

The background of the top half of the page features a large, faint, light blue seal of the State of Oregon. The seal is circular with the words "SEAL OF THE STATE OF OREGON" around the perimeter. Inside the seal, there is an eagle with spread wings perched on a shield. Below the shield, there is a ship on the left and a plow on the right, with a rising sun in the background. The year "1859" is at the bottom of the seal.

Enterprise Fund of the State of Oregon

**Department of
Environmental Quality**

**Clean Water State Revolving
Fund Loan Program**

For Fiscal Year Ended June 30, 2016

Secretary of State
Dennis Richardson

Audits Division, Director
Kip Memmott

Report 2017 – 10
June 2017

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FINANCIAL SECTION

Office of the Secretary of State

Dennis Richardson
Secretary of State

Leslie Cummings, Ph.D.
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Audits Division

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Independent Auditor's Report

The Honorable Kate Brown
Governor of Oregon

Richard Whitman, Director
Oregon Department of Environmental Quality

Report on the Financial Statements

We have audited the accompanying financial statements of the Clean Water State Revolving Fund (CWSRF) program, an enterprise fund of the State of Oregon, Department of Environmental Quality (department), as of and for the year ended June 30, 2016, and the related notes to the financial statements, as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on the financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the CWSRF program, an enterprise fund of the State of Oregon, Department of Environmental Quality, as of June 30, 2016, and the respective changes in financial position and cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 1.1.1, the financial statements of the CWSRF program, an enterprise fund of the State of Oregon, Department of Environmental Quality, are intended to present the financial position, the changes in financial position and cash flows that are attributable to the transactions of the CWSRF program. They do not purport to, and do not, present fairly the financial position of the Department of Environmental Quality or the State of Oregon as of June 30, 2016, the changes in their financial position, or their cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated June 19, 2017, on our consideration of the department's internal control over financial reporting relating to the CWSRF program 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* in considering the department's internal control over financial reporting and compliance.

Office of the Secretary of State, Audits Division

State of Oregon
June 19, 2017

**STATE OF OREGON
DEPARTMENT OF ENVIRONMENTAL QUALITY
CLEAN WATER STATE REVOLVING FUND LOAN PROGRAM
ENTERPRISE FUND
BALANCE SHEET
JUNE 30, 2016**

	Loan Fund	Administration	TOTAL
<hr/>			
Assets			
<i>Current Assets:</i>			
Cash and Cash Equivalents	\$ 228,208,525	\$ 3,453,696	\$ 231,662,221
Loan Interest Receivable	<u>2,125,861</u>	<u>-</u>	<u>2,125,861</u>
Total Current Assets	<u>230,334,386</u>	<u>3,453,696</u>	<u>233,788,082</u>
<i>Non-Current Assets:</i>			
Loans Receivable, Net	419,721,058	-	419,721,058
Loan Interest Receivable	<u>2,393,764</u>	<u>-</u>	<u>2,393,764</u>
Total Non-Current Assets	<u>422,114,822</u>	<u>-</u>	<u>422,114,822</u>
Total Assets	<u>\$ 652,449,208</u>	<u>\$ 3,453,696</u>	<u>\$ 655,902,904</u>
Liabilities and Net Position			
<i>Current Liabilities:</i>			
Accounts Payable	\$ -	\$ 10,408	\$ 10,408
Payroll Payable	-	111,362	111,362
Compensated Absences Payable	-	58,473	58,473
Due to Oregon DEQ	-	25,637	25,637
Bond Interest Payable	241,216	-	214,216
Bonds Payable	<u>1,516,774</u>	<u>-</u>	<u>1,516,774</u>
Total Current Liabilities	<u>1,757,990</u>	<u>205,880</u>	<u>1,963,870</u>
<i>Non-Current Liabilities:</i>			
Compensated Absences Payable	-	11,874	11,874
Bonds Payable	<u>21,607,843</u>	<u>-</u>	<u>21,607,843</u>
Total Non-Current Liabilities	<u>21,607,843</u>	<u>11,874</u>	<u>21,619,717</u>
Total Liabilities	<u>23,365,833</u>	<u>217,754</u>	<u>23,583,587</u>
<i>Net Position</i>			
Unrestricted	<u>629,083,375</u>	<u>3,235,942</u>	<u>632,319,317</u>
Total Net Position	<u>629,083,375</u>	<u>3,235,942</u>	<u>632,319,317</u>
Total Liabilities and Net Position	<u>\$ 652,449,208</u>	<u>\$ 3,453,696</u>	<u>\$ 655,902,904</u>

