

MINUTES OF THE TREASURY OVERSIGHT COMMITTEE
ORANGE COUNTY, CALIFORNIA

REGULAR MEETING

April 24, 2002

APPROVED

July 24, 2002

The Regular Meeting of the Treasury Oversight Committee (TOC) was held on April 24, 2002 and called to order by Charles Schroeder, Chair, at 3:00 p.m.

Committee Members:

Present:

Charles Schroeder, Chair
Robert Fauteux, Member of the Public
Michael Schumacher, CEO
Bill Habermehl, Department of Education

Absent:

David Sundstrom, Auditor-Controller

Also present were:

John Moorlach, Treasurer-Tax Collector; **Dick Hilde**, Assistant Treasurer; **Paul Cocking**, Assistant Investment Officer; **Julia Xue**, Financial Analyst; **Brett R. Barbre**, Public Information Officer; **Holly Henderson**, Director of Communications; **Wendy Margarita**, Department of Education; **Eli Littner** and **Alan Marcum**, Internal Audit; **John Abbott**, County Counsel; **Alan Beek**, member of the public.

1. Meeting Called to Order

Charles Schroeder called the meeting to order.

2. Welcome and self-introductions

Introductions were made.

3. Public Comments

There were none.

4. Approval of Minutes

The Minutes of the January 16, 2002 were reviewed.

Recommended Action: Mr. Schroeder called for a motion to approve the Minutes as presented. Mr. Fauteux moved to approve the minutes, 2nd by Mr. Habermehl. Passed 4-0.

5. Chairman's Report

The Chairman had no comments.

6. Treasurer's Report

- a. The Fourth Annual Treasurer's Conference was a success. It was held on February 7, 2002 at Disney's Grand Californian. All of the speakers were excellent and the event was completely sold out.
- b. Treasurer Moorlach, Superintendent Habermehl, and Auditor-Controller Sundstrom were all re-elected on March 5, 2002.
- c. The annual business plan has been completed for the Treasurer-Tax Collector's office.
- d. The city of Tustin is in the process of approving their participation in the county investment pool.
- e. Assembly Bill AB 2182, carried by Orange County Assemblyman John Campbell for the Treasurer, was voted out of the Assembly Banking & Finance Committee on a vote of 13-0 on April 22, 2002.
- f. The proposed changes to the Investment Policy Statement (IPS) were not submitted to the Board for approval. They will be revisited in the future.
- g. A commercial paper narrative (ATTACHMENT A) will be produced quarterly by the financial analyst.

7. December 31, 2000 Annual Audit

The Annual Audit is complete and is attached (ATTACHMENT B).

Recommended Action: Mr. Schroeder called for a motion to receive and file the report as presented. Mr. Schumacher moved to receive and file, 2nd by Mr. Fauteux. Passed 4-0.

8. December 31, 2001 Annual Audit Proposals

The SB 866 Audit has been put out to bid. There are two or three firms that have indicated an interest in submitting a bid.

9. Rating Agency Status

Moody's will be asked to rate the county investment polls as an addition to Fitch Ratings.

10. Public Comments

There were no Public Comments.

13. Schedule Next Meeting Date

After lengthy badgering of Mr. Barbre, the next regular meeting was scheduled for July 24, 2002 in the Treasurer's Office, Conference Room A, 3:00 p.m.

14. Adjournment

Mr. Schroeder called for a motion to adjourn. Mr. Habermehl moved to adjourn, 2nd by Mr. Schumacher. Passed 4-0.

The meeting was adjourned at 3:44 p.m.

ATTACHMENT A



COUNTY OF ORANGE

OFFICE OF THE TREASURER-TAX COLLECTOR

HALL OF FINANCE & RECORDS
12 CIVIC CENTER PLAZA, ROOM G76
P. O. BOX 4515
SANTA ANA, CA 92701

JOHN M. W. MOORLACH, C.P.A., CFP
TREASURER-TAX COLLECTOR
(714) 834-7625

To: Investment Management Committee
From: Julia Xue, Financial Analyst
Subject: CP(ABCP) holdings as of 3/31/2002
Date: April 24, 2002

[Albis Capital Corp.](#)

A1+/P1/NR NR//

\$500 million [asset-backed commercial paper](#) program primarily backed by trade and term receivables rated Aa3 and energy, metals and minerals products. Credit Enhancement and Liquidity Support are provided by **J.P.Morgan Chase** through 100% standby letter of credit and \$350 million loan facility respectively.

