FOOTHILL/EASTERN TRANSPORTATION CORRIDOR AGENCY

Financial Statements

June 30, 2018 and 2017

(With Independent Auditors' Report Thereon)

FOOTHILL/EASTERN TRANSPORTATION CORRIDOR AGENCY

Table of Contents

KPMG LLP
Suite 700
20 Pacifica
Irvine, CA 92618-3391

Independent Auditors' Report

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

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, 2018 and 2017, and the related notes to the financial statements, which collectively comprise the Agency's basic financial statements for the years then ended, 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 audits. We conducted our audits 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, 2018 and 2017, 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 and required supplementary information on pages 3–7 and pages 39–40, respectively, 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 audits 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

Irvine, California
October 1, 2018

This discussion and analysis of the financial performance of the Foothill/Eastern Transportation Corridor Agency (the Agency) provide an overview of the Agency's financial activities for the fiscal years ended June 30, 2018 and 2017. 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 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 revenue, but with a shortage of gas-tax revenue 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 and development impact fees, 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. The State Route 241, State Route 261, and State Route 133 toll roads serve as important, time-saving alternative routes to local freeways and arterial roads, with 69,049,893 transactions during the year ended June 30, 2018, compared to 67,004,684 annual transactions in 2017, and 63,375,504 transactions in 2016.

Financial Highlights

Tolls, fees, and fines earned in fiscal year 2018 (FY18) totaled $188,805 compared to $175,047 in fiscal year 2017 (FY17), an increase of 7.9%.

As of June 30, 2018 and 2017, the Agency had $356,374 and $382,819, respectively, of restricted cash and investments that were subject to master indentures of trust for the bonds outstanding at each date. The Agency also had $339,431 and $269,715, respectively, of unrestricted cash and investments.

The Agency's net position at June 30, 2018 and 2017 was $(1,579,796) and $(1,624,453), 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 of construction.

(In thousands)

Overview of the Financial Statements

The Agency's financial statements include its statements of net position, statements of revenue, 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 assets and liabilities of the Agency as well as certain items labeled as deferred outflows and inflows of resources. The current year's revenue 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 revenue, expenses, and changes in net position report the Agency's net position and related changes. Net position is the difference between the total of recorded assets and deferred outflows and the total of liabilities and deferred inflows. The recorded activities include all toll revenue and operating expenses related to the operation of the Foothill/Eastern Transportation Corridors, as well as the Agency's construction-related activities and related financing costs. Activities are financed by toll revenue, development impact fees, fees and fines, and investment income.

Financial Analysis

The following table summarizes the net position of the Agency as of June 30, 2018, 2017, and 2016:

	2018	Percentage increase (decrease)	2017	Percentage increase (decrease)	2016
Assets and deferred outflows:					
Current assets	$ 346,120	5.3 %	$ 328,543	33.7 %	$ 245,789
Capital assets, net	106,030	23.3	86,000	(70.6)	292,397
Other noncurrent assets	492,195	6.0	464,503	(6.9)	498,766
Deferred outflows	10,787	(5.3)	11,387	(11.3)	12,843
Total assets and deferred outflows	955,132	7.3	890,433	(15.2)	1,049,795
Liabilities and deferred inflows:					
Bonds payable	2,436,570	1.2	2,407,087	1.2	2,379,275
Net pension liability	7,417	(15.2)	8,742	(2.0)	8,918
Other liabilities	88,850	(9.7)	98,402	11.3	88,409
Deferred inflows	2,091	219.2	655	(20.5)	824
Total liabilities and deferred inflows	2,534,928	0.8	2,514,886	1.5	2,477,426
Net position	$ (1,579,796)	(2.7)	$ (1,624,453)	13.8	$ (1,427,631)

(In thousands)

The increases in current assets above are primarily attributable to the Agency's accumulation of additional cash reserves, as cash generated from operations has continued to surpass its immediate debt service requirements.

The following is a summary of the Agency's revenue, expenses, and changes in net position for the years ended June 30, 2018, 2017, and 2016:

	2018	Percentage increase (decrease)	2017	Percentage increase (decrease)	2016
Operating revenue:					
Tolls, fees, and fines	$ 188,805	7.9 %	$ 175,047	4.4 %	$ 167,635
Development impact fees	24,754	18.2	20,939	(26.1)	28,349
Other revenue	902	42.9	631	18.4	533
Total operating revenue	214,461	9.1	196,617	0.1	196,517
Operating expenses	29,889	4.5	28,601	5.5	27,105
Operating income	184,572	9.9	168,016	(0.8)	169,412
Nonoperating expenses, net	(139,915)	(61.7)	(364,838)	158.8	(140,953)
Change in net position	44,657		(196,822)		28,459
Net position at beginning of year	(1,624,453)	13.8	(1,427,631)	(2.0)	(1,456,090)
Net position at end of year	$ (1,579,796)	(2.7)	$ (1,624,453)	13.8	$ (1,427,631)

Tolls, fees, and fines comprised 88.0% of total revenue in FY18 compared to 89.0% of total revenue in FY17. Tolls, fees, and fines increased by 7.9% and 4.4%, respectively, over each of the two preceding years, primarily due to increases in toll transactions and inflationary toll rate increases. Development impact fees were $24,754 in FY18 and $20,939 in FY17, an increase of 18.2%, compared to a decrease of 26.1% in FY17. 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 $29,889 in FY18 compared to $28,601 in FY17, an increase of 4.5%. Included in operating expenses in FY18 is noncash depreciation expense on fixed assets of $5,563, compared to $5,884 in FY17. Excluding depreciation, operating expenses were $24,326 in FY18 and $22,717 in FY17, an increase of $1,609.

Net nonoperating expenses for FY18 include investment income of $5,567; interest expense of $142,245; bond remarketing costs of $882; and $2,355 of costs related to the removal of some of the agency's toll booths. For FY17, net nonoperating expenses include investment income of $2,855; interest expense of $141,939; and $7.1 million for a legal settlement and $218,571 for the write-off of construction in progress, as described further below. Accrual-basis interest expense included accretion on the Agency's capital appreciation bonds and convertible capital appreciation bonds of $28,974 and $27,336 in FY18 and in FY17, respectively. Interest expense in FY18 and FY17 also included noncash amortization of $509 and $476, respectively, related to a discount on the issuance of bonds; related to prepaid bond insurance of $257 and $219, respectively; and of $850 and $1,163, respectively, related to the deferred bond refunding costs.

