



Los Angeles World Airports

Annual Financial Report

for the Years Ended June 30, 2007 and 2006

ANNUAL FINANCIAL REPORT

For the Years Ended June 30, 2007 and 2006



DEPARTMENT OF AIRPORTS OF THE CITY OF LOS ANGELES, CALIFORNIA

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MACIAS GINI & O'CONNELL LLP
CERTIFIED PUBLIC ACCOUNTANTS & MANAGEMENT CONSULTANTS

3000 S Street, Suite 300
Sacramento, CA 95816
916.928.4600

2175 N. California Boulevard, Suite 645
Walnut Creek, CA 94596
925.274.0190

515 S. Figueroa Street, Suite 325
Los Angeles, CA 90071
213.286.6400

402 West Broadway, Suite 400
San Diego, CA 92101
619.573.1112

The Members of the Board of Airport Commissioners
of the City of Los Angeles, California

INDEPENDENT AUDITOR'S REPORT

We have audited the accompanying financial statements of the Los Angeles World Airports (Department of Airports of the City of Los Angeles, California) (LAWA), an Enterprise Fund of the City of Los Angeles, California, as of and for the years ended June 30, 2007 and 2006, as listed in the accompanying table of contents. These financial statements are the responsibility of LAWA's management. 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 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 LAWA'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 audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of LAWA as of June 30, 2007 and 2006, and the changes in its financial position and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

As described in Note 2, LAWA adopted the provisions of Governmental Accounting Standards Board (GASB) Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, and GASB Statement No. 50, *Pension Disclosures – an amendment of GASB Statement No. 25 and 27, for the year ended June 30, 2007*.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 14, 2007 on our consideration of LAWA'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 for the year ended June 30, 2007. 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 the 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.

The management's discussion and analysis on pages 3 through 17 and the pension and postemployment healthcare plans schedules of funding progress, on page 45 and 49, respectively, are not a required part of the financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming an opinion on LAWA's financial statements. The combining financial statements on pages 56 through 58 listed in the accompanying table of contents as supplemental information are presented for purposes of additional analysis and are not a required part of the financial statements. This supplemental information has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly stated in all material respects in relation to the financial statements taken as a whole.

Macias Jini & O'Connell LLP

Certified Public Accountants

Los Angeles, California
December 14, 2007

June 30, 2007 and 2006

Los Angeles World Airports (LAWA) is an independent and financially self-sufficient department of the City of Los Angeles, California (City) and is an enterprise fund comprised of four separate airports. LAWA owns and operates Los Angeles International Airport (LAX), Ontario International Airport (ONT), Van Nuys Airport (VNY), and Palmdale Regional Airport (PMD). The information presented in this "Management's Discussion and Analysis" (MD&A) is intended to be a narrative overview of LAWA's financial statements as of and for the years ended June 30, 2007 and 2006. We encourage readers to consider this information in conjunction with the accompanying financial statements.

The financial statements contained in this report are prepared in accordance with generally accepted accounting principles using the accrual basis of accounting. LAWA applies Governmental Accounting Standards Board (GASB) pronouncements as well as Financial Accounting Standards Board Statements and Interpretations, Accounting Principles Board Opinions, and Accounting Research Bulletins issued on or before November 30, 1989, unless such pronouncements conflict or contradict GASB pronouncements. LAWA recognizes the financial reporting model set forth in GASB 34, *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments*, and its related GASB pronouncements and interpretations, and hereby presents its financial statements in conformance with such pronouncements.

Financial Highlights of Airport Activities

For fiscal year 2007, LAWA increased its net assets by 9.2% to \$2.9 billion. The change in net assets of \$243.5 million is 40.9%, or \$70.7 million, greater than the change in net assets for prior fiscal year. This increase was the result of a combination of factors. Net nonoperating revenues at LAWA of \$165.7 million have increased \$44.7 million, or 36.9%, over the prior year. This growth is caused primarily by the net increase in the fair value of investments and higher interest income, which increased \$30.9 million and \$6.4 million, respectively. Capital grant contributions increased by \$19.5 million to \$82.1 million, which consisted primarily of increases of \$42.0 million at LAX partially offset by decreases of \$19.6 million and \$2.9 million at ONT and VNY, respectively. Capital grant contributions are comprised by two categories: Capital grant contributions that are for projects approved under the Federal Aviation Administration's Airport Improvement Program (AIP); and contributions from the Transportation Security Administration (TSA) for approved security-related capital reimbursement programs. For combined LAWA, fiscal year 2007 contributions from AIP grants increased by \$31.2 million, while TSA contributions dropped by \$11.7 million. In addition, LAWA's income from operations, excluding depreciation and amortization, was \$87.9 million, representing an increase of \$14.8 million, or 20.2%, from fiscal year 2006.

