Return to Agenda

Call to Order

REGULAR MEETING OF THE
MONTANA BOARD OF INVESTMENTS
DEPARTMENT OF COMMERCE
2401 Colonial Drive, 3rd Floor
Helena, Montana

April 2, 2013

AGENDA

Tab 1	**CALL TO ORDER – Mark Noennig, Chairman**	**10:00 AM**
	A. Roll Call B. Approval of the February 26-27, 2013 Meeting Minutes – ***Decision*** C. Public Comment – *Public Comment on issues with Board Jurisdiction* D. Department of Commerce Director, Meg O'Leary, Introduction – *Tentative*	
Tab 2	**EXECUTIVE DIRECTOR REPORTS – David Ewer**	**10:20 AM**
	A. Member Requests from Prior Meeting B. Emergency Preparedness C. CEM Benchmarking Study for 2012 D. Legislative Update (comments from our legislative liaisons) E. Board Education F. Web Site	
Tab 3	**ASSET ALLOCATION – Cliff Sheets, CFA and R. V. Kuhns**	**10:30 AM**
LUNCH SERVED		**12:00 PM**
CONTINUATION WITH TAB 3 – ASSET ALLOCATION		**12:30 PM**
Tab 4	**INVESTMENT MANAGER ADDITIONS – Cliff Sheets, CFA, Ethan Hurley and Rande Muffick, CFA**	**1:15 PM**
Tab 5	**POLICY REVIEW, Executive Director and Senior Management**	**1:30 PM**
	A. Staff Memorandum with Recommendations B. List of Policies and Rules C. Specific Policy Issues Raised by Members, if any D. Board Action on Policies **– *Decision***	
BREAK		**2:30 PM**
Tab 6	**CREDIT ENHANCEMENT, MONTANA FACILITY FINANCE AUTHORITY David Ewer and Michelle Barstad, Executive Directors**	**2:45 PM**
Tab 7	**IN-STATE LOAN PROGRAMS – Herb Kulow, CMB**	**3:30 PM**
RECAP OF STAFF TO DO LIST AND ADJOURNMENT		**4:00 PM**

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MONTANA BOARD OF INVESTMENTS
DEPARTMENT OF COMMERCE
2401 Colonial Drive, 3rd Floor
Helena, Montana

MINUTES OF THE MEETING
February 26 - 27, 2013

BOARD MEMBERS PRESENT:

Mark Noennig, Chairman
Kathy Bessette
Gary Buchanan
Bob Bugni
Karl Englund
Quinton Nyman
Jack Prothero
Marilyn Ryan
Jon Satre

LEGISLATIVE LIAISONS:

Senator Ed Buttrey – Absent
Representative Franke Wilmer – Present February 26,
arrived 9:00 AM, February 27, 2013

STAFF PRESENT:

Jason Brent, CFA,
Alternative Investments Analyst
Polly Boutin, Accountant
Geri Burton, Deputy Director
Richard Cooley, CFA, Portfolio Manager,
Fixed Income/STIP
Dana Chapman, Board Secretary
Frank Cornwell, CPA, Deputy
Financial Manager
Roberta Diaz, Accountant
David Ewer, Executive Director
Julie Flynn, Bond Program Officer
Tim House, Investment Operations Chief
Ed Kelly, Alternative Investments Analyst
Herb Kulow, MCMB,
Portfolio Manager, In-State Loan Program
April Madden, Accountant
Gayle Moon, CPA, Financial Manager
Rande Muffick, CFA, Portfolio Manager,
Public Equities
Chris Phillips, CFA, Investment Staff
Jon Putnam, CFA, FRM, Fixed Income
Investment Analyst
Nancy Rivera, Credit Analyst
John Romasko, CFA, CPA, Fixed Income
Investment Analyst
Nathan Sax, CFA, Portfolio Manager,
Fixed Income
Clifford A. Sheets, CFA,
Chief Investment Officer
Steve Strong, Equity Investment Analyst
Louise Welsh, Senior Bond Program Officer
Dan Zarling, CFA, Director of Research

GUESTS:

Becky Gratsinger, RV Kuhns and Associates
Jim Voytko, RV Kuhns and Associates
Mark Higgins, RV Kuhns and Associates
David Senn, Teachers' Retirement System
John Harrington, Legislative Audit Division
Mark Barry, Montana State Fund
Wayne Dykstra, Board Member, Montana State Fund
Rene Silverthorne, Controller, Montana State Fund

CALL TO ORDER

Board Chairman Mark Noennig called the regular meeting of the Board of Investments (Board) to order at 11:40 AM in the Board Room on the third floor at 2401 Colonial Drive, Helena, Montana. As noted above, a quorum of Board Members was present. Senator Ed Buttrey was absent.

> Board Member Jack Prothero made a Motion to approve the Minutes of the November 13 & 14, 2012 Board Meeting; Member Jon Satre seconded the Motion. The Motion was carried 9-0.
>
> Board Member Jack Prothero made a Motion to approve the Minutes of the Board Conference call special meeting on February 12, 2013. Member Jon Satre seconded the Motion. The Motion was carried 9-0.

Chairman Noennig noted the presence of newly appointed Board Members Kathy Bessette and Marilyn Ryan and asked each Board member to give a brief introduction of themselves and their background. Marilyn Ryan is the Board's Teachers' Retirement System (TRS) representative and Kathy Bessette represents agriculture.

Chairman Noennig asked for public comment. There was no public comment.

Chairman Noennig stated Commerce Director Meg O'Leary is unable to attend this meeting, but will attend a future meeting as her schedule permits.

ADMINISTRATIVE BUSINESS

Audit Committee Report

Audit Committee Chair Jon Satre reported on the items discussed at the Committee Meeting held prior to the regular Board Meeting. The Fiscal Year 2012 Financial-Compliance Audit prepared by the Legislative Audit Division is completed. The legislative performance audit is in process. Preparation work is ongoing and onsite work will commence in a month or two. The Committee also discussed emergency preparedness and received an update regarding the Securities and Exchange Commission foreign exchange issue with State Street Bank. Greg Gould from Luxan and Murfitt gave an update on the Pfizer class action lawsuit which MBOI is participating in.

Loan Committee Report

The Loan Committee met prior to the Board meeting. Committee Chair Jack Prothero reported the Committee approved one INTERCAP loan to Flathead Valley Community College in the amount of $2.4 million over a term of 10 years to finance costs for construction of a Nursing and Health Services Building. The Committee also approved one commercial loan in the amount of $1,407,058 to Paulson Enterprises, LLC over a 25 year term for construction of new office and laboratory buildings.

Human Resource Committee Report

The Human Resource Committee also met prior to the Board meeting. Committee Chair Karl Englund reported the Committee agreed to defer the review of staff salaries to a later date.

EXECUTIVE DIRECTOR'S REPORT

Overall Comments

Executive Director Ewer advised the Board's Fiscal Year 2012 Annual Report and financial statements were delivered to the Governor's office by calendar year end as required by law. The report and financial statements are posted on the web site.

The 2013 quarterly cost report is included in the Board packet and shows the most recent quarter and previous quarter costs.

Mr. Ewer also presented the Fiscal Year 2013 Work Plan which covers the next 24 months and systematically reviews issues likely to come before the Board during that time period. The Work Plan has a breakdown of items to be covered at each meeting including special agenda items. There are currently six Board meetings per calendar year.

Mr. Ewer advised staff is planning client outreach at the August meeting and will invite key state program officers who have significant trust or other monies invested with the Board.

Mr. Ewer noted the Board's Code of Ethics, which is reviewed annually, is included in the Board packet. As stated in the Governance Manual, the Code of Ethics is to be signed annually by staff and Board members. Staff has all signed for 2013.

The most significant Board related issue before the 2013 Legislature is the Board's budget which went to the Governor without changes. Pensions continue to be a major issue. Staff made a presentation before the select committee on state pensions, which meets regularly. Additional information requests have been received from legislative staff.

Member Karl Englund inquired where we are in the budget process. Executive Director Ewer noted there is still a long way to go until second reading. The Commerce (Board) budget did make it out of committee intact.

Representative Franke Wilmer advised the transmittal deadline for appropriation bills is March 28th. The 90 day session is scheduled to conclude April 27th but there is discussion about wrapping up sooner. The pay plan and retirement bills will be in the mix until the very end of the session.

Member Jack Prothero asked if there were any surprises this time in the legislature. Representative Wilmer stated that having served in two closely divided legislative sessions, the climate is more civil this session and not as many extreme bills have been introduced.

Executive Director Ewer encouraged Board Members to take advantage of training opportunities as they become available. He will continue to pass on relative training information as he receives it.

MONTANA LOAN PROGRAMS

Commercial and Residential Portfolio Reports

Mr. Herb Kulow reported that past due numbers for both the commercial and residential loan portfolios look good and are much better than the national averages.

Member Englund asked for an update on the Veterans' Home Loan Program. Mr. Kulow noted the bill proposed by Senator Cliff Larsen to allocate an additional $15 million to the program is moving along in the legislature. Loan applications continue to come in to the Board of Housing which manages the program. The 1.55% average yield to the Coal Tax Trust goes into the general fund and to date there have been no delinquencies.

Bond Program Reports

Activity Report

Ms. Louise Welsh presented the quarterly Activity Summary report and noted there were a couple of spikes due to larger loans. The new bond rate for the year has been set at 22 basis points.

Member England inquired why there seems to be a lack of applications from the eastern part of the state.

Ms. Welsh noted there are pending applications for Sidney, Savage Schools and Ritchey. Ms. Welsh added staff will be conducting a program informational workshop in Glendive this spring and will coordinate project site visits on the same trip.

Staff approved loans are listed below:

Borrower:	Park County
Purpose:	Construct a Search and Rescue Operations Building
Staff Approval Date:	October 3, 2012
Board Loan Amount:	$700,000
Other Funding Sources:	$0
Total Project Cost:	$700,000
Term:	15 Years

Borrower:	City of Forsyth
Purpose:	Municipal pool improvements
Staff Approval Date:	October 5, 2012
Board Loan Amount:	$137,800
Other Funding Sources:	$0
Total Project Cost:	$137,800
Term:	10 Years

Borrower:	Corvallis Rural Fire District
Purpose:	Refinance a fire engine
Staff Approval Date	November 7, 2012
Board Loan Amount:	$120,360
Other Funding Sources:	$0
Total Project Cost:	$120,360
Term:	4 years

Borrower:	Corvallis Rural Fire District
Purpose:	Refinance two fire stations
Staff Approval Date	November 7, 2012
Board Loan Amount:	$627,648
Other Funding Sources:	$0
Total Project Cost:	$627,648
Term:	10 years

Borrower:	Florence Rural Fire District
Purpose:	Construct a satellite fire station
Staff Approval Date	November 8, 2012
Board Loan Amount:	$300,000
Other Funding Sources:	$0
Total Project Cost:	$300,000
Term:	15 years

Borrower:	Town of Geraldine
Purpose:	Street and sidewalk project
Staff Approval Date	November 14, 2012
Board Loan Amount:	$30,000
Other Funding Sources:	$39,812
Total Project Cost:	$69,812
Term:	10 years

Borrower:	Town of Big Sandy
Purpose:	Wastewater sludge removal
Staff Approval Date	November 19, 2012
Board Loan Amount:	$71,000
Other Funding Sources:	$0
Total Project Cost:	$71,000
Term:	6 years

Borrower:	Reed Point School District
Purpose:	Maintenance vehicle and equipment
Staff Approval Date	November 26, 2012
Board Loan Amount:	$20,000
Other Funding Sources:	$0
Total Project Cost:	$20,000
Term:	3 years
Borrower:	Choteau County Hospital District dba Missouri River Medical Center (Fort Benton)
Purpose:	Replace roof and purchase equipment/software
Staff Approval Date	November 29, 2012
Board Loan Amount:	$ 107,178
Other Funding Sources:	$ 22,500
Total Project Cost:	$ 129,678
Term:	4 years

Borrower:	Bainville Public School District #64D
Purpose:	Remodel school building
Staff Approval Date	December 11, 2012
Board Loan Amount:	$ 800,000
Other Funding Sources:	$ 100,000
Total Project Cost:	$ 900,000
Term:	5 years

Borrower:	Darby Rural Fire District
Purpose:	Purchase a new fire engine
Staff Approval Date	December 13, 2012
Board Loan Amount:	$ 88,481
Other Funding Sources:	$ 78,099
Total Project Cost:	$ 166,580
Term:	10 years

Borrower:	City of Kalispell
Purpose:	Purchase several pieces of equipment and vehicles
Staff Approval Date	December 14, 2012
Board Loan Amount:	$375,000
Other Funding Sources:	$0
Total Project Cost:	$375,000
Term:	5 years

Borrower:	Town of Medicine Lake
Purpose:	Preliminary engineering report – wastewater
Staff Approval Date	December 20, 2012
Board Loan Amount:	$40,000
Other Funding Sources:	$0
Total Project Cost:	$40,000
Term:	3 years

Borrower:	Toole County
Purpose:	Digitize County Records
Staff Approval Date	December 26, 2012
Board Loan Amount:	$277,347
Other Funding Sources:	$0
Total Project Cost:	$277,347
Term:	5 years

Borrower:	Toole County
Purpose:	Purchase truck/trailer and two motor graders
Staff Approval Date	December 26, 2012
Board Loan Amount:	$447,156
Other Funding Sources:	$271,000
Total Project Cost:	$718,156
Term:	7 years

Borrower:	Toole County
Purpose:	Repave airport taxiway and construct hangar
Staff Approval Date	December 26, 2012
Board Loan Amount:	$ 145,394
Other Funding Sources:	$ 1,868,543
Total Project Cost:	$ 2,013,937
Term:	10 years

Borrower:	Toole County
Purpose:	Purchase maintenance truck
Staff Approval Date	December 26, 2012
Board Loan Amount:	$18,038
Other Funding Sources:	$0
Total Project Cost:	$18,038
Term:	6 years

MONTANA UNIVERSITY SYSTEM

Borrower:	University of Montana – Missoula
Purpose:	Purchase and install IT equipment
Staff Approval Date	November 20, 2012
Board Loan Amount:	$401,625
Other Funding Sources:	$364,160
Total Project Cost:	$765,785
Term:	3 years

CONSULTANT REPORT

RV Kuhns & Associates

Ms. Becky Gratsinger and Mr. Mark Higgins presented an overview of capital markets and investment performance for the quarter ending December 31, 2012. Ms. Gratsinger began the report by discussing recent economic and capital market developments. Overall, international assets produced strong returns while bonds did not fare as well during the fourth quarter. Real Estate (NCREIF) produced good across the board returns. The debt ceiling issue continues to impact markets and historically low interest rates continue to translate into very low bond returns. Inflation concerns loom on the horizon; however, have not materialized yet. Abundant monetary stimulation by the Fed has continued given the absence of any meaningful rise in inflation thus far.

Ms. Gratsinger reviewed the Annual Asset Class Performance and noted the different class performances comparing 2010 to 2011. For 2012, the best results were realized in the international small cap arena with financials leading the way. The Middle East region was in negative territory, but results were positive everywhere else including emerging markets. Financials accounted for a significant 24-25% of non-US markets and investors are embracing risk in equity and bond markets. Cash returns remain non-existent.

The $8.2 billion retirement plans show a very strong one year net return of 13.2% and realized a better return while taking less investment risk versus the overall peer universe with less volatility when taking all factors into account.

Member Buchanan noted the retirement return versus the benchmark show a negative 180 bp and asked where return was given back.

Mr. Cliff Sheets offered the private equity benchmark of S&P 1500 plus 4% caused the rolled up returns to be lower. Given the private equity pool underperformed its benchmark by almost 20 percent for the one-year period, and an approximate average weight of 13%, this would explain much of the plan underperformance. The custom benchmark for the retirement plans simply reflects the underlying pool benchmarks rolled up to reflect the actual asset allocation. The lag associated with private equity resulted in a very high public return hurdle for the one year period since it ended 9/30/12.

Ms. Gratsinger added equity market updraft and downdraft will both show a lag influence on private equities.

Member Prothero asked for an update on peers in asset allocation.

Ms. Gratsinger remarked that her firm has just updated its asset assumptions and fixed income return expectations have been lowered and the outlook for equities is more positive but volatility will still be a factor, especially if there is a return to fear mode. Equities have recovered a lot and the market is flirting with the 14,000 mark. Europe could still be an issue as emerging markets and other alternatives are getting a second look. Hedge funds have suffered. The lag in private equity valuations is reflected in MBOI's returns whereas some groups estimate returns to compensate for the lag.

Mr. Mark Higgins reviewed the Domestic Equity Pool. The roster of active managers has been reduced in accordance with the recent policy changes. The pool comprises 65% passive equities. T. Rowe Price has been a consistently good large cap core manager; however three analysts recently left the firm all at once. While they continue to have a deep team they will be monitored to alert for any changes. Analytic Investors' strategy, as a quant-based manager has not worked well during the bear market but they have recovered in the last two years. Artisan Partners have outperformed by 312 basis points since inception. Times Square has also done well; they were under close watch previously but they have recovered and are pretty solid. Alliance Bernstein, a small cap growth manager, has not performed well, but it's early yet.

Turning to the International Equity Pool managers, Alliance Bernstein international value has a highly volatile return pattern and it is appropriate to have them on the watch list. Martin Currie made some needed changes and Hansberger has trailed the market for five years, and tends to perform better in an up market.

Mr. Higgins reviewed fixed income manager performance for the quarter ending December 31, 2012, and noted the addition of high yield managers has helped returns. Post Advisors is off the watch list and they are showing a good recovery. Artio was acquired by Aberdeen two weeks ago giving perceptual stability; they liked the bond team.

<u>State Fund – Real Estate Allocation/Investment Policy Change</u>
Mr. Cliff Sheets, Mr. Rich Cooley and Mark Barry, VP, Corporate Support for Montana State Fund presented the proposed policy change for State Fund. Mr. Cooley presented the proposed revised investment policy statement for Board approval. Discussions by staff with State Fund have been ongoing for the past year to consider portfolio diversification options as low interest rates have led to a decrease in book yield of the bond portfolio. Staff is recommending and State Fund has agreed that the addition of core real estate to the fund will help offset the decline in book yield and increase diversification of the fund. The core real estate target will be set by policy at 5% of the total portfolio with a range between 3%-7%.

Mr. Sheets explained that with the erosion of book yield many options were considered including high yield and long term bonds. Core real estate funds encompass retail, commercial office, multi-family and industrial properties. Property income while not contractually mandated should allow for attractive dividend distributions. Additional advantages include mitigation of inflation to some extent and appreciation of the assets value as well as the added diversification. Drawbacks include limited liquidity and susceptibility to economic downturns.

Member Satre asked if real estate is subject to the J curve effect.Mr. Sheets advised investments will be made into existing portfolios, not start-ups or closed end funds which would be affected by the J curve. Real estate is still recovering and demand for core properties remains strong so now is a good time to initiate an investment in real estate. Economic conditions do not suggest any immediate risks that would cause a decline in the real estate market.

Mr. Mark Barry offered that by statute, State Fund must work with MBOI. The hardening of the market in 2000 meant a decrease in the number of policies written as the recession hit businesses. Premiums and investment income account for the only income, both of which have declined. Raising capital is not allowed. Business is restricted to one state, Montana, and insurance must be offered to all businesses in the state. After considering the available options, State Fund is in agreement to add core real estate into the portfolio.

Mr. Sheets requested the Board's approval of staff's recommended changes to the State Fund Investment Policy Statement adding the new asset class of core real estate and approving the asset range.

> Board Member Gary Buchanan made a Motion to approve the revised State Fund Insurance Investment Policy Statement to add core real estate with a target of 5% of the total portfolio and a range of +/-2% or 3%-7%. Member Karl Englund seconded the Motion. The Motion was carried 9-0.

INVESTMENT ACTIVITIES/REPORTS

Retirement System Asset Allocation Report
Mr. Cliff Sheets presented the asset allocation report for the quarter ending December 31, 2012 for the nine pension funds. Positive returns increased valuation nearly $83 million over the quarter. The increase reflected a positive return increase of .8% for international equity compared with a 1% decline for domestic equity, the weakest of all pools for the quarter. Private equity increased 0.2% despite $12 million in sales due to a positive return; fixed income was down slightly 0.2%, due to weaker returns. Real Estate increased 0.3% due to purchases of $29 million into the pool. The monthly withdrawals are averaging $46 million each month which comes from some asset sales, contributions, and asset pool income from fixed income and stock dividends producing negative cash flow overall each month. The average related sales required to meet costs is approximately $5 million per month. The amount of asset liquidation required will likely increase over time.

Comparison to State Street Public Fund Universe
Mr. Sheets presented the State Street Bank asset allocation and performance comparison charts and introduced a new chart using data from the Trust Universe Comparison Service (TUCS). The new chart compares the allocation to the major asset classes and shows the range of exposures to each broken into high, median and low, for funds with total assets over $5 billion. MBOI's public stock allocation is slightly above the median, combining both domestic and international stocks, while fixed income is slightly lower, and both real estate and private equity are above the median. Hedge funds remain at zero compared to other fund holdings with a low near zero to a high at 9.56%, however only about one-fourth of the funds surveyed had an exposure here. The public funds universe performance comparison for funds of $1 billion and above show MBOI in the median return range.

Member Bob Bugni noted the difference in peer comparison fund sizes as R.V. Kuhns utilizes comparisons with funds of $3 billion and above, while the TUCS uses $5 billion and above and the State Street Bank universe uses funds of $1 billion and over.

Mr. Sheets noted the smaller asset size in the State Street performance comparison captures more observations and staff will be exploring more standardized reports in the future.

Fixed Income
Mr. Nathan Sax presented the Fixed Income overview. Interest rates rose moderately in the fourth quarter, although they have been up and back several times over the quarter. GDP for the quarter was down 0.1% due to a decline in defense spending. The issue of the so called fiscal cliff has now moved on to the issue of automatic cuts or sequestration and in May the debt ceiling debate is looming, all considerations for both the internal and externally managed portfolios. Corporate bond spreads have narrowed over the past year and the world economy has calmed. While fixed income returns are expected to continue to fall liquidity needs dictate the need to continue with a 25% allocation.

All fixed income external managers outperformed this quarter and are ranked in the first or second quartile over three years. Post Advisors and Neuberger Berman own no treasuries as they are high yield managers. For 2012 an underweight in US Treasuries and an overweight position in corporate bonds worked in our favor. Together the nearly ¾ internally and ¼ externally managed core bond portfolio has outperformed by 188 basis points over three years and is ranked 6th overall since inception.

Aberdeen has recently purchased Artio Global, a positive move. They have offices in London and Philadelphia and $300 billion in assets.

Fixed Income External Manager Watch List
Mr. Sax reported Post Advisors has been removed from the watch list following a great year. Monitoring will continue but the worst appears to be over.

Member Prothero noted the board materials did not include the report on internally-managed non-investment grade holdings. Mr. Sheets responded that it was removed from the materials at the last meeting but will be available for future meetings.

Member Bugni noted Reams and Artio have the same performance as the internally managed portfolio at significantly higher cost and questioned the value. Given the long term track record of the internal management of fixed income assets he asked if it is prudent to pay higher fees rather than having the internal team managing these assets.

Mr. Sax advised both managers are more specialized and are taking higher risk and do not correlate to each other or the internally managed fixed income. Mr. Sheets added the fixed income diversification concept was introduced in 2008 to provide external resources not available with in house expertise and this reason is still true. Over time, we may outperform these managers, although that was not the case in 2012, net of fees. At some future point the assets may be moved in house, however there is no compelling reason to do so at this time, adding the core plus and high yield manager additions in 2009 added unique capabilities.

Short Term Investment Pool, State Fund Insurance and Treasurer's Fund Report
Mr. Richard Cooley reported spreads are compressed and low rates continue to suppress STIP the yield. Agency exposure continues to diminish and been reduced from 19% to 11% this quarter. Short term rates are still coming down as is the LIBOR rate. Portfolio yield is down 2-3 basis points. This quarter $55 million in corporates and $70 million in Yankee CDs were purchased.

Member Buchanan suggested inviting STIP participants from Yellowstone County and City of Billings to the May Board meeting in Billings. Mr. Cooley suggested including City of Laurel representatives as well.

Mr. Cooley stated there were no changes in the Treasurer's Fund over last quarter.

Mr. Cooley reported the State Fund Insurance portfolio value at quarter end December 31, 2012 is $1.3 billion. The quarter saw lower rates and tighter spreads and fund duration remains slightly shorter than the benchmark this quarter. The portfolio is underweight Treasuries and overweight in agencies, asset backed securities (ABS) and commercial mortgage backed securities (CMBS) versus its index benchmark. The total fixed income portion of the account outperformed by 34 basis points for the fourth quarter and outperformed by 226 basis points over the past year.

Member Satre asked if adding the real estate allocation to State Fund signals future changes in allocation.

Mr. Sheets stated no major changes in allocation are planned at this time although equity levels may be reassessed at a later date. Responding to a question from Member Satre as to how beneficial the addition of real estate would be, Mr. Sheets responded while it will help mitigate the decline, the issue of the ongoing decline in book yield requires a long time to move the portfolio as maturities roll off, unless market yields rise significantly. Projections indicate a drop of 25 basis points per year over the next two years. Mr. Cooley noted the aversion to risk of capital narrows the available options to stem this decline.

Mr. Jim Voytko added that the insurance industry is highly regulated and assets need to be available should they be needed for premium payers if losses are incurred. Additional options such as tiered rates and increased premiums are other alternatives to managing the business.

Montana Domestic Equity Pool (MDEP)
Mr. Rande Muffick reported on the Montana Domestic Equity Pool (MDEP) for the quarter ending December 31, 2012. Stocks have rallied over the past four years and although it's been a bumpy ride, overall the market is recovering well. The S&P 1500 has returned 7.51% over ten years. Generally when public equities do well, pensions do well.

The first stage of the recent restructuring, the increase of large cap stocks into passive index funds has occurred and the second stage of increased diversification to small and midcap stocks is underway. Contract negotiations are in the process with two managers, a small cap growth and a small cap value. Initial funding of $20-$25 million for each manager is expected at the end of March, comparable to Alliance Bernstein last year. In the search for growth/value midcap managers three finalists are in consideration with a decision expected soon. The search for midcap growth managers is challenging and continues. Track records are lacking or styles are too similar to provide the needed complement to the other manager.

Fiscal year returns reflect the first stage of the portfolio changes with closer tracking to the benchmark including some outperformance. The decision to overweight small and midcap stocks by both external managers and internal staff has added value.

Artisan Partners and TimesSquare Capital Management have struggled in the short term, both being out of favor; however, long term returns look good. Alliance Bernstein, hired last spring for small cap growth, has struggled due in part to the timing of the hire. In general, MDEP is improving, up 27 basis points year to date.

Montana International Equity Pool (MTIP)
Mr. Muffick reported on the Montana International Pool (MTIP) for the quarter ending December 31, 2012. The restructuring of MTIP approved by the Board last August is underway. The shift of large cap stocks into a passive index holding and the utilization of active managers for small cap and emerging markets where they are more likely to outperform should result in lower fees and increased performance. The move to large cap passive was completed in October and phase two, searching for small cap managers is underway.

Member Buchanan asked what the costs were to implement the move of assets.

Mr. Muffick stated the final total for BlackRock which handled the transition totaled approximately 8 basis points. The international pool has tracked closer to the benchmark since the changes and both MTIP and MDEP should track closer to the benchmark going forward.

Public Equity External Manager Watch List
Mr. Muffick stated the watch list has dwindled since the termination of several managers. Martin Currie has been removed due to improved performance. Their new portfolio manager has made a difference and turned things around. Alliance Bernstein remains on the list. Their deep value strategy assuming the risk of the distressed companies they invest in has been a struggle; however they do have comeback potential.

PUBLIC EQUITIES MANAGER WATCH LIST
February 2013

Manager	Style Bucket	Reason	$ Invested (mil)	Inclusion Date
Alliance Bernstein	International – LC Value	Performance	$99.5	August 2012

Private Asset Pool Reviews

Montana Private Equity Pool (MPEP)
Mr. Cliff Sheets presented the private equity report for the quarter ended December 31, 2012 as Mr. Ethan Hurley was absent. Mr. Sheets reported there is still significant cash distribution activity which showed a net positive cash flow for the fourth quarter. Two thirds of the exposure is in buy outs and the pool is well diversified by strategy and manager. Geographically 83% of holdings are in North America, the U.S. and Canada. Access to the best international investments is limited. Fund of funds make up 23.7% of the pool and will decline over time as the strategy to invest directly and escape umbrella fees will continue. Cash flows can be erratic and the five year returns still reflect the bear market. Private equity has done well in the last year; reporting lags one quarter.

Member Buchanan asked why Montlake Capital was not included on the watch list.Mr. Sheets stated they had a bad vintage year but are expected to improve, and do not have the kind of problems deserving of watch list inclusion.

Mr. Sheets summarized the one new commitment made since the August Board meeting, outlined in the table below. White Deer Energy comes with a strong GP and they have been quite successful. Their first fund raised $1 billion easily. Our initial commitment was $30 million but we were cut back to $20 million due to fund popularity. There were a lot of returning limited partners. Mr. Hurley learned about the fund while in Arizona and worked on accelerating the process to ensure inclusion of our commitment. The fee structure is typical and the general partners are investing a significant amount of their own cash.

Fund Name	Vintage	Subclass	Sector	Amount	Date
White Deer Energy II, LP	2013	Buyout	Energy	$20M	1/25/13

Montana Real Estate Pool (MTRP)
Mr. Sheets presented the real estate report for the quarter ended December 31, 2012. Capital calls continue to outpace distributions although distributions are picking up slightly. Returns were fairly strong for the quarter as real estate market conditions continue to show signs of improvement. There have been no new real estate commitments since November, although there will be one presented at the next Board meeting. CBRE has a $20 million commitment, although no cash has been called yet.

Partnership Focus List
There were no changes to the MPEP or MTRP Focus lists since the November 2012 Board Meeting.

Responding to a question from Member Prothero asking if real estate markets in general are improving, Mr. Sheets noted for recent commitments invested in the last two years it's too soon to tell. Value added is the main focus now and surprisingly core prices have continued to improve.

ADJOURNED
Chairman Noennig adjourned the Meeting for the day at 5:03 PM.

CALL TO ORDER – Day 2
February 27, 2012

Board Chairman Mark Noennig reconvened the meeting Wednesday, February 27, 2013 at 8:32 AM. Representative Franke Wilmer arrived at 9:00 AM. Chairman Noennig called for public comment; there was no public comment.

Securities Lending

Securities Lending, Mr. Clifford Sheets, CFA and R.V. Kuhns & Associates.
Mr. Cliff Sheets and Mr. Jim Voytko presented a detailed overview of securities lending. Securities lending is a common practice among institutional investors and provides added income on the owned securities by lending them to borrowers who need additional inventory to settle sales. The transfer of the assets to the borrower is protected by collateral in the form of cash or securities equal to 102% of the value for domestic, or 105% of value for international securities. The otherwise idle securities usually generate between 3-5 basis points, squeezing more return out of investments. This relatively small margin can boost overall fund ranking.

Mr. Sheets noted securities lending is not without risks. The borrower can default or the collateral can lose value and require additional cash to cover repayment. Additionally, securities lending can tie up your assets which limits flexibility in making allocation moves. During the financial crisis, the stretch for more yield on cash collateral caused default losses in many securities lending programs, though not at State Street. Highly rated short term securities were held in cash collateral pools to try and realize more return. The sudden market downturn and subsequent downgrade of securities caused maturities to be extended out and they traded at less than par even for non-asset backed holdings.

When cash collateral pools were frozen due to the rush on the part of some asset owners to leave the program, State Street Bank was pressured to separate out less liquid or more troubled securities into separate cash collateral pools and so a liquidity pool and duration pool were set up separately. State Street Bank allowed some clients out of the program and although they made some mistakes handling the crisis, they fared better than most. MBOI did not leave the program and consequently didn’t suffer any realized losses. Mr. Sheets noted our exposure to the duration component of the cash collateral pools is limited and relative exposure has decreased. Securities lending has become more closely monitored over the past three and a half years and now includes an annual review as part of the work plan.

Member Prothero asked how State Street Bank has performed in general and regarding security lending in particular.

Mr. Sheets stated having State Street Bank as our agent was beneficial during the market crisis. While they had some problems, they did a better job investing the collateral pools. Mr. Voytko noted the actions to split the collateral pools were reasonable given the circumstances, and added that by not leaving the program and forcing a loss on unrealized losses, most assets regained value. Over time there is a small possibility of loss but any loss will be offset by earnings.

Mr. Voytko presented the financial review of securities lending. Earnings were under $1 million in 2006 increasing to a peak of $12 million in 2008. As demand has diminished earnings have decreased but remain substantially higher than 2006 levels. Income of $2 million translates into an additional 3 basis points.

Mr. Sheets explained that through the custodial program with State Street Bank, we agree to lend until such time as the decision is made to no longer participate. We can direct that certain funds be excluded from security lending and also have the ability to set the quality standards of collateral or limit amounts or types of collateral used.

Member Karl Englund inquired the advantages of using a custodial bank vs. an outside agent.

Mr. Voytko noted there are advantages to having the custodian handle it, additionally those services are often bundled with other services. He added State Street Bank handled the financial crisis better than most.

Member Jon Satre asked if the recent changes in asset allocation of large cap investments to more passive holdings would affect the ability to participate in security lending.

Mr. Sheets explained that theoretically the move to more passive holdings should reduce security lending; however, most large caps are not in high demand, rather small and mid cap stocks have a higher demand. Over time the switch to passive holdings will restrict securities lending but the impact will be limited. Mr. Sheets added participating in securities lending involves minimum risk when you consider the big picture of other risks. Next year when the custodial bank search is conducted securities lending will be a consideration which will be addressed at the time of the search.

Benchmarks

Benchmarks, R.V. Kuhns & Associates, Inc.
Mr. Jim Voytko presented the benchmarking overview. The report was brought about by Board request. He relayed the question of how do you measure performance as truck metaphor. What do you need it for? What are you measuring? What are its costs, speed, load bearing ability, safety considerations, and how does it compare to others? A benchmark requires the consideration of all elements to give a complete portfolio performance picture. Mr. Mark Higgins explained the criteria for benchmark measurement follows the CFA Criteria for an Effective Benchmark:

1. Specified in advance
2. Appropriate
3. Measurable, you have to be able to determine
4. Unambiguous, you need to know the content
5. Reflective of the current available investment options
6. Accountable
7. Investable

An example of a benchmark which meets the above criteria is the S&P 500 Index. The benchmark contains holdings of common stock in large and mid-cap companies that covers about 75% of the U.S. public equities.

Mr. Higgins continued the current actuarial rate is 7.75%. Measurements are made against standardized market indices, peer ranking where Montana is measured against the universe of funds greater than $3 billion, comparisons to the target allocation index as well as the actual fund allocation are all measured. Periodic cost comparisons versus the peer universe are also conducted to determine if expenses are in line with the actual value received for those fees.

Mr. Voytko noted the Montana custom benchmark has changed over time, so performance is measured by the previous benchmarks. He reviewed the factors of controllability which staff and Board are able to use to affect outcome of performance. The areas which are most controllable are strategic asset allocation, maintaining sufficient diversity to attain an optimal risk/return ratio, manager selection and the corresponding investment costs of return versus value.

Mr. Voytko concluded tactical asset allocation where MBOI could establish a target allocation and compare the actual allocation index versus target allocation index to gauge whether deviations from target had a positive or negative impact is not currently used. Of the current performance evaluation measurements, this is the only area where a potential adjustment could be made. However, selling securities to raise cash or how much high yield to have are tactical to some extent. Many funds have a policy portfolio model rather than utilizing ranges for each asset. There will be an agenda item discussing asset allocation in more detail at the April 2, 2013 Board meeting. Asset ranges will be included in the discussion.

Executive Director David Ewer noted the current practice utilized for asset allocation is the use of ranges for each asset class. When using a policy portfolio model, a rise in assets necessitates a stronger rebalance factor. When the market experiences an updraft or downdraft ranges allow for more flexibility rather than an immediate need to rebalance. Staff would be restricted with such a narrow policy demanding frequent rebalancing.

Member Prothero asked if there is a concern about the wideness of asset allocation ranges.

Mr. Voytko stated the ranges were implemented years ago and nothing jumps out as being too wide or narrow.

Mr. Cliff Sheets added there have been no issues with the range width as the practice has been to remain near the midpoint of the total equity range. In 2006 staff considered becoming more similar to the global equity market and potentially increasing international and decreasing domestic stocks and therefore ranges were kept wide to allow for flexibility to go more globally without having to revise the asset allocation policy. In June 2012 the wide range of the international portfolio allowed flexibility as the portfolio came close to the low end of the range when markets declined.

Mr. Higgins explained the comparison to peer groups is not a perfect proxy, but does offer value. The BNY Mellon data base is for a peer group greater than $3 billion and has improved in quality. The comparison to “all public funds” varies due to late reporting by some funds and some are not included if the data is suspect before compiling the data. The drawback is that although fund size is comparable, the variations in asset allocation and the differences in funded status of the funds vary the data. Mr. Voytko added the only true comparison would be a mirror image fund; however, even a fund the same size is not necessarily a good criterion as risk tolerance and cash flow issues could be quite varied. Managers and asset allocation and fund operations are all areas where measurement is valid.

Mr. Sheets added peer benchmarking has its flaws as we do not know the plans asset allocation, some are restricted to fixed income. The peer universe is not transparent, although CEM does look at the different asset allocation mixes. Utilizing the State Street Bank peer universe gives additional context. Another factor is the one quarter lag of private equity which can make a significant difference. Any one year has a lot of volatility with multiple dimensions to measure, so all areas need to be looked at.

Mr. Voytko added the quarter to date will change the most, but the one, three and five year returns have a smoothing effect.

Executive Director Ewer noted performance for annualized ten year returns shows a positive relative return of 11 basis points. The Board has implemented important asset allocation changes focusing on the long term which is vital.

Mr. Higgins stated composite indices are best to measure traditional asset classes of equity and fixed income. The equity composite is valuable to measure manager performance by comparing to broad market indices and helped to weed out underperforming managers. The fixed income composite measures internal staff performance of the internally managed portfolios for security selection and style tilts. Private equity varies widely and is the most challenging to find a benchmark for. Private equity is illiquid and generally a 3-5% premium is used; MBOI uses 4%, which is high, but average. The short term horizon is fairly meaningless and it takes five, to seven, to ten years to account for the reporting lag. The private equity S&P 1500 plus 4% which is used is not an investible benchmark and therefore doesn't meet the threshold for benchmark criteria, but over ten years is useful.

Mr. Higgins continued all managers have their own benchmarks which we hold them accountable to. Mr. Voytko added underperformance may or may not be the symptom of a larger problem and needs to be looked at in depth. Sometimes managers pick an inappropriate benchmark, and even high performers will miss the mark some years.

Member Bugni asked if there is a trend of other funds moving assets to passive holdings and putting more focus on costs.

Mr. Voytko affirmed that seems to be a trend for public funds although the reasoning is not clear. Alternatives are also creeping up, perhaps looking for higher returns or to lower exposure to the market. The markets are driven by central bank action in pricing risk assets.

Mr. Higgins explained the actual allocation index for the Public Employees' Retirement measures all manager benchmarks and rolls up to the weighted average of our asset allocation so the manager effectiveness can be measured. For 2011 cost comparisons, MBOI has slightly lower than average costs. In conclusion, MBOI has a good framework for performance evaluation which is appropriately interpreted.

Wrap Up – To Do
Executive Director Ewer reviewed items to be completed for the next Board meeting. The Below Investment Grade worksheet will be included in future Board packets. Staff will contact Yellowstone County and invite local government officials as well as local bankers to the May 29-30, 2013 Board meeting to be held in Billings.

Public Comment
Chairman Noennig called for public comment on Board issues. There was no public comment.

ADJOURNMENT

There being no further business, the meeting was adjourned at 11:05 AM.

Next Meeting
The next regular meeting of the Board is a one day meeting and will be Tuesday, April 2, 2013 in Helena, Montana.

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

BOARD OF INVESTMENTS

APPROVE: ______________________________
Mark Noennig, Chairman

ATTEST: ______________________________
David Ewer, Executive Director

DATE: ______________________________

MBOI:drc
3/25/13

Return to Agenda

Executive Director Reports

MEMORANDUM

Montana Board of Investments

Department of Commerce

2401 Colonial Drive, 3rd Floor

Helena, MT 59601 (406) 444-0001

To: Members of the Board

From: David Ewer, Executive Director

Date: April 2, 2013

Subject: Executive Director Reports

Member Requests from Prior Meeting

Member Prothero requested that staff resume submitting the 'below investment grade' report on fixed income securities held by the Board. This report will now be included in the Board's packet.

Member Buchanan requested that staff contact Yellowstone County finance officials to provide an update regarding the Board's new Short Term Investment Pool (STIP) reserve policy. The Executive Director contacted Scott Turner, Yellowstone County Finance Director, and spoke at some length about STIP. The Board's ability to finance special improvement loans through INTERCAP was also discussed.

Emergency Preparedness and Additional Security Measures

Staff has recently re-checked our ability to continue cash-flow operations in the event our building is unexpectedly unavailable. Computer back-up systems and our off-site operation center have been reaffirmed as ready. The staff emergency call-down list has been updated and distributed.

We are in the middle planning stage of converting the Board's main building from a key-based entry system to a key-less one, which is already in place in most state buildings in Helena. This conversion will enhance our ability to monitor and control entry to the building.

CEM Benchmarking Study for 2012

We are in the beginning stage of submitting detailed cost, performance, and other information to CEM Benchmarking. CEM has a large client and data base making it possible to make specific comparisons to the Board's peers regarding pension assets, controlling for many variables. The final report will be presented to the Board at its August meeting.

Legislative Update (including comments from our Legislative Liaisons)

Staff will update the Board at the meeting and Sen. Buttrey and Rep. Wilmer will be invited to make comments.

Board Education

IFE, the Institute for Financial Education, sponsors an annual conference, "Market Makers", that is targeted to pension sponsors. Board members have found it instructional in the past. Staff emailed information about this conference, which will take place June 26-28th in Dana Point, California (about 50 miles south of Los Angeles). Currently, the conference agenda has not been posted, but is likely to be similar to last year's, (also sent previously to members). Please let staff know if you have an interest in attending. We can send up to three participants; staff suggests sending up to two Board members and one staff if there is Board member interest.

The Board's Web Site

The Board's web site is found at: http://www.investmentmt.com/default.mcpx. It provides web access to a large amount of Board information in a manner that is, one hopes, user friendly. Staff strives to keep it current. It would be very helpful for Board members to browse it and give us feedback on any aspect of our site. We have had no public comments regarding our site.

Return to Agenda

Investment Consultant

RVKuhns & ASSOCIATES, INC.

Asset Allocation Discussion

Montana Board of Investments

April 2, 2013

Mark Higgins, CFA

James Voytko

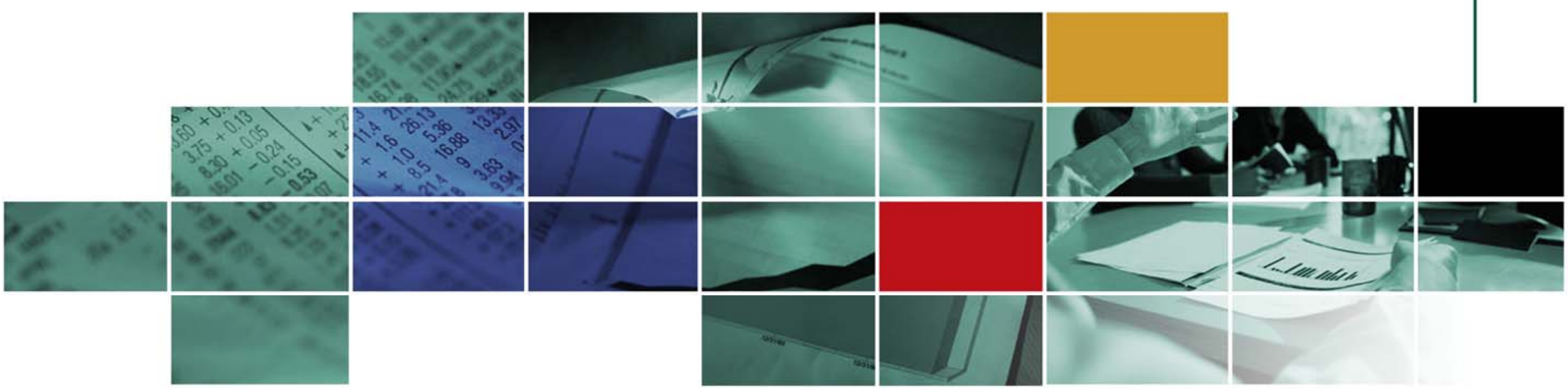


Table of Contents

What is Risk?

Risk is the Probability of Incurring a Permanent Impairment of Capital

Key Concepts

- **Investors expect to be compensated with higher returns in exchange for taking greater amounts of risk.**
- **While admittedly imperfect, risk metrics seek to describe investment attributes that may raise or lower the probability of capital impairment. Common descriptions of risk include:**

Volatility	Describes the expected variation in asset values over time.
Equity Beta	Measures embedded equity risk (i.e., the extent to which asset values move in sync with overall equity markets).
Liquidity	Measures the extent to which assets can be bought or sold (and the required pricing concessions to execute such transactions) in various market conditions.
Valuation	Measures the relative attractiveness of asset values based on historical parameters and future projections.
Headline Risk	Chance that an unexpected loss event could cause reputational damage.

Risk, Return, and Mean Variance Optimization (MVO)

- Introduced by Nobel Laureate, Harry Markowitz in 1952.
- MVO uses return VOLATILITY as the primary proxy for investment risk.
- Using inputs of expected return, volatility, and correlation for various asset classes, MVO enables investors to identify combinations of asset class allocations that maximize portfolio return for a given level of risk.
- By incorporating multiple assets with less than perfect correlation, investors can increase the expected long-term returns of the portfolio.

Why Does Volatility Matter?

Key Concepts

- Average returns are not equivalent to compound returns (i.e., geometric return) in the presence of return volatility.
- Difference between arithmetic and compound return stems primarily from the asymmetrical impact of negative returns.

Figure 1: Sample Return Stream and Resulting Returns

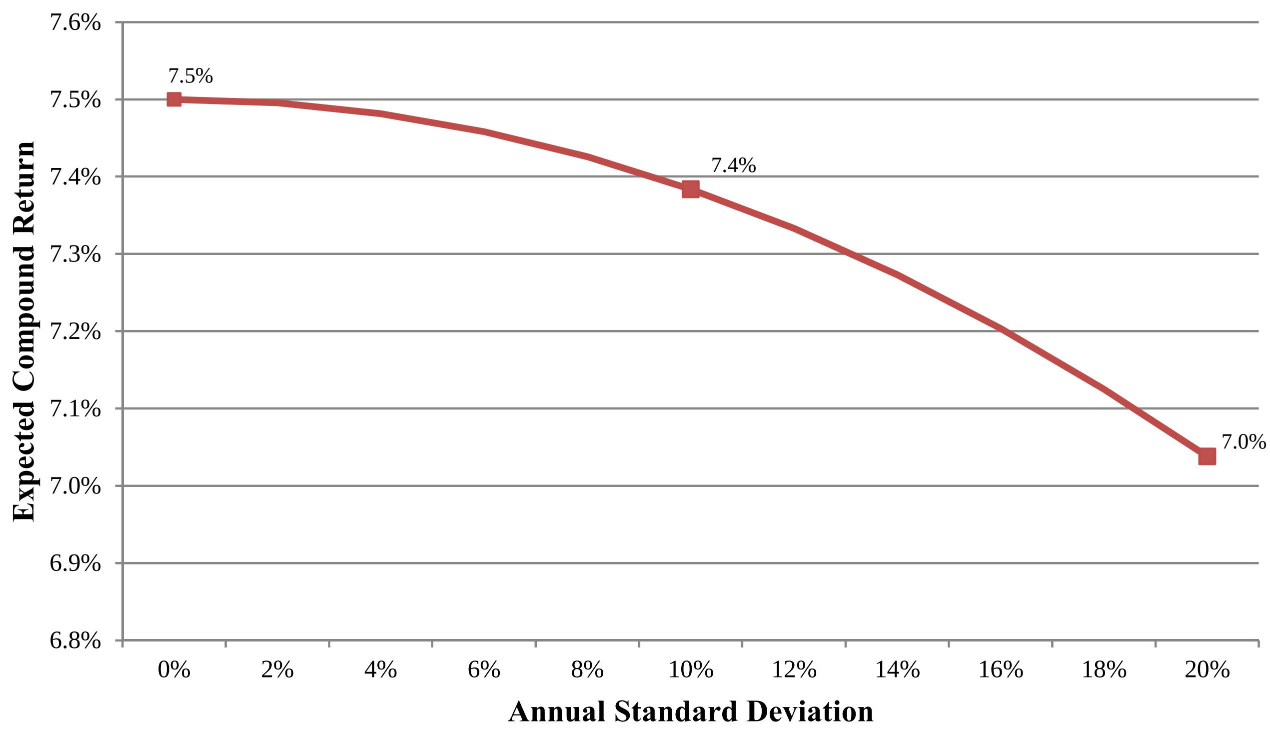
Year	Beginning Value	Return	Ending Value
Year 1	$100.00	15%	$115.00
Year 2	$115.00	(10%)	$103.50
Year 3	$103.50	(25%)	$77.63
Year 4	$77.63	20%	$93.15

Average Return	**= 0%**
Actual Loss	**= ($6.85)**
Effective Annualized Return	**= (1.76%)**

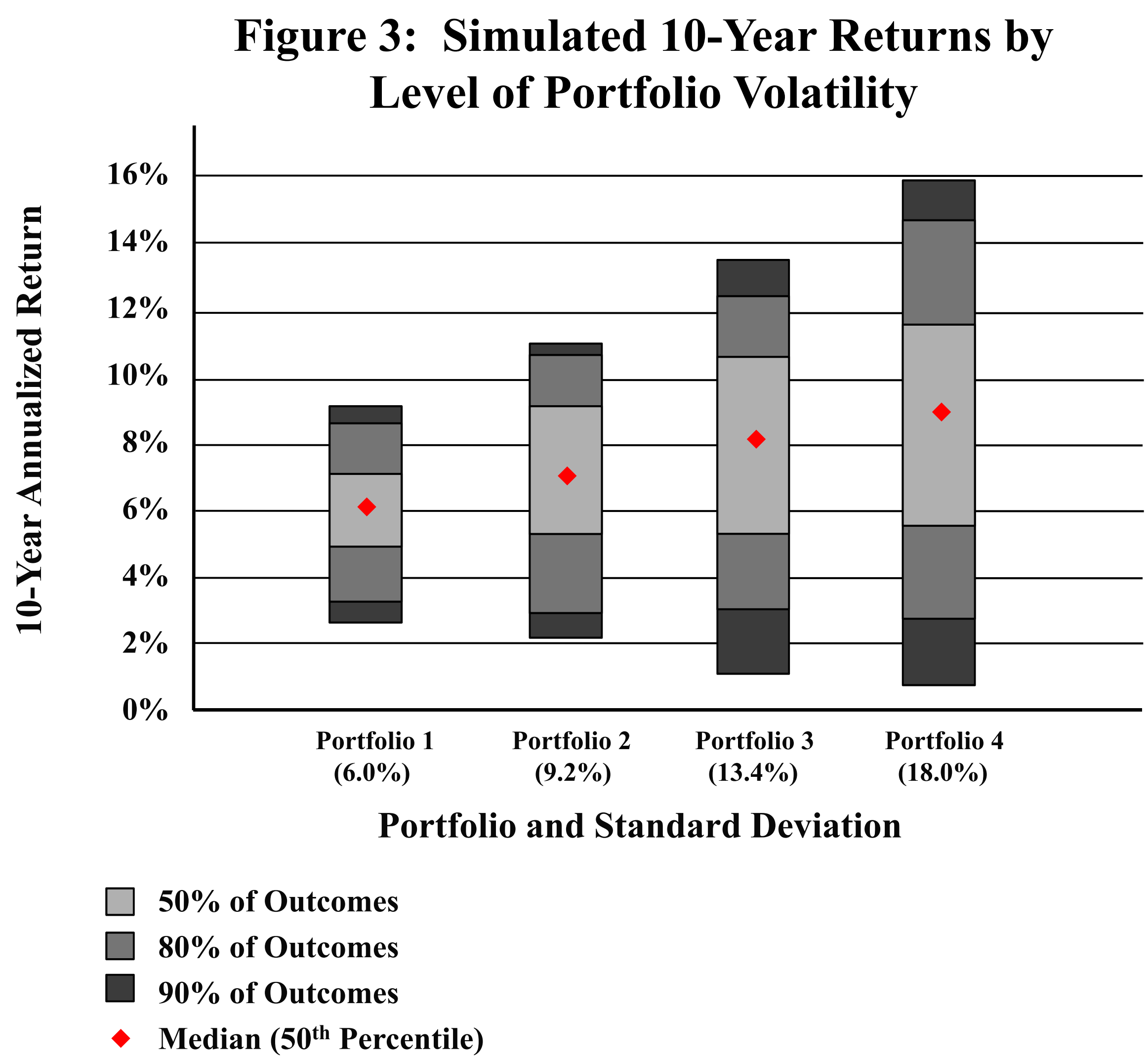
RVKuhns & ASSOCIATES, INC.

Volatility Reduces Expected Compound Returns

Figure 2: Expected Long-Term Compound Return by Level of Volatility



Volatility Also Widens the Distribution of Returns



How Do Asset Class Correlations Impact Returns?

Highlights

- Correlations of less than 1.0 enable investors to reduce portfolio risk without sacrificing return.
- Figure 4 illustrates a risk reduction of approximately 2.56%, which is generated by a two-asset portfolio with a 0.10 correlation.

Figure 4: Risk/Return Plot

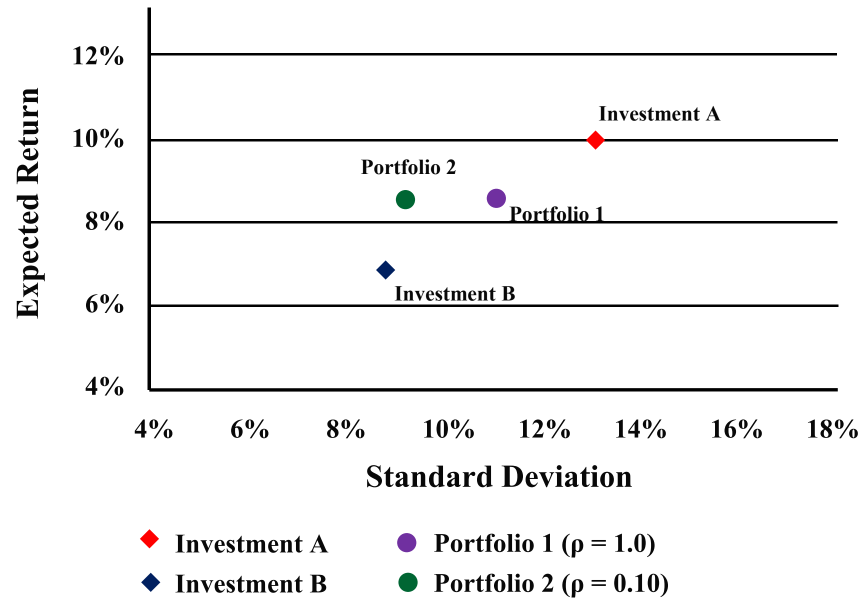


Figure 5: Investment Risk/Return Attributes

Metric	Investment A	Investment B
Return	10.00%	7.00%
Standard Deviation	13.20%	8.80%
Portfolio Weight	56%	44%

Figure 6: Portfolio Risk/Return Attributes

Metric	Portfolio 1	Portfolio 2
Correlation ($\rho_{A,B}$)	1.00	0.10
Return	8.68%	8.68%
Standard Deviation	11.26%	8.70%

MVO Shortcomings

1. Views volatility as the sole proxy for risk
2. Simplified assumption of risk/return trade-off fails to capture how real world investors weight gains versus losses
3. Ignores non-normal attributes of return distributions, and assumes returns are symmetrical
4. Treats correlation as a constant rather than a variable
5. Shows high sensitivity to small changes to input values
6. Unconstrained output yields highly concentrated portfolios rather than intended diversification
7. Ignores liquidity risks and corresponding rebalancing constraints

Importance of Asset Allocation

Asset Allocation is the Primary Driver of Portfolio Returns

- Multiple studies conclude that asset allocation is the most important determinant of total fund performance in the long run.

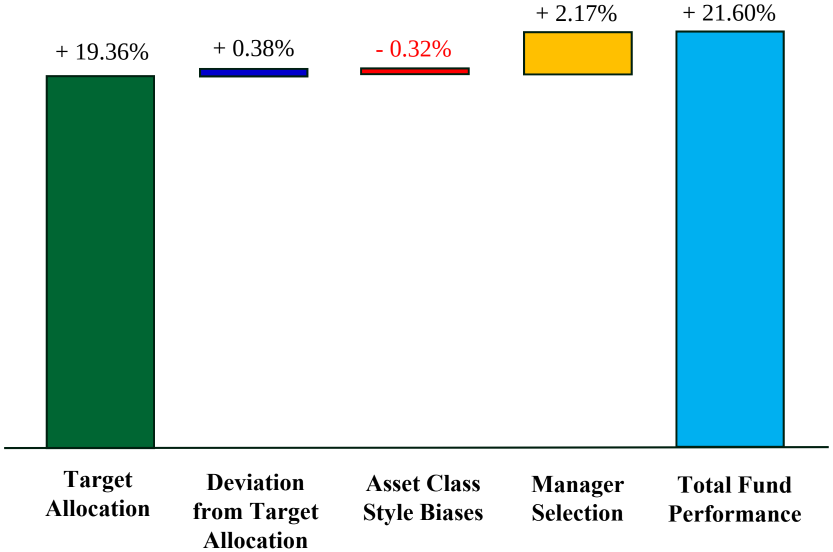
- Studies estimate that 90% of the volatility in annual fund returns is attributable to asset allocation (as opposed to individual manager selection).

- Manager selection, while potentially valuable, cannot compensate an investor for a poorly diversified or inappropriately allocated portfolio.

Source: Ibbotson, Roger G. and Paul D. Kaplan, 2000. "Does Asset Allocation Policy Explain 40%, 90%, or 100% of Performance?". Financial Analysts Journal. January/February 2000, Vol.56, No.1, pp.26-33.

Theory is Confirmed in Practice

Figure 7: Total Portfolio Return Attribution
(July 1, 2010 – June 30, 2011)



Highlights

- Each quarter, RVK completes an analysis of total portfolio return attribution for an endowment with ~$400 million in assets.
- Analysis decomposes return into:
  - Target Allocation (i.e., return of underlying benchmarks)
  - Deviation from Target Allocation
  - Style biases within each asset class (e.g., small cap U.S. equity overweight)
  - Manager selection (i.e., excess return)
- For the one-year period of analysis, 90% of portfolio performance is determined by the portfolio asset allocation.

Summary of Insights on Risk, MVO & Asset Allocation

- **Risk is best defined as the probability of suffering permanent capital impairment (i.e., losses that cannot be reversed with reference to target returns).**

- **Asset allocation is the most critical driver of long-term returns and return volatility (a key metric of risk).**

- **While admittedly imperfect, MVO is a powerful tool that can help the Board create a portfolio that is well-diversified and optimizes the expected risk/return trade-off.**

- **The Board has several additional tools available to manage other forms of risk**
  1. **Valuation Risk—**Measured tactical allocation provides flexibility to alter allocations to asset classes during periods of misvaluation.
  2. **Liquidity Risk—**Private equity and real estate pacing tools help maintain desired exposure to illiquid asset classes.
  3. **Manager Risk**—Monitoring by staff and third-party consultant reduces risk of and ensures timely response to manager underperformance.

Asset Allocation Review

Key Decisions

- Are the allowable asset classes acceptable?
  - Are there asset classes, such as hedge funds, that should be added?
  - Are there asset classes that should no longer be allowed?
- Are there recommended adjustments to the allowable asset class ranges?
- Should MBOI establish a specific target asset allocation?

