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FOOTHILL/EASTERN TRANSPORTATION CORRIDOR AGENCY

Financial Statements

June 30, 2011

(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:

We have audited the accompanying financial statements of Foothill/Eastern Transportation Corridor Agency (the agency) as of and for the year ended June 30, 2011, as listed in the table of contents. These financial statements are the responsibility of the Foothill/Eastern Transportation Corridor Agency's management. 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 of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Foothill/Eastern Transportation Corridor Agency's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Foothill/Eastern Transportation Corridor Agency as of June 30, 2011, and the changes in its financial position and its cash flows for the year then ended, in conformity with U.S. generally accepted accounting principles.

The management's discussion and analysis on pages 2 through 7 is not a required part of the basic financial statements, but is supplementary information required by U.S. generally accepted accounting principles. We have applied certain limited procedures, which consisted principally of inquiries of management, regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

KPMG LLP

September 19, 2011

This discussion and analysis of the Foothill/Eastern Transportation Corridor Agency's (the agency) financial performance provides an overview of the agency's financial activities for the fiscal year ended June 30, 2011. 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. 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.

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. Today, approximately 178,000 transactions are 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

Tolls, fees, and fines collected in fiscal year 2011 (FY11) totaled $114,715 compared to $113,623 in the prior fiscal year, an increase of 1.0%.

Interest and principal payments of $90,200 and $4,540, respectively, on the agency's long-term debt were made in FY11 compared to $70,513 and $10,300, respectively, in the prior fiscal year. Accrual basis interest was $90,092 in FY11 compared to $90,471 in the prior fiscal year, and accretion on the agency's capital appreciation bonds and convertible capital appreciation bonds totaled $42,780 in FY11, compared to $41,947 in the prior fiscal year.

As of June 30, 2011, the agency had $538,801 in restricted cash and investments governed under the 1995 and 1999 master indentures of trust. The agency also had $103,525 in unrestricted cash.

(Continued)

Total net deficit at June 30, 2011 was $(1,410,416) compared to $(1,378,798) in the prior fiscal year. The deficit results primarily from the recording of long-term debt, proceeds of which funded the construction of the corridors. Ownership was transferred to Caltrans upon completion. The net deficit is also a result of accretion recorded on the capital appreciation bonds, which was greater than principal payments made.

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the agency's financial statements, which comprise the statement of net deficit, statement of revenues, expenses, and changes in net deficit, statement of cash flows, and notes to 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 all recordable assets of the agency as well as all liabilities. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid. The statement of cash flows provides 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 statement of net deficit and the statement of revenues, expenses, and changes in net deficit report the agency's net deficit and related changes in them. Net deficit 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, all of the agency's construction-related activities, including the design, construction, and mitigation on the Foothill/Eastern Transportation Corridors, as well as all financing and administration costs, are reflected in the statements. The activities are financed by toll revenues, development impact fees, fees and fines, and investment income.

(Continued)

(In thousands)

Financial Analysis

The following table summarizes the assets, liabilities, and net deficit for the agency as of June 30, 2011 and 2010:

		2011	2010	Percentage increase (decrease)
Assets:				
Current assets	$	202,757	183,806	10.3%
Capital assets, net		344,116	350,176	(1.7)
Other noncurrent assets		446,174	452,389	(1.4)
Total assets		993,047	986,371	0.7
Liabilities:				
Bonds payable		2,338,023	2,299,783	1.7
Other liabilities		65,440	65,386	0.1
Total liabilities		2,403,463	2,365,169	1.6
Total net deficit	$	(1,410,416)	(1,378,798)	2.3

The purpose of the agency is to plan, finance, design, and construct the remaining portions of the corridor system and to operate and collect tolls from the patrons of the corridors to extinguish the related long-term bond debt. The debt, issued in the form of tax-exempt bonds, was issued initially to construct the toll roads. Subsequent to completion, the roads were transferred to Caltrans. The net deficit results primarily from using bond proceeds to construct the corridors, which were then contributed to Caltrans, and from the accretion of interest on the outstanding bonds.

Current assets have increased this year mainly due to higher development income fee revenue collected during the year and an increase in investments that are considered current rather than noncurrent.

Capital assets, net have decreased as a result of the completion and transfer to Caltrans of the Windy Ridge capital improvement project offset by additions to construction in progress related to the preliminary design and environmental planning costs associated with the 241 completion project.

