



**FOOTHILL/EASTERN TRANSPORTATION
CORRIDOR AGENCY**

Financial Statements

June 30, 2014 and 2013

(With Independent Auditors' Report Thereon)

**FOOTHILL/EASTERN TRANSPORTATION
CORRIDOR AGENCY**

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Independent Auditors' Report

The Honorable Board of Directors
Foothill/Eastern Transportation Corridor Agency:

Report on the Financial Statements

We have audited the accompanying financial statements of the Foothill/Eastern Transportation Corridor Agency (the agency), as of and for the years ended June 30, 2014 and 2013, and the related notes to the financial statements, which collectively comprise the agency's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Foothill/Eastern Transportation Corridor Agency as of June 30, 2014 and 2013, and the changes in its financial position and its cash flows for the years then ended, in accordance with U.S. generally accepted accounting principles.



Other Matters

Required Supplementary Information

U.S. generally accepted accounting principles require that *management's discussion and analysis* on pages 3–8 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

KPMG LLP

October 2, 2014

FOOTHILL/EASTERN TRANSPORTATION CORRIDOR AGENCY

Management's Discussion and Analysis

June 30, 2014 and 2013

(In thousands)

This discussion and analysis of the financial performance of the Foothill/Eastern Transportation Corridor Agency (the agency) provides an overview of the agency's financial activities for the fiscal years ended June 30, 2014 and 2013. Please read it in conjunction with the agency's financial statements and accompanying notes.

Background

The agency was formed in 1986 as a joint powers authority by the County of Orange and cities in Orange County, California to provide traffic relief to Orange County through the construction and operation of toll roads. The agency was created to plan, design, finance, construct, and operate the Foothill (State Route 241) and Eastern (State Route 241, State Route 261, and State Route 133) Toll Roads. The agency's primary focus is the operation of the facilities and collection of tolls to repay the related tax-exempt revenue bonds that were issued to construct the toll roads.

Planning began in the 1970s when local transportation studies identified the need for new highways, including the Foothill and Eastern Transportation Corridors (State Route 241, State Route 261, and State Route 133), to serve Orange County's growing population. In the early 1980s, the corridor was envisioned as a free highway funded through state or federal gas-tax revenues, but with a shortage of gas-tax revenues to fund transportation improvements and increasing costs of building new roads, local officials began to study alternative ways to fund road projects.

In the mid-1980s, two state laws were passed authorizing the agency to collect tolls and development impact fees to fund road construction. With a pledged revenue stream from future tolls, the agency issued nonrecourse, toll-revenue bonds to fund road construction, rather than relying on the uncertainty of state gas-tax revenue. The agency also reached an agreement with the California Department of Transportation (Caltrans) to assume ownership, liability, and maintenance of the State Route 241, State Route 261, and State Route 133 Toll Roads as part of the state highway system. This agreement eliminated the need for the agency to seek additional funding sources for road maintenance.

In 1993, the first 3.2-mile segment of the Foothill (State Route 241) Toll Road opened to traffic, the first toll road in Southern California to use FasTrak[®], an electronic toll collection system that allowed drivers to pay tolls without stopping at a toll booth. At June 30, 2014 and 2013, averages of approximately 177,000 and 180,000 transactions were recorded on the State Route 241, State Route 261, and State Route 133 Toll Roads every weekday, serving as an important, time-saving alternative route to local freeways, and arterial roads.

Financial Highlights

In December 2013, the agency issued \$2,274,617 of Series 2013 Toll Road Refunding Revenue Bonds (2013 Bonds); the proceeds of the issuance were used to refund the outstanding balance of its 1999 Bonds. As a result of this transaction, the ultimate maturity of the agency's long-term debt obligations has been extended from 2040 to 2053. In addition, the transaction is expected to improve near-term excess cash flow, provide greater latitude in managing toll rates, and create increased margin to withstand future economic downturns.

Tolls, fees, and fines collected in fiscal year 2014 (FY14) totaled \$138,923 compared to \$128,727 in the prior fiscal year, an increase of 7.9%.

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As of June 30, 2014 and 2013, the agency had \$517,347 and \$545,226, respectively, in restricted cash and investments that were subject to master indentures of trust for the bonds outstanding at each date (1995 and 2013 as of June 30, 2014). The agency also had \$129,990 and \$121,499 in unrestricted cash.

The agency's net position at June 30, 2014 and 2013 was \$(1,453,701) and \$(1,433,088), respectively. The negative net position results primarily from the inclusion in the agency's financial statements of its long-term debt obligations, which were used to fund construction of the corridors, but not the related capital assets, since ownership of the corridors was transferred to Caltrans upon completion.

Overview of the Financial Statements

The agency's financial statements include the statements of net position, statements of revenues, expenses, and changes in net position, statements of cash flows, and notes to the financial statements. The financial statements present the financial picture of the agency from the economic resources measurement focus using the accrual basis of accounting. These statements include the recordable assets of the agency as well as the liabilities. The current year's revenues and expenses are taken into account regardless of when cash is received or paid. The statements of cash flows provide information about the agency's cash receipts, cash payments, and net changes in cash resulting from operating, capital and related financing, and investing activities during the reporting period.

The statements of net position and the statements of revenues, expenses, and changes in net position report the agency's net position and related changes. Net position is the difference between the recorded assets and liabilities. The recorded activities include all toll revenues and operating expenses related to the operation of the Foothill/Eastern Transportation Corridors. In addition, the agency's construction-related activities, including the design, construction, and mitigation costs for the Foothill/Eastern Transportation Corridors as well as all financing and administration costs, are reflected in the statements. Activities are financed by toll revenues, development impact fees, fees and fines, and investment income.

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Financial Analysis

The following table summarizes the assets, liabilities, and net position of the agency as of June 30, 2014, 2013, and 2012:

	<u>2014</u>	<u>2013</u>	<u>Percentage increase (decrease)</u>	<u>2012</u>	<u>Percentage increase (decrease)</u>
Assets and deferred outflows:					
Current assets	\$ 269,020	230,443	16.7%	217,295	6.1%
Capital assets, net	384,343	367,352	4.6	353,871	3.8
Other noncurrent assets	394,047	442,748	(11.0)	456,365	(3.0)
Deferred outflows	13,822	—	100.0	—	—
Total assets and deferred outflows	<u>1,061,232</u>	<u>1,040,543</u>	2.0	<u>1,027,531</u>	1.3
Liabilities:					
Bonds payable	2,423,519	2,404,474	0.1	2,372,023	1.4
Other liabilities	91,414	69,157	32.2	67,759	2.1
Total liabilities	<u>2,514,933</u>	<u>2,473,631</u>	1.7	<u>2,439,782</u>	1.4
Net position	<u>\$ (1,453,701)</u>	<u>(1,433,088)</u>	1.4	<u>(1,412,251)</u>	1.5

The increases in capital assets in FY14 and FY13 are mainly due to expenditures associated with the All Electronic Tolling (AET) and 241 completion projects. The agency completed its conversion to AET in May 2014 and now offers a wider range of payment options for customers. For customers who do not use FasTrak® transponders, cashless tolling is based on license plate data. AET increases free-flowing traffic and ridership safety, and eliminates backups at toll plazas. It is expected that AET will also result in lower operating costs and will reduce long-term maintenance and equipment replacement costs.