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

**STATE OF OREGON
DEPARTMENT OF ENVIRONMENTAL QUALITY
CLEAN WATER STATE REVOLVING FUND LOAN PROGRAM
ENTERPRISE FUND
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN FUND NET POSITION
FOR THE FISCAL YEAR ENDED JUNE 30, 2016**

	Loan Fund	Administration	TOTAL
Operating Revenues			
Loan Interest Income	\$ 9,470,783	\$ -	\$ 9,470,783
Loan Fees	<u>4,519</u>	<u>1,658,919</u>	<u>1,663,438</u>
Total Operating Revenues	<u>9,475,302</u>	<u>1,658,919</u>	<u>11,134,221</u>
Operating Expenses			
Bond Interest	710,068	-	710,068
Principal Forgiveness on Loans	2,146,369	-	2,146,369
Bad Debt	(20,000)	-	(20,000)
Salaries and Benefits	-	1,353,566	1,353,566
Services and Supplies	-	277,642	277,642
Indirect Costs	<u>-</u>	<u>240,973</u>	<u>240,973</u>
Total Operating Expenses	<u>2,836,437</u>	<u>1,872,181</u>	<u>4,708,618</u>
Operating Income (Loss)	<u>6,638,865</u>	<u>(213,262)</u>	<u>6,425,603</u>
Non-Operating Revenues (Expenses)			
Federal Grants	20,313,450	-	20,313,450
Interest Income on Cash and Cash Equivalents	<u>1,460,502</u>	<u>23,344</u>	<u>1,483,846</u>
Total Non-Operating Revenues (Expenses)	<u>21,773,952</u>	<u>23,344</u>	<u>21,797,296</u>
Change in Net Position	28,412,817	(189,918)	28,222,899
Net Position –Beginning	<u>600,670,558</u>	<u>3,425,860</u>	<u>604,096,418</u>
Net Position – Ending	<u>\$ 629,083,375</u>	<u>\$ 3,235,942</u>	<u>\$ 632,319,317</u>

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

**STATE OF OREGON
DEPARTMENT OF ENVIRONMENTAL QUALITY
CLEAN WATER STATE REVOLVING FUND LOAN PROGRAM
ENTERPRISE FUND
STATEMENT OF CASH FLOWS
FOR THE FISCAL YEAR ENDED JUNE 30, 2016**

	Loan Fund	Administration	TOTAL
<hr/>			
Cash Flows from Operating Activities			
Receipts from Loan Fees	\$ 4,519	\$ 1,658,919	\$ 1,663,438
Payments to Vendors	(5,451)	(267,853)	(273,304)
Payments to Employees	-	(1,354,275)	(1,354,275)
Payments for Indirect Cost	<u>-</u>	<u>(262,138)</u>	<u>(262,138)</u>
Net Cash Provided (Used) by Operating Activities	<u>(932)</u>	<u>(225,347)</u>	<u>(226,279)</u>
Cash Flows from Noncapital Financing Activities			
Receipts from Federal Grants	20,313,450	-	20,313,450
Principal Payments on Bonds	(1,134,032)	-	(1,134,032)
Interest Payments on Bonds	<u>(900,235)</u>	<u>-</u>	<u>(900,235)</u>
Net Cash Provided (Used) in Noncapital Financing Activities	<u>18,279,183</u>	<u>-</u>	<u>18,279,183</u>
Cash Flows from Investing Activities			
Receipts from Treasury Interest Credits	1,460,502	23,344	1,483,846
Repayments from Loan Interest	9,160,640	-	9,160,640
Repayments from Loan Principal	22,979,056	-	22,979,056
Receipt from Settlement	20,000	-	20,000
Disbursements to Borrowers	<u>(38,498,053)</u>	<u>-</u>	<u>(38,498,053)</u>
Net Cash Provided (Used) in Investing Activities	<u>(4,877,855)</u>	<u>23,344</u>	<u>(4,854,511)</u>
Net Increase (Decrease) in Cash and Cash Equivalents	13,400,396	(202,003)	13,198,393
Cash and Cash Equivalents, Beginning	<u>214,808,129</u>	<u>3,655,699</u>	<u>218,463,828</u>
Cash and Cash Equivalents, Ending	<u>\$ 228,208,525</u>	<u>\$ 3,453,696</u>	<u>\$ 231,662,221</u>