The increase in bonds payable results from the current year accretion on the capital appreciation bonds totaling $42,780 offset by a principal payment of $4,540.

(Continued)

(In thousands)

The following is a summary of the agency's revenues, expenses, and changes in net deficit for the years ended June 30, 2011 and 2010:

	2011	2010	Percentage increase (decrease)
Operating revenues:			
Tolls, fees, and fines	$ 114,715	113,623	1.0%
Development impact fees	11,613	4,254	173.0
Other revenue	601	835	(28.0)
Total operating revenues	126,929	118,712	6.9
Operating expenses	35,290	24,043	46.8
Operating income	91,639	94,669	(3.2)
Nonoperating expenses, net	(123,257)	(105,371)	17.0
Change in net deficit	(31,618)	(10,702)	195.4
Net deficit at beginning of year	(1,378,798)	(1,368,096)	0.8
Net deficit at end of year	$ (1,410,416)	(1,378,798)	2.3

Revenues for the agency consist primarily of tolls, fees, and fines, which comprised 90.4% of total revenue in FY11 compared to 95.7% of total revenue in fiscal year 2010 (FY10). Tolls, fees, and fines increased 1.0% over the prior year primarily due to an increase in fee and fine collections and a slightly higher average toll per transaction realized in FY11. Development impact fees were $11,613 in FY11 compared to $4,254 in FY10, an increase of 173.0%. This increase is directly related to an upturn in residential and nonresidential development in several cities in Orange County within the area of benefit of the Foothill/Eastern Transportation Corridor.

Operating expenses were $35,290 in FY11 compared to $24,043 in FY10, an increase of 46.8%. This increase is due to the noncash expense for the contribution of capital assets to Caltrans related to the completion of the Windy Ridge capital improvement project. Also included in operating expenses is the noncash expense of depreciation on fixed assets of $3,034 compared to $3,418 in FY10. Operating expenses excluding contributions and depreciation decreased $341 from $19,750 in FY10 to $19,409 in FY11.

Nonoperating expenses, net consist of investment income of $9,497 and a net settlement expense recovery of $118 in connection with settling a lawsuit related to the agency's toll violation process, offset by interest expense of $132,872. For FY10, nonoperating expenses, net consist of investment income of $27,185, offset by interest expense of $132,418, amortization of $62, and settlement expense of $76. The decrease in investment income of $17,688 can be attributed to lower yields earned on investments. Interest expense comprises both interest payments and the change in accrued interest on long-term debt and accretion of bonds outstanding. Amortization represents capitalized bond issuance costs associated with the fixed rate Subordinate Lien Toll Road Revenue Bonds, Series 2007. The agency exercised the early redemption option of these bonds on January 15, 2010.

(In thousands)

Capital Assets, Net

The following table summarizes the capital assets, net of depreciation, at June 30:

		2011	2010
Construction in progress	$	313,877	318,157
Right-of-way acquisitions, grading, or improvements		15,539	15,539
Furniture and equipment		14,700	16,480
Total capital assets	$	344,116	350,176

Construction in progress at June 30, 2011 primarily represents 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 include 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 has outstanding bonds payable of $2,338,023 at June 30, 2011, an increase from the prior year of $38,240 due to the accretion of principal on capital appreciation bonds of $42,780, offset by a principal payment of $4,540. All of the agency's toll revenue, less certain expenses, as defined in the indentures of trust, is pledged to repay these bonds. There were no changes to the debt structure during FY11.

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 year ended June 30, 2011.

While tolls, fees, and fines revenue increased during FY11 and the agency continues to pay its operating costs and debt service, the agency made a proactive step in April 2009 to ensure that it met its required coverage ratio of 1.3x annual debt service in current and future years by establishing an escrow defeasance fund. Available surplus funds that are deposited with the trustee into the escrow fund can be used instead of toll revenues to pay debt service to assure that the debt service coverage ratio is met should revenues decline. During FY11, $13,500 was transferred into the escrow defeasance fund and used to pay debt service.

Economic Factors

The agency continues to operate in a fiscally conservative manner by reducing costs and spending resources only on the most important programs to keep its systems in a state of good repair.

