

**Attachment 1**

**Statement for the Record  
for the Senate Foreign Relations Committee Hearings  
on the Nomination for Director of the Peace Corps**

**News Stories about Mr. Gaddi Vasquez  
concerning the Financial Situation  
in Orange County and how it was  
a subject of Discussion and Controversy  
6 Months before the Bankruptcy**

**November 25, 2001**

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## **Introduction**

During the hearings held on November 14, 2001 on the nominee for Director of the United States Peace Corps, Congressman Cox defended Gaddi Vasquez by saying that nobody had seen the Orange County bankruptcy coming as if the bankruptcy that occurred in early December, 1994 were a bolt from the blue that caught everyone unaware.

We would like to rebut this assertion with a selection of articles taken from Orange County's leading newspaper, the "Orange County Register", starting over 6 months before the bankruptcy occurred and continuing right up to the bankruptcy itself which demonstrates that not only was it a matter of common knowledge that the County Treasurer Robert Citron was engaged in risky derivatives investments, but that the matter had been hotly debated in the election for Treasurer that occurred in June, 1995.

The final article from the "Orange County Register" rebuts the argument that was made by members of the Orange County Supervisors that they did not have legal authority to oversee Treasurer Citron's investment pool by showing that California Government Code Section 25303 required them to supervise the official conduct of independently elected officials such as Citron and their responsibility with regard to "the assessing, collecting, safekeeping, management and disbursement of public funds."

## **Article 1: Tustin withdraws from O.C. investment pool**

POLITICS: The city removes \$4 million from the fund, but Mayor Jim Potts criticizes the action.

***April 15, 1994***

Byline: RICKY YOUNG

The Orange County Register  
Credit:

Tustin has pulled \$4 million out of Orange County's investment pool, in a move Mayor Jim Potts says is pure politics.

Tustin Councilman Jeff Thomas \_ who is working on a campaign to unseat county Treasurer Bob Citron \_ initiated the withdrawal and called Citron's investments too risky.  
He took the action without telling the rest of the City Council.

"I went storming into the city manager's office," Potts said after he found out. "Jeff is manipulating the citizens' money for political gain. He's trying to besmirch Citron's record."

Thomas, a Republican, says he initiated the change because he wanted the city's money in lower-risk investments than those selected by Citron, a Democrat.

City Treasurer Ron Nault said he is uncomfortable with the fund and made the change after Thomas echoed his concern.

Citron invests \$6.5 billion of funds from 187 public agencies in reverse reimbursement agreements. That is, his office uses low-risk U.S. Treasury notes and bills as collateral to make higher-risk investments in corporate notes and bank certificates of deposit.

The Citron fund currently is earning interest at an annualized rate of 7.8 percent. Tustin moved its money to a more conservative state fund paying 4.19 percent interest.

At those rates, the city's money would make \$312,000 annually at the county fund, compared with \$167,000 in the state fund.

San Juan Capistrano and Garden Grove are the only other Orange County cities

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that do not invest in the county fund.

John Moorlach, an accountant running against Citron in the June 7 election, is using the higher-risk investments as his primary campaign issue.

Thomas is on Moorlach's financial committee, and the two acknowledge that they discussed the issue before Thomas went to the city treasurer.

## Article 2: Earnings champ takes heat in treasurer race

GOVERNMENT: Orange County  
Treasurer Bob Citron says he's being  
targeted for helping a Democrat.

**April 19, 1994**

Byline: CHRIS KNAP

The Orange County Register  
Credit:

For more than a decade, Robert L. Citron has been hailed for returning more earnings on Orange County's government deposits than any other local government treasurer in California \_ often twice as much.

But Citron now is defending himself against a challenger in the June 7 election. John M. Moorlach suggests that Citron earned these returns by overextending himself in complicated investments that risk huge losses. Moorlach supporters have phoned financial rating agencies, business publications and newspapers, questioning Citron's strategies.

After 24 years in office, the soft-spoken county treasurer finds himself struggling to maintain his composure as nervous investors phone in to make sure their Orange County bonds remain solid.

"When anybody's attacking your integrity, particularly with the reputation I have built up in this county, it's gut-wrenching. That gets to you," Citron said in an interview last week.

The county treasurer and tax collector, a non-partisan elected official, banks local property taxes and invests deposits for the county, its school boards and any other agencies that wish to join the pool. Citron has been so successful in the past 12 years \_ he's returning 7.8 percent compared with the state fund's 4.2 percent \_ that he now manages \$8 billion for 187 different agencies.

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"He is honest, hard-working and smart," former county budget chief Ron Rubino said when The Orange County Register profiled the treasurer in 1992. "I'd like to clone him and use him to head some of our other departments."

Last fall, the county supervisors praised him publicly for earning extra income that allowed the county to fund an anti-gang program in five cities plagued with gang violence. The supervisors, all Republicans, have endorsed his re-election, though he is a Democrat.

But Citron said he has anticipated trouble for four years, ever since he received a call from county Republican Party Chairman Thomas Fuentes.

Fuentes, Citron said, criticized him for lending his stationery for a partisan attack by Democrat Tom Umberg against Assemblyman Curt Pringle, who subsequently lost.

"Fuentes called me and said, 'My friends are talking

recall,'" Citron recalled. "I said, 'Don't threaten me, Tom.' From that time on, I knew he was out to get me."

Fuentes said it's no secret that he would like to see Citron retired from office.

"Citron is a liberal, partisan Democrat who has used his office for partisan purposes," and made campaign contributions to U.S. Sen. Diane Feinstein, D-Calif., and Assembly Speaker Willie Brown, D-San Francisco, Fuentes said.

Moorlach, who sits on the county Republican Party Central Committee, confirmed that he was approached by Assemblyman Mickey Conroy, R-Orange, an ally of Pringle and Fuentes, and urged to run against Citron.

Moorlach said his allies on the central committee should not obscure his criticism of Citron's investment strategies.

"This thing is not an issue of politics, it's an issue of policy. He's trying to paint me as some hand-picked drone who's got the Republican Party behind him. That's a transfer technique and it's just not going to cut the mustard."

At the heart of Moorlach's criticism is Citron's habit of expanding interest earnings by pledging government bonds to a dealer in return for cash, then using the cash to purchase short-term, higher-interest securities. In essence, the same investment is earning two returns \_ sometimes three.

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Many other cities, counties and states also engage in these complicated "reverse repurchases," experts agree, and done properly they inflate both the value of the portfolio and its earnings. Assistant Treasurer Matt Raabe said Citron has leveraged the \$8 million in pool deposits into a \$12 million portfolio.

"To someone who can't do this themselves, it sounds like a risky proposition," Raabe said. "But for people in the business, it's a slam dunk."

Citron and Raabe acknowledge that an investment manager can run into trouble with reverse repurchase agreements. If the market value of the bonds used as collateral falls, a dealer will want cash to bring the value of the collateral up to market value. If no cash is available, the investment manager may have to sell bonds at reduced value, creating a loss for the fund.

Citron and Raabe say they've been careful to keep enough investments liquid \_ in certificates of deposit and other quickly cashed instruments \_ to meet these "collateral calls" without problem.

Officials with the country's two largest bond-rating firms, Standard and Poor's and Moody's Investor Service, agreed Monday that Citron has enough liquidity in his portfolio to cover any short-term drop in market value.

Diane Brosen, director of short-term debt rating for

Standard and Poor's, said officials from her company met with Citron and Raabe on March 30 and talked at length about the county's portfolio. "We did not have any cause for concern with regard to the county's investment strategy," Brosen said.