(In thousands)

During the year ended June 30, 2017, the Agency agreed to settle several legal matters related to its planned route for extension of State Route 241 to connect with I-5. As a condition of the settlement, the Agency agreed to abandon consideration of this route and to pay $7.1 million to reimburse certain litigation costs incurred by the plaintiffs. Accordingly, the Agency recognized expense of $218,571 to write off previously incurred costs associated with planning for this route.

Capital Assets, Net

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

		2018	2017
Construction in progress	$	72,633	52,988
Right-of-way acquisitions, grading, or improvements		18,698	15,014
Furniture and equipment		14,699	17,998
Total capital assets, net	$	106,030	86,000

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, 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

At June 30, 2018, 2017, and 2016, the Agency had outstanding bonds payable of $2,436,570, $2,407,087, and $2,379,275, respectively. The changes in FY18 and FY17 are primarily attributable to the accretion of principal on capital appreciation bonds of $28,974 and $27,336, respectively.

All of the Agency's toll, fees, fines, and development impact fee 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, 2018 and 2017.

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, 2018. The new toll rates are projected to result in a 3.7% increase in transactional toll revenue and reflect increases of $0.15 to $0.20 for peak hour toll rates at the mainline plazas.

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 info@thetollroads.com.

FOOTHILL/EASTERN TRANSPORTATION
CORRIDOR AGENCY

Statements of Net Position

June 30, 2018 and 2017

(In thousands)

		2018	2017
Assets:			
Current assets:			
Cash and investments	$	217,664	181,985
Restricted cash and investments		117,122	137,177
Receivables:			
Accounts, net of allowance of $2,317 and $3,074, respectively		7,647	6,608
Fees		29	88
Interest		2,619	1,796
Other assets		1,039	889
Total current assets		346,120	328,543
Noncurrent assets:			
Cash and investments		121,767	87,730
Restricted cash and investments		239,252	245,642
Capital assets, net		106,030	86,000
Unamortized prepaid bond insurance		10,080	10,336
Note receivable – San Joaquin Hills Transportation Corridor Agency		121,096	120,795
Total noncurrent assets		598,225	550,503
Deferred outflows of resources:			
Unamortized deferral of bond refunding costs		9,070	9,921
Pension costs		1,717	1,466
Total assets and deferred outflows		955,132	890,433
Liabilities:			
Current liabilities:			
Accounts payable	$	9,417	14,612
Unearned revenue		21,830	23,179
Due to San Joaquin Hills Transportation Corridor Agency		6,075	8,475
Employee compensated absences payable		443	450
Interest payable		51,085	51,686
Total current liabilities		88,850	98,402
Net pension liability		7,417	8,742
Long-term bonds payable		2,436,570	2,407,087
Total liabilities		2,532,837	2,514,231
Deferred inflows of resources:			
Pension costs		2,091	655
Total liabilities and deferred inflows	$	2,534,928	2,514,886
Net position:			
Net investment in capital assets	$	(2,311,390)	(2,300,830)
Restricted		276,218	298,105
Unrestricted		455,376	378,272
Total net position	$	(1,579,796)	(1,624,453)

See accompanying notes to financial statements.

FOOTHILL/EASTERN TRANSPORTATION
CORRIDOR AGENCY

Statements of Revenue, Expenses, and Changes in Net Position

Years ended June 30, 2018 and 2017

(In thousands)

		2018	2017
Operating revenue:			
Tolls, fees, and fines	$	188,805	175,047
Development impact fees		24,754	20,939
Other revenue		902	631
Total operating revenue		214,461	196,617
Operating expenses:			
Toll compliance and customer service		9,597	9,246
Depreciation		5,563	5,884
Salaries and wages		3,881	3,623
Toll systems		1,768	1,711
Marketing		701	689
Insurance		805	779
Toll facilities		669	637
Professional services		5,725	4,865
Facilities operations, maintenance, and repairs		252	207
Other operating expenses		928	960
Total operating expenses		29,889	28,601
Operating income		184,572	168,016
Nonoperation revenue (expenses):			
Investment income		5,567	2,855
Loss on disposition of capital assets		(2,355)	(83)
Costs of bond remarketing transaction		(882)	—
Settlement expense (note 5)		—	(7,100)
Write-off of construction in progress (note 5)		—	(218,571)
Interest expense		(142,245)	(141,939)
Nonoperating expenses, net		(139,915)	(364,838)
Change in net position		44,657	(196,822)
Net position at beginning of year		(1,624,453)	(1,427,631)
Net position at end of year	$	(1,579,796)	(1,624,453)

See accompanying notes to financial statements.

FOOTHILL/EASTERN TRANSPORTATION CORRIDOR AGENCY

Statements of Cash Flows

Years ended June 30, 2018 and 2017

(In thousands)

		2018	2017
Cash flows from operating activities:			
Cash received from toll road patrons	$	184,017	178,396
Cash received from development impact fees		24,813	20,872
Cash received from other revenue		902	631
Cash payments to suppliers		(25,790)	(14,879)
Cash payments to employees		(4,028)	(3,813)
Net cash provided by operating activities		179,914	181,207
Cash flows from capital and related financing activities:			
Cash payments for acquisition of capital assets		(25,593)	(18,890)
Cash payment for legal settlement		—	(4,000)
Cash payments related to the disposition of capital assets		(2,355)	—
Cash payments in connection with bond remarketing transaction		(882)	—
Cash payments for interest		(112,256)	(112,771)
Net cash used in capital and related financing activities		(141,086)	(135,661)
Cash flows from investing activities:			
Cash receipts for interest and dividends		9,056	7,784
Cash receipts from the maturity and sale of investments		386,349	288,103
Cash payments for purchase of investments		(468,476)	(341,757)
Net cash used in investing activities		(73,071)	(45,870)
Net decrease in cash and cash equivalents		(34,243)	(324)
Cash and cash equivalents at beginning of year		97,964	98,288
Cash and cash equivalents at end of year (note 4)	$	63,721	97,964
Reconciliation of operating income to net cash provided by operating activities:			
Operating income	$	184,572	168,016
Adjustments to reconcile operating income to net cash provided by operating activities:			
Depreciation		5,563	5,884
Changes in operating assets and liabilities:			
Accounts receivable		(1,039)	(304)
Fees receivable		59	(67)
Due to/from San Joaquin Hills Transportation Corridor Agency		(2,400)	898
Other assets		(150)	62
Accounts payable		(5,195)	4,154
Unearned revenue		(1,349)	2,755
Net pension liability		(1,325)	(176)
Deferred outflows of resources related to pensions		(251)	293
Deferred inflows of resources related to pensions		1,436	(169)
Employee compensated absences payable		(7)	(139)
Total adjustments		(4,658)	13,191
Net cash provided by operating activities	$	179,914	181,207