[Autobahn Funding Corp.](#)

NR/P1/F1+ NR//

\$2.596 Billion [asset-backed commercial paper](#) program primarily backed by trade and term receivables, securities. Autobahn ABCP investors have a security interest in all of Autobahn's assets. Liquidity support is provided by **Deutsche Zentral-Genossenschafts Bank** and other P1-rated financial institutions.

[Barton Capital](#)

A1+/P1/NR NR//

\$7.681 billion [asset-backed commercial paper](#) program primarily backed by trade and term receivables. Credit Enhancement and Liquidity Support are provided by **Societe Generale** through letter of credit and 100% standby purchase facilities relating to each separate pool of receivables respectively.

[Bavaria GLB Corp](#)

A1/P1/NR NR//

\$1 Billion [asset-backed commercial paper](#) program primarily backed by securities rated Aa2 or higher issued by German Landes-banks. Its liquidity is supported by revolving loans by **Bayerische Hypo-und Vereinsbank AG, New York Branch**.

ATTACHMENT A

Concord Minute

A1/NR/F1

NR///

\$5 Billion asset-backed commercial paper program primarily backed by undivided percentage interests in long-term and short-term consumer and commercial receivables originated by US and non-US corporate entities. **Liberty Hampshire Company, LLC Dependent** is the sponsor with its liquidity commitments covering 100% of the face amount of CP outstanding.

Conduit Asset Backed Securities

NR/P1/F1+

NR///

\$1.5 Billion asset-backed commercial paper program primarily backed by debt securities rated at least Baa3 by Moody's. It has dynamic credit enhancement, and its liquidity support is provided by **ABN AMRO Bank N.V.**

Eiffel Funding

NR/P1/F1+

NR///

\$2.76 Billion asset-backed commercial paper program primarily backed by trade and term receivables, securities. Credit Enhancement and Liquidity Support are provided by **CDC Financial** through Committed Asset Purchase Agreement and Liquidity Asset Purchase Agreement respectively.

Galaxy Funding

A1+/P1/NR

NR///

\$10 billion asset-backed commercial paper program primarily backed by debt securities or financial assets rated at least Baa3 or better. Credit Enhancement is through letter of credit provided by a P-1 rated bank and Liquidity Support is by asset-specific revolving credit facility and liquidity asset purchase agreement.

Gannett Co.

A1/P1/NR

NR///

Gannett is a major media company that publishes 99 daily newspapers in U.S., incl. USA TODAY. It has a very strong cash flow generation. The company has \$6 billion in revolving credit agreements, which provide backup for the company's commercial paper program.

Lexington Parker

A1/NR/F1

NR///

\$4 Billion asset-backed commercial paper program primarily backed by undivided percentage interests in long-term and short-term consumer and commercial receivables originated by US and non-US corporate entities. **Liberty Hampshire Company, LLC Dependent** is the sponsor with its liquidity commitments covering 100% of the face amount of CP outstanding.

ATTACHMENT A

[Lockhart Funding LLC](#)

NR/P1/F1

NR///

\$2.0 Billion [asset-backed commercial paper](#) program primarily backed by debt securities rated at least Aaa by Moody's. Credit Enhancement and Liquidity Support are provided by **Zions Bank** through Letter of Credit and Liquidity Asset Purchase Agreement respectively.

[Moat Funding LLC](#)

A1+/P1/F1+

NR///

\$1.5 Billion [asset-backed commercial paper](#) program primarily backed by bank loans. Credit Enhancement and Liquidity Support are provided by **JP Morgan Chase Bank**

[Moriarty LLC](#)

A1+/P1/F1+

NR///

\$10 billion [asset-backed commercial paper](#) program primarily backed by rated corporate and structured debt. Credit Enhancement and Liquidity Support are provided by **Abbey National** through standby letter of credit and 100% program-wide liquidity loan commitment.

