

**MONTANA BOARD OF INVESTMENTS
DEPARTMENT OF COMMERCE**

**2401 Colonial Drive, 3rd Floor
Helena, Montana
May 8 & 9, 2007**

MINUTES

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

BOARD MEMBERS ABSENT: Elouise Cobell

STAFF PRESENT:

Polly Boutin, Accountant	Rande Muffick, CFA, Portfolio Manager
Jason Brent, Equity Investment Analyst	Jon Putnam, Equity Investment Analyst
Robert T. Bugni, CFA, Portfolio Manager	Nancy Rivera, Credit Analyst
Geri Burton, Deputy Director	Mari Rohrig, Accountant
Richard Cooley, CFA, Portfolio Manager	John Romasko, Fixed Income Investment Analyst
Kim Dallas, Program Assistant/Board Secretary	Coralie Sciuchetti, Accountant
Roberta Diaz, Accountant	Clifford A. Sheets, CFA, Chief Investment Officer
Tim House, Equity Investment Analyst	Jon Shoen, Equity Investment Analyst
Linda Hunter, Accountant	Steve Strong, Equity Investment Analyst
Ed Kelley, Portfolio Manager	Louise Welsh, Bond Program Officer
Teri Kolnik, Equity Investment Analyst	Charlie Williamson, Equity Investment Analyst
Herb Kulow, Portfolio Manager	Dan Zarling, CFA, Director of Research
Gayle Moon, Accounting Fiscal Manager	

GUESTS: Gordon Hoven, Piper Jaffray
Becky Gratsinger, R.V. Kuhns and Associates
Jim Voytko, R.V. Kuhns and Associates
Marvin Kraft, State Fund
Russell Bjorkman, Vice President, INTECH
Betsy Flavin, Executive Director, Public Funds, JanisIntech Institutional
Melvin Lindsey, Director of Institutional Investments, Julius Baer
Brett Gallagher, Portfolio Manager and Deputy Chief Investment Officer, Julius Baer
Scott Miller, Public Employees' Retirement System
Dave Senn, Executive Director, Teachers' Retirement System
Michelle Barstad, Executive Director, Montana Facility Finance Authority

CALL TO ORDER

Chairman Moore called the regular meeting of the Board of Investments (Board) to order at 1:00 p.m. in the conference room at 2401 Colonial Drive, 3rd Floor, Helena, Montana. As noted above, the meeting convened with eight members of the Board present. Member Cobell was absent.

Chairman Moore asked for approval of the February 21 & 22, 2007 minutes. Member Cohea asked that the section which included the paragraph on Senator Weinberg's discussion be revised to include more information.

Member Prothero motioned for approval of the February 21 & 22, 2007 minutes with the revision as requested by Member Cohea; Member Englund seconded the motion and the motion was passed 8-0. A copy of the revised minutes in reference to Senator Weinberg's comments is as follows:

State Senator Dan Weinberg Presentation

At the invitation of the staff, Senator Weinberg attended the meeting and expressed his concern about the issue of terrorism and investments. Senator Weinberg thanked Carroll South for allowing him the time and opportunity to speak on this topic.

Senator Weinberg spoke that Lou Dobbs (anchor of a nationally syndicated financial news radio report, The Lou Dobbs Financial Report, and is a columnist for Money magazine and U.S. News and World Report) recently talked about terror free investing. Mr. Dobbs stated that the results of a recent poll, 94 % of the viewers, do not believe that the companies that do business with nations that sponsor terrorism should be allowed to be listed on the New York Stock Exchange. That poll says that the public does not want investments to be made in countries that hurt others.

Senator Weinberg stated that there are ways to invest according to Montana's values and still make a profit. His concerns are that investments are not being made according to Montana values, as laid out in the constitution. The concern is also long-term security of the funds. Senator Weinberg suggests that Montana join the other 24 or 26 states that are trying to get the federal government to create a screen to give guidance about how to invest. Senator Weinberg wants Montana to be part of the solution, not part of problem.

Senator Weinberg further discussed what government has done. The State Department has refused to get involved. The Securities Exchange Commission stating that it would be inappropriate to publish a list of companies, it would be inappropriate to engage in any activity that might be conscrewed as providing investment advice.

Senator Weinberg introduced Blaine Townsend. Mr. Townsend is with Trillium Asset Management. Trillium Asset Management specialized exclusively in socially responsible investing. The use of social screens is very neutral when it comes to the financial outcomes of an investment. An investor can apply social screenings and still meet the financial objective, in a disciplined approach.