(Continued)

FOOTHILL/EASTERN TRANSPORTATION CORRIDOR AGENCY

Statements of Cash Flows

Years ended June 30, 2018 and 2017

(In thousands)

		2018	2017
Noncash capital and related financing and investing activities:			
Interest expense recorded for accretion of bonds outstanding	$	(28,974)	(27,336)
Amortization of bond discount recorded as interest expense		(509)	(476)
Amortization of deferred bond-refunding cost recorded as interest expense		(850)	(1,163)
Amortization of prepaid bond insurance recorded as interest expense		(257)	(219)
Write-off of construction in progress		—	(218,571)
Interest accrued on note receivable from San Joaquin Hills Transportation Corridor Agency		301	300
Change in unrealized gain/loss on investments		(3,853)	(3,230)
Amortization of discount/premium on investments		176	(1,468)

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 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 revenue and expenses from nonoperating items in the preparation of its financial statements. Operating revenue 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, in addition to costs associated with the Agency’s ongoing obligations for environmental mitigation and certain costs related to construction administration. All revenue and expenses not meeting this definition are reported as nonoperating revenue and expenses.

(b) Basis of Accounting

The financial statements are prepared using the accrual basis of accounting. Revenue is recognized when earned, and expenses are recognized when incurred.

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 revenue 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, except for money market funds, are stated at fair value on a recurring basis. Money market funds with maturities of one year or less are recorded at amortized cost.

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, receivables from patrons for violations and tolls, 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, 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. The cost of capital assets includes ancillary charges necessary to place the assets into their intended location and condition for use.

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 no longer has title to these assets. The costs of normal maintenance and repairs and mitigation that do not add value to the 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
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) Unearned Revenue

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

(i) Unamortized Deferral of Bond Refunding Costs

Deferred bond-refunding costs represent certain costs related to the issuance of 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) Pension Plan

Qualified permanent employees of the Agency participate in a cost-sharing, multiple-employer defined benefit pension plan administered by the Orange County Employees Retirement System (OCERS). For purposes of measuring the Agency's net pension liability, deferred outflows/inflows of resources related to pensions, and pension expense, information about the fiduciary net position of the plan and additions to/deductions from the plan's fiduciary net position have been determined on the same basis as they are reported by OCERS. For this purpose, plan contributions are recognized when they are due and payable in accordance with plan terms. Investments are reported at fair value.

(k) Revenue Recognition

Toll revenue is recognized at the time each vehicle passes through the toll plaza. Development impact fees are earned when building permits are issued and funds are collected by the member agencies. Other revenue is recognized when earned.

(Continued)

(l) Transactions with SJHTCA

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, 2018 and 2017, the Agency had net payables to SJHTCA of $6,075 and $8,475, respectively.

(m) Net Position

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

Net investment in capital assets: Represents the Agency's capital assets, net of accumulated depreciation, along with unamortized bond insurance and refunding costs, reduced by 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 revenue collected, net of related liabilities.

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

(n) 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 revenue and expenses during the reporting period. Actual results could differ from those estimates.

(o) Reclassifications

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

(In thousands)

(3) Development Impact Fees

The sources of development impact fees for the years ended June 30, 2018 and 2017 were as follows:

		2018	2017
City of Irvine	$	17,802	15,557
City of Lake Forest		2,585	2,583
City of Tustin		1,903	1,043
City of Yorba Linda		732	308
City of Mission Viejo		714	349
City of Anaheim		377	377
County of Orange		185	159
City of Orange		138	110
City of San Clemente		117	253
City of Rancho Santa Margarita		95	106
City of Santa Ana		83	—
City of Dana Point		17	—
City of San Juan Capistrano		6	94
	$	24,754	20,939

(4) Cash and Investments

Cash and investments as of June 30, 2018 and 2017 are classified in the accompanying financial statements, as follows:

		2018	2017
Current cash and investments	$	217,664	181,985
Noncurrent cash and investments		121,767	87,730
Current restricted cash and investments		117,122	137,177
Noncurrent restricted cash and investments		239,252	245,642
	$	695,805	652,534

(In thousands)

Cash and investments as of June 30, 2018 consist of the following:

		Cash and cash equivalents	Investments	Total
Cash on hand	$	1	—	1
Deposit accounts		15,275	—	15,275
Money market funds		4,375	—	4,375
California Asset Management Trust Cash Reserve Portfolio (CAMP)		—	42,522	42,522
Local Agency Investment Fund		—	7,036	7,036
Orange County Investment Pool		—	39	39
Certificates of deposit		—	59,500	59,500
U.S. Treasury securities		—	5,474	5,474
Federal agency, U.S. government-sponsored enterprise, and supranational notes		—	91,425	91,425
Investments held with trustee per debt agreements:				
Money market funds		23,447	—	23,447
Commercial paper		—	49,789	49,789
U.S. Treasury securities		20,623	99,870	120,493
Federal agency and U.S. government-sponsored enterprise notes and bonds		—	93,185	93,185
Corporate notes		—	183,244	183,244
Total	$	63,721	632,084	695,805

(In thousands)

Cash and investments as of June 30, 2017 consist of the following:

	Cash and cash equivalents	Investments	Total
Cash on hand	$ 1	—	1
Deposit accounts	16,275	—	16,275
Money market funds	22,259	—	22,259
Orange County Investment Pool	—	12,335	12,335
Certificates of deposit	—	8,500	8,500
U.S. Treasury securities	—	31,156	31,156
Federal agency, U.S. government-sponsored enterprise, and supranational notes	—	120,428	120,428
Corporate notes	—	80,593	80,593
Investments held with trustee per debt agreements:			
Money market funds	19,568	—	19,568
Commercial paper	—	31,006	31,006
U.S. Treasury securities	39,861	86,388	126,249
Federal agency and U.S. government-sponsored enterprise notes and bonds	—	119,034	119,034
Corporate notes	—	65,130	65,130
Total	$ 97,964	554,570	652,534

(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, 2018 and 2017, the carrying amounts of the Agency's cash deposits were $15,275 and $16,275, respectively, and the corresponding aggregate bank balances were $18,732 and $20,733, respectively. The differences of $3,457 and $4,458 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

(i) 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.

