# ORANGE COUNTY TREASURY

Report of the Schedule of Assets
Held by the County Treasury

As of June 30, 2015

MGO Certified Public Accountants

**ORANGE COUNTY TREASURY**
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## Independent Auditor's Report

The Honorable Board of Supervisors
County of Orange, California

### Report on the Financial Schedule

We have audited the accompanying modified cash-basis Schedule of Assets Held by the County Treasury (Schedule) of County of Orange, California (County), as of June 30, 2015, and the related notes to the financial schedule.

***Management's Responsibility for the Financial Schedule***

Management is responsible for the preparation and fair presentation of this financial schedule in accordance with the modified cash-basis of accounting described in Note 1; this includes determining that the modified cash-basis of accounting is an acceptable basis for preparation of the financial schedule in the circumstances. Management is also responsible for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of the financial schedule that is free from material misstatement, whether due to fraud or error.

***Auditor's Responsibility***

Our responsibility is to express an opinion on the financial schedule based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America 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 schedule is free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial schedule. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial schedule, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial schedule in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial schedule.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

***Opinion***

In our opinion, the financial schedule referred to above presents fairly, in all material respects, the assets held by the County Treasury of County of Orange, California, as of June 30, 2015, in accordance with the modified cash-basis of accounting as described in Note 1**.**

***Basis of Accounting***

We draw attention to Note 1 of the financial schedule, which describes the basis of accounting. The financial schedule is prepared on the modified cash-basis of accounting, which is a basis of accounting other than accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to that matter.

**Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated April 8, 2016, on our consideration of the County Treasurer's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering County Treasurer’s internal control over financial reporting and compliance.

Macias Gini & O'Connell LLP

Newport Beach, California
April 8, 2016

**ORANGE COUNTY TREASURY**

Schedule of Assets Held by the County Treasury

As of June 30, 2015

| | OCIP | OCEIP | Non-Pooled | Total |
|---|---|---|---|---|
| **CASH** | | | | |
| Cash On Hand | $ 45,151 | $ - | $ - | $ 45,151 |
| Demand Accounts | 6,377,627 | 114,950,794 | - | 121,328,421 |
| Total Cash | 6,422,778 | 114,950,794 | - | 121,373,572 |
| **INVESTMENTS, stated at fair value** | | | | |
| ***Orange County Investment Pool (OCIP):*** | | | | |
| Orange County Money Market Fund | 916,190,702 | - | - | 916,190,702 |
| Extended Fund | 2,603,359,802 | - | - | 2,603,359,802 |
| ***Orange County Educational Investment Pool (OCEIP):*** | | | | |
| Orange County Educational Money Market Fund | - | 1,167,943,414 | - | 1,167,943,414 |
| Extended Fund | - | 2,613,079,877 | - | 2,613,079,877 |
| ***Non-Pooled*** | - | - | 168,988,996 | 168,988,996 |
| Total Investments | 3,519,550,504 | 3,781,023,291 | 168,988,996 | 7,469,562,791 |
| **TOTAL ASSETS** | $3,525,973,282 | $3,895,974,085 | $ 168,988,996 | $7,590,936,363 |

See accompanying notes to the financial schedule.

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## 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accompanying Schedule of Assets Held by the County Treasury (Schedule) is intended to separately report deposits and investments in the County Treasury included in the basic financial statements of the County of Orange, State of California (County). For additional disclosure information and contingencies, please refer to the latest publication of the County Comprehensive Annual Financial Report.