David Brodsky, a vice president with Moody's, said his company examined Citron's fund in November. Brodsky also examined Orange County's current portfolio \_ a document released Monday by Citron \_ and called it "fairly standard."

But telephone calls from Moorlach supporter Chriss Street, a Corona del Mar stockbroker, have helped to generate stories in The Wall Street Journal and Derivatives Week, among other publications. Moorlach also confirms calling Brosen at Standard and Poor's.

"These are very precious funds that end up paying the salaries of the janitors, teachers and principals at my daughter's school district," Street said in explaining his motivation.

But others don't see a reason to be concerned.



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Los Angeles County's chief investment officer, a Tustin resident named George Jeffries, called Citron's office well-managed and the question of risk "a judgment call in a ball game."

"I can't agree with people crying wolf."

The Orange County Register

### **Article 3: O.C. treasurer's race stirs markets**

FINANCE: A political challenger has raised doubts about Robert Citron's aggressive investment strategies, making some investors nervous.

***April 24, 1994***

Byline: CHRIS KNAP

The Orange County Register  
Credit:

Irvine investment chief Jeff Niven was trying to structure a deal last week, but rumors about Orange County's investment pool kept getting in the way.

Investors who hold Irvine's notes, or are considering buying them, kept calling up, asking whether aggressive earning strategies by county Treasurer Robert L. Citron could backfire, creating a loss for the city.

Niven, who's been investing for Irvine for 18 years, would have gotten annoyed if he hadn't found it ironic. New York investment raters had given Irvine's notes their highest grade, but only on condition that he deposit the proceeds with Citron for safekeeping.

"Financial markets breed on uncertainty. They love drama," Niven said. "Right now all of Orange County's debt has a little story that goes along with it."

Costa Mesa accountant John M. Moorlach's political challenge to 23-year incumbent Citron has had a side effect that would never occur in a race for sheriff or mayor: As Moorlach and his supporters question the safety of Citron's investment strategies, doubts reverberate through the financial press and bounce back over the phone lines from New York.

The two major firms that rate investment risk, Moody's and Standard & Poor's, have expressed confidence in Citron's pool and in the soundness of bonds and notes backed by Orange County and local cities.

But Niven and others said some investors may not be mollified and will invest instead with some city that doesn't have to convince them it will still have money

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next year to pay back the bonds.

"If they can buy either one, and they're rated the same, they're going to go with the investment that doesn't have a story to it," Niven said.

County Administrative Officer Ernie Schneider exploded in anger last week when asked about the effect that the challenge to Citron's strategies could have on Orange County's financial reputation.

"In the realm of things that can be done in a political campaign, this is one of the worst," Schneider said. "These guys are putting the taxpayers of this county in jeopardy of having to pay millions more for bonds (should Orange County's financial ratings drop)."

Moorlach says he's just campaigning, not trying to create a run on the investment pool.

"We have no hard evidence that Citron's investments are insolvent, and we have no interest in running a campaign based on personal attack or innuendo. Full disclosure by Citron will cause no harm if in fact the investments are as solvent as he has represented them to be," Moorlach said.

The treasurer holds and invests deposits for 187 governmental agencies and funds, including county schools, which by law must use the county pool, and many local cities, which do not have to, Citron said.

Over the past five years he has returned interest at 8.84 percent, often twice that of the state investment pool, attracting business from cities outside the county, including Santa Barbara, Montebello and Atascadero, records provided by his office show.

To return that rate, Citron said he has used sophisticated leverage such as reverse repurchase agreements, in which cash is borrowed against securities and used to purchase more investments. The arbitrage, or difference between the return on the investment and the cost of the cash, becomes additional earnings for the pool.

Experts agree that the risk of this strategy is that interest rates will rise unexpectedly, driving down the value of the securities and driving up the price of cash. At some point, arbitrage is no longer profitable. Unless the investor has sufficient cash to buy the leveraged, or second-tier, securities, he may be forced to sell them in a depressed market, losing millions for the fund.

Citron and Assistant Treasurer Matthew R. Raabe said they have built numerous safeguards into their system, including investments in adjustable-rate securities that hold their market value when rates rise; a large reserve of cash and

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securities that can be used as collateral; and a regular influx of cash each year when municipalities bank property taxes.

But critics such as Chriss W. Street, a Corona del Mar stockbroker and contributor to Moorlach, don't believe Citron is covered.

"In my opinion, if interest rates go against him sufficiently, he'll create incredible damage," Street said. "He'll be paying more to borrow than he earns (with the cash)."

Street's doubts, which he acknowledges communicating to Standard & Poor's and Moody's, and to a reporter at The Wall Street Journal, have helped create widespread speculation that Citron may be in over his head if interest rates continue their recent rise.

Three outside experts contacted by The Orange County Register called Citron's strategy unusually aggressive for a municipal fund, but they declined to criticize him directly or second-guess his portfolio and holdings.

"As an outsider, I have misgivings that school districts and others are permitting their money to be leveraged in this fashion. You're not supposed to be playing games with other people's money," said Zane Mann, author of the monthly California Municipal Bond Adviser.

"But that is a personal opinion. The school districts could argue it is their duty to maximize interest. That is simply a point of view.

"So far this guy has been successful. He knows how to run a leveraged fund. If you know what you're doing, and your timing's right, then you're a genius. On the other hand, even if he's right, he could still get caught if rates go up sufficiently."

Peer Swann, president of the Irvine Ranch Water District, said finance officers at his agency looked closely at the Orange County fund before investing \$400 million, even simulating an increase in interest rates to see if their money would be safe.

"He has an aggressive position, but I don't think it's outside the realm of prudence. For him to have negative interest income, short-term rates would have to go up significantly and stay that way for a considerable period of time," Swann said.

"I don't feel at risk, period, from his investment strategies. I do feel at risk of having people lose confidence in the pool. The concern I have is in the perception. I think it's already harder to market commercial debt from Orange County."

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Swann said Lehman Bros. went to the market Friday to borrow \$30 million for the Sanitation Districts of Orange County. Buyers reacted sluggishly to the offering of commercial paper, a short-term debt instrument, and the agency had to pay 0.05 percent more in interest than it expected, about \$150,000 over the life of the deal.

"All investment in the financial world is done on trust," Swann said. "This is not like a city council race, where you can attack the other person. To create doubt in the stability of the investment pool is irresponsible."

But Moorlach said he knows no other way to campaign, other than to question publicly a strategy he considers too risky for public funds.

"What am I supposed to run on? What am I supposed to be asking?" Moorlach asked. "I don't think I'm being irresponsible. I think a lot of the public wants to know what's going on, and if

everything's fine with the portfolio, there shouldn't be any problems."

(CHART)

PROFILE

Robert L. Citron

Orange County treasurer-tax collector

Born:

California, April 14, 1925

Career: Hired as Orange County's deputy tax collector in 1960. Elected tax collector in 1970. Job combined with that of treasurer in 1973.

Home: Santa Ana, since 1960

Personal:

Married to Terry for 39 years.

Quote: "I've tried to run my office like it was my own personal business, for profit, for the taxpayers of Orange County." PROFILE

John M. Moorlach certified public accountant, certified financial planner

Born: Holland, Dec. 21, 1955

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Career: Partner, firm of Balser, Horowitz, Frank & Wakeling Home: Costa Mesa

Personal: Married 13 years, 3 children

Quote: "We've got a guy who's running for his seventh term as treasurer and has never been challenged. It's time to at least educate the voters."

## **Article 4: Citron defends his financial acumen**

Q&A: Despite rising interest rates, O.C.'s treasurer says agencies' money is safe.