For pension fund investors the fiduciary obligation is very serious. The laws are written to be much stricter for very good reason. The laws are good to ensure that people are acting prudently, investing wisely and strictly for the benefit of the beneficiary. The question is how to integrate social responsibility into the investment process. The investment community may be looking to the federal government to be setting regulation and oversight of companies.

The solution starts with the investment policies; it starts with the Montana values. Investors also need to make sure that proxy voting guidelines are in place and managers are being engaged and a line of communication is in place.

Staff Introductions

Ms. Gayle Moon introduced Ms. Polly Boutin as the newest addition to the accounting staff. Ms. Boutin was hired to train in Coralie Sciuchetti's position for six months prior to Ms. Sciuchetti's October retirement. Ms. Moon also announced that Ms. Mary Noack has accepted a new position as Network Administrator and that Accounting Technician position is currently being advertised. Ms. Mary Rohrig and Ms. Linda Hunter have moved to new positions within the accounting area and are now taking on new responsibilities.

EXTERNAL MANAGER PRESENTATIONS

INTECH

Mr. Cliff Sheets introduced Mr. Russell Bjorkman, INTECH and Ms. Betsy Flavin, JanisIntech Institutional. INTECH was recently selected as a Large Cap U.S. Enhanced Index manager for a portion of the externally managed Domestic Equity pool. Mr. Bjorkman and Ms. Flavin reviewed their firm and Large Cap U.S. Enhanced Index management strategy.

Julius Baer

Mr. Cliff Sheets introduced Mr. Melvin Lindsey and Mr. Brett Gallegher. Julius Baer was recently selected as a Core International Equity Manager for a portion of the externally managed International Equity pool. Mr. Lindsey and Mr. Gallegher reviewed their firm and International Equity management style.

ADMINISTRATIVE BUSINESS

Loan Committee Report

Mr. Jack Prothero, Committee Chair, reported that two items will come before the Board during the regular agenda, and that the Loan Committee will make its recommendation at that time.

Public Comment

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

EXECUTIVE DIRECTOR REPORTS

Legislative Update

Senate Bill 68 – This is one of the Board's two bills that would have kept certain alternative investment information and documents confidential.

Mr. South reported that this bill was heard and passed out of Senate Business and Labor. The bill was amended on the Senate floor and sent to Senate Finance and Claims where it was heard again, amended again, and passed on a 17 – 2 vote. Passed the Senate 45 – 5 and was sent to the House Appropriations Committee where it was heard on April 2 and "tabled" on April 18, effectively killing it.

Senate Bill 69 – This is the Board's second bill that increased the lending authority for the Value-Added and Infrastructure Loan Programs from \$50.0 million to \$70.0 million and \$80.0 million respectively.

Mr. South reported that this bill was heard and passed out of Senate Finance and Claims, and passed the Senate on a 38 – 11 vote. Heard in the House Taxation Committee and passed on an 18 – 0 vote. Passed 2nd reading in the House 93 – 7 and then sent to the House Appropriations. The Board submitted an amendment to "fix" a potential problem with the Commercial Loan Program (see agenda item

“Commercial Loan Program 25% Language”). This bill was amended and passed out of House Appropriations 17 – 2 and passed the House on 3rd reading 86 – 13. Rules had to be suspended in the Senate to receive the bill and concur with the House amendment. Rules were suspended and the Bill passed 3rd reading in the Senate 46 – 4 at noon on the last day of the session.

Senate Resolution 8:

This is one of several Senate resolutions confirming the Governor’s Board appointments. Board appointments confirmed are:

- Mr. James Turcotte, appointed for a term ending January 1, 2009.
- Mr. Terrill Moore, appointed for a term ending January 1, 2011.
- Ms. Maureen Fleming, appointed for a term ending January 1, 2011.
- Mr. Karl Englund, appointed for a term ending January 1, 2011.
- Mr. Jon Satre, appointed for a term ending January 1, 2011.

The resolution was heard and passed out of the Senate State Administration Committee on a 11 – 0 vote and passed the Senate 47 – 3. The resolution does not go before the House.

Senate Bill 467 – This bill as introduced would have dramatically revised Board member makeup and meeting schedules. This bill adds two legislators as ex-officio members of the Board of Investments. One member is appointed by the Senate President and one appointed by the House Speaker. Appointees must not be from the same political party and preference must be given to legislators with investment and/or finance experience.