During FY14, work continued in connection with the 241 Tesoro Extension that will lengthen the 241 by 5.5 miles, including the development of engineering plans, completion of environmental assessments, ongoing outreach and community input, and development of a financial strategy for the extension. When completed, the 241 Tesoro Extension will provide a valuable alternative route for commuters and residents in the surrounding area. Long-range planning efforts also continued related to the 241 completion project.

The category above labeled deferred outflows results from implementation of a new accounting pronouncement in FY14 and represents the amount by which the reacquisition price of the refunded bonds exceeded the net carrying value. This amount has been deferred and will be amortized over the remaining period during which the refunded bonds were scheduled to be paid.

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Following is a summary of the agency's revenues, expenses, and changes in net position for the years ended June 30, 2014, 2013, and 2012:

	<u>2014</u>	<u>2013</u>	<u>Percentage increase (decrease)</u>	<u>2012</u>	<u>Percentage increase (decrease)</u>
Operating revenues:					
Tolls, fees, and fines	\$ 138,923	128,727	7.9%	\$ 122,948	4.7%
Development impact fees	19,813	11,794	68.0	4,752	148.2
Other revenue	396	423	(6.4)	1,342	(68.5)
Grant revenue	<u>14</u>	<u>147</u>	(90.5)	<u>376</u>	(60.9)
Total operating revenues	159,146	141,091	12.8	129,418	9.0
Operating expenses	<u>24,066</u>	<u>22,481</u>	7.1	<u>21,994</u>	2.2
Operating income	135,080	118,610	13.9	107,424	10.4
Nonoperating expenses, net	<u>(155,693)</u>	<u>(139,447)</u>	11.7	<u>(109,259)</u>	27.6
Change in net position	(20,613)	(20,837)		(1,835)	1,035.5
Net position at beginning of year	<u>(1,433,088)</u>	<u>(1,412,251)</u>		<u>(1,410,416)</u>	0.1
Net position at end of year	<u><u>\$ (1,453,701)</u></u>	<u><u>(1,433,088)</u></u>		<u><u>\$ (1,412,251)</u></u>	1.5

Revenues for the agency consist primarily of tolls, fees, and fines, which comprised 87.3% of total revenue in FY14 compared to 91.2% of total revenue in FY13. Tolls, fees, and fines increased 7.9% and 4.7%, respectively, over each of the two preceding years, primarily due to toll rate increases and increases in toll transactions. Development impact fees were \$19,813 in FY14 and \$11,794 in FY13, an increase of 68%, compared to an increase of 148.2% in FY13. The amounts of development impact fees collected fluctuate from year to year depending on residential and nonresidential development in Orange County within the area of benefit.

Operating expenses were \$24,066 in FY14 compared to \$22,481 in FY13, an increase of 7.3%. Included in operating expenses is noncash depreciation expense on fixed assets of \$2,277 in FY14, compared to \$2,121 in FY13. Excluding depreciation, operating expenses were \$21,789 in FY14 and \$20,360 in FY13, an increase of \$1,429. The most significant element of this increase was attributable to marketing costs incurred to alert and educate patrons regarding the conversion to cashless tolling.

Net nonoperating expenses for FY14 include investment income of \$8,019, offset by interest expense of \$140,623; the cost of capital improvements contributed to Caltrans (\$1,729); a loss on disposition of capital assets of (\$434); and two items related to the long-term debt refinancing transaction: costs of \$20,890 that were paid and recorded as expense, and amortization of \$36 related to additional costs that were deferred on the agency's balance sheet. For FY13, the agency had a gain on sale of land of \$575, offset by an investment loss of \$1,905 and interest expense of \$137,146. Accrual basis interest expense included accretion on the agency's capital appreciation bonds and convertible capital appreciation bonds of \$35,142 and \$48,156 in FY14 and in FY13, respectively. Interest expense in FY14 included two additional noncash components: amortization of \$194

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related to a discount on the issuance of the 2013 Bonds and amortization of \$712 related to the deferred bond refunding cost from the transaction.

Capital Assets, Net

The following table summarizes the agency's capital assets, net of accumulated depreciation, at June 30:

	<u>2014</u>	<u>2013</u>	<u>2012</u>
Construction in progress	\$ 346,643	339,854	325,055
Right-of-way acquisitions, grading, or improvements	15,014	15,014	15,539
Furniture and equipment	<u>22,686</u>	<u>12,484</u>	<u>13,277</u>
Total capital assets	<u>\$ 384,343</u>	<u>367,352</u>	<u>353,871</u>

Construction in progress includes expenditures related to the AET project prior to its completion in FY14 and improvements in progress related to the 241 completion project. Right-of-way acquisitions, grading, or improvements include easements and environmental mitigation parcels. Furniture and equipment includes facility and toll revenue equipment related to the corridor operations facility, transponders, toll and violations collection equipment, toll booths and buildings, and changeable message signs.

More detailed information about the agency's capital assets is presented in note 5 to the financial statements.

Debt Administration

The agency had outstanding bonds payable of \$2,423,519, \$2,404,474, and \$2,372,023 at June 30, 2014, 2013, and 2012, respectively. The increases in FY14 and FY13 are partially attributable to the accretion of principal on capital appreciation bonds of \$35,142 and \$48,156, respectively. The remainder of the change in each year is attributable to the bond refunding transaction in FY14 and a principal payment of \$15,705 in FY13.

All of the agency's toll revenue, less certain expenses, as defined in the indentures of trust, is pledged to repay these bonds. The agency has several debt covenants contained in the master indentures of trust. Management of the agency represents that the agency was in compliance with all of its covenants as of and for the years ended June 30, 2014 and 2013.

Economic Factors

After consideration of toll rate recommendations from the agency's traffic consultant and the potential effects of traffic diversion, toll rates were approved by the agency's Board of Directors for implementation effective July 1, 2014. The new toll rates are projected to result in a 2.8% increase in transactional toll revenue and reflect increases of 2% for FasTrak® toll rates and rates for non-FasTrak transactions \$1.00 greater than the FasTrak® rates.

The agency continues to focus on customer incentives and promotions to attract new drivers, reward current customers, and increase total transactions and revenue.

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Contacting the Agency's Financial Management

This financial report is designed to provide a general overview of the agency's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Controller, Foothill/Eastern Transportation Corridor Agency, 125 Pacifica, Suite 100, Irvine, CA 92618 or to <http://www.thetollroads.com>.

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Statements of Net Position

June 30, 2014 and 2013

(In thousands)

	2014	2013
Assets:		
Current assets:		
Cash and investments	\$ 129,990	121,499
Restricted cash and investments	132,797	102,478
Receivables:		
Accounts, net of allowances of \$1,662 and \$976	3,392	1,765
Fees	20	327
Interest	1,380	2,424
Other assets	1,441	1,950
Total current assets	269,020	230,443
Noncurrent assets:		
Restricted cash and investments	384,550	442,748
Capital assets, net	384,343	367,352
Unamortized prepaid bond insurance	9,497	—
Total noncurrent assets	778,390	810,100
Deferred outflows of resources:		
Unamortized deferred bond refunding costs	13,822	—
Total assets and deferred outflows	1,061,232	1,040,543
Liabilities:		
Current liabilities:		
Accounts payable	9,174	7,984
Deferred revenue	16,415	13,984
Due to San Joaquin Hills Transportation Corridor Agency	5,102	2,486
Employee compensated absences payable	440	411
Interest payable	60,283	44,292
Current portion of bonds payable	—	25,160
Total current liabilities	91,414	94,317
Long-term bonds payable	2,423,519	2,379,314
Total liabilities	2,514,933	2,473,631
Net position:		
Invested in capital assets, net of related debt	(2,015,857)	(2,037,122)
Restricted	436,258	486,147
Unrestricted	125,898	117,887
Total net position	\$ (1,453,701)	(1,433,088)

See accompanying notes to financial statements.