The agency is also continuing to focus on customer incentives and promotions to maintain and build transactions and revenue and continued to offer quarterly promotions to attract new drivers and reward current customers throughout the year, including its "Drive-a-Week Free" campaign, "Refer-a-Friend" program, and monthly drawings for $1,000 in free tolls to accountholders who signed up to receive a chance to win each time they used the road.

Based on economic conditions, specifically the high unemployment rate in Southern California, the agency did not implement toll rate increases for FY11. However, toll rate increases were implemented for FY12 at all locations by $0.25 for cash transactions and 5%, rounded to the nearest $0.05, for FasTrak transactions.

The agency is focused on the 241 completion project. The project includes the completion of the State Route 241 Toll Road south from its current end near Rancho Santa Margarita and Mission Viejo to the I-5 Freeway near San Clemente. During fiscal year 2006, the agency's Board of Directors certified the Environmental Impact Statement/Supplemental Environmental Impact Report and selected a locally preferred Foothill-South alignment. In February 2008, the California Coastal Commission denied the approval of this alignment, and under the federal Coastal Zone Management Act, the agency filed an appeal of this decision with the U.S. Secretary of Commerce, which sustained the Coastal Commission decision in December 2008. The agency is continuing to pursue options for the 241 completion and has focused outreach at the state, local, and federal level to develop an acceptable alignment.

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 request for additional financial information should be addressed to the Controller, Foothill/Eastern Transportation Corridor Agency, 125 Pacifica, Suite 100, Irvine, California 92618 or to http://www.thetollroads.com.

FOOTHILL/EASTERN TRANSPORTATION CORRIDOR AGENCY

Statement of Net Deficit

June 30, 2011

(In thousands)

Assets		
Current assets:		
Cash and investments	$	103,525
Restricted cash and investments		92,627
Receivables:		
Accounts, net of allowance of $859		1,505
Fees		23
Interest		2,866
Total receivables		4,394
Due from San Joaquin Hills Transportation Corridor Agency		863
Other assets		1,348
Total current assets		202,757
Noncurrent assets:		
Restricted cash and investments		446,174
Capital assets, net		344,116
Total assets		993,047
Liabilities		
Current liabilities:		
Accounts payable		4,451
Deferred revenue		12,626
Due to San Joaquin Hills Transportation Corridor Agency		2,930
Employee compensated absences payable		441
Interest payable		44,992
Current portion of bonds payable		11,390
Total current liabilities		76,830
Long-term bonds payable		2,326,633
Total liabilities		2,403,463
Net Deficit		
Invested in capital assets, net of related debt		(1,993,907)
Restricted		479,966
Unrestricted		103,525
Total net deficit	$	(1,410,416)

See accompanying notes to financial statements.

FOOTHILL/EASTERN TRANSPORTATION CORRIDOR AGENCY

Statement of Revenues, Expenses, and Changes in Net Deficit

Year ended June 30, 2011

(In thousands)

Operating revenues:		
Tolls, fees, and fines	$	114,715
Development impact fees		11,613
Other revenues		601
Total operating revenues		126,929
Operating expenses:		
Contribution of capital improvements to Caltrans		12,847
Toll compliance and customer service		7,233
Salaries and wages		3,332
Toll systems		3,128
Depreciation		3,034
Toll collections		2,151
Marketing		1,030
Toll facilities		918
Insurance		708
Professional services		337
Facilities operations, maintenance, and repairs		187
Other operating expenses		385
Total operating expenses		35,290
Operating income		91,639
Nonoperating revenue (expenses):		
Investment income		9,497
Interest expense		(132,872)
Settlement expense recovery, net		118
Nonoperating expenses, net		(123,257)
Change in net deficit		(31,618)
Net deficit at beginning of year		(1,378,798)
Net deficit at end of year	$	(1,410,416)

See accompanying notes to financial statements.

