

Legislative Audit Division

State of Montana



Report to the Legislature

December 2003

Financial Audit

For the Fiscal Year Ended June 30, 2003

Board of Investments

Department of Commerce

This is our annual financial audit report on the Board of Investments (board) for the fiscal year ending June 30, 2003. The objectives of our financial audit included determining if the board's financial statements presented fairly its financial position and results of operations at and for the period ending June 30, 2003, with comparative totals at and for the period ending June 30, 2002. We issued unqualified opinions on the financial statements of the Board of Investments' Retirement Funds Bond Pool, Trust Funds Bond Pool, Short Term Investment Pool, Montana Domestic Equity Pool, Montana International Equity Pool, Montana Private Equity Pool, All Other Funds, and Enterprise Fund.

This report contains no recommendations.

Direct comments/inquiries to:
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Room 160, State Capitol
PO Box 201705
Helena MT 59620-1705

03-03

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FINANCIAL AUDITS

Financial audits are conducted by the Legislative Audit Division to determine if the financial statements included in this report are presented fairly and the agency has complied with laws and regulations having a direct and material effect on the financial statements. In performing the audit work, the audit staff uses standards set forth by the American Institute of Certified Public Accountants and the United States General Accounting Office. Financial audit staff members hold degrees with an emphasis in accounting. Most staff members hold Certified Public Accountant (CPA) certificates.

Government Auditing Standards, the Single Audit Act Amendments of 1996 and OMB Circular A-133 require the auditor to issue certain financial, internal control, and compliance reports. This individual agency audit report is not intended to comply with these requirements and is therefore not intended for distribution to federal grantor agencies. The Legislative Audit Division issues a statewide biennial Single Audit Report which complies with the above reporting requirements. The Single Audit Report for the two fiscal years ended June 30, 2003, will be issued by March 31, 2004. The Single Audit Report for the two fiscal years ended June 30, 2001, was issued on March 26, 2002. Copies of the Single Audit Report can be obtained by contacting:

Single Audit Coordinator
Office of Budget and Program Planning
State Capitol
Helena MT 59620
Phone (406) 444-3616

Legislative Audit Division
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John W. Northey, Legal Counsel



Deputy Legislative Auditors:
Jim Pellegrini, Performance Audit
Tori Hunthausen, IS Audit & Operations
James Gillett, Financial-Compliance Audit

December 2003

The Legislative Audit Committee
of the Montana State Legislature:

This is our financial audit report on the Board of Investments (board) for the fiscal year ending June 30, 2003. We performed this annual audit of the Board of Investments in compliance with Article VIII, section 13 of the Montana Constitution, and section 17-6-321, MCA. The objectives of our financial audit included determining if the board's financial statements presented fairly its financial position and results of operations at and for the period ending June 30, 2003, with comparative totals at and for the period ending June 30, 2002, and the board's compliance with laws and regulations which have a material and direct impact on the financial statements.

The Board of Investments, originally created in 1971, is attached to the Department of Commerce for administrative purposes. The board employs an executive director and an investment officer who in turn hire and manage board staff. The staff members advise the board, implement its decisions, and perform daily investment, economic development, and record keeping functions. Included in this report is a list of the members of the Board of Investments and Administrative Officials of the Board of Investments (page i).

This report contains unqualified Independent Auditor's Reports for each of the following eight sets of financial statements of the Board of Investments (page A-1): Retirement Funds Bond Pool, Trust Funds Bond Pool, Short Term Investment Pool, Montana Domestic Equity Pool, Montana International Equity Pool, Montana Private Equity Pool, All Other Funds, and Enterprise Fund. The Independent Auditor's Reports cover two fiscal years because the board presents two fiscal years in the financial statements for comparative purposes. The board's response to this report is on page C-1.

This report does not contain any recommendations to the board. The prior financial-compliance audit report, issued for fiscal year 2001-02, contained two recommendations to the board. We determined the board has implemented both recommendations contained in the prior audit report.

We thank the members of the Board of Investments and their staff for their cooperation and assistance during the audit.

Respectfully submitted,

Signature on File

Scott A. Seacat
Legislative Auditor

Appointed and Administrative Officials

Montana Board of Investments			<u>Term Expires</u>
	Richard Anderson, Chairman	Helena	1/2005
	Dennis Beams	Kalispell	1/2005
	Karen Fagg	Billings	1/2007
	Maureen Fleming	Missoula	1/2007
	Jay Klawon	Hamilton	1/2005
	Joel T. Long	Billings	1/2005
	Terry Moore	Billings	1/2007
	Tim Ryan	Bozeman	1/2005
	Calvin Wilson	Busby	1/2007

**Administrative Officials
Board of Investments
Department of Commerce**

Carroll South	Executive Director
Geri Burton	Deputy Director
James R. Penner	Chief Investment Officer
Gayle L. Moon	Accounting Fiscal Manager

For further information on the Montana Board of Investments contact Carroll South, Executive Director, at:

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e-mail: csouth@state.mt.us

Members of the audit staff involved in this audit were Geri Hoffman, Emlyn Neuman-Javornik, Hollie Koehler, and Jim Manning.

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LEGISLATIVE AUDIT DIVISION

Scott A. Seacat, Legislative Auditor
John W. Northey, Legal Counsel



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Jim Pellegrini, Performance Audit
Tori Hunthausen, IS Audit & Operations
James Gillett, Financial-Compliance Audit

INDEPENDENT AUDITOR'S REPORT

The Legislative Audit Committee
of the Montana State Legislature:

We have audited the accompanying Statement of Net Asset Value for the state of Montana Board of Investments, Retirement Funds Bond Pool, as of June 30, 2003 and 2002, and the related Statement of Changes in Net Asset Value and Statement of Investment Income and Distribution for the fiscal years then ended. These financial statements are the responsibility of the Board of Investments' management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the net asset value of the state of Montana Board of Investments, Retirement Funds Bond Pool, as of June 30, 2003 and 2002, and its changes in net asset value and investment income and distribution for the fiscal years then ended in conformity with accounting principles generally accepted in the United States of America.

Respectfully submitted,

Signature on File

James Gillett, CPA
Deputy Legislative Auditor

November 4, 2003

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**STATE OF MONTANA BOARD OF INVESTMENTS
RETIREMENT FUNDS BOND POOL FINANCIAL STATEMENTS**

STATEMENT OF NET ASSET VALUE JUNE 30, 2003 AND 2002

<u>Assets</u>	<u>2003</u>	<u>2002</u>
Cash	\$ 9,519,570	\$ 0
Security lending cash collateral (Notes 3 and 4)	82,134,484	171,445,667
Interest receivable	23,193,652	29,425,818
Investments managed at fair value (amortized cost of \$1,424,315,436 in 2003 and \$1,654,643,910 in 2002)(Notes 2 and 4)	<u>1,588,980,615</u>	<u>1,706,799,803</u>
Total assets	\$ <u>1,703,828,321</u>	\$ <u>1,907,671,288</u>
 <u>Liabilities</u>		
Income due participants (Note 2)	9,800,159	10,898,107
Security lending obligations (Notes 3 and 4)	82,134,484	171,445,667
Security lending expense payable	<u>87,402</u>	<u>230,520</u>
Total liabilities	<u>92,022,045</u>	<u>182,574,294</u>
Net asset value	\$ <u>1,611,806,276</u>	\$ <u>1,725,096,994</u>
Units Outstanding (Note 2)	14,541,546	16,657,667
Unit Value (Note 2)	\$ 110.84	\$ 103.56

**STATEMENT OF CHANGES IN NET ASSET VALUE
FOR THE FISCAL YEARS ENDED JUNE 30, 2003 AND 2002**

Net asset value, beginning of year	\$ 1,725,096,994	\$ 1,870,763,061
Value of units purchased by participants	0	300,000
Value of units sold by participants	(213,482,974)	(169,196,158)
Changes in fair value of investments managed	<u>100,192,256</u>	<u>23,230,091</u>
Net asset value, end of year	\$ <u>1,611,806,276</u>	\$ <u>1,725,096,994</u>

**STATEMENT OF INVESTMENT INCOME AND DISTRIBUTION
FOR THE FISCAL YEARS ENDED JUNE 30, 2003 AND 2002**

Investment income (Note 2)	\$ 132,188,754	\$ 128,622,973
Security lending income	1,825,473	4,973,512
Security lending expense	(1,653,821)	(4,454,025)
Administrative expenses	(262,848)	(297,444)
Income due participants, beginning of year	<u>10,898,107</u>	<u>12,818,352</u>
Income available for distribution	142,995,665	141,663,368
Distribution	<u>133,195,506</u>	<u>130,765,261</u>
Income due participants, end of year (Note 2)	\$ <u>9,800,159</u>	\$ <u>10,898,107</u>

The accompanying notes are an integral part of these financial statements.

**STATE OF MONTANA BOARD OF INVESTMENTS
RETIREMENT FUNDS BOND POOL**

**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2003 AND 2002**

1. HISTORY AND ORGANIZATION

The Board was created by an act of the Legislature to invest and manage the State of Montana's investment funds on a centralized basis. The Retirement Funds Bond Pool (RFBP) was created by the Board to allow qualifying funds, per section 17-6-201, MCA, to participate in a diversified pool. The RFBP was created on April 1, 1995, by the transfer of all fixed income and variable-rate securities owned by the Public Employees', Municipal Police Officers', Game Wardens', Sheriffs', Judges', Highway Patrol Officers', Teachers', Volunteer Firefighters' and Firefighters' Unified retirement funds.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Investments

RFBP investments are purchased in accordance with the statutorily mandated "Prudent Expert Principle". The RFBP portfolio includes corporate asset-backed, other corporate, U.S. government mortgage-backed, government, Yankee securities and cash investments. Corporate asset-backed securities represent debt securities collateralized by a pool of assets. U.S. government mortgage-backed securities reflect participation in a pool of residential mortgages. Government securities include direct and indirect obligations of the U.S. Treasury and state and local government bonds. Yankee bonds are U.S. dollar denominated bonds issued by foreign corporations and governments and U.S. companies issuing debt in foreign markets.

The RFBP portfolio includes structured financial instruments known as REMICs (Real Estate Mortgage Investment Conduits). REMICs are pass-through vehicles for multiclass mortgage-backed securities. Some RFBP REMICs are interest-only strips (IOs). Strip investments represent the separate purchase of the principal and interest cash flows of a mortgage security. IOs receive cash flow from the interest payment component on underlying mortgage loans. These securities, purchased for portfolio diversification and a competitive rate of return, are identified and reported as government mortgage-backed securities in the investment risk and portfolio disclosures. (See Note 4 on Investment Risk Categories and Note 6 for the Year End Portfolio.)

RFBP fixed income securities pay a fixed rate of interest until maturity while the variable-rate (floating-rate) securities pay a variable interest rate until maturity. The variable-rate securities float with LIBOR (London Interbank Offered Rate) or the weighted average of the net mortgage interest rates for the mortgage loan group. The three variable-rate securities, with a total amortized cost of \$450,000 and \$700,000, respectively, as of June 30, 2003 and 2002, are identified and reported as government mortgage-backed securities in the investment risk and portfolio disclosures. (See Note 4 on Investment Risk Categories and Note 6 for the Year End Portfolio.)

The RFBP, as an internal investment pool, invests its excess cash in the Board's Short Term Investment Pool, STIP, an external investment pool. An external investment pool commingles the moneys of more than one legally separate entity and invests, on the participants' behalf, in an investment portfolio. STIP participants include both state agencies and local governments. By meeting certain conditions, STIP, as a 2a7-like pool, is allowed to use amortized cost rather than fair value to report net assets to compute unit values.

Investments are presented in the Statement of Net Asset Value at fair value. Fair values are determined primarily by reference to market prices supplied to the Board by the Board's custodial bank, State Street Bank. Amortized cost, parenthetically disclosed, represents the original cost, adjusted for premium and discount amortization where applicable. Premiums and discounts are amortized/accreted using the straight-line or scientific method to the call, average life or maturity date of the securities. Amortized cost may also be referred to as book value.

Participant Units

The Public Employees', Municipal Police Officers', Game Wardens', Sheriffs', Judges', Highway Patrol Officers', Teachers', Volunteer Firefighters' and Firefighters' Unified retirement funds transferred all fixed income and variable-rate securities, at amortized cost, into the RFBP at the start-up date and were issued units according to the market value of each participant's portfolio. The initial unit value as of April 1, 1995, was \$100.00. Unit values thereafter are calculated weekly and at month end, based on portfolio pricing, to allow for participant transactions to occur as determined by the investment staff.

The June 30, 2003 unit value of \$110.84 increased from a June 30, 2002 unit value of \$103.56. Interest rates declined during the fiscal year by over one percent, which has the effect of increasing bond prices and the pool unit value. A one percent (1%) change in interest rates is expected to have a five to seven percent (5%-7%) inverse change in the unit value. RFBP investments are considered long-term in nature.

The Value of Units Sold by Participants of \$213.5 million for fiscal year 2003, as compared to \$169.2 million for fiscal year 2002 reflects the pension funds' portfolio rebalancing. RFBP units were sold to adjust the pension funds' portfolio towards the stated equity/fixed income asset allocation.

Broker Receivable/Payable

RFBP security transactions are recorded as of the trade date rather than the settlement date. Because of this generally accepted practice, the RFBP portfolio at June 30 may include receivables from brokers for securities sold, but not delivered, and payables to brokers for securities purchased, but not received.

Other

Accumulated income, recorded as Income Due Participants, is distributed monthly on the first calendar day of each month. Realized portfolio gains/losses are distributed at least annually to the participants.

Investment income reported in the Statement of Investment Income and Distribution includes interest accruals, realized gains/losses, amortization/accretion and miscellaneous income.

Administrative expenses incurred by the Board are charged daily to RFBP based on the Board's expenses applicable to RFBP. These expenses include costs for the custodial bank contract.

3. SECURITIES LENDING

Under the provisions of state statutes, the Board has, via a Securities Lending Authorization Agreement, authorized the custodial bank, State Street Bank and Trust, to lend the Board's securities to broker-dealers and other entities with a simultaneous agreement to return the collateral for the same securities in the future. During the period the securities are on loan, the Board receives a fee and the custodial bank must initially receive collateral equal to 102 percent of the fair value of the loaned securities and maintain collateral equal to not less than 100 percent of the fair value of the loaned security. The Board retains all rights and risks of ownership during the loan period.

During fiscal years 2003 and 2002, State Street lent, on behalf of the Board, certain securities held by State Street, as custodian, and received US dollar currency cash, US government securities, and irrevocable bank letters of credit. State Street does not have the ability to pledge or sell collateral securities unless the borrower defaults.

The Board did not impose any restrictions during fiscal years 2003 and 2002 on the amount of the loans that State Street made on its behalf. There were no failures by any borrowers to return loaned securities or pay distributions thereon during fiscal years 2003 and 2002. Moreover, there were no losses during fiscal years 2003 and 2002 resulting from a default of the borrowers or State Street.

During fiscal years 2003 and 2002, the Board and the borrowers maintained the right to terminate all securities lending transactions on demand. The cash collateral received on each loan was invested, together with the cash collateral of other qualified plan lenders, in a collective investment pool, the Securities Lending Quality Trust. The relationship between the average maturities of the investment pool and the Board's loans was affected by the maturities of the loans made by other plan entities that invested cash collateral in the collective investment pool, which the Board could not determine. On June 30, 2003 and June 30, 2002, the Board had no credit risk exposure to borrowers.

As of June 30, 2003, the carrying and fair values of the underlying securities on loan for the RFBP were \$63,891,788 and \$79,703,155 respectively. Cash collateral provided for the securities on loan totaled \$82,134,484.

As of June 30, 2002, the carrying and fair values of the underlying securities on loan for the RFBP were \$149,118,626 and \$165,121,529 respectively. Cash collateral provided for the securities on loan totaled \$171,445,667.

4. INVESTMENT RISK CATEGORIES

State of Montana investments are categorized below to give an indication of the level of risk assumed at June 30, 2003 and June 30, 2002. Category 1 includes investments that are insured or registered, or securities that are held by the Board or its agent in the Board's name. Not Categorized includes investments held by broker-dealers under securities loans with cash collateral.

Risk as of June 30, 2003

Category 1

<u>Security Investment Type</u>	<u>Securities Not On Loan</u>	<u>On Loan for Securities Collateral*</u>	<u>Not Categorized*</u>	<u>Carrying Amount</u>	<u>Fair Value</u>
Corporate Asset-Backed	\$ 10,000,000	\$ 0	\$ 0	\$ 10,000,000	\$ 10,000,000
Corporate Other	839,198,080	0	9,277,647	848,475,727	930,781,145
US Govt Mortgage-Backed	74,506,361	0	0	74,506,361	77,402,316
US Govt Direct/Indirect	326,000,808	0	53,620,070	379,620,878	449,442,686
Yankee Bonds	81,281,490	0	994,070	82,275,560	91,917,558
STIP	<u>29,436,910</u>	<u>0</u>	<u>0</u>	<u>29,436,910</u>	<u>29,436,910</u>
Total Investments	\$ 1,360,423,649	\$ 0	\$ 63,891,787	\$ 1,424,315,436	\$ 1,588,980,615
Securities Lending Collateral Investment Pool			\$ 82,134,484	\$ 82,134,484	\$ 82,134,484

*At June 30, 2003, these underlying securities with fair values of \$79,703,155 were loaned for cash collateral under a security lending agreement with the state's agent.

Risk as of June 30, 2002

Category 1

<u>Security Investment Type</u>	<u>Securities Not On Loan</u>	<u>On Loan for Securities Collateral*</u>	<u>Not Categorized*</u>	<u>Carrying Amount</u>	<u>Fair Value</u>
Corporate Asset-Backed	\$ 1,357,024	\$ 0	\$ 0	\$ 1,357,024	\$ 1,412,007
Corporate Other	1,094,406,725	0	8,963,955	1,103,370,680	1,109,175,400
US Govt Mortgage-Backed	60,869,572	0	0	60,869,572	63,326,005
US Govt Direct/Indirect	251,439,508	0	140,149,698	391,589,206	433,207,799
Yankee Bonds	88,899,073	0	4,973	88,904,046	91,125,210
State/Local Government	1,130,000	0	0	1,130,000	1,130,000
STIP	<u>7,423,382</u>	<u>0</u>	<u>0</u>	<u>7,423,382</u>	<u>7,423,382</u>
Total Investments	\$ 1,505,525,284	\$ 0	\$ 149,118,626	\$ 1,654,643,910	\$ 1,706,799,803
Securities Lending Collateral Investment Pool			\$ 171,445,667	\$ 171,445,667	\$ 171,445,667

*At June 30, 2002, these underlying securities with fair values of \$165,121,529 were loaned for cash collateral under a security lending agreement with the state's agent.

With the exception of the US government securities, the above instruments have credit risk as measured by major credit rating services. Credit risk is defined as the risk that the issuer of a fixed income security may default in making timely principal and interest payments. The Board of Investment's policy requires RFBP investments, at the time of purchase, to be rated investment grade as defined by Moody's or Standard & Poor's (S&P) rating services. The US government securities are guaranteed directly or indirectly by the US government.

Market risk for the above securities is caused by changes in the price or principal value of the security due to changes in interest rates and market liquidity.

As reported in the government mortgage-backed category, the RFBP portfolio holds REMICs totaling \$1,703,480 and \$2,503,357 in amortized cost, respectively, as of June 30, 2003 and June 30, 2002. These securities are based on separate or combined cash flows from principal and interest payments on underlying mortgages. The IOs are more sensitive to prepayments by mortgagors resulting from interest rate changes than other REMIC securities.

The IO REMIC securities purchased in August and September 1992 are being reduced periodically towards zero according to the expected average life of the underlying mortgages. The IO securities amortized cost is \$450,000 as of June 30, 2003 and \$700,000 as of June 30, 2002.

Corporate asset-backed securities represent debt securities collateralized by a pool of assets. The RFBP corporate asset-backed security is secured by lease payments and real estate. Credit risk for corporate asset backed securities is generally less than other corporate securities because assets are held by a third party.

As of June 30, 2003 and June 30, 2002, Enron Corp., and Burlington Industries, Inc. presented legal and higher credit risks to the Board.

The RFBP holds a \$7 million par 6.40% Enron bond maturing July 15, 2006 and a \$7 million par 6.95% Enron bond maturing July 15, 2028. The combined book value of these securities was \$13,582,030 as of November 30, 2001. On December 12, 2001, the Enron Corp. filed for Chapter 11 bankruptcy protection. Accordingly, the November 2001 book value for the two issues was reduced to \$5.6 million as of June 30, 2002. In October 2002, the book value was reduced to \$2.8 million for both issues. In July 2003, both issues were sold, on the market, for a total of \$2.36 million.

The Board owns a Burlington Industries, Inc., \$6 million par, 7.25% bond maturing September 15, 2005. In September 2000, the company announced a reduction of stockholders equity. Due to an increasing senior bank line and declining credit trend, the bond ratings for this issue were downgraded, in May 2001, by the Moody's and Standard & Poor's rating agencies. During fiscal year 2001, the book value of Burlington Industries Inc. was reduced from the August 31, 2000 book value of \$5,609,640 to \$2,400,000. Due to the company's filing for Chapter 11 bankruptcy protection on November 11, 2001, the book value was reduced to \$1,200,000. In October 2003, Burlington Industries, Inc. received court approval to sell its assets. This sale is expected to close in November 2003. Under the company's recovery plan, the Board will receive cash for its unsecured claim.

As of June 30, 2002, Rite Aid and WorldCom Inc. presented a higher credit risk to the Board.

The RFBP owned a Rite Aid \$7,000,000 par, 7.13% bond maturing January 15, 2007. In May 2000, the Board was subordinated to a secured bank line of credit on this issue and the bond ratings were downgraded by the Moody's and Standard & Poor's bond ratings agencies. Based on this subordination and ratings downgrade, the book value was reduced to \$5,600,000 as of June 30, 2000. During fiscal year 2001, the book value was further reduced to \$5,220,172. Due to an improving credit trend, amortization was resumed in June 2001. The book value of this security at June 30, 2002 was \$5,541,139. As of June 30, 2002, Rite Aid did not represent a credit risk. In December 2002, this bond was sold, on the market, for \$5,057,500 principal plus interest of \$206,427.

The RFBP portfolio included a \$6,000,000 par, 6.95% WorldCom Inc. bond maturing August 15, 2028. The book value of this bond, originally purchased at a discount, was \$5,477,400 on June 30, 2002. On July 21, 2002, WorldCom Inc. filed for Chapter 11 bankruptcy protection. As of July 31, 2002, the reduced book value was \$2,400,000. On November 7, 2002, the Attorney General for the State of Montana filed a lawsuit against certain WorldCom executives, directors and financial institutions associated with WorldCom such as Arthur Andersen and CitiGroup. The lawsuit, filed in Lewis and Clark County, Montana, alleges that the defendants filed "false and misleading registration statements" relating to the purchase of the bonds by the Montana Board of Investments. In December 2002, this bond was sold, on the market, for \$1.5 million.

5. DEUTSCHE BANK SECURITIES, INC. COMPLAINT

The Board received a summons and complaint, dated September 3, 2002, regarding the sale of a Pennzoil Quaker State, \$5 million par, 6.75% corporate bond maturing April 1, 2009. Deutsche Bank Securities claims a "breach of contract" for the March 25, 2002 sale of the bond at a price of \$94.669 plus accrued interest. Deutsche Bank Securities seeks damages of \$538,632 for the additional costs incurred to acquire the bond from third parties, plus any statutory interest, costs and expenses. On October 1, 2002, Shell Oil Company acquired Pennzoil and subsequently announced a public tender of Pennzoil Quaker State debt. The Board tendered the Pennzoil Quaker State holdings on October 8, 2002 at a price of \$113.099. The tender was accepted with a settlement date of November 1, 2002. On November 4, 2002, the Board received \$5,683,075 in principal and interest plus \$150,000 as a consent fee.

6. YEAR END PORTFOLIO

The June 30, 2003 RFBP portfolio is listed below. The security type percentage is based on the fair value ratio of the specific security investment type to the total portfolio.

<u>Security Name</u>	<u>Coupon</u>	<u>Maturity</u>	<u>Par</u>	<u>Book Value</u>	<u>Fair Value</u>	<u>% of Total</u>
AERO 1 HQ FIN TRUST	4.640	07/07/10	10,000,000	10,000,000	10,000,000	0.63%
Corporate Asset-Backed	1 Issue(s)		10,000,000	10,000,000	10,000,000	0.63%
AMERICA WEST AIRLINES EQUIPMENT TRUST	7.930	01/02/19	5,320,432	5,320,432	5,641,998	0.35%
AMERICAN AIRLINES 1991 EQUIPMENT TRUST	10.180	01/02/13	5,000,000	4,998,054	2,625,000	0.16%
AMERICAN AIRLINE EQUIPMENT TRUST	6.977	05/23/21	9,757,681	9,734,224	8,001,299	0.50%
AMERICAN TRANS AIR EQUIPMENT TRUST	8.039	07/15/17	11,660,741	11,660,741	12,379,720	0.77%
ARCHER DANIELS MIDLAND CO	10.250	01/15/06	3,500,000	3,497,230	4,206,077	0.26%
ASHLAND OIL CO	8.800	11/15/12	7,500,000	7,669,828	9,442,650	0.59%
ATCHISON TOPEKA + SANTA FE RY	6.550	01/06/13	7,475,000	7,475,000	8,617,844	0.54%
BANK ONE TEXAS	6.250	02/15/08	4,000,000	3,848,798	4,589,367	0.29%
BANKBOSTON NA	6.375	03/25/08	4,000,000	3,857,894	4,557,422	0.29%
BORDEN INC	9.250	06/15/19	5,500,000	5,339,560	3,575,000	0.22%
BORG WARNER AUTOMOTIVE INC	7.000	11/01/06	5,000,000	5,009,073	5,618,420	0.35%
BURLINGTON INDUSTRIES INC	7.250	09/15/05	6,000,000	1,200,000	2,520,000	0.16%
BURLINGTON NORTHN RR CO	7.970	01/01/15	3,901,688	3,901,688	4,820,659	0.30%
BURLINGTON NORTHN RR CO	6.940	01/02/14	3,748,199	3,748,199	4,493,457	0.28%
CNA FINL CORP	6.250	11/15/03	5,000,000	4,990,434	5,054,904	0.32%
CSX CORP	7.450	05/01/07	3,000,000	3,080,886	3,510,204	0.22%
CSX CORP	7.900	05/01/17	5,000,000	4,997,993	6,655,543	0.42%
CHAMPION INTERNATIONAL CORP	7.625	09/01/23	10,000,000	9,824,100	10,440,924	0.65%
CHAMPION INTERNATIONAL CORP	7.150	12/15/27	7,000,000	6,863,686	7,871,028	0.49%
CHICAGO + NORTH WESTERN RY	8.910	01/01/15	8,411,884	8,411,884	11,224,918	0.70%
CITIGROUP INC	7.875	05/15/25	6,000,000	6,115,269	7,851,025	0.49%
CITIGROUP INC	6.200	03/15/09	5,000,000	4,801,184	5,760,142	0.36%
CITICORP CAPITAL II	8.015	02/15/27	4,000,000	3,969,090	4,706,985	0.29%
CLEVELAND ELEC ILLUM CO	9.000	07/01/23	3,000,000	2,985,373	3,139,039	0.20%
CONTINENTAL AIRLINES EQUIPMENT TRUST	6.545	02/02/19	6,968,407	6,968,407	6,585,144	0.41%
CORPORATE PROPERTY INVS	7.750	08/15/04	5,000,000	5,016,454	5,292,636	0.33%
CORPORATE PROPERTY INVS	7.875	03/15/16	12,000,000	12,056,487	14,685,766	0.92%
DAYTON HUDSON CORP	7.650	08/01/23	1,500,000	1,504,596	1,564,902	0.10%
DEER PARK REFINING L P	6.470	12/15/08	5,747,700	5,685,976	6,494,115	0.41%
DELTA AIR LINES INC EQUIPMENT TRUST	10.140	08/14/12	2,000,000	2,000,000	1,550,000	0.10%
DELTA AIR LINES INC EQUIPMENT TRUST	10.140	08/14/12	4,000,000	3,986,170	3,100,000	0.19%
DELTA AIR LINES INC EQUIPMENT TRUST	10.000	06/05/11	1,971,000	1,956,080	1,527,525	0.10%
DELTA AIR LINES INC EQUIPMENT TRUST	10.000	06/05/13	3,000,000	3,000,000	1,200,000	0.08%
DILLARD DEPT STORES INC	7.750	07/15/26	2,000,000	1,982,546	1,795,000	0.11%
EL PASO NATURAL GAS CO	8.625	01/15/22	5,000,000	5,215,728	5,375,000	0.34%
ENRON CORP	6.400	07/15/06	7,000,000	1,400,000	1,347,500	0.08%
ENRON CORP	6.950	07/15/28	7,000,000	1,400,000	1,338,750	0.08%
ENSERCH CORP	7.125	06/15/05	5,000,000	5,026,211	5,368,758	0.34%
FMC CORP	6.375	09/01/03	8,000,000	7,998,799	8,020,000	0.50%
FIRST CHICAGO CORP	6.375	01/30/09	4,000,000	3,784,677	4,607,997	0.29%
FIRST INTERSTATE BANC SYSTEM MONTANA	7.500	10/01/06	11,620,000	11,620,000	11,620,000	0.73%
FIRST SECURITY CORP	6.875	11/15/06	6,000,000	5,982,752	6,876,818	0.43%
FIRST UNION CORP	7.050	08/01/05	5,000,000	5,018,666	5,521,324	0.35%
FIRST UNION BANK N C CHARLOTTE	5.800	12/01/08	6,000,000	5,635,902	6,767,097	0.42%
FLORIDA GAS TRANSMISSION CO	9.190	11/01/24	10,000,000	9,943,173	11,538,418	0.72%
FORD MOTOR CREDIT CO	6.750	05/15/05	5,000,000	4,992,793	5,272,852	0.33%
FORD MOTOR CREDIT CO	7.375	10/28/09	8,000,000	8,008,264	8,406,342	0.53%
GTE CORP	7.900	02/01/27	14,000,000	14,000,000	16,019,620	1.00%
GTE SOUTH INC	7.500	03/15/26	9,000,000	8,881,361	10,143,618	0.63%
GENERAL AMERICAN TRANSN EQUIPMENT TR	8.420	01/01/15	8,074,469	8,074,469	7,678,673	0.48%
GENERAL ELECTRIC CAPITAL CORP	8.125	05/15/12	5,000,000	5,254,175	6,439,407	0.40%
GENERAL MOTORS ACCEPTANCE CORP	0.000	12/01/12	25,000,000	13,761,459	13,048,025	0.82%
GENERAL MOTORS ACCEPTANCE CORP	6.125	08/28/07	5,000,000	5,016,147	5,210,905	0.33%
GENERAL RE CORP	0.000	07/30/37	375,723,766	22,931,763	23,264,816	1.46%
GEORGIA PACIFIC CORP	9.125	07/01/22	3,000,000	2,947,019	2,846,250	0.18%

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GEORGIA PACIFIC CORP	8.250	03/01/23	5,000,000	5,051,390	4,425,000	0.28%
GEORGIA PACIFIC CORP	8.625	04/30/25	3,000,000	3,151,293	2,730,000	0.17%
GEORGIA PACIFIC CORP	7.750	11/15/29	3,000,000	2,465,841	2,670,000	0.17%
GULF STATES UTILITIES CO	8.700	04/01/24	5,000,000	5,000,000	5,195,541	0.33%
ILLINOIS BELL TELEPHONE CO	6.625	02/01/25	2,000,000	1,796,058	2,078,544	0.13%
INTERNATIONAL PAPER CO	6.875	11/01/23	3,000,000	2,963,714	3,293,545	0.21%
JPM CAPITAL TRUST I	7.540	01/15/27	6,000,000	5,676,061	6,703,727	0.42%
KCT INTERMODAL TRANSPORTATION CORP	6.884	08/01/18	3,753,867	3,753,867	4,115,616	0.26%
K N ENERGY INC	6.650	03/01/05	3,000,000	3,018,967	3,211,962	0.20%
K N ENERGY INC	7.250	03/01/28	3,000,000	2,957,342	3,498,393	0.22%
KELLWOOD CO	7.625	10/15/17	12,000,000	11,810,194	11,580,000	0.72%
KERR MCGEE CORP	7.125	10/15/27	7,000,000	7,089,231	7,893,911	0.49%
KEYCORP	7.500	06/15/06	5,000,000	4,997,106	5,713,098	0.36%
LEHMAN BROTHERS HLDINGS INC	0.000	07/28/28	80,000,000	11,765,452	12,640,000	0.79%
MARSH + MCLENNAN COS INC	7.125	06/15/09	7,000,000	6,995,235	8,409,912	0.53%
MEAD CORP	7.350	03/01/17	11,000,000	10,991,606	13,469,784	0.84%
MED MAP LLC MONTANA	7.060	12/01/15	10,090,000	10,090,000	10,090,000	0.63%
MED MAP LLC MONTANA	7.000	06/01/21	6,325,000	6,325,000	6,325,000	0.40%
MERIDIAN TRAILER TRAIN	9.850	01/29/10	1,233,826	1,233,826	1,233,826	0.08%
MERIDIAN TRAILER TRAIN	9.850	01/29/08	1,270,340	1,270,340	1,270,340	0.08%
METROPOLITAN LIFE INSURANCE CO	7.450	11/01/23	10,000,000	9,834,554	10,553,979	0.66%
MILLENIUUM AMERICA INC	7.000	11/15/06	4,000,000	3,959,323	4,015,000	0.25%
MISSISSIPPI POWER + LIGHT CO	7.700	07/15/23	11,000,000	10,907,409	11,417,292	0.71%
MOBIL CORP	5.940	01/15/19	9,175,212	9,175,212	9,776,297	0.61%
MORGAN J P + CO INC	0.000	04/15/27	30,000,000	5,072,642	5,518,530	0.35%
NATIONWIDE FINANCIAL SERVICES INC	8.000	03/01/27	6,000,000	5,910,972	6,820,462	0.43%
NEW YORK LIFE INS CORP	7.500	12/15/23	5,000,000	4,799,418	5,314,722	0.33%
NEW YORK TEL CO	7.250	02/15/24	7,000,000	6,778,478	7,449,075	0.47%
NORAM ENERGY CORP	6.500	02/01/08	3,000,000	2,846,617	3,217,407	0.20%
NORFOLK SOUTHERN CORP	7.700	05/15/17	6,000,000	6,028,793	7,925,878	0.50%
NORTHWEST AIRLINES EQUIPMENT TRUST	6.810	08/01/21	10,602,981	10,177,661	10,496,951	0.66%
NORTHWEST AIRLINES EQUIPMENT TRUST	7.935	10/01/20	8,975,066	8,798,151	9,771,603	0.61%
OCCIDENTAL PETROLEUM CORP	7.200	04/01/28	13,000,000	12,850,132	15,729,767	0.98%
OCCIDENTAL PETROLEUM CORP	8.750	01/15/23	6,000,000	5,952,725	8,240,017	0.52%
OHIO POWER CO	7.300	04/01/24	4,000,000	3,700,717	4,318,169	0.27%
OLD REPUBLIC INTERNATIONAL CORP	7.000	06/15/07	5,000,000	4,998,929	5,809,485	0.36%
PPL MONTANA LLC	8.903	07/02/20	18,591,834	18,591,834	20,884,024	1.31%
PACIFIC BELL TEL CO	7.250	11/01/27	6,000,000	5,958,944	6,847,425	0.43%
PANHANDLE EASTERN CORP	8.625	04/15/25	5,000,000	5,078,987	5,632,007	0.35%
PANHANDLE EASTERN PIPE LINE CO	7.950	03/15/23	2,800,000	2,693,927	2,919,000	0.18%
PENNEY J C INC	9.750	06/15/21	3,788,000	3,788,000	3,944,255	0.25%
PENNEY J C INC	7.125	11/15/23	5,000,000	5,059,637	4,706,250	0.29%
PENNEY J C INC	7.650	08/15/16	2,000,000	1,960,601	1,937,500	0.12%
PHILLIPS PETROLEUM CO	7.125	03/15/28	11,000,000	10,843,577	12,455,141	0.78%
ST LOUIS SOUTHWESTERN RY CO	10.100	05/15/05	304,731	304,731	304,731	0.02%
SEARS ROEBUCK ACCEP CORP	7.500	10/15/27	10,000,000	10,080,567	11,084,306	0.69%
SECURITY CAP GROUP INC	7.700	06/15/28	3,000,000	3,548,969	3,652,647	0.23%
SHAWMUT BANK	8.625	02/15/05	5,000,000	5,076,582	5,531,552	0.35%
SONAT INC	7.000	02/01/18	3,000,000	2,999,668	2,490,000	0.16%
SOUTHERN UNION CO	7.600	02/01/24	10,000,000	9,873,583	10,135,414	0.63%
SOUTHWEST GAS CORP	7.500	08/01/06	6,000,000	6,088,245	6,606,503	0.41%
SOUTHWEST GAS CORP	8.375	02/15/11	6,000,000	5,983,767	6,993,878	0.44%
SOUTHWESTERN BELL TEL CO	7.250	07/15/25	7,000,000	7,124,640	7,231,162	0.45%
SOUTHWESTERN BELL TEL CO	7.000	11/15/27	3,000,000	2,996,637	3,337,258	0.21%
SUNAMERICA INC	8.125	04/28/23	13,000,000	13,018,547	17,089,310	1.07%
SUPER VALUE STORE	8.875	11/15/22	6,000,000	6,136,691	6,293,101	0.39%
SUPER VALUE INC	7.875	08/01/09	3,000,000	3,004,386	3,551,016	0.22%
TELE COMMUNICATIONS INC	7.875	08/01/13	3,000,000	2,868,374	3,646,527	0.23%
TENNECO PACKAGING INC	7.200	12/15/05	5,000,000	5,019,096	5,567,046	0.35%
TEXAS GAS TRANSMISSION CORP	7.250	07/15/27	3,000,000	2,759,456	3,407,938	0.21%
TEXAS UTILITIES ELEC CO	7.875	03/01/23	3,000,000	2,963,200	3,128,417	0.20%
TRANSCONTINENTAL GAS PIPE LINE	7.250	12/01/26	3,000,000	3,003,068	2,962,500	0.19%
TYSON FOODS INC	8.250	10/01/11	7,000,000	7,309,485	8,290,797	0.52%