[Motiva Enterprises LLC](#)

A1/P1/NR

A+/NR/NR

Houston, Texas-based Motiva, which upon completion of the sale of Texaco's interest will be owned evenly by units of Shell Oil and by Saudi Aramco. A maximum outstanding of \$1.25 billion commercial paper, the company maintains committed and unused bank facilities equal to 100% of the program size.

[Salomon Smith Barney Holding\(SSBH\)](#)

A1+/P1/F1+

AA-/Aa1/AA

SSBH is a subsidiary of Citigroup Inc. and an integral part of Citigroup Investment Bank. At Sept. 30, 2001, SSBH had \$11 billion in commercial paper and other short-term borrowings outstanding. It has sound liquidity, strong operating performance and also includes a significant element of support from Citigroup.

[SIGMA Finance Inc.](#)

A1+/P1/F1

AAA/Aaa/AAA

Structured Investment Vehicle backed by investment-grade securities and hedge positions with equity and capital notes used as credit enhancement.

ATTACHMENT A

[Tannehill Capital Co LLC](#)

A1/NR/F1

NR///

\$5 Billion [asset-backed commercial paper](#) program primarily backed by undivided percentage interests in long-term and short-term consumer and commercial receivables originated by US and non-US corporate entities. **Liberty Hampshire Company, LLC Dependent** is the sponsor with its liquidity commitments covering 100% of the face amount of CP outstanding.



ATTACHMENT B

PETER HUGHES, Ph.D., CPA, CIA, CFE
Director

400 Civic Center Drive West
Building 12, Room 232
Santa Ana, California 92701-4521

(714) 834-5475 Fax: (714) 834-2880

INTERNAL AUDIT DEPARTMENT

File No. 2107

April 18, 2002

County of Orange
Treasury Oversight Committee
12 Civic Center Plaza, Room G-76
Santa Ana, CA 92701-4521

INTERNAL AUDITOR'S REPORT

We have examined the Treasury management's assertions in the accompanying Summary of Investment Compliance Requirements which was included in the representation letter dated December 28, 2001, that Orange County Treasurer complied with California Government Code Sections 27130 through 27137 and related provisions of the Orange County Treasurer Investment Policy Statement for the Money Market and the Extended Funds during the year ended December 31, 2000. Treasury management is responsible for compliance with those requirements. Our responsibility is to express an opinion on Treasury management's assertions about Orange County Treasurer's compliance based on our examination.

Our examination was made in accordance with the attestation standards established by the American Institute of Certified Public Accountants, and accordingly included examining on a test basis evidence about the County Treasury's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our examination provides a reasonable basis for our opinion. Our examination does not provide a legal determination on the County Treasury's compliance with specified requirements.

As described in the accompanying schedule of Findings, Recommendations and Responses, Orange County Treasurer did not comply with some of the requirements regarding authorized investments, compensation agreement and voluntary participants that are applicable to its Investment Policy Statement for the Money Market and the Extended Funds.

In our opinion, except for the noncompliance described in the preceding paragraph, management's assertions that Orange County Treasurer complied with the aforementioned requirements during the year ended December 31, 2000, are fairly stated, in all material respects.

County of Orange
Treasury Oversight Committee
April 18, 2002

This report is intended solely for the information and use of the County Treasury Oversight Committee and is not intended to be and should not be used by anyone other than the party specified. However, this report is a matter of public record and its distribution is not limited.

Sincerely,

Dr. Peter Hughes, CPA
Director, Internal Audit

Other recipients of this audit report:

Members, Board of Supervisors
Members, Audit Oversight Committee
Michael Schumacher, Ph.D., County Executive Officer
Foreman, Grand Jury
John M.W. Moorlach, Treasurer-Tax Collector
Richard G. Hilde, Assistant Treasurer
Paul Gorman, Treasurer Accounting/Compliance Manager
Darlene Bloom, Clerk of the Board