FOOTHILL/EASTERN TRANSPORTATION
CORRIDOR AGENCY

Statement of Cash Flows

Year ended June 30, 2011

(In thousands)

Cash flows from operating activities:		
Cash received from toll road patrons	$	114,197
Cash received from development impact fees		11,604
Cash received from property rental		411
Cash received from miscellaneous revenue sources		161
Cash received from grant revenue		30
Cash payments to suppliers		(15,429)
Cash payments to employees		(3,527)
Net cash provided by operating activities		107,447
Cash flows from capital and related financing activities:		
Cash received for settlement expense recovery, net		118
Cash payments for equipment		(1,037)
Cash payments for construction in progress		(8,807)
Cash payments for interest and principal		(94,740)
Net cash used in capital and related financing activities		(104,466)
Cash flows from investing activities:		
Cash received from interest, net of realized gains and losses		12,753
Cash payments for purchase of investments		(235,951)
Cash received from the maturity and sale of investments		249,837
Net cash provided by investing activities		26,639
Net increase in cash and cash equivalents		29,620
Cash and cash equivalents at beginning of year		55,988
Cash and cash equivalents at end of year (note 4)	$	85,608
Reconciliation of operating income to net cash provided by operating activities:		
Operating income	$	91,639
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation		3,034
Contribution of capital improvements to Caltrans		12,847
Changes in operating assets and liabilities:		
Accounts receivable		(400)
Fees receivable		(9)
Accounts payable, less accounts payable for fixed assets and construction in progress		471
Deferred revenue		(178)
Due from San Joaquin Hills Transportation Corridor Agency		5
Due to San Joaquin Hills Transportation Corridor Agency		56
Other assets		47
Employee compensated absences payable		(65)
Total adjustments		15,808
Net cash provided by operating activities	$	107,447
Noncash transactions:		
Interest expense recorded for accretion of bonds outstanding	$	(42,780)
Unrealized loss on investments		(3,113)
Amortization of discount/premium on investments		179

See accompanying notes to financial statements.

(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, including thoroughfares and bridges. 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.

These 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 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 contribution expense, 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. As provided in GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That*

Use Proprietary Fund Accounting, the agency does not apply Financial Accounting Standards Board pronouncements issued after November 30, 1989.

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. generally accepted accounting principles. 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 in U.S. government securities, federal agency securities and corporate notes are carried at fair value based on quoted market prices. Commercial paper is carried at amortized cost (which approximates fair value). Treasury mutual funds are carried at fair value based on the fund's share price.

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, which are valued in total, and an estimated useful life in excess of one year. Such assets are recorded at cost.

The Foothill/Eastern Transportation Corridors and the related purchases of right-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 such assets or right-of-way. The costs of normal maintenance and repairs and mitigation that do not add value to the asset or materially extend asset lives are not capitalized.

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

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

Asset type	Useful life
Toll booths and buildings	28 – 30 years
Changeable message signs	15 years
Toll revenue equipment	5 years
Vehicles	5 years
Other equipment and furniture	3 – 5 years

(h) Deferred Revenue

Deferred revenue represents prepaid tolls collected from patrons using FasTrak®, an electronic toll collection system that allows drivers to pay tolls without stopping at a toll booth.

(i) Revenue Recognition

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

(j) Allocation of Common Costs

Expenses directly related to the agency were charged entirely to the agency, and those incurred on behalf of both the agency and SJHTCA were allocated between the two agencies based on the estimated benefit to each. In addition, the agency also has amounts due from SJHTCA related to SJHTCA FasTrak customers incurring tolls on the agency's corridors and other expenses and has amounts due to SJHTCA related to the agency's FasTrak customers incurring tolls on State Route 73. At June 30, 2011, the agency has a net payable due to SJHTCA of $2,067 for such items.

(In thousands)

(k) Net Assets

The agency's net assets are classified into the following net asset categories:

Invested in Capital Assets, Net of Related Debt: Capital assets, net of accumulated depreciation and outstanding principal balances of debt attributable to the acquisition, construction, and improvement of those assets and assets contributed to Caltrans.

Restricted: Net assets subject to externally imposed conditions that can be fulfilled by the actions of the agency or by the passage of time. These net assets relate primarily to restricted bond proceeds and certain revenues collected.

Unrestricted: All other categories of net assets.

(l) Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles 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.

