



**COUNTY OF LOS ANGELES
DEPARTMENT OF AUDITOR-CONTROLLER**

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JOHN NAIMO
ACTING AUDITOR-CONTROLLER

July 2, 2014

TO: Supervisor Don Knabe, Chairman
Supervisor Gloria Molina
Supervisor Mark Ridley-Thomas
Supervisor Zev Yaroslavsky
Supervisor Michael D. Antonovich

FROM: John Naimo
Acting Auditor-Controller

SUBJECT: **LOS ANGELES COUNTY TREASURY COMMUNICATION OF
INTERNAL CONTROL RELATED MATTERS FOR THE YEAR ENDED
JUNE 30, 2013**

California Government Code Section 26920 requires annual audits of the assets in the County Treasury, with an opinion on whether the Treasurer's statement of assets is presented fairly and in accordance with generally accepted accounting principles. We contracted with an independent Certified Public Accounting firm, Bazilio Cobb Associates (Bazilio), to audit the financial statements of the Los Angeles County Treasury for the year ended June 30, 2013. Bazilio conducted the audit under the Auditor-Controller's Master Agreement.

As part of the audit, Bazilio issued a report on the Communication of Internal Control Related Matters for the Year Ended June 30, 2013 (Attachment I). The report includes recommendations designed to strengthen internal controls over investment transactions, system access, change management, and software updates. The Treasurer's response, which is incorporated into Bazilio's report, indicates they generally agree with the findings and have taken action to implement the recommendations.

The internal control review was conducted in conjunction with the financial statement audit which we previously issued to your Board on January 2, 2014 (Attachment II).

Board of Supervisors
July 2, 2014
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Please call me if you have any questions, or your staff may call Robert Smythe at (213) 253-0101.

JN:AB:RS:MP

Attachments

c: William T Fujioka, Chief Executive Officer
Mark J. Saladino, Treasurer and Tax Collector
Public Information Office
Audit Committee



Los Angeles County Treasury
Communication of Internal Control Related Matters
Year Ended June 30, 2013

**LOS ANGELES COUNTY TREASURY
COMMUNICATION OF INTERNAL CONTROL RELATED MATTERS
YEAR ENDED JUNE 30, 2013**

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Board of Supervisors
County of Los Angeles, California

In planning and performing our audit of the financial statements of the Los Angeles County Treasury (Treasury) as of and for the year ended June 30, 2013, in accordance with auditing standards generally accepted in the United States of America, we considered the Treasury's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Treasury's internal control. Accordingly, we do not express an opinion on the effectiveness of the Treasury'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 deficiency in design exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or when the person performing the control does not possess the necessary authority or competence to perform the control effectively.

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.

The control matters listed on pages 2 to 5, are descriptions of other identified deficiencies in internal control that we determined did not constitute significant deficiencies or material weaknesses.

This communication is intended solely for the information and use of management, Board of Supervisors, others within the organization, and is not intended to be, and should not be, used by anyone other than these specified parties.

Los Angeles, California
November 15, 2013

Bazilio Cobb Associates, P.C.

LOS ANGELES COUNTY TREASURY
COMMUNICATION OF INTERNAL CONTROL RELATED MATTERS
YEAR ENDED JUNE 30, 2013

CURRENT YEAR'S COMMENTS

1. Strengthen Internal Controls Branch Monitoring of Trades and Broker/Dealer Approval

The Los Angeles County Treasury (Treasury) Board-approved Investment Policy, dated March 19, 2013, states that all investment transactions made by the Investment Office are to be reviewed by the Internal Controls Branch (ICB) to assure compliance with the Investment Policy. To meet the requirements of the Investment Policy, ICB uses two levels of review for investment trades. In addition, effective monitoring of internal control is one of the five components of effective internal control delineated in Committee of Sponsoring Organization of the Treadway Commission's (COSO) *Internal Control - Integrated Framework*, which requires timely monitoring of operating controls.

We selected a sample of forty purchases and sales trade tickets to verify the effectiveness of certain controls, such as the timely review of investment transactions performed by employees of ICB. While the first level reviews were performed timely, we noted the following:

- Nine (9) purchases and four (4) sales trade tickets were not reviewed timely by an ICB manager. In these instances, the ICB manager completed the second level review one to three months after the trade date.
- Four (4) sale trade tickets did not reflect ICB's management approval.

Although none of the investment transactions reviewed were in non-compliance with the Investment Policy, without timely reviews of investment trades by the management of ICB, the risk increases that investment trades may not be in compliance with the Investment Policy and errors may not be addressed in a timely manner.

Additionally, in reviewing the current list of brokers and dealers and supporting documentation to determine whether the approval process was followed, the Treasury was unable to provide the Compliance Questionnaire for six (6) of the twelve (12) selected brokers. Management did not provide the Compliance Questionnaires because the Treasury maintains records for brokers and dealers for seven years.

Recommendation

An ICB manager should review trades for compliance in a timely manner. ICB should maintain compliance records for all active brokers and dealers.

Management Response

ICB's practice is to document an initial review and a management review of all tickets/delivery instructions. The initial review is usually completed within one day of

LOS ANGELES COUNTY TREASURY
COMMUNICATION OF INTERNAL CONTROL RELATED MATTERS
YEAR ENDED JUNE 30, 2013

trading. We have policy limits entered into ResourceIQ to ensure trades align with the Investment Policy; ResourceIQ reports provide daily summaries over compliance. Management is immediately notified by staff if there are any deviations from the Investment Policy. Management will complete its review of the trade tickets within a timely manner. This secondary review assures the completeness of the initial review, and management's awareness of trading activities. Further, ICB will change its practice to request compliance questionnaires for all active brokers every 3 to 5 years.

2. Strengthen Access and Other Application Controls of the Systems Branch

Access Controls

Access controls limit or detect access to computer programs, data, and equipment and protect these resources from unauthorized modification, disclosure, loss, or impairment. They also serve as key controls for ensuring that staff duties and responsibilities are implemented in a way that safeguards applications. These controls are designed to reduce the risk of errors or fraud from occurring and going undetected.

The Treasury did not implement proper access controls over the ResourceIQ application during the audit year. For example:

- Certain employees of the Investment Office had unnecessary access to the ResourceIQ application. These employees process trade tickets and do not require ResourceIQ to process these transactions. Privileges should be granted on a need-only basis.
- A terminated employee remained on the access control list but the position was vacant. Management maintained the user profile as active to facilitate quick user profile setup, as the profile will be duplicated/used upon recruitment of a new employee.
- The access control list contained the following generic IDs: POLLER – used to run reports and post data in the system; TEST-CMO; TEST – IO; TEST –IC; SYS-POLLER; and SYS-ADMIN. The system does not track the activities of these generic users.

The conditions existed because the Treasury did not design and or implement proper access controls to prevent unauthorized activities or transactions.

A lack of audit and accountability results in the breakdown in detective (monitoring) controls which can have a direct impact on the Treasury's system and, consequently, the financial statements. Without uniquely identifiable administrative and user accounts, it is difficult to track the employee activities within the system. Additionally, audit trails aid in identifying potential malevolent activities which otherwise may go unnoticed.

