

Orange County Local Transportation Authority
(A Component Unit of the Orange
County Transportation Authority)

ANNUAL FINANCIAL AND
COMPLIANCE REPORT

Year Ended June 30, 2012

Orange County Local Transportation Authority
(A Component Unit of the Orange County Transportation Authority)

Audited Financial Statements

Year Ended June 30, 2012

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INDEPENDENT AUDITORS' REPORT

Board of Directors
Orange County Local Transportation Authority
Orange, California

We have audited the accompanying financial statements of the governmental activities and each major fund of the Orange County Local Transportation Authority (OCLTA), a component unit of the Orange County Transportation Authority (OCTA), as of and for the year ended June 30, 2012, which collectively comprise OCLTA's basic financial statements as listed in the table of contents. These financial statements are the responsibility of OCLTA's management. Our responsibility is to express opinions 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 and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. 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 OCLTA'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 the 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 opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities and each major fund of OCLTA as of June 30, 2012, and the respective changes in financial position of OCLTA for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 29, 2012, on our consideration of OCLTA's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and budgetary comparison information on pages 3 through 9 and 33 through 34 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the OCLTA's financial statements. The debt service budgetary comparison schedule included on page 35 is presented for purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The debt service budgetary comparison schedule has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the debt service budgetary comparison schedule is fairly stated in all material respects in relation to the financial statements as a whole.



Laguna Hills, California
October 29, 2012

**Orange County Local Transportation Authority
Management's Discussion and Analysis
(unaudited)
For the Fiscal Year Ended June 30, 2012**

As management of the Orange County Local Transportation Authority (OCLTA), we offer readers of the OCLTA's financial statements this narrative overview and analysis of the OCLTA's Measure M financial activities for the fiscal year ended June 30, 2012. We encourage readers to consider the information on financial performance presented in conjunction with the financial statements that begin on page 10. All amounts, unless otherwise indicated, are expressed in thousands of dollars.

Financial Highlights

- Total net assets of the OCLTA were \$428,380 and consisted of net assets invested in capital assets, of \$184,066; restricted net assets of \$12,002; and unrestricted net assets of \$232,312.
- Net assets increased \$48,909 during fiscal year 2011-12. This increase was primarily due to sales tax revenue and operating grants and contributions in excess of program costs.
- Total capital assets, net of accumulated depreciation, were \$184,066 at June 30, 2012.
- OCLTA's governmental funds reported combined ending fund balances of \$570,339, an increase of \$51,114 from the prior year. The increase is primarily due to increased operating grants and contributions related to grade separation projects, Metrolink Service Expansion Program (MSEP) and grade crossing projects.

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the OCLTA's basic financial statements, which are comprised of three components including government-wide financial statements, fund financial statements and notes to the financial statements. This report also contains required supplementary information in addition to the basic financial statements. Because the OCLTA is a governmental activity of the Orange County Transportation Authority (OCTA), governmental funds are used to account for its Measure M program activities. The basic financial statements include only the activities of the OCLTA.

Government-wide Financial Statements

The government-wide financial statements are designed to provide readers with a broad overview of the OCLTA's finances using the accrual basis of accounting, in a manner similar to a private-sector business.

Orange County Local Transportation Authority Management's Discussion and Analysis

The statement of net assets presents information on all of the OCLTA's assets and liabilities, with the difference between assets and liabilities reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the OCLTA is improving or deteriorating.

The statement of activities presents information showing how the OCLTA's net assets changed during the fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows.

The government-wide financial statements can be found on pages 10-11 of this report.

Fund Financial Statements

A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. Fund accounting is used to ensure and demonstrate compliance with Measure M finance-related legal requirements. The OCLTA uses governmental funds.

Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements; however, governmental fund financial statements focus on near-term inflows and outflows of spendable resources and on balances of spendable resources available at the end of the fiscal year. Such information may be useful in evaluating the OCLTA's near-term financing requirements.

Since the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. As a result, readers may better understand the long-term impact of the OCLTA's near-term financing decisions. Both the governmental funds balance sheet and related statement of revenues, expenditures and changes in fund balances provide a reconciliation to facilitate this comparison between governmental funds and governmental activities.

The OCLTA maintains two individual governmental funds which are considered to be major funds. Information is presented separately in the governmental funds balance sheet and in the related statement of revenues, expenditures and changes in fund balances for the OCLTA's major governmental funds.

The governmental funds financial statements can be found on pages 12-15 of this report.

Notes to the financial statements provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found on pages 16-32 of this report.

**Orange County Local Transportation Authority
Management's Discussion and Analysis**

The OCLTA adopts an annual budget for its two funds. A budgetary comparison schedule has been provided for the LTA special revenue fund as required supplementary information on page 33 and the LTA debt service fund as other supplementary information on page 35 to demonstrate compliance with the annual appropriated budget.

Government-wide Financial Analysis

As noted previously, net assets may serve over time as a useful indicator of the OCLTA's financial position. At June 30, 2012, the OCLTA's assets exceeded liabilities by \$428,380, a \$48,909 increase from June 30, 2011. Our analysis below focuses on the net assets (Table 1) and changes in net assets (Table 2) of the OCLTA's governmental activities.

Current and other assets increased by \$32,061 or 5% from June 30, 2011. The increase is primarily due to cash received from increased sales tax revenue and operating grants and contributions.

Approximately 43% of OCLTA's net assets reflect its investment in capital assets, the majority of which is land purchased for right-of-way.

Restricted net assets, which are resources subjected to external restrictions on how they may be used, increased \$1,807 from June 30, 2011.

Unrestricted net assets represent the portion of net assets that are available for general use as specified in the M1 and M2 programs without constraints established by debt covenants, enabling legislation, or other legal requirements. Unrestricted net assets from governmental activities changed from \$185,176 at June 30, 2011 to \$232,312 at June 30, 2012. This increase was primarily due to the increase in operating grants and contributions related to grade separation projects, MSEP and grade crossing projects.

Table 1
Orange County Local Transportation Authority
Net Assets

| | Governmental Activities | |
|--------------------------|-------------------------|------------|
| | 2012 | 2011 |
| Current and other assets | \$ 718,404 | \$ 686,343 |
| Capital assets, net | 184,066 | 184,100 |
| Total assets | 902,470 | 870,443 |
| Current liabilities | 116,701 | 132,981 |
| Long-term liabilities | 357,389 | 357,991 |
| Total liabilities | 474,090 | 490,972 |

**Orange County Local Transportation Authority
Management's Discussion and Analysis**

| | Governmental Activities | |
|---|-------------------------|------------|
| | 2012 | 2011 |
| Net assets: | | |
| Invested in capital assets, net of related debt | 184,066 | 184,100 |
| Restricted | 12,002 | 10,195 |
| Unrestricted | 232,312 | 185,176 |
| Total net assets | \$ 428,380 | \$ 379,471 |

Governmental activities increased the OCLTA's net assets by \$48,909. Sales taxes, which ultimately financed a significant portion of the OCLTA's net costs, increased by \$16,522, or 7%, from the prior year as a result of a slight improvement in the economy. Operating grants and contributions increased \$49,063, or 55%, from the prior year primarily due to reimbursements related to MSEP, grade crossing and grade separation projects.

OCLTA expenses shown on the statement of activities consist of:

| | Governmental Activities | |
|---------------------------------------|-------------------------|------------|
| | 2012 | 2011 |
| Supplies and services | \$ 49,059 | \$ 47,106 |
| Contributions to other local agencies | 179,647 | 159,815 |
| Infrastructure | 86,366 | 67,975 |
| Depreciation expense | 40 | 43 |
| Interest expense | 21,922 | 14,583 |
| Bond issuance costs | - | 2,181 |
| Transfer to other OCTA funds | 2,683 | 121,193 |
| Total expenses | \$ 339,717 | \$ 412,896 |

Total expenses decreased \$73,179, or 18% from the prior year primarily due to the transfer of \$120,000 to the Commuter and Urban Rail Endowment (CURE) Fund to fund the MSEP and rail operations in the prior year. The decrease was offset by increased contributions for grade separation projects and the Anaheim Regional Transportation Intermodal Center (ARTIC), as well as a continued effort for MSEP and grade crossing projects.