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US BANK NA MINNEAPOLIS	6.500	02/01/08	5,000,000	4,999,334	5,811,060	0.36%
ULTRAMAR DIAMOND SHAMROCK CORP	7.200	10/15/17	3,000,000	2,980,189	2,913,827	0.18%
UNION CARBIDE CHEMS + PLASTICS	8.750	08/01/22	6,000,000	6,304,824	6,256,814	0.39%
UNION OIL CO CALIFORNIA	7.000	05/01/28	9,000,000	8,684,829	10,222,552	0.64%
UNION OIL CO CALIFORNIA	6.700	10/15/07	5,000,000	4,993,068	5,340,694	0.33%
UNION PACIFIC RR CO	7.750	07/01/12	5,509,068	5,509,068	6,837,860	0.43%
UNION PACIFIC RESOURCES GROUP INC	7.050	05/15/18	12,000,000	11,927,453	14,868,479	0.93%
UNION TANK CAR CO	7.125	02/01/07	6,000,000	5,997,698	6,942,166	0.43%
UNION TANK CAR CO	7.450	06/01/09	5,000,000	5,000,000	6,052,045	0.38%
UNITED AIRLINES EQUIPMENT TRUST	7.032	10/01/10	9,408,328	9,337,475	7,855,954	0.49%
WAL MART STORES INC PASS THRU TRUST	7.490	06/21/07	4,066,288	4,041,365	4,837,037	0.30%
WELLS FARGO + CO	6.875	04/01/06	7,000,000	6,908,637	7,913,557	0.50%
WESTERN PROPERTIES TRUST	7.875	02/15/04	7,000,000	6,998,724	7,242,150	0.45%
WESTERN PROPERTIES TRUST	7.200	09/15/08	3,000,000	2,907,601	3,451,566	0.22%
WESTINGHOUSE ELECTRIC CORP	8.625	08/01/12	8,000,000	8,216,552	10,742,816	0.67%
WESTVACO CORP	7.000	08/15/23	5,000,000	4,538,104	5,181,670	0.32%
WESTVACO CORP	7.650	03/15/27	9,000,000	8,963,440	10,608,519	0.66%
WEYERHAEUSER CO	8.500	01/15/25	7,000,000	7,303,011	8,923,716	0.56%
WILLAMETTE INDUSTRIES INC	7.000	02/01/18	4,000,000	3,976,419	4,765,104	0.30%
WILMINGTON TRUST TUSCON ELECTRIC	10.211	01/01/09	9,350,148	9,350,148	9,350,148	0.58%
WINN DIXIE TRUST	0.000	09/01/24	70,000,000	10,857,643	13,300,000	0.83%
Corporate Other	139 Issue(s)		1,384,625,655	848,475,727	930,781,145	58.23%
FEDERAL HOME LOAN POOL G10173	6.000	01/01/09	1,882,158	1,878,688	1,963,326	0.12%
FEDERAL HOME LOAN POOL G30006	7.000	07/01/13	1,268,997	1,277,333	1,349,605	0.08%
FEDERAL HOME LOAN MTG PC REMIC IO	8.313	08/15/07	2,569,916	150,000	205,073	0.01%
FEDERAL HOME LOAN MTG PC REMIC IO	8.313	09/15/07	1,823,626	100,000	151,699	0.01%
FEDERAL HOME LOAN POOL C01523	5.000	03/01/33	14,854,419	14,725,608	15,115,532	0.95%
FEDERAL HOME LOAN POOL E00247	5.500	10/01/08	2,564,752	2,557,530	2,678,363	0.17%
FEDERAL HOME LOAN POOL E00659	6.000	04/01/14	1,795,855	1,794,478	1,875,546	0.12%
FEDERAL HOME LOAN POOL E01376	4.000	04/01/18	29,585,712	29,347,231	29,860,921	1.87%
FEDERAL HOME LOAN MTG PC REMIC	9.300	11/15/20	291,098	283,170	290,728	0.02%
FEDERAL NATIONAL MTG ASSN REMIC IO	8.438	08/25/07	2,659,291	200,000	235,236	0.01%
FEDERAL NATIONAL MTG ASSN REMIC	9.500	03/25/20	983,344	970,310	1,094,475	0.07%
FNMA POOL 109031	6.695	08/01/05	122,492	121,748	128,588	0.01%
FNMA POOL 303365	6.500	05/01/09	4,247,868	4,196,758	4,496,932	0.28%
FNMA POOL 303125	7.500	01/01/10	1,242,881	1,239,320	1,331,484	0.08%
FNMA POOL 303202	6.500	05/01/14	1,878,460	1,861,854	1,987,250	0.12%
FNMA POOL 303590	7.000	11/01/10	1,276,825	1,276,825	1,361,963	0.09%
FNMA POOL 313999	6.000	02/01/13	2,550,964	2,538,743	2,676,917	0.17%
FNMA POOL 572220	6.000	03/01/16	3,543,650	3,533,798	3,707,544	0.23%
FNMA POOL 592327	5.500	06/01/16	6,420,569	6,274,876	6,684,916	0.42%
GNMA II POOL 001254	9.500	09/20/19	47,986	47,776	54,350	0.00%
GNMA POOL 046249	10.000	12/15/10	22,052	21,939	25,237	0.00%
GNMA POOL 135544	10.000	01/15/16	77,143	76,779	90,653	0.01%
GNMA POOL 237102	9.500	11/15/17	31,755	31,597	35,978	0.00%
Government-Mortgage Backed	23 Issue(s)		81,741,813	74,506,361	77,402,316	4.84%
ASTRO OFFSHORE CORP USGG XI	6.000	12/20/19	13,307,000	13,307,000	13,307,000	0.83%
CALLABLE ZERO CPN TRUST	0.000	11/01/25	35,000,000	6,903,176	7,289,450	0.46%
ENSCO OFFSHORE CO USGG XI	6.360	12/01/15	8,333,421	8,333,421	9,187,930	0.57%
FEDERAL HOME LOAN MORTGAGE CORP	3.250	06/18/18	15,000,000	14,926,334	14,707,305	0.92%
FEDERAL HOME LOAN MORTGAGE CORP	0.000	06/21/32	100,000,000	13,621,311	14,187,000	0.89%
FEDERAL HOME LOAN BANKS	6.395	06/03/14	4,000,000	3,719,805	4,763,198	0.30%
FEDERAL HOME LOAN BANKS	7.000	08/26/19	8,000,000	7,973,226	9,881,864	0.62%
FEDERAL HOME LOAN BANKS	7.450	02/03/20	15,000,000	15,101,792	19,368,870	1.21%
FEDERAL HOME LOAN MORTGAGE CORP	8.250	06/01/26	8,000,000	8,368,915	11,052,960	0.69%
FEDERAL HOME LOAN MORTGAGE CORP	0.000	06/05/28	150,000,000	27,804,015	32,268,150	2.02%
FEDERAL HOME LOAN MORTGAGE CORP	0.000	09/14/29	100,000,000	16,955,503	18,288,000	1.14%
FEDERAL NATIONAL MORTGAGE ASSN	6.000	05/15/08	30,000,000	29,363,766	34,589,556	2.16%
FEDERAL NATIONAL MORTGAGE ASSN	7.250	01/15/10	17,000,000	16,996,138	21,023,961	1.32%
FEDERAL NATIONAL MORTGAGE ASSN	7.125	01/15/30	20,000,000	21,494,085	25,967,004	1.62%
FEDERAL NATIONAL MORTGAGE ASSN	6.625	11/15/10	5,000,000	5,160,332	6,040,566	0.38%

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GLOBAL INDUSTRIES LTD USGG XI	7.710	02/15/25	8,800,000	8,800,000	8,800,000	0.55%
STUDENT LOAN MARKETING ASSN	0.000	05/15/14	150,000,000	52,996,229	72,090,900	4.51%
TUNISIA REPUBLIC USGG	6.710	02/01/24	4,000,000	3,796,504	4,000,000	0.25%
USGG SHIPPING + CENAC TOWING USGG XI	7.000	05/15/21	11,719,000	11,719,000	11,719,000	0.73%
U S ARMY HOSPITALITY FUND	7.467	05/01/32	14,860,000	14,860,000	14,860,000	0.93%
UNITED STATES TREASURY BOND STRIP	0.000	11/15/11	19,000,000	14,469,399	17,674,651	1.11%
UNITED STATES TREASURY BONDS	7.250	05/15/16	21,000,000	21,777,798	27,936,563	1.75%
UNITED STATES TREASURY BONDS	7.500	11/15/16	19,000,000	19,573,128	25,807,343	1.61%
VESSEL MGMT SVCS INC USGG XI	6.080	05/20/24	12,600,000	12,600,000	14,036,526	0.88%
VESSEL MGMT SVCS INC USGG XI	6.750	06/15/25	9,000,000	9,000,000	10,594,890	0.66%
Government Direct-Indirect	25 Issue(s)		798,619,421	379,620,878	449,442,686	28.12%
AMERICAN PRESIDENT COS LTD	7.125	11/15/03	9,000,000	8,997,533	8,730,000	0.55%
AMERICAN PRESIDENT COS LTD	8.000	01/15/24	5,000,000	4,724,802	3,500,000	0.22%
CANADIAN NATIONAL RAILWAY CO	6.800	07/15/18	6,000,000	5,964,421	6,831,116	0.43%
CANADIAN PACIFIC LTD	9.450	08/01/21	5,000,000	5,148,870	7,291,402	0.46%
EASTERN ENERGY LTD	7.250	12/01/16	5,000,000	4,939,669	6,407,860	0.40%
EQUITABLE LIFE ASSUR SOC U S A	6.950	12/01/05	5,000,000	4,959,246	5,529,694	0.35%
GREAT LAKES POWER INC	9.000	08/01/04	5,000,000	4,997,456	5,341,167	0.33%
HOUSEHOLD FINANCE CORP	6.875	03/01/07	4,000,000	3,948,841	4,605,787	0.29%
HOUSEHOLD FINANCE CORP	6.500	11/15/08	5,000,000	4,832,347	5,792,618	0.36%
IBP FINANCIAL CO CANADA	7.450	06/01/07	3,000,000	2,999,188	3,255,000	0.20%
MACMILLAN BLOEDEL LTD	7.700	02/15/26	10,000,000	9,826,022	11,812,719	0.74%
PANAMERICAN BEVERAGES INC	7.250	07/01/09	6,000,000	5,964,548	6,720,000	0.42%
PHILIPS ELECTRONICS NV	7.750	04/15/04	5,000,000	4,988,182	5,242,630	0.33%
TRANSCANADA PIPELINES LTD	8.500	03/20/23	5,000,000	5,152,866	5,232,567	0.33%
UNITED MEXICAN STATES	8.000	09/24/22	5,000,000	4,831,569	5,625,000	0.35%
Yankee Bonds	15 Issue(s)		83,000,000	82,275,560	91,917,558	5.75%
SHORT TERM INVESTMENT POOL (STIP)			29,436,910	29,436,910	29,436,910	1.84%
Cash Equivalents	1 Issue(s)		29,436,910	29,436,910	29,436,910	2.44%
RFBP Total	204 Issue(s)		2,387,423,799	1,424,315,436	1,588,980,615	100.00%

LEGISLATIVE AUDIT DIVISION

Scott A. Seacat, Legislative Auditor
John W. Northey, Legal Counsel



Deputy Legislative Auditors:
Jim Pellegrini, Performance Audit
Tori Hunthausen, IS Audit & Operations
James Gillett, Financial-Compliance Audit

INDEPENDENT AUDITOR'S REPORT

The Legislative Audit Committee
of the Montana State Legislature:

We have audited the accompanying Statement of Net Asset Value for the state of Montana Board of Investments, Trust Funds Bond Pool, as of June 30, 2003 and 2002, and the related Statement of Changes in Net Asset Value and Statement of Investment Income and Distribution for the fiscal years then ended. These financial statements are the responsibility of the Board of Investments' management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the net asset value of the state of Montana Board of Investments, Trust Funds Bond Pool, as of June 30, 2003 and 2002, and its changes in net asset value and investment income and distribution for the fiscal years then ended in conformity with accounting principles generally accepted in the United States of America.

Respectfully submitted,

Signature on File

James Gillett, CPA
Deputy Legislative Auditor

November 4, 2003

B-11

**STATE OF MONTANA BOARD OF INVESTMENTS
TRUST FUNDS BOND POOL FINANCIAL STATEMENTS**

STATEMENT OF NET ASSET VALUE JUNE 30, 2003 AND 2002

<u>Assets</u>	<u>2003</u>	<u>2002</u>
Cash	\$ 10,238,624	\$ 0
Security lending cash collateral (Notes 3 and 4)	76,755,887	102,391,378
Interest receivable	18,928,190	21,432,301
Investments managed at fair value (amortized cost of \$1,139,041,264 in 2003 and \$1,125,137,879 in 2002)(Notes 2 and 4)	<u>1,251,081,198</u>	<u>1,154,302,005</u>
Total assets	\$ <u>1,357,003,899</u>	\$ <u>1,278,125,684</u>
 <u>Liabilities</u>		
Income due participants (Note 2)	\$ 7,509,196	\$ 6,911,434
Security lending obligations (Notes 3 and 4)	76,755,887	102,391,378
Security lending expense payable	<u>78,517</u>	<u>154,295</u>
Total liabilities	<u>84,343,600</u>	<u>109,457,107</u>
Net asset value	\$ <u>1,272,660,299</u>	\$ <u>1,168,668,577</u>
Units Outstanding (Note 2)	12,056,106	11,851,730
Unit Value (Note 2)	\$ 105.56	\$ 98.61

**STATEMENT OF CHANGES IN NET ASSET VALUE
FOR THE FISCAL YEARS ENDED JUNE 30, 2003 AND 2002**

Net asset value, beginning of year	\$ 1,168,668,577	\$ 1,175,369,082
Value of units purchased by participants	44,047,976	128,730,156
Value of units sold by participants	(21,937,900)	(150,143,501)
Changes in fair value of investments managed	<u>81,881,646</u>	<u>14,712,840</u>
Net asset value, end of year	\$ <u>1,272,660,299</u>	\$ <u>1,168,668,577</u>

**STATEMENT OF INVESTMENT INCOME AND DISTRIBUTION
FOR THE FISCAL YEARS ENDED JUNE 30, 2003 AND 2002**

Investment income (Note 2)	\$ 81,407,076	\$ 83,349,963
Security lending income	1,367,131	3,373,380
Security lending expense	(1,239,426)	(2,995,268)
Administrative expenses	(225,408)	(233,652)
Income due participants, beginning of year	<u>6,911,434</u>	<u>7,682,046</u>
Income available for distribution	88,220,807	91,176,469
Distribution	<u>80,711,611</u>	<u>84,265,035</u>
Income due participants, end of year (Note 2)	\$ <u>7,509,196</u>	\$ <u>6,911,434</u>

The accompanying notes are an integral part of these financial statements.

**STATE OF MONTANA BOARD OF INVESTMENTS
TRUST FUNDS BOND POOL**

**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2003 AND 2002**

1. HISTORY AND ORGANIZATION

The Board was created by an act of the Legislature to invest and manage the State of Montana's investment funds on a centralized basis. The Trust Funds Bond Pool (TFBP) was created by the Board to allow qualifying funds, per section 17-6-201, MCA, to participate in a diversified pool. The TFBP was created on October 1, 1995, by the transfer of all fixed income and variable-rate securities owned by the Coal Severance Tax Permanent Trust, Resource Indemnity Trust, Coal Tax Park Trust, Trust and Legacy, Coal Tax Cultural Trust and Treasure State Endowment Trust funds. Since the pool's creation in 1995, the funds listed below became participants in the TFBP:

University of Montana Endowment Fund	January 1996
Coal Severance Tax School Bond Contingency Fund	March 1996
Montana Pole Superfund	September 1996
State of Montana Section 457 Deferred Compensation Plan *	April 1997
Upper Clark Fork River Basin (UCFRB) Restoration	July 1999
Upper Clark Fork River Basin (UCFRB) Cost Recovery	July 1999
Streamside Tailings Operable Unit	July 1999
Treasure State Regional Water Systems	July 2000
Tobacco Trust Fund	January 2001
University of Montana Designated Fund	July 2002
University of Montana Other Fund	July 2002
Montana Tech of the U of M	March 2003

* In January 2002, the State of Montana Section 457 Deferred Compensation Plan withdrew from the TFBP.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Investments

TFBP investments are purchased in accordance with the statutorily mandated "Prudent Expert Principle". The TFBP portfolio includes corporate asset-backed, other corporate, U.S. government mortgage-backed, government, Yankee securities and cash investments. Corporate asset-backed securities represent debt securities collateralized by a pool of assets. U.S. government mortgage-backed securities reflect participation in a pool of residential mortgages. Government securities include direct and indirect obligations of the U.S. Treasury and state and local government bonds. Yankee bonds are U.S. dollar denominated securities issued by foreign corporations and governments and U.S. companies issuing debt in foreign markets.

The TFBP portfolio includes structured financial instruments known as REMICs (Real Estate Mortgage Investment Conduits). REMICs are pass-through vehicles for multiclass mortgage-backed securities. Strip investments represent the separate purchase of the principal and interest cash flows of a mortgage security. These securities, purchased for portfolio diversification and a competitive rate of return, are identified and reported as government mortgage-backed securities in the investment risk and portfolio disclosures. (See Note 4 on Investment Risk Categories and Note 7 for the Year End Portfolio.)

TFBP fixed income securities pay a fixed rate of interest until maturity while the variable-rate (floating-rate) securities pay a variable interest rate until maturity. The TFBP did not hold any variable rate securities as of June 30, 2003 and June 30, 2002.

Investments are presented in the Statement of Net Asset Value at fair value. Fair values for securities are determined primarily by reference to market prices supplied to the Board by the Board's custodial bank, State Street Bank. Amortized cost, parenthetically disclosed, represents the original cost, adjusted for premium and discount amortization where applicable. Premiums and discounts are amortized/accreted using the straight-line or scientific method to the call, average life or maturity date of the securities. Amortized cost may also be referred to as book value.

The TFBP, as an internal investment pool, invests its excess cash in the Board's Short Term Investment Pool, STIP, an external investment pool. An external investment pool commingles the moneys of more than one legally separate entity and invests, on the participants' behalf, in an investment portfolio. STIP participants include both state agencies and local governments. By meeting certain conditions, STIP, as a 2a7-like pool, is allowed to use amortized cost rather than fair value to report net assets to compute unit values.

Participant Units

The Coal Severance Tax Permanent Trust, Resource Indemnity Trust, Coal Tax Park Trust, Trust and Legacy, Coal Tax Cultural Trust, and Treasure State Endowment Trust funds transferred all fixed income and variable-rate securities, at amortized cost, into the TFBP at the start-up date and were issued units according to the fair value of each participant's portfolio. The initial unit value as of October 1, 1995, was \$100.00. Unit values are calculated weekly and at month end, based on portfolio pricing, to allow for participant transactions to occur as determined by the investment staff.

The June 30, 2003 unit value of \$105.56 increased from a June 30, 2002 unit value of \$98.61. Interest rates declined during the fiscal year, which has the effect of increasing bond prices and the pool unit value. A one percent (1%) change in interest rates is expected to have a five to seven percent (5%-7%) inverse change in the unit value. TFBP investments are considered long-term in nature and participants are not expected to sell units for liquidity for short-to-intermediate term needs.

Broker Receivable/Payable

TFBP security transactions are recorded as of the trade date rather than the settlement date. Because of this generally accepted practice, the TFBP portfolio at June 30 may include receivables from brokers for securities sold, but not delivered, and payables to brokers for securities purchased, but not received.

Other

Accumulated income, recorded as Income Due Participants, is distributed monthly on the first calendar day of each month. Realized portfolio gains/losses are distributed at least annually to the participants.

Investment income reported in the Statement of Investment Income and Distribution includes interest accruals, realized gains/losses, amortization/accretion and miscellaneous income.

Administrative expenses incurred by the Board are charged daily to TFBP based on the Board's expenses applicable to TFBP. These expenses include costs for the custodial bank contract.

3. SECURITIES LENDING

Under the provisions of state statutes, the Board has, via a Securities Lending Authorization Agreement, authorized the custodial bank, State Street Bank and Trust, to lend the Board's securities to broker-dealers and other entities with a simultaneous agreement to return the collateral for the same securities in the future. During the period the securities are on loan, the Board receives a fee and the custodial bank must initially receive collateral equal to 102 percent of the fair value of the loaned securities and maintain collateral equal to not less than 100 percent of the fair value of the loaned security. The Board retains all rights and risks of ownership during the loan period.

During fiscal years 2003 and 2002, State Street lent, on behalf of the Board, certain securities held by State Street, as custodian, and received US dollar currency cash, US government securities, and irrevocable bank letters of credit. State Street does not have the ability to pledge or sell collateral securities unless the borrower defaults.

The Board did not impose any restrictions during fiscal years 2003 and 2002 on the amount of the loans that State Street made on its behalf. There were no failures by any borrowers to return loaned securities or pay distributions thereon during fiscal years 2003 and 2002. Moreover, there were no losses during fiscal years 2003 and 2002 resulting from a default of the borrowers or State Street.

During fiscal years 2003 and 2002, the Board and the borrowers maintained the right to terminate all securities lending transactions on demand. The cash collateral received on each loan was invested, together with the cash collateral of other qualified plan lenders, in a collective investment pool, the Securities Lending Quality Trust. The relationship between the average maturities of the investment pool and the Board's loans was affected by the maturities of the loans made by other plan entities that invested cash collateral in the collective investment pool, which the Board could not determine. On June 30, 2003 and June 30, 2002, the Board had no credit risk exposure to borrowers.

As of June 30, 2003, the carrying and fair value of the underlying securities on loan for the Trust Funds Bond Pool was \$57,555,310 and \$70,451,001, respectively. The cash collateral provided for the securities on loan totaled \$76,755,887.

As of June 30, 2002, the carrying and fair value of the underlying securities on loan for the Trust Funds Bond Pool was \$106,007,425 and \$116,106,702, respectively. The collateral provided for the securities on loan totaled \$123,373,283 representing \$102,391,378 in cash and \$20,981,905 in securities collateral.

4. INVESTMENT RISK CATEGORIES

State of Montana investments are categorized below to give an indication of the level of risk assumed at June 30, 2003 and June 30, 2002. Category 1 includes investments that are insured or registered, or securities that are held by the Board or its agent in the Board's name. Not Categorized includes investments held by broker-dealers under securities loans with cash collateral.

Risk as of June 30, 2003

Category 1

<u>Security Investment Type</u>	<u>Securities Not On Loan</u>	<u>On Loan for Securities Collateral*</u>	<u>Not Categorized*</u>	<u>Carrying Amount</u>	<u>Fair Value</u>
Corporate Asset-Backed	\$ 12,255,000	\$ 0	\$ 0	\$ 12,255,000	\$ 12,255,000
Corporate Other	604,884,995	0	6,505,228	611,390,223	664,571,494
US Govt Mortgage-Backed	76,290,821	0	0	76,290,821	79,160,041
US Govt Direct/Indirect	245,586,129	0	51,050,082	296,636,211	340,815,409
Yankee Bonds	92,470,191	0	0	92,470,191	104,278,410
State and Local Government	13,884,836	0	0	13,884,836	13,886,862
STIP	<u>36,113,982</u>	<u>0</u>	<u>0</u>	<u>36,113,982</u>	<u>36,113,982</u>
Total Investments	\$ 1,081,485,954	\$ 0	\$ 57,555,310	\$ 1,139,041,264	\$ 1,251,081,198
Securities Lending Collateral Investment Pool			\$ <u>76,755,887</u>	\$ <u>76,755,887</u>	\$ <u>76,755,887</u>

*At June 30, 2003, these underlying securities, with a fair value of \$70,451,001, were loaned for cash collateral under a security lending agreement with the state's agent.

Risk as of June 30, 2002

Category 1

<u>Security Investment Type</u>	<u>Securities Not On Loan</u>	<u>On Loan for Securities Collateral*</u>	<u>Not Categorized*</u>	<u>Carrying Amount</u>	<u>Fair Value</u>
Corporate Asset-Backed	\$ 2,714,047	\$ 0	\$ 0	\$ 2,714,047	\$ 2,824,015
Corporate Other	689,693,208	0	9,228,927	698,922,135	700,891,576
US Govt Mortgage-Backed	52,444,484	0	0	52,444,484	53,774,861
US Govt Direct/Indirect	176,648,231	18,002,274	78,776,224	273,426,729	298,282,540
Yankee Bonds	74,094,573	0	0	74,094,573	74,990,810
State and Local Government	17,551,079	0	0	17,551,079	17,553,371
STIP	<u>5,984,832</u>	<u>0</u>	<u>0</u>	<u>5,984,832</u>	<u>5,984,832</u>
Total Investments	\$ 1,019,130,454	\$ 18,002,274	\$ 88,005,151	\$ 1,125,137,879	\$ 1,154,302,005
Securities Lending Collateral Investment Pool			\$ <u>102,391,378</u>	\$ <u>102,391,378</u>	\$ <u>102,391,378</u>

*At June 30, 2002, these underlying securities, with fair values of \$18,736,483 and \$97,370,219 respectively, were loaned for securities and cash collateral under a security lending agreement with the state's agent.

With the exception of the US government securities, the above instruments have credit risk as measured by major credit rating services. Credit risk is defined as the risk that the issuer of a fixed income security may default in making timely principal and interest payments. The Board of Investment's policy requires TFBP investments, at the time of purchase, to be rated investment grade as defined by Moody's or Standard & Poor's (S&P) rating services. The US government securities are guaranteed directly or indirectly by the US government.

Market risk for the above securities is caused by changes in the price or principal value of the security due to changes in interest rates and market liquidity.

As reported in the U.S. government mortgage-backed category, the TFBP portfolio holds REMICs totaling \$706,427 and \$1,265,484, respectively, at amortized cost, as of June 30, 2003 and June 30, 2002. These securities are based on separate or combined cash flows from principal and interest payments on underlying mortgages. When underlying mortgages are prepaid, the interest cash flows are reduced while principal cash flows are increased. If homeowners pay on mortgages longer than anticipated, the cash flow effect would be the opposite.

Corporate asset-backed securities represent debt securities collateralized by a pool of assets. The RFBP corporate asset-backed security is secured by lease payments and real estate. Credit risk for corporate asset backed securities is generally less than other corporate securities because assets are held by a third party.

As of June 30, 2003 and June 30, 2002, Enron Corp., and Burlington Industries, Inc. presented legal and higher credit risks to the Board.

The TFBP holds a \$2 million par, 6.75% Enron bond maturing August 1, 2009, a \$3 million par 6.40% Enron bond maturing July 15, 2006 and a \$3 million par 6.95% Enron bond maturing July 15, 2028. The combined book value of these securities, was \$7,560,870 as of November 30, 2001. On December 12, 2001, the Enron Corp. filed for Chapter 11 bankruptcy protection. Accordingly, the November 2001 book value for the three issues was reduced to \$3.2 million as of June 30, 2002. In October 2002, the book value was reduced to \$1.6 million for the three issues. In July 2003, the three issues were sold, on the market, for a total of \$1.35 million.

The Board owns a Burlington Industries, Inc., \$4 million par, 7.25% bond maturing September 15, 2005. In September 2000, the company announced a reduction of stockholders equity. Due to an increasing senior bank line and declining credit trend, the bond ratings for this issue were downgraded, in May 2001, by the Moody's and Standard & Poor's rating agencies. During fiscal year 2001, the book value of Burlington Industries Inc. was reduced from the August 31, 2000 book value of \$3,739,760 to \$1,600,000. Due to the company's filing for Chapter 11 bankruptcy protection on November 11, 2001, the book value was reduced to \$800,000. In October 2003, Burlington Industries, Inc. received court approval to sell its assets. This sale is expected to close in November 2003. Under the company's recovery plan, the Board will receive cash for its unsecured claim.

As of June 30, 2002, Rite Aid and WorldCom Inc. presented a higher credit risk to the Board.

The TFBP owns a Rite Aid \$3,000,000 par, 7.13% bond maturing January 15, 2007. In May 2000, the Board was subordinated to a secured bank line of credit on this issue and the bond ratings were downgraded by the Moody's and Standard & Poor's bond ratings agencies. Based on this subordination and ratings downgrade, the book value was reduced to \$2,400,000 as of June 30, 2000. During fiscal year 2001, the book value was further reduced to \$1,800,000. Due to an improving credit trend, amortization was resumed in June 2001. The book value of this security at June 30, 2002 is \$2,374,356. As of June 30, 2002, Rite Aid did not represent a credit risk. In December 2002, this bond was sold, on the market, for \$1.5 million in principal plus interest of \$45,719.

The TFBP portfolio includes a \$9,000,000 par, 6.95% WorldCom Inc. bond maturing August 15, 2028. The book value of this bond, originally purchased at a discount, was \$8,216,100 on June 30, 2002. On July 21, 2002, WorldCom Inc. filed for Chapter 11 bankruptcy protection. As of July 31, 2002, the reduced book value is \$3,600,000. On November 7, 2002, the Attorney General for the State of Montana filed a lawsuit against certain WorldCom executives, directors and financial institutions associated with WorldCom such as Arthur Andersen and CitiGroup. The lawsuit, filed in Lewis and Clark County, Montana, alleges that the defendants filed "false and misleading registration statements" relating to the purchase of the bonds by the Montana Board of Investments. In December 2002, this bond was sold, on the market, for \$2.7 million.

5. PARTICIPANT LOAN

In accordance with Senate Bill 495 enacted by the 2001 Legislature, the Coal Severance Tax Permanent Trust loaned 483,604 TFBP shares, with a book value of \$46,366,904, to the Trust and Legacy fund on July 2, 2001. The loan proceeds were deposited in the Trust and Legacy Fund. A loan receivable was recorded in the Coal Severance Tax Permanent Trust and a corresponding liability was recorded in the Guarantee Fund, a General Fund sub-fund. The August 2002 Special Legislative Session approved the request to record this activity in a state special revenue fund of the Office of Public Instruction rather than in the Guarantee Fund.

6. DEUTSCHE BANK SECURITIES, INC. COMPLAINT

The Board received a summons and complaint, dated September 3, 2002, regarding the sale of a Pennzoil Quaker State, \$8 million par, 6.75% corporate bond maturing April 1, 2009. Deutsche Bank Securities claims a "breach of contract" for the March 25 2002 sale of the bond at a price of \$94.669 plus accrued interest. Deutsche Bank Securities seeks damages of \$861,811 for the additional costs incurred to acquire the bond from third parties, plus any statutory interest, costs and expenses. On October 1, 2002, Shell Oil Company acquired Pennzoil and subsequently announced a public tender of Pennzoil Quaker State debt. The Board tendered the Pennzoil Quaker State holdings on October 8, 2002 at a price of \$113.099. The tender was accepted with a settlement date of November 1, 2002. On November 4, 2002, the Board received \$9,092,920 in principal and interest plus \$240,000 as a consent fee.

7. YEAR END PORTFOLIO

The June 30, 2003 TFBP portfolio is listed below. The security type percentage is based on the fair value ratio of the specific security investment type to the total portfolio.