**REPORT
ON ANNUAL AUDIT OF
TREASURY INVESTMENT COMPLIANCE
FOR THE
YEAR ENDED DECEMBER 31, 2000**

Issued: April 18, 2002

Audit Number 2107

Director:	Dr. Peter Hughes, CPA
Deputy Director:	Eli Littner, CPA
Audit Manager:	Alan Marcum, CPA
In-Charge Auditor:	Pamela L. Parisien, CPA
Staff Auditors:	Camille Gackstetter Winnie Soo, CPA



**COUNTY OF ORANGE
INTERNAL AUDIT DEPARTMENT**

**REPORT
ON ANNUAL AUDIT OF
TREASURY INVESTMENT COMPLIANCE
FOR THE
YEAR ENDED DECEMBER 31, 2000**

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COUNTY OF ORANGE

SUMMARY OF INVESTMENT COMPLIANCE REQUIREMENTS

SCHEDULE I

For Year-Ended 12/31/00

The investment compliance requirements presented in the California Government Code Sections 27130 through 27137 and related provisions of the Orange County Treasurer Investment Policy Statement are as follows:

Government Code Sections 27130 through 27137

1. The Legislature finds and declares that local agencies, including school districts, should participate in reviewing the policies that guide the investment of those funds. (Section 27130)
2. The Board of Supervisors in each county shall, if the county is investing surplus funds, establish a county treasury oversight committee that consists of from three to eleven members. (Section 27131)
3. The county treasury oversight committee shall consist of members appointed from the following: county treasurer; county auditor, auditor-controller or finance director; a representative appointed by the county board of supervisors; the county superintendent of schools or designee; a representative selected by a majority of the presiding officers of the governing bodies of the school or community college districts; a representative selected by a majority of the presiding officers of the legislative bodies of the special districts; up to five other members of the public who either have expertise or academic background in finance or are economically diverse and bipartisan in political registration. (Section 27132)
4. Committee members may not be employed by an entity that has contributed to the campaign of a candidate for the office of local treasurer, or contributed to the campaign of a candidate to be a member of a legislative body of any local agency that has deposited funds in the county treasury, in the previous three years or during the period that the employee is a member of the committee. (Section 27132.1)
5. Committee members may not directly or indirectly raise money for a candidate for local treasurer or a member of the governing board of any local agency that has deposited funds in the county treasury while a member of the committee. (Section 27132.2)
6. Committee members may not secure employment with bond underwriters, bond counsel, security brokerages or dealers, or with financial services firms with whom the treasurer is doing business during the period that the person is a member of the committee or for one year after leaving the committee. (Section 27132.3)
7. Committee meetings shall be open to the public and subject to the Ralph M. Brown Act. (Section 27132.4)
8. The county treasurer shall annually prepare an investment policy that will be reviewed and monitored by the county treasury oversight committee. The investment policy shall include the following: a listing of authorized securities or other instruments in which the treasurer may invest; maximum security terms; criteria for the selection of brokers and dealers; limits on the receipt of gifts; investment reporting requirements; cost calculation and apportionment policy for managing funds; deposit terms and conditions for voluntary participants; and funds withdrawal criteria. (Section 27133)

COUNTY OF ORANGE

SUMMARY OF INVESTMENT COMPLIANCE REQUIREMENTS
SCHEDULE I (Continued)
For Year-Ended 12/31/00

9. The county treasury oversight committee shall cause an annual audit to be conducted to determine the county treasury's compliance with the investment compliance requirements presented in the California Government Code Sections 27130 through 27137. (Section 27134)
10. The costs of complying with this article shall be county charges and may be included with those charges enumerated under Section 27013. (Section 27135)
11. Local or public agencies that have funds on deposit in the county treasury pool and seek to withdraw funds for the purpose of investing or depositing those funds outside the county treasury pool shall first submit the request for withdrawal to the county treasurer. The county treasurer shall evaluate each proposed withdrawal for its consistency with the criteria adopted pursuant to Section 27133. Prior to approving a withdrawal, the county treasurer shall find that the proposed withdrawal will not adversely affect the interests of the other depositors in the county treasury pool. (Section 27136)
12. The county treasury oversight committee shall not direct individual investment decisions, select individual investment advisors, brokers, or dealers, or impinge on the day-to-day operations of the county treasury. (Section 27137)

Orange County Treasurer Investment Policy Statement (IPS)