Table 2
Orange County Local Transportation Authority
Changes in Net Assets

| | Governmental Activities | |
|------------------------------------|-------------------------|--------|
| | 2012 | 2011 |
| Revenues: | | |
| Program revenues: | | |
| Charges for services | \$ 664 | \$ 437 |
| Operating grants and contributions | 138,986 | 89,923 |

**Orange County Local Transportation Authority
Management's Discussion and Analysis**

| | Governmental Activities | |
|-------------------------------------|-------------------------|------------|
| | 2012 | 2011 |
| General revenues: | | |
| Sales taxes | 252,132 | 235,610 |
| Unrestricted investment earnings | 12,158 | 11,555 |
| Total revenues | 403,940 | 337,525 |
| Expenses: | | |
| Measure M program | 339,717 | 412,896 |
| Indirect expense allocation | 15,314 | 18,021 |
| Increase/ (decrease) in net assets | 48,909 | (93,392) |
| Net assets - beginning, as restated | 379,471 | 472,863 |
| Net assets - end of year | \$ 428,380 | \$ 379,471 |

Financial Analysis of the OCLTA's Funds

As of June 30, 2012, the OCLTA's governmental funds reported combined ending fund balances of \$570,339, an increase of \$51,114 compared to 2011. The majority of fund balances, 96%, is assigned for transportation programs related to Measure M projects. Fund balance of \$12,002 is restricted for debt service on M2 sales tax revenue bonds issued to accelerate funding for M2 projects. The remaining fund balance of \$9,087 is considered nonspendable as the funds have been deposited with the State for condemnation deposits.

OCLTA's major governmental funds include the following significant changes:

The LTA fund increased by \$49,307, primarily due to an increase in operating grants and contributions for the MSEP, grade crossing and grade separation projects, and an increase in sales tax revenue due to the improving economy. This increase was offset by an increase in expenditures primarily for ARTIC and the grade separation projects.

Capital Asset and Debt Administration

Capital Assets

As of June 30, 2012, the OCLTA had \$184,066, net of accumulated depreciation, invested in a broad range of capital assets including land, improvements and machinery.

**Orange County Local Transportation Authority
Management's Discussion and Analysis**

A summary of the OCLTA's capital assets, net of depreciation, follows:

| | Governmental Activities | |
|-------------------------------|-------------------------|-------------------|
| | 2012 | 2011 |
| Land | \$183,304 | \$183,304 |
| Improvements | 1,086 | 1,086 |
| Machinery | 32 | 26 |
| Total capital assets | 184,422 | 184,416 |
| Less accumulated depreciation | (356) | (316) |
| Total capital assets, net | <u>\$ 184,066</u> | <u>\$ 184,100</u> |

More detailed information about the OCLTA's capital assets is presented in note 6 to the financial statements.

OCTA has outstanding capital expenditure commitments, the most significant of which are: \$46,477 for the MSEP, \$16,228 for the Sand Canyon Grade Separation project, \$27,915 for the Kraemer Boulevard Grade Separation project, and \$19,401 for the Placentia Avenue Grade Separation project.

Debt Administration

As of June 30, 2012, the OCLTA had \$377,570 in sales tax revenue bonds and commercial paper notes outstanding, as follows:

| | Governmental Activities | |
|-------------------------|-------------------------|------------------|
| | 2012 | 2011 |
| Sales tax revenue bonds | \$352,570 | \$ 352,570 |
| Commercial paper notes | 25,000 | 25,000 |
| Totals | <u>\$377,570</u> | <u>\$377,570</u> |

The OCLTA maintains an "AA+" rating from Standard & Poor's Corporation (S & P), an "AA+" rating from Fitch Ratings (Fitch) and an "Aa2" rating from Moody's Investors Services (Moody's) for its M2 Sales Tax Revenue Bonds.

Additional information on the OCLTA's short-term debt and long-term debt can be found in Notes 7 and 8 to the financial statements, respectively.

Economic and Other Factors

The OCLTA includes the Measure M program half cent sales tax which has delivered on promises made to the residents of Orange County in 1990, with over \$4 billion invested in improvements to freeways, streets and roads and transit services. M1 ended March 2011, and collection of sales tax under M2 began in April 2011. M2 was overwhelmingly approved by the voters of Orange County in 2006 because of the tangible results that were realized through M1. The passage of M2 has allowed for the continuation of transportation improvements for 30 more years. In an effort to expedite transportation projects, the OCTA Board approved the M2 Early Action Plan (EAP) in 2007, paving the way for financing

Orange County Local Transportation Authority Management's Discussion and Analysis

projects in 2007 through 2012. Under the EAP, five M2 freeway projects were scheduled to be under construction before revenues were collected in 2011.

As a result of an economic recession, which has led to an approximate 40% reduction in program revenue, project schedules and policy decisions required adjustments since the adoption of the EAP. In July 2010 the Board approved the comprehensive Capital Action Plan (CAP). The CAP expanded the scope of the EAP to include other priority OCTA capital projects. Despite the major impact to revenue assumptions, OCTA has made significant progress in implementing the plan through aggressively seeking additional grant funding and a competitive construction market. All major elements of the Board directed EAP and CAP are nearing completion and a new plan, M2020, outlining the projects and programs for all modes that can be accomplished between now and the year 2020 was adopted by the Board of Directors on September 10, 2012.

M2020 presents strategies to accelerate Measure M2 improvements by delivering early on promises made to the voters. Accelerating projects offers advantages including leveraging today's favorable bidding environment and low debt costs, minimizing the risk of future inflation, and bringing mobility improvements sooner. This plan also sets OCTA on a course to go beyond the early implementation projects if additional external funds can be accessed earlier.

The projects under M2020 include freeway improvements projects, transit capital projects, and rail transit projects. These, and other critical capital projects, will be captured in a more comprehensive capital program document that will continue to ensure coordinated project delivery and decision making with respect to resource management, funding, and procedures.

The OCLTA adopted its fiscal year 2012-13 annual budget on June 11, 2012. This \$581.2 million balanced budget includes both M1 and M2. The M1 budget totals \$111.6 million and includes payments to cities and the County of Orange for the fair share and competitive programs, investment in rolling stock for the MSEP, and the ARTIC project. The M2 budget totals \$469.6 million and includes funds for the grade separation projects, grade crossing and quiet zones, environmental mitigation and work related to several freeway projects that have been identified in the Board-approved CAP and M2020.

Contacting the OCLTA's Management

This financial report is designed to provide a general overview of the OCLTA's finances for all those with an interest in the OCLTA's finances and to demonstrate OCLTA accountability for the money it receives. Questions concerning any of the information provided in this report or requests for additional information should be addressed to the Finance and Administration Division of the Orange County Transportation Authority, 550 South Main Street, P.O. Box 14184, Orange, California 92863-1584.

ORANGE COUNTY LOCAL TRANSPORTATION AUTHORITY
(A Component Unit of the Orange County Transportation Authority)
Statement of Net Assets
June 30, 2012

| <i>(amounts expressed in thousands)</i> | Governmental Activities |
|---|------------------------------------|
| Assets | |
| Cash and investments | \$ 599,078 |
| Receivables: | |
| Interest | 1,500 |
| Operating grants | 16,049 |
| Other | 681 |
| Due from other governments | 83,385 |
| Condemnation deposits | 9,087 |
| Other assets | 2,001 |
| Assets held for resale | 6,623 |
| Capital assets: | |
| Nondepreciable | 183,304 |
| Depreciable, net | 762 |
| Total Assets | 902,470 |
| Liabilities | |
| Accounts payable | 26,361 |
| Accrued interest payable | 8,363 |
| Due to other governments | 38,759 |
| Unearned revenue | 12,547 |
| Other liabilities | 44 |
| Advance from other OCTA funds | 5,627 |
| Commercial paper notes | 25,000 |
| Noncurrent liabilities: | |
| Due within one year | 6,410 |
| Due in more than one year | 350,979 |
| Total Liabilities | 474,090 |
| Net Assets | |
| Invested in capital assets | 184,066 |
| Restricted for: | |
| Debt Service | 12,002 |
| Unrestricted for: | |
| Measure M program | 232,312 |
| Total Net Assets | \$ 428,380 |

See accompanying notes to the financial statements.

