

These minutes are Approved and Final. Full Board review and decision took place at the April 3, 2012  
Regular Meeting of the Board.

**MONTANA BOARD OF INVESTMENTS  
DEPARTMENT OF COMMERCE  
2401 Colonial Drive, 3<sup>rd</sup> Floor  
Helena, Montana**

**MINUTES OF THE MEETING  
February 21-22, 2012**

**BOARD MEMBERS PRESENT:**

Gary Buchanan, Chairman  
David Ageson  
Bob Bugni  
Karl Englund  
Mark Noennig  
Quinton Nyman  
Jack Prothero  
Jon Satre  
Jim Turcotte (via telephone)

**LEGISLATIVE LIAISONS PRESENT:**

Senator Joe Balyeat  
Representative Franke Wilmer

**STAFF PRESENT:**

Carol Ann Augustine, Board Secretary	Rande Muffick, CFA, Portfolio Manager, Public Equities
Jason Brent, CFA, Alternative Investments Analyst	Jon Putnam, CFA, FRM, Fixed Income Investment Analyst
Geri Burton, Deputy Director	Nancy Rivera, Credit Analyst
Richard Cooley, CFA, Portfolio Manager, Fixed Income/STIP	John Romasko, CFA, CPA, Fixed Income Investment Analyst
David Ewer, Executive Director	Nathan Sax, CFA, Portfolio Manager, Fixed Income
Tim House, Investment Operations Chief	Clifford A. Sheets, CFA, Chief Investment Officer
Ethan Hurley, Portfolio Manager, Alternative Investments	Steve Strong, Equity Investment Analyst
Ed Kelly, Alternative Investments Analyst	Louise Welsh, Bond Program Officer
Herb Kulow, MCMB, Portfolio Manager, In-State Loan Program	Dan Zarlring, CFA, Director of Research
Gayle Moon, CPA, Financial Manager	

**GUESTS:**

Norma Buchanan  
Becky Gratsinger, RV Kuhns and Associates  
Mark Higgins, RV Kuhns and Associates  
Pat Hurley  
Chuck Johnson, Associated Press  
Mike Manion, Attorney, Department of Administration  
Dore Schwinden, Director, Department of Commerce  
Jim Voytko, RV Kuhns and Associates  
Kris Wilkinson, Legislative Fiscal Division

### **CALL TO ORDER**

Board Chairman Gary Buchanan called the regular meeting of the Board of Investments (Board) to order at 1:09 PM in the Board Room on the third floor at 2401 Colonial Drive, Helena, Montana. As noted above, a quorum of Board Members was present.

Chairman Buchanan introduced new Board Member Bob Bugni; Member Bugni previously worked for the Board of Investments for several years and is well known to the Board and staff. He also introduced Dore Schwinden, Director of the Department of Commerce. Director Schwinden commented on the close working relationship that has been established between the Board of Investments and the Department of Commerce.

Chairman Buchanan reported that Board Member Karl Englund has accepted the position of Vice Chair of the Board.

Board Member Jack Prothero made a Motion to approve the Minutes of the November 15-16, 2011 Board Meeting; Member Jon Satre seconded the Motion. The Motion was carried 9-0.

### **ADMINISTRATIVE BUSINESS**

#### **Audit Committee Report**

Audit Committee Member Jon Satre reported that the Board's Audit Committee was scheduled to meet upon adjournment of the November 15-16, 2012 Board meeting to discuss the Board's fiscal year 2011 financial audit report which is prepared by the Legislative Audit Division; however, the Legislative Audit Division had to reschedule because they had not yet completed the audit.

The Legislative Audit Division concluded their audit and scheduled an Exit Conference meeting with the Board's Audit Committee on Thursday, December 15, 2011.

Ms. Tori Hunthausen, the State's Legislative Auditor, reported that the Legislative Audit Division completed its Financial Audit for the Fiscal Year Ended June 30, 2011 and the report contained an unqualified opinion for the Board's Consolidated Unified Investment Program and Enterprise Fund. In addition, she reported that the audit did not contain any recommendations to the Board.