Mr. South reported that this bill was heard and passed out of Senate Business and Labor 11 – 0 and passed the Senate 50 – 0. Heard and passed out of House Business and Labor 16 – 0 and passed the House on a 95 – 5 vote. Signed by Governor Schweitzer on April 10 and is effective upon passage and approval.

Senate Bill 468 – This bill would have moved one of the Board’s bond programs from the Board to the Department of Commerce and encourage the Board to invest funds internally as follows: *The board is urged under the prudent expert principle to invest up to 3% of retirement funds in 6 venture capital companies. Whenever possible, preference should be given to investments in those venture capital companies that demonstrate an interest in making investments in Montana-maximize returns after management fees by managing assets internally instead of hiring professional investment management companies.*

The bill was heard and tabled in Senate Business and Labor after testimony from the Board Chairman and Executive Director.

Senate Bill 489 – A constitutional amendment that would permit the Board to invest up to 25% of state trust funds in equities and will be put on the November 2008 ballot for voter approval.

Mr. South reported that the bill was heard and passed out of Senate Business and Labor on a 10 – 1 vote and passed the Senate 50 – 0. Heard and passed out of House State Administration 16 – 2 and passed the House with a 77 – 22 vote. It will be effective if approved by the voters in November 2008.

House Bill 63 – The Administration’s bill that appropriated \$100.0 million to the Teachers’ Retirement System and increased employer contributions to make the system actuarial sound.

The bill was heard and passed out of House State Administration 16 – 2. Passed House 2nd reading 91 – 9 and was sent to House Appropriations. Heard and passed out of House Appropriations 19 – 0 and passed House 3rd reading 87 – 11. Heard and passed out of Senate Finance and Claims 18 – 0 and

passed on Senate floor 44 – 6. During the process the \$100.0 million appropriation was reduced to \$50.0 million.

House Bill 125 – Appropriates \$1.4 million to repay the INTERCAP loan used for start up costs of the PERS Defined Contribution system.

The bill was heard and passed out of House State Administration 17 – 1. Passed House 2nd reading 89 – 11 and sent to House Appropriations. Heard and passed out of Appropriations 12 – 7 and passed House 3rd reading 62 – 38. Heard and passed out of Senate Finance and Claims 19 – 0 and passed on Senate floor 49 – 1. It is effective on passage and approval.

House Bill 131 – The Administration’s bill to make the Public Employees, Sheriffs, and Game Warden retirement systems actuarially sound. It raises employer contributions but does not appropriate a cash infusion in to the systems. It reduces the 3.0% Guaranteed Annual Base Adjustment for some systems to 1.5% for new employees.

The bill was heard and passed out of House State Administration 11 – 7. Passed House 3rd reading 78 – 21. Heard and passed out of Senate Finance and Claims 18 – 0 and passed Senate 3rd reading 42 – 8.

House Bill 771 – Requires additional information regarding the pension systems in the Board’s annual report.

Section 1. Reports on retirement system trust fund investments and benefits. (1) As soon as practical after the end of each calendar year, the board of investments shall publish a report on each retirement system trust fund invested by the board. The report may be part of an annual report required pursuant to Article VIII, section 13, of the Montana constitution or 17-5-1650 but must summarize the following with respect to each retirement system trust fund:

(a) asset allocation;

(b) past and expected investment performance;

(c) investment goals and strategies; and

(d) Montana public employees' retirement system investments and performance compared with the public employees' retirement system investments and performance in other states.

(2) The board of investments shall annually at a public meeting present the report described in subsection (1) to the public employees' retirement board provided for in 2-15-1009 and the teachers' retirement board provided for in 2-15-1010. The board shall also provide the report to the legislature pursuant to 5-11-210.

The bill was heard and passed out of House State Administration 18 – 0. Passed House 3rd reading 93 – 3. Heard and passed out of Senate State Administration 10 – 1 and passed Senate 3rd reading 48 – 2. The bill is effective June 1, 2007.

House Joint Resolution 59 – A Committee Bill to study the public retirement systems. The study will include looking at the actual structure of the defined benefit plans to ascertain if the structure could be changed.

The resolution was heard and passed out of House State Administration 18 – 0. Passed House 3rd reading 80 – 20. Heard and passed out of Senate State Administration 6 – 4 and passed Senate 3rd reading 45 – 5.

Senate Joint Resolution 29 – A Committee Bill to study the Board of Investments.

The resolution was heard and passed out of Senate Business and Labor on a 10 – 1 vote. Passed Senate 3rd reading 50 – 0. Heard and tabled in the House Business and Labor on the 88th legislative day.