<u>Security Name</u>	<u>Coupon</u>	<u>Maturity</u>	<u>Par</u>	<u>Book Value</u>	<u>Fair Value</u>	<u>% of Total</u>
AERO 1 HQ FINANCE TRUST	4.64	07/07/10	12,255,000	12,255,000	12,255,000	0.98%
Corporate Asset-Backed	1 Issue(s)		12,255,000	12,255,000	12,255,000	0.98%
AMERICA WEST AIRLINES EQUIPMENT TRUST	7.93	01/02/19	3,546,954	3,546,954	3,761,332	0.30%
AMERICAN AIRLINES 1991 EQUIPMENT TRUST	9.73	09/29/14	5,000,000	4,977,637	2,625,000	0.21%
AMERICAN AIRLINE EQUIPMENT TRUST	6.98	05/23/21	6,505,121	6,490,711	5,334,199	0.43%
AMERICAN TRANS AIR EQUIPMENT TRUST	8.04	07/15/17	6,278,860	6,278,860	6,666,003	0.53%
ARCHER DANIELS MIDLAND CO	10.25	01/15/06	5,000,000	4,995,609	6,008,681	0.48%
ASHLAND OIL CO	8.80	11/15/12	2,500,000	2,542,457	3,147,550	0.25%
BANK ONE	6.25	02/15/08	4,000,000	3,848,798	4,589,367	0.37%
BANKBOSTON NA	6.38	03/25/08	4,000,000	3,857,894	4,557,422	0.36%
BORDEN INC	9.25	06/15/19	1,500,000	1,455,821	975,000	0.08%
BORG WARNER AUTOMOTIVE INC	7.00	11/01/06	1,000,000	1,012,227	1,123,684	0.09%
BURLINGTON INDUSTRIES INC	7.25	09/15/05	4,000,000	800,000	1,680,000	0.13%
BURLINGTON NORTHERN INC	7.50	07/15/23	5,000,000	4,628,297	5,173,055	0.41%
BURLINGTON NORTHERN RR CO	7.97	01/01/15	3,901,688	3,901,688	4,820,659	0.39%
BURLINGTON NORTHERN SANTA FE RY	7.16	01/02/20	14,038,275	14,038,275	15,866,696	1.27%
CIT GROUP EQUIPMENT TRUST	6.49	01/05/21	12,228,472	12,228,472	12,545,860	1.00%
CIT GROUP INC	7.38	04/02/07	5,000,000	5,439,441	5,708,850	0.46%
CNA FINANCIAL CORP	6.25	11/15/03	10,000,000	10,054,219	10,109,808	0.81%
CNA FINANCIAL CORP	6.45	01/15/08	5,000,000	5,061,510	5,221,130	0.42%
CSX CORP	7.45	05/01/07	2,000,000	1,998,841	2,340,136	0.19%
CSX CORP	7.90	05/01/17	5,000,000	4,997,993	6,655,543	0.53%
CHAMPION INTERNATIONAL CORP	7.63	09/01/23	5,000,000	4,850,086	5,220,462	0.42%
CHAMPION INTERNATIONAL CORP	7.15	12/15/27	3,000,000	2,937,387	3,373,298	0.27%
CHICAGO + NORTH WESTERN RY	8.91	01/01/15	4,205,942	4,205,942	5,612,459	0.45%
CITIGROUP INC	7.88	05/15/25	4,000,000	4,076,846	5,234,016	0.42%
CITIGROUP INC	6.20	03/15/09	5,000,000	4,801,184	5,760,142	0.46%
CITICORP CAPITAL II	8.02	02/15/27	6,000,000	5,953,635	7,060,477	0.56%
CLEVELAND ELECTRIC ILLUM CO	9.00	07/01/23	2,000,000	1,990,249	2,092,693	0.17%
CLEVELAND ELECTRIC ILLUM CO	7.13	07/01/07	5,000,000	4,989,329	5,757,680	0.46%
CONAGRA INC	9.88	11/15/05	5,000,000	5,163,444	5,897,535	0.47%
CONTINENTAL AIRLINES EQUIPMENT TRUST	6.55	02/02/19	6,097,356	6,097,356	5,762,001	0.46%
CORPORATE PROPERTY REIT	7.75	08/15/04	5,000,000	5,016,454	5,292,636	0.42%
CORPORATE PROPERTY REIT	7.88	03/15/16	3,000,000	2,993,358	3,671,441	0.29%
DAYTON HUDSON CORP	7.65	08/01/23	2,745,000	2,753,240	2,863,770	0.23%
DEER PARK REFINING L P	6.47	12/15/08	2,873,850	2,832,701	3,247,057	0.26%
DELTA AIR LINES INC	10.14	08/14/12	1,000,000	1,000,000	775,000	0.06%
DELTA AIR LINES INC	10.14	08/14/12	2,000,000	1,993,085	1,550,000	0.12%
DELTA AIR LINES INC	10.00	06/05/13	2,000,000	2,000,000	800,000	0.06%
DILLARD DEPT STORES INC	7.75	07/15/26	3,000,000	2,973,819	2,692,500	0.22%
ENRON CORP	6.75	08/01/09	2,000,000	400,000	385,000	0.03%
ENRON CORP	6.40	07/15/06	3,000,000	600,000	577,500	0.05%
ENRON CORP	6.95	07/15/28	3,000,000	600,000	573,750	0.05%

<u>Security Name</u>	<u>Coupon</u>	<u>Maturity</u>	<u>Par</u>	<u>Book Value</u>	<u>Fair Value</u>	<u>% of Total</u>
ENSERCH CORP	7.13	06/15/05	5,000,000	5,026,144	5,368,758	0.43%
FMC CORP	6.38	09/01/03	4,000,000	3,999,628	4,010,000	0.32%
FIRST BANK NA	8.35	11/01/04	5,000,000	4,999,332	5,407,141	0.43%
FIRST CHICAGO CORP	6.38	01/30/09	4,000,000	3,784,677	4,607,997	0.37%
FIRST INTERSTATE BANC SYSTEM MONTANA	7.50	10/01/06	4,980,000	4,980,000	4,980,000	0.40%
FIRST SECURITY CORP	6.88	11/15/06	4,000,000	3,943,252	4,584,545	0.37%
FIRST UNION CORP	8.00	08/15/09	5,000,000	5,036,335	5,365,313	0.43%
FIRST UNION BANK	5.80	12/01/08	4,000,000	3,757,268	4,511,398	0.36%
FLORIDA GAS TRANSMISSION CO	9.19	11/01/24	5,000,000	5,000,000	5,769,209	0.46%
FLORIDA GAS TRANSMISSION CO	7.00	07/17/12	3,000,000	2,996,066	3,103,768	0.25%
FORD MOTOR CREDIT CO	6.75	05/15/05	5,000,000	5,004,963	5,272,852	0.42%
FORD MOTOR CREDIT CO	7.38	10/28/09	7,000,000	7,007,231	7,355,550	0.59%
GTE CORP	7.90	02/01/27	6,000,000	6,000,000	6,865,552	0.55%
GTE SOUTH INC	7.50	03/15/26	6,000,000	5,920,907	6,762,412	0.54%
GENERAL AMERICAN TRANSN CORP	8.42	01/01/15	8,074,469	8,074,469	7,678,673	0.61%
GENERAL MOTORS ACCEPTANCE CORP	0.00	12/01/12	25,000,000	13,750,330	13,048,025	1.04%
GENERAL MOTORS ACCEPTANCE CORP	6.13	08/28/07	5,000,000	5,016,147	5,210,905	0.42%
GEORGIA PACIFIC CORP	9.13	07/01/22	2,000,000	1,964,679	1,897,500	0.15%
GEORGIA PACIFIC CORP	8.25	03/01/23	5,000,000	5,059,874	4,425,000	0.35%
GEORGIA PACIFIC CORP	8.63	04/30/25	2,000,000	2,100,862	1,820,000	0.15%
GEORGIA PACIFIC CORP	7.75	11/15/29	2,000,000	1,643,894	1,780,000	0.14%
ILLINOIS BELL TEL CO	6.63	02/01/25	2,000,000	1,796,058	2,078,544	0.17%
INTERNATIONAL PAPER CO	6.88	11/01/23	2,000,000	1,975,809	2,195,697	0.18%
JPM CAPITAL	7.54	01/15/27	4,000,000	3,784,041	4,469,151	0.36%
KCT INTERMODAL TRANSPORTATION CORP	6.88	08/01/18	1,876,933	1,876,933	2,057,808	0.16%
K N ENERGY INC	7.25	03/01/28	2,000,000	1,959,119	2,332,262	0.19%
KELLWOOD CO	7.63	10/15/17	8,000,000	7,913,594	7,720,000	0.62%
KERR MCGEE CORP	7.13	10/15/27	3,000,000	3,038,242	3,383,105	0.27%
LEHMAN BROTHERS HOLDINGS INC	0.00	07/28/28	20,000,000	2,941,363	3,160,000	0.25%
MARSH + MCLENNAN COS INC	7.13	06/15/09	5,000,000	5,072,624	6,007,080	0.48%
MEAD CORP	7.35	03/01/17	4,000,000	3,996,948	4,898,103	0.39%
MED MAP L L C MONTANA	7.06	12/01/15	4,710,000	4,710,000	4,710,000	0.38%
MED MAP L L C MONTANA	7.00	06/01/21	4,865,000	4,865,000	4,865,000	0.39%
METROPOLITAN LIFE INSURANCE CO	7.45	11/01/23	5,000,000	4,894,144	5,276,990	0.42%
MILLENIUAM AMERERICA INC	7.00	11/15/06	1,000,000	989,831	1,003,750	0.08%
MISSISSIPPI POWER + LIGHT CO	7.70	07/15/23	4,000,000	3,969,278	4,151,742	0.33%
MOBIL CORP	5.94	01/15/19	9,175,212	9,175,212	9,776,297	0.78%
MORGAN J P + CO INC	0.00	04/15/27	70,000,000	11,836,164	12,876,570	1.03%
NATIONWIDE FINANCIAL SERVICES INC	8.00	03/01/27	4,000,000	3,940,648	4,546,974	0.36%
NEW YORK TEL CO	7.25	02/15/24	3,000,000	2,905,062	3,192,461	0.26%
NORAM ENERGY CORP	6.50	02/01/08	2,000,000	1,942,334	2,144,938	0.17%
NORFOLK SOUTHERN CORP	7.70	05/15/17	4,000,000	4,013,633	5,283,918	0.42%
NORFOLK SOUTHERN CORP	7.35	05/15/07	6,500,000	6,504,428	7,612,374	0.61%
NORTHWEST AIRLINES EQUIPMENT TRUST	6.81	08/01/21	11,486,563	11,167,055	11,371,697	0.91%
NORTHWEST AIRLINES EQUIPMENT TRUST	7.94	10/01/20	4,487,533	4,437,420	4,885,801	0.39%
OCCIDENTAL PETROLEUM CORP	7.20	04/01/28	7,000,000	6,872,758	8,469,875	0.68%
OCCIDENTAL PETROLEUM CORP	8.75	01/15/23	4,000,000	4,000,000	5,493,345	0.44%
OHIO POWER CO	7.30	04/01/24	4,000,000	3,700,717	4,318,169	0.35%
OLD REPUBLIC INTERNATIONAL CORP	7.00	06/15/07	4,000,000	3,999,143	4,647,588	0.37%
PPL MONTANA LLC	8.90	07/02/20	18,591,834	18,591,834	20,884,024	1.67%
PACIFIC BELL	7.25	11/01/27	4,000,000	3,972,629	4,564,950	0.36%
PANHANDLE EASTERN PIPE LINE CO	7.95	03/15/23	5,000,000	4,944,351	5,212,500	0.42%
PENNEY J C INC	7.13	11/15/23	3,000,000	3,035,782	2,823,750	0.23%
PENNEY J C INC	7.65	08/15/16	3,000,000	2,973,259	2,906,250	0.23%
PHILLIPS PETROLEUM CO	7.13	03/15/28	4,000,000	3,943,119	4,529,142	0.36%
SEARS ROEBUCK ACCEP CORP	7.50	10/15/27	5,000,000	5,017,150	5,542,153	0.44%

<u>Security Name</u>	<u>Coupon</u>	<u>Maturity</u>	<u>Par</u>	<u>Book Value</u>	<u>Fair Value</u>	<u>% of Total</u>
SECURITY CAP GROUP INC	7.70	06/15/28	2,000,000	2,365,979	2,435,098	0.19%
SONAT INC	7.00	02/01/18	2,000,000	1,999,778	1,660,000	0.13%
SOUTHERN UNION CO	7.60	02/01/24	10,000,000	9,246,324	10,135,414	0.81%
SOUTHWEST GAS CORP	7.50	08/01/06	4,000,000	4,239,838	4,404,336	0.35%
SOUTHWEST GAS CORP	8.38	02/15/11	8,000,000	8,009,170	9,325,171	0.75%
SOUTHWESTERN BELL TEL CO	7.25	07/15/25	3,000,000	3,053,417	3,099,070	0.25%
SOUTHWESTERN BELL TEL CO	7.00	11/15/27	2,000,000	1,997,758	2,224,838	0.18%
SPRINT CAPITAL CORP	5.88	05/01/04	5,000,000	5,000,000	5,134,453	0.41%
SUNAMERICA INC	8.13	04/28/23	7,000,000	7,040,706	9,201,936	0.74%
SUPER VALU INC	8.88	11/15/22	9,000,000	9,040,845	9,439,651	0.75%
SUPER VALU INC	7.88	08/01/09	7,000,000	6,986,589	8,285,704	0.66%
TELE COMMUNICATIONS INC	7.88	08/01/13	2,000,000	1,977,146	2,431,018	0.19%
TEXAS GAS TRANSMISSION CORP	7.25	07/15/27	2,000,000	1,839,637	2,271,959	0.18%
TEXAS UTILITIES ELEC CO	7.88	03/01/23	4,000,000	3,950,933	4,171,223	0.33%
TRAILER TRAIN CO	10.30	05/01/04	333,333	333,333	346,200	0.03%
TRANSCONTINENTAL GAS PIPE LINE	7.25	12/01/26	2,000,000	2,011,445	1,975,000	0.16%
TYSON FOODS INC	8.25	10/01/11	3,000,000	3,132,636	3,553,199	0.28%
ULTRAMAR DIAMOND SHAMROCK CORP	7.20	10/15/17	2,000,000	1,986,793	1,942,552	0.16%
UNION CARBIDE CHEMS + PLASTICS	8.75	08/01/22	4,000,000	4,203,216	4,171,209	0.33%
UNION OIL CO CALIFORNIA	7.20	05/15/05	5,000,000	4,999,305	5,447,391	0.44%
UNION OIL CO CALIFORNIA	7.00	05/01/28	6,000,000	5,769,208	6,815,035	0.54%
UNION PACIFIC RR CO	7.75	07/01/12	2,754,534	2,754,534	3,418,930	0.27%
UNION PACIFIC RESOURCES GROUP INC	7.05	05/15/18	6,000,000	5,936,528	7,434,239	0.59%
UNION TANK CAR CO	7.13	02/01/07	2,000,000	1,999,233	2,314,055	0.18%
UNION TANK CAR CO	7.45	06/01/09	5,000,000	5,000,000	6,052,045	0.48%
UNITED AIRLINES EQUIPMENT TRUST	7.03	10/01/10	9,408,328	9,293,700	7,855,954	0.63%
WELLS FARGO + CO	6.88	04/01/06	3,000,000	2,960,844	3,391,524	0.27%
WESTERN PROPERTIES REIT	7.88	02/15/04	6,000,000	5,998,906	6,207,557	0.50%
WESTERN PROPERTIES REIT	7.20	09/15/08	1,000,000	969,200	1,150,522	0.09%
WESTINGHOUSE ELECTRIC CORP	8.63	08/01/12	2,000,000	2,054,138	2,685,704	0.21%
WESTVACO CORP	7.00	08/15/23	5,000,000	4,538,104	5,181,670	0.41%
WESTVACO CORP	7.65	03/15/27	6,000,000	5,975,626	7,072,346	0.57%
WEYERHAEUSER CO	8.50	01/15/25	8,000,000	9,304,981	10,198,532	0.82%
WILLAMETTE INDUSTRIES INC	7.00	02/01/18	1,000,000	933,674	1,191,276	0.10%
WILMINGTON TRUST TUSCON ELECTRIC	10.21	01/01/09	4,675,074	4,675,074	4,675,074	0.37%
WINN DIXIE TRUST	0.00	09/01/24	64,509,810	10,006,064	12,256,864	0.98%
WORLDCOM INC	6.95	08/15/28	9,000,000	3,600,000	2,688,750	0.21%
Corporate Other	134 Issue(s)		769,850,143	611,390,223	664,571,494	53.12%
FEDERAL HOME LOAN POOL G10814	5.50	05/01/13	1,797,497	1,796,167	1,879,368	0.15%
FEDERAL HOME LOAN POOL G10173	6.00	01/01/09	806,639	805,152	841,426	0.07%
FEDERAL HOME LOAN POOL G30006	7.00	07/01/13	997,069	997,069	1,060,404	0.08%
FEDERAL HOME LOAN PC REMIC	9.15	10/15/20	294,570	291,118	315,839	0.03%
FEDERAL HOME LOAN PC REMIC	6.25	11/15/07	419,163	415,309	438,076	0.04%
FEDERAL HOME LOAN POOL CO1523	5.00	03/01/33	9,902,946	9,817,072	10,077,021	0.81%
FEDERAL HOME LOAN POOL E00247	5.50	10/01/08	1,075,541	1,072,513	1,123,184	0.09%
FEDERAL HOME LOAN POOL E00659	6.00	04/01/14	2,514,197	2,512,270	2,625,765	0.21%
FEDERAL HOME LOAN POOL E01376	4.00	04/01/18	19,723,808	19,564,821	19,907,280	1.59%
FNMA POOL 254233	5.00	03/01/17	12,418,573	12,003,590	12,851,768	1.03%
FNMA POOL 254631	5.00	02/01/18	14,102,930	14,347,059	14,589,757	1.17%
FNMA POOL 303202	6.50	05/01/14	2,817,689	2,792,781	2,980,874	0.24%
FNMA POOL 313999	6.00	02/01/13	1,275,482	1,269,371	1,338,459	0.11%
FNMA POOL 572220	6.00	03/01/16	3,543,650	3,533,798	3,707,544	0.30%
FNMA POOL 592327	5.50	06/01/16	4,938,899	4,826,827	5,142,243	0.41%
GNMA POOL 032974	9.50	09/15/09	33,652	31,999	37,076	0.00%
GNMA POOL 038164	10.00	01/15/10	80,150	79,903	90,922	0.01%
GNMA POOL 039321	10.00	12/15/09	32,690	32,591	36,960	0.00%

<u>Security Name</u>	<u>Coupon</u>	<u>Maturity</u>	<u>Par</u>	<u>Book Value</u>	<u>Fair Value</u>	<u>% of Total</u>
GNMA POOL 042547	10.00	10/15/10	17,024	16,969	19,297	0.00%
GNMA POOL 065459	11.50	04/15/13	11,683	11,554	13,988	0.00%
GNMA POOL 166690	9.00	06/15/16	17,948	17,844	20,162	0.00%
GNMA POOL 281467	9.00	09/15/19	55,263	55,045	62,629	0.01%
Government-Mortgage Backed	22 Issue(s)		76,877,065	76,290,821	79,160,041	6.33%
BENDER SHIPBUILDING + REPAIR USGG XI	6.20	09/30/12	11,956,425	11,956,425	11,956,425	0.96%
TVA TRUST	0.00	11/01/25	25,000,000	4,927,200	5,206,750	0.42%
FEDERAL HOME LOAN MORTGAGE CORP	3.25	06/18/18	20,000,000	19,901,778	19,609,740	1.57%
FEDERAL HOME LOAN MORTGAGE CORP	0.00	06/21/32	100,000,000	13,621,311	14,187,000	1.13%
FEDERAL HOME LOAN BANKS	6.40	06/03/14	6,000,000	5,579,707	7,144,797	0.57%
FEDERAL HOME LOAN BANKS	7.00	08/26/19	7,000,000	6,960,452	8,646,631	0.69%
FEDERAL HOME LOAN BANKS	7.45	02/03/20	10,000,000	10,067,861	12,912,580	1.03%
FEDERAL HOME LOAN MORTGAGE CORP	8.25	06/01/26	7,000,000	7,322,801	9,671,340	0.77%
FEDERAL HOME LOAN MORTGAGE CORP	0.00	06/05/28	50,000,000	9,268,005	10,756,050	0.86%
FEDERAL HOME LOAN MORTGAGE CORP	0.00	09/14/29	100,000,000	16,955,503	18,288,000	1.46%
FEDERAL NATIONAL MORTGAGE ASSN	6.00	05/15/08	15,000,000	14,681,883	17,294,778	1.38%
FEDERAL NATIONAL MORTGAGE ASSN	7.25	01/15/10	15,000,000	14,950,347	18,550,554	1.48%
FEDERAL NATIONAL MORTGAGE ASSN	7.13	01/15/30	25,000,000	27,157,135	32,458,755	2.59%
GLOBAL INDUSTRIES LTD USGG XI	7.71	02/15/25	8,800,000	8,800,000	8,800,000	0.70%
OXY GROWER I USGG XI	8.13	09/16/06	692,000	692,000	692,000	0.06%
REINAUER MARITIME CO LLC USGG XI	6.50	06/30/28	20,600,000	20,600,000	20,600,000	1.65%
STUDENT LOAN MARKETING ASSN	0.00	05/15/14	50,000,000	17,139,161	24,030,300	1.92%
T T BARGE SERVICES USGG XI	6.45	12/16/12	1,936,100	1,936,100	1,936,100	0.15%
TUNISIA AID USGG	6.71	02/01/24	4,000,000	3,796,504	4,000,000	0.32%
U S ARMY HOSPITALITY FUND USGG	7.47	05/01/32	9,906,667	9,906,667	9,906,667	0.79%
UNITED STATES TREASURY BONDS	7.25	05/15/16	14,000,000	14,487,718	18,624,375	1.49%
UNITED STATES TREASURY BONDS	7.50	11/15/16	6,000,000	6,154,741	8,149,687	0.65%
UNITED STATES TREASURY BONDS	3.63	04/15/28	28,411,750	29,300,911	34,586,868	2.76%
VESSEL MGMT SVCS INC USGG XI	6.08	05/20/24	20,472,000	20,472,000	22,806,013	1.82%
Government Direct-Indirect	24 Issue(s)		556,774,942	296,636,211	340,815,409	27.24%
AMERICAN PRESIDENT COS LTD	7.13	11/15/03	6,000,000	5,998,355	5,820,000	0.47%
CANADIAN NATIONAL RY CO	6.80	07/15/18	4,000,000	3,979,424	4,554,077	0.36%
EASTERN ENERGY LTD	7.25	12/01/16	10,000,000	9,879,339	12,815,720	1.02%
EQUITABLE LIFE ASSUR SOC U S A	6.95	12/01/05	5,000,000	4,959,246	5,529,694	0.44%
GREAT LAKES POWER INC	9.00	08/01/04	10,000,000	9,994,911	10,682,333	0.85%
HOUSEHOLD FINANCE CORP	6.88	03/01/07	3,000,000	2,961,631	3,454,340	0.28%
HOUSEHOLD FINANCE CORP	6.50	11/15/08	5,000,000	4,834,131	5,792,618	0.46%
IBP FINANCIAL CO CANADA	7.45	06/01/07	3,000,000	2,999,188	3,255,000	0.26%
MACMILLAN BLOEDEL LTD	7.70	02/15/26	5,000,000	4,888,077	5,906,360	0.47%
PANAMERICAN BEVERAGES INC	7.25	07/01/09	7,000,000	6,983,240	7,840,000	0.63%
TRANSAMERICA FINANCIAL CORP	0.00	09/01/12	20,000,000	10,431,148	10,895,702	0.87%
TRANSCANADA PIPELINES LTD	8.50	03/20/23	5,000,000	5,235,224	5,232,567	0.42%
UNITED MEXICAN STATES	8.00	09/24/22	20,000,000	19,326,278	22,500,000	1.80%
Yankee Bonds	13 Issue(s)		103,000,000	92,470,191	104,278,410	8.34%
BUTTE SILVER BOW MONTANA TAX INDL	6.89	07/01/05	5,025,000	5,025,000	5,025,000	0.40%
MONTANA STATE TAXABLE RENEW (4 ISSUES)	7.35-7.40	8/1/09-12	735,000	732,974	735,000	0.06%
MONTANA STATE BOARD HOUSING	8.45	08/01/39	1,150,000	1,150,000	1,150,000	0.09%
MONTANA CRP (96 ISSUES)	6.00-8.00	11/15/03-15	6,976,862	6,976,862	6,976,862	0.56%
State/Local Government	102 Issue(s)		13,886,862	13,884,836	13,886,862	1.11%
SHORT TERM INVESTMENT POOL			36,113,982	36,113,982	36,113,982	2.89%
Cash Equivalents	1 Issue(s)		36,113,982	36,113,982	36,113,982	2.89%
TFBP Total	297 Issue(s)		1,568,757,993	1,139,041,264	1,251,081,198	100.00%

LEGISLATIVE AUDIT DIVISION

Scott A. Seacat, Legislative Auditor
John W. Northey, Legal Counsel



Deputy Legislative Auditors:
Jim Pellegrini, Performance Audit
Tori Hunthausen, IS Audit & Operations
James Gillett, Financial-Compliance Audit

INDEPENDENT AUDITOR'S REPORT

The Legislative Audit Committee
of the Montana State Legislature:

We have audited the accompanying Statement of Net Asset Value for the state of Montana Board of Investments, Short Term Investment Pool, as of June 30, 2003 and 2002, and the related Statement of Changes in Net Asset Value and Statement of Investment Income and Distribution for the fiscal years then ended. These financial statements are the responsibility of the Board of Investments' management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the net asset value of the state of Montana Board of Investments, Short Term Investment Pool, as of June 30, 2003 and 2002, and its changes in net asset value and investment income and distribution for the fiscal years then ended in conformity with accounting principles generally accepted in the United States of America.

Respectfully submitted,

Signature on File

James Gillett, CPA
Deputy Legislative Auditor

November 4, 2003

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**STATE OF MONTANA BOARD OF INVESTMENTS
SHORT TERM INVESTMENT POOL FINANCIAL STATEMENTS**

STATEMENT OF NET ASSET VALUE JUNE 30, 2003 AND 2002

	<u>2003</u>	<u>2002</u>
<u>Assets</u>		
Cash	\$ 252,434	\$ 0
Interest receivable	619,408	1,426,446
Security lending cash collateral (Notes 3 and 4)	0	0
Unrealized loss (Note 2)	15,180	0
Investments managed at fair value (amortized cost of \$1,420,403,394 in 2003 and \$1,501,813,452 in 2002)(Notes 2 and 4)	<u>1,420,388,214</u>	<u>1,501,953,124</u>
Total assets	\$ <u>1,421,275,236</u>	\$ <u>1,503,379,570</u>
<u>Liabilities</u>		
Security lending expense payable	\$ 0	\$ 0
Unrealized gain (Note 2)	0	139,672
Income due participants	252,441	1,002,463
Security lending obligations(Notes 3 and 4)	<u>0</u>	<u>0</u>
Total liabilities	\$ <u>252,441</u>	\$ <u>1,142,135</u>
Net asset value	\$ <u>1,421,022,795</u>	\$ <u>1,502,237,435</u>
Units Outstanding (Note 2)	1,421,022,795	1,502,237,435
Unit Value (Note 2)	\$ 1	\$ 1

**STATEMENT OF CHANGES IN NET ASSET VALUE
FOR THE FISCAL YEARS ENDED JUNE 30, 2003 AND 2002**

Net asset value, beginning of year	\$ 1,502,237,435	\$ 1,681,620,625
Value of units purchased by participants	6,003,654,371	5,652,461,058
Value of units sold by participants	<u>(6,084,869,011)</u>	<u>(5,831,844,248)</u>
Net asset value, end of year	\$ <u>1,421,022,795</u>	\$ <u>1,502,237,435</u>

**STATEMENT OF INVESTMENT INCOME AND DISTRIBUTION
FOR THE FISCAL YEARS ENDED JUNE 30, 2003 AND 2002**

Investment income (Note 2)	\$ 21,605,295	\$ 47,498,749
Security lending income	209	850,240
Security lending expense	(187)	(761,481)
Administrative expenses	(322,224)	(321,480)
Income due participants, beginning of year	<u>1,002,463</u>	<u>2,929,723</u>
Income available for distribution	22,285,556	50,195,751
Distribution	<u>22,033,115</u>	<u>49,193,288</u>
Income due participants, end of year	\$ <u>252,441</u>	\$ <u>1,002,463</u>

The accompanying notes are an integral part of these financial statements.

**STATE OF MONTANA BOARD OF INVESTMENTS
SHORT TERM INVESTMENT POOL - NOTES TO FINANCIAL STATEMENTS**

JUNE 30, 2003 AND 2002

1. HISTORY AND ORGANIZATION

The Board was created by an act of the Legislature to invest and manage the State of Montana's investment funds on a centralized basis. The Short Term Investment Pool (STIP) was created by the Board to allow qualifying funds, per sections 17-6-201, 202 and 204, MCA, to participate in a diversified pool. Although state agencies are legally required to invest in STIP, local governments may voluntarily participate in STIP.

The purpose of STIP is to obtain the highest possible return, yet maintain a highly liquid position whereby funds may be invested for relatively short periods, one day or more, depending upon the participant's anticipated use of the funds. The investments and the income from STIP are owned by the participants, as they purchase units, and are managed on their behalf by the Board.

Although STIP is not registered with the Securities and Exchange Commission (SEC) as an investment company, the Board has as policy that STIP will, and does, operate in a manner consistent with the SEC's rule 2a7 of the Investment Company Act of 1940. In meeting certain conditions, STIP, as a 2a7-like pool, is allowed to use amortized cost rather than fair value to report net assets to compute unit values.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Investments

STIP investments are purchased in accordance with the statutorily mandated "Prudent Expert Principle". The STIP portfolio may include asset-backed securities, commercial paper, corporate and government securities, repurchase agreements, and variable-rate (floating-rate) instruments. These securities are purchased to provide shareholders with a diversified portfolio earning a competitive total rate of return.

Asset-backed securities represent debt securities collateralized by a pool of mortgage and non-mortgage assets such as trade and loan receivables, equipment leases, credit cards, etc. Commercial paper is unsecured short-term debt with maturities ranging from 1 to 270 days. Commercial paper issued at a discount, direct or by brokers, is backed by bank credit lines. Repurchase agreements (REPOs) represent an agreement between a seller and a buyer, usually of US government securities, whereby the seller agrees to repurchase the securities at an agreed upon price and stated time. Variable-rate (floating-rate) securities pay a variable rate of interest until maturity. The variable-rate securities float with LIBOR (London Interbank Offered Rate).

Investments held are reported at fair value, annually, based on market prices supplied to the Board by various pricing services. The difference between amortized cost and fair value is reflected as an unrealized gain or loss in the investments managed. The STIP investment portfolio consists of securities with a maximum maturity of 397 days or less with the exception of securities having rate reset dates. The portfolio is carried at amortized cost or book value.

Participant Units

The STIP unit value is fixed at \$1 for both participant buys and sells. A purchased unit earns income on the purchase date and ceases to earn income on the day before the unit is sold. Participants may buy or sell fractional shares. For fiscal years 2003 and 2002, income was distributed on the first calendar day of each month, with the exception of the June distribution. Income for June 2003 was distributed on the last calendar day of the month. Participants may automatically reinvest their income in additional units.

During fiscal years 2003 and 2002, the Board did not provide or obtain any legally binding guarantees to support the value of the participant units.

Broker Receivable/Payable

STIP security transactions are recorded as of the trade date rather than the settlement date. Because of this generally accepted practice, the STIP portfolio at June 30 may include receivables from brokers for securities sold, but not delivered, and payables to brokers for securities purchased, but not received.

Other

Administrative expenses incurred by the Board are charged daily to STIP based on the Board's expenses applicable to STIP.

3. SECURITIES LENDING

Under the provisions of state statutes, the Board has, via a Securities Lending Authorization Agreement, authorized the custodial bank, State Street Bank and Trust, to lend the Board's securities to broker-dealers and other entities with a simultaneous agreement to return the collateral for the same securities in the future. During the period the securities are on loan, the Board receives a fee and the custodial bank must initially receive collateral equal to 102 percent of the fair value of the loaned securities and maintain collateral equal to not less than 100 percent of the fair value of the loaned security. The Board retains all rights and risks of ownership during the loan period.

During fiscal years 2003 and 2002, State Street lent, on behalf of the Board, certain securities held by State Street, as custodian, and received US dollar currency cash, US government securities, and irrevocable bank letters of credit. State Street does not have the ability to pledge or sell collateral securities unless the borrower defaults.

The Board did not impose any restrictions during fiscal years 2003 and 2002 on the amount of the loans that State Street made on its behalf. There were no failures by any borrowers to return loaned securities or pay distributions thereon during fiscal years 2003 and 2002. Moreover, there were no losses during fiscal years 2003 and 2002 resulting from a default of the borrowers or State Street.

During fiscal years 2003 and 2002, the Board and the borrowers maintained the right to terminate all securities lending transactions on demand. The cash collateral received on each loan was invested, together with the cash collateral of other qualified plan lenders, in a collective investment pool, the Securities Lending Quality Trust. The relationship between the average maturities of the investment pool and the Board's loans was affected by the maturities of the loans made by other plan entities that invested cash collateral in the collective investment pool, which the Board could not determine. On June 30, 2003 and June 30, 2002, the Board had no credit risk exposure to borrowers.

As of June 30, 2003 and June 30, 2002, there were no securities on loan.

4. INVESTMENT RISK CATEGORIES

State of Montana investments are categorized below and on the following page to give an indication of the level of risk assumed at June 30, 2003 and June 30, 2002. Category 1 includes investments that are insured or registered or securities that are held by the Board or its agent in the Board's name. Not Categorized includes investments held by broker-dealers under securities loans with cash collateral.

