

MINUTES OF THE TREASURY OVERSIGHT COMMITTEE
ORANGE COUNTY, CALIFORNIA

REGULAR MEETING

January 28, 2009

The Regular Meeting of the Treasury Oversight Committee (TOC) was held on January 28th, 2009 and called to order by Robert Franz for Tom Mauk, Chair, at 11:00 AM.

Committee Members:

Present:

Robert Franz for Tom Mauk, CEO (Chair)
David Sundstrom, Auditor-Controller
Wendy Benkert for Bill Habermehl, O.C. Board of Education
George Jeffries, Treasurer, City of Tustin
Dr. Raghu Mathur, Chancellor, S.O.C.C.C.D.

Absent:

Also present were:

Chriss Street, Treasurer-Tax Collector; **Paul Gorman, Jennifer Burkhart, Paul Cocking, Fahad Haider, Anna Bryson** and **Yvette Clark** from the Treasurer's office; **Angie Daftary**, County Counsel; **Nancy Ishida, Christine Young**, and **Dat Thomas** from Auditor-Controller's office; **Lou Bronstein** from Supervisor Campbell's office and **April Rudge** from Supervisor Moorlach's office; **Darlene Hibbs, Gloria Hildman, Ella Nixon, Terry Fleskes, Don Hauptman** and **Abel Barboza** from the Grand Jury.

1) Meeting Called to Order

Mr. Franz called the meeting to order.

2) Welcome and self-introductions

Introductions were made.

3) Public Comments

None.

4) Approval of Prior Meeting Minutes

The Minutes of the October 30, 2008 Regular Meeting were reviewed.

Recommended Action: Mr. Franz called for a motion to approve the Minutes. Mr. Sundstrom moved to approve the Minutes, 2nd by Ms. Benkert, Passed 4-0 with 1 abstention from Dr. Mathur

5) Chairman's Report

None

6) Election of Chairman & Vice Chairman

- Mr. Jeffries nominated **Mr. Sundstrom for Chair**
- Motion seconded by Dr. Mathur
- All voted in favor. Passed 4-0 with abstention from Mr. Sundstrom
- Mr. Sundstrom then assumed the meeting as Chair

- Mr. Sundstrom nominated **Mr. Jeffries for Vice-Chair**
- Ms. Benkert seconded the motion
- All voted in favor. Passed 4-0 with abstention from Mr. Jeffries

7) Treasurer's Report

- Mr. Cocking gave an update on SIV's.
 - Whistlejacket had a slight deterioration on credit, otherwise it has remained at the same status
 - The resolution is moving in the manner anticipated and a quick resolution is not expected.
 - A specific time frame cannot be forecast, however it is the opinion of the Treasurer's office that if interest rates were to rise, then we would likely see a faster resolution.
 - The bulk of the securities are still highly rated.
- Mr. Sundstrom commented that he was surprised by a recent news article by the Orange County Register which implied that Whistlejacket has liquidated all of its "good" assets. It was confirmed that the Treasurer's office is of the understanding that the receiver, Deloitte, has not liquidated any of Whistlejacket's assets.
- Mr. Jeffries commented that the resolution of Whistlejacket is a microcosm of what former secretary of Treasury Paulson saw after he took money to buy the toxic assets. They had a hard time going after the toxic assets because they didn't know what was good or bad
- Mr. Street wanted to clarify that receivership and bankruptcy are entirely different from each other. A receiver protects bond holders because it administratively takes control away from the individuals who may not have managed the investment in the best interest of the capital note holders. Our office supports the receivership under the management of Deloitte & Touche.
- Mr. Sundstrom commented that another SIV, CC USA, was on credit watch negative. He believes it will be downgraded because all the SIV assets were moved onto the balance sheets of the sponsoring bank,

Citigroup. We can expect to see further downgrades until it pays off, however there is a high probability that we will get paid because they are receiving government help.

