Exhibit "1"

MEMO

DATE: October 13, 2017

TO: Fred Bruyns, Department of Consumer and Business Services, Workers Compensation Division

FROM: Claire Hertz, Chief Financial Officer, Beaverton School District

Mary Knigge, Chief Financial Officer, North Clackamas School District

Sarah Head, Director of Budget and Financial Services, Salem-Keizer Public Schools

RE: Response to proposed amendments to OAR 436-050-0150

This memo is in response to proposed amendments to OAR 436-050-0150 filed by DCBS on September 15, 2017. We propose the following changes to the proposed amendments to 436-050-0150, as noted below.

(4)- Financial Strength Analysis:

(c) The director will score the financial strength of an employer that is a municipal corporation as defined in ORS 297.405 that submits an audited ~~Comprehensive~~ Annual Financial Report, based on the following ratios:

(A) The **current ratio** is calculated by dividing current assets by current liabilities ~~plus deferred outflows~~.
(B) The **debt service ratio** is calculated by dividing total annual debt service by total annual revenue.
(C) The return-on-net assets ratio is calculated by dividing the sum of net income plus the income effect of the changes in pension obligations by the sum of ~~-~~net assets plus net pension liability. For fiscal years beginning after June 15, 2017 the return on net assets ratio is calculated by dividing sum of net income plus the income effect of the changes in pension and OPEB obligations by the sum of net assets plus net pension and OPEB liabilities.

(6) Financial strength based on municipal bond ratings.

Notwithstanding section (5) of this rule, a public self-insured employer with a municipal bond rating of ~~Aa3, AA-~~ A3, A-, or higher will be considered to have a strong financial strength rating.

The proposed change to (4) (c) is needed because not all government entities file a Comprehensive Annual Financial Report (CAFR) because of the additional cost and complexity associated with preparing a CAFR. The numbers needed to calculate the financial strength ratios should be available from an audited financial report, and requiring a CAFR may needlessly cause some entities to fail the ratio tests.

The proposed change to (4)(c)(A) is needed because deferred outflows are substantially not related to current commitments or liabilities, and will not be reflected in expenses in the next year. For financial reporting, "current" is defined as an asset providing resources or liability requiring the use of resources, which will be available (or used) within one year. Two common examples of deferred outflows are pension deferrals and deferred bond refunding losses. Pension deferrals are commonly amortized over five years, and bond refunding losses are typically amortized over much longer periods.

As an example, the **current ratio** for North Clackamas School District for the year ended June 30, 2016 calculated including and excluding deferred outflows is as follows:

Current Assets $56.5M / [Current Liabilities $41.0M + Deferred Outflows $39.7M] =.70

Current Assets $56.5M / Current Liabilities $41.0M = 1.38

Deferred Outflows in this example relate primarily to deferred loss on bond refunding, which is being amortized through 2031 and is substantially non-current.

The ratio calculation including deferred outflows is worth 0 points, and excluding deferred outflows is worth 2 points using DCBS' proposed scoring system.

The proposed change to (4)(c)(B) is recommended merely to provide clarification.

The proposed change to (4)(c)(C) is needed because a recent change in governmental accounting standards (GASB 68) now requires that future pension obligations be reported as a liability on the District's financial statements, regardless of how many years in the future this obligation is due. This has caused many governmental entities to report greatly increased Total Liabilities and greatly reduced or negative Net Position on the Statement of Net Position. These changes can significantly decrease **return on net assets ratio**, and provide a skewed picture of financial health. We propose that removing the pension liability and pension income effects from the **return on net assets ratio** calculation will provide a more accurate assessment of financial health. Additionally, a new accounting standard (GASB 75) is now in effect for financial statements beginning after June 15, 2017. This standard requires that future obligations related to post-employment benefits other than pensions (OPEB) be reported as a liability. We also propose a similar adjustment for the OPEB liability once this standard is used in financial reporting.

As an example, the **return on net assets ratio** for North Clackamas School District for the year ended June 30, 2016 calculated including and excluding Net Pension Liability (NPL) and Pension Income Effects (PIE) is as follows (negative amounts shown in parentheses):

Change in Net Position $(13.2M)/Net Position $11.2M = (118%)

[Change in Net Position $(13.2M) + PIE $28.2M]/[Net Position $(13.2M)+NPL $31.1M] = 35%

The ratio calculated including NPL and PIE is worth 0 points, and excluding NPL and PIE is worth 6 points using DCBS' proposed scoring system.

The proposed change to **(6) Financial strength based on municipal bond ratings** is needed because the criteria as stated exclude many entities with strong ratings. Ratings in the range of A1 to A3 or A+ to A- are considered strong, but are not included in the proposal. Without this change, many entities regarded as financially strong by external bond rating agencies and investors will not be considered strong by DCBS.

We appreciate your willingness to work with us to develop more meaningful methods of evaluation for school districts and other governmental entities. We would welcome further conversation before this proposal is finalized.