13. Investments maintained in the portfolios shall be consistent with those authorized per Government Code Sections 53601 et seq., 53631.5, and 53635, as stated in IPS Sections IV and V.
14. Investments maintained in the portfolios shall comply with investment criteria as stated in IPS Sections IV, V and VI, including the maximum allowable percentage by type of security, allowable percentage per issuer, maximum term limits and credit ratings requirements.
15. Treasurer, investment personnel, and Treasury Oversight Committee members shall annually complete the Statement of Economic Interests Disclosure (State of California Form 700) and must comply with the Orange County Gift Ban Ordinance which prohibits the receipt of specified gifts, as stated in IPS Section VII.
16. All security transactions must be executed through brokers/dealers and financial institutions that meet the selection criteria specified in IPS Section VIII and are placed on the list of qualified institutions.
17. All security transactions entered into by the Treasurer shall be conducted on a delivery-versus payment basis and a third party custodian, as stated in IPS Section X, shall hold securities.
18. Repurchase agreements are required to be collateralized by securities authorized under Government Code Section 53601 at a minimum of 102% of market value of the principal and accrued interest, and shall be adjusted no less frequently than weekly. Collateral is to be held by an independent third party with whom the treasurer has a current custodial agreement. Evidence of ownership must be supplied to the Treasurer and retained as stated in IPS Section XI.

COUNTY OF ORANGE
SUMMARY OF INVESTMENT COMPLIANCE REQUIREMENTS
SCHEDULE I (Continued)

For Year-Ended 12/31/00

19. The Treasurer will charge all pool participants for administrative and overhead costs of investing, depositing, banking, auditing, reporting, or otherwise handling or managing the funds as authorized by Government Code Section 27013, as stated in IPS Section XIV.
20. Local agencies that voluntarily deposit monies with the Treasurer must provide to the Treasurer a resolution adopted by its governing board stating that excess funds are available for investing, in compliance with requirements stated in IPS Section XV.
21. Withdrawal of participant funds shall require prior written approval from the Treasurer. Prior to approving the withdrawal request, the Treasurer shall make a finding of the effect of the withdrawal on the stability and predictability of the investments, as stated in IPS Section XVI.
22. The Treasurer shall provide monthly report and any audit report in accordance with Government Code Sections 53646 and 53686, as stated in IPS Section XIX.

FINDINGS, RECOMMENDATIONS, AND RESPONSES

I. Noncompliance noted with Investment Policy Statement Section IV – Authorized Investments

Section IV.10 of the Treasurer’s Investment Policy Statement effective as of January 2000 and July 2000 requires that medium-term notes eligible for investment “...shall be rated “A” or better by at least two of the following nationally recognized rating agencies: Standard and Poor’s, or Moody’s, or Fitch.”

We tested 97 purchases made during our audit period (1/1/00 to 12/31/00) for investment compliance. Of those 97 investments, we determined that 22 were medium-term notes. Of the 22 medium-term notes, we identified one note, SMM Trust 2000-B, purchased on 3/15/00 with a par value and cost of \$20,000,000 did not have an “A” rating or better by at least two nationally recognized rating services. The investment matured on 12/13/00 and the Treasurer received all principal and earned interest for the investment.

Upon review of the trade ticket, it was determined that the Assistant Investment Officer, who is no longer employed by the Treasurer, placed the trade and the trade ticket was signed by the Investment Officer.

Recommendation No. 1

We recommend that the Treasurer only purchase medium-term notes meeting the requirements of Section IV.10 of the Treasurer’s Investment Policy Statement.

Treasurer Response:

Partially Concur. We concur with the above recommendation however we do not concur with Internal Audit’s finding that the subject investment did not have an “A” rating or better by at least two nationally recognized rating services.

The subject investment in SMM Trust 2000-B (Trust) was secured by a total return swap agreement with Morgan Guaranty Trust Company of New York (MGT), Swap Counterparty. MGT provides the primary source of principal and interest payment to investors holding the securities. The guarantee and demand feature diversification standards of Section 2a-7(a)(3)(iii) of the Investment Company Act of 1940 state that a money market fund can rely on the credit quality of a guarantee in determining the credit quality of the underlying security.

