



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

KENNETH HAHN HALL OF ADMINISTRATION
500 WEST TEMPLE STREET, ROOM 525
LOS ANGELES, CALIFORNIA 90012-2766
PHONE: (213) 974-8301 FAX: (213) 626-5427

J. TYLER McCAULEY
AUDITOR-CONTROLLER

September 11, 2003

TO: Supervisor Yvonne Brathwaite Burke, Chair
Supervisor Gloria Molina
Supervisor Zev Yaroslavsky
Supervisor Don Knabe
Supervisor Michael D. Antonovich

FROM: J. Tyler McCauley *tm*
Auditor-Controller

SUBJECT: **REPORTS ON THE AUDIT OF THE COUNTY TREASURY**

Attached are two reports on our audit of the County Treasury. The reports are dated June 18, 2003, the last day of audit fieldwork as required by auditing standards.

Please call me if you have any questions, or your staff may call DeWitt Roberts at 626/293-1101.



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J. TYLER McCAULEY
AUDITOR-CONTROLLER

June 18, 2003

TO: Supervisor Yvonne Brathwaite Burke, Chair
Supervisor Gloria Molina
Supervisor Zev Yaroslavsky
Supervisor Don Knabe
Supervisor Michael D. Antonovich

FROM: J. Tyler McCauley *JTM*
Auditor-Controller

SUBJECT: **AUDIT OF THE COUNTY TREASURY AS OF DECEMBER 31, 2002**

Pursuant to Government Code Section 26920 through 26923, we examined the Treasurer and Tax Collector's (TTC) records relative to the amount and type of assets in the Treasury. Attached is our report on the Treasurer's Cash and Investments as of December 31, 2002.

The purpose of our review was to express an opinion as to the accuracy of the TTC's records relative to the amount and type of assets in the Treasury. We also reconciled the TTC's records with those of the Auditor-Controller to obtain reasonable assurance as to whether the TTC's records were free from material misstatement. We did not review the Treasurer's investment strategy, although we did review the TTC's compliance with the Government Code and the Board of Supervisors' Investment Policy.

It should be noted that this report is dated June 18, 2003 because auditing standards require us to date it as of the last day of fieldwork. It is actually being distributed on September 11, 2003.

JTM:PTM:DR:JS

Attachments

c: David E. Janssen, Chief Administrative Officer
Mark Saladino, Treasurer and Tax Collector
Public Information Officer
Violet Varona-Lukens, Executive Officer
Audit Committee Members

LOS ANGELES COUNTY TREASURY
FINANCIAL STATEMENTS
AS OF DECEMBER 31, 2002

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J. TYLER McCAULEY
AUDITOR-CONTROLLER

June 18, 2003

The Honorable Board of Supervisors
County of Los Angeles
383 Kenneth Hahn Hall of Administration
500 West Temple Street
Los Angeles, California 90012

**Auditor's Report on the County
Treasury as of December 31, 2002**

We have audited the Statement of Net Assets and Statement of Changes in Net Assets for the Los Angeles County's Treasury Pool as of December 31, 2002 and for the six months then ended. These financial statements are the responsibility of the Treasurer's management. Our responsibility is to express an opinion on these statements based on our audit.

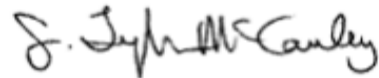
We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance that the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amount and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the cash and investments arising from transactions of the Treasurer as of December 31, 2002, and the results of its operations for the six months then ended in conformity with accounting principles generally accepted in the United States of America.

The accompanying statements do not include funds or investments of the Los Angeles County Employees Retirement Association, with the exception of amounts on deposit with the Treasurer as part of the External Investment Pool, which are intended mainly for warrant clearance. Retirement Association funds and investments are reported annually as of June 30th by a private accounting firm. These statements also do not

include investments made with the proceeds of debt issuance for the purpose of financing various County capital acquisitions. These investments are not part of Treasury Pool assets. These will also be audited by a private accounting firm.

It should be noted that this report is dated June 18, 2003 because auditing standards require us to date it as of the last day of fieldwork. It is actually being distributed on September 11, 2003.