#### **Human Resource Committee (HR) Report**

HR Committee Chair Karl Englund reported that 1% and 2% annual pay increases were recently granted for classified employees within the Department of Commerce. The HR Committee now recommends providing a 1% pay increase to all exempt employees, except the Executive Director. The 1% pay increase would take effect January 1, 2012.

HR Committee Chair Karl Englund made a Motion to approve a 1% annual pay increase for exempt staff, except the Executive Director; Member Quinton Nyman seconded the Motion. The Motion was carried 9-0.

HR Committee Chair Englund reported that the Committee reviewed and approved the proposed changes to the Organizational Chart, that include transitioning supervision of the INTERCAP Manager and the Network Administrator from the Executive Director to the Deputy Director.

HR Committee Chair Englund made a Motion to adopt the new Organizational Chart; Member Jack Prothero seconded the Motion. The Motion was carried 9-0.

#### Loan Committee Report

Loan Committee Chair Jack Prothero reported that the Committee discussed Tax Increment Financing (TIF) and concurred with staff's recommendation to continue to preclude TIF bonds or loans in the INTERCAP Program. Also, it was reported that the Committee considered a \$4,983,011 loan request from Anaconda School District to finance the renovation of their football stadium over a 10-year term. The Committee concurred with staff's recommendation to deny the loan based on their earlier discussion of TIF.

The Loan Committee is authorized to approve BOI loans from \$1-5 million. They authorized staff to proceed with processing and closing the following loan using the Board's standard Bond Program office procedures.

Borrower:	State of Montana Department of Transportation
Purpose:	Purchase replacement vehicles for the State Motor Pool.
LC Approval Date:	December 19, 2011
Board Loan Amount:	\$2,100,000
Other Funding Sources:	
Total Project Cost :	\$2,100,000
Term:	7 years

The Loan Committee also authorized a loan increase to the Town of Whitehall; the total amount of the interim loan is now \$3,300,000 in anticipation of USDA Rural Development long term financing its wastewater project.

#### 2012 Meeting Schedule

Mr. David Ewer proposed adding two Board Meetings to the schedule for a total of six meetings in 2012. Mr. Ewer suggested the agenda for the two additional meetings should differ from the quarterly performance meetings. He also asked to reschedule the October 2, 2012 meeting; it will be held October 4, 2012 instead. There was discussion regarding a possible Joint Board of Investments', Public Employees' Retirement System (PERS) and Teachers' Retirement System (TRS) Board Meeting in October. Staff will follow-up with PERS and TRS staff regarding this meeting and report back to the Board.

#### Public Comment

Chairman Buchanan called for public comment on Board issues. There was no public comment.

### **EXECUTIVE DIRECTOR'S REPORT**

#### Overall Comments

This was the first Board Meeting for Mr. David Ewer as Executive Director of the Board of Investments. Mr. Ewer addressed the Board regarding his management style and emphasis, and affirmed that we work for the people of Montana. He also noted that the Board's senior management, Cliff Sheets, CIO, Geri Burton, Deputy Director, Gayle Moon, Finance Manager, and Herb Kulow, Loan Portfolio Manager, now meet every week.

### Agendas Going Forward

Mr. David Ewer told the Board that having six meetings during the year will give the Board an opportunity to look at subjects other than performance, including the Short Term Investment Pool, operations, accounting and State cash management. Board Members are also encouraged to bring subjects of interest to the meetings.

### Changes to Governance Policy

Mr. Ewer introduced Mr. Mike Manion, Chief Attorney for the Department of Administration. They spoke to the Board about suggested changes to the Governance Policy relating to our procurement process. The changes will serve to reassert the Board's authority over the type of investments to be made. The Departments of Administration and Commerce agree with the recommended changes.

Board Member Karl Englund made a Motion to adopt the recommended changes to the Governance Policy; Member David Aageson seconded the Motion. The Motion was carried 9-0.