(Continued on next page)

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

**STATE OF OREGON
DEPARTMENT OF ENVIRONMENTAL QUALITY
CLEAN WATER STATE REVOLVING FUND LOAN PROGRAM
ENTERPRISE FUND
STATEMENT OF CASH FLOWS
FOR THE FISCAL YEAR ENDED JUNE 30, 2016**

(Continued from previous page)

**Reconciliation of Operating Income to Net Cash
Provided (Used) by Operating Activities**

Operating Income (Loss)	\$	6,638,865	\$	(213,262)	\$	6,425,603
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**Adjustments to Reconcile Operating Income to
Net Cash Provided (Used) by Operating Activities**

Loan Interest Receipts Reported						
as Operating Expense	(9,160,640)		-			(9,160,640)
Bond Interest Payments Reported						
as Operating Expense	900,235		-			900,235
Bad Debt Expense Reported						
as Operating Expense	(20,000)		-			(20,000)
Principal Forgiveness Expense Reported						
as Operating Expense	2,146,369		-			2,146,369
Amortization of Bond Discount	1,483		-			1,483
Amortization of Bond Premium	(198,324)		-			(198,324)
Net Changes in Assets and Liabilities						
Loan Interest Receivable	(310,143)		-			(310,143)
Accounts Payable	(5,451)		(4,002)			(9,453)
Payroll Payable	-		(7,079)			(7,079)
Due to Oregon DEQ	-		(7,374)			(7,374)
Bond Interest Payable	6,674		-			6,674
Compensated Absences Payable	-		6,370			6,370
Total Adjustments	<u>(6,639,797)</u>		<u>(12,085)</u>			<u>(6,651,882)</u>
Net Cash Provided (Used) by Operating Activities	<u>\$</u>	<u>(932)</u>	<u>\$</u>	<u>(225,347)</u>	<u>\$</u>	<u>(226,279)</u>

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

STATE OF OREGON
DEPARTMENT OF ENVIRONMENTAL QUALITY
CLEAN WATER STATE REVOLVING FUND LOAN PROGRAM
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2016

1.1 Summary of Significant Accounting Policies

The accompanying financial statements of the State of Oregon Department of Environmental Quality Clean Water State Revolving Fund have been prepared in conformity with generally accepted accounting principles (GAAP) as prescribed by the Governmental Accounting Standards Board (GASB).

1.1.1 Reporting Entity

The Oregon Clean Water State Revolving Fund (CWSRF) was established pursuant to Oregon Revised Statutes 468.423 – 468.440 and the 1987 amendments to the federal Clean Water Act. The purpose of the CWSRF is to provide low interest loans to local governments for the planning, design and construction of wastewater treatment facilities, implementation of nonpoint source pollution management plans, and the design and implementation of estuary management plans. The loan repayment period is a maximum of 30 years, and all repayments, including interest and principal, must be credited to the CWSRF.