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Statements of Revenues, Expenses, and Changes in Net Position

Years ended June 30, 2014 and 2013

(In thousands)

	2014	2013
Operating revenues:		
Tolls, fees, and fines	\$ 138,923	128,727
Development impact fees	19,813	11,794
Other revenues	396	423
Grant revenues	14	147
	<u>159,146</u>	<u>141,091</u>
Total operating revenues		
Operating expenses:		
Toll compliance and customer service	8,531	7,578
Toll systems	3,157	3,145
Salaries and wages	3,148	2,969
Toll collections	2,162	2,168
Depreciation	2,277	2,121
Professional services	470	1,702
Toll facilities	849	811
Insurance	811	774
Marketing	2,292	655
Facilities operations, maintenance, and repairs	186	200
Other operating expenses	183	358
	<u>24,066</u>	<u>22,481</u>
Total operating expenses		
Operating income	<u>135,080</u>	<u>118,610</u>
Nonoperating revenue (expenses):		
Gain (loss) on disposition of capital assets	(434)	575
Investment income (loss)	8,019	(1,905)
Contribution of capital improvements to Caltrans	(1,729)	(971)
Costs of bond refunding	(20,890)	—
Amortization of prepaid bond insurance	(36)	—
Interest expense	(140,623)	(137,146)
	<u>(155,693)</u>	<u>(139,447)</u>
Nonoperating expenses, net		
Change in net position	<u>(20,613)</u>	<u>(20,837)</u>
Net position at beginning of year	<u>(1,433,088)</u>	<u>(1,412,251)</u>
Net position at end of year	<u>\$ (1,453,701)</u>	<u>(1,433,088)</u>

See accompanying notes to financial statements.

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Statements of Cash Flows

Years ended June 30, 2014 and 2013

(In thousands)

	2014	2013
Cash flows from operating activities:		
Cash received from toll road patrons	\$ 142,343	129,005
Cash received from development impact fees	20,120	11,488
Cash received from miscellaneous revenue	35	70
Cash received from property rental	361	352
Cash received from grant revenue	14	319
Cash payments to suppliers	(21,112)	(15,970)
Cash payments to employees	(3,149)	(3,013)
	<u>138,612</u>	<u>122,251</u>
Net cash provided by operating activities		
Cash flows from capital and related financing activities:		
Cash receipt for disposition of capital assets	—	1,100
Cash payments for acquisition of capital assets	(17,231)	(16,759)
Cash payments for interest and principal	(48,791)	(105,100)
Cash paid in connection with bond refunding transaction	(101,041)	—
	<u>(167,063)</u>	<u>(120,759)</u>
Net cash used in capital and related financing activities		
Cash flows from investing activities:		
Cash receipts for interest and dividends	8,794	7,600
Cash receipts from the maturity and sale of investments	518,995	(397,012)
Cash payments for purchase of investments	(473,615)	399,064
	<u>54,174</u>	<u>9,652</u>
Net cash provided from investing activities		
Net increase in cash and cash equivalents	25,723	11,144
Cash and cash equivalents at beginning of year	<u>67,623</u>	<u>56,479</u>
Cash and cash equivalents at end of year (note 4)	<u>93,346</u>	<u>67,623</u>
Reconciliation of operating income to net cash provided by operating activities:		
Operating income	135,080	118,610
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation	2,277	2,121
Changes in operating assets and liabilities:		
Accounts receivable	(1,627)	(161)
Fees receivable	307	(306)
Other assets	509	(422)
Accounts payable	(2,980)	1,836
Deferred revenue	2,431	428
Due to/from San Joaquin Hills Transportation Corridor Agency	2,616	183
Employee compensated absences payable	(1)	(38)
	<u>3,532</u>	<u>3,641</u>
Total adjustments		
Net cash provided by operating activities	<u>\$ 138,612</u>	<u>122,251</u>

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	2014	2013
Noncash transactions:		
Bond refunding, including the following elements:		
New bonds issued	\$ 2,274,617	—
Bond discount	(41,008)	—
Escrow deposit to repay principal and accrued interest on refunded bonds	(2,289,693)	—
Transaction costs charged to expense	(20,890)	—
Prepaid bond insurance	(9,533)	—
Deferred loss recorded as deferred outflows of resources	(14,534)	—
Amortization of bond discount recorded as interest expense	(194)	—
Amortization of deferred bond refunding cost recorded as interest expense	(712)	—
Amortization of prepaid bond insurance	(36)	—
Interest expense recorded for accretion of bonds outstanding	(35,142)	(48,156)
Change in unrealized gain/loss on investments	(1,897)	(13,215)
Amortization of discount/premium on investments	(3,255)	3,611
Contribution of capital improvements to Caltrans	(1,729)	(971)
Loss on disposition of capital assets	(434)	—

See accompanying notes to financial statements.

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Notes to the Financial Statements

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(1) Reporting Entity

In recognition of the regional transportation needs in the County of Orange (County), the California State Legislature has enacted various amendments to the California Government Code to authorize the financing of bridges and major thoroughfares by joint powers agencies. Pursuant to such authorization, the Foothill/Eastern Transportation Corridor Agency (the agency) was created in January 1986 by a joint exercise of powers agreement. Current members are the County and the cities of Anaheim, Dana Point, Irvine, Lake Forest, Mission Viejo, Orange, Rancho Santa Margarita, San Clemente, San Juan Capistrano, Santa Ana, Tustin, and Yorba Linda (collectively, the member agencies). The purpose of the agency is to plan, design, construct, finance, administer funds for, and operate the Foothill and Eastern Transportation Corridors. The agency is governed by a Board of Directors comprising representatives from the member agencies. The agency has the power to, among other things, incur debt and establish and collect tolls.

The financial statements comprise the activities of the agency. There are no other organizations for which the agency is financially accountable or for which it is fiscally responsible. The agency and the San Joaquin Hills Transportation Corridor Agency (SJHTCA) are under common management and together are called the Transportation Corridor Agencies. However, each agency has an independent governing board.

(2) Summary of Significant Accounting Policies

The accounting policies of the agency are in conformity with U.S. generally accepted accounting principles (U.S. GAAP) applicable to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing accounting and financial reporting principles.

(a) Basis of Presentation

The agency records revenue in part from fees and other charges for services to external users and, accordingly, has chosen to present its financial statements using the reporting model for special-purpose governments engaged in business-type activities. This model allows all financial information for the agency to be reported in a single column in each of the accompanying financial statements.