### Investment Consultant RFP

Executive Director David Ewer recommended that the Board begin the request for proposal (RFP) process for a general investment consultant, as it is now considered 'best practices' within the fiduciary responsibilities of pension boards. RV Kuhns & Associates, Inc. is the Board's current consultant; their contract will expire in November 2011.

Member Jon Satre made a Motion to proceed with the RFP process for an investment consultant per staff's recommendations outlined in Mr. David Ewer's memo; Member Mark Noennig seconded the Motion. The Motion was carried 9-0.

### Permanent Coal Trust Fund Investment Policy Statement

Mr. Ewer presented the new investment policy statement for Board review and approval. The new policy replaces four current policies and will cover the Permanent Coal Trust; Treasure State Endowment Regional Water System Fund; Treasure State Endowment Fund; and Big Sky Economic Development Fund. Staff recommends Board approval of the new policy.

Member Jack Prothero made a Motion to approve the Permanent Coal Tax Trust Fund Investment Policy Statement; Member Karl Englund seconded the Motion. The Motion was carried 9-0.

### Tax Increment Financing

Mr. David Ewer spoke to the Board about Tax Increment Financing (TIF) and the Board's 1992 decision not to allow the INTERCAP Loan Program to be used for such loans, stating it falls outside the risk parameter for INTERCAP. Staff recommends approval of the revised INTERCAP Loan Policy that precludes TIF bonds or loans in the program.

Member David Aageson made a Motion to approve the revised INTERCAP Loan Policy; Member Karl Englund seconded the Motion. The Motion was carried 9-0.

### Performance Audit

Mr. Ewer reported that the Board is currently number five on the Legislative Audit Committee's list for a performance audit. The Legislative Audit Committee has never conducted a performance audit on the Board. Mr. Ewer believes the performance audit will take place sometime this summer.

### April Meeting

Mr. Ewer suggested the agenda for the April Board Meeting include asset allocation, private equity and costs. Chairman Gary Buchanan suggested Board travel and educational opportunities as agenda items. Chairman Buchanan encouraged Board Members to pursue training opportunities, including bringing the training to the Board. The Board's long range plans and goals could also be discussed. Several other Board Members offered ideas and suggestions to be covered at the April or other Board Meetings, including the current structure of investment pools and potential changes; a view of where the markets are and where they are going; the role of the Board regarding the actuarial return assumption on pension funds, contributions, and maximizing returns; review of the IFS study; and taking another look at hedge funds.

## **MONTANA LOAN PROGRAMS**

### Commercial and Residential Portfolios Report

Mr. Herb Kulow reported that the commercial and residential loan portfolios continue to decline as a result of the uncertain economy; however, he does have several potential projects.

As of February 6, 2012 the commercial loan portfolio totaled \$145,747,241; this included five outstanding reservations in the amount of \$5,979,800 and four loan commitments in the amount of \$9,858,259. Our two past due loans are SBA guaranteed, totaling \$212,099 or 0.15% of the total portfolio.

As of January 31, 2012 the residential loan portfolio totaled \$23,179,920 with no outstanding reservations. Eleven loans were past due totaling \$712,830 or 3.08% of the portfolio. Of those past due loans, nine were past due over 90 days totaling \$652,144, six of those loans were guaranteed totaling \$374,607 and three were conventional loans totaling \$277,537.

The Veterans Home Loan Mortgage Program has funded one loan for \$172,830; there are currently 12 outstanding reservations totaling \$1,932,259.

### Bond Program Reports

#### Activity Report

Ms. Louise Welsh reported on the remarketing of the INTERCAP bonds. The INTERCAP rate will be set on March 1, 2012 and the current loan rate of 1.95% is expected to drop one more time for borrowers.

Ms. Welsh presented the INTERCAP report for the period ending December 31, 2011. She told the Board that FY 2012 fundings are almost \$15 million and she expects that number to be \$24 million by the end of the year. Year to date commitments totaled \$19,474,393. Total loans outstanding are \$80,897,577; bonds outstanding are \$95,530,000.

Board Chairman Gary Buchanan commended Ms. Welsh on how well she handled the Anaconda School District loan request.