The CWSRF program is administered by the State of Oregon Department of Environmental Quality (DEQ). The CWSRF program consists of several funds to record loan and related activity, and an administrative fund that collects loan fees and pays the operating costs of the program, and are collectively referred to as the Fund. DEQ's primary responsibilities for the CWSRF include obtaining capitalization grants from the U.S. Environmental Protection Agency (EPA), soliciting potential interested parties for loans, negotiating loan agreements with eligible public agencies, reviewing and approving payment requests from loan recipients, monitoring the loan repayments, and conducting inspection and engineering reviews to ensure compliance with all applicable laws, regulations, and program requirements.

DEQ charges the Fund for staff time spent on CWSRF activities, and the Fund pays those expenses from the Administration fund. The charges include the salaries and benefits of the employees, as well as indirect costs allocated to the Fund. The rate of indirect cost is negotiated annually with EPA.

The Annual Financial Report is prepared for the U.S. Environmental Protection Agency as an Enterprise Fund of the State of Oregon, which uses the accrual basis of accounting. For the purpose of the State of Oregon's Comprehensive Annual Financial Report (CAFR), the Fund is included as a Governmental Fund – Special Revenue. Due to differences in basis of accounting, there may be differences between the amounts reported in these financial statements and the State of Oregon's CAFR.

1.1.2 Basis of Presentation – Fund Accounting

DEQ programs and accounts are organized by “funds”, each of which is a separate accounting entity. Each major program utilizes a separate set of self-balancing accounts to record the assets, liabilities, net position, revenues and expenses of their activities. DEQ’s CWSRF loan program is classified as a proprietary fund for the purposes of these financial statements, however DEQ treats this fund as a governmental fund. Proprietary funds contain two types of funds: Enterprise Funds and Internal Service Funds. The CWSRF loan program is accounted for in an Enterprise Fund. Enterprise Funds account for and report any activity for which fees are charged to external users for goods and services.

1.1.3 Measurement Focus and Basis of Accounting

The basic financial statements for the Fund are presented as an enterprise fund. As such, the Fund is accounted for using the flow of economic resources measurement focus and is maintained on the accrual basis of accounting, in accordance with State policy (OAM 15.40.00). Under the accrual basis of accounting, revenues are recognized when earned and expenses are recorded at the time the liabilities are incurred, regardless of the timing of the related cash flow. All revenues and expenses of the Fund are considered to be operating revenues and operating expenses, with the exception of federal grant income and interest income, which are considered to be non-operating revenue. All assets and liabilities associated with the operations of the Fund are included on the Balance Sheet.

1.1.4 Cash and Cash Equivalents

All monies of the Fund are deposited with the Office of the State Treasurer, which is responsible for maintaining these deposits in accordance with Oregon law. The Fund considers all such deposits to be cash and cash equivalents. Interest earnings on these deposits are received by the Fund on a monthly basis. The Fund has no other cash deposits or investments.

1.1.5 Loans Receivable/Bonds Receivable

Loans and Bonds are funded by federal capitalization grants, state matching funds, loan repayments and fund earnings. The CWSRF monies are disbursed to borrowers on a cost reimbursement basis. When borrowers have incurred qualifying expenses, they request a loan disbursement from the Fund, and at that time a disbursement is made and recorded in the Fund accounting records. Interest begins accruing when funds are disbursed to the borrower. After the project is complete, repayment begins with an interest only payment. Loans and bonds are fully amortized to assure full repayment by the loan or bond maturity date.

DEQ has been required, under the terms of several grant awards from EPA, to offer additional subsidization to certain borrowers. DEQ has chosen to offer this subsidization in the form of principal forgiveness and has implemented this in administrative rule (OAR 340-054-0065). Loans Receivable are stated net of the allowance for principal forgiveness.

During the year, the Fund received a \$20,000 settlement payment from a borrower whose loan was written off in a prior year. The write off was recorded as bad debt expense in a prior year; therefore, the settlement payment was recorded as a reduction of bad debt expense in the current year.

