



State of Oregon

OREGON SHORT TERM FUND

An Investment Pool of the State of Oregon

Financial Statements

For the Year Ended June 30, 2015

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OREGON SHORT TERM FUND
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FINANCIAL SECTION

Office of the Secretary of State

Jeanne P. Atkins
Secretary of State

Robert Taylor
Deputy Secretary of State



Audits Division

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Independent Auditor's Report

The Honorable Kate Brown, Governor of Oregon
The Honorable Ted Wheeler, State Treasurer
Oregon Investment Council
Oregon Short Term Fund Board

Report on the Financial Statements

We have audited the accompanying financial statements of the Oregon Short Term Fund, an investment pool of the State of Oregon, as of and for the year ended June 30, 2015, 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 these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free 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 Oregon Short Term Fund as of June 30, 2015, and the changes in financial position thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 1, the financial statements of the Oregon Short Term Fund, an investment pool of the State of Oregon, are intended to present the financial position and the changes in financial position of only the Oregon Short Term Fund. They do not purport to, and do not, present fairly the financial position of the Oregon State Treasury or the State of Oregon as of June 30, 2015, or the changes in their financial position for the year then ended in accordance 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 August 27, 2015, on our consideration of the Oregon State Treasury's 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* in considering the Oregon State Treasury's internal control over financial reporting and compliance.

Office of the Secretary of State, Audits Division

State of Oregon
August 27, 2015

State of Oregon
OREGON SHORT TERM FUND

Statement of Net Position

June 30, 2015

(Dollars in Thousands)

Assets:	
Cash and Cash Equivalents	\$ 2,591,761
Investments	10,995,852
Due from Department of Human Services (Note 5)	13,000
Due from Oregon Military Department (Note 5)	3,000
Accrued Interest Receivable	17,239
Securities Lending Collateral (Note 3)	500,384
	<hr/>
Total Assets	14,121,236
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Liabilities:	
Due to Oregon Employment Department (Note 6)	10
Due to Broker on Purchase	41,762
Obligations Under Securities Lending (Note 3)	500,384
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Total Liabilities	542,156
	<hr/>
Net Position:	
Held in Trust for Participants	13,579,080
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Total Net Position	\$ 13,579,080
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The accompanying notes are an integral part of the financial statements.

State of Oregon
OREGON SHORT TERM FUND
Statement of Changes in Net Position
For the Year Ended June 30, 2015
(Dollars in Thousands)

Additions:	
Participants' Contributions	\$ 54,823,382
Investment Income, Net of Expenses (Notes 1, 4)	63,768
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Total Additions	54,887,150
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Deductions:	
Participants' Withdrawals	54,208,334
Distributions of Interest to Participants	71,341
Securities Lending Agent Fee Expense	180
Securities Lending Borrowers' Rebate Expense	471
	<hr/>
Total Deductions	54,280,326
	<hr/>
Change in Assets Held in Trust for Participants	606,824
Net Position - Beginning	12,972,256
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Net Position - Ending (Note 7)	\$ 13,579,080
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The accompanying notes are an integral part of the financial statements.

OREGON SHORT TERM FUND

Notes to Financial Statements

June 30, 2015

(1) Summary of Significant Accounting Policies

Reporting Entity The Oregon Short Term Fund (the Fund) is a short-term cash investment vehicle. A number of local governments in Oregon as well as all State agencies participate in the Fund, thus it is an external investment pool as defined in Statement No. 31 of the Governmental Accounting Standards Board, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*.

The Fund is not registered with the U.S. Securities and Exchange Commission as an investment company. The State's investment policies are governed by Oregon Revised Statutes and the Oregon Investment Council (the Council). The State Treasurer is the investment officer for the Council and is responsible for all funds entrusted to the Oregon State Treasury (OST). These funds must be invested, and the investments managed, as a prudent investor would, exercising reasonable care, skill and caution. Investments in the Fund are further governed by portfolio guidelines recommended by the Oregon Short Term Fund Board, with Council approval, establishing diversification percentages and specifying the types and maturities of investments. The portfolio guidelines permit securities lending transactions as well as investments in repurchase agreements and reverse repurchase agreements. Portfolio guidelines are discussed in greater detail in the Investments section of Note 2.