RVK Capital Market Assumptions

Figure 8: Historical Asset Allocation Assumptions

(2011-2013)

Asset Class	2011 Return (Arithmetic)	2011 Standard Deviation	2011 Return (Compound)	2012 Return (Arithmetic)	2012 Standard Deviation	2012 Return (Compound)	2013 Return (Arithmetic)	2013 Standard Deviation	2013 Return (Compound)
Large/Mid Cap US Equity	8.00%	17.75%	6.57%	7.75%	17.75%	6.32%	7.75%	17.75%	6.32%
Small Cap US Equity	8.75%	21.75%	6.64%	8.50%	21.25%	6.48%	8.50%	21.25%	6.48%
Broad US Equity	8.15%	18.10%	6.67%	7.90%	17.95%	6.44%	7.90%	17.95%	6.44%
Dev'd Large/Mid Cap Int'l Equity	8.00%	18.75%	6.41%	8.00%	19.00%	6.37%	8.00%	19.00%	6.37%
Dev'd Small Cap Int'l Equity	8.75%	22.75%	6.45%	8.75%	23.00%	6.40%	8.75%	23.00%	6.40%
Emerging Markets Equity	10.50%	28.50%	7.00%	10.50%	29.00%	6.88%	10.50%	29.00%	6.88%
Broad International Equity	8.65%	20.10%	6.84%	8.65%	20.80%	6.71%	8.65%	20.80%	6.71%
Intermediate Duration Fixed Income	4.50%	5.50%	4.36%	4.25%	5.75%	4.09%	3.50%	5.75%	3.34%
Non-US Dev'd Sov'n Fixed UH	4.25%	9.75%	3.80%	4.00%	10.00%	3.52%	3.25%	10.25%	2.74%
High Yield Fixed Income	6.75%	14.50%	5.78%	7.25%	15.00%	6.22%	6.25%	15.00%	5.21%
Core Real Estate	7.00%	12.50%	6.28%	7.00%	12.50%	6.28%	7.00%	12.50%	6.28%
Non-Core Real Estate	10.00%	21.50%	7.96%	10.00%	22.50%	7.77%	10.00%	22.50%	7.77%
Private Equity	12.25%	30.25%	8.38%	11.75%	30.25%	7.87%	11.75%	30.25%	7.87%
Timber	8.25%	14.50%	7.29%	8.00%	14.50%	7.04%	7.75%	14.50%	6.79%
Cash Equivalents	2.25%	3.00%	2.21%	2.25%	3.00%	2.21%	2.25%	3.00%	2.21%
US Inflation	2.50%	3.00%	2.46%	2.50%	3.00%	2.46%	2.50%	3.00%	2.46%

RVK Capital Market Assumptions

Figure 9: Correlation Matrix
(2013)

	Large/Mid Cap US Equity	Small Cap US Equity	Broad US Equity	Dev'd Large/Mid Int'l Equity	Dev'd Small Int'l Equity	Emerging Market Equity	Broad International Equity	Int. Duration Fixed Income	Non-US Dev'd Sov'n Fixed UH	High Yield Fixed Income	Core Real Estate	Non-Core Real Estate	Private Equity	Timber	Cash Equivalents
Large/Mid Cap US Equity	1.00	0.85	0.99	0.84	0.77	0.75	0.83	0.21	0.07	0.60	0.27	0.24	0.70	0.05	0.01
Small Cap US Equity	0.85	1.00	0.89	0.77	0.76	0.74	0.79	0.11	0.00	0.62	0.21	0.16	0.69	0.06	-0.02
Broad US Equity	0.99	0.89	1.00	0.85	0.79	0.77	0.85	0.20	0.06	0.62	0.28	0.23	0.72	0.05	0.00
Dev'd Large/Mid Int'l Equity	0.84	0.77	0.85	1.00	0.92	0.82	0.99	0.01	0.33	0.65	0.36	0.24	0.70	0.01	-0.08
Dev'd Small Int'l Equity	0.77	0.76	0.79	0.92	1.00	0.86	0.94	0.07	0.36	0.70	0.38	0.25	0.66	0.05	-0.15
Emerging Markets Equity	0.75	0.74	0.77	0.82	0.86	1.00	0.89	-0.02	0.16	0.65	0.26	0.16	0.63	0.05	-0.15
Broad International Equity	0.83	0.79	0.85	0.99	0.94	0.89	1.00	0.00	0.31	0.68	0.34	0.23	0.71	0.02	-0.11
Int. Duration Fixed Income	0.21	0.11	0.20	0.01	0.07	-0.02	0.00	1.00	0.43	0.28	-0.04	-0.03	-0.18	-0.05	0.24
Non-US Dev'd Sov'n Fixed UH	0.07	0.00	0.06	0.33	0.36	0.16	0.31	0.43	1.00	0.09	0.01	-0.06	-0.03	-0.02	0.11
High Yield Fixed Income	0.60	0.62	0.62	0.65	0.70	0.65	0.68	0.28	0.09	1.00	0.14	0.09	0.48	-0.04	-0.08
Core Real Estate	0.27	0.21	0.28	0.36	0.38	0.26	0.34	-0.04	0.01	0.14	1.00	0.91	0.50	-0.02	0.09
Non-Core Real Estate	0.24	0.16	0.23	0.24	0.25	0.16	0.23	-0.03	-0.06	0.09	0.91	1.00	0.45	-0.05	-0.02
Private Equity	0.70	0.69	0.72	0.70	0.66	0.63	0.71	-0.18	-0.03	0.48	0.50	0.45	1.00	0.07	0.09
Timber	0.05	0.06	0.05	0.01	0.05	0.05	0.02	-0.05	-0.02	-0.04	-0.02	-0.05	0.07	1.00	0.36
Cash Equivalents	0.01	-0.02	0.00	-0.08	-0.15	-0.15	-0.11	0.24	0.11	-0.08	0.09	-0.02	0.09	0.36	1.00

Efficient Portfolios (Current Ranges)

Figure 10: Asset Allocation Analysis–Current Ranges

(Current Allocation as of February 28, 2013)

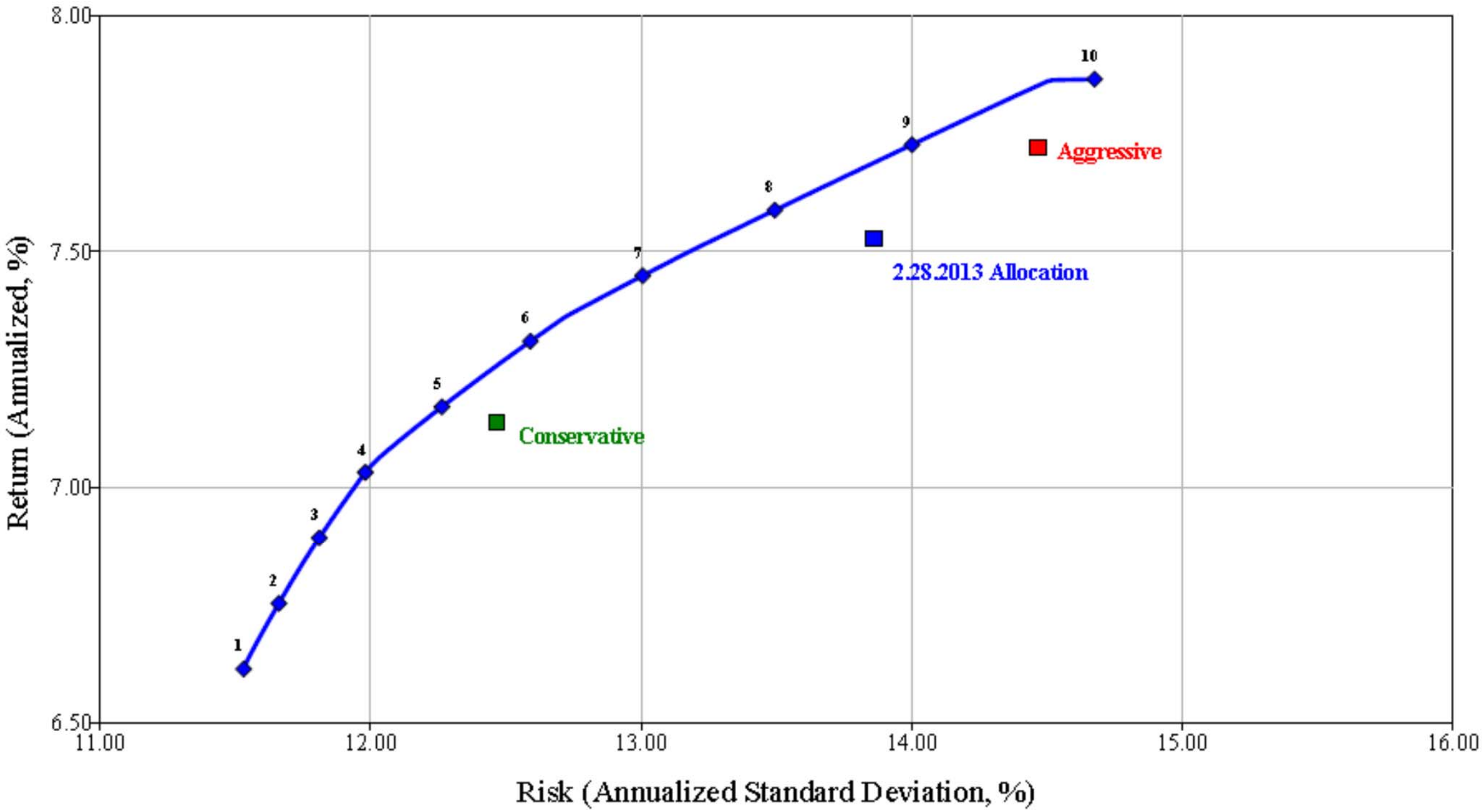
	Min	Max	2.28.2013 Allocation	Conservative	Aggressive
Large/Mid Cap US Equity	24.5	50	35.0	31.5	26.0
Small Cap US Equity	1	5.5	2.5	1.0	4.0
Dev'd Large/Mid Int'l Equity	7	30	11.8	10.5	16.6
Dev'd Small Int'l Equity	1.5	5	1.1	0.8	3.5
Emerging Markets Equity	0	3	4.3	3.7	6.0
Int. Duration Fixed Income	14	32	19.3	28.9	17.0
Non-US Dev'd Sov'n Fixed UH	0	3	0.7	0.7	0.7
High Yield Fixed Income	0	5	3.0	1.0	4.3
Core Real Estate	1.5	6.5	3.4	3.4	3.4
Non-Core Real Estate	1	7.5	4.4	4.4	4.4
Private Equity	9	15	12.5	12.5	12.5
Timber	0	2	0.6	0.6	0.6
Cash Equivalents	1	5	1.4	1.0	1.0
Total			100	100	100
Capital Appreciation			75	65	77
Capital Preservation			21	31	19
Alpha			0	0	0
Inflation			4	4	4
Expected Return			7.53	7.14	7.72
Risk (Standard Deviation)			13.86	12.47	14.47
Return (Compound)			6.65	6.42	6.76
Return/Risk Ratio			0.54	0.57	0.53
RVK Expected Eq Beta (LC US Eq = 1)			0.74	0.67	0.76
RVK Liquidity Metric (T-Bills = 100)			72	72	71

Total Equities have a range from 60% to 70%. Total Domestic Equity has a range from 30% to 50%. Total International Equity has a range from 15% to 30%. Total Fixed Income has a range of 22% to 32%. Total Real Estate has a range of 4% to 10%.

Efficient Frontier – Current Ranges

Figure 11: Portfolio Efficient Frontier—Current Ranges

(Current Allocation as of February 28, 2013)



Efficient Portfolios (Broad Ranges)

Figure 12: Asset Allocation Analysis—Broad Ranges
(Current Allocation as of February 28, 2013)

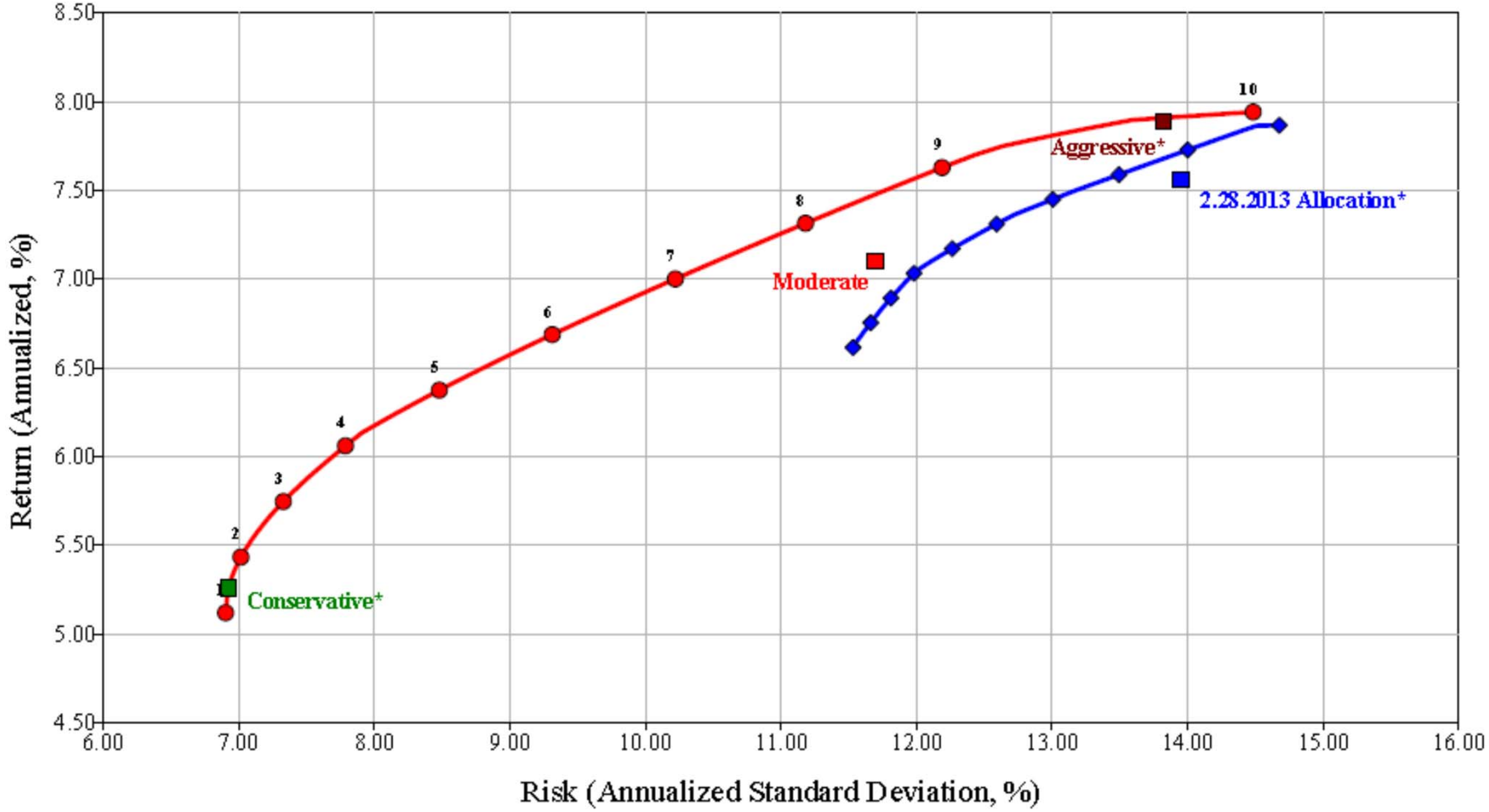
	Min	Max	2.28.2013 Allocation*	Conservative*	Moderate	Aggressive*
Broad US Equity	15	50	37.5	15.0	20.0	17.0
Broad International Equity	15	50	17.2	15.0	20.0	17.0
Int. Duration Fixed Income	25	75	19.3	55.0	20.0	15.0
Non-US Dev'd Sov'n Fixed UH	0	10	0.7	0.0	7.0	5.0
High Yield Fixed Income	0	10	3.0	0.0	5.0	5.0
Core Real Estate	0	10	3.4	5.0	10.0	10.0
Non-Core Real Estate	0	10	4.4	0.0	5.0	10.0
Private Equity	0	20	12.5	0.0	10.0	20.0
Timber	0	5	0.6	5.0	2.0	0.0
Cash Equivalents	1	5	1.4	5.0	1.0	1.0
Total			100	100	100	100
Capital Appreciation			75	30	60	69
Capital Preservation			21	60	28	21
Alpha			0	0	0	0
Inflation			4	10	12	10
Expected Return			7.56	5.26	7.10	7.89
Risk (Standard Deviation)			13.95	6.93	11.70	13.82
Return (Compound)			6.67	5.03	6.47	7.02
Return/Risk Ratio			0.54	0.76	0.61	0.57
RVK Expected Eq Beta (LC US Eq = 1)			0.74	0.35	0.59	0.66
RVK Liquidity Metric (T-Bills = 100)			72	81	64	54

*Used to differentiate different model portfolios with the same name.

Efficient Frontier – Broad Ranges

Figure 13: Portfolio Efficient Frontier—Broad Ranges

(Current Allocation as of February 28, 2013)



Monte Carlo Simulation Results—Current Ranges

1 Year	2.28.2013 Allocation	Conservative	Aggressive
Target 0%	74	75	73
Target 2%	68	69	68
Target 4%	62	63	63
Target 6%	56	56	56
Target 7.75%	**50**	**49**	**51**
Target 10%	43	41	44

3 Years	2.28.2013 Allocation	Conservative	Aggressive
Target 0%	83	84	82
Target 2%	76	77	75
Target 4%	67	67	67
Target 6%	57	56	57
Target 7.75%	**48**	**46**	**48**
Target 10%	36	33	38

5 Years	2.28.2013 Allocation	Conservative	Aggressive
Target 0%	86	88	86
Target 2%	79	80	79
Target 4%	69	70	70
Target 6%	57	56	58
Target 7.75%	**46**	**43**	**47**
Target 10%	32	28	33

10 Years	2.28.2013 Allocation	Conservative	Aggressive
Target 0%	92	93	92
Target 2%	85	86	85
Target 4%	74	74	74
Target 6%	58	56	59
Target 7.75%	**42**	**39**	**43**
Target 10%	24	19	26

Monte Carlo Simulation—Current Ranges

Figure 14: 1-Year Return

Metric	Probability of ≥ 0% Return	Probability of ≥ 7.75% Return
Conservative	75%	49%
Current (2/28/2013)	74%	50%
Aggressive	73%	51%

Figure 15: 10-Year Annualized Return

Metric	Probability of ≥ 0% Return	Probability of ≥ 7.75% Return
Conservative	93%	39%
Current (2/28/2013)	92%	42%
Aggressive	92%	43%

Highlights

- Each portfolio presents minimal trade-offs due to narrow constraints.
- All portfolios provide a reasonable probability of achieving a 7.75% annual return over 10 years.

Monte Carlo Simulation Results—Broad Ranges

1 Year	2.28.2013 Allocation	Conservative*	Moderate	Aggressive*
Target 0%	74	81	77	77
Target 2%	68	72	71	72
Target 4%	62	60	64	66
Target 6%	56	48	56	59
Target 7.75%	**50**	**37**	**49**	**53**
Target 10%	43	25	41	45

3 Years	2.28.2013 Allocation	Conservative*	Moderate	Aggressive*
Target 0%	83	90	86	86
Target 2%	76	80	79	80
Target 4%	67	64	69	71
Target 6%	57	44	57	61
Target 7.75%	**48**	**27**	**46**	**50**
Target 10%	36	11	32	38

5 Years	2.28.2013 Allocation	Conservative*	Moderate	Aggressive*
Target 0%	86	93	90	90
Target 2%	79	83	82	83
Target 4%	69	66	72	74
Target 6%	57	41	57	62
Target 7.75%	**46**	**21**	**44**	**50**
Target 10%	32	6	26	33

10 Years	2.28.2013 Allocation	Conservative*	Moderate	Aggressive*
Target 0%	92	97	94	94
Target 2%	85	90	88	89
Target 4%	74	69	77	79
Target 6%	58	36	58	64
Target 7.75%	**42**	**12**	**39**	**47**
Target 10%	24	1	18	26

RVKuhns & ASSOCIATES, INC.

Monte Carlo Simulation—Broad Ranges

Figure 16: 1-Year Return

Metric	Probability of ≥ 0% Return	Probability of ≥ 7.75% Return
Conservative	81%	37%
Moderate	77%	49%
Current (2/28/2013)	74%	50%
Aggressive	77%	53%

Figure 17: 10-Year Annualized Return

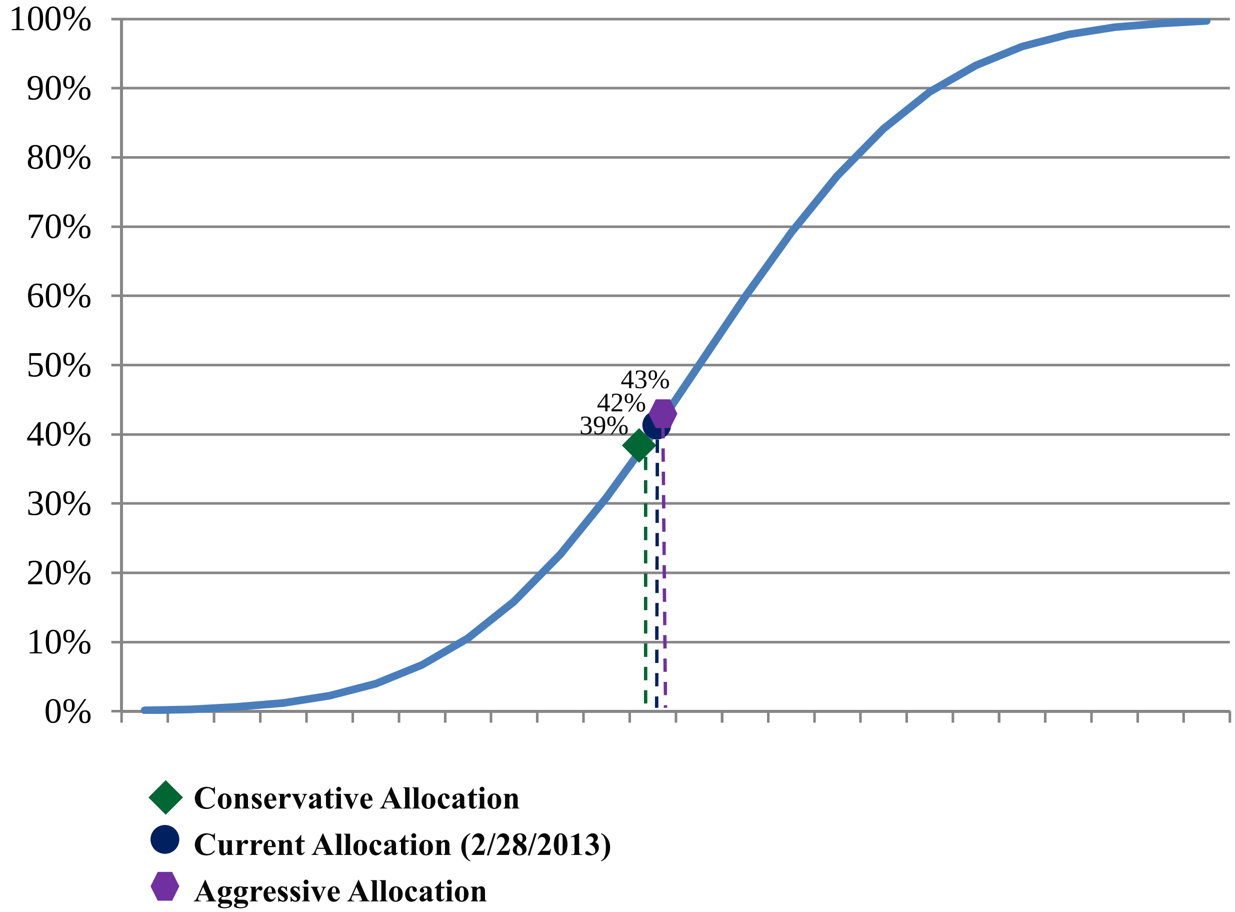
Metric	Probability of ≥ 0% Return	Probability of ≥ 7.75% Return
Conservative	97%	12%
Moderate	94%	39%
Current (2/28/2013)	92%	42%
Aggressive	94%	47%

Highlights

- Each portfolio presents moderate trade offs (particularly over a 10-year horizon)
- The current allocation seeks to balance these in a way that best suits Montana's objectives and constraints.
- A more aggressive risk profile creates a higher likelihood of meeting the 7.75% return objective, but at the cost of liquidity.

MVO Analysis – Monte Carlo Simulation

Figure 18: Cumulative Probability Distribution for Achieving 7.75% Return over 10 Years-Current Ranges



One Year Downside Risk (5% Chance)	
Conservative Allocation	-11.93%
Current Allocation	-13.80%
Aggressive Allocation	-14.53%

RVK Assessment of Liquidity (100=Highest; 0=Lowest)	
Conservative Allocation	72
Current Allocation	72
Aggressive Allocation	71

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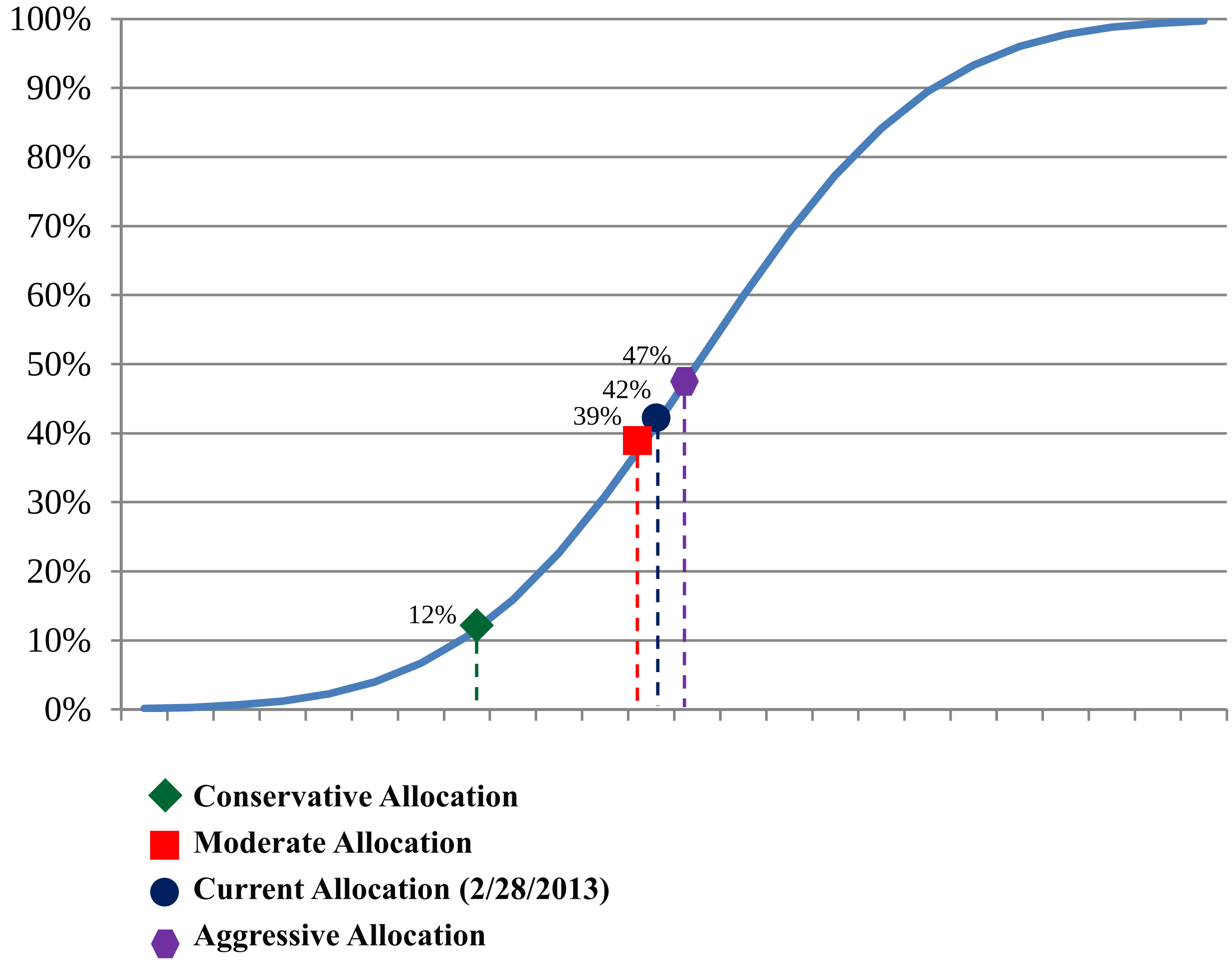
MVO Analysis – Monte Carlo Simulation

Figure 19: Cumulative Probability Distribution for Achieving 7.75% Return over 10 Years-Broad Ranges



One Year Downside Risk (5% Chance)

Conservative Allocation	-6.17%
Moderate Allocation	-10.83%
Current Allocation	-13.01%
Aggressive Allocation	-11.60%

RVK Assessment of Liquidity (100=Highest; 0=Lowest)

Conservative Allocation	81
Moderate Allocation	64
Current Allocation	72
Aggressive Allocation	54

Key Decisions

Asset Class Coverage

Figure 20: Current Asset Class Coverage at MBOI

Asset Class	Allowed?
U.S. Equity	Yes
Int'l Equity	Yes
Core Fixed Income	Yes
High Yield Fixed Income	Yes
Non-US Debt	Yes
Core Real Estate	Yes
Non-Core Real Estate	Yes
Timber	Yes
Private Equity	Yes
Other Real Assets (e.g., commodities, diversified inflation hedges)*	**No**
Hedge Funds	**No**

* TIPS are allowed in Core Fixed Income

Asset Class Range Adjustments

Figure 21: Detailed Asset Class Ranges—Current

Asset Class	Min	Max
U.S. Equity	30%	50%
International Equity	15%	30%
Core Fixed Income	14%	32%
High Yield Fixed Income	0%	5%
Non-US Debt	0%	3%
Core Real Estate	1.5%	6.5%
Non-Core Real Estate	1%	7.5%
Timber	0%	2%
Private Equity	9%	15%
Other Real Assets (e.g., commodities, diversified inflation hedges)*	N/A	N/A
Hedge Funds	N/A	N/A
Cash Equivalents	1%	5%

* TIPS are allowed in Core Fixed Income

Figure 22: Broad Asset Class Ranges—Current

Asset Class	Min	Max
Total Equity	60%	70%
Total Fixed Income	22%	32%
Total Real Estate	4%	10%

Example: Fixed Weight Target Allocation

Definition	A fixed-weight target allocation has a specific target weighting for each asset class in the portfolio. The objectives of establishing this target are to: 1. Measure the performance impact of allocation differences vs. the targets 2. Measure the performance impact of style biases within a given asset class (e.g., small cap stocks vs. total U.S. stocks)
Pros	1. Enables measurement of the impact of deviations from a specific target allocation. 2. Forces continual awareness of potential impact of allocation decisions when managing cash flows.
Cons	1. Many deviations from the target allocation are uncontrollable (e.g., distribution requirements). 2. Impact of allocation decisions must be evaluated over a long time horizon. 3. Ability to adjust asset classes is further limited by MBOI's use of illiquid assets, transition costs, and movement of assets in constantly fluctuating markets.

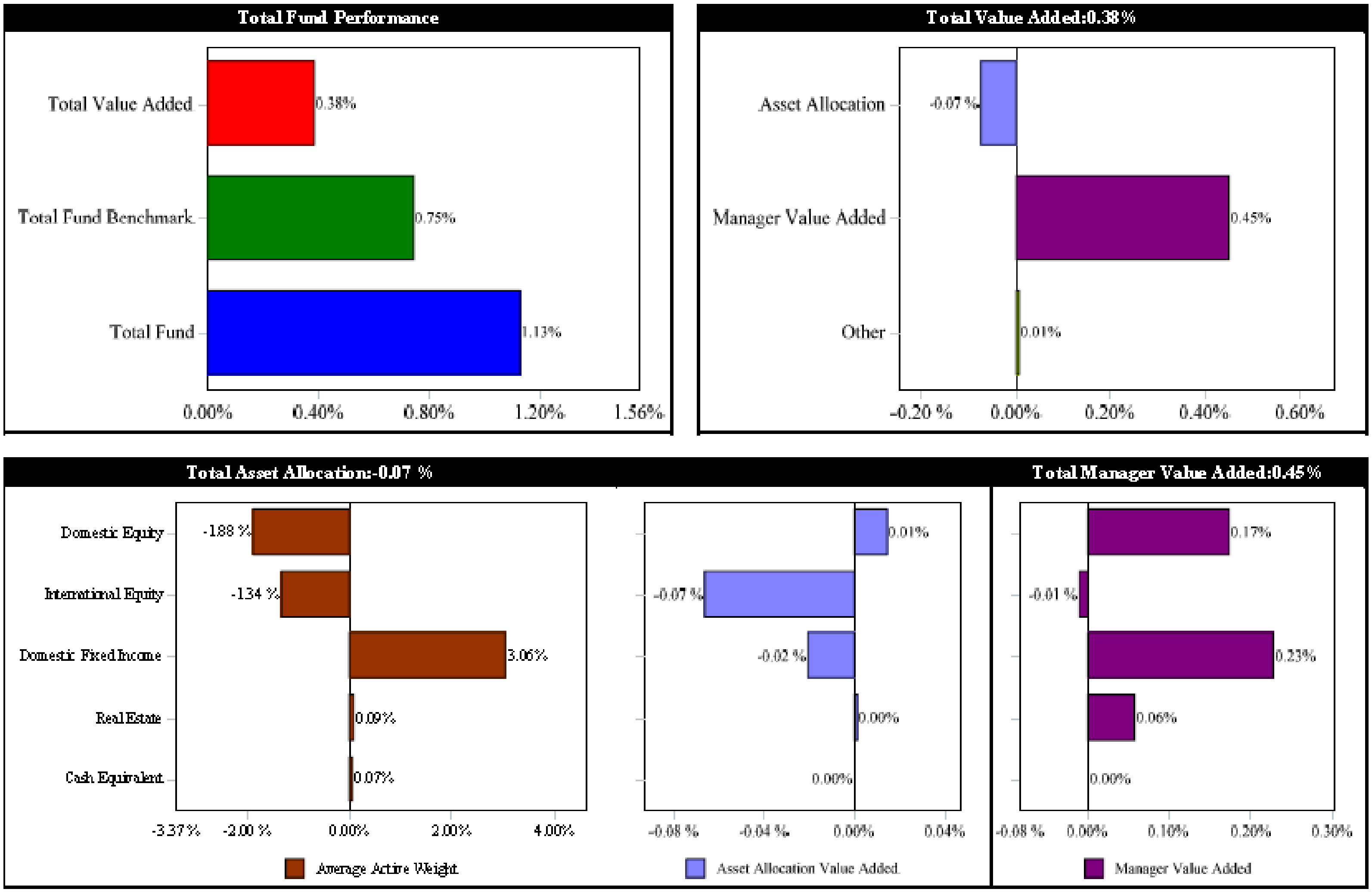
Fixed Weight Target vs. Actual Allocation

Figure 23: Fixed Weight Target Allocation Analysis
(Example Portfolio Period Ending 12/31/2012)

	12/31/2012 Allocation			Q4 2012 Performance		
Asset Class	Target Allocation	Actual Allocation	Variance	Target Index Return	Actual Composite Return	Variance
Domestic Equity	45.00%	42.38%	-2.62%	-0.38%	0.03%	0.41%
International Equity	10.00%	8.83%	-1.17%	5.89%	5.78%	-0.11%
Domestic Fixed Income	35.00%	38.64%	3.64%	0.28%	0.88%	0.60%
Real Estate	10.00%	10.08%	0.08%	2.35%	2.90%	0.55%
Cash Equivalents	0.00%	0.07%	0.07%	0.00%	0.06%	0.06%
TOTAL FUND	100.00%	100.00%	0.00%	0.75%	1.13%	0.38%

Total Fund Attribution

Figure 24: Q4 2012 Total Fund Attribution for Example Portfolio



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Return to Agenda

Investment Activity

MEMORANDUM

Montana Board of Investments
Department of Commerce
2401 Colonial Drive, 3rd Floor
Helena, MT 59601 (406) 444-0001

To: Members of the Board

From: Ethan Hurley, Portfolio Manager – Alternative Investments

Date: April 2, 2013

Subject: Montana Real Estate Pool (MTRP)

The table below summarizes the investment decisions made by Staff since the last Board Meeting. A commitment of $20M was made to GEM Realty Fund V, LP. The investment brief summarizing this fund and the general partner follows this memo.

Fund Name	Vintage	Subclass	Property Type	Amount	Date
GEM Realty Fund V, LP	2013	Opportunistic	Diverse	$20M	2/28/13

MEMORANDUM

Montana Board of Investments
Department of Commerce
2401 Colonial Drive, 3rd Floor
Helena, MT 59601 (406) 444-0001

To: Members of the Board

From: Rande R. Muffick, CFA

Date: April 2, 2013

Subject: Domestic Small Cap Equity Manager Selections

The objective of these manager searches was to identify additional domestic small cap equity managers in order to further diversify active management within the Montana Domestic Equity Pool (MDEP). These managers were expected to provide experienced and stable portfolio management teams with excellent long term performance records and offer portfolios that would complement the current small cap portfolios held within the pool.

Investment analysts at MBOI researched the universe of domestic small cap managers using an in house database to identify top performing managers in the style categories of growth and value. Our consultant, RV Kuhns, also suggested additional managers for consideration. Managers were vetted based upon having a domestic small cap strategy with a strong performance record over one, three, and five year periods. Further analysis on the managers included holdings-based analysis and returns-based analysis in order to compare the individual portfolios' performance and styles to each other, to the peer group, and to the relevant benchmarks (i.e. Russell 2000 Growth Index and Russell 2000 Value Index). This analysis included attribution analysis, upside/downside capture, fee structures, capacity issues, philosophy and process.

Staff then conducted interviews via conference calls with each firm and its portfolio managers with the most attractive candidates eventually being invited to an on-site visit at MBOI for a more detailed personal interview. RV Kuhns assisted throughout the process and provided value-added insight and recommendations.

The due diligence process culminated in the hiring of two domestic small cap equity managers. Metropolitan West Capital Management was chosen as a small cap value manager and ING Investment Management was chosen as a small cap growth manager. Each manager will begin with an initial funding of approximately $20 to $25 million. Both of these portfolios will add diversification in the areas of investment philosophy, methodology, and market performance.

Fee structures negotiated with these two new managers are in line with those of the current small cap growth and value managers that have been under contract with MBOI for several years. Staff anticipates funding to take place early in the second quarter and a transition manager will likely be used for the movement of funds.

MEMORANDUM

Montana Board of Investments
Department of Commerce
2401 Colonial Drive, 3rd Floor
Helena, MT 59601 (406) 444-0001

To: Members of the Board

From: David Ewer, Executive Director

Date: April 2, 2013

Subject: Board Policy and Rule Review

Purpose of Review

In line with our 24-month systematic work plan, this review has the following purposes:

1. Board member education as to the general structure and purpose of its various policies;
2. A due-diligence review by staff for compliance with Board policy;
3. An opportunity for Board members to raise an issue on a policy or a rule;
4. Recommended changes to some investment policies, which will be addressed by a separate memorandum by Cliff Sheets, Chief Investment Officer;
5. Recommended changes to the Board's Education Policy;
6. Recommended changes, mostly cleanup, to the Governance Manual, and a recommended new exhibit that would list the titles of all of the Board's policies and rules.

Staff will not review every policy or rule at the meeting. However, it is appropriate for members to focus on any policy of their choosing.

Both the Board's Governance Manual, which incorporates the Board's most over-arching policies, and many of the most significant investment policies are currently on the Board's web site. Staff is working to link additional policies and rules on the web site with a target completion date of March 28th.

Policy and ***Rule*** at the Board of Investments

'Policy' at the Board has a precise meaning: it is a written edict considered and passed by the full Board in an open meeting. Most of the Board's policies direct how its staff will do their jobs, what is delegated to them, what is not. The Board also has rules, but in recent years has chosen to set its formal edicts in policy, rather than by rule. Rule-making involves a prescribed process of notification and meetings primarily for the opportunity for public testimony, which must be considered and addressed. In general, rules are necessary when potentially contentious matters affect how a state agency will specifically implement a law.

Staff ***must*** abide by policy and rule. To be effective and truly meaningful, polices should be constructed carefully to minimize unintended consequences and be kept current.

The Board has many policies; they fall within four general groups:

1) **Governance**, the Board's most important 'rules of the road', and at the highest and most important level, the Board's Governance Manual itself. Other examples in this category are its Code of Ethics, Audit Committee Charter, and its Loan Committee Charter.

2) **Investments**, those dealing with the Board's fiduciary assets as opposed to its lending activities. These policies range from the high-level of "Montana Public Retirement Plans Investment Policy Statement" to the very specific, e.g., the "Noxious Weed Management Trust Fund". Investment policies have the most uniform structure of all of the Board's policies: they cover at a minimum introduction, objective, constraints, and for the more broad-ranging such as equities, also include policy directives on risk management, liquidity, allocation, and many other constraints.
3) **Operational**, those dealing with such matters as internal controls, continuation of operations, delegation of operational authority, human resources such as education and exempt staff pay plan.
4) **Lending Programs**, those dealing with the Board's various lending programs, e.g., its In-State loan programs, Veteran's Home Loan Program, and the INTERCAP Loan Program.

Rules at the Board of Investments

A list of the Board's rules still in effect is attached, along with a list of its current policies. Board rules have not been changed since 2000 and several apply to programs that are either dormant (e.g., Moral Obligation Economic Development Bond Program) or no longer exist in statute (e.g., the Montana Capital Company Act, repealed in 2011).

Staff Review

Staff has reviewed the Board's policies. No unusual 'outlier' situations were discovered. As noted, changes to investment policies will be addressed by Mr. Sheets. Recommendations to policies that would first go before any of the Board's Committees will be presented at the Board's May meeting. In consultation with the Chairman, staff does recommend some revisions to the Board's Education Policy. Staff is currently reviewing rules and may have recommendations at a later date.

Recommendations

Staff recommends the following:

1. Adopt changes, mostly cleanup, to the Governance Manual and a new Exhibit K listing all of the Board's current rules and policies, as per Attachment A; the proposed new wording is underlined and the proposed deleted wording is ~~stricken out~~.
2. Adopt changes to investment policies as recommended under separate memorandum by the Chief Investment Officer; and
3. Adopt changes to the Education Policy as contained in Attachment B; the proposed new wording is underlined and the proposed deleted wording is ~~stricken out~~.

Montana

Board of Investments

Governance Manual

TABLE OF CONTENTS

I. PURPOSE

One of the purposes of a public investment board Governance ~~Policy~~ Manual (~~Policy~~Manual) 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~~Manual. This ~~Policy~~ Manual 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.

II. BOARD MEMBER AUTHORITIES, DUTIES, AND ROLES

1. <u>General Duties Prescribed by Law</u>

A) The Unified Investment Program - The Montana Constitution requires that the Legislature provide for a Unified Investment Program for public funds. Section 17-6-201, MCA established the Unified Investment Program, created the Montana Board of Investments (the "Board") and gave the Board sole authority to invest state funds in accordance with state law and the state constitution. State law requires that the Board operate under the "prudent expert principle," defined as: 1) discharging its duties with the care, skill, prudence, and diligence that a prudent person acting in a like capacity with the same resources and familiar with like matters exercises in the conduct of an enterprise of a like character with like aims; 2) diversifying the holdings of each fund to minimize the risk of loss and maximize the rate of return; and 3) discharging its duties solely in the interest of and for the beneficiaries of the funds managed.

B) Economic Development Programs - In addition to managing the Unified Investment Program, the Legislature assigned to the Board the responsibilities of managing several loan programs.

2. <u>Board Membership</u> - The Board is comprised of nine voting members appointed by the Governor as prescribed in Section 2-15-124, MCA, subject to confirmation by the state Senate and comprised of the following:

- One member from the Public Employees' Retirement Board;
- One member from the Teachers' Retirement Board; and
- Seven members representing the financial community, small business, agriculture, and labor.

The Board also has two non-voting legislative liaisons, from different political parties, comprised of the following:

- One liaison member appointed by the President of the Senate; and
- One liaison member appointed by the Speaker of the House.

The Board is allocated to the Department of Commerce for administrative purposes as prescribed in Section 2-15-121, MCA. The following members have been appointed to the Board for a four-year term and confirmed by the State Senate:

Member	Location	Term Expires
Mark Noennig – Chairperson	**Billings**	**01/01/2017**
Kathy Bessette	**Havre**	**01/01/2017**
Bob Bugni	**Helena**	**01/01/2013**
Karl Englund	**Missoula**	**01/01/2015**
Gary Buchanan	**Billings**	**01/01/2015**
Quinton Nyman	**Helena**	**01/01/2015**
Jon Satre	**Helena**	**01/01/2015**
Marilyn Ryan	**Missoula**	**01/01/2017**
Jack Prothero	**Great Falls**	**01/01/2017**

3. **Board Chairperson -** As prescribed in §2-15-124, MCA the Governor shall designate the Chairperson, whose duty is to ensure that the Board operates consistent with state law, state rules, and Board policies. The Chairperson may make and second motions and vote. The Chairperson shall review and sign all meeting minutes and all resolutions approved by the Board. The Chairperson may appoint a Vice Chairperson to preside in his/her absence.

4. **Code of Ethics -** The Board shall create and adhere to a Code of Ethics for its members and staff. The Code shall be designed to ensure that Board members and Board staff have no conflicting interests that would harm the integrity of the Board, harm the clients for whom the Board invests funds, or interfere with the Boards fiduciary responsibility. The Code approved by the Board is attached as **Appendix B**.

5. **Governing Law -** The Board shall maintain and update as necessary a written and electronic manual of all its pertinent governing laws and shall post the manual on its website for public access.

6. **Quorum and Voting -** A majority of the Board membership (five members) constitutes a quorum to do business. A favorable vote of at least a majority of all members (five members) of the Board is required to adopt any resolution, motion, or other substantive decision, as prescribed in §2-15-124 MCA. For example, if only five members are present, all five members must approve a substantive motion.

7. **Board Meeting Frequency -** The Board meets quarterly and is subject to the call of the Chairperson if additional meetings are required. The frequency of Board meetings is subject to change at the direction of the Board.

8. **Notice of Meetings -** All meetings of the Board must be open to the public and noticed at least 48 hours prior to the meeting. A meeting may only be closed when the demands of individual privacy clearly exceed the merits of public disclosure and the Chairperson may not close the meeting without first stating the rationale for such closure.

9. **Meeting Agendas -** Meeting agendas are prepared by the Executive Director in consultation with the Chairperson. The Board may not take action on any substantive matter unless the matter is scheduled on the agenda. The meeting notice and the meeting agenda shall be posted on the Board's web site.

10. Public Participation - Section 2-3-103, MCA provides that the agenda for Board meetings must include an item allowing public comment on any public matter that may or may not be on the agenda and that is within the jurisdiction of the Board. The Board may not take substantive action on any matter discussed unless specific notice of that matter is included on an agenda and the public is provided an opportunity to comment on that matter. A letter from the Governor expressing the importance of compliance with this law is attached as **Appendix A**.

11. Committee Creation - The Board may:

A) Establish committees as necessary to conduct its business and charters shall be adopted for each committee describing the role, scope, and powers of the committee and the responsibilities of committee members.

B) The Board Chairperson may appoint and remove committee members. The Board has created an Audit Committee, a Loan Committee, and a Human Resources Committee and approved a charter for each. The charters are attached as **Appendices C**, **D**, and **E**.

C) All Committee Meetings must be open to the public and noticed on the Board's web site at least 48 hours prior to the meeting.

Current members of the committees are:

Audit	Loan	Human Resource
Jon Satre, Chairperson	Jack Prothero, Chairperson	Karl Englund, Chairperson
Gary Buchanan	Kathy Bessette	Quinton Nyman
Bob Bugni	Gary Buchanan	Jack Prothero
		Marilyn Ryan
		Jon Satre

12. Adoption of Resolutions - All resolutions committing the Board to issue bonds either directly or as a conduit issuer; or to enhance bonds issued by others as authorized by law must be approved by the Board at a public meeting and signed by the Chairperson and the Executive Director.

13. Selection of Custodial Bank and ~~Retainer~~ Investment Consultant - While this Governance ~~Policy~~ Manual delegates general contracting authority to the Executive Director, the Board reserves the right and the authority to make the final selection of the Custodial Bank and the ~~Retainer~~ Investment Consultant after which the Executive Director shall negotiate a contract.

14. Asset Allocation - The Board, as the fiduciary of the Unified Investment Program, is responsible for establishing the investment parameters of the Unified Investment Program. The Board has the authority to allocate portfolios to any asset class in the proportions it considers prudent, subject to such limitations as are contained in law and the Constitution. When the law or Constitution precludes certain investments, the Board is responsible for allocating portfolios to asset classes within the investment types permitted by law.

Asset allocation decisions may be made by the Board only in a public meeting. ***The authority to establish asset allocation ranges and targets rests solely with the Board and may not be delegated to staff.***

15. Administrative Rules – The Board has rule-making authority under state law. Administrative rules are regulations, standards or statements of applicability that implement, interpret, or set law or policy. Administrative rules can also describe the organization, procedures or practice requirements of the Board. ***The authority to revise Board Administrative Rules may not be delegated to staff.*** A list of Board Administrative Rules is attached as Appendix K.

~~15~~16. Investment Policy Statements - The Board shall create, maintain, and revise as necessary Investment Policy Statements (Statements) for each separate account it manages. The Statements shall cite the law establishing the account if such law exists, the permissible investments authorized by law, and establish an investment range for each of the permissible investments. The Board shall review such policies at least annually or more frequently at the request of Board staff. Statements may only be revised in a public meeting. All Statements shall be posted on the Board's web site for review by the public. ***The authority to approve Investment Policy Statements may not be delegated to staff.*** A list of Investment Policy Statements is attached as **Appendix K**.

~~16~~17. Coal Tax Trust Loan Policies - The Board shall create loan policies for each of the Coal Tax Trust loan programs assigned to it by law. The policies shall be based on the law creating the programs and may be revised from time to time as necessary to accommodate changes in the law or to enhance or clarify the programs. Substantive policy revisions may be made only by the Board at a public meeting. All loan policies shall be posted on the Board's web site. ***The authority to substantively revise Coal Tax Trust Loan Polices approved by the Board may not be delegated to staff.*** A list of Coal Tax Trust Loan Policies is attached as **Appendix K**.

~~17~~18. Bond Program Policies - The Board shall create policies for its various Bond Programs assigned to it by law. The policies shall be based on the law creating the programs and may be revised from time to time as necessary to accommodate changes in the law or to enhance or clarify the programs. Substantive policy revisions may be made only by the Board at a public meeting. All policies shall be posted on the Board's web site. ***The authority to substantively revise Bond Program Policies approved by the Board may not be delegated to staff.*** A list of Bond Program Policies is attached as **Appendix K**.

~~18~~19. Interest Rate Setting Process/Methodology - The Board shall establish and approve an interest rate setting process and methodology for loan programs for which it has discretion to set rates. Staff shall utilize the approved process and post the rates weekly on the Board's web site. ***The authority to revise interest rate setting processes and/or methodologies approved by the Board may not be delegated to staff.***

~~19~~20. Class Action Litigation Participation - The Board shall adopt, maintain, and revise as necessary a process and policy to ensure that it participates in all class action litigation to which it is entitled. The process and policy adopted by the Board is attached as **Appendix F**.

~~20~~21. Budget - The Executive Director shall prepare the Board's budget and staffing level recommendations for Board review and approval. After Board approval the budget is submitted to the

Department of Commerce for approval and then to the Governor's Office of Budget and Program Planning for final approval. The Board's budget is funded from two revenue sources.

A) The Investment Program is funded by fees charged the Board's clients. Because the Board's clients are state agencies, the Legislature sets the maximum fee the Board may charge which is then allocated by Board staff to all Board clients. The Board's methodology used to allocate charges to its clients is audited by the Legislative Auditor.

B) The Bond Program is funded by the "spread" between the interest paid on the bonds sold and the interest on loans made from the bond proceeds. The spread may be no greater than 1.5 percent. Because the Bond Program's clients are primarily non-state agencies, the Legislature does not set a maximum fee the Board may charge.

~~21~~22. **Board Staff -** The Board appoints the Executive Director who has general responsibility for selection, management, and the job performance of Board staff. The Board also appoints the Chief Investment Officer. The Board assigns the duties and sets the salaries of eight staff - the Executive Director, Chief Investment Officer, and six investment professional staff. The Board's functional organization chart is attached as **Appendix G**

III. DELEGATION OF AUTHORITY TO STAFF

The Board delegates to its the Executive Director and the Chief Investment Officer the following day to day duties required to carry out the Board's mission.

1. **Executive Director -** The Executive Director is empowered by the Board to administratively supervise all Board staff, to authorize expenditures, and to sign any and all documents required to conduct Board business, unless there are specific written policies or instructions from the Board to the contrary. These documents include, but are not limited to vendor contracts, commitments to investment managers, invoices, official letters detailing the position of the Board on any matter, resolutions approved by the Board, leases for Board owned buildings, authorizations to renovate and repair Board owned buildings, staff time sheets, and staff job descriptions. In exercising the delegated authority, the Executive Director shall provide the Board with the information and reports necessary for the Board to fulfill its fiduciary duty in monitoring and reviewing the actions of the Board staff and operations.

2. **Deputy Director -** To ensure continuity the Deputy Director is empowered by the Board to carry out the duties of the Executive Director in his/her absence unless there are specific written policies or instructions from the Board to the contrary. The Executive Director shall establish a written protocol to ensure continuity in his/her absence and such protocol was approved in **Resolution 218** and attached hereto as **Appendix I**.

3. **Chief Investment Officer -** The Chief Investment Officer is empowered by the Board to create and review Investment Policy Statements for Board approval, review and recommend changes in the asset allocation of all separate accounts, recommend new investment types permitted by law, and rebalance separate accounts as necessary to keep assets within the ranges authorized by the Board. The Chief Investment Officer is empowered by the Board to conduct searches for all external investment managers and make the final selection.

4. **Operations Delegation** - The Executive Director is authorized to administer the day-to-day operations of the Board. As an agency head, the Executive Director has all powers and authority normally vested in similar positions in other state agencies to include, but not be limited to, the hiring and firing of non-exempt staff, and the commitment of funds necessary for the efficient conduct of Board business. Exempt staff may only be terminated upon Board Approval. In carrying out these duties, the Executive Director shall ensure compliance with Board policies and directives, as well as applicable state and federal laws and regulations.

5. **Communications Delegation** - The Executive Director shall serve as the exclusive spokesperson for the Board when communicating with the Legislature, the Governor, the public, and the media, unless the Board Chairperson determines that, in certain situations, it would be more appropriate for the Chairperson or a selected Board Member to serve as the spokesperson.

6. **Investment Manager Contracts** - The Board in discharging its duties under the Montana Constitution and the Unified Investment Program (the "Program") enters into various contracts. For those contracts that are fundamental in enabling the Board to invest public funds and satisfy its legal duty under the Program, including its responsibility to "determine the type of investment to be made" (17-6-201 (5)(c), M.C.A.), the Board reserves to itself the sole discretion of entering into such contracts in compliance with its constitutional and statutory mandate. The Board delegates and directs the following:

- The Executive Director and the Chief Investment Officer are authorized jointly to contract for investment manager services and if deemed appropriate, terminate them.
- However, the Chief Investment Officer is authorized to have the final decision on external investment managers.
- Provided that, the Executive Director may be a part of any negotiation and at a minimum sign all contracts for investment manager services.
- And further provided that the Board's Legal Counsel review and sign all investment management contracts and review all other investment-related service contracts as the Executive Director or Chief Investment Officer deem necessary or advisable.
- All new investment manager contracts, commitments, and terminations along with sufficient other related information, and in particular, alternative investment managers and their key terms of the fund, shall be reported to the Board at its next scheduled meeting.

7. **All Other Contracts** - For all contracts not specifically investment manager contracts, such contracts both competitive and sole source, shall be processed according to the State's procurement and contracting laws. The Executive Director is authorized to negotiate and enter into all contracts necessary to carry out the Board's mission without advance approval of the Board, except for contracts with the Board's Custodial Bank and ~~Retainer~~ Investment Consultant. The Board shall approve the selection of the Custodial Bank and the ~~Retainer~~ Investment Consultant after which the Executive Director shall negotiate contracts with the firms. The Executive Director may approve contract extensions for which the Custodial Bank and ~~Retainer~~ Investment Consultant are eligible under the original contract terms. In compliance with state requirements and Board policies review by the Board's Legal Counsel is required for all contracts.

A) Legal Services - The Board delegates to the Executive Director the authority to provide appropriate legal representation for all Board activities. The Executive Director shall contract for legal services and ensure that there is no lapse in service. Legal services may be provided by a combination of private legal services contract, the Department of Commerce Legal Counsel, and the Attorney General's offices as appropriate. The Executive Director shall also ensure that the Board has legal representation for any class action litigation to which it is entitled to participate.

B) Building Management Services - The Executive Director is authorized to make all day to day decisions required in managing the Board's direct real estate program. These decisions include but are not limited to negotiating and signing leases, authorizing payment of invoices, authorizing repair and renovation, authorizing improvement and construction, and contracting with a Building Manager. The Board must approve the purchase and sale of all direct real estate.

C) Personal Services Contracts - The Executive Director is empowered to negotiate personal services contracts as necessary to ensure proper staffing levels and/or to obtain specialized services not otherwise available.

D) Interagency Agreements - The Executive Director is empowered to sign Interagency Agreements and contracts with other state agencies as necessary to fulfill the Board's mission and/or to implement recently enacted legislation.

8. Legal Action - When the Board is named as a defendant in a legal action the Executive Director is authorized to act on behalf of the Board with the advice of legal counsel and shall notify the Chairperson in a timely manner. The Executive Director may only initiate legal action with Board approval.

9. Class Action Litigation - The Executive Director is authorized to join class action lawsuits on behalf of the Board so that the Board may share in any distribution from the settlement, unless it is determined that legal action by the Board, independent of a class action lawsuit, is advisable as per the Class Action Litigation Policy **(Appendix F)**. The Executive Director may consult with legal counsel and Audit Committee members as necessary and shall report to the Board, at its next meeting, any decisions regarding class action suits.

10. Authorization of Investment Vendors - Board funds may not be committed, wired, or otherwise transferred to investment vendors without the specific approval by the Executive Director of such vendors as per **Resolution 217** approved by the Board and attached as **Appendix H.**

11. Authorization of Staff Transactions - Board staff may not transact business with investment vendors without the specific approval of the Executive Director as per **Resolution 217** approved by the Board and attached as **Appendix H.**

12. Credit Enhancement Implementation - The Executive Director is authorized to take all necessary action to implement credit enhancement activity authorized by the Board as per **Resolution 219** attached as **Appendix J**.

13. **Annual Report -** The Board is required by law to submit an annual report on all its activities by December 31. The Executive Director shall prepare and publish the annual report and review and approve all financial statements included in the report.

14. **Board Office Space -** The Executive Director shall provide for office space for the Board's operations and is authorized to negotiate and sign leases for office space as appropriate and in conformance with state policy.

15. **Legislative Duties -** The Executive Director shall represent the Board before the Legislature. Duties include, but are not limited to: recommending for Board approval proposed legislation to further the Board's mission; testifying on legislation that may impact the Board and its mission; and monitoring all legislation introduced to determine what if any impact such legislation may have on the Board and its mission. The Executive Director shall keep the Board informed on these activities as necessary during legislative sessions.

16. **Further Delegation by the Executive Director -** The Executive Director, while retaining responsibility for all delegated authority from the Board may further delegate the authority in writing (including signature authority) necessary to appropriate Board staff to conduct day-to-day Board activities.

OFFICE OF THE GOVERNOR
STATE OF MONTANA

BRIAN SCHWEITZER
GOVERNOR

JOHN BOHLINGER
LT. GOVERNOR

TO: Executive Branch Officers
Department Directors
Chairs and other Presiding Officers of All Executive Branch Boards, Bureaus, Commissions, Departments, Authorities, and Agencies

FROM: Governor Brian Schweitzer

DATE: October 16, 2012

RE: Public participation in agency decisions pursuant to § 2-3-103, MCA

Montana's public participation laws require me, as Governor, "to ensure that each board, bureau, commission, department, authority, agency, or officer of the executive branch of the state" adopts rules, setting forth policies and procedures to facilitate public participation in agency programs and decisions. Sec. 2-3-103(2), MCA. I have written you in past years to remind you of these important statutory obligations, and I take this opportunity to remind you of them again.

Montanans have a constitutional right to participate in the activities of their government. The "Right of Participation" is found at Article II, section 8 of the Montana Constitution, which provides:

> The public has the right to expect governmental agencies to afford such reasonable opportunity for citizen participation in the operation of the agencies prior to the final decision as may be provided by law.