At June 30, 2007, total assets at LAWA of \$3.9 billion increased \$521.1 million, or 15.4%, over fiscal year 2006. Of this growth, \$245.6 million came from increases in buildings, improvements and equipment, while Construction work-in-progress increased \$165.1 million. During fiscal year 2007, there were significant expenditures made for major capital projects currently underway to include: LAX noise mitigation projects of \$34.0 million, Southside airfield projects at LAX for \$185.7 million, interior improvements at the Tom Bradley International Terminal at LAX for \$64.7 million, in-line baggage screening systems for \$15.9 million at LAX, and reconstruction of ONT's Runway 26R for \$11.8 million.

LAWA depends primarily on passenger traffic to generate the majority of its aviation and related revenue. During fiscal year 2007, passenger traffic at LAWA stayed at the same level as fiscal year 2006 levels, or 68.6 million. During fiscal year 2006, passenger traffic at LAWA increased by 0.3 million, or 0.5%, over fiscal year 2005 levels to 68.6 million. However, LAWA is still below the peak level that it reached with 74.1 million in combined LAX and ONT passengers during FY2001.

Financial Highlights of Airport Activities (continued)

LAWA continues to support the residential sound insulation program. Funding for this program, which offers mitigation features that improve affected homes, has come primarily from Passenger Facility Charges (PFC) collected from certain enplaned passengers at LAWA. As of June 30, 2007 and 2006, the PFC collection rate is \$4.50 per airline ticket at LAX and \$3.00 at ONT. At the end of fiscal year 2007, cumulative PFC collections were \$1.215 billion, which consists of \$1.091 billion in passenger collections and \$124.2 million in interest. At the end of fiscal year 2006, cumulative PFC collections amounted to \$1.073 billion, of which \$0.964 billion were passenger collections and \$108.3 million was interest.

Income from Operations

Fiscal Year 2007 Compared to 2006. For the year fiscal ended June 30, 2007, LAWA had a \$4.3 million loss from operations, net of depreciation and amortization, showing a \$6.5 million improvement over the prior fiscal year's loss from operations of \$10.8 million. Operating revenues increased by \$38.3 million, or 6.2%, to \$659.0 million driven by concession revenue growth of \$25.2 million, or 10.5%, to \$265.1 million while Aviation revenues of \$388.1 million increased \$11.7 million, or 3.1%. Operating expenses displayed a lower amount and rate of growth than operating revenues by increasing \$23.6 million, or 4.3%, to \$571.1 million. The two major categories that significantly impacted this growth were: salaries and benefits, and materials and supplies. Salaries and benefits of \$303.7 million increased \$28.6 million, or 10.4%, while materials and supplies grew by \$9.2 million to \$50.5 million, or 22.3%. Decreases in contractual services and utilities expense of \$9.7 million or 5.6%, and \$2.8 million or 9.8%, respectively, partially offset the net growth in the remaining areas of operating expenses.

Fiscal Year 2006 Compared to 2005. For the fiscal year ended June 30, 2006, LAWA had a \$10.8 million loss from operations, net of depreciation and amortization, which is \$9.8 million greater than the prior fiscal year's loss from operations of \$1.0 million. Aviation revenues of \$376.4 million increased \$34.4 million, or 10.1%, and concession revenues grew by \$11.7 million, or 5.1%, to \$239.9 million. Partly offsetting this revenue improvement was growth in the two major operating expense categories: salaries and benefits and contractual services. Salaries and benefits of \$275.0 million increased \$37.4 million, or 15.8%, while contractual services of \$172.5 million grew by \$15.9 million, or 10.2%.

