

OREGON SHORT-TERM FUND

Financial Statements and Supplementary Information
for the years ended June 30, 2000 and 1999

OREGON SHORT-TERM FUND

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

The Honorable Jim Hill, State Treasurer, and
the Oregon Short-Term Fund Board
Oregon State Treasury
350 Winter Street NE, Suite 100
Salem, Oregon 97310-0840

INDEPENDENT AUDITOR'S REPORT

We have audited the accompanying financial statements of the Oregon Short-Term Fund (OSTF), as listed in the table of contents, as of and for the years ended June 30, 2000 and 1999. These financial statements are the responsibility of OSTF management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial status of the Oregon Short-Term Fund as of June 30, 2000 and 1999, and the changes in its net assets for the years then ended in conformity with generally accepted accounting principles.

Our audits were made for the purpose of forming an opinion on the financial statements taken as a whole. The accompanying Schedule of Investments and Cash Equivalents listed as supplementary information in the foregoing table of contents is presented for purposes of additional analysis and is not a required part of the financial statements of the OSTF. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly presented in all material respects in relation to the financial statements taken as a whole.

In accordance with *Government Auditing Standards*, we have also issued our report dated August 22, 2000, on our consideration of the OSTF's internal control over financial reporting and on our tests of its compliance with certain provisions of laws and regulations.

OREGON AUDITS DIVISION

<SIGNED>

Sharron E. Walker, CPA, CFE
Deputy Director

Fieldwork Completion Date:
August 22, 2000

OREGON SHORT-TERM FUND

Statement of Net Assets

(Dollars in thousands)

	<u>June 30, 2000</u>	<u>June 30, 1999</u>
Assets:		
Cash equivalents	\$ 2,923,232	\$ 2,515,417
Investments	3,295,980	4,143,830
Receivable from broker	-	49,746
Accrued interest receivable	<u>9,973</u>	<u>18,782</u>
 Total assets	 <u>6,229,185</u>	 <u>6,727,775</u>
Liabilities:		
Payable to broker	199,997	-
Payable to Employment (note 8)	42	-
Bank overdraft (note 7)	-	34,149
Obligations under securities lending (note 4)	<u>496,930</u>	<u>531,922</u>
 Total liabilities	 <u>696,969</u>	 <u>566,071</u>
 Net assets held in trust for participants (note 2)	 \$ <u>5,532,216</u>	 \$ <u>6,161,704</u>

See accompanying notes to financial statements.

OREGON SHORT-TERM FUND

Statement of Changes in Net Assets

(Dollars in thousands)

	Year ended <u>June 30, 2000</u>	Year ended <u>June 30, 1999</u>
Additions:		
Participants' contributions net of withdrawals	\$ -	\$ 785,167
Participants' contributions	32,273,752	-
Investment income, net of expenses (notes 2, 6)	<u>372,674</u>	<u>321,053</u>
Total additions	<u>32,646,426</u>	<u>1,106,220</u>
Deductions:		
Participants' withdrawals	32,902,445	-
Distributions of interest to participants	341,504	305,369
Securities lending agent fees expense	293	151
Securities lending borrowers' rebate expense	<u>31,672</u>	<u>21,649</u>
Total deductions	<u>33,275,914</u>	<u>327,169</u>
Net increase (decrease) in net assets	(629,488)	779,051
Net assets held in trust at beginning of year	<u>6,161,704</u>	<u>5,382,653</u>
Net assets held in trust at end of year (note 2)	\$ <u>5,532,216</u>	\$ <u>6,161,704</u>

See accompanying notes to financial statements.

OREGON SHORT-TERM FUND

Notes to Financial Statements

June 30, 2000 and 1999

(1) Organization of the Fund

The Oregon Short-Term Fund (Fund) is one of five asset classes approved for the investment of State of Oregon (State) funds. 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 the Oregon Revised Statutes and the Oregon Investment Council (Council). The State Treasurer is the investment officer for the Council and is responsible for all funds in the State Treasury. 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 issued by the Oregon Short-Term Fund Board, which establish diversification percentages and specify the types and maturities of investments. The portfolio guidelines permit securities lending transactions as well as investments in repurchase agreements and reverse repurchase agreements. The Fund was in compliance with all portfolio guidelines at June 30, 2000.