The Schedule includes the cash balances of all funds that the Office of the Treasurer-Tax Collector (Treasurer) pools for investing surplus funds according to California Government Code and the Treasurer's Investment Policy Statement (IPS). These public funds are called the Orange County Investment Fund (OCIF). Within the OCIF, the County maintains two external investment pools: the Orange County Investment Pool (OCIP) that includes the voluntary participants' funds; the Orange County Educational Investment Pool (OCEIP), which is utilized exclusively by the County's public school and community college districts; and various other non-pooled investment funds, including John Wayne Airport (JWA). The Treasurer is authorized by state law to pool funds for the County and other non-County entities for the purpose of benefiting from economies of scale, reduce duplication and to carry out consolidated banking and investment activities. The Schedule does not include cash and investments for the Orange County Employees Retirement System, CalOptima, certain deferred compensation funds and other debt reserve funds held in trust outside and independent of the County Treasury. The two external pools are not registered with the Securities and Exchange Commission (the "SEC") as an investment company. The two external pools do not have any legally binding guarantees of share values.

Unless otherwise required in a trust agreement or other financial document, assessment districts and public school and community college districts are required by legal provisions to deposit their funds with the County Treasurer. The OCEIP consists entirely of public school and community college districts' funds and therefore includes 100% involuntary participants. At June 30, 2015, the OCIP includes approximately 9.76% of involuntary participant deposits including funds for the Superior Court, certain assessment districts, and certain bond related funds for public school districts.

The Schedule is presented on the modified cash basis, which is a comprehensive basis of accounting other than generally accepted accounting principles in the United States of America (GAAP). Receipts are recognized when received by the Treasurer; disbursements are recognized when paid by the bank; and the value of investments is stated at fair value. The cash and investments primarily differ from the cash basis of accounting by the amount of outstanding checks of $153.0 million at June 30, 2015.

The Treasurer has stated required investments at fair value in the accompanying financial schedule. Management contracts with a third-party vendor and its custodian bank to provide pricing for the fair value of investments in the portfolio. The investments are marked to market and the net asset values (NAV) of the pools are calculated each business day.

The Treasurer values participants' shares in the pools using amortized cost. Specifically, the pools distribute income to participants based on their relative participation during the period. Income is calculated based on (1) realized investment gains and losses calculated on an amortized cost basis, (2) interest income at stated rates (both paid and accrued), (3) amortization of discounts and premiums on a straight-line basis, and reduced by (4) estimated investment and administrative expenses. This method differs from the fair value method used to value investments in this financial schedule because the amortized cost method does not distribute to participants all unrealized gains and losses in the fair values of the pools' investments.

## 2. DEPOSITS AND INVESTMENTS

The Treasurer is responsible for authorizing all County bank accounts and pursuant to California Government Code (CGC) Sections 27000.1-27000.5, 27130-27137 and 53600-53686, is responsible for conducting County investment activities of the County's investment pooled funds in addition to various individual investment accounts outside of the pooled funds.

The Treasurer further invests pooled funds from the OCIP and OCEIP into three funds, the Orange County Money Market Fund (OCMMF), the Orange County Educational Money Market Fund (OCEMMF) and the Extended Fund. On August 11, 2015, Standard & Poor's (S&P) reaffirmed an AAA Principal Stability Fund Rating (AAAm) for the OCMMF and the OCEMMF. The money market funds are required to maintain a NAV of between $0.995 and $1.005 to maintain an AAAm rating. Although not rated, JWA funds conform to the same rating criteria as the OCMMF and OCEMMF. Neither the Money Market Funds nor the Extended Fund have any legally binding guarantees of share values.

The maximum maturity of investments for the two Money Market Funds and JWA is 13 months with a maximum weighted average maturity (WAM) of 60 days. The maximum maturity of the Extended Fund is five years per CGC. The IPS provides that the Extended Fund shall have a duration not to exceed a leading 1-3 Year index +25%.

Pursuant to CGC Sections 27130-27137, the Board of Supervisors (Board) has established a Treasury Oversight Committee (TOC) that monitors and reviews the IPS annually and also ensures that the Treasurer has an audit annually, which includes limited tests of compliance with laws and regulations. The TOC consists of the County Executive Officer, the elected County Auditor-Controller, the County Superintendent of the Schools, or their respective designees, and four public members with a majority required to have expertise in public finance.