Change in Net Assets

Fiscal Year 2007 Compared to 2006. LAWA's change in net assets for fiscal year 2007 of \$243.5 million is comprised of the net operating loss of \$4.3 million, net nonoperating revenues of \$165.7 million and capital grant contributions of \$82.1 million. The growth of LAWA's change in net assets, or \$70.7 million, is 40.9% higher than the prior fiscal year results of \$172.9 million. This growth is caused primarily by a \$30.9 million increase in the fair value of investments resulting from the City of Los Angeles' pro-rata allocation from its investment pool to LAWA. Additionally, LAWA's interest income grew by \$6.4 million, or 16.3%, as a result of a positive market impact on its \$1.1 billion of invested cash. Also, \$19.5 million more in capital grant contributions were received from the U. S. Departments of Transportation and Homeland Security, than in the prior year, for a current year total of \$82.1 million.

Fiscal Year 2006 Compared to 2005. The change in net assets for the year ended June 30, 2006 is \$172.9 million, which is 24.5%, or \$34.0 million, higher than the prior fiscal year results of \$138.9 million. Contributing significantly to this increase is a \$60.8 million increase in capital grant

Change in Net Assets (continued)

contributions to \$62.6 million. During fiscal year 2006, net nonoperating revenues of \$121.1 million were \$17.0 million, or 12.3%, below the prior fiscal year results of \$138.1 million.

Net Asset Summary

Net assets serve as an indicator of LAWA's financial position. As of June 30, 2007, LAWA assets exceeded liabilities by \$2.877 billion.

A summary of LAWA's net assets for fiscal years (FY) 2007, 2006, and 2005 is shown below (in thousands):

Summary Statement of Net Assets

(Dollars in Thousands)

	FY2007	FY2006	FY2005
Assets:			
Current assets	\$ 647,957	\$ 629,052	\$ 670,497
Restricted assets	860,770	705,584	634,227
Capital assets, net	2,381,723	2,034,536	1,912,508
Deferred bond issuance expenses	3,732	3,947	4,371
Total assets	<u>3,894,182</u>	<u>3,373,119</u>	<u>3,221,603</u>
Liabilities:			
Current liabilities payable from unrestricted assets	282,760	78,495	88,122
Current liabilities payable from restricted assets	243,405	229,441	232,864
Long-term liabilities	490,571	431,281	439,607
Total liabilities	<u>1,016,736</u>	<u>739,217</u>	<u>760,593</u>
Net assets:			
Invested in capital assets, net of related debt	1,992,657	1,637,147	1,489,630
Restricted:			
Capital projects	645	16,040	16,288
Debt service	33,231	35,472	36,069
Special purpose	599,578	439,963	267,802
Unrestricted	251,335	505,280	651,221
Total net assets	<u>\$ 2,877,446</u>	<u>\$ 2,633,902</u>	<u>\$ 2,461,010</u>

Current Assets

Fiscal Year 2007 Compared to 2006. For fiscal year 2007, LAWA's current assets increased by \$18.9 million, or 3.0%, due to the \$153.5 million increase in cash with fiscal agent offset by a decrease of cash and pooled investments held by the City Treasurer of \$134.2 million. The cash with fiscal agent

June 30, 2007 and 2006

Current Assets (continued)

balance comes from LAWA issuing \$178.7 million of commercial paper used as a short term measure to fund increased capital project activity at LAX. The decrease to cash and pooled investments held by the City Treasurer is driven by daily operating activities at LAX and ONT airports. Receipts of unrestricted cash at these airports increased by \$119.7 million during fiscal year 2007, however, the outflow of cash used for unrestricted capital and related financing activities increased by \$173.2 million. The net result of these daily impacts reduced LAWA's unrestricted cash balance by 23.7% to \$431.9 million at year-end.

Fiscal Year 2006 Compared to 2005. For fiscal year 2006, LAWA's current assets decreased by \$41.4 million, or 6.2%, largely due to a \$45.6 million, or 7.5%, decrease in cash and pooled investments held by the City Treasurer to \$566.1 million. The primary reason for the cash and pooled investments decline is that net cash provided by operating activities declined by \$66.4 million to \$71.5 million. Although LAWA's receipts from customers increased by \$20.6 million, or 3.6% to \$618.3 million, the gain was offset by increases in payments for goods and services and payments to employees of \$51.4 million, or 23.1%, and \$31.3 million, or 13.2%, respectively.