J. Tyler McCauley, CPA
Auditor-Controller

JTM:PTM:DR:JS

Attachments

c: David E. Janssen, Chief Administrative Officer
Mark Saladino, Treasurer and Tax Collector
Public Information Officer
Violet Varona-Lukens, Executive Officer
Audit Committee Members

LOS ANGELES COUNTY TREASURY
STATEMENT OF NET ASSETS
AS OF DECEMBER 31, 2002

<u>INVESTMENTS AND ASSETS</u>	AMORTIZED COST	ACCRUED INTEREST PURCHASED	PRINCIPAL COST	FAIR VALUE
<u>INVESTMENTS IN THE EXTERNAL POOL</u>				
COMMERCIAL PAPER	\$ 3,810,597,858		3,810,597,858	3,810,533,567
CORPORATE AND DEPOSIT NOTES	355,042,759		355,042,759	355,382,550
MUNICIPALS	28,807,248		28,807,248	28,807,248
NEGOTIABLE CDS	963,996,954	9,132	964,006,086	965,241,112
U.S. AGENCIES	6,327,361,590	26,368	6,327,387,958	6,368,129,958
U.S. GOVERNMENT	955,329,970	607,390	955,937,360	959,557,390
TOTAL INVESTMENT IN THE EXTERNAL POOL	\$ 12,441,136,379	642,890	12,441,779,269	12,487,651,825
TREASURER CASH	\$ 29,996,183		29,996,183	29,996,183
TOTAL NET ASSETS HELD IN THE EXTERNAL POOL	\$ 12,471,132,562	642,890	12,471,775,452	12,517,648,008
<u>INVESTMENTS IN THE SPECIFIC INVESTMENT TRUST FUND</u>				
COLLATERALIZED TIME DEPOSITS	\$ 52,681,410		52,681,410	52,893,694
GUARANTEED INVESTMENTS CONTRACTS	83,086,407		83,086,407	83,086,407
MUNICIPALS	5,555,173		5,555,173	5,558,660
TRUST DEEDS	2,012,483		2,012,483	2,012,483
U.S. AGENCIES	10,586,166	3,743	10,589,909	10,798,572
U.S. GOVERNMENT	5,670,951	554	5,671,505	5,997,542
REPOs	505,545,000		505,545,000	505,545,000
TOTAL NET ASSETS IN THE SPECIFIC INVESTMENT TRUST FUND	\$ 665,137,590	4,297	665,141,887	665,892,358
TOTAL NET ASSETS IN THE TREASURY	\$ 13,136,270,152	647,187	13,136,917,339	13,183,540,366

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THIS STATEMENT

LOS ANGELES COUNTY TREASURY
STATEMENT OF CHANGES IN NET ASSETS
FISCAL YEAR ENDED DECEMBER 31, 2002

	COUNTY INVESTMENT POOL	SPECIFIC PURPOSE INVESTMENTS
INVESTMENT INCOME (LOSS):		
NET EARNINGS	\$ 143,913,216	\$ 15,119,596
NET INCREASE (DECREASE) IN FAIR VALUE OF INVESTMENTS	14,897,614	(82,762)
NET INCREASE RESULTING FROM INVESTMENT INCOME	\$ 158,810,830	\$ 15,036,834
ACTIVITY BY POOL PARTICIPANTS		
CONTRIBUTIONS BY POOL PARTICIPANTS	20,114,120,518	940,906,052
DISTRIBUTIONS TO POOL PARTICIPANTS	(20,300,734,327)	(891,103,597)
NET INCREASE (DECREASE) IN INVESTMENT TRANSACTIONS	\$ (186,613,809)	\$ 49,802,455
TOTAL INCREASE (DECREASE) IN NET ASSETS	\$ (27,802,979)	\$ 64,839,289
FAIR VALUE OF NET ASSETS HELD IN TRUST, JULY 1, 2002	12,545,450,987	601,053,069
FAIR VALUE OF NET ASSETS HELD IN TRUST, DECEMBER 31, 2002	\$ 12,517,648,008	\$ 665,892,358

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THIS STATEMENT

NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2002

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Treasurer and Tax Collector (TTC) records investment purchases, maturities and sales on the settlement date. Generally Accepted Accounting Principles (GAAP) requires that transactions be recorded on the trade date. The difference between the Treasurer's approach and GAAP required trade date accounting is immaterial. The County's investments are reported by the Treasurer at amortized cost.

In accordance with Government Accounting Standards Board (GASB) Statement 31, "Accounting and Financial Reporting for External Investment Pools," the accompanying financial statements reflect the fair value of investments. Special disclosures related to GASB 31 appear in Note 3.

