



COUNTY OF ORANGE

**OFFICE OF THE TREASURER-TAX
COLLECTOR**

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July 10, 2000

The Honorable Charles V. Smith
Chairman, Board of Supervisors
10 Civic Center Plaza, Fifth Floor
Santa Ana, CA 92701

Dear Supervisor Smith:

It is with great pleasure that I submit this annual report to you, our participants, and the residents of the County of Orange for the fiscal year ended June 30, 2000.

We have experienced another productive and positive year in my department. I am genuinely pleased with the results of the efforts pursued by my staff in both the Treasurer's and Tax Collector's offices. Therefore, it is with considerable pride and honor that I reflect on their accomplishments during this past fiscal year.

Investment Policy Statement

This fiscal year was unique in that we not only made our annual Investment Policy Statement review with the Board of Supervisors in December, but we also made a significant policy improvement at the June 20, 2000 Board of Supervisors meeting.

Our annual modifications continued to build upon an investment policy statement that has already been recognized by the Municipal Treasurers' Association of the U.S. and Canada with their Certificate of Excellence Award. This year we modified our Investment Policy Statement for new investment code changes resulting from the passage of Assembly Bill 343 (Campbell, Orange), a bill that was introduced and actively pursued through the Legislature to signing by the Governor by our office. Our legislative success with AB 343 is rather substantial. It accomplished a number of significant improvements to the investment code for the State of California. The code provisions for Commercial Paper allowed a maximum holding of 15 percent of the portfolio. The maximum could be increased to 30 percent if the weighted average maturity was 31 days or less. Due to the attractiveness of Commercial Paper from a credit quality perspective, for its liquidity, abundant availability, and its higher market yields, AB 343 accomplished two major improvements by increasing the maximum holding to 40 percent and

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eliminating the weighted average maturity limitation. Our local government investment pools are now more comparable to institutional money market funds. I am very proud of this legislative accomplishment. Orange County is back in a leadership mode and the modifications make great business sense and have garnered praise from many in the industry around the state. This Investment Policy Statement was distributed with our January 10, 2000 report.

For the past five years our Investment Policy Statement has been a model for a money market format within the California Investment Code. Fortunately, subsequent to the turbulent interest rate experiences of 1994, the yield curve has been relatively flat. This has allowed money market funds to perform competitively in the fixed income environment. However, we have funds on deposit that have a longer time line and the yield curve should be steepening in the future, as this is its historically normal structure. Accordingly, the Treasurer's Advisory Committee has deliberated on a safe and creative solution.

The new Investment Policy Statement is a culmination of more than five years of serious debate and contemplation by our Investment Management Committee, the Treasurer's Advisory Committee and the Treasury Oversight Committee. In the local government investment pool arena, the utilization of a money market fund and an extended short-term fund is a cutting edge and entrepreneurial. The Treasurer will allocate funds into the extended pool based on astute and supportable cash flow projections and an overall blended yield will be distributed to the participants. All business will be transacted through our existing money market pools. Funds that are not immediately needed will be invested with a weighted average maturity in excess of 90 days, capturing higher yields outside the money market thirteen month arena, with minimal risk. In fact, recently the top of the yield curve has been the twenty-four month maturities. This new blended format became effective on July 1, 2000. (See XII - Investment Policy Statement June 2000.)

Treasury Oversight Committee

The Treasury Oversight Committee continues to meet as best as possible on a quarterly basis to assist in the annual review of the Investment Policy Statement and our compliance to it. This fiscal year saw the revision of the Committee's bylaws. The major change resulted from another legislative introduction that we made and was included in AB 323 (Baldwin, San Diego). It reduced the length of time for a member that leaves the Committee to work for a financial services firm. The other material modification was the addition of a fifth member. This will allow for a quorum with three members present. (See XIII - Treasury Oversight Committee Bylaws.)

The compliance audit performed by the County's Internal Audit Department for the year ended December 31, 1998 was completed. (See XIV- Annual Compliance Audit.) The audit for the December 31, 1999 is in process.

I wish to acknowledge my appreciation to Robert Fauteux, Committee Chairman, Janice M. Mittermeier, County Executive Officer, David E. Sundstrom, Auditor- Controller, John Dean, Superintendent of the Orange County Department of Education, Charles Schroeder, our newest member and a finance professor at California State University in Fullerton, for their assistance in

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this critical area of responsibility. A copy of Mr. Fauteux's annual report to the Board of Supervisors is included in this report (see XV - Treasury Oversight Committee).