The investment practices and policies of the Treasurer are based on compliance with state law and prudent money management. The primary goal is to invest public funds in a manner which will provide maximum security of principal invested, with secondary emphasis on providing adequate liquidity to pool participants. The last goal is to achieve a market rate of return within the parameters of prudent risk management while conforming to all applicable statutes and resolutions governing the investment of public funds.

Interest is allocated to individual funds monthly based on the average daily balances on deposit with the Treasurer. Interest assigned to another fund due to management decision is recognized in the fund that reports the investments and is reported as a transfer to the recipient fund.

## A. Deposits

As of June 30, 2015, the carrying amount of noninterest-bearing deposits was $121.3 million, which consisted of demand accounts in financial institutions. The Treasurer has established separate bank and investment custody accounts for the County's school and community college participants.

The CGC Section 53652 et. seq. and the IPS prescribe the amount of collateral that is required to secure the deposit of public funds. The pledge to secure deposits is administered by the California Commissioner of Business Oversight. Collateral is required for demand deposits at 110% of all deposits not covered by Federal depository insurance (FDIC) if obligations of the United States and its agencies, or obligations of the State or its municipalities, school districts, and district corporations are pledged. Collateral of 150% is required if a deposit is secured by first mortgages or first trust deeds upon improved residential real property located in California. All such collateral is considered to be held by the pledging financial institutions' trust departments or agents in the name of the County. Obligations pledged to secure deposits must be delivered to an institution other than the institution in which the deposit is made; however, the trust department of the same institution may hold them. Written custodial agreements are required that provide, among other things, that the collateral securities are held separate from the assets of the custodial institution.

FDIC is available for interest and noninterest-bearing funds deposited at any on financial institution up to a maximum of $250,000.

Custodial Credit Risk-Deposits

The custodial credit risk for deposits is the risk that the County will not be able to recover deposits that are in the possession of an outside party. Deposits are exposed to custodial credit risk if they are not insured or collateralized. The County's deposits are not exposed to custodial credit risk, since all of its deposits are covered by FDIC or collateralized with securities held by the County or its agent in the County's name, in accordance with CGC section 53562.

## B. Investments

CGC Sections 53601 and 53635, Board of Supervisors' ordinances and resolutions, the County's IPS, the bond indenture documents, trust agreements, and other contractual agreements govern the investments that may be purchased and may include certain restrictions on investment maturity, maximum portfolio percentages, term, value, credit quality and timing to minimize the risk of loss. The IPS adds further restrictions to permitted investments from CGC. All investments must be U.S. dollar denominated. As of June 30, 2015, the Treasurer was in full compliance with the more restrictive IPS for the OCIP and OCEIP. However, on June 30, 2015, JWA purchased a $3.0 million Federal Farm Credit floating rate security with a final maturity of

496 days, which exceeds the IPS limit of 397 days. The security was sold on July 2, 2015, at no gain or loss to bring JWA back into compliance and the system compliance rules were updated.

The following table provides a summary listing of the authorized investments and selected restrictions as of June 30, 2015.

| Type of Investment | CGC % of Funds Permitted | Orange County IPS (%) | CGC Maximum Final Maturity | Orange County IPS Maximum Final Maturity (Long-Term-Extended Fund) | Orange County IPS Maximum Final Maturity (Short-Term – Money Market Fund) |
|---|---|---|---|---|---|
| U.S. Treasury Securities | 100% | 100% | 5 Years | 5 Years | 397 Days |
| U.S. Government Agency Securities | 100% | 100% Total, no more than 33% in one issuer | 5 Years | 5 Years | 397 Days |
| Municipal Debt | 100% | 30% Total, no more than 5% in one issuer except 10%- County of Orange | 5 Years | 5 Years | 397 Days |
| Medium-Term Notes | 30% | 30% Total, no more than 5% in one issuer | 5 Years | 5 Years | 397 Days |
| Bankers Acceptances | 40%, 30% of a single issuer | 40% Total, no more than 5% in one issuer | 180 Days | 180 Days | 180 Days |
| Commercial Paper | 40%, 10% of a single issuer | 40% Total, no more than 5% in one issuer | 270 Days | 270 Days | 270 Days |
| Negotiable Certificates of Deposits | 30% | 30% Total, no more than 5% in one issuer | 5 Years | 5 Years | 397 Days |
| Repurchase Agreements | 100% | 20% Total, no more than 10% in one issuer | 1 Year | 1 Year | 1 Year |
| Money Market Mutual Funds | 20% | 20% Total | N/A | N/A | N/A |
| Investment Pools | 100% | 20% Total, no more than 10% in one pool | N/A | N/A | N/A |
| Supranationals | 30% | 30% Total, no more than 5% in one issuer | 5 Years | 5 Years | 397 Days |