Risk as of June 30, 2003

Category 1

<u>Security Investment Type</u>	<u>Securities Not On Loan</u>	<u>On Loan for Securities Collateral</u>	<u>Not Categorized</u>	<u>Carrying Amount</u>	<u>Fair Value</u>
Asset-Backed Securities	733,397,874	0	0	733,397,874	733,410,024
Repurchase Agreements	56,000,000	0	0	56,000,000	56,000,000
Variable-Rate (Floating-Rate)	<u>631,005,520</u>	<u>0</u>	<u>0</u>	<u>631,005,520</u>	<u>630,978,190</u>
Total Investment	\$ <u>1,420,403,394</u>	\$ 0	\$ 0	\$ <u>1,420,403,394</u>	\$ <u>1,420,388,214</u>
Securities Lending Collateral Investment Pool		\$ 0	\$ 0	\$ 0	\$ 0

Risk as of June 30, 2002

Category 1

<u>Security Investment Type</u>	<u>Securities Not On Loan</u>	<u>On Loan for Securities Collateral</u>	<u>Not Categorized</u>	<u>Carrying Amount</u>	<u>Fair Value</u>
Commercial Paper	\$ 9,994,408	\$ 0	\$ 0	\$ 9,994,408	\$ 9,994,400
Asset-Backed Securities	912,373,688	0	0	912,373,688	912,371,066
Government Securities	44,400,000	0	0	44,400,000	44,365,368
Repurchase Agreements	44,000,000	0	0	44,000,000	44,000,000
Variable-Rate (Floating-Rate)	<u>491,045,356</u>	<u>0</u>	<u>0</u>	<u>491,045,356</u>	<u>491,222,290</u>
Total Investment	\$ <u>1,501,813,452</u>	\$ 0	\$ 0	\$ <u>1,501,813,452</u>	\$ <u>1,501,953,124</u>
Securities Lending Collateral Investment Pool			\$ 0	\$ 0	\$ 0

STIP investments' credit risk is measured by investment grade ratings given individual securities. Board of Investment's policy requires that STIP investments have the highest rating in the short term category by one and/or any Nationally Recognized Statistical Rating Organizations (NRSRO). The six NRSRO's include Standard and Poors, Moody's, Duff and Phelps, Fitch, IBCA and Thompson's Bank Watch.

Asset-backed securities have less credit risk than do securities not backed by pledged assets, while market risk for asset-backed securities is the same as market risk for similar non asset-backed securities.

While variable-rate securities have credit risk identical to similar fixed-rate securities, their market risk (income) is more sensitive to interest rate changes. However, their market risk (value/price) may be less volatile than fixed-rate securities because their value will usually remain at or near par as a result of their interest rates being periodically reset to maintain a current market yield.

There are no legal risks that the Board is aware of regarding any STIP investments.

5. YEAR END PORTFOLIO

The June 30, 2003 STIP portfolio is listed below. The security type percentage is based on the fair value ratio of the specific security investment type to the total portfolio.

<u>Security Name</u>	<u>Coupon</u>	<u>Maturity</u>	<u>Par</u>	<u>Amortized Cost</u>	<u>Fair Value</u>	<u>% Total</u>
CONCORD MINUTEMEN	discount	07/01/03	50,000,000	50,000,000	49,998,500	3.52%
EAGLE I CBO LTD	discount	07/01/03	23,011,000	23,011,000	23,010,540	1.62%
ZCM MATCHED FUNDING CORP	discount	07/02/03	20,000,000	19,999,261	19,998,000	1.41%
ZCM MATCHED FUNDING CORP	discount	07/03/03	20,000,000	19,998,522	19,998,600	1.41%
ADVANTAGE ASSET SECURITIES CORP	discount	07/07/03	20,000,000	19,995,667	19,996,200	1.41%
NEPTUNE FUNDING CORP	discount	07/08/03	32,255,000	32,246,784	32,247,904	2.27%
RHINELAND FUNDING CAPITAL	discount	07/09/03	20,000,000	19,994,222	19,995,000	1.41%
GOETHAM FUNDING CORP	discount	07/10/03	20,000,000	19,993,450	19,994,400	1.41%
ALTAMIRA FUNDING LLC	discount	07/11/03	20,000,000	19,992,722	19,993,800	1.41%
EAGLE I CBO LTD	discount	07/14/03	22,467,000	22,456,292	22,457,564	1.58%
NEWBURY FUNDS	discount	07/16/03	20,000,000	19,989,083	19,990,600	1.41%
ALTAMIRA FUNDING LLC	discount	07/17/03	20,000,000	19,988,356	19,990,200	1.41%
FAYETTE FUNDING LTD	discount	07/18/03	13,757,000	13,749,529	13,749,709	0.96%
LOCKHART FUNDING LLC	discount	07/18/03	20,000,000	19,987,628	19,989,200	1.41%
NEWBURY FUNDS	discount	07/21/03	15,000,000	14,989,500	14,990,700	1.05%
HERTZ FLEET FUNDING LLC	discount	07/22/03	17,000,000	16,987,604	16,988,950	1.19%
BUNGE ASSET FUNDING	discount	07/23/03	20,000,000	19,984,967	19,986,400	1.41%
BUNGE ASSET FUNDING	discount	07/24/03	20,000,000	19,984,283	19,985,800	1.41%

<u>Security Name</u>	<u>Coupon</u>	<u>Maturity</u>	<u>Par</u>	<u>Amortized Cost</u>	<u>Fair Value</u>	<u>% Total</u>
BAVARIA TRR CORP	discount	07/25/03	17,000,000	16,985,834	16,987,250	1.19%
BRYANT PARK FUNDING LLC	discount	07/28/03	20,000,000	19,982,000	19,983,400	1.41%
EMINENT FUNDING I	discount	07/29/03	20,000,000	19,981,333	19,982,600	1.41%
SUNBELT FUNDING CORP	discount	07/30/03	20,000,000	19,981,472	19,982,200	1.41%
HERTZ FLEET FUNDING LLC	discount	07/31/03	32,240,000	32,210,715	32,210,339	2.26%
ATOMIUM FUNDING CORP	discount	08/01/03	24,588,000	24,566,615	24,564,641	1.72%
NEPTUNE FUNDING CORP	discount	08/04/03	20,000,000	19,980,922	19,979,200	1.41%
TRICON CAPITAL CORP	discount	08/05/03	23,549,000	23,526,105	23,523,803	1.66%
RHINELAND FUNDING CAPITAL	discount	08/06/03	28,446,000	28,416,701	28,414,425	2.00%
DNA FINANCE CORP	discount	08/07/03	20,000,000	19,978,417	19,977,400	1.41%
HUDSON AMERICAN REALTY LLC	discount	08/07/03	40,000,000	39,946,144	39,953,200	2.81%
BAVARIA TRR CORP	discount	08/08/03	20,000,000	19,978,678	19,976,800	1.41%
LOCKHART FUNDING LLC	discount	08/11/03	20,000,000	19,974,944	19,974,800	1.41%
AUTOBAHN FUNDING CO LLC	discount	08/13/03	17,480,000	17,456,824	17,457,101	1.23%
THREE CROWNS FUNDING	discount	08/22/03	17,108,000	17,082,300	17,080,798	1.20%
ASSET-BACKED COMMERCIAL PAPER			733,901,000	733,397,874	733,410,024	51.64%
STATE STREET REPO	0.950	07/01/03	56,000,000	56,000,000	56,000,000	3.94%
REPURCHASE AGREEMENT			56,000,000	56,000,000	56,000,000	3.94%
AMERICAN HONDA FINANCE CORP	1.256	07/11/03	25,000,000	25,000,000	25,002,000	1.76%
AMERICAN EXPRESS CENTURION BANK	1.180	07/15/03	50,000,000	50,000,000	50,001,000	3.52%
K2 USA LLC	1.084	07/21/03	50,000,000	50,000,000	49,999,000	3.52%
AMERICAN HONDA FINANCE CORP	1.270	08/04/03	25,000,000	25,000,000	25,006,250	1.76%
MERRILL LYNCH + CO INC	1.580	08/04/03	39,000,000	39,008,240	39,017,160	2.75%
MHESAC	1.820	01/15/04	7,000,000	7,000,000	6,994,680	0.49%
GOLDMAN SACHS GROUP INC	1.360	02/06/04	40,000,000	40,000,000	39,935,600	2.81%
LINKS FINANCE LLC	1.150	02/17/04	50,000,000	50,000,000	50,061,000	3.52%
TANGO FINANCE CORP	1.289	03/05/04	55,000,000	54,997,280	55,000,000	3.87%
RATHGAR CAPITAL US CORP	1.280	03/08/04	40,000,000	40,000,000	39,996,000	2.82%
STANFIELD VICTORIA FINANCE LTD	1.170	03/15/04	50,000,000	50,000,000	49,997,500	3.52%
WHISTLEJACKET CAPITAL LTD	1.160	03/15/04	50,000,000	50,000,000	49,994,000	3.52%
BELFORD US CAPITAL CO	1.090	03/26/04	50,000,000	50,000,000	49,983,500	3.52%
PARKLAND USA LLC	1.088	04/19/04	50,000,000	50,000,000	49,990,500	3.52%
FIVE FINANCE INC	1.290	04/26/04	50,000,000	50,000,000	50,000,000	3.52%
VARIABLE-RATE(FLOATING RATES)			631,000,000	631,005,520	630,978,190	44.42%
TOTAL STIP			1,420,901,000	1,420,403,394	1,420,388,214	100.00%

LEGISLATIVE AUDIT DIVISION

Scott A. Seacat, Legislative Auditor
John W. Northey, Legal Counsel



Deputy Legislative Auditors:
Jim Pellegrini, Performance Audit
Tori Hunthausen, IS Audit & Operations
James Gillett, Financial-Compliance Audit

INDEPENDENT AUDITOR'S REPORT

The Legislative Audit Committee
of the Montana State Legislature:

We have audited the accompanying Statement of Net Asset Value for the state of Montana Board of Investments, Montana Domestic Equity/Montana Stock Pool, as of June 30, 2003 and 2002, and the related Statement of Changes in Net Asset Value and Statement of Investment Income and Distribution for the fiscal years then ended. These financial statements are the responsibility of the Board of Investments' management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the net asset value of the state of Montana Board of Investments, Montana Domestic Equity/Montana Stock Pool, as of June 30, 2003 and 2002, and its changes in net asset value and investment income and distribution for the fiscal years then ended in conformity with accounting principles generally accepted in the United States of America.

Respectfully submitted,

Signature on File

James Gillett, CPA
Deputy Legislative Auditor

November 4, 2003

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**STATE OF MONTANA BOARD OF INVESTMENTS
MONTANA DOMESTIC EQUITY/MONTANA STOCK POOL FINANCIAL STATEMENTS
STATEMENT OF NET ASSET VALUE JUNE 30, 2003 AND 2002**

<u>Assets</u>	MDEP (Note 1) <u>2003</u>	MTCP (Note 1) <u>2002</u>
Cash	\$	\$ 0
Security lending cash collateral (Notes 3 and 4)	19,085,755	16,128,704
Broker receivable for securities sold but not settled (Note 2)	0	68,588
Dividend receivable	1,917,421	1,533,196
Interest receivable	10,291	31,743
Investments managed at fair value (carrying value of \$2,474,861,073 in 2003 and \$1,829,268,116 in 2002)(Notes 2 and 4)	<u>2,577,470,669</u>	<u>1,883,054,092</u>
Total assets	\$ <u>2,598,484,136</u>	\$ <u>1,900,816,323</u>
 <u>Liabilities</u>		
Income due participants	\$ 2,041,555	\$ 1,478,632
Security lending expense payable	6,778	27,806
Administrative fee payable	18,034	0
Security lending obligations (Notes 3 and 4)	<u>19,085,755</u>	<u>16,128,704</u>
Total liabilities	<u>21,152,122</u>	<u>17,635,142</u>
Net asset value	\$ <u>2,577,332,014</u>	\$ <u>1,883,181,181</u>
Units Outstanding (Note 2)	24,311,482	5,948,621
Unit Value (Note 2)	\$ 106	\$ 317

**STATEMENT OF CHANGES IN NET ASSET VALUE
FOR THE FISCAL YEARS ENDED JUNE 30, 2003 AND 2002**

Net asset value, beginning of year	\$ 1,883,181,181	\$ 2,334,062,490
Value of MTCP units purchased by participants (Note 2)	14,398,568	82,356,740
Value of MTCP units sold by participants (Note 2)	(26,880,630)	(3,952,586)
Transfer of BGI and DFA investments to MDEP (Notes 1 and 2)	740,000,000	0
Value of MDEP units purchased by participants (Note 2)	25,000,000	0
Changes in fair value of investments managed (Note 2)	<u>(58,367,105)</u>	<u>(529,285,463)</u>
Net asset value, end of year	\$ <u>2,577,332,014</u>	\$ <u>1,883,181,181</u>

**STATEMENT OF INVESTMENT INCOME AND DISTRIBUTION
FOR THE FISCAL YEARS ENDED JUNE 30, 2003 AND 2002**

Investment income (Note 2)	\$ 29,807,948	\$ 28,439,057
Security lending income	382,440	592,676
Security lending expense	(308,191)	(488,155)
Administrative expenses (Note 2)	(984,146)	(1,030,112)
Income due participants, beginning of year	<u>1,478,632</u>	<u>720,694</u>
Income available for distribution	30,376,683	28,234,160
Distribution (Note 2)	<u>28,335,128</u>	<u>26,755,528</u>
Income due participants, end of year	\$ <u>2,041,555</u>	\$ <u>1,478,632</u>

The accompanying notes are an integral part of these financial statements.

STATE OF MONTANA BOARD OF INVESTMENTS
MONTANA DOMESTIC EQUITY/MONTANA STOCK POOL - NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2003 AND 2002

1. HISTORY AND ORGANIZATION

The Board was created by an act of the Legislature to invest and manage the State of Montana's investment funds on a centralized basis. The Montana Common Stock Pool (MTCP) was created by the Board to allow retirement and endowment funds, per section 17-6-201, MCA, the opportunity to participate in the equity market via a diversified pool. MTCP was created as of July 1, 1980, by the transfer of all common stock owned by the Public Employees' Retirement System, Teachers' Retirement System, and other funds into MTCP.

In March 1996, the Board approved the Investment Policy Statement to reflect the name change from the Montana Common Stock Pool to the Montana Stock Pool. The Montana Stock Pool is referred to as "Montcomp" or MTCP. This policy statement provided for the investment in common or preferred stock. The Investment Policy Statement was revised and approved in September 1996 to allow the investment in securities convertible into common or preferred stocks. In June 2000, the Board revised and approved the Investment Policy Statement to allow the investment in equity derivatives.

The board established creation of the Montana Domestic Equity Pool (MDEP) in April 2003. Effective May 1, 2003, the Public Employees', Municipal Police Officers', Game Wardens', Sheriffs', Judges', Highway Patrol Officers', Teachers', Volunteer Firefighters' and Firefighters' Unified retirement funds transferred all the Barclays Global Investors (BGI) S&P 500 Equity Index Fund A and the Dimensional Fund Advisors (DFA) US Small Cap Trust investments totaling \$740 million, at cost, from the All Other Funds portfolio to the new pool. The BGI investments were previously recorded in the All Other Funds financial statements for fiscal year 2002. The pension and endowment funds also exchanged their investment in the Montana Stock Pool (MTCP) for units in the new Montana Domestic Equity Pool (MDEP).

These financial statements present the Net Asset Value, Changes in Net Asset Value and Investment Income and Distribution of the Montana Domestic Equity Pool, as of June 30, 2003 and the fiscal year then ended, and the Net Asset Value, Changes in Net Asset Value and Investment Income and Distribution of the Montana Stock Pool as of June 30, 2002 and the fiscal year then ended.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Investments

MDEP/MTCP investments are purchased in accordance with the statutorily mandated "Prudent Expert Principle". The MDEP/MTCP portfolio may include common stock, equity index, preferred stock, convertible equity securities and equity derivatives. Common stock represents ownership units (shares) of a public corporation. Common stock owners are entitled to vote on director selection and other important matters as well as receive dividends on their holdings. Equity index investments are investments in selected mutual funds whose equity portfolios match a broad based index or composite. Preferred stock, as a class of stock, pays dividends at a specified rate and has preference in the payment of dividends and liquidation of assets. Preferred stock holders, ordinarily, do not have voting rights. Convertible securities are securities carrying the right to exchange, or "convert" the instrument for other securities of the issuer or of another issuer. This definition most often applies to preferred stocks or corporate bonds carrying the right to exchange for a fixed number of shares of the issuer's common stock. Equity derivatives "derive" their value from other equity instruments such as futures and options.

In June 2000, the Board approved a staff recommendation to securitize MTCP cash by investing in an equity derivative, the State Street Stock Performance Index Futures Fund (SPIFF). Portfolio cash is swept daily into SPIFF maintaining 100% equity exposure through holdings of stock index futures.

The MDEP, as an internal investment pool, invested its excess cash, on creation, in the Board's Short Term Investment Pool, STIP, an external investment pool. An external investment pool commingles the moneys of more than one legally separate entity and invests, on the participants' behalf, in an investment portfolio. STIP participants include both state agencies and local governments. By meeting certain conditions, STIP, as a 2a7-like pool, is allowed to use amortized cost rather than fair value to report net assets to compute unit values. In July 2003, the STIP account was closed and a SPIFF account was opened to securitize MDEP cash by investing in an equity derivative.

In January 2003, the Board approved a staff recommendation to hire Dimensional Fund Advisors, as an external manager, to invest in domestic small market capitalization (small cap) companies. Market capitalization refers to the value of a corporation as determined by the market price of its issued and outstanding common stock. US Small Cap companies are those companies whose market capitalization comprises the smallest 8 percent of the total market universe. The total market universe is defined as the aggregate capitalization of the NYSE, AMEX and NASDAQ firms.

Investments are presented in the statement of Net Asset Value at fair value. Equity investments, on valuation date, are stated at the closing price of the security's primary exchange. Carrying value, parenthetically disclosed, represents the equity security purchase price plus a fixed commission where applicable.

The increase in the fair and carrying values of the MDEP portfolio as of June 30, 2003 as compared to fair and carrying values of the MTCP portfolio as of June 30, 2002 is attributed, primarily, to the \$740 million transfer, at cost, of the BGI and DFA investments to the MDEP on May 1, 2003.

Participant Units

The Public Employees' Retirement System and the Teachers' Retirement System transferred all stock owned into MTCP at the start-up date and were issued units according to the fair value of their contribution, retaining their original total cost basis. The initial unit value as of July 1, 1980, was \$1,000. Unit values thereafter and until March 31, 2000 were calculated weekly and at the close of the last business day of the month, based on the fair value of MTCP equity holdings and other assets. Effective April 1, 2000, the unit values are calculated daily. Daily unit value calculations were discontinued as of January 1, 2003. Since January 2003, MTCP unit values are calculated weekly and at the close of the last business day of the month. Depending on stock market conditions and the investment officer's decision, MDEP participants may then buy or sell units on the first calendar day of each month.

On July 1, 1994, the initial unit value changed from \$1,000 to \$100. This change was required for the Board's new accounting system. On August 17, 2000, shareholders, on record, received one MTCP share for each MTCP share held as the result of a 2:1 split. The unit value on August 31, 2000, prior to the split, was \$1,014 while the unit value, after the split, was \$507.

On May 1, 2003, the pension funds transferred all the Barclays Global Investors (BGI) S&P 500 Equity Index Fund A and the Dimensional Fund Advisors (DFA) US Small Cap Trust investments, at cost, to the MDEP. On the same date, the pension and endowment funds transferred their MTCP investments, at cost, to the MDEP. The pension and endowment funds were issued units according to the fair value of each participant's portfolio. The initial MDEP unit value on May 1, 2003 was \$100. On conversion date, MTCP participants exchanged approximately 5.8 million MTCP units, valued at \$302 per unit, for 24.1 million MDEP units, issued at \$100 per unit.

As reported in the Statement of Changes in Net Asset Value, the value of MTCP units purchased by participants decreased \$68 million in fiscal year 2003 while the value of MTCP units sold increased by \$23 million based on changes in the market. The \$82 million in participant purchases in fiscal year 2002 reflect investment opportunities given the market conditions. The fiscal year 2003 and 2002 changes are the result of an asset allocation decision and do not reflect a change from the stated investment policy to increase retirement fund exposure to equity investments. MTCP participant purchases and sales from July 2002 to March 2003 were based on a MTCP per unit value ranging from \$259 per unit to \$308 per unit. In June 2003, the MDEP participants purchased units at \$105 per unit to fund \$25 million for the DFA US Small Cap Trust. The increase of \$471 million in the Change in Fair Value of Investments Managed reflects the equity market appreciation since fiscal year 2002.

Broker Receivable/Payable

MDEP/MTCP security transactions are recorded as of trade date rather than settlement date. Because of this generally accepted practice, the MDEP/MTCP portfolio at June 30 may include receivables from brokers for securities sold but not delivered, and payables to brokers for securities purchased but not received.

Other

Investment income reported in the Statement of Investment Income and Distribution includes dividend accruals, tax reclaim accruals, SPIFF gain/losses and miscellaneous income. MDEP/MTCP dividends are recorded on the ex-dividend date.

The MDEP/MTCP Income Available for Distribution is distributed as of the first calendar day of each month.

Administrative expenses incurred by the Board are charged daily to MDEP/MTCP based on the Board's expenses applicable to MDEP/MTCP. For fiscal year 2003, these expenses include \$966,446 for the Board and the custodial bank contract and \$17,700 in accruals for external manager fees. The fiscal year 2002 administrative expenses of \$1,030,112 represent Board expense and custodial bank contract fees.

3. SECURITIES LENDING

Under the provisions of state statutes, the Board has, via a Securities Lending Authorization Agreement, authorized the custodial bank, State Street Bank and Trust, to lend the Board's securities to broker-dealers and other entities with a simultaneous agreement to return the collateral for the same securities in the future. During the period the securities are on loan, the Board receives a fee and the custodial bank must initially receive collateral equal to 102 percent of the fair value of the loaned securities and maintain collateral equal to not less than 100 percent of the fair value of the loaned security. The Board retains all rights and risks of ownership during the loan period.

During fiscal years 2003 and 2002, State Street lent, on behalf of the Board, certain securities held by State Street, as custodian, and received US dollar currency cash, US government securities, and irrevocable bank letters of credit. State Street does not have the ability to pledge or sell collateral securities unless the borrower defaults.

The Board did not impose any restrictions during fiscal years 2003 and 2002 on the amount of the loans that State Street made on its behalf. There were no failures by any borrowers to return loaned securities or pay distributions thereon during fiscal years 2003 and 2002. Moreover, there were no losses during fiscal years 2003 and 2002 resulting from a default of the borrowers or State Street.

During fiscal years 2003 and 2002, the Board and the borrowers maintained the right to terminate all securities lending transactions on demand. The cash collateral received on each loan was invested, together with the cash collateral of other qualified plan lenders, in a collective investment pool, the Securities Lending Quality Trust. The relationship between the average maturities of the investment pool and the Board's loans was affected by the maturities of the loans made by other plan entities that invested cash collateral in the collective investment pool, which the Board could not determine. On June 30, 2003 and June 30, 2002, the Board had no credit risk exposure to borrowers.

As of June 30, 2003, the carrying and fair values of the underlying securities on loan for the Montana Stock Pool were \$19,578,118 and \$18,747,547 respectively. The collateral provided for the securities on loan totaled \$19,085,755 in cash.

As of June 30, 2002, the carrying and fair values of the underlying securities on loan for the Montana Stock Pool were \$20,924,469 and \$15,748,477 respectively. The collateral provided for the securities on loan totaled \$16,128,704 in cash.

4. INVESTMENT RISK CATEGORIES

State of Montana investments are categorized on the next page to give an indication of the level of risk assumed at June 30, 2003 and June 30, 2002. Category 1 includes investments that are insured or registered or securities that are held by the Board or its agent in the Board's name. Not Categorized includes investments held by broker-dealers under securities loans with cash collateral.

Risk as of June 30, 2003

Category 1

<u>Security Investment Type</u>		<u>Securities Not On Loan</u>		<u>On Loan for Securities Collateral*</u>		<u>Not Categorized*</u>		<u>Carrying Amount</u>		<u>Fair Value</u>
Common Stock Pool	\$	1,655,692,724	\$	0	\$	19,578,118	\$	1,675,270,842	\$	1,817,071,361
Equity Index Fund		710,000,000		0		0		710,000,000		661,781,844
DFA Small Cap Subtrust		55,000,000		0		0		55,000,000		62,981,234
SPIFF		34,575,711		0		0		34,575,711		35,621,710
STIP		<u>14,520</u>		<u>0</u>		<u>0</u>		<u>14,520</u>		<u>14,520</u>
Total Investment	\$	<u>2,455,282,955</u>	\$	<u>0</u>	\$	<u>19,578,118</u>	\$	<u>2,474,861,073</u>	\$	<u>2,577,470,669</u>
Securities Lending Collateral Investment Pool				\$		<u>19,085,755</u>		<u>19,085,755</u>		<u>19,085,755</u>

* At June 30, 2003, the underlying securities with fair values of \$18,747,547 were loaned for cash collateral under a security lending agreement with the state's agent.

Risk as of June 30, 2002

Category 1

<u>Security Investment Type</u>		<u>Securities Not On Loan</u>		<u>On Loan for Securities Collateral*</u>		<u>Not Categorized*</u>		<u>Carrying Amount</u>		<u>Fair Value</u>
Common Stock Pool	\$	1,802,361,379	\$	0	\$	20,924,469	\$	1,823,285,848	\$	1,877,185,006
SPIFF		<u>5,982,268</u>		<u>0</u>		<u>0</u>		<u>5,982,268</u>		<u>5,869,086</u>
Total Investment	\$	<u>1,808,343,647</u>	\$	<u>0</u>	\$	<u>20,924,469</u>	\$	<u>1,829,268,116</u>	\$	<u>1,883,054,092</u>
Securities Lending Collateral Investment Pool				\$		<u>16,128,704</u>		<u>16,128,704</u>		<u>16,128,704</u>

* At June 30, 2002, the underlying securities with fair values of \$15,748,477 were loaned for cash collateral under a security lending agreement with the state's agent.

5. OWENS-CORNING COMPLAINT

On October 11, 2002, the Board received a summons and complaint regarding the bankruptcy of Owens-Corning. The company seeks a determination that the dividend payments paid from October 1996 through July 2000 represent "fraudulent transfers under Chapter 11 Bankruptcy provisions and applicable state law, and are, therefore, voidable". The complaint states the Montana Board of Investments was the "recipient of dividends in the amount of \$357,099 for the relevant period". The Board has prepared a response to the complaint.

6. YEAREND PORTFOLIO

The June 30, 2003 MDEP portfolio is listed below. The security type percentage is based on the fair value ratio of the specific security investment type to the total portfolio.

<u>Security Name</u>	<u>Shares</u>	<u>Carrying Value</u>	<u>Fair Value</u>	<u>% of Total</u>
PFIZER INC	2,107,260	81,610,871	71,962,929	2.79%
MICROSOFT CORP	2,780,000	106,343,751	71,195,800	2.76%
GENERAL ELECTRIC CO	2,272,300	45,881,708	65,169,564	2.53%
CITIGROUP INC	1,483,866	25,334,534	63,509,465	2.46%
EXXON MOBIL CORP	1,462,912	39,595,791	52,533,170	2.04%
WAL MART STORES INC	800,000	41,490,700	42,936,000	1.67%
JOHNSON + JOHNSON	822,000	15,464,327	42,497,400	1.65%
AMERICAN INTERNATIONAL GROUP INC	693,750	35,332,768	38,281,125	1.49%
VERIZON COMMUNICATIONS	953,308	28,159,436	37,608,001	1.46%
WELLS FARGO + CO	700,000	11,979,499	35,280,000	1.37%
MERCK + CO INC	539,000	12,452,641	32,636,450	1.27%
J P MORGAN CHASE + CO	903,900	31,341,979	30,895,302	1.20%
INTEL CORP	1,450,000	9,366,714	30,136,800	1.17%
ABBOTT LABS	640,000	5,975,860	28,006,400	1.09%
INTERNATIONAL BUSINESS MACHINES	330,000	11,585,065	27,225,000	1.06%
COCA COLA CO	565,000	29,003,390	26,221,650	1.02%
AMERICAN EXPRESS CO	605,000	9,945,966	25,295,050	0.98%
CHEVRONTEXACO CORP	344,350	21,736,657	24,862,070	0.96%
BANK NEW YORK INC	840,000	38,384,653	24,150,000	0.94%
CISCO SYSTEMS INC	1,405,000	17,000,582	23,308,950	0.90%
DELL COMPUTER CORP	710,000	25,926,917	22,691,600	0.88%
UNITED TECHNOLOGIES CORP	320,000	10,837,605	22,665,600	0.88%
HOME DEPOT INC	670,000	24,260,388	22,190,400	0.86%
VIACOM INC	500,000	20,803,600	21,830,000	0.85%
CATERPILLAR INC	360,000	17,188,238	20,037,600	0.78%
DISNEY WALT CO	1,013,000	29,779,676	20,006,750	0.78%
MORGAN STANLEY	450,000	22,188,987	19,237,500	0.75%
WYETH	420,000	23,634,910	19,131,000	0.74%
ORACLE CORP	1,586,000	22,676,062	19,063,720	0.74%
BEST BUY CO INC	430,000	15,534,420	18,885,600	0.73%
SBC COMMUNICATIONS INC	727,400	20,127,789	18,585,070	0.72%
AMGEN INC	270,000	13,319,963	18,084,600	0.70%
TEXAS INSTRUMENTS INC	1,000,000	42,638,196	17,600,000	0.68%
DU PONT E I DE NEMOURS + CO	420,000	16,355,048	17,488,800	0.68%
NASDAQ 100 TRACKING	580,670	18,146,769	17,391,067	0.67%
ALCOA INC	656,600	21,913,342	16,743,300	0.65%
OMNICOM GROUP	232,000	15,365,117	16,634,400	0.65%
BANK AMERICA CORP	210,000	14,803,700	16,596,300	0.64%
AFLAC INC	531,200	16,579,715	16,334,400	0.63%
COMCAST CORP NEW	535,000	13,235,748	16,146,300	0.63%
PROCTER + GAMBLE CO	180,000	15,090,608	16,052,400	0.62%
MELLON FINANCIAL CORP	575,000	25,921,505	15,956,250	0.62%
ALTRIA GROUP INC	350,000	12,931,925	15,904,000	0.62%
MARSH + MCLENNAN COS INC	306,400	12,478,831	15,647,848	0.61%
KIMBERLY CLARK CORP	297,200	15,491,102	15,496,008	0.60%
EMC CORP	1,480,000	24,351,015	15,495,600	0.60%
CARDINAL HEALTH INC	240,000	14,888,490	15,432,000	0.60%
AUTOMATIC DATA PROCESSING INC	441,300	12,879,834	14,942,418	0.58%
COSTCO WHOLESALE CORP NEW	407,000	14,420,906	14,896,200	0.58%
EMERSON ELECTRIC CO	290,000	10,404,177	14,819,000	0.57%
FLEETBOSTON FINANCIAL CORP	489,500	10,113,595	14,543,045	0.56%
BRISTOL MYERS SQUIBB CO	509,000	20,882,003	13,819,350	0.54%

<u>Security Name</u>	<u>Shares</u>	<u>Carrying Value</u>	<u>Fair Value</u>	<u>% of Total</u>
WEYERHAEUSER CO	247,200	14,085,568	13,348,800	0.52%
MBNA CORP	600,000	11,209,405	12,504,000	0.49%
FIRST DATA CORP	300,000	10,565,785	12,432,000	0.48%
TYCO INTERNATIONAL LTD	650,000	8,294,033	12,337,000	0.48%
SYSCO CORP	410,000	11,779,895	12,316,400	0.48%
3M CO	93,800	9,468,540	12,098,324	0.47%
HEWLETT PACKARD CO	540,000	10,896,552	11,502,000	0.45%
AMDOCS LTD	477,700	13,692,324	11,464,800	0.44%
LILLY ELI + CO	160,000	9,970,910	11,035,200	0.43%
ALLTEL CORP	225,100	13,865,946	10,854,322	0.42%
UNITED PARCEL SERVICE INC	170,000	10,415,524	10,829,000	0.42%
AMBAC FINANCIAL GROUP INC	163,200	8,486,207	10,812,000	0.42%
INGERSOLL RAND COMPANY LIMITED	225,000	9,067,468	10,647,000	0.41%
AOL TIME WARNER INC	652,500	23,791,010	10,498,725	0.41%
BANK ONE CORP	280,000	9,881,272	10,410,400	0.40%
CONOCOPHILLIPS	187,080	11,179,840	10,251,984	0.40%
NOKIA CORP	619,800	3,390,239	10,183,314	0.40%
FRANKLIN RESOURCES INC	260,000	9,912,609	10,158,200	0.39%
FIFTH THIRD BANCORP	170,000	9,766,738	9,747,800	0.38%
SCHLUMBERGER LTD	200,000	11,070,456	9,514,000	0.37%
HONEYWELL INTERNATIONAL INC	350,000	11,114,280	9,397,500	0.36%
MARRIOTT INTERNATIONAL INC	236,600	9,430,734	9,090,172	0.35%
WATERS CORP	310,000	10,565,259	9,030,300	0.35%
WALGREEN CO	300,000	8,915,910	9,030,000	0.35%
ROYAL DUTCH PETROLEUM CO	188,800	10,078,555	8,801,856	0.34%
FEDERAL NATIONAL MTG ASSN	125,000	7,394,025	8,430,000	0.33%
CVS CORP	300,000	11,684,667	8,409,000	0.33%
UNION PACIFIC CORP	143,800	6,340,672	8,343,276	0.32%
WACHOVIA CORP	200,000	7,308,200	7,992,000	0.31%
TARGET CORP	200,000	4,234,527	7,568,000	0.29%
REEBOK INTERNATIONAL LTD	224,600	5,485,812	7,553,298	0.29%
GOLDMAN SACHS GROUP INC	90,000	7,774,885	7,537,500	0.29%
BOSTON SCIENTIFIC CORP	120,000	7,316,496	7,332,000	0.28%
MGIC INVESTMENT CORP WIS	155,000	9,726,764	7,229,200	0.28%
CHUBB CORP	120,000	6,591,192	7,200,000	0.28%
MEDTRONIC INC	150,000	6,582,300	7,195,500	0.28%
INTERNATIONAL PAPER CO	200,000	7,376,940	7,146,000	0.28%
CONAGRA INC	300,000	7,290,615	7,080,000	0.27%
HARLEY DAVIDSON INC	175,000	8,021,470	6,975,500	0.27%
DARDEN RESTAURANTS INC	366,000	6,730,081	6,946,680	0.27%
COMPUTER SCIENCES CORP	166,600	8,323,714	6,350,792	0.25%
GUIDANT CORP	142,500	5,021,772	6,325,575	0.25%
BP PLC	150,000	5,902,290	6,303,000	0.24%
ANADARKO PETE CORP	140,000	6,296,780	6,225,800	0.24%
KOHL'S CORP	120,000	6,314,400	6,165,600	0.24%
BIOMET INC	198,900	5,516,600	5,700,474	0.22%
AUTOZONE INC	75,000	5,252,783	5,697,750	0.22%
JOHN HANCOCK FINANCIAL SERVICES	181,400	7,105,120	5,574,422	0.22%
FORTUNE BRANDS INC	100,000	4,341,233	5,220,000	0.20%
CLOROX CO	120,200	5,125,881	5,126,530	0.20%
JOHNSON CONTROLS INC	55,000	4,420,422	4,708,000	0.18%
BAXTER INTERNATIONAL INC	180,000	4,976,774	4,680,000	0.18%
ELECTRONIC DATA SYSTEM CORP	206,700	4,779,556	4,433,715	0.17%
KNIGHT RIDDER INC	50,000	3,456,564	3,446,500	0.13%
XILINX INC	127,100	2,744,852	3,216,901	0.12%
SCHERING PLOUGH CORP	140,000	1,781,326	2,604,000	0.10%

<u>Security Name</u>	<u>Shares</u>	<u>Carrying Value</u>	<u>Fair Value</u>	<u>% of Total</u>
COMMON STOCK POOL TOTAL	1,924,496	1,675,270,842	1,817,071,361	70.50%
S & P 500 INDEX FUND A	2,583,931	710,000,000	661,781,844	25.68%
EQUITY INDEX FUND	2,583,931	710,000,000	661,781,844	25.68%
DIMENSIONAL FUND ADVISORS INC	103,702	55,000,000	62,981,234	2.44%
DFA SMALL CAP SUBTRUST	103,702	55,000,000	62,981,234	2.44%
STATE STREET SPIFF	287,927	34,575,711	35,621,710	1.38%
TOTAL EQUITY FUTURES	287,927	34,575,711	35,621,710	1.38%
SHORT TERM INVESTMENT POOL (STIP)	14,520	14,520	14,520	0.00%
CASH EQUIVALENTS	14,520	14,520	14,520	0.00%
MDEP TOTAL	<u>54,914,575</u>	<u>2,474,861,073</u>	<u>2,577,470,669</u>	<u>100.00%</u>

LEGISLATIVE AUDIT DIVISION

Scott A. Seacat, Legislative Auditor
John W. Northey, Legal Counsel



Deputy Legislative Auditors:
Jim Pellegrini, Performance Audit
Tori Hunthausen, IS Audit & Operations
James Gillett, Financial-Compliance Audit

INDEPENDENT AUDITOR'S REPORT

The Legislative Audit Committee
of the Montana State Legislature:

We have audited the accompanying Statement of Net Asset Value for the state of Montana Board of Investments, Montana International Equity Pool, as of June 30, 2003 and 2002, and the related Statement of Changes in Net Asset Value and Statement of Investment Income and Distribution for the fiscal years then ended. These financial statements are the responsibility of the Board of Investments' management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the net asset value of the state of Montana Board of Investments, Montana International Equity Pool, as of June 30, 2003 and 2002, and its changes in net asset value and investment income and distribution for the fiscal years then ended in conformity with accounting principles generally accepted in the United States of America.

