
Secretary of State

State of Oregon

OFFICE OF ENERGY

Small Scale Energy Loan Program

For the Years Ended June 30, 1998, and 1997



Audits Division

Secretary of State

State of Oregon

OFFICE OF ENERGY

Small Scale Energy Loan Program

For the Years Ended June 30, 1998, and 1997



Audits Division

OFFICE OF THE
SECRETARY OF STATE
Phil Keisling
Secretary of State
Suzanne Townsend
Deputy Secretary of State



AUDITS DIVISION
John Lattimer
Director

(503) 986-2255
FAX (503) 378-6767

Auditing for a Better Oregon

The Honorable John Kitzhaber, M.D.
Governor of Oregon
State Capitol
Salem, Oregon 97310

John Savage, Administrator
Office of Energy
625 Marion Street NE
Salem, Oregon 97310

This report presents the results of our annual audit on the Office of Energy, Small Scale Energy Loan Program (SELP).

As required by auditing standards, we performed the audit to obtain reasonable assurance about whether the financial statements and accompanying notes have been presented fairly by management. Our Independent Auditor's Report and the financial statements and notes for the years ended June 30, 1998, and 1997, are included in the Financial Section of this report. We concluded that the financial statements are fairly presented in accordance with generally accepted accounting principles.

Auditing standards also require us to review SELP's internal control and compliance with applicable laws and regulations. Our report on the results of those reviews is included in the Audit Results section of this report. We did not note any material weaknesses in internal control or instances of noncompliance.

We appreciate the cooperation and assistance of SELP management and staff during the course of this audit.

OREGON AUDITS DIVISION

John N. Lattimer
Director

Fieldwork Completion Date:
March 12, 1999

-iii-

T A B L E O F C O N T E N T S

	<u>Page</u>
SUMMARY	vii
INTRODUCTION.....	1
ORGANIZATION AND FUNCTIONS	1
FINANCIAL ACTIVITIES	1
AUDIT RESULTS	
REPORT ON INTERNAL CONTROL AND COMPLIANCE.....	5
FOLLOW UP ON PRIOR AUDIT FINDINGS	7
COMMENDATION	8
FINANCIAL SECTION	
INDEPENDENT AUDITOR’S REPORT	11
FINANCIAL STATEMENTS	
Balance Sheets – June 30, 1998, and 1997	EXHIBIT A..... 13
Statement of Revenues, Expenses and Changes in Retained Earnings – For the Years Ended June 30, 1998, and 1997....	EXHIBIT B..... 15
Statements of Cash Flows – For the Years Ended June 30, 1998, and 1997....	EXHIBIT C..... 17
Notes to the Financial Statements	19
SUPPLEMENTARY INFORMATION	
Year 2000 (Y2K) Information and Readiness Disclosure	29
Schedule of Debt Issued and Outstanding As of June 30, 1998.....	SCHEDULE A..... 31

SUMMARY

BACKGROUND

SELP is funded through the sale of general obligation bonds. Bond proceeds are loaned to individuals, businesses, organizations, and local governments in Oregon to finance projects that save otherwise wasted energy or produce renewable energy sources. The bonds are then paid off from the principal and interest payments received from program borrowers and from earnings on invested funds. Besides principal and interest payments, borrowers also pay fees which help fund SELP's operating costs.

AUDIT PURPOSE

The audit was conducted for the purpose of reporting on the financial statements of the Office of Energy, Small Scale Energy Loan Program (SELP) for the years ended June 30, 1998, and 1997, and on SELP's internal control and compliance with applicable laws and regulations.

AUDIT RESULTS

The audit resulted in an unqualified opinion, which is a conclusion that the financial statements taken as a whole are presented fairly.

INTRODUCTION

ORGANIZATION AND FUNCTIONS

In May 1980, the voters approved Article XI-J of the Oregon Constitution, authorizing the sale of general obligation bonds to finance small scale, local energy projects within Oregon. The bond program is administered by the Small Scale Energy Loan Program (SELP) within the Office of Energy which, in turn, is a part of the Department of Consumer and Business Services. SELP is authorized to issue and have outstanding bonds equal to one-half of one percent of the true cash value of all property in the state.

Oregon Revised Statutes chapter 470 provides for a Small Scale Energy Project Advisory Committee to review loan applications and make recommendations to the administrator of the Office of Energy. The seven committee members are appointed by the administrator to serve two-year terms.

The loan program finances energy conservation and renewable resource energy projects to meet local community or regional energy needs in Oregon. Renewable resources include water, wind, geothermal heat, solar radiation, biomass, and waste heat. SELP also funds projects that use alternative fuels, save transportation energy, and make products from recycled material. Program loans are made to individual residents, Oregon businesses, nonprofit organizations, municipal organizations, and state agencies.

FINANCIAL ACTIVITIES

SELP is funded through the sale of general obligation bonds. Bond proceeds are loaned to individuals, businesses, organizations, and local governments in Oregon to finance projects that save otherwise wasted energy or produce renewable energy sources. Loan repayments and fees from borrowers, as well as earnings on invested assets, are deposited in the Small Scale Local Energy Project Administration and Bond Sinking Fund. Those funds are used to make payments of principal and

interest on outstanding bonds, and to pay the administrative costs of operating the program.