(3) Development Impact Fees

The sources of development impact fees were the following for the year ended June 30, 2011:

City of Irvine	$	9,001
City of San Clemente		996
City of Tustin		579
City of Yorba Linda		463
City of Santa Ana		250
City of Orange		99
City of Lake Forest		93
City of Mission Viejo		63
County of Orange		51
City of Anaheim		9
City of San Juan Capistrano		5
City of Rancho Santa Margarita		4
	$	11,613

(In thousands)

(4) Cash and Investments

Cash and investments as of June 30, 2011 are classified in the accompanying financial statements as follows:

Cash and investments	$	103,525
Current restricted cash and investments		92,627
Noncurrent restricted cash and investments		446,174
	$	642,326

Cash and investments as of June 30, 2011 consist of the following:

		Cash and cash equivalents	Investments	Total
Cash on hand	$	118	—	118
Demand deposits		14,866	—	14,866
Money market		50,524	—	50,524
Commercial paper		—	17,979	17,979
Federal agency securities		—	62,861	62,861
Investments held with trustee per debt agreements		20,100	475,878	495,978
Total	$	85,608	556,718	642,326

(a) Cash Deposits

Custodial Credit Risk Related to Cash Deposits

The custodial credit risk for deposits is the risk that the agency will not be able to recover deposits or will not be able to recover collateral securities that are in possession of an outside party. This risk is mitigated in that, of the total cash balance, $118 was cash on hand, and $14,866 was insured by federal depository insurance and collateralized in accordance with Section 53652 of the California Government Code with securities held by the pledging financial institution in the agency's name.

At June 30, 2011, the carrying amount of the agency's cash deposits was $14,866 and the corresponding bank balance was $15,268. The difference of $402 was principally due to outstanding checks. The agency's petty cash fund and toll change funds totaled $118.

(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, maturity length, and maximum percentage investment. Both the policy and the agency's debt agreements state that, generally, all securities must be issued by companies with a long-term debt rating of at least "A" by two of the Nationally Recognized Rating Agencies (NRRA) or at least "AA" by one NRRA. The policy also indicates specific rating requirements for certain types of investments. Percentage limitations on specific types of securities are based on the purchase price of the security, as compared to the market value of the portfolio, at the time of purchase. The policy does not require sales in a portfolio for subsequent changes in market value of the total portfolio to avoid exceeding the prescribed allocation level.

(In thousands)

The table below identifies the investment types that are authorized by the agency's investment policy. The table also identifies certain provisions of the agency's investment policy that addresses interest rate risk and concentration of credit risk. This table does not address investments of debt proceeds held by bond trustee that are governed by the provisions of debt agreements of the agency, rather than by the general provisions of 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	25	N/A
Federal agency mortgage-backed securities	5 years	20	20	N/A
Negotiable certificates of deposit	5 years	30	30	"AA" or better by two NRRAs
Banker's acceptances	180 days	30	25	Drawn on and accepted by a bank that is rated "AA" or better by two NRRAs
Commercial paper	270 days	15	10% of outstanding paper of an issuing corporation	P1, A1, F1, or D1 by two NRRAs

(In thousands)

Authorized investment type	Maximum maturity	Maximum percentage of portfolio*	Maximum percentage investment in one issuer	Specific rating requirement
Repurchase agreements	90 days	25	25	N/A
Reverse repurchase agreements	30 days	10	10	N/A
Medium-term maturity corporate notes	5 years	30	30	N/A
State of California Local Agency Investment Fund	N/A	15	15	N/A
County or local agency investment pools	N/A	15	15	N/A
Asset-backed securities	5 years	20	20	"AAA" by one NRRA; issuer must have underlying rating of "A" or better from two NRRAs
Shares in a California common law trust	N/A	None	None	N/A
Money market mutual funds	N/A	15	15	N/A
Investment agreements	10 years	40	40	N/A
Bonds or notes issued by any municipality in the State of California	5 years	30	30	One of the two highest rating categories by Moody's and Standard & Poor's (S&P), and if rated by Fitch, in one of the two highest rating categories

Authorized investment type	Maximum maturity	Maximum percentage of portfolio*	Maximum investment in one issuer	Specific rating requirement
Bonds or notes issued by any state	5 years	30	30	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

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

At June 30, 2011, 5% or more of the agency's investments were in the U.S. Resolution Funding Corporation (RFCO), the Federal Home Loan Mortgage Corporation, the Federal National Mortgage Association, and the Federal Home Loan Bank as authorized by the agency's investment policy. These investments are 20%, 16%, 12%, and 11%, respectively, of the agency's total investments.

Investment of debt proceeds and toll revenues held by the agency's trustee are governed by provisions of the debt agreements, rather than by the general provisions of the California Government Code or the agency's investment policy. The following table identifies the investment types that are authorized for these moneys, and if noted, the specific rating requirements.

