Oregon Department of Veterans' Affairs

Annual Financial Report
Enterprise Funds
For The Fiscal Years Ended
June 30, 2006 and June 30, 2005

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 Years Ended June 30, 2006 and June 30, 2005

Jim Willis
Director

Bruce Shriver, CPA
Chief Financial Officer

<u>Report Prepared By</u>

Carol Clevenberg
Ron Weisser, CPA
Aaron Hunter, CPA

With the assistance of the
Financial Administration Division,
Administrative Services Division,
and Public Information Section

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EVENTS FROM THIS PAST YEAR:

Annually, the department participates in various activities and events that honor and serve Oregon's veteran community. Below are a few of the events held in 2006.

Director Jim Willis addresses delegates at the Gold Star Wives Convention, in a ceremony held at the Willamette National Cemetery.

Oregon's "Merci Train" boxcar, a gift from France for WWII assistance, resides at its new home in North Bend at the Coos County Historical and Maritime Museum.

Bag pipes play as flags of our Nation's past are presented by various veterans service organizations during the massing of colors ceremony held at the Capitol mall in Salem.

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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

September 22, 2006

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 years ended June 30, 2006, and June 30, 2005. 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 four 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 **Other Reports** section includes the Independent Auditor's report on compliance and internal control over financial reporting.

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 – According to the Oregon State Office of Economic Analysis *(OEA)*, the second quarter of 2006 initial estimate of job growth was an increase of 1.4 percent on an annual rate. This is the twelfth consecutive quarterly growth in jobs but breaks a string of eight quarters of growth above 2.0 percent. On a year-over-year *(Y/Y)* basis, jobs increased in the second quarter by 3.6 percent. Y/Y growth has been above 2.0 percent since the second quarter of 2004.

The slower pace of job growth for the second quarter was spread across a number of sectors. Volatile sectors such as wood products and food had seasonally adjusted job declines. But the last job losses for wholesale trade and leisure and hospitality occurred in the first quarter of 2004. Job losses in government also contributed to the slower growth. Construction, while registering job growth of 2.6 percent for the second quarter of 2006, had its first quarter in two years of job growth below five percent. Retail trade job growth of 1.0 percent is the first quarter below three percent growth since the first quarter of 2004.

Other sectors still pushed forward with strong growth in the second quarter. Computer and electronic products, transportation equipment, information, financial activities, professional and business services all kept their relative job growth numbers of the past two years.

The most recent Blue Chip Job Growth rankings place Oregon 5th in the nation. For Y/Y job growth, between June 2005 and June 2006, jobs increased by 59,300 or 3.59 percent. A year ago, Oregon ranked 8th.

Future Outlook – The OEA forecasts employment to rise by 3.2 percent for 2006, the strongest yearly growth since 1997. This annual job growth is pushed up by the strong first quarter growth of 6.3 percent. The job growth of the remaining two quarters of 2006 is projected to average 1.0 percent. Job growth in 2007 is projected to be 1.3 percent, reflecting the slowing growth projected for the national economy. The economy continues to expand with 1.6 percent job growth in 2008. Additional OEA forecasts for specific sectors of Oregon's economy are discussed in the following paragraphs.

Total private nonfarm employment will increase in 2006, growing by 3.9 percent. The sector will continue to improve through 2008. Total private nonfarm employment will grow 1.3 percent in 2007 and 1.7 percent in 2008. Manufacturing will increase by 2.9 percent in 2006 and then reflect mild declines of 0.5 percent in 2007 and 0.3 percent in 2008. Job levels will still be below average job levels in 2000. Private non-manufacturing jobs will increase by 4.0 percent in 2006, 1.6 percent in 2007 and 2.0 percent in 2008.

Wood product manufacturing is projected to be down 0.5 percent in 2006 and then decline by 2.6 percent in 2007 and 2008.

The sector that contains semiconductors, computer and electronic products, will show gains of 3.0 percent for 2006. The job outlook is more uncertain with declines of 0.8 percent in 2007 and 0.1 percent in 2008. The outer years are projected to keep this sector in a no growth pattern.

Transportation equipment will increase by 6.2 percent in 2006. Job gains will give way to a slight decline in 2007 with a decrease of 0.5 percent. Employment will slightly decline with a loss of 0.8 percent in 2008.

Construction will increase jobs at a strong 9.7 percent in 2006. Job growth will decline with a 1.0 percent drop in 2007 before a milder job growth of 0.8 percent in 2008.

Trade job growth will have similar growth this year compared to 2005. Retail trade job growth will be stronger in 2006 at 3.5 percent and grow 1.4 percent in 2007 and 1.9 percent in 2008. Wholesale trade will be positive in 2006 with annual job growth of 2.5 percent followed by job gains of 1.0 percent in 2007 and 0.8 percent in 2008.

Professional and business services and health services will see some of the strongest growth. Professional and business services will grow 4.9 percent in 2006 followed by 3.5 percent growth in 2007 and 3.8 percent in 2008. Health services will increase 3.6 percent, 2.0 percent, and 2.6 percent on average for the same years.

Leisure and hospitality, which includes accommodations and food services, is expected to grow by 3.4 percent in 2006, 1.8 percent in 2007, and 2.0 percent in 2008.

Government employment is expected to increase by 0.2 percent in 2006 followed by growth of 1.1 percent in 2007 and 2008. State and local government jobs will continue mild growth as tax revenues have improved with the stronger economy.

Population growth is expected to be higher than the U.S. average, but slower than the growth experienced in the mid-1990s. Growth will be slightly higher than during the recession over the next three years, with increases of 1.4 percent for each year.

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. Both federal and State laws govern eligibility requirements on who may receive a veterans' home loan. As of June 30, 2006, this Program had approximately 6,600 mortgage loans and contracts outstanding, with a principal balance of approximately $271 million.

- The ***Veterans' Home Program*** provides professional medical, nursing, rehabilitative, social and other support services primarily 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 residents and had occupancy of approximately 135 residents at June 30, 2006. The Department owns the OVH and as of October 1, 2003, has contracted with Veterans Care Centers of Oregon *(VCCO)*, a non-profit organization, to provide the services needed by the residents.

The major issue related to the Department's client base is that the composition and essential necessities 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. In addition, with the ongoing conflicts in Iraq and Afghanistan, it is becoming increasingly important to help meet the needs of our younger returning veterans.

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. The Department of Administrative Services and the Oregon Legislature maintain budgetary controls.

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, 2006, the Veterans' Loan Program had approximately $0.96 billion in assets *(primarily consisting of loan and contract receivables, cash and cash equivalents, and investment securities)* and about $0.84 billion in liabilities *(primarily consisting of general obligation bonds)*. Revenues from the Department's home loan program are primarily 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, 2006, the Veterans' Home Program had assets of approximately $12.9 million consisting primarily of capital assets, receivables and cash and cash equivalents and approximately $1.0 million in liabilities consisting primarily of short-term payables.

Debt Administration - The Department, with the approval of the State Treasurer's office, has authority to issue general obligation bonds to fund the home 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	Aa3
Fitch Ratings	AA-
Standard & Poor's	AA-

As of June 30, 2006, the Department had approximately $764 million in outstanding debt. During fiscal year 2006, the Department issued approximately $49 million in bonds and retired approximately $87 million.

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, 2006, the Department's Enterprise funds cash, cash equivalents *(excluding securities lending collateral)*, and investments totaled approximately $624.6 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 that 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.

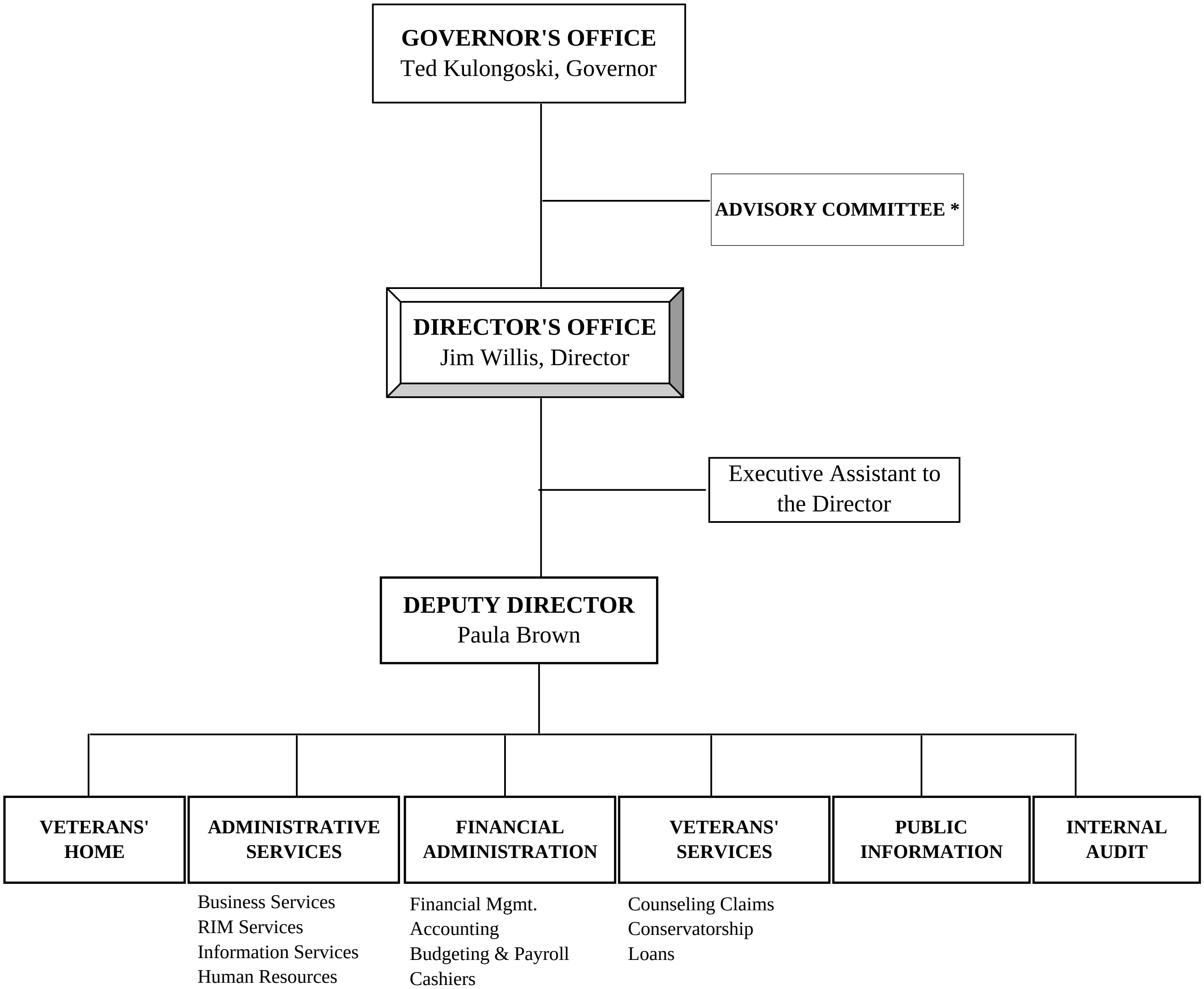
Independent Audit - The Secretary of State, Audits Division, has audited or contracted for the audit of the financial records, books of account, and transactions of the Department for the years ended June 30, 2006 and June 30, 2005. The auditors used generally accepted government auditing standards in 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 are very much appreciated.

Respectfully submitted,

Jim Willis
Director

Bruce W. Shriver
Chief Financial Officer



* 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
Evelyn F. Anderson	July 31, 2009	Irv Fletcher	December 31, 2006
Staryl C. Austin, Jr.	March 15, 2008	Robert Haltiner	March 15, 2008
Furlton M. Burns	March 15, 2008	Tino E. Ornelas	September 30, 2007
Walter R. Crews	March 15, 2008	Charles E. Schmidt	September 30, 2008
David Fairclo	March 15, 2008		

FINANCIAL SECTION

MERINA
& COMPANY, LLP
Certified Public Accountants and Consultants

CERTIFIED PUBLIC ACCOUNTANTS AND CONSULTANTS

PARTNERS
JOHN W. MERINA, CPA • KAMALA K. AUSTIN, CPA

INDEPENDENT AUDITORS' REPORT

The Honorable Theodore R. Kulongoski
Governor of Oregon
254 State Capitol
Salem, Oregon 97301-4047

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

We have audited the accompanying 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, 2006 and 2005, as listed in the accompanying table of contents. These financial statements are the responsibility of the State of Oregon, Department of Veterans' Affairs management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and *Government Auditing Standards*, issued by the Comptroller General of the United States of America. 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 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, 2006 and 2005, and the changes in its financial position, or, where applicable, its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

5499 AMY STREET • WEST LINN, OREGON 97068 • PHONE: (503) 723-0300 • FAX: (503) 723-9946 WWW.MERINACPAS.COM

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's Department of Veterans' Affairs, as of June 30, 2006 and 2005, the changes in its financial position, and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated September 22, 2006, on our consideration of the State of Oregon, Department of Veterans' Affairs internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* 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.

Our audit was conducted for the purpose of forming opinions on the basic financials statements that collectively comprise the Department's enterprise funds. The introductory section, other supplemental section, and statistical section as listed 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 audits of the basic financial statements and, accordingly, we express no opinion on them.