LOS ANGELES COUNTY TREASURY
COMMUNICATION OF INTERNAL CONTROL RELATED MATTERS
YEAR ENDED JUNE 30, 2013

Other Application Controls

- The version of ResourceIQ in use is 2.2.39, which is outdated and two versions behind the current version 2.2.41. This condition exists due to workload priorities, which prevented the Treasury from keeping up-to-date with new software versions and patches. If the version of the application is not current, this increases the Treasury's security, support and business risks. The Treasury is at risk to lose the ResourceIQ application and data, and may not be able to recover fully in the event of a disaster because of unsupported systems.
- No proper Information Technology (IT) change management policies and procedures existed for Treasury related applications. Prior incidences of IT changes were achieved through verbal communications and emails. Management indicated that this condition exists because of inadequate resources for policy conversion changes. Informal change management policies and procedures increase the risk of unauthorized and properly assessed changes, low change success rate, and significant delays in daily operations.

Recommendation

The Treasury should review its access control policies, and redesign and implement best practice policies and procedures that provide access on a need-only basis; remove IDs of employees immediately upon termination/resignation; restrict generic IDs to the test environment and remove all generic IDs from the production environment.

The Treasury should also implement a comprehensive Technology Information Policy that addresses change management and keeping up-to-date with new software versions and patches. In the interim, the Treasury should upgrade the ResourceIQ application to version 2.2.41.

Management Response

Access Controls

We agree the Investment Office staff were granted access to ResourceIQ, but we also confirmed through the application that they did not access the application since 1999, thereby eliminating the risk that was identified. We have removed access from the Investment Office staff. The terminated employee's profile was cancelled. We deleted generic IDs, however, there are some specific system accounts including POLLER and SYS-ADMIN that are required by ResourceIQ that cannot be deleted. We will perform periodic reviews of user access.

**LOS ANGELES COUNTY TREASURY
COMMUNICATION OF INTERNAL CONTROL RELATED MATTERS
YEAR ENDED JUNE 30, 2013**

Other Application Controls

As newer software versions, patches, or minor releases are provided by vendors, we often compare the added functionality, fixes, and security enhancements to our business requirements and determine if and when to implement while taking into consideration other potential risks including system downtime. As such, we planned accordingly and migrated the physical ResourceIQ server to a virtual environment and upgraded ResourceIQ to the latest software version 2.2.41 as of April 16, 2014.

We have implemented and continue to follow the comprehensive Information Technology and Security Policies approved by the Board of Supervisors and are enhancing our change management procedures to meet business needs and best practices.



**COUNTY OF LOS ANGELES
DEPARTMENT OF AUDITOR-CONTROLLER**

**Attachment II
Page 1 of 28**

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WENDY L. WATANABE
AUDITOR-CONTROLLER

January 2, 2014

TO: Supervisor Don Knabe, Chairman
Supervisor Gloria Molina
Supervisor Mark Ridley-Thomas
Supervisor Zev Yaroslavsky
Supervisor Michael D. Antonovich

FROM: Wendy L. Watanabe
Auditor-Controller

SUBJECT: **AUDIT OF THE LOS ANGELES COUNTY TREASURY FOR THE YEAR
ENDED JUNE 30, 2013**

California Government Code Section 26920 (Code) requires annual audits of the assets in the County Treasury, with an opinion on whether the Treasurer's statement of assets is presented fairly and in accordance with generally accepted accounting principles. We contracted with an independent Certified Public Accounting firm, Bazilio Cobb Associates (BCA), to audit the financial statements of the Los Angeles County Treasury for the year ended June 30, 2013.

BCA issued an unqualified opinion on the Treasurer's financial statements, indicating the statements are presented fairly and in conformity with accounting principles generally accepted in the United States of America (Attachment). As part of the audit, BCA reviewed the Treasurer's internal controls over financial reporting and identified no material weaknesses.

BCA also included results of an examination of the Treasurer's compliance with certain legal provisions, regulations, contracts and grant agreements. BCA noted no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Please call me if you have any questions, or your staff may call Robert Smythe at (213) 253-0101.

WLW:AB:RS:MP

Attachment

c: William T Fujioka, Chief Executive Officer
Mark J. Saladino, Treasurer and Tax Collector
Public Information Office
Audit Committee



Los Angeles County Treasury
Management's Discussion and Analysis and Financial
Statements with Independent Auditor's Report
June 30, 2013

**LOS ANGELES COUNTY TREASURY
MANAGEMENT’S DISCUSSION AND ANALYSIS AND
FINANCIAL STATEMENTS WITH
INDEPENDENT AUDITOR’S REPORTS
FOR THE YEAR ENDED JUNE 30, 2013**

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INDEPENDENT AUDITOR'S REPORT

Board of Supervisors
County of Los Angeles, California

Report on the Financial Statements

We have audited the accompanying financial statements of the Los Angeles County Treasury (Treasury), as of and for the year ended June 30, 2013, and the related notes to the financial statements, as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on the financial statements 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 statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Treasury's preparation and fair presentation of the financial statements 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 Treasury'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 statements.

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

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the Treasury, as of June 30, 2013, and the respective changes in financial position for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 1, the statements of the Treasury are intended to present the financial position and changes in financial position of only the Treasury. They do not purport to, and do not, present fairly the financial position of the County of Los Angeles, California, as of June 30, 2013, and the changes in its financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Other Matters

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis as listed in the table of contents be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated November 15, 2013 on our consideration of the Treasury'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 Treasury's internal control over financial reporting and compliance.

Los Angeles, California
November 15, 2013

Basilis Cobb Associates, P.C.

**LOS ANGELES COUNTY TREASURY
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED JUNE 30, 2013
(UNAUDITED)**

The Los Angeles County Treasurer and Tax Collector (Treasury) maintains two investment portfolios, the External Investment Pool (Pool) and the Specific Purpose Investment (SPI) portfolio. The Treasury manages the Pool on behalf of Pool participants through the authority delegated to it annually by the Los Angeles County Board of Supervisors. The primary objective of the Treasury's Investment Policy is to ensure the safety of principal. The secondary objective is to meet the liquidity needs of the Pool participants. The third objective is to achieve a return on funds invested. The Treasury accomplishes these objectives through the purchase of high quality fixed income investments, held to a designated maturity.

Mandatory Pool participants include the County of Los Angeles (County), local school and community college districts within the County and the Superior Courts. Voluntary participants in the Treasury consist of the Sanitation Districts, the Metropolitan Transportation Authority, the South Coast Air Quality Management District and certain other municipal agencies. There were approximately 2,000 Pool participants for the year ended June 30, 2013. The Treasury also maintains a SPI portfolio to manage specific investment objectives of certain Pool participants and voluntary participants. The individual investment strategies of the SPI are established by the needs of the requesting entity.

Other Specific Investments represent assets held by the Treasury, in a custodial capacity, pursuant to Section 1300.76.1, Title 28, California Code of Regulations (State Code).