During fiscal year 1998, SELP issued \$8.9 million in new bonds. New loans totaling \$1.1 million were approved during the year. At June 30, 1998, total bonds outstanding were \$189.3 million, and net loans receivable were \$160.4 million.

AUDIT RESULTS

OFFICE OF THE
SECRETARY OF STATE
Phil Keisling
Secretary of State
Suzanne Townsend
Deputy Secretary of State



AUDITS DIVISION
John Lattimer
Director

(503) 986-2255
FAX (503) 378-6767

Auditing for a Better Oregon

The Honorable John Kitzhaber, M.D.
Governor of Oregon
State Capitol
Salem, Oregon 97310

John Savage, Administrator
Office of Energy
625 Marion Street NE
Salem, Oregon 97310

**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE AND ON
INTERNAL CONTROL OVER FINANCIAL REPORTING BASED ON AN
AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE
WITH GOVERNMENT AUDITING STANDARDS**

We have audited the financial statements of the Office of Energy, Small Scale Energy Loan Program (SELP) as of and for the years ended June 30, 1998, and 1997, and have issued our report thereon dated March 12, 1999, which was unqualified. We conducted our audit in accordance with generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether SELP's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws and regulations, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered SELP's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of internal control over

financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving internal control over financial reporting and its operation that we consider to be material weaknesses.

This report is intended solely for the information and use of the management of the Office of Energy and of the Small Scale Energy Loan Program, the governor of the state of Oregon, and the Oregon Legislative Assembly, and is not intended to be and should not be used by anyone other than these specified parties.

OREGON AUDITS DIVISION

Sharron E. Walker, CPA, CFE
Deputy Director

March 12, 1999

FOLLOW UP ON PRIOR AUDIT FINDINGS

This section reports follow-up action taken by SELP management on findings included in our prior audit report issued for the period from July 1, 1996, to June 30, 1997. The scope of the prior audit was to express an opinion on SELP's financial statements.

Prior Audit Findings	Disposition
SELP continued to have weaknesses in its internal control to assure transactions and balances were accurately recorded in the proper period, particularly for cash and investment transactions.	SELP has implemented our recommendations. We were able to reconcile investment income from the general ledger balance to the subsidiary records prepared from Treasury records. SELP also has improved its cash reconciliation process so reconciliations are current and errors identified are corrected. Management continues to monitor and review the cash reconciliations. Finally, SELP has documented its internal control in a procedures manual.

COMMENDATION

The courtesies and cooperation extended by management and staff of the Office of Energy during the course of our audit were very commendable and sincerely appreciated.

AUDIT TEAM

Joel Leming, CPA, Audit Administrator

Bob Jordan, CPA

Kay Boeder, CPA, CFE

Stanley Mar

Nelson Okello

FINANCIAL SECTION

OFFICE OF THE
SECRETARY OF STATE
Phil Keisling
Secretary of State
Suzanne Townsend
Deputy Secretary of State



AUDITS DIVISION
John Lattimer
Director

(503) 986-2255
FAX (503) 378-6767

Auditing for a Better Oregon

The Honorable John Kitzhaber, M.D.
Governor of Oregon
State Capitol
Salem, Oregon 97310

John Savage, Administrator
Office of Energy
625 Marion Street NE
Salem, Oregon 97310

INDEPENDENT AUDITOR'S REPORT

We have audited the accompanying financial statements of the Office of Energy, Small Scale Energy Loan Program, as listed in the table of contents, as of and for the years ended June 30, 1998, and 1997. These financial statements are the responsibility of the management of the Office of Energy. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards and *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits 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 audits provide a reasonable basis for our opinion.

As discussed in Note 1, the financial statements present only the transactions and balances attributable to the activities of the Small Scale Energy Loan Program, and are not intended to present fairly the financial position of the Office of Energy, and the results of its operations and cash flows of its governmental fund types, fiduciary fund types, and accounting groups in conformity with generally accepted accounting principles.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Office of Energy, Small Scale Energy Loan Program, as of June 30, 1998, and 1997, and the results of its operations and cash flows for the years then ended in conformity with generally accepted accounting principles.

Our audits were performed for the purpose of forming an opinion on the financial statements taken as a whole. The Schedule of Debt Issued and Outstanding as of June 30, 1998, on page 31 is presented for purposes of additional analysis and is not a required part of the financial statements. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the financial statements taken as a whole.

The Year 2000 supplementary information on page 29 is not a required part of the financial statements but is supplementary information required by the Governmental Accounting Standards Board. We did not audit this information and do not express an opinion on it. In addition, we do not provide assurance that the department is or will become Year 2000 compliant, that the department's Year 2000 remediation efforts will be successful in whole or in part, or that parties with which the department does business will become Year 2000 compliant.

In accordance with *Government Auditing Standards*, we have also issued our report dated March 12, 1999, on our consideration of the Office of Energy, Small Scale Energy Loan Program's internal control over financial reporting and its compliance with certain laws and regulations. That report is separately presented in the Audit Results section of this report.