#### Staff Approved Loans Report

The Board reviewed this report for the period of July 1, 2011 through September 30, 2011.

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Borrower:	Ravalli County Economic Development Authority (Hamilton)
Purpose:	Ravalli Entrepreneurship Center parking lot expansion
Staff Approval Date:	October 13, 2011
Board Loan Amount:	\$70,000
Other Funding Sources:	
Total Project Cost:	\$70,000
Term:	10 years

Borrower:	Teton County
Purpose:	Building purchase for an ambulance station
Staff Approval Date:	October 27, 2011
Board Loan Amount:	\$ 75,000
Other Funding Sources:	\$ 90,000
Total Project Cost:	\$165,000
Term:	10 years

Borrower:	Town of Geraldine
Purpose:	Purchase 1991 Sutphen TS 4-door pumper fire truck
Staff Approval Date:	October 31, 2011
Board Loan Amount:	\$30,000
Other Funding Sources:	
Total Project Cost:	\$30,000
Term:	7 years

Borrower:	Sweet Grass County
Purpose:	Emergency road and bridge repairs from flooding in anticipation of federal aid
Staff Approval Date:	November 7, 2011
Board Loan Amount:	\$995,000
Other Funding Sources:	
Total Project Cost:	\$995,000
Term:	15 years

Borrower:	City of Kalispell
Purpose:	Purchase a dump truck and compactor
Staff Approval Date:	November 16, 2011
Board Loan Amount:	\$172,000
Other Funding Sources:	
Total Project Cost:	\$172,000
Term:	5 years

Borrower:	Lone Rock Elementary School District #13 (Stevensville)
Purpose:	Install a new septic system
Staff Approval Date:	November 18, 2011
Board Loan Amount:	\$40,000

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Other Funding Sources:	
Total Project Cost:	\$40,000
Term:	10 years

Borrower:	Town of Sheridan
Purpose:	Engineering services for wastewater improvements. Borrower reimbursed by USDA RD once the RD loan closes.
Staff Approval Date:	December 15, 2011
Board Loan Amount:	\$100,000
Other Funding Sources:	\$3,550,057-USDA RD Loan; \$3,190,249-USDA RD Grant; \$100,000-DNRC RR Grant; \$25,000-Borrower portion
Total Project Cost:	\$6,865,306
Term:	6 years



## MONTANA UNIVERSITY SYSTEM

Borrower:	Montana State University – Billings
Purpose:	Remove/Replace Rimrock Hall (residence hall) roof
Staff Approval Date:	October 27, 2011
Board Loan Amount:	\$500,000
Other Funding Sources:	
Total Project Cost:	\$500,000
Term:	10 years

Borrower:	Montana State University - Billings
Purpose:	Remodel Union Bookstore
Staff Approval Date:	October 31, 2011
Board Loan Amount:	\$580,000
Other Funding Sources:	\$120,000
Total Project Cost:	\$700,000
Term:	10 years

## CONSULTANT REPORTS

### RV Kuhns & Associates

Ms. Becky Gratsinger, Mr. Mark Higgins and Mr. Jim Voytko presented an overview of the Investment Performance Analysis Report, Quarter Ended December 31, 2011. (A complete copy of this report is kept on file with the documents of this meeting.)

## INVESTMENT ACTIVITIES/REPORTS

### Retirement System Asset Allocation Report

Mr. Cliff Sheets presented the Retirement System Asset Allocation Report for the quarter ended December 31, 2011. Mr. Sheets noted total equity was up 2.1% from the previous quarter to 65.7%, primarily reflecting the bounce in public stock returns. The allocation to fixed income decreased 1.3% to 26.1%, in part due to the sale of approximately \$33 million of RFBP units during the quarter, and the dilution effect of higher stock prices. The allocation to real estate also decreased slightly to 7.6% due to this dilution effect. Cash was kept very low, near the 1% minimum, because it is essentially a zero return asset class and no larger reserves were deemed necessary at this time. There were no new purchases of the real estate pool during the quarter. Net long term investments of \$11 million went into the pools.