# ORANGE COUNTY TREASURY

Notes to the Financial Schedule (Continued)

June 30, 2015

The current IPS expressly prohibits leverage, reverse repurchase agreements as defined by CGC, structured notes, structured investment vehicles, and derivatives. No investment may be purchased from an issuer that has been place on credit watch-negative by any of Nationally Recognized Statistical Rating Organizations (NRSROs), or whose credit rating by any of the NRSROs is less than the minimum rating required by the IPS for that class of security unless the issuer has a short-term rating of “A-1+” or “F1+” or a long-term rating of a least an “AA” or “Aa2” by S&P and Fitch or Moody’s, and the Treasurer has approved the purchase in writing prior to purchase.

Investments are stated at fair value and accounted for on a settlement day basis. Investments are marked to market on a daily basis and fair value pricing is obtained from the County’s custodian bank and Bloomberg. If the NAV of the Money Market Fund for either the OCMMF or the OCEMMF is less than $0.995 or greater than $1.005, portfolio holdings may be sold as necessary to maintain the ratio between $0.995 and $1.005.

Investment Disclosures

The following table presents a summary of the County’s investments and credit quality distribution and concentration of credit risk by investment type as a percentage of each pool’s fair value at June 30, 2015.

| | Fair Value | Principal | Interest Rate Range (%) | Maturity Range | Weighted Average Maturity (Years) | Ratings (2) | % of Portfolio |
|---|---|---|---|---|---|---|---|
| **OCIP (1)** | | | | | | | |
| U.S. Government Agencies | | | | | | | |
| FNMA Discount Notes | $ 20,525,000 | $ 20,525,000 | 0.06 - 0.08% | 7/1/15 - 7/8/15 | 0.008 | A-1 | 0.58% |
| FNMA Bonds | 515,130,542 | 511,999,161 | 0.07 - 1.24% | 7/2/15 - 12/20/17 | 1.367 | AA | 14.64% |
| FFCB Discount Notes | 25,718,933 | 25,725,000 | 0.26% | 9/28/15 - 10/19/15 | 0.280 | A-1 | 0.73% |
| FFCB Bonds | 205,833,733 | 205,710,691 | 0.14 - 1.09% | 7/2/15 - 6/25/18 | 0.602 | AA | 5.85% |
| FHLB Discount Notes | 199,983,250 | 199,987,000 | 0.03 - 0.12% | 7/1/15 - 8/19/15 | 0.071 | A-1 | 5.68% |
| FHLB Bonds | 448,493,852 | 447,368,168 | 0.12 - 1.64% | 7/10/15 - 12/20/18 | 1.207 | AA | 12.74% |
| FHLMC Discount Notes | 126,397,702 | 126,406,832 | 0.04 - 0.17% | 7/6/15 - 11/3/15 | 0.123 | A-1 | 3.59% |
| FHLMC Bonds | 518,553,134 | 516,966,689 | 0.09 - 1.08% | 7/17/15 - 6/22/18 | 1.481 | AA | 14.73% |
| Negotiable Certificates of Deposit | 55,007,240 | 55,000,000 | 0.12 - 0.34% | 7/31/15 - 12/1/15 | 0.092 | A-1 | 1.56% |
| Medium-Term Corporate Notes | | | | | | | |
| Corporate Notes | 43,895,049 | 41,997,598 | 0.90 - 1.08% | 1/31/17 - 8/15/18 | 2.490 | A | 1.25% |
| Corporate Notes | 202,844,148 | 199,623,224 | 0.35 - 1.49% | 7/8/15 - 12/15/18 | 1.678 | AA | 5.76% |
| Corporate Notes | 61,082,143 | 59,682,583 | 0.49 - 1.27% | 5/15/16 - 12/5/18 | 1.704 | AAA | 1.74% |
| Municipal Debt | 12,495,423 | 12,476,708 | 0.80% | 6/30/16 | 1.003 | AA | 0.36% |
| U.S. Treasuries | 917,948,334 | 914,767,283 | 0.24 - 0.98% | 9/15/15 - 4/15/18 | 1.098 | AA | 26.08% |
| Money Market Mutual Funds | 165,642,021 | 165,642,021 | 0.01 - 0.04% | 7/1/2015 | 0.078 | AAA | 4.71% |
| | **$ 3,519,550,504** | **$ 3,503,877,958** | | | **1.073 (3)** | | **100.00%** |