As management of the Pool, SPI portfolio and Other Specific Investments, we offer readers of the Treasury's financial statements this narrative overview and analysis of the financial activities of the Treasury for the year ended June 30, 2013. We hope that the information presented provides you with a solid understanding of the Treasury's financial status as of June 30, 2013.

Financial Highlights

- The Pool's total net position at June 30, 2013, was \$22.90 billion, an increase of \$1.48 billion (6.93%) from June 30, 2012.
- The Pool had trades payable of \$75 million at June 30, 2013, a decrease of \$1.05 billion (93.33%) from June 30, 2012. Trades payable decreased because of changes in the market conditions making it less beneficial to invest in trades settling at a future date.
- The investment income of the Pool decreased \$66.16 million (28.69%) from \$230.62 million for the year ended June 30, 2012, to \$164.46 million for the year ended June 30, 2013. The decrease in investment income was primarily due to a decline in investment yield. The yield on investments decreased from 0.93% in the prior year to 0.64% in the current year. This was primarily due to a general decrease in market yields during the year ended June 30, 2013 and to the maturity of older investments with higher yields.
- The Pool's net change in fair value of investments was a decrease of \$252.66 million for the year ended June 30, 2013, compared to an increase of \$54.10 million for the year ended June 30, 2012. The decrease is due to the decline in the market conditions during the year ended June 30, 2013. In the quarter preceding the fiscal year end, market interest rates spiked considerably higher, and the higher yields lowered the market value of the portfolio. The Treasurer's investment strategy is to buy and hold high quality fixed income investments to a designated maturity. The liquidity in the

**LOS ANGELES COUNTY TREASURY
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED JUNE 30, 2013
(UNAUDITED)**

Pool is adequate to meet cash flow requirements and, therefore, precludes the Treasurer from having to sell investments below original cost for purposes of meeting cash flow requirements.

- The Pool's allowable investment expenses totaled \$10.68 million for the year ended June 30, 2013. This represented approximately 4.68 basis points of the average daily cash balance for the year ended June 30, 2013.

Overview of the Financial Statements

This discussion and analysis are intended to serve as an introduction to the Treasury's basic financial statements. The Treasury's basic financial statements consist of two components:

- 1-A) Statement of Net Position, 1-B) Statement of Changes in Net Position
- 2) Notes to the Basic Financial Statements

The Statement of Net Position presents information on the assets and liabilities of the Pool, SPI and Other Specific Investments. The difference between the assets and liabilities is reported as net position.

The Statement of Changes in Net Position presents information on how the net position of the Pool, SPI and Other Specific Investments changed during the year ended June 30, 2013.

Statement of Net Position

The Pool's net position was \$22.90 billion at June 30, 2013, an increase of \$1.48 billion (6.93%) from June 30, 2012. The SPI net position was \$90.00 million, a decrease of \$13.67 million (13.18%) from the prior year. The Other Specific Investments net position was \$302 thousand.

The Pool had trades payable totaling \$75 million at June 30, 2013, a decrease of \$1.05 billion (93.33%) from June 30, 2012. The decrease was due to changes in market conditions making it less beneficial to invest in trades settling at a future date. The SPI had trades payable totaling \$40 million at June 30, 2013, an increase of \$40 million (100%) from June 30, 2012.

LOS ANGELES COUNTY TREASURY
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED JUNE 30, 2013
(UNAUDITED)

Net Position

A condensed summary of the net position for the Pool, SPI and Other Specific Investments are presented below:

Statement of Net Position External Investment Pool (In Thousands)				
	2013	2012	Increase/(Decrease)	
			Amount (\$)	Percentage (%)
Assets				
Cash	\$ 70,226	\$ 103,280	\$ (33,054)	-32.00%
Investments at Fair Value	22,869,383	22,161,406	707,977	3.19%
Trades Receivable	-	238,514	(238,514)	-100.00%
Interest Receivable	31,763	32,846	(1,083)	-3.30%
Total Assets	22,971,372	22,536,046	435,326	1.93%
Liabilities				
Trades Payable	75,000	1,123,745	(1,048,745)	-93.33%
Total Liabilities	75,000	1,123,745	(1,048,745)	-93.33%
Net Position	\$ 22,896,372	\$ 21,412,301	\$ 1,484,071	6.93%

Statement of Net Position Specific Purpose Investments (In Thousands)				
	2013	2012	Increase/(Decrease)	
			Amount (\$)	Percentage (%)
Assets				
Investments at Fair Value	\$ 129,620	\$ 103,203	\$ 26,417	25.60%
Interest Receivable	380	463	(83)	-17.93%
Total Assets	130,000	103,666	26,334	25.40%
Liabilities				
Trades Payable	40,000	-	40,000	100.00%
Total Liabilities	40,000	-	40,000	100.00%
Net Position	\$ 90,000	\$ 103,666	\$ (13,666)	-13.18%

Statement of Net Position Other Specific Investments (In Thousands)				
	2013	2012	Increase/(Decrease)	
			Amount (\$)	Percentage (%)
Assets				
Investments at Fair Value	\$ 302	\$ 302	\$ -	0.00%
Total Assets	302	302	-	0.00%
Net Position	\$ 302	\$ 302	\$ -	0.00%

LOS ANGELES COUNTY TREASURY
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED JUNE 30, 2013
(UNAUDITED)

Changes in Net Position

The additions include contributions by the Pool participants, investment income and changes in the fair value of investments. Investment expenses are shown as a deduction to additions to the Pool and to the SPI. Deductions represent distributions to Pool participants.

Pool

- Contributions by the Pool Participants were \$56.15 billion during the year ended June 30, 2013, an increase of \$5.25 billion (10.31%) from the prior year.
- The investment income of the Pool decreased \$66.16 million (28.69%) from \$230.62 million for the year ended June 30, 2012, to \$164.46 million for the year ended June 30, 2013. The earnings rate decreased from 0.93% to 0.64% in the current year. The decrease in the Pool earnings rate can be largely attributed to the decrease in market yields during the year ended June 30, 2013 and the maturity of older higher yielding investments. The average daily investment balance decreased from \$23.61 billion in the prior year ended June 30, 2012, to \$22.73 billion in the current year.
- The Pool's investment expenses, which are deducted from Investment Income, were \$10.68 million for the year ending June 30, 2013, an increase of \$654 thousand (6.53%) from the prior year. This increase was primarily due to an increase in the Treasury's expenses. The \$10.68 million in total investment expenses represented approximately 4.68 basis points of the average daily cash balance for the year ended June 30, 2013.
- The Pool's net change in fair value of investments was a decrease of \$252.66 million for the year ended June 30, 2013, compared to an increase of \$54.10 million for the year ended June 30, 2012. The decrease is due to the decline in the market conditions during the year ended June 30, 2013. In the quarter preceding the fiscal year end, market interest rates spiked considerably higher, and the higher yields lowered the market value of the portfolio. The Treasurer's investment strategy is to buy and hold high quality fixed income investments to a designated maturity. The liquidity in the Pool is adequate to meet cash flow requirements and, therefore, precludes the Treasurer from having to sell investments below original cost for purposes of meeting cash flow requirements.
- Distributions to Pool participants were \$54.56 billion during the year ended June 30, 2013, an increase of \$2.03 billion (3.86%) from the prior year.