Merina & Company

Merina & Company, LLP
West Linn, Oregon
September 22, 2006

STATE OF OREGON
DEPARTMENT OF VETERANS' AFFAIRS
STATEMENT OF NET ASSETS
PROPRIETARY FUNDS
JUNE 30, 2006 AND JUNE 30, 2005

	Enterprise Funds			
	Veterans' Loan Program		Veterans' Home Program	
	June 30, 2006	June 30, 2005	June 30, 2006	June 30, 2005
ASSETS				
Current Assets				
Cash and Cash Equivalents	$ 70,310,067	$ 74,807,764	$ 1,474,963	$ 1,414,057
Cash and Cash Equivalents - Restricted	4,002,196	4,537,629	-	-
Securities Lending Cash Collateral	56,088,643	84,522,242	189,105	248,379
Investments - Restricted	100,656,772	-	-	-
Receivables:				
Accrued Interest	3,240,750	3,876,695	-	-
Loan Cancellation Life Insurance Premiums	170,762	185,655	-	-
Resident Care Related	-	-	707,089	818,414
Other	34,301	11,731	51,800	-
Due from Other Funds	138,755	494,164	-	5,405
Real Estate Owned	-	96,048	-	-
Prepaid Expenses	27,271	8,115	571	553
Total Current Assets	234,669,517	168,540,043	2,423,528	2,486,808
Noncurrent Assets				
Cash and Cash Equivalents - Restricted	419,260,547	428,157,516	-	-
Investments	2,564,209	-	-	-
Investments - Restricted	26,342,808	134,928,764	-	-
Mortgage Loans and Contracts Receivable (Net)	266,034,069	284,220,290	-	-
Resident Care Receivable (Net)	-	-	2,614	3,572
Notes Receivable	176,040	360,000	-	-
Other Receivable	1,931,151	481,294	-	-
Deferred Underwriter's Discount	1,991,927	1,929,928	-	-
Capital Assets:				
Building, Property and Equipment	9,949,641	9,945,155	12,540,540	12,517,677
Improvements Other than Buildings	-	-	7,250	7,250
Land	-	-	600,073	600,073
Works of Art and Historical Treasures	85,170	85,170	70,000	70,000
Accumulated Depreciation	(5,647,415)	(5,391,789)	(2,738,926)	(2,449,306)
Total Noncurrent Assets	722,688,147	854,716,328	10,481,551	10,749,266
TOTAL ASSETS	$ 957,357,664	$ 1,023,256,371	$ 12,905,079	$ 13,236,074
LIABILITIES				
Current Liabilities				
Accounts Payable	$ 301,996	$ 361,717	$ 705,069	$ 873,212
Line of Credit Payable	1,000,000	-	-	-
Loan Cancellation Life Insurance Premium Payable	135,470	137,379	-	-
Loan Cancellation Life Insurance Claims Payable	13,762	-	-	-
Due to Other Funds	-	-	119,104	493,755
Deposit Liabilities	1,637,899	1,674,166	652	361
Accrued Interest on Bonds	8,234,121	9,891,835	-	-
Obligations under Securities Lending	56,088,643	84,522,242	189,105	248,379
Compensated Absences Payable	392,315	360,289	583	4,936
Arbitrage Rebate Payable	212,771	-	-	-
Bonds Payable-Maturing Within One Year (Net)	62,250,115	62,727,149	-	-
Matured Bonds Payable	4,002,196	4,537,629	-	-
Total Current Liabilities	134,269,288	164,212,406	1,014,513	1,620,643
Noncurrent Liabilities				
Bonds Payable-Maturing After One Year (Net)	701,016,462	738,766,577	-	-
Claims and Judgments Payable	15,518	-	6,994	-
Arbitrage Rebate Payable	891,286	402,055	-	-
Total Noncurrent Liabilities	701,923,266	739,168,632	6,994	-
TOTAL LIABILITIES	836,192,554	903,381,038	1,021,507	1,620,643
NET ASSETS				
Invested in Capital Assets	4,387,396	4,638,536	10,478,937	10,745,694
Net Assets, Unrestricted	116,777,714	115,236,797	1,404,635	869,737
TOTAL NET ASSETS	$ 121,165,110	$ 119,875,333	$ 11,883,572	$ 11,615,431

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

Enterprise Funds	
TOTAL	
June 30, 2006	June 30, 2005
$ 71,785,030	$ 76,221,821
4,002,196	4,537,629
56,277,748	84,770,621
100,656,772	-
3,240,750	3,876,695
170,762	185,655
707,089	818,414
86,101	11,731
138,755	499,569
-	96,048
27,842	8,668
237,093,045	171,026,851
419,260,547	428,157,516
2,564,209	-
26,342,808	134,928,764
266,034,069	284,220,290
2,614	3,572
176,040	360,000
1,931,151	481,294
1,991,927	1,929,928
22,490,181	22,462,832
7,250	7,250
600,073	600,073
155,170	155,170
(8,386,341)	(7,841,095)
733,169,698	865,465,594
$ 970,262,743	$ 1,036,492,445
$ 1,007,065	$ 1,234,929
1,000,000	-
135,470	137,379
13,762	-
119,104	493,755
1,638,551	1,674,527
8,234,121	9,891,835
56,277,748	84,770,621
392,898	365,225
212,771	-
62,250,115	62,727,149
4,002,196	4,537,629
135,283,801	165,833,049
701,016,462	738,766,577
22,512	-
891,286	402,055
701,930,260	739,168,632
837,214,061	905,001,681
14,866,333	15,384,230
118,182,349	116,106,534
$ 133,048,682	$ 131,490,764

STATE OF OREGON
DEPARTMENT OF VETERANS' AFFAIRS
STATEMENT OF REVENUES, EXPENSES, AND
CHANGES IN FUND NET ASSETS
PROPRIETARY FUNDS
FOR THE FISCAL YEARS ENDED JUNE 30, 2006 AND JUNE 30, 2005

	Enterprise Funds			
	Veterans' Loan Program		Veterans' Home Program	
	June 30, 2006	June 30, 2005	June 30, 2006	June 30, 2005
OPERATING REVENUES				
Interest Income:				
Mortgage Loans	$ 17,561,219	$ 21,225,116	$ -	$ -
Contracts	806,376	1,188,374	-	-
Investment Income	28,209,288	18,013,534	73,604	24,217
Loan Cancellation Life Insurance Premiums	1,962,357	2,523,140	-	-
Loan Cancellation Life Insurance Processing Fee	180,000	220,834	-	-
Resident Revenue (Net)	-	-	9,809,017	8,674,907
Other Fees and Charges	1,941,079	947,834	1,946	2,825
Conservatorship Fees	354,808	334,340	-	-
Gain on Sale of Foreclosed Property	7,551	139,199	-	-
TOTAL OPERATING REVENUES	51,022,678	44,592,371	9,884,567	8,701,949
OPERATING EXPENSES				
Bond Interest	35,121,631	37,103,554	-	-
Interest on Taxable Line of Credit	525,600	159,267	-	-
Salaries and Other Payroll Expenses	5,239,879	4,793,870	80,684	512,025
Bond Expenses	1,129,971	1,324,123	-	-
Securities Lending Investment Expense	2,910,155	2,199,165	10,346	4,349
Real Estate Owned Expense	9,485	47,490	-	-
Services and Supplies	2,174,420	1,776,839	157,869	208,319
Claims Expense - Loan Cancellation Life Insurance	2,952,064	4,637,009	-	-
Veterans' Home Operations	-	-	9,120,185	7,596,750
Depreciation Expense	255,626	359,441	289,619	287,472
Bad Debt Expense	(918,401)	(1,104,080)	-	-
Other Expenses	332,471	170,187	-	-
TOTAL OPERATING EXPENSES	49,732,901	51,466,865	9,658,703	8,608,915
OPERATING INCOME (LOSS)	1,289,777	(6,874,494)	225,864	93,034
Transfers				
Net Transfers from Veterans' Home Trust Fund	-	-	25,483	71,091
Capital Contributions	-	-	16,794	7,250
CHANGE IN NET ASSETS	1,289,777	(6,874,494)	268,141	171,375
NET ASSETS - Beginning	119,875,333	126,749,827	11,615,431	11,444,056
NET ASSETS - Ending	$ 121,165,110	$ 119,875,333	$ 11,883,572	$ 11,615,431

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

Enterprise Funds	
TOTAL	
June 30, 2006	June 30, 2005
$ 17,561,219	$ 21,225,116
806,376	1,188,374
28,282,892	18,037,751
1,962,357	2,523,140
180,000	220,834
9,809,017	8,674,907
1,943,025	950,659
354,808	334,340
7,551	139,199
60,907,245	53,294,320
35,121,631	37,103,554
525,600	159,267
5,320,563	5,305,895
1,129,971	1,324,123
2,920,501	2,203,514
9,485	47,490
2,332,289	1,985,158
2,952,064	4,637,009
9,120,185	7,596,750
545,245	646,913
(918,401)	(1,104,080)
332,471	170,187
59,391,604	60,075,780
1,515,641	(6,781,460)
25,483	71,091
16,794	7,250
1,557,918	(6,703,119)
131,490,764	138,193,883
$ 133,048,682	$ 131,490,764

STATE OF OREGON
DEPARTMENT OF VETERANS' AFFAIRS
STATEMENT OF CASH FLOWS
PROPRIETARY FUNDS
FOR THE FISCAL YEARS ENDED JUNE 30, 2006 AND JUNE 30, 2005

	Enterprise Funds	
	Veterans' Loan Program	
	June 30, 2006	June 30, 2005
Cash Flows from Operating Activities:		
Receipts from Customers	$ 3,716,004	$ 14,394,320
Receipts from Other Funds for Services	1,117,481	662,719
Loan Principal Repayments	64,809,583	86,915,345
Loan Interest Received	19,112,707	22,709,860
Payments to Employees for Services	(5,209,467)	(5,215,957)
Payments to Suppliers	(5,074,148)	(17,008,349)
Payments to Other Funds for Services	(588,723)	(535,686)
Distributions to Other Governments	-	-
Loans Made	(46,904,555)	(30,973,966)
Other Receipts (Payments)	100,192	178,587
Net Cash Provided (Used) in Operating Activities	31,079,074	71,126,873
Cash Flows from Noncapital Financing Activities:		
Proceeds from Bond Sales	49,000,000	60,000,000
Taxable Line of Credit Proceeds	30,000,000	40,000,000
Principal Payments on Bonds	(87,725,434)	(141,740,217)
Principal Payments on Taxable Line of Credit	(29,000,000)	(40,000,000)
Interest Payments on Bonds	(36,816,494)	(39,649,513)
Interest Payments on Taxable Line of Credit	(525,600)	(159,267)
Bond Issuance Costs	(1,193,064)	(1,288,927)
Transfers from Other Funds	-	-
Net Cash Provided (Used) in Noncapital Financing Activities	(76,260,592)	(122,837,924)
Cash Flows from Capital and Related Financing Activities:		
Acquisition of Capital Assets	(4,486)	-
Proceeds from Sale of Capital Assets	-	826
Net Cash Provided (Used) in Capital and Related Financing Activities	(4,486)	826
Cash Flows from Investing Activities:		
Purchases of Investments	(211,333,124)	(266,427,899)
Proceeds from Sales or Maturities of Investments	217,041,836	285,530,634
Interest on Investments and Cash Balances	25,547,193	18,754,278
Investment Income from Securities Lending	2,910,155	2,199,165
Investment Expense from Securities Lending	(2,910,155)	(2,199,165)
Net Cash Provided (Used) in Investing Activities	31,255,905	37,857,013
Net Increase (Decrease) in Cash and Cash Equivalents	(13,930,099)	(13,853,212)
Cash and Cash Equivalents - Beginning	507,502,909	521,356,121
Cash and Cash Equivalents - Ending	$ 493,572,810	$ 507,502,909
Reconciled to Statement of Net Assets:		
Cash and Cash Equivalents - Current	$ 70,310,067	$ 74,807,764
Cash and Cash Equivalents - Current, Restricted	4,002,196	4,537,629
Cash and Cash Equivalents - Noncurrent, Restricted	419,260,547	428,157,516
Cash and Cash Equivalents - Ending (shown above)	$ 493,572,810	$ 507,502,909

Enterprise Funds		Enterprise Funds	
Veterans' Home Program		TOTAL	
June 30, 2006	June 30, 2005	June 30, 2006	June 30, 2005
$ 9,919,746	$ 8,520,130	$ 13,635,750	$ 22,914,450
-	-	1,117,481	662,719
-	-	64,809,583	86,915,345
-	-	19,112,707	22,709,860
(77,903)	(128,902)	(5,287,370)	(5,344,859)
(8,737,873)	(7,778,433)	(13,812,021)	(24,786,782)
(1,134,932)	(12,007)	(1,723,655)	(547,693)
-	-	-	-
-	-	(46,904,555)	(30,973,966)
1,946	2,825	102,138	181,412
(29,016)	603,613	31,050,058	71,730,486
-	-	49,000,000	60,000,000
-	-	30,000,000	40,000,000
-	-	(87,725,434)	(141,740,217)
-	-	(29,000,000)	(40,000,000)
-	-	(36,816,494)	(39,649,513)
		(525,600)	(159,267)
-	-	(1,193,064)	(1,288,927)
25,482	71,091	25,482	71,091
25,482	71,091	(76,235,110)	(122,766,833)
1,182	(7,250)	(3,304)	(7,250)
-	-	-	826
1,182	(7,250)	(3,304)	(6,424)
-	-	(211,333,124)	(266,427,899)
-	-	217,041,836	285,530,634
63,258	19,868	25,610,451	18,774,146
10,346	4,349	2,920,501	2,203,514
(10,346)	(4,349)	(2,920,501)	(2,203,514)
63,258	19,868	31,319,163	37,876,881
60,906	687,322	(13,869,193)	(13,165,890)
1,414,057	726,735	508,916,966	522,082,856
$ 1,474,963	$ 1,414,057	$ 495,047,773	$ 508,916,966
$ 1,474,963	$ 1,414,057	$ 71,785,030	$ 76,221,821
-	-	4,002,196	4,537,629
-	-	419,260,547	428,157,516
$ 1,474,963	$ 1,414,057	$ 495,047,773	$ 508,916,966

STATE OF OREGON
DEPARTMENT OF VETERANS' AFFAIRS
STATEMENT OF CASH FLOWS
PROPRIETARY FUNDS
FOR THE FISCAL YEARS ENDED JUNE 30, 2006 AND JUNE 30, 2005

(Continued from prior page)