**ORANGE COUNTY TREASURY**

Notes to the Financial Schedule (Continued)

June 30, 2015

| | Fair Value | Principal | Interest Rate Range (%) | Maturity Range | Weighted Average Maturity (Years) | Ratings (2) | % of Portfolio |
|---|---|---|---|---|---|---|---|
| **OCEIP (1)** | | | | | | | |
| U.S. Government Agencies | | | | | | | |
| FNMA Discount Notes | $ 109,994,312 | $ 110,002,000 | 0.06- 0.12% | 7/2/15 - 10/7/15 | 0.110 | A-1 | 2.91% |
| FNMA Bonds | 527,827,705 | 524,491,839 | 0.10 - 1.24% | 7/2/15 - 12/20/17 | 1.380 | AA | 13.96% |
| FFCB Discount Notes | 9,999,620 | 10,000,000 | 0.04% | 8/4/15 | 0.096 | A-1 | 0.26% |
| FFCB Bonds | 193,142,971 | 192,964,309 | 0.04 - 1.09% | 7/30/15 - 6/25/18 | 0.709 | AA | 5.11% |
| FHLB Discount Notes | 194,494,384 | 194,502,000 | 0.03 - 0.15% | 7/10/15 - 10/21/15 | 0.100 | A-1 | 5.14% |
| FHLB Bonds | 501,667,362 | 500,546,832 | 0.07 - 1.64% | 7/23/15 - 12/20/18 | 1.097 | AA | 13.27% |
| FHLMC Discount Notes | 222,472,719 | 222,480,168 | 0.06 - 0.19% | 7/10/15 - 10/15/15 | 0.082 | A-1 | 5.88% |
| FHLMC Bonds | 483,637,479 | 482,097,311 | 0.14 - 1.08% | 9/4/15 - 6/22/18 | 1.588 | AA | 12.79% |
| Negotiable Certificates of Deposit | 58,007,280 | 58,000,000 | 0.24 - 0.34% | 7/16/15 - 12/1/15 | 0.076 | A-1 | 1.54% |
| Corporate Notes | 44,058,938 | 42,154,402 | 0.90 - 1.08% | 1/31/17 - 8/15/18 | 2.490 | A | 1.16% |
| Corporate Notes | 221,542,520 | 218,213,776 | 0.23 - 1.49% | 7/8/15 - 12/15/18 | 1.782 | AA | 5.86% |
| Corporate Notes | 61,310,203 | 59,905,417 | 0.48 - 1.27% | 5/15/16 - 12/5/18 | 1.704 | AAA | 1.63% |
| Municipal Debt | 12,542,077 | 12,523,292 | 0.80% | 6/30/16 | 1.003 | AA | 0.33% |
| U.S. Treasuries | 921,375,645 | 918,182,717 | 0.24 - 0.98% | 9/15/15 - 4/15/18 | 1.098 | AA | 24.37% |
| Money Market Mutual Funds | 218,950,076 | 218,950,076 | 0.01 - 0.04% | 7/1/2015 | 0.079 | AAA | 5.79% |
| | **$ 3,781,023,291** | **$ 3,765,014,139** | | | **1.016 (3)** | | **100.00%** |