The agency distinguishes operating revenues and expenses from nonoperating items in the preparation of its financial statements. Operating revenues and expenses generally result from the collection of tolls, fees, and fines on the corridors. The agency's operating expenses include depreciation, materials, services, and other expenses related to the operation of the corridors. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

(b) Basis of Accounting

The financial statements are prepared using the accrual basis of accounting. Revenues are recognized when earned, and expenses are recognized when incurred. During the year ended June 30, 2013, the Agency implemented GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources and Net Position*. During the year ended June 30, 2014,

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the Agency implemented GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities*.

Restricted resources are used in accordance with the agency's master indentures of trust. Unrestricted resources are used at the agency's discretion. When both restricted and unrestricted resources are available for use, it is the agency's policy to determine on a case-by-case basis when to use restricted or unrestricted resources.

(c) Budget

Fiscal year budgets are prepared by the agency's staff for estimated revenues and expenses. The Board of Directors adopts the annual budget at the June board meeting for the fiscal year commencing the following July. The approval of the budget requires the consent of at least two-thirds of the board members. No expenditures in excess of the total budget for each board-designated category are made without the approval of at least two-thirds of the board members, at which time a revised and amended budget is required to be submitted to the Board of Directors. All budgets are adopted on a basis consistent with U.S. GAAP. All budget appropriations lapse at year-end. Any budgeted expenses not incurred by each year-end must be reappropriated in the next fiscal year.

(d) Cash and Cash Equivalents

Cash and cash equivalents generally consist of cash on hand, demand deposits, and short-term investments with original maturities of three months or less from the date of acquisition.

(e) Investments

Investments are stated at fair value, generally based on quoted market prices.

The agency classifies investments as current or noncurrent based on how readily the investment is expected to be converted to cash and whether any restrictions limit the agency's ability to use the resources.

(f) Receivables

Receivables include amounts due from member agencies for development impact fees collected on behalf of the agency, credit card receivables, interoperable receivables due from other California toll agencies, patron violation receivables, and interest.

(g) Capital Assets

Capital assets include construction in progress, environmental mitigation sites, easements, the corridor operations facility, transponders, toll and violations collection equipment, toll booths, buildings, changeable message signs, vehicles, and furniture. Capital assets are defined by the agency as assets with an initial individual cost of more than five thousand dollars, with the exception of transponders that are valued in total, and an estimated useful life in excess of one year.

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As described further in note 5, the Foothill/Eastern Transportation Corridors and the related purchases of rights of way, for which title vests with the California Department of Transportation (Caltrans), are not included as capital assets because the agency does not have title to these assets. The costs of normal maintenance and repairs and mitigation that do not add value to capital assets or materially extend asset lives are not capitalized.

Capital assets are recorded at cost and are depreciated using the straight-line method over the following estimated useful lives:

Asset type	Useful life
Toll booths and buildings	20–30 years
Changeable message signs	15 years
Toll revenue equipment	5 years
Vehicles	5 years
Leasehold improvements, other equipment, and furniture	5–10 years

Assets determined to be impaired are recorded at the lower of cost or estimated net realizable value.

(h) *Deferred Revenue*

Deferred revenue represents prepaid tolls collected from patrons, including those using FasTrak®, an electronic toll collection system.

(i) *Unamortized Deferred Bond Refunding Costs*

Deferred bond refunding costs represent certain costs related to the issuance of the 2013 Bonds. These costs have been recorded as deferred outflows of resources, and are being amortized over the remaining period during which the refunded bonds were scheduled to be repaid, as more fully detailed in Note 6.

(j) *Revenue Recognition*

Toll revenue is recognized at the time the vehicle passes through the toll plaza. Other revenues are recognized when earned.

(k) *Allocation of Common Costs*

Expenses directly related entirely to the agency are charged to the agency, and those incurred on behalf of both the agency and SJHTCA are allocated between the two agencies based on the estimated benefit to each. In addition, the agency has amounts due from SJHTCA related to SJHTCA customers who incur tolls on the agency’s corridors and other expenses and amounts due to SJHTCA related to the agency’s customers who incur tolls on State Route 73. At June 30, 2014 and 2013, the agency had net payables to SJHTCA of \$5,102 and \$2,486, respectively.

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(l) Net Position

The agency's net position is classified within the following categories:

Invested in capital assets, net of related debt: Represents the agency's capital assets, net of accumulated depreciation and the outstanding principal balances of debt attributable to the acquisition, construction, and improvement of those assets.

Restricted: Represents the agency's assets subject to externally imposed conditions, related primarily to restricted bond proceeds and certain revenues collected, net of related liabilities.

Unrestricted: Represents the remainder of the agency's net position not included in the categories above.

(m) Use of Estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of certain assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(n) Comparative Data

Certain amounts reported in the prior year have been reclassified to conform to the current year presentation.

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(3) Development Impact Fees

The sources of development impact fees for the years ended June 30, 2014 and 2013 were as follows:

	<u>2014</u>	<u>2013</u>
City of Irvine	\$ 13,484	7,293
City of Lake Forest	2,512	537
City of Tustin	1,771	904
City of Mission Viejo	571	214
City of Yorba Linda	487	789
City of Anaheim	347	25
County of Orange	206	527
City of Rancho Santa Margarita	158	203
City of San Juan Capistrano	156	468
City of San Clemente	88	192
City of Santa Ana	29	629
City of Orange	4	8
City of Dana Point	—	5
	<u>\$ 19,813</u>	<u>11,794</u>

(4) Cash and Investments

Cash and investments as of June 30, 2014 and 2013 are classified in the accompanying financial statements as follows:

	<u>2014</u>	<u>2013</u>
Cash and investments	\$ 129,990	121,499
Current restricted cash and investments	132,797	102,478
Noncurrent restricted cash and investments	384,550	442,748
	<u>\$ 647,337</u>	<u>666,725</u>

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Cash and investments as of June 30, 2014 consist of the following:

	Cash and cash equivalents	Investments	Total
Cash on hand	\$ 1	—	1
Deposit accounts	19,640	994	20,634
Money market funds	3,220	—	3,220
Commercial paper	—	1,197	1,197
U.S. Treasury and RFCO securities	—	18,794	18,794
Federal agency securities	—	64,648	64,648
Corporate notes	—	27,594	27,594
State and local bonds	—	13,543	13,543
Investments held with trustee per debt agreements:			
Money market funds	36,935	—	36,935
Commercial paper	—	1,000	1,000
U.S. Treasury and RFCO securities	33,550	413,678	447,228
Federal agency securities	—	12,543	12,543
Total	<u>\$ 93,346</u>	<u>553,991</u>	<u>647,337</u>

Cash and investments as of June 30, 2013 consist of the following:

	Cash and cash equivalents	Investments	Total
Cash on hand	\$ 118	—	118
Deposit accounts	15,343	1,994	17,337
Money market funds	784	—	784
Commercial paper	3,499	19,059	22,558
Federal agency securities	—	98,157	98,157
Investments held with trustee per debt agreements:			
Money market funds	26,913	—	26,913
Commercial paper	—	8,612	8,612
U.S. Treasury and RFCO securities	20,966	246,489	267,455
Federal agency securities	—	118,347	118,347
Corporate notes	—	91,153	91,153
State and local bonds	—	15,291	15,291
Total	<u>\$ 67,623</u>	<u>599,102</u>	<u>666,725</u>

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(a) Cash Deposits

Custodial Credit Risk Related to Cash Deposits

Custodial credit risk for deposits is the risk that, in the event of failure of a depository financial institution, the agency will not be able to recover its deposits or will not be able to recover collateral securities that are in possession of an outside party.