OREGON AUDITS DIVISION

Sharron E. Walker, CPA, CFE
Deputy Director

March 12, 1999

State of Oregon
OFFICE OF ENERGY
SMALL SCALE ENERGY LOAN PROGRAM
BALANCE SHEETS
ENTERPRISE FUND
 JUNE 30, 1998, AND JUNE 30, 1997

ASSETS

	<u>1998</u>	<u>1997</u>
Cash and cash equivalents	\$ 41,015,974	\$ 31,135,483
Cash equivalents securities lending collateral	0	1,685,691
Investments (net)	6,412,032	6,863,372
Investment interest receivable	254,205	231,934
Unbilled arbitrage receivable	363,435	363,090
Loan interest receivable	1,506,791	1,602,751
Loan receivable (net)	160,380,953	169,930,749
Deferred bond issuance expense	68,326	0
Total Assets	<u>\$ 210,001,716</u>	<u>\$ 211,813,070</u>

LIABILITIES AND FUND EQUITY

Liabilities:		
Accounts payable	\$ 3,303	\$ 712
Matured bonds payable	600,400	838,325
Obligations under securities lending	0	1,685,691
Bond interest payable	5,861,702	6,107,354
Employee vacation payable	32,695	30,852
Arbitrage liability	442,181	496,458
Deferred income	125,050	162,051
Borrowers' reserve funds	3,887,060	3,621,616
Bonds payable	189,328,162	192,665,322
Total Liabilities	<u>200,280,553</u>	<u>205,608,381</u>
<u>Fund Equity:</u>		
Retained earnings	9,721,163	6,204,689
Total Liabilities and Fund Equity	<u>\$ 210,001,716</u>	<u>\$ 211,813,070</u>

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

State of Oregon
OFFICE OF ENERGY
SMALL SCALE ENERGY LOAN PROGRAM
STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN RETAINED EARNINGS
ENTERPRISE FUND
FOR THE FISCAL YEARS ENDED JUNE 30, 1998, AND JUNE 30, 1997

	<u>1998</u>	<u>1997</u>
Operating revenue:		
Interest on loans	\$ 14,733,653	\$ 12,985,942
Interest on investments	1,861,963	1,906,228
Application and commitment fees	6,716	76,711
Loan fees	8,352	18,719
Miscellaneous	110,942	566,050
Total operating revenue	<u>16,721,626</u>	<u>15,553,650</u>
Operating expense:		
Bond interest and debt service expense	12,009,625	13,036,805
Personal services	553,243	549,654
Services and supplies	508,658	439,944
Bad debt expense	133,626	10,187
Total operating expense	<u>13,205,152</u>	<u>14,036,590</u>
Net income	3,516,474	1,517,060
Retained earnings – beginning	6,204,689	4,616,607
Effect of GASB 31 to value securities at market value	0	71,022
Retained earnings – ending	<u>\$ 9,721,163</u>	<u>\$ 6,204,689</u>

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

State of Oregon
OFFICE OF ENERGY
SMALL SCALE ENERGY LOAN PROGRAM
STATEMENTS OF CASH FLOWS
ENTERPRISE FUND
FOR THE FISCAL YEARS ENDED JUNE 30, 1998, AND JUNE 30, 1997

	<u>1998</u>	<u>1997</u>
Operating income	\$ 3,516,474	\$ 1,517,060
Adjustments to reconcile operating income to cash provided by operating activities:		
Expenses not requiring outlay of cash:		
Bad debt	133,626	10,187
Arbitrage liability	(24,775)	428,100
Bond expenses	104,471	231,697
Interest received on investment reported as operating income	(1,861,963)	(1,906,228)
Bond interest and amortization reported as operating income	12,034,400	12,608,705
(Increase)/decrease in investment interest receivable	(22,271)	0
(Increase)/decrease in loan interest receivable	95,960	1,046,376
(Increase)/decrease in loan receivable	9,549,796	7,265,647
(Increase)/decrease in unbilled receivable	(345)	(365,828)
(Increase)/decrease in deferred charges	(68,326)	0
Increase/(decrease) in accounts payable	2,591	(40,029)
Increase/(decrease) in bond interest payable	(245,652)	(427,974)
Increase/(decrease) in obligation under securities lending	(1,685,692)	1,685,691
Increase/(decrease) in arbitrage payable	(54,277)	428,100
Increase/(decrease) in matured bonds payable	(237,925)	297,175
Increase/(decrease) in employee vacation payable	1,843	141
Increase/(decrease) in borrowers' reserve funds	281,592	1,247,145
Change in borrowers' reserve from market value change	(16,148)	279,270
Increase/(decrease) in deferred income	(37,000)	(37,000)
	<u>17,949,905</u>	<u>22,751,175</u>
Net cash provided (used) by operations	\$ 21,466,379	\$ 24,268,235

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

EXHIBIT C (CONTINUED)