- Mr. Cocking commented that this has worked out in our favor in the example of Rabobank's SIV, Tango. The assets were sold off, leaving only cash in the portfolio. Tango has maintained a high rating

8) Annual SB866 Audit of Treasurer's Compliance with CA Government Code and the IPS

- Mr. Gorman provided the background for the audit required by California Government Code Section 27134 and explained that this section's mandate is for the Treasury Oversight Committee to cause an annual audit every year to ensure compliance with CA Government Code Sections 27130-27137. The audit was previously performed by Internal Audit after it was determined that the Quarterly engagement with Fitch was not an audit and did not fulfill the mandate of the code. The Treasurer subsequently issued an RFP for the December 31, 2004 audit on which Internal Audit was invited to bid. Moreland & Associates was selected and awarded an initial 3 year engagement which was then extended 2 more years to the end of 2008.
- In 2008 Moreland merged with Macias Gini & Oconnell, LLP (Macias). The cost for the 2008 annual audit is not to exceed \$44,000/year. In addition to the audit Macias performs 3 quarterly agreed upon procedure engagements at a cost of \$17,000 per quarter. The annual cost for the audit and agreed upon procedure engagements is not to exceed \$105,000 per year. The agreed upon procedure (AUP) engagements do not rise to the level of an audit. If the quarterly AUP engagements are eliminated it will likely increase the cost of the annual audit. The quarterly AUP engagements are not required and it is recommended that the TOC determine whether to continue them.
- The Auditor-Controller's Internal Audit unit has performed daily monitoring of the Treasurer's investment portfolio compliance since October 2007. In addition to their work we have quarterly and annual work being performed by Macias. Additionally, the Treasurer's accounting and compliance staff performs daily reviews to ensure compliance with the IPS. Based on the level of redundancy between the Treasurer's staff, Auditor/Controller's staff and the external engagements, the issue before the TOC is whether to issue the RFP for the annual audit only or continue with the quarterly agreed upon procedure engagements as well as the annual audit.
- Mr. Sundstrom stated it costs his office approximately \$60,000 per year for daily compliance work. Ms. Ishida estimated about 1,300 staffing hours are utilized annually. She stated that they check 100% of all purchases in the investment portfolios with no discrepancies with the Treasurer's staff. She suggested the possibility of going back to sampling.

- Mr. Sundstrom added that Macias only does spot samples, typically six days per quarter. He feels it should be one way or the other, but not both. He prefers doing it in-house at \$60,000 a year rather than doing it externally for \$68,000 year with only spot treatment reviews.
- Mr. Gorman stated the scope of work included in the RFP for the 2004-2008 audits was a directive from the Audit Oversight Committee and a letter from Dr. Hughes indicating that the scope of work used by Internal Audit should be the basis for the ongoing audit and quarterly engagements.
- Dr. Mathur stated that even with budget challenges there is another way to look at it. Since we are dealing with billions of dollars in investments, the cost of \$105,000 is a small amount to pay for an internal and external audit. It allows the Treasurer's office and the TOC to be totally transparent while also providing the Board with an additional level of comfort.
- Mr. Gorman stated Moreland was originally billing at \$150/hour, and with partner rates in other firms at \$350/hour we will probably see cost increases.
- Mr. Sundstrom doesn't think it's a good idea that his group perform the SB 866 (CA GC Section 27134) audit work.
- Mr. Franz stated the daily audit was started about October 2007. He suggested that it may be a time for the TOC to evaluate the elements together. Assuming we continue to do the annual audit, the question is whether to include quarterly or daily compliance by the Auditor/Controller's office
- Ms. Ishida stated that Treasurer is doing good job overall being compliant.
- Mr. Sundstrom said he would suggest not to continue the redundant audits by his department. However, he would like to get input from the Board.
- Mr. Franz suggested possibly doing an RFP for the annual audit as well as the agreed-upon procedure engagements and raising the question once it goes to the Board.
- Mr. Sundstrom stated we should have a committee recommendation.
- Ms. Benkert expressed it should be enough auditing if the daily monitoring hasn't brought up any relevant issues. She believes staff time could be better spent, especially when we are not finding any differences from what is being done by another party.
- Mr. Jeffries commented that Mr. Sundstrom's work is the only one that drives down to specific pools (clarification by Mr. Gorman all pools are monitored by Macias and the Treasurer). This won't be picked up by other parties. He urges that it should be continued.
- Mr. Sundstrom asked for a general concurrence to present as a recommendation to the Board.
- Mr. Jeffries moved to continue the daily compliance monitoring by the Auditor's office. Dr. Mathur seconded.