	Enterprise Funds	
	Veterans' Loan Program	
	June 30, 2006	June 30, 2005
Reconciliation of Operating Income to Net Cash Provided (Used) by Operating Activities:		
Operating Income	$ 1,289,777	$ (6,874,494)
Adjustments to Reconcile Operating Income to Net Cash Provided (Used) by Operating Activities:		
Depreciation and Amortization of Capital Assets	255,626	359,441
Amortization of Bond Premium, Discount and Underwriter's Discount on Called Bonds	63,602	247,321
Bad Debt Expense	(918,401)	(1,104,080)
Interest Received on Investments Reported as Operating Revenue	(27,464,175)	(18,013,534)
Investment Expense	2,910,155	2,199,165
Interest Payments on Bonds Reported as Operating Expense	35,684,380	37,262,821
Bond Costs	1,029,220	1,076,802
Net Changes in Assets and Liabilities:		
Accounts and Interest Receivable	(7,678)	341,871
Due from Other Funds	355,409	-
Prepaid Items	(19,156)	11,334
Loans and Contracts Receivable	17,935,811	56,277,198
Accounts Payable	(166,725)	(778,351)
Due to Other Funds	-	-
Deposit Liabilities	99,203	178,585
Compensated Absences Payable	32,026	(57,206)
Total Adjustments	29,789,297	78,001,367
Net Cash Provided (Used) by Operating Activities	$ 31,079,074	$ 71,126,873
Noncash Investing and Capital and Related Financing Activities:		
Net Change in Fair Value of Investments	343,737	(1,472,614)
Capital Contributions	-	-
Foreclosed Property	-	563,724
Total Noncash Investing and Capital and Related Financing Activities	$ 343,737	$ (908,890)

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

Enterprise Funds		Enterprise Funds	
Veterans' Home Program		TOTAL	
June 30, 2006	June 30, 2005	June 30, 2006	June 30, 2005
$ 225,864	$ 93,034	$ 1,515,641	$ (6,781,460)
289,619	287,471	545,245	646,912
-	-	63,602	247,321
118,200	5,211	(800,201)	(1,098,869)
(73,604)	(24,217)	(27,537,779)	(18,037,751)
10,346	4,349	2,920,501	2,203,514
-	-	35,684,380	37,262,821
-	-	1,029,220	1,076,802
(7,761)	(154,941)	(15,439)	186,930
-	(5,405)	355,409	(5,405)
-	-	(19,156)	11,334
-	-	17,935,811	56,277,198
(212,968)	(84,867)	(379,693)	(863,218)
(374,651)	493,755	(374,651)	493,755
291	361	99,494	178,946
(4,352)	(11,138)	27,674	(68,344)
(254,880)	510,579	29,534,417	78,511,946
$ (29,016)	$ 603,613	$ 31,050,058	$ 71,730,486
-	-	343,737	(1,472,614)
-	7,250	-	7,250
-	-	0	563,724
$ -	$ 7,250	$ 343,737	$ (901,640)

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 – 408.090, and 408.360 – 408.490. 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.

In 1944 Oregon voters approved a constitutional amendment that authorized the creation of a Veterans' home and farm loan program. A year later the Department was established to administer this program. The Department's scope of services increased in 1949 when the Oregon Legislative Assembly authorized the Department, acting through the Director, to provide social services and rehabilitative relief by assisting veterans, dependents, and survivors in applying for state and federal benefits. In 1964 the Department's responsibilities were increased again as the Legislative Assembly authorized the Director of the Department to act as a conservator to certain veterans and their survivors through the management of their financial affairs. The most recent expansion of services came in 1993 when the Legislative Assembly authorized the Department to provide skilled nursing care to veterans residing at the Oregon Veterans' Home.

The Department's home loan program *(Veterans' Loan Program)* provides home purchase and home improvement loans at favorable interest rates to eligible veterans, within the limitations set forth in Oregon's Constitution and applicable laws. The Veterans' Loan Program is operated through earnings on program loans, which are 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 Veterans' Loan Program and the Veterans' Home Program are classified as proprietary fund activity. The basic financial statements and notes presented herein include only the proprietary fund activity of the Department. The Department has other programs, namely conservatorship duties and social services to veterans *(claims assistance & counseling)*, which are accounted for in other, non-proprietary funds. The financial activities of these programs have no material impact on proprietary fund activity and are 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.

The basic financial statements and notes presented 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. Therefore, private-sector standards of accounting and financial reporting are followed in accompanying proprietary fund financial statements to the extent that those standards do not contradict guidance of the GASB.

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. For budgetary purposes, these transactions are recognized when received or paid in cash as opposed to when they are susceptible to accrual.

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, resident-care related *(for Veterans' Home residents)* 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 fair market value. Cost is defined as the outstanding principal balance of the mortgage loan or contract on the date of foreclosure.

Prepaid Expenses

Prepaid expenses consist of postage on hand at year-end.

Capital Assets

Capital assets are recorded at cost. Depreciation is calculated using the straight-line method. 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. The Veterans' Building and the Oregon Veterans' Home are depreciated over their useful lives *(50 years and 40 years, respectively)*. Building-related assets are capitalized and then depreciated over the remaining estimated life of the building. Furniture, equipment, depreciable works of art, land improvements, and data processing hardware and software costing $5,000 or more are capitalized and then depreciated over a useful life of five years *(10 years for art work and land improvements)*.

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.

Excess Interest and Arbitrage Rebate Payable

The Department recognizes a liability in its financial records for any excess mortgage interest and investment earnings arising from the use of tax-exempt bond proceeds. The Department records the excess mortgage interest and investment earnings as a reduction of revenue.

Invested in Capital Assets

This is the Capital Asset component of Net Assets *(equity)* net of accumulated depreciation.

Operating Revenues and Expenses

Operating revenues include interest and fees on program loans, charges for resident-related care 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. All revenues and expenses not meeting this definition would be reported as nonoperating revenues and 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 is also included as miscellaneous bond expenses. Included in bond expenses are fees related to Series 73, 83, 84, and 85 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, 83, 84 and 85 variable rate bonds include Standby Bond Purchase Agreement commitment fees and remarketing agent fees *(See Note 7)*. These fees are payable quarterly in arrears.

Comparative Data and Reclassifications

Certain amounts presented in the prior year data have been reclassified in order to be consistent with the current year's presentation.

2. DEPOSITS AND INVESTMENTS

Deposits

The Veterans' Loan Program book balance of cash and cash equivalents as of June 30, 2006 was $70,310,067 for current, unrestricted cash and cash equivalents; $4,002,196 for current, restricted cash and cash equivalents; and $419,260,547 in restricted, noncurrent cash and cash equivalents *(combined total was $493,572,810)*. The bank balance of these Veterans' Loan Program cash balances was $469,247,632 as of the same date. The Veterans' Home Program book balance of cash and cash equivalents as of June 30, 2006 was $1,474,963 for current, unrestricted cash and cash equivalents. The bank balance of these Veterans' Home Program cash balances was $1,485,760 as of the same date. The combined book balance of cash and cash equivalents of all types for both programs was $495,047,773 at June 30, 2006.

A combined total of $470,733,392 *(Veterans' Loan Program with $469,247,632 and the Veterans Home Program with $1,485,760)* at June 30, 2006 was held in demand accounts with the State Treasurer and invested in the Oregon Short-Term Fund (OSTF). The OSTF is a cash and investment pool that is available for use by all state funds and eligible 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.

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 49 percent in U.S. government securities; 34 percent in short-term commercial paper; 15.4 percent in corporate notes; and the remainder in time certificates of deposit. 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 $24,567,363 with an insurance carrier as a reserve for loan cancellation life insurance. These monies are uncollateralized and are not insured under FDIC protection. The Department is required to keep on deposit an amount not less than the annual premium. At June 30, 2006 the Department estimated that required balance to be $3,888,000. That amount is shown as Cash and Cash Equivalents – Noncurrent, Restricted. The remainder of the balance at the insurance carrier is unrestricted and is disclosed as Cash and Cash Equivalents – Current. For additional information on these monies *(also called the Loan Cancellation Life Insurance Contingency Fund)* see Note 5.

The Department held $4,002,196 at the State's Fiscal Agent for redemption of the Department's bonds and coupons that have matured, but have not yet been redeemed. 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. This money is shown as Cash and Cash Equivalents – Restricted, a current asset. On June 30, 2005, the matured bonds payable balance was $4,537,629.

At June 30, 2005 the Department had a book balance of Cash and Cash Equivalents of $507,502,909, which was composed of $74,807,764 in current, unrestricted cash; $4,537,629 in current, restricted cash; and $428,157,516 in noncurrent, restricted cash. The bank balance for cash at June 30, 2005 was $507,518,253.

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. These funds must be invested, and the investments managed, as a prudent investor would, exercising reasonable care, skill and caution. Under an agreement with the State Treasury, the Department's investments do not include common stock. As of June 30, 2006, the State Treasurer invested the Department's funds primarily in U.S. government securities, commercial paper, corporate bonds, and investment agreements.

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 or transfer the agreement to a subsidiary or affiliate of the provider with a higher debt rating. In addition, Guaranteed Investment Contracts evidenced by contracts, rather than by securities, are uncategorized with regard to credit risk.

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 a current level of 105% of the repurchase price. The Repurchase Agreements have 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.

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, 2006. 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. The Guaranteed Investment Contracts and the Repurchase Agreements are presented on an amortized cost basis and their reported value is not materially different from fair value. As of June 30, 2006 the carrying value of the other investments below are equal to the fair value.

	Category 1	Category 2	Category 3	Carrying Amount
Investments				
Investments Held By State Treasurer				
U.S. Government And Agency Securities	$ 46,732,610	$ -	$ -	$ 46,732,610
Commercial Paper	8,241,932	-	-	8,241,932
Corporate Bonds	58,060,339	-	-	58,060,339
Total Investments Held By State Treasurer	$ 113,034,881	$ -	$ -	$ 113,034,881
Repurchase Agreements	6,232,040	-	-	6,232,040
Total By Risk category	$ 119,266,921	$ -	$ -	$ 119,266,921
Investments - Not Categorized				
Guaranteed Investment Contracts				$ 10,296,868
Investments Held By Broker-Dealers Under Securities Loans With Cash Collateral:				
U.S. Government And Agency Securities				55,143,822
Securities Lending Short-Term Collateral Investment Pool (Oregon Short-Term Fund Only):				56,227,312
Less:				
Securities Lending Amounts				(111,371,134)
Total Investments-Restricted				$ 129,563,789

The schedule below presents the schedule of interest rate risk and credit quality disclosure as of June 30, 2006.

Investment type	S&P Credit rating	Investment Maturities (in years): Less than 1 year	1-5 years	6-10 years	More than 10 years	Total Fair Value
U.S. Treasury Obligations	-	$	$	$	$	$
U.S. Agency Securities	AAA	41,799,460	4,933,151	-	-	46,732,611
Commercial Paper	A	8,241,932	-	-	-	8,241,932
Corporate Bonds	AAA	-	4,880,750	-	-	4,880,750
Corporate Bonds	AA	14,913,491	-	-	-	14,913,491
Corporate Bonds	BBB	5,853,330	2,564,209	-	-	8,417,538
Corporate Bonds	BB	19,900,000	-	-	-	19,900,000
Corporate Bonds	B	9,948,560	-	-	-	9,948,560
Guaranteed Investment Contracts and Repurchase Agreements	N/A	1,151,010	-	-	15,377,897	16,528,907
Total Investments		$ 101,807,783	$ 12,378,109	$ -	$15,377,897	$ 129,563,789

Concentration of Credit Risk:
Concentration of credit risk is the risk of loss attributed to the magnitude of investment in a single issuer. On June 30, 2006, 7.68% of the Department's total investments were in Ford Motor Credit Company, 6.36% in Black & Decker, 28.39% in Federal Home Loan Mortgage Corporation, 7.69% in Federal National Mortgage Association, 7.73% in Wal Mart Stores Inc, and 15.36% in General Motors Acceptance Corporation.

Restricted Assets

Included in Cash and Cash Equivalents and Investments are amounts designated as restricted. Restrictions on the Department's cash and investments can arise from Oregon's constitutional provision or enabling legislation, federal tax law relating to bond proceeds, bond covenants and from certain other contractual arrangements. The primary purpose of the restricted assets will be to meet upcoming debt service requirements. As of June 30, 2006, the Department had restricted assets of $552,826,532. As of June 30, 2005, the Department had restricted assets of $567,623,909.

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. 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. Both Oregon State Treasury and the broker-dealer borrowers maintain the right to terminate all securities lending transactions on demand. As a consequence, the maturities of investments made with cash collateral during the year generally do not match the maturities of their securities loans. On June 30, 2006, the Department had no securities on loan.

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. As of June 30, 2006, the fair value of all securities on loan from the OSTF was $1,027,628,515. The total cash collateral received for the securites on loan from OSTF was $1,048,759,710. The fair value of all investments made with the cash collateral received for those securities on loan was $1,047,819,815.

Total cash collateral received for securities on loan for the Department's proprietary funds was $56,277,748. Total fair value of all investments made with cash collateral was $56,227,312. Total securities on loan (Department's share of OSTF securities on loan) was $55,143,822.

Investment Income

The following table details the components of Investment Income for the years ended June 30, 2006 and June 30, 2005:

		June 30, 2006		June 30, 2005
Veterans' Loan Program:				
Investment Income: Accrual Basis	$	24,944,443	$	17,286,983
Securities Lending Revenue		2,910,155		2,199,165
Increase/(Decrease) in Fair Value of Investments		343,737		(1,472,614)
Investment Income	$	28,198,335	$	18,013,534
Veterans' Home Program:				
Investment Income: Accrual Basis	$	63,258	$	19,868
Securities Lending Revenue		10,346		4,349
Investment Income	$	73,604	$	24,217

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, 2006 is approximately $270 million. All mortgaged property is located within Oregon. 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 2006 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, 2006 from $5.80 million to $4.87 million, or approximately 1.80 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, 2006 and June 30, 2005.