At June 30, 2014 and 2013, the carrying amounts of the agency's cash deposits were \$19,640 and \$15,343, respectively, and the corresponding bank balances were \$21,296 and \$15,944, respectively. The differences of \$1,656 and \$601, respectively, were principally due to outstanding checks. The agency's custodial credit risk is mitigated in that the full amounts of the bank balances outlined above were insured by federal depository insurance or collateralized in accordance with Section 53652 of the California Government Code with securities held by the pledging financial institution in the agency's name.

(b) Investments

Credit Risk and Concentration of Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. Concentration of credit risk is the risk of loss attributed to the magnitude of an investment in a single issuer. The agency mitigates these risks by holding a diversified portfolio of high-quality investments. The agency's investment policy sets specific parameters by type of investment for credit quality, maximum maturity, and maximum percentage investment. Both the policy and the agency's debt agreements generally require that all securities must be issued by companies with a long-term debt rating of at least "A" by two of the Nationally Recognized Statistical Rating Organizations (NRSRO) or at least "AA" by one NRSRO. The policy also indicates specific rating requirements for certain types of investments. Further, there are percentage limitations on the purchase of specific types of securities, based on the purchase price of the security as compared to the market value of the total portfolio at the time of purchase. However, the policy does not require sales of individual securities due to subsequent changes in market value that cause their values to exceed the prescribed maximum percentages of the portfolio.

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The table below identifies the types of investments that are authorized by the agency's investment policy and certain provisions of the agency's policy that address interest rate risk and concentration of credit risk. This table does not address investments of debt proceeds held by the bond trustee, which are governed by the provisions of the agency's debt agreements rather than by the agency's investment policy.

Authorized investment type	Maximum maturity	Maximum percentage of portfolio*	Maximum percentage investment in one issuer	Specific rating requirement
U.S. Treasury bills, notes, and bonds	5 years	100	100	N/A
Federal agency and U.S. government-sponsored enterprise notes and bonds	5 years	100	35	N/A
Federal agency mortgage-backed securities	5 years	20	15	2nd highest ratings category by an NRSRO
Certificates of deposit	** 5 years	100	5	Long-term debt ratings in one of highest ratings categories by two NRSROs

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Authorized investment type	Maximum maturity	Maximum percentage of portfolio*	Maximum percentage investment in one issuer	Specific rating requirement
Negotiable certificates of deposit	5 years	30	5	Long-term debt ratings in one of highest ratings categories by two NRSROs
Bankers' acceptances	180 days	30	5	Drawn on and accepted by a bank that carries the highest short-term ratings category by one NRSRO
Commercial paper	270 days	25	Lesser of 5% of portfolio or 10% of outstanding paper of issuer	Highest short-term rating by a NRSRO
Repurchase agreements	90 days	25	5	N/A
Medium-term maturity corporate notes	5 years	30	5	Long-term debt rating in one of highest ratings categories by two NRSROs
State of California Local Agency Investment Fund	N/A	Lesser of \$50 million or 15% of portfolio	5	N/A
County or local agency investment pools	N/A	15	5	N/A

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<u>Authorized investment type</u>	<u>Maximum maturity</u>	<u>Maximum percentage of portfolio*</u>	<u>Maximum percentage investment in one issuer</u>	<u>Specific rating requirement</u>
Asset-backed securities	5 years	20	5	Highest rating by one NRSRO; issuer must also have one of the three highest ratings from two NRSROs
Shares in a California common law trust	N/A	20	5	Highest rating category by an NRSRO
Money market mutual funds	N/A	20	5	Highest applicable rating by two NRSROs
Bonds or notes issued by the State of California or by any local agency in the state	5 years	30	5	One of the three highest rating categories by at least two NRSROs
Bonds or notes issued by any state	5 years	30	5	One of the three highest rating categories by at least two NRSROs

* Excluding amounts held by trustee, which are subject to provisions of the bond indentures.

** The full amounts of principal and accrued interest must be insured by the Federal Deposit Insurance Corporation (FDIC) or the National Credit Union Administration (NCUA).

The investment of debt proceeds and toll revenues held by the agency's bond trustee is governed by provisions of the debt agreements, rather than by the general provisions of the California

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Government Code or the agency's investment policy. The following table identifies the investment types that are authorized for these funds, and if applicable, the specific rating requirements.

Investments authorized by debt agreements*	Specific rating requirement
U.S. Government obligations (including U.S. Treasury strips and RFCO strips)	N/A
U.S. Federal agency debt instruments	N/A
State and local government securities	One of the two highest rating categories by Moody's and S&P, and if rated by Fitch, in one of the two highest rating categories
Certificates of deposit insured by FDIC, Bank Insurance Fund (BIF), and Savings Association Insurance Fund (SAIF) or collateralized by U.S. government or federal agency obligations	N/A
Bankers' acceptances	Prime-1 or A3 or better by Moody's, A-1 or A or better by S&P and, if rated by Fitch, F-1 or A or better
Commercial paper	Prime-1 or better by Moody's and A-1 or better by S&P and, if rated by Fitch, F-1 or better
Repurchase agreements with terms up to 30 days, secured by U.S. government or federal agency obligations	A or better by both Moody's and S&P and, if rated by Fitch, A or better
Medium-term maturity corporate notes with maximum maturity of five years	One of the three highest applicable rating categories, or approved in writing, by S&P, and, if rated by Fitch, rated in one of the three highest applicable rating categories
Money market mutual funds	AAA-m-G, AAA-m, or AA-m by S&P and, if rated by Moody's, Aaa, Aa1, or Aa2 and, if rated by Fitch, AAA or AA
Investment agreements	N/A

* Other investments may be allowed if the agency certifies to the trustee that the investment was approved in writing by each rating agency, which has assigned a rating to the agency's bonds, and by the agency's bond insurer.

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At June 30, 2014 and 2013, all of the agency's investments were rated at or above the minimum levels required by its investment policy and its debt agreements, as shown below:

<u>Investment type</u>	<u>June 30, 2014</u>		<u>June 30, 2013</u>	
	<u>S&P</u>	<u>Moody's</u>	<u>S&P</u>	<u>Moody's</u>
U.S. Treasury bills	AA+	Aaa	AA+	Aaa
U.S. Treasury notes	AA+	Aaa	AA+	Aaa
U.S. Treasury strips	AA+	Aaa	AA+	Aaa
U.S. federal agency bonds	AA+	Aaa	AA+	Aaa
Money market funds	AAA _m	—	AAA _m	—
Commercial paper:				
ING	—	—	A-1	P-1
Union Bank	—	—	A-1	P-1
Abbey National LLC	—	—	A-1	P-1
Natixis	A-1	P-1	A-1	P-1
Corporate notes – Medium term:				
Bank of NY Mellon	A+	A1	A+	Aa3
Caterpillar	—	—	A-	A2
Metlife-Life Insurance Division	AA-	Aa3	AA-	Aa3
Metlife-Acquisition Financing Division	—	—	A-	A3
General Electric Capital	AA+	A1	AA+	A1
Coca Cola	—	—	AA-	Aa3
Target	—	—	A+	A2
Walmart	—	—	AA	Aa2
NY Life	AA+	Aaa	AA+	Aaa
Pepsi	—	—	A	A1
IBM	AA-	Aa3	AA-	Aa3
Toyota	—	—	A	Aa3
United Health Group	A	A3	—	—
State and local bonds:				
San Francisco Bay Area Toll Authority	AA	Aa3	AA-	Aa3
California State Revenue	A	Aa3	A	A1
Dallas Texas General Revenue	—	—	AA+	Aa1
Massachusetts State General Obligation	—	—	AA+	Aa1
New Mexico State	—	—	AAA	Aa1
New York State Development	AAA	Aa1	AAA	*
University of California Regents Revenue	AA	Aa2	AA	Aa1

* Rated AA by Fitch

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Custodial Credit Risk

Custodial credit risk for investments is the risk that the agency will not be able to recover the value of investment securities that are in the possession of an outside party. All securities owned by the agency are deposited in the agency's trustee bank with the exception of a money market account that is deposited in the agency's primary bank. Securities are not held in broker accounts.