ORANGE COUNTY LOCAL TRANSPORTATION AUTHORITY
(A Component Unit of the Orange County Transportation Authority)
Statement of Activities
Year Ended June 30, 2012

| <i>(amounts expressed in thousands)</i> | Expenses | Indirect Expense Allocation | Program Revenues | | Net (Expense) Revenue and Changes in Net Assets |
|---|------------|-----------------------------------|-------------------------|--|--|
| | | | Charges for Services | Operating Grants and Contributions | Governmental Activities |
| Program governmental activities: | | | | | |
| Measure M program | \$ 339,717 | \$ 15,314 | \$ 664 | \$ 138,986 | \$ (215,381) |
| Total governmental activities | 339,717 | 15,314 | 664 | 138,986 | (215,381) |
| General revenues: | | | | | |
| Sales taxes | | | | | 252,132 |
| Unrestricted investment earnings | | | | | 12,158 |
| Total general revenues | | | | | 264,290 |
| Change in net assets | | | | | 48,909 |
| Net assets - beginning | | | | | 379,471 |
| Net assets - ending | | | | | \$ 428,380 |

See accompanying notes to the financial statements.

ORANGE COUNTY LOCAL TRANSPORTATION AUTHORITY
(A Component Unit of the Orange County Transportation Authority)
Balance Sheet - Governmental Funds
June 30, 2012

| <i>(amounts expressed in thousands)</i> | LTA | LTA Debt Service | Total OCLTA |
|--|-------------------|---------------------|-------------------|
| Assets | | | |
| Cash and investments | \$ 587,078 | \$ 12,000 | \$ 599,078 |
| Receivables: | | | |
| Interest | 1,498 | 2 | 1,500 |
| Operating grants | 16,049 | - | 16,049 |
| Other | 681 | - | 681 |
| Due from other governments | 80,790 | - | 80,790 |
| Condemnation deposits | 9,087 | - | 9,087 |
| Total Assets | \$ 695,183 | \$ 12,002 | \$ 707,185 |
| Liabilities and Fund Balances | | | |
| Liabilities | | | |
| Accounts payable | \$ 26,361 | \$ - | \$ 26,361 |
| Due to other governments | 38,759 | - | 38,759 |
| Deferred revenue | 41,055 | - | 41,055 |
| Other liabilities | 44 | - | 44 |
| Advance from OCTA | 5,627 | - | 5,627 |
| Commercial paper notes | 25,000 | - | 25,000 |
| Total Liabilities | 136,846 | - | 136,846 |
| Fund Balances | | | |
| Nonspendable: | | | |
| Condemnation deposits | 9,087 | - | 9,087 |
| Restricted for: | | | |
| Debt service | - | 12,002 | 12,002 |
| Assigned to: | | | |
| Transportation programs | 549,250 | - | 549,250 |
| Total Fund Balances | 558,337 | 12,002 | 570,339 |
| Total Liabilities and Fund Balances | \$ 695,183 | \$ 12,002 | \$ 707,185 |

See accompanying notes to the financial statements.

ORANGE COUNTY LOCAL TRANSPORTATION AUTHORITY
(A Component Unit of the Orange County Transportation Authority)
Reconciliation of the Balance Sheet of Governmental Funds
to the Statement of Net Assets
June 30, 2012

(amounts expressed in thousands)

Amounts reported for governmental activities in the Statement of Net Assets (page 10) are different because:

| | | |
|--|-----------|------------------------------|
| Total fund balances (page 12) | \$ | 570,339 |
| Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds. | | 184,066 |
| Interest receivable on the Build America Bonds is not reported in the funds. | | 2,595 |
| Assets held for resale are not financial resources and, therefore, are not reported in the funds. | | 6,623 |
| Other long-term assets related to cost of issuance are not financial resources and, therefore, are not reported in the funds. | | 2,001 |
| Earned but unavailable revenue is not available to liquidate current liabilities and, therefore, is deferred in the funds. | | 28,508 |
| Interest payable on bonds outstanding is not due and payable in the current period and, therefore, is not reported in the funds. | | (8,363) |
| Long-term liabilities, including bonds payable, are not due and payable in the current period and, therefore, are not reported in the funds. | | <u>(357,389)</u> |
| Net assets of governmental activities (page 10) | \$ | <u><u>428,380</u></u> |

See accompanying notes to the financial statements.

ORANGE COUNTY LOCAL TRANSPORTATION AUTHORITY
(A Component Unit of the Orange County Transportation Authority)
Statement of Revenues, Expenditures and Changes in Fund Balances
Governmental Funds
Year Ended June 30, 2012

| <i>(amounts expressed in thousands)</i> | LTA | LTA Debt Service | Total OCLTA |
|--|-------------------|---------------------|-------------------|
| Revenues | | | |
| Sales taxes | \$ 252,132 | \$ - | \$ 252,132 |
| Contributions from other agencies | 139,007 | - | 139,007 |
| Interest | 5,393 | 6,967 | 12,360 |
| Miscellaneous | 665 | - | 665 |
| Total Revenues | 397,197 | 6,967 | 404,164 |
| Expenditures | | | |
| Current: | | | |
| General government: | | | |
| Supplies and services | 64,281 | - | 64,281 |
| Transportation: | | | |
| Contributions to other local agencies | 179,647 | - | 179,647 |
| Capital outlay | 86,372 | - | 86,372 |
| Debt service: | | | |
| Interest | 125 | 22,383 | 22,508 |
| Total Expenditures | 330,425 | 22,383 | 352,808 |
| Excess (deficiency) of revenues over (under) expenditures | 66,772 | (15,416) | 51,356 |
| Other financing sources (uses) | | | |
| Transfers in | - | 17,223 | 17,223 |
| Transfers from OCTA | 2,441 | - | 2,441 |
| Transfers out | (17,223) | - | (17,223) |
| Transfers to OCTA | (2,683) | - | (2,683) |
| Total other financing sources (uses) | (17,465) | 17,223 | (242) |
| Net change in fund balances | 49,307 | 1,807 | 51,114 |
| Fund balances - beginning | 509,030 | 10,195 | 519,225 |
| Fund balances - ending | \$ 558,337 | \$ 12,002 | \$ 570,339 |

See accompanying notes to the financial statements.

ORANGE COUNTY LOCAL TRANSPORTATION AUTHORITY
(A Component Unit of the Orange County Transportation Authority)
Reconciliation of the Statement of Revenues, Expenditures and Changes in
Fund Balances of Governmental Funds to the Statement of Activities
Year Ended June 30, 2012

(amounts expressed in thousands)

Amounts reported for governmental activities in the Statement of Activities (page 11) are different because:

| | |
|---|------------------|
| Net change in fund balances - total governmental funds (page 14) | \$ 51,114 |
| Governmental funds report capital outlays as expenditures. However, in the statement of activities the cost of those assets is allocated over their estimated useful lives and reported as depreciation and amortization expense. This is the amount by which capital outlays exceeded depreciation in the current period. | (34) |
| Revenues in the statement of activities that do not provide current financial resources are not reported as revenue in the funds. | (2,666) |
| The issuance of long-term debt (e.g., bonds) provides current financial resources to governmental funds, while the repayment of principal of long-term debt consumes current financial resources of governmental funds. Neither transaction, however, has any effect on net assets. Also, governmental funds report the effect of issuance costs, premiums, discounts, and similar items when debt is first issued, whereas these amounts are deferred and amortized in the statement of activities. This amount is the net effect of these differences in the treatment of long-term debt and related items. | 495 |
| Change in net assets of governmental activities (page 11) | \$ 48,909 |

See accompanying notes to the financial statements.

Orange County Local Transportation Authority
(A Component Unit of the Orange County Transportation Authority)

Notes to The Financial Statements

Year Ended June 30, 2012

(in thousands)

1. Summary of Significant Accounting Policies

Reporting Entity

In November 1990, Orange County voters approved the Revised Traffic Improvement and Growth Management Ordinance, known as Measure M. This implemented a one-half of one percent retail transaction and use tax to fund a specific program of transportation improvements in Orange County. The Orange County Local Transportation Authority (OCLTA) is responsible for administering the proceeds of the Measure M sales tax program. The original Measure M Program (M1) commenced on April 1, 1991 for a period of 20 years. Under M1, funds are required to be distributed to four modes: freeways, regional streets and roads, local streets and roads, and transit.

