# Oregon Department of Veterans' Affairs

**Annual Financial Report**
**Enterprise Funds**
**For The Fiscal Year Ended June 30, 2002**

*An Agency of the State Of Oregon*

***Serving Those Who Served***

# Annual Financial Report

## Enterprise Funds of the
## Oregon Department of Veterans' Affairs

*An Agency of the State of Oregon*

## For The Fiscal Year Ended June 30, 2002


**Jon Mangis**
Director

**Bruce Shriver, CPA**
Chief Financial Officer

**Report Prepared By**

John McIntyre, CPA
Ron Weisser, CPA
Lynette Horton
With the assistance of the
Financial Administration Division



Cover Photo:
Reveille at the Oregon State Fair grounds on the first day of the fair in 1949. Personnel from various military branches are represented. Photo courtesy of the Oregon State Archives and the Salem Public Library digital photography collection.
Photo source was the Oregon State Fair and Exposition Center, OFE0016.

**This page intentionally left blank**

# TABLE OF CONTENTS

**This page intentionally left blank**

### *A Salute to Oregon's Veterans and the United States Armed Forces*
### *Oregon State Fair, August 29, 2002*

*Veterans marched at the fairgrounds. From left: David Chambers, Lieutenant (USN Ret.), Chris Henry, 2nd Lieutenant (USMC), and Jerry Ovard, Technical Sergeant (USAF Ret.). David and Jerry are employees of the Department. At the time of the photo, Chris was a USDVA work-study student who assisted veterans at the Department.*

*Department Director Jon Mangis addressed the audience.*


*Employees answered questions at the Department's booth. Shown are Dalana Alyea, Sue Shaffer, and Chris Miller (at far right).*

We, the employees of the Oregon Department of Veterans' Affairs, are advocates for veterans, their dependents and survivors. We are dedicated to providing quality programs and services to meet their current and future needs.

## *OVERVIEW OF THE DEPARTMENT*

For over 50 years, the Oregon Department of Veterans' Affairs has provided quality service to veterans, their dependents and survivors. The Department has provided this assistance in a variety of ways to those who have given of themselves in the service of their country.

Services offered by the Department have included veterans' loans, benefits assistance, educational aid, and conservatorship. When the passage of time and external events changed the composition and needs of the veterans population, the Department responded to these changing needs by implementing changes in the structure of programs and by developing new programs and services.

Over the years, many changes have taken place within the Department. However, the commitment of the Department and its employees to providing the highest level of services to Oregon's veterans, dependents and survivors within the Department's available resources has remained constant.

***Department employees who served in the United States Armed Forces***
*Seated (from left): Dave Chambers, Aleta Harrison, Bob Ferder, Val Conley, Ed Gabriel, Arlene Baker, Herb Riley, and Robert Fleming. Standing: Thomas Weiss, John D'Angelo, Ron Weisser, Chris Miller, Jerry Ovard, Doug Dusenbery, Brad Killip, Bill French, Ed Van Dyke, Art Mauer, Matthew Trom, Patrick Callahan, Robert Curphey, Doug Yerke, Bill Kankkonen, Floyd Mecham, George Kudszus, Curt Schnepp, Paula Brown, Tom Cowan, and Jon Mangis.*

*Not pictured: David Fletcher, Gene Hancock, Denise Holtrop, John Hutchinson, Ron Jarchow, Ted Johnson, Ron Kincaid, Brent Koester, and Deborah Pruitt.*

Oregon

Theodore R. Kulongoski, Governor

**Oregon Department of Veterans' Affairs**
Oregon Veterans' Building
700 Summer Street NE
Salem, OR 97301-1285

SERVING
OREGON VETERANS
SINCE 1945

January 13, 2003

The Honorable Ted Kulongoski
Governor of the State of Oregon
State Capitol
Salem, Oregon 97301-4047

Citizens of Oregon

We are pleased to provide you with the Annual Financial Report of the Oregon Department of Veterans' Affairs *(the "Department")* Enterprise funds, for the fiscal year ended June 30, 2002. We believe the information presented herein is accurate in all material respects, that it is presented in a manner which fairly sets forth the financial position and results of operations of the Department's Enterprise funds, and that all disclosures necessary to enable the reader to gain an understanding of the Department's Enterprise funds' financial affairs have been included. The Department's Governmental and Fiduciary funds' financial statements are presented in the **Other Supplemental Section** for the purpose of additional analysis. The Department is responsible for both the accuracy of the data presented and the completeness and fairness of the presentation including all disclosures.

This report is organized and presented in three sections. The **Introductory Section** includes this transmittal letter and an organizational chart. The **Financial Section** includes the financial statements and accompanying notes, as well as the independent auditor's report on the financial statements. The **Other Supplemental Section** includes selected financial and programmatic information, much of which is presented on a multi-year basis.

The Department is an agency of the State of Oregon and is identified as the reporting entity of this Annual Financial Report. The Department provides a range of services for veterans such as mortgage and home improvement loans, a skilled care nursing facility, benefits and claims counseling, and other veterans' services.

This report has been prepared in accordance with generally accepted accounting principles as promulgated by the Governmental Accounting Standards Board, the Financial Accounting Standards Board, the American Institute of Certified Public Accountants, and other recognized standard-setting bodies. A summary of significant accounting policies of the Department is found in Note 1 of the financial statements.

## OREGON ECONOMY

***Recent Trends –*** The second quarter initial estimate of job growth was a slightly negative 0.5 percent at an annual rate. This follows the weak positive growth of 0.4 percent in the first quarter. The Oregon economy appears to be bottoming out of this recession. On a year-over-year *(Y/Y)* basis, jobs declined by 1.4 percent in the second quarter. The Y/Y growth has steadily improved since the fourth quarter of 2001, when jobs declined by 2.2 percent.

Manufacturing jobs grew at a positive 2.0 percent rate during the second quarter. This is the first positive growth rate since the second quarter of 2000. Non-manufacturing was still weak, falling by 0.9 percent. Within manufacturing, high tech jobs posted losses, continuing a slide that commenced in the first quarter of 2001. Lumber and wood products jobs posted gains along with a big surge in the transportation equipment sector. Among non-manufacturing sectors, construction, communications and utilities were down with large job losses. Non-health services also lost jobs. Job gains were recorded for both wholesale and retail trades as well as for transportation services. Health services and finance, insurance and real estate were essentially flat for the second quarter. Within the government sector, federal and state governments showed modest employment increases while local government had a slight decline in jobs.

The most recent Blue Chip Job Growth rankings place Oregon 40$^{th}$ in the nation. For Y/Y job growth, between June 2001 and June 2002, jobs decreased by 20,300 or negative 1.26 percent. A year ago, Oregon was also ranked 40$^{th}$.

***Future Outlook*** – After a seasonally adjusted increase in jobs during the first quarter of this year, the second quarter turned negative. But the negative was on the mild side and does not change Oregon's Office of Economic Analysis *(OEA)* view that the Oregon economy is bottoming out for this recession. Growth will be slow in the second half of this year before reaching above 2.0 percent growth in 2003. OEA forecasts employment to fall by 0.7 percent for 2002, matching the job loss of 2001. Although quarterly growth in 2003 will be above 2.0 percent, the yearly average of 1.7 percent reflects the slow growth coming into 2003. Job growth in 2004 is projected to be 2.2 percent. Additional OEA forecasts for specific sectors of Oregon's economy are discussed in the following paragraphs.

Manufacturing will decline sharply in 2002, falling by 4.3 percent. This sector will bottom out and start to improve in late 2002. Manufacturing will grow 2.0 percent in 2003 and 2.6 percent in 2004, but the level of employment will still be below average job levels in 2000. Non-manufacturing jobs will slightly decrease by 0.1 percent in 2002, increase by 1.7 percent in 2003, and 2.1 percent in 2004.

Lumber and wood products are projected to be up 0.8 percent in 2002 with a very mild increase of 0.6 percent expected in 2003. Employment is forecast to grow 0.3 percent in 2004.

The sector that contains semiconductors and electrical machinery will have a sharp downturn of 7.2 percent in 2002 before recovering to a job growth of 2.9 percent in 2003. This sector is expected to bottom out during the second half of this year with mild job gains into 2003. Jobs are expected to grow 4.2 percent in 2004.

Transportation equipment will decline by 9.5 percent in 2002. Although job gains surged in the second quarter of 2002, a large part of the gain is expected to be temporary. Jobs will fall by 1.0 percent in 2003. Positive growth will prevail at 1.5 percent in 2004.

Construction is expected to repeat the decline of 2001 with a decrease of 6.6 percent in 2002. Job growth will be a positive 1.1 percent in 2003 and 3.9 percent in 2004.

Trade job growth will remain relatively weak in 2002 with a decline of 0.1 percent. Job growth will be stronger in 2003 at 1.6 percent and in 2004 at 1.7 percent. Services should see annual job growth of 0.3 percent in 2002, 2.3 percent in 2003, and 2.8 percent in 2004.

Population growth is expected to be higher than the U.S. average, but slower than the growth experienced in the mid-1990's. Slower growth will prevail over the next three years, with increases of 1.0 percent in 2002, and 1.2 percent in 2003, and 1.3 percent in 2004.

## MAJOR INITIATIVES

***Current Service Efforts and Accomplishments*** - Article XI-A of the Oregon Constitution outlines the broad duties of the Department. The primary Oregon Revised Statutes governing the Department are Chapters 406 through 408. Following is a brief description of the Department's primary Enterprise funds' programs and activities.

- The ***Veterans' Loan Program*** provides home loans to Oregon veterans at favorable interest rates. Eligibility requirements on who may receive a veterans' home loan are governed by both federal and State laws. As of June 30, 2002, this Program had approximately 18,000 mortgage loans and contracts outstanding, with a principal balance of approximately $590 million.

- The ***Veterans' Home Program*** provides professional medical, nursing, rehabilitative, social and other support services to United States veterans residing in the Oregon Veterans' Home *(OVH)*, located in The Dalles, Oregon. The OVH, which opened in November 1997, has the capacity to serve 151 veterans and had an occupancy of approximately 100 residents at June 30, 2002. The Department owns the OVH and has entered into a contract with Healthcare for the Mid-Columbia Region to provide the daily services needed by the veteran residents.

The major issue related to the Department's client base is that the composition and needs of the veteran population are changing due to the passage of time and external events. As the veteran population ages, it is necessary to be more responsive to the increasing health and disability issues of the elderly.

## FINANCIAL INFORMATION

***Internal Controls*** - Management is responsible for establishing and maintaining internal controls designed to ensure the Department's assets are safeguarded against loss from unauthorized use or disposition and that financial transactions are properly executed in accordance with generally accepted accounting principles. These internal controls are designed to provide reasonable, but not absolute, assurance that these objectives are met. Budgetary controls are maintained by the Department of Administrative Services and the Oregon Legislature.

***Enterprise Funds*** - The Veterans' Loan Program and the Veterans' Home Program are enterprise funds and account for the Department's business-type activities. At June 30, 2002, the Veterans' Loan Program had approximately $1.44 billion in assets *(primarily consisting of loan and contract receivables, cash and cash equivalents, and investment securities)* and about $1.30 billion in liabilities *(primarily consisting of general obligation bonds)*. Revenues from the Department's home loan program are generated through interest on loans originated and investment income. These revenues are used to pay interest expense on outstanding debt and related program and administrative expenses. At June 30, 2002, the Veterans' Home Program had assets of approximately $12 million consisting primarily of capital assets, receivables and cash and cash equivalents.

***Debt Administration*** - The Department, with the approval of the State Treasurer's office, has authority to issue general obligation bonds to fund the Veterans' Loan Program. The Department's general obligation bonds are rated as part of the State of Oregon's general obligation bond program. The Department's most recent general obligation bond issue was rated as follows:

| | |
|---|---|
| Moody's Investor Service | Aa 2 |
| Fitch Investors Service | AA |
| Standard & Poor's | AA |

As of June 30, 2002, the Department had approximately $1.23 billion in outstanding bonds. During fiscal year 2002, the Department issued approximately $120 million in bonds and retired approximately $170 million. In addition, the Department had previously entered into a taxable line of credit agreement to help preserve certain refunding opportunities. During fiscal year 2002, the Department borrowed $60 million from the taxable line of credit and also paid off $80 million. As of June 30, 2002, the Department had repaid all borrowings from the taxable line of credit.

***Cash Management*** - All monies collected by the Department are turned over to the State Treasurer, who is responsible for the control of cash and the investment of State funds. On June 30, 2002, the Department's Enterprise funds cash, cash equivalents *(excluding securities lending collateral),* and investments totaled approximately $806 million. The Oregon Investment Council, of which the State Treasurer is a member, establishes investment policy for all State of Oregon funds. To further Oregon's economic growth, the Council's continuing policy has been to invest locally when investments of comparable yield, quality, and maturity can be found in-state without damaging portfolio diversity. Fortunately for Oregonians, State-imposed safeguards minimize the dangers of investing in highly leveraged financial instruments which have been a cause of national concern. The State Treasurer pools all available cash into the Oregon Short-Term Fund from which investments are made in a variety of instruments.

***Risk Management*** - The Department of Administrative Services, through the Insurance Fund, provides for the State's self-insurance programs and for the administration, investigation, and settlement of claims against the Insurance Fund. In accordance with legislative directives, the Insurance Fund must operate on an actuarially sound basis.

***Independent Audit*** - The Secretary of State, Audits Division, has audited the financial records, books of account, and transactions of the Department's Enterprise funds for the year ended June 30, 2002. The auditors used generally accepted government auditing standards in conducting the engagement. Their opinion on the financial statements is included in the Financial Section of this report.