Respectfully submitted,

Signature on File

James Gillett, CPA
Deputy Legislative Auditor

November 4, 2003

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**STATE OF MONTANA BOARD OF INVESTMENTS
MONTANA INTERNATIONAL EQUITY POOL FINANCIAL STATEMENTS**

STATEMENT OF NET ASSET VALUE JUNE 30, 2003 AND 2002

	<u>2003</u>	<u>2002</u>
<u>Assets</u>		
Cash	\$ 868,216	\$ 423,676
Security lending cash collateral (Notes 3 and 4)	78,496,331	67,179,838
Broker receivable for securities sold but not settled (Note 2)	953,991	2,109,271
Dividend and interest receivable	1,018,759	1,286,973
Investments managed at fair value (cost of \$489,383,398 in 2003 and \$442,872,610 in 2002) (Notes 2 and 4)	<u>470,729,781</u>	<u>429,605,702</u>
Total assets	\$ <u>552,067,078</u>	\$ <u>500,605,460</u>
<u>Liabilities</u>		
Income due participants	\$ 771,639	\$ 864,830
Broker payable for securities purchased but not settled (Note 2)	25,723,955	2,983,570
Security lending obligations (Note 3)	78,496,331	67,179,838
Security lending expense payable	52,149	79,443
Due to other funds	35,604	37,728
Unrealized foreign exchange market gain (loss)	(16,024)	(46,630)
Administrative fee payable	<u>335,584</u>	<u>356,125</u>
Total liabilities	<u>105,399,238</u>	<u>71,454,904</u>
Net asset value	\$ <u>446,667,840</u>	\$ <u>429,150,556</u>
Units Outstanding (Note 2)	5,356,076	4,709,766
Unit Value (Note 2)	\$ 83.39	\$ 91.12

**STATEMENT OF CHANGES IN NET ASSET VALUE
FOR THE FISCAL YEARS ENDED JUNE 30, 2003 AND 2002**

Net asset value, beginning of year	\$ 429,150,556	\$ 389,819,983
Value of units purchased by participants (Note 2)	51,046,000	72,500,000
Value of units sold by participants	(53,957)	0
Changes in current value of investments managed	<u>(33,474,759)</u>	<u>(33,169,427)</u>
Net asset value, end of year	\$ <u>446,667,840</u>	\$ <u>429,150,556</u>

**STATEMENT OF INVESTMENT INCOME AND DISTRIBUTION
FOR THE FISCAL YEARS ENDED JUNE 30, 2003 AND 2002**

Investment income (Note 2)	\$ 9,960,157	\$ 7,991,237
Security lending income	1,042,890	1,429,420
Security lending expense	(671,198)	(1,081,010)
Administrative expenses (Note 2)	(1,785,948)	(1,774,996)
Income due participants, beginning of year	<u>864,830</u>	<u>694,026</u>
Income available for distribution	9,410,731	7,258,677
Distribution (Note 2)	<u>8,639,092</u>	<u>6,393,847</u>
Income due participants, end of year	\$ <u>771,639</u>	\$ <u>864,830</u>

The accompanying notes are an integral part of these financial statements.

**STATE OF MONTANA BOARD OF INVESTMENTS
MONTANA INTERNATIONAL EQUITY POOL**

**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2003 and 2002**

1. HISTORY AND ORGANIZATION

The Board was created by an act of the Legislature to invest and manage the State of Montana's investment funds on a centralized basis. The Montana International Equity Pool (MTIP) was created by the Board to allow qualifying funds, per section 17-6-201, MCA, the opportunity to participate in the international equity market via a diversified pool. MTIP, approved by the Board in June 1996, consists of one pool investing in one or more separate funds. Currently, MTIP has investments with an internally managed fund, BOI Internal International, and four externally managed funds, Pyrford International, Schroder Investment Management NA, SG Yamaichi Asset Management Co., formerly SG Pacific Asset Management Inc. and Barclays Global Investors. On January 3, 1997, the MTIP was funded by the Public Employees', Municipal Police Officers', Game Wardens', Sheriffs', Judges', Highway Patrol Officers', Teachers', Volunteer Firefighters' and Firefighters' Unified retirement funds.

In fiscal year 2003, the Board funded external managers, Pyrford International, \$27 million, and Schroder Investment Management NA, \$9 million, for a total active investment funding of \$36 million. In May 2003, the Board funded the Barclays Global Investors (BGI) – MSCI Europe Index Fund with an initial \$15 million investment.

In fiscal year 2002, the Board funded \$15 million to BOI Internal International, \$12.5 million to SG Yamaichi Asset Management Co., formerly SG Pacific Asset Management, Inc., \$20 million to Pyrford International, and \$25 million to Schroder Investment Management NA for a total funding of \$72.5 million. In December 2002, SG Yamaichi Asset Management Co., formerly SG Pacific Asset Management Inc. changed its name to SG Yamaichi Asset Management Co.

Schroder Investment Management NA, and SG Yamaichi Asset Management Co., formerly SG Pacific Asset Management Inc., selected by the Board in October 1996, are authorized to invest in 11 Pacific Basin countries. These countries are Australia, China/Hong Kong, Indonesia, Japan, Korea, Malaysia, New Zealand, Philippines, Singapore, Taiwan and Thailand.

As approved by the Board, the BOI Internal International fund may invest in 20 European, North and South American countries. These countries are listed as follows:

Argentina	Chile	Ireland	Portugal
Austria	Denmark	Italy	Spain
Belgium	Finland	Mexico	Sweden
Brazil	Germany	Netherlands	Switzerland
Canada	Greece	Norway	United Kingdom

In March 2003, the Board voted to liquidate all BOI Internal International holdings in France. On October 30, 2003, the Board voted to add France to list of approved countries for the BOI Internal International portfolio. In October 2001, the Board added Greece to the list of approved countries.

In August 1998, the Board selected Pyrford International, as an external investment manager for Europe. With the exception of the North and South American countries of Canada, Argentina, Brazil, Chile, and Mexico, Pyrford International, as approved by the Board, may invest in the European countries listed above including France.

In August 2003, the Board invested in the BGI All Country Pacific Index Strategy Fund with an initial funding of \$15 million.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Investments

MTIP investments are purchased in accordance with the statutorily mandated "Prudent Expert Principle". The MTIP portfolio includes equity investments in five funds - BOI Internal International, Pyrford International, Schroder Investment Management NA, SG Yamaichi Asset Management Co., formerly SG Pacific Asset Management Inc. and the BGI - MSCI Europe Index Fund. The five funds may invest in securities of foreign-based corporations listed on legal and recognized foreign exchanges as well as domestic exchanges. Security types may include ordinary common shares, preferred shares, convertible securities, American Depositary Receipts (ADR's), Global Depositary Receipts (GDR's), and other global securities, as appropriate.

Common stock represents ownership units (shares) of a public corporation. Common stock owners are entitled to vote on director selection and other important matters as well as receive dividends on their holdings. Preferred stock pays a stipulated dividend and has a claim prior to that of common stock upon the earnings of a corporation. Convertible securities are securities carrying the right to exchange, or "convert" the instrument for other securities of the issuer or of another issuer. ADR's are receipts issued by a US depositary bank representing shares of a foreign stock or bonds held abroad by the foreign sub-custodian of the American depositary bank. GDR's are receipts issued by non-US bank depositaries, which represent shares of a foreign stock or bonds.

Broker Receivable/Payable

MTIP security transactions are recorded as of the trade date rather than settlement date. Because of this generally accepted practice, the MTIP portfolio at June 30 may include receivables from brokers for securities sold, but not delivered, and payables to brokers for securities purchased, but not received.

Valuation and Foreign Currency

Investments are presented in the statement of Net Asset Value at current US dollar value. The MTIP's fair value is derived from the Net Asset Value Per Share, as separately calculated, for the five funds - BOI Internal International, Pyrford International, Schroder Investment Management NA, SG Yamaichi Asset Management Co., formerly SG Pacific Asset Management Inc. and the BGI - MSCI Europe Index Fund. Each fund's Net Asset Value Per Share represents the per unit ownership of the fund's Net Assets. The Net Assets are the excess of the valued securities, cash, receivables and other assets over the fund's liabilities. Each fund's Net Assets are reported at current US dollar value after conversion, by the custodial bank, State Street Bank and Trust, from the foreign currency amounts.

State Street Bank, as custodian, is responsible for reporting the foreign currency transactions in both the local and base or functional (US dollar) currency. The five funds' cash, receivables, fair value of investment securities, other assets and liabilities are translated into US dollars at the Interactive Data Control (IDC) 11:00 a.m. Eastern Standard Time (EST) exchange rate as of the balance sheet date. Purchases and sales of investment securities, income and expenses are converted into US dollars using the Reuters noon EST exchange rate on the transaction date.

Currency exposures may be hedged, partially or fully, at the discretion of the manager to preserve the US dollar value of investments made. Currency speculation, such as over-hedging, reverse hedging or other trading activity not specifically aimed at preserving the US dollar value of investments, is not authorized.

Fair values for the funds holding the publicly traded securities are determined by reference to market prices supplied to the Board by the Board's custodial bank, State Street Bank and their primary pricing service, IDC. Equity investments, traded on a national security exchange, are stated at the last reported sales price on valuation day, while equity securities traded in the over-the-counter market are stated at the last quoted bid price.

Participant Units

The Public Employees', Municipal Police Officers', Game Wardens', Sheriffs', Judges', Highway Patrol Officers', Teachers', Volunteer Firefighters' and Firefighters' Unified retirement funds sold units in the Short Term Investment Pool at the start up date and were issued units in MTIP at an initial unit value of \$100. Unit values thereafter are calculated weekly and once a month at the close of the last business day of the month, based upon

the fair value of the MTIP equity holdings, other assets and liabilities. Based on the investment officers' decision, participants may then buy or sell units on the first business day of each month. All participant buys or sells occur after distribution of accumulated income.

Investment Income and Distribution

Investment Income represents the monthly income distributions to the MTIP from the investment manager funds. The funds' income distributions include dividends accrued as of the ex-dividend date, interest, tax refunds and securities lending income, and related income currency gains/losses. Income currency gains/losses result from the difference between the amount of dividend, interest and foreign withholding taxes accrued for the fund in US dollars and the amount received or paid in equivalent US dollars.

Realized gains/losses from the sale of securities and related foreign exchange transactions are retained by each fund. Realized foreign exchange gains/losses arise from sales and maturities of portfolio securities, sales of foreign currencies, and currency gains/losses realized between the trade and settlement dates.

The fiscal year 2003 administrative expense of \$1,785,948 represents \$1,358,700 in quarterly fees accrued and paid to the external managers per their contracts, and \$427,248 in monthly charges accrued and paid to the Board of Investments. The Board of Investments fee includes costs for the custodial bank contract. Administrative expenses incurred by the Board are charged daily to MTIP based on the Board's expenses applicable to MTIP.

The fiscal year 2002 administrative expense of \$1,774,996 represents \$1,322,540 in quarterly fees accrued and paid to the external managers per their contracts and \$452,456 in monthly charges accrued and paid to the Board of Investments. The Board of Investments fee includes costs for the custodial bank contract

The MTIP Income Available for Distribution is distributed at least monthly to the retirement fund participants, net of external manager fees and administrative expenses, on the first business day of the following month.

3. SECURITIES LENDING

Under the provisions of state statutes, the Board has, via a Securities Lending Authorization Agreement, authorized the custodial bank, State Street Bank and Trust, to lend the Board's securities to broker-dealers and other entities with a simultaneous agreement to return the collateral for the same securities in the future. During the period the securities are on loan, the Board receives a fee and the custodial bank must initially receive collateral equal to 105 percent of the fair value of the loaned securities and maintain collateral equal to not less than 100 percent of the fair value of the loaned security. The Board retains all rights and risks of ownership during the loan period.

During fiscal years 2003 and 2002, State Street lent, on behalf of the Board, certain securities held by State Street, as custodian, and received US dollar and foreign currency cash, US government securities, sovereign debt of foreign countries, and irrevocable bank letters of credit. State Street does not have the ability to pledge or sell collateral securities unless the borrower defaults.

The Board did not impose any restrictions during fiscal years 2003 and 2002 on the amount of the loans that State Street made on its behalf. There were no failures by any borrowers to return loaned securities or pay distributions thereon during fiscal years 2003 and 2002. Moreover, there were no losses during fiscal years 2003 and 2002 resulting from a default of the borrowers or State Street.

During fiscal years 2003 and 2002, the Board and the borrowers maintained the right to terminate all securities lending transactions on demand. The cash collateral received on each loan was invested, together with the cash collateral of other qualified plan lenders, in a collective investment pool, the Securities Lending Quality Trust. The relationship between the average maturities of the investment pool and the Board's loans was affected by the maturities of the loans made by other plan entities that invested cash collateral in the collective investment pool, which the Board could not determine. On June 30, 2003 and June 30, 2002, the Board had no credit risk exposure to borrowers.

As of June 30, 2003, the carrying and fair values of the underlying securities on loan for MTIP were \$75,267,314 and \$74,813,847, respectively. The collateral provided for the securities on loan totaled \$78,496,331 in cash collateral.

As of June 30, 2002, the carrying and fair values of the underlying securities on loan for MTIP were \$63,227,006 and \$65,695,692, respectively. The collateral provided for the securities on loan totaled \$67,264,338 representing \$67,179,838 in cash and \$84,500 in securities collateral.

4. INVESTMENT RISK CATEGORIES

State of Montana investments are categorized below to give an indication of the level of risk assumed at June 30, 2003 and June 30, 2002. Category 1 includes investments that are insured or registered, or securities that are held by the Board or its agent in the Board's name. Not Categorized includes investments held by broker-dealers under securities loans with cash collateral.

Risk as of June 30, 2003

<u>Security Investment Type</u>	<u>Category 1</u>					
	<u>Securities Not On Loan</u>	<u>On Loan for Securities Collateral*</u>	<u>Not Categorized*</u>	<u>Carrying Amount</u>	<u>Fair Value</u>	
BGI MSCI Europe Index	\$ 40,000,000	\$ 0	\$ 0	\$ 40,000,000	\$ 41,094,723	
BOI Internal International	114,468,681	0	18,460,365	132,929,046	132,270,563	
Pyford International	107,654,491	0	15,172,082	122,826,573	109,475,945	
Schroder Investment Mgmt.	98,495,947	0	21,876,365	120,372,312	113,041,041	
SG Yamaichi Asset Mgmt.	<u>53,496,965</u>	<u>0</u>	<u>19,758,502</u>	<u>73,255,467</u>	<u>74,847,509</u>	
Total Investment	\$ 414,116,084	\$ 0	\$ 75,267,314	\$ 489,383,398	\$ 470,729,781	
Securities Lending Collateral Investment Pool			<u>78,496,331</u>	<u>78,496,331</u>	<u>78,496,331</u>	

* At June 30, 2003, the underlying securities with fair values of \$74,813,847 were loaned for securities and cash collateral under a securities lending agreement with the state's agent.

Risk as of June 30, 2002

<u>Security Investment Type</u>	<u>Category 1</u>					
	<u>Securities Not On Loan</u>	<u>On Loan for Securities Collateral*</u>	<u>Not Categorized*</u>	<u>Carrying Amount</u>	<u>Fair Value</u>	
BOI Internal International	\$ 116,629,720	\$ 0	\$ 28,136,551	\$ 144,766,271	\$ 143,562,849	
Pyford International	81,720,536	0	15,782,786	97,503,322	89,775,488	
Schroder Investment Mgmt.	106,946,185	67,619	9,008,869	116,022,673	112,533,365	
SG Pacific Asset Mgmt.	<u>74,349,163</u>	<u>0</u>	<u>10,231,181</u>	<u>84,580,344</u>	<u>83,734,000</u>	
Total Investment	\$ 379,645,604	\$ 67,619	\$ 63,159,387	\$ 442,872,610	\$ 429,605,702	
Securities Lending Collateral Investment Pool			<u>67,179,838</u>	<u>67,179,838</u>	<u>67,179,838</u>	

* At June 30, 2002, the underlying securities with fair values of \$79,612 and \$65,616,079, respectively, were loaned for securities and cash collateral under a securities lending agreement with the state's agent.

The MTIP, through the above funds, has significant investments in 21 foreign countries. Future economic and political developments in these countries could adversely affect the liquidity or value, or both, of the securities held by the above funds in which MTIP is invested.

5. SUBSEQUENT EVENT

On July 1, 2003, the Board funded MTIP with a \$35 million purchase in the State Street Stock Performance Index Futures Fund (SPIFF). SPIFF shares were subsequently sold to fund \$25 million to the BGI-MSCI Europe Index Fund on July 3, 2003.

6. EXTERNAL MANAGERS

On October 30, 2003, the Board voted to retain Schroder Investment Management NA, hire Nomura Asset Management USA, Inc. and terminate SG Yamaichi Asset Management, Co. as active managers for the Board's Pacific Basin equity mandate. SG Yamaichi Asset Management, Co. ceased equity trading in the Pacific Basin on October 31, 2003. Upon transition, Nomura Asset Management USA, Inc. will begin equity trading in the Pacific Basin on December 1, 2003.

7. YEAR END PORTFOLIO

The combined investment portfolios for the five funds, as of June 30, 2003 are listed below by country. The percent is based on the total fair value of each security/country to the combined total portfolio fair value.

<u>Country</u>	<u>Security Name</u>	<u>Shares</u>	<u>Carrying Value</u>	<u>Fair Value</u>	<u>% of Total</u>
AUSTRALIA	AMCOR LIMITED	243,663	964,423	1,326,910	0.28%
AUSTRALIA	AMP LIMITED	148,000	522,449	493,303	0.10%
AUSTRALIA	AUSTRALIA/ NEW ZEALAND BANK GRP	109,380	1,166,272	1,365,149	0.29%
AUSTRALIA	BHP BILLITON LTD	846,745	4,401,144	4,906,392	1.04%
AUSTRALIA	BHP STEEL	200,816	373,182	500,999	0.11%
AUSTRALIA	BRAMBLES INDUSTRIES LTD	328,870	1,692,330	1,007,944	0.21%
AUSTRALIA	COCA COLA AMATIL	407,300	1,190,056	1,559,719	0.33%
AUSTRALIA	COMMONWEALTH BK OF AUSTRALIA	247,170	3,879,373	4,898,342	1.04%
AUSTRALIA	CSL LIMITED	75,700	985,510	606,680	0.13%
AUSTRALIA	FOSTERS GROUP	237,500	594,001	670,566	0.14%
AUSTRALIA	LEIGHTON HOLDINGS	50,000	291,591	335,325	0.07%
AUSTRALIA	LEND LEASE CORP	58,100	335,008	325,356	0.07%
AUSTRALIA	MACQUARIE INFRASTRUCTURE GRP	283,700	630,113	683,046	0.15%
AUSTRALIA	NATIONAL AUSTRALIA BANK	158,195	3,045,646	3,554,131	0.76%
AUSTRALIA	NEWS CORPORATION	463,300	3,701,493	3,479,975	0.74%
AUSTRALIA	PUBLISHING + BROADCASTING LTD	135,600	666,145	898,488	0.19%
AUSTRALIA	QANTAS AIRWAYS	499,700	1,054,461	1,095,855	0.23%
AUSTRALIA	RIO TINTO LIMITED	67,540	1,291,224	1,323,087	0.28%
AUSTRALIA	TABCORP HOLDINGS LTD	163,000	987,774	1,177,333	0.25%
AUSTRALIA	TELSTRA CORP	643,690	1,914,606	1,899,439	0.40%
AUSTRALIA	WESFARMERS	20,690	326,226	351,056	0.07%
AUSTRALIA	WESTFIELD HOLDINGS	81,090	642,793	793,992	0.17%
AUSTRALIA	WESTFIELD TRUST	94,780	192,381	219,296	0.05%
AUSTRALIA	WESTPAC BANKING CORP	287,200	2,192,748	3,129,923	0.66%
AUSTRALIA	WOODSIDE PETROLEUM	177,400	1,276,251	1,472,889	0.31%
AUSTRALIA	WOOLWORTHS LTD	99,311	706,768	833,868	0.18%
AUSTRALIA 26 ISSUE(S)		6,128,440	35,023,970	38,909,064	8.27%
BELGIUM	DEXIA	90,000	1,211,385	1,137,900	0.24%
BELGIUM	DEXIA	267,140	3,278,716	3,362,200	0.71%
BELGIUM	DEXIA STRIPS	129,140	0	1,483	0.00%
BELGIUM	FORTIS	30,000	554,936	520,891	0.11%
BELGIUM	INTERBREW	45,000	815,026	999,925	0.21%

<u>Country</u>	<u>Security Name</u>	<u>Shares</u>	<u>Carrying Value</u>	<u>Fair Value</u>	<u>% of Total</u>
BELGIUM 5 ISSUE(S)		561,280	5,860,063	6,022,399	1.28%
CHINA/HONG KONG	ASIA SATELLITE TEL	131,437	176,931	216,585	0.05%
CHINA/HONG KONG	ASM PACIFIC TECH	216,000	524,876	631,534	0.13%
CHINA/HONG KONG	CHEUNG KONG HOLDINGS	100,000	644,248	601,425	0.13%
CHINA/HONG KONG	CHINA MOBILE	248,500	1,059,067	586,344	0.12%
CHINA/HONG KONG	CHINA OILFIELD SER	3,422,000	818,700	767,939	0.16%
CHINA/HONG KONG	CHINA PHARMACEUTICAL	1,300,000	322,778	437,604	0.09%
CHINA/HONG KONG	CLP HOLDINGS	345,300	1,381,297	1,509,939	0.32%
CHINA/HONG KONG	CNOOC LTD	664,000	880,888	979,207	0.21%
CHINA/HONG KONG	COSCO PACIFIC LTD	354,000	342,693	372,242	0.08%
CHINA/HONG KONG	DAH SING FINANCIAL	116,800	531,612	581,143	0.12%
CHINA/HONG KONG	DENWAY MOTORS LTD	2,290,000	640,911	1,035,149	0.22%
CHINA/HONG KONG	FONGS INDUSTRIES	296,000	165,308	165,116	0.04%
CHINA/HONG KONG	FOUNTAIN SET HLDGS	640,000	478,347	570,392	0.12%
CHINA/HONG KONG	HONG KONG EXCHANGE	374,000	490,239	537,153	0.11%
CHINA/HONG KONG	HUTCHISON WHAMPOA	267,400	2,216,349	1,628,784	0.35%
CHINA/HONG KONG	JOHNSON ELECTRIC HOLDINGS	899,500	992,778	1,113,107	0.24%
CHINA/HONG KONG	LI + FUNG	306,000	396,039	394,363	0.08%
CHINA/HONG KONG	SINGAMAS CONTAINER	1,200,000	364,165	511,660	0.11%
CHINA/HONG KONG	SUN HUNG KAI PROPS	332,000	2,383,753	1,677,423	0.36%
CHINA/HONG KONG	SWIRE PACIFIC	136,500	623,489	596,892	0.13%
CHINA/HONG KONG	TECHTRONIC INDS	324,000	304,143	544,283	0.12%
CHINA/HONG KONG	TEXWINCA HOLDINGS	834,000	627,251	663,080	0.14%
CHINA/HONG KONG	VEDAN INTL	1,600,000	209,268	201,073	0.04%
CHINA/HONG KONG	WHARF HOLDINGS	857,000	1,753,432	1,648,468	0.35%
CHINA/HONG KONG	ZHEJIANG EXPRESSWAY	2,604,000	932,692	1,076,909	0.23%
CHINA/HONG KONG 25 ISSUE(S)		19,858,437	19,261,254	19,047,814	4.05%
FINLAND	NOKIA CORP	162,000	2,169,260	2,661,660	0.57%
FINLAND	SAMPO OYJ	330,000	3,352,173	2,421,525	0.51%
FINLAND 2 ISSUE(S)		492,000	5,521,433	5,083,185	1.08%
FRANCE	AIR LIQUIDE(L)	3,312	413,349	491,010	0.10%
FRANCE	AVENTIS SA	50,700	2,612,980	2,789,384	0.59%
FRANCE	CNP ASSURANCES	44,800	1,687,040	1,893,215	0.40%
FRANCE	SODEXHO ALLIANCE	96,266	3,087,456	2,597,855	0.55%
FRANCE	TOTAL SA	25,100	3,462,234	3,793,182	0.81%
FRANCE	VALEO	85,600	3,331,591	2,968,621	0.63%
FRANCE	VEOLIA ENVIRONNEMENT	6,100	124,820	125,388	0.03%
FRANCE 7 ISSUE(S)		311,878	14,719,470	14,658,656	3.11%
GERMANY	ALTANA AG	13,000	620,005	820,174	0.17%
GERMANY	BASF AG	67,000	2,637,136	2,862,146	0.61%
GERMANY	BAYERISCHE MOTOREN WERKE AG	85,000	2,752,905	3,269,925	0.69%
GERMANY	DEUTSCHE TELEKOM AG	125,000	1,833,623	1,900,000	0.40%
GERMANY	E ON AG	32,750	1,637,375	1,683,730	0.36%
GERMANY	HENKEL KGAA	8,400	469,628	520,023	0.11%
GERMANY	LINDE AG	40,000	1,178,448	1,480,912	0.31%
GERMANY	SAP AKTIENGESELLSCHAFT	41,300	1,340,415	1,206,786	0.26%
GERMANY	SCHERING AG	84,100	3,793,893	4,112,214	0.87%
GERMANY	SIEMENS AG NPV (REGD)	40,000	2,026,301	1,962,300	0.42%
GERMANY 10 ISSUE(S)		536,550	18,289,728	19,818,211	4.21%
INDONESIA	BK MANDIRI	448,500	37,198	36,695	0.01%
INDONESIA	BK PAN ID	9,225,000	225,656	346,636	0.07%
INDONESIA	H M SAMPOERNA	980,000	317,348	492,970	0.10%
INDONESIA	TELEKOMUNIKASI IND	2,276,500	1,050,510	1,276,220	0.27%
INDONESIA 4 ISSUE(S)		12,930,000	1,630,712	2,152,521	0.46%

<u>Country</u>	<u>Security Name</u>	<u>Shares</u>	<u>Carrying Value</u>	<u>Fair Value</u>	<u>% of Total</u>
IRELAND	ALLIED IRISH BANKS	253,968	3,234,359	3,794,289	0.81%
IRELAND	ANGLO IRISH BANK CP	130,000	1,111,805	1,141,243	0.24%
IRELAND	CRH	51,000	727,430	802,937	0.17%
IRELAND 3 ISSUE(S)		434,968	5,073,594	5,738,469	1.22%
ITALY	ENI	30,000	344,423	453,713	0.10%
ITALY	TIM SPA	260,000	1,174,381	1,280,869	0.27%
ITALY 2 ISSUE(S)		290,000	1,518,804	1,734,582	0.37%
JAPAN	AJINOMOTO CO INC	56,000	574,800	536,331	0.11%
JAPAN	ALPS ELECTRIC CO	29,000	355,696	371,451	0.08%
JAPAN	ARISAWA MANUFACTURING CO	14,500	260,042	347,783	0.07%
JAPAN	BANDAI CO	8,000	246,718	305,143	0.06%
JAPAN	BRIDGESTONE CORP	139,000	1,906,587	1,886,904	0.40%
JAPAN	CANON INC	24,000	723,185	1,101,312	0.23%
JAPAN	CHIBA BANK	87,000	296,137	308,657	0.07%
JAPAN	CSK CORPORATION	12,600	337,706	343,136	0.07%
JAPAN	DAI DAN CO	44,000	385,247	172,592	0.04%
JAPAN	DAIICHI PHARMACEUTICAL CO	52,200	765,091	679,915	0.14%
JAPAN	DAINIPPON INK+CHEM	220,000	437,423	445,222	0.09%
JAPAN	DAINIPPON SCREEN	83,000	283,893	406,446	0.09%
JAPAN	DON QUIJOTE	3,100	130,485	155,678	0.03%
JAPAN	DON QUIJOTE	3,100	128,606	159,034	0.03%
JAPAN	EAST JAPAN RAILWAY	710	3,543,112	3,157,527	0.67%
JAPAN	EISAI CO	30,800	824,621	633,571	0.13%
JAPAN	FUJI PHOTO FILM CO	61,000	1,985,261	1,762,815	0.37%
JAPAN	FUJI SEAL	2,800	75,571	85,813	0.02%
JAPAN	FUJITSU	151,000	2,065,731	618,713	0.13%
JAPAN	GLORY	7,000	153,825	155,070	0.03%
JAPAN	GUNZE LIMITED	65,000	247,088	244,680	0.05%
JAPAN	HITACHI	111,000	934,696	470,531	0.10%
JAPAN	HITACHI TRANSPORT SYSTEM	100,000	555,633	592,963	0.13%
JAPAN	HONDA MOTOR CO	36,700	1,334,896	1,390,673	0.30%
JAPAN	ITOCHEU CORP	158,000	363,669	397,385	0.08%
JAPAN	JAPAN AIRPORT TERM	94,000	725,706	542,511	0.12%
JAPAN	JFE HOLDING INC	38,400	436,961	575,640	0.12%
JAPAN	JSAT CORP JPY50000	148	385,388	457,281	0.10%
JAPAN	KANEKA CORP	92,000	697,652	566,979	0.12%
JAPAN	KEIHIN CORP	5,800	55,410	49,511	0.01%
JAPAN	KONAMI CORP	11,700	260,510	209,494	0.04%
JAPAN	KONICA CORPORATION	49,000	497,260	557,843	0.12%
JAPAN	KUBOTA CORP	119,000	316,593	323,081	0.07%
JAPAN	KURARAY CO	70,000	562,876	459,380	0.10%
JAPAN	MABUCHI MOTOR CO	6,300	527,767	481,649	0.10%
JAPAN	MATSUSHITA ELECTRIC IND	242,000	3,656,918	2,396,319	0.51%
JAPAN	MILLEA HOLDINGS INC	255	2,317,957	1,949,532	0.41%
JAPAN	MITSUBISHI CORP	90,000	706,104	624,360	0.13%
JAPAN	MITSUBISHI ELEC CP	232,000	743,357	753,529	0.16%
JAPAN	MITSUBISHI ESTATE	63,000	570,010	426,558	0.09%
JAPAN	MITSUBISHI RAYON	122,000	379,365	325,130	0.07%
JAPAN	MITSUBISHI TOKYO FIN	171	1,963,454	773,292	0.16%
JAPAN	mitsui + co	500,000	2,911,096	2,506,767	0.53%
JAPAN	mitsui chemicals I	91,000	408,804	420,612	0.09%
JAPAN	mitsui mining + sm	164,000	374,164	484,864	0.10%
JAPAN	mitsui trust holdings	173,000	384,697	380,362	0.08%
JAPAN	MURATA MFG CO	51,000	2,602,546	2,004,747	0.43%