This constitutional right is implemented by Montana statutes (Title 2, chapter 3, part 1, MCA) requiring every agency to develop procedures to permit and encourage public participation in agency decisions "that are of significant interest to the public." The statutes require agencies to provide adequate notice to the public and assist public participation. Meeting agendas must include an item allowing public comment on any public matter not on the agenda but within the agency's jurisdiction. Additionally, the agency may not act on any matter that was not included on the agenda and for which public comment on the matter was not allowed. Public comments must be incorporated into the official minutes of the meeting. The district courts may set aside agency decisions not in conformity with the public participation laws where a person's rights have been prejudiced. Model rules to implement these laws are found at ARM §§ 1.3.101 and 1.3.102.

As you know, this Administration takes very seriously the public's right to participate in the decisions of government, and I applaud your efforts to ensure this public right. If you or your agency needs assistance in crafting appropriate guidelines and rules to conform to Montana's public participation laws, feel free to contact my legal counsel, Ann Brodsky, for assistance (444-3558).

I. PURPOSE

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

II. STATE CODE OF ETHIC PROVISIONS

1. **<u>Monetary Provisions</u> -** The state's Ethics Code is found in Title 2, chapter 2, part 1, Montana Code Annotated. Legislative intent for the law is described in the statement of purpose:

> **Section 2-2-101. Statement of purpose. The purpose of this part is to set forth a code of ethics prohibiting conflict between public duty and private interest as required by the constitution of Montana. This code recognizes distinctions between legislators, other officers and employees of state government, and officers and employees of local government and prescribes some standards of conduct common to all categories and some standards of conduct adapted to each category. <u>The provisions of this part recognize that some actions are conflicts per se between public duty and private interest while other actions may or may not pose such conflicts depending upon the surrounding circumstances.</u>**

The underlined language (emphasis added) reflects the remainder of the state Ethics Code in that it is rather ambiguous and subject to interpretation. The underlined language seems to imply that it is the circumstances surrounding the action that may be more important in determining conflict rather than the action itself. Generally, the state's Ethics Code attempts to describe circumstances under which a public employee responsible for making material decisions impacting others may have a conflict of interest. The conflict could involve a personal or financial relationship with an existing or potential vendor/contractor/borrower or the receipt of a gift with monetary value from these entities if such a gift could influence an action favorable to the entity.

> **Section 2-2-104. A public officer, legislator, or public employee may not accept a <u>gift of substantial value</u> or a substantial economic benefit tantamount to a gift <u>that would tend improperly to influence</u> a reasonable person in the person's position to depart from the faithful and impartial discharge of the person's public duties or that the person knows or that a reasonable person in that position should know under the circumstances is primarily for the purpose of rewarding the person for official action taken.**

The underlined language (emphasis added) prohibits a public employee from receiving a "gift of substantial value" if such a gift would influence the recipients official action (assumed to be an action relating to the gift giver). This section apparently does not prevent public employees not serving in a "decision making" role from accepting gifts. Lending more ambiguity to this section is how a "gift of substantial value" is defined. Section 2-2-102(3) (a) describes a gift of substantial value as a gift with a value of $50.00 or more per individual unless the gift is not used and within 30 days of receipt is returned to the donor or donated to charity. The problem with this definition is there are no frequency limitations that might cap the cumulative effect of gifts over time, i.e. could one receive a $49.00 gift each day of the week and still not receive a "gift of substantial value?" In an extreme example, a person receiving a $49.00 gift every day of the year would have received gifts totaling $17,885 but would have never crossed the $50.00 substantial value threshold. Another potential problem is how the recipient would know the value of the gift without a pricing source. A pen for example, could be nothing more than an advertising prop or could be worth well over $50.00 dollars.

While the preceding discussion highlights the ambiguities and "subject to interpretation" provisions in the state Ethics Code, another section of state law is more on target as it relates to public employees who serve in material decision-making capacities. These provisions are found in Title 45 "Crimes" with a short title of "Criminal Code of 1973."

> **Section 45-7-104 (2) "No public servant having any discretionary function to perform in connection with contracts, purchases, payments, claims, or other pecuniary transactions of the government shall solicit, accept, or agree to accept any pecuniary benefit from any person known to be interested in or likely to become interested in any such contract, purchase, payment, claim, or transaction."**

This provision is very blunt and to the point but is tempered somewhat later in subsection (5) (b):

> **"This section shall not apply to trivial benefits incidental to personal, professional, or business contacts and involving no substantial risk of undermining official impartiality."**

Discretionary function is not defined here but a definition in the state Ethics Code likely describes the type of discretion referred to here. Section 2-2-102(5) states:

> **"Official act" or "official action" means a vote, decision, recommendation, approval, disapproval, or other action, including inaction, that involves the use of discretionary authority.**

The above provisions would seem to prevent any Board member or staff who has any responsibility for scoring/selecting investment vendors and contractors, or recommending/approving loans from receiving any type of monetary benefit from current or potential vendors, contractors, or borrowers unless the benefit is "trivial" which is subject to interpretation. While "pecuniary" is not defined here, the dictionary describes it as "consisting of or measured in money" and in Section 45-2-101(56) is defined as "benefit in the form of money, property, commercial interest, or anything else the primary significance of which is economic gain."

2. **<u>Relationship Provisions</u> -** The state Ethics Code prohibits certain types of relationships that may improperly interfere with a public employee's partiality.

> **Section 2-2-105, MCA (1) The requirements in this section are intended as rules of conduct, and violations constitute a breach of the public trust and public duty of office or employment in state or local government.**
> **(2) Except as provided in subsection (4), a public officer or public employee may not acquire an interest in any business or undertaking that the officer or employee has reason to believe may be directly and substantially affected to its economic benefit by official action to be taken by the officer's or employee's agency. ***

(4) When a public employee who is a member of a quasi-judicial board or commission or of a board, commission, or committee with rulemaking authority is required to take official action on a matter as to which the public employee has a conflict created by a personal or private interest that would directly give rise to an appearance of impropriety as to the public employee's influence, benefit, or detriment in regard to the matter, the public employee shall disclose the interest creating the conflict prior to participating in the official action.
(5) A public officer or public employee may not perform an official act directly and substantially affecting a business or other undertaking to its economic detriment when the officer or employee has a substantial personal interest in a competing firm or undertaking.
***(3) Has been excluded because it is not immediately relevant.**

This provision relates directly to the official duties of Board members and staff who are involved in the decision making process. Subsection (2) prevents a public employee from acquiring a personal or financial interest in an entity that they believe could benefit from future action the public employee may take. Examples would be a Board member or staff taking a financial interest in a business that had a loan request pending upon which the Board member or staff would ultimately act. Subsection (5) is the reverse situation in which a public employee has a financial or personal interest in a business that is a direct competitor of a business with a pending loan request before the Board. The competing interest of the Board member or staff could color the ultimate decision. Subsection (4) is specifically aimed at quasi-judicial Board members, such as the Board. It recognizes that lay board members have day-to-day business interests some of which may come before them in their official capacity as board members. Specific examples of this would be board members who are bank officials or employees when loan requests submitted by their bank are considered by the Board.

3. Time and Facilities Provisions - The state Ethics Code prohibits public employees from conducting private business on state time or facilities.

Section 2-2-121 (2) A public officer or a public employee may not: (a) subject to subsection (7), use public time, facilities, equipment, supplies, personnel, or funds for the officer's or employee's private business purposes

This provision prohibits public employees from using state time, facilities, etc. to conduct private business. Private business is not defined here but would likely mean conducting some type of business generating revenue rather than sending an occasional personal e-mail or making a personal phone call. This interpretation of private business is further reinforced by the reference to subsection (7) which states:

A listing by a public officer or a public employee in the electronic directory provided for in 30-17-101 of any product created outside of work in a public agency is not in violation of subsection (2)(a) of this section. The public officer or public employee may not make arrangements for the listing in the electronic directory during work hours.

This language implies that the reference to private business is in fact a bona fide business that produces a product for sale that may be listed in the "Made in Montana" electronic directory provided by the Department of Commerce.

4. Dual Salaries Provisions - The Ethics Code prohibits public employees from drawing two salaries from public agencies for the same period of time.

> **Section 2-2-104(3)(a) Except as provided in subsection (3)(b), a public officer, legislator, or public employee may not receive salaries from two separate public employment positions that overlap for the hours being compensated, unless: the public officer, legislator, or public employee reimburses the public entity from which the employee is absent for the salary paid for performing the function from which the officer, legislator, or employee is absent; or the public officer's, legislator's, or public employee's salary from one employer is reduced by the amount of salary received from the other public employer in order to avoid duplicate compensation for the overlapping hours.**

This provision prohibits a Board member who is also a public employee from receiving compensation from both sources for the same period of time. For example, if a Board member spent two days away from a public employee job to attend Board meetings and was a salaried employee who remained on a public payroll during the period, he/she could not receive per diem for attending the Board meeting. However, as clarified later in the state Ethics Code if the Board member was an hourly employee who took accrued leave or compensation time to attend the meeting he/she would be eligible for per diem for Board attendance.

This provision is reinforced in the law that governs quasi-judicial Boards:

> **2-15-124 (7) Unless otherwise provided by law, each member is entitled to be paid $50 for each day in which he is actually and necessarily engaged in the performance of board duties, and he is also entitled to be reimbursed for travel expenses, as provided for in 2-18-501 through 2-18-503, incurred while in the performance of board duties. Members who are full-time salaried officers or employees of this state or of a political subdivision of this state are not entitled to be compensated for their service as members except when they perform their board duties outside their regular working hours or during time charged against their annual leave, but such members are entitled to be reimbursed for travel expenses as provided for in 2-18-501 through 2-18-503. Ex officio board members may not receive compensation but shall receive travel expenses.**

III. RATIONALE FOR A BOARD OF INVESTMENTS CODE OF ETHICS

The Board's composition does not lend itself to the "pay to play" problems that have been discovered in other investment Boards. There are no elected officials on the Board as voting members nor do any elected officials exert any influence on the Board's decision making process. Therefore campaign contributions to any Montana elected official will have no impact on the Board's decision to hire or fire an investment vendor, make or deny a loan, or to conduct business with a political contributor.

Perhaps the greatest potential for conflicts of interest of Board members and staff is with private investment vendor relationships. The Board's mission requires it to have numerous relationships with these vendors; including investment managers, investment brokers, investment consultants, investment and custodian banks, and commercial banks. Vendors selected by the Board to provide these services will receive millions in fees during the contract period. Therefore, the process for establishing and terminating these relationships must be based on well established protocol. When existing and potential vendors provide any type of financial benefits to persons who are ultimately responsible for selecting and maintaining these relationships a potential conflict could exist.

The type of "financial benefit" does not have to be direct to create a potential conflict of interest. There are firms in the investment business who sponsor conferences couched as educational in nature but are in fact a not so subtle attempt to get "buyers" and "sellers" of services (vendors) in the same place at the same time. Generally, the service "buyers", such as the Board are provided a host of "free" amenities to attend and mix with potential vendors. Basically, it is the vendors paying for the amenities provided free to the buyers.

While it is difficult to put a dollar value on these amenities, the cost to the vendors of providing free services to potential buyers is a "gift equivalent."

This restriction does not apply to meals/beverages provided at investor conferences held by General Partners in which the Board is a Limited Partner. This is the only opportunity Board Members/staff have to meet and interact with other Limited Partners and hear the General Partner discuss the strategy and progress of the fund. Because of the significant number of Limited Partners in the larger General Partnerships, the General Partners do not usually visit the Limited Partners individually but rather host periodic investor meetings.

The second greatest potential for conflict of interest involves the Board's economic development role. The Board manages several loan programs that lend Coal Tax Trust funds to hundreds of Montana borrowers. If Board members or staff in the "decision making loop" have personal or financial relationships with local lenders or borrowers whose loans are pending, serious conflicts could occur.

Also, Board employees are unique in state government because many of them have state-provided access to financial research tools and information that could benefit them when investing a personal portfolio. While research information obtained by staff in the course of normal job duties may provide incidental knowledge and benefit to the management of a personal portfolio, state time and facilities must not be used for personal enrichment. Personal security trading must not be conducted on state time/facilities nor should staff conduct any type of business enterprise on state time and facilities.

The Board adopts the following Code of Ethics (Code) for its members and staff to: ensure that the conduct of members and staff conform to state law, that potential conflicts of interest are reduced or eliminated and; that the Board's fiduciary reputation is not damaged in perception or in fact. All Board members and staff shall sign the Code annually and all new members and staff shall sign when appointed or hired. By signing the Code, each Board member and staff pledges to the best of his/her ability to comply with all provisions of the Code.

IV. BOARD OF INVESTMENTS CODE OF ETHICS PROVISIONS

1. Monetary Provisions

A) Board members/staff shall not attend conferences if any of the actual costs to the Board of attending such conferences are subsidized by current or potential investment vendors. However, Board members/staff may attend if the Board pays the actual cost for such attendance. If the conference is truly educational and otherwise worthwhile Board funds should be used to cover costs for member/staff attendance. These costs would include transportation, lodging, meals, and reasonable registration fees.

This restriction does not apply to meals/beverages provided at investor conferences held by General Partners in which the Board is a Limited Partner as this is usually the only opportunity Board Members/staff have to meet and interact with other Limited Partners and hear the General Partner discuss the strategy and progress of the fund.

B) A gift from current or potential vendors sent to a Board member/staff at the member's or staff's home or at the Board's office shall be donated to charity if the perceived value of the gift exceeds $50.00. The Board member/staff should immediately notify the Executive Director of such gift, the disposition of such gift, and the Executive Director shall maintain a log of such gifts and their disposition. Such gifts received by the Executive Director shall be immediately reported to the Board Chairperson.

C) A perishable gift from current or potential vendors to a Board member/staff at the Board's office with a perceived value of less than $50.00 shall be shared with all Board staff. The Executive Director shall maintain a log of such gifts and their disposition.

D) A non-perishable gift from current or potential vendors to a Board member/staff at the Board's office with a perceived value of less than $50.00 shall be auctioned and the auction proceeds deposited in the "employee fund." The Executive Director shall maintain a log of such gifts and their disposition.

E) All restaurant dinners attended by Board members\staff and current or potential investment vendors, or lenders shall be "no host."

F) The above meal restriction does not apply to Board members\staff attending meetings held by the General Partner of private equity funds, private real estate funds, or other private funds in which the Board is a Limited Partner.

2. Relationship Provisions

A) Board staff who have a material personal or financial relationship with a current or potential vendor shall recuse themselves from participating in any part of the decision to select, negotiate a contract with, or terminate the services of the vendor and shall not attempt to influence in any way Board members/staff who are part of the decision making process.

B) Board members who have a material personal or financial relationship with a current or potential vendor shall recuse themselves from participating in any part of the decision to select or terminate the services of the vendor and shall not attempt to influence in any way Board members/staff who are part of the decision making process. If the Board, as an entity, has the final authority to make the decision the Board member with the relationship shall, at the Board's public meeting, divulge in general terms the relationship and abstain from voting. Such abstention and the reason for the abstention shall be recorded in the meeting minutes.

C) Board staff who have a material personal or financial relationship with a current or potential lender or borrower shall recuse themselves from participating in any part of the decision to participate or not participate in the loan with the current or potential lender or borrower and shall not attempt to influence in any way Board members/staff who are part of the decision making process.

D) Board members who have a material personal or financial relationship with a current or potential lender or borrower shall recuse themselves from participating in any part of the decision to participate or not participate in the loan with the current or potential lender or borrower and shall not attempt to influence in any way Board members/staff who are part of the decision making process. If the Board, as an entity, has the final authority to make the decision the Board member with the relationship shall, at the Board's public meeting, divulge in general terms the relationship and abstain from voting. Such abstention and the reason for the abstention shall be recorded in the meeting minutes.

E) Board members may vote on INTERCAP loans made to local governments in the jurisdiction in which a Board member resides. Board members represent the entire state on the Board regardless of where they may reside.

3. Time and Facilities Provision

A) Board staff shall not use state time and facilities to conduct private business; which includes the researching of securities for personal portfolios, the trading of securities; or conduct any activities for a revenue generating business.

4. Dual Salaries Provision

A) Board members who are also public employees shall inform the Executive Director if they are in a public employee salaried position that continues to pay their salaries while they are carrying out Board activity for which they are entitled to per diem. Board members in this status shall not receive per diem for the same hours for which their salaries are paid but shall receive travel, meal, and lodging entitlement, and reimbursement for out of pocket expenses as do other Board members. This provision does not apply if the public employee takes accrued leave or compensatory time from the public employee position in order to carry out Board activities.

I have read and understand the Montana Board of Investments Code of Ethics and agree to the best of my ability to comply with all its provisions.

____
Board member/staff Date

Delegated Authority

This Charter delegates authority to Board staff and the Loan Committee as follows:

- Board staff may approve federally-guaranteed loans of any size without concurrence of the Loan Committee.
- Board staff may approve all Coal Tax Trust and INTERCAP loans up to $1.0 million without concurrence of the Loan Committee, provided that the underwriting for such loans complies with all provisions of the relevant loan policies approved by the Board.
- Board staff may authorize enhancement of up to $1.0 million in Montana Facility Finance Authority Act (MFFA) bonds, without concurrence of the Loan Committee.
- Board staff may approve all Coal Tax Trust and INTERCAP loans greater than $1.0 million and up to $5.0 million only with concurrence of the Loan Committee.
- Board staff may authorize enhancement of MFFA bonds greater than $1.0 million and up to $5.0 million, only with concurrence of the Loan Committee. Enhancement of MFFA bonds greater than $5.0 million shall be reviewed by the Loan Committee and recommended to the full Board for final approval.
- All non federally-guaranteed Coal Tax Trust and INTERCAP loans in excess of $5.0 million shall be reviewed and approved by the Loan Committee and recommended to the full Board for final approval.

For purposes of this Charter, loan amounts include only the Board's portion of a participation loan.

Loan Parameters

- Commercial maximum loan size is limited by law to 10.0 percent of the Coal Tax Trust.
- Value-Added maximum loan size is limited by law to 1.0 percent of the Coal Tax Trust.
- Value-Added minimum loan size is set by law at $250,000.
- Maximum amount of Value-Added loans outstanding is limited by law to $70.0 million.
- Infrastructure maximum loan size is limited by law to $16,666 per each job created.
- Infrastructure minimum loan size is set by law at $250,000.
- Maximum amount of Infrastructure loans outstanding is limited by law to $80.0 million.
- Maximum Board participation in Commercial loans is 80.0 percent.
- Board participation in Value-Added loans is set by law at 75.0 percent.
- Infrastructure loans are made directly to local government entities.

Purpose of Committee

The purpose of the Loan Committee is:

- To provide the due diligence required for Coal Tax Trust loans, and enhancement of MFFA bonds in an amount greater than $1.0 million.
- To review and approve Coal Tax Loan Program Policy and Residential Loan Program Policy prior to presentation to the Board.
- Provide guidance regarding pricing of loans.

The Committee is charged with:

- Reviewing and taking appropriate action on all staff recommendations for non federally-guaranteed Coal Tax Trust loans, INTERCAP loans, and the enhancement of MFFA bonds in excess of $1.0 million and up to $5.0 million.
- Reviewing staff recommendations for non federally-guaranteed Coal Tax Trust loans and INTERCAP loans in excess of $5.0 million and enhancement of MFFA bonds in excess of $5.0 million and making a recommendation to the full Board.
- Reviewing staff recommendations to issue additional INTERCAP bonds and recommending to the full Board approval of the recommendation as modified by the Committee.

Committee Membership

The Committee shall consist of at least three Board Members.

Members shall be appointed by the Board Chair who shall notify the Board of all appointments as they are made. The Chair shall appoint for membership to the Committee only those individuals who the Chair believes in his/her judgment are qualified to perform the due diligence duties of the Committee as set forth in this Charter. The Chair shall designate one member of the Committee as its chairperson. The Chair may remove a Committee member at any time and appoint a replacement to complete the removed Member's term, provided the Chair notifies the Board of the removal and the reasons at the time of the removal.

Committee Structure and Operations

Loans greater than $1.0 million up to $5.0 million: Staff shall provide hard copy loan approval recommendations to each Committee Member. Such documents shall include all pertinent information required by Members to fulfill their obligations under this Charter. After reviewing such documents, the Committee may meet in person or telephonically as required to perform their obligations under this Charter.

Committee Members may require that certain loan provisions, loan participation share (when permitted by law), or loan covenants recommended by staff be revised. If two Committee Members do not concur with staff recommendations for loan approval as modified or revised by Members, the staff recommendation shall be forwarded to the full Board at a public meeting in which the lender and the borrower may be present.

Loans and Bond Enhancement Greater than $5.0 million: Staff shall provide hard copy loan approval recommendations to each Committee Member. Such documents shall include all pertinent information required by Members to fulfill their obligations under this Charter. After reviewing such documents, the Committee may meet in person or telephonically as required to perform their obligations under this Charter.

Committee Members may require that certain loan provisions, loan participation share (when permitted by law), or loan covenants recommended by staff be revised. Such revisions shall be incorporated into the staff recommendations and if the staff recommendations with any such revisions are approved by at least two Members, the recommendations shall be forwarded to the full Board for a final decision. If the staff recommendations with any such revisions are not approved by at least two Members, the lender and the borrower may appeal such decision to the full Board at its next regularly scheduled meeting.

Committee Duties and Responsibilities
The following are the general duties and responsibilities of the Committee:

- Review staff recommendations to approve Coal Tax Trust loans, INTERCAP loans, and MFFA bond enhancement greater than $1.0 million and up to $5.0 million and suggest revisions or modifications to the staff recommendations as necessary.
- Concur or not concur with staff recommendations as revised or modified by Committee Members.
- Review staff recommendations to approve Coal Tax Trust loans, INTERCAP loans, and MFFA bond enhancement in excess of $5.0 million and recommend to the full Board modifications to and approval of the staff recommendations.
- Review staff recommendations to approve the issuance of Municipal Finance Consolidation Act bonds and the purchase of tendered bonds that have not been remarketed and recommend to the full Board modifications to and approval of the staff recommendations.
- Provide, when necessary and appropriate, an appeals function for lenders and borrowers whose loan applications have been disapproved by staff.
- Review staff-recommended revisions to the various loan program policies/applications and recommend to the full Board the approval, denial, or modifications of such revisions.
- When necessary and prudent, recommend to the full Board the waiver of certain loan policy provisions, as long as such waiver is limited to the merits of an individual loan application and is considered by the Committee to be in the public interest.
- Advise the Executive Director and the Assistant Investment Officer - in-state investments (AIO) on the setting of interest rates where permitted by law.
- Consult with the Executive Director and the AIO on portfolio risk and loan parameters.
- Advise the Executive Director on the job performance of the AIO.
- Prepare and deliver to the Board, at such time as the Board shall request and as required by this Charter, reports concerning the activities and recommendations of the Committee
- Any other duties or responsibilities expressly delegated to the Committee by the Board from time to time relating to in-state investments.

Reports
A written summary of the actions taken, recommendations and decisions made by the Committee shall be presented to the Board at the next Board meeting following the action/decision.

Resources and Authority of the Committee
The Committee shall have the resources and authority appropriate to discharge its duties and responsibilities.

Purpose of the Audit Committee
To assist the Board in fulfilling its oversight responsibilities for the financial reporting process, the system of internal control, the audit process, and the Board's process for monitoring compliance with laws and regulations and its code of ethical conduct.

Authority
The Audit Committee has authority to conduct or authorize investigations into any matters within its scope of responsibility. It is empowered to:

- Retain outside counsel, accountants, or others to advise the committee or assist in the conduct of an investigation.
- Seek any information it requires from employees — all of whom are directed to cooperate with the committee's requests — or external parties.
- Meet with Board officers, external auditors, or outside counsel, as necessary.

Composition
The Audit Committee will consist of at least three members of the Board. The Board Chair shall serve as an ex-officio member of the Audit Committee. The Board Chair will appoint committee members and the committee chair. Each committee member will be both independent and financially literate, as defined by the Board. At least one member shall have expertise in financial reporting or auditing.

Meetings
The Audit Committee will meet at least twice a year, with authority to convene additional meetings, as circumstances require. All committee members are expected to attend each meeting, in person or via teleconference. The committee will invite members of management, auditors, or others to attend meetings and provide pertinent information as necessary. It will hold private meetings with auditors (see below) and executive sessions. Meeting agendas will be prepared and provided in advance to committee members, along with appropriate briefing materials. Minutes will be prepared.

Responsibilities
The committee will carry out the following responsibilities:

Financial Statements

- Review with management and the external auditors:
  - the results of the audit, including any difficulties encountered.
  - significant accounting and reporting issues, including complex or unusual transactions and highly judgmental areas,
  - recent professional and regulatory pronouncements, and understand their impact on the financial statements,
  - review the annual financial statements, and consider whether they are complete, consistent with information known to committee members, and reflect appropriate accounting principles,
  - review other sections of the annual report before release and consider the accuracy and completeness of the information, and
  - review with management and the external auditors all matters required to be communicated to the committee under generally accepted auditing standards.

- Understand how management develops interim financial information, and the nature and extent of internal and external auditor involvement.
- Review interim financial reports with management and the external auditors, before filing with state agencies and constituent groups, and consider whether they are complete and consistent with the information known to committee members.

Internal Control

- Consider the effectiveness of the Board's internal control systems, including financial reporting and information technology security and control.
- Understand the scope of internal and external auditors' review of internal control over financial reporting, and obtain reports on significant findings and recommendations, together with management's responses.

Internal Audit

- Review with management and the Internal Auditor the charter, plans, activities, staffing and organizational structure of the internal audit activity.
- Ensure there are no unjustified restrictions or limitations, and review and concur in the appointment, replacement or dismissal of the Internal Auditor.
- Review the effectiveness of the internal audit activity, including compliance with The Institute of Internal Auditors' *Standards for the Professional Practice of Internal Auditing.*
- On a regular basis, meet separately with the Internal Auditor to discuss any matters that the committee or internal audit believes should be discussed privately.

External Audits

- Review any external auditors' proposed audit scope and approach, including coordination of audit effort with internal audit.
- Review the performance of the external auditors.
- Review and confirm the independence of the external auditors.
- On a regular basis, meet separately with the external auditors to discuss any matters that the committee or auditors believe should be discussed privately.

Compliance

- Review the effectiveness of the system for monitoring compliance with laws and regulations and the results of management's investigation and follow-up (including disciplinary action) of any instances of noncompliance.
- Review the findings of any examinations by regulatory agencies, and any auditor observations.
- Review the process for communicating the code of ethics to Board personnel, and for monitoring compliance therewith.
- Obtain regular updates from management and Board legal counsel regarding compliance matters.

Reporting Responsibilities

- Regularly report to the Board about committee activities, issues, and related recommendations.
- Provide an open avenue of communication between internal audit, the external auditors, and the Board.
- Report annually to the Board's constituent groups, describing the committee's composition, responsibilities and how they were discharged, and any other information required by rule.
- Review any other reports the Board issues that relate to committee responsibilities.

Other Responsibilities

- Perform other activities related to this charter as requested by the Board.
- Institute and oversee special investigations as needed.
- Review and assess the adequacy of the committee charter annually, requesting board approval for proposed changes.
- Confirm annually that all responsibilities outlined in this charter have been carried out.
- Evaluate the committee's and individual members' performance on a regular basis.

Purpose of Committee

The purpose of the Human Resources Committee is to discharge the Board's responsibilities relating to personnel matters of all Board staff and compensation of the Board's exempt staff.

Committee Membership

The Committee shall consist of at least three Board Members.

Members shall be appointed by the Board Chair who shall notify the Board of all appointments as they are made. The Chair shall appoint for membership to the Committee only those individuals who the Chair believes in his/her judgment are qualified to perform the duties of the Committee as set forth in this charter. The Chair may remove a Committee member at any time and appoint a replacement to complete the removed member's term, provided the Chair notifies the Board of the removal and the reasons at the time of the removal.

Committee Structure and Operations

The Chair shall designate one member of the Committee as its chairperson. The Committee shall meet in person or telephonically as it deems necessary or appropriate, and at least two times per year, at a place and time determined by the Committee chairperson

The Committee may invite such staff to its meetings as it may deem desirable or appropriate, consistent with the maintenance of the confidentiality of performance and compensation discussions. The Board's Executive Director ("Director") should not attend any meeting where the Director performance or compensation is discussed, unless specifically invited by the Committee.

If one member of the Committee cannot attend a meeting, the remaining two members of the Committee, acting unanimously, shall have the power to take any action necessary or convenient to the efficient discharge of its responsibilities. No action of the Committee shall be valid unless approved by at least two members of the Committee.

Committee Duties and Responsibilities

The following are the general duties and responsibilities of the Committee:

- In consultation with the Director and Chief Investment Officer ("CIO"), establish and periodically review the general compensation policies applicable to the Board's employees, and oversee the development and implementation of compensation programs. This activity includes the commissioning of peer salary surveys, the review of such surveys, and the establishing of pay ranges based on the surveys.

- Review and recommend the compensation and incentive programs, and modifications and amendments thereto, applicable to the exempt Board staff and other employees of the Board whose compensation has a component that includes the relationship of the Board's investment performance to compensation and the basis for calculating such compensation. Discharge any responsibilities imposed on the Committee by any of these programs.

- Review and recommend the specific levels of compensation, including salaries, incentives, benefits and perquisites, of the Director, CIO and the other exempt Board staff and of other staff as the Board may have authority over with respect to compensation.

- Review and approve goals and objectives relevant to the compensation, including incentive compensation, of the Director, CIO, and other exempt staff. In setting long-term goals and objectives relevant to the long-term incentive component of those goals and objectives, the Committee shall consider, among other factors, the Board's investment performance and return relative to investment performance at comparable investment boards, the awards given to the CIO and investment staff in past years and the provisions of the Board's compensation plan for exempt staff.

- Oversee the Director in developing Job Profiles and performance criteria for all exempt staff.

- Evaluate and advise the Board concerning the performance of the Director, the CIO, and other exempt staff against established goals and objectives.

- Recommend the Director's, CIO's, and exempt staff compensation level for the coming year based on this evaluation and recommend, as appropriate, a course of action to remedy deficiencies observed or improve performance.

- Review and advise the Board concerning and, if deemed appropriate, retain consultants to advise the Committee regarding industry compensation practices and trends in order to assess the adequacy and competitiveness of the Board's compensation programs. Retain as necessary consultants to advise on other personnel issues.

- Prepare and deliver to the Board, at such time as the Board shall request, reports concerning the activities and recommendations of the Committee and disclose the compensation policies applicable to the Director, CIO, and exempt Board staff. Discuss the relationship of the Board's investment performance to exempt staff compensation and the basis for the compensation awarded during such period.

- Oversee the Director in development and maintenance of a succession plan for exempt staff and other key employees, and report to the Board the Committee's recommendations regarding succession.

- In consultation with the Director, oversee regulatory compliance with respect to compensation matters.

- Consider and act on written employee appeals and grievances when the Director is unable to resolve differences with exempt employees.

- Prepare and issue the evaluations and reports required under "Committee Reports" below.

- Any other duties or responsibilities expressly delegated to the Committee by the Board from time to time relating to exempt staff performance and compensation.

Committee Reports

The Committee shall produce the following reports and provide them to the Board.

- An annual Report of the Human Resources Committee on exempt staff compensation.

- An annual performance evaluation of the Committee comparing the performance of the Committee with the requirements of this charter. The performance evaluation should also recommend to the Board any changes to this charter deemed necessary or desirable by the Committee. The performance evaluation by the Committee shall be conducted in such manner as the Committee deems appropriate. The report to the Board may take the form of an oral report by the chairperson of the Committee or any other member of the Committee designated by the Committee to make this report.

- A written summary of the actions taken, recommendations and decisions made by the Committee, which shall be presented to the Board at the next Board meeting following the action/decision.

Resources and Authority of the Committee

The Committee shall have the resources and authority appropriate to discharge its duties and responsibilities, including the authority to select, retain, terminate, and approve the fees and other retention terms of special legal counsel or other experts or consultants, as it deems appropriate, subject to state procurement rules. With respect to compensation consultants retained to assist in the evaluation of staff this authority shall be vested solely in the Committee.

I. Principles

1. The Board of Investments manages the assets entrusted to it "in accordance with the prudent expert principle" which requires that the Board act "with the care, skill, prudence, and diligence, under the circumstances then prevailing, that a prudent person acting in a like capacity with the same resources and familiar with like matters exercises in the conduct of an enterprise of a like character and with like aims." Montana Code Sec. 17-6-201. See also, Montana Constitution, Art. VIII, Sec. 13.

2. Claims under state and federal securities laws arising out of losses on securities under the Board's management are assets subject to the Board's fiduciary duty of prudent management. Accordingly, the Board should take reasonable steps to identify and recover on such claims. Such steps may include:

- Participating as passive class member in class actions brought by others, and filing a proof of claim when action is settled/resolved.
- Enhanced participation as class member in class actions brought and led by others, by considering objections or comments on settlements
- Active participation in class action litigation, including serving as a "lead plaintiff" or "co-lead plaintiff" pursuant to the Private Securities Litigation Reform Act
- Separate litigation on behalf of the Board

3. The Board will delegate to qualified service providers the responsibility to take steps to identify, analyze, pursue and collect upon securities law claims. The duties of each service provider shall be clearly articulated as a matter of contract and the Board shall adopt prudent, documented procedures to monitor the implementation of its policies.

II. Policies

1. The Board shall take reasonable, cost-effective steps to identify, pursue and collect upon claims under state and federal securities laws for losses suffered by the Board on its investments because of alleged or proven violations of securities laws.

2. A proof of claim should be filed on behalf of the Board in connection with every securities class action litigation settlement or judgment in which the Board is a member of the plaintiff class.

3. Because pursuing securities litigation as an active plaintiff, either by separate lawsuit or by serving as a lead plaintiff in a class action, imposes on the Board a separate fiduciary responsibility to other class members (in the case of lead plaintiff status), administrative, legal and other burdens and possibly out-of-pocket expense, the Board will not consider separate litigation or lead plaintiff status with respect to any claim unless the losses suffered with respect to the particular securities are at least $1,000,000. When losses exceed that amount, the Board may commence separate litigation or apply for lead or co-lead plaintiff status, after receiving advice from the Board's General Counsel that it is in the interest of the Board to do so. The criteria to be considered in deciding whether to commence separate litigation or apply for lead plaintiff status are set forth on Attachment 1.

4. If the Board has suffered losses of $500,000 or more, and the Board is not pursuing separate litigation or acting as lead or co-lead plaintiff in a class action, the Board may play an enhanced role, which may include review of the terms of any settlement, including applications for legal fees, to determine if the Board should file a comment or objection with respect to the settlement, or opt out of the class. The criteria for deciding whether to opt out are set forth on Attachment 1. The Board is authorized to direct the filing of a comment or objection

5. The Board will act only as a passive class member with respect to any claim in which the losses suffered are less than $500,000. Proofs of claim will be filed on behalf of the Board upon a settlement or final judgment awarding damages in relevant class actions.

6. The Board delegates to its Audit Committee the decision to seek lead or co-lead plaintiff status or to play an enhanced role in a class action under Paragraphs 3 and 4.

7. The Executive Director, the Chief Investment Officer, the Board's General Legal Counsel, and the Board's Investment Consultant shall receive reports from the Monitoring Legal Firm, regarding the status of all securities class action litigation matters in which the Board is or could be a member. The Executive Director shall receive such reports at least monthly and upon each filing of proofs of claim.

III. Roles and Authority

1. Board Role and Authority:

- Review staff reports regarding securities litigation matters
- Periodically review and, as appropriate, modify this Policy
- Establish, periodically review and, as appropriate, modify Protocols for implementation of this Policy
- Select a securities class action "Monitoring Firm" to identify and evaluate potential claims and oversee the process for selecting such firm
- Approve, modify or terminate agreements with service providers responsible for implementation of this Policy

2. Audit Committee Role and Authority:

- Authorize commencement of separate litigation or filing of motion for lead plaintiff or co-lead plaintiff status or support for another's application for lead plaintiff status, consistent with this Policy
- Approve settlement of separate litigation or class action in which the Board is lead plaintiff or co-lead plaintiff, consistent with Board Policy
- Authorize opting out of a class settlement, consistent with this Policy
- Authorize filing of objections and comments on settlements, consistent with Board Policy.
- Receive and review staff reports on the status of matters other than passive claim filings.

Staff Role and Authority

- Circulate to Board members, Board General Legal Counsel, and Investment Consultant the reports from the Custodian and Monitoring Firm showing status of all securities litigation matters in which the Board may have an interest (e.g. date case filed, date of settlement, due date for claim filing, date Board's claim filed, date of recovery).
- Approve, circulate, and review responses to requests for proposals for Monitoring Firm services for and make recommendations to Board regarding selection
- Monitor, with assistance from the Board's General Counsel, performance of the Monitoring firm and report deficiencies to the Board
- As appropriate, recommend to the Board modifications to this Policy and Implementation Protocols

3. *Board General Counsel Role and Authority:*

- Assist in the preparation of Requests for Proposals for a Monitoring Firm, review responses and make recommendation to Board members and staff regarding candidates.
- Assist in negotiations of terms and agreements with Monitoring Firm, with assistance from the Board's Investment Consultant.
- Review, prior to submission to the Audit Committee, all recommendations from the Monitoring Firm regarding whether to commence separate litigation or seek lead plaintiff or co-lead plaintiff designation, or to opt out of or object to class settlements.
- Review, prior to submission to the Audit Committee, all recommendations from Monitoring Firm regarding proposed settlements of separate actions brought by the Board or class actions in which the Board is lead or co-lead plaintiff
- Review, prior to submission to the Audit Committee, all recommendations from Monitoring Firm regarding whether to file objections to or comments upon settlements.
- Supervise and monitor outsides Legal Counsel's conduct of litigation when Board pursues separate litigation or acts as lead or co-lead plaintiff

4. *Custodian Role and Authority*

- Maintain and communicate data necessary to identify the Board's securities holdings and transactions in order to determine if the Board is a class member and calculate losses
- Collect and distribute to the Monitoring Firm all notices regarding the commencement, class certification and settlement of class action lawsuits in which the Board has an interest as an actual or potential class member
- Collect, record on the Board's custody statements and deposit into appropriate accounts for investment, proceeds from the Board's claims

5. *Custodian/Class Action Role and Authority*

- Establish and implement procedures to identify all securities class actions filed by others in which the Board is or may be a class member

- Collect and distribute to Monitoring all official notices of pendency of class actions in which the Board, according to this Policy, may consider applying for lead plaintiff status or pursuing separate litigation
- Timely file accurate proofs of claim on behalf of the Board in all class actions in which the Board may participate as class member and notify the Monitoring Firm.
- Provide necessary custody data to the Monitoring Firm.

6. Monitoring Firm Role and Authority

- Ensure by written communication that the Custodian has filed the appropriate documents for Board participation in pending class action litigation.
- Identify circumstances in which the Board may have incurred investment losses in excess of the minimum threshold which give rise to potentially meritorious claims for the Board which are not yet the subject of litigation.
- Evaluate claims over $1,000,000 and recommend whether the Board should pursue separate litigation or lead or co-lead plaintiff designation
- Evaluate settlements of actions in which Board is not lead plaintiff where losses exceed $500,000 and recommend whether Board should object to, comment upon or opt out of settlement
- File objections to and comments upon settlements as authorized

Implementation

These Policies shall be implemented in accordance with a written statement of procedures to be adopted by the Board incorporated as Attachment 1.

ATTACHMENT 1

Considerations Relevant to Deciding Whether to Pursue Separate Litigation or Lead or Co-Lead Plaintiff Status

Will the Board add value by volunteering to lead or co-lead litigation in view of the fiduciary responsibilities (as class action lead or co-lead plaintiff), administrative burdens and costs that are associated with separate litigation and acting as lead or co-lead plaintiff?

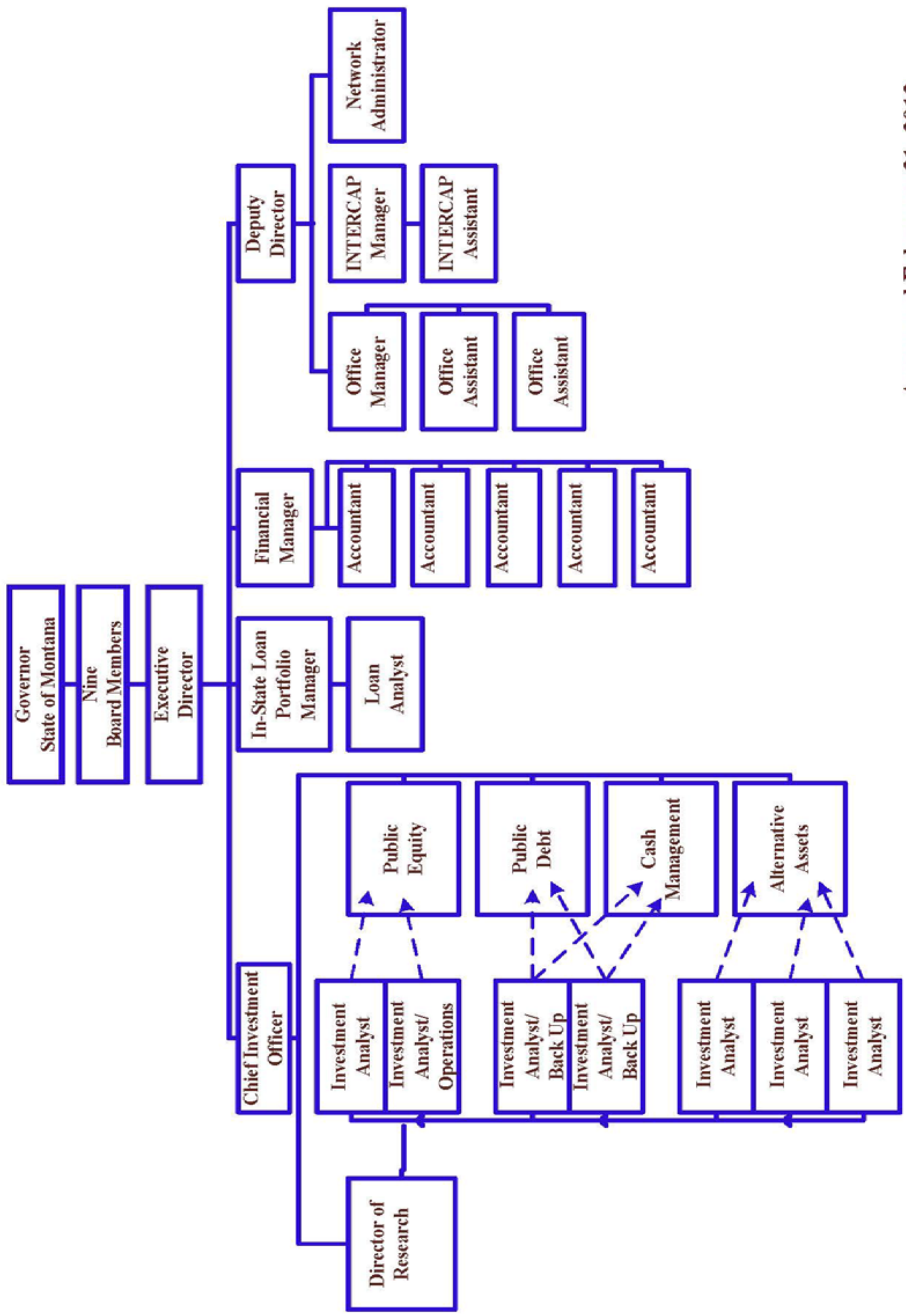
1. Size of the Board's damages measured by standards applicable to securities litigation
2. Strength of claims, including evaluation of defenses
3. Special circumstances which render the Board's claims different from, stronger or weaker than claims of typical class members such that it would be in the interest of the Board to act as lead or co-lead plaintiff
4. Venue of litigation
5. Resources available to pay a significant judgment (e.g. financial condition of potential defendants, availability of insurance, potential for bankruptcy)
6. Qualifications of other lead plaintiff candidates and their counsel, and likelihood that the Board would be selected a lead or co-lead plaintiff
7. Relation of claims to other corporate governance issues of special interest to the Board, and impact on other Board holdings
8. Potential for non-monetary remedies of special importance to the Board which other class members/lead plaintiffs may not pursue
9. Costs to the Board of separate litigation/lead or co-lead plaintiff status such as discovery, legal fees and Board staff time and resources needed to monitor litigation more actively
10. Potential exposure to counterclaims/court costs, and willingness of litigation counsel to indemnify the Board against such exposure.

Considerations Relevant to Deciding Whether to Opt Out, Object to or Comment on Settlements

Is the Board receiving fair value for its claims? Does the likely gain to the Board to be achieved by objecting to or commenting on a settlement outweigh the costs of engaging counsel to file the objection/comment? Should the Board risk losing the certain recovery the settlement provides in order to opt out of the class and pursue separate claims independently?

1. Financial value of settlement to class as a whole and the Board in particular
2. Non-monetary (e.g. corporate governance) aspects of settlement, or the lack thereof
3. Amount of attorneys fees sought and merits of attorneys fee claim
4. Expense and risk (including value which might be lost if settlement is disrupted or rejected) associated with opting out, commenting or objecting in relation to expected benefits of doing so.

Montana Board of Investment Functional Organization Chart



Approved February 21, 2012

WHEREAS, the Montana Board of Investments (Board) maintains several accounts with investment firms for the purchase and sale of stocks, bonds, covered options, purchase options (stock open indicies, interest rate options, foreign currency options), repurchase agreements, reverse repurchase agreements, and other securities and property, which accounts are described on Appendix "A" attached hereto and incorporated herein; and

WHEREAS, the Board desires to provide a procedure for the future designation or removal of Board staff for purposes of acting on behalf of the Board to deal with investment firms in connection with such accounts; and

WHEREAS, the Board desires to provide flexibility for future changes in accounts, investment firms and in Board staff with authority to act on behalf of the Board relative to such accounts; and

WHEREAS, the Board adopted Resolution No. 199 on October 31, 2002 for the foregoing purposes.

NOW, THEREFORE:

RESOLVED, that the Board intends that this resolution supersedes in every respect and replaces in its entirety Resolution No. 199

RESOLVED, that the Board of Investments hereby designates its Executive Director as agent of the Board to deal with investments firms in connection with Board accounts with such firms; and that the investment firms are hereby authorized to deal with the Executive Director or the Executive Director's designated staff as agents of the Board; to accept all orders for purchases and sales and all instructions given by any of them on behalf of the Board as and for the action of the Board without further inquiry as to their authority; to receive any funds, securities or property for the account of the Board; to sell, assign, transfer or deliver either in bearer form, in street certificates or in such names as said persons or any of them shall direct, any funds, securities or other property held for the account of the Board, to said persons or any of them or as they or any of them shall in writing, or verbally with subsequent confirmation in writing, order; and to send or communicate all confirmation, notices, demands and other communications to them or any of them and to the Attention of the Board of Investments, P.O. Box 200126, Helena, MT 59620-0126.

FURTHER RESOLVED, that the establishment and maintenance of all of the accounts, hereinafter described in Appendix "A," and the actions of the Executive Director or the Executive Director's designated staff members shown in Appendix "A," acting on behalf of the Board dealing with investment firms related to said accounts since January 21, 1993, are hereby approved and ratified.

FURTHER RESOLVED, that the Board hereby authorizes its Executive Director to close any of the accounts listed in Appendix "A", to open new accounts, to designate additional staff members to act on behalf of the Board for the purpose of dealing with investment firms regarding any account, and to remove the authority of any of the named staff members or other staff members designated by him/her to act on behalf of the Board for purposes of dealing with investment firms regarding any account.

FURTHER RESOLVED, that an investment firm may act in reliance upon the foregoing resolution and subsequent designations by the Executive Director of staff members who may act on behalf of the

Board until receipt of written notice that the authority of the designated staff member to act on behalf of the Board has been terminated.

FURTHER RESOLVED, that the Executive Director shall annually, on or around the regularly scheduled October Board meeting, provide a report to the Board showing the staff members and the accounts added to or deleted from Appendix A, which information shall include the date on which the addition or deletion occurred.

Dated and approved this 6th day of November 2007.

ATTEST

By: ____________________________
Chairman

WHEREAS, the Montana Board of Investments (Board) has delegated certain critical authority and duties to its Executive Director that must be exercised and performed in the absence of the Executive Director; and

WHEREAS, the Executive Director may be incapacitated or temporarily absent from the office under circumstances that render the Executive Director unavailable to exercise such authority and perform such duties,

NOW, THEREFORE:

RESOLVED, that the Executive Director or the Deputy Director shall notify the Board Chairperson immediately at any time the Executive Director, due to incapacity or a temporary absence from the office, is unable to perform his/her duties; and

FURTHER RESOLVED, that "incapacity" means the occurrence of a mental or physical disability rendering the Executive Director incapable of exercising his/her authority and carrying out his/her duties; and

FURTHER RESOLVED, that during an incapacity of the Executive Director, the Deputy Director is hereby designated Acting Executive Director; and

FURTHER RESOLVED, that the Executive Director may, after notifying the Board Chairperson, delegate his/her executive authority to the Deputy Director to serve as Acting Executive Director during periods of official travel or authorized leave away from the Board's office, if in the judgment of the Executive Director, such delegation would be in the best interest of the Board; and

FURTHER RESOLVED, that during any period that the Deputy Director is not available to assume the role of Acting Executive Director pursuant to the provisions of this Resolution, the Chief Investment Officer shall serve as Acting Executive Director; and

FURTHER RESOLVED, that the Acting Executive Director shall operate only within the authority and parameters established in the Board's Governance Policy.

Dated and approved this 6th day of November 2007.

ATTEST

By: ______________________________

Chairman

Be It Resolved by the Montana Board of Investments (the "Board") as follows:

Section 1. Recitals.

Section 1.01. History, Authorization of Unified Investment Program and the Board. Article VIII, Section 13 of the Montana Constitution (the "Constitution") directs the legislature to provide for a unified investment program for public funds and public retirement system and state compensation insurance fund assets. The Legislature, pursuant to Title 17, Chapter 6, Part 21, Montana Code Annotated (the "Unified Investment Program Act"), has created and directed the Board to administer the unified investment program mandated by the Constitution. The Board has the primary authority to invest state funds, and to determine the types of investments to be made, subject to the restrictions of the Constitution and the Unified Investment Program Act.

Section 1.02. History, Authorization of Montana Economic Development Board and Municipal Finance Consolidation Act Bonds. The 1983 Legislature created the Montana Economic Development Authority Board ("MEDB"), to among other things issue notes and bonds to finance loans to and the purchase of bonds and notes of Montana governmental units, to establish or replenish reserves securing the payments of its bonds and notes, and to finance all expenditures incident to and necessary or convenient to carry out the provisions of Title 17, Chapter 5, Part 16, Montana Code Annotated (the "Municipal Finance Consolidation Act" or "MFCA Act"). As set forth in Section 17-5-1602(2)(b) of the Municipal Finance Consolidation Act, the State's goal was to foster the provisions of efficient capital markets, to reduce costs of borrowing and, among other things, to provide additional security for the payment of bonds and notes held by investors. In conjunction with issuing its Municipal Finance Consolidation Act Bonds in 1985, the MEDB adopted Resolution No. 68 on July 24, 1985, establishing a Municipal Finance Consolidation Act Reserve Fund (the "Reserve Fund") to secure bonds or obligations issued under the Municipal Finance Consolidation Act ("MFCA Bonds"). Pursuant to a Resolution, the MEDB and the Board entered into a Security Agreement whereby the Board agreed to make an interest bearing loan to the MEDB to restore any deficiency in the Reserve Fund and also agreed, for a fee, to purchase MFCA Bonds tendered for purchase and not remarketed. Each series of MFCA Bonds credit enhanced by the Board is approved by resolution by the Board. The Board has never been called upon to make any loans or purchase any of these Bonds.

Section 1.03. Authorization for the Board to Issue Municipal Finance Consolidation Act Bonds. Pursuant to Chapter 581, Montana Session Laws of 1987, the Board assumed the role of the MEDB with respect to the issuance of the Montana Finance Consolidation Act Bonds and other bond programs authorized by the State. The Board issued its first series of Intermediate Term Capital Program (INTERCAP) Municipal Finance Consolidation Act Bonds in 1987 (the "Series 1987 INTERCAP Bonds"). The Series 1987 INTERCAP Bonds and all series of INTERCAP Bonds subsequently issued by the Board have also been secured by the Reserve Fund. In the Resolution authorizing and approving the issuance of the Series 1987 INTERCAP Bonds, the Board approved the Indenture of Trust pursuant to which the Series 1987 INTERCAP Bonds were to be issued and secured (the "1987 Trust Indenture"); agreed to make an interest bearing loan to the Reserve Fund and agreed, for a fee, to purchase any Series 1987 INTERCAP Bonds tendered for repurchase that were not remarketed (the "Authorizing Resolution"). In 1991, the INTERCAP program was expanded, requiring a new Trust Indenture (the "1991 Trust Indenture"), securing the INTERCAP Bonds, that was approved by the Board. Each subsequent series of INTERCAP Bonds issued by the Board have been approved by an Authorizing Resolution and a Supplemental Indenture. The Authorizing Resolutions, the 1991 Trust Indenture and Supplemental Indenture are collectively referred to as the "Bond Documents." The Board has never been called on to make a loan to the Reserve Fund or purchase tendered MFCA Bonds under the Bond Documents.

Section 1.04. History, Authorizations, Montana Facility Finance Authority Bonds. Pursuant to Chapter 703, Montana Session Laws of 1987, now codified in Montana Code Annotated, Title 90, Chapter 7, Parts 1, 2 and 3, as amended (the "MFFA Act"), the Montana Health Facility Finance Authority, now the Montana Facility Finance Authority (the "MFFA") is authorized to issue revenue bonds to finance nonprofit hospitals, prelease centers and other nonprofit health-care providers or entities. The MFFA has created a capital reserve account to provide additional security ("Capital Reserve Account") for the Bonds it issues under the MFFA Act ("MFFA Bonds"). Pursuant to the MFFA Act, the Board is authorized to loan money to the MFFA for deposit in its capital reserve account and to purchase its bonds and notes. Pursuant to resolutions of the Board relating to each series of MFFA Bonds for which credit enhancement is provided, the Board is authorized to enter into an agreement with the MFFA whereby the Board agrees to make an interest bearing loan to the Capital Reserve Account to restore any deficiency (the "MFFA Capital Reserve Account Agreement"). For each series of MFFA Bonds credit enhanced by the Board, the Board has by Resolution approved entering into additional Capital Reserve Account Agreements. The Board has never been called upon to make a loan to the MFFA Capital Reserve Account. To date, the Board has not entered into any agreements to purchase tendered MFFA Bonds.

Section 1.05. Previous Credit Enhancement Policies. The Board adopted a "Credit Enhancement Policy" on February 17, 2006.

Section 2. Findings and Determinations of the Board.

Section 2.01. The Board desires to continue to enhance the marketability of bonds and notes issued under both the MFCA Act and the MFFA Act and to assist the Board and the MFFA in obtaining the lowest possible interest rates on loans to eligible governmental units and non-profit corporations providing needed and essential services and facilities to the public.

Section 2.02. The Board adopts this resolution to codify and clarify the circumstances under which the Board has and will continue to provide credit enhancement; to authorize its Executive Director to honor and fulfill the Board's obligations under the Bond Documents (and Capital Reserve Account Agreement); and to make this resolution a part of the Board Governance Policy.

Section 2.03. Resolution No. 68 adopted by the Montana Economic Development Board on July 24, 1985, establishing the Reserve Fund to secure bonds or obligations issued by the Board [is attached hereto as Schedule 1 and incorporated by reference.]

Section. 3. Decision to Provide Credit Enhancement; source of Credit Enhancement.

Section 3.01. The decision to provide credit enhancement as authorized by the MFFA Act and the MFCA Act shall be made by the Board pursuant to a duly authorized resolution of the Board related to each series of Bonds to be issued.

Section 3.02. The Board's policy shall be to provide credit enhancement when it is prudent to do so and in the Board's judgment would result in a lower interest rate to the borrowers under the MFCA Act and MFFA Act than could be otherwise obtained.

Section 3.03. The funds in the Unified Investment Program from which the Board's Credit Enhancement obligations could be satisfied include, but are not limited to: the Permanent Fund sub-fund of the Coal Tax Trust, the Short Term Investment Pool, and the Treasurer's Fund.

Section 4. Duties of the Executive Director.

Section 4.01. Loans. When required under the terms of the Bond Documents, the Executive Director of the Board is authorized to loan funds to the Board Reserve Fund and the MFFA Capital Reserve Account pursuant to the requirements of the Bond Documents.

Section 4.02. Purchase of Bonds. When required to do so under the Bond Documents, the Executive Director is authorized to purchase Bonds pursuant to the requirements of the Bond Documents.

Section 4.03. Use of Funds. The Executive Director is authorized to determine which legally available funds to use for the above purposes.

Section 4.04. Notification of Board. If the Executive Director makes a loan to the Reserve Funds, Capital Reserve Account or purchases bonds pursuant to the Bond Documents, he/she shall notify Board members via e-mail within three (3) business days of such action and provide a full report to the Board at its next regularly scheduled meeting specifying the reasons for such action, the dollar amount, the terms, and the funding source for the loan or bond purchase.

Section 5. Effective Date; No Repeals Policy.

Section 5.01. This resolution shall become effective upon passage by the Board and execution and certification by the Chairman of the Board. This Resolution shall supersede in every respect and replace in its entirety the "Credit Enhancement Policy" adopted by the Board on February 17, 2006.

Section 5.02. This resolution is not intended and shall not be construed to modify any commitment, obligations or agreements, the Board has made pursuant to any duly authorized resolution or agreement relating to Bonds issued under the MFCA Act or the MFFA Act.

Section 5.03. The policies and procedures established by resolution become an integral part of the Board's Governance Policy.

Dated and approved this 14th day of May 2008.

ATTEST

By: ______________________________
Chairman

CERTIFICATE OF MINUTES RELATING TO
RESOLUTION NO. 068

Issuer: Montana Economic Development Board

Kind, date, time and place of meeting: A board meeting held on July 24, 1985, at 8:00 o'clock a.m. at Jorgenson's Holiday Motel in Helena, Montana.

Members present: Pat McKittrick, Jack Schotte, Yvonne Snider, Karen Locke, John Orth, and Jerry Sullivan.

Members absent: Steve Brown.

Documents attached:
Minutes of said meeting (pages):

RESOLUTION NO. 068

RESOLUTION OF THE MONTANA ECONOMIC DEVELOPMENT BOARD ESTABLISHING A MUNICIPAL FINANCE CONSOLIDATION ACT RESERVE FUND

I, the undersigned, being the fully qualified and acting recording officer of the public body issuing the obligations referred to in the title of this certificate, certify that the documents attached hereto, as described above, have been carefully compared with the original records of the public body in my legal custody, from which they have been transcribed; that the documents are a correct and complete transcript of the minutes of a meeting of the governing body at the meeting, insofar as they relate to the obligations; and that the meeting was duly held by the governing body at the time and place and was attended throughout by the members indicated above, pursuant to call and notice of such meeting given as required by law.

WITNESS my hand officially as such recording officer this 24 day of July, 1985.

John Orth

John Orth
Secretary

RESOLUTION 068

Member Jack Schutte introduced the following resolution and moved its adoption:

RESOLUTION OF THE MONTANA ECONOMIC DEVELOPMENT BOARD ESTABLISHING A MUNICIPAL FINANCE CONSOLIDATION ACT RESERVE FUND

BE IT RESOLVED by The Montana Economic Development Board (the Board) as follows:

1. Recitals. The Board is authorized and directed by Title 17, Chapter 5, Part 15, Montana Code Annotated, as amended (the Act) to create funds and accounts necessary to implement the Act, including a municipal consolidation finance act reserve fund and other funds and accounts; to issue and sell bonds and notes for the purpose of financing programs thereunder; and to secure the bonds and notes pursuant to an indenture of trust and resolution. Pursuant to the Act, the Board has undertaken a Cash Anticipation Financing Program to acquire Notes issued by local government units (the Borrowers) to finance their cash flow requirements. To provide funds to acquire the Notes, the Board has authorized the execution of an Indenture of Trust (the Indenture) between the Board and First Trust Company of Montana (the Trustee) pursuant to which the Board is authorized to issue and sell its Bonds. In order to provide for the segregation of and accounting for certain of its revenues and funds and in furtherance of the Act, the Board hereby determines it necessary and appropriate to adopt this resolution (the Resolution).

2. Definitions. Capitalized terms used but not defined herein shall have the meanings assigned them in the Indenture.

3. Municipal Finance Consolidation Act Reserve Fund. The Board hereby creates and establishes the Municipal Finance Consolidation Act Reserve Fund and authorizes the creation of accounts therein for the purpose of securing one or more series of bonds or obligations issued by the Board. Accounts may be created pursuant to indentures or resolutions with respect to series of bonds or obligations secured thereby and may be held by a trust and invested pursuant to the provisions of such indentures or resolutions. A reserve fund requirement may be established with respect to each account. So long as the reserve fund requirement of each

account is maintained, all investment income therefrom may be transferred to other accounts and funds of the Board as provided in the indenture and resolution securing the bonds.