SPI

- Contributions by SPI participants were \$1.25 billion during the year ended June 30, 2013, an increase of \$188.89 million (17.76%) from the prior year. The increase was primarily due to an increase in contributions by the Sanitation Districts.
- SPI investment income increased by \$336 thousand (28.64%) from the prior year. The increase was primarily due to the income earned by the Puente Hills Habitat Preservation Authority and Sanitation Districts on new investments made in the latter part of the year ended June 30, 2013.

**LOS ANGELES COUNTY TREASURY
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED JUNE 30, 2013
(UNAUDITED)**

- The SPI's net change in fair value of investments was a decrease of \$2.31 million for the year ended June 30, 2013, compared to a decrease of \$144 thousand for the year ended June 30, 2012. The decrease is due to the decline in the market conditions during year ended June 30, 2013.
- Distributions to the SPI participants of \$1.27 billion were approximately \$231.18 million (22.35%) higher than the prior year's figure of \$1.03 billion. The increases in distributions are primarily due to the increase in distributions to Sanitation Districts.

Other Specific Investments

- There were no new contributions by participants during the year ended June 30, 2013.
- Distributions to participants were approximately \$1 thousand during the years ended June 30, 2013 and 2012.

All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, additions and deductions are reported in this statement for some items that will result in cash flows only in future fiscal periods.

**LOS ANGELES COUNTY TREASURY
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED JUNE 30, 2013
(UNAUDITED)**

A summary of the changes in net position for the Pool, SPI and Other Specific Investments are presented below:

Statement of Changes in Net Position External Investment Pool (In Thousands)							
	2013		2012		Increase/(Decrease)		
					Amount (\$)	Percentage (%)	
Additions:							
Contributions by Participants	\$	56,145,004	\$	50,895,404	\$	5,249,600	10.31%
Investment Income:							
Interest Income		164,460		230,623		(66,163)	-28.69%
Investment Expenses		(10,676)		(10,022)		(654)	6.53%
Net Increase (Decrease) in Fair Value of Investments		<u>(252,661)</u>		<u>54,097</u>		<u>(306,758)</u>	-567.05%
Net Investment Income (Loss)		<u>(98,877)</u>		<u>274,698</u>		<u>(373,575)</u>	-135.99%
Total Additions		<u>56,046,127</u>		<u>51,170,102</u>		<u>4,876,025</u>	9.53%
Deductions:							
Distributions to Participants		<u>54,562,056</u>		<u>52,531,830</u>		<u>2,030,226</u>	3.86%
Net Increase (Decrease) in Net Position		1,484,071		(1,361,728)		2,845,799	-208.98%
Net Position, Beginning of Year		<u>21,412,301</u>		<u>22,774,029</u>		<u>(1,361,728)</u>	-5.98%
Net Position, End of Year	\$	<u>22,896,372</u>	\$	<u>21,412,301</u>	\$	<u>1,484,071</u>	6.93%

Statement of Changes in Net Position Specific Purpose Investments (In Thousands)							
	2013		2012		Increase/(Decrease)		
					Amount (\$)	Percentage (%)	
Additions:							
Contributions by Participants	\$	1,252,557	\$	1,063,671	\$	188,886	17.76%
Investment Income:							
Interest Income		1,509		1,173		336	28.64%
Investment Expenses		(42)		(33)		(9)	27.27%
Net Decrease in Fair Value of Investments		<u>(2,311)</u>		<u>(144)</u>		<u>(2,167)</u>	-1504.86%
Net Investment Income (Loss)		<u>(844)</u>		<u>996</u>		<u>(1,840)</u>	-184.74%
Total Additions		<u>1,251,713</u>		<u>1,064,667</u>		<u>187,046</u>	17.57%
Deductions:							
Distributions to Participants		<u>1,265,379</u>		<u>1,034,202</u>		<u>231,177</u>	22.35%
Net Increase (Decrease) in Net Position		(13,666)		30,465		(44,131)	144.86%
Net Position, Beginning of Year		<u>103,666</u>		<u>73,201</u>		<u>30,465</u>	41.62%
Net Position, End of Year	\$	<u>90,000</u>	\$	<u>103,666</u>	\$	<u>(13,666)</u>	-13.18%

LOS ANGELES COUNTY TREASURY
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED JUNE 30, 2013
(UNAUDITED)

Statement of Changes in Net Position Other Specific Investments (In Thousands)						
	2013		2012		Increase/(Decrease)	
	2013	2012	2013	2012	Amount (\$)	Percentage (%)
Additions:						
Investment Income	\$ -	\$ -	\$ -	\$ -	-	0.00%
Net Increase in Fair Value of Investments	1	1	1	1	-	0.00%
Net Investment Income	1	1	1	1	-	0.00%
Total Additions	1	1	1	1	-	0.00%
Deductions:						
Distributions to Participants	1	1	1	1	-	0.00%
Net Increase (Decrease) in Net Position	-	-	-	-	-	0.00%
Net Position, Beginning of Year	302	302	302	302	-	0.00%
Net Position, End of Year	\$ 302	\$ 302	\$ 302	\$ 302	-	0.00%

Request for Information

This financial report is designed to provide a general overview of the Treasury's finances for all interested parties. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Los Angeles County Treasurer and Tax Collector, 500 West Temple Street, Room 437, Los Angeles, California 90012-2766.

LOS ANGELES COUNTY TREASURY
STATEMENT OF NET POSITION
JUNE 30, 2013
(In Thousands)

	External Investment Pool	Specific Purpose Investments	Other Specific Investments
Assets			
Treasurer Cash	\$ 70,226	\$ -	\$ -
Investments:			
Commercial Paper	6,007,442	-	-
Corporate and Deposit Notes	280,080	1,559	-
Local Agency Investment Fund	32,000	49,476	-
Los Angeles County Securities	-	4,945	-
Mortgage Trust Deeds	-	69	-
Negotiable Certificates of Deposit	3,946,103	-	-
U.S. Agency Securities	11,906,172	73,470	-
U.S. Treasury Securities:			
U.S. Treasury Notes	597,611	-	-
U.S. Treasury Bills	99,975	-	302
U.S. Treasury Bonds	-	101	-
Total Investments	22,869,383	129,620	302
Interest Receivable	31,763	380	-
Total Assets	22,971,372	130,000	302
Liabilities			
Trades Payable	75,000	40,000	-
Total Liabilities	75,000	40,000	-
Total Net Position Held in Trust	\$ 22,896,372	\$ 90,000	\$ 302

The accompanying notes are an integral part of these financial statements.