Treasurer's Advisory Committee

The Treasurer's Advisory Committee continues to be a professional resource in critiquing and constructing the technical aspects of the Investment Policy Statement. Their collective and continued wisdom has been an invaluable asset to the County. I would like to extend my deep appreciation to: Jeffery M. Thomas, Chairman, Blake E. Christian, C.P.A., Vice Chairman, Bruce A. Hughes, Esq., C.P.A., Clyde E. Kendzierski, George N. Jeffries, John L. Nelson, Ed.D. and Wendy Margarita, Ed.D. Dr. Nelson retired during the year to pursue a career change in the Bay Area. This upcoming fiscal year we will be establishing terms and nominating new members. This Committee membership has been virtually intact from prior to my appointment in 1995. This core group has been critical to our overall success!

Investment Management Committee

Our investment management committee has completed another admirable year in its market research. This past year, the committee accurately predicted all but one of the Federal Open Market Committee decisions on interest rates prior to their meetings bringing our record of accurately anticipating the FOMC's decisions to 39 out of 41 regularly scheduled meetings. This diligence to market analysis has generated additional basis points in yield for our participants this year thanks to our anticipating a tightening of interest rates.

The investment staff, along with our volunteer student interns, continues to compile and update an impressive data base of issuers whose capital assets and credit ratings have been thoroughly reviewed, researched and approved as qualifying, permissible investments.

Information provided in each of our monthly reports, including this one, is informative and displayed a professional acumen concerning the direction of short-term interest rates. Accordingly, our investment performance was enhanced as we benefited from a shorter weighted average maturity as a result of the research provided. It is a pleasure to state in our monthly reports that the charts, tables, graphs and numerical representations have been provided to our readers solely as a general overview of the economic and market conditions which the Treasurer utilizes in making investment decisions.

Legislative Pursuits

As you can tell from our Investment Policy Statement and Treasury Oversight Committee narratives, we're quite pleased with our 1999 legislative accomplishments.

Assembly Bill 343, our centerpiece submittal, was signed by the Governor on July 28, 1999. We are very thankful to Assembly Member Bill Campbell for his leadership in carrying this legislation. (See the

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first page of this letter, Investment Policy Statement.)

Senate Bill 275 modified the preparation options for the monthly statement of cash receipts and disbursements. (See Monthly Statement of Cash Receipts and Disbursements.)

Assembly Bill 323 finally corrected the untenable portion of Senate Bill 866 that caused our original Treasury Oversight Committee to resign en masse. (See Treasury Oversight Committee.)

Assembly Bill 343 also corrected a definitional concern raised in Senate Bill 866 regarding Board of Supervisors= approval of all borrowings. The author, former State Senator Quentin Kopp, did not mean for bank overdrafts to be included. Our legislation clarified this issue. AB 343 also established an issuers limitation of ten percent. Prior to our legislation, the only diversification limit was by product type. Accordingly, we are very proud of this introduction into the code.

Assembly Bill 1679 added a better definition of Medium Term Notes, one imitating ours in the Investment Policy Statement. This bill was also signed by the Governor.

During the legislative session of 2000 we have had Senator John Lewis carry Senate Bill 1493, which permits the accrual method of distributing investment income. Although this method is considered a generally accepted accounting principle and mandated by the Securities and Exchange Commission, it is not explicitly provided for in the California Investment Code. It should be soon, as this legislation has been moving without opposition and any and all amendments that were proposed have been agreeable with our office. (See Apportionment of Commingled Pool Interest Earnings.)

Monthly Statement of Cash Receipts and Disbursements

We continued to issue a separate statement of cash receipts and disbursements each month to the Board of Supervisors and the Clerk of the Board. This report is required by State Code Section 27063. This past year we were able to successfully pass legislation that was signed by the Governor that also allows the Auditor-Controller to prepare this report. After a lengthy study, the Auditor-Controller determined that his department could not produce a report that provided the detail that our investment software has been presenting to the Board of Supervisors. Accordingly, we will continue providing this report in the same format. However, the Auditor-Controller and I will submit legislation next year eliminating this requirement.

Apportionment of Commingled Pool Interest Earnings

We have prepared a forecast for the timing of the County Investment Pools April and May 2000 interest apportionments. We anticipate posting April and May to participants= cash accounts in the County general ledger by July 10 and August 7 respectively. April, May and June 2000 interest earnings and administrative fees for all participants will be accrued in the County general ledger as of June 30, 2000.