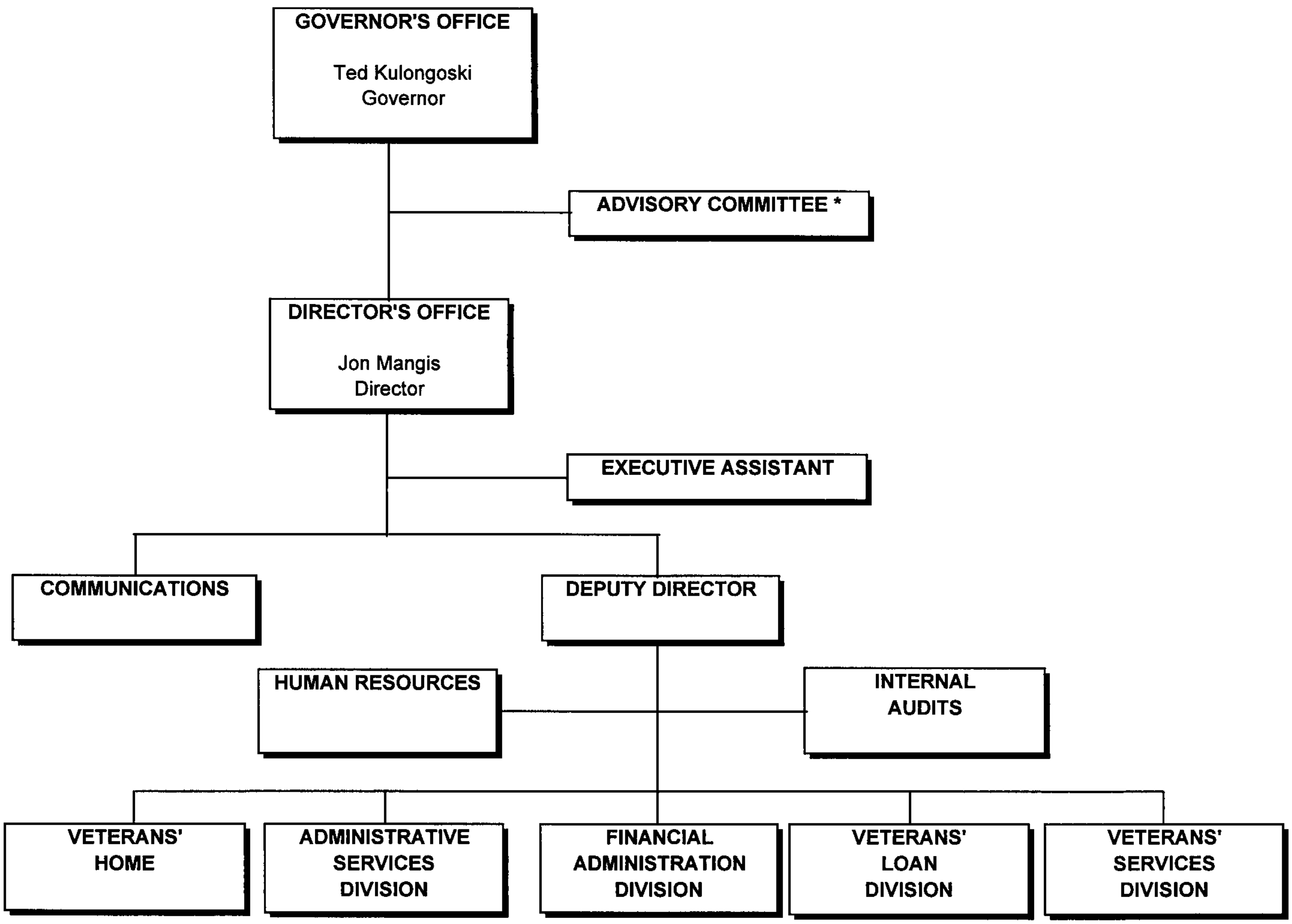
***Acknowledgements*** - The preparation of this report reflects the combined efforts of the Department's staff. The professionalism, commitment, and effort of the individuals involved is very much appreciated.

Respectfully submitted,

Jon A. Mangis
Director

Bruce W. Shriver
Chief Financial Officer

## OREGON DEPARTMENT OF VETERANS' AFFAIRS




* The Advisory Committee is a nine-member advisory body appointed by the Governor for four-year terms. The committee advises the Director concerning matters of the operations of the Department and issues affecting veterans and their dependents and survivors who reside in this state.

| Advisory Committee Members | Term Expires | Advisory Committee Members | Term Expires |
|---|---|---|---|
| Dale S. Albee | March 15, 2003 | Walter R. Crews | March 15, 2004 |
| Evelyn F. Anderson | July 31, 2005 | Robert Haltiner | March 15, 2004 |
| Staryl C. Austin, Jr. | March 15, 2004 | Harold C. Jordan | December 31, 2006 |
| Robert B. Brown | March 15, 2004 | Jim Willis | September 30, 2004 |
| Fulton M. Burns | March 15, 2004 | | |

**This page intentionally left blank**

*Dedication of the old Salem Armory (Liberty and Ferry Streets in Salem). Date: 1902. Photo courtesy of the Oregon State Archives and the Salem Public Library digital photograph collection of Ben Maxwell.*


*A military marching band (possibly Spanish-American War soldiers or veterans) on State Street in Salem. Date: unknown. Photo courtesy of the Oregon State Archives and the Salem Public Library digital photograph collection of Ben Maxwell.*

OFFICE OF THE
SECRETARY OF STATE
Bill Bradbury
Secretary of State

AUDITS DIVISION
Cathy Pollino
Director

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

*Auditing for a Better Oregon*

The Honorable Ted Kulongoski
Governor of Oregon
254 State Capitol
Salem, Oregon 97301-4047

Jon Mangis, Director
Department of Veterans' Affairs
700 Summer Street NE
Salem, Oregon 97301-1285

## INDEPENDENT AUDITOR'S REPORT

We have audited the accompanying basic financial statements of the enterprise funds of the state of Oregon Department of Veterans' Affairs (department), as of and for the year ended June 30, 2002, as listed in the table of contents. These financial statements are the responsibility of the department's 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 and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. 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 basic financial statements present only the department's enterprise funds and do not purport to, and do not, present fairly the financial position of the state of Oregon as of June 30, 2002, and the changes in its financial position and cash flows for the year 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 enterprise funds of the state of Oregon, Department of Veterans' Affairs, as of June 30, 2002, and the changes in financial position and cash

255 Capitol Street NE • Suite 500 • Salem, Oregon 97310
INTERNET: Audits.hotline@state.or.us • http://www.sos.state.or.us/audits/audithp.htm

flows thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements that comprise the department's enterprise funds. The other data in this report, designated as the introductory and other supplementary information sections in the table of contents, are presented for purposes of additional analysis and are not a required part of the basic financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on it.

In accordance with *Government Auditing Standards,* we have also issued our report dated December 19, 2002 on our consideration of the state of Oregon, Department of Veterans' Affairs enterprise funds' internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit. That report is separately presented in the other reports section as listed in the table of contents.

OREGON AUDITS DIVISION

Bill Bradbury
Secretary of State

December 19, 2002

STATE OF OREGON
DEPARTMENT OF VETERANS' AFFAIRS
**STATEMENT OF NET ASSETS**
PROPRIETARY FUNDS
JUNE 30, 2002

| | Enterprise Funds | | |
|---|---|---|---|
| | Veterans' Loan Program | Veterans' Home Program | TOTAL |
| **ASSETS** | | | |
| **Current Assets** | | | |
| Cash and Cash Equivalents | $ 444,789,334 | $ 492,654 | $ 445,281,988 |
| Cash and Cash Equivalents - Restricted | 9,172,761 | - | 9,172,761 |
| Investments | 146,910,925 | - | 146,910,925 |
| Securities Lending Cash Collateral | 33,442,192 | 34,495 | 33,476,687 |
| Receivables: | | | |
| Accrued Interest | 8,479,863 | - | 8,479,863 |
| LCLI Premiums | 332,500 | - | 332,500 |
| Other | 10,900 | 457,000 | 467,900 |
| Due From Other Funds | 26,747 | - | 26,747 |
| Real Estate Owned | 351,966 | - | 351,966 |
| Supplies Inventory and Prepaid Expenses | 45,272 | 793 | 46,065 |
| Total Current Assets | 643,562,460 | 984,942 | 644,547,402 |
| **Noncurrent Assets** | | | |
| Cash and Cash Equivalents - Restricted | 62,679,004 | - | 62,679,004 |
| Investments - Restricted | 141,733,260 | - | 141,733,260 |
| Mortgage Loans and Contracts Receivable (Net) | 582,527,538 | - | 582,527,538 |
| Deferred Underwriter's Discount | 2,413,889 | - | 2,413,889 |
| Capital Assets: | | | |
| Building, Property and Equipment | 9,681,670 | 12,479,114 | 22,160,784 |
| Land | - | 89,500 | 89,500 |
| Works of Art and Historical Treasures | 85,170 | 40,000 | 125,170 |
| Accumulated Depreciation | (4,215,939) | (1,526,424) | (5,742,363) |
| Total Noncurrent Assets | 794,904,592 | 11,082,190 | 805,986,782 |
| **TOTAL ASSETS** | $ 1,438,467,052 | $ 12,067,132 | $ 1,450,534,184 |
| **LIABILITIES** | | | |
| **Current Liabilities** | | | |
| Accounts Payable | $ 410,616 | $ 457,983 | $ 868,599 |
| Loan Cancellation Life Insurance Premium Payable | 562,197 | - | 562,197 |
| Deposit Liabilities | 2,154,231 | 7,097 | 2,161,328 |
| Accrued Interest on Bonds | 20,183,563 | - | 20,183,563 |
| Obligations under Securities Lending | 33,442,192 | 34,495 | 33,476,687 |
| Compensated Absences Payable | 552,488 | 16,746 | 569,234 |
| Bonds Payable-Maturing Within One Year (Net) | 114,325,964 | - | 114,325,964 |
| Arbitrage Rebate Payable | 186,645 | - | 186,645 |
| Matured Bonds Payable | 9,172,761 | - | 9,172,761 |
| Total Current Liabilities | 180,990,657 | 516,321 | 181,506,978 |
| **Noncurrent Liabilities** | | | |
| Bonds Payable-Maturing After One Year (Net) | 1,114,049,596 | - | 1,114,049,596 |
| Arbitrage Rebate Payable | 319,483 | - | 319,483 |
| Total Noncurrent Liabilities | 1,114,369,079 | - | 1,114,369,079 |
| **TOTAL LIABILITIES** | 1,295,359,736 | 516,321 | 1,295,876,057 |
| **NET ASSETS** | | | |
| Invested in Capital Assets, net of related debt (restated) | 5,550,901 | 11,082,190 | 16,633,091 |
| Net Assets, unrestricted | 137,556,415 | 468,621 | 138,025,036 |
| **TOTAL NET ASSETS** | $ 143,107,316 | $ 11,550,811 | $ 154,658,127 |

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

STATE OF OREGON
DEPARTMENT OF VETERANS' AFFAIRS
**STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET ASSETS**
PROPRIETARY FUNDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2002

| | Enterprise Funds | | |
|---|---|---|---|
| | Veterans' Loan Program | Veterans' Home Program | TOTAL |
| **OPERATING REVENUES** | | | |
| Interest Income: | | | |
| Mortgage Loans | $ 43,749,526 | $ - | $ 43,749,526 |
| Contracts | 3,522,372 | - | 3,522,372 |
| Investment Income | 35,956,850 | 13,983 | 35,970,833 |
| Loan Cancellation Life Insurance (LCLI) Processing Fee | 425,004 | - | 425,004 |
| Other Fees and Charges | 1,447,451 | 5,465,696 | 6,913,147 |
| Conservatorship Fees | 338,136 | - | 338,136 |
| Gain on Sale of Foreclosed Property | 172,472 | - | 172,472 |
| **TOTAL OPERATING REVENUES** | 85,611,811 | 5,479,679 | 91,091,490 |
| **OPERATING EXPENSES** | | | |
| Bond Interest | 68,560,732 | - | 68,560,732 |
| Interest on Taxable Line of Credit | 580,883 | - | 580,883 |
| Salaries and Other Payroll Expenses | 6,974,557 | 218,460 | 7,193,017 |
| Bond Expenses | 868,243 | - | 868,243 |
| Securities Lending Investment Expense | 522,316 | 590 | 522,906 |
| Real Estate Owned Expense | 73,308 | - | 73,308 |
| Services and Supplies | 2,480,268 | 54,645 | 2,534,913 |
| Veterans' Home Operations | - | 5,238,567 | 5,238,567 |
| Depreciation Expense | 538,555 | 331,368 | 869,923 |
| Bad Debt Expense | (906,906) | - | (906,906) |
| Other Expenses | 180,045 | - | 180,045 |
| **TOTAL OPERATING EXPENSES** | 79,872,001 | 5,843,630 | 85,715,631 |
| **OPERATING INCOME (LOSS)** | 5,739,810 | (363,951) | 5,375,859 |
| **Transfers** | | | |
| Net Operating Transfers from Veterans' Home Trust Fund | - | 1,380 | 1,380 |
| **CHANGE IN NET ASSETS** | **5,739,810** | **(362,571)** | **5,377,239** |
| **NET ASSETS - Beginning** | 94,931,080 | 11,873,382 | 106,804,462 |
| Prior Period Adjustment | 42,361,426 | - | 42,361,426 |
| Cumulative Effect of Change in Accounting Principles | 75,000 | 40,000 | 115,000 |
| **NET ASSETS - Beginning, restated** | 137,367,506 | 11,913,382 | 149,280,888 |
| **NET ASSETS - Ending** | $ 143,107,316 | $ 11,550,811 | $ 154,658,127 |