LOS ANGELES COUNTY TREASURY
STATEMENT OF CHANGES IN NET POSITION
FOR THE YEAR ENDED JUNE 30, 2013
(In Thousands)

	External Investment Pool	Specific Purpose Investments	Other Specific Investments
ADDITIONS:			
Contributions by Pool Participants	\$ 56,145,004	\$ 1,252,557	\$ -
Investment Income:			
Interest Income	164,460	1,509	-
Investment Expenses	(10,676)	(42)	-
Net Increase (Decrease) in Fair Value of Investments	(252,661)	(2,311)	1
Net Investment Income (Loss)	(98,877)	(844)	1
Total Additions	56,046,127	1,251,713	1
DEDUCTIONS:			
Distributions to Pool Participants	54,562,056	1,265,379	1
Net Increase (Decrease) in Net Position	1,484,071	(13,666)	-
Net Position, Beginning of Year	21,412,301	103,666	302
Net Position, End of Year	\$ 22,896,372	\$ 90,000	\$ 302

The accompanying notes are an integral part of these financial statements.

**LOS ANGELES COUNTY TREASURY
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2013**

Note 1 - Summary of Significant Accounting Policies

The Financial Reporting Entity

The Los Angeles County Treasurer and Tax Collector (Treasury) is responsible for tax collection, banking, investment and accountability of public funds. The Treasury maintains two investment portfolios, the External Investment Pool portfolio (the Pool) and the Specific Purpose Investments (SPI) portfolio with approximately \$22.90 billion and \$90 million, respectively, in net position as of June 30, 2013. The Treasury also maintains Other Specific Investments totaling approximately \$302 thousand at June 30, 2013. The State of California allows the Board of Supervisors (Board) the ability to delegate the investment authority to the Treasury in accordance with Section 53607 of the California Government Code. On an annual basis, the Board delegates the investment authority to the Treasury.

External Investment Pool

The Pool is managed by the Treasury on behalf of the Pool participants that include the County of Los Angeles (County) and other entities that are required by State statutes to participate in the Pool such as, local school districts, community colleges and the Superior Courts. Voluntary participants in the Treasury consist of the Sanitation Districts, the Metropolitan Transportation Authority, the South Coast Air Quality Management District and certain other municipal agencies. The purpose of the Pool is to provide safe, liquid investment opportunities for pooled surplus funds deposited into the Treasury. Net Earnings on Pool investments are allocated monthly to Pool participants by the County Auditor-Controller based upon each participant's average daily cash balance in the allocation period. Investment gains and losses are proportionately shared by participants as an increase or reduction in investment, net of investment expenses. Section 27013 of the California Government Code authorizes the Treasury to deduct certain Treasury-related administrative fees. The Pool is not registered with the Securities and Exchange Commission (SEC) as an investment company.

Specific Purpose Investments

The Treasury maintains the SPI portfolio to manage specific investments requested by specific entities with the approval of the Treasury. Investment income/loss distribution is credited/debited to the specific entity for which the investment was made.

Other Specific Investments

Other Specific Investments represents assets held by the Treasury pursuant to Section 1300.76.1, Title 28, California Code of Regulations (State Code). The investments are held in the Treasury's Special Safekeeping Account on behalf of the County's Community Health Plan (CHP). The funds were assigned to the California Commission of Corporations to meet CHP deposit requirements imposed by the California Code of Regulations.

Treasury's Investment Strategy

The Treasury's investment strategy is based on three prioritized objectives. The primary objective is to ensure the safety of principal, the secondary objective is to provide sufficient cash to meet disbursement

LOS ANGELES COUNTY TREASURY
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2013

Note 1 - Summary of Significant Accounting Policies (Continued)

needs and the third objective is to achieve a return. The cash flow needs of the Pool participants are monitored daily to ensure that sufficient liquidity is maintained to meet the needs of participants. The Treasury's basic investment strategy is to buy and hold, to a designated maturity, high quality fixed income investments.

The SPI portfolio is used to account for the net position of individual investment accounts, in aggregate. The related investment activity occurs separately from the Pool and is provided as a service to Pool participants and external public entities. The individual investment strategies are targeted for the needs of the requesting entity.

The Other Specific Investments are used to account for the assets placed with the Treasury pursuant to State Code. The investment activity occurs separately from the County's Pool and the related investment strategies are governed by State Code.

Measurement Focus, Basis of Accounting and Financial Statement Presentation

The accompanying basic financial statements are prepared using the economic resources measurement focus and the accrual basis of accounting. The accompanying basic financial statements present only the statement of net position and statement of changes in net position of the Pool, SPI and Other Specific Investments, and are not intended to present fairly, the financial position and changes in financial position of the County of Los Angeles as a whole in conformity with U.S. generally accepted accounting principles. Contributions from pool participants are recognized as contributions in the period in which they are received. Distributions to pool participants are recognized in the period in which they are distributed.

Earnings on investments are recognized as revenue in the period in which they are earned and investment costs are recognized as an expense when incurred, regardless of the timing of related cash flows. In accordance with generally accepted accounting principles (GAAP), the Treasury records investment purchases and sales on the trade date. In accordance with Governmental Accounting Standards Board (GASB) Statement 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*, the accompanying financial statements reflect the fair value of investments. Fair value is determined monthly. Special disclosures related to GASB 31 appear in Note 3. Pool participants' cash balances and withdrawals are based on amortized cost. The Treasury has prepared its deposit and investments disclosures in accordance with the provisions of GASB Statement No. 40, *Deposit and Investment Risk Disclosures, an amendment to GASB Statement No. 3*. The related disclosures appear in Note 3.

Trades Payable

Trades payable represents the purchase of investments by the Treasury where payment has not been made as of June 30, 2013. Trades payable totaled \$75 billion for the Pool and \$40 million for the SPI at June 30, 2013.

LOS ANGELES COUNTY TREASURY
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2013

Note 1 - Summary of Significant Accounting Policies (Continued)

Trades Receivable

Trades receivable represents securities that have been called but have not settled at June 30, 2013. There was no trades receivable for the Pool and SPI at June 30, 2013.

Use of Estimates

The preparation of the basic financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts in the financial statements. Actual results could differ from the estimates.

New Accounting Pronouncements

In December 2010, the GASB issued Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*. The objective of this Statement is to incorporate into the GASB's authoritative literature certain accounting and financial reporting guidance that is included in the following pronouncements issued on or before November 30, 1989, which does not conflict with or contradict GASB pronouncements: Financial Accounting Standards Board (FASB) Statements and Interpretations, Accounting Principles Board Opinions, and Accounting Research Bulletins of the American Institute of Certified Public Accountants' (AICPA) Committee on Accounting Procedure. The requirements of this Statement are effective for the Treasury's financial statements for periods beginning after December 15, 2011. The application of the codification requirements changed the Treasury's financial statement disclosure references.

In June 2011, the GASB issued Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*. The objective of this Statement is to improve financial reporting by standardizing the presentation of deferred outflows of resources and deferred inflows of resources and their effects on a government's net position. The requirements of this Statement are effective for the Treasury's financial statements for periods beginning after December 15, 2011. The application of the revised guidance of Statement No. 63 changed the terminology of net assets to net position, but did not have a material impact on the Treasury's financial statements.