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The agency mitigates this risk by matching maturity dates, to the extent possible, with the agency's expected cash flow.

A summary of the agency's investments held at June 30, 2014 that are governed by the agency's investment policy and its bond agreements, including money market funds of \$40,155 and U.S. Treasury securities of \$33,550 that are considered cash equivalents, is as follows:

Investment type	Fair value	Remaining maturity (in years)			
		Less than one	One to two	Two to five	More than five
U.S. Treasury notes	\$ 282,750	89,400	18,386	174,964	—
RFCO strips	118,270	8,988	8,939	25,769	74,574
Federal agency securities	77,191	20,847	26,520	29,824	—
U.S. Treasury bills	56,041	56,041	—	—	—
Money market funds	40,155	40,155	—	—	—
Corporate notes	27,594	16,444	5,008	6,142	—
State and local bonds	13,543	1,421	12,122	—	—
U.S. Treasury strips	8,961	—	—	—	8,961
Commercial paper	2,197	2,197	—	—	—
Certificates of deposit	994	—	994	—	—
Total	\$ 627,696	235,493	71,969	236,699	83,535

At June 30, 2014, with the exception of investments issued or explicitly guaranteed by the U.S. government (including instruments issued by the U.S. Resolution Funding Corporation, or RFCO) and money market mutual funds, there were no investments in any issuers that accounted for 5% or more of the agency's total investments, other than investments with Federal National Mortgage Association that represented 6% of the agency's total investments, as permitted by the agency's investment policy and the applicable bond indentures.

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A summary of the agency's investments held at June 30, 2013 that are governed by the agency's investment policy and its bond agreements, including money market funds of \$27,697, U.S. Treasury securities of \$20,966, and commercial paper of \$3,499 that are considered cash equivalents, is as follows:

Investment type	Fair value	Remaining maturity (in years)			
		Less than one	One to two	Two to five	More than five
Federal agency securities	\$ 216,504	68,540	86,744	61,220	—
RFCO strips	122,639	8,988	8,938	25,903	78,810
Corporate notes	91,153	37,324	39,524	14,305	—
U.S. Treasury notes	86,225	30,769	19,335	36,121	—
U.S. Treasury bills	50,143	50,143	—	—	—
Money market funds	27,697	27,697	—	—	—
Commercial paper	31,170	31,170	—	—	—
State and local bonds	15,291	2,933	5,920	6,438	—
U.S. Treasury strips	8,448	—	—	—	8,448
Certificates of deposit	1,994	—	—	1,994	—
Total	\$ 651,264	257,564	160,461	145,981	87,258

At June 30, 2013, with the exception of investments issued or explicitly guaranteed by the U.S. government (including instruments issued by the U.S. Resolution Funding Corporation, or RFCO) and money market mutual funds, there were no investments in any issuers that accounted for 5% or more of the agency's total investments, other than the following: Federal National Mortgage Association, Federal Home Loan Mortgage Corporation, Federal Farm Credit Bank, and Federal Home Loan Bank. Investments in these issuers represented 10%, 9%, 9%, and 6%, respectively, of the agency's total investments, as permitted by the agency's investment policy and the applicable bond indentures.

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(5) Capital Assets

Capital assets activity for the year ended June 30, 2014 was as follows:

	Balance at beginning of year	Additions	Transfers/ deletions	Balance at end of year
Construction in progress	\$ 339,854	19,345	(12,556)	346,643
Right-of-way acquisitions, grading, or improvements	15,014	—	—	15,014
Furniture and equipment	30,483	12,913	(4,044)	39,352
	<u>385,351</u>	<u>32,258</u>	<u>(16,600)</u>	<u>401,009</u>
Accumulated depreciation	<u>(17,999)</u>	<u>(2,277)</u>	<u>3,610</u>	<u>(16,666)</u>
	<u>\$ 367,352</u>	<u>29,981</u>	<u>(12,990)</u>	<u>384,343</u>

Capital assets activity for the year ended June 30, 2013 was as follows:

	Balance at beginning of year	Additions	Transfers/ deletions	Balance at end of year
Construction in progress	\$ 325,055	15,770	(971)	339,854
Right-of-way acquisitions, grading, or improvements	15,539	—	(525)	15,014
Furniture and equipment	31,295	1,328	(2,140)	30,483
	<u>371,889</u>	<u>17,098</u>	<u>(3,636)</u>	<u>385,351</u>
Accumulated depreciation	<u>(18,018)</u>	<u>(2,121)</u>	<u>2,140</u>	<u>(17,999)</u>
	<u>\$ 353,871</u>	<u>14,977</u>	<u>(1,496)</u>	<u>367,352</u>

Right-of-way acquisitions, grading, and improvements include easements and environmental mitigation parcels. Furniture and equipment include transponders, toll and violations collection equipment, tollbooths and buildings, vehicles, and leasehold improvements.

Transfers/Deletions

During the year ended June 30, 2014, the agency completed its All Electronic Tolling (AET) conversion project and expenditures of \$10,827 related to the installation of new toll equipment were transferred from construction in progress.

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Ownership of the Foothill/Eastern Transportation Corridor construction, rights-of-way, grading, and improvements was transferred to Caltrans during the year ended June 30, 1999 upon satisfaction of all conditions contained within the Cooperative Agreements between the agency and Caltrans. The agency incurs additional costs for improvements and enhancements to the thoroughfares previously transferred to Caltrans. These improvements and enhancements are covered by separate project-specific Cooperative Agreements with Caltrans. They are transferred to Caltrans on an ongoing basis and recognized as contribution expense; expenses of \$1,729 and \$971 were recognized during the years ended June 30, 2014 and 2013, respectively. The balance of construction in progress at June 30, 2014 represents additional capital improvements, primarily the 241 completion project, that will also be transferred to Caltrans upon completion.