State of Oregon
OFFICE OF ENERGY
SMALL SCALE ENERGY LOAN PROGRAM
STATEMENTS OF CASH FLOWS (continued)
ENTERPRISE FUND
FOR THE FISCAL YEARS ENDED JUNE 30, 1998, AND JUNE 30, 1997

	<u>1998</u>	<u>1997</u>
Net cash provided (used) by operations	\$ 21,466,379	\$ 24,268,235
Cash flows from non-capital financing activities:		
Proceeds from bond sales	8,930,000	0
Principal payments on bonds	(12,440,000)	(14,160,000)
Interest payments on bonds	(12,081,677)	(12,805,006)
Net cash provided by non-capital financing activities	<u>(15,591,677)</u>	<u>(26,965,006)</u>
Cash flows from investing activities:		
Proceeds from sale and maturities of investments	496,554	13,150,096
Market value change in securities carrying value	(16,148)	(279,270)
Interest received on investments	1,839,692	1,893,439
Net cash provided by investing activities	<u>2,320,098</u>	<u>14,764,265</u>
Net increase/(decrease) in cash and cash equivalents	8,194,800	12,067,494
Cash and cash equivalents at beginning of period	32,821,174	20,753,680
Cash and cash equivalents at end of period	<u>\$ 41,015,974</u>	<u>\$ 32,821,174</u>
Cash and cash equivalents in State Treasury	\$41,015,974	31,135,483
Cash equivalents securities lending collateral	0	1,685,691
Total	<u>\$ 41,015,974</u>	<u>\$ 32,821,174</u>

State of Oregon
OFFICE of ENERGY
SMALL SCALE ENERGY LOAN PROGRAM
Notes to the Financial Statements
Enterprise Fund
June 30, 1998, and June 30, 1997

(1)

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization

The Small Scale Energy Loan Program (SELP) was created through the adoption of Article XI-J of the Oregon Constitution in May 1980. SELP is a part of the state of Oregon and its Office of Energy. Effective July 1, 1995, the Department of Energy became the Office of Energy in the Department of Consumer and Business Services.

Basis of Presentation

The accompanying financial statements have been prepared in conformity with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB), the Financial Accounting Standards Board (FASB), and the American Institute of Certified Public Accountants (AICPA).

The accounts of the Office of Energy are organized on the basis of funds and account groups, each of which is considered a separate accounting entity with a self-balancing set of accounts. The state accounts for SELP as an enterprise fund. Enterprise funds are used for operations that are financed and operated in a manner similar to private business enterprises, where the costs of providing goods and services to the general public on a continuing basis are intended to be financed or recovered primarily through user charges.

Under the auspices of GASB Statement No. 20, SELP does not apply FASB pronouncements issued after November 30, 1989, for proprietary activities, unless GASB amends its pronouncements to specifically adopt FASB pronouncements issued after that date.

Basis of Accounting

Enterprise funds use the flow of economic resources measurement focus and financial statements are presented on the accrual basis. Under the accrual basis of accounting, revenues are recognized when they are earned and expenses are recognized when the liabilities are incurred. All assets and liabilities associated with the operations of these funds are included on the balance sheet. Fund equity (i.e. net total assets) is shown as retained earnings.

SELP accounting policies conform to the Oregon Accounting Manual and generally accepted accounting principles as applicable to state governments. SELP general ledger transactions are recorded on a cash basis. These cash basis transactions have been converted to the accrual basis for financial reporting.

Notes to the Financial Statements (continued)
June 30, 1998, and June 30, 1997

Budgets

The Office of Energy's budget is approved by the Legislature biennially. The Emergency Board of the Legislature approves any increase in the budget that may be necessary during the interim. Limitations are financed from revenues of self-supporting activities and lapse at the end of the biennium. Any Legislative limitation established for SELP applies only to administrative costs that are separated in the approved budget.

Cash, Cash Equivalents and Investments

Cash and cash equivalents are defined as cash held in the State Treasury and cash on deposit outside the State Treasury. All SELP moneys are held in the Oregon Short Term Fund (OSTF) and are considered cash equivalents, which is a cash and investment pool having characteristics of a demand deposit account. The State Treasurer participates in securities lending with a portion of the OSTF. The Office's share of the cash collateral received from broker-dealers is not material at June 30, 1998. The State Treasurer made no allocation of collateral to the Office at June 30, 1998

Investments are stated at market value consistent with Governmental Accounting Standards Statement Number 31. In implementing this pronouncement, the Office has restated assets, liabilities and income for 1997. Investments at June 30, 1997, were increased by \$399,662. Borrowers' reserve liability was increased \$279,270 and investment income was increased \$49,370. The change in investment value that is related to market value increases prior to July 1, 1996 of \$71,022 is shown as a prior period adjustment to retained earnings at June 30, 1997.

Properties acquired through foreclosure proceeding or by acceptance of deeds in lieu of foreclosure are included in investments and are recorded at the lower of cost or fair market value. Cost is defined as the outstanding principal balance of the mortgage loan or contract on the date of foreclosure. Professional appraisers estimated fair market value. The lower of cost or fair market value is then adjusted for estimated selling expenses to arrive at the new realizable value.