Restricted Assets

Fiscal Year 2007 Compared to 2006. Restricted assets of \$860.8 million increased by \$155.2 million, or 22.0%, resulting from the growth in restricted invested cash and pooled investments held by the City Treasurer (excluding securities lending program (SLP) collateral and fair value adjustment) of \$123.1 million, or 25.2%, to \$611.0 million. SLP collateral and fair value adjustment are equivalent cash transactions allocated by the City Treasurer that represent LAWA's prorata share of the City's investment in marketable securities as discussed in Note 3 of the accompanying notes to financial statements. Increases to SLP collateral and adjustment for market valuation balances of \$21.8 million and \$13.1 million, respectively, added to the growth in restricted assets. PFC receivables decreased \$1.1 million, or 5.3% to \$19.9 million.

Fiscal Year 2006 Compared to 2005. Restricted assets of \$705.6 million increased by \$71.4 million, or 11.3%, resulting from growth in the portion of invested cash and pooled investments held by the City Treasurer (excluding securities lending collateral and fair value adjustment) of \$71.8 million, or 17.2%, to \$487.9 million. A \$17.8 million increase in the adjustment for market valuation partially counterbalanced the growth. Additionally, PFC receivables increased \$5.3 million, or 33.4% to \$21.0 million.

Capital Assets

Fiscal Year 2007 Compared to 2006. Net capital assets at LAWA of \$2.4 billion reflect an increase of \$347.2 million, or 17.1%, due primarily to a \$245.6 million increase in buildings, improvements, and equipment and a \$165.1 million increase in construction work in process. Significant capital expenditures were made at LAX for noise mitigation projects, Southside airfield projects, interior improvements at the Tom Bradley International Terminal, and in-line baggage screening systems. A substantial portion of this growth was offset by an \$82.9 million, or 7.8%, increase in accumulated depreciation.

Capital Assets (continued)

The table on the following page lists fiscal year 2007 expenditures of major capital improvement projects. Commitments for the major capital projects listed on this table are included in the total commitment amount of \$53.2 million, as shown in Note 10 (b) of the accompanying notes to financial statements.

Major Capital Expenditures
Fiscal Year 2007
 (Dollars in Millions)

Project Name by Airport Location	Expenditure	Purpose
LAX		
Tom Bradley International Terminal	\$ 64.7	Interior improvements and security upgrades.
Noise Mitigation	34.0	Residential acquisition and soundproofing.
Security Program	7.4	Perimeter/cargo upgrades, passenger checkpoint modifications.
In-Line Baggage Screening	15.9	Screening of check-in baggage prior to passenger boarding.
Southside Airfield Improvement	185.7	Move southern-most runway 50 feet to allow greater distance between aircraft.
Total	<u>\$ 307.7</u>	
ONT		
Runway 26R	\$ 11.8	Reconstruction of the runway.
In-Line Baggage Screening	7.9	Screening of check-in baggage prior to passenger boarding.
Total	<u>\$ 19.7</u>	
VNY		
Maintenance Yard Relocation	\$ 4.1	Construction of approximately 20,000 sq. ft. of buildings, shop space and utilities. Also, grading and paving of 3.5 acres for this yard.
Other Capital Expenditures	<u>\$ 79.6</u>	
LAWA TOTAL	<u>\$ 411.1</u>	

Fiscal Year 2006 Compared to 2005. Net capital assets at LAWA of \$2.035 billion reflect an increase of \$122.0 million, or 6.4%, due primarily to a \$139.9 million increase in buildings, improvements, and equipment and a \$63.4 million increase in construction work in process. Significant capital expenditures were made at LAX for noise mitigation projects, the new Southside airfield, interior improvements at the

Capital Assets (continued)

Tom Bradley International Terminal, and in-line baggage screening systems. Most of the growth was offset by the increase in accumulated depreciation of \$83.9 million, or 8.6%, to \$1.066 billion.

Total Liabilities

Fiscal Year 2007 Compared to 2006. At June 30, 2007, total liabilities of \$1.017 billion increased by \$277.5 million, or 37.5%. The factors contributing to this increase stem from the combined growth of \$218.2 million in current liabilities plus a \$59.3 million increase in long-term liabilities.