***April 24, 1994***

Byline: The Orange County Register  
Credit:

The phone lines of local financiers have been buzzing the past two weeks with speculation over the investment strategies of Orange County Treasurer-Tax Collector Robert L. Citron.

In 23 years as the head of the county's investment pool, Citron consistently has returned interest at twice the rate of the more conservative state investment pool, earning millions for local school districts, cities and county government. But interest rates have risen 1 percent in the past six weeks, deflating the value of many of the notes that Citron holds. Several private investment funds that engage in leveraged investment strategies have had major \_ and very public \_ losses. John M. Moorlach, a candidate for the treasurer's job, says Citron is risking a similar loss.

Register staff writer Chris Knap interviewed municipal-bond experts, municipal treasurers and Citron opponents, and put together these questions. The answers were provided by Citron and Assistant Treasurer Matthew R. Raabe.

Q. You've said one of the ways you boost earnings on your \$8 billion in deposits is to purchase government securities and use them as collateral for large cash loans, which you invest in other notes. The Wall Street Journal reported that you had to put up \$140 million in additional collateral because the market value of the notes you had pledged fell. Doesn't that collateral call represent a loss to the fund? And when you have to put up additional collateral, doesn't that eliminate interest earnings on that money? A. Actually, we've now had to put up \$300 million in additional collateral since interest rates began rising in March, but none of that money has been lost. We used securities in our portfolio as the collateral, and we're still earning interest on those notes, at what is called the coupon, or face, rate. When the borrowing term ends, we get those notes back. As long as we hold those notes until maturity, we lose nothing on them. We still have an additional \$700 million available to use as collateral should interest rates continue to increase. But if you were watching the market Thursday, you saw the interest rate on five-year treasury notes drop 15 basis points (0.15 percent). We don't think we'll need all of that collateral.

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Q. I understand that borrowing cash in this way, known as reverse repurchase, allows you to earn arbitrage, or profit, on the difference between the cost of the cash and investment earnings. But when interest rates climb as they've done in the past few weeks, doesn't the cost of borrowing cash go up as well, even on the deals you've already structured? Isn't there a danger that arbitrage earnings will drop sharply, or even reverse, and you'll lose money?

A. Yes and no. When interest rates increase, so does our borrowing cost. That means we may not earn as much extra income as we had earned before. Over the 15 years we have been doing these transactions, we have had spreads between borrowing costs and reinvestments as small as 25 basis points (0.25 percent) to more than 300 basis points (3 percent). Right now, our average spread is around 150 basis points, so we still have a good profit margin. Q. Let's talk about Newport-Mesa and the other three school districts in south county that sold \$200 million in taxable bonds so they could generate arbitrage earnings. I understand that deal expires in June. Now let's suppose they decide, for whatever reason, not to sell new bonds and continue the deal for another year. That leaves you stuck with the five-year Federal National Mortgage Association securities purchased with their money. In a letter you sent the districts last year, you said the investment pool would absorb their securities if they wanted out. According to your letter, the coupon (face) rate of those two sets of securities is 5.4 percent and 4.8 percent. Aren't those bad investments for the fund at the current interest rates?

A. Not really. The investment pool has always owned the securities purchased for the school districts and, as an accounting mechanism, we have designated the interest to go to the schools. This allows the schools to know exactly how much interest they will earn on their investment. If the schools decide not to sell new bonds, the pool would continue to own the securities and would receive all the interest. It's important to note that each of the four districts has already earned an additional \$1 million in interest income from this transaction. That pays for additional education programs that would not otherwise be available.

Q. I've been told that you have about \$760 million of these taxable bonds out, on behalf of various agencies. Are all of these funds wrapped up in reverse repurchases? What is the total value of bonds in your fund purchased with leveraged cash? What if arbitrage earnings top out, and all of the agencies ask to get out? Will you have enough money to purchase all of the leveraged bonds, or will you have to sell some of them at a loss?

A. All of the taxable issuances are invested in the reverse-repurchase agreements, as are other monies. We have approximately \$12 billion in reverse repurchases, and those investments are based on the cash-flow information provided to us by the participants in our pool. These participants have told us they intend to stay in the investment pool. If they change their mind and decide to withdraw their funds, we have enough cash available to



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let them get out without having to sell any securities. Q. But what if interest rates keep rising? If rates go up another percentage point in the next two months, or two points, will you run out of collateral and be forced to sell some of these bonds short (at less than face value)? How would you extricate yourself if the worst happened?

A. All investment managers have plans for changes in interest rates. However, you can't make a plan for a worst-case scenario, because if you did, you would have to sacrifice any opportunity to earn a good return. For example, even if all of our money was invested in the very shortest-term securities available, we would still have the risk of losses if every participant left the pool. As money managers, it's our job to assess the most likely interest-rate risks and make plans accordingly. I can't discuss the specifics of my contingency plans, because part of an investment manager's strength in the investment markets is that the other investors don't know your plans. If they did, they could take investment positions that would allow them to take advantage of your needs.

The Orange County Register

## **Article 5: Bergeson ends support of treasurer**

candidate

POLITICS: The state senator says she is uncertain of the accuracy of the challenger's campaign.

***April 29, 1994***

Byline: CHRIS KNAP

The Orange County Register  
Credit:

State Sen. Marian M. Bergeson has withdrawn her endorsement of county treasurer hopeful John M. Moorlach, citing a concern over his campaign tactics.

Moorlach and his supporters have accused 23-year Treasurer Robert L. Citron of risking local governments' deposits by using high-return investment strategies. Citron defends his strategies as aggressive but prudent.

Last week, Orange County Republican Party Chairman Thomas Fuentes confirmed that Citron is being targeted by the local GOP, even though the job is nonpartisan, because he is a "liberal, partisan Democrat."

But municipal finance experts told The Orange County Register that charges by Moorlach have worried investors and made it more difficult to sell securities backed by Orange County governments. Tustin withdrew its money from the county pool after encouragement from a Moorlach supporter.

"I'm not ready to say (Moorlach's campaign) is a dirty-tricks scheme \_ I just don't know," Bergeson said. "(But) I felt that if this was going to be politicized, that I didn't want any part of it."

Moorlach said he was stunned and a bit mystified when Bergeson, R-Newport Beach, called him Monday and asked that he stop using her name.

"It was one of those phone calls where she was so polite and so positive, but just wanted her name withdrawn. If she stands by that, I will be very disappointed," Moorlach said.

Bergeson is unopposed in her campaign for the 5th District seat on the Board of Supervisors, and Moorlach, a Costa Mesa accountant, considered her support valuable enough to list her as his campaign chairwoman.

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All five incumbent supervisors have endorsed Citron, citing the millions of dollars in extra interest he has earned for local governments and school boards over the past 10 years, often twice the return of the more conservative state investment pool.

In an interview Thursday, Bergeson said she didn't know she was Moorlach's campaign chairwoman until a reporter told her.

Moorlach has been questioning the security of Citron's methods in interviews over the past several weeks with The Wall Street Journal, Bond Buyer and local newspapers.

Moorlach points out that Citron has been pledging securities in his portfolio as collateral for cash loans and reinvesting the proceeds. Citron banks the difference between the interest earned on the securities and the cost of the loans, profit known in the financial world as arbitrage.

Citron acknowledges that his plans carry risk should interest rates rise unexpectedly, but says he has built numerous safeguards into his strategy.

Two weeks ago Tustin, spurred by Moorlach supporter and Tustin Councilman Jeff Thomas, pulled its \$4 million from the pool, generating a splash of publicity. Municipal-bond experts began to report that investors were shying away from Orange County-backed bonds.

"What I read in the paper caused me concern," Bergeson said.