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	Second highest ratings category by an NRSRO
Supranational agency notes and bonds	5 Years	30	5	Second highest ratings category by an NRSRO

(In thousands)

Authorized investment type		Maximum maturity	Maximum percentage of portfolio*	Maximum percentage investment in one issuer	Specific rating requirement
Certificates of deposit	**	5 Years	100	5	Long-term debt rating in one of the highest ratings categories by two NRSROs
Certificates of Deposit Account Registry Service		5 Years	30	5	Long-term debt rating in one of the highest ratings categories by two NRSROs
Negotiable certificates of deposit		5 Years	30	5	Long-term debt rating in one of the highest ratings categories by two NRSROs
Banker's 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 an 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 the highest ratings categories by two NRSROs

Authorized investment type	Maximum maturity	Maximum percentage of portfolio*	Maximum percentage investment in one issuer	Specific rating requirement
State of California Local Agency Investment Fund	N/A	Lesser of $65 million or 15% of portfolio	5	N/A
County or local agency investment pools	N/A	15	5	N/A
Shares in a California common law trust	N/A	20	5	Highest rating category by an NRSRO
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
Money market mutual funds	N/A	20	5	Highest applicable rating by two NRSROs
Bonds or notes issued by the State of California, any local agency in the state, or any other 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

The investment of debt proceeds and toll revenue held by the Agency's bond trustee is 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 funds, and if applicable, the specific rating requirements:

Investments authorized by debt agreements	Specific rating requirement
U.S. government obligations	N/A
U.S. federal agency debt instruments	N/A
State and local government debt 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, savings accounts, deposit accounts, or money market deposits insured by the FDIC	N/A
Certificates of deposit collateralized by U.S. government or federal agency obligations	N/A
Federal funds or 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 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, one of the three highest applicable rating categories

Investments authorized by debt agreements		Specific rating requirement
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

* 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.

At June 30, 2018 and 2017, 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:

	June 30, 2018		June 30, 2017	
Investment type	**S&P**	**Moody’s**	**S&P**	**Moody’s**
U.S. Treasury bills	A-1+	P-1	A-1+	P-1
U.S. Treasury notes	AA+	Aaa	AA+	Aaa
Federal agency, U.S. government-enterprise, and supranational notes and bonds*	AA+/AAA	Aaa	AA+/A-1+	Aaa/P-1
Money market funds	AAAm	Aaa-mf	AAAm	Aaa-mf
CAMP	AAA	NR	—	—
Local Agency Investment Fund	NR	NR	—	—
Orange County Investment Pool	NR	NR	NR	NR
Commercial paper:				
Bank of Tokyo – Mitsubishi UFJ Ltd	—	—	A-1	P-1
General Electric Company	A-1	P-1	A-1+	P-1
Rabobank USA Fin Corp	A-1	P-1	A-1	P-1
Toyota Motor Corp	A-1+	P-1	A-1+	P-1
Certificates of deposit:				
Toronto Dominion Holdings	A-1+	P-1	A-1+	P-1
Bank of Montreal Chicago	A-1	P-1	—	—
Bank of Nova Scotia Houston	A-1	P-1	—	—
Royal Bank Canada	A-1+	P-1	—	—
Nordea Bank AB	A-1+	P-1	—	—

Investment type	June 30, 2018 S&P	June 30, 2018 Moody's	June 30, 2017 S&P	June 30, 2017 Moody's
Corporate notes – Medium term:				
Apple Inc.	AA+	Aa1	AA+	Aa1
American Honda Finance	A+	A2	A+	A1
Bank of America Corp	A-	A3	—	—
Berkshire Hathaway Inc	AA	Aa2	AA	Aa2
Charles Schwab Corp	A	A2	A	A2
Chevron Corporation	AA-	Aa2	AA-	Aa2
Cisco Systems	AA-	A1	AA-	A1
Deere & Company	A	A2	A	A2
Exxon Mobil Corp	AA+	Aaa	AA+	Aaa
General Dynamics	A+	A2	—	—
General Electric Co	—	—	AA-	A1
HSBC USA Corp	A	A2	—	—
IBM	A+	A1	—	—
Intel Corp	A+	A1	A+	A1
JP Morgan Chase & Co	A-	A3	A-	A3
Oracle Corporation	AA-	A1	AA-	A1
Paccar Financial	A+	A1	A+	A1
Pepsico Inc	A+	A1	A+	A1
Pfizer Inc	AA	A1	AA	A1
PNC Financial Services Group	A	A2	A	A2
Qualcomm Inc	—	—	A	A1
State Street Bank	A	A1	—	—
Toyota Motor Corp	AA-	Aa3	AA-	Aa3
US Bancorp	A+	A1	A+	A1
Visa Inc	A+	A1	A+	A1
Wells Fargo and Company	A-	A2	A	A2

* Ratings are indicated to the extent available. However, in some instances, discounted federal agency bonds are not rated.

(ii) *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.

(iii) *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.