Current liabilities payable from unrestricted assets increased by \$204.3 million, due primarily to the issuance of \$178.7 million in commercial paper notes and a \$23.5 million increase in contracts and accounts payable. Current liabilities payable from restricted assets are up by \$14.0 million, or 6.1%, due partly to the increased allocation by the City Treasurer for the SLP collateral's offsetting liability of \$21.8 million, which is substantially reduced by the \$8.3 million decline in contracts and accounts payable.

Long-term liabilities of \$490.6 million increased by \$59.3 million, or 13.7%, due in large part to the recognition of \$92.6 million of the liability resulting from cash payments received and interest earned from LAX tenants of passenger terminal facilities who still paid for the rent increases under protest. These disputed payments were made by the terminal tenants as a result of a Board of Airport Commissioners resolution to recover a greater amount of operating expenses through an increase to the maintenance and operations rent (M&O rent) effective from January 1, 2006. Because the payments were not recorded as revenue, the liability is the offset to the rental receipts and related interest earned through June 30, 2007. As a result of these disputed payments, no related revenue will be recognized until this matter is resolved. This matter is discussed in more detail under Note (14) of the accompanying notes to financial statements.

Partially reducing this increase were principal reductions in the bonded debt liability balance at LAX and ONT of \$12.4 million and \$21.6 million, respectively. LAWA's bonds are rated periodically by the three major credit agencies: Standard & Poor's, Moody's, and Fitch. For LAX, the ratings at June 30, 2007 are AA, Aa3, and AA for each credit agency, respectively. For ONT, the ratings are A, A2, and A, respectively. For both LAX and ONT, the ratings have not changed from the prior fiscal year. LAWA's bonded indebtedness is discussed in more detail under Note (5) of the accompanying notes to financial statements. Also, there was an increase of \$1.2 million, or 4.0%, in long-term employee benefits as a result of the growth in number of LAWA employees during fiscal year 2007.

Fiscal Year 2006 Compared to 2005. At June 30, 2006, total liabilities of \$739.2 million decreased by \$21.4 million, or 2.8%. The factors contributing to this decrease are decreases in both current and long-term liabilities. Long-term liabilities of \$431.3 million decreased by \$8.3 million, or 1.9%, due primarily to a \$15.3 million transfer of the current portion of the bonded indebtedness to end the fiscal year at \$322.6 million. LAWA's bonds are rated periodically by the three major credit agencies: Standard & Poor's, Moody's, and Fitch. For LAX, the ratings at June 30, 2006 are AA, Aa3, and AA, respectively. For ONT, the ratings are A, A2, and A, respectively. For both LAX and ONT, the ratings have not

Total Liabilities (continued)

changed from the prior fiscal year. The decrease in long-term liabilities was offset by a \$7.5 million, or 33.0%, increase in employee benefits to \$30.2 million.

Highlights of Changes in Net Assets

The following table illustrates a condensed summary of changes in net assets for FY 2007, 2006, and 2005:

Summary Statement of Changes in Net Assets

(Dollars in Thousands)

	FY2007	FY2006	FY2005
Operating revenue	\$ 659,025	\$ 620,699	\$ 574,233
Operating expenses excluding depreciation and amortization	(571,087)	(547,529)	(499,057)
Income from operations before depreciation and amortization	87,938	73,170	75,176
Depreciation and amortization	(92,230)	(83,945)	(76,189)
Operating (loss) income	(4,292)	(10,775)	(1,013)
Other nonoperating revenue, net	165,748	121,077	138,065
Income before capital grant contributions	161,456	110,302	137,052
Capital grant contributions	82,088	62,590	1,798
Change in net assets	243,544	172,892	138,850
Net assets at beginning of year	2,633,902	2,461,010	2,322,160
Net assets at end of year	\$ 2,877,446	\$ 2,633,902	\$ 2,461,010

Passengers

Fiscal Year 2007 Compared to 2006. When compared to the previous year, total passengers at LAWA decreased slightly by approximately 0.1%, or 69,258 in fiscal year 2007 to 68,589,559 annual passengers. This change is comprised of the small growth at LAX of 77,892 passengers to 61,534,823 that was offset by a decline of 147,150 passengers at ONT to 7,054,736.