A copy of the memo titled “Legislative Update” written by Carroll South is kept on file at the Montana Board of Investments.

Commercial Loan Program 25% Language

Mr. Carroll South reported that based on staff research of the Commercial Loan Program since its inception, staff has interpreted the 25 percent language as a legislative intent “target” rather than a statutory “cap.” Historically, the “target or cap” interpretation mattered little because outstanding Commercial Loans never approached 25 percent of the Trust. However, the Program has grown significantly in recent years and outstanding loan principal is currently approaching 25 percent of the Trust.

During a January Legislative Audit conference, staff asked the Auditor’s legal staff to opine on the issue of whether the 25 percent is a target or a cap. The Auditor’s legal opinion implied that the 25 percent was a cap rather than a target. When the opinion was received in March, Senate Bill 69 had passed the Senate and been assigned to the House Appropriations Committee but had not yet been heard.

Staff prepared the following amendment to Senate Bill 69:

17-6-305. Investment of ~~up to twenty-five percent~~ of coal tax trust fund in Montana economy -- report by board. (1) Subject to the provisions of [17-6-201\(1\)](#), the board shall endeavor to invest ~~up to~~ 25% of the permanent coal tax trust fund established in [17-6-203\(6\)](#) in the Montana economy, with special emphasis on investments in new or expanding locally owned enterprises. Investments made pursuant to this section do not include investments made pursuant to [17-6-309\(2\)](#). For purposes of calculating the 25% of the permanent coal tax trust fund, the board shall include all funds listed in [17-5-703\(1\)](#). The portion of the permanent coal tax trust fund contained in portfolios formerly administered by the Montana board of science and technology development is included in the 25% of the trust fund allocated to the board for in-state investment under this section. 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.

The amendment simply states that whatever the intent of the 25 percent language, it does not preclude the Board from investing more than 25 percent of the Trust in Commercial Loans if it is “prudent” to do so and if the loans will “benefit the Montana economy.”

Mr. South requests the Boards approval for staff to prepare a policy that will outline the prioritization process for the Commercial Loan Program and the drafted policy will be presented for Board consideration and decision at the August meeting. Member Fleming motioned for approval of staffs request; Member Turcotte seconded the motion and the motion was approved 8-0.

Domestic Equity Pool (MDEP) Reorganization/Staff Reorganization

Mr. Carroll South and Mr. Cliff Sheets presented a staff recommendation that Board approve (1) the liquidation of the internally-managed domestic equity portfolio; (2) the redeployment of staff currently allocated to the internally-managed portfolio; and (3) a revised allocation for MDEP.

The internally-managed domestic equity portfolio has historically been tilted towards “mega-cap” stock and its performance has struggled to match that of the Standard & Poor’s 500 Index. During the period 1998 through 2006, the internally managed portfolio underperformed the Index by an average of 1.67 percent annually.

Staff believes that it is prudent and in the best interest of the pension funds to liquidate the portfolio and transition the assets into other strategies. The staff dedicated to this portfolio has made a diligent effort to improve the portfolio performance and their efforts are greatly appreciated.

Currently there are 16 professional investment positions authorized by the Board. Ten of these positions (63%) are dedicated exclusively to the internally-managed equity portfolio. The domestic equity portfolio comprises just 14 percent of pension fund portfolios and less than 9 percent of the total investment portfolio.

Staff proposes that the investment staff currently assigned to the internally managed portfolio be redeployed in other capacities per the revised functional organization chart that is part of this recommendation. These new positions will participate in the management of both public and alternative asset classes to provide assistance in managing pension and total fund portfolios.

Mr. Cliff Sheets then introduced to the Board the concept of the revised asset allocation for MDEP. There are four strategy categories that will be used as the framework for constructing the Large Cap portion of the MDEP: Passive, Enhanced Index, Style-based (Value and Growth), Partial Long/Short. While recognizing the efficiency of the large cap U.S. Equity market, there is potential to add value by employing certain investment strategies to add incremental returns in a risk-constrained manner and hire the best managers within the strategies.

In order to generate excess return over the Large Cap benchmark some risk is unavoidable. The additional risk and the anticipated excess return should be pursued in a manner that controls overall portfolio risk while providing diversification in terms of both the individual managers and their strategies. The following strategies were discussed along with a proposed initial weighting and long-term policy guideline limits by strategy. These weightings were proposed in the context of the Large-Cap component of the pool only.