9) Review Current Bylaws

No discussion or action to current bylaws

10) Discuss a Proposed Amendment to Current Investment Policy Statement (IPS) regarding California Debt

- Mr. Street requested that we revise the current IPS to allow the Treasurer's office to purchase Revenue Anticipation Warrants (RAWs) from the State.
- Ms. Burkhart suggested expanding the IPS to include all debt from State to be exempt from the rating criteria.
- Mr. Street explained that warrants are registered items. They are very high confidence investments that are issued & registered in such a way that they are paid in priority. For example, if warrants were issued to the schools, they would be second priority to General Obligation Bonds
- Ms. Benkert stated she doesn't believe schools or community colleges will be issued RAWs this year.
- Mr. Street believes we will be seeing these instruments in our portfolio & we should get TOC's approval to go to the Board. Mr. Sundstrom commented that if these instruments are senior to interest payments on Gen Ob debt, then that is very good.
- Ms. Burkhart stated registered warrants are already allowed in the IPS. The issue at hand is if the credit rating of the state goes down then the current IPS language would not allow them to be purchased. County Counsel has already reviewed CA government code and agrees we are allowed to buy them. Our IPS is more restrictive than government code.
- Mr. Jeffries stated he is not sure whether RAWs are negotiable. If they can be negotiated, then the local agency would present them to the local treasurer. The negotiability issue should be researched.
- Mr. Sundstrom stated that his office was looking into registered warrants. He is very concerned that the Controller made good on his pledge not to pay welfare administration costs. We have to have a way to pay that payroll. Government code has no rating requirement.
- State's rating is now A2, which doesn't fit into IPS parameters.
- Mr. Sundstrom asked what concentration of local municipal debt purchases is the Treasurer's office recommending.
- Mr. Cocking responded about 5-10% concentration. How much they would buy would depend on the term. Anything under 13 months would go to the Money Market Fund. About \$200 million would be the estimated exposure.
- Mr. Jeffries stated that he urged maximum flexibility.
- Mr. Franz stated he believe the struggle was in relaxing the rating criteria as a lot has been done to establish the current credit quality/ratings as our guideline.

- Mr. Cocking stated that, excluding the Extended Fund, we have \$180 million in municipal debt right now. Mr. Street stated if he had to, he would probably sell OCTA bonds and replace them with RAWs if they became available.
- Mr. Jeffries stated that Mr. Street's primary concern is Orange County. Orange County and the State seem to be a fair return for the pool, and entirely safe. I don't think the Treasurer is going to be buying anything non-registered warrant type, unless he's pretty sure it's going to be paid back. Mr. Jeffries also stated this is something that you have to do to help your own people.
- Mr. Sundstrom suggested that this issue be deferred one meeting. He would like to see a white paper with all items on risk & seniority and determine then if the risk is moderate & can be absorbed at these extreme circumstances of the County. If so, then the TOC can endorse the concept at that level & take it to the Board with the extra caveat that this is a big decision & under emergency circumstances.
- Mr. Street stated that we have about two months maximum to do this.
- Mr. Sundstrom made a motion to generally approve in concept & come back within 60 days with details for review. Mr. Jeffries seconded motion. Approved by all.

11) Public Comments

None

12) Schedule Next Meeting Date

- A special meeting shall be within 60 days with more information concerning RAW's.

13) Adjournment

- a) Mr. Sundstrom adjourned the meeting at 12:36 p.m.