Throughout the fiscal year we have been communicating with the Auditor-Controller and have agreed to the utilization of the accrual method. We have been espousing this approach for quite some time. The Auditor-Controller has concurred with this position and has requested individual accrual accounts. We are currently working with our Information Systems staff to update our software to comply with this agreed to arrangement. This issue has involved a considerable amount of time by many key members of the County's financial management team. We wish to acknowledge our appreciation to Mr. David Sundstrom, Auditor-Controller, for his leadership role in this regard.

During June the Treasurer-Tax Collector posted an adjustment of \$1,265,700.40 to reduce interest earnings for County commingled pool participants. The adjustment was to recover an overpayment related to interest earned on \$12.2 million resident in Fund 691- Unapportioned Interest Fund for the period June 1996 through March 1998. The interest earned on this \$12.2 million while it was in Fund 691 was distributed to County commingled pool participants as part of their monthly interest apportionment for this period. Included in the \$1,265,700.40 is a reconciling adjustment of \$170,237.09 to agree the general ledger to the Treasurer's reconciled balance and our SunGard investment accounting records. The methodology and computations for the adjustment were reviewed by the Internal Audit Department and we have included their report on the review as an attachment to this month's report (see XVI - Fund 691 Unapportioned Interest Fund).

Triple-A Rated Pool

Our professional management, policies, procedures, oversight, award winning Investment Policy Statement and this full disclosure Treasury Management report (which is provided to you by the tenth day of the subsequent month), has maintained an AAAA/V-1+@ rating for the investment pools by Fitch IBCA.

Compliance

Our ability to monitor the Investment Policy Statement compliance has been documented in the regular internal noncompliance report summary, including our related prompt rectification, provided in each monthly report. Our compliance is also documented in Fitch IBCA's quarterly reports which are included in our monthly reports in a prompt manner (see XVII - Fitch IBCA Compliance Audit Report for the Quarter Ended March 31, 2000).

Staffing Changes

This fiscal year we had two major staff changes in key treasury positions which were absorbed or filled with minimal transitional issues. Leysa Amador, CCM, resigned to stay home with her three young children. Judy Jacobson, our Investment Officer, has temporarily included the cash management manager duties under her purview. Assistant Investment Officer Bill Eberhardt resigned to take a position with a more competitive remuneration package. Paul Cocking, a former intern and part-time employee, was recruited away from Pacific Life to fill this position. Because of his familiarity with our staff and office, there were minimal transitional concerns.

Annual Business Plan

We are using this annual report to provide a copy of our fourth annual Business Plan (see XVIII - 2000 Business Plan). Our Business Plan clearly delineates the tasks performed by this department and discusses our plans for the next fiscal year. It also provides a detailed explanation of our performance measurements and how we are achieving them.

Litigation Settlements

The litigation settlement proceeds were distributed on February 24, 2000. This should conclude the activities pursued to rectify the damages perpetrated on the County by those firms that performed their financial services in a grossly negligent manner.

Treasurer=s Conference

On February 3, 2000, our office hosted the second annual Orange County Treasurer=s Conference. The conference, entitled "Orange County Finances: 2000 and Beyond," was well received and garnered extremely positive feedback from the attendees. Our Host Committee did a wonderful job and is already planning the third annual conference scheduled for February 1, 2001.

GASB 31

Our conservative Money Market Investment Pools provide a safe, liquid, and competitive money market yield at a net asset value in the \$1 range. The investments are marked-to-market on a daily basis and comply with Governmental Accounting Standards Board (GASB) 31, which became effective on June 15, 1997. Accordingly, none of our participants that prepare Comprehensive Annual Financial Reports, including the County, reported a fair market value adjustment for the fiscal year ended June 30, 2000.

Economic Observations for the Year

Beguilingly referred to as the most powerful man in the industrialized world, Alan Greenspan, the chairman of the Federal Open Market Committee (FOMC), held the financial markets at bay during the last 12 months. Concerned that the combination of a strong economy with no inflation was unsustainable, the FOMC has tightened interest rates 175 basis points since June 30, 1999 (Exhibit 1).

Month after month we saw our incredibly good economy just get better. Reports continued to show that everybody has a job, productivity is staying up and prices are stable. The soaring stock markets and the insatiable consumer made an unbeatable combination.