On November 7, 2006, Orange County voters approved the renewal of Measure M for a period of 30 more years from April 1, 2011 to March 31, 2041. Renewed Measure M (M2) allocates funds to freeway, street and road, transit, and environmental improvements.

On June 20, 1991, under the authority of Senate Bill 838, the Orange County Transportation Authority (OCTA) was formed as a special district by merging several agencies and funds, including the OCLTA, a component unit of the OCTA. Accordingly, the OCLTA's financial activities are included with the financial activities of OCTA for financial reporting purposes.

The OCTA governing board (Board) consists of 17 voting members and functions as the OCLTA governing board. Measure M requires that an eleven-member Taxpayer's Oversight Committee (TOC) monitors the use of Measure M funds and ensures that all revenue collected from Measure M is spent on voter-approved transportation projects.

These financial statements include only the activities of the OCLTA, a component unit of the OCTA. These financial statements are not intended to present the activities of OCTA.

Basis of Presentation

The OCLTA's basic financial statements consist of government-wide statements, including a statement of net assets and a statement of activities, and fund financial statements which provide a more detailed level of financial information.

Government-wide Statements: The statement of net assets and the statement of activities report information on all of the OCLTA. The effect of significant interfund activity has been removed from these statements. The OCLTA provides only governmental activities which are supported principally by sales taxes.

Orange County Local Transportation Authority
Notes to The Financial Statements

Year Ended June 30, 2012
(in thousands)

The statement of activities demonstrates the degree to which the OCLTA Measure M program expenses are offset by program revenues. Program expenses include direct expenses, which are clearly identifiable with Measure M, and allocated indirect expenses. Interest expense related to the sales tax revenue bonds and commercial paper is reported as a direct expense of the Measure M program. The borrowings are considered essential to the creation or continuing existence of the Measure M program. For the year ended June 30, 2012, interest expense of \$21,922 was included in Measure M program costs. Program revenues include: 1) charges to customers or applicants who purchase, use, or directly benefit from services or privileges provided by Measure M; and 2) grants and contributions that are restricted to meeting the operational or capital requirements of the Measure M program. Taxes and other items, which are properly not included among program revenues, are reported instead as general revenues.

Fund Financial Statements: The fund financial statements provide information about the OCLTA's governmental funds. The OCLTA considers all of its Measure M funds as major governmental funds. They are comprised of the following:

- *Local Transportation Authority (LTA) Fund* - This fund is the general operating fund for the OCLTA and accounts for revenues received and expenditures made for the implementation of the Orange County Traffic Improvement and Growth Management Plan. Financing is provided by a one-half percent sales and use tax assessed for 20 years pursuant to Measure M, which became effective April 1, 1991, and was recently renewed for an additional 30 years from April 1, 2011 to March 31, 2041. The Measure M ordinance requires that sales tax revenues only be expended on projects included in the ordinance. A decision to use the revenues for any other purpose must be put to the voters in another election.
- *LTA Debt Service Fund* - This fund accounts for the resources accumulated and payments made for principal and interest on long-term debt of the OCLTA.

Measurement Focus and Basis of Accounting

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned, and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the OCLTA considers revenues to be available if they are collected within 90 days of the end of the fiscal period. Expenditures generally are recorded when a liability is incurred; however, principal and interest expenditures on long-term debt of governmental funds are recorded only when payment is due.

Orange County Local Transportation Authority
Notes to The Financial Statements

Year Ended June 30, 2012
(in thousands)

Those revenues susceptible to accrual are sales taxes collected and held by the state at year-end on behalf of the OCLTA, intergovernmental revenues and interest revenue. In applying the susceptible-to-accrual concept to intergovernmental revenues, there are essentially two types of revenues. In one, monies must be expended on the specific purpose or project before any amounts will be paid to the OCLTA; therefore, revenues are recognized based upon the expenditures incurred. In the other, monies are virtually unrestricted and are usually revocable only for failure to comply with prescribed requirements. These resources are reflected as revenues at the time of receipt, or earlier if the susceptible-to-accrual criteria are met.

Cash and Investments

The OCLTA maintains cash and investments in a pool with other OCTA cash and investments and in accordance with the Annual Investment Policy (AIP) adopted by the Board on May 8, 1995, and most recently amended January 9, 2012. The AIP complies with, or is more restrictive than, the California Government Code (Code). Separate investment manager accounts are maintained for the proceeds of bond issues, with the earnings for each bond issue accounted for separately. Pooled cash and investment earnings are allocated based on average daily dollar account balances.

Investments in U.S. government and U.S. agency securities, medium term notes, repurchase agreements, variable and floating rate securities, commercial paper, mortgage and asset-backed securities, and corporate notes are carried at fair value based on quoted market prices, except for securities with a remaining maturity of one year or less at purchase date, which are carried at cost. Treasury mutual funds are carried at fair value based on each fund's share price. The Orange County Investment Pool (OCIP) is carried at fair value based on the value of each participating dollar as provided by the OCIP. The state-managed Local Agency Investment Fund (LAIF) is carried at fair value based on the value of each participating dollar as provided by LAIF.

The AIP requires that assets in the portfolio consist of the following investments, with maximum permissible concentrations based on book value, and may be more restrictive than applicable state statutes for the following investment types: OCTA notes and bonds, U.S. treasuries, federal instrumentality securities, federal agencies, State of California and local agency obligations, bankers acceptance, commercial paper, negotiable certificates of deposit, repurchase agreements, medium-term maturity corporate securities, money market funds, other mutual funds, mortgage or asset-backed securities, LAIF, OCIP, variable and floating rate securities and bank deposits. Investment agreements are also allowed for bond issues.

Interfund Transactions

During the course of operations, numerous transactions occur between individual funds involving goods provided or services rendered and transfers of revenues from funds authorized to receive the revenue to funds authorized to expend it. Outstanding interfund balances are reported as due to/from other funds. Any residual balances outstanding

Orange County Local Transportation Authority
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between the Measure M program governmental activities and other OCTA funds are reported in the government-wide financial statements as due to/from other OCTA funds.

OCTA allocates indirect costs related to administrative services from certain funds to benefiting funds. For fiscal year 2011-12, \$15,314 of administrative services were charged to the OCLTA and are reported as general government expenditures in the governmental funds.

Capital Assets

Capital assets including land, right-of-way improvements, and machinery and equipment, are reported in the government-wide financial statements. Capital assets are defined by the OCLTA as assets with an initial, individual cost of more than \$5 and a useful life exceeding one year. Assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair value at the date of donation. The costs of normal maintenance and repairs that do not add to the value of an asset or materially extend an asset's life are not capitalized.

Freeway construction and certain purchases of right-of-way property, for which title vests with the California Department of Transportation (Caltrans), are included in capital outlay. Infrastructure consisting primarily of freeway construction and right-of-way acquisition is not recorded as a capital asset in those instances where the OCLTA does not intend to maintain or operate the property when complete.

Right-of-way improvements and machinery and equipment are depreciated using the straight line method over the following estimated useful lives:

| <u>Asset Type</u> | <u>Useful Life</u> |
|---------------------------|--------------------|
| Right-of-way improvements | 10-30 years |
| Machinery and equipment | 3-10 years |

Assets Held for Resale

OCLTA holds title to property in connection with the purchase of rights-of-way for infrastructure not held by OCLTA (see above). These assets are reported as assets held for resale in the government-wide financial statements and will be sold and the proceeds reimbursed to the project that funded the expenditure.

Long-Term Debt

In the government-wide financial statements, long-term debt is reported as a liability in the statement of net assets. Bond premiums and discounts and bond refunding costs, as well as issuance costs, are deferred and amortized over the life of the bonds using the straight-line method, which approximates the effective interest method. Bonds payable are reported net of the applicable bond premium or discount and deferred bond refunding loss. Bond issuance costs are reported as other assets and amortized over the life of the related debt.