According to ORS 293.265 and 295.002, state agencies must deposit all funds with depositories qualified by the OST. Undesignated funds not required to meet current demands are deposited in the Fund; therefore, state agencies are considered involuntary participants of the Fund. Because the Fund operates as a demand deposit account for state agency participants, the portion of the Fund belonging to state agency (internal) participants is classified as cash and cash equivalents in the State's Comprehensive Annual Financial Report. The portion of the Fund belonging to local government (external) participants is reported in an investment trust fund in the State's Comprehensive Annual Financial Report.

Basis of Accounting These statements are prepared using the economic resources measurement focus and the accrual basis of accounting. Trade date accounting is observed, which means that purchases and sales of securities are recorded on the day the trade takes place with a corresponding payable to, or receivable from, the broker. Changes in the fair value of investments are recognized at the end of each year. The fair value of investments is determined annually and is equal to market price.

Cash and Cash Equivalents Investments with original maturities of three months or less are considered cash equivalents and are reported at amortized cost, which approximates fair value. Cash and Cash Equivalents also include cash in banks.

Investments Investments with remaining maturities of fewer than ninety days are carried at amortized cost, provided that the fair value of these instruments is not significantly affected by the impairment of the credit standing of the issuer or by other factors. Amortized cost approximates fair value. Investments with longer maturities are carried at fair value.

Participants' equity; distributions of interest Participants' account balances in the Fund are determined by the amount of participants' deposits, adjusted for withdrawals and distributed interest. The Fund has not provided or received any legally binding guarantees regarding balances in the Fund. Interest is calculated and accrued daily on each participant's account based on the ending account balance and a variable interest rate determined periodically by the OST. When a participant's account is overdrawn, negative interest accrues daily at the determined rate plus a premium. OST accumulates an amount to offset potential losses based on historical default rates, as part of Total Net Position (See Note 7). This balance is reviewed at the end of every month, and is considered in setting the rate paid to participants, exclusive of unrealized gains and losses. Interest is distributed monthly on the last business day of the month. If the last day of the month is a weekend or holiday, interest is accrued through the last calendar day of the month and posted on the last business day.

OREGON SHORT TERM FUND

Notes to Financial Statements

June 30, 2015

(2) Deposits and Investments

Deposits On June 30, 2015 the Fund held a \$57.0 million book balance in deposits with a bank balance of \$13.8 million. Insurance and collateral requirements for deposits are established by banking regulations and Oregon law. Where interest-bearing balances exceed the Federal Deposit Insurance amount of \$250,000, the balances are covered by collateral held in a multiple financial institution collateral pool (ORS 295.015) administered by the OST in the Public Funds Collateralization Program (PFCP). As of June 30, 2015, \$2.1 million of demand deposits were covered by FDIC insurance and \$11.7 million of demand deposits were collateralized under the PFCP.

Investments On June 30, 2015, the Fund had a net position of \$13.6 billion, \$2.6 billion of which is classified as Cash and Cash Equivalents on the Statement of Net Position. The Fund's portfolio rules establish the Fund's permitted investments and provide guidelines for managing the various types of risk associated with these investments (see the current portfolio rules at [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)). The different risks are discussed below.