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

STATE OF OREGON
DEPARTMENT OF VETERANS' AFFAIRS
**STATEMENT OF CASH FLOWS**
PROPRIETARY FUNDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2002

| | Enterprise Funds | | |
|---|---|---|---|
| | Veterans' Loan Program | Veterans' Home Program | TOTAL |
| **Cash Flows from Operating Activities:** | | | |
| Receipts from Customers | $ 1,799,042 | $ 5,566,381 | $ 7,365,423 |
| Receipts from Other Funds for Services | 621,663 | - | 621,663 |
| Loan Principal Repayments | 165,593,471 | - | 165,593,471 |
| Loan Interest Received | 48,005,898 | - | 48,005,898 |
| Payments to Employees for Services | (6,979,943) | (216,319) | (7,196,262) |
| Payments to Suppliers | (1,775,956) | (5,398,993) | (7,174,949) |
| Payments to Other Funds for Services | (1,319,062) | (4,851) | (1,323,913) |
| Loans Made | (76,205,733) | - | (76,205,733) |
| Other Receipts (Payments) | 368,923 | 7,097 | 376,020 |
| Net Cash Provided (Used) in Operating Activities | 130,108,303 | (46,685) | 130,061,618 |
| **Cash Flows from Noncapital Financing Activities:** | | | |
| Proceeds from Bond Sales | 120,163,188 | - | 120,163,188 |
| Loan Proceeds | 60,000,000 | - | 60,000,000 |
| Principal Payments on Bonds | (169,974,083) | - | (169,974,083) |
| Principal Payments on Loans | (80,000,000) | - | (80,000,000) |
| Interest Payments on Bonds | (71,733,255) | - | (71,733,255) |
| Interest Payments on Loans | (580,883) | - | (580,883) |
| Bond Issuance Costs | (1,783,618) | - | (1,783,618) |
| Transfers from other funds | - | 1,380 | 1,380 |
| Net Cash Provided (Used) in Noncapital Financing Activities | (143,908,651) | 1,380 | (143,907,271) |
| **Cash Flows from Capital and Related Financing Activities:** | | | |
| Acquisition of Capital Assets | (295,599) | (11,497) | (307,096) |
| Proceeds from Sale of Fixed Assets | 2,544 | - | 2,544 |
| Net Cash Provided (Used) in Capital and Related Financing Activities | (293,055) | (11,497) | (304,552) |
| **Cash Flows from Investing Activities:** | | | |
| Purchases of Investments | (66,725,395) | - | (66,725,395) |
| Proceeds from Sales or Maturities of Investments | 83,534,265 | - | 83,534,265 |
| Interest on Investments and Cash Balances | 29,134,042 | 13,394 | 29,147,436 |
| Investment Income from Securities Lending | 522,316 | 590 | 522,906 |
| Investment Expense from Securities Lending | (522,316) | (590) | (522,906) |
| Net Cash Provided (Used) in Investing Activities | 45,942,912 | 13,394 | 45,956,306 |
| Net Increase (Decrease) in Cash and Cash Equivalents | 31,849,509 | (43,408) | 31,806,101 |
| Cash and Cash Equivalents - Beginning | 442,430,164 | 536,062 | 442,966,226 |
| Prior Period Adustments Restating Beginning Cash | 42,361,426 | - | 42,361,426 |
| Cash and Cash Equivalents - Ending | $ 516,641,099 | $ 492,654 | $ 517,133,753 |
| ***Reconciled to Statement of Net Assets*** | | | |
| *Cash and Cash Equivalents - current* | $ 444,789,334 | $ 492,654 | $ 445,281,988 |
| *Cash and Cash Equivalents - current, restricted* | 9,172,761 | - | 9,172,761 |
| *Cash and Cash Equivalents - noncurrent, restricted* | 62,679,004 | - | 62,679,004 |
| *Cash and Cash Equivalents - Ending (shown above)* | $ 516,641,099 | $ 492,654 | $ 517,133,753 |

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

STATE OF OREGON
DEPARTMENT OF VETERANS' AFFAIRS
**STATEMENT OF CASH FLOWS**
PROPRIETARY FUNDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2002

| | Enterprise Funds | | |
|---|---|---|---|
| | Veterans' Loan Program | Veterans' Home Program | TOTAL |
| **Reconcilation of Operating income to Net cash provided (used) by Operating Activities** | | | |
| Operating Income | $ 5,739,810 | $ (363,951) | $ 5,375,859 |
| Adjustments to Reconcile Operating Income to Net Cash Provided (Used) by Operating Activities: | | | |
| Depreciation and Amortization | 538,555 | 331,368 | 869,923 |
| Amortization of Bond Premium, Discount and Underwriter's Discount on called bonds | 28,791 | - | 28,791 |
| Bad Debt Expense | (906,906) | - | (906,906) |
| Interest Income Reported as Operating Revenue | (35,956,850) | (13,983) | (35,970,833) |
| Investment Expense | 522,316 | 590 | 522,906 |
| Interest Payments on Bonds Reported as Operating Expense | 69,141,615 | - | 69,141,615 |
| Bond Costs | 868,243 | - | 868,243 |
| Net Changes in Assets and Liabilities: | | | |
| Accounts and Interest Receivable | 804,118 | 100,685 | 904,803 |
| Prepaid Items | (34,484) | (524) | (35,008) |
| Loans and Contracts Receivable | 89,508,522 | - | 89,508,522 |
| Accounts Payable | (347,808) | (110,108) | (457,916) |
| Deposit Liabilities | 193,920 | 7,096 | 201,016 |
| Compensated Absences Payable | 8,461 | 2,142 | 10,603 |
| Total Adjustments | 124,368,493 | 317,266 | 124,685,759 |
| Net Cash Provided (Used) by Operating Activities | $ 130,108,303 | $ (46,685) | $ 130,061,618 |
| **Noncash Investing and Capital and Related Financing Actvities** | | | |
| Net Change in Fair value of Investments | $ 6,783,131 | $ - | $ 6,783,131 |
| Foreclosed Property | 433,278 | - | 433,278 |
| Total Noncash Investing and Capital Related Financing Activities | $ 7,216,409 | $ - | $ 7,216,409 |

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

**_STATE OF OREGON_**
**_DEPARTMENT OF VETERANS' AFFAIRS_**
**_PROPRIETARY FUNDS_**
**_NOTES TO THE FINANCIAL STATEMENTS_**
**_JUNE 30, 2002_**

*The accompanying financial statements of the Proprietary Funds of the Oregon Department of Veterans' Affairs (the "Department") have been prepared in conformity with generally accepted accounting principles (GAAP) as prescribed by the Governmental Accounting Standards Board (GASB), the Financial Accounting Standards Board (FASB), and the American Institute of Certified Public Accountants (AICPA). Under the auspices of GASB Statement No. 20, the Department does not apply Financial Accounting Standards Board (FASB) pronouncements issued after November 30, 1989 for proprietary activities unless GASB amends its pronouncements to specifically adopt FASB pronouncements issued after that date. The Department complies with the State of Oregon guidelines in applying GAAP following GASB Statement No. 20.*

## 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### Reporting Entity

The Department is a part of the State of Oregon reporting entity. The Department operates under the provisions of the Oregon Constitution article XI-A and primarily Oregon Revised Statutes *(ORS)* chapters 406, 407, 408.010 – 408.110, and 408.360 – 408.530. The Department's director is appointed by the Governor with input from the Advisory Committee and is subject to confirmation by the Oregon Senate. The director must be a war veteran chosen on the basis of his or her executive and administrative ability. The Advisory Committee is a nine-member board, appointed by the Governor that acts in an advisory capacity to the director concerning all matters upon which the director requests counsel. The State Legislature has significant ability to influence funding, approve the Department's budget, and pass laws governing the Department.

The Department was created in 1945 to help veterans in obtaining benefits under federal, state, and local programs and to undertake the Veterans' Loan Program to provide home and farm loans to veterans at favorable interest rates. The Veterans' Loan Program is operated through earnings of the program itself, which is financed through the sale of tax-exempt general obligation bonds. These bonds are then retired through principal and interest payments received from borrowers and earnings from invested funds.

The Oregon Veterans' Home *(Veterans' Home Program)* provides skilled nursing and Alzheimer's disease care to some of Oregon's most vulnerable veterans. The single-story, 75,000 square foot facility offers care in a home-like environment, complementing the philosophy of personal independence.

The basic financial statements and notes presented herein include only the proprietary fund activity of the Department, namely the Veterans' Loan Program and the Veterans' Home Program. The Department operates other programs which have no material impact on the proprietary fund activity of the Department. The financial activity of these non-proprietary programs is presented in the **Other Supplemental Section**.

**Measurement Focus of Accounting and Basis of Presentation**

The accounts of the Department are organized on the basis of funds. A fund is defined as a fiscal and accounting entity with a self-balancing set of accounts recording assets, liabilities, and equities which are segregated for the purpose of carrying on specific activities or attaining certain objectives in accordance with special regulations or restrictions.

The Veterans' Loan Program and the Veterans' Home Program are accounted for as Proprietary funds. The focus of Proprietary fund measurement is upon determination of operating income, changes in net assets, financial position, and cash flows, which is similar to private-sector business. Proprietary funds are presented using the accrual basis of accounting and the flow of economic resources measurement focus. Under the accrual basis of accounting, revenues are recognized when they are earned and expenses are recognized when the liabilities are incurred.

**Budgetary Process**

The Oregon Legislature approves budgets for a biennial period. Operating expenses are subject to limitation and bond related expenses are subject to administrative limitation. Both types of limitations lapse at the end of the biennium. Budgets are adopted on a basis which differs from generally accepted accounting principles and financial reporting standards in the treatment of bond proceeds, loan purchases, and acquisition and depreciation of capital assets. For budgetary purposes, these transactions are treated on a cash basis and other operating revenues and expenses are on an accrual basis.

**Cash and Cash Equivalents**

Cash and Cash Equivalents include: cash on hand, cash and investments held by the State Treasury in the Oregon Short-Term Fund *(OSTF)*, cash deposits held by the State's fiscal agent for payment of matured bonds and coupons, and cash deposits held by the agency's loan cancellation life insurance carrier. All monies held in the OSTF are considered to be cash equivalents, which is a cash and investment pool having characteristics of a demand deposit account.

**Investments and Investment Income**

The Department's investments are stated at fair value. Quoted market values were used to value investments except for non-participating interest-earning investments. Non-participating interest-earning investment contracts are exempt from fair value reporting and are shown on the financial statements at amortized cost.

Investment Income includes changes in the fair value of investments and is recognized as a revenue in the Statement of Revenues, Expenses and Changes in Fund Net Assets. Realized gains based on the net increase in fair value of investments are included as a component of Investment Income.

**Securities Lending Cash Collateral**

The State Treasurer participates in securities lending with a portion of the OSTF. The Department's share of the cash collateral received from broker-dealers is disclosed in the Statement of Net Assets as Securities Lending Cash Collateral.

**Receivables**

Receivables are shown net of an allowance for uncollectible accounts. Receivables included are amounts due that represent revenues earned or accrued in the current period. Types included in this classification relate to interest, mortgage loans receivable, loan cancellation life insurance premiums, and other miscellaneous receivables.

**Real Estate Owned**

Properties acquired through foreclosure proceedings or by acceptance of deeds in lieu of foreclosure are recorded at the lower of cost or net realizable value. Cost is defined as the outstanding principal balance of the mortgage loan or contract on the date of foreclosure. Professional appraisers estimate fair market value. The lower of cost or fair market value is adjusted, if necessary, for estimated selling expenses to arrive at the net realizable value shown on the financial statements.

**Supplies Inventories and Prepaid Expenses**

Supplies inventories, which consist primarily of operating supplies, are stated at cost utilizing the first-in, first-out cost valuation method. Prepaid expense include prepaid postage on hand at year-end. In Proprietary funds, inventories are recorded as expenses when used.

**Capital Assets**

Capital assets are recorded at cost. Depreciation is calculated using the straight-line method. Property and equipment are depreciated over a period of five years. The Veterans' Building and the Oregon Veterans' Home are depreciated over their useful life *(50 years and 40 years, respectively)*. Building-related assets are capitalized and then depreciated over the remaining estimated life of the building. Gain or loss on the sale of an asset is determined by taking the difference between the carrying value *(cost less depreciation)* and the sale price. Furniture and equipment assets costing $5,000 or more are capitalized and then depreciated over a useful life of five years.

**Compensated Absences Payable**

Employees accrue vacation leave at various accrual rates with a maximum accumulation of 350 hours per management employee and 300 hours per classified employee. Employees can be paid up to a maximum of 250 hours of accrued vacation leave at termination. Accumulated 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 non-vesting, accumulated sick pay benefits.

**Arbitrage Rebate Payable**

The Department discloses a liability to the federal government for excess earnings on tax-exempt bonds. The Department treats excess earnings that are rebateable to the federal government as a reduction of revenue.

**Invested in Capital Assets, net of related debt**

This is the component of Net Assets *(equity)* net of accumulated depreciation and reduced by any outstanding balances of bonds or other borrowings that are attributable to the acquisition, construction, or improvement of those assets.

**Operating Revenues and Expenses**

Operating revenues include interest and fees on program loans as well as earnings on cash and investments related to Veterans' Loan and Veterans' Home programs. Administrative expenses, depreciation related to capital assets, and bond program related expenses are considered operating expenses.