Note 2 – Treasurer Cash

As of June 30, 2013, the Treasury maintained accounts in five banks. The carrying amount of the Treasury's total deposits in financial institutions was \$69.83 million plus \$0.40 million in cash in the Treasury's vault.

Under California Government Code Section 53652, each financial institution in California is required to pledge a pool of securities as collateral against all of its public deposits. California Government Code Section 53651 delineates the types of eligible securities, and the required collateral percentage, generally at 110%. In addition, under California Government Code Section 53653, the Treasury has discretion to waive security for the portion of any deposits as insured pursuant to federal law. Through contractual agreement, the Treasury has opted to waive security for the portion of deposits which is federally insured.

**LOS ANGELES COUNTY TREASURY
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2013**

Note 2 – Treasurer Cash (Continued)

The Dodd-Frank Act provided that all funds held in a non-interest bearing transaction account be fully insured by the Federal Deposit Insurance Corporation (FDIC) from December 31, 2010 through December 31, 2012. Effective January 1, 2013, the unlimited insurance expired, but the FDIC insurance up to the legal maximum of \$250,000 per account remained in effect. Accordingly, effective January 1, 2013, the banks reinstated the collateralization requirements and collateralized the Treasury's deposits over the maximum limit of \$250,000.

Note 3 – Investments

California Government Code Sections 53601 and 53635 authorize the Treasury to invest the Pool and SPI funds (Note 1) in obligations of the United States Treasury, federal agencies, municipalities, asset-backed securities, mortgage-backed securities, bankers' acceptances, commercial paper rated A-1 by Standard and Poor's Corporation (S&P) or P-1 by Moody's, negotiable certificates of deposit, medium-term notes, corporate notes, repurchase agreements, reverse repurchase agreements, time deposits, shares of beneficial interest of a Joint Powers Authority that invests in authorized securities, shares of beneficial interest issued by diversified management companies known as money market mutual funds (MMF) registered with the Securities and Exchange Commission, the State of California's Local Agency Investment Fund (LAIF), and guaranteed investment contracts. As permitted by the California Government Code, the Treasury developed, and the Board adopted, an Investment Policy that further defines and restricts the limits within which the Treasury may invest. The investments are managed by the Treasury which reports investment activity to the Board on a monthly basis. The Treasury also maintains Other Specific Investments which are invested pursuant to State Code.

Investments are stated at fair value, except for certain non-negotiable securities that are reported at cost, which approximates to fair value, because they are not transferable and have terms that are not affected by changes in market interest rates, such as mortgage trust deeds, Los Angeles County securities, and investments in the LAIF. The fair value of investments is determined monthly and is provided by the custodian bank. The method used to determine the value of participant's equity withdrawn is based on the book value, which is the amortized cost, of the participant's percentage participation on the date of such withdrawals.

Investments in LAIF are governed by the California Government Code and overseen by a five member Local Investment Advisory Board as designated by the California Government Code. As of June 30, 2013, the total amount invested by all California local governments and special districts in LAIF was \$21.21 billion. LAIF is part of the State of California's Pooled Money Investment Account (PMIA), which as of June 30, 2013 had a balance of \$58.80 billion. The PMIA is not SEC registered, but is required to invest according to the California Government Code. Included in the PMIA's investment portfolio are certain derivative securities or similar products in the form of structured notes totaling \$400 million, and asset-backed securities totaling \$753.40 million at June 30, 2013. Collectively, these represent 1.96% of the PMIA balance of \$58.80 billion. The SPI holdings in the LAIF investment pool as of June 30, 2013, were \$49.48 million, which were valued using a fair value factor provided by LAIF.

LOS ANGELES COUNTY TREASURY
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2013

Note 3 – Investments (Continued)

The table below identifies the investment types that are authorized by the County, along with the related concentration of credit limits:

Authorized Investment Type	Maximum Maturity		Maximum Percentage of Portfolio		Maximum Investment In One Issuer		Minimum Rating	
	Gov. Code	Pool Policy	Gov. Code	Pool Policy	Gov. Code	Pool Policy	Gov. Code	Pool Policy
U.S. Treasury Notes, Bills and Bonds	5 years	None (1)	None	None	None	None	None	None
U.S. Agency Securities	5 years	None (1)	None	None	None	None	None	None
Local Agency Obligations	5 years	5 years (2)	None	10%	None	10%	None	None (2)
Bankers' Acceptances	180 days	180 days	40%	40%	30%	\$650 million	None	P-1
Commercial Paper	270 days	270 days	40%	40%	10%	\$1 billion	A-1/P-1	A-1/P-1
Certificate of Deposits (3)	5 years	3 years	30%	30%	None	\$650 million	None	P-1/A
Corporate Medium-Term Notes (4)	5 years	3 years	30%	30%	None	\$650 million	A	A-1/P-1/A
Repurchase Agreement	1 year	30 days	None	\$1 billion	None	\$500 million	None	None
Reverse Repurchase Agreement	92 days	92 days	20%	\$500 million	None	\$250 million	None	None
Securities Lending Agreements	92 days	92 days	20%	20% (5)	None	None	None	None
Money Market Mutual Funds	N/A	N/A	20%	15%	10%	10%	AAA	AAA
L.A.I.F.	N/A	N/A	None	\$50 million (6)	None	None	None	None
Asset-Back Securities	5 years	5 years	20%	20%	None	\$650 million	AA	AA (7)

- (1) Pursuant to the California Government Code 53601, the Board granted authority to make investments in U.S. Treasury Notes, Bills and Bonds, and U.S. Agency Securities that have maturities beyond 5 years.
- (2) Any obligation issued or caused to be issued on behalf of other County affiliates must have a minimum rating of A3 (Moody's) or A- (S&P) and the maximum maturity is limited to thirty years. All other Local Agencies are limited to 5 years.
- (3) Euro Certificate of Deposits are further restricted to a maximum maturity of one year and a maximum percentage of portfolio of 10%.
- (4) Floating Rate Notes are further restricted to a maximum maturity of five years, maximum of 10% of the portfolio, and maximum investment in one issuer of \$650 million. The maximum maturity may be seven years, provided that the Board's authorization to exceed maturities in excess of five years is in effect, of which \$100 million par value may be greater than five years to maturity.
- (5) The maximum par value is limited to a combined total of reverse repurchase agreements and securities lending agreements of 20% of the base value of the portfolio.
- (6) The maximum percentage of the portfolio is based on the investment limit established by LAIF for each account, not by Pool Policy. Bond proceeds are considered a one-time deposit, have no maximum deposit amount, and are maintained on thirty-day increments.
- (7) All Asset-Backed securities must be rated at least "AA" and the issuer's corporate debt rating must be at least "A".