A. Interest rate and credit risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The Fund staff manages this risk by limiting the period of the reset date (reset) or maturity of the investments held by the Fund. The portfolio rules require that at least 50 percent of the portfolio mature or reset within 93 days; not more than 25 percent of the portfolio may mature or reset in over a year; and no investments may mature or reset over three years from settlement date. The June 30, 2015 holdings are shown in the schedule below. For variable rate securities, the next interest rate reset date is used instead of the maturity date. For variable rate securities, in a fixed rate period that will switch to variable rate at a later date, the maturity is based on the final maturity of the security, not the next variable reset date. For fixed rate securities with a put option, the date upon which the put option is fully exercisable for at least 100% of the face value is used instead of the maturity date, and for variable rate securities with a put option, the earlier of the next variable reset date or the put date is used instead of the maturity date. For asset-backed securities, the weighted average life will be used as a proxy for the maturity date.

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligation. The Fund's policies provide for a composite minimum weighted average credit quality rating for the Fund's holdings to be the equivalent of a AA Standard and Poor's (S&P) rating. This composite is calculated based on the median rating if three agencies rate the security, the lower rating if two ratings are available, or the single rating if only one rating is available. On June 30, 2015, the fund's composite weighted average rating was equivalent to S&P's AA based on the method described above. U.S. Treasuries and all unrated federal agency securities were also assumed to be rated AAA for the composite rating, as these securities are backed by the U.S. government.

The minimum ratings for corporate notes at the time of purchase are an S&P rating of A-, a Moody's rating of A3 or a Fitch rating of A-. Commercial paper is required to have a minimum short-term credit rating at the time of purchase from two of three ratings services; minimum ratings are S&P of A-1, Moody's of P-1 and Fitch of F-1. Foreign government securities are required to have a minimum credit rating from S&P of AA-, Moody's of Aa3 or Fitch of AA-. Asset-backed securities are required to have long-term ratings of AAA, Aaa or AAA, or short-term ratings of A-1+, P-1 or F-1+ by S&P, Moody's, and Fitch, respectively.

Fund policies allow securities downgraded below the minimum required ratings at the time of purchase to be retained at the Director of Capital Markets' discretion. Rating groups were determined using the lowest actual rating from S&P, Moody's or Fitch, and are shown below:

OREGON SHORT TERM FUND
Notes to Financial Statements
June 30, 2015

Interest Rate and Credit Risk
(Dollars in Thousands)

Classification	Rating	One to Three				Par Value
		93 Days or Less	94-366 Days	Years	Total	
U.S. Treasury	Not Rated	\$ 1,140,080	\$ 25,041	\$ 505,752	\$ 1,670,873	\$ 1,670,000
Agency Securities	Not Rated(3)	776,149	-	370,794	1,146,943	1,145,770
Agency Discount Notes	Not Rated(3)	1,938,100	-	-	1,938,100	1,938,197
Municipal Commercial Paper	A-1+	325,813	-	-	325,813	
	A-1	221,776	-	-	221,776	
		547,589	-	-	547,589	547,629
Municipal Obligations	AA	54,996	12,043	-	67,039	
	A	-	8,500	15,082	23,582	
		54,996	20,543	15,082	90,621	90,560
Non U.S. Government Commercial Paper	A-1+	10,000	-	-	10,000	10,000
Non U.S. Government Obligations	AAA	-	-	5,536	5,536	
	AA	-	10,152	135,615	145,767	
	A	12,049	25,357	20,660	58,066	
		12,049	35,509	161,811	209,369	207,000
Corporate Commercial Paper	A-1	97,000	-	-	97,000	97,000
Corporate Obligations	AA	761,568	54,012	170,847	986,427	
	A	3,526,439	149,184	858,745	4,534,368	
	BBB(1)	533,726	50,623	296,071	880,420	
		4,821,733	253,819	1,325,663	6,401,215	6,388,675
Asset-Backed Securities	AAA	446,224	521,923	304,716	1,272,863	
	A-1+	48,185	22,607	-	70,792	
		494,409	544,530	304,716	1,343,655	1,342,761
Time Certificates of Deposit	Not Rated(2)	75,200	-	-	75,200	75,200
Cash	Not Rated	57,048	-	-	57,048	57,048
Total		\$ 10,024,353	\$ 879,442	\$ 2,683,818	\$ 13,587,613	\$ 13,569,840