4. Other Funds and Accounts. Nothing contained in this Resolution shall be deemed to limit the authority of the Board to create other funds and accounts pursuant to the Act in addition to the Municipal Finance Consolidation Act Reserve Fund.

Chairman

MONTANA BOARD OF INVESTMENTS ADMINISTRATIVE RULES		
ADMINISTRATIVE RULES		
Rule No.	**Rule Title**	**Effective Date**
Municipal Finance Consolidation Program		
8.97.715	Definitions	3/22/1996
8.97.716	Scope of Subchapter 7	10/16/1992
8.97.717	Description of Municipal Finance Consolidation Act Programs	3/22/1996
8.97.718	Application Procedure	3/22/1996
8.97.719	Criteria For Evaluation of all Program Applications	3/22/1996
8.97.720	Agreements	3/22/1996
8.97.722	General Term, Interest Rates, Fees and Charges	3/22/1996
8.97.724	Closing Requirements	3/22/1996
Montana Capital Companies		
8.97.801	Purpose	12/16/1983
8.97.802	Definitions	3/16/1990
8.97.803	Application Procedure to Become a "Certified" Montana Capital	3/16/1990
8.97.804	Application Procedure to Become a "Qualified" Montana Capital	12/11/1987
8.97.805	Completed Application Date	12/11/1987
8.97.806	Amendment of Application	12/16/1983
8.97.807	Allocation of Tax Credits	3/16/1990
8.97.808	Quarterly Reporting of Qualified Investments	12/16/1983
8.97.809	Reservation of Tax Credits	12/11/1987
Organizational Rules		
8.97.1101	Organizational Rule	2/11/2000
Citizen Participation Rules and Procedural Rules		
8.97.1201	Citizen Participation Rules	2/11/2000
8.97.1202	Procedural Rules	2/11/2000
General Requirements for All Investments in Mortgages and Loans		
8.97.1301	Definitions	2/11/2000
8.97.1308	Authorized Loan Types	2/11/2000
8.97.1309	Authorized Applicants	2/11/2000
8.97.1310	Loan Program Policies	2/11/2000
Additional Requirements for Commercial, Multi-Family Federally Guaranteed Loans & Economic Development Linked Deposits		
8.97.1502	Interest Rate Reduction for Loans Funded from the Coal Tax Trust	2/11/2000
Bonds & Notes of Board, Loan Loss Reserve Account, Purchase of Montana Capital Company Debentures		
8.97.1601	Bonds and Notes of Board	10/14/1988
Economic Development Bond Program		
8.97.1701	Definitions	5/26/1989
8.97.1702	Description of Economic Development Bond Programs	5/26/1989
8.97.1703	Confidentiality of Information	5/26/1989
8.97.1704	Allocation of Capacity	5/26/1989
8.97.1705	False or Misleading Statements	5/26/1989
8.97.1706	Application and Financing Fees, Costs and Other Charges	5/26/1989
8.97.1707	Application Procedures and Public Hearing Requirements	5/26/1989
8.97.1708	Public Interest Criteria	5/26/1989
8.97.1709	Thirty Day Review Requirement	5/26/1989
Moral Obligation Economic Development Bond Program		
8.97.1801	Description of MOBP Program	5/26/1989
8.97.1802	Eligibility Requirements of MOBP Program	5/26/1989
8.97.1803	Criteria For Evaluating Applications for Project Financing Under the MOBP Program	5/26/1989
8.97.1804	Interest Rates	5/26/1989
8.97.1805	Closing of Loans	5/26/1989
Stand Alone Economic Development Bond Program		
8.97.1901	Description of the SABP Program	5/26/1989
8.97.1902	Eligibility Requirements of SABP Program	5/26/1989
8.97.1903	Criteria For Evaluating Applications for Project Financing Under the SABP Program	5/26/1989

MONTANA BOARD OF INVESTMENTS ADMINISTRATIVE RULES		
ADMINISTRATIVE RULES		
Rule No.	**Rule Title**	**Effective Date**
Conservation Reserve Payment Enhancement Program		
8.97.2001	Definitions	12/22/1989
8.97.2002	Description and Goals of the State CRP Enhancement Program	12/22/1989
8.97.2003	General State CRP Program Requirements	12/22/1989
8.97.2004	Eligibility Criteria For State CRP Program	12/22/1989
8.97.2005	Holdback For Esabishment of Cover Emergency Use of Cover	12/22/1989
8.97.2006	Permissible Uses of Loan Funds	12/22/1989
8.97.2007	Application Procedures for State CRP Program - Loan Requirements for the Application/Borrower	12/22/1989
8.97.2008	Application Procedures for CRP Program - Loan Agreement, Closing, Funding	12/22/1989
8.97.2009	Determination of Loan Amount	12/22/1989
Rules Implementing The Montana Enironmental Policy Act		
8.97.2101	Adoption of MEPA Rules	9/14/1990
8.97.2102	General Requirements of the Environmental Review Process	2/11/2000

MONTANA BOARD OF INVESTMENTS				
INVESTMENT POLICY STATEMENTS				
MU #	Policy	Policy Path/File Name Link	Date	Revised
MU11	Abandoned Mine	M:\POLICY\Updated IPS\Abandoned Mine ips Feb 2011		02/2011
MU66	Big Sky Econonomic Development Fund	M:\POLICY\Updated IPS\Big Sky Econ Dev ips Aug 2007	08/2007	
MU3F	Butte Area One Restoration Fund	M:\POLICY\Updated IPS\Butte Area One MU3F Fund 08219 ips Feb 11	02/2011	
MU3H	Clark Fork Restoration Fund	M:\POLICY\Updated IPS\Clark Fork MU3H Fund 08221 ips Feb 2011		02/2011
MU3A	Clark Fork Site Response Action Fund	M:\POLICY\Updated IPS\Clark Fork MU3A Fund 08212 ips Feb 2011		02/2011
MU53	Coal Tax Park Trust	M:\POLICY\Updated IPS\Coal Tax Park Trust Fund 2-2004		02/2004
MU40	Core Internal Bond Portfolio	M:\POLICY\Updated IPS\CIBP Core Internal Bond Port ips Feb 09	02/2009	
MU63	Cultural Trust Fund	M:\POLICY\Updated IPS\Cultural Trust Fund 2-2004		02/2004
MU3S	East Helena Compensation	M:\POLICY\Updated IPS\East Helena Compensation Nov 2012	11/14/2012	
MU1Z	Endowment for Children	M:\POLICY\Updated IPS\Endow for Children ips Aug 2007	08/2007	
MU16	FWP License Account	M:\POLICY\Updated IPS\FWP License MU16 ips Feb 2011		02/2011
MU13	FWP Mitigation Trust	M:\POLICY\Updated IPS\FWP Mitigation MU13 ips Feb 2011		02/2011
MU51	FWP Real Property Trust Fund	M:\POLICY\Updated IPS\FWP real property ips Sept 2003	09/2003	
MU33	Group Benefits	M:\POLICY\Updated IPS\Group Benefits MU33 ips Feb 2011		02/2011
MU60	Highway 93 Bond Proceeds	M:\POLICY\Updated IPS\Highway93 Bond Proceeds ips June 05	06/2005	
MU96	Historical Society Trust Funds	M:\POLICY\Updated IPS\Historical Society ips 11-30-2010		11/30/2010
MU48	Montana Domestic Equity Pool	M:\POLICY\Updated IPS\MDEP ips May 2012		05/2012
MU38	Montana International Pool	M:\POLICY\Updated IPS\MTIP ips Aug 2012		08/2012
MU14	Montana Pole Superfund	M:\POLICY\Updated IPS\MT Pole Superfund MU14 ips Feb 2011		02/2011
MU47	Montana Private Equity Pool	M:\POLICY\Updated ISP\MPEP ips 8-12-2010	08/12/2010	
	Montana Public Retirement Plans	M:\POLICY\Updated IPS\Pensions ips 8-21-12		08/21/2012
MU1A	Montana Real Estate Pool	M:\POLICY\Updated ISP\MTRP ips 12-1-2010		12/1/2010
MU3Q	Montana University System Group Insurance	M:\POLICY\Udated IPS\MUS Group Ins MU3Q ips 8-14-11	8/17/2011	
MUXX	Montana University System Group Insurance	M:\POLICY\Udated IPS\MUS Group Ins MUXX ips Feb 2011	02/2011	
MU61	Noxious Weed MU61 ips Feb 2011	M:\POLICY\Updated IPS\Noxious Weed MU61 ips Feb 2011		02/2011
MU1Y	Older Montanans Trust Fund	M:\POLICY\Updated IPS\Older Mont Trust ips Aug 2007	08/2007	
MU49	Permanent Coal Trust Funds	M:\POLICY\Updated IPS\Permanent Coal Tax Trust Policy		02/21/2012
N/A	Public Markets Manager Evaluation Policy	M:\POLICY\Updated IPS\Public Markets Manager Evaluation Policy	02/22/2012	
MU52	Resource Indemnity Trust Fund	M:\POLICY\Updated IPS\Resource ips Sept 2003	09/2003	
MU30	Retirement Funds Bond Pool	M:\POLICY\Updated IPS\RFBP MU30 ips Feb 2011	02/2011	
MU36	Short Term Investment Pool	M:\POLICY\Updated IPS\STIP ips Nov 2012		11/14/2012
MU3I	Smelter Hill Feb 2011	M:\POLICY\Updated IPS\Smelter Hill MU3I Fund 08222 ips Feb 2011		02/2011
MU26	State Fund Insurance	M:\POLICY\Updated IPS\State Fund ips Feb 2013	2/26/2013	
MU19	Streamside Tailings	M:\POLICY\Updated IPS\Streamside Tailings ips 11-07	11/2007	
MU27	Subsequent Injury	M:\POLICY\Updated IPS\Subsequent injury ips March 03	03/2003	
MU62	Tobacco Trust	M:\POLICY\Updated IPS\TobaccoTrust ips Jan 03	01/2003	
MU65	Treasure State Endowment Funds	M:\POLICY\Updated IPS\Treasure St Funds 09040 & 09044 ips June 04	05/2004	
MU64	Treasure State Regional Water Funds	M:\POLICY\Updated IPS\Treasure St Funds 09046 & 09047 ips June 04	05/2004	
MU10	Treasurers Fund MU10	M:\POLICY\Update IPS\Treasurers Fund MU10 ips Feb 2011		02/2011
MU58	Trust & Legacy	M:\POLCIY\Updated IPS\Trust & Legacy ips Aug 07	08/2007	
MU41	Trust Funds Investment Pool	M:\POLICY\Updated IPS\TFIP MU41 2011		02/2011
	U of M Endowments	M:\POLICY\Updated IPS\U of M Endowments ips Dec 03	12/2003	
MU79	U of M Operating Funds	M:\POLICY\Updated IPS\U of M Operating Funds ips July 02	07/2002	
MU3P	Upper Blackfoot Response	M:\POLICY\Updated IPS\UBMC IPS Feb 2011		02/2011
MU22	Upper Clark Fork River Basin Reserve Fund	M:\POLICY\Updated IPS\UCFRB Reserve Fund 02200 ips Jan 04	01/2004	
MU21	Upper Clark Fork River Basin Restoration Fund	M:\POLICY\Updated IPS\UCFRB Restoration Fund 02937 ips Jan 04	01/2004	
MU55	Wildlife Habitat Trust ips	M:\POLICY\Updated IPS\Wildlife Habitat Trust ips Sep 03	09/2003	
MU30	Zortman/Landusky Long Term Water	M:\POLICY\Updated IPS\ZORTMAN MU30 Fund 02540 ips Feb 2011		02/2011
MU67	Zortman/Landusky Trust	M:\POLICY\Udated IPS\ZORTMAN Trust MU67 Fund 09005 ips Feb 2011		02/2011

MONTANA BOARD OF INVESTMENTS			
POLICIES			
Policy Title	**Policy Path/FileName Link**	**Date**	**Revised**
Governance Policies			
Audit Committee Charter Policy	M:\Boardmtg\Audit Comm\Auditor_Internal Controls\Internal Control Policy	11/2007	08/2012
Ethics Policy	M:\POLICY\Ethics Policy\Code of Ethics	11/06/2007	
Governance Policy	M:\POLICY\Governance Policy\Governance Policy rev 022112	11/06/2007	02/21/2012
Human Resources Committee Charter Policy	M:\Boardmtg\Human Res Comm\HR Committee Charter	04/15/2005	
Loan Committee Charter Policy	M:\Boardmtg\Loan Comm\Loan Committee Charter rev 0811	6/24/2005	08/16/2011
Operational Policies			
Board Education Policy	M:\POLICY\Board Education Policy 071411	07/14/2011	
Exempt Staff Pay Plan Policy	M:\Personnel\Policies\Exempt Pay Plan	11/2008	10/04/2012
Internal Control Policy	M:\POLICY\Updated IPS\Internal Control Policy	11/2007	08/2012
Resolution 217 (Agent/Account Authorization)	M:\ADMIN\Resolution 217\Resolution 217 Authorization Ewer.docx	11/06/2007	
Resolution 218 Deputy Director	M:\ADMIN\Resolution 218\Corporate Resolution 218	11/06/2007	
Resolution 219 (Credit Enhancement)	M:\ADMIN\Resolution 219\Credit Enhancement Resolution 219 May 14 2008		05/14/2008
Securities Litigation Charter Policy	M:\CONTRACT\Securities Litigation\Securities_Litigation Policy		11/10/2005
Coal Tax Trust Policies			
Approved Lender Policy	M:\POLICY\In-State\Approved Lender Application		06/2004
Commercial Loan Policy	M:\POLICY\In-State\CommLoanPolicy 08-2009		08/12/2009
Infrastruction Loan Policy & App	M:\POLICY\In-State\Infrastructure Loan Policy & App 08-2009		08/12/2009
Residential Loan Policy	M:\POLICY\In-State\ResidentialMortgagePolicy		08/18/2005
Value Added Loan Policy	M:\POLICY\In-State\Value-Added Policy & App 08-2009		08/12/2009
Veteran's Home Loan Policy	M:\POLICY\In-State\Vet Policy 7-18-12	8/21/2012	
Bond Program Policies			
INTERCAP Policy	M:\POLICY\INTERCAP Program Requirements	05/2012	
University System INTERCAP Loan Policy	M:\POLICY\University System Intercap Loan Policy	5/18/2006	

MONTANA BOARD OF INVESTMENTS
BOARD EDUCATION POLICY

~~Approved: July 14, 2011~~

I. PURPOSE

The purpose of this Board Education Policy is to establish guidelines and procedures for members of the Montana Board of Investments that recognize and affirm the importance of education to the success of fulfilling their fiduciary responsibilities.

II. POLICY OBJECTIVES

1. All Board Members will ~~be able to leverage continuing~~have education opportunities to maintain the knowledge they need to carry out their fiduciary responsibilities and engage in effective group discussion, debate and decision making~~ with regard to the Fund as a whole~~.

2. Newly appointed or elected Board Members will be provided with the general introductory knowledge they need to enable them to effectively participate in Board and Committee deliberations in a timely manner.

3. Board Members will have the opportunity to learn through networking with the Trustees of other public retirement systems and learn of alternate approaches to common issues and problems.

III. ASSUMPTIONS AND PRINCIPLES

1. Board Members are responsible for making policy decisions affecting all major aspects of plan administration. They, therefore, ~~must~~ should acquire an appropriate level of knowledge of all significant facets of the investment management process rather than specializing in particular areas.

2. A variety of educational methods are ~~necessary and appropriate~~encouraged since no single, educational method is optimal.

3. The Board Education Policy is not intended to dictate that Board Members attend only specific conferences or programs. Although a list is included in this Policy as a reference, the Policy is a framework for the types of opportunities that ~~the~~ Board Members ~~should~~ may use in their fiduciary education.

MONTANA BOARD OF INVESTMENTS
BOARD EDUCATION POLICY

IV. POLICY GUIDELINES

1. GENERAL PROVISIONS

A. All Board Members are encouraged to develop and maintain their knowledge and understanding of the issues involved in the policy direction and management of the Montana Board of Investments throughout their terms as Board Members.

B. Board Members are encouraged to develop an appropriate level of knowledge across a broad spectrum of issues, including:

i. Governance and fiduciary duty
ii. Actuarial policies and pension funding
iii. Best practices in total fund, asset class composite and investment manager monitoring, funding and decision-making
iv. Key institutional investment management concepts, including, but not limited to:
   a. Portfolio management theory and strategies
   b. Asset class attributes and investment strategies
   c. Performance evaluation concepts

C. Board Members are encouraged to help seek out, evaluate and take advantage of appropriate educational tools, which may include, but are not limited to:

i. External conferences, seminars, workshops, roundtables, courses or similar vehicles
ii. In-house presentations by the Board's service providers, staff, or non-affiliated investment experts
iii. Relevant periodicals, trade journals, textbooks, electronic media, etc.

~~D. The Board Chair shall review and evaluate available educational conferences and bring to the attention of the Board those they believe are appropriate. Board Members may also bring forward appropriate educational conferences for consideration.~~

~~E.~~D. Standards for determining the appropriateness of a potential educational opportunity shall include, without limitation:

i. The extent to which the opportunity is expected to provide Board Members with the knowledge they need to carry out their roles and responsibilities, and

MONTANA BOARD OF INVESTMENTS
BOARD EDUCATION POLICY

ii. The expected return on investment of the program, taking into account the expected educational benefits weighed against the expected costs, such as travel, lodging and related expenses.

~~F.~~ iii. Board Members are encouraged to assist in identifying the educational vehicles that best meet their needs, and to ~~attempt to meet the following minimum goals:~~

~~i.~~ s~~Secure~~seek an appropriate level of knowledge in each of the areas listed in Section IV. 1. B. of this Policy.~~y; and~~

~~ii. Attend one external conference annually, preferably one that is (1) highly relevant to current investment issues before the board and/or, (2) specifically dealing with public fund issues, and (3) additive to external education events attended by fellow MTBOI Board Members.~~

~~Due diligence activities such as meetings with existing or prospective service providers shall not substitute for other educational programs.~~

~~G.~~E. The Board shall establish an annual budget to cover the cost of providing continuing fiduciary education for its Board Members. The Board shall reimburse Board members for all reasonable and necessary expenses incurred in attending educational programs encouraged hereunder as provided in this Policy.

~~H.~~F. Each Board Member is encouraged to report to the Board on the most important knowledge or information gained from the conference/seminar/workshop attended and recommend whether to attend in the future.

2. BOARD MEMBER ORIENTATION PROGRAM

A. An orientation program will be formalized and maintained for the benefit of new Board Members.

~~B. All new Board Members shall be required to participate in the orientation program within a reasonable time. Current Board Members are invited to participate at their option.~~

~~C.~~B. The aim of the orientation program shall be to ~~ensure~~ provide relevant information/education so that new Board Members are in a position to contribute fully to Board and Committee deliberations and effectively carry out their fiduciary duties as soon as possible after joining the Board.

MONTANA BOARD OF INVESTMENTS
BOARD EDUCATION POLICY

~~D.~~C. The orientation program ~~shall~~ may include:

i. In-person introduction to MTBOI management and staff

ii. A tour of the staff office

iii. An orientation handbook, which ~~is~~ may be presented to Board Members via an orientation seminar. The handbook and/or accompanying seminar should cover the following:
   a. Most recent Governance Policy and Investment Policy Statements
   b. Roles and responsibilities of Board Members, Committees and staff
   c. An overview of ~~relevant~~ State laws relevant to fund management
   d. Material from legal counsel on fiduciary responsibility
   e. Copies of Board and general operating policies and procedures
   f. Most recent Comprehensive Annual Financial Report
   g. Most recent Actuarial Valuation Report and Asset Liability Study
   h. Most recent Investment performance report
   i. Most recent MTBOI budget
   j. Up-to-date organization chart
   k. Names and telephone numbers of other MTBOI Board Members and Staff

~~iv. A briefing by MTBOI legal counsel on the role of the Board and fiduciary responsibility~~

~~v. A briefing by MTBOI management on the history of the Montana Board of Investments~~

3. ATTENDANCE AT EDUCATIONAL CONFERENCES AND SEMINARS

A. Illustrative examples of conferences that Board Members may consider attending would include:

i. Council of Institutional Investors (CII)
ii. Institutional Investor Conference on Alternative Investments
iii. Institutional Investor Conference on Fund Management
iv. International Foundation of Employee Benefit Plans
v. Portfolio Concepts and Management sponsored by the Wharton School, University of Pennsylvania (Wharton)
vi. Public Pension Investment Management Program (SACRS)

MONTANA BOARD OF INVESTMENTS
BOARD EDUCATION POLICY

vii. Semi-annual conference sponsored by the State Association of County Retirement Systems (SACRS)

~~Board Members wishing to attend other conferences or seminars will submit their request to the Board Chair for approval.~~

B. All Board Member out of state travel to be reimbursed by the Board will be first approved by the Chair after consultation with the Executive Director.

C. In attending ~~external~~ conferences, preference will be given to those sponsored by educational institutions or pension industry associations as opposed to conferences with agendas that are largely determined and executed by current or potential vendors to the MTBOI.

~~D. In no event will the expense of attending a Professional Conference by a Board Member who attends the Professional Conference in his or her own professional capacity be reimbursed by the Board. Only with the written permission of the Board may a Board Member attend a Professional Conference in his or her capacity as a Board Member.~~

MONTANA BOARD OF INVESTMENTS
BOARD EDUCATION POLICY

I. PURPOSE

The purpose of this Board Education Policy is to establish guidelines and procedures for members of the Montana Board of Investments that recognize and affirm the importance of education to the success of fulfilling their fiduciary responsibilities.

II. POLICY OBJECTIVES

1. All Board Members will have education opportunities to maintain the knowledge they need to carry out their fiduciary responsibilities and engage in effective group discussion, debate and decision making.

2. Newly appointed or elected Board Members will be provided with the general introductory knowledge they need to enable them to effectively participate in Board and Committee deliberations in a timely manner.

3. Board Members will have the opportunity to learn through networking with the Trustees of other public retirement systems and learn of alternate approaches to common issues and problems.

III. ASSUMPTIONS AND PRINCIPLES

1. Board Members are responsible for making policy decisions affecting all major aspects of plan administration. They, therefore, should acquire an appropriate level of knowledge of all significant facets of the investment management process rather than specializing in particular areas.

2. A variety of educational methods are encouraged since no single, educational method is optimal.

3. The Board Education Policy is not intended to dictate that Board Members attend only specific conferences or programs. Although a list is included in this Policy as a reference, the Policy is a framework for the types of opportunities that Board Members may use in their fiduciary education.

IV. POLICY GUIDELINES

1. GENERAL PROVISIONS

A. All Board Members are encouraged to develop and maintain their knowledge and understanding of the issues involved in the policy direction and management of the Montana Board of Investments throughout their terms as Board Members.

B. Board Members are encouraged to develop an appropriate level of knowledge across a broad spectrum of issues, including:

i. Governance and fiduciary duty
ii. Actuarial policies and pension funding
iii. Best practices in total fund, asset class composite and investment manager monitoring, funding and decision-making
iv. Key institutional investment management concepts, including, but not limited to:
   a. Portfolio management theory and strategies
   b. Asset class attributes and investment strategies
   c. Performance evaluation concepts

C. Board Members are encouraged to help seek out, evaluate and take advantage of appropriate educational tools, which may include, but are not limited to:

i. External conferences, seminars, workshops, roundtables, courses or similar vehicles
ii. In-house presentations by the Board's service providers, staff, or non-affiliated investment experts
iii. Relevant periodicals, trade journals, textbooks, electronic media, etc.

D. Standards for determining the appropriateness of a potential educational opportunity shall include, without limitation:

i. The extent to which the opportunity is expected to provide Board Members with the knowledge they need to carry out their roles and responsibilities, and

ii. The expected return on investment of the program, taking into account the expected educational benefits weighed against the expected costs, such as travel, lodging and related expenses.

iii. Board Members are encouraged to assist in identifying the educational vehicles that best meet their needs, and to seek an appropriate level of knowledge in each of the areas listed in Section IV. 1. B. of this Policy.

E. The Board shall establish an annual budget to cover the cost of providing continuing fiduciary education for its Board Members. The Board shall reimburse Board members for all reasonable and necessary expenses incurred in attending educational programs encouraged hereunder as provided in this Policy.

F. Each Board Member is encouraged to report to the Board on the most important knowledge or information gained from the conference/seminar/workshop attended and recommend whether to attend in the future.

2. Board Member Orientation Program

A. An orientation program will be formalized and maintained for the benefit of new Board Members.

B. The aim of the orientation program shall be to provide relevant information/education so that new Board Members are in a position to contribute fully to Board and Committee deliberations and effectively carry out their fiduciary duties as soon as possible after joining the Board.

C. The orientation program may include:

i. In-person introduction to MTBOI management and staff

ii. A tour of the staff office

iii. An orientation handbook, which may be presented to Board Members via an orientation seminar. The handbook and/or accompanying seminar should cover the following:
  a. Most recent Governance Policy and Investment Policy Statements
  b. Roles and responsibilities of Board Members, Committees and staff
  c. An overview of State laws relevant to fund management
  d. Material from legal counsel on fiduciary responsibility
  e. Copies of Board and general operating policies and procedures
  f. Most recent Comprehensive Annual Financial Report
  g. Most recent Actuarial Valuation Report and Asset Liability Study
  h. Most recent Investment performance report
  i. Most recent MTBOI budget
  j. Up-to-date organization chart
  k. Names and telephone numbers of other MTBOI Board Members and Staff

3. Attendance at Educational Conferences and Seminars

A. Illustrative examples of conferences that Board Members may consider attending would include:

i. Council of Institutional Investors (CII)
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iii. Institutional Investor Conference on Fund Management
iv. International Foundation of Employee Benefit Plans
v. Portfolio Concepts and Management sponsored by the Wharton School, University of Pennsylvania (Wharton)
vi. Public Pension Investment Management Program (SACRS)
vii. Semi-annual conference sponsored by the State Association of County Retirement Systems (SACRS)

B. All Board Member out of state travel to be reimbursed by the Board will be first approved by the Chair after consultation with the Executive Director.

C. In attending conferences, preference will be given to those sponsored by educational institutions or pension industry associations as opposed to conferences with agendas that are largely determined and executed by current or potential vendors to the MTBOI.

MEMORANDUM

Montana Board of Investments
Department of Commerce
2401 Colonial Drive, 3rd Floor
Helena, MT 59601 (406) 444-0001

To: Members of the Board

From: Clifford A. Sheets, CFA, Chief Investment Officer

Date: April 2, 2013

Subject: Revised Investment Policy Statements

The purpose of this memo is to summarize the changes to investment policy statements that are being recommended for approval by the Board.

There were also minor changes made to a handful of policies that were simply technical in nature. These policies are not being presented here for approval. These changes include:

- Changing the reference to various “Lehman” fixed income benchmarks to “Barclays”
- Removing dated references to historical asset amounts or sector exposures in some fixed income separate account investment policy statements.
- Where missing, adding boiler plate language regarding the ability of the account to lend individual securities.

Otherwise, the changes to investment policies which we are submitting for approval are summarized below.

Separate Accounts

<u>Streamside Tailings</u> (MU19)

- Increase STIP range to allow for necessary liquidity. The amount of necessary liquidity is approximately the next 12 months of expected expenditures.
- Re-format to align with the new investment policy statement (IPS) format for accounts holding individual securities

<u>UCFRB Restoration</u> (MU21)

- Increase STIP range to allow for necessary liquidity. The amount of necessary liquidity is approximately the next 12 months expected expenditures.
- Re-format to align with the new IPS format for accounts holding individual securities

<u>Butte Area One</u> (MU3F)

- Increase STIP range to allow for necessary liquidity. The amount of necessary liquidity is dependent on local authorities’ plans. The proposed increase in the STIP range will allow for maturities of individual securities without being forced to reinvest in long term securities if the expected expenditures accelerate.

Montana State University Operating Funds (MU81)

- This is a new policy statement altogether where one did not exist previously. At this time it contemplates only the use of STIP and TFIP as eligible investments.

Montana Tech Operating Funds (MU80)

- This is a new policy statement altogether where one did not exist previously. At this time it contemplates only the use of STIP and TFIP as eligible investments.

Investment Pools

Core Internal Bond Pool (CIBP) (MU40)

- The language regarding credit quality was changed to clarify the expectation that purchases shall be investment grade. It also now addresses the situation where a holding may have been downgraded to below investment grade, and requires an internal rating if there are no public ratings.
- Ranges for the various bond market sector exposures have been changed to reflect the changes in the benchmark and portfolio management preferences. The cash item has been removed in this table since the amount of cash held is simply a by-product of the duration decision and should not be constrained in and of itself.

Trust Funds Investment Pool (TFIP) (MU41)

- The language regarding credit quality was changed to clarify the expectation that purchases shall be investment grade. It also now addresses the situation where a holding may have been downgraded to below investment grade, and requires an internal rating if there are no public ratings.
- Ranges for the various bond market sector exposures have been changed to reflect the changes in the benchmark and portfolio management preferences. The cash item has been removed in this table since the amount of cash held is simply a by-product of the duration decision and should not be constrained in and of itself.

Montana Private Equity Pool (MPEP) (MU47)

- Several grammatical changes were made and clarifications or simplifications of language describing the types of underlying strategies and risks.
- The table showing strategies and policy ranges was simplified and the ranges tightened for venture capital and debt-related strategies.
- The individual manager limit exception for fund-of-funds managers was removed since it is no longer relevant given the current portfolio composition.
- The Due Diligence section was removed since this is a matter of implementation more so than policy, and staff has developed its own checklist that encompasses all of these items and more. The checklist is used as part of the normal underwriting process that is conducted prior to a commitment decision being made.

Montana Real Estate Pool (MTRP) (MU1A)

- The allocation section at the outset of the policy was removed since the allocation to the pool is controlled by the Public Retirement Plans investment policy statement.
- Several minor grammatical changes were made.

- Language regarding policy constraints was modified to reflect current practices regarding disclosure to the Board.
- Language regarding the "region/location" in the diversification section was changed to remove reference to potential future changes which would be implicit in any policy revision. Also, a restriction in reference to diversification within the Timberland portfolio was removed since this may be difficult to meet was not clear as to the time reference for such measurement.
- The language describing the benchmark for the pool was changed to better clarify the index being used and to acknowledge the inherent risk differences between the funds held in the pool and the index.

Other Policies

Public Markets Manager Evaluation Policy

- This policy was modified to remove the language referencing contract terms and the required issuance of RFP's on an as-needed basis or in conjunction with a manager contract expiration. The RFP process was removed as a requirement of the procurement process by the Board in February, 2012.

This completes the summary of changes being made to the various policies listed above. Staff recommends the Board approve the changes to these policies. Following this memo are red-lined copies of each policy and a clean copy reflecting the proposed changes.

I also want to make note of the MTIP pool investment policy in the context of the restructuring efforts that were recommended and adopted by the Board last August. You may recall that as part of the restructuring of the pool it was contemplated that the benchmark of the pool be changed to the MSCI ACW ex-US IMI index. The IPS for the pool now reflects this new benchmark, yet the restructuring has not yet been implemented. This index holds a higher weighting in small cap stocks than the prior benchmark. Thus, a review of the portfolio holdings by manager will currently show a level of small cap manager weighting that is below the revised range for small cap (the range was increased from 5-15% to 10-16%). This is simply due to the pending nature of the restructure. It was acknowledged during the August Board meeting that the new benchmark would not go into effect until the restructuring was completed.

STREAMSIDE TAILINGS OPERABLE SETTLEMENT FUND (MU19) (FUND 02520) INVESTMENT POLICY STATEMENT

INTRODUCTION

~~The purpose of an investment policy statement is to give the investment manager guidance in developing an investment program to achieve the objectives agreed upon and enable the client, the Department of Environmental Quality (DEQ), to monitor the progress of the plan.~~

The purpose of this investment policy statement is to outline the account objectives, permissible investments, and constraints that will guide the management of the portfolio. The policy is designed to give the investment manager flexibility to achieve in a prudent manner the investment objectives of the client, the Department Environmental Quality (DEQ) to implement remedial actions to the area covered by the Streamside Tailings Operable Unit in accordance with the ARCO Settlement Consent Decree.

BACKGROUND INFORMATION

January 1999

In November 1998, a Consent Decree between the State, the United States, the Atlantic Richfield Company (ARCO), and others was entered into in order to settle certain litigation and to provide funding for the implementation of the remedy for the Streamside Tailings Operable Unit of the Silver Bow Creek/Butte Area (original portion) NPL Site. The settlement involves, among other things, payment by ARCO of $80 million, over a period of three years. Those funds and the earnings from the investment of those funds are to be used by the State and EPA for the purpose of remediating the mine waste contamination at the Streamside Tailings Operable Unit over an estimated twelve-year period, with any funds, including earnings, which are not ultimately required for the remediation of the Streamside Tailings Operable Unit to be used by the State for natural resource damage restoration purposes.

ARCO payments:

March 1999	$15 million
July 1999	$15 million principal plus $7 million interest ($22.0 million total)
July 2000	$25 million principal plus $3.886 million interest ($28.886 million total)
July 2001	$25 million principal plus $1.891 million interest ($26.891 million total)
Total	**$92.777 million**

Interest was calculated using the income yield on the Trust Funds Bond Pool.

November 2007

Major construction is projected to end during Fiscal Year 2012. At that time, a small fund balance will be needed to fund operations and maintenance going forward and the remaining balance will be transferred to the Upper Clark Fork Restoration Fund (MU21). The fund balance at that time is expected to be mostly TFBP units.

March 2013

The timing of expenditures has been slower than expected. Major construction is projected to continue through 2018.

~~To maximize investment earning, we are proposing a higher asset allocation range for TFBP holdings. We currently have sufficient cash flow and maturities to fund expenses thru FY12 without selling TFBP units and probably have room to buy additional TFBP units.~~

STREAMSIDE TAILINGS OPERABLE SETTLEMENT FUND (MU19) (FUND 02520)
INVESTMENT POLICY STATEMENT

OBJECTIVES

~~Return Requirement: To maximize the total rate of return through a diversified portfolio of fixed income assets.~~

~~Current Income: Current income is important since interest earned, in addition to principle, is used to fund the cleanup activities.~~

~~Risk Tolerance: This is a State special revenue fund having an average ability to assume interest rate risk. Risk tolerance will decline if long-term investments have to be liquidated earlier than estimated in the cash draw down schedule. Investments in the Trust Funds Bond Pool (TFBP) will be allowed.~~

Risk and Return:

A combination of current income, total return, and use of principle will be necessary to fund expected expenditures. It will require a return in excess of the assumed risk free rate to fund current projected expenditures, as well as possible future cost over runs. This account has an average ability to assume interest rate risk. Some risk of loss of principal must be taken to provide a return sufficient to fund objectives. An allocation to the Trust Funds Investments Pool (TFIP) will be made to obtain exposure to a diversified fixed income portfolio. An allocation to U.S. Treasuries, U.S. Agencies and Corporate securities may be made to provide a greater certainty of cash flows from maturities. Risk tolerance will decline if long-term investments have to be liquidated earlier than estimated to meet the cash draw down schedule.

~~CONSTRAINTS~~

~~Liquidity Needs: Liquidity will be needed to fund cash draw down schedule. The Board will use its investment discretion to determine the appropriate mix of long-term investments and STIP units, considering the dates of receipt of funds and the funding needs indicated by the cash draw down schedule to be provided by DEQ.~~

~~Time Horizon: This fund is considered an intermediate-term fund that has a time horizon beyond one year.~~

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

~~Legal Considerations: This fund is governed by state regulations, specifically, the "prudent expert principle" which requires the Board of Investments to: (a) discharge the duties with the care, skill, prudence, and diligence, under the circumstances then prevailing, that a prudent person acting in a like capacity with the same resources and familiar with like manners exercises in the conduct of an enterprise of a like character with like aims; (b) diversify the holdings of each fund within the unified investment program to minimize the risk of loss and to maximize the rate of return unless, under the circumstances, it is solely prudent not to do so; and (c) discharge the duties solely in the interest of and for the benefit of the funds forming the unified investment program.~~

~~The Montana Constitution does not allow equity type investments in non-retirement funds.~~

~~Unique Circumstance: The project being financed through this fund is the remediation of environmental contamination at one operable unit of a federal Superfund site. The nature of construction/remediation work includes the potential for cost overruns and unexpected expenses. DEQ will use its best efforts to inform~~

STREAMSIDE TAILINGS OPERABLE SETTLEMENT FUND (MU19) (FUND 02520) INVESTMENT POLICY STATEMENT

~~the Board of Investments of any expected overruns or changes in the cash draw schedule and will attempt to provide notice of such changes as much in advance as possible.~~

~~Client Preference: None~~

~~BACKGROUND INFORMATION~~

~~January 1999~~
~~In November 1998, a Consent Decree between the State, the United States, the Atlantic Richfield Company (ARCO), and others was entered into in order to settle certain litigation and to provide funding for the implementation of the remedy for the Streamside Tailings Operable Unit of the Silver Bow Creek/Butte Area (original portion) NPL Site. The settlement involves, among other things, payment by ARCO of $80 million, over a period of three years. Those funds and the earnings from the investment of those funds are to be used by the State and EPA for the purpose of remediating the mine waste contamination at the Streamside Tailings Operable Unit over an estimated twelve-year period, with any funds, including earnings, which are not ultimately required for the remediation of the Streamside Tailings Operable Unit to be used by the State for natural resource damage restoration purposes.~~

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~~Total~~	**~~$92.777 million~~**

~~Interest was calculated using the income yield on the Trust Funds Bond Pool.~~

~~November 2007~~
~~Major construction is projected to end during Fiscal Year 2012. At that time, a small fund balance will be needed to fund operations and maintenance going forward and the remaining balance will be transferred to the Upper Clark Fork Restoration Fund (MU21). The fund balance at that time is expected to be mostly TFBP units.~~

~~To maximize investment earning, we are proposing a higher asset allocation range for TFBP holdings. We currently have sufficient cash flow and maturities to fund expenses thru FY12 without selling TFBP units and probably have room to buy additional TFBP units.~~

STREAMSIDE TAILINGS OPERABLE SETTLEMENT FUND (MU19) (FUND 02520) INVESTMENT POLICY STATEMENT

~~CASH FLOW SUMMARY~~
~~(In millions)~~

~~Fiscal Year~~	~~Addition to Fund~~	~~Book Value~~	~~Market Value~~	~~Total Inv. Income~~	~~Income Yield~~
~~1999~~	~~$14.9~~	~~$14.9~~	~~$14.9~~	~~$0.317~~	
~~2000~~	~~20.4~~	~~35.3~~	~~34.4~~	~~2.319~~	
~~2001~~	~~29.8~~	~~65.1~~	~~66.5~~	~~4.484~~	
~~2002~~	~~28.4~~	~~93.5~~	~~96.1~~	~~6.125~~	
~~2003~~	~~0.0~~	~~93.5~~	~~99.8~~	~~6.396~~	~~6.84%~~
~~2004~~	~~0.3~~	~~93.8~~	~~95.5~~	~~6.131~~	~~6.55~~
~~2005~~	~~(1.6)~~	~~92.2~~	~~94.7~~	~~5.611~~	~~6.03~~
~~2006~~	~~(5.4)~~	~~86.8~~	~~85.3~~	~~4.824~~	~~5.39~~
~~2007~~	~~(3.2)~~	~~83.6~~	~~82.7~~	~~4.669~~	~~5.48~~

ASSET ALLOCATION
(at market)

~~FIXED INCOME~~	~~6-05~~	~~6-06~~	~~6-07~~	~~Existing Ranges~~	~~Proposed Ranges~~
~~U.S Government/Agency Securities~~					
~~Domestic~~	~~17.9%~~	~~19.4%~~	~~13.4%~~	~~0-50%~~	
~~Mortgage-Backed~~	~~3.1~~	~~2.7~~	~~2.3~~	~~0-25~~	
~~Subtotal~~	~~21.0%~~	~~22.1%~~	~~15.7%~~		
~~Corporate Securities~~					
~~Domestic~~	~~14.2~~	~~10.0~~	~~8.7~~	~~0-30~~	
~~Trust Funds Bond Pool (TFBP)~~	~~58.6~~	~~65.1~~	~~67.5~~	~~30-70~~	~~50-95~~
~~Short-Term Investment Pool (STIP)~~	~~6.2~~	~~2.8~~	~~8.1~~	~~0-10~~	
~~TOTAL FIXED INCOME~~	~~100.0%~~	~~100.0%~~	~~100.0%~~	~~100.0%~~	

STREAMSIDE TAILINGS OPERABLE SETTLEMENT FUND (MU19) (FUND 02520)
INVESTMENT POLICY STATEMENT

Fixed Income	Range
U.S. Treasury Bonds	0-30%
U.S. Agency Bonds	0-30%
Corporate Bonds	0-10%
Trust Funds Investment Pool (TFIB)	50-90%
Short Term Investment Pool (STIP)	0-30%
Total Fixed Income	100%

OTHER CONSIDERATIONS

Liquidity Needs:
Material annual expenditures are projected in each year through 2018 in the initial cash draw down schedule provided by DOJ. The timing of expenditures within the calendar year will be somewhat uncertain, thus necessitating a significant cash balance be available to meet these needs without forcing an inordinate amount of TFIP sales in any one year. There will be significant seasonality in the pattern of expenditures. Liquidity needs will be met with a combination of cash on hand, earnings, maturities and sales of investments. The minimum (STIP) balance will be the expected next one year of expenditures less expected maturities of individual securities prior to any adjustment to reflect funding needs.

Maturity Horizon:
The maturity horizon of the investments utilized is designed to meet the liabilities of the client with income, maturities and a reasonable amount of sales of securities and TFIP units. The liabilities are the cash needs for restoration expenditures as provided and updated by the DOJ. Expenditures are projected to occur through 2020.

Investment Limits:
1. To reduce the risk of loss on individual corporate bonds, investment purchases in any one credit will be limited to 1% of the market value of the fund at the date of purchase or 2% of the lowest projected fund balance before the securities mature, whichever is lower.
2. Corporate bond sector (Industrial, Finance, and Utility) exposure shall be constrained to no more than a 4% exposure at the time of purchase, or 6% at any time over the future projected fund balance.
3. The quality rating of any corporate bond shall be in the top of the single-A rating classification or better at the time of purchase. (e.g., A1/A+ or higher), and have at least two ratings.
4. Exposure to the securities of any one U.S. Agency are limited to 5%, and in no event will an agency security be purchased if it carries a rating lower than that of the U. S. Government.

Legal Considerations:
This fund is governed by state regulations, specifically, the "prudent expert principle" which requires the Board of Investments to: (a) discharge the duties with the care, skill, prudence, and diligence, under the circumstances then prevailing, that a prudent person acting in a like capacity with the same resources and

familiar with like matters exercises in the conduct of an enterprise of a like character with like aims; (b) diversify the holdings of each fund within the unified investment program to minimize the risk of loss and to maximize the rate of return unless, under the circumstances, it is solely prudent not to do so; and (c) discharge the duties solely in the interest of and for the benefit of the funds forming the unified investment program.

The Montana Constitution does not allow equity type investments in non-retirement funds.

ADMINISTRATIVE

Securities Lending:

Section 17-1-113, MCA, authorizes the Board to lend securities held by the state. The Board may lend its publicly traded securities held in the investment pools, through an agent, to other market participants in return for compensation. Currently, through an explicit contract, State Street Bank and Trust, the state's custodial bank, manages the state's securities lending program. The Board seeks to assess the risks, such as counterparty and reinvestment risk, associated with each aspect of its securities lending program. The Board requires borrowers to maintain collateral at 102 percent for domestic securities and 105 percent for international securities. To ensure that the collateral ratio is maintained, securities on loan are marked to market daily and the borrower must provide additional collateral if the value of the securities on loan increases. In addition to the strict collateral requirements imposed by the Board, the credit quality of approved borrowers is monitored continuously by the contractor. From time to time, Staff or the investment manager may restrict a security from the loan program upon notification to State Street Bank. Staff will monitor the securities lending program, and the CIO will periodically report to the Board on the status of the program.

STREAMSIDE TAILINGS OPERABLE SETTLEMENT FUND (MU19) (FUND 02520) INVESTMENT POLICY STATEMENT

INTRODUCTION

The purpose of this investment policy statement is to outline the account objectives, permissible investments, and constraints that will guide the management of the portfolio. The policy is designed to give the investment manager flexibility to achieve in a prudent manner the investment objectives of the client, the Department Environmental Quality (DEQ) to implement remedial actions to the area covered by the Streamside Tailings Operable Unit in accordance with the ARCO Settlement Consent Decree.

BACKGROUND INFORMATION

January 1999

In November 1998, a Consent Decree between the State, the United States, the Atlantic Richfield Company (ARCO), and others was entered into in order to settle certain litigation and to provide funding for the implementation of the remedy for the Streamside Tailings Operable Unit of the Silver Bow Creek/Butte Area (original portion) NPL Site. The settlement involves, among other things, payment by ARCO of $80 million, over a period of three years. Those funds and the earnings from the investment of those funds are to be used by the State and EPA for the purpose of remediating the mine waste contamination at the Streamside Tailings Operable Unit over an estimated twelve-year period, with any funds, including earnings, which are not ultimately required for the remediation of the Streamside Tailings Operable Unit to be used by the State for natural resource damage restoration purposes.

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November 2007

Major construction is projected to end during Fiscal Year 2012. At that time, a small fund balance will be needed to fund operations and maintenance going forward and the remaining balance will be transferred to the Upper Clark Fork Restoration Fund (MU21). The fund balance at that time is expected to be mostly TFBP units.

March 2013

The timing of expenditures has been slower than expected. Major construction is projected to continue through 2018.

OBJECTIVES

Risk and Return:

A combination of current income, total return, and use of principle will be necessary to fund expected expenditures. It will require a return in excess of the assumed risk free rate to fund current projected expenditures, as well as possible future cost over runs. This account has an average ability to assume interest rate risk. Some risk of loss of principal must be taken to provide a return sufficient to fund

STREAMSIDE TAILINGS OPERABLE SETTLEMENT FUND (MU19) (FUND 02520)
INVESTMENT POLICY STATEMENT

objectives. An allocation to the Trust Funds Investments Pool (TFIP) will be made to obtain exposure to a diversified fixed income portfolio. An allocation to U.S. Treasuries, U.S. Agencies and Corporate securities may be made to provide a greater certainty of cash flows from maturities. Risk tolerance will decline if long-term investments have to be liquidated earlier than estimated to meet the cash draw down schedule.

ASSET ALLOCATION
(at Market)

Fixed Income	Range
U.S. Treasury Bonds	0-30%
U.S. Agency Bonds	0-30%
Corporate Bonds	0-10%
Trust Funds Investment Pool (TFIB)	50-90%
Short Term Investment Pool (STIP)	0-30%
Total Fixed Income	100%

OTHER CONSIDERATIONS

Liquidity Needs:
Material annual expenditures are projected in each year through 2018 in the initial cash draw down schedule provided by DOJ. The timing of expenditures within the calendar year will be somewhat uncertain, thus necessitating a significant cash balance be available to meet these needs without forcing an inordinate amount of TFIP sales in any one year. There will be significant seasonality in the pattern of expenditures. Liquidity needs will be met with a combination of cash on hand, earnings, maturities and sales of investments. The minimum (STIP) balance will be the expected next one year of expenditures less expected maturities of individual securities prior to any adjustment to reflect funding needs.

Maturity Horizon:
The maturity horizon of the investments utilized is designed to meet the liabilities of the client with income, maturities and a reasonable amount of sales of securities and TFIP units. The liabilities are the cash needs for restoration expenditures as provided and updated by the DOJ. Expenditures are projected to occur through 2020.

Investment Limits:
1. To reduce the risk of loss on individual corporate bonds, investment purchases in any one credit will be limited to 1% of the market value of the fund at the date of purchase or 2% of the lowest projected fund balance before the securities mature, whichever is lower.
2. Corporate bond sector (Industrial, Finance, and Utility) exposure shall be constrained to no more than a 4% exposure at the time of purchase, or 6% at any time over the future projected fund balance.
3. The quality rating of any corporate bond shall be in the top of the single-A rating classification or better at the time of purchase. (e.g., A1/A+ or higher), and have at least two ratings.

STREAMSIDE TAILINGS OPERABLE SETTLEMENT FUND (MU19) (FUND 02520)
INVESTMENT POLICY STATEMENT

4. Exposure to the securities of any one U.S. Agency are limited to 5%, and in no event will an agency security be purchased if it carries a rating lower than that of the U. S. Government.

Legal Considerations:
This fund is governed by state regulations, specifically, the "prudent expert principle" which requires the Board of Investments to: (a) discharge the duties with the care, skill, prudence, and diligence, under the circumstances then prevailing, that a prudent person acting in a like capacity with the same resources and familiar with like matters exercises in the conduct of an enterprise of a like character with like aims; (b) diversify the holdings of each fund within the unified investment program to minimize the risk of loss and to maximize the rate of return unless, under the circumstances, it is solely prudent not to do so; and (c) discharge the duties solely in the interest of and for the benefit of the funds forming the unified investment program.

The Montana Constitution does not allow equity type investments in non-retirement funds.

ADMINISTRATIVE

Securities Lending:

Section 17-1-113, MCA, authorizes the Board to lend securities held by the state. The Board may lend its publicly traded securities held in the investment pools, through an agent, to other market participants in return for compensation. Currently, through an explicit contract, State Street Bank and Trust, the state's custodial bank, manages the state's securities lending program. The Board seeks to assess the risks, such as counterparty and reinvestment risk, associated with each aspect of its securities lending program. The Board requires borrowers to maintain collateral at 102 percent for domestic securities and 105 percent for international securities. To ensure that the collateral ratio is maintained, securities on loan are marked to market daily and the borrower must provide additional collateral if the value of the securities on loan increases. In addition to the strict collateral requirements imposed by the Board, the credit quality of approved borrowers is monitored continuously by the contractor. From time to time, Staff or the investment manager may restrict a security from the loan program upon notification to State Street Bank. Staff will monitor the securities lending program, and the CIO will periodically report to the Board on the status of the program.

MONTANA BOARD OF INVESTMENTS
INVESTMENT POLICY STATEMENT
UPPER CLARK FORK RIVER BASIN (UCFRB) RESTORATION FUND ~~(FUND 02937)~~MU21
~~JANUARY 2004~~

INTRODUCTION

~~The purpose of an investment policy statement is to give the investment manager guidance in developing an investment program to achieve the objectives agreed upon and enable the client, the Department of Justice (DOJ), to monitor the progress of the plan.~~
The purpose of this investment policy statement is to outline the account objectives, permissible investments, and constraints that will guide the management of the portfolio. The policy is designed to give the investment manager flexibility to achieve in a prudent manner the investment objectives of the client, the Department of Justice (DOJ) to implement restoration actions on the Upper Clark Fork River Basin in accordance with the ARCO Settlement Consent Decree.

BACKGROUND INFORMATION

June 1999
On April 19, 1999, a consent decree entered into between the Atlantic Richfield Company (ARCO) and the State of Montana was approved by the Court, partially settling the lawsuit, Montana v. ARCO, USDC No. CV-83-317-H-PGH. In addition to payment of litigation costs and transfer to the State of two million dollars worth of land, ARCO has agreed to pay the State $118 million on or before July 18, 1999, plus interest from April 6, 1998. The interest to be paid by ARCO is to be based on the yield of the TFBP and the total cash payment should be approximately $128 million. The settlement amount is for environmental damages arising from injuries to the State's natural resources in the upper Clark Fork River Basin. Under the terms of the consent decree, and as required by law, the settlement amount and the interest thereon are to be deposited in the UCFRB Restoration Fund and may be used only to restore, replace or acquire the equivalent of the natural resources which were injured as a result ARCO's and its predecessors releases of hazardous substances.

July 1999
On July 19, 1999 ARCO paid the State $151,357,147. $119,348,156 was deposited into this account. This payment included the $118 million principal due plus interest from April 6, 1998.

DOJ is forecasting project spending of $5-7 million a year starting in calendar year 2001. In addition, Fish, Wildlife & Parks will be able to spend $3.7 million over the next 10 years. DOJ will also have some administrative expenses before 2001.

During July we purchased $70 million units in the TFPB and $20.5 million (par) corporate securities.

~~Since~~ 1999 - 2008
~~Since~~From 1999, the Citizen's Task Force and the Trustee Restoration Council ~~have~~ had been recommending that only interest earned on the principle in the coming years be expended, unless the trustee finds that it is appropriate to invade the principle to fund significant or time-critical projects.

The account balance ~~has~~ had been growing since spending ha~~s~~d not exceeded income ~~in any fiscal year from 2000 thru 2003 (see table on page 3).~~.
2009 In September 2009 the State purchased the Spotted Dog Ranch for a price of $15.2 million. Expenditures are expected to be in the $10 to $12 million range annually through 2018.

OBJECTIVES

~~Return Requirement: To maximize the total rate of return through a diversified portfolio of fixed income assets.~~

MONTANA BOARD OF INVESTMENTS
INVESTMENT POLICY STATEMENT
UPPER CLARK FORK RIVER BASIN (UCFRB) RESTORATION FUND ~~(FUND 02937)~~MU21
~~JANUARY 2004~~

~~Current Income: Current income is important since interest earned can be used to fund projects and for related administrative expenses.~~

~~Risk Tolerance: This is a State special revenue fund having an average ability to assume interest rate risk. Risk tolerance will decline if long-term investments have to be liquidated earlier than estimated.~~

Risk and Return:
A combination of current income, total return, and use of principle will be necessary to fund expected expenditures. It will require a return in excess of the assumed risk free rate to fund current projected expenditures, as well as possible future cost over runs. This account has an average ability to assume interest rate risk. Some risk of loss of principal must be taken to provide a return sufficient to fund objectives. An allocation to the Trust Funds Investments Pool (TFIP) will be made to obtain exposure to a diversified fixed income portfolio. An allocation to U.S. Treasuries, U.S. Agencies and Corporate securities may be made to provide a greater certainty of cash flows from maturities. Risk tolerance will decline if long-term investments have to be liquidated earlier than estimated to meet the cash draw down schedule.

~~CONSTRAINTS~~

~~Liquidity: Liquidity will be needed to fund restoration activities and related expenses. It is expected that the principal balance of $118 million will not be spent at least for the next few years.~~

~~Time Horizon: The fund is considered a long-term fund that has a time horizon beyond one year.~~

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

~~Legal Considerations: This fund is governed by state regulations, specifically, the "prudent expert principle" which requires the Board of Investments to: (a) discharge its duties with the care, skill, prudence, and diligence, under the circumstances then prevailing, that a prudent person acting in a like capacity with the same resources and familiar with like matters exercises in the conduct of an enterprise of a like character with like aims; (b) diversify the holdings of each fund within the unified investment program to minimize the risk of loss and to maximize the rate of return unless, under the circumstances, it is solely prudent not to do so; and (c) discharge the duties solely in the interest of and for the benefit of the funds forming the unified investment program.~~

~~The Montana Constitution does not allow equity type investments in non-retirement funds.~~
~~Unique Circumstances: The Governor is the trustee and has appointed a trustee restoration council consisting of the natural resource agency heads, his chief of staff and the Attorney General, as well as a citizen's task force to make recommendations on how to use the restoration fund.~~

~~Client Preference: None.~~

~~UPPER CLARK FORK RIVER BASIN (UCFRB) RESTORATION FUND~~
~~BACKGROUND INFORMATION~~

~~June 1999~~
~~On April 19, 1999, a consent decree entered into between the Atlantic Richfield Company (ARCO) and the State of Montana was approved by the Court, partially settling the lawsuit, Montana v. ARCO, USDC No. CV-83-317-H-PGH. In addition to payment of litigation costs and transfer to the State of two million dollars worth of land, ARCO has agreed to pay the State $118 million on or before July 18, 1999, plus~~

MONTANA BOARD OF INVESTMENTS
INVESTMENT POLICY STATEMENT
UPPER CLARK FORK RIVER BASIN (UCFRB) RESTORATION FUND ~~(FUND 02937)~~MU21
~~JANUARY 2004~~

~~interest from April 6, 1998. The interest to be paid by ARCO is to be based on the yield of the TFBP and the total cash payment should be approximately $128 million. The settlement amount is for environmental damages arising from injuries to the State's natural resources in the upper Clark Fork River Basin. Under the terms of the consent decree, and as required by law, the settlement amount and the interest thereon are to be deposited in the UCFRB Restoration Fund and may be used only to restore, replace or acquire the equivalent of the natural resources which were injured as a result ARCO's and its predecessors releases of hazardous substances.~~

~~July 1999~~
~~On July 19, 1999 ARCO paid the State $151,357,147. $119,348,156 was deposited into this account. This payment included the $118 million principal due plus interest from April 6, 1998.~~

~~DOJ is forecasting project spending of $5-7 million a year starting in calendar year 2001. In addition, Fish, Wildlife & Parks will be able to spend $3.7 million over the next 10 years. DOJ will also have some administrative expenses before 2001.~~

~~During July we purchased $70 million units in the TFPB and $20.5 million (par) corporate securities.~~

~~Since 1999~~
~~Since 1999, the Citizen's Task Force and the Trustee Restoration Council have been recommending that only interest earned on the principle in the coming years be expended, unless the trustee finds that it is appropriate to invade the principle to fund significant or time-critical projects.~~

~~The account balance has been growing since spending has not exceeded income in any fiscal year from 2000 thru 2003 (see table on page 3).~~

~~UPPER CLARK FORK RIVER BASIN (UCFRB) RESTORATION FUND~~
~~CASH FLOW SUMMARY~~
~~(in millions)~~

~~Fiscal Year~~	~~Addition to Fund~~	~~Book Value~~	~~Market Value~~	~~Total Inv. Income~~	~~Income Return~~	~~Spending/ Expenses~~
~~1999~~		~~$0.5~~	~~$0.5~~	~~$0.003~~		
~~7/31/99~~		~~119.6~~	~~118.9~~	~~N/A~~		
~~2000~~	~~6.8~~	~~126.4~~	~~122.9~~	~~8.108~~		~~$1.3~~
~~2001~~	~~4.3~~	~~130.7~~	~~132.3~~	~~9.299~~	~~7.23%~~	~~5.0~~
~~2002~~	~~6.9~~	~~137.6~~	~~140.8~~	~~9.514~~	~~7.09~~	~~2.6~~
~~2003~~	~~5.2~~	~~142.8~~	~~155.2~~	~~9.510~~	~~6.78~~	~~4.3~~
~~2004~~	~~6.5~~	~~149.3~~	~~154.0~~	~~10.043~~	~~6.88~~	~~3.5~~
~~9/30/04~~	~~1.4~~	~~150.7~~	~~157.4~~			

MONTANA BOARD OF INVESTMENTS
INVESTMENT POLICY STATEMENT
UPPER CLARK FORK RIVER BASIN (UCFRB) RESTORATION FUND ~~(FUND 02937)~~MU21
~~JANUARY 2004~~

	~~6-02~~	~~6-03~~	~~6-04~~	~~9-03~~	~~Ranges~~
~~U.S. Government/Agency Securities~~					
~~Domestic~~	~~3.2%~~	~~3.0%~~	~~2.7%~~	~~2.7%~~	~~0-30%~~
~~Mortgage-Backed~~	~~0.0~~	~~0.0~~	~~0.0~~	~~0.0~~	~~0-25~~
~~Corporate Securities~~					
~~Domestic~~	~~7.4~~	~~9.7~~	~~9.3~~	~~5.7~~	~~0-20~~
~~International (U.S. Pay)~~	~~0.0~~	~~0.0~~	~~0.0~~	~~0.0~~	~~0-10~~
~~Trust Funds Bond Pool (TFBP)~~	~~84.3~~	~~83.3~~	~~84.6~~	~~88.4~~	~~70-95~~
~~Short-Term Investment Pool (STIP)~~	~~5.1~~	~~4.0~~	~~3.4~~	~~3.2~~	~~2-10~~
~~Total Fixed-Income~~	~~100.0%~~	~~100.0%~~	~~100.0%~~	~~100.0%~~	~~100.0%~~

~~UPPER CLARK FORK RIVER BASIN (UCFRB) RESTORATION FUND~~

ASSET ALLOCATION
(at Market)

	Range
U.S. Treasury Bonds	0-30%
U.S. Agency Bonds	0-30%
Corporate Bonds	0-10%
Trust Funds Investment Pool (TFIB)	50-90%
Short Term Investment Pool (STIP)	0-30%
Total Fixed Income	100%

OTHER CONSIDERATIONS

Liquidity Needs:
Material annual expenditures are projected in each year through 2018 in the initial cash draw down schedule provided by DOJ. The timing of expenditures within the calendar year will be somewhat uncertain, thus necessitating a significant cash balance be available to meet these needs without forcing an inordinate amount of TFIP sales in any one year. There will be significant seasonality in the pattern of expenditures. Liquidity needs will be met with a combination of cash on hand, earnings, maturities and sales of investments. The minimum (STIP) balance will be the expected next one year of expenditures less expected maturities of individual securities prior to any adjustment to reflect funding needs.