Passive Component: The passive strategy component would be reduced from its present weighting of 43 percent of Large Cap holdings to a target of 15 percent within a range of 10 – 30 percent.

Enhanced Index Component: Staff proposed the allocation be increased to a target of 27 percent, within a range of 20 – 30 percent.

Value/Growth Component: Staff proposed the allocation for this component be 28 percent, within a range of 25 – 33 percent.

Enhanced Alpha Component: Staff proposed an initial target of 15% for the component within a range of 15-33% of Large-Cap. It's expected this component will grow over time as confidence is gained in the strategy and managers.

Small/Mid Cap Strategies: Staff proposed maintaining the current active manager lineup with core, value, and growth managers for both the small and mid market cap segments of the pool.

Board approval of the staff reorganization and domestic equity pool structure was requested. Member Terry Cohea motioned for approval of staff recommendations as presented; Member Englund seconded the motion and the motion was passed 8-0.

State Fund Building

At the May 18, 2006 Board of Investments Board meeting, the Board approved a staff recommendation to authorize a real estate allocation in the State Fund investment portfolio up to the cost of a new building. With this approval, staff advertised to solicit responses from property owners with property sufficiently sized and appropriately located. Two locations have been determined by the Board and State Fund staff to be appropriate locations for the construction of a 100,000 sq. ft. Class A office building.

The first choice is a site in downtown Helena adjacent to the Great Northern Town Center and near the new Federal Courthouse buildings. However, the site is only suitable if the City of Helena finances and builds a 350 space parking structure adjacent to or attached to the building (the City owns the adjacent property). Board and State Fund staffs have met several times with City of Helena officials to discuss the specifics of a joint construction venture in which the City would own and maintain the parking structure and negotiate a long term lease with the Board for the parking spaces.

Pursuing this site will require close coordination and cooperation among City, Board, and State Fund staff and will require official action by the City Commission authorizing the issuance of bonds to finance the parking structure. While there are two separate construction projects involved, each project is totally dependent upon the other. The City cannot finance and construct the parking structure without the building and a long-term parking space lease and the building cannot meet its parking requirements without the parking structure. Preliminary discussions with the City have concluded that it is in the best interest of all parties to jointly select and hire an architect to design and supervise both structures but contract separately for the construction of each project.

The selection of this site will require formal agreements by three parties - the City of Helena, the Board, and the State Fund. The three parties would be involved in the selection of an architect and the State Fund must agree to pay over the term of the parking lease, the rate required by the City to make the parking structure financially feasible. The parking cost for the State Fund in this scenario is an "operational" cost, rather than a "return on investment" cost required if the parking structure were held in the State Fund investment portfolio. Should this site not be feasible for any reason, staff recommend pursuing the feasibility of a second site.

The second choice is the Nob Hill site. This site is a new mixed-use development immediately adjacent to the new Interstate 15 interchange in the South section of Helena. This site is readily visible and accessible from the interstate and has ample space available for the 100,000 square foot building and 350 parking spaces. This is a simpler site on which to construct a building and requisite parking because it does not depend upon the action of a third party for parking. However, because it is a new development, certain amenities and services available to the State Fund staff at the downtown site may not be available here.

The memorandum of understanding between the Board and the City of Helena was approved by the City Commission on May 7, 2007. Therefore the City has agreed to issue the bonds which will finance the parking structure.

Recommendation: Staff recommends that the Board authorize its staff to continue to work with City of Helena officials and the State Fund staff to negotiate the details and agreements required for construction at the downtown site. Once the necessary agreements are in place, staff further recommend that they be authorized to purchase the site and begin the planning/design process. The City of Helena and the Board would jointly issue a Request for Proposal for architectural/engineering services so one entity would be responsible for designing and supervising both projects. Separate construction contracts would be issued for each project, with the City assuming responsibility for the parking structure and the Board assuming responsibility for the building.

Member Englund motioned for approval of the staff recommendation with the removal of the alternative second choice site of Nob Hill. Member Fleming seconded the motion and the motion was passed 8-0.

Custodial Bank Request for Proposals

Mr. Carroll South reported that the Board's current custodial contract with State Street Bank and Trust expires later in the year. Staff recommends that the Board authorize the issuance of an RFP for custodial bank services. Staff will screen and score responses from qualified banks and present a recommendation to the Board in August. The Board will make the final selection of a custodial bank based on staff recommendation.

Member Prothero motioned for approval of the staff recommendation as presented; Member Paull seconded the motion and the motion was passed 8-0.