The FOMC's "gradual" approach to slowing the economy dominated the marketplace. Nervously reacting to any interpretation of an economic release or Greenspan speech, the financial markets lacked

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direction. Weak economic news was explained away as a "one-month anomaly."

It appears, however, that the consumer has started to cut back. Not only are borrowing costs higher, but skyrocketing crude oil prices (Exhibit 2) are seriously taking a bite out of household incomes. Has the FOMC successfully engineered the ultimate economic "soft-landing?"

During the fiscal year ended June 30, 1999, we experienced a declining interest rate environment and maintained a higher average weighted maturity of 82 days. For this fiscal year we addressed the rising interest rate environment by reducing our average weighted maturity to 79 days and acquired a significant percentage of floating rate notes, which reset shortly after each FOMC rate tightening.

Our gross yields out-performed our benchmark, the 90-day T-Bill, by 24 to 84 basis points with an average of 48 basis points (see IV, Benchmark Comparisons). During the last few months of this Fiscal Year our gross yield exceeded the yield on the 30-year T-Bond, something that we haven't seen since the fall-winter period of the last fiscal year. This phenomenon has occurred due to the continuance of a flat yield curve that has had dramatic inversions during these past few years (see Benchmark Graphs).

The portfolio's net yields also exceeded our in-house money market average benchmark and Standard & Poor's Local Government Investment Pool (LGIP) Index. We also continued to perform satisfactorily with rated, first tier, institutional money market funds with balances similar to ours (see Exhibit 3). We even did a comparison recently of our net yield with that of the State Treasurer's Local Agency Investment Pool. Our money market pool yields exceeded this longer average duration LGIP during the entire fiscal year. This should be the case in a rising rate environment (see Exhibit 4).

We continue to provide professional money management services to the county at a 12.5 basis point overhead expense ratio, making us extremely competitive against our private and public sector benchmarks. Our Investment Management Committee has had another year of investment results that we can all be proud of.

Tax Collection

Tax collection services continue to excel due to the dedication and enthusiasm of my staff. The initiation of in-house monthly training sessions on the many components of the County's Assessment Tax System (ATS) has improved employee knowledge and skill levels. The establishment of monthly assessment and collection issue meetings between the Assessor's Business Division and the Tax Collector's Delinquent Collection Division has improved communications concerning difficult collection matters.

The continuation of new technology applications, such as the automatic imaging of tax bills and notices, a new cashiering system, the upgrading of employee personal computers and network software, the completion of enhancements to the property tax remittance processing system, and the implementation of an automated bank reconciliation system, has all had an impact. In addition, increased diligence in monitoring bankruptcy filings by property taxpayers has resulted in additional tax collections. Electronic tax payment alternatives such as ACH Debits and Credits, Wire Transfers and Credit Cards continue to be offered, with payments by credit cards at record levels. The Y2K system enhancements initiated by

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us worked perfectly. Our collection percentages exceed State averages and remain at record levels. We continue to enhance our goodwill by participating in such events as **A**Small Business Tax Day[®] at California State University in Fullerton and providing foreign delegations with overviews of our property tax system.

Although the County continues to grow, our tax collection division's staffing has remained at the reduced post-bankruptcy levels. Your good Board approved the addition of three more staff members to assist in this area for the upcoming fiscal year, and we anticipate relieving the stress caused by our successful economy.

Other County Involvements

I have the privilege of serving as a board member of the Orange County Employees Retirement System. This Board meets monthly, and I have been serving on the Additional Retiree Benefit Account (ARBA) Ad Hoc Committee, which concluded its research efforts at the end of 1999. This Committee was reconstituted in 2000 to communicate our findings and recommendations to the County of Orange. I have the privilege of chairing this Committee, and we are dialoging with the appropriate County officials to get their concurrence on a simple accounting apportionment to better protect this benefit from the vagaries of the investment markets. I also serve as a member of the County's Audit Oversight Committee, which meets quarterly and as an ex-officio member of the Public Financing Advisory Committee, which meets biweekly.

This past year, I have also served as a member of the Results Oriented Government (ROG) Steering Committee, which meets monthly. This committee has advised the County and its paid consultants on our performance measurement efforts and has completed its stated purposes and is still doing some ongoing review functions. It was also reconstituted to review annual budget presentation format ideas and improvements.