Interest Receivable

Interest receivable on investments and loans is recorded at its expected recoverable amount; therefore, no allowance for doubtful accounts is recorded for accrued interest receivable.

Loans Receivable

Receivables are shown net of uncollectible accounts. The allowances for uncollectible accounts at June 30, 1998 and 1997, were \$1,907,548 and \$1,773,922, respectively.

Fixed Assets and Depreciation

Fixed assets are stated at historical cost or estimated historical cost if the original cost is not determinable. Fixed assets costing less than \$5,000 or having a useful life of less than two years are not capitalized. SELP has no capitalized assets.

Compensated Absences

Employees accrue vacation leave at various accrual rates and may generally be paid for up to a maximum of 250 hours of accrued vacation leave at termination. Accumulated

Notes to the Financial Statements (continued)
June 30, 1998, and June 30, 1997

vacation leave is recorded as an expense and a liability of those funds as the benefits accrue to the employees. No liability is recorded for nonvesting, accumulated sick pay benefits.

Bond Expenses

Bond issuance costs are capitalized and written off over the term of the bonds. Bond premiums and discounts associated with a particular bond issue are deferred and amortized over the term of the bond issue, using the bonds outstanding method of amortization.

(2)

CASH AND INVESTMENTS

SELP funds are held by the State Treasurer. The State Treasurer is the investment officer for funds on deposit in the State Treasury. The State's investment policies are governed by statute, and are overseen by the Oregon Investment Council. The State Treasurer may invest in any instrument which persons of prudence, discretion, and intelligence would invest in for their own account. State moneys may be deposited in any trust company, savings and loan association, or bank or mutual savings bank or branch office in that capacity within the State. The state is authorized to use demand deposits and certificates of deposit. At June 30, 1998 and 1997, SELP funds were invested primarily in US government securities.

Cash and investments are legally required to be segregated into the Loan Fund and the Sinking Fund. Cash and investments at June 30, 1998, and 1997, respectively consisted of:

	<u>June 30, 1998</u>		<u>June 30, 1997</u>	
	<u>Cash</u>	<u>Investments</u>	<u>Cash</u>	<u>Investments</u>
Loan Fund	\$ 5,199,313	\$ 0	\$ 4,654,776	\$ 0
Sinking Fund				
Program Account	11,711,304	3,554,839	7,879,518	3,879,495
Bond Reserve	2,991,000	0	2,991,000	0
Principal & Interest	16,872,313	0	11,522,348	0
Extraordinary Expense	2,336,777	0	2,336,777	0
Deferred Revenue		0	0	0
Borrowers' Accounts	1,304,867	2,582,193	912,739	2,708,877
Fiscal Agent Cash	600,400	0	838,325	0
Assets held by agency	0	275,000	0	275,000
TOTAL	<u>\$ 41,015,974</u>	<u>\$ 6,412,032</u>	<u>\$31,135,483</u>	<u>\$ 6,863,372</u>

Cash Deposits

At June 30, 1998, the book balance of cash and cash equivalents was \$41,015,974. The bank balance was \$41,038,705, of which \$40,438,305 was held in demand accounts with the State Treasurer and invested in the Oregon Short Term Fund (OSTF) and \$600,400 was held by the State's fiscal agent. State Treasurer demand deposit accounts and time certificates of deposit investments of the OSTF are held in state banks and insured or collateralized in excess of FDIC coverage for a minimum of 25 percent in accordance with state statute.

Notes to the Financial Statements (continued)
June 30, 1998, and June 30, 1997

At June 30, 1997, the book balance of cash and cash equivalents was \$32,821,174 less the \$1,685,691 of cash equivalent securities under securities lending agreements for a net book balance of \$31,135,483. The bank balance was \$32,839,981, of which \$32,001,656 was held in demand accounts with the State Treasurer and invested in the Oregon Short Term Fund (OSTF) and \$838,325 was held by the State's fiscal agent.

Securities in the OSTF are held by the State Treasurer's agent in the name of the state of Oregon. They consist of 39 percent in U.S. government securities; 41 percent in short-term commercial paper; and the remainder in time certificates of deposit, bankers acceptances, and re-purchase agreements. Earnings on the OSTF are allocated on a pro-rata basis of daily account balances.

On June 30, 1998, the State's fiscal agent (Bank of New York) was holding SELP funds totaling \$600,400 for redemption of bonds and coupons which had matured but had not yet been redeemed. On June 30, 1997, the state's agent (Mellon Bank) was holding SELP funds totaling \$838,325 for redemption of bonds and coupons which had matured but had not yet been redeemed. This amount is included in SELP's cash. These funds are not collateralized, but are insured by the FDIC up to \$100,000 per bondholder. If a bondholder has other accounts with Mellon Bank, the combined account balances are insured up to \$100,000.

Investments

SELP's investments are categorized below to give an indication of the level of risk assumed by SELP at year-end. Category 1 includes investments that are insured or registered, with securities held by SELP or its agent in SELP's name. Category 2 includes uninsured and unregistered investments, with securities held by the counterpart's trust department or agent in SELP's name. Category 3 includes uninsured and unregistered investments, with the securities held by the counterpart or by its trust department or agent but not in SELP's name.