1.1.6 Long-Term Obligations

Long term obligations of the Fund consist of bonds issued to provide the required State matching funds for the federal capitalization grants, and the non-current portion of compensated absences. Bonds issued on behalf of the CWSRF are reported on the Balance Sheet net of the related premium or discount. Bond premium and discount are amortized over the life of the bond issues. Bond premium and discount are reported in the Statement of Revenues, Expenses and Changes in Fund Net Position as bond interest expense.

1.1.7 Compensated Absences

Employees accumulate earned but unused vacation and sick leave benefits. There is no liability for unpaid accumulated sick leave since the State does not pay any amounts when employees separate from State service. A liability for vacation leave (compensated absences) is accrued when incurred as employees may be paid for up to a maximum of 300 hours of accrued vacation leave upon separation from State service

1.2 Cash and Cash Equivalents

On June 30, 2016, the book balance of cash and cash equivalents was \$231,662,221 and the bank balance was \$231,675,820. All cash in the Fund is deposited in demand accounts with the State Treasurer in the Oregon Short-Term Fund (OSTF), a cash and investment pool for use by all state agencies.

The custodial credit risk for deposits is the risk that, in the event of a bank failure, the State Treasurer will not be able to recover deposits or will not be able to recover collateral securities that are in the possession of an outside party. The CWSRF does not have a policy regarding custodial credit risk for deposits; however, the insurance and collateral requirements for deposits in the OSTF are established by banking regulations and Oregon law.

Further details of the investments and a copy of the OSTF audited annual financial report may be obtained by writing to the Oregon State Treasury, 350 Winter Street NE, Suite 100, Salem, Oregon 97301-3896 or located at the following web site:

[http://www.oregon.gov/treasury/Divisions/Investment/Pages/Oregon-Short-Term-Fund-\(OSTF\).aspx](http://www.oregon.gov/treasury/Divisions/Investment/Pages/Oregon-Short-Term-Fund-(OSTF).aspx)

1.3 Loans Receivable

The Fund makes loans to qualified entities at interest rates ranging from zero percent to the market rate (see ORS 468.440). Interest rates vary depending on the length of the loan, the type of loan, and program rules (at OAR 340-054). Rates range from 25% of the bond rate for 5 year loans to 55% of the bond rate for 30 year loans. Recipients make semiannual or, in some cases, annual payments, and must begin loan principal and interest repayments within one year of the date the facility is operationally complete and ready for the purpose it was planned, designed, and built or the project is completed, as determined by DEQ. There is an allowance account for that portion of loan disbursements that will not be repaid due to principal forgiveness offered to some borrowers. Principal forgiveness is offered to some borrowers, based on criteria in administrative rule, to comply with a requirement included in DEQ's grant agreement with EPA. There is no additional allowance account, because Fund management believes all existing

borrowers will pay as agreed. The detail of loans receivable as of June 30, 2016 is as follows:

Loans Receivable	\$421,364,685
Principal Forgiveness on Disbursements	<u>(1,643,627)</u>
Net Loans Receivable, 6/30/2016	<u>\$419,721,058</u>

1.4 Bonds Payable

In July 2003 EPA agreed to the use of the CWSRF Fund assets to pay the principal and interest on general obligation bonds that were previously issued by the State to provide the 20 percent state matching funds as required by the Clean Water Act. The following table summarizes bonds outstanding as of June 30, 2016:

Original Issue

Series	Due Dates	Interest Range	Original Amount
2008A	2009-2028	2%-4.5%	4,800,000
2009A	2010-2030	2%-4%	4,890,000
2010A	2011-2030	2%-3.75%	4,945,000
2012P ¹	2014-2033	1.5%-5.0%	4,235,000
2013K ¹	2014-2024	2.0%-5.0%	4,015,000
2015E ¹	2016-2026	5.0%	4,040,000
		Total:	\$ 26,925,000

¹2012P, 2013K and 2015E are bond issuances designated by the Oregon State Treasury. Internally DEQ CWSRF uses 2012A, 2013A and 2015A to identify the portions of the larger bond issuance for which the CWSRF is individually responsible.