According to ORS 295.025, state agencies must deposit all funds with depositories qualified by the State Treasury. Undesignated funds not required to meet current demand 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 on the combined balance sheet 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.

(2) Summary of Significant Accounting Policies

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. Interest income and expenses are recognized on an accrual basis. 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 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 equivalents also includes cash in banks totaling \$4,184,000 at June 30, 2000, and \$16,257,000 at June 30, 1999.

OREGON SHORT-TERM FUND

Notes to Financial Statements (continued)

June 30, 2000 and 1999

Investments. Investments with remaining maturities of up to ninety days are carried at amortized cost, which 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. 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 State Treasury. The interest rate approximates the actual yield of the Fund 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 but posted on the last business day.)

The following table describes the equity of internal and external participants in the Fund's net assets, and shows that net assets are composed of participants' account balances and undistributed and unrealized gains (losses). The presentation for June 30, 1999 has been changed in that \$1,082,000 in retained earnings is classified as "Undistributed and unrealized gains (losses)" instead of "Participants' account balances" in order to conform to the presentation for June 30, 2000.

	<u>June 30, 2000</u>	<u>June 30, 1999</u>
Net assets held in trust for participants:		
Equity of internal participants	\$ 2,885,972	\$ 3,390,994
Equity of external participants	<u>2,646,244</u>	<u>2,770,710</u>
	\$ <u>5,532,216</u>	\$ <u>6,161,704</u>
Net assets consist of:		
Participants' account balances	\$ 5,538,044	\$ 6,166,737
Undistributed and unrealized gains (losses)	<u>(5,828)</u>	<u>(5,033)</u>
	\$ <u>5,532,216</u>	\$ <u>6,161,704</u>
Participants' fair value (net assets divided by participants' account balances)	\$ <u>.999</u>	\$ <u>.999</u>

OREGON SHORT-TERM FUND

Notes to Financial Statements (continued)

June 30, 2000 and 1999

(3) Cash Equivalents and Investments (Dollars in Thousands)

Three categories of credit risk apply to cash equivalents and investments of the Oregon Short-Term Fund:

1. Insured or registered, or securities held by the State or by its agent in the State's name.
2. Uninsured or unregistered, with securities held by the counterparty's trust department or agent in the State's name. (The Fund held no investments in this category at June 30, 2000).
3. Uninsured or unregistered, with securities held by the counterparty or its trust department or agent not in the State's name.

Investments and cash equivalents held in each category are reported in the Schedule of Custodial Category Risk.

Schedule of Custodial Category Risk
June 30, 2000
(Dollars in thousands)

	Yield	Maturity dates	Par value	Category		Reported amount*
				1	3	
Investments and cash equivalents— categorized:						
Not on loan:						
U.S. Government agency	6.16% - 7.20%	7/5/00 - 10/1/01	\$ 2,521,530	2,449,679		\$ 2,449,679
Bankers' acceptance	6.67%	9/25/00	27,000	26,577		26,577
Commercial paper	6.21% - 6.79%	7/5/00 - 9/20/00	2,697,031	2,683,431		2,683,431
Time certificates of deposit	6.59% - 6.67%	7/19/00 - 8/16/00	74,550	21,338	53,212	74,550
			5,320,111	<u>5,181,025</u>	<u>53,212</u>	5,234,237
Investments and cash equivalents— not categorized:						
Held by broker-dealers under securities loans:						
U.S. Government agency	6.49% - 7.17%	2/1/01 - 10/1/01	496,000			484,654
Securities lending collateral short-term investment fund	5.38% - 6.85%	7/5/00 - 12/15/05	496,930			496,137
			992,930			980,791
			\$ <u>6,313,041</u>			\$ <u>6,215,028</u>

* Reported amount is a combination of amortized cost and fair value. See Note 2.

OREGON SHORT-TERM FUND

Notes to Financial Statements (continued)

June 30, 2000 and 1999

(4) Securities Lending

The State Treasury has authorized its custodian to act as its agent in the lending of 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 securities lending agreements.

The State's securities lending agent lent short-term and fixed income securities and received as collateral U.S. dollar-denominated cash. Securities lent at year-end for cash collateral are presented as "not categorized" in the schedule of custodial credit risk. Cash collateral is invested in a short-term investment fund maintained by the custodial agent. The Fund's share of the short-term investment fund is presented as "not categorized" in the schedule of custodial credit risk.