As of June 30, 1998, the investment portfolio consisted of:

	<u>Risk Category</u>			<u>Carrying Amount</u>	<u>Fair Value</u>
	<u>1</u>	<u>2</u>	<u>3</u>		
Investments:					
US Government	\$6,137,032			\$6,137,032	\$ 6,137,032
Preferred Stock	275,000			275,000	275,000
Total Investments	<u>\$6,412,032</u>			<u>\$6,412,032</u>	<u>\$ 6,412,032</u>

SELP holds 2,750 shares of TreeSource, Inc. preferred stock subject to the following rights: \$100 per share liquidation preference; limited voting rights; cumulative dividends payable quarterly in advance at the prime rate, with a minimum rate of 6% and a maximum rate of 9%; convertible into TreeSource, Inc. common stock at \$7.50 per share after April 30, 1999; and redeemable at the original issue price plus any accrued dividends at the option of the Board of Directors, in the form of cash or in exchange for senior unsecured debt with 12% coupon. The holders of the Series A preferred stock will be granted voting

Notes to the Financial Statements (continued)
June 30, 1998, and June 30, 1997

control of the TreeSource, Inc. Board of Directors in the event the Company misses three consecutive quarterly dividend payments, four quarterly dividend payments within twenty-four months or a total of eight quarterly dividend payments. There are no arrearages in the quarterly dividends. This stock was received by court order as part of the settlement in a Chapter 11 bankruptcy reorganization.

Securities Lending Program

In accordance with state investment policies, state agencies may participate in securities lending and the state has, through Securities Lending Authorization Agreements, authorized its custodians to lend the State's securities pursuant to a form of loan agreement. There have been no significant violations of the provisions of securities lending agreements during the period of these financial statements.

During the year, the state's custodians lent short-term and fixed income securities and received as collateral US dollar cash, US government and agency securities, or letters of credit. Borrowers were required to deliver collateral for each loan equal to not less than 102% of the market value of the loaned security. The custodians did not have the ability to pledge or sell collateral securities absent a borrower default, and the state did not impose any restrictions during the fiscal year on the amount of the loans the custodians made on its behalf. The state, through its securities lending agreements, is fully indemnified against borrower default. There were no losses during the year from the failure of borrowers to return loaned securities and no recoveries of amounts from prior losses.

The maturities of investments made with cash collateral during the year generally did not match the maturities of their securities loans. On June 30, 1998, the state had no credit risk exposure to borrowers. On June 30, 1998, SELP had no securities on loan.

SELP's cash balances are invested in the OSTF, as is the cash of other state agencies. As of June 30, 1998, the market value of the collateral held and the value of the securities on loan, including accrued income, from the OSTF was \$460,796,000 and \$452,054,000, respectively. There was no allocation to SELP of securities on loan from the OSTF at June 30, 1998.

As of June 30, 1997, the market value of the collateral held and the value of the securities on loan, including accrued income, from the OSTF was \$272,531,250 and \$266,331,457, respectively. SELP's allocated portion of the securities on loan from the OSTF at June 30, 1997, was \$1,685,691.

Notes to the Financial Statements (continued)
June 30, 1998, and June 30, 1997

(3)

LOANS RECEIVABLE

The loan and contract receivable portfolio includes state agency loans. All mortgaged property is located within the state. The loan portfolio value and associated statewide concentration of credit risk is:

	<u>June 30, 1998</u>	<u>June 30, 1997</u>
Loans and contracts	\$ 162,288,501	\$171,704,671
State agency loans	<u>18,907,860</u>	<u>19,246,563</u>
Credit risk exposure	<u>\$ 143,380,641</u>	<u>\$152,458,108</u>

SELP uses the allowance method to estimate uncollectible mortgage loans and contracts receivable. The allowance for all new loans and contracts is based primarily upon the percent of new loans. The allowance is periodically adjusted by management to accommodate changes in economic conditions, non-performing assets, historical loss experience, and other conditions which may affect the ultimate collectibility of the mortgage loans and contracts. In 1998, SELP management determined that the balance of the allowance account was sufficient to cover projected losses for the loan and contract portfolio.

(4)

BONDS PAYABLE AND DEBT SERVICE

The table below provides a summary of general obligation bond transactions of SELP for the fiscal years ended June 30, 1998, and June 30, 1997:

	<u>June 30, 1998</u>	<u>June 30, 1997</u>
Bonds payable – beginning	\$ 194,380,000	\$ 208,540,000
Bonds issued	8,930,000	0
Bonds retired	<u>(12,440,000)</u>	<u>(14,160,000)</u>
Bonds payable - ending	190,870,000	194,380,000
Discount on bonds payable	<u>(1,541,838)</u>	<u>(1,714,678)</u>
Net bonds payable	<u>\$ 189,328,162</u>	<u>\$ 192,665,322</u>

Notes to the Financial Statements (continued)
June 30, 1998, and June 30, 1997

Following is a schedule of future debt service requirements to maturity as of June 30, 1998.