(In thousands)

A summary of the Agency's investments held at June 30, 2018 that are governed by the Agency's investment policy and its bond agreements, including money market funds of $27,822 and U.S. Treasury securities of $20,623 that are considered cash equivalents, is as follows:

			Remaining maturity (in years)			
Investment type		Fair value	Less than one	One to two	Two to five	More than five
Federal agency, U.S. government-sponsored enterprise, and supranational notes and bonds	$	184,610	69,111	77,581	37,918	—
Corporate notes		183,244	58,313	55,480	69,451	—
U.S. Treasury securities		125,967	71,877	9,820	44,270	—
Certificates of deposit		59,500	59,500	—	—	—
Commercial paper		49,789	49,789	—	—	—
CAMP		42,522	42,522	—	—	—
Money market funds		27,822	27,822	—	—	—
Local Agency Investment Fund		7,036	7,036	—	—	—
Orange County Investment Pool		39	39	—	—	—
Total	$	680,529	386,009	142,881	151,639	—

At June 30, 2018, with the exception of investments issued or explicitly guaranteed by the U.S. government 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 Home Loan Bank, CAMP, and Federal National Mortgage Association that represented 7%, 6%, and 5%, respectively, of the Agency's total investments, as permitted by the Agency's investment policy and the applicable bond indentures.

A summary of the Agency's investments held at June 30, 2017 that are governed by the Agency's investment policy and its bond agreements, including money market funds of $41,827 and U.S. Treasury securities of $39,861 that are considered cash equivalents, is as follows:

			Remaining maturity (in years)			
Investment type		Fair value	Less than one	One to two	Two to five	More than five
Federal agency, U.S. government-sponsored enterprise, and supranational notes and bonds	$	239,462	121,163	46,393	71,906	—
U.S. Treasury securities		157,405	125,277	7,280	24,848	—
Corporate notes		145,723	50,234	42,305	53,184	—
Money market funds		41,827	41,827	—	—	—
Commercial paper		31,006	31,006	—	—	—
Orange County Investment Pool		12,335	12,335	—	—	—
Certificates of deposit		8,500	8,500	—	—	—
Total	$	636,258	390,342	95,978	149,938	—

(In thousands)

At June 30, 2017, with the exception of investments issued or explicitly guaranteed by the U.S. government 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 Home Loan Bank, Federal National Mortgage Association, and Federal Home Loan Mortgage Corporation that represented 10%, 10%, and 8%, respectively, of the Agency's total investments, as permitted by the Agency's investment policy and the applicable bond indentures.

(iv) Fair Value Measurements

Because investing is not a core part of the Agency's mission, the Agency has determined that the disclosures related to these investments only need to be disaggregated by major type and has chosen a tabular format for disclosing the levels within the fair value hierarchy established by U.S. GAAP. The hierarchy is based on the valuation inputs used to measure the fair value of the asset, as follows:

- Level 1 inputs are quoted prices in active markets for identical assets.
- Level 2 inputs are significant other observable inputs.
- Level 3 inputs are significant, unobservable inputs.

Debt securities classified as Level 2 in the fair value hierarchy are valued using a matrix pricing technique. Matrix pricing is used to value securities based on the securities' relationship to benchmark quoted prices. Commercial paper is valued based on quoted prices in active markets of similar securities.

At June 30, 2018 and 2017, the Agency had the following fair value measurements:

	June 30, 2018			
Investment type	**Fair value**	**Quoted prices in active markets for identical assets (Level 1)**	**Significant other observable inputs (Level 2)**	**Significant unobservable inputs (Level 3)**
Federal agency, U.S. government-sponsored enterprise, and supranational notes and bonds	$ 184,610	—	184,610	—
Corporate notes	183,244	—	183,244	—
U.S. Treasury securities	125,967	—	125,967	—
Certificates of deposit	59,500	—	59,500	—
Commercial paper	49,789	—	49,789	—
Total	$ 603,110	—	603,110	—

(In thousands)

Excluded from the table above are money market funds of $27,822, which are reported at amortized cost, and funds on deposit with CAMP, the Local Agency Investment Fund, and the Orange County Investment Pool, which collectively aggregate to $49,597 and are not subject to fair value measurement categorization.

	June 30, 2017			
Investment type	Fair value	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Federal agency, U.S. government-sponsored enterprise, and supranational notes and bonds	$ 239,462	—	239,462	—
U.S. Treasury securities	157,405	—	157,405	—
Corporate notes	145,723	—	145,723	—
Commercial paper	31,006	—	31,006	—
Certificates of deposit	8,500	—	8,500	—
Total	$ 582,096	—	582,096	—

Excluded from the table above are money market funds of $41,827, which are reported at amortized cost, and funds on deposit with the Orange County Investment Pool of $12,335, which are not subject to fair value measurement categorization.

(5) Capital Assets

Capital assets activity for the year ended June 30, 2018 was as follows:

	Balance at beginning of year	Additions	Transfers/ deletions	Balance at end of year
Construction in progress	$ 52,988	19,645	—	72,633
Right-of-way acquisitions, grading, or improvements	15,014	3,684	—	18,698
Furniture and equipment	47,139	2,264	(1,737)	47,666
	115,141	25,593	(1,737)	138,997
Accumulated depreciation	(29,141)	(5,563)	1,737	(32,967)
	$ 86,000	20,030	—	106,030

(In thousands)

Capital assets activity for the year ended June 30, 2017 was as follows:

	Balance at beginning of year	Additions	Transfers/ deletions	Balance at end of year
Construction in progress	$ 256,268	15,291	(218,571)	52,988
Right-of-way acquisitions, grading, or improvements	15,014	—	—	15,014
Furniture and equipment	45,727	2,850	(1,438)	47,139
	317,009	18,141	(220,009)	115,141
Accumulated depreciation	(24,612)	(5,884)	1,355	(29,141)
	$ 292,397	12,257	(218,654)	86,000

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

Transfers/Deletions

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. The balance of construction in progress represents capital improvement projects, most of which will also be transferred to Caltrans upon completion and recognized as contribution expense.

During the year ended June 30, 2017, the Agency agreed to settle several legal matters related to its planned route for extension of State Route 241 to connect with I-5. As a condition of the settlement, the Agency agreed to abandon consideration of this route and to pay $7.1 million to reimburse certain litigation costs incurred by the plaintiffs. Accordingly, the Agency recognized expenses of $218,571 to write off previously incurred costs associated with planning for this route. Further, the Agency committed to spend $28 million for land acquisitions and habitat restoration projects to benefit the San Mateo Creek and its watershed.