The Orange County Register

## **Article 6: Treasurer says gains offset losses**

GOVERNMENT: County official Robert Citron explains his investment actions.

**May 8, 1994**

Byline: CHRIS KNAP

The Orange County Register  
Credit:

The late-winter jump in interest rates spurred Orange County Treasurer Robert L. Citron to cash in \$200 million in devalued securities, costing the county investment pool \$8.46 million, transaction records and interviews show.

Citron said the losses were balanced by the sale of \$275 million in high-performing securities, which brought the county \$8.97 million in profit. "We came out with a net gain, overall, and prepared ourselves to re-enter the market in 30 to 45 days to obtain investments at higher interest yields," Citron said. "The trading we did was not at all unusual."

Experts in municipal finance contacted by The Orange County Register said a loss is sometimes necessary when an investment turns sour. But an investor for the state of California who takes a more conservative stance than Citron said he would not want to have to explain such a loss to the cities and counties that deposit with him.

"Losses can cause a lot of questions and concerns," said William Sherwood, chief of investments for the \$26 billion pool run by the state treasurer. "It's something that we quite frankly don't like to do. We buy and hold (until maturity)."

But Sherwood added that municipal investors such as Citron who hold depositors' funds for a longer term sometimes do trade at a loss so they can reinvest at a higher return.

"If they are extending into another security that will give them a better return in the long run, it may be a beneficial trade for the overall portfolio," Sherwood said.

Citron, Orange County's elected treasurer for 23 years, has been greatly praised in the past few years for earning returns as high as 10 percent on his \$8 billion in deposits \_ generally twice the returns of the state pool.

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But this year, he is facing an election challenge from Costa Mesa accountant John M. Moorlach and has had to defend his strategies, which Moorlach has called too risky.

The strategies include the use of:

Reverse repurchases, in which securities are pledged as collateral for cash loans.

Adjustable-rate securities, which can parallel market rates or move opposite them.

Inverse step-ups, where interest goes up according to a fixed schedule, minus an indexed rate.

Citron has said that he seeks to avoid market losses by holding investments until they mature and pay off at full value. But he and his assistant, Matthew Raabe, acknowledged in interviews that they do sometimes trade at a loss, if market conditions dictate.

Interest rates have climbed 2 percentage points since October, devaluing many securities purchased last year. Citron, who charts investment strategy for his office, said he decided that two of those he'd purchased in 1993 should be sold while they still had some market value.

According to transaction journals and treasurer's officials:

A \$100 million certificate of deposit issued by the Bayerische Landesbank was sold March 17 for \$95.15 million, a loss of \$4.8 million. Raabe said the CD was an inverse floater \_ it had an adjustable interest rate that would have paid more if rates dropped. "That's one of those securities you say, 'I wish I hadn't bought that,' " Raabe said.

On March 29, the county sold \$100 million worth of floating rate Federal Home Loan Bank securities. The securities were paying 4.445 percent but might have gone lower. "We thought the return would hit the floor," Raabe said. The county took a \$3.6 million loss.

To offset the losses Citron sold:

\$225 million in Merrill-Lynch corporate notes, an inverse step-up investment then paying 8.32 percent. That March 15 transaction earned the fund \$5.48 million in profit.

A \$50 million certificate of deposit issued by ABN-Amro, another European bank, which was paying 9.12 percent. The CD sold March 3 at \$3.48 million

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profit. Citron said he was uncomfortable with the credit quality of both of the high-performing investments.

Raabe said the \$475 million in cash generated by those transactions is being held in 30-day U.S. Treasury notes, which pay a 4.5 percent return.

"Our view is that interest rates will top out in early summer," Raabe said. "If we get a 6.75 percent (return) on all of that money, that will make more in the long run that we gave up on the short end.

"We could have held these securities until they matured and never taken any loss at all \_ but we would have given up the opportunity to take more interest earnings in the future. We would be trading interest earnings for political cover, and we don't think that's right."

The Orange County Register

## **Article 7: Moorlach fires another salvo at Citron**

POLITICS: The incumbent county treasurer calls the attack the 'dying gasps' of his challenger's campaign.

**June 3, 1994**

Byline: CHRIS KNAP

The Orange County Register  
Credit:

Costa Mesa accountant John Moorlach has renewed his attack on incumbent county Treasurer Robert L. Citron, comparing Citron's investment of public funds to the "savings-and-loan fiasco" that cost taxpayers billions.

Moorlach, who wants to knock the 23-year Orange County treasurer out of his seat during Tuesday's election, said an eight-page investment critique he sent to county supervisors Monday was meant as a wake-up call.

"Regardless of who is elected on June 7, Orange County has a bleak future for its fiscal assets," Moorlach said. "The

supervisors need to know that their goose is no longer laying golden eggs."

But Citron dismissed the attack as "the dying gasps of a candidate who started out on this track and has been greatly derailed."

Citron said the county's \$8 billion investment pool "is in no way in the same position as the (failed) savings-and-loan institutions. The pool is still making tremendous returns. In March we earned 7.61 percent, and in April it was 7.59. In the same period, the state's investment pool returned 4.33 percent."

Moorlach's campaign, the first challenge that Citron has faced in more than 20 years, was fueled by partisan rancor over Citron's support of a fellow Democrat four years ago, and local Republicans have not tried to hide it.

Moorlach's recent campaign statements show contributions from GOP Assemblymen Mickey Conroy of Orange and Gil Ferguson of Newport Beach and county GOP chief Thomas Fuentes, among other prominent Republicans.

But the most acrimonious debate has been generated over an intensely complicated and highly speculative subject: the complex investment strategies that have allowed Citron to bring in double the earnings of other, more

## **Attachment 1: Gaddi Vasquez and the Orange County Bankruptcy**

conservative public finance pools.

After initially coming on strong, including pointed attacks on Citron's investment strategies printed in national financial publications, Moorlach fell silent last month.

He acknowledged Tuesday that his campaign was hurt when state Sen. Marian Bergeson, R-Newport Beach, pulled back her endorsement in late April, saying she was worried that his attacks had threatened the financial stability of county investments.

But Moorlach said he remains convinced, after more than a month of analyzing public documents, that Citron has gambled dangerously on the belief that interest rates will stay low.

By investing in short-term "reverse repurchase" arrangements, and using the money to buy long-term bonds, Citron has earned an arbitrage, or differential profit, that even Moorlach says gave the county "incredible performance numbers."

But if interest rates continue to rise, as they have in the past six months, Citron will be stuck with billions of dollars worth of bonds returning less-than-market rates, Moorlach said. If he's forced to sell the bonds in a down market, the losses could cut into principal.

"I'm not trying to cry wolf or scream fire in a theater," Moorlach said. "All I'm saying is, 'Board of Supervisors, look, this is risky.' If interest rates rise, based on how he's grown his garden, the harvest isn't going to be very attractive. Win, lose or draw, the problem's still there."

Citron said Moorlach's dire scenarios are based on speculation. "We don't believe that situation will crop up," Citron said. "If interest rates do go up, not all of the securities we have will (lose value) in that way."

"We may not be earning the very high interest rates, but we are still predicting that we will earn no less than 6.5 percent in the fiscal year that begins July 1."

### **SIDEBAR**

#### **COUNTY TREASURER-TAX COLLECTOR**

The treasurer keeps county funds on deposit for more than 100 public agencies in Orange and surrounding counties, investing surpluses for the public's benefit. As tax collector, he or she bills property owners for taxes owed. Current pay is \$96,000. The term of office is four years. The job and election are nonpartisan. Robert L. Citron, 69



## **Attachment 1: Gaddi Vasquez and the Orange County Bankruptcy**

Incumbent treasurer-tax collector. The Santa Ana resident was hired as an Orange County deputy tax collector in 1960, and was elected to the top job in 1970. In 1973 his office was combined with that of the treasurer and he won that post. He has received good marks for his performance as treasurer, and in 1988 was named by City and State Magazine as the year's outstanding municipal-finance officer. He has not faced an election challenge since 1970.