Orange County Local Transportation Authority
Notes to The Financial Statements

Year Ended June 30, 2012
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In the fund financial statements, governmental funds recognize bond premiums and discounts, as well as bond issuance costs, in the current period. The face amount of debt is reported as other financing sources. Premiums received on debt issuances are reported as other financing sources, while discounts on debt issuances are reported as other financing uses. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures.

Contributions to Other Agencies

Contributions to other agencies primarily represent sales tax revenues received by the OCLTA disbursed to cities for competitive projects, the local fair share program, and the senior mobility program, and to other agencies for projects which are in accordance with the Measure M ordinance.

Net Assets

In the government-wide financial statements, net assets represent the difference between assets and liabilities and are classified into three categories:

- *Invested in capital assets* - This balance reflects the net assets of the OCLTA that are invested in capital assets. These net assets are generally not accessible for other purposes.
- *Restricted net assets* - This balance represents net assets that are not accessible for general use because their use is subject to restrictions enforceable by third parties. The government-wide statement of net assets reports net assets restricted by external parties for debt service.
- *Unrestricted net assets* - This balance represents those net assets that are available for general use as specified in the M1 and M2 programs.

Fund Balances

The governmental fund financial statements present fund balances based on classifications that comprise a hierarchy that is based primarily on the extent to which OCLTA is bound to honor constraints on the specific purposes for which amounts can be spent.

The classifications used in the governmental fund financial statements are as follows:

- *Nonspendable* - amounts that cannot be spent either because they are not in spendable form or because they are legally or contractually required to be maintained intact.
- *Restricted* - amounts that can be spent only for specific purposes because of constitutional provisions or enabling legislation or because of constraints that are externally imposed by creditors, grantors, contributors, or the laws or regulations of other governments.

Orange County Local Transportation Authority
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- *Assigned* – amounts that do not meet the criteria to be classified as restricted or committed but that are intended to be used for specific purposes. OCLTA’s assigned fund balance represents the remaining amounts reported in governmental funds. The Board retains the authority to assign fund balance.

When both restricted and unrestricted resources are available for use, it is OCLTA’s policy to use restricted resources first and then unrestricted resources as they are needed. When using unrestricted fund balance amounts, OCLTA applies the default established by GASB 54, whereby the committed amounts would be reduced first followed by the assigned amounts.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect certain reported amounts and disclosures during the reporting period. As such, actual results could differ from those estimates.

2. Reconciliation of Government-wide and Fund Financial Statements

Explanation of Certain Differences Between the Governmental Funds Balance Sheet and the Government-wide Statement of Net Assets

The governmental funds balance sheet includes a reconciliation between fund balances - total governmental funds and net assets - governmental activities as reported in the government-wide statement of net assets.

One element of that reconciliation explains that “Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds.” The details of this \$184,066 difference are as follows:

| | |
|---|-------------------------|
| Capital assets | \$184,422 |
| Less accumulated depreciation | <u>(356)</u> |
| Net adjustment to increase fund balances - total governmental funds to arrive at net assets - governmental activities | <u><u>\$184,066</u></u> |

Another element of that reconciliation explains that “Long-term liabilities, including bonds payable, are not due and payable in the current period and therefore are not reported in the funds.” The details of this \$(357,389) difference are as follows:

| | |
|---|----------------------------|
| Bonds payable | \$ (352,570) |
| Plus unamortized bond issuance premium (to be amortized to interest expense) | <u>(4,819)</u> |
| Net adjustment to decrease fund balances - total governmental funds to arrive at net assets - governmental activities | <u><u>\$ (357,389)</u></u> |

Orange County Local Transportation Authority
Notes to The Financial Statements

Year Ended June 30, 2012
(in thousands)

Explanation of Certain Differences Between the Governmental Funds Statement of Revenues, Expenditures and Changes in Fund Balances and the Government-wide Statement of Activities

The governmental funds statement of revenues, expenditures and changes in fund balances includes a reconciliation between net changes in fund balances - total governmental funds and change in net assets - governmental activities as reported in the government-wide statement of activities.

One element of that reconciliation explains that "Governmental funds report capital outlays as expenditures. However, in the statement of activities the cost of those assets is allocated over their estimated useful lives and reported as depreciation and amortization expense." The details of this \$34 difference are as follows:

| | |
|---|-------------|
| Capital outlay | \$ 6 |
| Depreciation expense | (40) |
| | <hr/> |
| Net adjustment to increase net change in fund balances - total governmental funds to arrive at change in net assets - governmental activities | \$ 34 |
| | <hr/> <hr/> |

Another element of that reconciliation states that "The issuance of long-term debt (e.g., bonds) provides current financial resources to governmental funds, while the repayment of the principal of long-term debt consumes the current financial resources of governmental funds. Neither transaction, however, has any effect on net assets. Also, governmental funds report the effect of issuance costs, premiums, discounts, and similar items when debt is first issued, whereas these amounts are deferred and amortized in the statement of activities." The details of this \$495 difference are as follows:

| | |
|--|-------------|
| Change in accrued interest | \$ (16) |
| Amortization of premium | 602 |
| Amortization of issuance costs | (91) |
| | <hr/> |
| Net adjustment to increase net change in fund balances - total governmental funds to arrive at change in net assets -governmental activities | \$ 495 |
| | <hr/> <hr/> |

3. Cash and Investments

Cash and investments are comprised of the following at June 30, 2012:

| | |
|--------------------------------------|-------------|
| Investments: | |
| With OCTA Commingled Investment Pool | \$ 398,529 |
| With Trustee | 200,549 |
| | <hr/> |
| Total cash and investments | \$ 599,078 |
| | <hr/> <hr/> |

Orange County Local Transportation Authority
Notes to The Financial Statements

Year Ended June 30, 2012
(in thousands)

Total deposits and investments are reported in the financial statements as:

| | |
|----------------------------|-------------------|
| Cash and Investments | \$ 599,078 |
| Total Cash and Investments | <u>\$ 599,078</u> |

As of June 30, 2012, OCLTA had the following investments:

| Investment | Fair Value | Principal | Interest Rate Range | Maturity Range | Weighted Average Maturity (Years) |
|--------------------------------------|------------------|------------------|-------------------------|---------------------|-----------------------------------|
| OCTA Commingled Investment Pool | \$398,529 | \$397,834 | Discount .125%-8.00% | 7/1/12- 6/26/17 | 1.62 |
| U.S. Treasury Notes | 21,336 | 21,358 | .375% - 1.75% | 7/31/12- 4/15/13 | .32 |
| U.S. Agency Notes | 57,248 | 57,682 | Discount .25%-6.045% | 7/30/12- 5/29/13 | .34 |
| Medium Term Notes | 34,201 | 35,013 | 1.95%-7.00% | 7/1/12- 5/15/13 | .48 |
| Mortgage and Asset Backed Securities | 12,432 | 12,495 | .299%-6.5% | 7/18/13- 2/15/16 | 2.27 |
| Variable Rate Notes | 702 | 702 | Discount | 2/22/13 | .65 |
| Money Market & Mutual Funds | 65,647 | 65,647 | Variable | 7/1/12 | 1 Day |
| Commercial Paper | 8,983 | 8,983 | Discount | 7/2/12- 11/19/12 | .21 |
| Total Investments | <u>\$599,078</u> | <u>\$599,714</u> | | | |
| Portfolio Weighted Average Maturity | | | | | 1.43 |

Interest Rate Risk

OCTA manages exposure to declines in fair value from increasing interest rates by having an investment policy that limits maturities to five years while also staggering maturities. OCTA maintains a low duration strategy, targeting an estimated average portfolio duration of three years or less, with the intent of reducing interest rate risk. Portfolios with low duration are less volatile, therefore, less sensitive to interest rate changes. In accordance with the OCTA investment policy, amounts restricted for debt service reserves are invested in accordance with the maturity provision of their specific indenture, which may extend beyond five years.

Orange County Local Transportation Authority
Notes to The Financial Statements

Year Ended June 30, 2012
(in thousands)

As of June 30, 2012, OCLTA was a participant in OCTA's commingled investment pool which had mortgage and asset-backed securities totaling \$39,034. The underlying assets are consumer receivables that include credit cards, auto and home loans. The securities have a fixed interest rate and are rated AAA by at least two of the three nationally recognized rating services organizations.