LOS ANGELES COUNTY TREASURY
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2013

Note 3 – Investments (Continued)

Risk Disclosures

As of June 30, 2013, the major classes of the investments consisted of the following (in thousands):

<u>Pool</u>	<u>Fair Value</u>	<u>Principal</u>	<u>Interest Rate Range (%)</u>	<u>Maturity Range</u>	<u>Weighted Average Maturity in Years</u>
Commercial Paper	\$ 6,007,442	\$ 6,007,538	0.09% - 0.23%	07/01/13 - 09/19/13	0.05
Corporate and Deposit Notes	280,080	279,193	0.25% - 2.15%	09/16/13 - 09/28/15	1.27
Los Angeles County Securities	32,000	32,000	0.57% - 0.61%	06/30/14 - 06/30/15	1.47
Negotiable Certificates of Deposit	3,946,103	3,946,740	0.12% - 1.23%	07/01/13 - 06/25/15	0.25
U.S. Agency Securities	11,906,172	12,086,733	0.09% - 8.00%	08/01/13 - 07/17/19	3.06
U.S. Treasury Securities:					
U.S. Treasury Notes	597,611	596,674	0.25% - 2.38%	10/31/13 - 05/31/18	2.49
U.S. Treasury Bills	99,975	99,940	0.16%	11/14/2013	0.38
Total Investments	\$ 22,869,383	\$ 23,048,818			1.75

<u>SPI</u>			<u>Interest Rate Range (%)</u>	<u>Maturity Range</u>	<u>Weighted Average Maturity in Years</u>
Local Agency Investments Fund	\$ 49,476	\$ 49,476	0% - 12.50%	07/01/13 - 10/25/37	0.76
Corporate and Deposit Notes	1,559	1,535	3.75%	11/14/14	1.38
Mortgage Trust Deeds	69	69	5.50%	01/01/14 - 04/01/17	3.37
Los Angeles County Securities	4,945	4,945	5.00%	09/02/21	8.18
U.S. Agency Securities	73,470	75,576	0.50% - 3.24%	02/28/17 - 05/30/28	8.49
U.S. Treasury Securities:					
U.S. Treasury Bonds	101	85	7.25%	05/15/16	2.88
Total Investments	\$ 129,620	\$ 131,686			5.39

<u>Other Specific Investments</u>			<u>Interest Rate Range (%)</u>	<u>Maturity Range</u>	<u>Weighted Average Maturity in Years</u>
U.S. Treasury Bills	\$ 302	\$ 302	0.08%	12/05/13	0.43
Total Investments	\$ 302	\$ 302			0.43

LOS ANGELES COUNTY TREASURY
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2013

Note 3 – Investments (Continued)

Interest Rate Risk

The Treasury manages the Pool's exposure to declines in fair value by limiting its weighted average maturity to a target of 1.5 years, in accordance with the Investment Policy. For purposes of computing weighted average maturity, the maturity date of variable-rate notes is the stated maturity.

57.17% of the Pool's \$22.87 billion in investments at June 30, 2013, mature in six months or less. Of the remainder, 35.48% have a maturity of more than one year. At June 30, 2013, the weighted average maturity in years for the Pool was 1.75.

The California Government Code and the Investment Policy allow the Treasury to purchase floating rate notes, that is, any instruments that have a coupon interest rate that is adjusted periodically due to changes in a base or benchmark rate. The Investment Policy limits the amount of floating rate notes to 10% of the Pool portfolio. The Investment Policy also prohibits the purchase of inverse floating rate notes and hybrid or complex structured investments and for the year ended June 30, 2013, there were none.

At June 30, 2013, the Pool contained floating rate notes at fair value of \$757.88 million (3.31% of the Pool). The notes are tied to one-month and three-month London Interbank Offered Rate (LIBOR) with monthly and quarterly coupon resets. The fair value of variable securities is generally less susceptible to changes in value than fixed rate securities because the variable-rate coupon resets back to the market rate on a periodic basis. There were several variable rate notes at fair value of \$6.87 million in the SPI and no variable rate notes in the Other Specific Investments.

Fair value fluctuates with interest rates, and increasing interest rates could cause fair value to decline below original cost. County management believes the liquidity in the portfolios is adequate to meet cash flow requirements and to preclude the County from having to sell investments below original cost for that purpose.

Custodial Credit Risk

Custodial credit risk for investments is the risk that the Treasury will not be able to recover the value of investment securities that are in the possession of an outside party. Investments are exposed to custodial credit risk if the securities are uninsured, are not registered in the name of the Treasury and are held by either the counterparty, or the counterparty's trust department or agent but not in the Treasury's name. At year-end, all Pool, SPI and Other Specific Investment securities, except for the County Improvement Bonds and Bond Anticipation Notes (BANs), certain certificates of participation issued by County entities, LAIF and mortgage trust deeds, were either held by the Treasury or by the custodian bank in the name of the Treasury. The bonds, BANs, and certain certificates of participation were held in the Treasury's vault and are recorded in the Los Angeles County Securities line item. The mortgage trust deeds were held and administered by Bank of America. The LAIF investments were held by the State of California.

LOS ANGELES COUNTY TREASURY
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2013

Note 3 – Investments (Continued)

Credit Risk and Concentration of Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. Concentration of credit risk is the risk of loss attributed to the magnitude of an investment in a single issuer. The County mitigates these risks by holding a diversified portfolio of high quality investments.

The Investment Policy establishes acceptable credit ratings for investments from any two Nationally Recognized Statistical Rating Organizations (NRSRO). For an issuer of short-term debt, the rating must be no less than A-1 (S&P) or P-1 (Moody's), while an issuer of long term debt shall be rated no less than an "A." All investments purchased during the year ended June 30, 2013 met the credit rating criteria in the Investment Policy, at the issuer level. However, while the NRSROs did rate the issuer of the investments purchased, the NRSRO did not, in all instances, rate the investment itself (e.g., commercial paper, bankers' acceptance, corporate and deposit notes, and negotiable certificates of deposit). Accordingly, for purposes of reporting the credit quality distribution of investments in the table shown on page 20, some investments are reported as not rated.

The Investment Policy also permits investments in LAIF, pursuant to California Government Code Section 16429.1. At June 30, 2013, a portion of the SPI was invested in LAIF, which is unrated as to credit quality.

The Investment Policy, approved annually by the Board, limits the maximum total par value for each permissible security type (e.g. commercial paper and certificates of deposit) to a certain percentage of the Pool portfolio. Exceptions to this are obligations of the United States government, and United States government agencies or government-sponsored enterprises, which do not have a limit. Further, the Treasury restricts investments in any one issuer based on the issuer's ratings from a NRSRO. For bankers' acceptances, certificates of deposit, corporate notes and floating rate notes, the highest issuer limit, for those issuers with ratings of P-1/Aaa (Moody's) and A-1/AAA (S&P), was \$650 million, approximately 2.84% of the Pool's investment balance at June 30, 2013. For commercial paper, the highest issuer limit, for those issuers with ratings of P-1/Aaa (Moody's) and A-1/AAA (S&P), was \$1 billion, or 4.37% of the Pool's investment balance as of June 30, 2013.

