

Date: September 5, 2007

Subject: Custodial Bank Selection Recommendation

Recommendation – Staff recommend that the Board approve the selection of State Street Bank as its custodial bank subject to successful contract negotiations.

History – State Street Bank, the current custodian, was first hired by the Board in December 1993 under a seven year contract. Prior to the expiration of the contract in 2000, the Board issued a Request for Proposals (RFP) for custodial banking services. State Street Bank was the only respondent and the Board entered into another seven year contract that expires October 31, 2007.

Current Selection Process – A RFP for custodial banking was issued through State Procurement on June 11, 2007 with a response due date of July 13. Responses were received from JP Morgan, Northern Trust, and State Street Bank. After reviewing the responses, staff sent a list of additional questions to each respondent and scheduled interviews and demonstrations at the Board's office on July 31, August 1, and August 2. Three days of interviews and demonstrations spawned more questions and another set of follow up questions were sent to each respondent.

Based on JP Morgan's responses to the RFP and the two sets of follow up questions the firm was eliminated from further consideration. Northern Trust and State Street Bank were interviewed and provided further demonstrations at the Board's offices on August 27 and 28. Cliff, Gayle, and the Executive Director conducted consensus scoring on August 31 that resulted in scores of 70 and 80 respectively for Northern Trust and State Street Bank. The scoring was then reviewed and approved by State Procurement. Staff from R.V. Kuhns, Geri Burton, and Chris Phillips, our contracted employee, assisted through out the RFP and scoring processes.

Contract Details – One of the ancillary benefits of going through a custodial bank search was that staff discovered these banks provide services to other clients that board staff are currently handling internally.

Participant Accounting – The Board manages seven investment pools that operate similar to mutual funds. Board staff currently enter investment pool data into two separate accounting systems provided by the custodian, a securities accounting system

residing at the custodian's facility and a participant accounting system residing at the Board's facility.

Under the new contract, State Street will host the participant accounting system at its office and all data entered into one system will flow to the other with no additional manual entry. This single entry process will reduce errors and make Board accounting reconciliation activities easier. Additionally, because the participant accounting system will be housed at State Street's facility, the bank will assume the responsibility of printing and mailing participant statements.

Back Office Alternative Investment Services – The Board is currently increasing pension fund investments in Private Equity and Real Estate and systematically hiring additional managers. Most of these investments are in Limited Partnerships that are labor intensive from an accounting perspective. Further, General Partner capital calls and capital distributions can be difficult to interpret and record accurately. Currently, State Street Bank is entering this data in its performance platform, while Board staff are interpreting the data and recording it in State Street's securities accounting system.

Under the new contract, State Street will assume all of these duties. The capital calls and distributions will be interpreted by State Street staff who have extensive experience with these managers. State Street staff will enter the data in the securities accounting system which will then flow to the performance platform with no further manual entry.

Cash Movement – State Street has a "Cash Module" system that will simplify and expedite the movement of cash to and from local government bank accounts and the wiring of capital call funds to alternative investment managers. State Street will assume the responsibility of providing ACH services to and from banks for local government Short Term Investment Pool participants. Board staff currently use a system for this purpose supplied by US Bank. The Module will also be used to wire funds for capital calls and investment manager fees.

Fees – The RFP required respondents to submit a flat annual fee for all contract services during the first four years of a maximum seven year contract (the fee cannot increase during the four year period). Any annual increases for the remaining three years will be the lesser of the Consumer Price Index or 5.0 percent. The "best and final" fee offered by Northern Trust and State Street was \$1.4 million and \$1.5 million respectively. Fees comprised 20 points of a total 100 in consensus scoring and both firms received scores of 15 in the fee category. The current contract with State Street is nearing \$1.0 million annually and increases slightly when additional alternative investment managers are hired.

When the new contract fee is viewed historically, it seems reasonable. The first annual fee with State Street in 1993 was \$450,000. At the end of the new four year contract period in 2011 the fee will be \$1,500,000 or less than a 7.0 percent annual increase during the 18-year period. During that period the Board's investment portfolio will have grown significantly, from \$4.65 billion to \$13.2 billion as of June 30, 2007 and will

likely grow an additional 5.0 percent to 6.0 percent annually through 2011. The portfolio is also much more complex with international exposure and significantly more alternative investment managers. In 1993, the Board had just two alternative investment managers. As of June, 2007 the Board had committed to 89 individual private equity and private real estate funds that need to be tracked separately and is continuing to make commitments. Additionally, as discussed above State Street will be assuming additional duties currently carried out by Board staff.

If you would like more detailed information about the RFP process and the scoring, staff will make that information available to you.