Borrowers were required to deliver cash collateral for each loan equal to not less than 102% of the market value of the loaned security. The State did not impose any restrictions during the year on the amount of the loans that the securities lending agent made on its behalf. 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 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, 2000, the State had no credit risk exposure to borrowers related to securities on loan.

(5) Derivatives

The Governmental Accounting Standards Board's Technical Bulletin No. 94-1, *Disclosures about Derivatives and Similar Debt and Investment Transactions*, defines derivatives as contracts whose value depends on, or derives from, the value of an underlying asset, reference rate, or index. Derivatives are generally used to enhance return while managing the overall risk of the Fund. Derivatives are not acceptable collateral for repurchase agreements, and the Fund does not hold or issue derivative financial instruments for trading purposes. Following is a summary of derivatives held by the Fund.

Asset-backed securities. The Fund participates in a short-term investment fund maintained by the securities lending agent in which the cash collateral received from securities loans is invested. At June 30, 2000, the Fund's balance in the fund totaled \$496,137,000 at fair value. Investments in asset-backed securities accounted for 8.9% of the total fair value of the fund maintained by the securities lending agent at June 30, 2000. At June 30, 1999, the Fund's balance in the fund totaled \$532,088,000 at fair value. Investments in asset-backed securities accounted for 8.3% of the total fair value of the fund maintained by the securities lending agent at June 30, 1999. (Investments in this category are limited to 10% of the portfolio.) These securities are issued by major bank holding companies and are collateralized by the revenue streams arising from the banks' credit card and auto loan portfolios.

Floating rate notes. The Fund held floating rate notes issued by U.S. government agencies totaling \$1,050,120,000 at June 30, 1999. (No floating rate notes were held at June 30, 2000.) The coupon rates on

these notes are typically reset once per week with reference to a U.S. Treasury bill rate. Floating rate notes are reported at fair value or amortized cost depending on their remaining maturities as described in note 2, above. The short-term investment fund maintained by the securities lending agent in which the Fund participates also invests in floating rate instruments. At June 30, 2000, 18.4% of the total fair value of the securities lending agent's fund was invested in asset-backed securities and bank notes with floating rates based on the one-month or three-month LIBOR. At June 30, 1999, 16.8% of the total fair value of the securities lending agent's fund was invested in asset-backed securities and bank notes with floating rates based on the one-month or three-month LIBOR. At June 30, 2000, 22.3% of the total fair value of the securities lending agent's fund was invested in U.S. Government agency securities with floating rates based on the one-month or three-month LIBOR. At June 30, 1999, 17.9% of the total fair value of the securities lending agent's fund was invested in U.S. Government agency securities with floating rates based on the one-month LIBOR, the federal funds rate, or the prime rate.

(6) Management Fees

In accordance with ORS 293.718, the State Treasury may deduct monthly 0.25 basis points of the most recent market value of assets under management for administration and portfolio management. For the years ended June 30, 2000 and 1999, the State Treasury charged the Fund a monthly rate of 0.25 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 \$1,836,918 and \$1,254,000 for the years ended June 30, 2000 and 1999, respectively.

(7) Bank Overdraft

A bank overdraft existed at June 30, 1999. Bank overdrafts are a recognized and expected occurrence in the operation of the Fund. Daily investment decisions must be made by 1:00 PM Pacific time to coincide with closing of the financial markets; however, the investment officer does not always have full information on net deposits and withdrawals of Fund participants until later in the day.

(8) Payable to Employment

The State Treasury maintains accounts separate from the Fund which contain employment benefit and trust funds in the name of the Oregon Department of Employment, which is also a participant in the Fund. The State Treasury processes transfers of employment taxes between state agencies and the Oregon Department of 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 a payable to Employment.