<u>Country</u>	<u>Security Name</u>	<u>Shares</u>	<u>Carrying Value</u>	<u>Fair Value</u>	<u>% of Total</u>
JAPAN	NEC CORP	119,000	437,368	594,628	0.13%
JAPAN	NGK SPARK PLUG CO	81,000	589,231	567,995	0.12%
JAPAN	NICHIREI CORP	98,000	317,137	341,970	0.07%
JAPAN	NIDEC CORPORATION	5,200	339,812	343,419	0.07%
JAPAN	NIPPON CABLE SYS	16,000	142,971	149,240	0.03%
JAPAN	NIPPON ELEC GLASS	19,000	197,529	200,641	0.04%
JAPAN	NIPPON MINING HOLDINGS	500	1,568	1,083	0.00%
JAPAN	NIPPON OIL CORP	187,000	789,573	811,385	0.17%
JAPAN	NIPPON TEL+TEL CP	583	4,812,853	2,286,846	0.49%
JAPAN	NIPPON TV NETWORK	6,750	1,297,009	804,435	0.17%
JAPAN	NIPPON UNIPAC HOLD	434	2,183,831	1,695,157	0.36%
JAPAN	NIPPON YUSEN KK	118,000	403,347	459,913	0.10%
JAPAN	NISHIMATSU CONSTRUCTION	103,000	306,113	349,981	0.07%
JAPAN	NISSAN MOTOR CO	50,900	464,246	486,639	0.10%
JAPAN	NOMURA HOLDINGS	185,000	2,576,379	2,348,032	0.50%
JAPAN	NSK	115,000	364,674	365,855	0.08%
JAPAN	NTT DOCOMO	753	1,976,511	1,630,481	0.35%
JAPAN	OJI PAPER CO	69,000	356,467	301,686	0.06%
JAPAN	OMRON CORP	94,000	1,424,337	1,585,259	0.34%
JAPAN	ORIX CORP	6,500	326,765	359,442	0.08%
JAPAN	OSAKA GAS CO	251,000	618,391	620,837	0.13%
JAPAN	PROMISE CO	31,500	1,902,247	1,177,889	0.25%
JAPAN	RICOH CO	172,000	2,988,880	2,810,443	0.60%
JAPAN	ROHM CO	19,700	2,797,256	2,147,599	0.46%
JAPAN	SANKEN ELECTRIC CO	55,000	411,979	487,820	0.10%
JAPAN	SANKYO CO	36,100	942,204	900,433	0.19%
JAPAN	SANYO CHEMICAL IND	24,000	165,932	148,107	0.03%
JAPAN	SEIKO EPSON CORP	2,600	57,186	77,302	0.02%
JAPAN	SHIMAMURA CO	5,800	348,197	320,250	0.07%
JAPAN	SHIN ETSU CHEM CO	21,100	735,885	720,466	0.15%
JAPAN	SHINKO ELEC INDS	16,800	324,296	327,395	0.07%
JAPAN	SHOWA SHELL SEKIYU	126,200	781,895	905,970	0.19%
JAPAN	SMC CORP	15,500	1,351,679	1,305,059	0.28%
JAPAN	SOMPO JAPAN INS	324,000	1,679,108	1,767,395	0.38%
JAPAN	SONY CORP	56,100	2,962,882	1,579,163	0.34%
JAPAN	SUMITOMO BAKELITE	153,000	857,677	638,376	0.14%
JAPAN	SUMITOMO ELEC INDS	212,000	1,763,264	1,548,399	0.33%
JAPAN	TAKASHIMAYA CO	98,000	491,706	487,245	0.10%
JAPAN	TAKEDA CHEM INDS	117,100	4,759,634	4,320,242	0.92%
JAPAN	TEIJIN	315,000	1,159,442	787,008	0.17%
JAPAN	TERUMO CORP	31,100	535,189	516,715	0.11%
JAPAN	TOHO CO	75,800	550,639	665,361	0.14%
JAPAN	TOKYO ELECTRON	5,200	200,534	246,413	0.05%
JAPAN	TOPPAN PRINTING CO	105,000	1,119,326	752,030	0.16%
JAPAN	TOSTEM INAX HOLDING	21,000	312,057	302,561	0.06%
JAPAN	TOYOTA MOTOR CORP	224,800	6,371,877	5,822,428	1.24%
JAPAN	USS	6,500	214,247	329,128	0.07%
JAPAN	YAMADA DENKI CO	15,300	321,252	337,664	0.07%
JAPAN	YAMAHA MOTOR CO	43,000	339,352	362,765	0.08%
JAPAN	YAMANOUCHI PHARM	75,900	2,573,342	1,978,488	0.42%
JAPAN	YAMATO TRANSPORT	56,000	606,832	619,813	0.13%
JAPAN	YOKOGAWA ELECTRIC	64,000	483,502	494,091	0.10%
JAPAN	YORK BENIMARU CO	19,000	438,723	396,377	0.08%
JAPAN 100 ISSUE(S)		7,785,004	100,874,643	85,584,102	18.18%

<u>Country</u>	<u>Security Name</u>	<u>Shares</u>	<u>Carrying Value</u>	<u>Fair Value</u>	<u>% of Total</u>
KOREA	HYUNDAI DEPARTMENT	31,400	709,211	699,238	0.15%
KOREA	HYUNDAI MOTOR CO	39,930	903,613	1,056,332	0.22%
KOREA	K T + G CORPORATION	21,530	159,968	177,536	0.04%
KOREA	KANGWON LAND	5,950	640,415	662,495	0.14%
KOREA	KOOKMIN BANK	94,812	2,760,580	2,857,457	0.61%
KOREA	KT + G CORPORATION	11,090	150,011	182,899	0.04%
KOREA	KT CORP	45,900	1,186,365	904,689	0.19%
KOREA	LG ELECTRONICS INC	20,450	772,051	852,583	0.18%
KOREA	POSCO	5,908	552,674	613,304	0.13%
KOREA	POSCO	25,400	526,493	665,226	0.14%
KOREA	SAMSUNG ELECTRONIC	23,291	3,439,962	6,921,980	1.47%
KOREA	SAMSUNG FIRE + MAR	19,140	1,026,101	930,962	0.20%
KOREA	SHINSEGAE CO LTD	10,015	1,200,122	1,563,665	0.33%
KOREA 13 ISSUE(S)		354,816	14,027,566	18,088,365	3.84%
MALAYSIA	BRITISH AMERICAN TOBACCO	32,000	309,793	328,421	0.07%
MALAYSIA	GAMUDA BERHAD	520,000	712,617	841,579	0.18%
MALAYSIA	GENTING BERHAD	126,000	419,255	497,368	0.11%
MALAYSIA	MALAYAN BK BHD	550,300	1,266,114	1,245,416	0.26%
MALAYSIA	MAXIS COMMUN BHD	204,000	275,235	306,000	0.07%
MALAYSIA	OYL INDS BERHAD	50,400	214,081	341,526	0.07%
MALAYSIA	PERUSAHAAN OTOMOBIL	100,000	211,641	213,158	0.05%
MALAYSIA	RESORTS WORLD BHD	416,500	853,603	1,074,132	0.23%
MALAYSIA 8 ISSUE(S)		1,999,200	4,262,337	4,847,600	1.03%
NETHERLANDS	ABN AMRO HOLDINGS NV	138,228	2,326,258	2,642,922	0.56%
NETHERLANDS	AEGON NV	484,723	6,598,470	4,853,826	1.03%
NETHERLANDS	AHOLD (KON) NV	245,197	4,490,177	2,035,765	0.43%
NETHERLANDS	IHC CALAND NV	11,603	555,704	592,398	0.13%
NETHERLANDS	ING GROEP NV	152,320	4,387,875	2,670,170	0.57%
NETHERLANDS	ING GROEP NV	60,000	1,006,660	1,042,472	0.22%
NETHERLANDS	KON KPN NV	120,000	766,265	850,238	0.18%
NETHERLANDS	KONINKLIJKE PHILIPS ELECTRS NV	150,000	4,260,106	2,866,500	0.61%
NETHERLANDS	REED ELSEVIER NV	42,000	501,401	495,329	0.11%
NETHERLANDS	ROYAL DUTCH PETROLEUM CO	101,000	5,327,405	4,708,620	1.00%
NETHERLANDS	ROYAL DUTCH PETROLEUM CO	99,700	4,846,938	4,627,704	0.98%
NETHERLANDS	STMICROELECTRONICS NV	52,000	1,915,094	1,081,080	0.23%
NETHERLANDS	TPG NV	117,500	2,114,256	2,040,158	0.43%
NETHERLANDS	UNILEVER NV	30,000	1,799,844	1,620,000	0.34%
NETHERLANDS	WOLTERS KLUWER	148,004	3,370,697	1,784,583	0.38%
NETHERLANDS 15 ISSUE(S)		1,952,275	44,267,149	33,911,765	7.20%
NEW ZEALAND	TELECOM CORP OF NEW ZEALAND	244,900	549,757	751,294	0.16%
NEW ZEALAND 1 ISSUE(S)		244,900	549,757	751,294	0.16%
SINGAPORE	CITY DEVELOPMENTS	144,000	351,144	363,066	0.08%
SINGAPORE	DBS GROUP HOLDINGS	210,786	1,587,995	1,232,877	0.26%
SINGAPORE	KEPPEL CORP	140,000	384,721	389,551	0.08%
SINGAPORE	MOBILEONE	1,005,000	759,773	764,736	0.16%
SINGAPORE	SEMBCORP LOGISTICS	480,000	543,060	512,436	0.11%
SINGAPORE	SINGAPORE AIRLINES	62,000	372,752	366,156	0.08%
SINGAPORE	SINGAPORE POST	381,000	131,464	147,121	0.03%
SINGAPORE	SINGAPORE PRESS HD	53,536	669,805	556,337	0.12%
SINGAPORE	UNISTEEL TECHNOLOGY LTD	667,500	254,063	278,599	0.06%
SINGAPORE	UNITED OVERSEAS BANK	314,000	2,095,310	2,211,016	0.47%
SINGAPORE	VENTURE CORP LTD	36,000	266,613	329,131	0.07%
SINGAPORE 11 ISSUE(S)		3,493,822	7,416,702	7,151,026	1.52%
SPAIN	ABERTIS INFRAESTRUCTURAS SA	41,800	287,116	584,172	0.12%

<u>Country</u>	<u>Security Name</u>	<u>Shares</u>	<u>Carrying Value</u>	<u>Fair Value</u>	<u>% of Total</u>
SPAIN	BANCO BILBAO VIZCAYA ARGENTARI	261,500	2,983,644	2,743,135	0.58%
SPAIN	BBVA (BILB VIZ ARG)	429,300	4,545,620	4,510,826	0.96%
SPAIN	ENAGAS S A	49,300	416,362	421,772	0.09%
SPAIN	ENDESA S A	123,400	2,397,454	2,011,420	0.43%
SPAIN	ENDESA S A	279,900	3,666,802	4,686,348	1.00%
SPAIN	TELEFONICA MOVILES	45,000	318,014	361,213	0.08%
SPAIN	TELEFONICA S A	30,528	1,600,283	1,055,353	0.22%
SPAIN	TELEFONICA S A	486,409	5,552,579	5,647,118	1.20%
SPAIN 9 ISSUE(S)		1,747,137	21,767,874	22,021,357	4.68%
SWEDEN	ASSA ABLOY	65,000	673,682	629,298	0.13%
SWEDEN	ATLAS COPCO AB	60,000	1,280,210	1,517,811	0.32%
SWEDEN 2 ISSUE(S)		125,000	1,953,892	2,147,109	0.46%
SWITZERLAND	LONZA GROUP AG	23,980	1,429,195	1,097,604	0.23%
SWITZERLAND	NESTLE S A	115,500	4,156,525	5,971,350	1.27%
SWITZERLAND	NESTLE S A	20,330	4,286,298	4,194,925	0.89%
SWITZERLAND	NOVARTIS AG	132,900	4,315,082	5,290,749	1.12%
SWITZERLAND	NOVARTIS AG	136,000	5,148,989	5,381,566	1.14%
SWITZERLAND	ROCHE HOLDINGS AG	109,510	8,179,025	8,589,891	1.82%
SWITZERLAND	SWATCH GROUP	5,700	537,877	516,537	0.11%
SWITZERLAND	SWISS REINSURANCE	84,900	6,519,493	4,703,957	1.00%
SWITZERLAND	UBS AG	121,500	5,622,087	6,758,721	1.44%
SWITZERLAND	ZURICH FINANCIAL SERVICES GROUP	18,890	4,683,407	2,252,213	0.48%
SWITZERLAND 10 ISSUE(S)		769,210	44,877,976	44,757,513	9.51%
TAIWAN	ADVANCED SEMICONDUCTOR ENGR	180,000	538,200	527,400	0.11%
TAIWAN	BENQ CORP	89,632	556,143	610,663	0.13%
TAIWAN	CHINA STEEL	31,375	317,107	429,838	0.09%
TAIWAN	COMPAL ELECTRONIC	87,900	464,666	590,688	0.13%
TAIWAN	HON HAI PRECISION IND LTD	9,000	67,500	65,268	0.01%
TAIWAN	HON HAI PRECISION IND LTD	72,193	554,224	545,057	0.12%
TAIWAN	SYNNEX TECHNOLOGY INTL CORP	105,165	551,940	594,182	0.13%
TAIWAN	TAIWAN SEMICNDCTR MFG CO LTD	165,940	1,717,145	1,672,675	0.36%
TAIWAN	UNITED MICROELECTRONICS CORP	140,000	485,800	525,000	0.11%
TAIWAN 9 ISSUE(S)		881,205	5,252,725	5,560,771	1.18%
THAILAND	BANGKOK BANK	171,000	258,935	274,560	0.06%
THAILAND	KASIKORNBANK PCL	868,500	632,768	810,862	0.17%
THAILAND	LAND + HOUSES	1,833,000	322,855	414,213	0.09%
THAILAND	NATIONAL FINANCE PUBLIC	716,200	218,279	257,246	0.05%
THAILAND	PTT EXPLORATION + PRD	94,100	232,214	360,373	0.08%
THAILAND	SIAM CEMENT CO	40,000	158,017	159,848	0.03%
THAILAND	TELECOMASIA RIGHTS	163,895	0	0	0.00%
THAILAND 7 ISSUE(S)		3,886,695	1,823,068	2,277,101	0.48%
UNITED KINGDOM	BARCLAYS	660,360	5,005,238	4,903,615	1.04%
UNITED KINGDOM	BOOTS GROUP	61,000	645,005	652,774	0.14%
UNITED KINGDOM	BP PLC	162,384	7,341,018	6,823,376	1.45%
UNITED KINGDOM	BP PLC	462,000	3,505,220	3,203,854	0.68%
UNITED KINGDOM	BRITISH SKY BROADCAST	206,000	1,940,631	2,282,634	0.48%
UNITED KINGDOM	CADBURY SCHWEPPE	26,000	568,854	628,680	0.13%
UNITED KINGDOM	COMPASS GROUP	969,000	6,586,940	5,224,713	1.11%
UNITED KINGDOM	EXEL	145,000	1,570,891	1,488,269	0.32%
UNITED KINGDOM	GALLAHER GROUP	237,000	2,264,530	2,326,957	0.49%
UNITED KINGDOM	GLAXOSMITHKLINE PLC	117,000	2,795,524	2,361,214	0.50%
UNITED KINGDOM	GLAXOSMITHKLINE PLC	144,779	6,366,890	5,869,341	1.25%
UNITED KINGDOM	HSBC HOLDINGS PLC	103,200	1,210,289	1,224,136	0.26%
UNITED KINGDOM	HSBC HOLDINGS PLC	80,000	4,215,912	4,728,800	1.00%

<u>Country</u>	<u>Security Name</u>	<u>Shares</u>	<u>Carrying Value</u>	<u>Fair Value</u>	<u>% of Total</u>
UNITED KINGDOM	INTERCONTINENTAL H	177,966	1,202,619	1,262,783	0.27%
UNITED KINGDOM	KINGFISHER	300,000	1,291,476	1,372,511	0.29%
UNITED KINGDOM	LEGAL + GENERAL GP	2,589,240	4,646,042	3,589,010	0.76%
UNITED KINGDOM	PRUDENTIAL PLC	275,121	3,174,840	1,666,145	0.35%
UNITED KINGDOM	RECKITT BENCKISER PLC	50,000	794,811	917,483	0.19%
UNITED KINGDOM	RENTOKIL INITIAL	295,300	868,314	922,194	0.20%
UNITED KINGDOM	REUTERS GROUP	705,000	4,477,792	2,044,596	0.43%
UNITED KINGDOM	ROYAL BK SCOT GRP	150,000	3,333,564	4,207,879	0.89%
UNITED KINGDOM	SCOTTISH + SOUTHERN ENERGY	147,000	1,372,906	1,513,648	0.32%
UNITED KINGDOM	SHELL TRANS + TRADING PLC	56,000	2,069,827	2,231,600	0.47%
UNITED KINGDOM	SMITHS GROUP	300,000	3,113,697	3,480,164	0.74%
UNITED KINGDOM	SYNTHESTRATEC	3,010	1,644,199	2,162,142	0.46%
UNITED KINGDOM	TESCO	570,000	2,008,601	2,062,232	0.44%
UNITED KINGDOM	TIBBETT + BRITTEN	94,700	887,865	785,252	0.17%
UNITED KINGDOM	TOMKINS	389,837	1,431,913	1,460,266	0.31%
UNITED KINGDOM	UNILEVER	68,964	604,717	549,089	0.12%
UNITED KINGDOM	UNITED UTILITIES	218,000	2,191,395	2,118,824	0.45%
UNITED KINGDOM	VODAFONE GROUP	4,716,236	10,208,304	9,222,251	1.96%
UNITED KINGDOM	VODAFONE GROUP	10,000	173,500	196,500	0.04%
UNITED KINGDOM 32 ISSUE(S)		14,490,097	89,513,324	83,482,934	17.73%
UNITED STATES	BGI MSCI INDEX FUND EUROPE	6,119,194	40,000,000	41,094,723	8.73%
UNITED STATES 1 ISSUE(S)		6,119,194	40,000,000	41,094,723	8.73%
EQUITIES TOTAL 302 ISSUE(S)		85,392,108	483,486,041	464,840,561	98.75%
UNITED KINGDOM	BAE SYSTEMS, 7.45%, 11/29/2003	6,392	10,141	2,004	0.00%
FIXED INCOME TOTAL 1 ISSUE(S)		6,392	10,141	2,004	0.00%
UNITED STATES	STATE STREET BANK + TRUST CO	5,887,216	5,887,216	5,887,216	1.25%
CASH TOTAL 1 ISSUE(S)		5,887,216	5,887,216	5,887,216	1.25%
GRAND TOTAL 304 ISSUE(S)		91,285,716	489,383,398	470,729,781	100.00%

LEGISLATIVE AUDIT DIVISION

Scott A. Seacat, Legislative Auditor
John W. Northey, Legal Counsel



Deputy Legislative Auditors:
Jim Pellegrini, Performance Audit
Tori Hunthausen, IS Audit & Operations
James Gillett, Financial-Compliance Audit

INDEPENDENT AUDITOR'S REPORT

The Legislative Audit Committee
of the Montana State Legislature:

We have audited the accompanying Statement of Net Asset Value for the state of Montana Board of Investments, Montana Private Equity Pool, as of June 30, 2003 and 2002, and the related Statement of Changes in Net Asset Value and Statement of Investment Income and Distribution for the fiscal years then ended. These financial statements are the responsibility of the Board of Investments' management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the net asset value of the state of Montana Board of Investments, Montana Private Equity Pool, as of June 30, 2003 and 2002, and its changes in net asset value and investment income and distribution for the fiscal years then ended in conformity with accounting principles generally accepted in the United States of America.

Respectfully submitted,

Signature on File

James Gillett, CPA
Deputy Legislative Auditor

November 4, 2003

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**STATE OF MONTANA BOARD OF INVESTMENTS
MONTANA PRIVATE EQUITY POOL FINANCIAL STATEMENTS**

STATEMENT OF NET ASSET VALUE JUNE 30, 2003 AND 2002

<u>Assets</u>	<u>2003</u>	<u>2002</u>
Cash	\$ 0	\$ 0
Dividend receivable	199,575	0
Investments managed at fair value (carrying value of \$278,790,323 in 2003 and \$184,109,131 in 2002)(Notes 2 and 4)	<u>305,349,864</u>	<u>197,351,619</u>
Total assets	\$ <u>305,549,439</u>	\$ <u>197,351,619</u>
 <u>Liabilities</u>		
Income due participants	\$ 7,361,863	\$ 9,309,822
Total liabilities	<u>7,361,863</u>	<u>9,309,822</u>
Net asset value	\$ <u>298,187,576</u>	\$ <u>188,041,797</u>
Units Outstanding (Note 2)	2,915,343	1,930,959
Unit Value (Note 2)	\$ 102.28	\$ 97.38

**STATEMENT OF CHANGES IN NET ASSET VALUE
FOR THE FISCAL YEARS ENDED JUNE 30, 2003 AND 2002**

Net asset value, beginning of year	\$ 188,041,797	\$ 0
Transfer of Private Equity investments to MPEP (Notes 1, 2 and 5)	0	159,799,310
Value of units purchased by participants (Notes 1, 2 and 5)	121,828,726	15,000,000
Value of units sold by participants	(22,752,654)	0
Changes in fair value of investments managed	<u>11,069,707</u>	<u>13,242,487</u>
Net asset value, end of year	\$ <u>298,187,576</u>	\$ <u>188,041,797</u>

**STATEMENT OF INVESTMENT INCOME AND DISTRIBUTION
FOR THE FISCAL YEARS ENDED JUNE 30, 2003 AND 2002**

Investment income (Note 2)	\$ 4,924,275	\$ 9,359,200
Administrative expenses	(3,056,068)	(49,378)
Income due participants, beginning of year	<u>9,309,822</u>	<u>0</u>
Income available for distribution	11,178,029	9,309,822
Distribution (Note 2)	<u>3,816,166</u>	<u>0</u>
Income due participants, end of year	\$ <u>7,361,863</u>	\$ <u>9,309,822</u>

The accompanying notes are an integral part of these financial statements.

STATE OF MONTANA BOARD OF INVESTMENTS
MONTANA PRIVATE EQUITY POOL

NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2003 AND 2002

1. HISTORY AND ORGANIZATION

The Board was created by an act of the Legislature to invest and manage the State of Montana's investment funds on a centralized basis. The Montana Private Equity Pool (MPEP) was established by the Board to allow retirement funds, per section 17-6-201, MCA, the opportunity to participate in the venture capital and leveraged buyout markets and other private equity investments via a diversified pool. The Board approved creation of the MPEP in April 2002. Effective May 1, 2002, the Public Employees', Municipal Police Officers', Game Wardens', Sheriffs', Judges', Highway Patrol Officers', Teachers', Volunteer Firefighters' and Firefighters' Unified retirement funds transferred all their venture capital and leveraged buyout investments, at cost, totaling \$159,799,310, and cash of \$15,000,000 to the new pool. These investments were previously recorded in the All Other Funds financial statements for fiscal year 2001.

Given the complexity and specialization of private equity investment, the Board contracts with six private equity managers to invest in venture capital, leveraged buyout and other private equity investments. The retained private equity managers include Adams Street Partners, formerly Brinson Partners, Kohlberg, Kravis, Roberts and Company, (KKR), Welsh Carson Anderson and Stowe, Madison Dearborn Partners, Lexington Partners and Oaktree Capital Management. According to Board policy, the external managers may not invest more than 20% of total private equity invested capital in non-US company partnerships unless the fund is a designated non-US fund.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Investments

Montana Private Equity Pool investments are purchased in accordance with the statutorily mandated "Prudent Expert Principle". The MPEP portfolio includes venture capital, leveraged buyout, mezzanine, distressed debt, special situation and secondary investments. Venture capital represents private equity investments in early stage financing of rapidly growing companies with an innovative product or service. Leveraged buyouts (LBO's) permit an investment group to acquire a company by leveraging debt, as a financing technique, to establish a significant ownership position on behalf of the company's current management team. Mezzanine investments are the subordinated debt and/or equity of privately owned companies. The debt holder participates in equity appreciation through conversion features, such as rights, warrants, and/or options. Distressed debt represents the private and public debt of companies that appear unlikely to meet their financial obligations. This debt is attractive to investors, not for repayment of interest and principal, which are unlikely to be paid, but for the claim placed on the firm's value by unpaid creditors. Without undue principal risk, distressed debt investment managers seek capital appreciation through the sale of restructured debt obligations or newly issued securities. Special situation investments include the investment in the exploration for oil and/or gas reserves or in the development of proven reserves, investment in land to harvest timber, and investments that have a special component usually related to geographical, economic, or social issues. Secondary investments are investments in previously owned limited partnerships. These investments may be direct or via a general partner specializing in secondary investments. Private equity investments are long-term, by design, and extremely illiquid.

In creating the pool, the Board chose to securitize MPEP cash by investing in an equity derivative, the State Street Stock Performance Index Futures Fund (SPIFF). Portfolio cash is swept daily into SPIFF maintaining 100% equity exposure through holdings of stock index futures.

Investments are presented in the Statement of Net Asset Value at fair value. Because no recognized market exists for private equity investment, the MPEP investments, on valuation date, are stated at the fair value reported in the most recent external managers' valuation reports. Carrying value, parenthetically disclosed, represents the private equity security purchase price.

Broker Receivable/Payable

MPEP security transactions are recorded as of trade date rather than settlement date. Because of this generally accepted practice, the MPEP portfolio at June 30 may include receivables from brokers for securities sold but not delivered, and payables to brokers for securities purchased but not received.

Participant Units

The pension funds transferred all their venture capital and leveraged buyout investments, at cost, into the MPEP at the start-up date and were issued units according to the fair value of each participant's portfolio and cash contribution. The initial unit value as of May 1, 2002 was \$100. Although unit values are calculated at month end, the pool portfolio will be priced at least quarterly at the fair value reported in the external managers' valuation reports. Given the quarterly portfolio valuations, pool participant transactions will most likely occur on a quarterly basis. Based on the investment officer's decision, participants may buy, reinvest or sell units on the first business day of each month. All participant buys, reinvestments or sells occur after distribution of accumulated income.

Investment Income and Distribution

Investment Income reported in the Statement of Investment Income and Distribution includes cash dividends, interest, realized gains and losses, and miscellaneous income received from July 1, 2002 to June 30, 2003 for fiscal year 2003 and income received from May 1 through June 30, 2002 for fiscal year 2002. MPEP dividends are recorded on the ex-dividend date.

The MPEP Income Available for Distribution is distributed or reinvested, on behalf of the nine retirement fund participants, at least quarterly or as determined by the Investment Officer. Any cash distributions or reinvestments will occur on the first business day of the following month. The Income Available for Distribution is net of MPEP external manager fees and administrative expenses.

The fiscal year 2003 administrative expense of \$3,056,068 represents fees paid to the external managers of \$2,816,202 per their contracts and \$239,866 paid to the Board of Investments. The Board of Investments fee includes costs for the custodial bank contract. Administrative expenses incurred by the Board are charged daily to MPEP based on the Board's expenses applicable to MPEP.

The fiscal year 2002 administrative expense of \$49,378 represents fees paid to the external managers of \$15,384 per their contracts and \$33,994 paid to the Board of Investments for May and June 2002. The Board of Investments fee includes costs for the custodial bank contract. Administrative expenses incurred by the Board are charged daily to MPEP based on the Board's expenses applicable to MPEP.

Security Lending

Because there is no active security lending market for this asset class, MPEP does not participate in security lending.

3. COMMITMENTS

Private equity investments, typically, represent a seven to ten year commitment characterized by capital calls occurring during the first five years with distributions to the investor over the remaining term of the investment. The original and remaining commitments and their respective carrying and fair values, as of June 30, 2003, are listed on the next page.

Commitments as of June 30, 2003

<u>Security Investment</u>	<u>Original Commitment Date</u>	<u>Original Commitment</u>	<u>Commitment Remaining</u>	<u>Carrying Value</u>	<u>Fair Value</u>
Separate Account Partnerships	Jan 1988/Apr 1990	\$ 14,000,000	\$ 438,015	\$ 2,758,047	\$ 1,589,724
Venture Partnership Acquisition Fund II	April 1990	4,000,000	0	222,480	152,797
Brinson Venture Capital Fund III	March 1992	10,000,000	0	7,716,521	4,648,985
Brinson Venture Capital Fund IV	May 1999	15,000,000	1,191,667	13,508,333	7,458,694
Brinson Non-US Partnership Trust	January 1999	10,000,000	6,353,313	3,451,684	3,436,403
Brinson Partnership Trust 1996-2001	March 1996	105,000,000	58,385,803	42,128,356	34,305,668
Adams Street Partnership Trust 2002	August 2001	40,000,000	36,438,000	3,562,000	3,440,837
Adams Street Partnership US Fund 2003	January 2003	20,000,000	20,000,000	600,000	600,000
Adams Street Partners Fund V	August 2001	40,000,000	40,000,000	0	0
KKR 1986, 1987 Fund	August 1987	25,300,000	0	16,140,016	10,881,550
KKR 1993 Fund	December 1990	25,000,000	0	4,617,565	5,153,789
KKR 1996 Fund	July 1996	100,000,000	0	66,575,256	78,196,100
KKR European Fund	August 1999	25,000,000	14,099,346	10,900,654	8,846,513
Lexington Capital Partners V	May 2001	50,000,000	40,896,299	7,734,562	9,241,177
Madison Dearborn Partners IV	January 2001	22,509,475	19,231,452	1,873,480	1,223,077
Madison Dearborn Global IV	September 2002	2,490,525	0	2,490,525	2,669,113
Oaktree Capital IVB	September 2002	75,000,000	15,000,000	59,184,066	97,022,629
Welsh Carson Anderson & Stowe IX	September 2000	<u>25,000,000</u>	<u>11,500,000</u>	<u>10,538,031</u>	<u>11,443,301</u>
Total Private Equity Commitments		\$ <u>608,300,000</u>	\$ <u>263,533,895</u>	\$ <u>254,001,576</u>	\$ <u>280,310,357</u>

4. INVESTMENT RISK

Private equity investments are recognized as investments with a higher degree of risk with a higher return potential than traditional equity investments. Portfolio diversification of risk is to be achieved through multiple partnership relationships and investments diversified by time, financing stage, industry sector, investment size and geographical region. Private equity investments typically have a low correlation relative to other investment asset classes and should contribute to the reduction of portfolio risk and the enhancement of expected returns on a total investment portfolio basis.

5. RESTATEMENT

On the Statement of Changes in Net Asset Value for the fiscal year ended June 30, 2002, the Value of Units Purchased by Participants has been restated as \$15,000,000 from \$174,799,310 to reflect the transfer of \$159,799,310 of the Private Equity venture capital and leveraged buyout investments to the Montana Private Equity Pool (MPEP).

6. NOTICE OF LIABILITY

The Montana Board of Investments is a limited partner in the private equity partnership of O'Donnell & Masur L.P. O'Donnell&Masur L.P. invested in Gardiner Communications, Inc. All partners of O'Donnell & Masur L.P. received a Notice of Liability from the Internal Revenue Service claiming unpaid federal corporate taxes for Gardiner Communications, Inc. As a recipient of the distributions on the sale and dissolution of Gardiner Communications, Inc., the Board faces potential liability. O'Donnell&Masur L.P. has retained legal counsel to represent all partners receiving a Notice of Liability. On September 5, 2003, legal counsel filed a petition on the Montana Board of Investment's behalf in U.S. Tax Court to perfect the Board's right to contest this matter.

7. YEAR END PORTFOLIO

The June 30, 2003 MPEP portfolio is listed below. The security type percentage is based on the fair value ratio of the specific security investment type to the total portfolio.

<u>Security Name</u>	<u>Shares</u>	<u>Carrying Value</u>	<u>Fair Value</u>	<u>% of Total</u>
ALTA SUBORDINATED DEBT PARTNERS III	139,989	139,989	146,632	0.05%
AUSTIN VENTURES III	249,043	249,043	455,553	0.15%
CAPITAL PARTNERS HOLDINGS II A	44,815	44,815	327,721	0.11%
GATEWAY VENTURE PARTNERS III	284,596	284,596	50,669	0.02%
INTERWEST PARTNERS IV	275,177	275,177	8,007	0.00%
MATRIX PARTNERS III L P	68,064	68,064	16,174	0.01%
NEW ENTERPRISE ASSOCIATES V LP	253,338	253,338	57,955	0.02%
NORO MOSELEY PARTNERS II L P	174,476	174,476	144,512	0.05%
O DONNELL + MASUR L P	352,319	352,319	202,980	0.07%
SOUTH ATLANTIC PARTNERS II L P	72,202	72,202	7,706	0.00%
SPROUT CAPITAL VI	275,956	275,956	35,980	0.01%
SUMMIT VENTURE II	128,881	128,881	3,429	0.00%
WCAS CAPITAL PARTNERS II	285,716	285,716	132,034	0.04%
WILLIAM BLAIR PARTNERS III LP	153,476	153,476	372	0.00%
SEPARATE ACCOUNT PARTNERSHIPS	2,758,047	2,758,047	1,589,724	0.52%
VENTURE PARTNERSHIP ACQUISITION II	222,480	222,480	152,797	0.05%
VENTURE PARTNERSHIP ACQUISITION	222,480	222,480	152,797	0.05%
BRINSON VENTURE CAPITAL III SECONDARY	1,333,805	1,333,805	910,383	0.30%
BRINSON VENTURE PARTNERS III SECONDARY	2,823,405	2,823,405	1,414,314	0.46%
BRINSON VENTURE CAPITAL FUND III	1,166,670	1,166,670	910,383	0.30%
BRINSON VENTURE PARTNER FUND III	2,392,642	2,392,642	1,413,905	0.46%
INSTITUTIONAL VENTURE CAPITAL FUND III	7,716,521	7,716,521	4,648,985	1.52%
BRINSON VENTURE CAPITAL FUND IV	13,508,333	13,508,333	7,458,694	2.44%
BRINSON VENTURE CAPITAL FUND IV	13,508,333	13,508,333	7,458,694	2.44%
BRINSON NON US PARTNERSHIP FUND	3,451,684	3,451,684	3,436,403	1.13%
BRINSON PARTNERSHIP FUND TRUST	42,128,356	42,128,356	34,305,668	11.23%
BRINSON PARTNERSHIP TRUST	45,580,040	45,580,040	37,742,071	12.36%
ADAMS STREET NON US PARTNERSHIP FUND	570,000	570,000	557,933	0.18%
ADAMS STREET PARTNERSHIP FUND	3,592,000	3,592,000	3,482,904	1.14%
ADAMS STREET PARTNERS TRUST	4,162,000	4,162,000	4,040,837	1.32%
ADAMS STREET TOTAL	73,947,421	73,947,421	55,633,108	18.22%
KKR 1986, 1987	16,140,016	16,140,016	10,881,550	3.56%
KKR 1993	4,617,565	4,617,565	5,153,789	1.69%
KKR 1996	66,575,256	66,575,256	78,196,100	25.61%
KKR EUROPEAN FUND	10,900,654	10,900,654	8,846,513	2.90%
KKR TOTAL	98,233,491	98,233,491	103,077,952	33.76%
LEXINGTON CAPITAL PARTNERSHIP V LP	7,734,562	7,734,562	9,241,177	3.03%
LEXINGTON CAPITAL TOTAL	7,734,562	7,734,562	9,241,177	3.03%
MADISON DEARBORN CAPITAL PARTNERSHIP IV	1,873,480	1,873,480	1,223,077	0.40%
MDP IV GLOBAL INVESTMENTS LP	2,490,525	2,490,525	2,669,113	0.87%
MADISON DEARBORN TOTAL	4,364,005	4,364,005	3,892,190	1.27%
OAKTREE CAPITAL OPPORTUNITIES FUND IVB LP	59,184,066	59,184,066	97,022,629	31.77%
OAKTREE CAPITAL TOTAL	59,184,066	59,184,066	97,022,629	31.77%
WELSH CARSON ANDERSON STOWE IX	10,538,031	10,538,031	11,443,301	3.75%

<u>Security Name</u>	<u>Shares</u>	<u>Carrying Value</u>	<u>Fair Value</u>	<u>% of Total</u>
WELSH CARSON ANDERSON STOWE TOTAL	10,538,031	10,538,031	11,443,301	3.75%
TOTAL PRIVATE EQUITIES	254,001,576	254,001,576	280,310,357	91.80%
STATE STREET SPIFF	202,392	24,788,747	25,039,507	8.20%
TOTAL EQUITY FUTURES	202,392	24,788,747	25,039,507	8.20%
MPEP TOTAL	254,203,968	278,790,323	305,349,864	100.00%

LEGISLATIVE AUDIT DIVISION

Scott A. Seacat, Legislative Auditor
John W. Northey, Legal Counsel



Deputy Legislative Auditors:
Jim Pellegrini, Performance Audit
Tori Hunthausen, IS Audit & Operations
James Gillett, Financial-Compliance Audit

INDEPENDENT AUDITOR'S REPORT

The Legislative Audit Committee
of the Montana State Legislature:

We have audited the accompanying Statement of Net Investments Managed for the state of Montana Board of Investments, All Other Funds, as of June 30, 2003 and 2002, and the related Statement of Net Investment Income and Statement of Changes in Net Investments Managed for the fiscal years then ended. These financial statements are the responsibility of the Board of Investments' management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the net investments managed by the Montana Board of Investments, All Other Funds, as of June 30, 2003 and 2002, and its net investment income and changes in its net investments managed for the fiscal years then ended in conformity with accounting principles generally accepted in the United States of America.