¹ Securities rated BBB on this table continue to meet investment quality rules as discussed above, as they have at least one rating of S&P A-, Moody's A3 or Fitch A

² TCD's are considered deposits for purposes of credit quality, and are fully covered by FDIC and state PFCP programs

³ GASB 40 states that U.S. federal debt is considered to be without credit risk. For credit quality rules, federal debt is considered to be highest quality, except when rated differently

B. Custodial credit risk

Custodial credit risk for investments is the risk that, in the event of a transactional counterparty failure, the government will not be able to recover the value of an investment or collateral securities in the possession of an outside party. The Fund's portfolio rules provide that broker/dealers meet certain qualifications and that investments are delivered to and held by a third-party custodian, which holds the Fund's securities in the State of Oregon's name. Time certificates of deposit (TCDs) are not exposed to custodial credit risk, as they are covered by FDIC insurance of \$0.7 million and the balance of \$74.5 million is covered by the PFCP (ORS 295.015) administered by the OST.

OREGON SHORT TERM FUND

Notes to Financial Statements

June 30, 2015

C. Concentration of credit risk

Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer. The Fund rules provide that the maximum that may be invested in any one issuer, as a percentage of the fund's total investments, is 33 percent for U.S. Agency securities, 10 percent for foreign governments and instrumentalities, 5 percent for both commercial paper and corporate notes and 10 percent for all securities and support commitments with the exception of U.S. Treasury (100 percent) and Government Agency securities (33 percent per issuer). On June 30, 2015, the Fund did not hold investments with any one issuer that exceeded these limits. The schedule below lists those issuers where holdings are greater than 5 percent.

Schedule of issuers - Holdings Greater Than Five Percent (Dollars in Thousands)

<u>Issuer Name</u>	<u>Reported Amount</u>	<u>Percent of Holding</u>
Federal Home Loan Bank	\$1,877,682	13.90%
U.S Treasury	1,670,873	12.37%

D. Foreign currency risk

The Fund portfolio rules prohibit investments that are not U.S. dollar-denominated; therefore, the Fund is not exposed to this risk.

(3) Securities Lending

The OST has authorized its custodian to act as its agent in lending the Fund's securities pursuant to a form of loan agreement, in accordance with Fund investment policies. There have been no significant violations of the provisions of the securities lending agreement. The State's securities lending agent lent short-term and fixed income securities and received as collateral U.S. dollar-denominated cash and U.S. Treasury securities. Borrowers were required to deliver collateral for each loan equal to not less than 102 percent of the market value of the loaned security. The State may pledge or sell the collateral securities received only in the event of a borrower default. The State has the ability to impose restrictions on the amount of the loans that the securities lending agent made on its behalf. Several such restrictions were made during the year ended June 30, 2015. The State is fully indemnified by its securities lending agent against losses due to borrower default. There were no losses during the year from the failure of borrowers to return loaned securities.

The Fund's lending agent uses a fund to reinvest cash collateral received on behalf of the Fund and other Oregon state agencies managed by the OST, exclusive of the Oregon Public Employees Retirement Fund. At June 30, 2015 the Fund's allocated portion of the market value of repurchase agreements held by the fund was approximately \$247,000,000. Effective January 2014, the guidelines for the reinvestment of cash collateral were revised with further constraints to reduce overall risk. As permitted under the fund's Declaration of Trust (Declaration), participant purchases and redemptions are transacted at \$1.00 per unit ("constant value") based on the amortized cost of the fund's investments. Accordingly, the securities lending collateral held and the obligation to the lending agent are both stated at constant value on the Statement of Net Position. The balances of securities on loan, collateral received and invested collateral at market value are presented in the schedule below.