**Bond Expenses**

Bond premiums and discounts associated with a particular bond issue are amortized over the life of the bond issue using the bonds outstanding method of amortization. These expenses are charged or credited to interest expense.

Miscellaneous bond expenses are primarily recorded as expenses when incurred. Amortization of Underwriter's discounts are also included as miscellaneous bond expenses. Included in bond expenses are fees related to Series 73 variable-rate bonds, amortization of prepaid remarketing fees from fixed-rate conversions, expenses of the matured bond and coupon account with the State's Fiscal Agent, and bond attorney fees.

Expenses of Series 73 variable rate bonds include Standby Bond Purchase Agreement commitment fees and remarketing agent fees *(See Note 7)*. These fees are payable quarterly in arrears.

## 2. DEPOSITS AND INVESTMENTS

**Deposits**

As of June 30, 2002 the book balance of Cash and Cash Equivalents was $445,281,988 for current, unrestricted cash and cash equivalents; $9,172,761 for current, restricted cash and cash equivalents; $62,679,004 in restricted, noncurrent cash and cash equivalents *(combined total was $517,133,753)*. The bank balance of these cash balances was $517,093,346.

Of these monies, $480,559,160 was held in demand accounts with the State Treasurer and invested in the Oregon Short Term Fund *(OSTF)*, which is maintained by the State Treasurer. The OSTF is a cash and investment pool that is available for use by all funds and local governments. State Treasurer demand deposit accounts and time certificates of deposit investments of the Oregon Short Term Fund held in state banks are insured or collateralized in excess of Federal Deposit Insurance Corporation *(FDIC)* coverage for a minimum of 25 percent in accordance with State statute. Because the pool operates as a demand deposit account, each fund type's portion of this pool is classified on the Statement of Net Assets as Cash and Cash Equivalents.

The Department's monies in the OSTF are subject to FDIC coverage of $100,000. Balances over that amount are insured by a statewide collateral pool, a multiple financial institution collateral pool that protects public deposits pursuant to Oregon Revised Statutes *(ORS)* 295.015. Earnings on the OSTF are allocated based on daily account balances and a variable interest rate determined periodically by the State Treasurer. Securities in the OSTF are primarily held by the State Treasurer's agent in the name of the State of Oregon. They consist of 46 percent in U.S. government securities; 40 percent in short-term commercial paper; and the remainder in time certificates of deposit and securities lending holdings. A copy of the OSTF audited annual financial report may be obtained by writing to the Oregon State Treasury, 350 Winter St NE Suite 100, Salem, OR 97301-3896.

In addition, the Department held $27,361,426 with an insurance carrier as a reserve for loan cancellation life insurance. These monies are uncollateralized and are not insured under FDIC protection and are shown as Cash and Cash Equivalents – Current, unrestricted. For additional information on these monies *(also called the Loan Cancellation Life Insurance Contingency Fund)* see Note 5.

The Department held $9,172,761 at the State's Fiscal Agent for redemption of the Department's bonds and coupons that have matured, but have not yet been redeemed. This money is show as Cash and Cash Equivalents – Restricted, a current asset. These funds are deposited at the Bank of New York and are backed by the full faith and credit of the Bank of New York. Further, these funds, while not collateralized, are insured up to $100,000 per bondholder as specified by FDIC regulations.

**Investments**

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. The State Treasurer is prohibited from investing in common stock pursuant to ORS 293.736. As of June 30, 2002, the State Treasurer invested the Department's funds primarily in U.S. government securities, international bonds, and corporate bonds.

A portion of the proceeds of Bond Series 75, 76, 77, 79, and 80 are invested in specified accounts called Guaranteed Investment Contracts. These monies are held by institutions outside of the State Treasury. The Guaranteed Investment Contracts feature fixed rates of return over the length of the contracts. The Guaranteed Investment Contract accounts are currently uncollateralized but are subject to collateralization by the providers in the event that the debt rating of a provider falls below a specified level.

A portion of the proceeds of Bond Series 81 and 82 are invested in Repurchase Agreements. These investments are fully collateralized with permitted securities at 103% of the repurchase price. Repurchase Agreements, like the Department's Guaranteed Investment Contracts, feature fixed rates of return over the length of the contract. In the event of a rating downgrade of the seller, the collateralization levels may be increased. Both Guaranteed Investment Contracts and Repurchase Agreements are investments evidenced by contracts, rather than by securities, and are uncategorized with regard to credit risk.

There are three categories of credit risk that apply to investments:

- Category 1 includes investments that are insured or registered, or for which the securities are held by the Department or its agent in the Department's name.
- Category 2 includes uninsured and unregistered investments for which the securities are held by the counterparty's trust department or agent in the Department's name.
- Category 3 includes uninsured and unregistered investments for which the securities are held by the counterparty or by its trust department or agent but not in the Department's name.

The schedule below presents the credit risk and carrying amount *(fair value)* as of June 30, 2002. The Department's portion of securities lending balances in the OSTF is unclassified with regard to risk and is included in the investment schedule below.

| | Category | | | Carrying |
|---|---|---|---|---|
| | 1 | 2 | 3 | Amount |
| **Investments** | | | | |
| Investments held by State Treasurer | | | | |
| U.S. Government and agency securities | $ 144,647,543 | $ - | $ - | $ 144,647,543 |
| International Bonds | 46,263,969 | - | - | 46,263,969 |
| Corporate Bonds | 62,482,184 | - | - | 62,482,184 |
| Total Investments held by State Treasurer | $ 253,393,696 | $ - | $ - | $ 253,393,696 |
| **Investments - Not Categorized** | | | | |
| Guaranteed Investment Contracts | | | | $ 30,614,126 |
| Repurchase Agreements | | | | 4,636,363 |
| Investments held by broker-dealers under securities loans with cash collateral: | | | | |
| U.S. Government and agency securities | | | | $ 32,564,750 |
| Securities Lending Short-Term collateral Investment Pool (Oregon Short-Term Fund only): | | | | $ 33,494,008 |
| Less: | | | | |
| Securities Lending Amounts | | | | $ (66,058,758) |
| **Total Investments** | | | | $ 288,644,185 |
| ***Compared To Financial Statements*** | | | | |
| **Investments – Unrestricted** | | | | 146,910,925 |
| **Investments – Restricted** | | | | 141,733,260 |
| **Total Investments** | | | | $ 288,644,185 |

## Restricted Assets

Included in Cash and Cash Equivalents and Investments are amounts recorded in the Department's Debt Service Reserve Account. Funds in the Debt Service Reserve Account are restricted for retirement of future bond principal and interest. As of June 30, 2002, the Debt Service Reserve Account had a balance of $204,412,264, which included $62,679,004 in cash and $141,733,260 in net investments *(fair value)*. These balances are shown as Cash and Cash Equivalents – Restricted *(Noncurrent)*. In addition, the Department had funds held by the State's Fiscal Agent which were restricted for payment of matured bonds and interest payable. These balances are shown as Cash and Cash Equivalents – Restricted, a current asset.

## Securities Lending

In accordance with State investment policies, state agencies may participate in securities lending transactions. The Oregon State Treasury has, through a Securities Lending Agreement, authorized its custodian, State Street Bank and Trust Company *("State Street")*, to lend the Department's securities to broker-dealers and banks pursuant to a form of loan agreement. Both Oregon State Treasury and the broker-dealer borrowers maintained the right to terminate all securities lending transactions on demand. There have been no significant violations of the provisions of securities lending agreements.

During the year, State Street lent the Department's fixed income securities and received as collateral U.S. dollar-denominated cash. Borrowers were required to deliver cash collateral for each loan equal to at least 102% of the fair value of the security on loan. Oregon State Treasury did not impose any restrictions during the year on loans of the Department's fixed income securities. The Oregon State Treasury is fully indemnified by State Street against losses due to borrower default, and there were no losses during the year from the failure of borrowers to return securities on loan. However, the Department had no securities on loan as of June 30, 2002, and therefore no cash collateral was invested on the Department's behalf by State Street. Also, because the Department had no securities on loan as of June 30, 2002, it had no credit risk exposure to borrowers.

The Department's cash balances are invested in the OSTF, a cash and investment pool managed by the Oregon State Treasury which is available for use by all state funds and local governments. State Street is authorized to lend OSTF securities in return for U.S. dollar-denominated cash. State Street is also authorized by the Securities Lending Agreement to invest this cash collateral in a short-term investment pool maintained by State Street. At June 30, 2002 the pool had an average weighted maturity of 295 days. Since the securities loans are callable on demand by either the lender or borrower, the life of the loans at June 30, 2002 is effectively one day and consequently does not generally match the life of the investments in the pool. The Department's allocated portion of the OSTF securities on loan and the related collateral is presented in the schedule of investments shown above. As of June 30, 2002, the fair value of the securities on loan from the OSTF and the fair value of securities purchased with the cash collateral were $525,113,868 and $540,098,364, respectively.

## Investment Income

The following table details the components of Investment Income for the year ended June 30, 2002:

| | | June 30, 2002 |
|---|---|---|
| ***Veterans' Loan Program:*** | | |
| Investment income: Accrual basis | $ | 28,651,402 |
| Securities lending revenue | | 522,317 |
| Increase/(Decrease) in fair value of investments | | 6,783,131 |
| Investment income | $ | 35,956,850 |
| ***Veterans' Home Program:*** | | |
| Investment income: Accrual basis | $ | 13,393 |
| Securities lending revenue | | 590 |
| Investment income | $ | 13,983 |

## 3. MORTGAGE LOANS AND CONTRACTS RECEIVABLE

Mortgage loans and contracts receivable are secured by real property, which is repossessed if the receivable becomes uncollectible. Most new loan and contract agreements made during the period from May 1971 through December 1991 contain a provision authorizing the Department to adjust the interest rate. Loan agreements *(excluding contracts)* made subsequent to December 1991 have fixed interest rates.

The loan and contract receivable portfolio at June 30, 2002 is approximately $593 million. All mortgaged property is located within Oregon. The Department is exposed to a statewide concentration of credit risk in the amount of approximately $593 million.

The Department uses the allowance method to estimate uncollectible mortgage loans and contracts receivable. The allowance is periodically adjusted by management to accommodate changes in economic conditions, nonperforming assets, historical loss experience, and other conditions that may affect the ultimate collectibility of the mortgage loans and contracts. In 2002 the Department determined the balance of the allowance account to be in excess of projected losses for the remaining loan and contract portfolio. Accordingly, the account balance was reduced at June 30, 2002 from $11.3 million to $10.35 million, or approximately 1.75 percent of gross loans and contracts receivable.

The following table details the mortgage loans and contracts receivable and allowance accounts as disclosed on the balance sheet for June 30, 2002.

| | | June 30, 2002 |
|---|---|---|
| Loans Receivable | $ | 556,017,331 |
| Contracts Receivable | | 36,860,207 |
| Total Loans and Contracts Receivable | $ | 592,877,538 |
| Less: Allowance for Principal Losses | | (10,350,000) |
| Net Loans and Contracts Receivable | $ | 582,527,538 |

Included in mortgage loans receivable are loans that will not amortize at their current monthly payment amounts. These loans became non-amortizing primarily through borrowers' choosing to extend the repayment term of their loans in lieu of accepting increased monthly principal and interest installments resulting from loan interest rate increases. The option to allow a borrower to extend the repayment life of the loan rather than accept an increase in the monthly principal and interest installment amount was the result of legal action brought against the Department by the Associated Oregon Veterans in 1985. As of June 30, 2002, there were approximately 390 non-amortizing accounts with an aggregate principal balance of approximately $36,561,000. This represents 6.3 percent of the total net loans and contracts receivable.

**Related Party Transactions: Home Loans to Employees**

Department employees are entitled to apply for an ODVA home loan if they meet the eligibility criteria, namely military service and citizenship in the state, and also underwriting standards such as those related to credit history and income level. The interest rate on the home loan and other terms and conditions of these loans are identical to those home loans made to non-employees. During the fiscal year ended June 30, 2002, the department made no new home loans to its eligible veteran employees. At June 30, 2002 the balance of existing home loans was $455,566 based on loans made to seven employees, including two Department managers. This amount represents less than 0.1% of the total loans and contracts receivable.

**Troubled Debt Restructurings**

The Department makes every reasonable attempt to keep a borrower in the home purchased under the Veterans' Loan Program. In order to avoid foreclosure one method of working with borrowers is to temporarily reduce loan payments for borrowers. This is allowed under ORS 407.095. During the year ended June 30, 2002, the Department provided this relief to some borrowers and deferred loan interest income of approximately $20,800. This interest amount was subsequently capitalized on these loans. In total, $947,500 in loans were restructured in this fashion. From these restructured loans the Department received $52,200 in mortgage interest income during the fiscal year.