As a result of the swap agreement, this security represents exposure to AAA/Aa1 (long-term) rated Morgan Guaranty Trust Company of New York. The Offering Memorandum states that ratings on the SMM securities will change with the short-term or long-term rating of the Swap Counterparty.

Internal Audit Response:

While we disagree with the Treasurer’s characterization and interpretation of this complex investment instrument, we found that the Treasurer has not continued to purchase any further securities offered by SMM Trust 2000-B. Since there have been no further purchases of SMM Trust 2000-B and since all interest and principal payments were received when the subject investment matured on 12/13/00, no further work is required.

II. Noncompliance noted with Investment Policy Statement Section XIV – Compensation Agreement

Section XIV of the Treasurer’s Investment Policy Statement effective as of January 2000 and July 2000 requires that “The Treasurer shall annually prepare a proposed budget revenue estimate, providing a detailed itemization of all estimated costs which comprise the administrative fee charged in accordance with California Government Code Section 27013...the administrative and overhead fee will be reviewed by the Treasury Oversight Committee on an annual basis.”

During our review of the Treasury Oversight Committee meeting minutes during our audit period (1/1/00 to 12/31/00) we determined that the administrative and overhead fee for fiscal year 2000 was not presented to the Treasury Oversight Committee for review.

Recommendation No. 2

We recommend that the Treasurer comply with their Investment Policy Statement and California Government Code Section 27013 and annually submit the administrative and overhead costs for the pool participants to the Treasury Oversight Committee for review.

Treasurer Response:

Concur. The Treasury Oversight Committee, in their January 16, 2002 meeting, reviewed the administrative and overhead costs for 2000 and 2001.

III. Noncompliance noted with Investment Policy Statement Section XV – Voluntary Participants

Section XV of the Treasurer’s Investment Policy Statement effective as of July 2000 states “Monies deposited by local agencies approved for entry into the Treasurer’s Investment Pool will be invested in the Money Market Fund. To participate in the Extended Fund, the local agency must sign a waiver indicating their understanding of the possible NAV (Net Asset Value) risk involved.”

Treasury staff informed us that all monies deposited into the Orange County Investment Pool are commingled between the Money Market and Extended funds. Individual deposits into the pool are not identified as deposits into one specific fund. In effect, any pool participant with monies invested in the Orange County Investment Pool after July 2000 (when the Extended Fund was established) has a percentage of their holdings invested in the Extended Fund. Therefore, all voluntary participants are participating (investing) in the Extended Fund.

Since the Extended Fund was not established until July 2000 and the Investment Policy Statement requirement did not become effective until that time, we determined any participant established subsequent to that date should have signed a waiver indicating their understanding of the possible NAV risk. Of the two new voluntary participants established during calendar year ended 12/31/00, we found that one participant, Mesa Consolidated Water District, was subject to this requirement. However we were unable to locate a signed waiver form in the participants file indicating their understanding of the possible NAV risk related to participating in the Extended Fund.

Recommendation No. 3

We recommend that Treasurer include a standard section in their voluntary participant agreements stating that the agency is aware of the possible NAV risk related to participating in the Extended Fund.

Treasurer Response:

Concur. The Treasurer will include a standard section in their voluntary participant agreements stating that agency is aware of the possible NAV risk related to participating in the Extended Fund.

Recommendation No. 4

We recommend that Treasurer request that Mesa Consolidated Water District sign a waiver form indicating their understanding of the possible NAV risk related to participating in the Extended Fund.

Treasurer Response:

Concur. The Treasurer will comply with this request by May 31, 2002.

IV. Noncompliance noted with Investment Policy Statement Section XV – Voluntary Participants

Section XV of the Treasurer’s Investment Policy Statement effective as of January 2000 and July 2000 requires that voluntary participants “...comply with the requirements of Section 53684 of the California Government Code and provide to the Treasurer a resolution adopted by its governing board stating that excess funds are available for the purpose of investment. The resolution shall specify that the local agency authorizes the investment of excess funds pursuant to Section 53684...”.