Bonds Outstanding

Series	Balance 6/30/2015	Increases	Decreases	Balance 6/30/2016	Due Within One Year
2008A	3,527,743	-	209,032	3,318,711	216,774
2009A	3,180,000	-	220,000	2,960,000	250,000
2010A	3,940,000	-	210,000	3,730,000	215,000
2012P ¹	4,030,000	-	150,000	3,880,000	160,000
2013K ¹	3,705,000	-	345,000	3,360,000	355,000
2015E ¹	4,040,000	-	-	4,040,000	320,000
Total:	\$ 22,422,743	-	\$ 1,134,032	\$ 21,288,711	\$ 1,516,774

¹2012P, and 2013K and 2015E are bond issuances designated by the Oregon State Treasury. Internally DEQ CWSRF uses 2012A, 2013A and 2015A to identify the portions of the larger bond issuance for which the CWSRF is individually responsible.

The bond interest rates noted above differ depending on the term of the individual security. Thus, those securities with the longest term yield the highest interest rate.

The following table summarizes the amounts necessary to pay all future bonded debt principal and interest requirements as of June 30, 2016 for each year during the next five-year period ending June 30, 2021, and in five year increments thereafter.

Years Ending June 30	Bond Principal	Bond Interest	Total Debt Service
2017	1,516,774	869,808	2,386,582
2018	1,514,516	809,345	2,323,861
2019	1,714,839	741,045	2,455,884
2020	1,847,581	662,847	2,510,428
2021	1,747,903	583,687	2,331,590
2022 - 2026	8,480,645	1,721,744	10,202,389
2027 - 2031	3,876,453	390,720	4,267,173
2032 - 2033	590,000	17,850	607,850
Total:	\$ 21,288,711	\$ 5,797,046	\$ 27,085,757

1.5 Changes in Long-Term Liabilities

The liability for compensated absences is calculated based on the vacation accrual at June 30, 2016 for each employee whose duties include CWSRF related activities. Bonds payable includes amounts payable on bonds issued to benefit the CWSRF fund, and also includes the unamortized amounts of bond discount or premium.

The long term liability activity for the year ended June 30, 2016 was as follows:

	Beginning Balance 7/1/2015	Increases	Decreases	Ending Balance 6/30/2016	Due Within One Year
Bonds Payable	22,422,743	-	1,134,032	21,288,711	1,516,774
Issuance Premium	2,054,124	-	198,324	1,855,800	
Issuance Discount	(21,377)	-	(1,483)	(19,894)	
<i>Total Bonds Payable</i>	24,455,490	-	1,330,873	23,124,617	1,516,774
Compensated Absences	63,977	70,347	63,977	70,347	58,473
Total Long-term Liabilities:	24,519,467	70,347	1,394,850	23,194,964	1,575,247

1.6 Loan Fees

In order to support administration and project management costs, loan fees are assessed on loans originating after 1992. A fee of 0.50 percent is assessed on the outstanding loan principal balance and is collected annually, beginning with the second loan payment.

Fees are deposited to a separate Treasury account and are used only for administrative and project management costs. Planning loans are not assessed annual fees in order to encourage Oregon communities to complete more planning.

1.7 Employee Retirement Plan

Plan Description

As part of the State of Oregon, the Public Employees Retirement System (PERS) provides defined benefit and defined contribution retirement plans to the Fund's employees. PERS is a cost-sharing multiple-employer defined benefit pension plan. All benefits of PERS are established by the legislature pursuant to ORS Chapters 238 and 238A. Tier One/Tier Two Retirement Benefit plan, established by ORS Chapter 238, is closed to new members hired on or after August 29, 2003. The Oregon Public Service Retirement Plan (OPSRP), established by ORS 238A, provides benefits to members hired on or after August 29, 2003. The Individual Account Program (IAP) is a defined contribution plan. Beginning January 1, 2004, all member contributions are deposited into the members IAP account. The pension plans provide pension benefits, death benefits, and disability benefits.

PERS issued a separate, publicly available, audited financial report that may be obtained from the Fiscal Services Division, Public Employees Retirement System, P.O. Box 23700, Tigard, Oregon 97281-3700.