Date	Principal	Interest	Total Debt Service
1999	\$ 18,390,000	\$ 11,493,888	\$ 29,883,888
2000	13,230,000	10,721,404	23,951,404
2001	13,720,000	10,001,024	23,721,024
2002	13,885,000	9,232,550	23,117,550
2003	12,790,000	8,438,444	21,228,444
Thereafter	<u>118,855,000</u>	<u>49,132,237</u>	<u>167,987,237</u>
TOTAL	<u>\$ 190,870,000</u>	<u>\$ 99,019,547</u>	<u>\$ 289,889,547</u>

No bonds were called prior to stated maturity during the fiscal years ended June 30, 1998, and 1997.

(5)

DEFINED BENEFIT RETIREMENT PLAN

SELP employees participate in the Oregon Public Employee's Retirement System (PERS), a cost-sharing multiple employer benefit plan. All SELP employees are eligible to participate in the system after completing six months of service. PERS is administered by the Public Employees Retirement Board under the guidelines of the Oregon Revised Statutes, chapter 238. The PERS retirement allowance, payable monthly for life, may be selected from twelve retirement benefit options. Options include survivorship benefits and lump sum refunds. The basic benefit formula is 1.67 percent of a member's final average salary multiplied by the member's number of years of service. Benefits also may be calculated under either a money match or an annuity-plus-pension computation if a greater benefit results. PERS also provides death and disability benefits. A copy of the Oregon Public Employees Retirement System annual financial report may be obtained from PERS, P. O. Box 73, Portland, Oregon 97207-0073.

Covered employees are required by state statute to contribute 6.0 percent of their salary to the plan. Current law permits employers to pay employee contributions to the Retirement Fund. SELP is required by statute to contribute actuarially computed amounts as determined by PERS. Rates are subject to change as a result of subsequent actuarial valuations. Currently, the rate is 8.46 percent of each covered employee's salary. The amounts contributed by SELP for the years ending June 30, 1998, 1997, and 1996, were \$59,140, \$62,484 and \$66,108, respectively, equal to the required contributions for each year. No pension liability existed at June 30, 1998, determined in accordance with Statement No. 27 of the Governmental Accounting Standards Board.

(6)

UNEMPLOYMENT BENEFITS

State agencies are subject to the Department of Employment Act. State employees who qualify are entitled to benefit payments during periods of unemployment. Each state agency is required to reimburse the Oregon Employment Department for benefit payments made to former employees. There is no practical method of estimating the amount of future benefit payments which may be made to former employees for wage credits earned prior to June 30. Consequently, this potential obligation is not included in the accompanying financial statements. There were no charges to SELP for the fiscal year ended June 30, 1998.

(7)

LITIGATION

During the ordinary course of business, SELP becomes involved in litigation regarding its lending activities. The program is represented in these actions by the Attorney General of the State of Oregon. As of June 30, 1998, SELP was not currently a party to litigation which would materially affect the financial position of the program.

(8)

SUBSEQUENT EVENTS

SELP called bonds on July 1, 1998 totaling \$5,905,000.

On October 14, 1998, the program issued \$31,555,000 in bonds. On January 1, 1999, SELP called \$25,380,000 of bonds that included 1985 Series D, 1991 Series B, 1991 Series C, 1991 Series D, 1992 Series D and 1992 Series E.

In February 1999 SELP entered into a contract to sell \$25,995,000 of bonds for delivery on October 5, 1999. The money from the 1999 Series A bonds will be used to call the 1987 Series A and 1987 Series B bonds on January 1, 2000.

On March 16, 1999, SELP intends to sell \$20,055,000 of bonds.

SUPPLEMENTARY INFORMATION

State of Oregon
OFFICE OF ENERGY
Small Scale Energy Loan Program
Supplementary Information
June 30, 1998

(UNAUDITED)

Year 2000 (Y2K) Information and Readiness Disclosure

The following disclosure is required by the Governmental Accounting Standards Board and is provided under the provisions of the Year 2000 Information and Readiness Disclosure Act, Public Law 105-271.

The year 2000 issue is a result of shortcomings in many electronic data systems and other electronic equipment that may adversely affect SELP's operations as early as fiscal year 1999.

The Government Accounting Standards Board has identified the following stages as necessary to implement a Year 2000-compliant system:

Stages	Description
Awareness	Establish a budget and project plan for dealing with the Y2K issue.
Assessment	Identify the systems and components for which Y2K compliance work is needed.
Remediation	Make changes to systems and equipment.
Validation & Testing	Validate and test the changes that were made during the Remediation Stage.

SELP has completed the Awareness and Assessment Stages described in the table above. SELP has also completed the Remediation and Validation and Testing Stages for systems critical to its operations, such as the Loan Servicing and Accounting System and the Cash Flow Forecasting Model.

Because of the unprecedented nature of the year 2000 issue, its effect and the success of related remediation efforts will not be fully determinable until the year 2000 and thereafter. The Office cannot assure that it is or will be year 2000 ready, that SELP's remediation efforts will be completely successful, or that parties with whom SELP does business will be year 2000 ready.