State Ethics Law

Mr. Carroll South presented to the Board copies of the state's "Code of Ethics" law and other pertinent sections of law for Board review. The subject of ethics was addressed in the Independent Fiduciary Services review, and Board and staff have discussed the drafting of an ethics policy specifically for the Board members and staff.

Chairman Moore asked Mr. South to draft a Board specific ethics policy for review at the August Board meeting.

ADJOURNED

The meeting adjourned for the day at 5:05 p.m.

CALL TO ORDER

The meeting was reconvened Wednesday, May 9, 2007 at 8:00 a.m. with eight members of the Board present. Member Cobell was absent.

BOND PROGRAM

Activity Report

The Board reviewed this report for the period ending March 31, 2007.

Staff Approved Loans Report

Ms. Louise Welsh reported that:

Borrower:	Town of Columbus
Purpose:	To finance costs associated with a storm sewer project.
Staff Approval Date	February 15, 2007
Board Loan Amount:	\$800,000
Term:	10 years

Borrower:	Whitehall School District
Purpose:	To finance the purchase and installation of a new natural gas boiler
Staff Approval Date	March 1, 2007
Board Loan Amount:	\$100,000
Term:	10 years

Borrower:	City and County of Butte-Silver Bow
Purpose:	To finance the purchase of a new Caterpillar PM-201 Cold Planer
Staff Approval Date	March 12, 2007
Board Loan Amount:	\$736,843
Term:	10 years

Borrower:	Stillwater County
Purpose:	To finance costs associated with constructing and equipping a new dispatch center
Staff Approval Date	March 30, 2007
Board Loan Amount:	\$214,000 total; two separate loans \$130,500 for construction costs over a 10-year term and \$83,500 for equipment over a (6) six-year term
Term:	10 years and 6 years

Borrower:	Flathead County Water Sewer District No. 8 – Happy Valley (Whitefish)
Purpose:	To finance costs associated with a preliminary engineering report (PER)
Staff Approval Date	March 30, 2007
Board Loan Amount:	\$25,000
Term:	3 years

has been approved by staff.

INTERCAP Loan Policy Updates

On February 22, 2007 the Board authorized staff to increase the INTERCAP Revolving Loan Program's maximum loan term to 15 years. With that authorization Ms. Louise Welsh recommended the following updates to the INTERCAP loan policy:

1. **SPECIFIC REQUIREMENTS FOR ALL INTERCAP LOANS**
 - (a) Three weeks prior to needing funds, borrower must notify the Board of the desire to borrow draw down funds.
 - (b) Prior to receiving funds the borrower must complete ~~three~~ two sets of loan documents that include:
 - (1) Eligible governments must adhere to State law when financing capital projects and cannot finance projects for a longer term than allowed. Board staff will consider the maximum loan term authorized in statute, as well as the repayment ability of the eligible borrower, when reviewing loan requests. In addition, loan terms cannot exceed the useful life of the project being financed.
2. **SHORT TERM LOANS SPECIFIC CRITERIA (Sec. 6 of the Application)**
 - (a) Short term INTERCAP loans may be made ~~up to one year~~ to cover two types of needs:
3. **GENERAL FUND DEBT LOANS SPECIFIC CRITERIA (Sec. 9A of the Application)**
 - (c) Loan terms are limited to 15 years, useful life of the project, or borrower term limit per State statute, whichever is less.
 - (d) Statutory authority for general fund loans are;
 - b. Cities and Towns; ~~7-5-4306 and 7-7-4101;~~ 7-7-4101, 7-7-4201 & 7-5-4306 or 7-7-4101 & 7-7-4104;
4. **ENTERPRISE DEBT LOANS SPECIFIC CRITERIA (Sec. 9B of the Application)**
 - (c) In most cases the obligation is not secured by the full faith and credit of the issuer and the obligation does not require voter approval. However an election ~~is~~ may be required for county water and sewer districts.
 - (g) Enterprise debt loans have a maximum term of 15 years or useful life of the project, whichever is less.
5. **SPECIFIC CRITERIA FOR GENERAL OBLIGATION LOANS (Sec. 9C of Application)**
 - (f) Loan terms are limited to 15 years, or useful life of the project, whichever is less.
6. **RURAL FIRE DISTRICT AND FIRE SERVICE AREA LOANS (Sec. 9D of Application)**

- (f) Loan terms are limited to 15 years, useful life of the project, or borrower term limit per State statute, whichever is less.