		June 30, 2006		June 30, 2005
Loans Receivable	$	262,390,301	$	278,245,063
Contracts Receivable		8,519,768		11,775,227
Total Loans and Contracts Receivable	$	270,910,069	$	290,020,290
Less: Allowance for Principal Losses		(4,876,000)		(5,800,000)
Net Loans and Contracts Receivable	$	266,034,069	$	284,220,290

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, 2006, there were 173 non-amortizing accounts with an aggregate principal balance of approximately $16,977,000. This represents 6.38 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, 2006, the department made one new home loan to an eligible veteran employee. At June 30, 2006 the balance of existing home loans was $482,307 based on loans made to four employees. This amount represents less than 0.2% of the total loans and contracts receivable. At June 30, 2005 the balance of existing home loans was $130,793 based on loans made to three employees.

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, 2006, the Department provided this relief to some borrowers and deferred loan interest income of approximately $1,000. This interest amount was subsequently capitalized on these loans. In total, $100,700 in loans were restructured in this fashion. From these restructured loans the Department received approximately $2,600 in mortgage interest income during the fiscal year. During the year ended June 30, 2005, the Department provided this relief to some borrowers and deferred loan interest income of approximately $9,100. This interest amount was subsequently capitalized on these loans. In total, $321,900 in loans were restructured in this fashion. From these restructured loans the Department received approximately $8,200 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 years ended June 30, 2006 and June 30, 2005:

		June 30, 2006		June 30, 2005
Veterans' Loan Program				
Building, Property, and Equipment	$	9,949,642	$	9,945,155
Less: Accumulated Depreciation		(5,647,415)		(5,391,789)
Building, Property and Equipment, Carrying Value	$	4,302,227	$	4,553,366
Works of Art and Historical Treasures, Non-Depreciating	$	85,170	$	85,170
Total Capital Assets, Net	$	4,387,397	$	4,638,536
Veterans' Home Program				
Building, Property and Equipment	$	12,540,539	$	12,517,677
Improvements Other than Buildings		7,250		7,250
Works of Art and Historical Treasures, Depreciating		30,000		30,000
Less: Accumulated Depreciation		(2,738,925)		(2,449,306)
Depreciable Capital Assets, Carrying Value	$	9,838,864	$	10,105,621
Works of Art and Historical Treasures, Non-Depreciating		40,000		40,000
Land		600,073		600,073
Total Capital Assets, Net	$	10,478,937	$	10,745,694
Total Capital Assets, Net	$	14,866,334	$	15,384,230

The following table provides detail on the balances and activities of the Department's Proprietary fund capital assets for the year ended June 30, 2006:

	Beginning Balance	Increases	Decreases	Ending Balance
Capital Assets Not Being Depreciated:				
Land	$ 600,073	$ -	$ -	$ 600,073
Works of Art and Historical Treasures	125,170	-	-	125,170
Total Capital Assets Not Being Depreciated	725,243	-	-	725,243
Capital Assets Being Depreciated:				
Buildings	19,594,818	-	-	19,594,818
Improvements Other than Buildings	7,250			7,250
Property and Equipment	2,868,014	27,348	-	2,895,362
Works of Art and Historical Treasures	30,000	-	-	30,000
Total Capital Assets Being Depreciated	22,500,082	27,348	-	22,527,430
Less Accumulated Depreciation:				
Buildings	(5,241,811)	(364,875)	-	(5,606,686)
Improvements Other Than Buildings		(725)	-	(725)
Property and Equipment	(2,578,534)	(176,645)	-	(2,755,179)
Works of Art and Historical Treasures	(20,750)	(3,000)	-	(23,750)
Total Accumulated Depreciation	(7,841,095)	(545,245)	-	(8,386,340)
Total Capital Assets, Net	$ 15,384,230	$ (517,897)	$ -	$ 14,866,333

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 June 30. The balance of the LCLI Contingency Fund is disclosed in Note 2.

6. BONDS PAYABLE AND DEBT SERVICE

The table below provides a summary of general obligation bond transactions of the Department for the fiscal years ended June 30, 2005 and June 30, 2006:

Bonds Payable (Par) at June 30, 2004	$	882,145,000
Bonds Issued		60,000,000
Bonds Retired		(140,020,000)
Bonds Payable *(Par)* at June 30, 2005	$	802,125,000
Bonds Issued		49,000,000
Bonds Retired		(87,190,000)
Bonds Payable *(Par)* at June 30, 2006	$	763,935,000

Shown below are the components of net bonds payable as disclosed on the balance sheet for June 30, 2006:

		Current		Noncurrent		Total
Bonds Payable (Par)	$	62,245,000	$	701,690,000	$	763,935,000
Premium on Bonds Sold		63,734		34,611		98,345
Discount on Bonds Sold		(58,619)		(708,150)		(766,769)
Net Bonds Payable	$	62,250,115	$	701,016,462	$	763,266,577

The following schedule summarizes future debt service requirements to maturity as of June 30, 2006:

Fiscal Year	***Principal***	***Interest*** [(1)]	***Total***
2007	$ 62,245,000	$ 37,442,944	$ 99,687,944
2008	62,185,000	32,450,342	94,635,342
2009	42,075,000	27,381,040	69,456,040
2010	2,135,000	25,347,741	27,482,741
2011	2,045,000	25,237,151	27,282,151
2012-2016	12,165,000	124,539,303	136,704,303
2017-2021	393,275,000	75,113,849	468,388,849
2022-2026	37,110,000	39,933,939	77,043,939
2027-2031	44,220,000	29,864,978	74,084,978
2032-2036	45,880,000	19,507,152	65,387,152
2037-2041	53,740,000	8,136,044	61,876,044
2042-2043	6,860,000	372,019	7,232,019
TOTAL	$ 763,935,000	$ 445,326,502	$ 1,209,261,502

Shown below are the outstanding bond issues and their final maturities *(in fiscal years)* as of June 30, 2006:

		Original Coupon Rates				Final
Series	**Dated**	**From**	**To**	**Issued**	**Outstanding**	**Maturity**
LXI (61)	January 1, 1980	7.000	15.000%	300,000,000	60,000,000	2009
LXII (62)	April 1, 1980	8.500	11.250%	300,000,000	50,000,000	2008
LXIII (63)	July 1, 1980	7.300	20.000%	300,000,000	50,000,000	2008
73 [(1)]	December 1, 1985	6.875	7.000%	740,000,000	370,000,000	2019
75	October 1, 1995	3.900	6.000%	70,000,000	9,495,000	2027
76A	April 1, 1997	3.950	6.050%	40,000,000	9,165,000	2028
77	April 1, 1998	3.850	5.300%	40,000,000	18,390,000	2029
78A	March 1, 2000	4.000	5.500%	10,000,000	540,000	2023
78B	July 6, 2000	5.800	5.800%	10,000,000	1,590,000	2023
79A	March 1, 2000	4.550	6.000%	22,000,000	7,065,000	2032
80A	August 15, 2000	4.300	5.700%	35,000,000	15,155,000	2032
81	September 1, 2001	5.125	5.250%	60,150,000	33,665,000	2042
82	June 1, 2002	5.375	5.500%	60,000,000	29,330,000	2042
83[(1)]	December 15, 2004	Variable		30,000,000	30,000,000	2039
84[(1)]	June 29, 2005	Variable		30,000,000	30,000,000	2040
85[(1)]	June 21, 2006	Variable		49,000,000	49,000,000	2041
Total Bonds Outstanding as of June 30, 2006:					$ 763,935,000	

(1) $370,000,000 of Series 73E,F,G and H; $30,000,000 of Series 83; $30,000,000 of Series 84; and $49,000,000 of Series 85 are Variable Demand Rate bonds and are included at an assumed interest rate at June 30, 2006, of 3.94%, 3.97%, 3.97%, and 3.99% respectively. See Note 7 for further information on these bonds.

7. DEMAND BONDS

SERIES 73

Included in long-term debt at June 30, 2006 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)* on the applicable bonds 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 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, 2006. 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 following the last day of the applicable purchase period. Tender advances could be paid off earlier 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, 2006, the Department is required to pay a yearly commitment fee, which is payable quarterly in arrears, at a rate of 0.08 percent per annum, applied to the purchase commitment discussed above.

The present purchase commitments by the banks will generally remain in effect to the earlier of *(a)* June 30, 2007 for JP Morgan Chase Bank and November 30, 2015 for Bayerische Landesbank *(scheduled expiration dates)*, 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 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; or upon the occurrence of an event of default. However, Bayerische

Landesbank does have the option to terminate its purchase commitment obligations, at its sole discretion, as of June 30, 2007.

SERIES 83, 84, AND 85

Included in long-term debt at June 30, 2006 is $30,000,000 of State of Oregon, General Obligation, Veterans' Welfare Variable Rate Bonds, Series 83, $30,000,000 of State of Oregon, General Obligation, Veterans' Welfare Variable Rate Bonds, Series 84, and $49,000,000 of State of Oregon, General Obligation, Veterans' Welfare Variable Rate Bonds, Series 85. 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 Agent *(Bear, Stearns & Co. Inc.)* on the applicable bonds is authorized to use its best efforts to sell the repurchased bonds at face value by adjusting the interest rate on a weekly basis for Series 83 & 84 and on a daily basis for Series 85. The Remarketing Agent for such bonds will determine the interest rate borne by the 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, Dexia Credit Local, will commit to purchase any Series 83, 84, and 85 unremarketed bonds, 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, 2006. 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*) for the time period up to 91 days; at the bank's base rate plus 1% for the time period covering 92 days up to the day before the end of the purchase commitment period; at the bank's base rate plus 2% for the time period thereafter. If the tender advance is in default, interest would accrue at the bank's base rate plus 2.5%. 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 on the earliest to occur of (a) the date the applicable bonds are paid in full; (b) the conversion date of all or a portion of the applicable bonds to a fixed rate or indexed rate; or (c) the effective date of delivery of a substitute alternative liquidity facility. If repayment of any tender advances does not occur within the specified timeframes contained in the SBPA, a default would have occurred.

The bank's present purchase commitment consists of the payment of the purchase price equal to the principal of and up to 34 days of accrued interest calculated at a rate of 12 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 the bank may be reduced from time to time upon occurrence of certain events specified in the SBPA. As of June 30, 2006, the Department is required to pay a yearly commitment fee, which is payable quarterly in arrears, at a rate of .0925 percent per annum, applied to the purchase commitment defined above.

The present purchase commitment by the bank will generally remain in effect to the earlier of *(a)* June 28, 2013 *(scheduled termination date)*, unless extended at the option of the bank; (b) the date in which all of the applicable bonds are no longer outstanding; *(c)* the business day prior to the conversion of all or a portion of the applicable bonds to a fixed or indexed interest rate; (*d)* 30 days following the Department's receipt from the bank of a notice to terminate its purchase commitment arising from an event of default; *(e)* the business day prior to the effective date of delivery of a substitute alternative liquidity facility; (f) the date on which the purchase commitment with respect to the applicable bonds has been terminated in accordance with the SBPA; and (g) upon the effective date of an occurrence of a special event of default.

8. SHORT TERM DEBT

The Department entered into a revolving line of credit agreement on December 27, 2005 to help preserve certain refunding opportunities that may be used to finance veterans' housing loans. The revolving line of credit is with KeyBank National Association and interest rates on draws are based on a LIBOR index *(London InterBank Offered Rate)* or the bank's prime rate. Draws on the revolving line of credit are used to refund certain bonds. A subsequent long term bond issue then refunds the draws. The borrowing limit on the revolving line of credit cannot exceed $30 million. As of June 30, 2006, the Department had an outstanding balance of $1,000,000 from its revolving line of credit.

Beginning Balance	Issued	Repaid	Ending Balance
$ 0	$ 30,000,000	$ 29,000,000	$ 1,000,000

9. INTERFUND TRANSACTIONS

At June 30, 2006, the Veterans' Loan Program had outstanding interfund receivables of $138,755, which consisted of $119,104 due from the Veterans' Home Program for allocation of department expenses related to the operation of the Oregon Veterans' Home and $19,651 due from the Department's Conservatorship Trust Fund. The balances are shown as a "Due from Other Funds" on the Statement of Net Assets.

At June 30, 2005, the Veterans' Loan Program had outstanding interfund receivables of $494,164, which consisted of $493,755 due from the Veterans' Home Program for allocation of department expenses related to the operation of the Oregon Veterans' Home and $409 due from the Department's Conservatorship Trust Fund. The Veterans' Home Program had outstanding receivables of $5,405 due from the Veterans' Home Trust Fund related to capital improvements made at the Oregon Veterans' Home.

10. EMPLOYEE RETIREMENT PLAN

The 2003 Oregon Legislature created the Oregon Public Service Retirement Plan (OPSRP). Public employees hired on or after August 29, 2003 become part of OPSRP, unless membership was previously established in the Oregon Public Employee's Retirement System (PERS). OPSRP is a hybrid (defined contribution/defined benefit) pension plan with two components: the Pension Program (defined benefit) and the Individual Account Program (defined contribution). Beginning January 1, 2004, PERS member contributions were deposited into the Individual Account Program (IAP) portion of OPSRP. PERS members retain their existing PERS accounts, but any future member contributions will be deposited in the member's

IAP account, not into the member's PERS account. A copy of the Oregon Public Employees Retirement System annual financial report may be obtained from Fiscal Services Division, PERS, PO Box 23700, Tigard, Oregon 97281-3700.

<u>Oregon Public Employee's Retirement System (PERS)</u>
The Department's employees who were plan members before August 29, 2003 participate in the Oregon Public Employee's Retirement System (PERS), a cost-sharing multiple-employer defined benefit pension plan. PERS is administered by the Public Employees Retirement Board under the guidelines of Oregon Revised Statutes, chapter 238. The PERS retirement allowance, payable monthly for life, may be selected from several retirement benefit options. Options include survivorship benefits and lump sum payments. PERS also provides death and disability benefits.