Treasurer's Investment Strategy

The Los Angeles County Treasurer maintains two portfolios. The Pooled Surplus Investment portfolio is used to account for net assets of the County's Investment Pool. The Treasurer's investment strategy for the Investment Pool is to maintain principal and to provide sufficient cash to meet disbursements. The cash flow needs of the pool members are monitored daily to ensure that sufficient liquidity is maintained to meet the needs of participants. The Treasurer's basic investment philosophy is to buy and hold, to a designated maturity, high quality fixed income investments.

The Specific Purpose Investment (SPI) portfolio is used to account for the net assets of individual investment accounts, in aggregate. The related investment activity occurs separately from the County's investment pool and is provided as a service to external investors. The individual investment strategies are targeted for the needs of the requesting entity.

2. BANK DEPOSITS

As of December 31, 2002, the Treasurer maintained accounts in five banks. The carrying amount of the Treasurer's total deposits was \$29,865,714, plus \$130,469 in cash in the Treasurer's vault. Of the amount on deposit in the banks, \$3,711,316 was covered by federal depository insurance or collateralized with securities monitored by the State Local Agency Security fund. The remaining balance of \$26,154,398 was uninsured and uncollateralized.

Under 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. Depending upon the type of security in the pool, the pool must have a minimum market value of 110 to 150 percent of the total amount of the public deposits.

NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2002

The Local Agency Security Program of the State of California Office of the Treasurer confirmed that the pools of collateral related to the Treasurer's deposits were maintained at required levels as of December 31, 2002.

3. INVESTMENTS

Government Code Sections 53601 and 53635 authorize the Treasurer to invest the Investment Pool and SPI funds (Notes 4 and 5, respectively) in obligations of the United States Treasury, federal agencies, municipalities, asset-backed securities, bankers' acceptances, commercial paper rated A-1 by Standard and Poor's Corporation or P-1 by Moody's Commercial Paper Record, negotiable certificates of deposit, medium-term notes, repurchase agreements and reverse repurchase agreements. Also, Government Code Section 53601(l) provides for additional investments under certain circumstances. These investments can include promissory notes, subordinated notes, guaranteed interest agreements, and floating rate notes.

The investments are managed by the County Treasurer who reports to the Board of Supervisors on a monthly basis. In addition, Government Code Section 27131 and 27132 requires that the County establish a County Treasury Oversight Committee to review and monitor the County's investment policy. The committee membership includes the Treasurer and Tax Collector, Auditor-Controller, Chief Administrative Officer, Superintendent of Schools and a non-county representative.

Investments held by the County Treasurer are stated at fair value, except for certain investment contracts that are reported at cost because they are not transferable and have terms that are not affected by changes in market interest rates. The fair value of each participant's position in the pool is the same as the value of the pool shares. The method used to determine the value of participant's equity withdrawn is based on the book value of the participant's percentage participation on the date of such withdrawals.

The County's investment pool consists of voluntary and involuntary participants. The School Districts and the Courts are required by legal provisions to participate in the County's investment pool. The total percentage share of the Treasurer's pool that relates to these involuntary external pool participants is 43.5%. The Los Angeles County and related entities' share is 47.4%. Voluntary external pool participants in the County's investment pool including Sanitation Districts, the Metropolitan Transportation Authority, the South Coast Air Quality Management District and certain municipal agencies make up the remaining 9.1% of the pool. The deposits held for these entities are included in the County's Investment Pool and SPI funds. Certain specific investments have been made by the County, as requested by external

NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2002

depositors. This investment activity occurs separately from the County's Investment Pool and is reported in the SPI fund.

Safekeeping of Securities

At December 31, 2002, all County Investment Pool and SPI Investments were safekept by the Bank of New York, except for the bonds and Bond Anticipation Notes (BANs), certain certificates of participation issued by Los Angeles County entities, the State Investment Pool investment and the trust deed mortgages.

The bonds, BANs and certain certificates of participation were held in the Treasurer's vault and the trust deed mortgages were held and administered by various branches of Bank of America or by the Treasurer.

In accordance with GASB Statement Number 3, the County's Investments are categorized to give an indication of the level of credit risk assumed as of December 31, 2002. Category 1 includes investments that are insured or registered or for which the securities are held by the County or its agent in the agent's nominee name, with subsidiary records listing the County, as the legal owner. Category 2 includes uninsured and unregistered investments for which the securities are held by the counterparty's trust department or agent in the County's name. Category 3 includes uninsured and unregistered investments for which the securities are held by the counterparty or by the counterparty's trust department or agent but not in the County's name.