Contributions

PERS funding policy provides for monthly employer contributions at actuarially determined rates. These contributions, expressed as a percentage of covered payroll, are intended to accumulate sufficient assets to pay benefits when due. The rates in effect for the fiscal year ended June 30, 2016 for state agencies general service members were 12.31% for Tier One/Tier Two and 6.51% for OPSRP. The IAP member contribution as set by statute is 6% and is currently paid by state agencies.

Employer contributions for the fiscal year ended June 30, 2016 were \$64,000 for Tier One/Tier Two and \$23,887 for OPSRP. Member contributions for the fiscal year ended June 30, 2016 were \$53,210.

Pension Liabilities, Pension Expense, Deferred Outflows of Resources, and Deferred Inflows of Resources

At June 30, 2016, the State of Oregon reported a liability of \$1.1 billion for its proportionate share of the net pension liability. The net pension liability was measured as of June 30, 2015, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of December 31, 2013. The State's proportion of the net pension liability was based on a projection of the State's long-term share of contributions of all participating employers, actuarially determined. At the June 30, 2015 measurement date, the State's proportion was 19.7%.

The Fund's portion of the net pension liability was not specifically identified. See Note 14. Employee Retirement Plans, in the State of Oregon Comprehensive Annual Financial Report, for more detail.

1.8 Other Postemployment Benefit Plans

The Fund's employees may be eligible to participate in health insurance plans and other benefit plans after retirement, collectively known as Other Postemployment Benefits (OPEB). OPEB plans are offered through the Public Employees Retirement System (PERS) as established by

ORS 238 and the Public Employees Benefit Board (PEBB) as established by ORS 243. A copy of the audited annual financial report may be obtained from Fiscal Services Division, Public Employees Retirement System, P.O. Box 23700, Tigard, Oregon 97281-3700.

Retirement Health Insurance Account

The Retirement Health Insurance Account (RHIA) is a cost-sharing multiple-employer OPEB plan which provides a payment of up to \$60 toward the monthly cost of health insurance for eligible PERS members. To be eligible for the RHIA subsidy, the member must: 1) have eight years or more of qualifying service in PERS at the time of retirement or receive a disability allowance as if the member had eight years or more creditable service in PERS, 2) receive both Medicare Parts A and B coverage, and 3) enroll in a PERS-sponsored health insurance plan.

The Department is required by statute to contribute actuarially computed amounts as determined by PERS. Rates are subject to change as a result of subsequent actuarial valuations. The rate of each covered employee's salary for the fiscal year end June 30, 2016 was 0.53 percent. Combined employer contributions for the years ended June 30, 2016, 2015 and 2014, was approximately \$4,370, \$5,445 and \$5,165, respectively, equal to the required contributions each year.

Retiree Health Insurance Premium Account

The Retiree Health Insurance Premium Account (RHIPA) is a single-employer OPEB plan that provides for payment of the average difference between the health insurance premiums paid by retired state employees, under contracts entered into by the PERS Board, and the health insurance premiums paid by state employees who are not retired. Retired state employees are qualified to receive the RHIPA subsidy if they had eight or more years of qualifying service in PERS at the time of retirement or are receiving a disability pension calculated as if they had eight or more years of qualifying service, but are not eligible for federal Medicare coverage.

The Department is required by statute to contribute actuarially computed amounts as determined by PERS. Rates are subject to change as a result of subsequent actuarial valuations. The rate of each employee's covered salary for the fiscal year ended June 30, 2016 was 0.44 percent. The Fund's actual contribution for the year ended June 30, 2016, 2015 and 2014 was approximately \$3,719, \$2,370, and \$2,310, respectively, which was equal to the actuarial required contribution.