Respectfully submitted,

Signature on File

James Gillett, CPA
Deputy Legislative Auditor

November 4, 2003

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**STATE OF MONTANA BOARD OF INVESTMENTS
ALL OTHER FUNDS FINANCIAL STATEMENTS**

STATEMENT OF NET INVESTMENTS MANAGED, JUNE 30, 2003 AND 2002

<u>Assets</u>	<u>2003</u>	<u>2002</u>
Investments managed at fair value (amortized cost of \$1,360,107,546 in 2003 and \$1,821,584,803 in 2002) (Notes 2 and 11)	\$ 1,403,338,502	\$ 1,760,474,593
Security lending cash collateral (Notes 3 and 6)	56,643,400	109,960,231
Interest receivable	12,921,901	14,386,158
Broker receivable for securities sold but not settled (Note 2)	<u>1,276,972</u>	<u>187,961</u>
Total assets	\$ <u>1,474,180,775</u>	\$ <u>1,885,008,943</u>
 <u>Liabilities</u>		
Unrealized gain (loss)	\$ 43,230,956	\$ (61,110,210)
Security lending obligations	56,643,400	109,960,231
Security lending expense payable	66,939	169,433
Broker payable for securities purchased but not settled (Note 2)	1,592,849	25,000,000
Accounts payable	<u>9,430</u>	<u>11,098</u>
Total liabilities	\$ <u>101,543,574</u>	\$ <u>74,030,552</u>
Net investments managed	\$ <u>1,372,637,201</u>	\$ <u>1,810,978,391</u>

**STATEMENT OF NET INVESTMENT INCOME
FOR THE FISCAL YEARS ENDED JUNE 30, 2003 AND 2002**

<u>Income</u>		
Investment income (Note 2)	\$ 77,235,644	\$ 84,377,228
Realized gain on sales (Note 2)	33,141,817	35,239,199
Amortization/accretion	330,020	566,184
Security lending income	<u>1,568,875</u>	<u>3,388,755</u>
Total income	\$ <u>112,276,356</u>	\$ <u>123,571,366</u>
 <u>Expenses</u>		
Administrative expenses	1,287,070	4,841,455
Security lending expense	<u>1,379,262</u>	<u>2,985,977</u>
Total expenses	\$ <u>2,666,332</u>	\$ <u>7,827,432</u>
Net investment income	\$ <u>109,610,024</u>	\$ <u>115,743,934</u>

The accompanying notes are an integral part of these financial statements.

**STATE OF MONTANA BOARD OF INVESTMENTS
ALL OTHER FUNDS FINANCIAL STATEMENTS**

**STATEMENT OF CHANGES IN NET INVESTMENTS MANAGED
FOR THE FISCAL YEARS ENDED JUNE 30, 2003 AND 2002**

	<u>2003</u>	<u>2002</u>
Total net investments managed, beginning of year	\$ 1,810,978,391	\$ 1,674,511,341
Net investment income	109,610,024	115,743,934
Income remitted to agencies	<u>(108,145,767)</u>	<u>(115,437,360)</u>
Increase (decrease) in interest receivable	(1,464,257)	(306,574)
Increase (decrease) in broker receivable (Note 2)	1,089,011	(652,935)
Increase (decrease) in security lending cash collateral (Notes 3 and 6)	(53,316,831)	(6,366,788)
Investments purchased	1,322,395,416	1,398,613,388
Transfer of Private Equity investments to MPEP (Notes 2 and 10)	0	(159,799,310)
Transfer of BGI and DFA investments to MDEP (Note 2)	(740,000,000)	0
Investments sold, matured and called (Note 10)	<u>(1,044,202,693)</u>	<u>(1,077,446,586)</u>
Increase (decrease) in book value of investments	(461,807,277)	161,367,492
Increase (decrease) in book value of investments due to net amortization of discounts and premiums	330,020	566,184
(Increase) decrease in broker payable (Note 2)	23,407,151	(24,756,779)
(Increase) decrease in accounts payable	1,668	992
(Increase) decrease in due to other funds	0	18,827
(Increase) decrease in security lending obligations (Notes 3 and 6)	53,316,831	6,366,788
(Increase) decrease in security lending expense payable	<u>102,494</u>	<u>229,843</u>
Net investments managed, end of year	\$ <u>1,372,637,201</u>	\$ <u>1,810,978,391</u>

The accompanying notes are an integral part of these financial statements.

NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2003 AND 2002

1. HISTORY AND ORGANIZATION

The Board was created by an act of the Legislature to invest and manage the State of Montana's investment funds on a centralized basis per section 17-6-201, MCA. The All Other Funds (AOF) investments and income are owned by various State of Montana agencies and managed on their behalf by the Board.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Investments

The AOF investments are purchased in accordance with the statutorily mandated "Prudent Expert Principle" and applicable investment restrictions of the participants. The AOF portfolio includes securities classified as corporate asset-backed, other corporate, US government mortgage-backed, US government, Yankee bonds, equity index, real estate, mortgages and loans. Corporate asset-backed securities represent debt securities collateralized by a pool of assets. US government mortgage-backed securities reflect participation in a pool of residential mortgages. US government securities include direct obligations of the US Treasury and indirect obligations of the US government. Yankee bonds are US dollar denominated bonds issued by foreign corporations and governments and US companies issuing debt in foreign markets. Equity index investments are investments in selected mutual funds whose equity portfolios match a broad based index or composite.

The AOF portfolio includes structured financial instruments known as REMICs (Real Estate Mortgage Investment Conduits). REMICs are pass-through vehicles for multiclass mortgage-backed securities. Strip investments represent the separate purchase of the principal and interest cash flows of a mortgage security. These securities, purchased for portfolio diversification and a competitive rate of return, are identified and reported as government mortgage-backed securities in the investment risk and portfolio disclosures. (See Note 6 on Investment Risk Categories and Note 11 for the Year End Portfolio.)

AOF fixed income securities pay a fixed rate of interest until maturity while the variable-rate (floating-rate) securities pay a variable interest rate until maturity. The variable-rate securities float with LIBOR (London Interbank Offered Rate) or the weighted average of the net mortgage interest rates for the mortgage loan group. The one variable-rate security, with an amortized cost of 17,889,456 as of June 30, 2003 is identified and reported as a government mortgage-backed security in the investment risk and portfolio disclosures. (See Note 6 on Investment Risk Categories and Note 11 for the Year End Portfolio.)

Effective May 1, 2002, all the venture capital and leveraged buyout investments totaling \$159,799,310, at cost, were transferred to the new Montana Private Equity Pool (MPEP). These investments were held by the Public Employees', Municipal Police Officers', Game Wardens', Sheriffs', Judges', Highway Patrol Officers', Teachers', Volunteer Firefighters' and Firefighters' Unified retirement funds.

Effective May 1, 2003, all the Barclays Global Investors (BGI) S&P 500 Equity Index Fund A and the Dimensional Fund Advisors (DFA) US Small Cap Trust investments totaling \$740 million, at cost, were transferred from the All Other Funds portfolio to the new Montana Domestic Equity Pool (MDEP). These investments were held by the Public Employees', Municipal Police Officers', Game Wardens', Sheriffs', Judges', Highway Patrol Officers', Teachers', Volunteer Firefighters' and Firefighters' Unified retirement funds.

Investments are presented in the Statement of Net Investments Managed at fair value. Fair values for publicly traded securities are determined primarily by reference to market prices supplied to the Board by the Board's custodial bank, State Street Bank and Trust. The real estate investments and residential and multi-family mortgages are valued based on a discounted cash flow. The commercial in-state coal tax loans and the nonparticipating repurchase agreements are reported at amortized cost. Amortized cost, parenthetically disclosed, represents the original cost, adjusted for premium and discount amortization where applicable. Premiums and discounts are amortized/accreted using the straight-line or scientific method to the call, average life or maturity date of the securities. Amortized cost may also be referred to as book value.

Broker Receivable/Payable

All Other Funds security transactions are recorded as of the trade date rather than the settlement date. Because of this generally accepted practice, the AOF portfolio at June 30 may include receivables from brokers for securities sold but not delivered, and payables to brokers for securities purchased but not received.

Montana Mortgages and Loans Receivable

The Montana mortgages and loans receivable, included in the Net Investments Managed at Fair Value, represent residential mortgages and multifamily commercial loans funded by the Public Employees' and Teachers' pension funds and other loans funded by the Coal Severance Tax Trust fund. The Coal Severance Tax Trust loan portfolio includes loans made by the Montana Science and Technology Alliance (MSTA) Board. The MSTA Board was abolished on July 1, 1999 and by law, the MSTA portfolio was assigned to the Board of Investments (BOI). (See Note 7 for the Montana mortgages and loans portfolio.)

As of June 30, 2003 and 2002, there were no uncollectible account balances for Montana mortgages and loans receivable.

However, during fiscal year 2002, the Board of Investments staff wrote off loan principal balances detailed as follows:

<u>Borrower</u>	<u>Funding Source</u>	<u>Funding Date</u>	<u>Funding Amount</u>	<u>Charge-off Date</u>	<u>Charge-off Amount</u>
Pasta Montana, L.L.C.	BOI	February 1999	\$ 5,468,337	September 2001	\$ 206,599
Pasta Montana, L.L.C.	MSTA	January 1997	350,000	September 2001	12,551
Pasta Montana, L.L.C.	MSTA	January 1997	500,000	September 2001	19,803
Nature, Inc.	MSTA	July 1989-June 1995	1,100,000	June 2002	505,213
Optima Industries, Inc.	MSTA	Dec 1991-Jan 1994	700,000	June 2002	560,500
Ultrafem, Inc.	MSTA	Dec 1991-Oct 1992	<u>700,000</u>	June 2002	<u>490,302</u>
Total			\$ <u>8,818,337</u>		\$ <u>1,794,968</u>

Investment Income

Investment income reported in the Statement of Net Investment Income includes fixed income and mortgage interest earnings, real estate income, private equity income through April 30, 2002, commercial loan interest earnings and commitment fees.

Realized Gain on Sales

Realized gain on sales reported in the Statement of Net Investment Income represents the net gain/loss resulting from the sale of fixed income, private equity and pool investments. In fiscal year 2003, the sale of pool units from the Montana Private Equity Pool (MPEP), Trust Funds Bond Pool (TFBP), Retirement Funds Bond Pool (RFBP) and the Montana Stock Pool (MTCB) generated a net gain to participants of \$41,475,231. The sale of pool units in fiscal year 2002 from the Montana Stock Pool, Montana Real Estate Investment Pool (MTRP), Retirement Funds Bond Pool and Trust Funds Bond Pool resulted in a net gain to participants of \$14,001,245.

3. SECURITIES LENDING

Under the provisions of state statutes, the Board has, via a Securities Lending Authorization Agreement, authorized the custodial bank, State Street Bank and Trust, to lend the Board's securities to broker-dealers and other entities with a simultaneous agreement to return the collateral for the same securities in the future. During the period the securities are on loan, the Board receives a fee and the custodial bank must initially receive collateral equal to 102 percent of the fair value of the loaned securities and maintain collateral equal to not less than 100 percent of the fair value of the loaned security. The Board retains all rights and risks of ownership during the loan period.

During fiscal years 2003 and 2002, State Street Bank lent, on behalf of the Board, certain securities held by State Street, as custodian, and received US dollar currency cash, US government securities, and irrevocable bank letters of credit. State Street does not have the ability to pledge or sell collateral securities unless the borrower defaults.

The Board did not impose any restrictions during fiscal years 2003 and 2002 on the amount of the loans that State Street Bank made on its behalf. There were no failures by any borrowers to return loaned securities or pay distributions thereon during fiscal years 2003 and 2002. Moreover, there were no losses during fiscal years 2003 and 2002 resulting from a default of the borrowers or State Street Bank.

During fiscal years 2003 and 2002, the Board and the borrowers maintained the right to terminate all securities lending transactions on demand. The cash collateral received on each loan was invested, together with the cash collateral of other qualified plan lenders, in a collective investment pool, the Securities Lending Quality Trust. The relationship between the

average maturities of the investment pool and the Board's loans was affected by the maturities of the loans made by other plan entities that invested cash collateral in the collective investment pool, which the Board could not determine. On June 30, 2003 and June 30, 2002, the Board had no credit risk exposure to borrowers.

As of June 30, 2003, the carrying and fair value of the underlying securities on loan for the All Other Funds was \$49,363,730 and \$55,128,809, respectively. The collateral provided for the securities on loan totaled \$56,643,400 in cash collateral.

As of June 30, 2002, the carrying and fair value of the underlying securities on loan for the All Other Funds was \$101,344,163 and \$106,533,000, respectively. The collateral provided for the securities on loan totaled \$109,960,231 in cash collateral.

4. COAL TAX LOAN AND MORTGAGE COMMITMENTS

The Board makes firm commitments to fund loans from the Coal Severance Tax Trust fund. These commitments have expiration dates and may be extended according to the Board's policies. As of June 30, 2003, the Board had committed but not yet purchased \$57,672,181 in loans from Montana lenders, compared to \$81,172,614 as of June 30, 2002. In addition to the above commitments, lenders had reserved \$41,421,046 for loans as of June 30, 2003, compared to \$89,331,230 on the same date in 2002.

The Board makes firm commitments to fund mortgages from the Public Employees' and Teachers' retirement funds. As of June 30, 2003 and 2002, the Board had committed but not yet purchased from Montana lenders mortgages totaling \$392,275 and \$10,634,477, respectively. Lenders had reserved no funding for mortgages as of June 30, 2003, compared to \$11,622,197 as of June 30, 2002.

5. PENSION FUND REAL ESTATE INVESTMENTS

100 North Park Building

In January 1996, the Board, on behalf of the Public Employees' and Teachers' Retirement funds, purchased the 100 North Park Avenue Building in Helena, Montana as a real estate investment. Acquired for a cost of \$4,864,326, the building carries a fair value of \$5,573,173 as of June 30, 2003. During fiscal year 2003, building improvements and leasing fees totaling \$129,465 were added to the cost of the building. Building improvements and elevator renovations totaling \$612,127 were added to the cost of the building in fiscal year 2002. The three-story building provides office space for approximately eight to ten tenants.

2401 Colonial Drive Building

In August 1997, the Board authorized the construction of an office building, as a real estate investment owned equally by the Public Employees' and Teachers' Retirement funds. Construction costs, including interest capitalization, totaled \$6,481,741 as of June 30, 2000. For fiscal year 2003, \$155,800 was expended on building landscaping, leasing fees, lighting and construction. In fiscal year 2002, landscaping and leasing fees of \$153,452 were added to the building cost. The three-story building, providing office space for three tenants, was occupied in November 1999. As of June 30, 2003, the building carries a cost and fair value of \$6,987,238 and \$7,581,770, respectively.

The schedule below details the minimum future rentals for both buildings on the non-cancelable operating leases as of June 30, 2003 and 2002:

Minimum future rentals for the year ending June 30, 2003:

<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009+</u>	<u>Total</u>
\$241,763	\$181,792	\$164,149	\$155,328	\$129,439	\$0	\$872,471

Minimum future rentals for the year ending June 30, 2002:

<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008+</u>	<u>Total</u>
\$945,147	\$194,572	\$134,601	\$134,601	\$134,601	\$44,867	\$1,588,389

California Street Property

In December 1998, the Board acquired a parcel of land adjacent to the Colonial Drive building to provide for additional parking. This land was purchased for \$204,835. As of June 30, 2003 the property carries a fair value of \$207,667.

Bozeman Office Building

In August 1999, the Board authorized the purchase of a new office building in Bozeman, Montana. When construction is complete, this building will be a real estate investment owned equally by the Public Employees' and Teachers' Retirement funds. The building will be occupied by four state agencies and is located on state school trust land. The Board anticipates completion of the building purchase in December 2003.

Ninth Avenue Building

In November 2000, the Board reviewed the transfer of the Public Employees' Retirement Administration (PERA) office building, located at 1712 Ninth Avenue, Helena, to the Board of Investments. By issuance of a corrective deed, the Board of Investments was named owner and building manager for the use and benefit of the PERA. During fiscal years 2003 and 2002, architect fees, remodeling construction and interest capitalization totaling \$129,465 and \$220,097, respectively, were added to the building cost for a yearend book value of \$489,187. As of June 30, 2003, the building is valued at \$565,413.

6. INVESTMENT RISK CATEGORIES

State of Montana investments are categorized below and on the next page to give an indication of the level of risk assumed at June 30, 2003 and June 30, 2002. Category 1 includes investments that are insured or registered, or securities that are held by the Board or its agent in the Board's name. Not Categorized includes investments held by broker-dealers under securities loans with cash collateral. Long-term investments are carried at amortized cost and short-term investments are carried at original cost.

Risk as of June 30, 2003

**Long-Term Investments
Category 1**

<u>Security Investment Type</u>	<u>Securities Not On Loan</u>	<u>On Loan for Securities Collateral*</u>	<u>Not Categorized*</u>	<u>Carrying Amount</u>	<u>Fair Value</u>
Corporate Asset-Backed	\$ 27,192,828	\$ 0	\$ 0	\$ 27,192,828	\$ 28,069,081
Corporate Other	238,439,395	0	3,986,781	242,426,176	262,880,396
US Govt Direct/Indirect	262,143,080	0	44,897,100	307,040,180	330,784,346
US Govt Mortgage-Backed	89,289,805	0	0	89,289,805	92,741,823
Yankee Bonds	18,479,589	0	479,849	18,959,438	20,603,889
Total	\$ 635,544,697	\$ 0	\$ 49,363,730	\$ 684,908,427	\$ 735,079,535

Direct Investments

Equity Index Fund	79,000,000	69,958,153
Equity Other	15	17
Real Estate	13,512,086	13,927,253
MT Mortgages and Loans	442,681,780	444,368,306
Total Long-Term	1,220,102,308	1,263,333,264

Short-Term Investments

Municipal Investor Account	138,412,389	138,412,389
US Bank Sweep	1,592,849	1,592,849
Total Short-Term	140,005,238	140,005,238
TOTAL INVESTMENTS	\$ 1,360,107,546	\$ 1,403,338,502

Securities Lending Collateral Investment Pool	\$ 56,643,400	\$ 56,643,400	\$ 56,643,400
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*At June 30, 2003, these underlying securities, with a fair value of \$55,128,809 were loaned for cash collateral under a security lending agreement with the state's agent.

Risk as of June 30, 2002

Long-Term Investments
Category 1

<u>Security Investment Type</u>		<u>Securities Not On Loan</u>	<u>On Loan for Securities Collateral*</u>	<u>Not Categorized*</u>	<u>Carrying Amount</u>	<u>Fair Value</u>
Corporate Asset-Backed	\$	28,679,968	\$ 0	\$ 0	28,679,968	\$ 29,213,792
Corporate Other		270,180,796	0	11,169,378	281,350,174	291,826,927
US Govt Direct/Indirect		191,532,198	0	89,325,679	280,857,877	292,276,188
US Govt Mortgage-Backed		96,166,718	0	0	96,166,718	98,004,751
Yankee Bonds		<u>10,111,731</u>	<u>0</u>	<u>839,106</u>	<u>10,950,837</u>	<u>10,934,060</u>
Total	\$	<u>596,671,411</u>	\$ 0	<u>101,334,163</u>	<u>698,005,574</u>	<u>722,255,718</u>

Direct Investments

Equity Index Fund					539,000,000	446,705,722
Real Estate					13,066,341	13,600,605
MT Mortgages and Loans					<u>556,512,888</u>	<u>562,912,548</u>
Total Long-Term					<u>1,806,584,803</u>	<u>1,745,474,593</u>

Short-Term Investments

Repurchase Agreement					<u>15,000,000</u>	<u>15,000,000</u>
Total Short-Term					<u>15,000,000</u>	<u>15,000,000</u>
TOTAL INVESTMENTS				\$	<u>1,821,584,803</u>	<u>1,760,474,593</u>
Securities Lending Collateral Investment Pool			\$	<u>109,960,231</u>	<u>109,960,231</u>	<u>109,960,231</u>

*At June 30, 2002, these underlying securities, with a fair value of \$106,533,000 were loaned for cash collateral under a security lending agreement with the state's agent.

With the exception of the US government securities, the fixed income instruments have credit risk as measured by major credit rating services. Credit risk is defined as the risk that the issuer of a fixed income security may default in making timely principal and interest payments. The Board of Investment's policy requires AOF fixed income investments, at the time of purchase, to be rated an investment grade as defined by Moody's and Standard & Poor's (S&P) rating services. The US government securities are guaranteed directly or indirectly by the US government.

Market risk for the above securities is caused by changes in the price or principal value of the security due to changes in interest rates and market liquidity.

As reported in the U.S. government mortgage-backed category, the AOF portfolio holds a REMIC with an amortized cost of \$17,889,456 as of June 30, 2003. The REMIC securities are based on separate or combined cash flows from principal and interest payments on underlying mortgages. When underlying mortgages are prepaid, the interest cash flows are reduced while principal cash flows are increased. If homeowners pay on mortgages longer than anticipated, the cash flow effect would be the opposite.

Corporate asset-backed securities are based on cash flows from principal and interest payments on underlying auto loan receivables, credit card receivables, and other assets. These securities, while sensitive to prepayments due to interest rate changes, have less credit risk than securities not backed by pledged assets. Market risk is also less because principal is paid back prior to the maturity date of the securities.

As of June 30, 2001, Service Corp. presented a credit risk to the Board. The AOF portfolio held a \$5 million par, 6% Service Corp. bond maturing December 15, 2005. By February 2001, both the Moody's and S&P bond rating agencies downgraded the bond ratings for this issue below investment grade. The December 31, 2000 book value of \$4,807,240 was reduced to \$4,000,000 as of June 30, 2001. In April 2002, this bond was sold, on the market, for \$4,752,500 including interest.

As of June 30, 2002, Enron Corp. presented a legal and higher credit risk to the Board. The AOF portfolio holds a \$3 million par 6.75% Enron bond maturing August 1, 2009. The Enron Corp. filed for Chapter 11 bankruptcy protection on December 12, 2001. Accordingly, the November 2001 book value was reduced from \$2,610,000 to \$600,000 as of June 30, 2002. In March 2003, this issue was sold, on the market, for \$472,500.

7. MONTANA MORTGAGES AND LOANS

The Montana mortgages and loans portfolio is shown below.

<u>Montana Mortgages and Loans</u>	<u>2003 Book Value</u>	<u>2002 Book Value</u>
Multifamily Commercial Loans	\$ 10,173,421	\$ 14,555,217
Residential Mortgages	195,687,788	309,482,740
Science and Technology Alliance*	14,287,541	14,733,670
Department of Natural Resources**	46,366,904	46,366,904
Department of Justice	1,902,000	1,827,000
Montana Facility Finance	1,543,021	1,636,510
Local Government Infrastructure	9,050,975	10,289,391
Value-added Loans	6,854,640	6,627,953
Commercial Loans	<u>156,815,490</u>	<u>150,993,503</u>
Permanent Coal Trust Loans	236,820,571	232,474,931
Total Montana Mortgages and Loans	\$ 442,681,780	\$ 556,512,888

* The Montana Science and Technology Alliance (MSTA) loans include funding for research and development, mezzanine and seed capital loans.

**In accordance with Senate Bill 495 enacted by the 2001 Legislature, the Coal Severance Tax Permanent Trust loaned 483,604 TFBP shares, with a book value of \$46,366,904, to the Department of Natural Resources, Trust and Legacy fund on July 2, 2001. The loan proceeds were deposited in the Trust and Legacy Fund. A loan receivable was recorded in the Coal Severance Tax Permanent Trust and a corresponding liability was recorded in the Guarantee Fund, a General Fund sub-fund. The August 2002 Special Legislative Session approved the request to record this activity in a state special revenue fund of the Office of Public Instruction rather than in the Guarantee Fund.

8. DEUTSCHE BANK SECURITIES, INC. COMPLAINT

The Board received a summons and complaint, dated September 3, 2002, regarding the sale of a Pennzoil Quaker State, \$2 million par, 6.75% corporate bond maturing April 1, 2009. Deutsche Bank Securities claims a "breach of contract" for the March 25, 2002 sale of the bond at a price of \$94.669 plus accrued interest. Deutsche Bank Securities seeks damages of \$215,453 for the additional costs incurred to acquire the bond from third parties, plus any statutory interest, costs and expenses. On October 1, 2002, Shell Oil Company acquired Pennzoil and subsequently announced a public tender of Pennzoil Quaker State debt. The Board tendered the Pennzoil Quaker State holdings on October 8, 2002 at a price of \$113.099. The tender was accepted with a settlement date of November 1, 2002. On November 4, 2002, the Board received \$2,273,230 in principal and interest plus \$60,000 as a consent fee.

9. LOAN GUARANTEES

As of June 30, 2003, loan guarantees provided by the Coal Severance Tax Permanent Trust to the Enterprise Fund and the Facility Finance Authority, formerly known as the Montana Health Facility Authority, totaled \$110,596,691. Board of Investment exposure to bond issues of the Enterprise Fund was \$74,478,374 while exposure to bond issues and surety bonds of the Facility Finance Authority was \$36,118,317.

As of June 30, 2002, loan guarantees provided by the Coal Severance Tax Permanent Trust to the Enterprise Fund and the Facility Finance Authority, formerly known as the Montana Health Facility Authority, total \$98,222,157. Board of Investment exposure to bond issues of the Enterprise Fund is \$60,335,799 while exposure to bond issues and surety bonds of

the Facility Finance Authority is \$37,886,358. Due to the correction of an error, loan guarantees as of June 30, 2002 were previously reported as \$97,218,949 and exposure to bond issues and surety bonds of the Facility Finance Authority were previously reported as \$36,883,150.

10. RESTATEMENT

On the Statement of Changes in Net Investments Managed for the fiscal year ended 2002, the Investments Sold, Matured and Called has been restated as \$1,077,446,586 from \$1,237,245,896 to reflect the transfer of \$159,799,310 of the Private Equity venture capital and leveraged buyout investments to the Montana Private Equity Pool (MPEP).

11. YEAR END PORTFOLIO

The June 30, 2003 All Other Funds portfolio is listed below. The security type percentage is based on the fair value ratio of the specific category of securities to the total portfolio.

<u>Security Name</u>	<u>Coupon</u>	<u>Maturity</u>	<u>Par</u>	<u>Book Value</u>	<u>Fair Value</u>	<u>% of Total</u>
AMERICREDIT AUTOMOBILE TRUST	7.150	08/12/04	40,351	40,351	40,364	0.00%
AMERICREDIT AUTOMOBILE TRUST	6.740	05/05/05	2,657,121	2,656,918	2,674,143	0.19%
J P MORGAN CHASE COMMERCIAL MTG TRST	4.200	07/12/35	24,375,819	24,495,559	25,354,574	1.81%
CORPORATE ASSET-BACKED			27,073,292	27,192,828	28,069,081	2.00%
AMERICAN AIRLINE EQUIPMENT TRUST	6.977	05/23/21	4,065,701	4,054,336	3,333,874	0.24%
AMERICAN TRANS AIR EQUIPMENT TRUST	8.039	07/15/17	4,484,900	4,484,900	4,761,431	0.34%
ASHLAND INC	7.830	08/15/05	10,000,000	10,000,000	10,917,790	0.78%
BANK OF AMERICA	7.875	05/16/05	5,000,000	5,168,927	5,583,651	0.40%
BANK ONE	6.250	02/15/08	2,000,000	1,924,399	2,294,683	0.16%
BANKBOSTON NA	6.375	03/25/08	2,000,000	1,928,947	2,278,711	0.16%
BORG WARNER AUTOMOTIVE INC	7.000	11/01/06	4,000,000	4,049,890	4,494,736	0.32%
BURLINGTON NORTHERN RR CO	6.940	01/02/14	3,748,199	3,748,199	4,493,457	0.32%
BURLINGTON NORTHERN SANTA FE RY	7.160	01/02/20	4,679,425	4,679,425	5,288,899	0.38%
CIT GROUP EQUIPMENT TRUST	6.490	01/05/21	8,152,315	8,152,315	8,363,907	0.60%
CIT GROUP INC	5.750	09/25/07	5,000,000	5,181,005	5,496,038	0.39%
CIT GROUP INC	5.625	05/17/04	5,000,000	4,998,288	5,158,811	0.37%
CSX CORP	7.450	05/01/07	5,000,000	4,997,102	5,850,340	0.42%
CITIGROUP INC	5.750	05/10/06	1,000,000	999,949	1,102,727	0.08%
CITIGROUP INC	6.000	02/21/12	5,000,000	4,998,401	5,703,307	0.41%
CONSOLIDATED NATURAL GAS CO	7.250	10/01/04	10,000,000	9,994,382	10,681,098	0.76%
CONTINENTAL AIRLINES EQUIPMENT TRUST	6.563	02/15/12	5,000,000	5,024,369	5,289,050	0.38%
DELTA AIR LINES INC EQUIPMENT TRUST	6.417	07/02/12	10,000,000	9,959,721	10,462,500	0.75%
DETROIT EDISON CO	5.200	10/15/12	5,000,000	4,935,623	5,363,124	0.38%
ENSERCH CORP	6.375	02/01/04	5,000,000	4,987,186	5,104,548	0.36%
FMC CORP	6.375	09/01/03	3,000,000	2,999,034	3,007,500	0.21%
FIRST BANK NA	8.350	11/01/04	5,000,000	4,999,332	5,407,141	0.39%
FIRST CHICAGO CORP	6.375	01/30/09	2,000,000	1,892,339	2,303,999	0.16%
FIRST SECURITY CORP	6.875	11/15/06	5,000,000	4,996,939	5,730,682	0.41%
FIRST UNION CORP	7.050	08/01/05	5,000,000	4,987,426	5,521,324	0.39%
FIRST UNION CORP	7.100	08/15/04	1,000,000	999,426	1,061,614	0.08%
FORD MOTOR CREDIT CO	6.700	07/16/04	10,000,000	10,027,546	10,395,580	0.74%
GENERAL ELECTRIC CAPITAL CORP	5.375	03/15/07	10,000,000	10,236,550	11,034,565	0.79%
GENERAL MOTORS ACCEPTANCE CORP	7.500	07/15/05	9,000,000	8,996,513	9,656,229	0.69%
GENERAL MOTORS ACCEPTANCE CORP	6.125	08/28/07	5,000,000	5,007,620	5,210,905	0.37%
J P MORGAN CHASE + CO	5.350	03/01/07	5,000,000	4,981,617	5,496,613	0.39%
KCT INTERMODAL EQUIPMENT TRUST	6.884	08/01/18	3,753,867	3,753,867	4,115,616	0.29%
K N ENERGY INC	6.650	03/01/05	7,000,000	7,044,256	7,494,577	0.53%
KEY CORP	7.500	06/15/06	5,000,000	4,997,106	5,713,098	0.41%
MARSH AND MCLENNAN COS INC	6.625	06/15/04	1,000,000	999,049	1,049,782	0.07%
MARSH AND MCLENNAN COS INC	7.125	06/15/09	3,000,000	2,995,568	3,604,248	0.26%
NATIONSBANK CORP	7.750	08/15/04	5,000,000	4,981,577	5,358,711	0.38%
NATIONWIDE FINANCIAL SERVICES INC	6.250	11/15/11	5,000,000	5,344,042	5,538,589	0.39%
NORFOLK SOUTHERN CORP	7.350	05/15/07	3,500,000	3,499,064	4,098,971	0.29%