The Department is required by statute to contribute actuarially computed amounts as determined by PERS (the agency). Rates are subject to change as a result of subsequent actuarial valuations. The rate of each covered employee's salary for fiscal year 2006 was 4.71 percent. Employer contributions for the years ending June 30, 2006, 2005, and 2004 were $160,266, $162,536 and $287,918, respectively, equal to the required contributions for each year.

<u>Oregon Public Service Retirement Plan (OPSRP)</u>
The Pension Program, a cost-sharing multiple-employer defined benefit pension plan, is the defined benefit portion of Oregon Public Service retirement Plan (OPSRP). The Pension Program is administered by the Public Employees Retirement Board under the guidelines of Oregon Revised Statutes, chapter 238A. The Pension Program monthly pension benefit is payable for life and, after the death of the member, payable to the designated beneficiary at either the same amount or one-half of the amount, depending on the option the member chose at retirement. If the monthly pension benefit is less than $200, or the monthly death benefit payable to the beneficiary of a deceased member is less than $200, a lump sum payment that represents the actuarial equivalent of the present value of the pension or death benefit will be paid to the member or the deceased member's beneficiary.

The Department is required by statute to contribute actuarially computed amounts as determined by PERS (the agency). Rates are subject to change as a result of subsequent actuarial valuations. The rate of each covered employee's salary for fiscal year 2006 was 8.04 percent. Employer contributions for the year ending June 30, 2006 and 2005 were $129,835 and $27,964, respectively, equal to the required contributions for each year.

The Individual Account Program (IAP) is the defined contribution portion of OPSRP. The IAP is administered by the Public Employees Retirement Board under the guidelines of Oregon Revised Statutes, chapter 238A. It is applicable to all new hires on or after August 29, 2003 and for active PERS members as of January 1, 2004. Covered employees are required by State statute to contribute 6.0 percent of their salary to the plan. Current law requires employers that had been paying the member contributions into PERS to pay employee contributions to the IAP until at least December 31, 2005. Employer contributions for the years ending June 30, 2006 and 2005 were $204,163 and $207,051 respectively, equal to the required contributions for each year.

11. LEASE COMMITMENT AND RECEIVABLES

The Department leases office space to state agency tenants at its headquarters in Salem. For the fiscal year ended June 30, 2006, the total rental income received from tenants was $631,539. Lease agreements were signed with two tenant agencies in June of 2004 with no change in the lease payment. Each lease term is for three years and expires on June 30, 2007. A lease with a third tenant agency began in July 2005 and will expire on June 30, 2007. A new lease with a fourth tenant agency began in September 2005 and will expire on June 30, 2007. The total future rental income for all four leases is $653,166. Future rental income may increase to a higher rental rate due to inflation. The approximate historical cost of this office space is $2,186,054 with a carrying value of $1,267,005 *(historical cost less accumulated depreciation of $919,049)*.

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 for the cost of servicing is based on independent biennial actuarial forecasts and administrative expenses, less any available fund balance in the Insurance Fund from the prior biennium.

Risk Management Division of the Department of Administrative Services is the State's manager for self-insurance, insurance and risk control. Risk Management Division investigates, evaluates and resolves claims for damage to state property and for loss or injury to the public arising out of state activities. Division staff consult with and advise state agencies on claim related loss control issues. State agencies are responsible for informing Risk Management Division in a timely fashion when they become aware that property or liability damage has occurred.

During the fiscal years ended June 30, 2006 and June 30, 2005 there has been no significant reductions in insurance coverage in any risk category. Also, for the past six fiscal years *(July 1, 2000 through June 30, 2006)* there have been no claims that exceeded the Department's property or liability coverage.

13. COMPARATIVE DATA/RECLASSIFICATIONS

Comparative total data for the prior year have been presented only for individual enterprise funds in the fund financial statements in order to provide an understanding of the changes of financial position and operations of these funds. Also, certain amounts presented in prior year data have been reclassified in the current year. In the Veterans' Home Program, if these amounts had been presented comparatively to the prior year, it would increase Salaries & Other Payroll Expenses by $551,148, increase Services & Supplies expense by $197,584, and decrease Veterans' Home Operations expense by $748,732. In the Veteran's Loan Program, if these amounts had been presented comparatively to the prior year, it would decrease Salaries & Other Payroll Expenses by $551,148, Services & Supplies expense by $197,584, and Other Fees & Charges revenue by $748,732.

14. ALLOWANCES IN PROPRIETARY FUND VETERANS' HOME PROGRAM

Revenues in the Veterans' Home Program are reported net of discounts and allowances in the accompanying financial statements. The amounts netted against Resident Related Revenues are $118,200 for fiscal year 2006 and $5,211 for fiscal year 2005.

15. SUBSEQUENT EVENTS

The following subsequent event occurred after June 30, 2006:

On September 27, 2006, the Department elected to draw $11,030,000 from the revolving line of credit with Key Bank National Association.

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OTHER SUPPLEMENTAL SECTION

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Governmental Funds

General Fund
The General Fund accounts for general governmental operations that are financed by legislatively approved appropriations funded from general revenues. For the Department, general government activities are related to services to veterans. Specifically, these activities include counseling and other services to veterans and partial funding of the Department's conservatorship responsibilities. In addition, the General Fund makes available educational aid to certain veterans, as well as financial assistance and training to County Veterans' Service Offices and Veterans' Organizations.

Special Revenue Funds
Special revenue funds are used to account for specific revenues that are legally restricted to expenditure for particular purposes.

Veterans' Trust Accounts - The Department accepts donations that can be used to operate the Oregon Veterans' Home in Wasco County, Oregon, and to provide its residents with amenities to enhance their quality of life. The fund is composed of donations and interest earnings. In addition, the Department maintains other veteran-related trust accounts.

UNAUDITED
STATE OF OREGON
DEPARTMENT OF VETERANS' AFFAIRS
BALANCE SHEET
GOVERNMENTAL FUNDS
JUNE 30, 2006 and JUNE 30, 2005

	General Fund		Special Revenue Fund	
			Veterans' Home Trust	
	June 30, 2006	June 30, 2005	June 30, 2006	June 30, 2005
ASSETS				
Current Assets				
Cash and Cash Equivalents	$ -	$ -	$ 591,656	$ 480,023
Securities Lending Cash Collateral	-	-	75,381	84,870
Receivables:				
Due from State General Fund	462,450	139,073	-	-
Due from Other Funds	-	-	3,512	3,210
Prepaid Items	103	270	-	-
Total Current Assets	462,553	139,343	670,549	568,103
TOTAL ASSETS	$ 462,553	$ 139,343	$ 670,549	$ 568,103
LIABILITIES				
Current Liabilities				
Accounts Payable	$ 462,450	$ 139,073	$ -	$ -
Due to Other Funds/Agencies	-	-	-	5,405
Obligations under Securities Lending	-	-	75,381	84,870
Total Current Liabilities	462,450	139,073	75,381	90,275
TOTAL LIABILITIES	$ 462,450	$ 139,073	$ 75,381	$ 90,275
FUND BALANCES				
Reserved for Prepaid Items	$ 103	$ 270	$ -	$ -
Unreserved, Undesignated Fund Balance	-	-	595,168	477,828
TOTAL FUND BALANCES	$ 103	$ 270	$ 595,168	$ 477,828
TOTAL LIABILITIES AND FUND BALANCES	$ 462,553	$ 139,343	$ 670,549	$ 568,103

	Special Revenue Fund		Governmental Funds	
	Other Veterans' Trust Accounts		TOTAL	
	June 30, 2006	June 30, 2005	June 30, 2006	June 30, 2005
	$ 94,049	$ 107,221	$ 685,705	$ 587,244
	11,970	18,945	87,351	103,815
	-	-	462,450	139,073
	-	-	3,512	3,210
	-	-	103	270
	106,019	126,166	1,239,121	833,612
	$ 106,019	$ 126,166	$ 1,239,121	$ 833,612
	$ -	$ -	$ 462,450	$ 139,073
	-	-	-	5,405
	11,970	18,945	87,351	103,815
	11,970	18,945	549,801	248,293
	$ 11,970	$ 18,945	$ 549,801	$ 248,293
	$ -	$ -	$ 103	$ 270
	94,049	107,221	689,217	585,049
	$ 94,049	$ 107,221	$ 689,320	$ 585,319
	$ 106,019	$ 126,166	$ 1,239,121	$ 833,612

UNAUDITED

STATE OF OREGON

DEPARTMENT OF VETERANS' AFFAIRS

COMBINED STATEMENT OF REVENUES, EXPENDITURES

AND CHANGES IN FUND BALANCES

GOVERNMENTAL FUNDS

FOR THE FISCAL YEARS ENDED JUNE 30, 2006 and JUNE 30, 2005

	General Fund		**Special Revenue Fund** Veterans' Home Trust	
	June 30, 2006	June 30, 2005	June 30, 2006	June 30, 2005
Revenues				
Donations	$ -	$ -	$ 124,966	$ 112,702
Interest Income	-	-	25,271	11,640
Other	-	-	-	-
Total Revenues	-	-	150,237	124,342
Expenditures				
Veterans' Services				
Personal Services	647,660	763,292	-	-
Services and Supplies	58,531	121,352	16,794	7,446
Dues and Subscriptions	-	-	726	685
Securities Lending Investment Expense	-	-	5,505	2,276
Other Professional Services	-	-	3,561	2,097
State Treasury Charges	-	-	-	-
Trust Fund Grants	-	-	-	-
Special Payments	1,894,537	395,643	-	-
Total Expenditures	2,600,728	1,280,287	26,586	12,504
Other Financing Sources (Uses)				
State Appropriations	2,600,728	1,280,287	-	-
Operating Transfer In from DMV	-	-	19,172	17,026
Operating Transfer In Intra-fund	-	-	-	-
Operating Transfer Out to Veterans Home	-	-	(25,483)	(6,091)
Operating Transfer Out Intra-fund	-	-	-	(65,000)
Total Other Financing Sources (Uses)	2,600,728	1,280,287	(6,311)	(54,065)
Net Change in Fund Balance	-	-	117,340	57,773
Beginning Fund Balance	270	126	477,828	420,055
Change in Reserve for Prepaid Items	(167)	144	-	-
Ending Fund Balance	$ 103	$ 270	$ 595,168	$ 477,828

Special Revenue Fund		Governmental Funds	
Other Veterans' Trust Accounts		TOTAL	
June 30, 2006	June 30, 2005	June 30, 2006	June 30, 2005
$ 500	$ 2,500	$ 125,466	$ 115,202
4,621	2,902	29,892	14,542
-	-	-	-
5,121	5,402	155,358	129,744
-	-	647,660	763,292
-	-	75,325	128,798
-	-	726	685
-	-	5,505	2,276
651	523	4,212	2,620
121	122	121	122
14,260	3,046	14,260	3,046
-	-	1,894,537	395,643
15,032	3,691	2,642,346	1,296,482
-	-	2,600,728	1,280,287
-	-	19,172	17,026
-	-	-	-
-	-	(25,483)	(6,091)
(3,261)	-	(3,261)	(65,000)
(3,261)	-	2,591,156	1,226,222
(13,172)	1,711	104,168	59,484
107,221	105,510	585,319	525,691
-	-	(167)	144
$ 94,049	$ 107,221	$ 689,320	$ 585,319

UNAUDITED

STATE OF OREGON

DEPARTMENT OF VETERANS' AFFAIRS

SCHEDULE OF LEGISLATIVE AUTHORIZATION (NON-GAAP BUDGETARY BASIS)

COMPARED TO ACTUAL EXPENDITURES SUBJECT TO BUDGET

GOVERNMENTAL FUND

FOR THE BIENNIUM ENDING JUNE 30, 2007

	General Fund		
	2005-2007 Budget	First Year Actual June 30, 2006	Second Year Balance
General Fund:			
Veterans' Services Division - Appropriation	**$** 6,230,178	$ 2,592,795	$ 3,637,383
Total General Fund	**$** 6,230,178	$ 2,592,795	$ 3,637,383

Fiduciary Fund

<u>Private Purpose Trust Fund</u>
Private Purpose Trust Funds, a type of Fiduciary Fund, account for trust arrangements, other than those properly reported in pension trust funds or investment trust funds, under which principal and income benefit individuals, private organizations, or other governments.

Conservatorship Private Purpose Trust Fund - The Department acts as conservator of estates of approximately 195 veterans, survivors, and minor or helpless children of veterans who the court has determined are unable to manage their own financial affairs. Revenue sources include Social Security monies, U.S. Department of Veterans' Affairs benefits, investment income, and other sources of income.