Guaranteed Investment Contracts, Money Market Fund, the State Investment Pool and Trust Deed investments are not evidenced by securities that exist physically and, per GASB Number 3, are not classified into credit risk categories. The County's Investments are categorized on the following schedule:

NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2002

COUNTY INVESTMENT POOL	CATEGORY			FAIR VALUE	INTEREST RATE RANGE	MATURITY RANGE
	1	2	3			
COMMERCIAL PAPER	\$ 3,810,533,567	\$ -	\$ -	\$ 3,810,533,567	1.20% - 1.41%	01/01/03 - 03/03/03
CORPORATE AND DEPOSIT NOTES	355,382,550	-	-	355,382,550	1.42% - 7.13%	01/15/03 - 03/15/05
MUNICIPALS	28,807,248	-	-	28,807,248	1.76% - 4.96%	06/30/05 - 08/01/07
NEGOTIABLE CDS	965,241,112	-	-	965,241,112	1.31% - 2.70%	01/03/03 - 05/30/03
U.S. AGENCIES	6,368,129,958	-	-	6,368,129,958	1.23% - 9.25%	01/13/03 - 12/01/08
U.S. GOVERNMENT	959,557,390	-	-	959,557,390	2.13% - 4.75%	01/31/03 - 08/31/04
TOTAL	<u>\$ 12,487,651,825</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 12,487,651,825</u>		

SPI	CATEGORY			FAIR VALUE	INTEREST RATE RANGE	MATURITY RANGE
	1	2	3			
MUNICIPALS	\$ 5,558,660	\$ -	\$ -	\$ 5,558,660	5.00% - 7.00%	01/02/05 - 09/02/21
U.S. AGENCIES	10,798,572	-	-	10,798,572	3.88% - 7.13%	04/30/03 - 11/13/07
U.S. GOVERNMENT	5,997,542	-	-	5,997,542	1.58% - 11.25%	01/02/03 - 05/15/16
REPO	505,545,000	-	-	505,545,000	4.53%	6/30/04
TOTAL	<u>\$ 527,899,774</u>	<u>\$ 0</u>	<u>\$ 0</u>			

GUARANTEED INVESTMENT CONTRACTS				83,086,407	2.83%	6/26/03
COLLATERALIZED TIME DEPOSITS				52,893,694	---	12/31/03
TRUST DEEDS				2,012,483	4.50% - 6.83%	9/01/04 - 04/01/17
TOTAL				<u>\$ 665,892,358</u>		

NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2002

The County has not provided nor obtained any legally binding guarantees during the six months ended December 31, 2002 to support the value of shares in the Treasurer's External Investment Pool.

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 portfolio is adequate to meet cash flow requirements and to preclude the County from having to sell investments below original cost for that purpose.

The earned rate, which includes net gains on investment sold, on all investments held by the County Treasurer for the six months ended December 31, 2002 was 2.45%.

The unrealized gain on investments held in the Treasurer's Investment Pool was \$45,872,556 and the unrealized gain on investments held on SPI was \$750,471, as of December 31, 2002. These amounts take into account all changes in fair value (including purchases, sales, and redemptions) that occurred during the six months.

Derivatives

The California Government Code and the County's investment guidelines allow the County Treasurer 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 County's investment guidelines limit the amount of floating rate notes to 10% of the Los Angeles County Treasury Pool portfolio and prohibit the purchase of inverse floating rate notes and hybrid or complex structured investments. As of December 31, 2002, the County's Investment Pool contained floating rate notes at par of \$846,029,248 (6.8% of the Investment Pool).

Included in the floating rate notes are Marina del Rey Certificates of Participation (COPs), which were issued by the County to finance fiscal year 1992-93 General Fund operations, issuance cost, and required reserves. The certificates are payable only from Marina del Rey operating lease revenues and other Marina del Rey associated revenues. These COPs have a variable interest rate, payable semi-annually, with a maturity date of August 1, 2007.

The Board of Supervisors authorized the Treasurer to purchase Los Angeles County Capital Asset Leasing Corporation's (LACCAL) BANS for the County's Investment Pool, which are floating rate notes. 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

NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2002

bonds. LACCAL issues BANS and sells them to the Treasurer periodically, based on cash needs. As part of the 2002-2003 Debt Management Guidelines, the Board authorized the issuance of an aggregate amount of BANS not to exceed \$60 million. As of December 31, 2002, the County's Investment Pool had \$10,000,000 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.