<u>Security Name</u>	<u>Coupon</u>	<u>Maturity</u>	<u>Par</u>	<u>Book Value</u>	<u>Fair Value</u>	<u>% of Total</u>
NORTHWEST AIRLINES EQUIPMENT TRUST	6.810	08/01/21	4,417,909	4,353,593	4,373,730	0.31%
OLD REPUBLIC INTERNATIONAL CORP	7.000	06/15/07	3,000,000	2,999,358	3,485,691	0.25%
PPL MONTANA LLC	8.903	07/02/20	4,647,959	4,647,959	5,221,006	0.37%
SOUTHWEST GAS CORP	8.375	02/15/11	4,000,000	3,995,341	4,662,586	0.33%
SPRINT CAPITAL CORP	5.875	05/01/04	1,500,000	1,497,605	1,540,336	0.11%
UNION OIL CO CALIFORNIA	7.200	05/15/05	5,000,000	4,999,305	5,447,391	0.39%
UNION PACIFIC CORP	6.400	02/01/06	5,000,000	4,989,927	5,528,081	0.39%
UNION PACIFIC RESOURCES GROUP INC	7.000	10/15/06	5,000,000	4,990,323	5,697,631	0.41%
UNION TANK CAR CO	7.125	02/01/07	2,000,000	1,999,233	2,314,055	0.16%
WACHOVIA CORP	4.950	11/01/06	5,000,000	4,992,686	5,405,098	0.39%
WAL MART STORES INC PASS THRU TRUST	8.450	07/01/04	986,489	986,489	1,054,414	0.08%
WELLS FARGO + CO	5.900	05/21/06	1,000,000	999,289	1,108,250	0.08%
WESTERN PROPERTIES REIT	7.875	02/15/04	2,000,000	1,999,635	2,069,186	0.15%
WESTERN PROPERTIES REIT	7.200	09/15/08	1,000,000	969,200	1,150,522	0.08%
CORPORATE OTHER			241,936,763	242,426,176	262,880,395	18.73%
ENSCO OFFSHORE CO USGG XI	6.360	12/01/15	12,500,132	12,500,132	13,781,895	0.98%
FEDERAL HOME LOAN MORTGAGE CORP	4.750	10/11/12	40,000,000	39,840,080	41,048,068	2.93%
FEDERAL HOME LOAN MORTGAGE CORP	5.125	05/13/13	20,000,000	20,000,000	20,220,728	1.44%
FEDERAL FARM CREDIT BANKS	3.875	02/01/05	20,000,000	19,906,316	20,812,718	1.48%
FEDERAL FARM CREDIT BANKS	4.875	11/15/06	5,000,000	4,952,042	5,452,792	0.39%
FEDERAL FARM CREDIT BANKS	4.875	02/15/07	5,000,000	4,999,202	5,469,564	0.39%
FEDERAL FARM CREDIT BANKS	4.000	02/15/05	10,000,000	9,992,400	10,432,920	0.74%
FEDERAL HOME LOAN MORTGAGE CORP	6.250	07/15/04	10,000,000	9,977,943	10,527,104	0.75%
FEDERAL HOME LOAN MORTGAGE CORP	5.625	03/15/11	10,000,000	10,071,713	11,418,639	0.81%
FEDERAL HOME LOAN MORTGAGE CORP	6.000	06/15/11	15,000,000	14,989,422	17,502,402	1.25%
FEDERAL HOME LOAN MORTGAGE CORP	3.250	11/15/04	10,000,000	9,890,703	10,276,859	0.73%
FEDERAL NATIONAL MORTGAGE ASSOCIATION	6.000	05/15/08	5,000,000	4,893,961	5,764,926	0.41%
FEDERAL NATIONAL MORTGAGE ASSOCIATION	0.000	06/01/17	14,600,000	5,938,809	7,438,723	0.53%
FEDERAL NATIONAL MORTGAGE ASSOCIATION	7.250	01/15/10	8,000,000	8,377,268	9,893,629	0.71%
FEDERAL NATIONAL MORTGAGE ASSOCIATION	7.000	07/15/05	2,000,000	2,009,925	2,221,943	0.16%
FEDERAL NATIONAL MORTGAGE ASSOCIATION	6.625	10/15/07	15,000,000	16,192,225	17,555,573	1.25%
FEDERAL NATIONAL MORTGAGE ASSOCIATION	6.625	11/15/10	10,000,000	10,320,663	12,081,131	0.86%
FEDERAL NATIONAL MORTGAGE ASSOCIATION	6.000	12/15/05	2,000,000	2,017,531	2,209,540	0.16%
FEDERAL NATIONAL MORTGAGE ASSOCIATION	5.250	06/15/06	5,000,000	5,031,326	5,490,183	0.39%
FEDERAL NATIONAL MORTGAGE ASSOCIATION	5.875	02/14/06	5,000,000	4,925,306	5,516,972	0.39%
FEDERAL NATIONAL MORTGAGE ASSOCIATION	5.740	01/21/09	8,000,000	7,556,838	8,206,522	0.58%
FEDERAL NATIONAL MORTGAGE ASSOCIATION	2.750	09/12/06	27,000,000	27,000,000	27,268,383	1.94%
GLOBAL INDUSTRIES LTD USGG XI	7.710	02/15/25	4,400,000	4,400,000	4,400,000	0.31%
GUARANTEED EXPORT TRUST PDVSA	6.280	06/15/04	705,882	705,882	731,520	0.05%
MAYBANK NAVIGATION CO LLC USGG XI	7.620	07/25/20	4,375,000	4,375,000	4,593,269	0.33%
NORTH AMERICAN SHIP BUILDING USGG XI	5.840	02/15/06	1,920,000	1,920,000	2,019,341	0.14%
PERFORADORA CENT S A DE C V USGG XI	5.630	07/15/11	16,647,000	16,634,495	17,571,574	1.25%
ROWAN COS INC USGG XI	5.880	03/15/12	20,452,000	20,452,000	23,077,832	1.64%
TRICO MARINE INTERNATIONAL USGG XI	6.080	09/01/06	4,375,000	4,375,000	4,653,163	0.33%
MAYBANK NAVIGATION CO LLC USGG XI	5.900	09/16/13	2,794,000	2,794,000	3,146,435	0.22%
GOVERNMENT DIRECT-INDIRECT			314,769,014	307,040,180	330,784,346	23.57%
FEDERAL HOME LOAN POOL G10814	5.500	05/01/13	7,189,988	7,184,667	7,517,470	0.54%
FEDERAL HOME LOAN POOL G10173	6.000	01/01/09	672,199	670,111	701,188	0.05%
FEDERAL HOME LOAN POOL E00247	5.500	10/01/08	579,138	571,731	604,792	0.04%
FEDERAL HOME LOAN POOL E00540	6.000	03/01/13	4,800,845	4,785,855	5,019,884	0.36%
FEDERAL HOME LOAN POOL E00659	6.000	04/01/14	4,669,223	4,665,643	4,876,420	0.35%
FNMA POOL 190985	7.500	08/01/09	1,723,488	1,723,487	1,846,353	0.13%
FNMA POOL 254140	5.500	01/01/17	20,714,828	20,630,901	21,554,750	1.54%
FNMA POOL 254233	5.000	03/01/17	12,418,573	12,003,590	12,851,768	0.92%
FNMA POOL 254631	5.000	02/01/18	9,401,953	9,564,706	9,726,505	0.69%
FNMA POOL 303590	7.000	11/01/10	1,915,237	1,915,237	2,042,945	0.15%
FNMA POOL 313999	6.000	02/01/13	2,550,964	2,538,743	2,676,917	0.19%
FNMA POOL 572220	6.000	03/01/16	1,771,825	1,766,899	1,853,772	0.13%

<u>Security Name</u>	<u>Coupon</u>	<u>Maturity</u>	<u>Par</u>	<u>Book Value</u>	<u>Fair Value</u>	<u>% of Total</u>
FNMA POOL 592327	5.500	06/01/16	3,457,229	3,378,779	3,599,570	0.26%
GOVERNMENT NATIONAL MORTGAGE ASSOC	2.196	04/16/20	17,950,842	17,889,456	17,869,489	1.27%
GOVERNMENT-MORTGAGE BACKED			89,816,333	89,289,805	92,741,823	6.61%
CASE CORP	6.250	12/01/03	5,000,000	4,998,428	5,018,750	0.36%
HOUSEHOLD FINANCE CORP	6.875	03/01/07	3,000,000	2,961,631	3,454,340	0.25%
HOUSEHOLD FINANCE CORP	6.500	01/24/06	5,000,000	5,036,880	5,550,799	0.40%
IBP FINANCIAL CO CANADA	7.450	06/01/07	4,000,000	3,998,918	4,340,000	0.31%
PANAMERICAN BEVERAGES INC	7.250	07/01/09	2,000,000	1,963,581	2,240,000	0.16%
YANKEE BONDS			19,000,000	18,959,438	20,603,889	1.47%
S & P 500 INDEX FUND B	N/A	N/A	555,010	79,000,000	69,958,153	4.99%
EQUITY INDEX FUND			555,010	79,000,000	69,958,153	4.99%
OCEAN WEST HOLDING CORP	N/A	N/A	100	15	17	0.00%
EQUITY OTHER			100	15	17	0.00%
CALIFORNIA STREET, HELENA, MONTANA	N/A	N/A	204,835	204,835	207,667	0.01%
2401 COLONIAL DRIVE, HELENA, MONTANA	N/A	N/A	6,987,238	6,987,238	7,581,000	0.54%
NINTH AVENUE, HELENA, MONTANA	N/A	N/A	489,187	489,187	565,413	0.04%
100 NORTH PARK AVENUE, HELENA, MT	N/A	N/A	5,830,825	5,830,825	5,573,173	0.40%
EQUITY REAL ESTATE			13,512,086	13,512,086	13,927,253	0.99%
MT MULTI FAMILY/COMMERCIAL LOANS	N/A	N/A	10,173,421	10,173,421	10,135,819	0.72%
MONTANA RESIDENTIAL MORTGAGES	N/A	N/A	195,687,788	195,687,788	197,411,916	14.07%
MONTANA PERMANENT COAL TRUST LOANS	N/A	N/A	236,820,571	236,820,571	236,820,571	16.88%
MORTGAGES/LOANS			442,681,780	442,681,780	444,368,306	31.67%
US BANK MUNICIPAL INVESTOR ACCOUNT	1.600	N/A	138,412,389	138,412,389	138,412,389	9.86%
US BANK SWEEP	0.300	07/01/03	1,592,849	1,592,849	1,592,849	0.11%
CASH EQUIVALENTS			140,005,238	140,005,238	140,005,238	9.98%
TOTAL ALL OTHER FUNDS			<u>1,289,349,616</u>	<u>1,360,107,546</u>	<u>1,403,338,502</u>	<u>100.00%</u>

LEGISLATIVE AUDIT DIVISION

Scott A. Seacat, Legislative Auditor
John W. Northey, Legal Counsel



Deputy Legislative Auditors:
Jim Pellegrini, Performance Audit
Tori Hunthausen, IS Audit & Operations
James Gillett, Financial-Compliance Audit

INDEPENDENT AUDITOR'S REPORT

The Legislative Audit Committee
of the Montana State Legislature:

We have audited the accompanying Statement of Net Assets of the Enterprise Fund of the state of Montana Board of Investments as of June 30, 2003 and 2002, and the related Statement of Revenues, Expenses, and Changes in Fund Net Assets and Statement of Cash Flows for the fiscal years then ended. These financial statements are the responsibility of the Board of Investments' management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in note 1, the financial statements present only the Enterprise Fund of the Montana Board of Investments and are not intended to present fairly the financial position, of the state of Montana as of June 30, 2003 and 2002, and the results of operations and cash flows for the fiscal years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the state of Montana Board of Investments' Enterprise Fund as of June 30, 2003 and 2002, and the results of its operations and cash flows of its Enterprise Fund for the fiscal years then ended in conformity with accounting principles generally accepted in the United States of America.

Respectfully submitted,

Signature on File

James Gillett, CPA
Deputy Legislative Auditor

November 4, 2003

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**STATE OF MONTANA BOARD OF INVESTMENTS ENTERPRISE FUND
STATEMENT OF NET ASSETS AS OF JUNE 30, 2003 AND 2002**

Assets	<u>2003</u>	<u>2002</u>
Current assets:		
Cash and cash equivalents (Note 1)	\$ 10,762,957	\$ 7,810,496
Interest receivable	1,050,039	1,167,493
Notes/loans receivable (Note 1)	6,356,754	4,448,775
Short-term investments (Note 2)	8,954,343	1,443,516
Due from other funds	179	0
Prepaid expenses	<u>36</u>	<u>74</u>
Total current assets	<u>27,124,308</u>	<u>14,870,354</u>
Noncurrent assets:		
Noncurrent assets restricted:		
Notes/loans receivable (Note 1)	47,751,994	45,801,121
Investments (Note 2)	3,496,317	3,706,017
Total assets restricted	<u>51,248,311</u>	<u>49,507,138</u>
Notes/loans receivable (Note 1)	7,662,518	9,237,788
Investments (Note 2)	175,000	414,067
Capitalized cost of issue (Note 1)	1,220,532	984,976
Equipment	12,239	12,239
Accumulated depreciation	(6,120)	(4,162)
Total noncurrent assets	<u>60,312,480</u>	<u>60,152,046</u>
Total assets	\$ <u>87,436,788</u>	\$ <u>75,022,400</u>
Liabilities		
Current liabilities:		
Advances	\$ 101,272	\$ 171,547
Due to other funds	7,259	4,802
Accrued expenses	11,018	2,277
Accrued interest payable	649,706	801,857
Deferred cost of issue recovery	17,785	17,785
Arbitrage rebate tax payable	73,344	71,839
Compensated absences	12,040	17,775
Current bonds/notes payable (Note 4)	<u>74,266,636</u>	<u>59,329,761</u>
Total current liabilities	<u>75,139,060</u>	<u>60,417,643</u>
Noncurrent liabilities		
Bonds/notes payable (Note 4)	7,188,600	9,709,409
Compensated absences	18,929	16,047
Deferred cost of issue recovery	17,785	35,569
Arbitrage rebate tax payable	<u>97,294</u>	<u>100,215</u>
Total noncurrent liabilities	<u>7,322,608</u>	<u>9,861,240</u>
Total liabilities	\$ <u>82,461,668</u>	\$ <u>70,278,883</u>
Net Assets		
Invested in capital assets, net of related debt	\$ 6,119	\$ 8,077
Restricted (Note 1)	2,852,753	2,460,293
Unrestricted	<u>2,116,248</u>	<u>2,275,147</u>
Total net assets (Note 8)	\$ <u>4,975,120</u>	\$ <u>4,743,517</u>
Total liabilities and net assets	\$ <u>87,436,788</u>	\$ <u>75,022,400</u>

The accompanying notes are an integral part of these financial statements.

**STATE OF MONTANA BOARD OF INVESTMENTS ENTERPRISE FUND
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET ASSETS
FOR THE FISCAL YEARS ENDED JUNE 30, 2003 AND 2002**

Operating revenue	<u>2003</u>	<u>2002</u>
Reimbursements	\$ 20,403	\$ 12,992
Investment income	339,106	575,823
Security lending income	0	135
Financing income	<u>2,595,717</u>	<u>2,892,571</u>
Total operating revenue	<u>2,955,226</u>	<u>3,481,521</u>
Operating expenses		
Personal services	198,973	172,187
Contracted services	38,174	65,035
Supplies and materials	4,382	7,801
Communications	7,051	8,177
Travel	3,906	4,535
Rent	38,749	38,312
Repair and maintenance	499	1,460
Indirect and other costs	35,662	33,038
Depreciation expense	1,958	1,669
Arbitrage rebate tax expense	81,862	47,065
Security lending expense	0	121
Debt service		
Interest expense	1,675,336	2,526,438
Trustee fee expense	40,541	41,239
Bond issuance cost amortization expense	142,349	164,118
Other debt service expense	156,915	140,283
Total operating expenses	<u>2,426,357</u>	<u>3,251,478</u>
Operating income	<u>528,869</u>	<u>230,043</u>
Nonoperating (expense):		
Transfers out (Note 6)	<u>(297,266)</u>	<u>0</u>
Change in net assets	231,603	230,043
Beginning net assets	4,743,517	4,513,474
Ending net assets (Note 8)	\$ <u>4,975,120</u>	\$ <u>4,743,517</u>

The accompanying notes are an integral part of these financial statements.

**STATE OF MONTANA BOARD OF INVESTMENTS ENTERPRISE FUND
STATEMENT OF CASH FLOWS FOR THE YEARS ENDED JUNE 30, 2003 AND 2002**

	<u>2003</u>		<u>2002</u>
Cash flows from operating activities:			
Receipts for sales and services	\$ 20,403	\$	12,992
Payments to suppliers for goods and services	(126,042)		(158,624)
Payments to employees	<u>(193,186)</u>		<u>(182,437)</u>
Net cash (used for) operating activities	<u>(298,825)</u>		<u>(328,069)</u>
Cash flows from non-capital financing activities:			
Payment of principal and interest on bonds and notes	(5,128,094)		(6,842,701)
Proceeds from issuance of bonds and notes	15,476,643		1,043,636
Payment of bond issue costs	(335,330)		0
Transfers to other funds (Note 6)	<u>(297,266)</u>		<u>0</u>
Net cash (used for) provided by non-capital financing activities	<u>9,715,953</u>		<u>(5,799,065)</u>
Cash flows from capital and related financing activities:			
Acquisition of fixed assets	0		(6,411)
Net cash (used for) capital and related financing activities	<u>0</u>		<u>(6,411)</u>
Cash flows from investing activities:			
Collections for principal and interest on loans	25,005,756		17,449,926
Cash payments for loans	(24,688,342)		(17,120,612)
Purchase of investments	(11,979,150)		(312,298)
Proceeds from security lending	0		135
Security lending costs	0		(121)
Proceeds from sales or maturities of investments	4,914,061		1,363,000
Interest on investments	366,287		550,491
Payments for arbitrage rebate tax	<u>(83,279)</u>		<u>(247,622)</u>
Net cash (used for) provided by investing activities	<u>(6,464,667)</u>		<u>1,682,899</u>
Net increase (decrease) in cash and cash equivalents	2,952,461		(4,450,646)
Cash and cash equivalents, July 1	<u>7,810,496</u>		<u>12,261,142</u>
Cash and cash equivalents, June 30	<u>10,762,957</u>		<u>7,810,496</u>
Reconciliation of net income to net cash (used for) operating activities:			
Net income	528,869		230,043
Adjustments to reconcile net income to net cash (used for) operating activities			
Depreciation	1,958		1,668
Interest on investments	(339,106)		(575,823)
Financing income	(2,595,717)		(2,892,571)
Interest expense	2,015,141		2,872,078
Security lending income	0		(135)
Security lending expense	0		121
Arbitrage rebate tax expense	81,862		47,065
Change in assets and liabilities:			
Increase/decrease in due from other funds	(179)		0
Increase/decrease in other assets	38		15
Increase/decrease in other payables	8,741		459
Increase/decrease in due to other funds	2,421		(7,221)
Increase/decrease in compensated absences payable	<u>(2,853)</u>		<u>(3,768)</u>
Total adjustments	<u>(827,694)</u>		<u>(558,112)</u>
Net cash (used for) operating activities	\$ <u>(298,825)</u>	\$	<u>(328,069)</u>
Schedule of noncash transactions:			
Increase/decrease in fair value of investments	\$ 1,303	\$	68,500
Total noncash transactions	\$ 1,303	\$	68,500

The accompanying notes are an integral part of these financial statements.

STATE OF MONTANA BOARD OF INVESTMENTS ENTERPRISE FUND

NOTES TO FINANCIAL STATEMENTS
FOR THE FISCAL YEARS ENDED JUNE 30, 2003 AND JUNE 30, 2002

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

a. Basis of Accounting

The Board uses the accrual basis of accounting for the Enterprise Fund. Under the accrual basis of accounting, expenses are recorded when incurred and revenues are recorded when earned. The financial statements are prepared from the Statewide Accounting, Budgeting, and Human Resource System (SABHRS) and information contained in the bond trustee statements. The statements include the financial activity administered by the Board in the Enterprise Fund.

b. Presentation of Programs

The Board uses the Enterprise Fund to account for its programs created under the Economic Development Bond Act and the Municipal Finance Consolidation Act.

Economic Development Bond Act programs include:

- The Industrial Development Bond Program (IDB) provides access to limited economic development projects through the issuance of conduit debt.
- The Conservation Reserve Enhancement Program (CRP), created in 1990 by issuing bonds, allows farmers to receive a lump sum payment by assigning their federal CRP contract to the Board. The farmers under contract must comply with seeding and other requirements. The Conservation Reserve Enhancement Program is funded by the Montana Trust Funds Bond Pool.
- The Family Friendly Business Loan Program provides zero interest loans to qualified business owners who hire participants of the Families Achieving Independence in Montana (FAIM) employment and training component.

Municipal Finance Consolidation Act programs include:

- The INTERCAP loan program provides funds to eligible Montana governments to finance capital expenditures for up to ten years.
- The Irrigation District Pooled Loan Program provided funds for the Board to purchase the refunding bonds from participating irrigation districts for the purpose of prepaying the U.S. Department of Interior, Bureau of Reclamation Projects Loans.
- The School District Pooled Refunding Program provided funds for the Board to purchase the general obligation refunding bonds of participating Montana School Districts.

c. Fixed Asset Depreciation

The equipment fixed assets recorded in the Enterprise Fund are depreciated on a straight-line basis, with salvage value, in accordance with state policy.

d. Receivables

The Enterprise Fund notes/loan receivables of \$61,771,266 as of June 30, 2003, and \$59,487,684 as of June 30, 2002, represent loans made to Montana businesses and local governments. As of June 30, 2003 and 2002, there were no uncollectible account balances.

e. Capitalized Cost of Issue

The Enterprise Fund capitalized cost of issue asset of \$1,220,532 and \$984,976 as of June 30, 2003 and June 30, 2002, respectively, represents paid bond issuance costs which have been capitalized and are being amortized, using the straight-line method, over the life of the bond.

f. Cash and Cash Equivalents

For purposes of the Statement of Cash Flows, the Enterprise Fund considers all highly liquid investments with an original maturity of three months or less when purchased to be cash equivalents. Cash and cash equivalents, as identified in the Statement of Net Assets, are as follows:

	<u>June 30, 2003</u>	<u>June 30, 2002</u>
Cash in treasury	\$ 13,726	\$ 17,612
Cash with fiscal agent	2,243,569	(245,742)
Short Term Investment Pool (STIP)	142,680	80,417
First American treasury obligation class D corporate trust fund	<u>8,362,982</u>	<u>7,958,209</u>
Cash and cash equivalents	\$ <u>10,762,957</u>	\$ <u>7,810,496</u>

Due to the correction of an error, the Cash in Treasury as of June 30, 2002 has been restated from \$16,794 to \$17,612 and the June 30, 2002 Cash and Cash Equivalents total has been restated from \$7,809,678 to \$7,810,496.

The Enterprise Fund invests its excess cash in the Board's Short Term Investment Pool, STIP, an external investment pool. An external investment pool commingles the moneys of more than one legally separate entity and invests, on the participants' behalf, in an investment portfolio. STIP participants include both state agencies and local governments. By meeting certain conditions, STIP, as a 2a7-like pool, is allowed to use amortized cost rather than fair value to report net assets to compute unit values.

g. Restricted Assets

The Statement of Net Assets for the Enterprise Fund reports restricted assets. Net assets are reported as restricted when constraints placed on net asset use are either:

- a. Externally imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments.
- b. Imposed by law through constitutional provisions or enabling legislation.

The net assets of all Enterprise Fund programs with the exception of MEDB (Montana Economic Development Bonds) Guarantee Fund Account, MEDB Guarantee CRP Note Reserve, MEDB Contingency Account, MEDB Family Friendly Account and CRP are restricted under bond indentures governing the use of these funds.

2. INVESTMENTS

The deposits and investments in the Enterprise Fund are restricted by the bond trust indentures to the following: government and agency obligations, certificates of deposits, repurchase agreements, and investment agreements. Deposits and investments must be made with Montana banks or in the Short Term Investment Pool (STIP) administered by the Board. The deposits and investments are combined on the Board's financial statements.

Investments are presented in the Statement of Net Assets at fair value. Investment fair values for publicly traded securities are determined primarily by reference to market prices supplied to the Board's trustee. Amortized cost, or carrying value, represents the original cost, adjusted for premium and discount amortization where applicable. Premiums and discounts are amortized/accreted using the straight-line method to the maturity date of the securities.

The Board's investments in the Enterprise Fund are classified on the next page as to credit risk by Category 1, which includes investments that are insured or registered, or securities held by the Board or its agent in the Board's name.

Risk as of June 30, 2003

Long-Term Investments

<u>Investment Type</u>	<u>Category 1</u>	<u>Carrying Value</u>	<u>Fair Value</u>
Government Securities	\$ <u>3,509,883</u>	\$ <u>3,509,883</u>	\$ <u>3,671,317</u>
Total long-term investments	\$ <u>3,509,883</u>	\$ <u>3,509,883</u>	\$ <u>3,671,317</u>

Short-Term Investments

Government Securities	\$ <u>8,922,955</u>	\$ <u>8,922,955</u>	\$ <u>8,954,343</u>
Total short-term investments	\$ <u>8,922,955</u>	\$ <u>8,922,955</u>	\$ <u>8,954,343</u>
Securites Lending Collateral Investment Pool	\$ <u>0</u>	\$ <u>0</u>	\$ <u>0</u>

Risk as of June 30, 2002

Long-Term Investments

<u>Investment Type</u>	<u>Category 1</u>	<u>Carrying Value</u>	<u>Fair Value</u>
Government Securities	\$ <u>3,953,192</u>	\$ <u>3,953,192</u>	\$ <u>4,120,084</u>
Total long-term investments	\$ <u>3,953,192</u>	\$ <u>3,953,192</u>	\$ <u>4,120,084</u>

Short-Term Investments

Government Securities	\$ <u>1,418,888</u>	\$ <u>1,418,888</u>	\$ <u>1,443,516</u>
Total short-term investments	\$ <u>1,418,888</u>	\$ <u>1,418,888</u>	\$ <u>1,443,516</u>
Securites Lending Collateral Investment Pool	\$ <u>0</u>	\$ <u>0</u>	\$ <u>0</u>

There were no derivative transactions during the above fiscal years for investments held by the trustee.

3. SECURITY LENDING

The Enterprise Fund is a participant in the Board's Short Term Investment Pool (STIP).

Under the provisions of state statutes, the Board has, via a Securities Lending Authorization Agreement, authorized the custodial bank, State Street Bank and Trust, to lend the Board's STIP securities to broker-dealers and other entities with a simultaneous agreement to return the collateral for the same securities in the future. During the period the securities are on loan, the Board receives a fee and the custodial bank must initially receive collateral equal to 102 percent of the fair value of the loaned securities and maintain collateral equal to not less than 100 percent of the fair value of the loaned security. The Board retains all rights and risks of ownership during the loan period.

During fiscal years 2003 and 2002, State Street lent, on behalf of the Board, certain STIP securities held by State Street, as custodian, and received US dollar currency cash, US government securities, and irrevocable bank letters of credit. State Street does not have the ability to pledge or sell collateral securities unless the borrower defaults.

The Board did not impose any restrictions during fiscal years 2003 and 2002 on the amount of the loans that State Street made on its behalf. There were no failures by any borrowers to return loaned securities or pay distributions thereon during fiscal years 2003 and 2002. Moreover, there were no losses during fiscal years 2003 and 2002 resulting from a default of the borrowers or State Street.

During fiscal years 2003 and 2002, the Board and the borrowers maintained the right to terminate all securities lending transactions on demand. The cash collateral received on each loan was invested, together with the cash collateral of other qualified plan lenders, in a collective investment pool, the Securities Lending Quality Trust. The relationship between the average maturities of the investment pool and the Board's loans was affected by the maturities of the loans made by other plan entities that invested cash collateral in the collective investment pool, which the Board could not determine. On June 30, 2003 and June 30, 2002, the Board had no credit risk exposure to borrowers.

4. BONDS PAYABLE

Long-Term Bonds Payable

Economic Development Bonds (EDB) and Municipal Finance Consolidation Act Bonds (MFCAB)

These bonds are issued under the Economic Development Bond Act, and the Municipal Finance Consolidation Act, for the purpose of assisting Montana's small businesses and local governments in obtaining low cost financing. Outstanding obligations are listed as follows (in thousands):

Bonds Payable as of June 30, 2003

<u>Program</u>	<u>Series</u>	<u>Amount Issued</u>	<u>Interest Range %</u>	<u>Principal Payments</u>		<u>Balance June 30, 2003</u>
				<u>FY 2004</u>	<u>@ Maturity</u>	
Municipal Finance Consolidation Act Bonds (Irrigation Program) (1)	1988	4,976	6.60-7.75	520	130 (2014)	1,707
Municipal Finance Consolidation Act Bonds (School District Pooled Refunding Program) (3)	1991	6,234	4.75-6.50	287	294 (2005)	581
Conservation Reserve Enhancement Program (CRP Bonds) (2)		<u>6,977</u>	6.00-8.00	<u>1,270</u>	30 (2011)	<u>6,977</u>
Total Bonds Payable		\$ <u>18,187</u>		\$ <u>2,077</u>		\$ <u>9,265</u>
Less Current Portion (FY2003 Principal Payments)						(<u>2,077</u>)
Total Long-Term Bonds Payable						\$ <u>7,188</u>

Bonds Payable as of June 30, 2002

<u>Program</u>	<u>Series</u>	<u>Amount Issued</u>	<u>Interest Range %</u>	<u>Principal Payments</u>		<u>Balance June 30, 2002</u>
				<u>FY 2003</u>	<u>@ Maturity</u>	
Municipal Finance Consolidation Act Bonds (Irrigation Program) (1)	1988	4,976	6.60-7.75	515	130 (2014)	2,180
Municipal Finance Consolidation Act Bonds (School District Pooled Refunding Program) (3)	1991	6,234	4.75-6.50	285	294 (2005)	866
Conservation Reserve Enhancement Program (CRP Bonds) (2)		<u>8,703</u>	6.00-8.00	<u>1,240</u>	43 (2011)	<u>8,703</u>
Total Bonds Payable		\$ <u>19,913</u>		\$ <u>2,040</u>		\$ <u>11,749</u>
Less Current Portion (FY2002 Principal Payments)						(<u>2,040</u>)
Total Long-Term Bonds Payable						\$ <u>9,709</u>

(1) The Board issued these bonds to provide funds to purchase the Refunding Bonds of participating Irrigation Districts for the purpose of prepaying the U.S. Department of Interior, Bureau of Reclamation Projects Loans. The Irrigation Bonds and the interest thereon are payable solely from the collection of a special tax or assessment which is a lien against real property in the Irrigation District. While the Irrigation Bonds are not obligations of the State of Montana, the bonds are limited obligations of the Board due to an irrevocable pledge to lend money for deposit by the Trustee of the Irrigation

District Pooled Loan Program Reserve Account E in an amount equal to any deficiencies therein on any payment date. The Indenture does not permit the issuance of additional bonds.

(2) The Conservation Reserve Enhancement Program is funded by the Montana Trust Funds Bond Pool.

(3) The Board issued these bonds to provide funds to purchase the general obligation refunding bonds of participating Montana School Districts. The School District Refunding Bonds and the interest thereon are payable from real property taxes levied within the school district. The 1991 Bonds are limited obligations of the Board, and are not a debt or liability of the State of Montana, and neither the faith and credit nor the taxing power of the state is pledged to the payment of principal of or interest on the bonds.

Fiscal year 2004 debt service requirements (principal & interest) are listed below (in thousands):

<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009+</u>	<u>Total</u>
\$2,680	\$2,352	\$1,785	\$1,648	\$1,629	\$1,544	\$11,638

Fiscal year 2003 debt service requirements (principal & interest) are listed below (in thousands):

<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008+</u>	<u>Total</u>
\$2,849	\$2,789	\$2,459	\$1,889	\$1,750	\$3,226	\$14,962

Current Bonds Payable

The Enterprise Fund is authorized to issue INTERCAP bonds under the Municipal Finance Consolidation Act. These bonds may not aggregate more than \$120 million as amended by the 2003 Legislature. Previously, INTERCAP bonds may not aggregate more than \$80 million through June 30, 2011 and then \$75 million thereafter. The INTERCAP bonds provide funds for the Board to make loans to eligible government units. The bonds are not a debt or liability of the State of Montana. The bonds are limited obligations of the Board payable solely from: a) repayments of principal and interest on loans made by the Board to participating eligible Montana governments; b) investment income under the indenture; and c) an irrevocable pledge by the Board. The Board has no taxing power. These bonds may be redeemed, at the bondholder's option, any March 1, prior to maturity. The Board did not enter into an arms-length financing agreement to convert the bonds "put", but not resold into some other form of long-term obligation. Accordingly, these bonds, considered demand bonds, are recorded as current liabilities of the Enterprise Fund. The INTERCAP obligations at June 30, 2003 and June 30, 2002, are listed below (in thousands):

<u>Series</u>	<u>Amount Issued</u>	<u>Interest Range</u>	<u>Maturity</u>	<u>Balance June 30, 2003</u>	<u>Balance June 30, 2002</u>
1992	6,500	Variable	2005	6,075	6,075
1994	7,500	Variable	2009	6,975	7,005
1995	7,500	Variable	2010	7,115	7,150
1997	10,000	Variable	2017	9,740	9,775
1998	12,500	Variable	2018	12,285	12,285
2000	15,000	Variable	2025	15,000	15,000
2003	<u>\$15,000</u>	Variable	2028	<u>15,000</u>	<u>0</u>
Total INTERCAP Debt	<u>\$74,000</u>			<u>72,190</u>	<u>57,290</u>
Current Portion of Long-Term Bonds Payable				<u>2,077</u>	<u>2,040</u>
Total Current Bonds Payable				<u>\$74,267</u>	<u>\$59,330</u>

5. OTHER DEBT

Conduit Debt

In this program, the Board is authorized to issue stand-alone industrial revenue bonds, under the Economic Development Act, as conduit (no commitment) debt. Assets and revenues of the borrower are pledged to repay the bonds. Because the Board has no obligation for this debt, these bond issues are not reflected on the Board's financial statements. Bonds issued by the Board as conduit (no-commitment) debt are listed below (in thousands):

<u>Project</u>	<u>Issue Date</u>	<u>Maturity Date</u>	<u>Amount Issued</u>	<u>Balance June 30, 2003</u>	<u>Balance June 30, 2002</u>
MT Cenex (Farmers Union)	August 1985	09/01/2010	\$ 3,925	\$ 3,925	\$ 3,925
Colstrip	October 1989	12/30/2015	60,800	57,300	59,100
Yellowstone Energy (BGI)	July 1993	12/31/2019	118,345	117,345	117,645
Stillwater Mining	July 2000	07/01/2020	30,000	30,000	30,000
Gainey Foundation	October 2002	09/01/2014	6,000	6,000	0
Total conduit debt			<u>\$ 219,070</u>	<u>\$ 214,570</u>	<u>\$ 210,670</u>

In this program, the Board is authorized to issue Qualified Zone Academy Bonds (QZAB), under the Municipal Finance Consolidation Act, as conduit (no commitment) debt. The revenues, and in some cases the taxing power, of the borrower are pledged to repay the bonds. Because the Board has no obligation for this debt, these bond issues are not reflected on the Board's financial statements. Bonds issued by the Board as conduit (no-commitment) debt are listed below (in thousands):

<u>Project</u>	<u>Issue Date</u>	<u>Maturity Date</u>	<u>Amount Issued</u>	<u>Balance June 30, 2003</u>	<u>Balance June 30, 2002</u>
Huntley Project K-12 Schools	December 2000	07/01/2013	\$ 750	\$ 750	\$ 750
Total conduit debt			<u>\$ 750</u>	<u>\$ 750</u>	<u>\$ 750</u>

6. TRANSFERS OUT

In fiscal year 2003, the Enterprise Fund transferred \$297,266 to the Board of Investment's Investment account.

7. INTERCAP PROGRAM LOAN COMMITMENTS

The Board makes firm commitments to fund loans from the INTERCAP loan program. As of June 30, 2003 and 2002, respectively, the Board committed to make loans to eligible Montana governments totaling \$20,170,082 and \$26,023,707.

8. NET ASSETS

Net Assets represents the accumulated net profits of the Enterprise Fund programs. The Net Assets for fiscal years ended June 30, 2003 and June 30, 2002 include \$192,823 and \$191,520, respectively, in unrealized appreciation/depreciation in reporting the fair value of the Enterprise Fund investments.

MONTANA BOARD OF INVESTMENTS

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November 21, 2003

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LEGISLATIVE AUDIT DIV.

Scott A. Seacat, Legislative Auditor
Legislative Audit Division
Room 135, State Capitol
Helena MT 59620-1705

Dear Scott:

We appreciate the services your office provides to the Board of Investments in reviewing our procedures, internal controls, and accounting practices. The Board invests nearly \$9.0 billion of public funds and during the past fiscal year handled investments for 544 state and local government accounts. Our complex operation utilizes five different accounting systems to accurately track investments in various asset classes.

We take the responsibility of managing the constitutionally-established Unified Investment Program very seriously and depend upon your objective annual review of our operations to detect any problems that we may not observe.

Sincerely yours,


Mr. Carroll South, Executive Director
Montana Board of Investments