John Moorlach, 38

Certified public accountant and certified financial planner with the firm of Balser, Horowitz, Frank & Wakeling. The Costa Mesa resident has a bachelor's degree in business administration from California State University, Long Beach. He has been practicing as an accountant and financial planner since 1976. Moorlach also is active in local Republican Party politics, including membership on the Orange County Republican Central Committee.

The Orange County Register

## **Article 8: Citron likely to keep long-time hold on office**

TAX COLLECTOR-TREASURER: Attacks on his reputation backfired, the incumbent said as he held the lead Tuesday.

**June 8, 1994**

Byline: CHRIS KNAP

The Orange County Register  
Credit:

Robert L. Citron, Orange County's treasurer-tax collector for nearly a quarter of a century, appeared headed to another four-year term Tuesday.

Citron was leading accountant John Moorlach in the early returns. "I believe the voters understood what this election was all about," Citron said. "The partisan attacks, and the attacks on my reputation as an investor of public funds, were irresponsible and they have backfired."

Moorlach said it was too early to concede. He declined to apologize for his campaign style.

"I feel we dealt with the issues," he said. "We ran a clean campaign. I have no regrets."

Although his job is non-partisan, Citron's Democratic party registration and occasional support of other Democrats prompted a strong challenge from local Republicans.

Moorlach, a member of the county Republican Central Committee, was backed by county Republican Chairman Tom Fuentes and GOP Assemblymen Mickey Conroy and Gil Ferguson among other prominent Republicans.

Citron has received high marks \_ including endorsements from all five incumbent supervisors \_ for his handling of \$8 billion in public funds. Citron's sophisticated investment strategy has frequently earned county depositors twice what the state investment pool was paying.

But Moorlach, a certified public accountant from Costa Mesa, turned that praise upside down during his campaign, charging that Citron was taking dangerous chances that risked the loss of principal deposits.

## **Attachment 1: Gaddi Vasquez and the Orange County Bankruptcy**

The turning point for Moorlach may have come in late April, when his honorary campaign chairman, state Sen. Marian Bergeson, R-Newport Beach, pulled back her endorsement.

Citron, 69, of Santa Ana, was hired as an Orange County deputy tax collector in 1960 and elected to the top job in 1970.

Moorlach, 38, has a degree in business administration from California State University, Long Beach. He has been practicing as an accountant and financial planner since 1976.

Register staff writer Gina Shaffer contributed to this report.

The Orange County Register

## **Article 9: O.C.'S SKY DIDN'T FALL**

GOVERNMENT: Critics of the tactics of Treasurer Robert L. Citron had predicted financial doom.

***September 9, 1994***

Byline: CHRIS KNAP

The Orange County Register  
Credit:

A few months ago, Orange County Treasurer Robert L. Citron was bracing himself against a barrage of authoritative-sounding criticism.

The Wall Street Journal said his investment strategies were "similar (to what) caused the collapse of numerous savings-and-loan institutions."

The Bond Buyer, a New York finance-industry weekly, quoted Tustin's city treasurer saying Citron's search for high yields was "heading to a nasty business."

Derivatives Week, another Wall Street publication, found a bond expert who said Citron's \$8 billion pool was "a scandal waiting to happen. ... On (Wall) Street, we call this kind of leveraged reverse (repurchase) strategy 'the death spiral.' "

Costa Mesa accountant John Moorlach, whose campaign against Citron fueled stories in the financial press, declared, "Regardless of who is elected June 7, Orange County has a bleak future for its fiscal assets."

Well, the campaign is over, interest rates are leveling out, and to tweak a line from Mark Twain, reports of Bob Citron's death spiral appear to have been greatly exaggerated.

Citron, the county's investment chief for 24 years, sold two investments at a loss during the 10-month jump in interest rates, out of more than 500. The \$8.5 million in losses was balanced by cashing in other securities at a \$9 million profit, he says.

At the end of the fiscal year, Citron had returned 7.67 percent to the 180-odd public agencies who invest in his pool. That was eight basis points \_ 8 hundredths of 1 percent \_ below his prediction for the year. It was 67 basis points more than the earnings Orange County had planned on, figures provided

## Attachment 1: Gaddi Vasquez and the Orange County Bankruptcy

by his office show.

The return was 2.68 percent more than the three-times-larger, state-run investment pool earned for other California

municipalities.

"All those dire predictions never came true," Assistant Treasurer Matthew R. Raabe said. "It would appear that our investments were pretty well on target."

In fact, county government's budget managers say they relied on Citron's arbitrage strategy to dig them out of a hole last year: The county issued \$200 million in taxable notes \_ in effect borrowing at 3.95 percent interest \_ and Citron invested it in a series of higher-paying investments. Those secondary investments, known as reverse repurchases, returned 7 percent. After costs, the county earned \$20 million.

"That's what is helping us survive," county budget manager Steve Franks said.

This year, Citron has been asked to invest \$600 million the county has borrowed; arbitrage earnings are expected to be at least \$40 million.

In total, according to figures provided by Franks and Auditor Steve Lewis, Citron's investments will bring the county general fund \$120 million this fiscal year, more than the county's share of local property taxes.

"He has gone out and done a heck of a job as far as I'm concerned," said Lewis, an independent elected official. "To (earn this interest) the county has taken some risks, but in my opinion the risks appear to be very well managed."

Moorlach, who lost in the June election, was unrepentant in an interview this week, noting that leveraged private investment funds have continued to collapse, despite the leveling off of interest rates.

"I had predicted a pretty steep price to pay," Moorlach said. "I think it's too early to say that Citron has escaped that."

During the campaign, Moorlach was accused by county officials of scaring jittery bond buyers, driving up the cost of Orange County's borrowing. Citron and Raabe said he also alarmed cities and school districts who invest in Orange County's pool \_ raising fears that others would join Tustin and pull out their money, creating a run on the pool.

Again, Moorlach defended his actions. He volunteered that he went to city officials in Costa Mesa after the June election and tried to convince them to pull out of the county pool. They refused.

## **Attachment 1: Gaddi Vasquez and the Orange County Bankruptcy**

"I was overly cautious (in the campaign). I was too

conservative in my remarks. I had people tell me, 'Make it (the investment pool) crash,' " Moorlach said. "I didn't want to do that."

Citron said he expects the county investment pool's earnings to drop this year to 6.5 percent in a delayed reaction to last winter's devaluation of the bond market.

The state fund, which more closely mirrors the ups and downs of the market, has experienced increased earnings \_ a 60 basis point (.6 percent) increase since June.

"I still don't think (leveraged repurchases are) a safe strategy," Moorlach said. "Whether he knows what he's doing, I don't know. We might factor in luck."

Citron was reluctant to be interviewed for this story, contending that any publicity could bring back the bad vibrations that make investors nervous.

"As far as rubbing Moorlach's nose in what he said, I'm not interested in doing that," said Citron, 69. "I'm not interested in creating another controversy.

"Sixty-one percent is not a landslide, but it's certainly a strong election by the people of their faith in me. People just didn't believe what (critics) were saying."

The Orange County Register

## **Article 10: Citron's investment report rebuts**

primary challenger

GOVERNMENT: The treasurer-tax collector defends his strategy on securities.