UNAUDITED

STATE OF OREGON

DEPARTMENT OF VETERANS' AFFAIRS

STATEMENT OF FIDUCIARY NET ASSETS

FIDUCIARY FUND

JUNE 30, 2006 and JUNE 30, 2005

	Private Purpose Trust Fund	
	Conservatorship Program	
	June 30, 2006	June 30, 2005
ASSETS		
Current Assets		
Cash and Cash Equivalents	$ 21,930,882	$ 22,651,978
Investments	1,515,437	1,954,473
Security Lending Cash Collateral	2,850,927	4,093,794
Receivables:		
Accrued Interest	87,748	57,263
Other	5,550	12,281
Total Current Assets	26,390,544	28,769,789
Noncurrent Assets		
Contract Receivables	45,163	45,163
Conservatorship Real Property	3,397,982	3,404,266
Conservatorship Personal Property	350,818	384,582
Total Noncurrent Assets	3,793,963	3,834,011
TOTAL ASSETS	$ 30,184,507	$ 32,603,800
LIABILITIES		
Current Liabilities		
Due to Other Funds	$ 19,651	$ 409
Obligations under Securities Lending	2,850,927	4,093,794
Total Current Liabilities	2,870,578	4,094,203
Noncurrent Liabilities		
Mortgages on Conservatorship Real Property	1,763,350	1,582,309
Total Noncurrent Liabilities	1,763,350	1,582,309
TOTAL LIABILITIES	4,633,928	5,676,512
NET ASSETS		
Net Assets Held in Trust for Individuals	25,550,579	26,927,288
TOTAL NET ASSETS	$ 25,550,579	$ 26,927,288

UNAUDITED

STATE OF OREGON

DEPARTMENT OF VETERANS' AFFAIRS

STATEMENT OF CHANGES IN

FIDUCIARY NET ASSETS

FIDUCIARY FUND

FOR THE FISCAL YEARS ENDED JUNE 30, 2006 and JUNE 30, 2005

	Private Purpose Trust Fund	
	Conservatorship Program	
	June 30, 2006	June 30, 2005
ADDITIONS		
Contributions:		
Veterans' Benefits	$ 7,221,851	$ 7,209,055
Investment Income:		
Interest Income	1,039,932	638,021
Valuation Changes and Redemptions of Investments	(136,694)	(384,778)
TOTAL ADDITIONS	$ 8,125,089	$ 7,462,298
DEDUCTIONS		
Veterans' Services: Beneficiary Care	$ 9,355,268	$ 9,454,495
Securities Lending Investment Expense	146,530	114,949
TOTAL DEDUCTIONS	9,501,798	9,569,444
Net Increase/ (Decrease)	(1,376,709)	(2,107,146)
CHANGE IN NET ASSETS	(1,376,709)	(2,107,146)
BEGINNING NET ASSETS	26,927,288	29,034,434
ENDING NET ASSETS	$ 25,550,579	$ 26,927,288

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STATISTICAL SECTION

UNAUDITED
STATE OF OREGON
DEPARTMENT OF VETERANS' AFFAIRS
COMPARATIVE STATEMENT OF REVENUES, EXPENSES AND
CHANGES IN FUND NET ASSETS
PROPRIETARY FUND - VETERANS' LOAN PROGRAM only
FOR THE FISCAL YEARS ENDED 1997 - 2006

	June 30, 2006	June 30, 2005	June 30, 2004	June 30, 2003
OPERATING REVENUES				
Mortgage Loan Interest Income	$ 17,561,219	$ 21,225,116	$ 26,789,783	$ 36,742,510
Contract Interest Income	806,376	1,188,374	1,698,531	2,535,147
Investment Income *(2)*	28,209,288	18,013,534	13,338,726	24,675,139
Gain on Sale of Foreclosed Property	7,551	139,199	493,409	39,121
Gain (Loss) on Sale of Investments *(2)*	-	-	-	-
Loan Cancellation Life Insurance Premiums *(3)*	1,962,357	2,523,140	2,704,444	3,642,487
Loan Cancellation Life Insurance Processing Fees	180,000	220,834	425,004	425,004
Other Fees and Charges	1,941,079	947,834	939,950	1,189,691
Conservatorship Fees	354,808	334,340	345,750	364,510
TOTAL OPERATING REVENUES	$ 51,022,678	$ 44,592,371	$ 46,735,597	$ 69,613,609
OPERATING EXPENSES				
Bond Interest Expense	$ 35,121,631	$ 37,103,554	$ 44,537,191	$ 58,066,877
Interest on Taxable Line of Credit	525,600	159,267	-	7,500
Salaries and Other Payroll Expenses	5,239,879	4,793,870	5,875,969	6,838,554
Bond Expenses	1,129,971	1,324,123	1,155,355	909,379
Securities Lending Investment Expense	2,910,155	2,199,165	1,899,175	630,893
Real Estate Owned Expense	9,485	47,490	52,526	80,757
Services and Supplies	2,174,420	1,776,839	2,140,262	2,958,497
Claims Expense - Loan Cancellation Life Insurance *(3)*	2,952,064	4,637,009	4,927,874	5,121,239
Depreciation Expense	255,626	359,441	408,883	431,391
Bad Debt Expense	(918,401)	(1,104,080)	(1,656,784)	(1,744,700)
Special Payments	-	-	-	51,000
Other Expenses	332,471	170,187	-	210,232
TOTAL OPERATING EXPENSES	$ 49,732,901	$ 51,466,865	$ 59,340,451	$ 73,561,619
Income/ (Loss) before Extraordinary or Special Items	$ 1,289,777	$ (6,874,494)	$ (12,604,854)	$ (3,948,010)
Extraordinary or Special Items:				
Loss on Extinguishment of Debt	$ -	$ -	$ -	$ -
Gain from Litigation	-	-	-	-
CHANGE IN NET ASSETS	$ 1,289,777	$ (6,874,494)	$ (12,604,854)	$ (3,948,010)
NET ASSETS				
Beginning Net Assets *(1)*	$ 119,875,333	$ 126,749,827	$ 139,354,681	$ 143,302,691
Prior Period Adjustment	-	-	-	-
Cumulative Effect of Change in Accounting Principle	-	-	-	-
Beginning Net Assets, Restated	$ 119,875,333	$ 126,749,827	$ 139,354,681	$ 143,302,691
Ending Net Assets	$ 121,165,110	$ 119,875,333	$ 126,749,827	$ 139,354,681

(1) Prior to the fiscal year ended June 30, 2002, the term "Retained Earnings" was used. It has the same meaning as "Net Assets".
(2) 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.
(3) Starting in fiscal year 2003, the Department included the activity of the Loan Cancellation Life Insurance program in the Statement of Revenues, Expenses, And Changes In Fund Net Assets.

June 30, 2002	June 30, 2001	June 30, 2000	June 30, 1999	June 30, 1998	June 30, 1997
$ 43,749,526	$ 50,861,579	$ 57,259,424	$ 68,967,805	$ 84,739,050	$ 101,149,885
3,522,372	4,562,401	5,648,408	7,603,132	10,413,658	13,302,547
35,956,850	57,521,901	38,492,961	48,834,865	80,184,016	88,584,123
172,472	9,052	16,892	32,324	106,330	292,921
-	-	-	-	-	(771,619)
-	-	-	-	-	-
425,004	425,004	399,937	327,540	433,763	497,874
1,447,451	1,342,762	1,402,798	1,055,894	932,092	884,689
338,136	353,417	345,554	322,973	334,784	334,328
$ 85,611,811	$ 115,076,116	$ 103,565,974	$ 127,144,533	$ 177,143,693	$ 204,274,748
$ 68,560,732	$ 85,455,556	$ 93,957,700	$ 117,276,619	$ 153,677,775	$ 186,918,415
580,883	-	-	-	-	-
6,974,557	6,932,307	6,886,703	6,829,801	6,952,431	6,958,822
868,243	925,722	819,421	952,673	1,478,508	1,774,314
522,316	1,156,100	2,006,704	1,607,492	1,588,540	4,656,093
73,308	57,863	42,230	49,096	50,806	79,340
2,480,268	2,741,678	2,679,295	3,055,525	3,473,771	3,197,130
-	-	-	-	-	-
538,555	453,159	360,840	317,751	338,820	235,128
(906,906)	(1,078,111)	(1,227,068)	(3,346,273)	(2,934,825)	(3,217,416)
-	-	-	-	-	-
180,045	74,888	42,749	42,477	53,475	32,406
$ 79,872,001	$ 96,719,162	$ 105,568,574	$ 126,785,161	$ 164,679,301	$ 200,634,232
$ 5,739,810	$ 18,356,954	$ (2,002,600)	$ 359,372	$ 12,464,392	$ 3,640,516
$ -	$ (17,231)	$ (11,888)	$ (12,271,433)	$ (3,870,466)	$ (5,676,618)
-	-	-	654,385	-	-
$ 5,739,810	$ 18,339,723	$ (2,014,488)	$ (11,257,676)	$ 8,593,926	$ (2,036,102)
$ 94,931,080	$ 76,591,357	$ 78,605,845	$ 89,863,521	$ 78,681,347	$ 80,717,449
42,556,801	-	-	-	-	-
75,000	-	-	-	2,588,248	-
$ 137,562,881	$ 76,591,357	$ 78,605,845	$ 89,863,521	$ 81,269,595	$ 80,717,449
$ 143,302,691	$ 94,931,080	$ 76,591,357	$ 78,605,845	$ 89,863,521	$ 78,681,347

UNAUDITED

STATE OF OREGON

DEPARTMENT OF VETERANS' AFFAIRS

COMPARATIVE STATEMENT OF REVENUES, EXPENSES AND CHANGES IN FUND NET ASSETS

PROPRIETARY FUND - VETERANS' HOME PROGRAM only

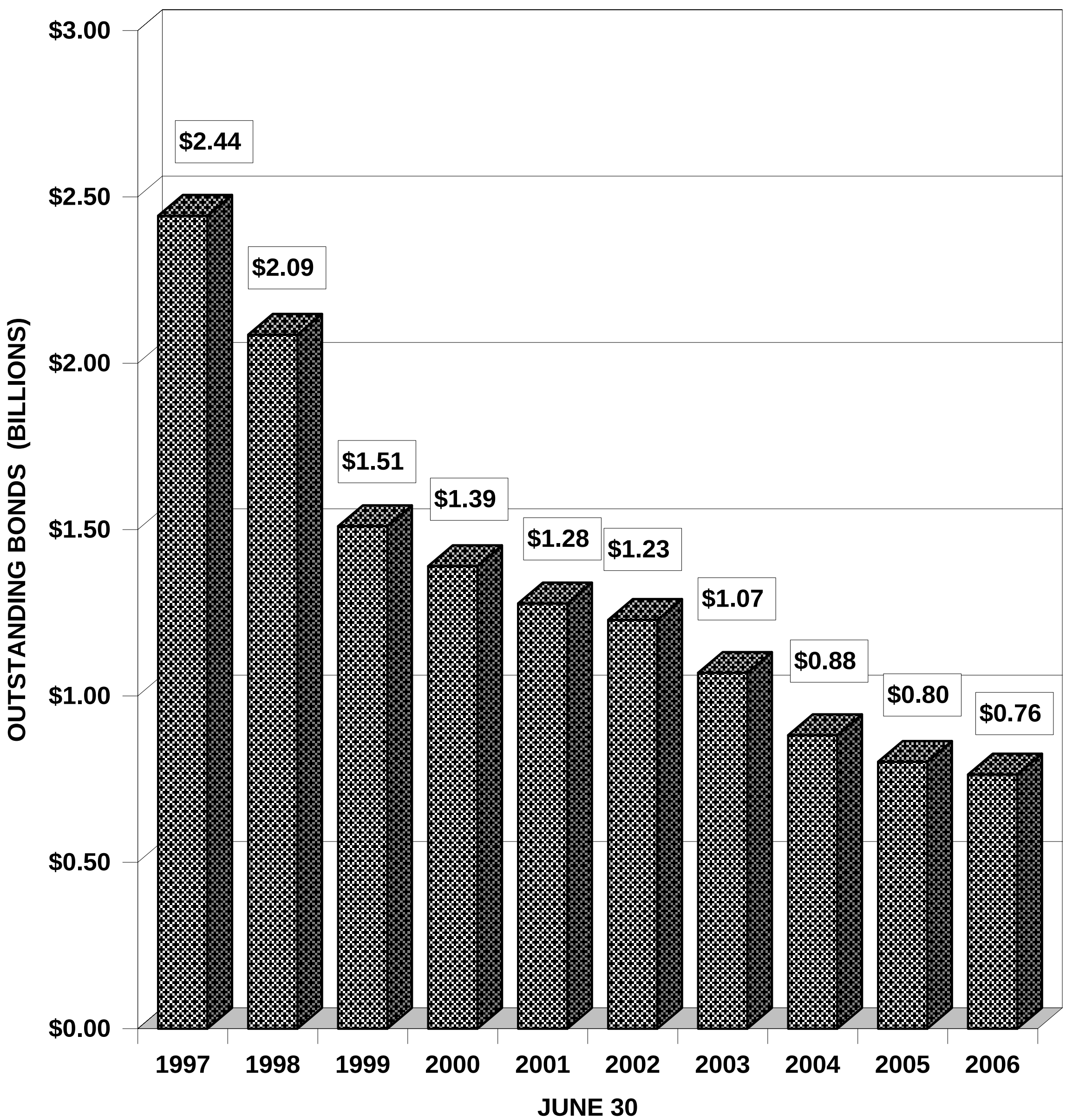
FOR THE FISCAL YEARS ENDED 1997 - 2006

	June 30, 2006	June 30, 2005	June 30, 2004	June 30, 2003
OPERATING REVENUES				
Investment Income	$ 73,604	$ 24,217	$ 8,390	$ 8,487
Resident Revenue	9,927,217	8,680,118	6,157,125	5,044,610
Other Fees and Charges	1,947	2,825	2,134	-
TOTAL OPERATING REVENUES	$ 10,002,768	$ 8,707,160	$ 6,167,649	$ 5,053,097
OPERATING EXPENSES				
Salaries and Other Payroll Expenses	$ 80,684	$ 512,025	$ 213,063	$ 205,262
Securities Lending Investment Expense	10,346	4,349	1,846	654
Services and Supplies	157,869	208,319	107,766	134,843
Veterans' Home Operations	9,120,186	7,596,750	6,181,784	4,732,459
Depreciation Expense	289,619	287,472	288,918	353,480
Bad Debt Expense	118,200	5,211	(100)	1,600
TOTAL OPERATING EXPENSES	$ 9,776,904	$ 8,614,126	$ 6,793,277	$ 5,428,298
OPERATING INCOME (LOSS)	$ 225,864	$ 93,034	$ (625,628)	$ (375,201)
Transfers				
Net Transfers from Veterans' Home Trust Fund	$ 25,483	$ 71,091	$ 298,257	$ 17,709
Capital Contributions	16,794	7,250	9,000	-
CHANGE IN NET ASSETS	$ 268,141	$ 171,375	$ (318,371)	$ (357,492)
NET ASSETS				
Beginning Net Assets	$ 11,615,431	$ 11,444,056	$ 11,762,427	$ 12,114,469
Prior Period Adjustment	-	-	-	5,450
Cumulative Effect of Change in Accounting Principle	-	-	-	-
Beginning Net Assets, Restated	$ 11,615,431	$ 11,444,056	$ 11,762,427	$ 12,119,919
Net Contributed Construction Capital	-	-	-	-
Ending Net Assets	$ 11,883,572	$ 11,615,431	$ 11,444,056	$ 11,762,427