| | Fair Value | Principal | Interest Rate Range (%) | Maturity Range | Weighted Average Maturity (Years) | Ratings (2) | % of Portfolio |
|---|---|---|---|---|---|---|---|
| **Non- Pooled (1)** | | | | | | | |
| U.S. Government Agencies | | | | | | | |
| FNMA Discount Notes | $ 499,925 | $ 500,000 | 0.15% | 9/30/15 | 0.252 | A-1 | 0.30% |
| FNMA Bonds | 12,405,669 | 12,361,000 | 0.09 - 0.27% | 7/28/15 - 12/21/15 | 0.229 | AA | 7.34% |
| FFCB Bonds | 7,721,157 | 7,705,000 | 0.14 - 0.28% | 7/2/15 - 4/18/16 | 0.124 | AA | 4.57% |
| FHLB Bonds | 13,866,424 | 13,860,000 | 0.07 - 0.25% | 7/23/15 - 1/4/16 | 0.078 | AA | 8.21% |
| FHLMC Bonds | 5,273,986 | 5,270,000 | 0.09 - 0.25% | 7/17/15 -10/16/15 | 0.115 | AA | 3.12% |
| GNMA Bonds | 93,653 | 90,193 | 6.25% | 9/20/29 | 14.236 | AA | 0.05% |
| Corporate Notes | 4,432,325 | 4,390,000 | 0.22 - 0.41% | 7/1/15 - 6/1/16 | 0.397 | AA | 2.62% |
| Municipal Debt | 73,901,072 | 73,825,000 | 0.05 - 0.12% | 7/1/15 - 8/15/15 | 0.041 | AA | 43.73% |
| Repurchase Agreements | 1,081,500 | 1,081,500 | 6.20% | 8/15/19 | 4.129 | AA | 0.64% |
| | **$ 168,988,996** | **$ 168,796,581** | | | **0.101 (3)** | | **100.00%** |

(1) Legend:
- FNMA - Federal National Mortgage Association
- FFCB - Federal Farm Credit Bank
- FHLB - Federal Home Loan Bank
- FHLMC - Federal Home Loan Mortgage Corporation
- GNMA - Government National Mortgage Association

(2) The County obtains credit ratings from S&P, Moody’s, and Fitch. The ratings indicative of the greatest degree of risk have been disclosed at a minimum. Ratings modifiers (numbers, + and -) have been eliminated.

(3) Total portfolio weighted average maturity

## Investment in County of Orange Taxable Pension Obligation Bonds 2015 Series A

On January 13, 2015, the OCIP and the OCEIP purchased a portion of the County issued Taxable Pension Obligation Bonds 2015, Series A (2015 POBs) in the principal amount of $25.0 million. The 2015 POBs were issued with a fixed coupon rate of 0.80% and a maturity in June 2016. The obligation of the County to pay principal and interest on the 2015 POBs is an obligation imposed by law and is absolute and unconditional. As of June 30, 2015, the outstanding principal amount of the 2015 POBs is $25.0 million. The bonds are rated AA- by S&P. The County's investment in the 2015 POBs is disclosed herein as Municipal Debt.

## Temporary Transfers to Orange County School Districts

The Board's Resolution No. 15-016, dated March 10, 2015, authorized the Treasurer to make temporary transfers to school districts for fiscal years 2015-2016, 2016-2017, 2017-2018 and 2018-2019 to address their short-term cash flow needs. In fiscal year 2014-2015, the Treasurer made temporary transfers to two Orange County school districts as required by state law and authorized by the Board's Resolution No. 13-016. The loans are secured by tax receipts to be received by the Treasurer as the banker for the school districts and as of June 30, 2015 there were no loans outstanding.