***October 13, 1994***

Byline: CHRIS KNAP

The Orange County Register  
Credit:

Orange County Treasurer-Tax Collector Robert L. Citron was strongly criticized during the June primary by opponent John Moorlach, a Costa Mesa accountant who suggested that the

treasurer's aggressive strategies were risking public funds.

In an annual report sent last week to 187 public agencies that invest in the county fund, Citron strives to refute that criticism, saying the "paper losses" that Moorlach pointed to will never be realized because the fund seldom sells an investment before it matures at full value.

"In periods of rising interest rates, securities purchased one year ago are worth less today (on the market) than when they are originally purchased," Citron said. "An actual gain or loss would only be incurred if the investor sells the security prior to its maturity date."

Citron also said reverse repurchase arrangements \_ leveraged investments that Moorlach criticized as too risky \_ earned \$251 million for county investors, the equivalent of an additional 2 percent yield.

His report points to the long-term stability of the \$8 billion pool, noting that the average annual yield for the past 10 years was 8.9 percent. Last year, the return was 7.74 percent.

California's \$25 billion state investment pool yielded 4.4 percent last year.

Citron said the county pool still is returning more than 7 percent interest, but he expects yields to drop to 6.5 percent by the end of the fiscal year.

In part, the yields will fall because Citron had invested in inverse adjustable-rate securities, which began to yield less as interest rates rose.

## **Attachment 1: Gaddi Vasquez and the Orange County Bankruptcy**

Citron said that if he could have predicted that interest rates would rise, he would not have purchased these "derivative" securities.

"Former President Harry Truman once defined that a successful leader or business head made the correct decisions 80 percent of the time," Citron wrote. "I realize that my decisions could be wrong 20 percent of the time. This probability of error keeps me diligent to see that any miscalculations of economic conditions do not have an overly negative effect on our investors."

Moorlach was not available for comment late Wednesday.

The Orange County Register



**Article 11: Citron foe had opposed funds plan**

***December 2, 1994***

Byline: RICKY YOUNG

The Orange County Register  
Credit:

Costa Mesa accountant John Moorlach could have stuck out a billion-dollar raspberry Thursday and told the voters of Orange County, "I told you so."

Moorlach, 38, predicted investment-pool doomsday in his campaign to unseat Treasurer Bob Citron in June. He lost, getting 39 percent of the vote.

"I can't be smug, it's a very sad day," Moorlach said Thursday. "I tried to warn everybody and nobody understood. There will be lots of victims. School kids will not get proper funding. Our taxpayers are going to suffer."

Even if he had won, Moorlach said, investments were locked in. All he would have been able to do was minimize some losses.

Now, Moorlach fears, the problem could compound itself if investors ask to get out, lenders ask for more money and interest rates continue to go up.

The Orange County Register

## **Article 12: O.C. fund down \$1.5 billion**

FINANCE: The treasurer's investment strategy creates a bond-market 'paper' loss that amounts to \$600 for every county resident.

***December 2, 1994***

Byline: CHRIS KNAP

The Orange County Register  
Credit:

Orange County's investment fund lost \$1.5 billion in value over the past nine months, an amount that could cripple local

governments if they are forced to absorb what are now "paper" losses.

The revelation of the bond market losses Thursday by county Treasurer Robert L. Citron rocked the nation's financial markets. Experts said it is the largest decline ever disclosed by a municipal investment fund \_ equal to \$600 for every Orange County resident.

Citron and other county officials downplayed the loss as similar to declines in nearly every bond fund in recent months. But he also froze the fund for 30 days and told investors they would lose 20 percent if they tried to withdraw their deposits. Experts said it will be difficult for the county to avoid booking substantial losses.

Citron's controversial practice of borrowing against investments in the fund \_ which allowed the county to add \$12 billion in bonds to its \$7.8 billion in deposits \_ backfired when rising interest rates cut the bonds' value and multiplied the losses.

His decision to put one-third of the fund in highly volatile securities known as "derivatives" compounded the problem.

"If he thought he was going to insulate himself from the market, he was wrong," said Joe Mysak, editor of Grant's Municipal Bond Observer in New York. "We haven't seen the last of these losses."

The county's top finance officers called a press conference Thursday to try to squelch rumors that the fund had collapsed.

## **Attachment 1: Gaddi Vasquez and the Orange County Bankruptcy**

"It is not a crisis and is not a catastrophe," Assistant County Treasurer Matt Raabe said. "We are not concerned that the fund is going under."

But to prevent a run that would force the county to sell at a huge loss, Citron froze the fund and told officials from 180 local agencies that they will lose 20 percent of their deposits if they want out.

That strategy \_ which some investors said was contrary to their agreement with the county \_ appeared to have quieted withdrawal demands from the most restive investor, the Irvine Ranch Water District.

"I'm certainly not going to exercise (my withdrawal option) if I'm going to take a 20 percent haircut," said IRWD President Peer A. Swan, whose agency has \$300 million with the county.

Either a run of withdrawals by depositors or the cancellation of credit by major brokers who have lent the county billions could force the county to sell at the \$1.5 billion loss.

If interest rates hold steady and investors stay in the pool, the losses may never be realized.

"We plan to remain calm in our school district," said Jackie Price of the Capistrano Unified School District, which does not have the option of withdrawing from the fund. "We encourage all other public agencies to remain calm. ... We implore people to remain calm."

Similar bets by municipal investment pools have caused several spectacular crashes, most recently the collapse of a Cuyahoga County, Ohio, investment pool that lost \$114 million last month.

Many bond industry observers said Thursday that Orange County will not be able to avoid a similar crash, as Citron political opponent John Moorlach, a Costa Mesa accountant, had predicted earlier this year.

"(Moorlach) was absolutely right as rain and now we're going to pay hell for it," said Irvine investment broker Grant Bettingen. "(The county) is going to lose \$1 billion to \$2 billion and they are not going to be able to pooh-pooh that."

But Raabe and other officials insisted that the worst will not come.

"Nationwide there are many bond funds and mutual funds that invest in government securities. Substantially all of those have suffered paper losses over the last year," Raabe said. "We are in exactly the same position. ... We have not to date incurred any actual losses."

## **Attachment 1: Gaddi Vasquez and the Orange County Bankruptcy**

Citron described the loss as 7.5 percent of the market value of \$12 billion in securities controlled by the fund, modest compared with the 10 percent of value lost by some private funds.

"What I did was not irresponsible in any way shape or form," Citron said.

Over the past five years, Orange County has earned rates almost double the state of California's Municipal Investment Pool, principally through investments based on cash borrowed against government securities.

In the past five years the additional earnings from these investments helped the fund average an 8.6 percent return. Last year it paid 7.74 percent.

But as the Federal Reserve pushed interest rates up from 3.25 percent in February to 5.5 percent Nov. 15, the market value of the bonds Citron has borrowed against declined, forcing him to either invest more cash or sell the leveraged securities at a loss.

To avoid taking such a loss, Citron has put up \$650 million in additional cash since August, according to assistant treasurer Raabe. Current cash reserves are just \$350 million.

A consultant hired by the county, Capital Risk Market Advisors, identified the lack of ready cash as the single biggest problem facing the county's fund. A secondary problem is the possibility that further interest rate increases will cause additional market losses.

Every local agency contacted by The Orange County Register Thursday said it would stay in the fund temporarily, but many expressed grave concerns.

Andrew Czorny, treasurer for the Orange County Water District, said his agency has \$110 million in assets tied up in the fund and has counted on investment earnings that may never materialize \_ a problem that could affect water rates.

"(But) if we pull our money we will cut our own throats because we will have lost more than we could gain by investing elsewhere," Czorny said.