OREGON SHORT-TERM FUND

Supplementary Information
for the year ended June 30, 2000

OREGON SHORT-TERM FUND

Schedule of Investments and Cash Equivalents

June 30, 2000

(Dollars in thousands)

	<u>Par value</u>	<u>Reported amount</u>	<u>Percentage</u>
Investments and cash equivalents not on loan – categorized:			
U.S. Government agency securities:			
Agency bonds:			
Federal Farm Credit Bank	\$ 489,000	487,252	
Total agency bonds	<u>489,000</u>	<u>487,252</u>	7.8%
Agency discount notes:			
Federal Farm Credit Bank	807,908	774,879	
Federal Home Loan Mortgage Corporation	1,069,622	1,033,716	
Farmer Mac	25,000	24,015	
Tennessee Valley Authority	<u>130,000</u>	<u>129,817</u>	
Total agency discount notes	<u>2,032,530</u>	<u>1,962,427</u>	31.6%
Total U.S. Government agency securities	<u>2,521,530</u>	<u>2,449,679</u>	39.4%
Bankers' acceptances:			
Bank of America	<u>27,000</u>	<u>26,577</u>	0.4%

OREGON SHORT-TERM FUND

Schedule of Investments and Cash Equivalents, continued

(Dollars in thousands)

	<u>Par value</u>	<u>Reported amount</u>	<u>Percentage</u>
Commercial paper:			
Gas transmission:			
Equitable Resources Inc.	\$ 235,183	\$ 234,748	3.8%
Financial:			
American Honda Finance	240,000	237,471	
Associates Corp. North America	30,000	29,716	
Ciesco L.P.	35,000	34,859	
Cortez Capital	155,687	155,224	
Ford Motor Credit	200,000	199,691	
FPL Fuels, Inc.	42,800	42,730	
Gateway Fuel Co	87,069	86,211	
General Electric Capital Corp	30,000	29,989	
General Motors Acceptance Corp	145,000	143,599	
Toyota Motor Credit Corp	25,000	24,941	
Total financial	<u>990,556</u>	<u>984,431</u>	15.8%
Industrial:			
AES Hawaii, Inc.	95,000	94,371	
AES Shady	142,496	141,078	
Arnold Fuel, Inc.	36,909	36,802	
Total industrial	<u>274,405</u>	<u>272,251</u>	4.4%

OREGON SHORT-TERM FUND

Schedule of Investments and Cash Equivalents, continued

(Dollars in thousands)

	Par value	Reported amount	Percentage
Commercial paper continued:			
Utility-electric:			
Allegheny Energy	\$ 182,600	\$ 181,431	
Kansas City P&L	32,000	31,868	
Madison Gas & Electric	16,000	15,974	
Midamerican Energy Company	88,600	88,439	
Pacific Corp	10,000	9,983	
Pacific Gas & Electric Co	47,288	47,238	
Penn Electric Co	30,000	29,960	
Potomac Electric	116,513	116,186	
So California Edison Co	231,000	230,570	
South Carolina E&G	13,400	13,336	
South Carolina Fuel	22,758	22,679	
Southwestern Public Service	32,000	31,925	
Tampa Electric	20,000	19,967	
Virginia Electric & Power	85,000	84,558	
Wisconsin Electric Fuel	28,782	28,709	
Total utility-electric	955,941	952,823	15.3%
Utility-gas:			
Laclede Gas Compny	51,000	50,607	
Peoples Energy	145,500	144,299	
Peoples Gas & Light	35,000	34,853	
Songs Fuel	9,446	9,419	
Total utility-gas	240,946	239,178	3.9%
Total commercial paper	2,697,031	2,683,431	43.2%

OREGON SHORT-TERM FUND

Schedule of Investments and Cash Equivalents, continued

(Dollars in thousands)

	Par value	Reported amount	Percentage
Time certificates of deposit:			
American Pacific Bank	\$ 2,350	\$ 2,350	
Bank of Astoria	4,800	4,800	
Bank of the Cascades	16,600	16,600	
Bank of the Northwest	3,000	3,000	
Centennial Bank	28,800	28,800	
Northern Bank of Commerce	1,000	1,000	
Pacific Continental Bank	11,000	11,000	
Premierwest Bank	7,000	7,000	
Total time certificates of deposit	74,550	74,550	1.2%
Total investments and cash equivalents—categorized	5,320,111	5,234,237	84.2%
Investments and cash equivalents – not categorized:			
Held by broker-dealers under securities loans:			
U.S. Government agency securities	496,000	484,654	
Securities lending collateral short-term investment fund	496,930	496,137	
Total investments and cash equivalents—not categorized	992,930	980,791	15.8%
Total investments and cash equivalents	\$ 6,313,041	6,215,028	100.0%