Maturity Horizon:
The maturity horizon of the investments utilized is designed to meet the liabilities of the client with income,

MONTANA BOARD OF INVESTMENTS
INVESTMENT POLICY STATEMENT
UPPER CLARK FORK RIVER BASIN (UCFRB) RESTORATION FUND ~~(FUND 02937)~~MU21
~~JANUARY 2004~~

maturities and a reasonable amount of sales of securities and TFIP units. The liabilities are the cash needs for restoration expenditures as provided and updated by the DOJ. Expenditures are projected to occur through 2020.

Investment Limits:
1. To reduce the risk of loss on individual corporate bonds, investment purchases in any one credit will be limited to 1% of the market value of the fund at the date of purchase or 2% of the lowest projected fund balance before the securities mature, whichever is lower.
2. Corporate bond sector (Industrial, Finance, and Utility) exposure shall be constrained to no more than a 4% exposure at the time of purchase, or 6% at any time over the future projected fund balance.
3. The quality rating of any corporate bond shall be in the top of the single-A rating classification or better at the time of purchase. (e.g., A1/A+ or higher), and have at least two ratings.
4. Exposure to the securities of any one U.S. Agency are limited to 5%, and in no event will an agency security be purchased if it carries a rating lower than that of the U. S. Government.

Legal Considerations:
This fund is governed by state regulations, specifically, the "prudent expert principle" which requires the Board of Investments to: (a) discharge the duties with the care, skill, prudence, and diligence, under the circumstances then prevailing, that a prudent person acting in a like capacity with the same resources and familiar with like matters exercises in the conduct of an enterprise of a like character with like aims; (b) diversify the holdings of each fund within the unified investment program to minimize the risk of loss and to maximize the rate of return unless, under the circumstances, it is solely prudent not to do so; and (c) discharge the duties solely in the interest of and for the benefit of the funds forming the unified investment program.

The Montana Constitution does not allow equity type investments in non-retirement funds.

ADMINISTRATIVE

Securities Lending:

Section 17-1-113, MCA, authorizes the Board to lend securities held by the state. The Board may lend its publicly traded securities held in the investment pools, through an agent, to other market participants in return for compensation. Currently, through an explicit contract, State Street Bank and Trust, the state's custodial bank, manages the state's securities lending program. The Board seeks to assess the risks, such as counterparty and reinvestment risk, associated with each aspect of its securities lending program. The Board requires borrowers to maintain collateral at 102 percent for domestic securities and 105 percent for international securities. To ensure that the collateral ratio is maintained, securities on loan are marked to market daily and the borrower must provide additional collateral if the value of the securities on loan increases. In addition to the strict collateral requirements imposed by the Board, the credit quality of approved borrowers is monitored continuously by the contractor. From time to time, Staff or the investment manager may restrict a security from the loan program upon notification to State Street Bank. Staff will monitor the securities lending program, and the CIO will periodically report to the Board on the status of the program.

MONTANA BOARD OF INVESTMENTS
INVESTMENT POLICY STATEMENT
UPPER CLARK FORK RIVER BASIN (UCFRB) RESTORATION FUND MU21

INTRODUCTION

The purpose of this investment policy statement is to outline the account objectives, permissible investments, and constraints that will guide the management of the portfolio. The policy is designed to give the investment manager flexibility to achieve in a prudent manner the investment objectives of the client, the Department of Justice (DOJ) to implement restoration actions on the Upper Clark Fork River Basin in accordance with the ARCO Settlement Consent Decree.

BACKGROUND INFORMATION

June 1999

On April 19, 1999, a consent decree entered into between the Atlantic Richfield Company (ARCO) and the State of Montana was approved by the Court, partially settling the lawsuit, Montana v. ARCO, USDC No. CV-83-317-H-PGH. In addition to payment of litigation costs and transfer to the State of two million dollars worth of land, ARCO has agreed to pay the State $118 million on or before July 18, 1999, plus interest from April 6, 1998. The interest to be paid by ARCO is to be based on the yield of the TFBP and the total cash payment should be approximately $128 million. The settlement amount is for environmental damages arising from injuries to the State's natural resources in the upper Clark Fork River Basin. Under the terms of the consent decree, and as required by law, the settlement amount and the interest thereon are to be deposited in the UCFRB Restoration Fund and may be used only to restore, replace or acquire the equivalent of the natural resources which were injured as a result ARCO's and its predecessors releases of hazardous substances.

July 1999

On July 19, 1999 ARCO paid the State $151,357,147. $119,348,156 was deposited into this account. This payment included the $118 million principal due plus interest from April 6, 1998.

DOJ is forecasting project spending of $5-7 million a year starting in calendar year 2001. In addition, Fish, Wildlife & Parks will be able to spend $3.7 million over the next 10 years. DOJ will also have some administrative expenses before 2001.

During July we purchased $70 million units in the TFPB and $20.5 million (par) corporate securities.

1999 - 2008

From 1999, the Citizen's Task Force and the Trustee Restoration Council had been recommending that only interest earned on the principle in the coming years be expended, unless the trustee finds that it is appropriate to invade the principle to fund significant or time-critical projects.

The account balance had been growing since spending had not exceeded income.

2009

In September 2009 the State purchased the Spotted Dog Ranch for a price of $15.2 million. Expenditures are expected to be in the $10 to $12 million range annually through 2018.

MONTANA BOARD OF INVESTMENTS
INVESTMENT POLICY STATEMENT
UPPER CLARK FORK RIVER BASIN (UCFRB) RESTORATION FUND MU21

OBJECTIVES

Risk and Return:
A combination of current income, total return, and use of principle will be necessary to fund expected expenditures. It will require a return in excess of the assumed risk free rate to fund current projected expenditures, as well as possible future cost over runs. This account has an average ability to assume interest rate risk. Some risk of loss of principal must be taken to provide a return sufficient to fund objectives. An allocation to the Trust Funds Investments Pool (TFIP) will be made to obtain exposure to a diversified fixed income portfolio. An allocation to U.S. Treasuries, U.S. Agencies and Corporate securities may be made to provide a greater certainty of cash flows from maturities. Risk tolerance will decline if long-term investments have to be liquidated earlier than estimated to meet the cash draw down schedule.

ASSET ALLOCATION
(at Market)

Fixed Income	**Range**
U.S. Treasury Bonds	0-30%
U.S. Agency Bonds	0-30%
Corporate Bonds	0-10%
Trust Funds Investment Pool (TFIB)	50-90%
Short Term Investment Pool (STIP)	0-30%
Total Fixed Income	**100%**

OTHER CONSIDERATIONS

Liquidity Needs:
Material annual expenditures are projected in each year through 2018 in the initial cash draw down schedule provided by DOJ. The timing of expenditures within the calendar year will be somewhat uncertain, thus necessitating a significant cash balance be available to meet these needs without forcing an inordinate amount of TFIP sales in any one year. There will be significant seasonality in the pattern of expenditures. Liquidity needs will be met with a combination of cash on hand, earnings, maturities and sales of investments. The minimum (STIP) balance will be the expected next one year of expenditures less expected maturities of individual securities prior to any adjustment to reflect funding needs.

Maturity Horizon:
The maturity horizon of the investments utilized is designed to meet the liabilities of the client with income, maturities and a reasonable amount of sales of securities and TFIP units. The liabilities are the cash needs for restoration expenditures as provided and updated by the DOJ. Expenditures are projected to occur through 2020.

MONTANA BOARD OF INVESTMENTS
INVESTMENT POLICY STATEMENT
UPPER CLARK FORK RIVER BASIN (UCFRB) RESTORATION FUND MU21

<u>Investment Limits:</u>

1. To reduce the risk of loss on individual corporate bonds, investment purchases in any one credit will be limited to 1% of the market value of the fund at the date of purchase or 2% of the lowest projected fund balance before the securities mature, whichever is lower.
2. Corporate bond sector (Industrial, Finance, and Utility) exposure shall be constrained to no more than a 4% exposure at the time of purchase, or 6% at any time over the future projected fund balance.
3. The quality rating of any corporate bond shall be in the top of the single-A rating classification or better at the time of purchase. (e.g., A1/A+ or higher), and have at least two ratings.
4. Exposure to the securities of any one U.S. Agency are limited to 5%, and in no event will an agency security be purchased if it carries a rating lower than that of the U. S. Government.

<u>Legal Considerations</u>:

This fund is governed by state regulations, specifically, the "prudent expert principle" which requires the Board of Investments to: (a) discharge the duties with the care, skill, prudence, and diligence, under the circumstances then prevailing, that a prudent person acting in a like capacity with the same resources and familiar with like matters exercises in the conduct of an enterprise of a like character with like aims; (b) diversify the holdings of each fund within the unified investment program to minimize the risk of loss and to maximize the rate of return unless, under the circumstances, it is solely prudent not to do so; and (c) discharge the duties solely in the interest of and for the benefit of the funds forming the unified investment program.

The Montana Constitution does not allow equity type investments in non-retirement funds.

ADMINISTRATIVE

<u>Securities Lending:</u>

Section 17-1-113, MCA, authorizes the Board to lend securities held by the state. The Board may lend its publicly traded securities held in the investment pools, through an agent, to other market participants in return for compensation. Currently, through an explicit contract, State Street Bank and Trust, the state's custodial bank, manages the state's securities lending program. The Board seeks to assess the risks, such as counterparty and reinvestment risk, associated with each aspect of its securities lending program. The Board requires borrowers to maintain collateral at 102 percent for domestic securities and 105 percent for international securities. To ensure that the collateral ratio is maintained, securities on loan are marked to market daily and the borrower must provide additional collateral if the value of the securities on loan increases. In addition to the strict collateral requirements imposed by the Board, the credit quality of approved borrowers is monitored continuously by the contractor. From time to time, Staff or the investment manager may restrict a security from the loan program upon notification to State Street Bank. Staff will monitor the securities lending program, and the CIO will periodically report to the Board on the status of the program.

MONTANA BOARD OF INVESTMENTS
BUTTE AREA ONE RESTORATION FUND (MU3F) (FUND 08219)
INVESTMENT POLICY STATEMENT

INTRODUCTION

The purpose of this investment policy statement is to outline the account objectives, permissible investments, and constraints that will guide the management of the portfolio. The policy is designed to give the investment manager flexibility to achieve in a prudent manner the investment objectives of the client, the Department of Justice (DOJ) to implement the remedial action ("the Remedy") on the Butte Area One Restoration in accordance with the ARCO Settlement Consent Decree.

BACKGROUND INFORMATION

In August 2008, a Consent Decree was entered between the State of Montana and Atlantic Richfield Company (ARCO), in order to settle certain litigation and to provide for the funding of the restoration action at Butte Area One (BAO). The settlement involves, among other things, payment by ARCO of $28.0 million including accrued interest from April 1, 2006. Those funds and the earnings from the investment of those funds are to be used by the State for the purpose of restoration of the BAO over an estimated seven year period.

Major construction is projected to begin during calendar year 2009 and end during calendar year 2018.

The project being financed through this fund is for projects that restore, replace or acquire the equivalent of injured natural resources or lost services. The nature of restoration work includes the potential for cost overruns and unexpected expenses. DOJ will use its best efforts to inform the Board of Investments of any expected overruns or changes in the cash draw schedule and will attempt to provide notice of such changes as much in advance as possible.

OBJECTIVES

Risk and Return:

Earnings alone will not be sufficient to fund expected expenditures nor will the principle provided by the settlement be sufficient. A combination of current income, total return, and use of principle will be necessary to fund the expected expenditures. It will require a return in excess of the assumed risk free rate to fund current projected expenditures, as well as possible future cost over runs. This account has an average ability to assume interest rate risk. Some risk of loss of principal must be taken to provide a return sufficient to fund objectives. An allocation to the Trust Funds ~~Bond~~ Investments Pool (~~TFBP~~TFIP) will be made to obtain exposure to a diversified fixed income portfolio. An allocation to U.S. Treasuries, U.S. Agencies and Corporate securities may be made to provide a greater certainty of cash flows from maturities. Risk tolerance will decline if long-term investments have to be liquidated earlier than estimated to meet the cash draw down schedule.

There was $28.1 million in the account as of December 31, 2008, invested solely in the Short-term Investment Pool (STIP).The risk and return factors along with other considerations result in the expected asset allocation shown below.

MONTANA BOARD OF INVESTMENTS
BUTTE AREA ONE RESTORATION FUND (MU3F) (FUND 08219)
INVESTMENT POLICY STATEMENT

Asset Allocation

~~**Fixed Income**~~	~~**Range**~~
~~U.S. Treasury Bonds~~	~~0-10%~~
~~U.S. Agency Bonds~~	~~0-50%~~
~~Corporate Bonds~~	~~0-10%~~
~~Trust Funds Investment Pool (TFBP)~~	~~30-70%~~
~~Short Term Investment Pool (STIP)~~	~~0-20%~~
~~**Total Fixed Income**~~	~~100%~~

Fixed Income	**Range**
U.S. Treasury Bonds	0-10%
U.S. Agency Bonds	0-50%
Corporate Bonds	0-10%
Trust Funds Investment Pool (TFIP)	0-70%
Short Term Investment Pool (STIP)	0-50%
Total Fixed Income	100%

OTHER CONSIDERATIONS

Liquidity Needs:
Material annual expenditures are projected in each year through 2018 in the initial cash draw down schedule provided by DOJ. The timing of expenditures within the calendar year will be somewhat uncertain, thus necessitating a significant cash balance be available to meet these needs without forcing an inordinate amount of TFBP sales in any one year. There will be significant seasonality in the pattern of expenditures. Liquidity needs will be met with a combination of cash on hand, earnings, maturities and sales of investments. The minimum Short Term Investment Pool (STIP) balance will be the expected next one year of expenditures less expected maturities of individual securities prior to any adjustment to reflect funding needs.

Maturity Horizon:
The maturity horizon of the investments utilized is designed to meet the liabilities of the client with income, maturities and a reasonable amount of sales of securities and ~~TFBP~~ TFIP units. The liabilities are the cash needs for restoration expenditures as provided by the DOJ at the outset of the account and as modifications are made in ensuring years. At this time expenditures are expected to occur commencing immediately and each year through 2015, with the majority occurring during years 2010 - ~~2018~~2015.

MONTANA BOARD OF INVESTMENTS
BUTTE AREA ONE RESTORATION FUND (MU3F) (FUND 08219)
INVESTMENT POLICY STATEMENT

Investment Limits:

1. To reduce the risk of loss on individual corporate bonds, investment purchases in any one credit will be limited to 1% of the market value of the fund at the date of purchase or 2% of the lowest projected fund balance before the securities mature, ~~which ever~~whichever is lower.
2. Corporate bond sector (Industrial, Finance, and Utility) exposure shall be constrained to no more than a 4% exposure at the time of purchase, or 6% at any time over the future projected fund balance.
3. The quality rating of any corporate bond shall be in the top of the single-A rating classification or better at the time of purchase. (e.g., A1/A+ or higher), and have at least two ratings.
4. Exposure to the securities of any one U.S. Agency are limited to 5%, and in no event will an agency security be purchased if it carries a rating ~~that is less than top-rated (AAA) at the time of purchase~~ lower than that of the U. S. Government.

Legal Considerations:

This fund is governed by state regulations, specifically, the "prudent expert principle" which requires the Board of Investments to: (a) discharge the duties with the care, skill, prudence, and diligence, under the circumstances then prevailing, that a prudent person acting in a like capacity with the same resources and familiar with like matters exercises in the conduct of an enterprise of a like character with like aims; (b) diversify the holdings of each fund within the unified investment program to minimize the risk of loss and to maximize the rate of return unless, under the circumstances, it is solely prudent not to do so; and (c) discharge the duties solely in the interest of and for the benefit of the funds forming the unified investment program.

The Montana Constitution does not allow equity type investments in non-retirement funds.

ADMINISTRATIVE

Securities Lending:

Section 17-1-113, MCA, authorizes the Board to lend securities held by the state. The Board may lend its publicly traded securities held in the investment pools, through an agent, to other market participants in return for compensation. Currently, through an explicit contract, State Street Bank and Trust, the state's custodial bank, manages the state's securities lending program. The Board seeks to assess the risks, such as counterparty and reinvestment risk, associated with each aspect of its securities lending program. The Board requires borrowers to maintain collateral at 102 percent for domestic securities and 105 percent for international securities. To ensure that the collateral ratio is maintained, securities on loan are marked to market daily and the borrower must provide additional collateral if the value of the securities on loan increases. In addition to the strict collateral requirements imposed by the Board, the credit quality of approved borrowers is monitored continuously by the contractor. From time to time, Staff or the investment manager may restrict a security from the loan program upon notification to State Street Bank. Staff will monitor the securities lending program, and the CIO will periodically report to the Board on the status of the program.

MONTANA BOARD OF INVESTMENTS
BUTTE AREA ONE RESTORATION FUND (MU3F) (FUND 08219)
INVESTMENT POLICY STATEMENT

INTRODUCTION

The purpose of this investment policy statement is to outline the account objectives, permissible investments, and constraints that will guide the management of the portfolio. The policy is designed to give the investment manager flexibility to achieve in a prudent manner the investment objectives of the client, the Department of Justice (DOJ) to implement the remedial action ("the Remedy") on the Butte Area One Restoration in accordance with the ARCO Settlement Consent Decree.

BACKGROUND INFORMATION

In August 2008, a Consent Decree was entered between the State of Montana and Atlantic Richfield Company (ARCO), in order to settle certain litigation and to provide for the funding of the restoration action at Butte Area One (BAO). The settlement involves, among other things, payment by ARCO of $28.0 million including accrued interest from April 1, 2006. Those funds and the earnings from the investment of those funds are to be used by the State for the purpose of restoration of the BAO over an estimated seven year period.

Major construction is projected to begin during calendar year 2009 and end during calendar year 2018.

The project being financed through this fund is for projects that restore, replace or acquire the equivalent of injured natural resources or lost services. The nature of restoration work includes the potential for cost overruns and unexpected expenses. DOJ will use its best efforts to inform the Board of Investments of any expected overruns or changes in the cash draw schedule and will attempt to provide notice of such changes as much in advance as possible.

OBJECTIVES

<u>Risk and Return:</u>
Earnings alone will not be sufficient to fund expected expenditures nor will the principle provided by the settlement be sufficient. A combination of current income, total return, and use of principle will be necessary to fund the expected expenditures. It will require a return in excess of the assumed risk free rate to fund current projected expenditures, as well as possible future cost over runs. This account has an average ability to assume interest rate risk. Some risk of loss of principal must be taken to provide a return sufficient to fund objectives. An allocation to the Trust Funds Investments Pool (TFIP) will be made to obtain exposure to a diversified fixed income portfolio. An allocation to U.S. Treasuries, U.S. Agencies and Corporate securities may be made to provide a greater certainty of cash flows from maturities. Risk tolerance will decline if long-term investments have to be liquidated earlier than estimated to meet the cash draw down schedule.

There was $28.1 million in the account as of December 31, 2008, invested solely in the Short-term Investment Pool (STIP).The risk and return factors along with other considerations result in the expected asset allocation shown below.

MONTANA BOARD OF INVESTMENTS
BUTTE AREA ONE RESTORATION FUND (MU3F) (FUND 08219)
INVESTMENT POLICY STATEMENT

Asset Allocation

Fixed Income	Range
U.S. Treasury Bonds	0-10%
U.S. Agency Bonds	0-50%
Corporate Bonds	0-10%
Trust Funds Investment Pool (TFIP)	0-70%
Short Term Investment Pool (STIP)	0-50%
Total Fixed Income	100%

OTHER CONSIDERATIONS

Liquidity Needs:
Material annual expenditures are projected in each year through 2018 in the initial cash draw down schedule provided by DOJ. The timing of expenditures within the calendar year will be somewhat uncertain, thus necessitating a significant cash balance be available to meet these needs without forcing an inordinate amount of TFBP sales in any one year. There will be significant seasonality in the pattern of expenditures. Liquidity needs will be met with a combination of cash on hand, earnings, maturities and sales of investments. The minimum Short Term Investment Pool (STIP) balance will be the expected next one year of expenditures less expected maturities of individual securities prior to any adjustment to reflect funding needs.

Maturity Horizon:
The maturity horizon of the investments utilized is designed to meet the liabilities of the client with income, maturities and a reasonable amount of sales of securities and ~~TFBP~~ TFIP units. The liabilities are the cash needs for restoration expenditures as provided by the DOJ at the outset of the account and as modifications are made in ensuring years. At this time expenditures are expected to occur commencing immediately and each year through 2015, with the majority occurring during years 2010 - 2015.

Investment Limits:
1. To reduce the risk of loss on individual corporate bonds, investment purchases in any one credit will be limited to 1% of the market value of the fund at the date of purchase or 2% of the lowest projected fund balance before the securities mature, whichever is lower.
2. Corporate bond sector (Industrial, Finance, and Utility) exposure shall be constrained to no more than a 4% exposure at the time of purchase, or 6% at any time over the future projected fund balance.
3. The quality rating of any corporate bond shall be in the top of the single-A rating classification or better at the time of purchase. (e.g., A1/A+ or higher), and have at least two ratings.
4. Exposure to the securities of any one U.S. Agency are limited to 5%, and in no event will an agency security be purchased if it carries a rating lower than that of the U. S. Government.

MONTANA BOARD OF INVESTMENTS
BUTTE AREA ONE RESTORATION FUND (MU3F) (FUND 08219)
INVESTMENT POLICY STATEMENT

Legal Considerations:

This fund is governed by state regulations, specifically, the "prudent expert principle" which requires the Board of Investments to: (a) discharge the duties with the care, skill, prudence, and diligence, under the circumstances then prevailing, that a prudent person acting in a like capacity with the same resources and familiar with like matters exercises in the conduct of an enterprise of a like character with like aims; (b) diversify the holdings of each fund within the unified investment program to minimize the risk of loss and to maximize the rate of return unless, under the circumstances, it is solely prudent not to do so; and (c) discharge the duties solely in the interest of and for the benefit of the funds forming the unified investment program.

The Montana Constitution does not allow equity type investments in non-retirement funds.

ADMINISTRATIVE

Securities Lending:

Section 17-1-113, MCA, authorizes the Board to lend securities held by the state. The Board may lend its publicly traded securities held in the investment pools, through an agent, to other market participants in return for compensation. Currently, through an explicit contract, State Street Bank and Trust, the state's custodial bank, manages the state's securities lending program. The Board seeks to assess the risks, such as counterparty and reinvestment risk, associated with each aspect of its securities lending program. The Board requires borrowers to maintain collateral at 102 percent for domestic securities and 105 percent for international securities. To ensure that the collateral ratio is maintained, securities on loan are marked to market daily and the borrower must provide additional collateral if the value of the securities on loan increases. In addition to the strict collateral requirements imposed by the Board, the credit quality of approved borrowers is monitored continuously by the contractor. From time to time, Staff or the investment manager may restrict a security from the loan program upon notification to State Street Bank. Staff will monitor the securities lending program, and the CIO will periodically report to the Board on the status of the program.

Pending Approval: April 2 2013

MONTANA BOARD OF INVESTMENTS
MONTANA STATE UNIVERSITY (MU81) (FUND 80200)
INVESTMENT POLICY STATEMENT

INTRODUCTION

This account is an operating account with high liquidity needs but does have a core amount that is long term in nature and can be invested in the TFIP to achieve a higher level of investment income.

OBJECTIVES

The objective is to increase the investment income above that available in STIP.

PERMISSABLE INVESTMENTS

This account may invest in STIP and TFIP. It is not anticipated that individual securities will be held in this account.

ASSET ALLOCATION
(at market)

FIXED INCOME	Range
Trust Funds Investment Pool (TFIP)	0-30%
Short-term Investment Pool (STIP)	70-100%
Total Fixed Income	100.0%

LEGAL CONSIDERATIONS

This fund is governed by state regulations, specifically, the "prudent expert principle" which requires the Board of Investments to: (a) discharge its duties with the care, skill, prudence, and diligence, under the circumstances then prevailing, that a prudent person acting in a like capacity with the same resources and familiar with like manners exercises in the conduct of an enterprise of a like character with like aims; (b) diversify the holdings of each fund within the unified investment program to minimize the risk of loss and to maximize the rate of return unless, under the circumstances, it is clearly prudent not to do so; and (c) discharge the duties solely in the interest of and for the benefit the funds forming the unified investment program. The Montana Constitution does not allow equity type investments in non-retirement accounts.

Pending Approval: April 2 2013

MONTANA BOARD OF INVESTMENTS
MONTANA TECH (UM) (MU80) (FUND 80500)
INVESTMENT POLICY STATEMENT

INTRODUCTION

This account is an operating account with high liquidity needs but does have a core amount that is long term in nature and can be invested in the TFIP to achieve a higher level of investment income.

OBJECTIVES

The objective is to increase the investment income above that available in STIP.

PERMISSABLE INVESTMENTS

This account may invest in STIP and TFIP. It is not anticipated that individual securities will be held in this account.

ASSET ALLOCATION
(at market)

FIXED INCOME	Range
Trust Funds Investment Pool (TFIP)	0-30%
Short-term Investment Pool (STIP)	70-100%
Total Fixed Income	100.0%

LEGAL CONSIDERATIONS

This fund is governed by state regulations, specifically, the "prudent expert principle" which requires the Board of Investments to: (a) discharge its duties with the care, skill, prudence, and diligence, under the circumstances then prevailing, that a prudent person acting in a like capacity with the same resources and familiar with like manners exercises in the conduct of an enterprise of a like character with like aims; (b) diversify the holdings of each fund within the unified investment program to minimize the risk of loss and to maximize the rate of return unless, under the circumstances, it is clearly prudent not to do so; and (c) discharge the duties solely in the interest of and for the benefit the funds forming the unified investment program. The Montana Constitution does not allow equity type investments in non-retirement accounts.

MONTANA BOARD OF INVESTMENTS
CORE INTERNAL BOND PORTFOLIO (CIBP MU40)
INVESTMENT POLICY STATEMENT

INTRODUCTION

The purpose of this policy statement is to provide a broad strategic framework for fixed income investments within the Core Internal Bond Portfolio (CIBP). The CIBP is managed internally by MBOI staff on behalf of the Retirement Funds Bond Pool (RFBP). The portfolio managers are governed by the investment management guidelines contained herein. The broad investment strategy is core-like and is to be benchmarked against the Barclays Capital Aggregate Bond Index.

OBJECTIVES

Strategic: Attain~~ing~~ competitive investment returns in the fixed income markets while diversifying investment risk. The primary objective of the Core Internal Bond Portfolio is to provide diversified exposure to the various sectors of the bond market for the benefit of pension fund participants in a prudent and cost effective manner. The internal portfolio will also provide primary liquidity to retirement fund participants. Finally, the CIBP will act as the foundation or core of the fixed income asset class and as a complement to the higher risk mandates run by external bond managers.

Performance: The return objective of the CIBP is to achieve an annualized time weighted total return exceeding that of the Barclays Capital Aggregate Bond Index over a three year rolling period.

PERMITTED INVESTMENTS

- Debt obligations of the U.S. Government, including its agencies and instrumentalities. These include Treasuries, Treasury Inflation Protected Securities (TIPS) and fixed and floating rate agency obligations.
- Dollar denominated debt obligations of developed country foreign governments.
- Dollar denominated debt obligations of index-eligible supranational agencies.
- Dollar denominated debt obligations of domestic and foreign corporations (Yankee bonds) up to 2% of portfolio assets per issuer. These may include trust preferred securities and be fixed or floating rate coupon structures.
- Securitized assets, including U.S. Agency mortgage pass through securities (MBS), non agency MBS (limited to 3% of portfolio market value in total), collateralized mortgage obligations (CMOs), commercial mortgage backed securities (CMBS), hybrid ARMS and asset backed securities.
- When-issued securities.
- Rule 144a securities.
- Medium term notes.

PROHIBITED INVESTMENTS

- Over the counter derivatives, including interest rate swaps and credit default swaps.
- Short sales and securities margin loans.
- Bank loans.
- Interest only (IO) and principal only (PO) mortgage strips.
- Companion/residual/equity tranches of CMOs or other structured securitizations.
- Capital securities (convertible from fixed to floating)
- Inverse floaters.
- Convertible bonds.

MONTANA BOARD OF INVESTMENTS
CORE INTERNAL BOND PORTFOLIO (CIBP MU40)
INVESTMENT POLICY STATEMENT

CONSTRAINTS

Credit quality: Securities must be rated investment grade, or no lower than triple-B-minus, by ~~one~~ two nationally recognized securities rating organizations (NRSRO) at ~~the~~ time of purchase, with the exception of non-rated securities issued or guaranteed by agencies or instrumentalities of the U.S. Government. ~~Split rated securities may not exceed 3% of portfolio market value.~~ Securities downgraded below investment grade may be held at the manager's discretion. Non-rated securities will be assigned an internal rating.

Duration: The weighted average effective duration of the portfolio, including cash, must be within 20% of the duration of the Lehman Aggregate Bond index.

Sector: The portfolio sector exposure will be maintained within the ranges highlighted in the table below. Recent exposures by sector for the portfolio and benchmark index are shown for reference.

ASSET ALLOCATION SECTORS & RANGES
~~12/31/08~~
(At market)

Sectors	~~CIBP~~	~~Agg Index~~	**Policy Ranges**
U.S. Treasury	~~5.30%~~	~~25.07%~~	**~~10~~15-~~35~~45**
Government-Related	~~7.96~~	~~13.54~~	**5-~~25~~15**
Total Government	~~13.26~~	~~38.61~~	**20-~~55~~60**
MBS ~~(Fixed Rate)~~	~~36.46~~	~~36.63~~	**20~~-50~~-40**
~~Hybrid ARMS~~	~~0.00~~	~~2.95~~	**~~0-10~~**
Asset-Backed Securities	~~0.00~~	~~0.59~~	**0-~~5~~7**
CMBS	~~3.29~~	~~3.55~~	**0-~~10~~12**
Total Structured	~~39.75~~	~~43.72~~	**20-~~75~~59**
Corporate Credit	~~44.32~~	~~17.67~~	**10-~~35~~40**
~~Cash (STIP)~~	~~2.67~~	~~0.00~~	**~~0-10~~**
Total	~~100.0%~~	~~100.0%~~	**100.0%**

~~Current portfolio exceptions to the above policy ranges will be addressed over time depending on market conditions with the objective of moving within compliance.~~

LIQUIDITY

Liquidity needs for the fixed income program are low, as participant capital allocated to the pool is not expected to change dramatically on short notice. Nevertheless, the underlying assets held are predominantly publicly traded securities which can normally be liquidated in a relatively short period to accommodate broad asset allocation changes between fixed income and other asset categories held by retirement plan participants. Assets considered to be generally illiquid will be limited to 10% of the portfolio's market value.

MONTANA BOARD OF INVESTMENTS
CORE INTERNAL BOND PORTFOLIO (CIBP MU40)
INVESTMENT POLICY STATEMENT

ADMINISTRATIVE

Securities Lending:

Section 17-1-113, MCA, authorizes the Board to lend securities held by the state. The Board may lend its publicly traded securities held in the investment pools, through an agent, to other market participants in return for compensation. Currently, through an explicit contract, State Street Bank and Trust, the state's custodial bank, manages the state's securities lending program. The Board seeks to assess the risks, such as counterparty and reinvestment risk, associated with each aspect of its securities lending program. The Board requires borrowers to maintain collateral at 102 percent for domestic securities and 105 percent for international securities. To ensure that the collateral ratio is maintained, securities on loan are marked to market daily and the borrower must provide additional collateral if the value of the securities on loan increases. In addition to the strict collateral requirements imposed by the Board, the credit quality of approved borrowers is monitored continuously by the contractor. From time to time, Staff or the investment manager may restrict a security from the loan program upon notification to State Street Bank. Staff will monitor the securities lending program, and the CIO will periodically report to the Board on the status of the program.

MONTANA BOARD OF INVESTMENTS
CORE INTERNAL BOND PORTFOLIO (CIBP MU40)
INVESTMENT POLICY STATEMENT

INTRODUCTION

The purpose of this policy statement is to provide a broad strategic framework for fixed income investments within the Core Internal Bond Portfolio (CIBP). The CIBP is managed internally by MBOI staff on behalf of the Retirement Funds Bond Pool (RFBP). The portfolio managers are governed by the investment management guidelines contained herein. The broad investment strategy is core-like and is to be benchmarked against the Barclays Capital Aggregate Bond Index.

OBJECTIVES

Strategic: Attain competitive investment returns in the fixed income markets while diversifying investment risk. The primary objective of the Core Internal Bond Portfolio is to provide diversified exposure to the various sectors of the bond market for the benefit of pension fund participants in a prudent and cost effective manner. The internal portfolio will also provide primary liquidity to retirement fund participants. Finally, the CIBP will act as the foundation or core of the fixed income asset class and as a complement to the higher risk mandates run by external bond managers.
Performance: The return objective of the CIBP is to achieve an annualized time weighted total return exceeding that of the Barclays Capital Aggregate Bond Index over a three year rolling period.

PERMITTED INVESTMENTS

- Debt obligations of the U.S. Government, including its agencies and instrumentalities. These include Treasuries, Treasury Inflation Protected Securities (TIPS) and fixed and floating rate agency obligations.
- Dollar denominated debt obligations of developed country foreign governments.
- Dollar denominated debt obligations of index-eligible supranational agencies.
- Dollar denominated debt obligations of domestic and foreign corporations (Yankee bonds) up to 2% of portfolio assets per issuer. These may include trust preferred securities and be fixed or floating rate coupon structures.
- Securitized assets, including U.S. Agency mortgage pass through securities (MBS), non agency MBS (limited to 3% of portfolio market value in total), collateralized mortgage obligations (CMOs), commercial mortgage backed securities (CMBS), hybrid ARMS and asset backed securities.
- When-issued securities.
- Rule 144a securities.
- Medium term notes.

PROHIBITED INVESTMENTS

- Over the counter derivatives, including interest rate swaps and credit default swaps.
- Short sales and securities margin loans.
- Bank loans.
- Interest only (IO) and principal only (PO) mortgage strips.
- Companion/residual/equity tranches of CMOs or other structured securitizations.
- Capital securities (convertible from fixed to floating).
- Inverse floaters.
- Convertible bonds.

MONTANA BOARD OF INVESTMENTS
CORE INTERNAL BOND PORTFOLIO (CIBP MU40)
INVESTMENT POLICY STATEMENT

CONSTRAINTS

Credit quality: Securities must be rated investment grade, or no lower than triple-B-minus, by two nationally recognized securities rating organizations (NRSRO) at time of purchase, with the exception of non-rated securities issued or guaranteed by agencies or instrumentalities of the U.S. Government. Securities downgraded below investment grade may be held at the manager's discretion. Non-rated securities will be assigned an internal rating.

Duration: The weighted average effective duration of the portfolio, including cash, must be within 20% of the duration of the Lehman Aggregate Bond index.

Sector: The portfolio sector exposure will be maintained within the ranges highlighted in the table below. Recent exposures by sector for the portfolio and benchmark index are shown for reference.

ASSET ALLOCATION SECTORS & RANGES
(At market)

Sectors	Policy Ranges
U.S. Treasury	**15-45**
Government-Related	**5-15**
Total Government	**20-60**
MBS	**20-40**
Asset-Backed Securities	**0-7**
CMBS	**0-12**
Total Structured	**20-59**
Corporate Credit	**10-40**
Total	**100.0%**

LIQUIDITY

Liquidity needs for the fixed income program are low, as participant capital allocated to the pool is not expected to change dramatically on short notice. Nevertheless, the underlying assets held are predominantly publicly traded securities which can normally be liquidated in a relatively short period to accommodate broad asset allocation changes between fixed income and other asset categories held by retirement plan participants. Assets considered to be generally illiquid will be limited to 10% of the portfolio's market value.

MONTANA BOARD OF INVESTMENTS
CORE INTERNAL BOND PORTFOLIO (CIBP MU40)
INVESTMENT POLICY STATEMENT

ADMINISTRATIVE

Securities Lending:

Section 17-1-113, MCA, authorizes the Board to lend securities held by the state. The Board may lend its publicly traded securities held in the investment pools, through an agent, to other market participants in return for compensation. Currently, through an explicit contract, State Street Bank and Trust, the state's custodial bank, manages the state's securities lending program. The Board seeks to assess the risks, such as counterparty and reinvestment risk, associated with each aspect of its securities lending program. The Board requires borrowers to maintain collateral at 102 percent for domestic securities and 105 percent for international securities. To ensure that the collateral ratio is maintained, securities on loan are marked to market daily and the borrower must provide additional collateral if the value of the securities on loan increases. In addition to the strict collateral requirements imposed by the Board, the credit quality of approved borrowers is monitored continuously by the contractor. From time to time, Staff or the investment manager may restrict a security from the loan program upon notification to State Street Bank. Staff will monitor the securities lending program, and the CIO will periodically report to the Board on the status of the program.

MONTANA BOARD OF INVESTMENTS
TRUST FUNDS INVESTMENT POOL (MU41) (FUND 07112)
INVESTMENT POLICY STATEMENT

INTRODUCTION

The purpose of this policy statement is to provide a broad strategic framework for investments within the Trust Funds Investment Pool (TFIP). The pool's participants consist primarily of the state's trust funds. The pool is designed to provide the participants exposure to a portfolio of diversified income-producing assets. The pool's assets include an investment grade fixed income portfolio managed internally by MBOI staff, one or more core real estate funds, and one or more high yield fixed income funds. Allocation across these asset classes is limited to the following ranges. The use of high yield fixed income and core real estate investments are justified in order to diversify the sources of income provided by the pool, however are constrained to prudent levels of maximum exposure given their unique and somewhat more volatile return patterns.

Asset Class	Minimum	Maximum
Investment grade fixed income	0%	100%
High yield fixed income	0%	10%
Core real estate	0%	8%

The primary component of the pool consists of the investment grade fixed income portfolio. The investment guidelines governing the management of that portfolio are contained herein. The other asset categories represented in the pool are advised by external managers. Specific portfolio guidelines that prohibit or constrain certain types of securities or real estate investments will be addressed in the managers' specific investment guidelines. A brief description of these other asset classes follows.

High Yield Fixed Income: This sector consists of predominantly U.S. corporate credits, whether in the form of bonds or loans that are rated below investment grade. These assets carry a higher risk of default than investment grade securities and accordingly provide a higher level of income or yield commensurate with that risk.

Core Real Estate: Equity investment in operating and substantially-leased institutional quality real estate in the traditional property types (apartment, office, retail, industrial and hotel). Net long-term returns historically have been in the 4.0 percent to 6.0 percent range (inflation-adjusted and net of fees) and are typically comprised of greater levels of income (i.e., two-thirds of long-term total returns) with appreciation matching or exceeding inflation.

OBJECTIVES: Investment Grade Fixed Income Portfolio

Strategic: Attaining a competitive stream of income in the fixed income markets while diversifying investment risk. The primary objective of the Trust Fund Bond Pool portfolio is to provide diversified exposure to the various sectors of the investment grade bond market for the benefit of fund participants in a prudent and cost effective manner. In this sense the portfolio investment strategy is core-like and is to be benchmarked against the Barclays Capital Aggregate Bond Index. The portfolio will also provide primary liquidity to fund participants and to facilitate allocation between the other asset classes held in the pool.

Performance: The objective of the TFBP is to achieve a moderate yield to advantage to the Barclays Capital Aggregate bond index. Ideally, the annualized time weighted total return will exceed that of the Barclays Capital Aggregate Bond Index over a three year rolling period.

MONTANA BOARD OF INVESTMENTS
TRUST FUNDS INVESTMENT POOL (MU41) (FUND 07112)
INVESTMENT POLICY STATEMENT

PERMITTED INVESTMENTS: Investment Grade Fixed Income Portfolio

- Debt obligations of the U.S. Government, including its agencies and instrumentalities. These include Treasuries, Treasury Inflation Protected Securities (TIPS) and fixed and floating rate agency obligations.
- Dollar denominated debt obligations of developed country foreign governments.
- Dollar denominated debt obligations of index-eligible supranational agencies.
- Dollar denominated debt obligations of domestic and foreign corporations (Yankee bonds) up to 2% of portfolio assets per issuer. These may include Trust Preferred securities and be fixed or floating rate coupon structures.
- Securitized assets, including U.S. Agency mortgage pass-through securities (MBS), non-agency MBS (limited to 3% of portfolio market value in total), collateralized mortgage obligations (CMO's), commercial mortgage backed securities (CMBS), hybrid ARMS and asset backed securities (ABS).
- When issued securities.
- Rule 144a securities.
- Medium term notes.
- Short term investment pool (STIP).
- Loans for the Montana CRP Program.

PROHIBITED INVESTMENTS: Investment Grade Fixed Income Portfolio

- Over the counter derivatives, including interest rate swaps and credit default swaps.
- Short sales and securities margin loans.
- Bank loans.
- Interest only (IO) and principal only (PO) mortgage strips.
- Companion/residual/equity tranches of CMO's or other structured securities.
- Capital securities (convertible from fixed to floating).
- Inverse floaters.
- Convertible bonds.

CONSTRAINTS: Investment Grade Fixed Income Portfolio

Credit quality: ~~Individually held s~~Securities must be rated investment grade, or no lower than triple-B minus, by ~~one~~ two nationally recognized securities rating organizations (NRSRO) at ~~the~~ time of purchase, with the exception of non-rated securities issued or guaranteed by agencies or instrumentalities of the U.S. Government. ~~Split rated securities may not exceed 3% of portfolio market value.~~ Securities downgraded below investment grade may be held at the portfolio manager's discretion. Non-rated securities will be assigned an internal "equivalent" rating.

Duration: The weighted average effective duration of the portfolio, including cash, must be within 20% of the duration of the Barclays Capital Aggregate Bond index.

Sector: The portfolio sector exposure will be maintained within the ranges highlighted in the table below. Recent exposures by sector for the portfolio and benchmark index are shown for reference.

MONTANA BOARD OF INVESTMENTS
TRUST FUNDS INVESTMENT POOL (MU41) (FUND 07112)
INVESTMENT POLICY STATEMENT

ASSET ALLOCATION SECTORS & RANGES
~~3/31/09~~
(At market)

Sectors	~~TFBP~~	~~Agg Index~~	**Policy Ranges**
U.S. Treasury	~~7.82~~	~~26.17~~	**10-~~35~~45**
Government Related	~~23.33~~	~~13.90~~	**5-~~25~~20**
Total Government	~~**31.15%**~~	~~**40.07%**~~	**~~20~~15-~~55~~65**
MBS ~~(Fixed Rate)~~	~~24.47~~	~~36.04~~	**~~20~~15-~~50~~40**
~~Hybrid ARMS~~	~~0.00~~	~~2.67~~	~~**0-10**~~
Asset Backed Securities	~~1.12~~	~~0.55~~	**0-~~5~~10**
CMBS	~~4.79~~	~~3.25~~	**0-10**
Total Structured	~~**30.38%**~~	~~**42.51%**~~	**~~20~~15-75**
Corporate Credit	~~**35.53%**~~	~~**17.42%**~~	**~~10~~15-~~35~~45**
Cash (STIP)	~~**2.94%**~~	~~**0.00%**~~	**0-10**
Total	~~**100.00%**~~	~~**100.00%**~~	**100.00%**

~~Current portfolio exceptions to the above policy ranges will be addressed over time depending upon market conditions with the objective of moving within compliance.~~

LIQUIDITY: Investment Grade Fixed Income Portfolio

Liquidity needs for the fixed income program are low, as participant capital allocated to the pool is not expected to change dramatically on short notice. Nevertheless, the underlying assets held are predominantly publicly traded securities which can normally be liquidated in a relatively short period to accommodate asset allocation changes between the internally managed fixed income portfolio and other asset categories held by the Trust Funds pool. Assets considered to be generally illiquid will be limited to 10% of the portfolio's market value.

ADMINISTRATIVE

Securities Lending: Section 17-1-113, MCA, authorizes the Board to lend securities held by the state. The Board may lend its publicly traded securities held in the investment pools, through an agent, to other market participants in return for compensation. Currently, through an explicit contract, State Street Bank and Trust, the state's custodial bank, manages the state's securities lending program. The Board seeks to assess the risks, such as counterparty and reinvestment risk, associated with each aspect of its securities lending program. The Board requires borrowers to maintain collateral at 102 percent for domestic securities and 105 percent for international securities. To ensure that the collateral ratio is maintained, securities on loan are marked to market daily and the borrower must provide additional collateral if the value of the securities on loan increases. In addition to the strict collateral requirements imposed by the Board, the credit quality of approved borrowers is monitored continuously by the contractor. From time to time, Staff or the investment manager may restrict a security from the loan program upon notification to State Street Bank. Staff will monitor the securities lending program, and the CIO will periodically report to the Board on the status of the program.

MONTANA BOARD OF INVESTMENTS
TRUST FUNDS INVESTMENT POOL (MU41) (FUND 07112)
INVESTMENT POLICY STATEMENT

INTRODUCTION

The purpose of this policy statement is to provide a broad strategic framework for investments within the Trust Funds Investment Pool (TFIP). The pool's participants consist primarily of the state's trust funds. The pool is designed to provide the participants exposure to a portfolio of diversified income-producing assets. The pool's assets include an investment grade fixed income portfolio managed internally by MBOI staff, one or more core real estate funds, and one or more high yield fixed income funds. Allocation across these asset classes is limited to the following ranges. The use of high yield fixed income and core real estate investments are justified in order to diversify the sources of income provided by the pool, however are constrained to prudent levels of maximum exposure given their unique and somewhat more volatile return patterns.

Asset Class	Minimum	Maximum
Investment grade fixed income	0%	100%
High yield fixed income	0%	10%
Core real estate	0%	8%

The primary component of the pool consists of the investment grade fixed income portfolio. The investment guidelines governing the management of that portfolio are contained herein. The other asset categories represented in the pool are advised by external managers. Specific portfolio guidelines that prohibit or constrain certain types of securities or real estate investments will be addressed in the managers' specific investment guidelines. A brief description of these other asset classes follows.

High Yield Fixed Income: This sector consists of predominantly U.S. corporate credits, whether in the form of bonds or loans that are rated below investment grade. These assets carry a higher risk of default than investment grade securities and accordingly provide a higher level of income or yield commensurate with that risk.

Core Real Estate: Equity investment in operating and substantially-leased institutional quality real estate in the traditional property types (apartment, office, retail, industrial and hotel). Net long-term returns historically have been in the 4.0 percent to 6.0 percent range (inflation-adjusted and net of fees) and are typically comprised of greater levels of income (i.e., two-thirds of long-term total returns) with appreciation matching or exceeding inflation.

OBJECTIVES: Investment Grade Fixed Income Portfolio

Strategic: Attaining a competitive stream of income in the fixed income markets while diversifying investment risk. The primary objective of the Trust Fund Bond Pool portfolio is to provide diversified exposure to the various sectors of the investment grade bond market for the benefit of fund participants in a prudent and cost effective manner. In this sense the portfolio investment strategy is core-like and is to be benchmarked against the Barclays Capital Aggregate Bond Index. The portfolio will also provide primary liquidity to fund participants and to facilitate allocation between the other asset classes held in the pool.

Performance: The objective of the TFBP is to achieve a moderate yield to advantage to the Barclays Capital Aggregate bond index. Ideally, the annualized time weighted total return will exceed that of the Barclays Capital Aggregate Bond Index over a three year rolling period.

MONTANA BOARD OF INVESTMENTS
TRUST FUNDS INVESTMENT POOL (MU41) (FUND 07112)
INVESTMENT POLICY STATEMENT

PERMITTED INVESTMENTS: Investment Grade Fixed Income Portfolio

- Debt obligations of the U.S. Government, including its agencies and instrumentalities. These include Treasuries, Treasury Inflation Protected Securities (TIPS) and fixed and floating rate agency obligations.
- Dollar denominated debt obligations of developed country foreign governments.
- Dollar denominated debt obligations of index-eligible supranational agencies.
- Dollar denominated debt obligations of domestic and foreign corporations (Yankee bonds) up to 2% of portfolio assets per issuer. These may include Trust Preferred securities and be fixed or floating rate coupon structures.
- Securitized assets, including U.S. Agency mortgage pass-through securities (MBS), non-agency MBS (limited to 3% of portfolio market value in total), collateralized mortgage obligations (CMO's), commercial mortgage backed securities (CMBS), hybrid ARMS and asset backed securities (ABS).
- When issued securities.
- Rule 144a securities.
- Medium term notes.
- Short term investment pool (STIP).
- Loans for the Montana CRP Program.

PROHIBITED INVESTMENTS: Investment Grade Fixed Income Portfolio

- Over the counter derivatives, including interest rate swaps and credit default swaps.
- Short sales and securities margin loans.
- Bank loans.
- Interest only (IO) and principal only (PO) mortgage strips.
- Companion/residual/equity tranches of CMO's or other structured securities.
- Capital securities (convertible from fixed to floating).
- Inverse floaters.
- Convertible bonds.

CONSTRAINTS: Investment Grade Fixed Income Portfolio

Credit quality: Securities must be rated investment grade, or no lower than triple-B minus, by two nationally recognized securities rating organizations (NRSRO) at time of purchase, with the exception of non-rated securities issued or guaranteed by agencies or instrumentalities of the U.S. Government. Securities downgraded below investment grade may be held at the portfolio manager's discretion. Non-rated securities will be assigned an internal "equivalent" rating.

Duration: The weighted average effective duration of the portfolio, including cash, must be within 20% of the duration of the Barclays Capital Aggregate Bond index.

Sector: The portfolio sector exposure will be maintained within the ranges highlighted in the table below. Recent exposures by sector for the portfolio and benchmark index are shown for reference.

MONTANA BOARD OF INVESTMENTS
TRUST FUNDS INVESTMENT POOL (MU41) (FUND 07112)
INVESTMENT POLICY STATEMENT

ASSET ALLOCATION SECTORS & RANGES

(At market)

Sectors	Policy Ranges
U.S. Treasury	**10-45**
Government Related	**5-20**
Total Government	**15-65**
MBS	**15-40**
Asset Backed Securities	**0-10**
CMBS	**0-10**
Total Structured	**15-75**
Corporate Credit	**15-45**
Cash (STIP)	**0-10**
Total	**100.00%**

LIQUIDITY: Investment Grade Fixed Income Portfolio

Liquidity needs for the fixed income program are low, as participant capital allocated to the pool is not expected to change dramatically on short notice. Nevertheless, the underlying assets held are predominantly publicly traded securities which can normally be liquidated in a relatively short period to accommodate asset allocation changes between the internally managed fixed income portfolio and other asset categories held by the Trust Funds pool. Assets considered to be generally illiquid will be limited to 10% of the portfolio's market value.

ADMINISTRATIVE

Securities Lending: Section 17-1-113, MCA, authorizes the Board to lend securities held by the state. The Board may lend its publicly traded securities held in the investment pools, through an agent, to other market participants in return for compensation. Currently, through an explicit contract, State Street Bank and Trust, the state's custodial bank, manages the state's securities lending program. The Board seeks to assess the risks, such as counterparty and reinvestment risk, associated with each aspect of its securities lending program. The Board requires borrowers to maintain collateral at 102 percent for domestic securities and 105 percent for international securities. To ensure that the collateral ratio is maintained, securities on loan are marked to market daily and the borrower must provide additional collateral if the value of the securities on loan increases. In addition to the strict collateral requirements imposed by the Board, the credit quality of approved borrowers is monitored continuously by the contractor. From time to time, Staff or the investment manager may restrict a security from the loan program upon notification to State Street Bank. Staff will monitor the securities lending program, and the CIO will periodically report to the Board on the status of the program.

MONTANA PRIVATE EQUITY POOL (MPEP) INVESTMENT POLICY STATEMENT

This policy is effective immediately upon adoption and supersedes all previous Montana Private Equity Pool (MPEP) policies.

INTRODUCTION

The purpose of this policy statement is to provide investment objectives, strategies, and constraints for private equity investments, which are consolidated into the Montana Private Equity Pool (MPEP). The Board approved the creation of MPEP at the April 2, 2002 Board meeting, and the pool was created on May 1, 2002. This statement provides a basis on which to invest in private equity partnerships. MPEP investments consist of private partnership funds which are selected and managed by internal investment staff. The underlying assets held in these funds are managed by external managers with the expertise and experience to prudently manage these types of investments.

OBJECTIVES

Attaining enhanced investment returns from private equity investments while diversifying investment risk is the strategic objective of MPEP. The objective includes the following components:

- Achieve diversification benefits by investing pension fund portfolios in non-traditional (i.e. equity and fixed income) domestic and international capital markets
- Achieve higher risk-adjusted portfolio returns by investing in private investments that are actively managed to add value using principles and tactics often not available in the public marketplace
- Achieve superior investment returns within the respective investment strategies that make up the pool
- Ancillary strategic objectives associated with private equity investments include, but are not limited to the following:
  a. Develop secondary market capabilities to prudently either divest private equity assets prior to maturity or liquidation or invest in established partnerships in the secondary market
  b. Establish key general partner relationships that may enhance partnership and direct investment opportunities

Return Requirement: There is no generally accepted benchmark index for private equity performance comparisons. Characteristically, private equity partnership investments are impacted by the "J-curve" effect, in which fees and transaction costs create negative returns during the initial investment years before distributions are realized. Private equity investing requires a long time horizon in order to realize the value provided by the creation or restructuring of private companies.

- The performance objective for MPEP is the achievement of long-term net returns (after management fees and general partner's carried interest) above a benchmark reflecting public equity market returns plus an appropriate premium to compensate for the higher degree of risk**.**

MONTANA PRIVATE EQUITY POOL (MPEP)
INVESTMENT POLICY STATEMENT

- The benchmark established for MPEP is an annualized rate of return 400 basis points above the Standard & Poor's 1500 Index which is a proxy for the broad domestic stock market.

Risk: Private equity investments incur a higher degree of risk with a higher return potential than traditional equity investments. Portfolio diversification of risk is achieved through multiple partnership relationships and investments diversified by time, stage of financing, industry sector, investment size and geographical region.

RESPONSIBILITES AND DELEGATION

Board: The Board shall approve and revise the MPEP Investment Policy Statement as necessary, oversee MPEP performance, delegate decision making to Staff as appropriate and authorize investment and other decisions not delegated to Staff. The Board delegates to Staff the authority to screen, evaluate and select private equity managers ~~who meet the due diligence guidelines of this policy~~.

Staff: Staff assigned to the MPEP will be responsible for~~to~~:

- Making~~e~~ recommendations to the Board concerning MPEP Strategy and Investment Policy changes
- Managing~~e~~ day-to-day operations, delegating~~e~~ work to external resources as appropriate, and overseeing all due diligence activity
- Screening, evaluating~~e~~ and selecting private equity managers ~~who meet the due diligence guidelines of this policy~~ and informing the Board at its next meeting: 1) which managers were selected; and 2) how the selection of the manager fulfills the strategy and objectives of MPEP.
- Monitoring and reporting to the Board the performance of the MPEP and the individual managers in the MPEP
- Managing~~e~~ on an ongoing basis any external resources and notifying the Board of any material changes in these resources
- Reporting any deviations from this Policy to the Board

INVESTMENT SELECTION PROCESS

Portfolio Management: Staff reviews and selects appropriate funds to fulfill the objectives of the pool. The management of the underlying assets will be executed by the General Partners of Fund-of-Funds and/or Direct Limited Partnerships. Fund-of-Funds managers may be chosen to manage assets where particular expertise is required and cannot be provided by Staff or where the Fund-of-Funds manager can cost-effectively provide relevant information/assistance to Staff in the selection of Direct Limited Partnership investments.

Staff shall oversee the construction and maintenance of a pacing analysis. The pacing analysis will use historical private equity data to estimate the level of new commitments needed to maintain MPEP assets at a level that is consistent with MPEP and Pension strategies. The pacing analysis will be reviewed and updated at least biennially.

MONTANA PRIVATE EQUITY POOL (MPEP)
INVESTMENT POLICY STATEMENT

Staff shall continually review MPEP investments for compliance and performance relative to the following:

- Pace and timing of investment commitments, funding and return of capital;
- Diversity of sectors (industry, geographical, investment style, and others as appropriate);
- Stated objectives specific to the investment;
- The benchmark established for the MPEP

Eligible Investments: Private equity partnership interests are eligible MPEP investments. These private equity partnerships may be Direct Limited Partnerships or vehicles that primarily invest in Direct Limited Partnerships, including Fund-of-Funds and Secondary Funds. MPEP may co-invest with private equity managers in transactions that are suitable for inclusion into a private equity partnership. Individual public or private securities received as distributions from funds and equitized liquidity funds are also permitted to be held in MPEP. Individual public securities received as distributions will be liquidated over a reasonable time period dependent on market conditions.

Strategies and Limitations: Private equity investments are typically classified as follows:

- **Buyout and Corporate**: Investments in leveraged buyouts, management buyouts, debt restructuring, or other acquisition strategies and financial restructuring strategies.
- **Venture Capital**: Investments in relatively small but rapidly growing private companies in various stages of development.
- **Distressed**: Either debt or equity securities in troubled companies are purchased and held with the intention of selling them or negotiating a work out plan ~~for a profit~~ prior to ~~a~~or during ~~–~~ potential bankruptcy or formal restructuring proceedings. ~~as fundamentals improve or with the intention to negotiate a work out plan~~~~while the investment manager negotiates with the bankruptcy court. As a workout plan is put into action, the value of the distressed securities appreciates and can be profitably liquidated.~~
- **Mezzanine:** Privately negotiated subordinated debt investments, usually with an equity warrant attached at a relatively low cost.
- **Special Situations**: Typically, specific industry strategies and unconventional investment opportunities ~~are so classified~~.
- **Secondary**: Purchase of private equity interests from the limited partners of private equity funds. Secondary funds will be classified based on underlying assets~~ type~~.

MONTANA PRIVATE EQUITY POOL (MPEP)
INVESTMENT POLICY STATEMENT

The following table provides a guideline range with respect to MPEP's strategy diversification. It is important to note that these ranges reference the sum of the pool's net asset value and uncalled commitments.

Strategy	**Policy Range**[1]
Buyout and Corporate	40% - 75%
Venture Capital	10% - ~~50~~25%
~~Distressed~~Debt-related (Distressed, not-for-control, & Mezzanine)	0% - ~~40~~25%
~~Mezzanine~~	~~0% - 20%~~
~~Special Situations~~	~~0% - 35%~~

[1]Based on net asset value + uncalled committed capital.

For the purpose of these strategy ranges, Special Situations and Secondary funds will be classified in the category that is most reflective of the underlying investments in the funds.

No more than 7.5% of the aggregate of MPEP net asset value plus uncalled committed capital should be in a single Direct Limited Partnership. No more than 15% of the aggregate of MPEP net asset value plus uncalled committed capital should be placed with a single fund manager~~, except that up to 25% may be placed with a single manager of Fund-of-Funds or Secondary Funds~~.

Risk Considerations: Private Equity investments ~~may~~ typically involve the following risks:

- **Financial Risk**: These investments may employ financial leverage (debt) leading to a higher degree of volatility in investment returns. Buyout strategies are characterized by the use of significant levels of debt in their capital structures.
- **Operating and Business Risk**: These investments typically involve ~~above average~~ operating and business risk, due to risks associated with the underlying businesses being acquired. ~~development of new products, new business models, new markets or inexperienced management teams.~~
- **Valuation Risk**: Given the lack of public pricing of the underlying private equity investments, ~~partnership reporting of~~unrealized asset valuations are based on appraised values. ~~shall be evaluated to determine if an appropriate valuation discipline is being followed.~~
- **Structure Risk**: The funds involve extensive legal documentation which set out terms that address investment constraints, fund governance, costs, and the distribution of economic returns to investors. ~~must be reviewed by legal counsel as part of the due diligence process.~~
- **Country Risk**: Investing in international alternative investments include all of the risks associated with this particular asset class along with political, economic, and currency risks associated with investing outside of the U.S.
- **Manager Risk**: Fund managers have significant discretion in investing partnership assets. This may lead to funds which are poorly diversified or which contain investments that had not been anticipated by investors. Private equity

MONTANA PRIVATE EQUITY POOL (MPEP)
INVESTMENT POLICY STATEMENT

funds are often dependent on a few key investment staff, the loss of which may materially impact fund operations.