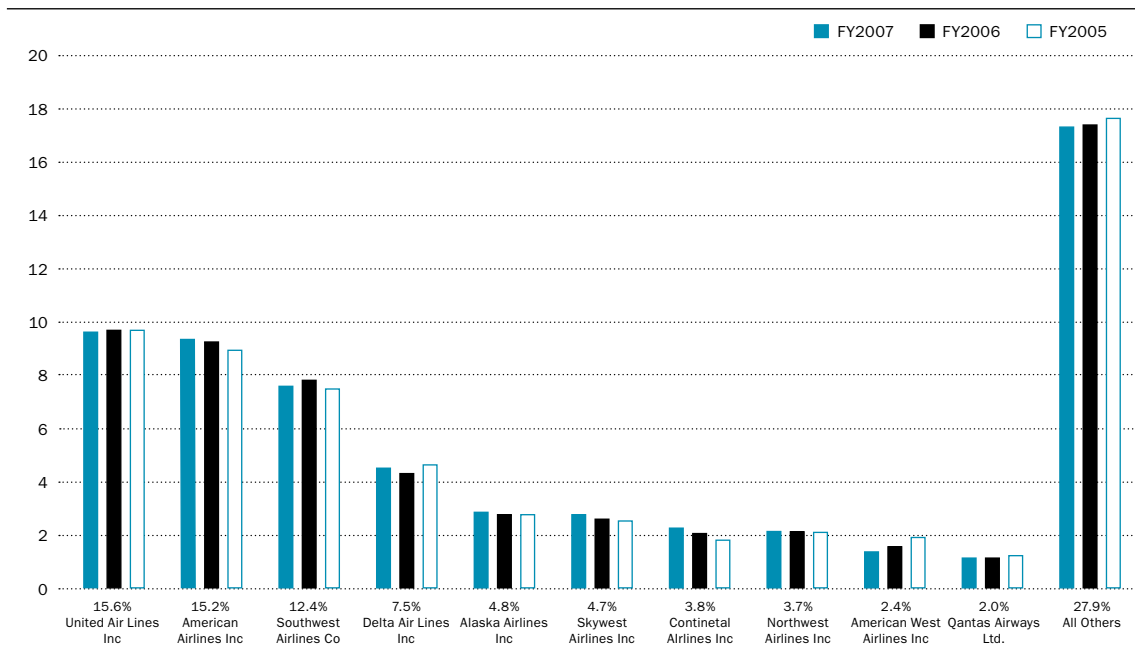
Fiscal Year 2006 Compared to 2005. When compared to the previous year, total passengers at LAWA increased by approximately 0.5%, or 349,000 in fiscal year 2006 to 68,658,817 annual passengers. Slight passenger growth was seen at LAWA's two major airports, LAX and ONT. LAX passengers grew by about 171,000, or 0.3% to 61,456,931, while ONT passengers grew by about 179,000, or 2.6% to 7,201,886.

June 30, 2007 and 2006

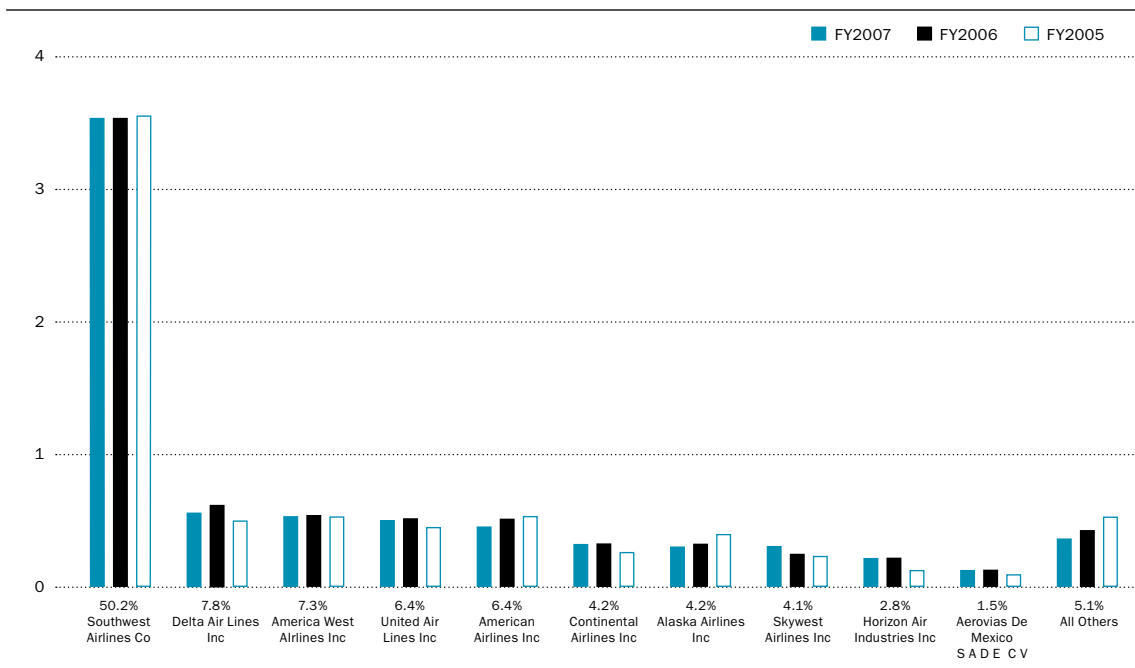
Passengers (continued)