## 4. CAPITAL ASSETS

The following table details the net capital assets of the Veterans' Loan and Veterans' Home Programs for the year ended June 30, 2002:

| | | June 30, 2002 |
|---|---|---|
| **Veterans' Loan Program** | | |
| Building, Property and Equipment | $ | 9,681,670 |
| Less: Accumulated Depreciation | | (4,215,939) |
| Building, Property and Equipment, carrying value | $ | 5,465,731 |
| Works of Art and Historical Treasures, non-depreciating | $ | 85,170 |
| Total Capital Assets, net | $ | 5,550,901 |
| **Veterans' Home Program** | | |
| Building, Property and Equipment | $ | 12,479,114 |
| Less: Accumulated Depreciation | | (1,526,424) |
| Building, Property and Equipment, carrying value | $ | 10,952,690 |
| Works of Art and Historical Treasures, non-depreciating | $ | 40,000 |
| Land | | 89,500 |
| Total Capital Assets, net | $ | 11,082,190 |
| **Total Capital Assets, net** | $ | 16,633,091 |

The following table provides detail on the balances and activities of the Department's Proprietary fund capital assets for the year ended June 30, 2002:

| | Beginning Balance | Increases | Decreases | Ending Balance |
|---|---|---|---|---|
| ***Capital assets not being depreciated:*** | | | | |
| Land | $ 89,500 | $ - | $ - | $ 89,500 |
| Works of Art and Historical Treasures | - | 125,170 | - | 125,170 |
| Total Capital Assets not being depreciated | 89,500 | 125,170 | - | 214,670 |
| ***Capital assets being depreciated:*** | | | | |
| Buildings | 19,601,313 | - | - | 19,601,313 |
| Property and Equipment | 2,512,388 | 57,253 | 10,170 | 2,559,471 |
| Total Capital Assets being depreciated | 22,113,701 | 57,253 | 10,170 | 22,160,784 |
| ***Less accumulated depreciation for:*** | | | | |
| Buildings | (3,604,513) | (454,233) | - | (4,058,746) |
| Property and Equipment | (1,267,928) | (415,689) | - | (1,683,617) |
| Total accumulated depreciation | (4,872,441) | (869,922) | - | (5,742,363) |
| **Total Capital assets, net** | $ 17,330,760 | $ (687,499) | $ 10,170 | $ 16,633,091 |

## 5. LOAN CANCELLATION LIFE INSURANCE

The Department offers Loan Cancellation Life Insurance *(LCLI)* to approved borrowers and their spouses through a contract with a private insurance company. Historically subsidized from the Oregon War Veterans' Fund *(a dedicated fund of the Department created under Article XI-A of the Oregon Constitution)*, the Department collects the premiums from borrowers and remits collected premiums, less an administrative fee, to the private insurance company. Upon the death of an insured person, either the account balance will be paid in full, or the amount of insurance in force will be paid and applied toward the account balance.

The Loan Cancellation Life Insurance Contingency Fund is a special fund consisting of amounts generated by the group policy and interest earned on the fund balance. Monies in the LCLI account are held and controlled by the insurance carrier during the contract period. The fund stabilizes rate experience developed under the group loan cancellation life insurance policy. Annual accounting of premiums, claims, administrative costs, and interest earnings are provided by the insurance carrier for the fund once a year, at August 31. The balance of the LCLI Contingency Fund is disclosed in Note 2 as Cash and Cash Equivalents – Current, unrestricted.

## 6. BONDS PAYABLE AND DEBT SERVICE

The table below provides a summary of general obligation bond transactions of the Department for the fiscal year ended June 30, 2002:

| | | |
|---|---|---|
| Bonds Payable *(Par)* at June 30, 2001 | $ | 1,278,305,000 |
| Bonds Issued | | 120,150,000 |
| Bonds Retired | | (169,920,000) |
| Bonds Payable *(Par)* at June 30, 2002 | $ | 1,228,535,000 |

Shown below are the components of net bonds payable as disclosed on the balance sheet for June 30, 2002:

| | | Short Term | | Long Term | | Total |
|---|---|---|---|---|---|---|
| Bonds Payable (Par) | $ | 114,175,000 | $ | 1,114,360,000 | $ | 1,228,535,000 |
| Premium on Bonds Sold | | 204,924 | | 490,001 | | 694,925 |
| Discount on Bonds Sold | | (53,960) | | (800,405) | | (854,365) |
| Net Bonds Payable | $ | 114,325,964 | $ | 1,114,049,596 | $ | 1,228,375,560 |

The following schedule summarizes future debt service requirements to maturity as of June 30, 2002:

| ***Fiscal Year*** | ***Principal*** | ***Interest*** | ***Total*** |
|---|---|---|---|
| 2003 | $ 114,175,000 | $ 63,173,000 | $ 177,348,000 |
| 2004 | 104,620,000 | 55,062,988 | 159,682,988 |
| 2005 | 84,845,000 | 47,715,889 | 132,560,889 |
| 2006 | 65,045,000 | 41,566,843 | 106,611,843 |
| 2007 | 65,315,000 | 36,410,090 | 101,725,090 |
| 2008-2012 | 177,815,000 | 112,446,699 | 290,261,699 |
| 2013-2017 | 119,840,000 | 89,183,788 | 209,023,788 |
| 2018-2022 | 315,295,000 | 61,683,148 | 376,978,148 |
| 2023-2027 | 58,710,000 | 42,540,664 | 101,250,664 |
| 2028-2032 | 48,950,000 | 26,816,220 | 75,766,220 |
| 2033-2037 | 30,790,000 | 16,176,976 | 46,966,976 |
| 2038-2042 | 38,670,000 | 7,143,581 | 45,813,581 |
| 2043-2047 | 4,465,000 | 119,969 | 4,584,969 |
| TOTAL | $ 1,228,535,000 | $ 600,039,855 | $ 1,828,574,855 |

**NOTE:** $370,000,000 of Series 73E,F,G and H Variable Demand Rate bonds are included at an assumed interest rate of 1.35%, the rate in effect at June 30, 2002

Shown below are the outstanding bond issues and their final maturities *(in fiscal years)* as of June 30, 2002:

| **Series** | **Dated** | **Issued** | **Outstanding** | **Final Maturity** |
|---|---|---|---|---|
| LIX (59) | August 1, 1979 | $ 200,000,000 | $ 40,000,000 | 2004 |
| LX (60) | November 1, 1979 | 200,000,000 | 60,000,000 | 2005 |
| LXI (61) | January 1, 1980 | 300,000,000 | 140,000,000 | 2009 |
| LXII (62) | April 1, 1980 | 300,000,000 | 130,000,000 | 2009 |
| LXIII (63) | July 1, 1980 | 300,000,000 | 130,000,000 | 2009 |
| LXIV (64) | October 1, 1980 | 300,000,000 | 50,000,000 | 2010 |
| LXVI (66) | June 1, 1981 | 240,000,000 | 10,000,000 | 2003 |
| 73 | December 1, 1985 | 740,000,000 | 370,000,000 | 2020 |
| 75 | October 1, 1995 | 70,000,000 | 41,470,000 | 2027 |
| 76A | April 1, 1997 | 40,000,000 | 30,240,000 | 2029 |
| 77 | April 1, 1998 | 40,000,000 | 36,095,000 | 2030 |
| 78A | March 1, 2000 | 10,000,000 | 7,845,000 | 2024 |
| 78B | July 6, 2000 | 10,000,000 | 7,980,000 | 2024 |
| 79A | March 1, 2000 | 22,000,000 | 20,505,000 | 2032 |
| 80A | August 15, 2000 | 35,000,000 | 34,250,000 | 2033 |
| 81 | September 1, 2001 | 60,150,000 | 60,150,000 | 2043 |
| 82 | June 1, 2002 | 60,000,000 | 60,000,000 | 2043 |
| Total Bonds Outstanding as of June 30, 2002: | | | $ 1,228,535,000 | |

**Debt Refunding: Series 81 Bond Sale and Refunding**

On September 25, 2001, the Department issued $60,150,000 of Series 81 general obligation bonds with an average interest rate of 5.20 percent. These bonds were issued to refund $9,999,937.50 of Series 60, $9,999,937.50 of Series 62, and $9,999,937.50 of Series 64 as well as to refund a taxable line of credit of $30,000,000. The average interest rate of the debt refunded was 6.17 percent. The current refunding of these bonds increases the total debt service payment over the next 40 years *(assuming no bond calls of Series 81 occur)* by approximately $97 million while resulting in an economic gain of approximately $1.8 million.

**Debt Refunding: Series 82 Bond Sale and Refunding**

On June 19, 2002, the Department issued $60,000,000 of Series 82 general obligation bonds with an average interest rate of 5.45 percent. These bonds were issued to refund $10,000,000 of Series 59, $10,000,000 of Series 61, and $10,000,000 of Series 63 as well as to refund a taxable line of credit of $30,000,000. The average interest rate of the debt refunded was 4.62 percent. The current refunding of these bonds increases the total debt service payment over the next 40 years *(assuming no bond calls of Series 82 occur)* by approximately $60 million while resulting in an economic gain of approximately $277 thousand.

## 7. DEMAND BONDS

Included in long-term debt at June 30, 2002 is $370,000,000 of State of Oregon, General Obligation, Veterans' Welfare Variable Rate Demand Bonds, Series 73 E, F, G & H. The bonds are general obligations of the State of Oregon and are payable from revenues and reserves of the Veterans' Loan Program. These bonds may be tendered by the bondholder on specified dates at a price equal to principal plus accrued interest.

The Department's Remarketing Agents *(J.P. Morgan Securities Inc. and Morgan Stanley Dean Witter)* are authorized to use their best efforts to sell the repurchased bonds at face value by adjusting the interest rate on a weekly basis. The interest rate borne by each series of bonds will be determined by the designated Remarketing Agent for such bonds.

In the event the bonds cannot be remarketed, they will be purchased as specified by the Standby Bond Purchase Agreement *(SBPA)*. Under the SBPA, JPMorgan Chase Bank, formerly known as Morgan Guaranty Trust Company, will commit to purchase any Series 73 E and G unremarketed bonds, and Bayerische Landesbank Girozentrale will commit to purchase any Series 73 F and H unremarketed bonds, in each case subject to certain conditions set forth in the SBPA.

No tender advances or draws have been necessary to purchase any unremarketed bonds under the SBPA. Therefore, no tender advances or draws are outstanding as of June 30, 2002. If a tender advance did occur, it would accrue interest at the bank's base rate *(either a prime lending rate or the federal funds rate plus ½ of 1%, whichever is higher)*. If the tender advance is in default, interest would accrue at the bank's base rate plus 1%. Interest on tender advances must generally be repaid first before the principal portion of a tender advance is repaid. In most cases, tender advances are required to be paid off in approximately two years. Tender advances could be paid off earlier than two years if the Department elected to do so. If repayment of any tender advances does not occur within the specified timeframes contained in the SBPA, a default would have occurred.

Each bank's present purchase commitment consists of the payment of the purchase price equal to the principal of and up to 40 days of accrued interest calculated at a rate of 14 percent per annum, if any, on the bonds of the applicable series tendered for purchase and not remarketed on the purchase date. The purchase commitment of each bank may be reduced from time to time upon occurrence of certain events specified in the SBPA. As of June 30, 2002, the Department is required to pay a yearly commitment fee which is payable quarterly in arrears, at a rate of .125 percent per annum, applied to the purchase commitment defined above.

The present purchase commitments by the banks will remain in effect to the earlier of (a) June 24, 2003 *(scheduled expiration date)*, unless extended at the option of the bank; (b) the conversion of all outstanding bonds of a given series to either a variable rate period ending after the scheduled expiration date or a fixed *(or term)* rate; (c) the date on which no bonds of a given series are outstanding; (d) the date on which the commitment with respect to a particular series has been terminated in accordance with the SBPA.

## 8. SHORT TERM DEBT

The Department has entered into a taxable line of credit agreement to help preserve certain refunding opportunities that may be used to finance veterans' housing loans. The taxable line of credit is with KeyBank National Association and the interest rate is based on a LIBOR index *(London InterBank Offered Rate)* or the bank's prime rate. The borrowing limit on the line of credit can not exceed $30 million. As of June 30, 2002, the Department had no outstanding balance from its taxable line of credit.

The following table provides detail on the balances and activities of the Department's short-term taxable line of credit financing *(disclosed as Notes Payable)* for the fiscal year ended June 30, 2002:

| | Beginning Balance | Increases | Decreases | Ending Balance |
|---|---|---|---|---|
| Notes Payable | $ 20,000,000 | $ 60,000,000 | $ 80,000,000 | $ -- |

## 9. INTERFUND TRANSACTIONS

At June 30, 2002, the Veterns' Loan Program had an outstanding receivable of $26,747 due from the Department's Conservatorship Trust Fund.

## 10. EMPLOYEE RETIREMENT PLAN

The Department's employees participate in the Oregon Public Employees Retirement System *(PERS)*, a cost-sharing multiple-employer public employee defined benefit pension plan. All Department 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 ORS Chapter 238. The PERS retirement allowance, payable monthly for life, may be selected from 12 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 may also 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, which are established by state statutes. A copy of the PERS annual financial report may be obtained by writing to the Fiscal Services Division, Public Employees Retirement System, 11410 SW 68$^{th}$ Parkway, Tigard, OR 97223.

Covered employees are required by state statute to contribute 6.0 percent of their salaries to the plan. Current law permits employers to pay employee contributions to the Retirement Fund. The Department 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 9.49 percent of each covered employee's salary. The Veterans' Loan and Home Programs payroll for employees covered by PERS for the years ended June 30, 2002, June 30, 2001, and June 30, 2000 were approximately $5,240,000, $5,130,000, and $5,220,000, respectively. Employer contributions to PERS for these employees for the years ended June 30, 2002, June 30, 2001, and June 30, 2000 were approximately $518,000, $524,000, and $528,000, respectively.

## 11. PRIOR PERIOD ADJUSTMENT

During the fiscal year ended June 30, 2002, the Department recorded a prior period adjustment of $42,361,426 due to clarification of ownership of the Loan Cancellation Life Insurance Contingency Fund. In July 2001 the Oregon Attorney General's office advised the Department on the treatment of monies held in this account and deemed them to be assets of the Oregon War Veterans' Fund. As a result, the Department is recognizing these monies as an asset thus restating beginning Net Assets, as of July 1, 2001. *(For additional information on this account see Note 5.)*

## 12. RISK FINANCING

The State of Oregon administers property and casualty insurance programs covering State government through its Central Services Fund *(Insurance Fund)*. The Insurance Fund services claims for direct physical loss or damage to State property; tort liability claims brought against the State, its officers, employees, or agents; worker's compensation; employee dishonesty; and faithful performance coverage for certain key positions required by law to be covered, and other key positions.