### Comparison to State Street Public Fund Universe

Mr. Sheets reviewed a comparison of the two large pension plans to the State Street public fund universe in terms of relative performance and asset allocation as a supplement to the RV Kuhns public fund universe return comparison.

Mr. Sheets pointed out that the cash allocation is low, fixed income and public equities are close to the median weight, and real estate and private equity are above average, though not as much as indicated here when considering other surveys of public fund asset allocation.

## Private Asset Pool Reviews

### Private Equity (MPEP)

Mr. Ethan Hurley presented a comprehensive overview of the private equity portfolio for the quarter ended September 30, 2011, including total exposure by strategy; market value exposure by industry; geographic and investment vehicle exposure; and returns for the overall portfolio and by fund. The report also showed quarterly cash flow for the portfolio through December 31, 2011.

One new commitment was made since the November 2011 Board meeting:

<b>Fund Name</b>	<b>Vintage</b>	<b>Subclass</b>	<b>Sector</b>	<b>Amount</b>	<b>Date</b>
Gridiron Capital Fund II, LP	2011	Small Buyout	Diverse	\$15M	12/1/11

Mr. Hurley compared the performance of the private equity portfolio to the State Street Private Equity Index.

## ADJOURNED

Chairman Buchanan adjourned the Meeting for the day at 5:05 PM.

**CALL TO ORDER – Day 2**  
**February 22, 2012**

Board Chairman Gary Buchanan reconvened the meeting Wednesday, February 22, 2012 at 8:32 AM with seven members of the Board present. Board Members Quinton Nyman and Jim Turcotte were absent.

**Public Comment**

Chairman Buchanan called for public comment on Board issues. There was no public comment.

**INVESTMENT ACTIVITIES/REPORTS, continued**

**Private Asset Pool Reviews**

Mr. Cliff Sheets distributed a report of Real Estate Performance by Fund Category in response to a general question regarding real estate performance during the prior day. Mr. Sheets pointed out that the real estate market lagged stocks and credit-related bonds during the bear market and has also lagged on the upside during the rally in "risk" assets. There has been a lag in the performance of Value-add compared to Core since performance turned positive in early 2010 however we expect to catch up in relative returns in the higher risk real estate categories once core returns enter a more stable period.

**Real Estate (MTRP)**

Mr. Ethan Hurley presented a comprehensive overview of the following private edge reports for the third quarter: total exposure by strategy; market value exposure by property type; total exposure by geography; and time weighted return of the portfolio and internal rates of return by fund. The report also showed quarterly cash flow for the portfolio through December 31, 2011.

One new commitment was made since the November 2011 Board meeting. This was an add-on to a prior commitment.

<b>Fund Name</b>	<b>Pool</b>	<b>Subclass</b>	<b>Sector</b>	<b>Amount</b>	<b>Date Funded (Core) or Date of Decision</b>
Angelo Gordon Core Plus Realty Fund III, LP	MTRP	Value-add	Diverse	\$10 M	12/20/11

**Partnership Focus List**

There were no changes to the MPEP and MTRP Partnership Focus Lists since the November 2011 Board Meeting. Mr. Ethan Hurley reported that we are closely monitoring a limited number of managers; he will bring them before the Board if and when it is appropriate.

**Public Asset Pool Reviews**

**Domestic Equity (MDEP)**

Mr. Rande Muffick reported on the Montana Domestic Equity Pool as of December 31, 2011, including a summary of recent market trends. Mr. Muffick told the Board that domestic managers struggled while international outperformed. We currently have \$2.7 billion in the domestic equity pool. Being overweight in mid and small caps added to performance of the pool as both cap sizes outperformed large caps in the quarter; large cap managers continue to lag their benchmarks. The strategy is to continue to overweight mid caps and small caps and to diversify active management in these areas.

International Equity (MTIP)

Mr. Muffick presented the Montana International Equity Pool Report for the period ending December 31, 2011 and reviewed market trends during the quarter. We currently have \$2 billion in the pool and plan to increase small cap and emerging market allocations.