- **Industry Risk**: Private equity firms are permitted to invest in a wide variety of industries without many restrictions. Diversification across industries is the means by which this risk is controlled in a private equity portfolio.

Evaluation Criteria:

- Managers shall demonstrate relevant experience in or directly applicable to the market in which they propose to invest
- Managers shall demonstrate that they are specifically qualified to pursue the proposed strategy in the market in which they propose to invest
- Managers shall demonstrate the requisite skills and experience necessary to execute successfully the proposed strategy, including evidence from similar endeavors of their ability to work successfully with Limited Partners
- Managers shall dedicate sufficient time and effort to the proposed opportunity and make, within the context of the particular investment, a meaningful personal financial commitment
- The Manager's proposed strategy and business plan shall be set forth in sufficient detail to permit substantive and meaningful review of the opportunity, verification of the investment concept, and of the risk factors
- The risk/reward trade-off in the particular market in which the Manager proposes to invest shall be attractive based on reasonable assumptions
- Uniqueness of the investment strategy relative to existing Managers
- Integrity and experience of the key principals, employees and the reputation of the firm
- Quality of the partnership corporate governance, including controls and reporting systems
- Relationships with other Limited Partners, particularly public investment boards~~.~~
- Past ~~financial~~ investment performance
- Appropriateness of terms and conditions and alignment of interests of the firm's principals with the Limited Partners
- ~~Reasonable ratio of committed capital by the managing principals~~

~~**Due Diligence:** A due diligence review by Staff and any external resources utilized by Staff shall include at least the following:~~

- ~~Discussions with the managing principals of the Partnership under review for investment~~
- ~~Review and analysis of all pertinent offering documents including: offering memorandum, subscription agreements, private placement memorandums and operative investment agreements~~
- ~~Consideration of potential conflicts of interest, if any, posed by the proposed investment and prior investments and activities of the firm~~
- ~~Review and analysis of the investment concept, including entry and exit strategies and terms including fees, principal participation and structure~~

MONTANA PRIVATE EQUITY POOL (MPEP)
INVESTMENT POLICY STATEMENT

- ~~Review and analysis of the appropriateness of the proposed investment with the MPEP Strategy and Guidelines~~
- ~~Review of news articles and public reports regarding the partnership and its managing principals, prior investments, and investment strategy~~
- ~~Review and analysis of the partnership investment performance record including both prior and current investments~~
- ~~Consideration of relative size of the proposed investment relative to the partnership's prior investment funds and distribution of investment responsibilities between managing principals.~~
- ~~Investigation of special terms and conditions, management fees and legal "side letter" agreements with past and present investors~~
- ~~Determining the ability and stability of the management team and the investment organization~~
- ~~Review disclosure of any lawsuits, litigation involving the general partner, its principals, employees and prior funds~~

MONITORING AND REPORTING

Monitoring:

- Staff shall monitor both individual Managers within MPEP and overall performance of MPEP
- Staff shall assess the performance of Managers relative to the following criteria:
    1. Objectives established by the Managers or the principals managing the investment relative to their stated performance objectives
    2. Degree of risk undertaken
    3. Performance comparisons to other managers with similar investment styles and/or within the same vintage year
    4. The MPEP performance versus the selected benchmark

Reporting:

- Managers shall submit periodic reports to facilitate Staff's monitoring of the Managers' conformance to MPEP policy and performance objectives
- Staff shall provide quarterly ~~and annual~~ reports to the Board that include the results of such monitoring of Managers

OTHER CONSIDERATIONS

Liquidity: Private equity investments are extremely illiquid and participation in these investments is limited to the nine pension funds.

Time Horizon: Private equity investments are classified as long-term in nature. Private equity investment fund positions generally represent 7 to 12 year commitments usually characterized by capital calls occurring during years 1 through 5 with distributions of income or principal realizations during the latter years of the fund life. The final term of a

MONTANA PRIVATE EQUITY POOL (MPEP)
INVESTMENT POLICY STATEMENT

partnership may sometimes be increased in one-year increments as needed to liquidate underlying assets.

Tax Considerations: Since the investments are made exclusively for the pension funds, there are no tax implications applicable to the MPEP. However, partnerships in which MPEP invests may be structured to minimize tax implications for private investors.

Legal: Legal constraints on the management of investment funds for the State of Montana are defined in MCA 17-6-201. Unified investment program - general provisions:

The unified investment program directed by Article VIII, section 13, of the Montana constitution to be provided for public funds must be administered by the Board of Investments in accordance with the prudent expert principle, which requires any investment manager to:

(a) discharge his duties with the care, skill, prudence, and diligence, under the circumstances then prevailing, that a prudent person acting in a like capacity with the same resources and familiar with like matters exercises in the conduct of an enterprise of like character with like aims;
(b) diversify holdings of each fund to minimize the risk of loss and maximize the rate of return, unless under the circumstances it is clearly prudent not to do so, and;
(c) discharge his duties solely in the interest of and for the benefit of the funds.

Client Preferences: MCA section 17-6-201 (3) (b) states…"The Board is urged under the prudent expert principle to invest up to three percent (3%) of retirement funds in Venture Capital companies. Whenever possible, preferences should be given to investments in those Venture Capital companies which demonstrate an interest in making investments in Montana."

MONTANA PRIVATE EQUITY POOL (MPEP)
INVESTMENT POLICY STATEMENT

This policy is effective immediately upon adoption and supersedes all previous Montana Private Equity Pool (MPEP) policies.

INTRODUCTION

The purpose of this policy statement is to provide investment objectives, strategies, and constraints for private equity investments, which are consolidated into the Montana Private Equity Pool (MPEP). The Board approved the creation of MPEP at the April 2, 2002 Board meeting, and the pool was created on May 1, 2002. This statement provides a basis on which to invest in private equity partnerships. MPEP investments consist of private partnership funds which are selected and managed by internal investment staff. The underlying assets held in these funds are managed by external managers with the expertise and experience to prudently manage these types of investments.

OBJECTIVES

Attaining enhanced investment returns from private equity investments while diversifying investment risk is the strategic objective of MPEP. The objective includes the following components:

- Achieve diversification benefits by investing pension fund portfolios in non-traditional (i.e. equity and fixed income) domestic and international capital markets
- Achieve higher risk-adjusted portfolio returns by investing in private investments that are actively managed to add value using principles and tactics often not available in the public marketplace
- Achieve superior investment returns within the respective investment strategies that make up the pool
- Ancillary strategic objectives associated with private equity investments include, but are not limited to the following:
    a. Develop secondary market capabilities to prudently either divest private equity assets prior to maturity or liquidation or invest in established partnerships in the secondary market
    b. Establish key general partner relationships that may enhance partnership and direct investment opportunities

Return Requirement: There is no generally accepted benchmark index for private equity performance comparisons. Characteristically, private equity partnership investments are impacted by the “J-curve” effect, in which fees and transaction costs create negative returns during the initial investment years before distributions are realized. Private equity investing requires a long time horizon in order to realize the value provided by the creation or restructuring of private companies.

- The performance objective for MPEP is the achievement of long-term net returns (after management fees and general partner’s carried interest) above a benchmark reflecting public equity market returns plus an appropriate premium to compensate for the higher degree of risk**.**

- The benchmark established for MPEP is an annualized rate of return 400 basis points above the Standard & Poor's 1500 Index which is a proxy for the broad domestic stock market.

Risk: Private equity investments incur a higher degree of risk with a higher return potential than traditional equity investments. Portfolio diversification of risk is achieved through multiple partnership relationships and investments diversified by time, stage of financing, industry sector, investment size and geographical region.

RESPONSIBILITES AND DELEGATION

Board: The Board shall approve and revise the MPEP Investment Policy Statement as necessary, oversee MPEP performance, delegate decision making to Staff as appropriate and authorize investment and other decisions not delegated to Staff. The Board delegates to Staff the authority to screen, evaluate and select private equity managers.

Staff: Staff assigned to the MPEP will be responsible for:

- Making recommendations to the Board concerning MPEP Strategy and Investment Policy changes
- Managing day-to-day operations, delegating work to external resources as appropriate, and overseeing all due diligence activity
- Screening, evaluating and selecting private equity managers and informing the Board at its next meeting: 1) which managers were selected; and 2) how the selection of the manager fulfills the strategy and objectives of MPEP.
- Monitoring and reporting to the Board the performance of the MPEP and the individual managers in the MPEP
- Managing on an ongoing basis any external resources and notifying the Board of any material changes in these resources
- Reporting any deviations from this Policy to the Board

INVESTMENT SELECTION PROCESS

Portfolio Management: Staff reviews and selects appropriate funds to fulfill the objectives of the pool. The management of the underlying assets will be executed by the General Partners of Fund-of-Funds and/or Direct Limited Partnerships. Fund-of-Funds managers may be chosen to manage assets where particular expertise is required and cannot be provided by Staff or where the Fund-of-Funds manager can cost-effectively provide relevant information/assistance to Staff in the selection of Direct Limited Partnership investments.

Staff shall oversee the construction and maintenance of a pacing analysis. The pacing analysis will use historical private equity data to estimate the level of new commitments needed to maintain MPEP assets at a level that is consistent with MPEP and Pension strategies. The pacing analysis will be reviewed and updated at least biennially.
Staff shall continually review MPEP investments for compliance and performance relative to the following:

- Pace and timing of investment commitments, funding and return of capital;
- Diversity of sectors (industry, geographical, investment style, and others as appropriate);
- Stated objectives specific to the investment;
- The benchmark established for the MPEP

Eligible Investments: Private equity partnership interests are eligible MPEP investments. These private equity partnerships may be Direct Limited Partnerships or vehicles that primarily invest in Direct Limited Partnerships, including Fund-of-Funds and Secondary Funds. MPEP may co-invest with private equity managers in transactions that are suitable for inclusion into a private equity partnership. Individual public or private securities received as distributions from funds and equitized liquidity funds are also permitted to be held in MPEP. Individual public securities received as distributions will be liquidated over a reasonable time period dependent on market conditions.

Strategies and Limitations: Private equity investments are typically classified as follows:

- **Buyout and Corporate**: Investments in leveraged buyouts, management buyouts, debt restructuring, or other acquisition strategies and financial restructuring strategies.
- **Venture Capital**: Investments in relatively small but rapidly growing private companies in various stages of development.
- **Distressed**: Either debt or equity securities in troubled companies are purchased and held with the intention of selling them or negotiating a work out plan prior to or during potential bankruptcy or formal restructuring proceedings.
- **Mezzanine:** Privately negotiated subordinated debt investments, usually with an equity warrant attached at a relatively low cost.
- **Special Situations**: Typically, specific industry strategies and unconventional investment opportunities **Secondary**: Purchase of private equity interests from the limited partners of private equity funds. Secondary funds will be classified based on underlying assets.

The following table provides a guideline range with respect to MPEP's strategy diversification. It is important to note that these ranges reference the sum of the pool's net asset value and uncalled commitments.

Strategy	Policy Range[1]
Buyout and Corporate	40% - 75%
Venture Capital	10% - 25%
Debt-related (Distressed, not-for-control, & Mezzanine)	0% - 25%

[1]Based on net asset value + uncalled committed capital.

For the purpose of these strategy ranges, Special Situations and Secondary funds will be classified in the category that is most reflective of the underlying investments in the funds.

No more than 7.5% of the aggregate of MPEP net asset value plus uncalled committed capital should be in a single Direct Limited Partnership. No more than 15% of the aggregate of MPEP net asset value plus uncalled committed capital should be placed with a single fund manager.

Risk Considerations: Private Equity investments typically involve the following risks:

- **Financial Risk**: These investments may employ financial leverage (debt) leading to a higher degree of volatility in investment returns. Buyout strategies are characterized by the use of significant levels of debt in their capital structures.
- **Operating and Business Risk**: These investments typically involve operating and business risk, due to risks associated with the underlying businesses being acquired. **Valuation Risk**: Given the lack of public pricing of the underlying private equity investments, unrealized asset valuations are based on appraised values.
- **Structure Risk**: The funds involve extensive legal documentation which set out terms that address investment constraints, fund governance, costs, and the distribution of economic returns to investors. **Country Risk**: Investing in international alternative investments include all of the risks associated with this particular asset class along with political, economic, and currency risks associated with investing outside of the U.S.
- **Manager Risk**: Fund managers have significant discretion in investing partnership assets. This may lead to funds which are poorly diversified or which contain investments that had not been anticipated by investors. Private equity funds are often dependent on a few key investment staff, the loss of which may materially impact fund operations.
- **Industry Risk**: Private equity firms are permitted to invest in a wide variety of industries without many restrictions. Diversification across industries is the means by which this risk is controlled in a private equity portfolio.

Evaluation Criteria:

- Managers shall demonstrate relevant experience in or directly applicable to the market in which they propose to invest
- Managers shall demonstrate that they are specifically qualified to pursue the proposed strategy in the market in which they propose to invest
- Managers shall demonstrate the requisite skills and experience necessary to execute successfully the proposed strategy, including evidence from similar endeavors of their ability to work successfully with Limited Partners
- Managers shall dedicate sufficient time and effort to the proposed opportunity and make, within the context of the particular investment, a meaningful personal financial commitment

- The Manager's proposed strategy and business plan shall be set forth in sufficient detail to permit substantive and meaningful review of the opportunity, verification of the investment concept, and of the risk factors
- The risk/reward trade-off in the particular market in which the Manager proposes to invest shall be attractive based on reasonable assumptions
- Uniqueness of the investment strategy relative to existing Managers
- Integrity and experience of the key principals, employees and the reputation of the firm
- Quality of the partnership corporate governance, including controls and reporting systems
- Relationships with other Limited Partners, particularly public investment boards
- Past investment performance
- Appropriateness of terms and conditions and alignment of interests of the firm's principals with the Limited Partners

MONITORING AND REPORTING

Monitoring:

- Staff shall monitor both individual Managers within MPEP and overall performance of MPEP
- Staff shall assess the performance of Managers relative to the following criteria:
  1. Objectives established by the Managers or the principals managing the investment relative to their stated performance objectives
  2. Degree of risk undertaken
  3. Performance comparisons to other managers with similar investment styles and/or within the same vintage year
  4. The MPEP performance versus the selected benchmark

Reporting:

- Managers shall submit periodic reports to facilitate Staff's monitoring of the Managers' conformance to MPEP policy and performance objectives
- Staff shall provide quarterly reports to the Board that include the results of such monitoring of Managers

OTHER CONSIDERATIONS

Liquidity: Private equity investments are extremely illiquid and participation in these investments is limited to the nine pension funds.

Time Horizon: Private equity investments are classified as long-term in nature. Private equity investment fund positions generally represent 7 to 12 year commitments usually characterized by capital calls occurring during years 1 through 5 with distributions of income or principal realizations during the latter years of the fund life. The final term of a partnership may sometimes be increased in one-year increments as needed to liquidate underlying assets.

Tax Considerations: Since the investments are made exclusively for the pension funds, there are no tax implications applicable to the MPEP. However, partnerships in which MPEP invests may be structured to minimize tax implications for private investors.

Legal: Legal constraints on the management of investment funds for the State of Montana are defined in MCA 17-6-201. Unified investment program - general provisions:

The unified investment program directed by Article VIII, section 13, of the Montana constitution to be provided for public funds must be administered by the Board of Investments in accordance with the prudent expert principle, which requires any investment manager to:

(a) discharge his duties with the care, skill, prudence, and diligence, under the circumstances then prevailing, that a prudent person acting in a like capacity with the same resources and familiar with like matters exercises in the conduct of an enterprise of like character with like aims;
(b) diversify holdings of each fund to minimize the risk of loss and maximize the rate of return, unless under the circumstances it is clearly prudent not to do so, and;
(c) discharge his duties solely in the interest of and for the benefit of the funds.

Client Preferences: MCA section 17-6-201 (3) (b) states…"The Board is urged under the prudent expert principle to invest up to three percent (3%) of retirement funds in Venture Capital companies. Whenever possible, preferences should be given to investments in those Venture Capital companies which demonstrate an interest in making investments in Montana."

REAL ESTATE INVESTMENT GUIDELINES AND RANGES

The Montana Real Estate Pool (MTRP) was created to permit the nine Montana Retirement Systems to participate in a diversified real estate portfolio, consisting of commercial real estate and timberland. Real estate investments in the MTRP shall be consistent with the following guidelines:~~.~~

~~a. **Allocation Size**~~

~~The target allocation range for real estate shall be 4.0 percent to 10.0 percent of the total Retirement Systems' assets, with the Timberland allocation subject to a maximum upper limit of 2.0 percent of total Retirement System assets. The real estate target range is long-term in nature, and the allocation percentage will fluctuate according to the relative values among real estate and the other asset classes of the Retirement Systems.~~

~~b.~~a. **Permissible Investment Structures/Vehicles and Public/Private Allocations**

Investment Structures/Vehicles. The MTRP will include real estate investments, consisting of both open-end and closed-end pooled funds, the advantages and disadvantages of which are described in the following table.

VEHICLE	ADVANTAGES	DISADVANTAGES	LIQUIDITY
Open-Ended Fund	1. Property type diversification. 2. Geographic diversification. 3. Existing investment portfolio to evaluate. 4. Existing manager and fund performance record. 5. Infinite life. 6. Can redeem units in fund.	1. Passive investor. 2. Cannot replace manager. 3. Cannot influence manager decisions regarding acquisitions, financings, and sales. 4. Fee level and structures lack alignment of interests. 5. Lack of manager co-investment. 6. Historically have not sold assets to harvest gains.	Typically within 90 days unless there is an investor queue.
Closed-Ended Fund	1. Skilled value-added/ opportunistic management. 2. Manager organizations and track records. 3. Manager co-investment. 4. Manager-investor enhanced alignment of interests. 5. Asset liquidations by end of term of fund.	1. Illiquid-specified term. 2. Typically blind pools. 3. Cannot redeem interest. 4. Passive investor. 5. Cannot influence manager decisions regarding acquisitions, financings, and sales.	Typically 7 to 10 year terms.

Open-end Commingled Funds. The MTRP portfolio may have ~~a~~ significant exposure to open-end commingled funds. The open-end fund investments shall be made primarily to provide (1) timely access to large existing, well-diversified portfolios, (2) reasonable property type and geographic diversification, (3) exposure to larger properties (i.e., over $50 mil.), and (4) reasonable liquidity (i.e., ability to purchase or redeem within 90 days unless there is an investor queue). Reasonable due diligence shall be completed to evaluate open-end commingled funds consistent with these objectives.

Closed-end Commingled Funds. The MTRP portfolio may have ~~a~~ significant exposure to closed-end commingled funds. The closed-end fund investments may be made to obtain exposure to timberland and value-added and opportunistic real estate investments. Reasonable due diligence shall be completed prior to selecting closed-end fund investments.

Liquidity. The table below describes different levels of liquidity of real estate investments.

PORTFOLIO LIQUIDITY RANGES	
Degree of Liquidity	**Investment Type**
LIQUID (i.e., can redeem within 30 days if no queue exists)	Select Open-End Funds
MODERATE LIQUIDITY (i.e., can redeem within 90 to 120 days if no queue exists)	Open-End Funds
ILLIQUID (i.e., liquidity is subject to GP discretion until fund termination.)	Closed-End Funds

~~c.~~b. **Expected Investments.**

The categories utilized to classify MTRP real estate investments are: Timberland, Core, Value-Added, and Opportunistic. With the exception of Timberland, the categories are differentiated primarily by risk/return attributes rather than by property type. A description of each category follows.

Timberland. Equity investment in land that is populated with or is intended to produce commercially harvestable timber. Net inflation-adjusted returns are expected to be 5.0 percent to 7.0 percent. Proceeds from the sale of timber and ancillary revenue opportunities, such as recreational leases, will account for the majority of the real return, while land appreciation is expected to approximate the rate of inflation.

Core. Equity investment in operating and substantially-leased institutional quality real estate in the traditional property types (apartments, office, retail, industrial and hotel). Net returns historically have been in the 4.0 percent to 6.0 percent range (inflation-adjusted and net of fees) and are typically comprised of greater levels of income (i.e., 67.0 percent of total returns) with appreciation matching or exceeding inflation.

Value-Added. Equity or debt interests in assets requiring rehabilitation, redevelopment, development, lease-up or repositioning. Net returns historically have been in the ~~8%-10%~~ 8.0 percent to 10.0 percent range (inflation-adjusted and net of fees). Value-added investments frequently involve the repositioning of distressed assets (i.e., not fully leased and operating). For example, a value-added investment may be an office building that is 40.0 percent vacant and needs significant capital to rehabilitate and reposition the property. Investment may also include non-traditional property types (e.g., manufactured housing) which may contain greater risk. Value-added investments typically are expected to generate ~~above-core~~returns in excess of core returns through the leasing-up of a property, which increases the end value by increasing in-~~-~~place income and, in many cases, decreasing the capitalization rate used in selling the asset due to the reduced asset risk resulting from stabilized occupancy.

Value-added returns are typically more dependent than core on appreciation returns with purchase prices based on ~~income in place~~in-place income or asset replacement cost (i.e., at a discount to replacement cost).

Opportunistic. Equity or debt investment in real estate properties, operating companies, and other investment vehicles involving significant investment risk. Risk may include real estate, financial restructuring, and non-real estate risk. Net returns have been in the 12.0 percent or higher range (inflation-adjusted and net of fees). Opportunistic investing includes distressed assets, financial restructurings, and/or financial engineering opportunities (e.g., foreclosing on a mortgage and selling the equity interest) and potentially the purchase of REITs or REOCs. Investments may also be made in non-traditional property types (e.g., self-storage), which typically contain greater risk. Opportunistic returns typically require even greater appreciation returns than value-added (e.g., 50.0 percent of total returns) and in many cases are originated with minimal income in place.

~~d.~~c. **Policy Constraints.**

Policy range targets for MTRP will be reviewed and adjusted periodically going forward with respect to MTRP exposures. Policy range targets include those dealing with investment category (see below), property type (Section ~~f~~e. 1.), geography (Section ~~f~~e. 2.), and leverage (Section ~~g~~f. 1.). ~~With the exception of the leverage policy range target, policy ranges will be measured based on the net asset value of MTRP holdings. Targets may be adjusted on an annual basis and will be reflected in the MTRP quarterly performance reports.~~ Portfolio exposures to these factors will be presented quarterly. Because MTRP investments have limited liquidity, it will typically be impractical to correct deviations from policy range targets through the purchase or sale of assets. Therefore, if actual portfolio holdings should fall outside of policy guidelines, the MTRP shall refrain from investing in funds that would be expected to increase the deviation from policy ranges.

The following table sets forth the long-term investment category policy ranges for the portfolio.

INVESTMENT AND PORTFOLIO RISK/RETURN RANGES

Risk/Return	Nominal Return (Net)*	Policy Range
Core plus Timberland	6-8%	35%-65%
Value-Added	10-12%	20%-45%
Opportunistic	13-15%	10%-30%

* Assumes 2.5% inflation overall and 100 basis points core management fee, 200 basis points value-added and timberland management and incentive fees, and 300 basis points opportunistic management and incentive fees.

~~e.~~d. **Income and Appreciation Return Mix.**

Real estate investments, depending on their risk/return level, offer varying proportions of expected income/cash yield and appreciation returns. Investments providing higher income/cash yield returns typically will be preferred among investments of comparable expected total returns since income/cash yield returns provide greater return certainty and therefore lower risk. In addition, investments providing preferred or senior income/cash yield returns typically will be preferred among investments providing comparable returns because such features enhance the certainty of return.

~~f.~~e. **Diversification.**

The MTRP portfolio diversification is important in reducing portfolio risk and accomplishing superior risk-adjusted returns. The impact of investments on portfolio diversification, portfolio risk, and risk-adjusted returns shall be considered when evaluating prospective investments. Additionally, the portfolio may have over-weighted exposure in select property types or regions~~ as desired~~.

1. **Property Type.** Property type diversification is one of the most important diversification features in terms of impact on returns. The property types have historically performed differently during economic cycles. Residential and industrial investments have historically outperformed the other property types during economic downturns. Office has historically underperformed during economic downturns, as reduced tenant demand results in lower rents, higher owner operating and build-out costs, and reduced income and cash flow. Hotels historically also have underperformed during economic downturns.

   Diversification ranges are based on the universe of available real estate investments and institutional investor portfolio information. The following table provides a guideline range with respect to the MTRP property type diversification.

PROPERTY TYPE DIVERSIFICATION RANGES	
Property Type	**Policy Range**
Timberland	0%-35%
Office	15%-45%
Retail	10%-40%
Industrial	5%-35%
Residential	10%-40%
Hotel/Other	5%-25%

2. **Region/Location.** The importance of location to the long-term value of real estate is based on the economic fundamentals and the other risk attributes (e.g., weather, earthquake and local government impact) of U.S. and international regions. The distribution of real estate investments by geographic region shall be monitored for compliance with the broad ranges set forth in the table below.

~~Policy range targets with respect to regional exposures may be established and adjustedand adjusted on an annual basis.~~

REGIONAL DIVERSIFICATION RANGES	
Regions	**Policy Range**
West	20%-45%
South	10%-40%
Midwest	5%-25%
East	20%-45%
International	0%-30%

Because domestic commercial timberland is primarily concentrated in the South and the Pacific Northwest, the preceding regional diversification ranges shall apply only to non-timberland real estate holdings. ~~Timberland holdings shall be managed such that, upon maturity of the timberland strategy, no more than 50% of timberland holdings will be concentrated in a single timber-growing region.~~

3. **Other.** In addition to property type and regional diversification, there are other real estate factors that impact the portfolio risk which may be reduced through diversification. These portfolio factors may include, but are not limited to, the following:

   a. **Investment Structure.** Equity, preferred equity, first mortgage debt or mezzanine equity. **Investments in public CMBS and REITs are not preferred**.

   b. **Life Cycle.** Land, development/redevelopment, leasing (i.e., less than 90% leased) and operating (i.e., over 90% leased).

   c. **Investment Size.** $0-$10 mil., $10-$20 mil., $20-$50 mil., $50-$100 mil., $100 mil.+.

While no formal diversification ranges are set forth for the above portfolio risk factors, these and other factors may be monitored in assessing overall portfolio risk and expected return.

~~g.~~f. **Other Risk Factors**.

1. **Leverage.** Leverage is a significant risk factor. Its importance is magnified during an economic downturn when decreasing property values and stricter lending terms can lead to unexpected increased leverage levels. It may be the case that the leverage level increases as market conditions worsen.

   On an individual fund basis, the leverage level can range up to 75.0 percent. Leverage consists of the combined borrowing at the property level and the fund level. On a select basis, the leverage may exceed 75.0 percent for a given investment, if it is determined to be reasonable to do so. Leverage shall be monitored on an individual fund level, and new investments shall be made with the intention that the total MTRP portfolio leverage shall not exceed 60.0 percent.

LEVERAGE RANGES	
Risk	**Range**
Timberland	0%-30%
Core	0%-50%
Non-Core	0%-75%
Total Real Estate Portfolio	0%-60%

2. **Monitoring and Control.** All investments will be made through investment vehicles providing full discretion to investment managers.

3. **Manager Concentrations.** The MTRP exposure to each manager shall be reviewed regularly to determine the reasonableness of each. No manager shall have under management more than 25.0 percent of the MTRP's net asset value, unless specifically approved by the Board.

~~4.~~ **Benchmark.** The MTRP benchmark shall be the NCREIF ~~Fund Index –~~ Open End Diversified Core Equity Index (NFI-ODCE), as a broad measure of investment in low-leveraged commercial real estate. It should be noted that because of the allocation to non-core real estate funds, the pool will be exposed to higher levels of real estate risk which should provide an expected return advantage versus core real estate over long time periods. ~~reasonably adjusted to provide comparable risk/return with the MTRP portfolio given the level of non-core exposure.~~ Because MTRP's underlying funds typically report their returns 30-~~60~~ 90 days after quarter-end, the benchmark will be compared on a one-quarter lagged basis. Benchmarking of the Pool should emphasize the comparison of longer-term performance data, ideally a period of time sufficient to encompass an entire real estate market cycle.

REAL ESTATE INVESTMENT GUIDELINES AND RANGES

The Montana Real Estate Pool (MTRP) was created to permit the nine Montana Retirement Systems to participate in a diversified real estate portfolio, consisting of commercial real estate and timberland. Real estate investments in the MTRP shall be consistent with the following guidelines:

a. **Permissible Investment Structures/Vehicles and Public/Private Allocations**

Investment Structures/Vehicles. The MTRP will include real estate investments, consisting of both open-end and closed-end pooled funds, the advantages and disadvantages of which are described in the following table.

VEHICLE	ADVANTAGES	DISADVANTAGES	LIQUIDITY
Open-Ended Fund	1. Property type diversification. 2. Geographic diversification. 3. Existing investment portfolio to evaluate. 4. Existing manager and fund performance record. 5. Infinite life. 6. Can redeem units in fund.	1. Passive investor. 2. Cannot replace manager. 3. Cannot influence manager decisions regarding acquisitions, financings, and sales. 4. Fee level and structures lack alignment of interests. 5. Lack of manager co-investment. 6. Historically have not sold assets to harvest gains.	Typically within 90 days unless there is an investor queue.
Closed-Ended Fund	1. Skilled value-added/ opportunistic management. 2. Manager organizations and track records. 3. Manager co-investment. 4. Manager-investor enhanced alignment of interests. 5. Asset liquidations by end of term of fund.	1. Illiquid-specified term. 2. Typically blind pools. 3. Cannot redeem interest. 4. Passive investor. 5. Cannot influence manager decisions regarding acquisitions, financings, and sales.	Typically 7 to 10 year terms.

Open-end Commingled Funds. The MTRP portfolio may have significant exposure to open-end commingled funds. The open-end fund investments shall be made primarily to provide (1) timely access to large existing, well-diversified portfolios, (2) reasonable property type and geographic diversification, (3) exposure to larger properties (i.e., over $50 mil.), and (4) reasonable liquidity (i.e., ability to purchase or redeem within 90 days unless there is an investor queue). Reasonable due diligence shall be completed to evaluate open-end commingled funds consistent with these objectives.

Closed-end Commingled Funds. The MTRP portfolio may have significant exposure to closed-end commingled funds. The closed-end fund investments may be made to obtain exposure to timberland and value-added and opportunistic real estate investments. Reasonable due diligence shall be completed prior to selecting closed-end fund investments.

Liquidity. The table below describes different levels of liquidity of real estate investments.

PORTFOLIO LIQUIDITY RANGES	
Degree of Liquidity	**Investment Type**
LIQUID (i.e., can redeem within 30 days if no queue exists)	Select Open-End Funds
MODERATE LIQUIDITY (i.e., can redeem within 90 to 120 days if no queue exists)	Open-End Funds
ILLIQUID (i.e., liquidity is subject to GP discretion until fund termination.)	Closed-End Funds

b. **Expected Investments.**

The categories utilized to classify MTRP real estate investments are: Timberland, Core, Value-Added, and Opportunistic. With the exception of Timberland, the categories are differentiated primarily by risk/return attributes rather than by property type. A description of each category follows.

Timberland. Equity investment in land that is populated with or is intended to produce commercially harvestable timber. Net inflation-adjusted returns are expected to be 5.0 percent to 7.0 percent. Proceeds from the sale of timber and ancillary revenue opportunities, such as recreational leases, will account for the majority of the real return, while land appreciation is expected to approximate the rate of inflation.

Core. Equity investment in operating and substantially-leased institutional quality real estate in the traditional property types (apartments, office, retail, industrial and hotel). Net returns historically have been in the 4.0 percent to 6.0 percent range (inflation-adjusted and net of fees) and are typically comprised of greater levels of income (i.e., 67.0 percent of total returns) with appreciation matching or exceeding inflation.

Value-Added. Equity or debt interests in assets requiring rehabilitation, redevelopment, development, lease-up or repositioning. Net returns historically have been in the 8.0 percent to 10.0 percent range (inflation-adjusted and net of fees). Value-added investments frequently involve the repositioning of distressed assets (i.e., not fully leased and operating). For example, a value-added investment may be an office building that is 40.0 percent vacant and needs significant capital to rehabilitate and reposition the property. Investment may also include non-traditional property types (e.g., manufactured housing) which may contain greater risk. Value-added investments typically are expected to generate returns in excess of core returns through the leasing-up of a property, which increases the end value by increasing in-place income and, in many cases, decreasing the capitalization rate used in selling the asset due to the reduced asset risk resulting from stabilized occupancy. Value-added returns are typically more dependent than core on appreciation returns with purchase prices based on in-place income or asset replacement cost (i.e., at a discount to replacement cost).

Opportunistic. Equity or debt investment in real estate properties, operating companies, and other investment vehicles involving significant investment risk. Risk may include real estate, financial restructuring, and non-real estate risk. Net returns have been in the 12.0 percent or higher range (inflation-adjusted and net of fees). Opportunistic investing includes distressed assets, financial restructurings, and/or financial engineering opportunities (e.g., foreclosing on a mortgage and selling the equity interest) and potentially the purchase of REITs or REOCs. Investments may also be made in non-traditional property types (e.g., self-storage), which typically contain greater risk. Opportunistic returns typically require even greater appreciation returns than value-added (e.g., 50.0 percent of total returns) and in many cases are originated with minimal income in place.

c. **Policy Constraints.**

Policy range targets for MTRP will be reviewed and adjusted periodically going forward with respect to MTRP exposures. Policy range targets include those dealing with investment category (see below), property type (Section e. 1.), geography (Section e. 2.), and leverage (Section f. 1.). Portfolio exposures to these factors will be presented quarterly. Because MTRP investments have limited liquidity, it will typically be impractical to correct deviations from policy range targets through the purchase or sale of assets. Therefore, if actual portfolio holdings should fall outside of policy guidelines, the MTRP shall refrain from investing in funds that would be expected to increase the deviation from policy ranges.

The following table sets forth the long-term investment category policy ranges for the portfolio.

INVESTMENT AND PORTFOLIO RISK/RETURN RANGES

Risk/Return	Nominal Return (Net)*	Policy Range
Core plus Timberland	6-8%	35%-65%
Value-Added	10-12%	20%-45%
Opportunistic	13-15%	10%-30%

* Assumes 2.5% inflation overall and 100 basis points core management fee, 200 basis points value-added and timberland management and incentive fees, and 300 basis points opportunistic management and incentive fees.

d. **Income and Appreciation Return Mix.**

Real estate investments, depending on their risk/return level, offer varying proportions of expected income/cash yield and appreciation returns. Investments providing higher income/cash yield returns typically will be preferred among investments of comparable expected total returns since income/cash yield returns provide greater return certainty and therefore lower risk. In addition, investments providing preferred or senior income/cash yield returns typically will be preferred among investments providing comparable returns because such features enhance the certainty of return.

e. **Diversification.**

The MTRP portfolio diversification is important in reducing portfolio risk and accomplishing superior risk-adjusted returns. The impact of investments on portfolio diversification, portfolio risk, and risk-adjusted returns shall be considered when evaluating prospective investments. Additionally, the portfolio may have over-weighted exposure in select property types or regions.

1. **Property Type.** Property type diversification is one of the most important diversification features in terms of impact on returns. The property types have historically performed differently during economic cycles. Residential and

industrial investments have historically outperformed the other property types during economic downturns. Office has historically underperformed during economic downturns, as reduced tenant demand results in lower rents, higher owner operating and build-out costs, and reduced income and cash flow. Hotels historically also have underperformed during economic downturns.

Diversification ranges are based on the universe of available real estate investments and institutional investor portfolio information. The following table provides a guideline range with respect to the MTRP property type diversification.

PROPERTY TYPE DIVERSIFICATION RANGES	
Property Type	**Policy Range**
Timberland	0%-35%
Office	15%-45%
Retail	10%-40%
Industrial	5%-35%
Residential	10%-40%
Hotel/Other	5%-25%

2. **Region/Location.** The importance of location to the long-term value of real estate is based on the economic fundamentals and the other risk attributes (e.g., weather, earthquake and local government impact) of U.S. and international regions. The distribution of real estate investments by geographic region shall be monitored for compliance with the broad ranges set forth in the table below.

REGIONAL DIVERSIFICATION RANGES	
Regions	**Policy Range**
West	20%-45%
South	10%-40%
Midwest	5%-25%
East	20%-45%
International	0%-30%

Because domestic commercial timberland is primarily concentrated in the South and the Pacific Northwest, the preceding regional diversification ranges shall apply only to non-timberland real estate holdings.

3. **Other.** In addition to property type and regional diversification, there are other real estate factors that impact the portfolio risk which may be reduced through diversification. These portfolio factors may include, but are not limited to, the following:

   a. **Investment Structure.** Equity, preferred equity, first mortgage debt or mezzanine equity. **Investments in public CMBS and REITs are not preferred**.

b. **Life Cycle.** Land, development/redevelopment, leasing (i.e., less than 90% leased) and operating (i.e., over 90% leased).

c. **Investment Size.** $0-$10 mil., $10-$20 mil., $20-$50 mil., $50-$100 mil., $100 mil.+.

While no formal diversification ranges are set forth for the above portfolio risk factors, these and other factors may be monitored in assessing overall portfolio risk and expected return.

f. **Other Risk Factors**.

1. **Leverage.** Leverage is a significant risk factor. Its importance is magnified during an economic downturn when decreasing property values and stricter lending terms can lead to unexpected increased leverage levels. It may be the case that the leverage level increases as market conditions worsen.

   On an individual fund basis, the leverage level can range up to 75.0 percent. Leverage consists of the combined borrowing at the property level and the fund level. On a select basis, the leverage may exceed 75.0 percent for a given investment, if it is determined to be reasonable to do so. Leverage shall be monitored on an individual fund level, and new investments shall be made with the intention that the total MTRP portfolio leverage shall not exceed 60.0 percent.

LEVERAGE RANGES	
Risk	**Range**
Timberland	0%-30%
Core	0%-50%
Non-Core	0%-75%
Total Real Estate Portfolio	0%-60%

2. **Monitoring and Control.** All investments will be made through investment vehicles providing full discretion to investment managers.

3. **Manager Concentrations.** The MTRP exposure to each manager shall be reviewed regularly to determine the reasonableness of each. No manager shall have under management more than 25.0 percent of the MTRP's net asset value, unless specifically approved by the Board.

Benchmark. The MTRP benchmark shall be the NCREIF Open End Diversified Core Equity Index (NFI-ODCE), as a broad measure of investment in low-leveraged commercial real estate. It should be noted that because of the allocation to non-core real estate funds, the pool will be exposed to higher levels of real estate risk which should provide an expected return advantage versus core real estate over long time periods. Because MTRP's underlying funds typically report their returns 30-90 days after quarter-end, the benchmark will be compared on a one-quarter lagged basis. Benchmarking of the Pool should emphasize the comparison of longer-term performance data, ideally a period of time sufficient to encompass an entire real estate market cycle.

MONTANA BOARD OF INVESTMENTS
PUBLIC MARKETS MANAGER EVALUATION POLICY

INTRODUCTION

The purpose of this policy is to broadly define the monitoring and evaluation of external public markets managers. This policy also provides a basis for the retention and/or termination of managers employed within the Montana Domestic Equity Pool (MDEP), the Montana International Equity Pool (MTIP), the Retirement Funds Bond Pool (RFBP), and the Trust Funds Investment Pool (TFIP).

The costs involved in transitioning assets between managed portfolios can be significant and have the potential to detract from returns. Therefore it is important that the decision process be based on a thorough assessment of relevant evaluation criteria prior to implementing any manager changes. Staff will consider such costs when deciding to add or subtract to manager weights within the pools as well as in deciding to retain or terminate managers.

MONITORING PROCESS

Periodic Reviews: Staff will conduct periodic reviews of the external managers and will document such periodic reviews and subsequent conclusions. Periodic reviews may include quarterly conference calls on portfolio performance and organizational issues as well as reviews conducted in the offices of the Montana Board of Investments (MBOI) and on-site at the offices of the external managers. Reviews will cover the broad manager evaluation criteria indicated in this policy as well as further, more-detailed analysis related to the criteria as needed.

Continual Assessment: Staff will make a continual assessment of the external managers by establishing and maintaining manager profiles, monitoring company actions, and analyzing the performance of the portfolios managed with the use of in-house data bases and sophisticated analytical systems, including systems accessed through the Master Custodian and the Investment Consultant. This process culminates in a judgment which takes into account all aspects of the manager's working relationship with MBOI, including portfolio performance.

Staff will actively work with the Investment Consultant in the assessment of managers which will include use of database research, conference calls and discussions specific to each manager, and in any consideration of actions to be taken with respect to managers.

~~It is also important to note that our manager contracts are limited to a seven year term. While we may choose to issue a RFP at any time as deemed appropriate, this contractual provision will eventually force us to issue a RFP to which the manager may respond and be subject to re-evaluation against his/her peers.~~

MANAGER EVALUATIONS

The evaluation of managers includes the assessment of the managers with respect to the following qualitative and quantitative criteria.

MONTANA BOARD OF INVESTMENTS
PUBLIC MARKETS MANAGER EVALUATION POLICY

Qualitative Criteria:

- Firm ownership and/or structure
- Stability of personnel
- Client base and/or assets under management
- Adherence to investment philosophy and style (style drift)
- Unique macroeconomic and capital market events that affect manager performance
- Client service, reporting, and reconciliation issues
- Ethics and regulatory issues
- Compliance with respect to contract and investment guidelines
- Asset allocation strategy changes that affect manager funding levels

Quantitative Criteria:

- Performance versus benchmark – Performance of managers is evaluated on a three-year rolling period after fees.
- Performance versus peer group – Performance of managers is evaluated on a three-year rolling period before fees.
- Performance attribution versus benchmark – Performance of managers is evaluated on a quarterly and annual basis.
- Other measures of performance, including the following statistical measures:
    - Tracking error
    - Information ratio
    - Sharpe ratio
    - Alpha and Beta

PERFORMANCE MEASUREMENT

Performance calculations and relative performance measurement compared to the relevant benchmark(s) and peer groups are based on a daily time-weighted rate of return. The official book of record for performance measurement is the Master Custodian.

The performance periods relevant to the manager review process will depend in part on market conditions and whether any unique circumstances are apparent that may impact a manager's performance strength or weakness. Generally, however, a measurement period should be sufficiently long to enable observation across a variety of different market conditions. This would suggest a normal evaluation period of three to five years.

ACTIONS

Watch List Status: Staff will maintain a "Watch List" of external managers that have been noted to have deficiencies in one or more evaluation criteria. An external manager may be put on the "Watch List" for deficiencies in any of the above mentioned criteria or for any other reason deemed necessary by the Chief Investment Officer (CIO). A manager may be removed from the "Watch List" if the CIO is satisfied that the concerns which led to such status have been remedied and/or no longer apply.

MONTANA BOARD OF INVESTMENTS
PUBLIC MARKETS MANAGER EVALUATION POLICY

Termination: The CIO may terminate a manager at any time for any reason deemed to be prudent and necessary and consistent with the terms of the appropriate contract.

ROLES AND RESPONSIBILITIES

CIO: The CIO is responsible for the final decision regarding retention of managers, placement on and removal of "Watch List" status, and termination of managers.

Staff: Staff is responsible for monitoring external managers, portfolio allocations and recommending allocation changes to the CIO, and recommending retention or termination of external managers to the CIO.

Investment Consultant: The consultant is responsible for assisting staff in monitoring and evaluating managers and for reporting independently to the Board on a quarterly basis.

External Managers: The external managers are responsible for all aspects of portfolio management as set forth in their respective contracts and investment guidelines. Managers also must communicate with staff as needed regarding investment strategies and results in a consistent manner. Managers must cooperate fully with staff regarding administrative, accounting, and reconciliation issues as well as any requests from the Investment Consultant and the Custodian.

MONTANA BOARD OF INVESTMENTS
PUBLIC MARKETS MANAGER EVALUATION POLICY

INTRODUCTION

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The costs involved in transitioning assets between managed portfolios can be significant and have the potential to detract from returns. Therefore it is important that the decision process be based on a thorough assessment of relevant evaluation criteria prior to implementing any manager changes. Staff will consider such costs when deciding to add or subtract to manager weights within the pools as well as in deciding to retain or terminate managers.

MONITORING PROCESS

Periodic Reviews: Staff will conduct periodic reviews of the external managers and will document such periodic reviews and subsequent conclusions. Periodic reviews may include quarterly conference calls on portfolio performance and organizational issues as well as reviews conducted in the offices of the Montana Board of Investments (MBOI) and on-site at the offices of the external managers. Reviews will cover the broad manager evaluation criteria indicated in this policy as well as further, more-detailed analysis related to the criteria as needed.

Continual Assessment: Staff will make a continual assessment of the external managers by establishing and maintaining manager profiles, monitoring company actions, and analyzing the performance of the portfolios managed with the use of in-house data bases and sophisticated analytical systems, including systems accessed through the Master Custodian and the Investment Consultant. This process culminates in a judgment which takes into account all aspects of the manager’s working relationship with MBOI, including portfolio performance.

Staff will actively work with the Investment Consultant in the assessment of managers which will include use of database research, conference calls and discussions specific to each manager, and in any consideration of actions to be taken with respect to managers.

MANAGER EVALUATIONS

The evaluation of managers includes the assessment of the managers with respect to the following qualitative and quantitative criteria.

Qualitative Criteria:

- Firm ownership and/or structure
- Stability of personnel
- Client base and/or assets under management
- Adherence to investment philosophy and style (style drift)
- Unique macroeconomic and capital market events that affect manager performance

MONTANA BOARD OF INVESTMENTS
PUBLIC MARKETS MANAGER EVALUATION POLICY

- Client service, reporting, and reconciliation issues
- Ethics and regulatory issues
- Compliance with respect to contract and investment guidelines
- Asset allocation strategy changes that affect manager funding levels

Quantitative Criteria:
- Performance versus benchmark – Performance of managers is evaluated on a three-year rolling period after fees.
- Performance versus peer group – Performance of managers is evaluated on a three-year rolling period before fees.
- Performance attribution versus benchmark – Performance of managers is evaluated on a quarterly and annual basis.
- Other measures of performance, including the following statistical measures:
    - Tracking error
    - Information ratio
    - Sharpe ratio
    - Alpha and Beta

PERFORMANCE MEASUREMENT

Performance calculations and relative performance measurement compared to the relevant benchmark(s) and peer groups are based on a daily time-weighted rate of return. The official book of record for performance measurement is the Master Custodian.

The performance periods relevant to the manager review process will depend in part on market conditions and whether any unique circumstances are apparent that may impact a manager's performance strength or weakness. Generally, however, a measurement period should be sufficiently long to enable observation across a variety of different market conditions. This would suggest a normal evaluation period of three to five years.

ACTIONS

Watch List Status: Staff will maintain a "Watch List" of external managers that have been noted to have deficiencies in one or more evaluation criteria. An external manager may be put on the "Watch List" for deficiencies in any of the above mentioned criteria or for any other reason deemed necessary by the Chief Investment Officer (CIO). A manager may be removed from the "Watch List" if the CIO is satisfied that the concerns which led to such status have been remedied and/or no longer apply.

Termination: The CIO may terminate a manager at any time for any reason deemed to be prudent and necessary and consistent with the terms of the appropriate contract.

MONTANA BOARD OF INVESTMENTS
PUBLIC MARKETS MANAGER EVALUATION POLICY

ROLES AND RESPONSIBILITIES

CIO: The CIO is responsible for the final decision regarding retention of managers, placement on and removal of “Watch List” status, and termination of managers.

Staff: Staff is responsible for monitoring external managers, portfolio allocations and recommending allocation changes to the CIO, and recommending retention or termination of external managers to the CIO.

Investment Consultant: The consultant is responsible for assisting staff in monitoring and evaluating managers and for reporting independently to the Board on a quarterly basis.

External Managers: The external managers are responsible for all aspects of portfolio management as set forth in their respective contracts and investment guidelines. Managers also must communicate with staff as needed regarding investment strategies and results in a consistent manner. Managers must cooperate fully with staff regarding administrative, accounting, and reconciliation issues as well as any requests from the Investment Consultant and the Custodian.

MEMORANDUM

Montana Board of Investments
Department of Commerce
2401 Colonial Drive, 3rd Floor
Helena, MT 59601 (406) 444-0001

To: Members of the Board

From: David Ewer, Executive Director

Date: April 2, 2013

Subject: Board's Relationship with the Montana Finance Facility Authority

Legal Authority to Lend Money to Montana Facility Finance Authority

In 1991, legislation was passed that states in part, "the board of investments may, upon terms and conditions as the board considers reasonable: 1) loan money to the authority for deposit in the capital reserve account; and 2) purchase bonds and notes issued by the authority."

Board's Financial Support to the Authority

The Board credit enhances some, but not all, of the Montana Facility Finance Authority's (the "Authority") bonds, saving Montana hospitals millions in interest expense due to the Board's high credit rating. Critical Access Hospitals (hospitals with 25 beds or less) would have been unable to access the tax-exempt bond market without the Board's credit enhancement. Exhibit A shows the outstanding enhanced bonds for both the Authority and the Board's INTERCAP program. The credit support for the two programs is different. The Board enhances both INTERCAP and Authority bonds by pledging to replenish the reserve fund so sufficient funds are available to pay bond principal and interest. The Board also enhances INTERCAP bonds by agreeing to purchase bonds that have been tendered but not remarketed; the Board does not enhance Authority bonds this way.

The Board currently enhances $119 million in Authority bonds (including $6 million for the State's developmental disability facility) and $107 million in INTERCAP bonds. Before calling on the credit enhancement, the Authority's own bond reserves, which are substantial, are to be used first. The Authority's bond reserves would provide about one year to resolve a problem. Also, the Authority has significant fund balances (see Exhibit B) that would provide at least an additional year for a work-out. The Board pays only the semi-annual principal and interest as needed to replenish the reserve fund as described in the paragraph above, not the full principal immediately.

Authority Payments, Performance, and Lack of Credit Enhancement Elsewhere

Since inception, the Authority has paid over $2.3 million in enhancement fees (credited to the Permanent Coal Trust Fund). No bonds have ever defaulted and all are current. While bond insurance and letters of credit were available before the financial meltdown of 2008, few, maybe none, are available today. Due to the small size of the hospitals that have received the Board's credit enhancement, none would have been able to access those enhancements, even when they were available.

Board's Governance to Implement Bond Enhancement to Authority

The Board's Governance Manual authorizes the Executive Director to take all necessary action to implement credit enhancement activity per Resolution 219. Resolution 219 identifies which funds could be used to satisfy performance, including the Permanent Coal Trust Fund, Treasurer's Fund and Short

Term Investment Pool (STIP). The investment policy statement for each of these funds acknowledges that such performance is an eligible investment activity.

Underwriting the Credit Enhancement

Providing credit enhancement is not automatic. Board staff first review the credit and bring it to the Board's Loan Committee for approval. The full Board has the ultimate say and, as per its Resolution 219 (Exhibit C), must approve a separate credit enhancement resolution for every bond receiving credit enhancement.

Board's Credit Enhancement Fee

The Board currently charges a one-time fee for the credit enhancement it provides. The Board has broad discretion on setting reasonable terms and conditions and has no requirement to set bond enhancement prices at a market rate. Also, the law does not identify which fiduciary assets the Board may pledge. To date, all credit enhancement fees have been applied to the Permanent Coal Trust Fund, even though the Board has identified two other possible funding sources, the Treasurer's Fund and STIP.

The fee schedule (Exhibit D) considers the term of the credit enhancement, the structure of the bond issue and the organizational entity (governmental or not-for-profit). As an example, the Board's most recent credit enhancement was for $12 million INTERCAP bonds, maturing in 25 years. The Board received $156,000 for this credit enhancement.

Board as a Rated Credit

Both Moody's Investors Service and Fitch Ratings rate the Board's credit enhanced bonds. Moody's is Aa3, Fitch is AA-. The rating is based on an assessment of the fiscal capacity of the Board, its total leverage, and the relative size of outstanding and new proposed debt versus the funds available for credit enhancement. A summary of Moody's rating rationale is in Exhibit E.

Considerations Regarding the Fee Schedule for Credit Enhancement

The Board's credit enhancement is both a valuable resource that benefits borrowers and a significant contingent liability that is disclosed in the Board's footnotes to its financial statements. The Board has the dual role of reducing borrowing costs by credit enhancing bonds as permitted by statute, and considering and assessing an appropriate charge for the risk/benefits taken by the funds that ultimately bear the risk of funding a defaulted bond. The Board is not required to credit enhance any bonds.

Authority's Executive Director

Michelle Barstad, the Authority's Executive Director, will be available to answer questions and to give an overview as to the status and possible future requests to the Board. Members of the Authority Board will be invited as well.

Staff Review and Comments

Staff has reviewed the status of the Authority's program relying on the Board's credit enhancement and has no recommendations for change. Staff is comfortable with maintaining the Board's current credit enhancement fee schedule.

Exhibit A

MONTANA BOARD OF INVESTMENTS
Total Enhancements by the Permanent Coal Trust Fund
as of 3-31-13

Bond Issue	Issue Date	Maturity Date	Reserve Fund	Amount Issued	Amount Outstanding			Principal[1]	Interest[2]	Total Exposure
MONTANA BOARD OF INVESTMENTS (MBOI)										
Irrigation Dist. Pooled Prgm.	08/16/88	08/01/13	76,000	4,976,214	70,000			70,000	5,390	75,390
INTERCAP 1997	03/01/97	03/01/17	750,104	10,000,000	9,210,000	*		9,210,000	20,262	9,230,262
INTERCAP 1998	03/01/98	03/01/18	937,640	12,500,000	11,875,000	*		11,875,000	26,125	11,901,125
INTERCAP 2000	09/13/00	03/01/25	1,124,903	15,000,000	14,470,000	*		14,470,000	31,834	14,501,834
INTERCAP 2003	05/01/03	03/01/28	1,124,904	15,000,000	14,525,000	*		14,525,000	31,955	14,556,955
INTERCAP 2004	04/01/04	03/01/29	1,387,383	18,500,000	18,200,000	*		18,200,000	40,040	18,240,040
INTERCAP 2007	03/01/07	03/01/32	1,124,819	15,000,000	14,775,000	*		14,775,000	32,505	14,807,505
INTERCAP 2010	03/01/10	03/01/35	899,756	12,000,000	11,975,000	*		11,975,000	26,345	12,001,345
MBOI Sub-total			$ 7,425,508	$ 102,976,214	$ 95,100,000		**MBOI Subtotal**	**95,100,000**	**214,456**	**95,314,456**
MONTANA FACILITY FINANCE AUTHORITY (MFFA)										
Bond Issues										
MLP 98A-Big Horn County	02/01/98	02/01/18	115,650	1,425,000	490,000			490,000	24,900	514,900
MLP 98D-Lewis&Clark Co.(c	02/01/98	02/01/18	69,875	860,000	295,000			295,000	14,990	309,990
MLP 00A-Marcus Daly Hospit	03/01/00	08/01/20	292,100	3,440,000	1,800,000			1,800,000	108,000	1,908,000
Montana Developmental Cent	09/01/03	06/01/19	1,017,926	11,510,000	5,960,000			5,960,000	269,218	6,229,218
MLP 05A-Marias Medical Cer	04/01/05	01/01/28	290,401	4,030,000	2,385,000			2,385,000	116,795	2,501,795
MLP 05B-Montana Children's	04/01/05	01/01/24	767,510	9,720,000	6,360,000			6,360,000	318,503	6,678,503
MLP 06A-Northern MT Hospi	03/01/06	10/01/15	667,000	6,670,000	2,175,000			2,175,000	115,475	2,290,475
MLP 07A-Marcus Daly Hospit	01/31/07	08/01/27	533,533	7,135,000	5,835,000			5,835,000	240,294	6,075,294
MLP 07B-Northeast Montana	05/10/07	05/01/32	863,364	12,515,000	11,370,000			11,370,000	505,513	11,875,513
MLP 07C-St. Luke Communit	06/27/07	01/01/32	1,644,728	23,500,000	20,215,000			20,215,000	960,613	21,175,613
MLP 08A-Glendive Medical C	07/01/08	07/01/18	2,098,388	30,000,000	27,825,000			27,825,000	1,310,539	29,135,539
MLP 10A-Powell County Men	08/11/10	07/01/36	1,184,009	15,000,000	15,000,000			15,000,000	682,770	15,682,770
MLP 10D-Community Medica	12/29/10	06/01/35	1,901,716	19,015,000	19,015,000			19,015,000	1,011,714	20,026,714
MFFA Bonds Sub-total			$11,446,200	$ 144,820,000	$ 118,725,000		**MFFA Bond Issues**	**118,725,000**	**5,679,322**	**124,404,322**
Surety Bonds										
Alternatives, Inc. (97)	11/01/97	10/01/17	888,064	2,925,000	1,015,000	**		1,015,000	66,640	245,720
Alternatives, Inc. (06)	07/13/06	10/01/26		7,920,000	6,120,000	**		6,120,000	314,419	642,344
Missoula Correctional Service	10/15/98	10/01/18	450,730	5,580,000	2,285,000	**		2,285,000	124,713	455,733
Great Falls Prerelease (05)	12/22/05	04/01/21	432,295	4,500,000	2,954,157	**		2,954,157	81,868	432,295
Boyd Andrew Community Ser	07/01/00	10/01/20		2,245,000	1,210,000	**		1,210,000	153,567	199,338
Boyd Andrew Community Ser	05/01/04	04/01/14	346,035	250,000	44,796	**		44,796	2,347	31,224
Boyd Andrew Community Ser	08/04/05	10/01/20		1,200,000	754,045	**		754,045	38,574	115,473
Community, Counseling, & Co	08/08/06	10/01/27	710,576	9,250,000	7,280,000	**		7,280,000	335,156	710,600
Boyd Andrew Community Ser	08/08/06	10/01/27	391,937	5,085,000	4,005,000	**		4,005,000	184,306	391,950
MFFA Surety Bonds Sub-total			$3,219,637	$ 38,955,000	$ 25,667,998		**MFFA Surety Bonds**	**25,667,998**	**1,301,590**	**3,224,677**
MFFA Sub-total				**$ 183,775,000**	**$ 121,949,677**		**MFFA Subtotal**	**144,392,998**	**6,980,911**	**127,628,998**
Grand Total				**$ 286,751,214**	**$ 217,049,677**					
							TOTAL ENHANCEMENTS BY PERMANENT COAL TRUST FUND	**239,492,998**	**7,195,367**	**222,943,454**

*Parity INTERCAP Bonds
**Surety Reserve, maximum BOI exposure

Exhibit B

MONTANA FACILITY FINANCE AUTHORITY
DEPARTMENT OF COMMERCE
A COMPONENT UNIT OF THE STATE OF MONTANA
STATEMENT OF NET ASSETS - ENTERPRISE FUND
JUNE 30, 2012 AND 2011

	2012	2011
ASSETS:		
Current Assets:		
Cash & Cash Equivalents (Note 2)	$ 3,371,977	$ 2,985,160
Interest Receivable	856	594
Accounts Receivable	643	0
Short Term Notes Receivable (Note 4)	322,539	270,460
Securities Lending Collateral (Note 2)	7,068	39,026
Due From Primary Government	0	0
Prepaid Expenses	1,641	42
Total Current Assets	3,704,724	3,295,282
Noncurrent Assets:		
Long Term Notes Receivable (Note 4)	804,039	903,988
Investments	55,459	49,792
Capital Assets (Note 1)	31,436	45
Total NonCurrent Assets	890,934	953,825
Total Assets	$ 4,595,658	$ 4,249,107
LIABILITIES:		
Liabilities:		
Current Liabilities:		
Accounts Payable	$ 9,394	$ 10,318
Due to Primary Government	972	1,228
Secuities Lending Liability (Note 2)	7,068	39,026
Current Portion of LT Payables	16,428	0
Compensated Absences	14,118	11,935
Total Current Liabilities	$ 47,980	$ 62,507
Noncurrent Liabilities:		
Compensated Absences	22,228	19,649
LT Payables	31,372	0
Est Claims Payable-Non Current	11,834	
OPEB Implicit Rate Subsidy (Note 6)	29,015	20,096
Total Noncurrent Liabilities	94,449	39,745
Total Liabilities	142,429	102,252
Net Assets		
Invested in Capital Assets Net of Related Debt	$ 31,436	$ 45
Total Unrestricted Net Assets	4,421,793	4,146,810
Total Net Assets (Note 7)	$ 4,453,229	$ 4,146,855
Total Net Assets and Liabilitites	$ 4,595,658	$ 4,249,107

The accompanying notes to the financial statements are an integral part of this statement.

Exhibit C

RESOLUTION 219

MONTANA BOARD OF INVESTMENTS CREDIT ENHANCEMENT OF BONDS

ADOPTED May 14, 2008

Be It Resolved by the Montana Board of Investments (the "Board") as follows:

Section 1. Recitals.