(6) Long-Term Obligations

Following is a summary of changes in long-term obligations during the year ended June 30, 2014:

	Balance at beginning of year	Additions/ accretions	Reductions	Balance at end of year	Due within one year
Series 2013 Toll Road Refunding					
Revenue Bonds:					
Current interest bonds	\$ —	1,947,490	—	1,947,490	—
Capital appreciation bonds	—	135,083	—	135,083	—
Convertible capital appreciation bonds	—	201,770	—	201,770	—
Series 1999 Toll Road Refunding					
Revenue Bonds:					
Current interest bonds	696,375	—	(696,375)	—	—
Capital appreciation bonds	838,079	25,416	(863,495)	—	—
Convertible capital appreciation bonds	690,030	—	(690,030)	—	—
Series 1995A Senior Lien Toll Road Revenue Bonds:					
Current interest bonds	179,990	—	—	179,990	—
Total bonds payable	2,404,474	2,309,759	(2,249,900)	2,464,333	—
Less unamortized discount on 2013 bonds	—	(41,008)	194	(40,814)	
Total bonds payable less unamortized discount	\$ <u>2,404,474</u>	<u>2,268,751</u>	<u>(2,249,706)</u>	<u>2,423,519</u>	

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Following is a summary of changes in long-term obligations during the year ended June 30, 2013:

	<u>Balance at beginning of year</u>	<u>Additions/ accretions</u>	<u>Reductions</u>	<u>Balance at end of year</u>	<u>Due within one year</u>
Series 1999 Toll Road Refunding Revenue Bonds:					
Current interest bonds	\$ 712,080	—	(15,705)	696,375	25,160
Capital appreciation bonds	789,923	48,156	—	838,079	—
Convertible capital appreciation bonds	690,030	—	—	690,030	—
Series 1995A (fixed rate) Senior Lien Toll Road Revenue Bonds:					
Current interest bonds	<u>179,990</u>	<u>—</u>	<u>—</u>	<u>179,990</u>	<u>—</u>
Total bonds payable	<u>\$ 2,372,023</u>	<u>48,156</u>	<u>(15,705)</u>	<u>2,404,474</u>	<u>25,160</u>

Toll Road Revenue Bonds

The 1995 Unrefunded Bonds are current interest bonds. Interest on the bonds is payable semiannually at a rate of 5.00% and is capitalized through January 1, 2032. The bonds are scheduled to mature on January 1, 2035. However, the bonds are subject to early redemption, at the option of the agency, beginning January 1, 2005 by payment of accrued interest and principal with no premium. Further, as a condition of the 2013 bond refunding transaction described below, the agency has covenanted to redeem the bonds in the principal amounts of \$50,720, \$59,765, and \$69,505 on January 1, 2033, 2034, and 2035, respectively.

In August 1999, the agency issued serial, term, and capital appreciation toll road refunding revenue bonds (1999 Bonds) in the aggregate principal amount of \$1,588,144 consisting of current interest bonds in the principal amount of \$831,965, convertible capital appreciation bonds in the principal amount of \$388,223, and capital appreciation bonds in the principal amount of \$367,956. The 1999 Bonds have been subordinate to the remaining 1995 Unrefunded Bonds of \$179,990 and have been collateralized by net revenues, as defined in the master indentures, consisting primarily of toll revenues less current expenses.

Interest on the 1999 current interest bonds has been payable semiannually at rates ranging from 4.38% to 5.75%. The bonds have been scheduled to mature in annual installments through January 15, 2040. The bonds have been subject to early redemption, at the option of the agency, by payment of accrued interest, principal, and a premium of up to 1.00%.

The 1999 capital appreciation bonds have accrued interest at rates ranging from 5.63% to 6.09%, compounded semiannually, and have been scheduled to mature in annual installments from January 15, 2017 to January 15, 2038. The bonds have been subject to early redemption, at the option of the agency, by payment of accrued interest, principal, and a premium of up to 2.00%.

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(In thousands)

The 1999 convertible capital appreciation bonds have accrued interest, payable semiannually based on accreted amounts, at rates ranging from 5.80% to 5.88% compounded semiannually. The bonds have been scheduled to mature in annual installments from January 15, 2020 to January 15, 2029. The bonds have been subject to early redemption, at the option of the agency, beginning January 15, 2014 by payment of accrued interest, principal, and a premium of up to 1.00%.

In December 2013, the agency issued \$2,274,617 of Series 2013 Toll Road Refunding Revenue Bonds (2013 Bonds); the proceeds of the issuance were used to refund the outstanding balance of the 1999 Bonds. As a result of this transaction, the ultimate maturity of the agency's long-term debt obligations has been extended from 2040 to 2053. The reacquisition price of the refunded bonds exceeded their net carrying amount by \$14,534; this amount is considered a deferred loss for accounting purposes, and is being amortized through 2040, the remaining period during which the refunded bonds were scheduled to be repaid. In addition, the agency incurred bond insurance premiums of \$9,533, which is being amortized over the life of the 2013 bonds, and other transaction costs of \$20,890, which has been recorded as expense. The 2013 Bonds were issued at a discount of \$41,009, which is being amortized over the life of the bonds. The agency's total scheduled debt service payments increased by approximately \$1,831,885, resulting in an economic loss (as measured by the difference in present value of the scheduled debt service payments on the old and new debt) of approximately \$61,097.

The 2013 current interest bonds include \$1,374,440 of Senior Term Bonds that mature in installments from January 2042 through January 2053; \$375,000 of Term Rate Bonds that mature in installments from January 2050 through January 2053; and \$198,050 of Junior Lien Bonds that mature in installments from January 2023 through January 2043. Interest on the 2013 current interest bonds is payable semiannually at rates ranging from 5.00% to 6.50%. The Senior Term Bonds and the Junior Lien Bonds are subject to early redemption on or after January 15, 2024, at the option of the agency, by payment of principal and accrued interest. The Term Rate Bonds are subject to early redemption, at the option of the agency, by payment of principal and accrued interest, on or after the dates ranging from July 15, 2017 through July 15, 2022.

The 2013 capital appreciation bonds accrue interest at rates ranging from 3.75% to 7.125%, compounded semiannually, and are scheduled to mature in annual installments from January 2020 to January 2042. The bonds are subject to early redemption, at the option of the agency, based on an independent make-whole calculation.

The 2013 convertible capital appreciation bonds accrue interest, compounded semiannually based on accreted amounts, at rates ranging from 5.30% to 6.85% through January 15, 2024. After this date, interest is payable semiannually based on accreted amounts. The bonds are scheduled to mature in annual installments from January 2025 to January 2042. The bonds are subject to early redemption on or after January 15, 2031, at the option of the agency, by payment of the accreted amounts and accrued interest.

The master indentures of trust require the trustee to hold bond proceeds, toll revenues, and any other proceeds included in pledged funds for debt service. These moneys are included in the restricted cash and investments held by the trustee. The pledge of toll revenues for payment of the 2013 bonds is subject to prior lien in favor of the 1995 Bonds.

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June 30, 2014 and 2013

(In thousands)

Following is a summary of the annual debt service requirements by fiscal year for the agency's long-term debt obligations as of June 30, 2014:

	<u>Principal</u>	<u>Interest⁽¹⁾</u>	<u>Total</u>
2015	\$ —	121,770	121,770
2016	—	121,770	121,770
2017	—	121,770	121,770
2018	—	121,770	121,770
2019	—	121,770	121,770
2020–2024	39,253	634,744	673,997
2025–2029	60,458	738,441	798,899
2030–2034	116,511	711,008	827,519
2035–2039	357,765	837,351	1,195,116
2040–2044	433,792	678,833	1,112,625
2045–2049	715,860	315,252	1,031,112
2050–2053	740,694	84,200	824,894
	<u>\$ 2,464,333</u>	<u>4,608,679</u>	<u>7,073,012</u>

⁽¹⁾ Includes payments scheduled on January 1 and January 15 of the indicated fiscal year and July 1 and July 15 of the following fiscal year, to coincide with the annual debt service calculations used for covenant compliance purposes.