Of the two new voluntary participants established during calendar year ended 12/31/00, we found that the Treasurer accepted one resolution, 99-628 adopted by the Board of Directors of the Costa Mesa Sanitary District, that did not contain the verbiage required by Section 53684 and the Investment Policy Statement Section XV stating that excess funds are available for the purpose of investment.

Recommendation No. 5

We recommend that the Treasurer obtain from the Costa Mesa Sanitary District a revised resolution that contains the required verbiage that excess funds are available for the purpose of investment.

Treasurer Response:

Concur. The Treasurer will comply with this request by May 31, 2002.

**APPENDIX
TREASURER MANAGEMENT RESPONSE**



COUNTY OF ORANGE
OFFICE OF THE TREASURER-TAX COLLECTOR
HALL OF FINANCE & RECORDS
12 CIVIC CENTER PLAZA, ROOM G76
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April 17, 2002

RECEIVED
APR 17 2002

Dr. Peter Hughes, CPA
Director, Internal Audit
County of Orange
400 Civic Center Drive West
Building 12, Room 232
Santa Ana, CA 92701-4521

INTERNAL AUDIT

Dear Dr Hughes:

Pursuant to Audit Oversight Committee Administrative Procedure No. 1, we have prepared our response to the draft results of your examination of the investment compliance requirements presented in California Government Code Sections 27130 through 27137, and related provisions of the Orange County Treasurer Investment Policy Statement, for the year ended December 31, 2000. The recommendation numbers used in your report references our response.

Recommendation No. 1:

We recommend that the Treasurer only purchase medium-term notes Meeting the requirements of Section IV.10 of the Treasurer's Investment Policy Statement.

Treasurer-Tax Collector response:

Partially Concur. We concur with the above recommendation however we do not concur with Internal Audit's finding that the subject investment did not have an "A" rating or better by at least two nationally recognized rating services.

The subject investment in SMM Trust 2000-B (Trust) was secured by a total return swap agreement with Morgan Guaranty Trust Company of New York (MGT), Swap Counterparty. MGT provides the primary source of principal and interest payment to investors holding the securities. The guarantee and demand feature diversification standards of Section 2a-7(a)(3)(iii) of the Investment Company Act of 1940 state that a money market fund can rely on the credit quality of a guarantee in determining the credit quality of the underlying security.

As a result of the swap agreement, this security represents exposure to AAA/Aa1 (long-term) rated Morgan Guaranty Trust Company of New York. The Offering Memorandum states that ratings on the SMM securities will change with the short-term or long-term rating of the Swap Counterparty.

APPENDIX
TREASURER MANAGEMENT RESPONSE (cont'd)

Dr. Peter Hughes, CPA
Page 2

Recommendation No. 2:

We recommend that the Treasurer comply with their Investment Policy Statement and California Government Code Section 27013 and annually submit the administrative and overhead costs of the pool participants to the Treasury Oversight Committee for review.

Treasurer-Tax Collector response:

Concur. The Treasury Oversight Committee, in their January 16, 2002 meeting, reviewed the administrative and overhead costs for 2000 and 2001.

Recommendation No. 3:

We recommend that Treasurer include a standard section in their voluntary participant agreements stating that the agency is aware of the possible NAV risk related to participating in the Extended Fund.

Treasurer-Tax Collector response:

Concur. The Treasurer will include a standard section in their voluntary participant agreements stating that agency is aware of the possible NAV risk related to participating in the Extended Fund.

Recommendation No. 4:

We recommend that Treasurer request that Mesa Consolidated Water District sign a waiver form indicating their understanding of the possible NAV risk related to participating in the Extended Fund.

Treasurer-Tax Collector response:

Concur. The Treasurer will comply with this request by May 31, 2002.

Recommendation No. 5:

We recommend that the Treasurer obtain from the Costa Mesa Sanitary District a revised resolution that contains the required verbiage that excess funds are available for the purpose of investment.

Treasurer-Tax Collector response:

Concur. The Treasurer will comply with this request by May 31, 2002.

If you have additional questions or follow-up comments, please contact Paul Gorman, Treasury Accounting/Compliance Manager at 834-2288.

Very truly yours,



John M. W. Moorlach, C.P.A., CFP™
Treasurer-Tax Collector