Treasurer's Report

Attached please find the Treasury Management Report for the County of Orange for the month, quarter and year ended June 30, 2000. In order to assist you in reading this report, please note that the **A**current balances[®] reflect the investments recorded in the portfolios for each particular fund for the period ending June 30, 2000. Each pool has an average maturity of less than ninety days, with a net asset value (NAV) falling within the range of \$0.9950 and \$1.0050. All investments are marked to the market at the end of the reporting period due to the narrow valuation range prescribed by the Pools= Investment Policy Statement.

The reports reflect the **A**par[®] value (face value), the **A**book[®] value (cost to the County of the investment) and **A**market[®] value (the price of each security at the close of the market on the last trading day of the month). The difference between the **A**market[®] value and **A**book[®] value is the unrealized gain or (loss). The **A**Detail Transaction Report Section[®] is provided in compliance with California Government Code Section 53607, which requires that the Treasurer file such a report with the Board of Supervisors, from

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whom his investment authority has been delegated.

Conclusion

I continue to be very thankful for the opportunity to serve our community in this capacity. It has been an honor to assist in the continuing process of renewing Orange County's financial standing in the municipal community. I am grateful to my staff for the extraordinary efforts they have provided in making this department a success story. Your encouragement and continued assistance have also helped to make it so.

Very truly yours,

[Note: Original, signed letter on file with Clerk of the Board.]

John M. W. Moorlach, C.P.A., CFP
Treasurer-Tax Collector, County of Orange

FED Funds Target Rate 06/01/99 - 06/30/00

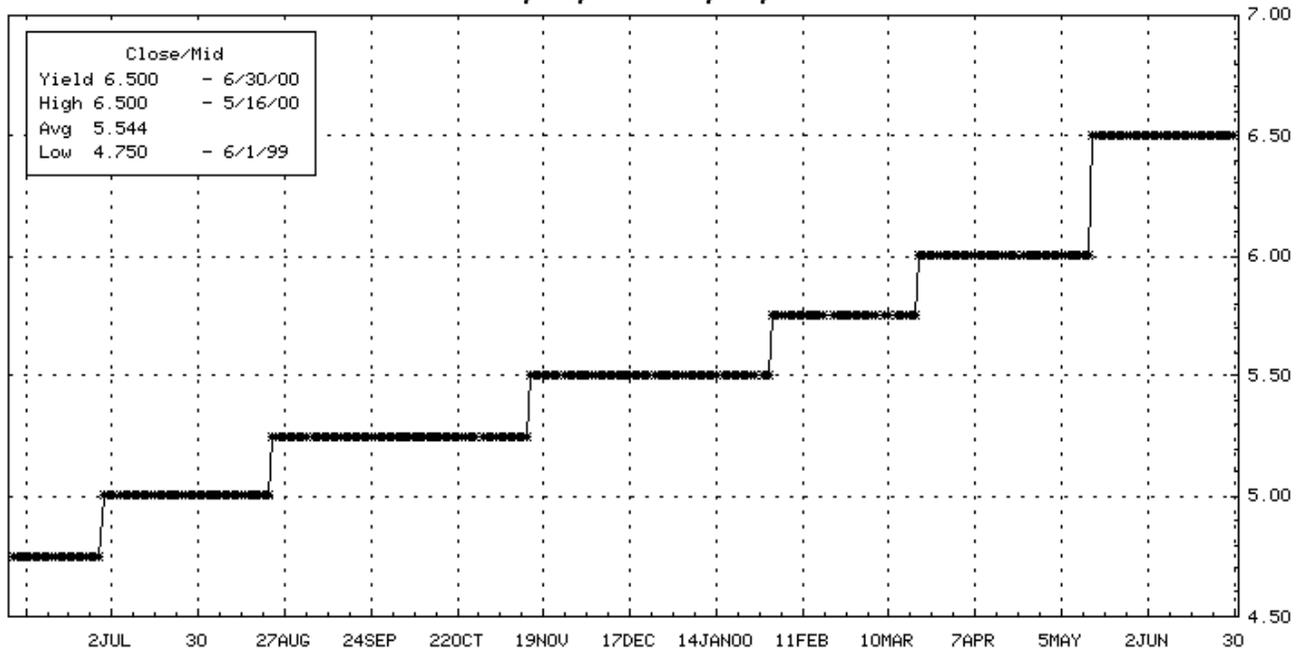


EXHIBIT 1

International Petroleum Exchange 06/01/99 - 06/30/00



EXHIBIT 2

MONTHLY YIELD COMPARISON

For The Period August 1995 to June 2000