As of June 30, 2012, OCTA's commingled investment pool and OCLTA held the following variable rate notes (LIBOR refers to the London Interbank Offered Rate):

| Investment | Fair Value | Coupon Multiplier | Coupon Reset Date |
|---------------------------|-----------------|--------------------------|-------------------|
| American Express | \$ 941 | LIBOR + 170 basis points | Monthly |
| Caterpillar Financial | 702 | LIBOR + 16 basis points | Quarterly |
| Citigroup | 680 | LIBOR + 85 basis points | Quarterly |
| Goldman Sachs | 642 | LIBOR + 100 basis points | Quarterly |
| Morgan Stanley | 838 | LIBOR + 98 basis points | Quarterly |
| New York Life | 999 | LIBOR + 26 basis points | Quarterly |
| PACCAR Financial | 632 | LIBOR + 45 basis points | Monthly |
| Target Corporate Series | 1,103 | LIBOR + 17 basis points | Quarterly |
| VF Corporate Notes | 500 | LIBOR + 75 basis point | Quarterly |
| Total Variable Rate Notes | <u>\$ 7,037</u> | | |

Custodial Credit Risk

Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, a government will not be able to recover its deposits or will not be able to recover collateral securities that are in the possession of an outside party. The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty (e.g., broker-dealer) to a transaction, a government will not be able to recover the value of its investment or collateral securities that are in the possession of another party. OCTA's investment policy requires that a third party bank custody department hold all securities owned by OCTA. All trades are settled on a delivery versus payment basis through OCTA's safekeeping agent. At June 30, 2012, OCTA did not have any deposits or securities exposed to custodial credit risk and there was no securities lending.

Credit Risk

The AIP sets minimum acceptable credit ratings for investments from any of the three nationally recognized rating services organizations: S&P, Moody's, and Fitch. For an issuer of short-term debt, the rating must be no less than A-1 (S&P), P-1 (Moody's), or F-1 (Fitch), while an issuer of long-term debt shall be rated no less than an "A" by two of the three rating services. LAIF and the OCTA Commingled Investment Pool is not rated.

Orange County Local Transportation Authority
Notes to The Financial Statements

Year Ended June 30, 2012
(in thousands)

The following is a summary of the credit quality distribution and concentration of credit risk by investment type as a percentage of each pool's fair value at June 30, 2012. (NR means Not Rated, US means obligation of the United States (U.S.) government or obligations explicitly guaranteed by the U. S. government):

| Investments | S&P | Moody's | Fitch | % of Portfolio |
|---------------------------------------|-----|---------|-------|----------------|
| OCTA Commingled Investment Pool | NR | NR | NR | 66.37% |
| Held by Trustee: | | | | |
| U.S. Treasury Notes | AA | Aaa | AAA | 3.58% |
| U.S. Agency Notes | AA | Aaa | AAA | 9.60% |
| Medium Term Notes: | | | | |
| Corporate Notes | AA | Aaa | AAA | 0.63% |
| Corporate Notes | AA | Aa | AA | 0.65% |
| Corporate Notes | AA | Aa | A | 0.34% |
| Corporate Notes | AA | Aa | NR | 1.08% |
| Corporate Notes | AA | A | A | 0.09% |
| Corporate Notes | AA | A | NR | 0.65% |
| Corporate Notes | A | Aa | AA | 0.33% |
| Corporate Notes | A | A | AA | 0.36% |
| Corporate Notes | A | A | A | 1.23% |
| Corporate Notes | A | A | NR | 0.14% |
| Corporate Notes | A | Baa | A | 0.15% |
| Corporate Notes | A | NR | A | 0.08% |
| Mortgage and Asset Backed Securities: | | | | |
| Securities | AAA | Aaa | AAA | 1.10% |
| Securities | AAA | Aaa | NR | 0.58% |
| Securities | AA | Aaa | AAA | 0.05% |
| Securities | NR | Aaa | AAA | 0.12% |
| Securities | NR | Aaa | NR | 0.23% |
| Variable Rate Notes | A | A | A | 0.12% |
| Money Market and Mutual Funds | AAA | Aaa | AAA | 11.01% |
| Commercial Paper: | | | | |
| Various | A-1 | P-1 | F1 | 0.88% |
| Various | A-1 | P-1 | NR | 0.63% |
| Total | | | | <u>100%</u> |

Orange County Local Transportation Authority
Notes to The Financial Statements

Year Ended June 30, 2012
(in thousands)

Concentration of Credit Risk

At June 30, 2012, OCTA did not exceed the AIP maximum concentrations as stated below:

Issuer/Counter-Party Diversification Guidelines for All Securities Except Federal Agencies, Federal Instrumentalities, Investment Agreements, Repurchase Agreements and 91 Express Lanes Debt.

- 5% for any one corporation, bank, local agency, special purpose vehicle or other corporate name for one or more series of securities.

Issuer/Counter-Party Diversification Guidelines for Federal Agencies, Federal Instruments and Repurchase Agreements.

- 35% for any one Federal Agency or Federal Instrumentalities.
- 50% for any one repurchase agreement counter-party name if the maturity/term is less than or equal to 7 days.
- 35% for any one repurchase agreement counter-party name if the maturity/term is greater than 7 days.

Investment in State Investment Pool

OCTA is a voluntary participant in LAIF which is regulated by the California Government Code. The Investment Advisory Board provides oversight for LAIF, consisting of five members as designated by statute, which includes the Treasurer of the State of California. The fair value of OCTA's investment in this pool is reported in the accompanying financial statements based upon OCTA's pro-rata share of the fair value provided by LAIF for the entire LAIF portfolio (in relation to the amortized cost of that portfolio). The balance available for withdrawal is based on the accounting records maintained by LAIF, which are recorded on an amortized cost basis.

4. Due From/To Other Governments

Amounts due from other governments as of June 30, 2012 are \$80,790 and are comprised of \$47,681 of sales taxes, \$33,100 for project reimbursements and \$9 related to other miscellaneous transactions.

Amounts due to other governments as of June 30, 2012 are \$38,759 and are comprised of \$38,097 for transportation projects and \$662 other miscellaneous transactions.

Orange County Local Transportation Authority
Notes to The Financial Statements

Year Ended June 30, 2012
(in thousands)

5. Related Party Transactions and Interfund Transfers

Related party transactions:

During fiscal year 2011-12, transfers of \$2,683 from OCLTA to OCTA were made for the fare stabilization and senior mobility programs. Additionally, \$2,441 was transferred from OCTA to OCLTA as contributions for program expenditures.

OCTA advanced monies to OCLTA to cover expenditures such as election costs, administrative costs, and accrued interest. Interest accrues monthly at an interest rate representing OCTA's rate of return on short-term investments, adjusted each July (1.94% for fiscal year 2011-12). As of June 30, 2012, OCLTA owes OCTA \$5,627.

Interfund Transfers:

During fiscal year 2011-12, the LTA Fund transferred \$17,223 to the LTA Debt Service Fund for debt service payments.

6. Capital Assets

Capital assets activity for the OCLTA governmental activities for the year ended June 30, 2012 was as follows:

| | Beginning Balance | Increases | Decreases | Ending Balance |
|---|----------------------|-----------|-----------|-------------------|
| Capital assets, not being depreciated: | | | | |
| Land | \$ 183,304 | \$ - | \$ - | \$ 183,304 |
| Total Measure M capital assets, not being depreciated | 183,304 | - | - | 183,304 |
| Capital assets, being depreciated: | | | | |
| Right-of-way improvements | 1,086 | - | - | 1,086 |
| Machinery and equipment | 26 | 6 | - | 32 |
| Total capital assets, being depreciated | 1,112 | 6 | - | 1,118 |
| Less accumulated depreciation for: | | | | |
| Right-of-way improvements | (298) | (37) | - | (335) |
| Machinery and equipment | (18) | (3) | - | (21) |
| Total accumulated depreciation | (316) | (40) | - | (356) |
| Total Measure M capital assets, being depreciated, net | 796 | (34) | - | 762 |
| Total Measure M capital assets, net | \$ 184,100 | \$ (34) | \$ - | \$ 184,066 |

Depreciation expense charged to the Measure M program was \$40.