Section 1.01. History, Authorization of Unified Investment Program and the Board. Article VIII, Section 13 of the Montana Constitution (the "Constitution") directs the legislature to provide for a unified investment program for public funds and public retirement system and state compensation insurance fund assets. The Legislature, pursuant to Title 17, Chapter 6, Part 21, Montana Code Annotated (the "Unified Investment Program Act"), has created and directed the Board to administer the unified investment program mandated by the Constitution. The Board has the primary authority to invest state funds, and to determine the types of investments to be made, subject to the restrictions of the Constitution and the Unified Investment Program Act.

Section 1.02. History, Authorization of Montana Economic Development Board and Municipal Finance Consolidation Act Bonds. The 1983 Legislature created the Montana Economic Development Authority Board ("MEDB"), to among other things issue notes and bonds to finance loans to and the purchase of bonds and notes of Montana governmental units, to establish or replenish reserves securing the payments of its bonds and notes, and to finance all expenditures incident to and necessary or convenient to carry out the provisions of Title 17, Chapter 5, Part 16, Montana Code Annotated (the "Municipal Finance Consolidation Act" or "MFCA Act"). As set forth in Section 17-5-1602(2)(b) of the Municipal Finance Consolidation Act, the State's goal was to foster the provisions of efficient capital markets, to reduce costs of borrowing and, among other things, to provide additional security for the payment of bonds and notes held by investors. In conjunction with issuing its Municipal Finance Consolidation Act Bonds in 1985, the MEDB adopted Resolution No. 68 on July 24, 1985, establishing a Municipal Finance Consolidation Act Reserve Fund (the "Reserve Fund") to secure bonds or obligations issued under the Municipal Finance Consolidation Act ("MFCA Bonds"). Pursuant to a Resolution, the MEDB and the Board entered into a Security Agreement whereby the Board agreed to make an interest bearing loan to the MEDB to restore any deficiency in the Reserve Fund and also agreed, for a fee, to purchase MFCA Bonds tendered for purchase and not remarketed. Each series of MFCA Bonds credit enhanced by the Board is approved by resolution by the Board. The Board has never been called upon to make any loans or purchase any of these Bonds.

Section 1.03. Authorization for the Board to Issue Municipal Finance Consolidation Act Bonds. Pursuant to Chapter 581, Montana Session Laws of 1987, the Board assumed the role of the MEDB with respect to the issuance of the Montana Finance Consolidation Act Bonds and other bond programs authorized by the State. The Board issued its first series of Intermediate Term Capital Program (INTERCAP) Municipal Finance Consolidation Act Bonds in 1987 (the "Series 1987 INTERCAP Bonds"). The Series 1987 INTERCAP Bonds and all series of INTERCAP Bonds subsequently issued by the Board have also been secured by the Reserve Fund. In the Resolution authorizing and approving the issuance of the Series 1987 INTERCAP Bonds, the Board approved the Indenture of Trust pursuant to which the Series 1987 INTERCAP Bonds were to be issued and secured (the "1987 Trust Indenture"); agreed to make an interest bearing loan to the Reserve Fund and agreed, for a fee, to purchase any Series 1987 INTERCAP Bonds tendered for repurchase that were not remarketed (the "Authorizing Resolution"). In 1991, the INTERCAP program was expanded, requiring a new Trust Indenture (the "1991 Trust Indenture"), securing the INTERCAP Bonds, that was approved by the Board. Each subsequent series of INTERCAP Bonds issued by the Board have been approved by an Authorizing Resolution and a Supplemental Indenture. The Authorizing Resolutions, the 1991 Trust Indenture and Supplemental Indenture are collectively referred to as the "Bond Documents." The Board has never been called on to make a loan to the Reserve Fund or purchase tendered MFCA Bonds under the Bond Documents.

Section 1.04. History, Authorizations, Montana Facility Finance Authority Bonds. Pursuant to Chapter 703, Montana Session Laws of 1987, now codified in Montana Code Annotated, Title 90, Chapter 7, Parts 1, 2 and 3, as amended (the "MFFA Act"), the Montana Health Facility Finance Authority, now the Montana Facility Finance Authority (the "MFFA") is authorized to issue revenue bonds to finance nonprofit hospitals, prelease centers and other nonprofit health-care providers or entities. The MFFA has created a capital reserve account to provide additional security ("Capital Reserve Account") for the Bonds it issues under the MFFA Act ("MFFA Bonds"). Pursuant to the MFFA Act, the Board is authorized to loan money to the MFFA for deposit in its capital reserve account and to purchase its bonds and notes. Pursuant to resolutions of the Board relating to each series of MFFA Bonds for which credit enhancement is provided, the Board is authorized to enter into an agreement with the MFFA whereby the Board agrees to make an interest bearing loan to the Capital Reserve Account to restore any deficiency (the "MFFA Capital Reserve Account Agreement"). For each series of MFFA Bonds credit enhanced by the Board, the Board has by Resolution approved entering into additional Capital Reserve Account Agreements. The Board has never been called upon to make a loan to the MFFA Capital Reserve Account. To date, the Board has not entered into any agreements to purchase tendered MFFA Bonds.

Section 1.05. Previous Credit Enhancement Policies. The Board adopted a "Credit Enhancement Policy" on February 17, 2006.

Section 2. Findings and Determinations of the Board.

Section 2.01. The Board desires to continue to enhance the marketability of bonds and notes issued under both the MFCA Act and the MFFA Act and to assist the Board and the MFFA in obtaining the lowest possible interest rates on loans to eligible governmental units and non-profit corporations providing needed and essential services and facilities to the public.

Section 2.02. The Board adopts this resolution to codify and clarify the circumstances under which the Board has and will continue to provide credit enhancement; to authorize its Executive Director to honor and fulfill the Board's obligations under the Bond Documents (and Capital Reserve Account Agreement); and to make this resolution a part of the Board Governance Policy.

Section 2.03. Resolution No. 68 adopted by the Montana Economic Development Board on July 24, 1985, establishing the Reserve Fund to secure bonds or obligations issued by the Board [is attached hereto as Schedule 1 and incorporated by reference.]

Section. 3. Decision to Provide Credit Enhancement; source of Credit Enhancement.

Section 3.01. The decision to provide credit enhancement as authorized by the MFFA Act and the MFCA Act shall be made by the Board pursuant to a duly authorized resolution of the Board related to each series of Bonds to be issued.

Section 3.02. The Board's policy shall be to provide credit enhancement when it is prudent to do so and in the Board's judgment would result in a lower interest rate to the borrowers under the MFCA Act and MFFA Act than could be otherwise obtained.

Section 3.03. The funds in the Unified Investment Program from which the Board's Credit Enhancement obligations could be satisfied include, but are not limited to: the Permanent Fund sub-fund of the Coal Tax Trust, the Short Term Investment Pool, and the Treasurer's Fund.

Section 4. Duties of the Executive Director.

Section 4.01. Loans. When required under the terms of the Bond Documents, the Executive Director of the Board is authorized to loan funds to the Board Reserve Fund and the MFFA Capital Reserve Account pursuant to the requirements of the Bond Documents.

Section 4.02. Purchase of Bonds. When required to do so under the Bond Documents, the Executive Director is authorized to purchase Bonds pursuant to the requirements of the Bond Documents.

Section 4.03. Use of Funds. The Executive Director is authorized to determine which legally available funds to use for the above purposes.

Section 4.04. Notification of Board. If the Executive Director makes a loan to the Reserve Funds, Capital Reserve Account or purchases bonds pursuant to the Bond Documents, he/she shall notify Board members via e-mail within three (3) business days of such action and provide a full report to the Board at its next regularly schedule meeting specifying the reasons for such action, the dollar amount, the terms, and the funding source for the loan or bond purchase.

Section 5. Effective Date; No Repeals Policy.

Section 5.01. This resolution shall become effective upon passage by the Board and execution and certification by the Chairman of the Board. This Resolution shall supersede in every respect and replace in its entirety the "Credit Enhancement Policy" adopted by the Board on February 17, 2006.

Section 5.02. This resolution is not intended and shall not be construed to modify any commitment, obligations or agreements, the Board has made pursuant to any duly authorized resolution or agreement relating to Bonds issued under the MFCA Act or the MFFA Act.

Section 5.03. The policies and procedures established by resolution become an integral part of the Board's Governance Policy.

Dated and approved this 14th day of May 2008.

ATTEST

By: ____________________________

Chairman

Exhibit C

CERTIFICATE OF MINUTES RELATING TO
RESOLUTION NO. 068

Issuer: Montana Economic Development Board

Kind, date, time and place of meeting: A board meeting held on July 24, 1985, at 8:00 o'clock a.m. at Jorgenson's Holiday Motel in Helena, Montana.

Members present: Pat McKittrick, Jack Schutte, Yvonne Snider, Karen Locke, John Orth, and Jerry Sullivan.

Members absent: Steve Brown.

Documents attached:
Minutes of said meeting (pages):

RESOLUTION NO. 068

RESOLUTION OF THE MONTANA ECONOMIC DEVELOPMENT BOARD ESTABLISHING A MUNICIPAL FINANCE CONSOLIDATION ACT RESERVE FUND

I, the undersigned, being the fully qualified and acting recording officer of the public body issuing the obligations referred to in the title of this certificate, certify that the documents attached hereto, as described above, have been carefully compared with the original records of the public body in my legal custody, from which they have been transcribed; that the documents are a correct and complete transcript of the minutes of a meeting of the governing body at the meeting, insofar as they relate to the obligations; and that the meeting was duly held by the governing body at the time and place and was attended throughout by the members indicated above, pursuant to call and notice of such meeting given as required by law.

WITNESS my hand officially as such recording officer this 24 day of July, 1985.

John Orth

John Orth
Secretary

Exhibit C

RESOLUTION 068

Member Jack Schutte introduced the following resolution and moved its adoption:

RESOLUTION OF THE MONTANA ECONOMIC DEVELOPMENT BOARD ESTABLISHING A MUNICIPAL FINANCE CONSOLIDATION ACT RESERVE FUND

BE IT RESOLVED by The Montana Economic Development Board (the Board) as follows:

1. Recitals. The Board is authorized and directed by Title 17, Chapter 5, Part 15, Montana Code Annotated, as amended (the Act) to create funds and accounts necessary to implement the Act, including a municipal consolidation finance act reserve fund and other funds and accounts; to issue and sell bonds and notes for the purpose of financing programs thereunder; and to secure the bonds and notes pursuant to an indenture of trust and resolution. Pursuant to the Act, the Board has undertaken a Cash Anticipation Financing Program to acquire Notes Issued by local government units (the Borrowers) to finance their cash flow requirements. To provide funds to acquire the Notes, the Board has authorized the execution of an Indenture of Trust (the Indenture) between the Board and First Trust Company of Montana (the Trustee) pursuant to which the Board is authorized to issue and sell its Bonds. In order to provide for the segregation of and accounting for certain of its revenues and funds and in furtherance of the Act, the Board hereby determines it necessary and appropriate to adopt this resolution (the Resolution).

2. Definitions. Capitalized terms used but not defined herein shall have the meanings assigned them in the Indenture.

3. Municipal Finance Consolidation Act Reserve Fund. The Board hereby creates and establishes the Municipal Finance Consolidation Act Reserve Fund and authorizes the creation of accounts therein for the purpose of securing one or more series of bonds or obligations issued by the Board. Accounts may be created pursuant to indentures or resolutions with respect to series of bonds or obligations secured thereby and may be held by a trust and invested pursuant to the provisions of such indentures or resolutions. A reserve fund requirement may be established with respect to each account. So long as the reserve fund requirement of each

Exhibit C

account is maintained, all investment income therefrom may be transferred to other accounts and funds of the Board as provided in the indenture and resolution securing the bonds.

4. Other Funds and Accounts. Nothing contained in this Resolution shall be deemed to limit the authority of the Board to create other funds and accounts pursuant to the Act in addition to the Municipal Finance Consolidation Act Reserve Fund.

Chairman

Exhibit D

BOI ENHANCEMENT FEE SCHEDULE

<u>Term</u>

First 10 years	2 basis points/year (20 max)
11-15 years	3 basis points/year (15 max)
16-20 years	5 basis points/year (25 max)
> 20 years	10 basis points/year

<u>Bond Type</u>

Government obligation		0 basis points
Revenue:	Government	10 basis points
	Private	20 basis points (A) 30 basis points (BAA) 50 basis points (non-rated)

<u>Reserve Fund</u>

Pooled:	= Annual Debt Service	10 basis points
	< Annual Debt Service	25 basis points
Non-pooled:	= Annual Debt Service	25 basis points
	< Annual Debt Service	50 basis points

TOTAL BOI FEE (BASIS POINTS)
TOTAL FEE BASED ON PAR

Exhibit E

MOODY'S
INVESTORS SERVICE

Announcement: Moody's affirms Aa3/VMIG 1 rating on Montana Board of Investment's Municipal Finance Consolidation Act Bonds

Global Credit Research - 15 Aug 2012

$220 million of parity debt affected

New York, August 15, 2012 -- Moody's has affirmed the Aa3/VMIG 1 ratings and stable outlook on the Montana Board of Investment's Municipal Finance Consolidation Act Bonds, consisting primarily of the INTERCAP Revolving Program. Approximately $95 million is outstanding.

RATING RATIONALE

The Aa3 rating is based on the Montana Board of Investments' (the Board) irrevocable pledge to pay principal and interest on the bonds if amounts in the bond fund and reserve account should be insufficient, as well as the Board's pledge to purchase any tendered bonds if necessary. The Board maintains more than adequate resources to meet both of these commitments. Additionally, loan repayments from participating governmental units are pledged to the repayment of the bonds.

STRENGTHS

- Board of Investment's irrevocable pledge to lend funds, if needed, to the reserve account and/or purchase tender bonds

- History of sizable resources available to the Board to cover payments on outstanding bonds

- Conservative investment of available resources and liquidity

- Board of Investments' moderate debt exposure

- Underlying programs are well managed, with no loans ever requested of the Board of Investments

-- No history of bonds being tendered

CHALLENGES

- Available balances can be negatively affected by economic slowing, state fiscal stress, and investment policy decisions

- Potential for additional debt issuance backed by the Board of Investments

Outlook

The outlook for the Board's Municipal Finance Consolidation Act bonds is stable, based on the Board's conservative policies and sound management of the funds under its responsibility, including the Treasurer's Fund substantial liquid balances deposited in the short-term investment pool.

WHAT COULD MAKE THE RATING GO UP

- Stricter limitations on potential board debt exposure

WHAT COULD MAKE THE RATING GO DOWN

- Major erosion of funds available to the board to lend to the authority

- Significant increase in board's debt exposure

- Shift away from the board's conservative management of available funds

Exhibit E

The principal methodology used in this rating was based on evaluating factors we believe are relevant to the credit profile of the issuer, such as i) the business risk and competitive position of the issuer versus others within its industry or sector, ii) the capital structure and financial risk of the issuer, iii) the projected performance of the issuer over the near to intermediate term, iv) the issuer's history of achieving consistent operating performance and meeting budget or financial plan goals, v) the debt service coverage provided by such revenue stream, vii) the legal structure that documents the revenue stream and the source of payment, and viii) the issuer's management and governance structure related to the payment. These attributes were compared against other issuers both within and outside of the Montana Board of Investments core peer group. The Montana Board of Investment ratings are believed to be comparable to ratings assigned to other issuers of similar credit risk.

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Return to Agenda

Montana Loan Program

MEMORANDUM

Montana Board of Investments
Department of Commerce
2401 Colonial Drive, 3rd Floor
Helena, MT 59601 (406) 444-0001

To: Board of Directors

From: Herb Kulow, CMB

Date: April 2, 2013

Subject: In-State Loan Program

The following slide presentation will be discussed during the April 2, 2013 Board meeting. The narrative that follows the slide presentation is much more detailed and is for information purposes and will not be discussed in detail. However, if any Board members have any questions concerning the narrative, feel free to ask those questions during the presentation.

MEMORANDUM

Montana Board of Investments
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2401 Colonial Drive, 3rd Floor
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To: Board of Directors

From: Herb Kulow, CMB

Date: April 2, 2013

Subject: In-State Loan Program

The following is a brief summary of the evolution of the In-State Loan Program.

IN-STATE LOAN PROGRAM HISTORY

In 1983, the Legislature implemented Initiative 95, which was called the Build Montana program. The Legislature created the Economic Development Board (MEDB), which was governed by a seven member board appointed by the Governor. It also created the In-State Investment trust created within the Coal Tax Trust allocating 25% of the coal tax revenue to the In-State Investment trust. MEDB was to make in-state investments from the new trust. Since only 25% of the revenue flowed into the new In-State Investment trust and no corpus was allocated from the Coal Tax Trust to the investment trust, there was limited money to invest in Montana businesses.

The 1984 Legislature expanded the original Board of Investments (BOI), established by the 1971 Legislature, to include two Pension Board representatives and increased the size of the Board from five to seven members.

In 1985, the Legislature added Section 3 to 17-6-201, MCA which reads, in part *"The Board may not make a direct loan to an individual borrower. The purchase of a loan or a portion of a loan originated by a financial institution is not considered a direct loan."* Title 17-6-312, MCA states in part, *"state participation in any loan to a business enterprise, except for a loan guaranteed by a federal agency, must be limited to 80% of the outstanding loan. The state shall participate in the security for a loan in the same proportion as the loan participation amount."*

The law cited above prevents the Board from becoming a direct lender; ensures that there will always be financial institution participation in the In-State Loan Program (Program) loans; prevents political pressure to make loans; and prevents the Board from taking a subordinate position in a participation loan. Because financial institutions share loan risk and loan collateral, they perform due diligence prior to submitting the loan application to BOI. Due diligence performed by BOI staff is in addition to that performed by the applicant. Requiring BOI to purchase loans solely from financial institutions makes the ultimate success of the Program totally dependent upon the willingness of financial institutions to utilize the Program. (In 1995, the Infrastructure Loan Program allowed MBOI to become a direct lender for the Infrastructure Loan Program only.)

The 1987 Legislature abolished both the existing MEDB and the BOI and created a new Montana Board of Investments (MBOI) with a nine member board. This new MBOI is representative of what the current Board looks like. The Legislature transferred all of the MEDB staff and duties to the new MBOI as well as the existing staff and duties of the abolished BOI.

In 1991, the Legislature liquidated the existing In-State Investment Fund, originally established by the 1983 Legislature, by transferring the Fund into the Coal Tax Trust, rather than it being a sub fund within the Coal Tax Trust. The Legislature encouraged MBOI to invest 25% of the Coal Tax Trust in Montana businesses.

Additionally in 1991, the Legislature enacted a program that is arguably the greatest incentive for Montana businesses to create new jobs, by creating **17-6-318, MCA, the job creation interest rate reduction for business loan participations**. The statute has been improved by the legislature four times since 1991, with the last change coming during the 2005 legislature. The statute does not apply to the Value-added loan program, the Link deposit loan program or the Intermediary Relending program. It allows the borrower to apply, through the lender, for an interest rate reduction equal to 5 basis points for every net new job created as a result of the loan in which MBOI participates, up to a maximum of 250 basis points. The interest rate reduction only applies to the participated portion of the loan held by MBOI. The net new jobs must pay at least the Montana minimum wage, which is currently $16,224, and at least one full new job must be created. A new job must pay at least $34,932, excluding benefits, which is considered the state's private annual wage. The state's private annual wage is determined by the Montana Department of Labor and Industry and changes every July 1.

The 1991 Legislature also enacted **17-6-319, MCA, Incentive to financial institutions for small business loan participation**. The law allows MBOI to reduce the posted interest rate by 50 basis points for any participated loan, which in total, is less than 0.05% of the permanent coal tax trust fund. That amount is currently $423,000 and it changes every July 1.

The 1995 Legislature created the Infrastructure Loan Program (17-6-316, MCA) and allocates $50 million of Coal Tax Trust money for the program. The program allows the MBOI to become a direct lender to local government entities for infrastructure as defined in 7-15-4288(4), MCA. The municipal unit would own the infrastructure and lease it to the basic sector business using the infrastructure. The amount of the loan is determined by the number of jobs created by the basic sector business tenant. Depending on how the basic sector business using the infrastructure files its income taxes, it may be able to deduct the payment made to the municipal unit (lease payment) from its Montana income tax liability. As of 12-31-12, the In-State Loan program had $22,014,291 of infrastructure loans outstanding. All of these loans are performing as agreed.

In 1997 the Legislature abolished the Montana Science and Technology Board (MSTB), which was established by the 1985 Legislature to invest in high-risk investments in Montana. The Department of Commerce becomes the successor in interest and has the responsibility to manage the loans and investments made by the MSTB. However, the 1999 Legislature transferred those investments to MBOI. As of 12-31-12, MBOI manages $10,519,623 of those investments. There are currently six investments within this portfolio; one investment is in a Montana venture fund, three investments are in research and development companies, one investment is with a state university doing research and development and one investment in a software company. All but the software company are performing as agreed.

The 2000 Legislature created another In-State Loan program called the Value-added loan program. The interest rates and term are legislated. The program was created to spur the creation or saving of Montana jobs. It is a participation loan program in which MBOI can participate up to 75% of the lender's loan.

The legislature allocated $50 million of Coal Tax Trust money for this program. As of 12-31-12 the Value-added loan program had an outstanding balance of $2,010,640. All of the loans have been performing as agreed.

The 2003 Legislature added two additional loan programs; the Intermediary Relending Program (IRP) and the Seasoned Loan Program. The IRP program was allocated $5 million from the Coal Tax Trust, which is a revolving loan fund. The interest rate was fixed at 2.00% and the term was 30 years. The local economic development organizations have three years to loan the money to local businesses. After the first three years, the loan is amortized over the remaining 27 years with quarterly principal and interest payments to MBOI. The loan proceeds are to be used as matching funds for the U.S Department of Agriculture rural development loan program or other federal revolving loan programs. As of 12-31-12 there were 14 local economic development organizations utilizing the program with total outstanding loan balances of $3,038,732. All of the IRP loans are performing as agreed.

The seasoned loan program was originated to allow the MBOI to purchase seasoned performing loans from local economic development organizations, which would provide additional loan funds from the organizations. To date, this program has only been used once and it was used to accommodate the expansion of a basic sector business that also used the infrastructure loan program. As of 12-31-12 the outstanding seasoned loan balance was $542,722. This loan is performing as agreed.

In 2007, the Legislature increased the allocation to the infrastructure loan program from $50 million to $80 million and the Value-added loan program from $50 million to $70 million. The legislature also more accurately defined the limitations of the 25% usage of Coal Tax Trust money for the In-State Loan program (17-6-305, MCA). Prior to this legislation, it appeared to MBOI the 25% was a "cap" on how much Coal Tax Trust money was available to MBOI to participate in lender loans. It also clarifies what should and should not be included in the calculation of the 25%. Those loan programs that have separate allocations; Infrastructure, Value-Added and IRP loans balances were excluded from the calculation, while the science and technology investments were included. On 3-31-07, just before the end of the legislative session, the percentage of the In-State Loan program to the Coal Tax Trust reached 24.60%. The outstanding loan portfolio was over $203 million with the Coal Tax Trust totaling approximately $800 million, leaving MBOI with only approximately $3.2 million of lendable funds. On the second to the last day of the legislative session, Section 17-6-305(1), MCA was amended to read, in part, *"This subsection does not prohibit the board from investing more than 25% of the permanent coal tax trust fund in the Montana economy if it is prudent to do so and the investments will benefit the Montana economy."* This change allows MBOI greater flexibility in its ability to service the economic growth of Montana. As of 12-31-12, the percentage of loans to the Coal Tax Trust was 12.43%

Finally, the 2011 Legislature added to 17-6-308 MCA Subsection 5, allowing $15 million of Coal Tax Trust money to be allocated for residential loans to qualified Montana veterans. 17-6-308(5) MCA states, *"(5) The board shall allow the board of housing to administer $15 million of the permanent coal tax trust fund for the purposes of the Montana veterans' home loan mortgage program provided for in Title 90, chapter 6, part 6."* As of 12-31-12, MBOI had funded 38 veteran loans totaling $6,705,729 and also had 19 reservations totaling $3,474,301. Both the funded loans and the reservations account for nearly 66.66% of the total allocation of $15 million. The original sponsor of the bill has proposed an additional allocation of $15 million of Coal Tax Trust money to the 2013 Legislature. As of the date of this writing, the bill is still flowing through the legislative process.

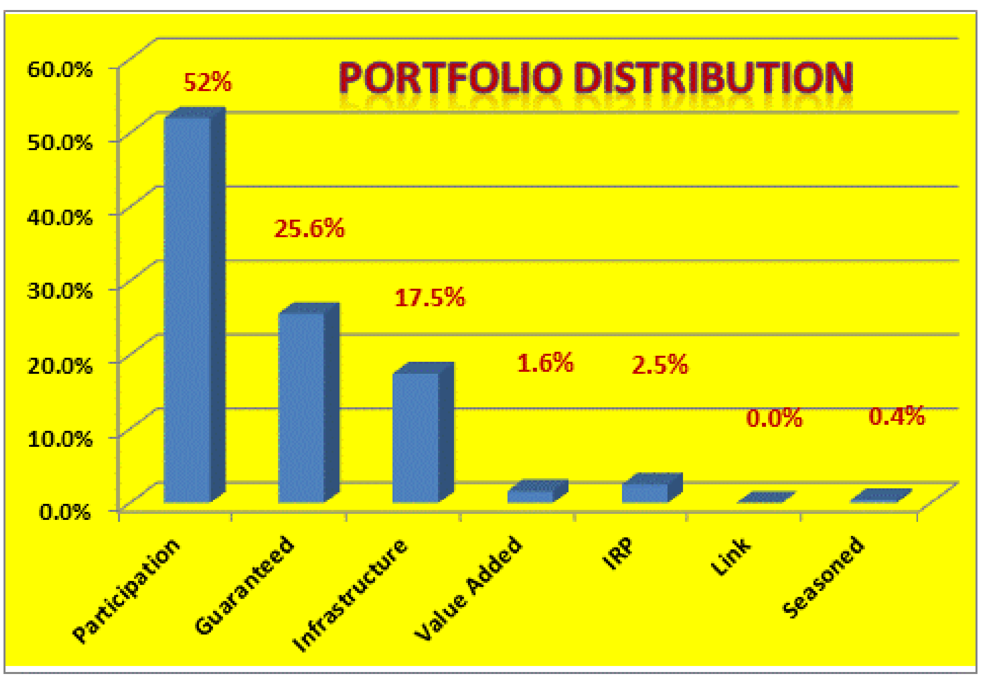
Lenders have always had the opportunity to accept deposits from the State Treasury, paying the current rate of interest and securing those deposits with government securities for amounts above the FDIC insurance coverage. In times of low lender liquidity and high loan demand and/or at times of volatile upward moving interest rates on deposits, lenders would offer to accept state money (in this case Coal Tax Trust money) at the interest rate posted on the MBOI interest rate sheet for a fixed period of time. They would then link that deposit to a specific loan, matching the term of the loan with the term of the State's deposited funds. This way the lender can fix an interest rate for a borrower for up to 25 years knowing it has matched its asset, the loan, with a corresponding State deposit. Interest is paid quarterly to MBOI as well as the amount of principal paid on the loan. This program only has one loan and it is scheduled to pay off in May 2013. The posted Link Deposit interest rates are not reflective of normal municipal deposit interest rates, due to the current economic conditions and lender's excess liquidity.

The Program also invests in Montana residential mortgages, but funds those loans with retirement monies. Retirement funds currently have an actuarial return requirement of 7.75%, while current residential mortgage interest rates are half the actuarial interest rate. As a result, MBOI is not investing in Montana residential mortgages. However, when residential interest rates were near or over the actuarial rate of 7.75%, MBOI had substantial investments in Montana residential mortgages. The program peaked in 2002 with total outstanding Montana residential mortgages of $324 million. As of 12-31-12 residential mortgages reflected an outstanding balance of $17,617,242. Since 2000, there has been no principal loss on any residential loan in the portfolio.

The In-State Loan program staff manages the following loan categories:

<u>Current In-State Loan Programs</u>

Participation - Non Guarantee	Intermediary Relending progr
Participation - Guaranteed	Seasoned Loan Program
Infrastructure	Link Deposits
Value-added	Veterans Home Mortgage Lo
Science and Technology	Residential Loans



As can be seen in the adjoining chart, Participated loans comprise 52% ($64,327,999) of the portfolio followed by Federally Guaranteed loans with 25.6% ($31,681,756) and Infrastructure loans at 17.5% ($22,014,291). There is only one Link Deposit loan in the amount of $14,311, which matures in May 2013, at which time it will be paid.

As of 12-31-12, the In-State Loan program staff manages the investments that appear below.

In-State Loan Portfolio as of 12-31-12

Loan Type		Balance	Percentage	Legislative Allocation
Participations		64,327,999	52.04%	
Guaranteed loans				
FSA	928,925			
RBS	26,520,353			
SBA	4,232,478			
Total Guaranteed Loans		31,681,756	25.63%	
Infrastructure		22,014,291	17.81%	80,000,000
IRP		3,038,732	2.46%	5,000,000
Value Added		2,010,641	1.63%	70,000,000
Seasoned		522,742	0.42%	
Link Deposit		14,311	0.01%	
Grand Total		123,610,472	100.00%	

Veteran's Home Loan Program as of 12-31-12

	Balance	
Outstanding Balance	6,705,729	15,000,000
Reservations	3,474,301	

Montana Residential Mortgages as of 12-31-12

	Balance
Residential Portfolio	17,617,242

Science and Technology 12-31-12

		Balance
		10,519,623
Montana University System	8,380,992	
Glacier Venture Fund	1,000,000	
Emerald Bio Agriculture	725,356	
McLaughlin Research Institute	251,671	
Deaconess Research Institute	161,603	
Gateway Software	1	

HISTORICAL AND CURRENT CONDITION OF THE IN-STATE LOAN PROGRAM

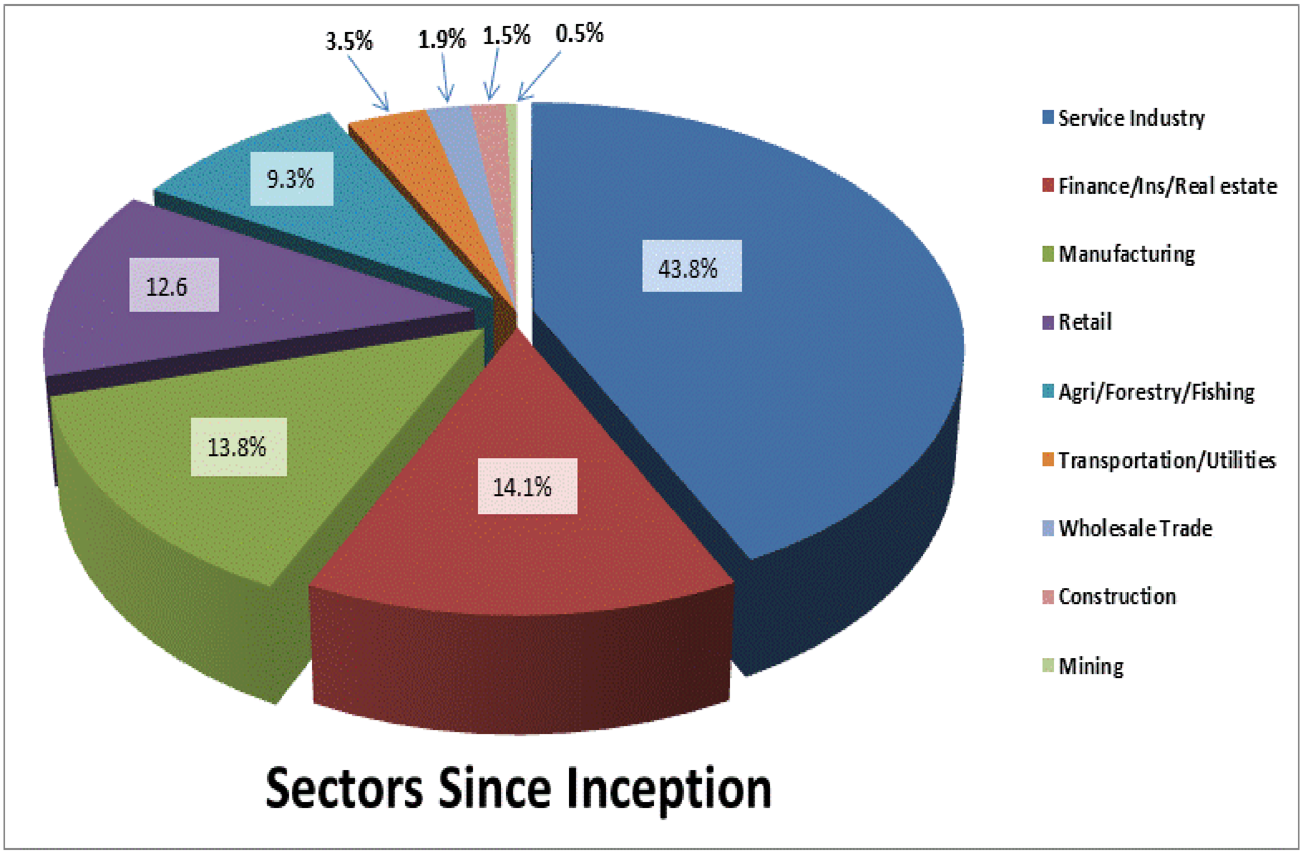
Since the inception of the Program, MBOI has funded $661,563,972 through 12-31-12. The chart below lists the top 10 counties participating in the Program from inception and the portfolio as of 12-31-12.

Just missing the "since inception" top 10 was Madison County at $13,713,553 and Beaverhead County at $10,874,710. There were lenders in 44 counties that have participated in the commercial loan program since inception. In contrast, lenders in only 20 counties are currently participating in the In-State Loan Program as of 12-31-12.

County	Since Inception Funded Balance	Percentage	12/31/2012 Outstanding Balance	Percentage
MISSOULA	127,556,406	19.48%	30,740,412	24.87%
YELLOWSTONE	101,182,110	15.45%	28,867,394	23.35%
GALLATIN	99,385,036	15.18%	17,631,955	14.26%
CASCADE	60,767,015	9.28%	13,451,301	10.88%
LEWIS AND CLARK	54,540,792	8.33%	12,181,140	9.85%
FLATHEAD	47,159,507	7.20%	7,756,999	6.28%
PARK	22,709,631	3.47%	724,332	0.59%
LAKE	19,610,616	3.00%	382,921	0.31%
SILVER BOW	18,584,476	2.84%	7,251,413	5.87%
RAVALLI	15,016,227	2.29%	2,140,884	1.73%
Total	566,511,816	86.52%	121,128,751	97.99%

To present another look at the distribution of the 12-31-12 commercial loan portfolio, page 6-A has Montana divided into six areas. Each area shows the amount of federally guaranteed loans and non-guaranteed loans. Within the Southeastern section of Montana, Yellowstone County accounts for all but $24,473 of the total and that loan is in Rosebud County. Likewise the Northeastern part of the state has very few loans with MBOI, although, due to the development in the Bakken oil area, staff has received considerably more inquiries from lenders in that area.

The following chart and table show the primary business sectors that are included in the In-State Loan portfolio. MBOI categorizes the loans in nine different business sectors; service, finance/insurance/real estate, manufacturing, retail trade, agriculture/forestry/fishing, transportation/utilities/commerce, wholesale, construction and mining. The service industry has been and remains the largest sector. The service industry includes, but is not limited, to hotel/motel, restaurants, professional offices, health care facilities and auto repair to name a few. Since inception, MBOI has participated in over 390 individual loans in the service industry sector.



	Since Inception		12/31/2012	
	Funded Balance	Percentage	Outstanding Balance	Percentage
SERVICE INDUSTRY	280,272,107	42.81%	67,635,145	54.72%
FINANCE/INSURANCE/REAL ESTATE	92,042,583	14.06%	15,366,997	12.43%
MANUFACTURING	90,540,415	13.83%	4,260,854	3.45%
RETAIL TRADE	82,360,147	12.58%	22,192,293	17.95%
AGRICULTURE/FORESTRY/FISHING	61,022,673	9.32%	1,258,018	1.02%
TRANSPORTATION/UTILITIES/COMM.	22,670,985	3.46%	11,956,190	9.67%
WHOLESALE TRADE	12,597,833	1.92%	662,189	0.54%
CONSTRUCTION	10,106,827	1.54%	123,709	0.10%
MINING	3,139,768	0.48%	155,078	0.13%
Grand Totals	654,753,337		123,610,473	

One noticeable change is the percentage of manufacturing loans since inception and as of 12-31-12. The difference, in large part, can be attributed to the payoff of a substantial manufacturing loan of approximately $9,200,000 in December 2010. If this loan was not paid off, after estimating approximately $500,000 of pay down by 12-31-12, the 12-31-12 manufacturing percentage would be approximately 10% compared to 3.45%. When comparing percentages, agricultural loans are also down substantially. This is due to new agricultural loans not being added as fast as the existing agricultural loans are being paid down.

Historically, within the service industry sector, hotels/motels comprised 30.33% of the total of that sector and as of 12-31-12, hotel/motels comprised 12.12% of the portfolio. There are currently six hotel/motel loans in the portfolio, two of which are federally guaranteed. When considering only "at risk", which would be non-guaranteed hotel/motel loans, the percentage falls to 8.54% of the service sector. In April 1993, the Board felt it had too much "at risk" exposure in the hotel/motel industry and limited MBOI's participation in the hotel/motel loans to not more than a 50%. As of 6-30-92, the portfolio had "at risk" hotel/motel loans representing 12.46% of the portfolio. Although not policy, staff still operates under the 1993 Board directive.

MBOI posts its current commercial interest rates on its website. The interest rates change every Thursday. Staff establishes the commercial loan interest rates by using the Federal Home Loan Bank – Seattle, long-term, fixed-rate amortizing, interest rates. This is the interest rate amount financial institutions would pay if they were to borrower money from the Federal Home Loan Bank – Seattle. Staff then "marks up" those interest rates from between 225 basis points for the five-year interest rate, to 275 basis points for the 25-year interest rate. Interest rates for commercial government guaranteed loans are discounted 40 basis points, for every term. The reason for the discount is primarily because there is less risk associated with guaranteed loans than non-guaranteed loans. A copy of the current interest rates, for the period from March 21, 2013 to March 27, 2013, is found on the following page 8-A. Previous to the current Federal Home Loan Bank – Seattle index pricing, staff used the 10-year government as the pricing index, but feel the current index is more representative of the cost of borrowing for lenders.

Lenders are the customers of MBOI and not the borrowers. Lenders must submit a reservation form, reserving an interest rate and dollar amount for a one-year period prior to or with their commercial loan application. There is a one-quarter of one-percent (0.25%) reservation fee, which is refunded if the loan closes and is funded within one year from the date of the reservation. The lender may extend this reservation two additional years with the payment of an additional one-quarter of one-percent for each of the additional two years.

One of the many advantages of the In-State Loan Program is the reserved interest rate is fixed for the term of the loan. In addition, if interest rates go down during the reservation period, the lender/borrower can reapply for the new lower interest rate with the payment of another reservation fee. MBOI will refund the last reservation fee paid upon funding the loan. The program allows the lender/borrower to "walk the interest rates down" with the payment of additional reservation fees, and insulates the lender/borrower from the upward movement of interest rates.

In addition to the long-term fixed interest rates, the lender/borrower can apply for an interest rate reduction resulting from the creation of new jobs by the borrower as a result of the MBOI participating loan, which lowers the interest rate on the participated portion of the loan held by MBOI. The maximum interest rate reduction applicable to the participated portion of the loan is 2.50%. This equates to 5 basis points for every new job created up to a maximum of 50 new jobs. Since inception, 50.43% of individual loan units, representing $415,917,969, (63.52% of the total dollars of the portfolio) were impacted by the creation of new jobs. As of 12-31-12, 40.77% of individual loan units in the portfolio, representing $74,924,168, (60.61% of the total dollars of the portfolio) were impacted by the creation of new jobs.

The impact of the reduction of interest rates, due to the creation of jobs, plus those loan programs which the legislature establishes the interest rates,(Value-added, and the Intermediary Relending Program), have reduced the overall potential yield of the loan portfolio. Staff cannot determine the exact financial impact on potential earnings flowing to the general fund, to which all earnings of the Program flow, however the table below shows the significant reduction in investment income resulting from a 2.50%

interest rate reduction on a $1.0 million dollar loan over a 10-year term with annual payments. In this example, the original interest rate is 5.50%, represented by the amortization on the left and the amortization on the right reflects a 3.00% interest rate after the 2.50% interest rate reduction. The reduced earnings, in this example, are $80,216.95 over 10 years. The legislature instructs the Board to consider the return to the State by considering the long-term benefit to the Montana economy provided by businesses to which loans are made, not just the yield on the portfolio. This language expresses legislative intent that the MBOI view economic development as an integral component of the program.

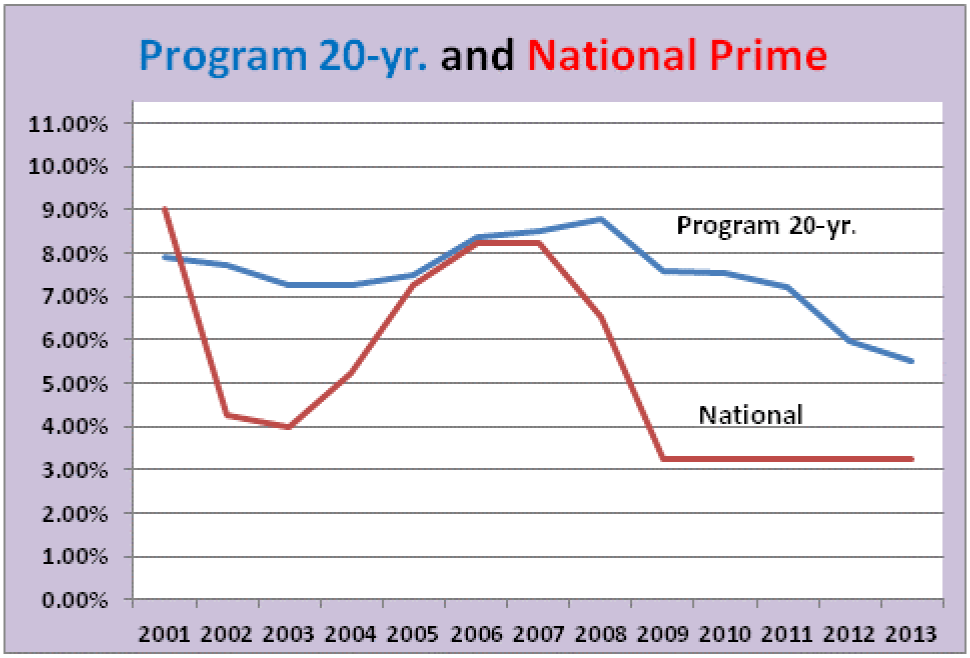
Date	Payment	Interest	Principal	Balance	Date	Payment	Interest	Principal	Balance
05/01/13	106,586.29	27,500.00	79,086.29	920,913.71	05/01/13	99,293.84	15,000.00	84,293.84	915,706.16
05/01/14	106,586.29	25,325.13	81,261.17	839,652.54	05/01/14	99,293.84	13,735.59	85,558.25	830,147.91
05/01/15	106,586.29	23,090.44	83,495.85	756,156.69	05/01/15	99,293.84	12,452.22	86,841.63	743,306.28
05/01/16	106,586.29	20,794.31	85,791.98	670,364.71	05/01/16	99,293.84	11,149.59	88,144.25	655,162.03
05/01/17	106,586.29	18,435.03	88,151.26	582,213.44	05/01/17	99,293.84	9,827.43	89,466.41	565,695.62
05/01/18	106,586.29	16,010.87	90,575.42	491,638.02	05/01/18	99,293.84	8,485.43	90,808.41	474,887.21
05/01/19	106,586.29	13,520.05	93,066.25	398,571.77	05/01/19	99,293.84	7,123.31	92,170.54	382,716.67
05/01/20	106,586.29	10,960.72	95,625.57	302,946.20	05/01/20	99,293.84	5,740.75	93,553.09	289,163.58
05/01/21	106,586.29	8,331.02	98,255.27	204,690.93	05/01/21	99,293.84	4,337.45	94,956.39	194,207.19
05/01/22	106,586.29	5,629.00	100,957.29	103,733.63	05/01/22	99,293.84	2,913.11	96,380.74	97,826.45
05/01/23	106,586.29	2,852.67	103,733.62	0.01	05/01/23	99,293.84	1,467.40	97,826.45	0.01
	Interest paid	172,449.24				Interest paid	92,232.29		

In most cases, over the past 15 years, the yield generated by the Program has exceeded the yield of the 10-year governments, even after taking into consideration the interest rate reduction due to the creation of jobs. The average maturity of the 12-31-12 portfolio is approximately 13 years and for that reason the 10-year government interest rate was chosen as a comparison.

The portfolio yield has shown a general decline since 1997. As national prime continued to decline, so did the MBOI yield. The interest rates offered by MBOI at this time are the lowest since 2000. The MBOI 20-year monthly-payment participation can be reserved at 5.47%, as of 3-21-13. On 12-6-12, the 20-year interest rate hit a low of 5.11%. In 2008, the MBOI posted 20-year interest rate hit a high of 8.77%. That is only a differential of 3.66%. The national prime interest rate, during that same period of time, hit a high of 9.00% in January 2001 and a low of 3.25% in December 2008. That is a differential of 5.75%. MBOI's interest rates do not move as quickly or dramatically as the national prime interest rate or other similar indexes, primarily because MBOI interest rates are long term, whereas national prime is a very short-term interest rate. When borrowers look to lower their interest, most borrowers look at the short-term interest rates and give little consideration to the long term impact upon their business by converting from a long-term fixed interest rate to an interest rate offered by the lender tied to a short-term index, like national prime, Libor, a Treasury index or a Federal Home Loan Bank index.

Since the Program does not refinance existing debt, once the lender repurchases the loan, the lender is unable to resell it to MBOI when rates begin to escalate. The main reason the Program does not refinance existing debt is because the Coal Tax Trust money is to be used for economic development and by refinancing existing debt, the economic development associated with that debt has already occurred.

The chart below shows the relationship between national prime and the Program interest rates. The Program interest rates have remained relatively stable over the reported years until 2008 when national prime and the Program interest rate index began to fall. The Program interest rates fell less dramatically than did national prime. Likewise, as national prime increases, Program interest rates will increase more slowly, providing lenders an opportunity to lock in lower interest rates for the new loans they present to staff for consideration.



The purpose and use of the Coal Tax Trust is defined in the following sections:

> ***17-6-303. Purpose of the coal tax trust fund.*** *The people of Montana establish that the intent of the permanent coal tax trust fund, as created by Article IX, section 5, of the Montana constitution, is:*
> *(1) to compensate future generations for the loss of a valuable and depletable resource and to meet any economic, social, and environmental impacts caused by coal development not otherwise provided for by other coal tax sources; and*
> *(2) to develop a stable, strong, and diversified economy which meets the needs of Montana residents both now and in the future while maintaining and improving a clean and healthful environment as required by Article IX, section 1, of the Montana constitution.*

> ***17-6-304. Use of the coal tax trust fund for economic development.*** *Objectives for investment of the permanent coal tax trust fund are to diversify, strengthen, and stabilize the Montana economy and to increase Montana employment and business opportunities while maintaining and improving a clean and healthful environment.*

In making the decision to participate in a lender's loan, staff is driven by the "prudent expert principle" as defined in 17-6-201(1)(a), which states:

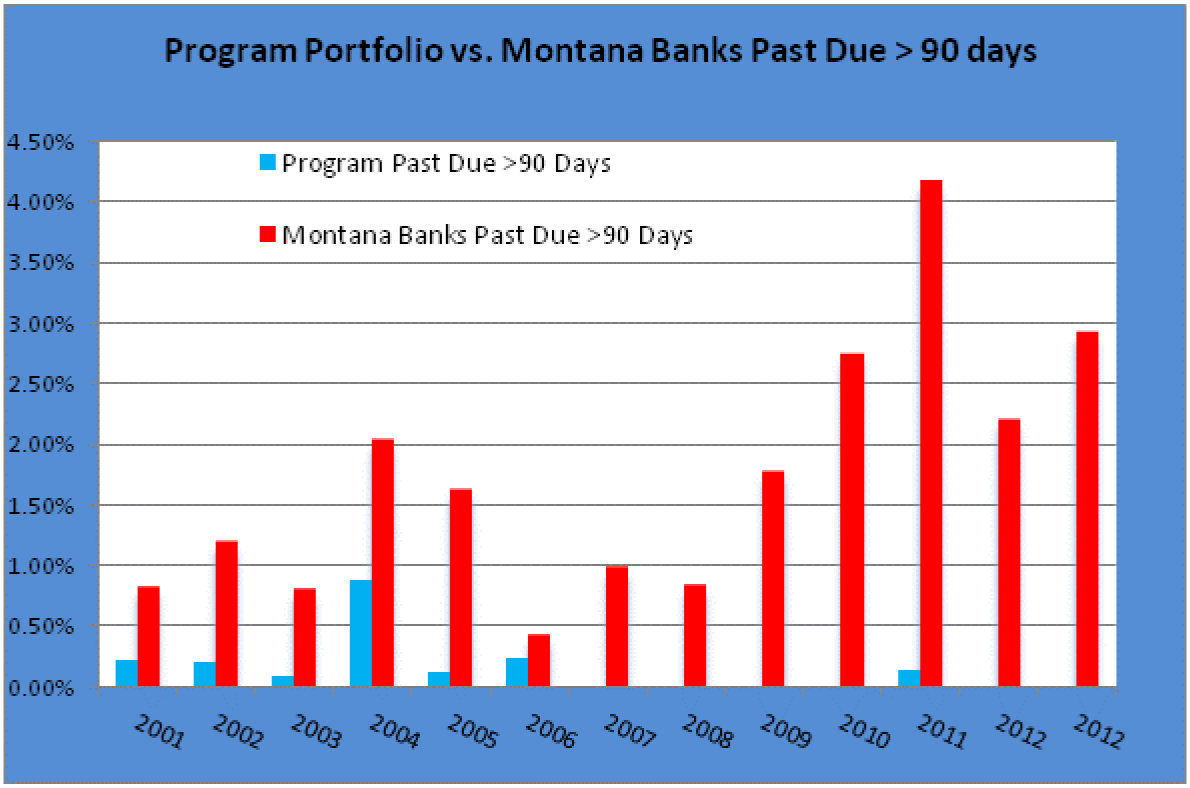
17-6-201. Unified investment program -- general provisions. *(1) The unified investment program directed by Article VIII, section 13, of the Montana constitution to be provided for public funds must be administered by the board of investments in accordance with the prudent expert principle, which requires an investment manager to:*
(a) discharge the duties with the care, skill, prudence, and diligence, under the circumstances then prevailing, that a prudent person acting in a like capacity with the same resources and familiar with like matters exercises in the conduct of an enterprise of a like character with like aims.

Staff does an in-depth analysis of all loans presented for consideration by lenders, other than government guaranteed loans and link deposit loans. This analysis considers character, collateral, capacity, competition and economic conditions. Not all loans are recommended for approval by staff. All loans up to a MBOI participated amount of $1,000,000 are approved by an internal loan committee. Loans which have a MBOI participation amount of $1,000,000 up to $5,000,000 are reviewed by the Board Loan Committee, which makes a decision and reports that decision to the full Board. All loans which have a MBOI participated amount of $5,000,000 or more are reviewed by the Board Loan Committee, which makes a decision and presents that decision to the full Board for their approval. Staff has no lending authority.

Since fiscal year end 2001, the delinquency percentage of the Program portfolio has fared very well when compared to the delinquency of commercial loans held by Montana lenders. The percentages are even more impressive when considering, as of fiscal year ending 6-30-07, the outstanding portfolio balance was over $195 million and the number of loans over 90 days past due was zero. The table below compares the commercial loan past due percentages for the In-State Loan portfolio, the State of Montana lenders and all banks in the United States as presented by the Federal Reserve System. Montana lenders have fared better than the rest of the banks in the nation and the MBOI portfolio was even better than the Montana lenders.

Date	MBOI past due loans over 90 days	Montana Lender's past due loans over 90 days	Federal Reserve Bank all banks past due loans over 90 days
6/30/2001	0.21%	0.82%	1.67%
6/30/2002	0.20%	1.20%	1.70%
6/30/2003	0.08%	0.80%	1.56%
6/30/2004	0.87%	2.04%	1.21%
6/30/2005	0.12%	1.63%	1.01%
6/30/2006	0.23%	0.42%	0.99%
6/30/2007	0.00%	0.98%	1.58%
6/30/2008	0.00%	0.84%	4.04%
6/30/2009	0.00%	1.78%	7.68%
6/30/2010	0.00%	2.75%	8.61%
6/30/2011	0.14%	4.18%	6.98%
6/30/2012	0.00%	2.21%	4.91%
12/31/2012	0.00%	2.93%	4.08%

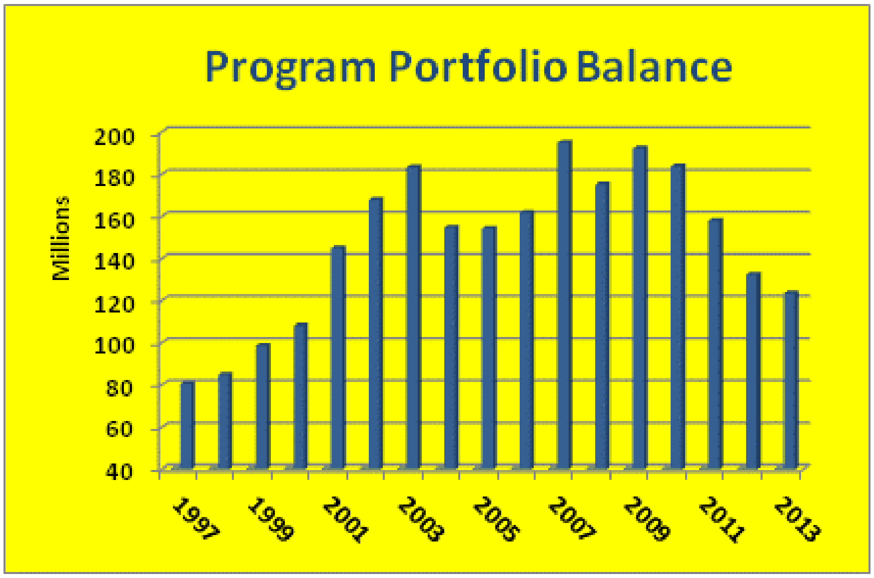
The following graph shows the delinquency percentage for the Program portfolio compared to the delinquency percentage for all Montana lenders assembled from the FDIC June 30 call reports. The last percentage is as of 12-31-12 rather than June 30. It represents a graphic presentation of the previous table, but only considering Montana loans and lenders. No visible blue bar on the graph indicates there were no past due loans over 90 days in the Program portfolio.



There are a number of reasons for the impressively low past due percentages of the Program portfolio. The lenders do not send staff loans that are not of the highest quality. In almost all cases, the lenders will have discussed the proposed loan with staff prior to submission of the application. Most areas of concern will have already been addressed and either corrected or the application is not submitted. Secondly, staff's expertise in conducting credit analysis. The portfolio manager joined MBOI in 2000 and has over 45 years banking/credit experience, which includes being president of three different banks. The senior credit analyst joined MBOI in 2006 and has over 19 years of credit experience, most recently with Wells Fargo, California as a problem credit work-out specialist. Additionally, Montana lenders know their customers and their customer's businesses in much more detail than other states. The Montana lenders usually correct the situation before it gets out of control and foreclosure and/or liquidation occurs. Finally, staff immediately contacts the lender if a loan appears to be habitually delinquent or staff feels there is an imminent danger with the credit. The lender is the servicer, and as such retains all of the financial information concerning the company. Staff does not receive monthly, quarterly or annual financial information from the company or lender.

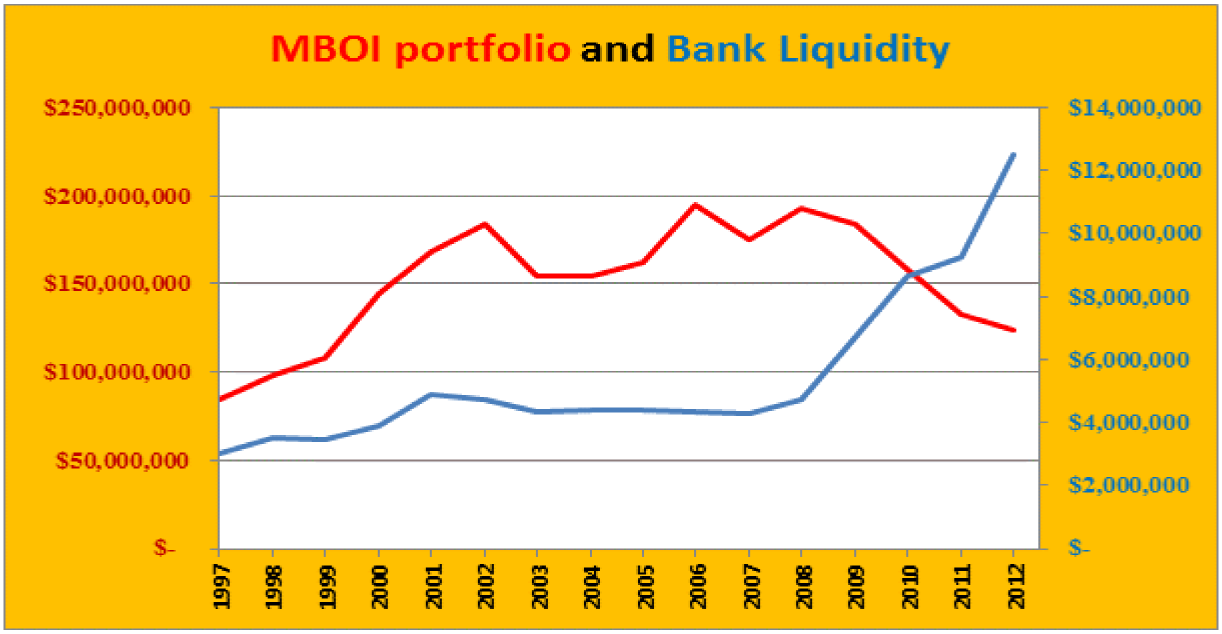
Since 2002, only a portion of one loan has been recorded as a loss in the amount of $206,599. That loan was originally participated in 1997.

In 1998 and 1999, the national prime rate averaged 8.125%. The Program's 20-year interest rate averaged 8.12%, which is very unusual considering the premium that should be charged for the interest rate and credit risk taken over the 20-year term. In February 1999, Mr. South, the Executive Director of MBOI, presented the third and final part of a three part "Strategies and Options" for the Program. It primarily included a review of the current Administrative Rules (Rules) and making a recommendation of either adoption of the Rules as is, revisions or rejection. It was determined that the existing Program Rules and its operational parameters made it very difficult for financial institutions to intimately understand the Program parameters. On June 9, 1999, there was a public hearing to consider the proposed amendment to repeal the Rules or a portion of them, or full adoption of Rules pertaining to the Program. There was no public participation at the hearing nor was there any written testimony. Ultimately 90% of the Rules were repealed in favor of a Board commercial loan policy, which we still have today, although it has been amended from time to time. In addition to establishing a commercial loan policy, staff was allowed to accept refinancing of existing debt as long as at least 15% of the loan amount contained new money for expansion or remodeling. Lenders could also consider some previously excluded soft construction costs as hard costs.



While lender liquidity remained relatively flat from 1998 to 2003, increasing only approximately $2,300,000, the Program outstanding loan balances increased from $84,853,000 on 6-30-98 to $183,440,551 on 6-30-03, an increase of $98,600,000.

The portfolio balances also reflect, in part, the amount of liquidity the Montana lenders have and their loan demand. Since the melt-down in 2008 and the tightening of credit standards by the regulators and lenders, loan demand has diminished and lender liquidity has increased. Today, with Montana lenders having excess liquidity, they have no particular desire to participate a portion of their loans to MBOI. This may or may not be good for the ultimate borrower, who in most cases will be signing a variable interest rate note. Whereas, if the loan was participated with MBOI, up to 80% of that participated loan could be a long-term fixed interest rate for up to 25 years for non-guaranteed loans and up to 30 years for a guaranteed loan. The graph below shows, as lender liquidity increased, beginning in 2007, the Program portfolio began to decrease in 2008, as lenders repurchased the participated portion of their loans.



Although MBOI and the lender/borrower have all signed a commitment letter, which commits the lender/borrower to keep the participation for the term of the loan, MBOI allows the lender to repurchase the participated portion if they can show a financial advantage will accrue to the borrower. With the current prime of 3.25%, it is easy for the lender to show a financial advantage when repurchasing and repricing a loan with an interest rate from 6.00% to 8.00%.