June 30, 2002	June 30, 2001	June 30, 2000	June 30, 1999	June 30, 1998	June 30, 1997
$ 13,983	$ 38,155	$ 23,186	$ 5,071	$ 48,778	$ 225,812
5,465,696	5,194,921	4,557,751	3,515,679	525,972	-
-	23,828	-	45	-	-
$ 5,479,679	$ 5,256,904	$ 4,580,937	$ 3,520,795	$ 574,750	$ 225,812
$ 218,460	$ 203,790	$ 181,504	$ 144,965	$ 105,910	$ -
590	1,917	1,969	344	4,846	34,907
54,645	313,874	180,485	162,834	1,059,288	-
5,238,567	4,773,004	3,945,157	3,088,796	1,086,621	-
331,368	329,069	329,069	329,069	207,848	-
-	-	-	-	-	-
$ 5,843,630	$ 5,621,654	$ 4,638,184	$ 3,726,008	$ 2,464,513	$ 34,907
$ (363,951)	$ (364,750)	$ (57,247)	$ (205,213)	$ (1,889,763)	$ 190,905
$ 1,380	$ 16,503	$ 14,798	$ 9,960	$ 28,218	$ -
-	-	-	-	-	-
$ (362,571)	$ (348,247)	$ (42,449)	$ (195,253)	$ (1,861,545)	$ 190,905
$ 11,873,382	$ 12,102,071	$ 12,111,240	$ 12,195,253	$ 12,719,647	$ 202,077
563,658	-	-	-	-	12,272
40,000	-	-	-	-	-
$ 12,477,040	$ 12,102,071	$ 12,111,240	$ 12,195,253	$ 12,719,647	$ 214,349
-	119,558	33,280	111,240	1,337,151	12,314,393
$ 12,114,469	$ 11,873,382	$ 12,102,071	$ 12,111,240	$ 12,195,253	$ 12,719,647

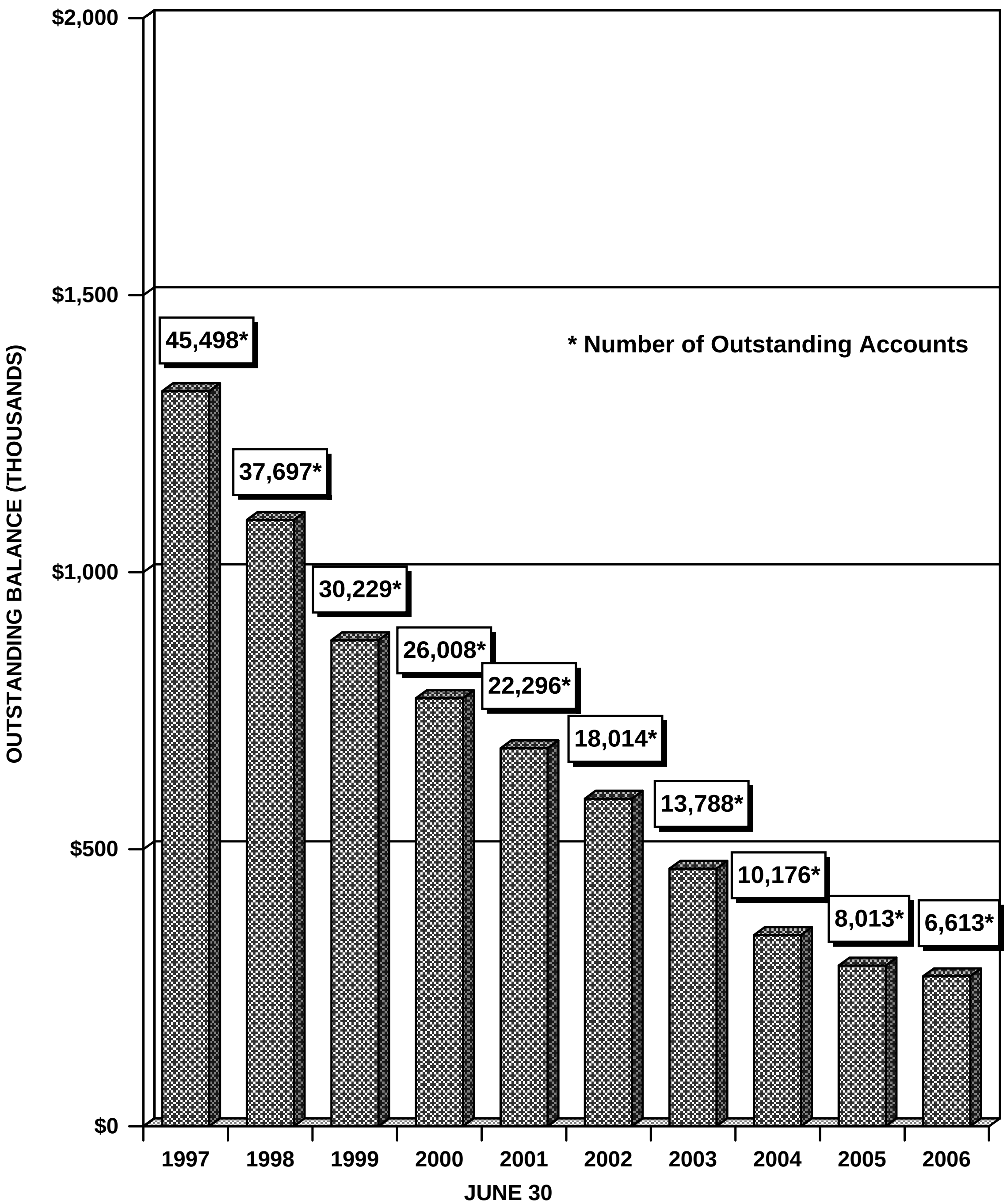
UNAUDITED
OREGON DEPARTMENT OF VETERANS' AFFAIRS

COMPARATIVE SUMMARY OF BONDS OUTSTANDING



Source: Financial Statements of the Oregon Department of Veterans' Affairs.

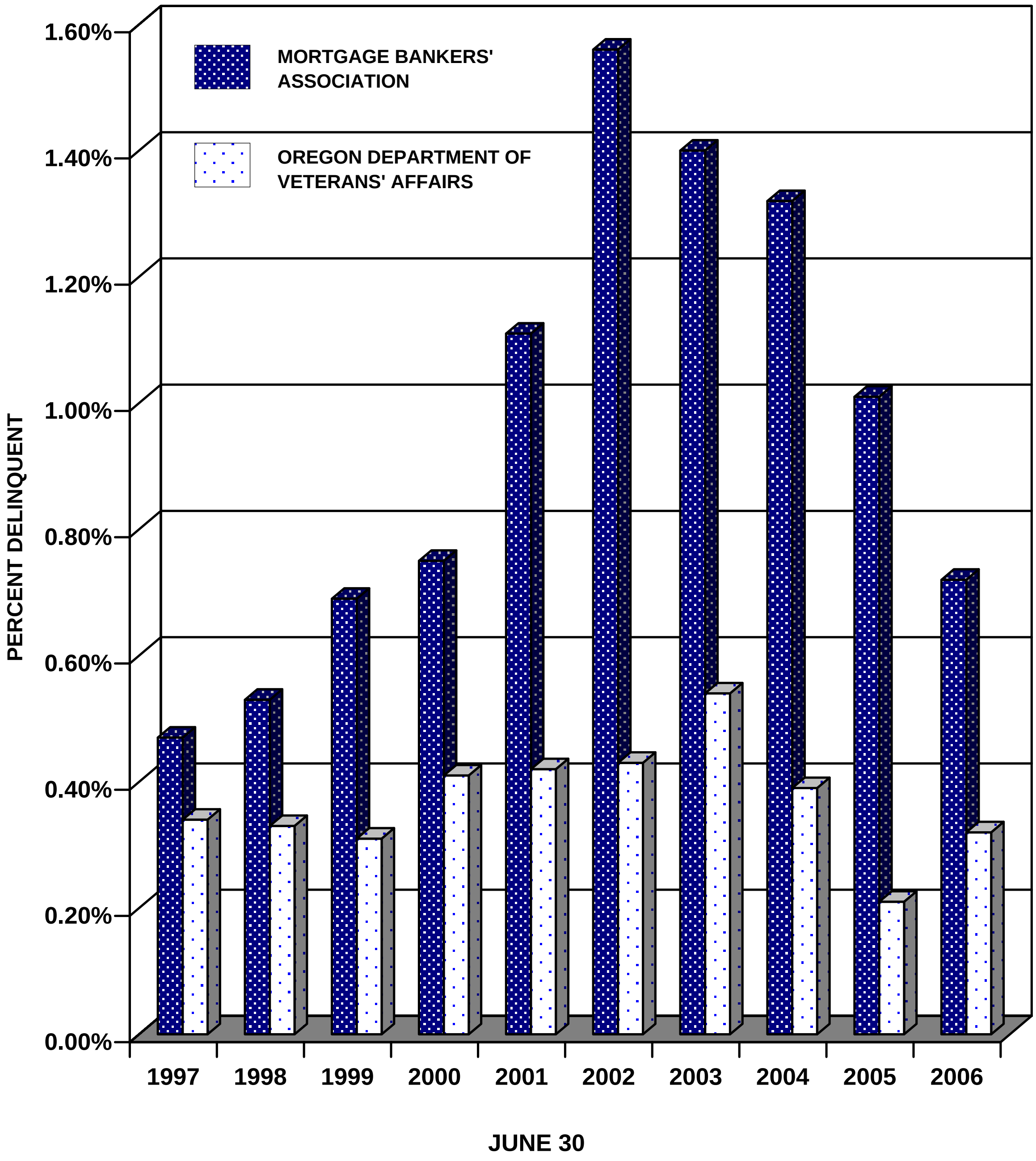
UNAUDITED
OREGON DEPARTMENT OF VETERANS' AFFAIRS
COMPARATIVE SUMMARY OF LOANS AND CONTRACTS OUTSTANDING



Sources: Statistical Reports and Financial Statements of the Oregon Department of Veterans' Affairs.

UNAUDITED
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. 90+ Day Delinquencies includes past due loans and loans in foreclosure.

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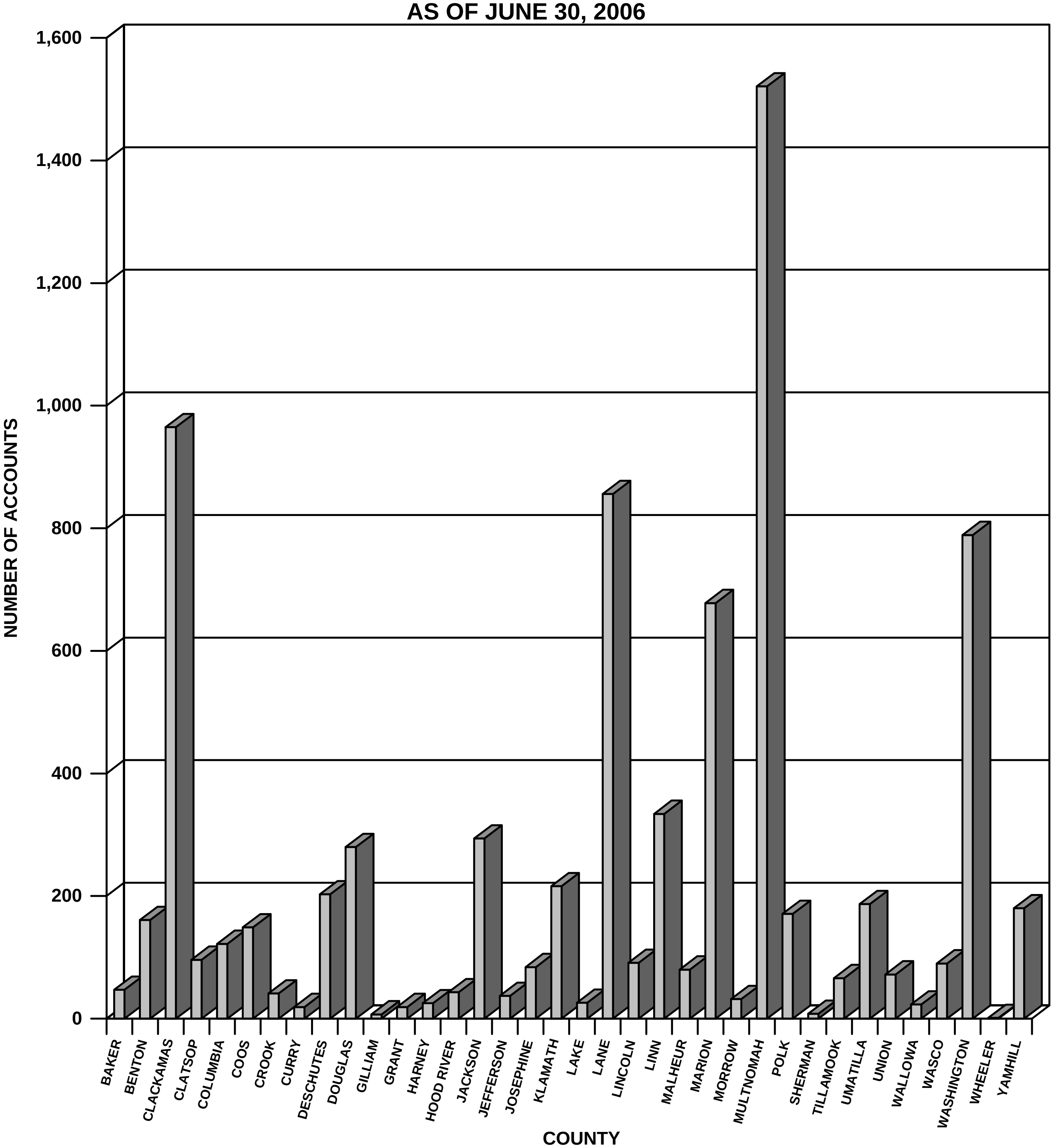
OREGON DEPARTMENT OF VETERANS' AFFAIRS