Czorny said major investors had been told by the treasurer just one month ago that the county had \$2 billion in cash, enough to return investment principal to any investors who wanted out.

About 40 percent of the investors in the fund, including the Orange County Transportation Agency (\$1 billion in deposits), the Orange County Sanitation Districts (\$450 million) and the Irvine Ranch Water District (\$300 million), are discretionary depositors who can put their money elsewhere.

## **Attachment 1: Gaddi Vasquez and the Orange County Bankruptcy**

But when IRWD's Swan approached county officials last week and asked for his deposits, he was told he would not be able to collect the money for 30 days. Tuesday, Swan said, he learned that he would also have to take a 20 percent loss \_ his share of the market decline.

"I'm not panicked about the deal," Swan said. "The most prudent thing to do would be to take the money out. But for the benefit of the people of the county I would be willing to leave the money there, as long as I can participate in the (investment) review committee."

County Administrative Officer Ernie Schneider said the county has put together a team of management experts and investment consultants who will propose a strategy for repositioning the fund \_ possibly by purchasing investments that would pay off if interest rates rise further.

Register staff writers Elliot Blair Smith, Liz Pulliam, Cheryl Downey and Dan Froomkin contributed to this report.

The Orange County Register

THE ORANGE GROVE

## **Article 13: Officials ignored signs of risky investments**

***December 5, 1994***

Byline: SCOTT PEOTTER

Credit:

Now it has finally hit the fan!

The sky is falling over the Orange County Board of Supervisors in a multi-billion dollar fiasco. We have now discovered that the concerns John Moorlach had regarding the safety of the Orange County Investment Pool (OCIP), in his race for county treasurer against Robert L. Citron, were true. Higher returns do mean higher risks.

The board of supervisors has bragged about how much "free" money the county treasurer had delivered to the board so that they could continue their pet projects without having to raise taxes. They must have figured that the treasurer was responsible directly to the voters and that they didn't need to look over his shoulder, as long as that free money kept coming in. Besides, the elected auditor/controller, Steve Lewis, kept giving Citron a clean bill of health.

Now we find out that the OCIP is in trouble and that they want "cooperation" from their investors (i.e., they want to freeze the assets) amid huge losses because of Citron's inordinate risks.

Now we as taxpayers in "conservative" Orange County may be forced to make up the huge losses that have already occurred. Some estimates are that the "market" value of the OCIP is presently valued at only 50 cents on the dollar. This would translate into a loss of \$3.7 billion if it were liquidated today.

All of the county's schools as well as several other

governmental agencies (over 180 agencies) have assets "invested" in the fund.

Some school districts, like Irvine and Newport-Mesa, and water boards like Irvine Ranch Water District have actually borrowed additional funds in order to invest in the OCIP hoping to make more interest than they pay (a practice called arbitrage). Those school district notes are due next June.

Citron has said that he holds the bonds that he buys to maturity and therefore never loses capital. However, when his "bull" market bets flounder in a "bear" market, the rate of return for his fund drops rapidly.

Now, when any agency wants its money out because it can get a better return

## **Attachment 1: Gaddi Vasquez and the Orange County Bankruptcy**

elsewhere \_ Merrill Lynch has reportedly recommended that the OCTA put its money elsewhere \_ Citron may be forced to sell his bonds before maturity in order to pay back the money.

To compound this problem, Citron has leveraged his funds through reverse repurchase agreements. In other words, there was originally \$7.4 billion invested but Citron has borrowed against this twice and invested the loan proceeds for a total of \$22 billion in investments.

In simple math this means that every 10 percent the overall principal value goes down, the actual loss against the original principal is 30 percent. In Citron's press release, he indicated that the OCIP has a "paper loss" of 7 percent, or \$1.5 billion. This is, however, deceiving because of the above mentioned leveraging. His actual paper loss (if you use his \$1.5 billion number) is over 20 percent.

On top of all Citron's safe investments are \$5.6 billion in derivatives, which are selling for no more than 50 cents on the dollar (if you can find a buyer).

In the October Bond Buyer magazine reported that county commissioners in Cuyahoga County, Ohio had closed down their treasurer's fund because of similar investment strategies and losses in the fund and that the county commission was going to guarantee the investors their principal.

Another example is Odessa Junior College in Texas, which lost half of all its investments and, according to the Sept. 23 Wall Street Journal , had to borrow on an emergency basis and raise property taxes to pay for it.

This is a financial disaster in the highest magnitude and one that was evident for those who wanted to investigate.

But the responsible governmental agencies or governmental officials didn't understand what Citron was doing and/or trusted him blindly. The elected officials who had direct responsibility didn't provide proper oversight.

These include Auditor/Controller Steve Lewis (who endorsed Citron in his re-election), Supervisor-elect Marian Bergeson (who publicly disavowed John Moorlach during the campaign and who authored the bill allowing Citron to leverage tax monies), and County Chief Administrative Officer Ernie Schneider (who also publicly objected to Moorlach's concerns and is now in charge of the management team to "correct" this problem).

Those less culpable, but no less responsible, are the financial directors of the various governmental agencies and the elected officials that are their bosses.

What do we as taxpayers do? Demand Citron's resignation effective

## **Attachment 1: Gaddi Vasquez and the Orange County Bankruptcy**

immediately and have the board appoint John Moorlach (if he is willing to serve) since he was one of the first to identify the problem and call for correction.

For the rest of the responsible parties, I will leave that up to the taxpayers, but I will remind the voters that three Fullerton City Council members were recalled because they raised their utility tax by a mere 2 percent.

If the OCIP ends up losing 50 percent of its value, that translates into almost \$3,000 for every registered voter in this county.

THE ISSUE: County officials in a position to know better allowed the risky investment practices of the Orange County Investment Pool to continue.

THE WRITER: Mr. Peotter is an architect and vice chairman of the Irvine Planning Commission.

The Orange County Register



**Article 14: REPERCUSSIONS Riley's statement on  
Chapter 9 filing**

***December 7, 1994***

Byline: The Orange County Register

Credit:

The following statement was issued Tuesday by Thomas F. Riley, chairman of the Orange County Board of Supervisors:

"As one of the dozen major investors in the treasurer's investment pool, the Orange County Board of Supervisors late this afternoon authorized the filing of petitions under Chapter 9 of the Bankruptcy Code. We took this action on behalf of the county and the other investors so that the current financial situation can be resolved in an orderly fashion and claims related to the

investments can be efficiently restructured without any disruption in the operations of the county or that of the other participants in the investment pools.

"It is important that everyone understand that, as a result of this action, the county remains in control of all of its

operations, and retains all political and protective powers and authority over property and revenues.

"The filing will have no impact on the delivery of services by the County of Orange. Police, fire, paramedic and other services will not be impacted.

"We took this action today in response to the decision by a number of investment bankers to decline to roll over or renew existing reverse-repurchase agreements held by the investors in the amount of \$1.2 billion. This action resulted in a default of the agreements, necessitating immediate action.

"We elected to file Chapter 9 because it provides a centralized forum within which to resolve any and all competing claims while assuring that nothing related to the problems of the fund interferes with the county's ability to provide all essential services that the residents and businesses of Orange County have come to expect from their government.

"The Board of Supervisors feels that this action will enable the county and other public-agency investors to continue to meet all their obligations. At the same time, the board believes that the action that was authorized today will facilitate a sensible and timely resolution of the issues, resulting in an equitable distribution of

## **Attachment 1: Gaddi Vasquez and the Orange County Bankruptcy**

the assets of the treasurer's investment fund.

"We have begun to hold briefings with major pool participants, which will continue throughout the week. We have also been in contact with Governor Pete Wilson, Senator Dianne Feinstein, state Attorney General Dan Lungren's office and the Securities and Exchange Commission."