(In thousands)

(6) Long-Term Obligations

The following is a summary of changes in long-term obligations during the year ended June 30, 2018:

	Balance at beginning of year	Additions/ accretions	Reductions	Balance at end of year	Due within one year
Series 2013 Toll Road Refunding Revenue Bonds:					
Senior Term Current Interest Bonds	$ 1,749,440	—	—	1,749,440	—
Junior Lien Current Interest Bonds	198,050	—	—	198,050	—
Capital Appreciation Bonds	161,310	9,841	—	171,151	—
Convertible Capital Appreciation Bonds	241,578	14,963	—	256,541	—
Series 2015 Toll Road Refunding Revenue Bonds:					
Capital Appreciation Bonds	96,190	4,170	—	100,360	—
Total bonds payable	2,446,568	28,974	—	2,475,542	$ —
Less unamortized discount on 2013 bonds	(39,481)	—	509	(38,972)	
Total bonds payable, less unamortized discount	$ 2,407,087	28,974	509	2,436,570	

The following is a summary of changes in long-term obligations during the year ended June 30, 2017:

	Balance at beginning of year	Additions/ accretions	Reductions	Balance at end of year	Due within one year
Series 2013 Toll Road Refunding Revenue Bonds:					
Senior Term Current Interest Bonds	$ 1,749,440	—	—	1,749,440	—
Junior Lien Current Interest Bonds	198,050	—	—	198,050	—
Capital Appreciation Bonds	152,053	9,257	—	161,310	—
Convertible Capital Appreciation Bonds	227,495	14,083	—	241,578	—
Series 2015 Toll Road Refunding Revenue Bonds:					
Capital Appreciation Bonds	92,194	3,996	—	96,190	—
Total bonds payable	2,419,232	27,336	—	2,446,568	$ —
Less unamortized discount on 2013 bonds	(39,957)	—	476	(39,481)	
Total bonds payable, less unamortized discount	$ 2,379,275	27,336	476	2,407,087	

In February 2015, the Agency issued $87,008 of Senior Lien Toll Road Refunding Revenue Bonds (2015 Capital Appreciation Bonds); together with certain funds held in trust, the proceeds of the issuance were used to refund certain outstanding revenue bonds. The bonds accrue interest at rates ranging from 4.21% to 4.42%, compounded semiannually, and are scheduled to mature in annual installments from January 2033 to January 2035.

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 certain outstanding revenue bonds. The reacquisition price of the refunded bonds exceeded their net carrying amount by $14,534; this amount was 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. The 2013 Bonds were issued at a discount of $41,009, which is being amortized over the life of the bonds.

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 dates ranging from July 15, 2017 through July 15, 2022.

During August 2017, $125,000 of the 2013 Term Rate Bonds were remarketed, resulting in a reduction in the applicable interest rate from 5.00% to 3.95%. In connection with the remarketing transaction, the Agency incurred expenses of $882.

The 2013 capital appreciation bonds accrue interest at rates ranging from 3.750% 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, pledged revenue, and any other amounts pledged for repayment of the bond debt described above. The balance of pledged funds held by the trustee are included in restricted cash and investments.

Included in principal at June 30, 2018 and 2017 is $113,918 and $84,944, respectively, related to accreted principal on convertible capital appreciation bonds and capital appreciation bonds.

(In thousands)

A portion of the net proceeds of a prior bond refunding was 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, 2018 and 2017, the amounts of the previously refunded 1995 bonds outstanding, which were previously eliminated from the financial statements as a result of the refunding, are $763,868 and $785,650, respectively.

The 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, 2018:

		Principal	Interest[1]	Junior lien interest[1]	Total
2019	$	—	98,694	12,764	111,458
2020		4,401	98,953	12,764	116,118
2021		7,739	99,540	12,764	120,043
2022		10,857	100,492	12,764	124,113
2023		14,286	101,606	12,754	128,646
2024–2028		56,120	663,967	62,487	782,574
2029–2033		180,829	685,563	56,076	922,468
2034–2038		238,533	804,929	40,125	1,083,587
2039–2043		386,432	740,079	14,864	1,141,375
2044–2048		674,940	349,611	—	1,024,551
2049–2053		901,405	125,692	—	1,027,097
	$	2,475,542	3,869,126	237,362	6,582,030

[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.

(7) Commitments and Contingencies

(a) Toll Collection and Revenue Management System Agreements

The Agency and SJHTCA have entered into agreements with contractors for various services, including toll collection systems operation and maintenance. The agreements expire on various dates through June 30, 2025 and are cancelable by the Agency, without further obligation, with advance written notice.

(b) Project Costs

As of June 30, 2018, the Agency has outstanding commitments and contracts related to construction activities of approximately $44 million.

(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 in accordance with the Agency's master indentures of trust, as applicable.

(e) Mitigation Payment and Loan Agreement

On November 10, 2005, the Agency's board of directors and the board of directors of 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 SJHTCA to mitigate for anticipated loss of revenue due to the construction of the State Route 241 to I-5 connection project. All scheduled payments totaling $120,000 were made to SJHTCA as of June 2009 and were recorded as construction in progress.

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. Payments of accrued interest and outstanding principal would begin in the fiscal year when SJHTCA achieved a surplus in revenue in excess of the amount needed to meet the debt coverage requirement. All principal and accrued interest would be due and payable on January 1, 2037 to the extent that SJHTCA had surplus revenue available to pay all amounts due. The Agreement also stipulated that the Agency would not be obligated to make loans to SJHTCA prior to securing the necessary funds for constructing the State Route 241 to I-5 connection project unless the Agency determined that it would not build the project. If the commencement and diligent pursuit of the construction of the State Route 241 to I-5 connection project did not occur by June 30, 2015, the mitigation payments would be added to the principal amount of the loan. No amounts were loaned in connection with this arrangement.

On August 14, 2014, the Agency's board of directors and the board of directors of SJHTCA approved an agreement that provided for termination of the Agreement concurrently with the closing of a refinance transaction proposed by SJHTCA. The closing of this refinance transaction occurred on November 6, 2014. The termination agreement also provided for SJHTCA to pay $120,000 to the Agency, in annual installments beginning January 15, 2025 equal to 50% of SJHTCA's surplus funds as defined in the agreement. Interest accrual based on the average annual yield of the State of California Pooled Money Investment Account commenced upon closing of the transaction and interest is payable annually beginning January 15, 2025.