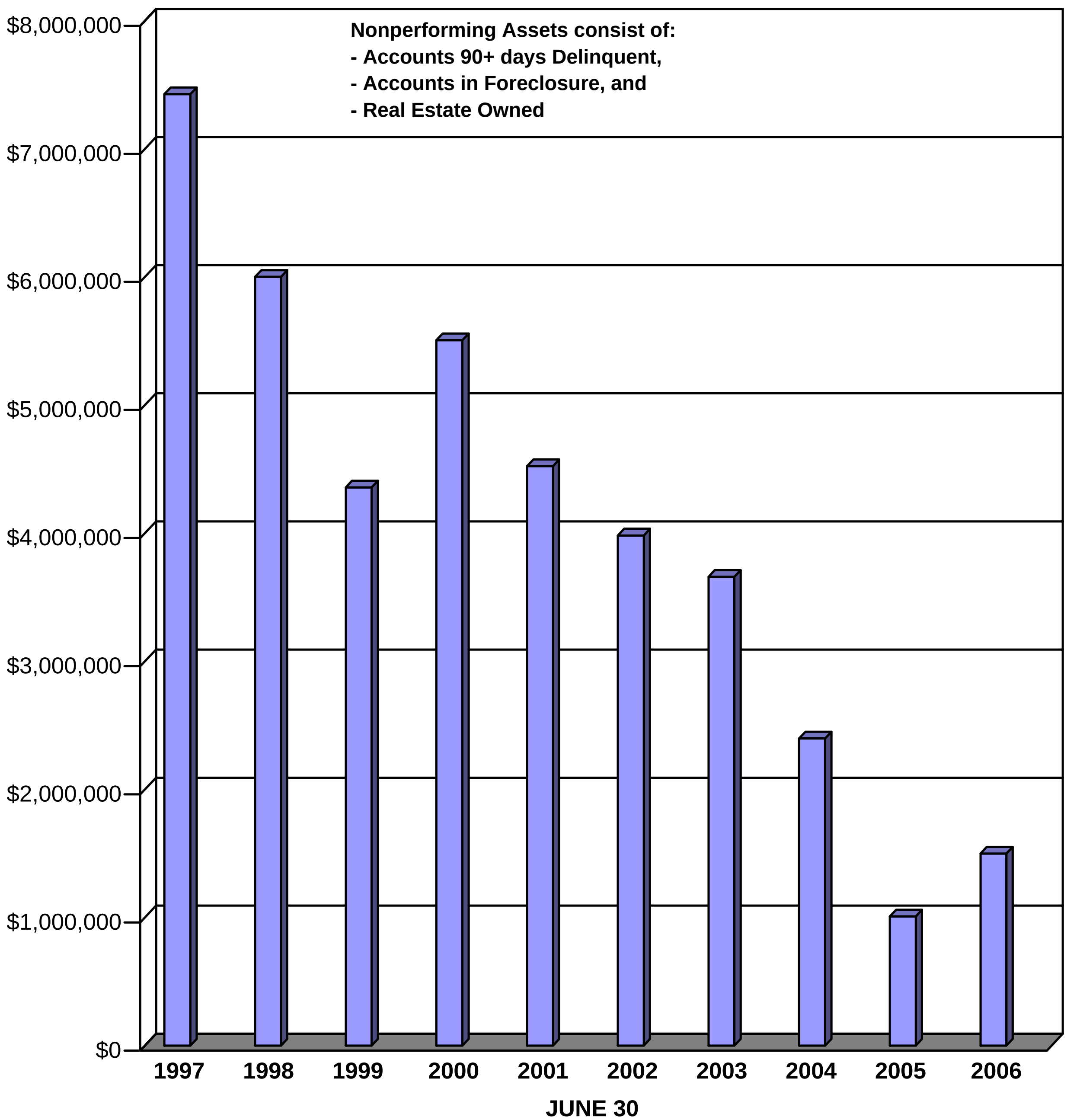
OUTSTANDING LOAN AND CONTRACT ACCOUNTS BY COUNTY
AS OF JUNE 30, 2006



Source: Oregon Department of Veterans' Affairs.

UNAUDITED
OREGON DEPARTMENT OF VETERANS' AFFAIRS

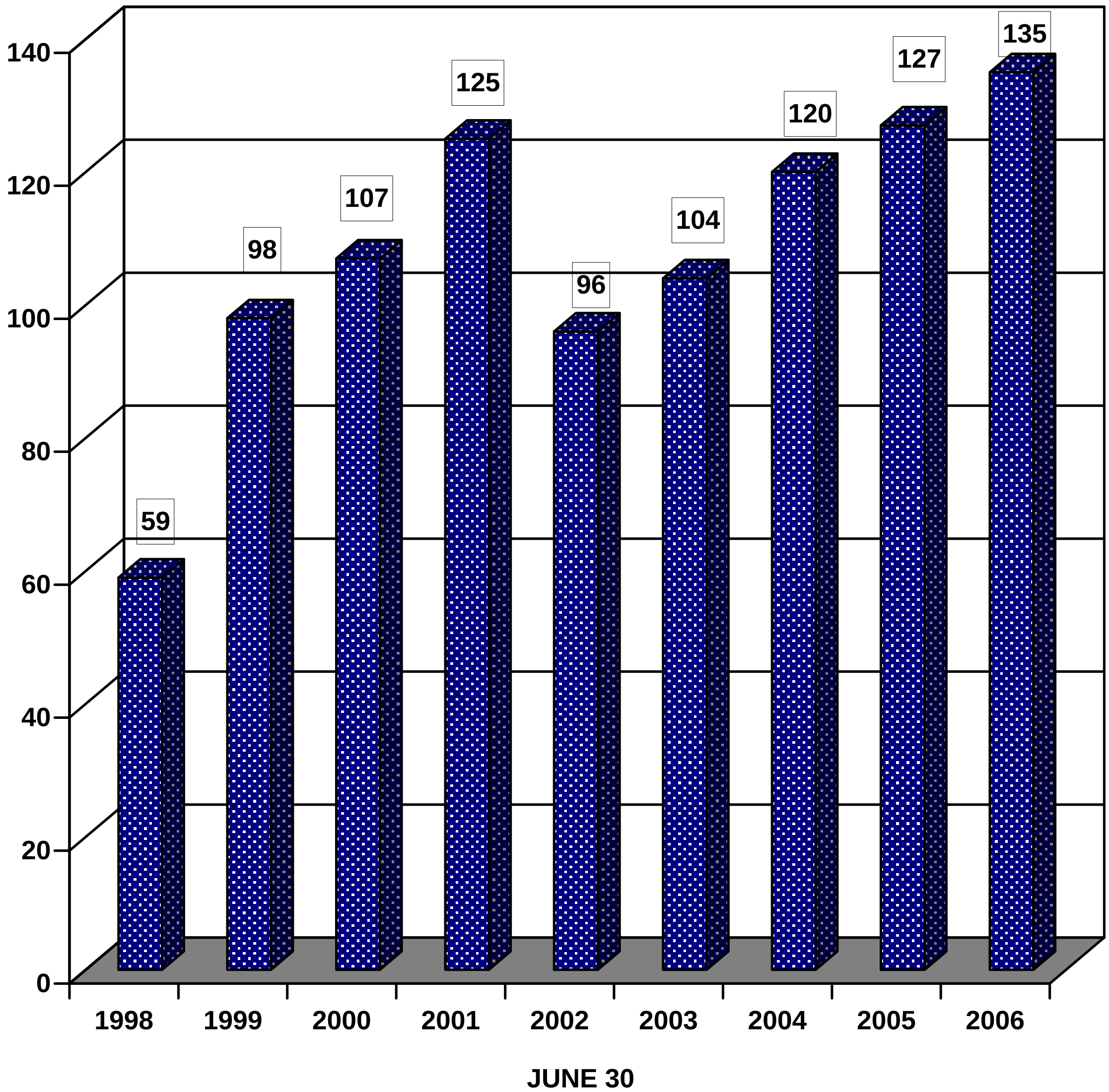
COMPARATIVE SUMMARY OF NONPERFORMING ASSETS



Sources: Statistical Reports and Financial Statements of the Oregon Department of Veterans' Affairs.

UNAUDITED
OREGON DEPARTMENT OF VETERANS' AFFAIRS

RESIDENTS CENSUS AT THE OREGON VETERANS' HOME

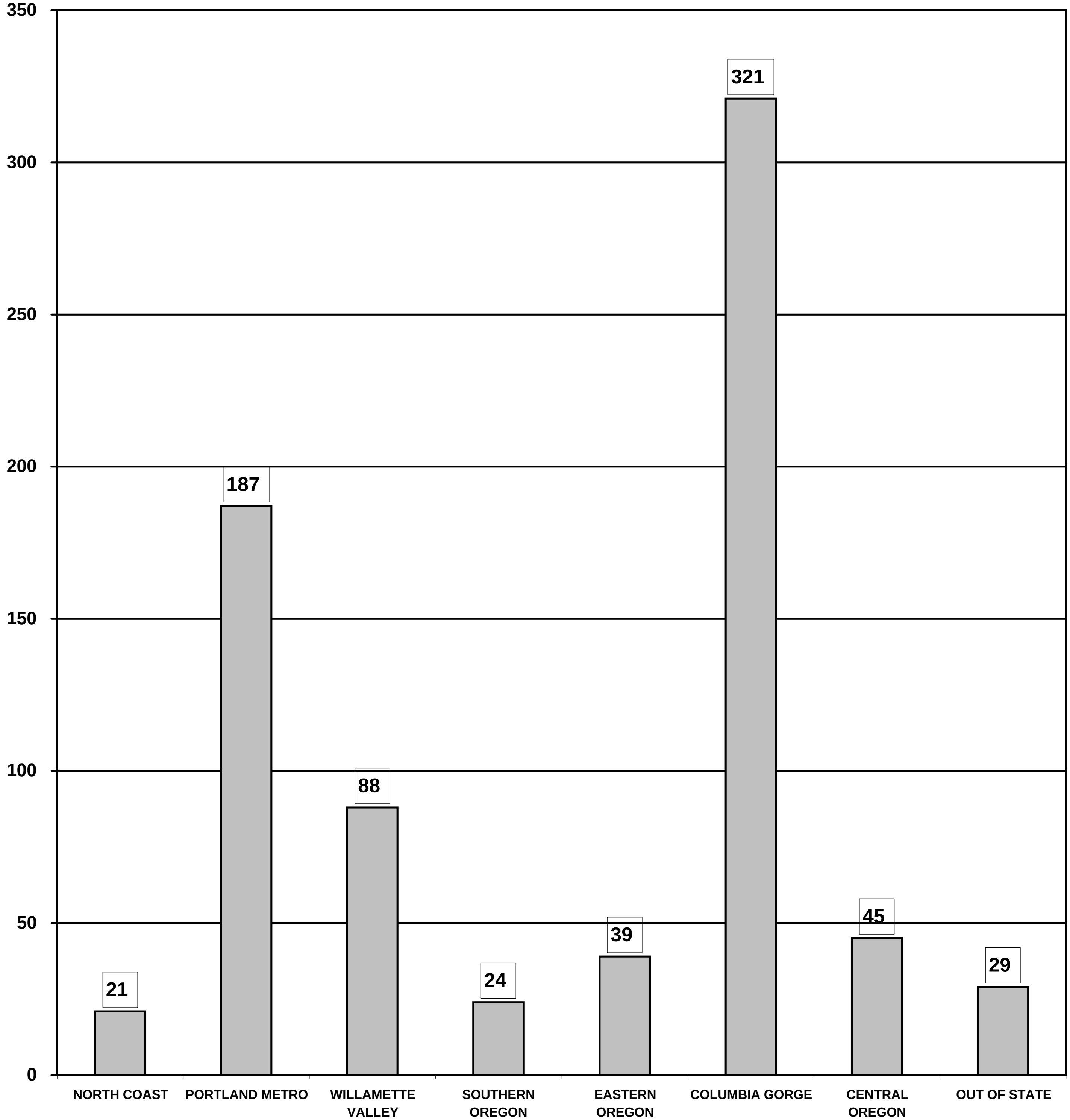


Source: Oregon Department of Veterans' Affairs.

UNAUDITED

OREGON DEPARTMENT OF VETERANS' AFFAIRS

CUMULATIVE RESIDENT ADMISSIONS BY GEOGRAPHIC AREA
NOVEMBER 1, 1997 THROUGH JUNE 30, 2006



Source: Oregon Department of Veterans' Affairs.

OTHER REPORTS

MERINA
& COMPANY, LLP
Certified Public Accountants and Consultants

CERTIFIED PUBLIC ACCOUNTANTS AND CONSULTANTS

PARTNERS
JOHN W. MERINA, CPA • KAMALA K. AUSTIN, CPA

REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

The Honorable Theodore R. Kulongoski
Governor of Oregon
254 State Capitol
Salem, Oregon 97301-4047

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

We have audited the accompanying financial statements of the enterprise funds for the State of Oregon, Department of Veterans' Affairs (Department), as of and for the year ended June 30, 2006, and have issued our report thereon dated September 22, 2006. 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.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Oregon Department of Veterans' Affairs 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 an opinion 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 reportable 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 caused by error or fraud 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.

5499 AMY STREET • WEST LINN, OREGON 97068 • PHONE: (503) 723-0300 • FAX: (503) 723-9946 WWW.MERINACPAS.COM

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Oregon Department of Veterans' Affairs financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, 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 or other matters that are required to be reported under *Government Auditing Standards*.

We noted certain matters that we reported to management of the Oregon Department of Veterans' Affairs, in a separate letter dated September 22, 2006.

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

Merina & Company

Merina & Company, LLP
West Linn, Oregon
September 22, 2006

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, TTY 503-373-2217

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