As a state agency, the Department participates in the Insurance Fund. The cost of servicing insurance claims and payments is covered by charging an assessment to each State entity based on its share of services provided in a prior period. The total statewide assessment of each coverage is based on independent biennial actuarial forecasts and administrative expenses, less any available fund balance in the Insurance Fund from the prior biennium.

## 13. SUBSEQUENT EVENTS

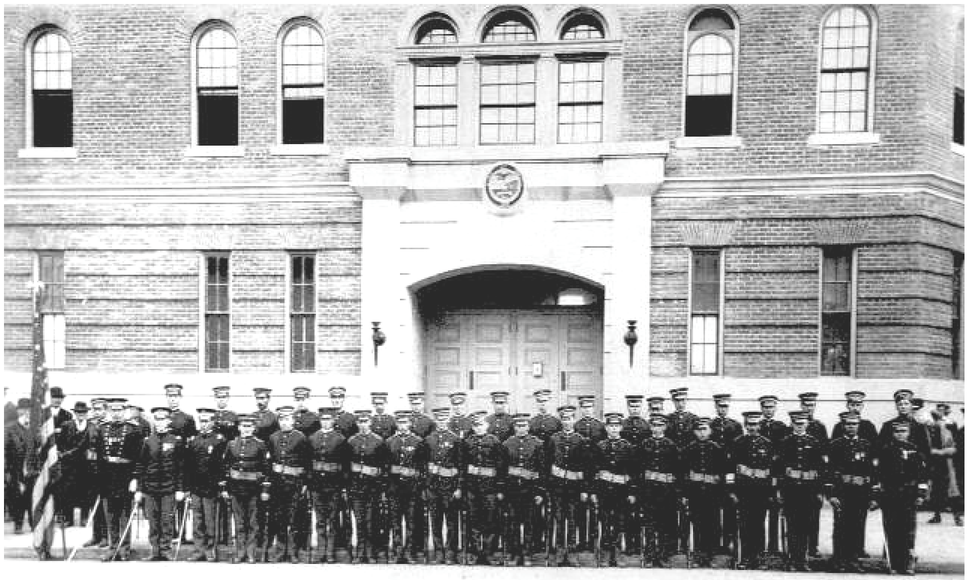
**October 1, 2002 Bond Call - Series 64, 75 ,76A, 77, 78A, 78B, 79A and 80A**

On October 1, 2002, the Department called the following general obligation bonds: $10,000,000 of Series 64, $3,220,000 of Series 75, $1,930,000 of Series 76A, $755,000 of Series 77, $555,000 of Series 78A, $555,000 of Series 78B, $1,070,000 of Series 79A, and $550,000 of Series 80A general obligation bonds.

## 14. CHANGE IN ACCOUNTING PRINCIPLES

During the fiscal year ended June 30, 2002 the Department implemented new accounting standards issued by the Governmental Accounting Standards Board. Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, as amended by Statement 37, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments: Omnibus,* establishes new financial reporting standards for state and local governments. These financial statement requirements present a significant change in the financial reporting model. In particular, the Department classified historical treasures and works of art which were specifically addressed for accounting treatment in the new accounting pronouncements. In the Veterans' Loan Program a cumulative effect of change in accounting principle for $75,000 was recorded which restated beginning Net Assets. In the Veterans' Home Program, a similar cumulative effect of change in accounting principle for $40,000 was recorded which also restated beginning Net Assets.

This page intentionally left blank



*Salem's first Oregon National Guard unit, Company M. Background is the old Salem Armory on Ferry Street. Date: 1912. Photo courtesy of Oregon State Archives and the Salem Public Library; photo source was the Statesman Journal newspaper.*

*Flag raised at the new Oregon State Capital, on January 13, 1941. Photo courtesy of the Oregon State Archives and the Salem Public Library's digital photograph collection of Ben Maxwell.*


*Victory Book Campaign in Salem. Books were collected for military personnel during World War II. Date: 1942. Photo courtesy of the Oregon State Archives and the Salem Public Library; photo source was the Oregon State Library, OSL0022.*

This page intentionally left blank

## *Fund Financial Statements*

***UNAUDITED***

STATE OF OREGON

DEPARTMENT OF VETERANS' AFFAIRS

**COMBINING STATEMENT OF NET ASSETS**

GENERAL FUND AND PRIVATE PURPOSE TRUST FUNDS

JUNE 30, 2002

| | Governmental Fund: General Fund | Private Purpose Trust Fund: Conservatorship Trust |
|---|---|---|
| **ASSETS** | | |
| **Current Assets** | | |
| Cash and Cash Equivalents | $ - | $ 21,134,939 |
| Investments | - | 2,532,749 |
| Securities Lending Cash Collateral | - | 1,489,978 |
| Receivables: | | |
| Accrued Interest | - | 35,436 |
| Contracts | - | 140,671 |
| Due from State General Fund | 151,707 | - |
| Due from Other Funds | 3,764 | - |
| Other | - | - |
| Supplies | 137 | - |
| Total Current Assets | 155,608 | 25,333,773 |
| **Noncurrent Assets** | | |
| Conservatorship Real Property | - | 3,790,966 |
| Conservatorship Personal Property | - | 767,400 |
| Total Noncurrent Assets | - | 4,558,366 |
| **TOTAL ASSETS** | $ 155,608 | $ 29,892,139 |
| **LIABILITIES** | | |
| **Current Liabilities** | | |
| Accounts Payable | $ 139,097 | $ - |
| Due to Other Funds | - | 30,511 |
| Obligations under Securities Lending | - | 1,489,978 |
| Compensated Absences Payable | 16,374 | - |
| Total Current Liabilities | 155,471 | 1,520,489 |
| **Noncurrent Liabilities** | | |
| Mortgages on Conservatorship Real Property | - | 1,158,969 |
| **TOTAL LIABILITIES** | 155,471 | 2,679,458 |
| **Net Assets Held in trust for Individuals** | - | 27,212,681 |
| **Fund Balance: Reserved for Prepaid Expenses** | 137 | - |
| **TOTAL NET ASSETS & FUND BALANCES** | 137 | 27,212,681 |
| **TOTAL LIABILITIES AND NET ASSETS & FUND BALANCE** | $ 155,608 | $ 29,892,139 |

| Private Purpose Trust Fund: Veterans' Trust Accounts | Total |
|---|---|
| $ 501,966 | $ 21,636,905 |
| - | 2,532,749 |
| 34,961 | 1,524,939 |
| | |
| - | 35,436 |
| - | 140,671 |
| - | 151,707 |
| - | 3,764 |
| 1,684 | 1,684 |
| - | 137 |
| 538,611 | 26,027,992 |
| | |
| - | 3,790,966 |
| - | 767,400 |
| - | 4,558,366 |
| $ 538,611 | $ 30,586,358 |
| | |
| $ - | $ 139,097 |
| - | 30,511 |
| 34,961 | 1,524,939 |
| - | 16,374 |
| 34,961 | 1,710,921 |
| | |
| - | 1,158,969 |
| | |
| 34,961 | 2,869,890 |
| 503,650 | 27,716,331 |
| - | 137 |
| | |
| 503,650 | 27,716,468 |
| | |
| $ 538,611 | $ 30,586,358 |

***UNAUDITED***

STATE OF OREGON

DEPARTMENT OF VETERANS' AFFAIRS

**COMBINING STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES & NET ASSETS**

GENERAL FUND & PRIVATE PURPOSE TRUST FUNDS

FOR THE FISCAL YEAR ENDED JUNE 30, 2002

| | Governmental Fund: General Fund | Private Purpose Trust Fund: Conservatorship Trust |
|---|---|---|
| **Revenues** | | |
| **Contributions** | | |
| Veterans' Benefits | $ - | $ 7,603,493 |
| Donations | - | - |
| Other | - | - |
| **Investment Income** | | |
| Interest Income | - | 471,747 |
| **TOTAL REVENUES** | - | 8,075,240 |
| **Expenditures** | | |
| Securitites Lending Investment Expenditure | - | 25,194 |
| Beneficiary Care | - | 8,475,388 |
| Other Expenditures | - | - |
| **Veterans' Services** | | |
| Personal Services | 648,139 | - |
| Services and Supplies | 58,142 | - |
| Special Payments | 496,776 | - |
| **TOTAL EXPENDITURES** | 1,203,057 | 8,500,582 |
| **Excess of Revenues over Expenditures** | (1,203,057) | (425,342) |
| **Other Financing Sources** | | |
| State Appropriations | 1,203,057 | - |
| Operating Interagency transfers in | - | - |
| Operating Transfer In/(Out) to Other Trust funds | - | - |
| Operating transfers out | - | - |
| Total Other Financing Sources | 1,203,057 | - |
| **Net Change in Fund Balances & Net Assets** | - | (425,342) |
| **Beginning Fund Balance, unreserved** | - | n/a |
| **Beginning Net Assets held in trust for individuals** | n/a | 27,638,023 |
| **Ending Fund Balance, unreserved** | - | n/a |
| **Ending Net Assets held in trust for individuals** | $ n/a | $ 27,212,681 |

| Private Purpose Trust Fund: Veterans' Trust Accounts | Total |
|---|---|
| $ - | $ 7,603,493 |
| 131,776 | 131,776 |
| 2,457 | 2,457 |
| 11,550 | 483,297 |
| 145,783 | 8,221,023 |
| 492 | 25,686 |
| - | 8,475,388 |
| 21,290 | 21,290 |
| - | 648,139 |
| - | 58,142 |
| - | 496,776 |
| 21,782 | 9,725,421 |
| 124,001 | (1,504,398) |
| - | 1,203,057 |
| 10,143 | 10,143 |
| - | - |
| (1,380) | (1,380) |
| 8,763 | 1,211,820 |
| 132,764 | (292,578) |
| n/a | - |
| 370,886 | 28,008,909 |
| n/a | - |
| $ 503,650 | $ 27,716,331 |

***UNAUDITED***

STATE OF OREGON

DEPARTMENT OF VETERANS' AFFAIRS

**SCHEDULE OF LEGISLATIVE AUTHORIZATION (NON-GAAP BUDGETARY BASIS)**

**COMPARED TO ACTUAL EXPENDITURES SUBJECT TO BUDGET**

GENERAL FUND

FOR THE BIENNIUM ENDED JUNE 30, 2003

| | 2001-2003 Budget | First Year Actual June 30, 2002 | Second Year Balance |
|---|---|---|---|
| General Fund: | | | |
| Veterans' Services Division - Appropriation | $ 2,529,198 | $ 1,197,801 | $ 1,331,397 |
| Total General Fund | $ 2,529,198 | $ 1,197,801 | $ 1,331,397 |

# *Statistical Section*

STATE OF OREGON
DEPARTMENT OF VETERANS' AFFAIRS
**COMPARATIVE STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET ASSETS**
PROPRIETARY FUNDS - VETERANS' LOAN PROGRAM only
FOR THE FISCAL YEARS 1993 - 2002

| | June 30, 2002 | June 30, 2001 | June 30, 2000 | June 30, 1999 |
|---|---|---|---|---|
| **REVENUES** | | | | |
| Mortgage Loan interest income | $ 43,749,526 | $ 50,861,579 | $ 57,259,424 | $ 68,967,805 |
| Contract interest income | 3,522,372 | 4,562,401 | 5,648,408 | 7,603,132 |
| Investment income | 35,956,850 ** | 57,521,901 ** | 38,492,961 ** | 48,834,865 ** |
| Gain on Sale of Foreclosed Property | 172,472 | 9,052 | 16,892 | 32,324 |
| Gain (Loss) on Sale of Investments | - ** | - ** | - ** | - ** |
| Loan Cancellation Life Insurance (LCLI) Processing Fees | 425,004 | 425,004 | 399,937 | 327,540 |
| Other Fees and Charges | 1,447,451 | 1,342,762 | 1,402,798 | 1,055,894 |
| Conservatorship Fees | 338,136 | 353,417 | 345,554 | 322,973 |
| **TOTAL REVENUES** | $ 85,611,811 | $ 115,076,116 | $ 103,565,974 | $ 127,144,533 |
| **EXPENSES** | | | | |
| Bond Interest Expense | $ 68,560,732 | $ 85,455,556 | $ 93,957,700 | $ 117,276,619 |
| Interest on Taxable Line of Credit | 580,883 | - | - | - |
| Salaries and Other Payroll Expenses | 6,974,557 | 6,932,307 | 6,886,703 | 6,829,801 |
| Bond Expenses | 868,243 | 925,722 | 819,421 | 952,673 |
| Securities Lending Investment Expense | 522,316 | 1,156,100 | 2,006,704 | 1,607,492 |
| Real Estate Owned Expense | 73,308 | 57,863 | 42,230 | 49,096 |
| Services and Supplies | 2,480,268 | 2,741,678 | 2,679,295 | 3,055,525 |
| Depreciation Expense | 538,555 | 453,159 | 360,840 | 317,751 |
| Bad Debt Expense | (906,906) | (1,078,111) | (1,227,068) | (3,346,273) |
| Other Expenses | 180,045 | 74,888 | 42,749 | 42,477 |
| **TOTAL EXPENSES** | $ 79,872,001 | $ 96,719,162 | $ 105,568,574 | $ 126,785,161 |
| Income/ (Loss) before Extraordinary or Special Items | $ 5,739,810 | $ 18,356,954 | $ (2,002,600) | $ 359,372 |
| Extraordinary or Special items: | | | | |
| Loss on Extinguishment of Debt | $ - | $ (17,231) | $ (11,888) | $ (12,271,433) |
| Gain from Litigation | - | - | - | 654,385 |
| **CHANGE IN NET ASSETS** | $ 5,739,810 | $ 18,339,723 | $ (2,014,488) | $ (11,257,676) |
| **NET ASSETS** | | | | |
| Beginning Net Assets * | $ 94,931,080 | $ 76,591,357 | $ 78,605,845 | $ 89,863,521 |
| Prior Period Adjustment | 42,361,426 | - | - | - |
| Cumulative Effect of Change in Accounting Principle | 75,000 | - | - | - |
| Beginning Net Assets, restated | $ 137,367,506 | $ 76,591,357 | $ 78,605,845 | $ 89,863,521 |
| Ending Net Assets, restated | $ 143,107,316 | $ 94,931,080 | $ 76,591,357 | $ 78,605,845 |

* Prior to the fiscal year ended June 30, 2002, the term "Retained Earnings" was used. It has the same meaning as "Net Assets".