Investments authorized by debt agreements*	Specific rating requirement
Government obligations (including U.S. Treasury strips and RFCO strips)	N/A
Federal agency debt instruments	N/A
Municipal 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
Negotiable certificates of deposit insured by FDIC, BIF, and SAIF or secured by government obligations	Two highest ratings by two NRRAs
Banker's 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	A or better by both Moody's and S&P and, if rated by Fitch, A or better
Medium-term maturity corporate notes	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	AAAm-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.

(In thousands)

At June 30, 2011, all of the agency's investments held were rated at or above the minimum required rating per the agency's investment policy and debt agreements: the federal agency securities, U.S. Treasury bills, U.S. Treasury notes, and U.S. Treasury strips that were held by the agency were rated AAA by S&P and AAA by Moody's; the RFCO strips were rated AAA by Moody's; commercial paper was rated A-1+ by S&P and P1 by Moody's; the money market funds were rated AAA by S&P, and the medium-term corporate notes were rated Aaa by Moody's and AA+ by S&P.

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, which 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 governed by both the agency's investment policy and its bond agreements, including money market funds of $50,524, and investments held with trustee of $20,100 that are considered cash equivalents held at June 30, 2011, is as follows:

		Remaining maturity			
Investment type	**Fair value**	**12 months or less**	**13 to 24 months**	**25 to 60 months**	**More than 60 months**
Federal agency securities	$ 272,230	100,924	78,834	92,472	—
RFCO strips	123,153	8,975	8,899	25,573	79,706
U.S. Treasury notes	91,053	32,374	29,282	29,397	—
U.S. Treasury bills	52,370	52,370	—	—	—
Money market funds	50,524	50,524	—	—	—
Commercial paper	29,564	29,564	—	—	—
U.S. Treasury strips	6,567	—	—	—	6,567
Corporate notes	1,881	1,881	—	—	—
Total	$ 627,342	276,612	117,015	147,442	86,273

(In thousands)

(5) Capital Assets

Capital assets consist of the following:

		Balance at beginning of year	Additions	Transfers/ deletions	Balance at end of year
Construction in progress	$	318,157	8,567	(12,847)	313,877
Right-of-way acquisitions, grading, or improvements		41,526	—	—	41,526
Furniture and equipment		33,630	1,254	(2,689)	32,195
		393,313	9,821	(15,536)	387,598
Impairment loss on right-of-way acquisitions, grading, or improvements		(25,987)	—	—	(25,987)
Furniture and equipment accumulated depreciation		(17,150)	(3,034)	2,689	(17,495)
	$	350,176	6,787	(12,847)	344,116

Impairment of Capital Assets

In fiscal year 2005, the agency adopted Governmental Accounting Standards Board Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*. This resulted in recording a noncash impairment loss on right-of-way acquisitions, grading or improvements of $25,987 related to mitigation parcels held that will ultimately be conveyed to other owners for no consideration and excess parcels that have lost value due to accessibility or other factors. This write-down did not reflect any physical change to the properties; rather it was to reflect the development cycle of mitigation assets.

Transfer of Ownership

Ownership of the Foothill/Eastern Transportation Corridor construction, right-of-way, grading, and improvements were 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. For the year ended June 30, 2011, the agency incurred expenditures for improvements and enhancements to major thoroughfares already transferred to Caltrans. The improvements and enhancements are covered by separate project-specific Cooperative Agreements with Caltrans and are transferred on an ongoing basis. The balance of construction in progress represents capital improvements in progress, primarily the 241 completion project. Upon completion, these capital assets will also be transferred to Caltrans and recognized as a contribution expense.

(Continued)

(In thousands)

(6) Long-Term Obligations

The following is a summary of changes in long-term obligations during the year ended June 30, 2011:

		Balance at beginning of year	Additions/ accretions	Reductions	Balance at end of year	Due within one year
Series 1999 Toll Road Refunding Revenue Bonds:						
Current Interest Bonds	$	728,010	—	(4,540)	723,470	11,390
Capital Appreciation Bonds		701,753	42,780	—	744,533	—
Convertible Capital Appreciation Bonds		690,030	—	—	690,030	—
Series 1995A (fixed rate) Senior Lien Toll Road Revenue Bonds:						
Current Interest Bonds		179,990	—	—	179,990	—
Total bonds payable	$	2,299,783	42,780	(4,540)	2,338,023	11,390

Toll Road Revenue Bonds

In August 1999, the agency issued serial, term, and capital appreciation toll road refunding revenue bonds (1999 Refunding 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 Refunding Bonds are subordinate to the remaining 1995 Unrefunded Bonds of $179,990 and are collateralized by net revenues, as defined in the master indentures, consisting primarily of toll revenues less current expenses.