Public Employees Benefit Board Plan

The Public Employees Benefit Board (PEBB) plan is a single-employer plan which offers medical, dental and vision benefits to eligible retired employees. Chapter 243 of the Oregon Revised Statutes assigns PEBB the authority to establish and amend the benefit provisions of the PEBB Plan. The PEBB Plan allows qualifying retired employees to continue their healthcare on a self-pay basis until eligible for Medicare, usually at age 65. The PEBB Plan funding policy provides for contributions at amounts sufficient to fund benefits on a pay-as-you-go basis. Active employees do not make contributions. Participating retirees pay their own monthly premiums based on a blended premium rate since retirees are pooled together with active employees for insurance rating purposes. PEBB activity is reported as part of the State of Oregon's annual report and does not issue a separate financial report.

The State of Oregon's liability for the primary government was \$55.5 million for the fiscal year ended June 30, 2016. The Fund's portion of this liability was not specifically identified.

1.9 Commitments

As of June 30, 2016 the CWSRF has active loan agreements in the amount of \$222,871,928 and has disbursed a total of \$67,963,605 in cash to these active borrowers. The amount of undisbursed loan commitments is, therefore, \$154,908,323.

1.10 Risk Financing

The Department of Administrative Services, Enterprise Goods and Services, Risk Management section (Risk Management) administers the State's property, liability, and workers' compensation insurance program. Risk Management has found it is more economical to manage the risk of loss internally and, therefore, minimizes the purchase of commercial insurance policies to the extent possible. The monies set aside by Risk Management under Chapter 278 of the Oregon Revised Statutes are used to service the following risks:

- Direct physical loss or damage to State property
- Tort liability claims brought against the State, its officers, employees, or agents
- Inmate injury
- Workers' compensation
- Employee dishonesty
- Faithful performance bonds for key positions as required by law and additional positions as determined by agency policy

Risk Management purchases commercial insurance for specific insurance needs not covered by self-funding. For example, the self-insured property and liability program is backed by an excess property policy with a limit of \$400 million and a blanket commercial crime policy with a limit of \$20 million. The amount of claim settlements did not exceed commercial insurance coverage for each of the past three fiscal years.

All State agencies, commissions, and boards participate in the self-insured property and liability program. Risk Management allocates the cost of claims and claim administration by charging an assessment to each State agency, based on its share of losses. Statewide risk charges are based on independent biennial actuarial forecasts and division expenses, less any available fund balance from the prior biennium.

The CWSRF participates in this risk financing program through DEQ, which, as a State agency, is a participant. Settlements have not exceeded insurance coverage in each of the past three years.

1.11 Subsequent Events

On August 3, 2016 the federal fiscal year 2016 capitalization grant from EPA was awarded, in the amount of \$15,094,000. This amount provides additional capitalization for the CWSRF program.

OTHER REPORT

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Secretary of State

Leslie Cummings, Ph.D.
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Independent Auditor's 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 Kate Brown
Governor of Oregon

Richard Whitman, Director
Oregon Department of Environmental Quality

We have audited, in accordance with the 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, the financial statements of the Clean Water State Revolving Fund (CWSRF) program, an enterprise fund of the State of Oregon, Department of Environmental Quality (department) as of and for the year ended June 30, 2016, and the related notes to the financial statements, which collectively comprise the CWSRF program's basic financial statements, and have issued our report thereon dated June 19, 2017.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the department's internal control over financial reporting (internal control) related to the CWSRF program to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the department's internal control. Accordingly, we do not express an opinion on the effectiveness of the department's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. *A material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. *A significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the department's CWSRF program's financial statements are free from 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*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the department's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the department's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Office of the Secretary of State, Audits Division

State of Oregon
June 19, 2017

About the Secretary of State Audits Division

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

Audit Team

Mary E. Wenger, CPA, Deputy Director
Kelly L. Olson, CPA, Audit Manager
Diane Farris, CPA, Principal Auditor
Kalindi Devi-Dasi, Staff Auditor

This report, a public record, is intended to promote the best possible management of public resources. Copies may be obtained from:

website: <http://sos.oregon.gov/audits>

phone: 503-986-2255

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The courtesies and cooperation extended by officials and employees of the Department of Environmental Quality during the course of this audit were commendable and sincerely appreciated.