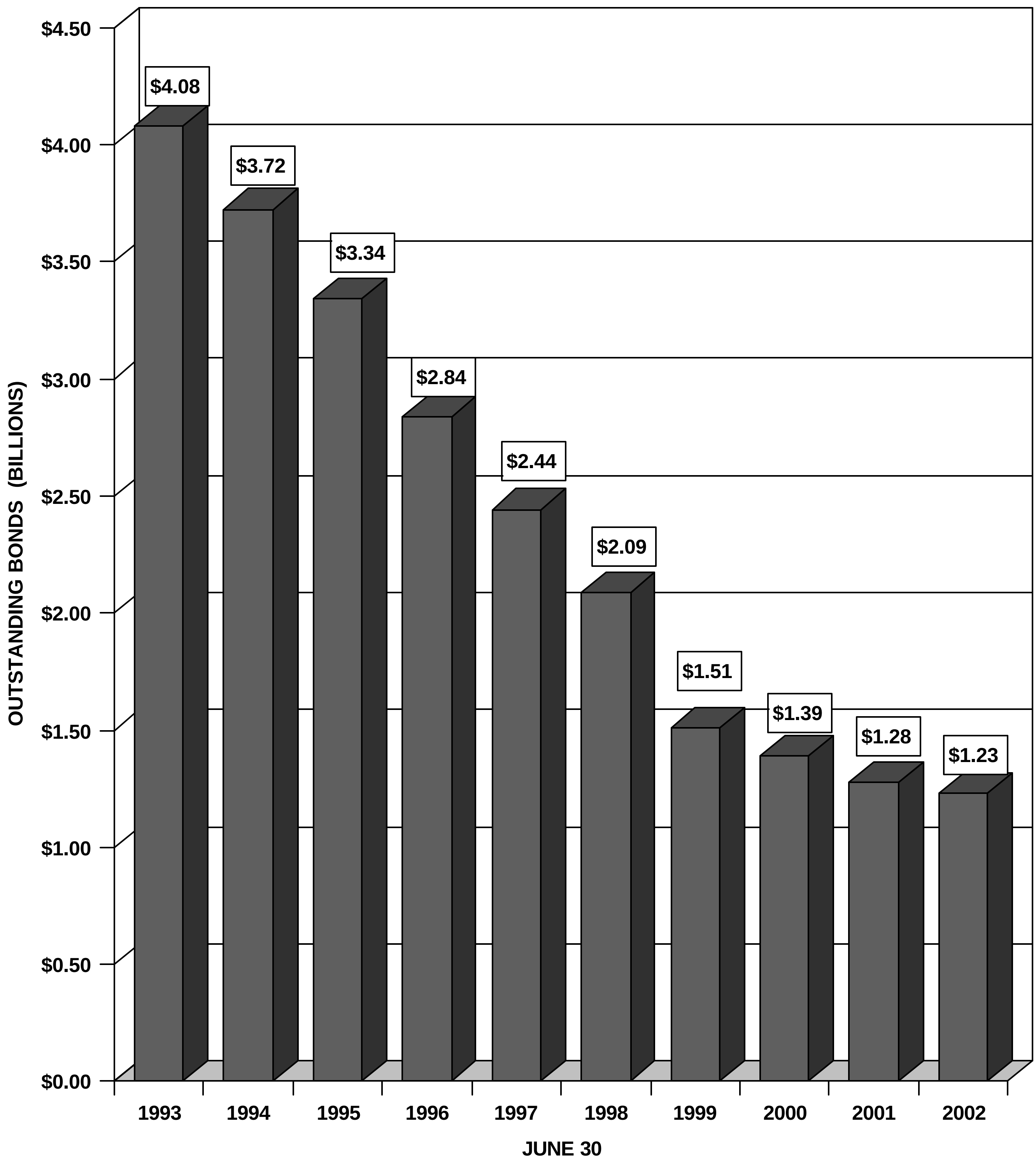
** Investment income includes change in fair value, as required by GASB Statement 31, beginning in the fiscal year ending June 30, 1998. Gain or loss on sale of investments is not reported under GASB Statement 31.

**Prepared without audit.**

| June 30, 1998 | | June 30, 1997 | June 30, 1996 | June 30, 1995 | June 30, 1994 | June 30, 1993 |
|---|---|---|---|---|---|---|
| $ 84,739,050 | | $ 101,149,885 | $ 119,299,277 | $ 137,627,560 | $ 164,565,886 | $ 201,176,801 |
| 10,413,658 | | 13,302,547 | 16,741,582 | 19,925,191 | 24,434,197 | 29,464,196 |
| 80,184,016 | ** | 88,584,123 | 91,392,885 | 106,181,662 | 101,205,742 | 101,338,575 |
| 106,330 | | 292,921 | 438,213 | 354,743 | 329,949 | 465,495 |
| - | ** | (771,619) | (1,265,290) | (2,295,346) | 29,299,910 | 3,398,096 |
| 433,763 | | 497,874 | 561,115 | 601,875 | 560,297 | 631,995 |
| 932,092 | | 884,689 | 742,319 | 459,468 | 463,561 | 477,882 |
| 334,784 | | 334,328 | 335,634 | 325,256 | 322,367 | 269,248 |
| $ 177,143,693 | | $ 204,274,748 | $ 228,245,735 | $ 263,180,409 | $ 321,181,909 | $ 337,222,288 |
| $ 153,677,775 | | $ 186,918,415 | $ 215,402,978 | $ 259,118,354 | $ 284,932,969 | $ 310,980,757 |
| - | | - | - | - | - | - |
| 6,952,431 | | 6,958,822 | 7,374,399 | 7,963,439 | 7,919,633 | 8,559,277 |
| 1,478,508 | | 1,774,314 | 2,310,443 | 2,677,130 | 2,665,458 | 2,911,507 |
| 1,588,540 | | 4,656,093 | - | - | - | - |
| 50,806 | | 79,340 | 170,172 | 232,218 | 240,393 | 358,231 |
| 3,473,771 | | 3,197,130 | 3,317,255 | 3,091,085 | 3,390,725 | 2,911,833 |
| 338,820 | | 235,128 | 417,097 | 522,733 | 1,233,864 | 796,225 |
| (2,934,825) | | (3,217,416) | (3,858,097) | (7,126,322) | - | - |
| 53,475 | | 32,406 | 23,258 | 20,052 | 12,800 | 17,209 |
| $ 164,679,301 | | $ 200,634,232 | $ 225,157,505 | $ 266,498,689 | $ 300,395,842 | $ 326,535,039 |
| $ 12,464,392 | | $ 3,640,516 | $ 3,088,230 | $ (3,318,280) | $ 20,786,067 | $ 10,687,249 |
| $ (3,870,466) | | $ (5,676,618) | $ (10,519,290) | $ (4,112,981) | $ - | $ - |
| - | | - | - | 3,283,024 | - | - |
| $ 8,593,926 | | $ (2,036,102) | $ (7,431,060) | $ (4,148,237) | $ 20,786,067 | $ 10,687,249 |
| $ 78,681,347 | | $ 80,717,449 | $ 88,148,509 | $ 92,296,746 | $ 71,510,679 | $ 60,823,430 |
| - | | - | - | - | - | - |
| 2,588,248 | | - | - | - | - | - |
| $ 81,269,595 | | $ 80,717,449 | $ 88,148,509 | $ 92,296,746 | $ 71,510,679 | $ 60,823,430 |
| $ 89,863,521 | | $ 78,681,347 | $ 80,717,449 | $ 88,148,509 | $ 92,296,746 | $ 71,510,679 |