As a result of this agreement, the aggregate payments of $120,000 that were made to SJHTCA through 2009 were reclassified during 2015 as a note receivable from SJHTCA and a reduction of construction in progress.

(8) Corridor Operations Facility Lease

In January 2000, the Agency, along with SJHTCA, relocated to the corridor operations facility. At that time, an operating 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, 2018 and 2017 of $671 and $605, respectively.

(9) Employees' Retirement Plans

Defined Benefit Plan – Qualified permanent employees of the Agency participate in a cost-sharing multiple-employer defined benefit pension plan (the Plan) administered by OCERS, a public employee retirement system established in 1945. The Plan is subject to the provisions of the County Employees Retirement Law of 1937 (California Government Code Section 31450 et. seq.); the California Public Employees' Pension Reform Act of 2013 (Government Code Section 7522 et. seq.); and other applicable statutes.

(a) Benefits

The Plan provides retirement, disability, and death benefits to eligible plan members and their beneficiaries. Monthly retirement benefits are determined by benefit formulas that depend upon the classification of employees, the date of entering membership in OCERS or a reciprocal plan, retirement age, years of service, and final average compensation. The Agency's members hired prior to January 1, 2013 are subject to a benefit formula of 2.0% of final average compensation per year of service, based upon retirement at age 55. Members hired on or after January 1, 2013 are subject to a benefit formula of 2.5% at 67.

Amounts payable for retired members are subject to annual cost-of-living adjustments based upon changes in the Consumer Price Index for the prior calendar year. Adjustments are limited to a maximum increase or decrease of 3% per year.

(b) Contributions

Employer and employee contribution requirements are determined as percentages of covered payroll amounts and vary based upon the age of each employee at the date of entering membership in OCERS or a reciprocal plan. Employer contribution rates are determined using the entry age normal actuarial cost method based upon a level percentage of payroll. Employer contribution rates ranged from 11.40% to 61.89% for the year ended December 31, 2017, and from 11.79% to 62.66% for the year ended December 31, 2016. Employee contributions are established by the OCERS Board of Retirement and guided by applicable state statutes. Employee contribution rates ranged from 8.75% to 16.35% for the year ended December 31, 2017, and from 8.73% to 16.50% for the year ended December 31, 2016. The contributions from the Agency recognized by the Plan, measured as the total amounts of additions to the Plan's fiduciary net position for the years ended December 31, 2017 and 2016, were $1,024 and $1,038, respectively, and equaled 100% of the required contributions, and represented 24.4% and 26.6% of the Agency's covered payroll, respectively.

(In thousands)

(c) Pension Liabilities, Pension Expense, and Deferred Outflows/Inflows of Resources

For purposes of reporting under GASB Statement No. 68, *Accounting and Financial Reporting for Pensions,* OCERS arranged for determination of the Plan's collective net pension liability; deferred outflows and inflows of resources related to pensions; and pension expense, as well as the proportionate share of each amount applicable to the Plan's participating employers, using measurement dates of December 31, 2017 and 2016, with respective actuarial valuations as of December 31, 2016 and 2015 and standard procedures to roll forward to the respective measurement dates that correspond with the Agency's reporting dates of June 30, 2018 and 2017. The proportionate shares of these amounts attributable to the Transportation Corridor Agencies have been determined by OCERS's actuary based upon actual employer contributions within each rate group and further allocated between the Agency and SJHTCA on the basis of their respective shares of covered payroll to determine the amounts reportable by the Agency, as indicated below:

		June 30	
		2018	**2017**
Collective net pension liability – OCERS	$	4,952,099	5,191,217
Proportionate share attributable to Transportation Corridor Agencies		10,243	12,423
Share allocable to Foothill/Eastern Transportation Corridor Agency		7,417	8,742
Agency's proportion (percentage) of the collective net pension liability		0.15%	0.17%
Collective deferred outflows of resources – OCERS	$	795,890	570,539
Proportionate share attributable to Transportation Corridor Agencies		1,622	1,133
Share allocable to Foothill/Eastern Transportation Corridor Agency		1,114	817
Collective deferred inflows of resources – OCERS	$	1,178,768	756,043
Proportionate share attributable to Transportation Corridor Agencies		3,249	886
Share allocable to Foothill/Eastern Transportation Corridor Agency		2,091	655
Collective pension expense – OCERS	$	529,375	600,371
Proportionate share attributable to Transportation Corridor Agencies		1,331	2,032
Share allocable to Foothill/Eastern Transportation Corridor Agency		827	1,235

(In thousands)

The Agency's deferred outflows of resources related to pensions as of June 30, 2018 and 2017 are attributable to the following:

		2018	2017
Net difference between projected and actual earnings on pension plan investments	$	—	674
Changes of assumptions		1,006	—
Differences between expected and actual experience		108	143
Contributions to the plan subsequent to the measurement date of the collective net pension liability		603	649
Total deferred outflows related to pensions	$	1,717	1,466

The Agency's deferred inflows of resources related to pensions as of June 30, 2018 and 2017 are attributable to the following:

		2018	2017
Differences between expected and actual experience	$	1,025	288
Net difference between projected and actual earnings on pension plan investments		848	—
Changes of assumptions or other inputs		218	367
Total deferred inflows related to pensions	$	2,091	655

The amount of $603, representing as of June 30, 2018 the Agency's balance of deferred outflows of resources related to contributions subsequent to the measurement date, will be recognized as a reduction of the net pension liability in the year ending June 30, 2019. The other amounts of the Agency's balances of deferred outflows and deferred inflows of resources as of June 30, 2018 will be recognized as net reductions of pension expense as follows:

Year ending June 30:		
2019	$	(178)
2020		(246)
2021		(325)
2022		(246)
2023		18
	$	(977)

(d) Actuarial Assumptions and Other Inputs

The following significant methods and assumptions were used to measure the Plan's total pension liability as of December 31, 2017 and 2016:

- Actuarial experience study – Three-year periods ended December 31, 2016 and 2013, respectively
- Inflation rate – 2.75% and 3.00%, respectively
- Projected salary increases – 4.25% to 17.50%, depending upon service and nature of employment
- Cost-of-living adjustments – 2.75% and 3.00%, respectively

The mortality assumptions were based, respectively, on the results of the actuarial experience studies for the period January 1, 2014 through December 31, 2016 using the Headcount-Weighted RP-2014 Healthy Annuitant Mortality Table projected generationally using the two-dimensional Scale MP-2016 and for the period January 1, 2011 through December 31, 2013 using the RP-2000 Combined Healthy Mortality Table projected with the Society of Actuaries Scale BB to 2020. The mortality assumptions were then customized to account for the Plan's membership experience.