## Interest Rate Risk – Investments

This is the risk that changes in interest rates will adversely affect the fair value of an investment. Generally, investments of longer maturities are more sensitive to changes in market interest rates. Declines in the fair value of investments are managed by limiting the length of the maturity of the securities. In general, the maximum maturity allowed is five years unless the Board has granted express authority either specifically or as part of an investment policy. Actual weighted average days to maturity by investment type for the funds invested in the Pools are presented in the preceding table.

The OCIP of $3.5 billion and the OCEIP of $3.8 billion at June 30, 2015, have 37.44% and 39.99%, respectively, of their investments maturing in six months or less, 60.99% and 58.54%, respectively, of the investments maturing between six months and three years, and 1.57% and 1.47%, respectively, maturing from three to five years. There was an additional $169 million in non-pooled assets held at June 30, 2015, with 97.26% of these investments maturing within six months, 2.68% in six months to five years, and 0.06% maturing in 13 years.

As of June 30, 2015, variable-rate notes comprised 4.17% and 4.74% of the OCIP and OCEIP, respectively. The notes are tied to the Federal funds rate, 90-day Treasury Bill rate, one-month and three-month London Interbank Offered Rate (LIBOR) with daily, monthly and quarterly coupon resets. The fair value of variable-rate securities is generally less susceptible to changes in value because the variable-rate coupon resets back to a market rate on a periodic basis. Effectively, at each reset date, a variable-rate investment reprices back to par value, eliminating interest rate risk at each periodic reset. For purposes of computing weighted average maturity (WAM), the maturity date of variable-rate notes is the length of time until the next reset date rather than the stated maturity.

## ORANGE COUNTY TREASURY

Notes to the Financial Schedule (Continued)

June 30, 2015

The annual average daily investment balance of the OCIP and the OCEIP was approximately $3.5 billion and $3.7 billion, respectively, with an annual gross yield of 0.42% and 0.41%, respectively, for the pools, for the year ended June 30, 2015.

Interest Rate Risk – Weighted Average Maturity (Money Market Funds)

At June 30, 2015, the OCMMF and OCEMMF amounted to approximately $916 million and $1.2 billion, respectively. In accordance with the Board formally approved IPS, the Treasurer manages the pool's exposure to declines in fair value for deposits and investments by limiting the WAM to 60 days in the Money Market Funds. At June 30, 2015, the WAM of the OCMMF was 54 days and the OCEMMF was 58 days. At the same date, the NAV of the Money Market Funds for both pools was $1.00 (in absolute dollar amounts).

Interest Rate Risk – Duration (Extended Fund)

At June 30, 2015, the Extended Fund (which includes funds from both OCIP and OCEIP) balance was approximately $5.2 billion. Of this amount, the OCIP owned 49.9% and the OCEIP owned 50.1%. In accordance with the IPS, the Treasurer manages investment related risk for deposits and investments by limiting duration to +25% of a leading 1-3 Year index (2.34). The portfolio duration for the Extended Fund as of June 30, 2015 was 1.38 years. This was computed using the Macaulay duration method, which calculates the maturity date of callable bonds using their final maturity date.

As of June 30, 2015, the Extended Fund had the following duration by investment type:

| Investment Type | Fair Value | Portfolio % | Macaulay Duration (In Years) |
|---|---|---|---|
| Medium-Term Corporate Notes | $ 509,615,752 | 9.77% | 1.94 |
| Municipal Debt | 25,037,500 | 0.48% | 1.00 |
| U.S. Treasuries | 1,839,323,979 | 35.26% | 1.09 |
| U.S. Government Agencies | 2,842,462,448 | 54.49% | 1.47 |
| Total Fair Value | $ 5,216,439,679 | 100.00% | |
| Portfolio Duration | | | 1.38 |

Custodial Credit Risk – Investments

For an investment, custodial credit risk is the risk that in the event of the failure of the counterparty, the County will not be able to recover the value of its investments or collateral securities that are in possession of an outside party. The IPS does not permit investments in uninsured and unregistered securities not held by the County. The Treasurer utilizes third party delivery versus payment (DVP), which mitigates any custodial credit risk. Securities purchased by the Treasurer are held by third party custodians in their trust department to mitigate custodial credit risk. At year-end, in accordance with the IPS, the County's external investment pools and specific investments did not have any securities exposed to custodial credit risk, and the Treasurer did not have any securities lending during the year (or at year-end).