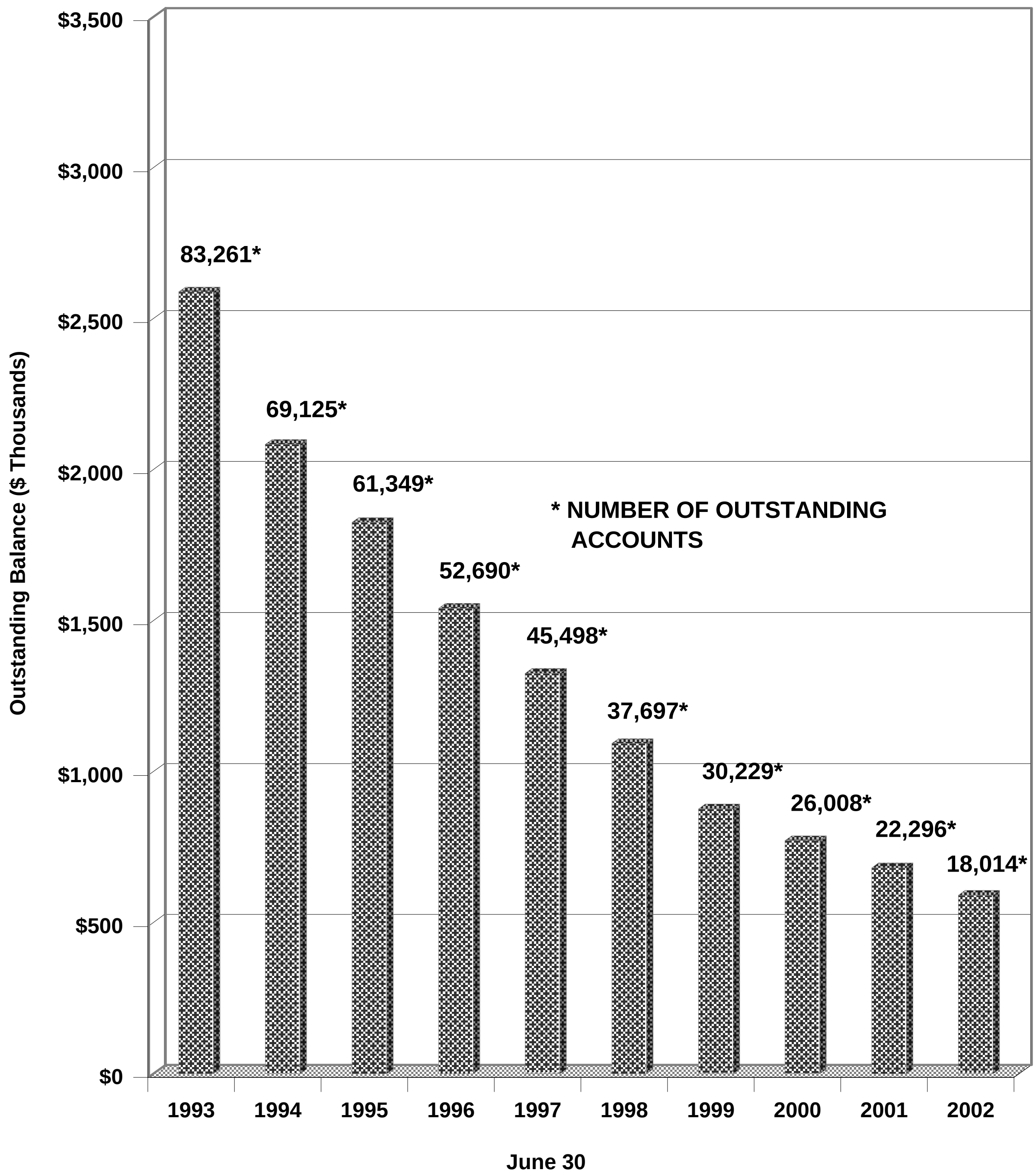
OREGON DEPARTMENT OF VETERANS' AFFAIRS

## COMPARATIVE SUMMARY OF BONDS OUTSTANDING




**Source: Financial Statements of the Oregon Department of Veterans' Affairs.**
**Prepared without audit.**

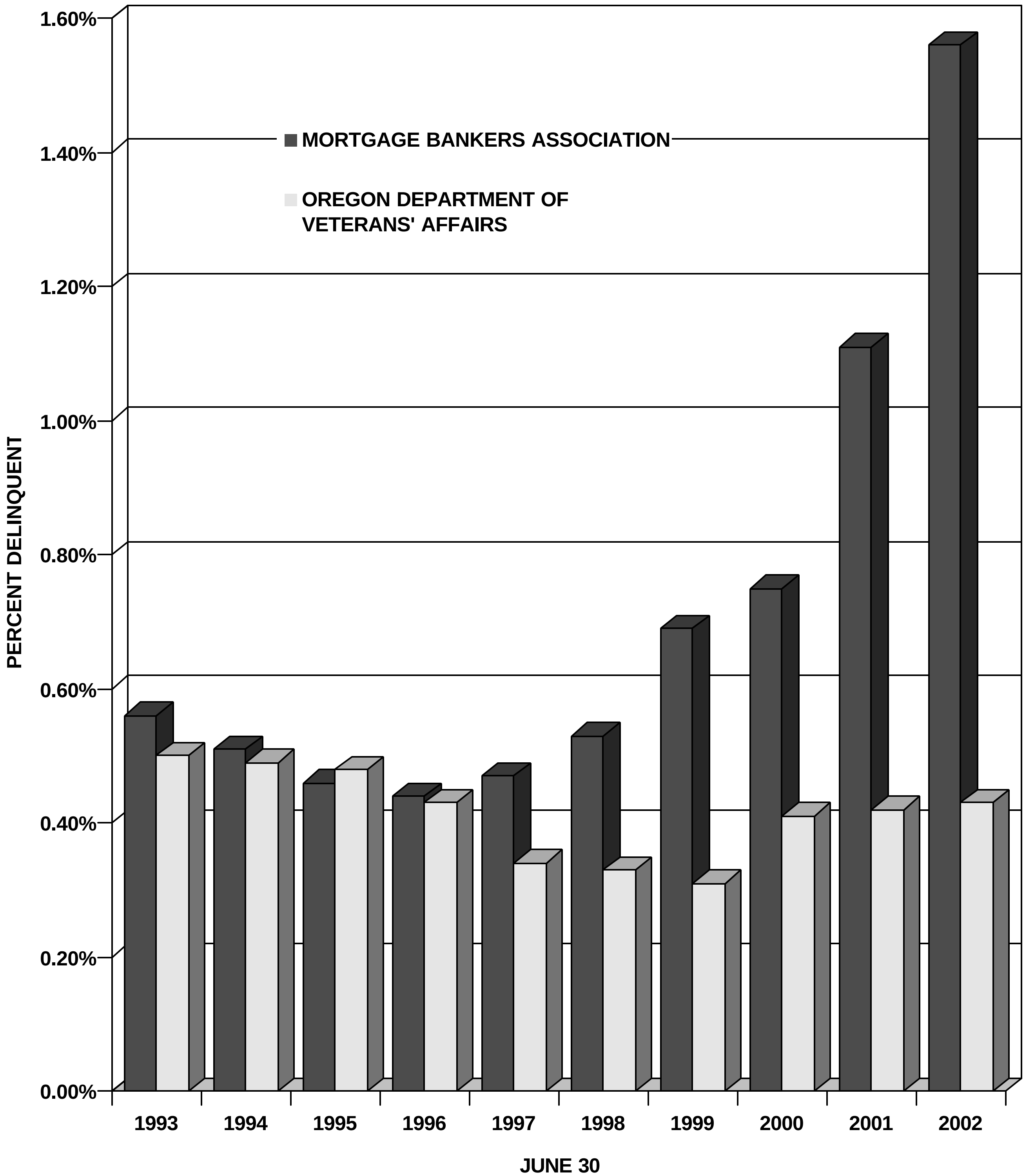
## OREGON DEPARTMENT OF VETERANS' AFFAIRS
## COMPARATIVE SUMMARY OF LOANS AND CONTRACTS OUTSTANDING




**Sources: Statistical Reports and Financial Statements of the Oregon Department of Veterans' Affairs. Prepared without audit.**

OREGON DEPARTMENT OF VETERANS' AFFAIRS

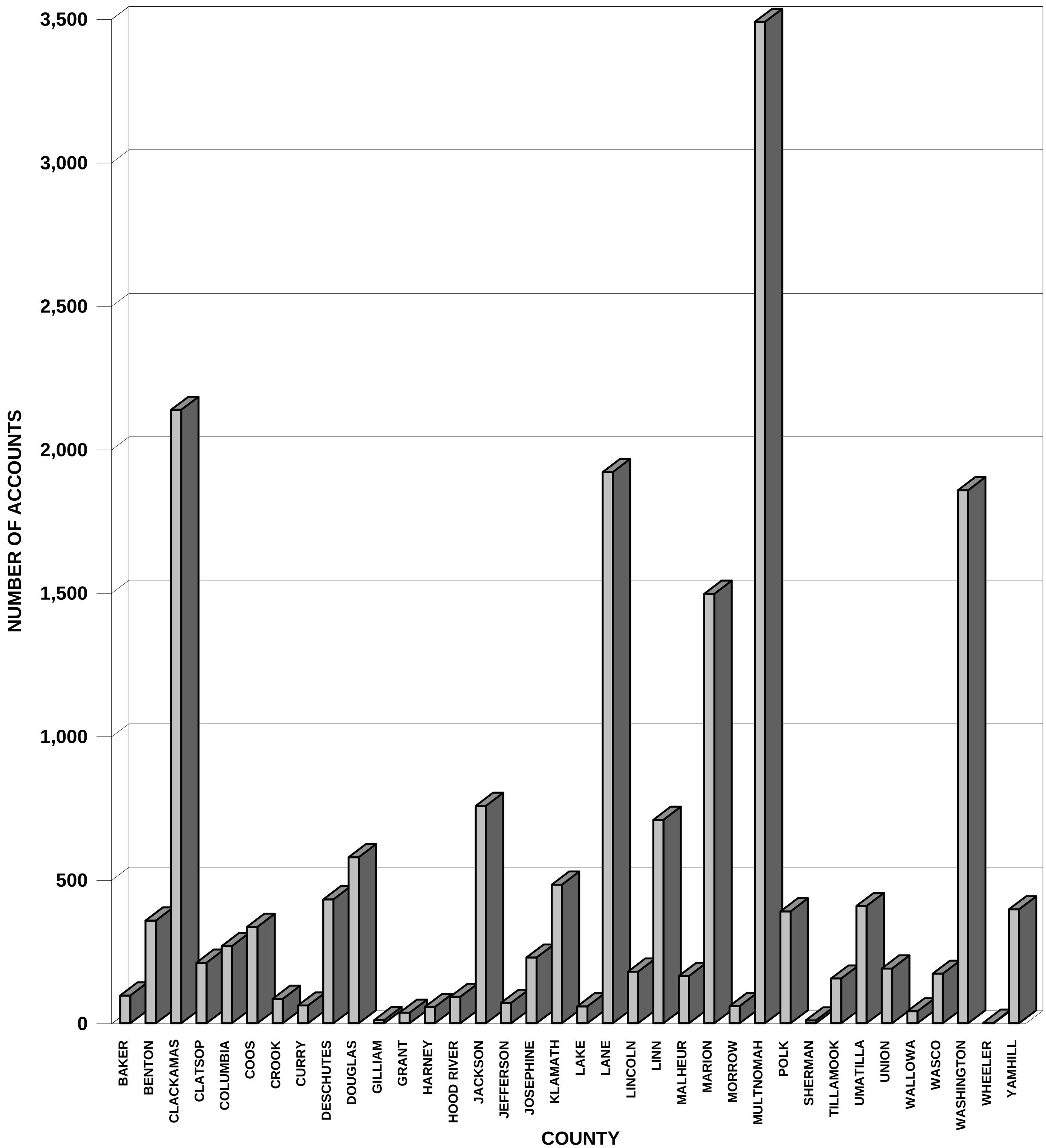
## COMPARATIVE SUMMARY OF 90+ DAY DELINQUENCIES




**Sources: National Delinquency Survey (Oregon, All Loans) - Mortgage Bankers Association and the Oregon Department of Veterans' Affairs.**
**Prepared without audit.**

OREGON DEPARTMENT OF VETERANS' AFFAIRS

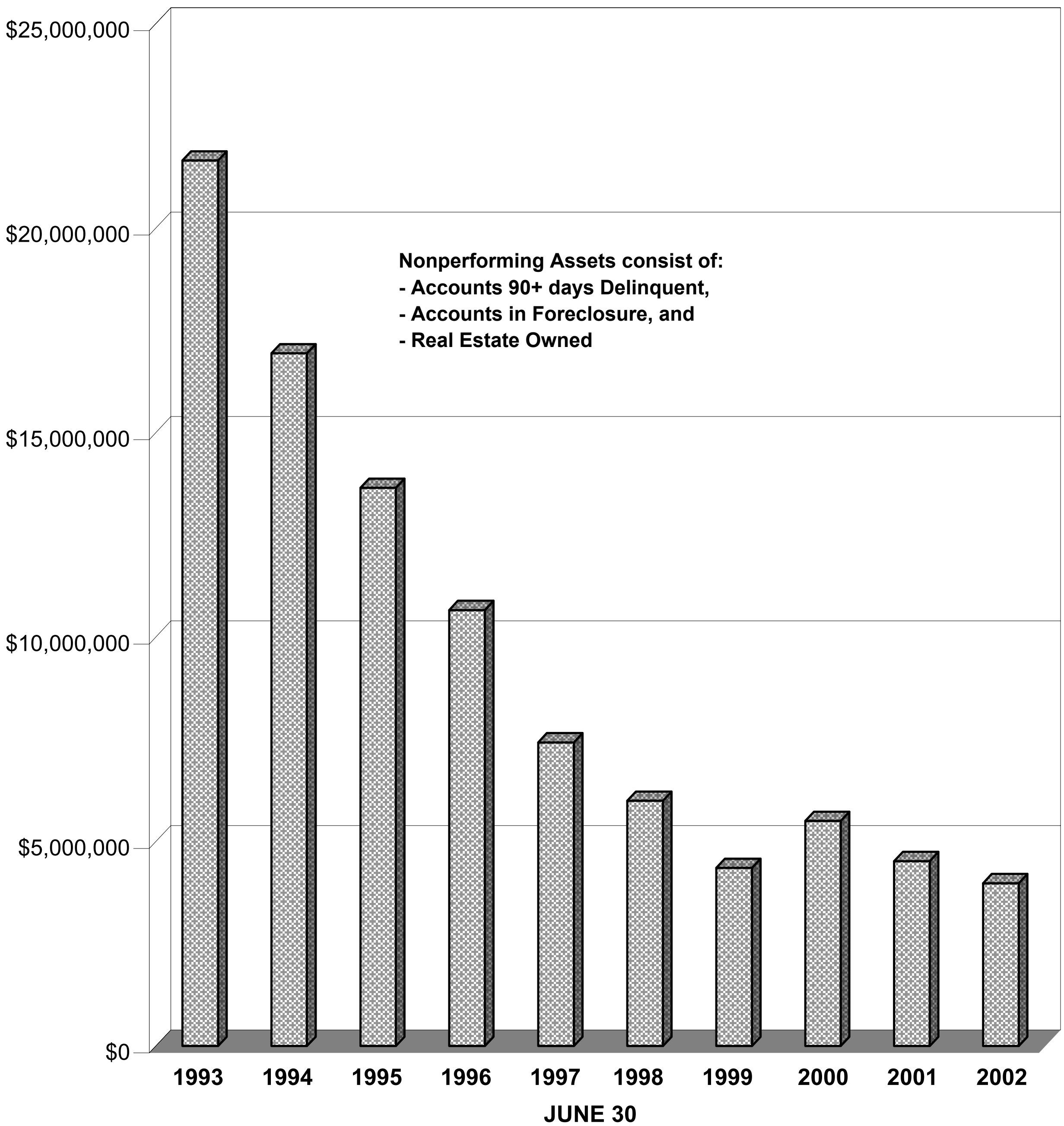
## OUTSTANDING LOAN AND CONTRACT ACCOUNTS BY COUNTY
## AS OF JUNE 30, 2002




**Source: Oregon Department of Veterans' Affairs.**
**Prepared without audit.**

OREGON DEPARTMENT OF VETERANS' AFFAIRS

## COMPARATIVE SUMMARY OF NONPERFORMING ASSETS




**Sources: Statistical Reports and Financial Statements of the Oregon Department of Veterans' Affairs. Prepared without audit.**

***Other Reports***

**This page intentionally left blank**

OFFICE OF THE
SECRETARY OF STATE
Bill Bradbury
Secretary of State

AUDITS DIVISION
Cathy Pollino
Director

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

*Auditing for a Better Oregon*

The Honorable Ted Kulongoski
Governor of Oregon
254 State Capitol
Salem, Oregon 97301-4047

Jon Mangis, Director
Department of Veterans' Affairs
700 Summer Street NE
Salem, Oregon 97301-1285

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

We have audited the basic financial statements of the enterprise funds of the state of Oregon, Department of Veterans' Affairs (department), as of and for the year ended June 30, 2002, and have issued our report thereon dated December 19, 2002. We conducted our audit in accordance with auditing standards generally accepted in the United States of America 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 the department's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, 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 the department'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 the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a condition in which the design or

255 Capitol Street NE • Suite 500 • Salem, Oregon 97310
INTERNET: Audits.hotline@state.or.us • http://www.sos.state.or.us/audits/audithp.htm

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 the internal control over financial reporting and its operation that we consider to be material weaknesses. However, we noted other matters involving the internal control over financial reporting, which we have reported to management of the department in a separate letter.

This report is intended solely for the information and use of the Oregon Department of Veterans' Affairs management, 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

Bill Bradbury
Secretary of State

December 19, 2002

The Oregon Department of Veterans' Affairs (ODVA) intends to comply with the Americans with Disabilities Act (The ADA), PL101-336. The ADA provides that no qualified person with a disability shall be kept from participation in (or be denied a benefit of) the services, programs, or activities of ODVA because of that disability. For additional information or how to file a complaint, please contact ODVA's ADA coordinator.

ADA Coordinator 503-373-2380


**Oregon Department of Veterans' Affairs**
700 Summer ST NE, Salem, OR 97301-1285
503-373-2373, FAX 503-373-2362, TDD 503-373-2217


This information is also available in alternate formats, upon request.