State of Oregon
OFFICE OF ENERGY
SMALL SCALE ENERGY LOAN PROGRAM
SCHEDULE OF DEBT ISSUED AND OUTSTANDING
 ENTERPRISE FUND
 JUNE 30, 1998

<u>Bond Series</u>	<u>Dated Date</u>	<u>Final Maturity</u>	<u>Amount Issued</u>	<u>Amount Outstanding</u>
1981 A	Jul-81	Jan-03	\$ 19,700,000	\$ -0-
1982 A	Oct-82	Jan-03	2,340,000	-0-
1983 A	Jul-83	Jan-06	18,495,000	-0-
1984 A	Apr-84	Jul-07	18,000,000	-0-
1984 B	Jul-84	Jul-06	10,300,000	-0-
1984 C	Nov-84	Jul-06	8,750,000	-0-
1985 A	Oct-85	Jul-96	6,900,000	-0-
1985 B	Oct-85	Jan-04	7,000,000	-0-
1985 C	Dec-85	Jul-05	10,500,000	-0-
1985 D	Dec-85	Jan-08	5,840,000	4,230,000
1986 A	Jul-86	Jan-06	8,000,000	-0-
1987 A	Jun-87	Jan-17	16,500,000	14,835,000
1987 B	Oct-87	Jul-15	14,850,000	12,650,000
1987 C	Oct-87	Jan-99	5,100,000	-0-
1987 D	Dec-87	Jan-99	3,850,000	-0-
1988 A	May-88	Jul-04	6,000,000	-0-
1988 B	May-88	Jul-04	1,000,000	-0-
1988 C	May-88	Jul-98	1,000,000	-0-
1989 A	Feb-89	Jul-05	5,000,000	-0-
1989 B	Feb-89	Jan-15	5,700,000	-0-
1989 C	Feb-89	Jul-99	1,000,000	-0-
1990 A	Jan-90	Jan-06	3,000,000	-0-
1990 B	Jan-90	Jul-11	3,150,000	2,390,000
1990 C	Jan-90	Jul-00	1,000,000	-0-
1990 D	Oct-90	Jul-05	4,000,000	-0-
1990 E	Oct-90	Jan-07	15,430,000	5,905,000
1990 F	Oct-90	Jul-00	1,000,000	-0-
1991 A	Dec-91	Jan-08	4,800,000	3,680,000
1991 B	Dec-91	Jan-17	3,225,000	2,655,000
1991 C	Dec-91	Jul-07	1,025,000	790,000
1991 D	Dec-91	Jul-02	500,000	300,000
1992 A	Apr-92	Jul-05	11,475,000	8,415,000
1992 B	Apr-92	Jan-03	1,755,000	930,000
1992 C	Sep-92	Jan-08	4,700,000	3,030,000
1992 D	Sep-92	Jan-22	16,300,000	15,610,000
1992 E	Sep-92	Jan-08	5,280,000	3,420,000
1992 F	Sep-92	Jan-06	16,710,000	11,715,000
1993 A	Jun-93	Jan-13	25,165,000	20,230,000
1993 B	Jun-93	Jul-13	16,305,000	14,535,000
1994 A	May-94	Jul-09	2,000,000	1,700,000
1994 B	May-94	Jul-07	19,325,000	15,175,000
1994 C	May-94	Jul-15	4,015,000	3,650,000
1994 D	May-94	Jul-15	14,960,000	14,325,000
1994 E	Oct-94	Jul-11	15,000,000	14,315,000
1994 F	Oct-94	Jul-11	7,010,000	6,525,000
1994 G	Oct-94	Jul-06	1,000,000	930,000
1998 A	Mar-98	Jan-14	3,000,000	3,000,000
1998 B	Mar-98	Jan-02	5,930,000	5,930,000
			\$ 382,885,000	\$ 190,870,000

FACTS ABOUT THE SECRETARY OF STATE AUDITS DIVISION

The mission of the Audits Division is to “Protect the Public Interest and Improve Oregon Government.” The Oregon Constitution provides that the Secretary of State shall be, by virtue of his office, Auditor of Public Accounts. The Audits Division exists to carry out this duty. The division reports to the elected Secretary of State and is independent of the Executive, Legislative, and Judicial branches of Oregon government. The division audits all state officers, agencies, boards, and commissions and oversees audits and financial reporting for local governments.

DIRECTORY OF KEY OFFICIALS

Director

Deputy Director

Deputy Director

John N. Lattimer

Sharron E. Walker, CPA, CFE

Catherine E. Pollino, CGFM



This report, which is a public record, is intended to promote the best possible management of public resources.

If you received a copy of an audit and no longer need it, you may return it to the Audits Division. We maintain an inventory of past audit reports. Your cooperation will help us save on printing costs.

Oregon Audits Division
Public Service Building
Salem, Oregon 97310

503-986-2255

We invite comments on our reports through our Hotline or Internet address.

Hotline: 800-336-8218

Internet: Audits.Hotline@state.or.us

<http://www.sos.state.or.us/audits/auditthp.htm>

Auditing to Protect the Public Interest and Improve Oregon Government