OREGON SHORT TERM FUND
Notes to Financial Statements
June 30, 2015

Schedule of Securities Lending Balances
(Dollars in Thousands)

	Securities on Loan at		Invested Cash Collateral at
	Fair Value	Collateral Received	Fair Value
U.S. Agency Securities	\$ 83,541	\$ 85,215	\$ 85,220
U.S. Treasury	650,110	663,830 ¹	357,113
Corporate Notes	75,134	76,735 ²	58,077
Total	\$ 808,785	\$ 825,780	\$ 500,410

¹ Cash Collateral \$357,095, US Treasury \$306,735

² Cash Collateral \$58,074, Corporate Notes \$18,661

The State and borrowers maintained the right to terminate all securities lending transactions on demand. As a consequence, the maturities of investments made with cash collateral generally do not match the maturities of the securities loans. As of June 30, 2015, the State had no credit risk exposure to borrowers related to securities on loan.

(4) Management Fees

In accordance with ORS 293.718, the OST may deduct monthly 0.435 basis points of the most recent market value of assets under management for administration and portfolio management. For the year ended June 30, 2015 the OST charged the Fund a monthly rate of 0.30 basis points based on average daily balances in the Fund. The fee is deducted from investment income before distributions to participants. Fees charged to the Fund totaled \$5.4 million for the year ended June 30, 2015.

(5) Receivables from the Oregon Department of Health and Human Services and Oregon Military Department

The Oregon Department of Human Services entered into an agreement in April of 2015 to borrow up to \$15 million for the purpose of interim financing until revenues from provider tax and other funds become available. Interest is charged at a fixed rate equal to two (2) percent per annum. The loan will mature on the earlier of December 31, 2015 or on the date OST determines the Fund requires repayment to meet current Fund requirements.

The Oregon Military Department entered into an agreement in April of 2015 to borrow up to \$3 million for the purpose of interim financing until revenues from federal reimbursement funds become available. Interest is charged at a fixed rate equal to two (2) percent per annum. The loan will mature on the earlier of September 30, 2015 or on the date OST determines the Fund requires repayment to meet current Fund requirements.

OREGON SHORT TERM FUND

Notes to Financial Statements

June 30, 2015

(6) Payable to the Oregon Employment Department

The OST maintains accounts separate from the Fund which contains employment benefit and trust funds in the name of the Oregon Employment Department (Employment), which is also a participant in the Fund. The OST processes transfers of employment taxes and benefit payments between state agencies and Employment. Occasionally a transfer will be recorded between participants' accounts on one day, but the transfer of cash between the Fund and the employment benefit and trust funds does not take place until the following day, creating either a receivable from or payable to Employment.

(7) Equity of Internal and External Participants

The following table describes the equity of internal and external participants in the Fund's net position, and shows that net position is composed of participants' account balances less undistributed and unrealized losses:

Net position held in trust for participants (in thousands):	
Equity of internal participants	\$ 8,128,541
Equity of external participants	<u>5,450,539</u>
	<u>\$ 13,579,080</u>
Net position consist of (in thousands):	
Participants' Account Balances	\$ 13,483,936
Undistributed and Unrealized Gains	47,497
Allowance for Potential Defaults	<u>47,647</u>
	<u>\$ 13,579,080</u>
Participants' Fair Value (Net Position divided by Participants' Account Balances)	<u>100.71%</u>

OTHER REPORTS

Office of the Secretary of State

Jeanne P. Atkins
Secretary of State

Robert Taylor
Deputy Secretary of State



Audits Division

Gary Blackmer
Director

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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
The Honorable Ted Wheeler, State Treasurer
Oregon Short Term Fund Board
Oregon Investment Council

We have audited, 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, the financial statements of the Oregon Short Term Fund, an external investment pool of the State of Oregon, as of and for the year ended June 30, 2015, and the related notes to the financial statements and have issued our report thereon dated August 27, 2015.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Oregon State Treasury's internal control over financial reporting (internal control) to determine 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 Oregon State Treasury's internal control. Accordingly, we do not express an opinion on the effectiveness of Oregon State Treasury'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 Oregon Short Term Fund'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 entity'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 entity'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
August 27, 2015