The graph also reflects that the Program is not in total control of its outstanding loan balance. Of course, staff could refuse to allow the lenders to repurchase the participated portion of the loan, however, if there is a reasonable financial advantage to the borrower, which should ultimately make that borrower stronger by reducing their interest expense, staff feels bound to grant the lender's request. The Program's main objective is not to increase outstanding portfolio balances and generate high yields, but to assist in the development of a strong and stable Montana economy; an economy which encourages the creation of jobs and the expansion of local businesses.

Staff also knows the liquidity lenders currently enjoy will diminish over time, at which point lenders will once again call on MBOI to participate in their commercial loans, resulting in increased Program loan participations.

RESIDENTIAL LOAN PROGRAMS

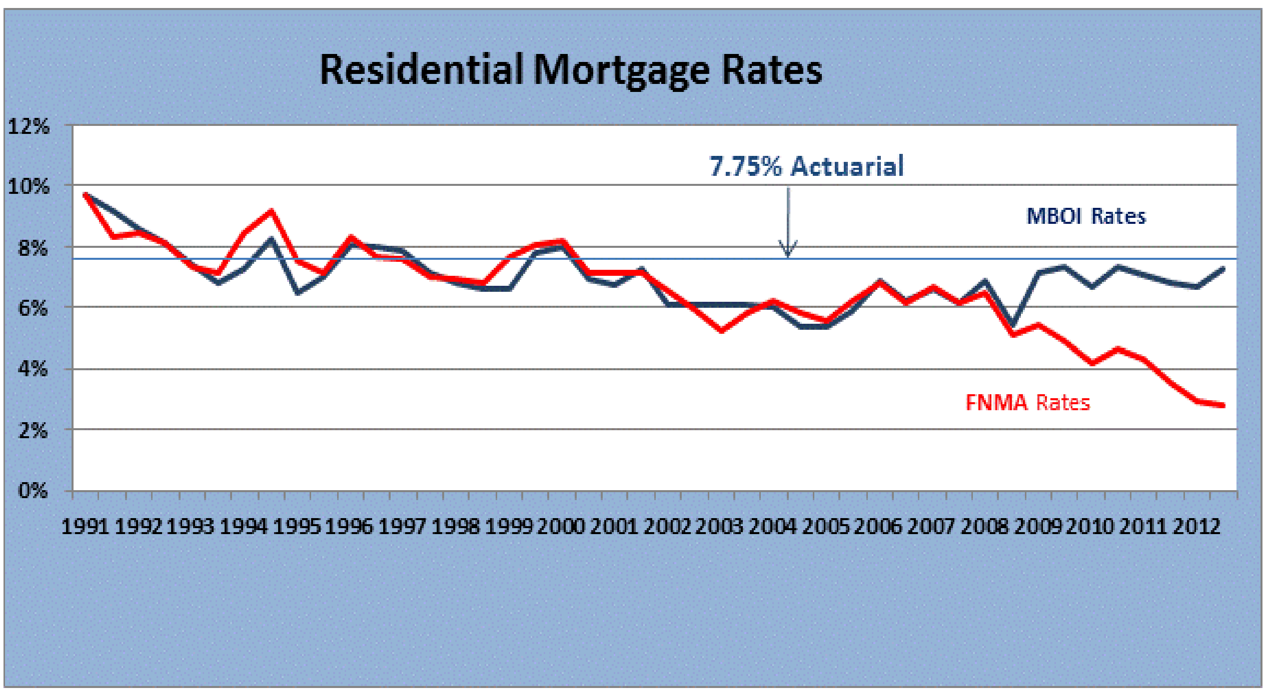
Staff manages two different residential mortgage programs: the Veterans Home Loan Mortgage Program (VHLMP) and the Montana Residential Loan Program (Residential Loan Program). The VHLMP is funded with Coal Tax Trust money and the Residential Loan Program is funded with pension money.

The VHLMP was established by the legislature in 2011 and was allocated $15million of Coal Tax Trust money. The program is administered by the Montana Board of Housing (BOH). As administrator, they process all applications, service and, if necessary collect, all approved loans. They also do all of the reporting to MBOI on a monthly basis. Staff reviews all appraisals and approves or denies the appraisals. Upon receipt of all required loan documents from the originator/lender, the BOH requests funding from MBOI. Veterans must be honorably discharged, have 100% of their guarantee award available, the home must be the Veteran's permanent residence and must have a minimum of $2,500 to apply to the purchase price of the home. MBOI compensates BOH for their services with a 75 basis point fee, which is deducted from the interest rate on the loan. The current yield to MBOI is approximately 1.60%.

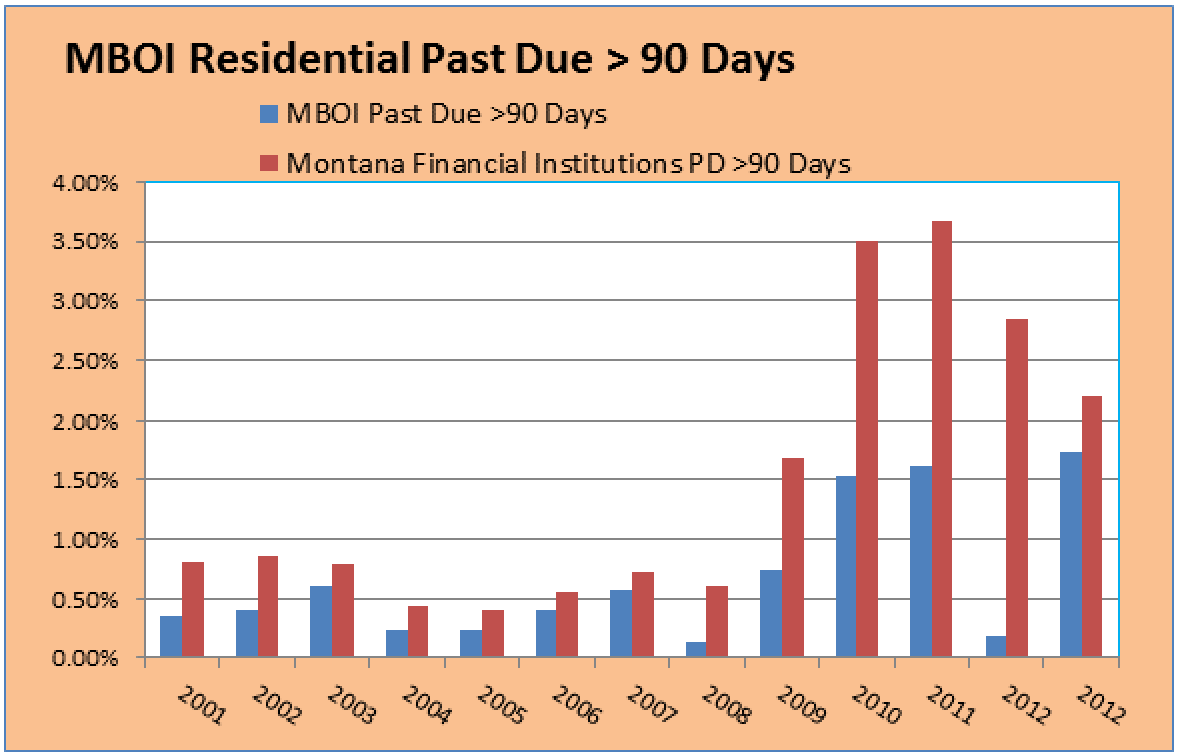
As of 12-31-12 there were 39 loans funded totaling $6,705,729. There were 19 reservations totaling $3,474,301. The first VHLMP was purchased by MBOI on 1-23-12. Since this is a new program, there is no historical data. There are also no past due loans.

The Residential Loan Program has been in existence since at least 1991 and has always used pension funds to invest in Montana residential mortgages. The main reason for investing pension funds is because of the long term nature of both the investment and the pensions. In addition, mortgage interest rates provided a reasonable rate of return for the pensions. During the 1990s, the MBOI residential interest rates averaged 7.64% while the market residential interest rates averaged 7.85%. MBOI intentionally discounted its interest rate to encourage Montana lenders to use MBOI rather than another secondary market investor. The average MBOI residential interest rate was close to the actuarial rate of 7.75%. The residential loan balances continued to grow from a low in 1994 of $99,775,000 to a high of $324,038,000 in 2002. In 2003, residential interest rates fell to less than 6.00% and the Board chose not to invest in any additional Montana residential mortgages. As a result, the residential portfolio dramatically decreased due to the lack of investments in new residential mortgages and the high volume of refinancing of existing portfolio mortgages. Although MBOI did not discontinue the program, it no longer offered a discount to use the MBOI program and ultimately, in 2007, MBOI priced the interest rates well above prevailing secondary market residential rates. That pricing continues to exist today. As of 12-31-12, the residential mortgage portfolio reflected an outstanding balance of $17,617,242.

The chart below reflects the MBOI residential interest rates compared to FNMA rates as of June 30 of each year. It also shows the pension actuarial rate at 7.75%.



The residential mortgage program offers conventional, FHA guaranteed and VA guaranteed financing. As a result, the performance of the portfolio has been very good. The underwriting process was/is strict and is not unconventional. MBOI did/does NOT do second mortgages, requires verification of income, requires a formal appraisal, provides a term amortization and no ballooning loans. For these reasons, plus high quality underwriting standards, the residential loan portfolio reflects very low past due percentages when compared to other Montana lenders. The chart below is the MBOI residential past due percentages since 2001. All of the dates are as of June 30 of the reporting year, except for 2012 which also reflects the December 31, 2012 past due percentage. There is one abnormality in the past due percentages, which can easily be explained, and that is the low past due percentage on 6-30-12. As of 6-30-12, there was only one loan past due over 90 days in the amount of $37,334, compared to 6-30-11 with 3 past due loans over 90 days totaling $175,743 and 5 loans past due over 90 days as of 12-31-12 totaling $305,135. The portfolio past due percentage will naturally get higher as the outstanding balance continues to decline. Since 2001, MBOI has not recorded a loss in the residential loan portfolio.



Mortgages are originated by Montana lenders and sold to MBOI. Through a Memorandum of Agreement dated January 2005, the BOH processes all lender applications, collections of past due loans and reporting of MBOI residential loans. The originating lender is still responsible for servicing the loan. Prior to January 2005, MBOI underwrote all residential mortgage applications with a staff of two. With declining residential interest rates and the Board's decision not to invest in Montana residential loans at the prevailing interest rates, it was appropriate to consider an alternative for processing residential mortgages. Since the BOH is in the residential mortgage business, MBOI chose to contract with the BOH to provide these services.

Current residential mortgage interest rates continue to be at historical lows. Since MBOI has not discontinued the residential mortgage program, it is just a matter of time when residential interest rates will creep back up to investable levels, but until then, MBOI will sit on the sidelines until that time arrives.

Finally, MBOI inherited the Montana Science and Technology (Science and Tech) loans through legislative action in 1999. Since that time Executive Director South managed that program. In 2012 the current Executive Director, Mr. Ewer, delegated that responsibility to Program staff. Staff did a review of the investments held in the Science and Tech portfolio and made a recommendation to write- down the existing balance from $12,050,331 to $10,554,064, a total write-down of $1,496,267. It was agreed by the Board that the write-down would more accurately reflect the value of the Science and Tech investment.

THE FUTURE OF THE PROGRAM

As indicated previously, the growth of the portfolio is dependent on the activity of the Montana lenders and their willingness to use the Program. As the lender's liquidity is decreased, their participation with MBOI should increase.

Staff has developed satellite programs consistent with the commercial loan policy to provide more financing alternatives for the lenders. In 2006, staff finalized a "small loan pool" to allow lenders to package loans under $500,000 into a pool and participate 80% of that pool to MBOI. All loans included in the pool had to have a loan-to-value of less than 75% and a debt coverage ratio of 1.35 or greater. The lenders could submit the "pool" under one loan application. This program funded one pool, which has since been paid in full.

Another satellite program, developed by staff in 2012, allows MBOI to participate in Low Income Housing Tax Credit loans. Previous to this time, staff did not participate in subsidizing housing projects. However, since tax credits provide substantial equity in the various projects, staff felt it should consider participating in these types of loans. To date we have participated in two such projects.

In the future, staff will continue to try to develop new satellite programs to assist the Montana economy and provide additional tools for its toolbox of programs and lenders.

Program staff will continue to assist other areas of the Department of Commerce (DOC) in the administration of new programs being implemented by them. When the legislature authorized money for the Wood Products Revolving Loan Fund, the DOC contacted Program staff for assistance in originating loan and collateral documents. They also asked staff to assist in analyzing credits and, at times, staff sat in on loan committee meetings.

Program staff was an important part in the development, analysis, implementation and review of the State Small Business Credit Initiative program in the fall of 2011. Staff developed the loan policy, application, review and analysis process and serves as a member of the executive and loan committee. Program staff did ALL of the credit analysis for every loan presented for consideration. As a result, Montana was the first state in the nation to request and receive all of its $13,000,000 Treasury allocation.

Staff intends to visit a majority of the lenders in the state in 2013, either through banker's association meetings or visits directly to the lenders. The In-State Loan Program has an excellent reputation of achievement. Staff intends to protect that reputation with prudent investments in the businesses in Montana to assist in the development of a stable, strong and diversified economy, which meets the needs of Montana residents both now and in the future, while maintaining and improving a clean and healthful environment.

In-State Loan Program

Presented by:

Herb Kulow, CMB

Senior Portfolio Manager

and

Nancy Rivera, Credit Analyst

In-State Loan Program

- **Topics for Todays Discussion:**
  - **Coal Tax Trust Loan Programs**
  - **Performance**
  - **Residential Mortgage Program – Pension Funds**
  - **Summary**

In-State Loan Program – Coal Tax Trust

- Participation – Non-Guaranteed
- Participation – Guaranteed
- Infrastructure
- Value-Added
- Intermediary Relending Program
- Seasoned Loans
- Link Deposit
- Veterans Home Loan Mortgage Program
- Science and Technology

In-State Loan Program – Coal Tax Trust

- **Participation Loans**
  - May loan up to 25% of Trust (Trust = $ 861.2 million)
  - Maximum loan size is 10% of Trust ($86.1 million)
  - Board participation up to 80% of loan or 100% of the guaranteed amount
  - Fixed-rate financing up to 25-years
  - Loans made in participation with lenders who service loans
  - Interest rates set off Federal Home Loan Bank - Seattle rates
  - Job creation credits may reduce interest rate up to 2.5%
  - Currently $123.6 million principal outstanding

In-State Loan Program – Coal Tax Trust

- **Infrastructure Loan Program**
  - Up to $80.0 million of the Trust is available
  - Maximum loan size = $16,666 times jobs created
  - Minimum loan size = $250,000
  - Loans to local government for infrastructure
  - No lenders involved – Board lends directly to local governments
  - Business for which infrastructure is provided must:
    - Create at least 15 full-time jobs
    - Be a "basic sector" business
  - Business pays local government a use fee to repay loan
  - Use fee is pledged to the Board
  - Use fee is credited against the Montana income taxes of the business
  - Job creation credits may reduce interest rate up to 2.5%
  - Currently $22.0 million principal outstanding

In-State Loan Program – Coal Tax Trust

- **Value-Added Loan Program**
  - Up to $70.0 million of the Trust is available
  - Maximum loan size = $8.6 million (1% of Trust)
  - Minimum loan size = $250,000
  - Maximum 15-year loan term
  - Jobs must be created by "value-added" businesses
  - Interest rate 1st 5 years is 2% if 15 jobs are created
  - Interest rate 1st 5 years is 4% if 10 jobs are created
  - Interest rate 2nd 5 years is 6%
  - Standard posted rate for the last 5 years
  - Board participates at 75% with lenders by law
  - Can not pay dividends or bonuses to owners while loan is outstanding
  - Currently $2.0 million principal outstanding

In-State Loan Program – Coal Tax Trust

- **<u>Intermediary Relending Loan Program</u>**
  - **Up to $5.0 million of the Trust available**
  - **Maximum loan size = $500,000**
  - **No lenders involved – Board lends directly to:**
    - **Local economic development organizations**
  - **Organizations must match loan with other government funds**
  - **Interest capped at 2% for 30-year term**
  - **Interest payments only for first 3 years**
  - **Principal and interest next 27 years**
  - **Currently $3.0 million principal outstanding**

In-State Loan Program – Coal Tax Trust

- **Seasoned Loans**
  - Board purchases portion (up to 80%) of seasoned/mature loan from economic development organization
- **Link Deposit**
  - Lender accepts coal tax money as deposit for specific term
  - Interest on deposit posted on MBOI rate sheet
  - Deposit matures annually, but guaranteed for a specific term
  - Secured by qualifying securities for amount over FDIC coverage
  - Links deposit to lender loan
  - Lender pays interest quarterly and reduces deposit amount by principal reduction of Linked loan.

In-State Loan Program – Coal Tax Trust

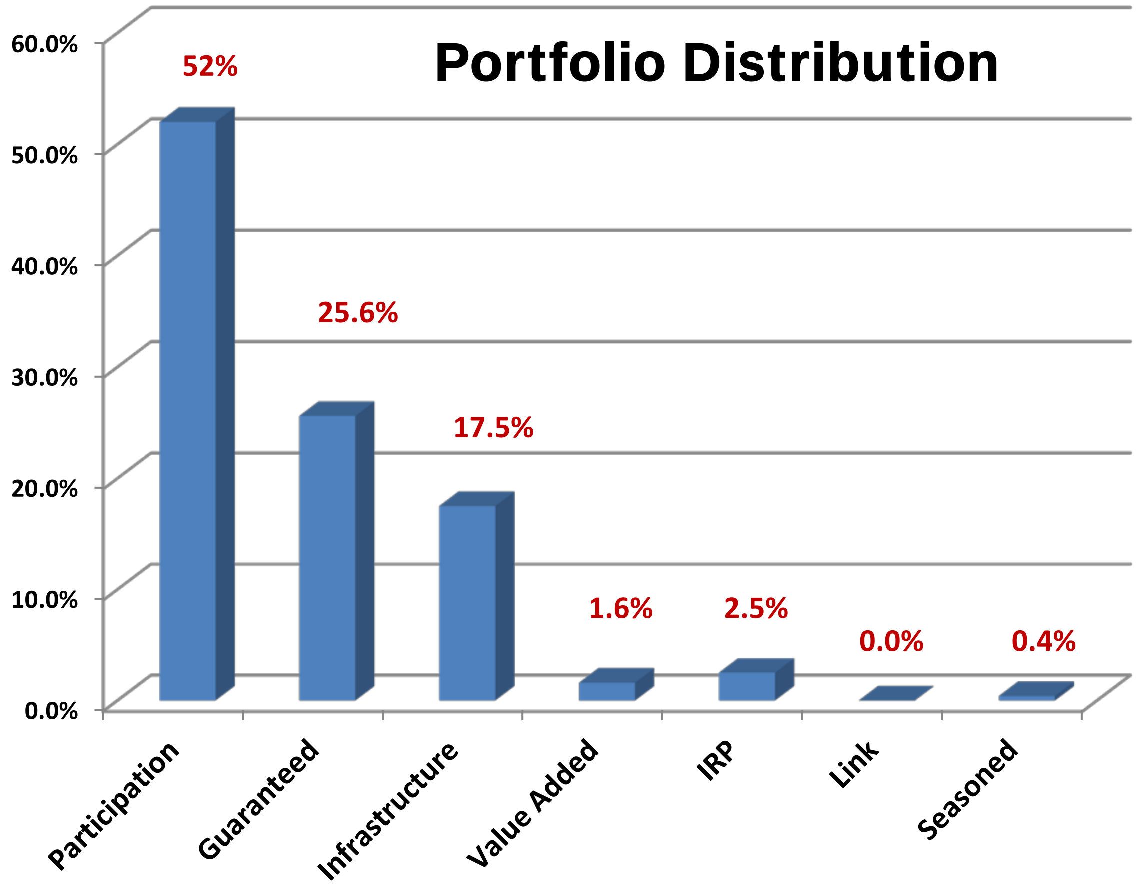
- **Veterans Home Loan Mortgage Program**
  - **Loan partially guaranteed by government**
  - **Only qualified veterans residing in Montana**
  - **Minimum $2,500 equity applies to purchase price of house**
  - **Automated underwriting – approved eligible only**
  - **Must have full allocation of veteran's benefits**
  - **30-year term priced at 1% less than market rates**
  - **Montana Board of Housing administers program and services loans**

In-State Loan Program – Coal Tax Trust

- **Science and Technology**
  - MBOI becomes successor in interest in 1999
- **Loans Currently Outstanding**

Montana University System	$8,380,992
Glacier Venture Fund	1,000,000
Emerald Bio	725,356
McLaughlin Research Institute	251,671
Deaconess Research Institute	161,603
Gateway Software	1
Total Science and Technology	$10,519,623

In-State Loan Program

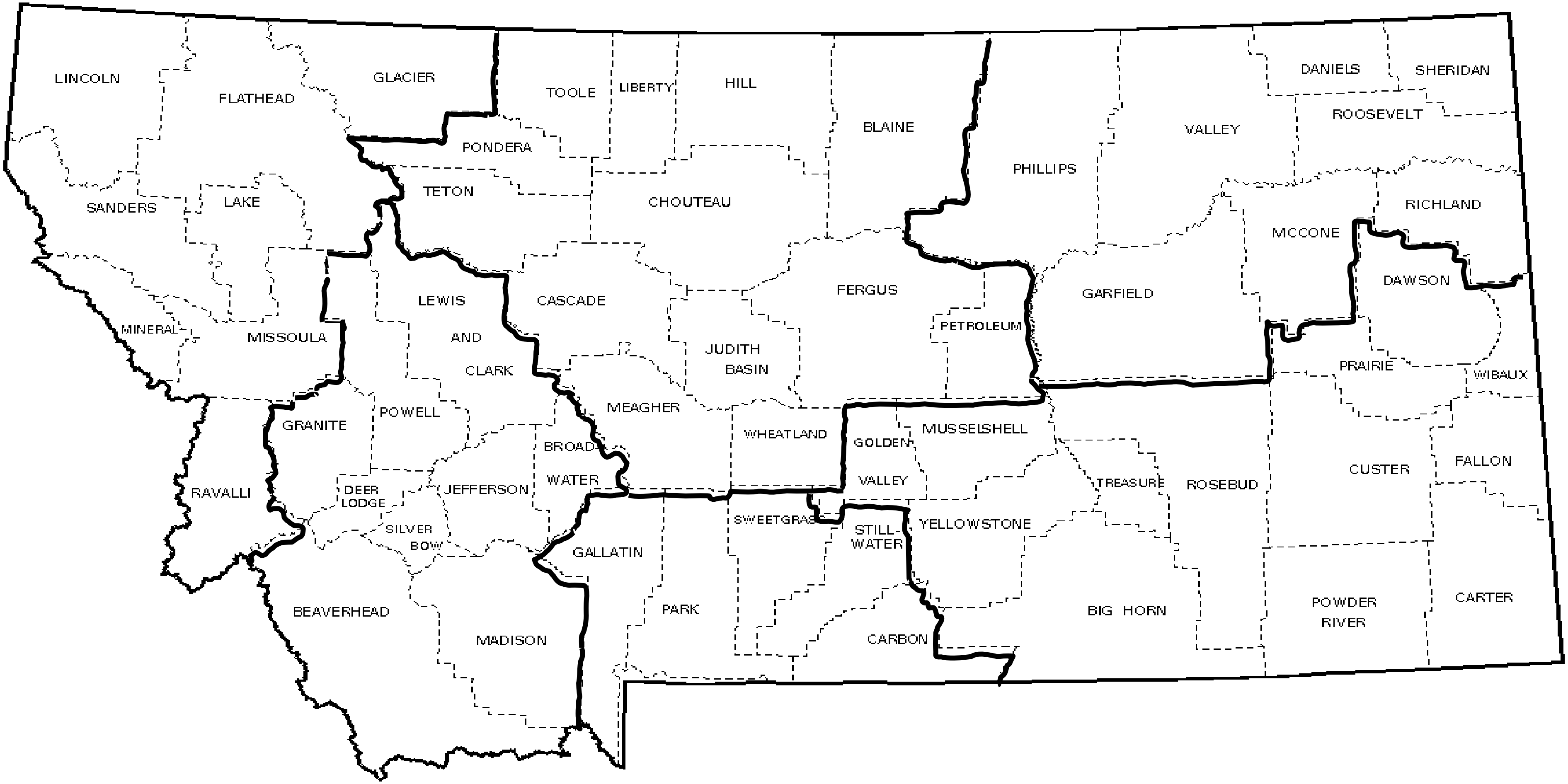


Participated loans comprise 52% ($64,327,999) of the portfolio followed by Federally Guaranteed loans with 25.6% ($31,681,756) and Infrastructure loans at 17.5% ($22,014,291). There is only one Link Deposit loan in the amount of $14,311, which will be paid in May 2013.

NW Montana
$ 7,657,500 Guaranteed
$33,363,700 Non Gtd
$41,021,200 Total

North Central Montana
$ 3,692,200 Guaranteed
$10,354,900 Non Gtd
$14,047,100 Total

NE Montana
$ 272,700 Guaranteed
$ 222,800 Non Gtd
$ 495,500 Total

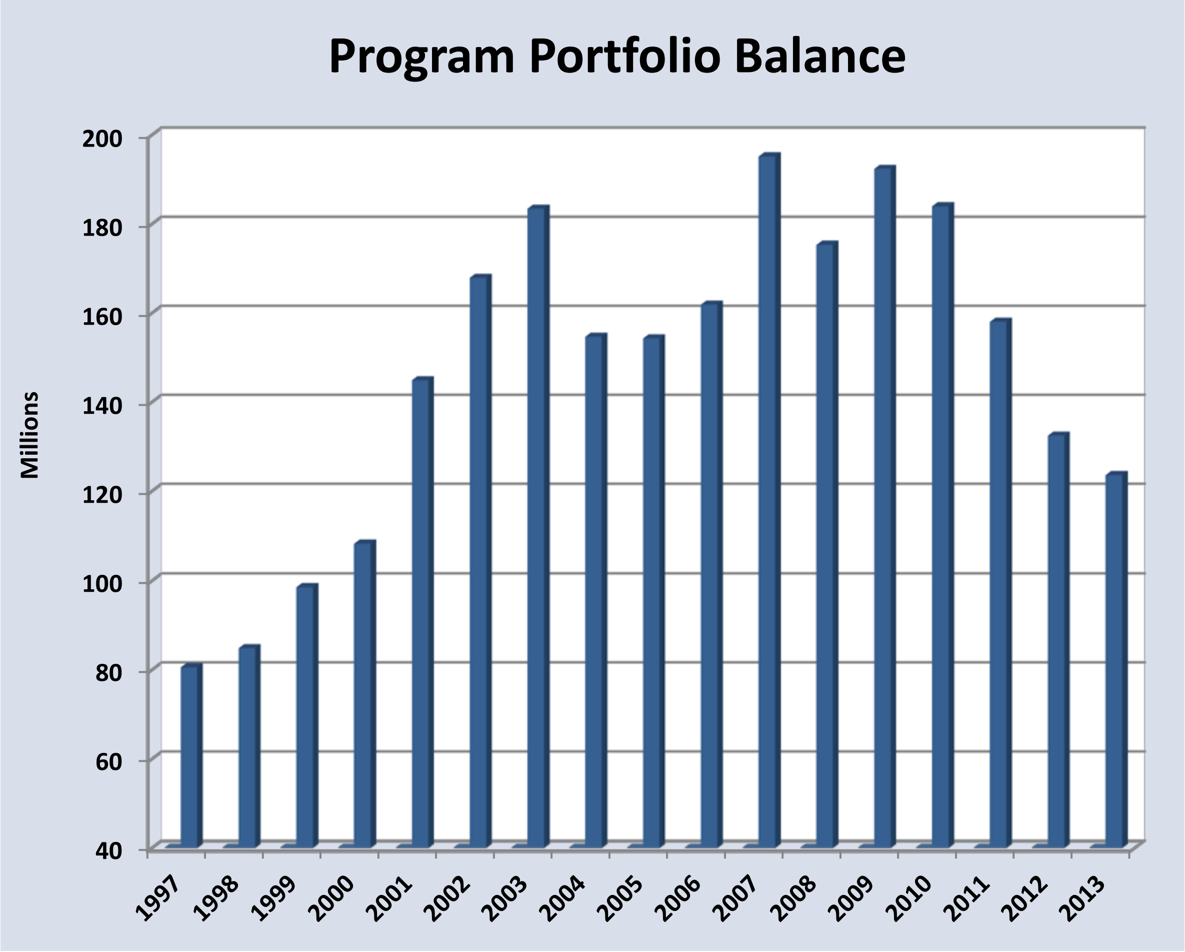


SW Montana
$17,813,600 Guaranteed
$ 1,956,900 Non Gtd
$19,770,900 Total

South Central Montana
$ 1,521,800 Guaranteed
$17,862,500 Non Gtd
$19,384,300 Total

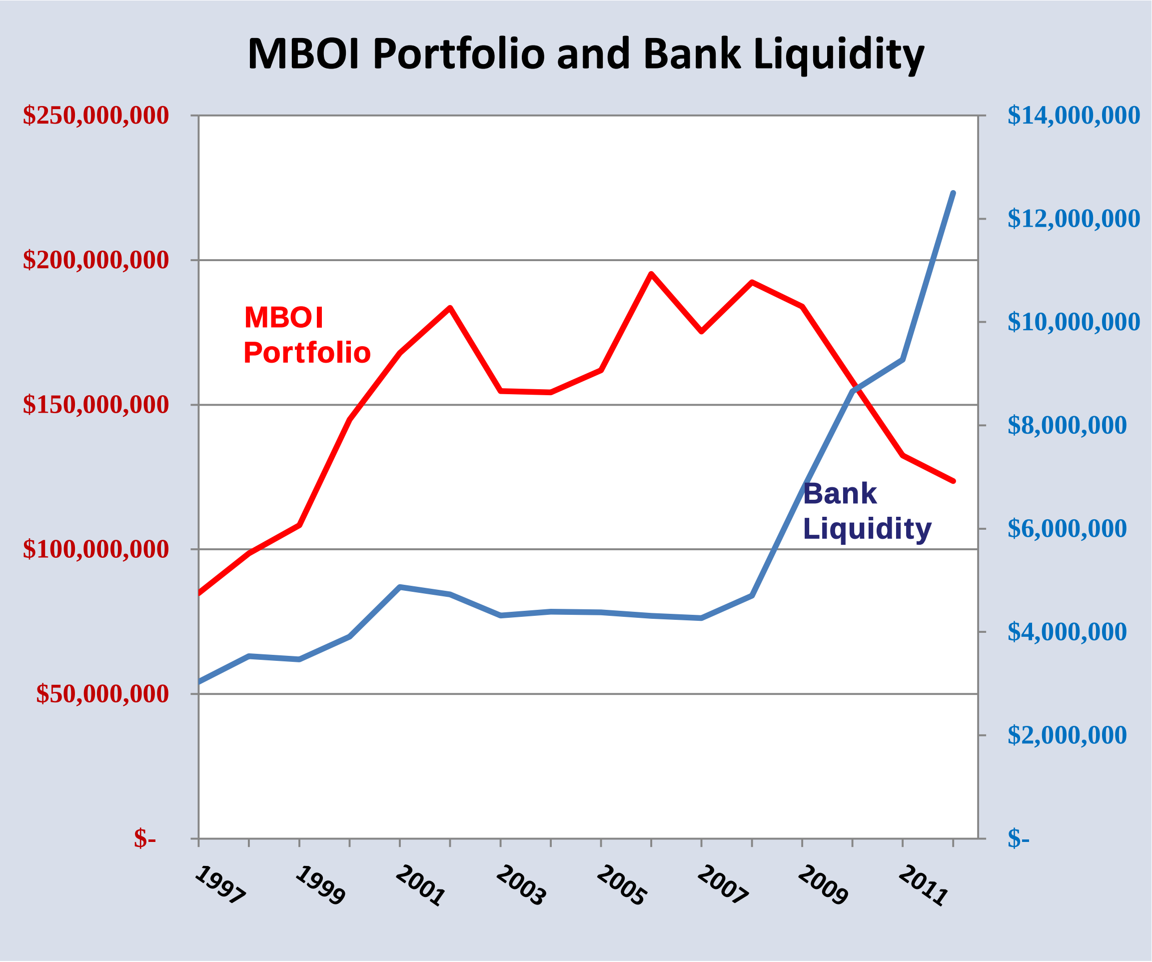
SE Montana
$ 738,200 Guaranteed
$28,153,600 Non Gtd
$28,891,800 Total

In-State Loan Program



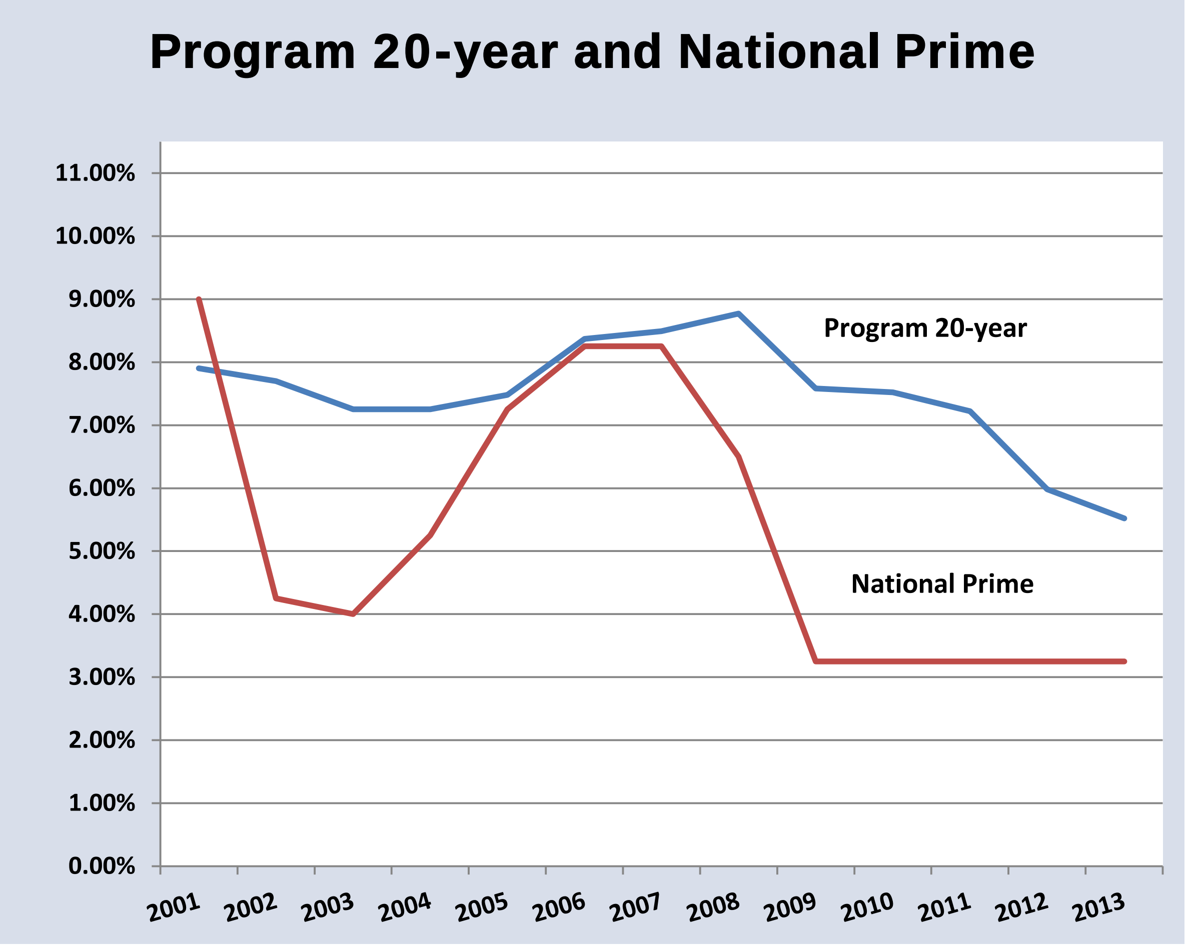
Prior to 1999, the Program operated under Administrative Rules (Rules). It was determined that the Rules made it very difficult for the lenders to understand and to use the Program. As a result, in June 1999, at a public hearing, which no one showed up at, it was decided to repeal 90% of the existing Rules and replace them with Policy. As a result, lenders began to use the program more. The Program portfolio increased from $84,853,000 on 6-30-98 to $183,440,551 on 6-30-03, an increase of $98,600,000.

In-State Loan Program



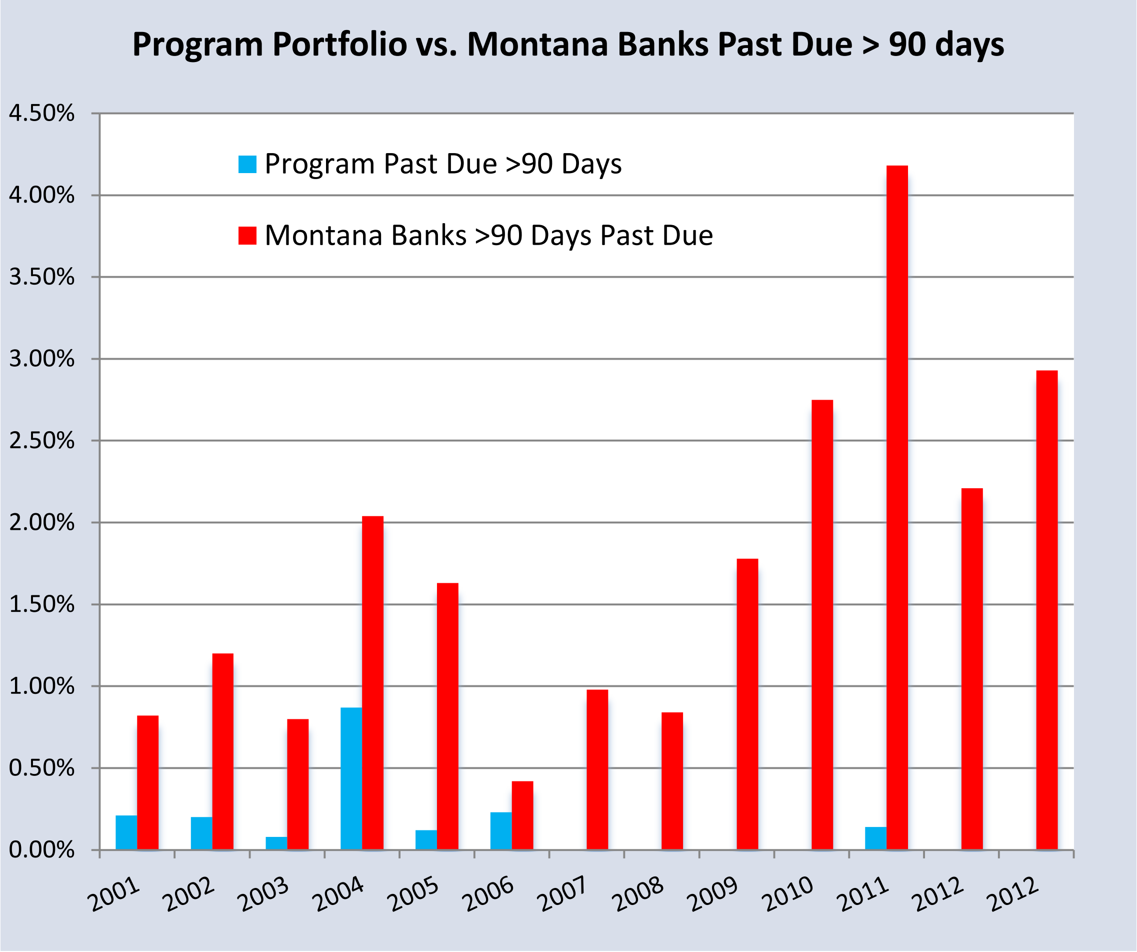
Since the start of the melt-down in 2008 and the tightening of credit standards by the regulators and lenders, loan demand has diminished and lender liquidity has increased. Today, with Montana lenders having excess liquidity, they have no particular desire to participate a portion of their loans to MBOI. As lenders tried to find ways to absorb their excess liquidity, they turned to the Program to repurchase participated loans. Prior to the repurchase of the loan, the lender must submit, in writing, the financial advantage that would accrue to the borrower as a result of the repurchase. If the financial advantage is reasonable, staff will allow the repurchase. As a result, the Program's portfolio has decreased from $192,377,000 as of 6-30-08 to $123,610,000 as of 12-31-12.

In-State Loan Program



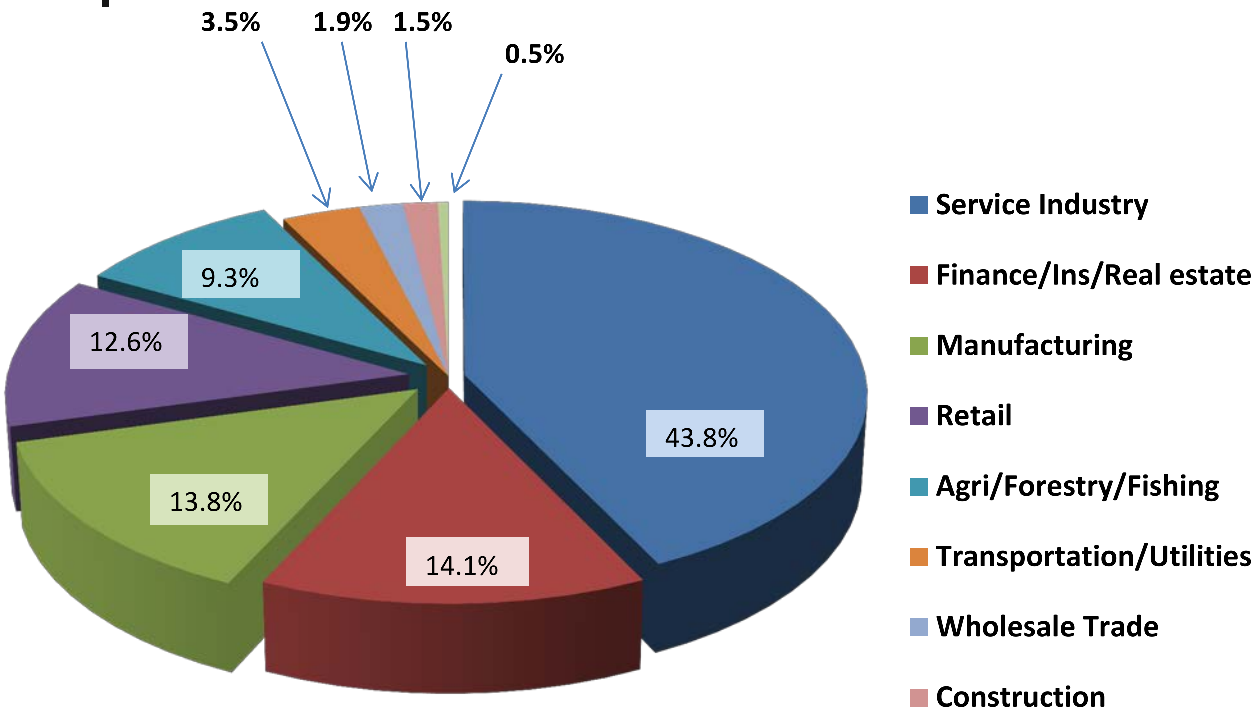
Program interest rates have fallen sharply since 2008 after hitting a high of 8.77% and a low of 5.11% in 2012. Program interest rates are influenced by national prime, but national prime is not the index. The index is the FHLB – Seattle amortizing fixed interest rates. Program interest rates change every Thursday.

In-State Loan Program



The Program has an impressive commercial loan past due history, which has always been well below the over 90 days past due percentage of Montana lenders. Years showing no blue column indicate there were no commercial loans over 90 days past due during that period. There are six such periods reflected on this graph. The Program has written off a portion of one loan in the amount of $206,599 in 2002. The loan was originated in 1997.

In-State Loan Program



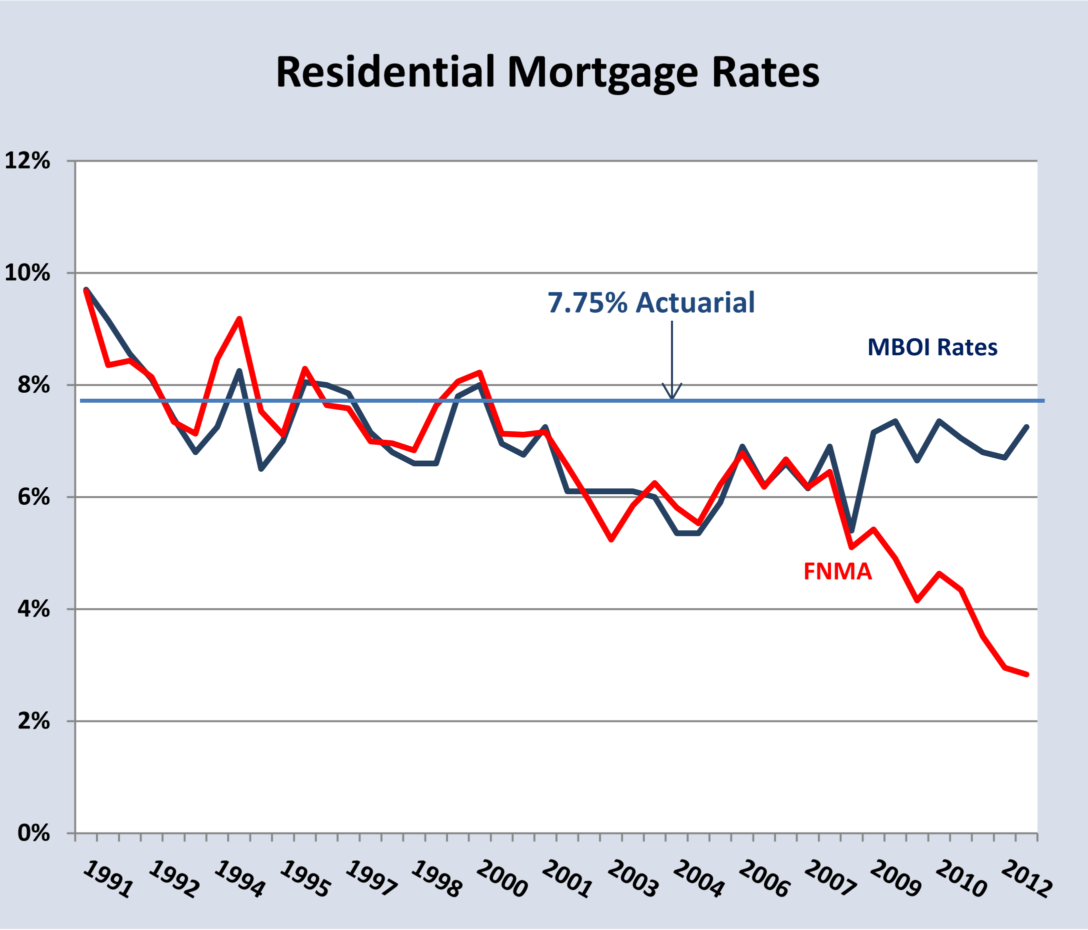
Sectors Since Inception

The service sector is comprised primarily of hotel/motel, restaurants, professional offices, health care facilities and auto repair. Historically hotel/motel comprised 30.33% of that total service sector. In 1993, the Board felt it had too much exposure in the hotel/motel industry. At that time the "at risk" (non-guaranteed) loans represented 12.46% of the portfolio. As a result, the Board established a maximum participation percentage in hotel/motel loans of 50%. The Program still operates under this directive. As of 12-31-12 the "at risk" hotel/motel loans are 8.54% of the portfolio.

Residential Mortgage Program – Pension Funds

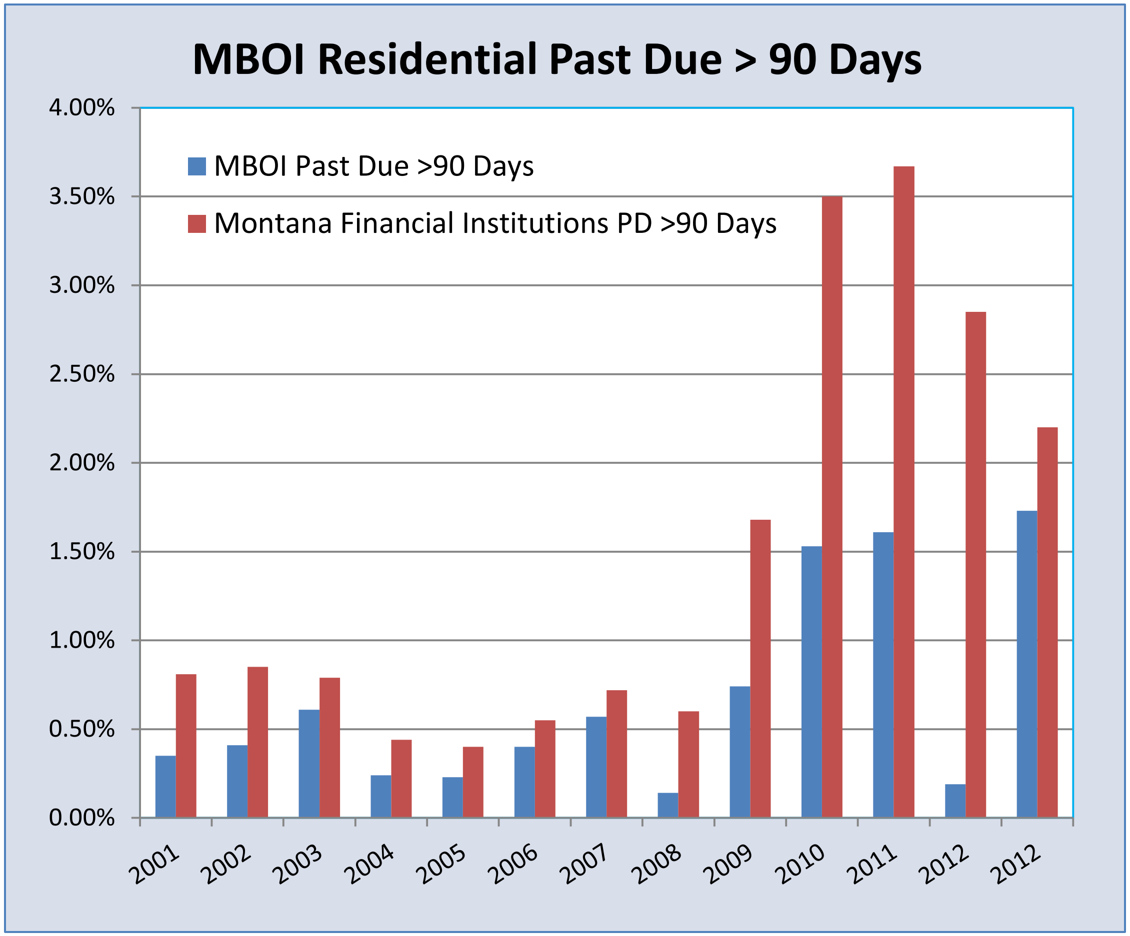
- Residential Loans
  - Montana residential mortgages only
  - Mortgages serviced by lender
  - Board of Housing provides accounting
  - Portfolio peaked in 2002 at $324.0 million
  - Program scaled down due to low mortgage interest rates
  - Interest rates set off Freddie Mac rates
  - Current principal outstanding as of 12-31-12 is $17.6 million

Residential Mortgage Portfolio



In all of the 1990s, MBOI residential interest rates averaged 7.65% while the market residential interest rates averaged 7.85%. During that time MBOI discounted the market's interest rate to encourage lenders to sell their Montana residential loans to MBOI. As interest rates decreased in early 2000, the Board made a decision not to invest in any additional Montana residential mortgages. This was primarily driven by the fact that the pension fund's actuarial rate was at 7.75% and it was difficult to achieve 7.75% in a 6.00% or lower residential interest rate market. Instead of discontinuing the residential loan program, MBOI increased the interest rate offered to purchase residential mortgages. As a result, Montana lenders chose other secondary market investors to sell their loans. The higher residential interest rate philosophy is still in effect today with MBOI.

In-State Loan Program



- **The MBOI investments in Montana residential mortgages uses pension funds rather than Coat Tax Trust money. The residential portfolio peaked in 2002 at $324,038,000. The outstanding residential portfolio, as of 12-31-12 is $17,617,242. Since the residential portfolio is funded with pension money, which has an actuarial rate of 7.75%, current interest rates do not allow MBOI to be competitive in today's residential mortgage market.**
- **The past due history of the residential portfolio has been very good, especially since the melt-down of 2008. As the outstanding portfolio balance continues to decrease, the probability of increased past due percentage also increases due to lower portfolio balances.**

Summary

- In-State Loan Programs created by the Legislature
  - Currently 9 Coal Tax loan programs
- Policies are user friendly and understandable
- Size of Program portfolio determined by economy and lender liquidity
- Portfolio consists of high quality credits
- Very experienced and knowledgeable Program staff
- Program staff developed the State Small Business Credit Initiative program, the small loan pool and Low Income Housing Tax Credit loan programs using the existing commercial loan policy
- Residential loan program is currently dormant due to very low residential market interest rates

Montana Board of Investments Meetings

All meetings

- Are public and duly noticed in advance
- Require that substantive decision items be scheduled, identified and publicized
- Will invite the public for comments at every meeting
- Have minutes taken and previous ones approved

Quarterly meetings - February, May, August, and November

- Standard business
  - Performance of prior period or year end
  - Activity of prior period
  - Investment consultant
  - Quarterly cost sheet
  - Board member education and training opportunities
- Actuarial Status & Asset Allocation implications
- Loan, Audit and Human Resource and any ad-hoc committees meet
- Rotation of topics to provide 24 month systematic review

Semi-Annual meetings - April and October

- In depth coverage on certain (to be determined) topics
- April - Asset Allocation at a strategic level
- Additional systematic review of topics to complete 24-month rotation
- Subcommittees meet only as needed

Additional Board Topics for 24-month Systematic Review, either (A) annually or at least (B) biennially

- Investment Policy Statements (A)
- Board's budget (A)
- Cost reporting including CEM, Inc. analysis (A)
- Accounting and internal data systems (A)
- Annual report and financial statements (A)
- Staffing levels and compensation (A)
- Securities Lending (A)
- Securities Litigation (A)
- Accounting, GAAP, audits and internal control standards, compliance and execution (A)
- PERS and TRS relationship (A)
- Ethics policy – affirmations (A)
- Resolution 217 update (typically November) (A)
- Board member training and staying current efforts (A)
- General operations (e.g. day to day, landlord, disaster recovery, vendor review) (A/B)
- BOI website (B)
- Custodial bank relationship, performance, continuity (B)
- Customer relationships especially large customers such as State Fund (B)
- Legislative session and interim matters (B)
- Outreach, especially commercial and municipal missions (B)
- The Board as a rated investment credit, a bond issuer and a credit enhancer (B)

Proposed Work Plan 2013

Feb. 26-27	(Pre-Board meeting new member orientation) **Quarterly Meeting's standard business and subcommittee meetings** Securities Lending Benchmark presentation (from RVK) State Fund-Investment Policy change and State Fund presentation - Decision Annual Report and Financial Statements Ethics Customer outreach INTERCAP Additional Bonds - Decision Legislative Update
April 2	**Semi-Annual (non-quarterly) Meeting** Asset allocation All policy review Economic development and other BOI loan programs Montana Facility Finance Authority Emergency/Disaster preparedness Web site Legislative update
May 29-30	**Quarterly Meeting (Billings) standard business and subcommittee meetings** Legislative update INTERCAP finance team follow-up
August 20-21	**Quarterly Meeting standard business and subcommittee meetings** Costs (including reviewing CEM Benchmarking Inc. results) MBOI Budget Accounting and internal control systems Fiscal Year performance through June 30th Non-pension investment funds and agency user presence/presentations Custodial bank RFP and selection timetable for Oct. 2014
October 8	**Semi-Annual (non-quarterly) Meeting** RVK – topic to be determined Board's real estate holdings in Montana
Nov. 19-20	**Quarterly Meeting standard business and subcommittee meetings** Actuarial Status & Asset Allocation Implications Affirm or Revise Asset Allocation Resolution 217 PERS/TRS annual update Securities litigation status Exempt Staff Annual Performance

MONTANA BOARD OF INVESTMENTS
ACRONYM INDEX

ACH........ Automated Clearing House

ADR........ American Depository Receipts

AOF........ All Other Funds

ARC........ Actuarially Required Contribution

BOI........ Board of Investments

CFA........ Chartered Financial Analyst

EM........ Emerging Market

FOIA........ Freedom of Information Act

FWP........ Fish Wildlife and Parks

FX........ Foreign Exchange

IPS........ Investment Policy Statement

MBOH........ Montana Board of Housing

MBOI........ Montana Board of Investments

MDEP........ Montana Domestic Equity Pool

MFFA........ Montana Facility Finance Authority

MPEP........ Montana Private Equity Pool

MPT........ Modern Portfolio Theory

MSTA........ Montana Science and Technology Alliance

MTIP........ Montana International Pool

MTRP........ Montana Real Estate Pool

MTSBA........ Montana School Boards Association

MVO........ Mean-Variance Optimization

NAV........ Net Asset Value

MONTANA BOARD OF INVESTMENTS
ACRONYM INDEX

PERS .... Public Employees' Retirement System

PFL .... Partnership Focus List

QZAB .... Qualified Zone Academy Bonds

QSCB .... Qualified School Construction Bonds

RFBP .... Retirement Funds Bond Pool

RFP .... Request for Proposal

SABHRS .... Statewide Accounting Budgeting and Human Resource System

SLQT .... Securities Lending Quality Trust

SSBCI .... State Small Business Credit Initiative

STIP .... Short Term Investment Pool

TFBP .... Trust Funds Bond Pool

TFIP .... Trust Funds Investment Pool

TIF .... Tax Increment Financing

TIFD .... Tax Increment Financing District

TRS .... Teachers' Retirement System

TUCS .... Trust Universe Comparison Service

VIX .... Volatility Index

2013 CALENDAR

01 New Year's Day
21 M.L. King Day

JANUARY						
S	M	T	W	Th	F	S
		1	2	3	4	5
6	7	8	9	10	11	12
13	14	15	16	17	18	19
20	21	22	23	24	25	26
27	28	29	30	31		

JULY						
S	M	T	W	Th	F	S
	1	2	3	4	5	6
7	8	9	10	11	12	13
14	15	16	17	18	19	20
21	22	23	24	25	26	27
28	29	30	31			

04 Independence Day

18 Presidents Day

FEBRUARY						
S	M	T	W	Th	F	S
					1	2
3	4	5	6	7	8	9
10	11	12	13	14	15	16
17	18	19	20	21	22	23
24	25	26	27	28		

AUGUST						
S	M	T	W	Th	F	S
				1	2	3
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11	12	13	14	15	16	17
18	19	20	21	22	23	24
25	26	27	28	29	30	31

29 Good Friday
31 Easter Sunday

MARCH						
S	M	T	W	Th	F	S
					1	2
3	4	5	6	7	8	9
10	11	12	13	14	15	16
17	18	19	20	21	22	23
24	25	26	27	28	29	30
31						

SEPTEMBER						
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15	16	17	18	19	20	21
22	23	24	25	26	27	28
29	30					

02 Labor Day

APRIL						
S	M	T	W	Th	F	S
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14	15	16	17	18	19	20
21	22	23	24	25	26	27
28	29	30				

OCTOBER						
S	M	T	W	Th	F	S
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6	7	8	9	10	11	12
13	14	15	16	17	18	19
20	21	22	23	24	25	26
27	28	29	30	31		

14 Columbus Day
31 Halloween

12 Mother's Day
27 Memorial Day

Billings Meeting

MAY						
S	M	T	W	Th	F	S
			1	2	3	4
5	6	7	8	9	10	11
12	13	14	15	16	17	18
19	20	21	22	23	24	25
26	27	28	29	30	31	

NOVEMBER						
S	M	T	W	Th	F	S
					1	2
3	4	5	6	7	8	9
10	11	12	13	14	15	16
17	18	19	20	21	22	23
24	25	26	27	28	29	30

11 Veterans Day
28 Thanksgiving Day

16 Father's Day

JUNE						
S	M	T	W	Th	F	S
						1
2	3	4	5	6	7	8
9	10	11	12	13	14	15
16	17	18	19	20	21	22
23	24	25	26	27	28	29
30						

DECEMBER						
S	M	T	W	Th	F	S
1	2	3	4	5	6	7
8	9	10	11	12	13	14
15	16	17	18	19	20	21
22	23	24	25	26	27	28
29	30	31				

25 Christmas Day