4. COUNTY INVESTMENT POOL

The TTC maintains the County's Investment Pool, which includes all funds in the County pool deposited by County entities and external legal entities. The purpose of the pool is to provide safe, liquid investment opportunities for pooled surplus funds deposited into the County Treasury. Interest earned on pool investments is deposited monthly based upon the average daily deposit balance during the allocation period. Investment gains and losses are proportionately shared by the entities participating in the pool as an increase or reduction in investment net of administrative costs.

Investments purchased with the intent to be held to maturity are accounted for in the non-trading portion of the County Investment Pool. Investments purchased with the intent to be sold prior to maturity are accounted for in the trading portion of the County's Investment Pool. During the period July 1, 2002 through December 31, 2002, the Treasurer did not purchase any investments for trading purposes.

5. SPECIFIC PURPOSE INVESTMENTS

The Treasurer maintains the SPI Portfolio to manage specific investments requested by specific entities with the approval of the Treasurer. Revenue/loss distribution is credited to the specific entity for which the investment was made.

6. MUNICIPAL SECURITIES IN SPI

As of December 31, 2002, the Municipal Securities category of the SPI fund includes the following investments:

A Rancho Palos Verdes Redevelopment Agency Tax Allocation Bond for \$5,455,000 issued on December 2, 1997. 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.

NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2002

A Calle Del Barco Community Improvement Bond for \$100,173 issued in 1979. It earns an interest rate of 7% per annum and matures on January 2, 2005.

7. TRUST DEED MORTGAGES

In December 1986 and October 1987, the Board of Supervisors approved the disbursing of funds for trust deed mortgages as part of the settlements of the Flying Triangle and the Abalone Cove landslide litigation. Such disbursements are authorized under 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 \$8,500,000.

The trust deeds, which are fully secured, have terms of 15 to 30 years and fixed interest rates of between 5.5% and 6.825%, except for one loan that had a variable rate of 4.5% on December 31, 2002. They are included with the General Fund investments of SPI. As of December 31, 2002, the General Fund investments of the SPI fund contained \$2,012,483 in Trust Deed Mortgages.

8. INVESTMENT PURCHASE COMMITMENTS

At December 31, 2002, the County had open trade commitments with one broker to purchase investments approximating \$42,155,000 in the County's Investment Pool account with settlement dates subsequent to December 31, 2002. These investment transactions had not been recorded as of December 31, 2002 since the County had not taken delivery of the securities nor earned interest on the investments until the settlement date. By January 7, 2003, the County had purchased the investments.



J. TYLER McCAULEY
AUDITOR-CONTROLLER

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

KENNETH HAHN HALL OF ADMINISTRATION
500 WEST TEMPLE STREET, ROOM 525
LOS ANGELES, CALIFORNIA 90012-2766
PHONE: (213) 974-8301 FAX: (213) 626-5427

June 18, 2003

TO: Supervisor Yvonne Brathwaite Burke, Chair
Supervisor Gloria Molina
Supervisor Zev Yaroslavsky
Supervisor Don Knabe
Supervisor Michael D. Antonovich

FROM: J. Tyler McCauley *tm*
Auditor-Controller

SUBJECT: **REPORT ON COMPLIANCE AND ON INTERNAL CONTROLS OVER
FINANCIAL REPORTING**

We have audited the financial statements of the Los Angeles County Treasury Pool as of and for the six months ended December 31, 2002, and have issued our report thereon dated June 18, 2003. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and California Government Code Section 26920 through 26923.

Compliance

As part of obtaining reasonable assurance about whether the Treasurer and Tax Collector's (TTC's) financial statements are free of material misstatement, we performed tests of its compliance with certain provision of laws and regulations, 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 object of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no material instances of noncompliance that are required to be reported under Government Auditing Standards.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the TTC's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over

financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

This report is intended solely for the information and use of the Board of Supervisors and the TTC management and is not intended to be and should not be used by anyone other than these specified parties.

It should be noted that this report is dated June 18, 2003 because auditing standards require us to date it as of the last day of fieldwork. It is actually being distributed on September 11, 2003.

JTM:PTM:DR:JS

c: David E. Janssen, Chief Administrative Officer
Mark Saladino, Treasurer and Tax Collector
Violet Varona-Lukens, Executive Officer
Public Information Officer
Audit Committee