The Pool and SPI had the following U.S. Agency securities in a single issuer that represent 5 percent or more of total investments at June 30, 2013, (in thousands):

Issuer	Pool		SPI	
	Fair Value	% of Portfolio	Fair Value	% of Portfolio
Federal Farm Credit Bank	\$ 1,945,648	8.51%	\$ 9,278	7.16%
Federal Home Loan Bank	4,528,590	19.80%	54,032	41.68%
Federal Home Loan Mortgage Corporation	2,513,571	10.99%	2,080	1.60%
Federal National Mortgage Association	2,918,363	12.76%	8,081	6.23%

LOS ANGELES COUNTY TREASURY
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2013

Note 3 – Investments (Continued)

Safekeeping Securities

At June 30, 2013, all Pool, SPI investments and Other Specific Investments were safe kept by Citibank N.A., except for the County Improvement Bonds and Bond Anticipation Notes (BANs), certain certificates of participation issued by County entities, LAIF and mortgage trust deeds.

The bonds, BANs, and certain certificates of participation were held in the Treasury's vault and are recorded in the Los Angeles County Securities line item. The mortgage trust deeds were held and administered by Bank of America.

The County has not provided nor obtained any legally binding guarantees during the year ended June 30, 2013, to support the value of shares in the Pool.

Investment Income

The earnings rate, which includes investment income, net of allowable investment expenses, on all Pool investments held by the Treasury for the year ended June 30, 2013, was 0.64% on an average daily investment balance of the Pool portfolio of \$22.73 billion.

Investment expenses allocated by the County to the Pool include administrative costs such as salaries and benefits, services and supplies, overhead and equipment totaling \$10.68 million for the year ended June 30, 2013.

The change in fair value of investments consists of both unrealized and realized gains and losses. Realized gains and losses on investments held in more than one fiscal year and sold in the current year were included as a change in the fair value of investments reported in the prior year(s) (as an unrealized gain or loss) and the current year (as a realized gain or loss). Securities in the aggregate amount of \$8.04 billion in the Pool and \$1.26 billion in the SPI were called or sold, respectively, during the year with a net gain of \$2.86 million for the Pool and a net loss of \$127 thousand for the SPI, respectively. The net decrease in the fair value of investments for the year ended June 30, 2013, was \$252.66 million for the Pool and a net decrease of \$2.31 million for the SPI. There was a \$413 net increase in the fair value of investments for the Other Specific Investments for the year ended June 30, 2013.

Mortgage Trust Deeds

In December 1986 and October 1987, the Board approved the disbursing of funds for mortgage trust deeds as part of the settlements of the Flying Triangle and the Abalone Cove landslide litigation. Such disbursements are authorized under California Government Code Section 23004, the County's power to compromise and make payment of claims being implicit in the County's power to sue and be sued. Per the Flying Triangle and Abalone Cove settlements, the combined amount of all mortgage loans is not to exceed \$8.50 million.

The trust deeds, which are fully secured, have terms of 15 to 30 years and fixed interest rate of 5.50%. As of June 30, 2013, \$69 thousand in mortgage trust deeds are included in the SPI portfolio.

**LOS ANGELES COUNTY TREASURY
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2013**

Note 4 – Interest Receivable

Interest receivables consist of interest accrued on investments including interest purchased with certain securities. At June 30, 2013, the Pool had \$31.76 million of interest receivable of which \$4.13 million represents accrued interest purchased. At June 30, 2013, the SPI portfolio had \$380 thousand of interest receivable and no accrued interest purchased.

Note 5 – Related Party

Los Angeles County Securities – External Investment Pool

The Board authorized the Treasury to purchase Los Angeles County Capital Asset Leasing Corporation's (LACCAL) BANs for the Pool, which are floating rate notes. The LACCAL BANs comprised 4.22% of the total floating rate notes as of June 30, 2013. LACCAL is a nonprofit corporation established by the Board to issue tax-exempt bonds to finance the purchase of certain equipment on behalf of the County. The BANs were created to provide LACCAL with operating cash prior to the sale of financing bonds. LACCAL issues BANs and sells them to the Treasury periodically, based on cash needs. The Board authorized the issuance of an aggregate amount of BANs not to exceed \$67.50 million for the year ended June 30, 2013. As of June 30, 2013, the Pool had \$32 million invested in LACCAL BANs.

BANs are payable within five years of the purchase date. In addition, the BANs are issued with a formal agreement that, in the event they are not liquidated by the end of the five-year period, they convert to capital leases with a three-year term secured by County real property.

Los Angeles County Securities – Specific Purpose Investments (SPI)

The Los Angeles County Securities category included the Rancho Palos Verdes Redevelopment Agency Tax Allocation Bond for \$5.17 million issued on December 2, 1997 with \$4.95 million outstanding at June 30, 2013. It earns an interest rate of 5% per annum and matures in September 2021. The original loan provided funding for landslide mitigation measures in the Abalone Cove area pursuant to a 1987 settlement agreement.

Note 6 – Interest Apportionment

Earnings realized on investments based on amortized cost are distributed to Pool participants and are calculated using the accrual basis of accounting. Section 27013 of the California Government Code authorizes the Treasury to deduct administrative fees related to investments. The net realized earnings on investments are apportioned by the Auditor-Controller to the Pool participants monthly, based on the participants' average daily cash balances. During the year ended June 30, 2013, the Pool apportioned \$144.85 million of investment earnings, compared to the previous year's apportionment of \$220.01 million.

LOS ANGELES COUNTY TREASURY
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2013

Note 7 – Investment Pool Composition

As of June 30, 2013, the Investment Pool participants by percentage of net position consist of:

<u>Participant Allocation</u>	
Consolidated School Districts	53.89%
County of Los Angeles	32.36%
County Bond Proceeds and Repayment Funds	4.13%
Consolidated Sanitation Districts	2.88%
South Coast Air Quality Management District	2.61%
Metropolitan Transportation Authority	1.49%
Other Municipal Agencies	2.64%
Total	<u>100.00%</u>

The School Districts and the Superior Courts are required by legal provisions to participate in the Pool. At June 30, 2013, the total percentage share of the Pool that relates to these participants in addition to Los Angeles County and related entities whose participation is required was 86.25%. Voluntary participants in the Treasury consist of the Sanitation Districts, the Metropolitan Transportation Authority, the South Coast Air Quality Management District and certain municipal agencies. The total percentage share of the Pool for voluntary participants was 13.75% at June 30, 2013.

**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***

INDEPENDENT AUDITOR'S REPORT

Board of Supervisors
County of Los Angeles, 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 financial statements of the Los Angeles County Treasury (Treasury), as of and for the year ended June 30, 2013, and the related notes to the financial statements, which collectively comprise the Treasury's basic financial statements, and have issued our report thereon dated November 15, 2013.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Treasury'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 opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Treasury's internal control. Accordingly, we do not express an opinion on the effectiveness of the Treasury'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 Treasury'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 Treasury's financial statements are 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 statement 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 Treasury'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 Treasury's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Los Angeles, California
November 15, 2013

Basilio Cobb Associates, P.C.