7. SPECIAL OR RURAL IMPROVEMENT DISTRICT LOANS (Sec. 9E of Application)

- (g) Subject to 7-12-2171(b), loans in excess of \$250,000 require a marketability opinion from underwriters.
- (h) Maximum loan term is 15 years or useful life of the project, whichever is less.

Loan Committee Chair Prothero presented Loan Committee recommendation for approval of these INTERCAP Loan Policy updates as presented; Member Turcotte seconded the motion and the motion was passed 8-0.

Montana Facility Finance Authority/St. Luke Community Healthcare Network

Michelle Barstad presented Master Loan Program, Resolution No. 217 entitled: “Resolution relating to Health Care Revenue Bonds (Master Loan Program) of the Montana Facility Finance Authority; authorizing loans to the Authority for its Capital Reserve Account securing such Bonds and the execution and delivery of a tenth amendment to Capital Reserve Account Agreement.” On April 12, 2007, the MFFA Board approved issuing approximately \$29 million of bonds for financing the St. Luke Community Healthcare Network project, pending BOI approval of Resolution No. 217.

Loan Committee Chair Prothero presented Loan Committee recommendation for approval of Resolution No. 217 as presented; Member Englund seconded the motion and the motion was passed 7-0. Member Turcotte abstained.

MONTANA LOAN PROGRAMS

Commercial and Residential Portfolios Report

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

Infrastructure Loan Updates

Mr. Herb Kulow updated the Board on the DIRECTV loan that was approved by the Board. As of March 31, 2007 DIRECTV employed 1,016 full-time employees; 93% retention ratio compared to their budget projection of 60% retention. Eighty-four percent of the employee’s employed came from a low to moderate income job.

Mr. Kulow also updated the Board on the Zoot Enterprises loan that was approved by the Board. As of March 31, 2007 Zoot Enterprises employed 330 employees, 258 new jobs have been created since the loan was funded. The average salary, without benefits, is \$51,000.

QUARTERLY PERFORMANCE REPORTS

The Quarterly Performance Report for the period ending March 31, 2007 was presented.

INVESTMENT ACTIVITY

Retirement System Asset Allocation Report

Mr. Cliff Sheets presented the Retirement Systems Asset Allocation Report as of March 31, 2007.

Private Equity (MPEP)

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

<u>Fund Name</u>	<u>Vintage</u>	<u>Subclass</u>	<u>Amount</u>	<u>Date</u>
HarbourVest 2007 Direct Fund	2007	Co-Invest	\$20 M	4/10/2007
Lehman Brothers Merchant Banking IV, LP	2007	Buyout	\$15 M	3/19/07
MatlinPatterson Global Opportunities Partners III, LP	2007	Distressed	\$30 M	3/26/2007
MHR Institutional Partners Fund III LP	2007	Distressed	\$25 M	3/19/2007
Total New Commitments			\$90 M	

Real Estate (MTRP)

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

<u>Fund Name</u>	<u>Vintage</u>	<u>Subclass</u>	<u>Sector</u>	<u>Amount</u>	<u>Date</u>
Beacon Capital Strategic Partners V	2007	Opportunistic	Office	\$25 M	3/2/2007
CIM Group III	2007	Opportunistic	Urban Centers	\$25 M	3/2/2007
Liquid Realty Partners IV	2007	Opportunistic	Secondaries	\$30 M	3/2/2007
Rothschild Five Arrows Realty Securities V	2007	Value Added	Various	\$30 M	3/2/2007
Total New Commitments				\$110 M	

Domestic Equity (MDEP)

Mr. Cliff Sheets presented the Montana Domestic Equity Pool Report as of March 31, 2007 and a summary of the current investment strategy for the internally-managed portfolio as prepared by Rande Muffick, the Portfolio Manager.

Mid Cap Transition Summary

Mr. Cliff Sheets presented a report to the Board on the Small and Mid-Cap Transition. The search for non-large capitalization domestic equity managers began with the RFP issued in September 2006. The objective of the RFP was to add active managers in the Mid-Cap market segment, and diversify the Small Cap exposure by adding additional active managers.

The objective of the Mid-Cap transition was to transfer \$255 million to three active managers while maintaining exposure to the Mid-Cap equity markets. BGI was selected as the transition manager based on best execution and lower cost per trade. The transition trades were implemented on February 14, 2007 and the active mid cap managers assumed portfolio responsibility on February 22, 2007. The cost of the transition or "Total Implementation Shortfall" was -32bps or \$830,896. The main components were \$334,887 in transaction costs (commissions, taxes, spread and market impact) and \$496,009 in opportunity costs that reflect the tracking error or the security price variance between the original and target portfolios.