### **SIDEBAR**

#### **KEY PLAYERS**

#### **LOCAL FINANCIAL FIGURES**

John Moorlach, certified public accountant

As Citron's Republican opponent in the June election, Moorlach sounded the alarm about the county's investment strategy and predicted it would bring financial ruin. Moorlach refused to delight in Citron's resignation, however, calling the former treasurer's actions a "major misjudgment." Moorlach has submitted proposals to county officials to protect the fund, and said he might ask supervisors to appoint him acting treasurer/tax collector. Peer A. Swan, financial consultant and president of Irvine Ranch Water District

A \$100 million withdrawal by the water district last month forced county fund managers to acknowledge a potential \$1.5 billion loss and to clamp down on remaining deposits to prevent a full-scale run on the crash. In October, Swan said, he expressed concerns to Citron about potential bond-market losses in the fund. Despite assurances that there was enough cash to ride out the dip in the bond market, Swan said, he decided to withdraw one-fourth of the district's \$400 million investment, in \$ 50 million increments on Nov. 3 and Nov. 10. The district is the fund's fourth-largest investor.

John L. Nelson, Assistant Superintendent for Business Services at the Orange County Department of Education

Nelson is serving as point man for all of Orange County's school districts during the crisis. As the education department's chief fiscal officer, he is serving as a clearinghouse of information for local districts, trying to answer their questions about their legal obligations and fiscal options. State law requires school districts to invest 100 percent of their money in the county treasury.

The Orange County Register

**Attachment 1: Gaddi Vasquez and the Orange County Bankruptcy**

The Orange County Register

## Article 15: O.C. FILES FOR BANKRUPTCY

ORANGE COUNTY VOICES

***December 8, 1994***

Byline:  
Credit:

Officials say Treasurer Robert Citron, who resigned, was solely responsible for his collapsing fund. He answered only to voters. Many Register readers still want to hold the Board of Supervisors accountable.

"Controlling the county's purse strings is the only way voters have of controlling the power of the Orange County bureaucracy. If the bureaucracy is unable to accept the financial limits that we place on them and instead gamble our money away, then all the bureaucracy involved should be fired."

\_ Earle Richmond, 53, law student, Irvine

"The Orange County Board of Supervisors should voluntarily resign over their current financial problems. Malpractice suits should be filed!"

\_ Wes Jones, 43, unemployed, Anaheim

"Talk about mismanagement!"

\_ Nancy L. Smith, 51, facilities coordinator, Huntington Beach

"The handling of the investment pool ought to have a lot more regulation since we're talking about taxpayer capital at risk here. These funds should be reviewed, and the investments they're making should be closely monitored."

\_ Frank X. Smith, 39, sales manager, Huntington Beach

"I suggest all the property taxpayers withhold payment of the first half of property taxes on Dec. 10 to prove a point that we're fed up with the Orange County Board of Supervisors and their inability to accept any responsibility for anything that they do." \_ John Warren, 54, appraiser, Cypress

"The county treasurer did very well in the Reagan and Bush administrations. It took a Democrat president to cripple the fund." \_ Jim Meehan, 57, silk screener, Costa Mesa

"I don't believe the county Board of Supervisors are at fault. This was Citron's

## **Attachment 1: Gaddi Vasquez and the Orange County Bankruptcy**

baby. Anyone trying to fob off responsibility to somewhere else is barking up a no-blame tree."

\_ Dan Mehlhorn, 38, software engineer, Anaheim

WHAT DO YOU THINK?

Do you have questions about the county's financial situation? Comments about officials' handling of the investment funds? Call Infoline: The number is (714) 550-4636, category 7259. We'll answer your questions and print the best comments in Friday's paper. Please be sure to leave your name and a daytime phone number. Fax, E-mail us: You can also fax your questions or comments to us at (714) 542-5037, or E-mail us at [ocronline@delphi.com](mailto:ocronline@delphi.com).

## **Article 16: EXERCISE OF POWER Board had the right to interfere**

LAW: Supervisors have oversight over how county officers perform their duties.

***December 31, 1994***

Byline: JEAN O. PASCO

The Orange County Register  
Credit:

Orange County supervisors repeatedly have protested that they didn't have legal authority to oversee Treasurer Robert L. Citron's handling of the county's ill-fated investment pool, unaware that state law provided them the tools to do so.

Government Code Section 25303 requires them to supervise the official conduct of even independently elected officials such as Citron and emphasizes their responsibility with regard to "the assessing, collecting, safekeeping, management and disbursement of public funds."

A separate code section says the chairman of the Board of Supervisors, auditor and district attorney can demand to "examine the books and count the money in the treasury ... whenever they wish."

Ever since Dec. 1, when the county announced a \$1.5 billion drop in value in the \$7.4 billion pool \_ losses currently are estimated at \$2 billion \_ supervisors have denied they could have done much to avert declaring the nation's largest municipal bankruptcy on Dec. 6.

But The Orange County Register showed four of the five supervisors the Government Code section Thursday and Friday, and none knew of their power and responsibility.

"It's been increasingly clear to me that the Board of

Supervisors didn't exercise proper oversight," Supervisor William Steiner said. "This is a very bitter lesson, and we need to go forward."

## **Attachment 1: Gaddi Vasquez and the Orange County Bankruptcy**

Supervisor Roger Stanton said his not-as-yet-released plan for restructuring county government will make clear the line of accountability.

"The era of unquestioning trust in our public administrators is over," Stanton said. "From this point on, I'm going to get in the face of every elected department head. If we're going to be put on the line for their actions, they're going to be accountable to us, whether it's proscribed by state code or not."

Said board Chairman Gaddi Vasquez: "I think the processes that we as supervisors depended on to make the treasurer-tax collector accountable have been found lacking, and therefore we need to take corrective action. That's exactly what we're in the process of doing."

Supervisor Harriett Wieder declined to be interviewed. Wieder and Supervisor Thomas Riley, both retiring, will spend their last day as supervisors Tuesday.

Riley said Friday that there was nothing in Citron's conduct "that gave us any reason to question him."

Marian Bergeson, who takes over next week for Riley, said Citron was responsible for the investment fund \_ but supervisors had final oversight.

"I think because of this, county government is never going to be the same," she said. "You're going to see a level of accountability you've never seen before."

Experts attempting to straighten out the crippled portfolio found it inflated by loans that used borrowed securities as collateral. The loans backed highly structured notes whose profitability depended on stable or declining interest rates. But rates rose six times in 10 months this year, undermining their value and leading to the fund's crash.

The code section notes that, though the board has authority to "supervise county officers in order to insure that they faithfully perform their duties," supervisors cannot perform the duties for them and cannot "direct the manner in which the duties are performed."

Matt Ross, spokesman for the state Attorney General's Office, said the board cannot fire elected officials or tell county officers how to do their jobs, but it does have final authority over the county budget and can "make its influence known," Ross said.

### **SIDEBAR**

#### **STATE LAW**

The State Government Code explicitly gives county boards of supervisors

## **Attachment 1: Gaddi Vasquez and the Orange County Bankruptcy**

authority over other independently elected officials, including the county treasurer. The law:

Section 25303, Supervision of officers.

The board of supervisors shall supervise the official conduct of all county officers, and officers of all districts and other subdivisions of the county, and particularly insofar as the functions and duties of such county officers and officers of all districts and subdivisions of the county relate to the assessing, collecting, safekeeping, management or disbursement of public funds. It shall see that they faithfully perform their duties, direct prosecutions for delinquencies when necessary require them to renew their official bond, make reports and present their books and accounts for inspection..