Following is a summary of the annual debt service requirements by fiscal year for the agency's long-term debt obligations as of June 30, 2013:

	<u>Principal</u>	<u>Interest⁽¹⁾</u>	<u>Total</u>
2014	\$ 25,160	87,918	113,078
2015	30,205	86,452	116,657
2016	42,990	84,579	127,569
2017	40,081	92,213	132,294
2018	44,693	96,371	141,064
2019–2023	344,407	455,514	799,921
2024–2028	492,391	461,514	953,905
2029–2033	419,321	699,969	1,119,290
2034–2038	421,406	874,246	1,295,652
2039–2040	543,820	32,284	576,104
	<u>\$ 2,404,474</u>	<u>2,971,060</u>	<u>5,375,534</u>

⁽¹⁾ Includes payments scheduled on January 1 and January 15 of the indicated fiscal year and July 1 and July 15 of the following fiscal year, to coincide with the annual debt service calculations used for covenant compliance purposes.

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Included in principal at June 30, 2014 and 2013 is \$9,726 and \$771,930, respectively, related to accreted principal on convertible capital appreciation bonds and capital appreciation bonds.

The net proceeds of the 1999 Bonds plus additional 1995 series moneys were used to purchase U.S. government securities, which were placed in an irrevocable escrow fund to be used for the debt service payments related to a previously refunded portion of the 1995 bonds. As of June 30, 2014 and 2013, the amounts of the previously refunded 1995 bonds outstanding, which were previously eliminated from the financial statements as a result of the refunding, were \$751,498 and \$706,471, respectively.

(7) Commitments and Contingencies

(a) Toll Collection and Revenue Management System Agreements

The agency and SJHTCA have entered into agreements with various contractors for customer service center operations, hardware maintenance, toll collection systems operation and maintenance, and violation processing. The agreements expire on various dates through October 31, 2015 and are cancelable by the agency, without further obligation, upon written notice, generally within 90 days.

(b) Project Costs

As of June 30, 2014, the agency has outstanding commitments and contracts for improvements on existing construction of approximately \$33,119.

(c) Litigation

The agency is a defendant in various legal actions. Management believes that the ultimate resolution of these actions will not have a significant effect on the agency's financial position or results of operations.

(d) Risk Management

The agency maintains insurance coverage for various risks, including but not limited to property, liability, earthquake, and flood coverage. Coverage is purchased at levels in accordance with the agency's master indentures of trust.

(e) Mitigation Payment and Loan Agreement

On November 10, 2005, the agency's Board of Directors and the Board of Directors of the SJHTCA, entered into a Mitigation Payment and Loan Agreement (the Agreement). The terms of the Agreement called for the agency to make payments totaling \$120,000 over four years to the SJHTCA to mitigate for anticipated loss of revenue due to the construction of the 241 completion project. All scheduled payments totaling \$120,000 were made to the SJHTCA as of June 2009.

In addition, the agency committed to provide loans to SJHTCA on an as-needed basis up to \$1,040,000, subject to the terms of the Agreement, to assist SJHTCA in achieving its required debt service coverage ratio of 1.3x. The Agreement was amended on March 1, 2011 to reflect the modification of the SJHTCA's debt service coverage ratio from 1.3x to 1.0x. The Agreement

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provides that the agency loans will be made only to the extent that surplus revenues are available and all findings and determinations required by law are met, including California Government Code Section 66484.3, paragraph (f), which requires that the following findings must be met before the agency can make a loan: 1) the agency will benefit mutually financially by sharing and/or loaning revenues with SJHTCA, 2) the agency possesses adequate financial resources to fund all costs of construction of existing and future projects that it plans to undertake prior to the final maturity of the loan, and 3) the funding of the loan will not materially impair its financial condition or operations during the term of the loan. The Agreement also stipulates that the agency will not be obligated to make loans to SJHTCA prior to securing the necessary funds for constructing the 241 completion project unless the agency has determined that it will not build the project. The agency is also not required to increase toll rates to ensure sufficient revenues are available. Further, any liens or revenue pledges required in order to finance the 241 completion project and certain other capital projects would have priority over loans to the SJHTCA. If the commencement and diligent pursuit of the construction of the 241 completion project does not occur by December 31, 2015, the mitigation payments will be added to the principal of the loan. Accrued interest will not count toward the \$1,040,000 principal limitation. Payments of accrued interest and outstanding principal will begin in the fiscal year when SJHTCA has a surplus in revenues that exceeds the amount needed to meet the debt coverage requirement. All principal and accrued interest will be due and payable on January 1, 2037 to the extent that SJHTCA has surplus revenues available to pay all amounts due. At June 30, 2014 and 2013, no amounts were outstanding on the loan.

On August 14, 2014, the agency's Board of Directors and the Board of Directors of SJHTCA approved an agreement that would provide for termination of the Mitigation Payment and Loan Agreement concurrently with the closing of a refinance transaction proposed by SJHTCA. If the transaction does not close by July 1, 2015, the Agreement would not be terminated. The termination agreement also provides for SJHTCA to pay \$120,000 to the agency, in annual installments beginning January 15, 2025 equal to 50% of SJHTCA's Surplus Funds. Interest accrual based on the average annual yield of the State of California Pooled Money Investment Account would commence upon closing of the refinance transaction and interest would be payable annually beginning January 15, 2025.

(8) Corridor Operations Facility Lease

In January 2000, the agency, along with SJHTCA, relocated to the Corridor Operations Facility. At that time, a lease agreement was executed between the agency (lessor) and SJHTCA (lessee). The lease agreement expires at the earliest occurrence of 1) dissolution of the agency, 2) sale of the facility, or 3) dissolution of SJHTCA. Lease payments are based on the estimated fair market rental value and are adjusted annually. The agency received lease revenue for the years ended June 30, 2014 and 2013 of \$361 and \$352, respectively.

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(9) Employees' Retirement Plan

The agency's employees participate in the Orange County Employees Retirement System (OCERS), a cost-sharing multiple-employer public employee retirement system established in 1945. OCERS provides for retirement, death, disability, and cost-of-living benefits and is subject to the provisions of the County Employees Retirement Law of 1937 and other applicable statutes. OCERS issues a publicly available financial report that includes financial statements and required supplementary information for the cost-sharing plans that are administered by OCERS. This report can be obtained from OCERS at 2223 Wellington Avenue, Santa Ana, CA 92701.

Plan members contribute a percentage of their annual covered salaries at actuarially determined rates based on the age of entry into the plan. For employees who were hired prior to January 1, 2013, the agency paid up to 7% of each employee's required contribution through June 30, 2013. However, this percentage was reduced to 4.5% as of July 1, 2013, and to 2.0% as of July 1, 2014. At July 1, 2015, a final 2% reduction will occur, resulting in no payment by the agency toward the employees' required contributions. The agency also makes required employer contributions, as a percentage of each employee's covered salary, which will continue to be paid into the plan. The agency has contributed \$872, \$773, \$766, and \$800 to the plan for the years ended June 30, 2014, 2013, 2012, and 2011, respectively.