The \$95 million Small Cap transition was coordinated internally because the large number of relatively illiquid holdings in the legacy DFA Small Cap portfolio eliminated the cost advantage of using an outside transition manager. The objective was to gradually transition funds to the two active managers who could apply their trading expertise in constructing their active portfolios. Trades were coordinated so that market exposure was maintained on a daily basis. The transition required ten buy-sell transactions that took place over a six week time period with an average trade size of \$5 million for each of the two active portfolio managers. The process was completed on March 27, 2007.

Update on Large Cap US Equity Search

Mr. Cliff Sheets presented a report to the Board on the Large Cap US Equity Search. The RFP was issued on February 23, 2007. It encompassed large cap long-only style-based mandates (value and growth) and a partial long/short mandate. The partial long/short mandate is also referred to as "enhanced alpha," or 130/30. This strategy was discussed in detail at the February 2007 Board Meeting.

Staff received a total of 165 responses. Seventy-seven responses from long-only value money managers, seventy-five responses from long-only growth money managers and thirteen responses were received from money managers in the partial long/short category.

Staff and RVK completed the preliminary scoring on April 16 and 17, 2007. The result was the selection of six semi-finalists in each category - long-only value, long-only growth, and partial long/short. The semi-finalist interviews were held on April 30 and May 1, 2007 by conference call. Twelve finalists were selected, 3 – Value Managers, 4 – Growth Managers, and 5 – 130/30 Managers. The finalist interviews will be in-person, in Seattle on May 21 & 22, 2007. Staff intends to make the final selection by the end of that week. Once the final selections have been made, staff will begin the contract phase which will likely take at least a month. Thus, any actual transitions to any of the new managers are not expected before late July or August.

In summary, the RFP process is moving along to the final stage. We have a good group to choose from in making the final selections. Thanks to RV Kuhns staff and Geri Burton who have helped filter and organize the manager information and keep the process on schedule.

International Equity (MTIP)

Mr. Cliff Sheets presented the Montana International Equity Pool Report for the period ending March 31, 2007.

Fixed Income

Mr. Cliff Sheets presented the Fixed Income Overview and Strategy, the Below Investment Grade Holdings Report, the Short-Term Investment Pool, State Fund Insurance and Treasurer's Fund Portfolio Reports as prepared by the respective portfolio managers, Mr. Bob Bugni and Mr. Richard Cooley. No Board action is required on these items.

Investment Policy Statements

Mr. Cliff Sheets presented three Investment Policy Statements which have been modified as outlined below. The changes are presented for approval by the Board.

Short-Term Investment Pool (STIP) – The benchmark was changed from a return index based on three month Treasury Bill returns (T-Bill return X 1.05) to a one month LIBOR return index. This LIBOR index better represents the type of securities being used in the portfolio, primarily commercial paper, and is a common proxy for private market lending rates as opposed to US government short term borrowing rates. Further, the policy now adds a peer group measure, the iMoneynet First Tier Institutional (gross of fees) index. This is a series that captures the returns of institutional money market funds with similar top-tier quality restrictions as STIP.

Noxious Weed Management Trust Fund – This account is a Constitutional Trust which implies a degree of permanency that should minimize liquidity needs. Previously the account held a ladder of bonds maturing over 1 – 5 years. The policy now contemplates the use of the Trust Funds Bond Pool in lieu of direct holdings. The individual bond holdings will be transitioned into this pool as they mature over time.

Group Benefits – This account is the reserve for the State self-insured employees' health insurance plan. The account balances have increased over the past several years which enable the account to assume more interest rate risk. Accordingly, the maximum maturity is being increased from two years to five years. The minimum STIP balance is being set at \$10 million to assure a certain amount of liquidity. The fixed income holdings are limited to a maximum exposure per non-government credit of 3%, and bonds must be rated at least A- or A1.

Member Jack Prothero motioned for approval of the changes as presented; Member Paull seconded the motion and the motion was passed 8-0.

NEXT MEETING

The next regularly scheduled meeting of the Board will be August 21 & 22, 2007 in Bozeman, MT.

ADJOURNMENT

There being no further business, the meeting was adjourned at 11:15 a.m.

BOARD OF INVESTMENTS

APPROVE: _____
Terry Moore, Chairman

ATTEST: _____
Carroll South, Executive Director

DATE: _____