Public Equity External Manager Watch List

Mr. Muffick reported no changes to the Manager Watch List during the quarter. One manager, Artio Global, which had an international core mandate, was terminated due to poor performance. Mr. Muffick and Mr. Mark Higgins presented information about the managers currently on the Watch List shown below:

**MANAGER WATCH LIST**  
February 2012

Manager	Style Bucket	Reason	\$ Invested (mil)	Inclusion Date
Western Asset	Domestic – LC Enhanced	Performance, Tracking Error	\$151	March 2008
Martin Currie	International – LC Growth	Performance, Risk Controls	\$89	February 2009
Columbus Circle	Domestic – LC Growth	Performance, Process	\$137	May 2011
TimesSquare	Domestic – MC Growth	Performance	\$99	August 2011

Montana International Equity Pool (MTIP) Transition

Mr. Rande Muffick presented a report on the transition of assets within the international equity pool as a result of the termination of Artio Global in January. The overall cost of the transition was \$145,931, or approximately 14 basis points of the market value.

Member Bob Bugni thanked Rande Muffick for his service to the MPERA Board's Employee Investment Advisory Council as BOI's representative. Mr. Muffick has played a key role in reviewing the recommendations of MPERA's consultant and advising their Board.

Prime Brokerage Transition

Mr. Cliff Sheets reported on the transition of prime broker assets from Citigroup to State Street's Enhanced Custody Model. No cost was incurred for the transition.

Manager Evaluation Policy

Mr. Cliff Sheets presented revisions to the Public Markets Manager Evaluation Policy for Board approval. The policy was changed to accommodate fixed income managers.

Member Jack Prothero made a Motion to approve the Public Markets Manager Evaluation Policy; Member Karl Englund seconded the Motion. The Motion was carried 9-0.

Mr. Sheets reported that staff are performing due diligence in order to add an external manager. Information about the manager, including the steps taken to reach the final decision, will be presented to the Board at the meeting following hiring of the manager.

Fixed Income

Mr. Nathan Sax presented the Fixed Income overview and strategy for the Retirement and Trust Fund Bond Pools. Mr. Sax noted that corporate bonds significantly outperformed treasuries and high yield spreads ended the year at 7.02%. There is now some optimism about the US economy and less concern regarding the European sovereign debt crisis.

Mr. Sax presented the Non-Investment Grade Holdings Report. He told the Board we are expecting to recover \$.26 on the dollar from the Lehman Brothers bankruptcy.

Fixed Income External Manager Watch List

Mr. Nathan Sax presented a manager watch list for the first time since the hiring of external managers in Fixed Income began in 2008. The first manager identified as one of concern is Post Advisors, as shown below:

Manager	Strategy	Reason	Amount Invested (\$ millions)	Inclusion Date
Post Advisors	Public High Yield	Performance	\$55 RFBP \$98 TFIP	February, 2012

Mr. Richard Cooley reported on the Short Term Investment Pool, State Fund Insurance and Treasurer's Fund portfolios. Mr. Cooley noted that money market spreads continued to widen into early January 2012 producing a fair amount of yield for the STIP portfolio. Libor rates increased by 20.7 basis points for the quarter but have steadily gone down since the first of the year.

Mr. Cooley presented the State Fund Insurance report for the quarter ended December 31, 2011. Mr. Cooley stated that he and Mr. David Ewer recently had a very productive meeting with State Fund.

**ADJOURNMENT**

There being no further business, Chairman Buchanan adjourned the meeting at 11:18 AM.

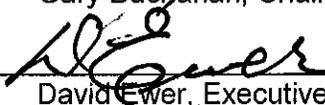
Next Meeting

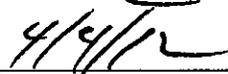
The next regular meeting of the Board will be Tuesday, April 3, 2012 in Helena, Montana.

*Complete copies of all reports presented to the Board are on file with the Board of Investments.*

**BOARD OF INVESTMENTS**

APPROVE:   
Gary Buchanan, Chairman

ATTEST:   
David Ewer, Executive Director

DATE:   
4/4/12