Orange County Local Transportation Authority
Notes to The Financial Statements

Year Ended June 30, 2012
(in thousands)

7. Short-Term Debt

On January 28, 2008, OCLTA was authorized to issue up to \$400,000 in Renewed Measure M Subordinate Tax-Exempt Commercial Paper Notes Series A and Series B (M2 Notes). As a requirement for the issuance of the M2 Notes, OCTA entered into an irrevocable direct-pay Letter of Credit and Reimbursement Agreement issued on a several and not joint basis with Dexia Credit Local, Bank of America, N.A., BNP Paribas, and JP Morgan Chase Bank, National Association as liquidity support for the M2 Notes.

In December 2010, OCLTA issued taxable and tax-exempt sales tax revenue bonds for the M2 program (see note 8). \$75,000 of the bonds issued was used to pay down the M2 Notes, bringing the outstanding balance to \$25,000. The M2 Notes program and supporting Letter of Credit were reduced from \$400,000 to \$50,000.

In October 2011, the Board approved the selection of JP Morgan Chase Bank, N.A. (JP Morgan) to serve as the successor Letter of Credit provider for the M2 Notes. The JP Morgan Letter of Credit expires in November 2014.

As of June 30, 2012, OCLTA had outstanding M2 Notes in the amount of \$25,000. Interest is payable on the respective maturity dates of the M2 Notes, which are the earlier of 270 days from date of issuance or program termination. The maximum allowable interest rate on the M2 Notes is 12.0%. The average issuance rate during fiscal year 2011-12 was 0.32%.

Changes in Short-Term Debt

Short-term debt activity for the year ended June 30, 2012, was as follows:

| | Beginning Balance | Issued | Redemptions | Ending Balance |
|----------------------------------|----------------------|------------|-------------|-------------------|
| Tax exempt commercial paper – M2 | \$ 25,000 | \$ 287,500 | \$ 287,500 | \$ 25,000 |
| Total short-term debt | \$ 25,000 | \$ 287,500 | \$ 287,500 | \$ 25,000 |

8. Long-Term Debt

Sales Tax Revenue Bonds

On December 9, 2010, OCLTA issued \$293,540 in Measure M2 Sales Tax Revenue Bonds, 2010 Series A (Taxable Build America Bonds) and \$59,030 in 2010 Series B (Tax-Exempt Bonds), to finance and refinance the costs of certain transportation projects located in Orange County, to restructure the Tax Exempt Commercial Paper (TECP) Program, and to fund capitalized interest and costs of issuance related to the 2010 Series Bonds. A reserve fund is not required in connection with the 2010 Series Bonds per the bond indenture. The transaction closed on December 23, 2010. A total of \$75,000 was used to refund outstanding TECP. The Measure M sales tax is the source of revenue for repaying this debt.

Orange County Local Transportation Authority
Notes to The Financial Statements

Year Ended June 30, 2012
(in thousands)

A summary of the bonds outstanding is as follows:

| | 2010 Series A (Taxable Build America Bonds) | 2010 Series B (Tax-Exempt Bonds) |
|--------------------------|---|--|
| Issuance date | 12/9/10 | 12/9/10 |
| Original issue amount | \$ 293,540 | \$ 59,030 |
| Original issue premium | - | 6,023 |
| Net bond proceeds | \$ 293,540 | \$ 65,053 |
| Issuance costs | \$ 1,905 | \$ 274 |
| Interest rate | 5.56% - 6.91% | 3.00% - 5.00% |
| Annual principal payment | \$8,915 - \$20,900 | \$6,410 - \$8,530 |
| Maturity | 2041 | 2020 |
| Bonds outstanding | \$ 293,540 | \$ 59,030 |
| Plus unamortized premium | - | 4,819 |
| Total | \$ 293,540 | \$ 63,849 |

Annual debt service requirements on the sales tax revenue bonds as of June 30, 2012, are as follows:

| Year Ending June 30 | Principal | Interest |
|---------------------|------------|------------|
| 2013 | \$ 6,410 | \$ 22,383 |
| 2014 | 6,600 | 22,191 |
| 2015 | 6,865 | 21,927 |
| 2016 | 7,210 | 21,584 |
| 2017 | 7,475 | 21,317 |
| 2018-2022 | 42,620 | 101,178 |
| 2023-2027 | 52,025 | 87,930 |
| 2028-2032 | 64,575 | 68,621 |
| 2033-2037 | 80,430 | 44,221 |
| 2038-2041 | 78,360 | 13,830 |
| Total | \$ 352,570 | \$ 425,182 |

Changes in Long-Term Liabilities

Long-term liabilities activity for the year ended June 30, 2012, was as follows:

| | Beginning Balance | Additions | Reductions | Ending Balance | Due within One Year |
|---|----------------------|-----------|------------|-------------------|------------------------|
| Measure M program activities: | | | | | |
| Sales tax revenue bonds | \$ 352,570 | \$ - | \$ - | \$ 352,570 | \$ 6,410 |
| Unamortized premium | 5,421 | - | 602 | 4,819 | - |
| Total Measure M program activities long-term liabilities | \$ 357,991 | \$ - | \$ 602 | \$ 357,389 | \$ 6,410 |

Orange County Local Transportation Authority
Notes to The Financial Statements

Year Ended June 30, 2012
(in thousands)

Pledged Revenue

OCLTA has debt issuances outstanding that are repaid and secured by the pledging of certain revenues. The amount and terms of the debt commitments are indicated in the bonds outstanding table found on page 29. The purposes for which the proceeds of the debt issuances were utilized are disclosed in the debt description located on page 28.

For the year ended June 30, 2012, debt service payments as a percentage of the pledged gross revenue net of the local fair share program and other expenses as required by the debt agreement, are indicated in the following table:

| Description of Pledged Revenue | Annual Amount of Net Pledged Revenue | Annual Debt Service Payments | Pledged Revenue Coverage |
|----------------------------------|--------------------------------------|------------------------------|--------------------------|
| Measure M2 Net Sales Tax Revenue | \$ 197,989 | \$ 15,425 * | 12.84 |

* OCLTA received \$6,958 in Build America Bonds subsidy to offset annual debt service payments for Measure M2 Sales Tax Revenue Bonds. OCLTA set aside \$11,192 in a capitalized interest account to fund a portion of the annual debt service payments for Measure M2 Sales Tax Revenue Bonds.

9. Commitments and Contingencies

Purchase Commitments

The OCLTA has various long-term outstanding contracts that extend over several years and rely on future years' revenues. Total commitments at June 30, 2012, were \$682,004, the majority of which relate to the expansion of Orange County's freeway and road systems.

Federal Grants

The OCLTA receives federal grants for transportation projects and other reimbursable activities which are subject to audit by the grantor agency. Although the outcome of any such audits cannot be predicted, it is management's opinion that these audits would not have a material effect on the OCLTA's financial position or changes in financial position.

10. Effect of New Pronouncements

GASB Statement No. 60

In November 2010, GASB issued Statement No. 60, Accounting and Financial Reporting for Service Concession Arrangements. The objective of this Statement is to improve financial reporting by addressing issues related to service concession arrangements (SCAs), which are a type of public-private or public-public partnership. This statement is effective for OCLTA's fiscal year ending June 30, 2013.

Year Ended June 30, 2012
(in thousands)

GASB Statement No. 61

In November 2010, GASB issued Statement No. 61, The Financial Reporting Entity: Omnibus – an amendment of GASB Statements No. 14 and No. 34. The objective of this Statement is to improve financial reporting for a governmental financial reporting entity. This statement is effective for OCLTA's fiscal year ending June 30, 2013.

GASB Statement No. 62

In June 2011, GASB issued Statement No. 62, Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements. The objective of this Statement is to incorporate into the GASB's authoritative literature certain accounting and financial reporting guidance that is included in FASB and AICPA pronouncements issued on or before November 30, 1989 which does not conflict with or contradict GASB pronouncements. This statement is effective for OCLTA's fiscal year ending June 30, 2013.