The discount rates used to measure the Plan's total pension liability were 7.00% and 7.25% at December 31, 2017 and 2016, respectively. The projection of cash flows used to determine the discount rates assumed that plan member contributions will be made at the current contribution rates and that employer contributions will be made at actuarially determined rates. Based on those assumptions, the Plan's fiduciary net position was projected to be available to make all projected future benefit payments for current plan members. Therefore, the long-term expected rate of return on plan investments was applied to all periods of projected benefit payments to determine the total pension liability. The long-term expected rate of return should be determined without reduction for plan administrative expense. The investment return assumptions are net of administrative expenses, assumed to be 14 and 16 basis points, respectively. The investment rate of return assumptions remained the same for reporting purposes due to the immaterial impact administrative expenses has on the overall assumed rate of return. The long-term expected rates of return on plan investments were determined using a building-block method in which best-estimate ranges of expected future real rates of return are developed for each major asset class. These returns are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentages and by adding expected inflation and deducting expected investment expenses.

(In thousands)

The target allocation and projected arithmetic real rate of return for each major asset class, after deducting inflation but before deducting investment expenses, used in the derivation of the long-term expected rate of return assumptions for each measurement date are summarized in the following table:

	December 31, 2017		December 31, 2016	
	Target allocation	**Long-term expected real rate of return**	**Target allocation**	**Long-term expected real rate of return**
Asset class:				
Global equity	35.00 %	6.38 %	— %	— %
Core bonds	13.00	1.03	10.00	0.73
High yield bonds	4.00	3.52	—	—
Bank loan	2.00	2.86	—	—
TIPS	4.00	0.96	—	—
Emerging market debt	4.00	3.78	3.00	4.00
Real estate	10.00	4.33	10.00	4.96
Core infrastructure	2.00	5.48	—	—
Natural resources	10.00	7.86	—	—
Risk mitigation	5.00	4.66	—	—
Mezzanine/distressed debts	3.00	6.53	—	—
Private equity	8.00	9.48	6.00	9.60
Large cap U.S. equity	—	—	14.90	5.92
Small/Mid cap U.S. equity	—	—	2.73	6.49
Developed international equity	—	—	10.88	6.90
Emerging international equity	—	—	6.49	8.34
Global bonds	—	—	2.00	0.30
Diversified credit (U.S.)	—	—	8.00	4.97
Diversified credit (non-U.S.)	—	—	2.00	6.76
Hedge funds	—	—	7.00	4.13
GTAA	—	—	7.00	4.22
Real return	—	—	10.00	5.86
Total	100.00 %		100.00 %	

(In thousands)

The following table presents the Agency's proportionate share of the Plan's net pension liability, calculated using the discount rates used in each year's actuarial valuation (7.0% for 2018 and 7.25% for 2017), as well as what its proportionate share of the net pension liability would be if it were calculated using a discount rate one percentage point lower (6.0% and 6.25%, respectively) or one percentage point higher (8.0% and 8.25%, respectively) than the assumed discount rate:

		June 30	
		2018	**2017**
Net pension liability, as calculated:			
With assumed discount rate	$	7,417	8,742
With a 1% decrease		12,121	12,745
With a 1% increase		3,596	5,448

(e) Plan's Fiduciary Net Position

OCERS provides publicly available financial information, including comprehensive annual financial reports and actuarial valuations at www.ocers.org. Detailed information about the Plan's fiduciary net position is included in the comprehensive annual financial report for the fiscal year ended December 31, 2017, which may also be obtained by calling (714) 558-6200.

Defined Contribution Plan – The Agency also sponsors a defined contribution plan under the provisions of Internal Revenue Code Section 457 that permits employees to defer portions of their pretax compensation. The Agency provides matching contributions to a related Section 401(a) plan, at a rate of 50% of the employees' deferral contributions, up to a maximum of 2% of each employee's related compensation. In connection with this plan, the Agency incurred $76 and $72 of expense for the years ended June 30, 2018 and 2017, respectively.

FOOTHILL/EASTERN TRANSPORTATION CORRIDOR AGENCY

Required Supplementary Information

Schedule of Net Pension Liability and Related Ratios

(Amounts in thousands)

(Unaudited)

	Plan year ended December 31			
	2017	2016	2015	2014
Agency's proportion (percentage) of the collective net pension liability	0.15 %	0.17 %	0.16 %	0.15 %
Agency's proportionate share (amount) of the collective net pension liability	$ 7,417	8,742	8,918	7,556
Agency's covered payroll	4,191	3,908	4,083	4,287
Agency's proportionate share of the collective net pension liability as a percentage of its covered payroll	177 %	224 %	218 %	176 %
Plan's fiduciary net position as a percentage of the total pension liability	74.93 %	71.16 %	67.10 %	69.42 %

Note – GASB Statement No. 68 requires a 10-year schedule presenting the items above. The applicable information has been presented for the periods since the statement was adopted, and will be supplemented as the same information becomes available for future periods.

See accompanying independent auditors' report.

FOOTHILL/EASTERN TRANSPORTATION CORRIDOR AGENCY

Required Supplementary Information

Schedule of Agency Contributions

(Amounts in thousands)

(Unaudited)

		Fiscal year ended June 30			
		2018	**2017**	**2016**	**2015**
Actuarially determined contributions	$	1,024	1,038	949	896
Contributions recognized		(1,024)	(1,038)	(949)	(896)
Difference	$	—	—	—	—
Agency's covered payroll	$	4,191	3,908	4,083	4,287
Contributions recognized as a percentage of covered payroll		24.4 %	26.6 %	23.2 %	20.9 %

Note – GASB Statement No. 68 requires a 10-year schedule presenting the items above. The applicable information has been presented for the periods since the statement was adopted, and will be supplemented as the same information becomes available for future periods.

See accompanying independent auditors' report.