Credit Risk – Investments

This is the risk that an issuer or other counterparty to an investment may not fulfill its obligations. To mitigate this risk, the IPS, which is more restrictive than the CGC, places minimum acceptable credit ratings for investments from any two of the following NRSROs: S&P, Moody's, or Fitch. For an issuer of short-term debt, the rating must be no less than "A-1" or "SP-1" (S&P), "P-1" or "MIG 1/VMIG 1" (Moody's), or "F1" (Fitch), while an issuer of long-term debt shall be rated no less than an "A" in the Money Market Funds and "AA" in the Extended Fund. Municipal debt issued by the County is exempt from the above credit rating requirements. As of June 30, 2015, the County's external investment pools and specific investments were in compliance with the IPS limits.

Concentration of Credit Risk

This is the risk of loss attributed to the magnitude of a government's investment in a single issuer. To mitigate this risk, the IPS, which is more restrictive than the CGC, limits the amount of exposure to any one single issuer. As of June 30, 2015, all investments were in compliance with state law and the IPS single issuer limits.

Foreign Currency Risk

The IPS requires all securities to be U.S. dollar denominated. The County investments pools are not exposed to foreign currency risk.

## 3. SUBSEQUENT EVENTS

Annual IPS Change

The Board of Supervisors approved the 2016 IPS on December 15, 2015, which included changes to allowed investments and revisions to conform to CGC. The following changes to the IPS were approved by the Board: excluded government securities with maturities of 30 days or less from the 33% limit to match S&P's money market mutual fund rating guidelines and authorized investments of up to $50.0 million per pool in the Local Agency Investment Fund (LAIF). These IPS changes in addition to other minor changes are not considered a significant change to the overall structure for the prudent investment of the balances entrusted to the Treasurer.

Credit Rating Upgrade of 2015 Taxable Pension Obligation Bonds

As of June 30, 2015, the OCIP and OCEIP held $25.0 million of Orange County Taxable Pension Obligation Bonds, 2015 Series A. These bonds were assigned a credit rating of AA- by S&P when issued and upgraded to AA on December 28, 2015. Also on December 28, 2015, S&P upgraded Orange County's Issuer Credit Rating (ICR) to AA+ from AA, while Fitch Ratings affirmed their Implied General Obligation (GO) Bonds rating of AA+. On December 17, 2015, Moody's affirmed their Orange County's Aa1 issuer credit rating.

Purchase of 2016 Taxable Pension Obligation Bonds

In January 2016, the investment pools purchased $153.0 million of Orange County Taxable Pension Obligation Bonds, 2016 Series A, maturing in phases from August 1, 2016 to June 30, 2017 at rates of 0.753% to 1.088%. These bonds were issued with an assigned long-term rating of AA from S&P, and assigned long-term and short-term ratings of AA and F1+, respectively, from Fitch Ratings.

**Independent Auditor's Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance With *Government Auditing Standards***

The Honorable Board of Supervisors
County of Orange, California

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the Schedule of Assets Held by the County Treasury (Schedule) of County of Orange, California (County), as of June 30, 2015, and the related notes to the financial schedule, and have issued our report thereon dated April 8, 2016.

**Internal Control Over Financial Reporting**

In planning and performing our audit of the financial schedule, we considered the County Treasurer's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial schedule, but not for the purpose of expressing an opinion on the effectiveness of the County Treasurer's internal control. Accordingly, we do not express an opinion on the effectiveness of the County Treasurer's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

**Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the Treasurer's financial schedule is free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial schedule amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

**Purpose of this Report**

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Macias Gini & O'Connell LLP

Newport Beach, California
April 8, 2016