GASB Statement No. 63

In June 2011, GASB issued Statement No. 63, Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position. This Statement provides financial reporting guidance for deferred outflows of resources and deferred inflows of resources and the resulting net position. This statement is effective for OCLTA's fiscal year ending June 30, 2013.

GASB Statement No. 64

In June 2011, GASB issued Statement No. 64, Derivative Instruments: Application of Hedge Accounting Termination Provisions – an amendment of GASB Statement No. 53. The objective of this Statement is to clarify whether an effective hedging relationship continues after the replacement of a swap counterparty or a swap counterparty's credit support provider. This Statement sets forth criteria that establish when the effective hedging relationship continues and hedge accounting should continue to be applied. As OCLTA does not have derivative instruments, this statement does not apply to OCLTA.

GASB Statement No. 65

In March 2012, GASB issued Statement No. 65, Items Previously Reported as Assets and Liabilities. This statement establishes accounting and financial reporting standards that reclassify, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities and recognizes, as outflows of resources or inflows of resources, certain items that were previously reported as assets and liabilities. This statement is effective for OCLTA's fiscal year ending June 30, 2014.

Orange County Local Transportation Authority
Notes to The Financial Statements

Year Ended June 30, 2012
(in thousands)

GASB Statement No. 66

In March 2012, GASB issued Statement No. 66, Technical Corrections - 2012 - an amendment of GASB Statements No. 10 and No. 62. The objective of this statement is to improve accounting and financial reporting for a governmental financial reporting entity by resolving conflicting guidance that resulted from the issuance of two pronouncements, Statements No. 54, Fund Balance Reporting and Governmental Fund Type Definitions and No. 62, Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements. This statement is effective for OCLTA's fiscal year ending June 30, 2014.

GASB Statement No. 67

In June 2012, GASB issued Statement No. 67, Financial Reporting for Pension Plans - an amendment of GASB Statement No. 25. The objective of this statement is to improve financial reporting by state and local governmental pension plans. This statement is effective for OCTA's fiscal year ending June 30, 2014.

GASB Statement No. 68

In June 2012, GASB issued Statement No. 68, Accounting and Financial Reporting for Pensions - an amendment of GASB Statement No. 27. The primary objective of this Statement is to improve accounting and financial reporting by state and local governments for pensions. It also improves information provided by state and local governmental employers about financial support for pensions that is provided by other entities. This statement is effective for OCTA's fiscal year ending June 30, 2015.

ORANGE COUNTY LOCAL TRANSPORTATION AUTHORITY
(A Component Unit of the Orange County Transportation Authority)
Required Supplementary Information
Budgetary Comparison Schedule - LTA Fund (Budgetary Basis)
Year Ended June 30, 2012

| <i>(amounts expressed in thousands)</i> | Budgeted Amounts | | Actual Amounts | Variance with Final Budget |
|--|---------------------|---------------------|-------------------|-------------------------------|
| | Original | Final | | |
| Revenues: | | | | |
| Sales taxes | \$ 243,148 | \$ 243,148 | \$ 252,132 | \$ 8,984 |
| Contributions from other agencies | 208,225 | 208,225 | 208,403 | 178 |
| Interest | 4,579 | 4,579 | 5,393 | 814 |
| Miscellaneous | 814 | 814 | 665 | (149) |
| Total revenues | 456,766 | 456,766 | 466,593 | 9,827 |
| Expenditures: | | | | |
| Current: | | | | |
| General government | 117,781 | 121,419 | 93,033 | 28,386 |
| Transportation: | | | | |
| Contributions to other local agencies | 275,564 | 263,601 | 181,161 | 82,440 |
| Capital outlay | 258,382 | 258,382 | 147,664 | 110,718 |
| Debt service: | | | | |
| Interest on long-term debt and commercial paper | 250 | 250 | 125 | 125 |
| Total expenditures | 651,977 | 643,652 | 421,983 | 221,669 |
| Excess (deficiency) of revenues over (under) expenditures | (195,211) | (186,886) | 44,610 | 231,496 |
| Other financing sources (uses): | | | | |
| Transfers from OCTA | - | - | 2,441 | 2,441 |
| Transfers out | (15,309) | (15,309) | (17,223) | (1,914) |
| Transfers to OCTA | (3,961) | (3,961) | (2,683) | 1,278 |
| Total other financing sources (uses) | (19,270) | (19,270) | (17,465) | 1,805 |
| Net change in fund balance | \$ (214,481) | \$ (206,156) | \$ 27,145 | \$ 233,301 |

Reconciliation to GAAP:

| | |
|--|-----------|
| Net change in fund balance (budgetary basis) | \$ 27,145 |
| Less: Estimated revenues for encumbrances outstanding at June 30 | 69,396 |
| Add: Current year encumbrances outstanding at June 30 | 91,558 |
| Net change in fund balance (GAAP basis) | \$ 49,307 |

See accompanying notes to the required supplementary information.

Orange County Local Transportation Authority
(A Component Unit of the Orange County Transportation Authority)

Notes to Required Supplementary Information

Year Ended June 30, 2012

(in thousands)

1. Budgetary Data

The OCLTA establishes accounting control through formal adoption of an annual operating budget for the LTA and the debt service governmental funds. The operating budget is prepared in conformity with accounting principles generally accepted in the United States (GAAP) except for multi-year contracts, for which the entire amount of the contract is budgeted and encumbered in the year of execution. The adopted budget can be amended by the Board to increase both appropriations and estimated revenues as unforeseen circumstances come to management's attention. Budgeted expenditure amounts represent original appropriations adjusted for supplemental appropriations during the year. Division heads are authorized to approve appropriation transfers within major objects subject to approval by the Finance and Administration Division. Major objects are defined as Salaries and Benefits, Supplies and Services and Capital Outlay. Appropriation transfers between major objects require approval of the Board. Accordingly, the legal level of budgetary control, that is the level that expenditures cannot exceed appropriations, for budgeted funds, is at the major object level for the budgeted governmental funds. A Fourth Quarter Budget Status Report, June 2012 is available from the OCTA Finance and Administration Division. With the exception of accounts which have been encumbered, appropriations lapse at year end.

There were no excess of expenditures over appropriations for fiscal year 2011-12.

ORANGE COUNTY LOCAL TRANSPORTATION AUTHORITY
(A Component Unit of the Orange County Transportation Authority)
Other Supplementary Information
Budgetary Comparison Schedule - LTA Debt Service Fund (Budgetary Basis)
Year Ended June 30, 2012

| <i>(amounts expressed in thousands)</i> | Budgeted Amounts | | Actual Amounts | Variance with Final Budget |
|--|------------------|-----------------|-------------------|-------------------------------|
| | Original | Final | | |
| Revenues: | | | | |
| Contributions from other agencies | \$ 6,958 | \$ - | \$ - | \$ - |
| Interest | 116 | 7,074 | 6,967 | (107) |
| Total revenues | 7,074 | 7,074 | 6,967 | (107) |
| Expenditures: | | | | |
| Debt service: | | | | |
| Interest on long-term debt and commercial paper | 22,383 | 22,383 | 22,383 | - |
| Total expenditures | 22,383 | 22,383 | 22,383 | - |
| Deficiency of revenues under expenditures | (15,309) | (15,309) | (15,416) | (107) |
| Other financing sources: | | | | |
| Transfers in | 15,309 | 15,309 | 17,223 | 1,914 |
| Total other financing sources | 15,309 | 15,309 | 17,223 | 1,914 |
| Net change in fund balance | \$ - | \$ - | \$ 1,807 | \$ 1,807 |



**INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER
FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS
BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED
IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

Board of Directors
Orange County Local Transportation Authority
Orange, California

We have audited the financial statements of the governmental activities and each major fund of the Orange County Local Transportation Authority (OCLTA), a component unit of the Orange County Transportation Authority (OCTA), as of and for the year ended June 30, 2012, and have issued our report thereon dated October 29, 2012. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

Management of OCLTA is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered OCLTA's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of OCLTA's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of OCLTA's internal control over financial reporting.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. *A material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined previously.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether OCLTA's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

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

A handwritten signature in cursive script that reads "Vavrieh, Train, Dug & Co., LLP".

Laguna Hills, California
October 29, 2012