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 mature on January 1, 2035. 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.

Interest on the 1999 current interest bonds is payable semiannually at rates ranging from 4.38% to 5.75%. The bonds mature in annual installments from January 15, 2004 to January 15, 2040. The bonds are subject to early redemption, at the option of the agency, beginning January 15, 2010 by payment of accrued interest, principal, and a premium of up to 1.00%.

The 1999 capital appreciation bonds accrue interest at rates ranging from 5.63% to 6.09%, compounded semiannually. The bonds mature in annual installments from January 15, 2017 to January 15, 2038. The bonds are subject to early redemption, at the option of the agency, beginning January 15, 2010 by payment of accrued interest, principal, and a premium of up to 2.00%.

The 1999 convertible capital appreciation bonds accrue interest at rates ranging from 5.80% to 5.88% compounded semiannually. Interest is payable semiannually based on accreted amounts commencing on

(In thousands)

January 15, 2010. The bonds mature in annual installments from January 15, 2020 to January 15, 2029. The bonds are 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%.

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 following is a summary of the agency's annual debt service requirements by fiscal year for the 1995 Senior Lien Toll Road Revenue Bonds and the 1999 Toll Road Refunding Bonds as of June 30, 2011:

		Principal	Interest[(1)]	Total
2012	$	11,390	89,690	101,080
2013		15,705	88,990	104,695
2014		25,160	87,918	113,078
2015		30,205	86,452	116,657
2016		42,990	84,579	127,569
2017 – 2021		260,717	473,501	734,218
2022 – 2026		340,776	552,614	893,390
2027 – 2031		563,675	489,747	1,053,422
2032 – 2036		403,797	818,585	1,222,382
2037 – 2040		643,608	471,210	1,114,818
	$	2,338,023	3,243,286	5,581,309

(1) Includes payments on January 1 and January 15 of such fiscal year and July 1 and July 15 of the next fiscal year.

Included in principal is $678,384 related to accreted principal on convertible capital appreciation bonds and capital appreciation bonds.

The net proceeds of the 1999 Refunding 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 the refunded bonds. As of June 30, 2011, the amount of the refunded bonds outstanding, which were previously eliminated in the financial statements as a result of the refunding, was $612,618.

(7) Commitments and Contingencies

(a) Toll Collection and Revenue Management System Agreements

The agency and SJHTCA entered into agreements with various contractors for a customer service center, hardware maintenance, toll collection systems operation and maintenance, toll attendant staffing and supervision, and violation processing. The agreements expire on various dates through

October 31, 2015. Additionally, all agreements are cancelable by the agency, without further obligation, upon written notice, generally within 90 days.

(b) Project Costs

As of June 30, 2011, the agency has outstanding commitments and contracts for remaining corridor construction of the 241 completion project and improvements on existing construction of approximately $11,107.

(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, with the Board of Directors of the SJHTCA, entered into a Mitigation Payment and Loan Agreement (the Agreement). The terms of the Agreement call 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, subject to the terms of the Agreement, on an as-needed basis, to SJHTCA up to $1,040,000 to assist SJHTCA in achieving its debt service coverage 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 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 and that any liens or revenue pledges required in order to finance the 241 completion project and certain other capital projects would have priority

(Continued)

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, 2011, no amounts were outstanding on the loan.

(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 the SJHTCA. Future minimum lease payments receivable from SJHTCA under the lease agreement at June 30, 2011 are $396 through June 30, 2012. Future minimum payments are based on the fair market rental value and adjust annually.

(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, California 92701.

Plan members contribute a percentage of their annual covered salary at actuarially determined rates based on the age of entry into the plan; however, the agency pays up to 7% of the employee's required contribution. The agency is also required to contribute a percentage of each employee's covered salary into the plan. The agency has contributed 100% of its required contributions of approximately $800, $806, and $827 to the plan for the years ended June 30, 2011, 2010, and 2009, respectively.