The following charts illustrate the top ten airlines at LAX and ONT by number of passengers for FY2007, FY2006, and FY2005:

LAX - Passengers of Top Ten Carriers and Their Current Year % of Marketshare (Passengers in Millions)



ONT - Passengers of Top Ten Carriers and Their Current Year % of Marketshare (Passengers in Millions)





Operating Revenues

LAWA derives its operating revenues from several major airport business activities. The following table illustrates a comparative summary of the major operating revenue categories in FY 2007, 2006, and 2005:

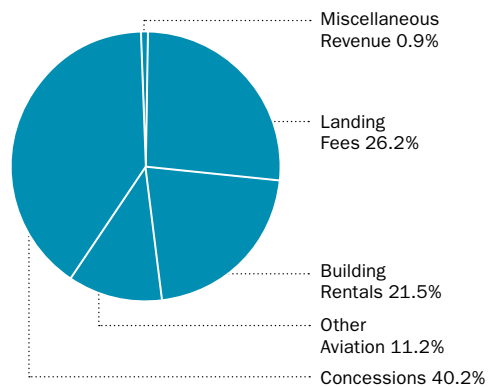
Summary of Operating Revenues

(Dollars in Thousands)

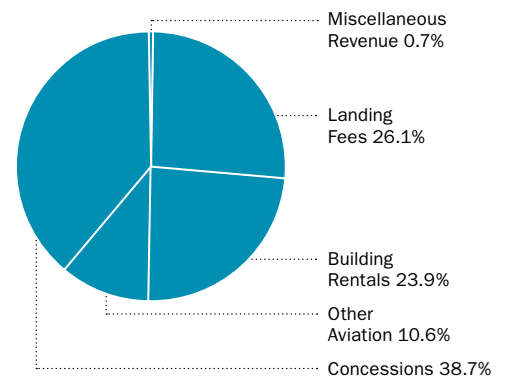
	FY2007	FY2006	FY2005
Landing fees	\$ 172,495	\$ 162,037	\$ 147,990
Building rentals	141,521	148,320	133,635
Other aviation revenue	74,114	66,024	60,336
Concession revenue	265,112	239,936	228,230
Airport sales and services	3,306	2,463	2,575
Miscellaneous revenue	2,477	1,919	1,467
Total operating revenue	\$ 659,025	\$ 620,699	\$ 574,233

The following charts illustrate the distribution of the major sources of operating revenues for fiscal years 2007, 2006, and 2005:

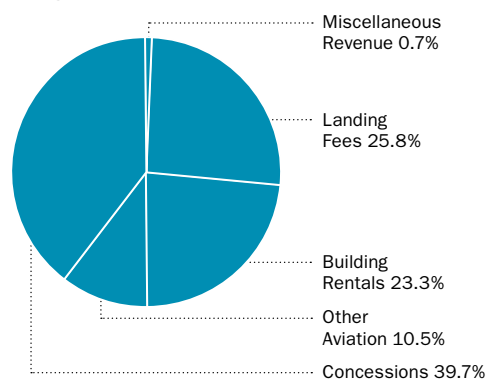
FY2007
Operating Revenues \$659.0 Million



FY2006
Operating Revenues \$620.7 Million



FY2005
Operating Revenues \$574.2 Million



June 30, 2007 and 2006

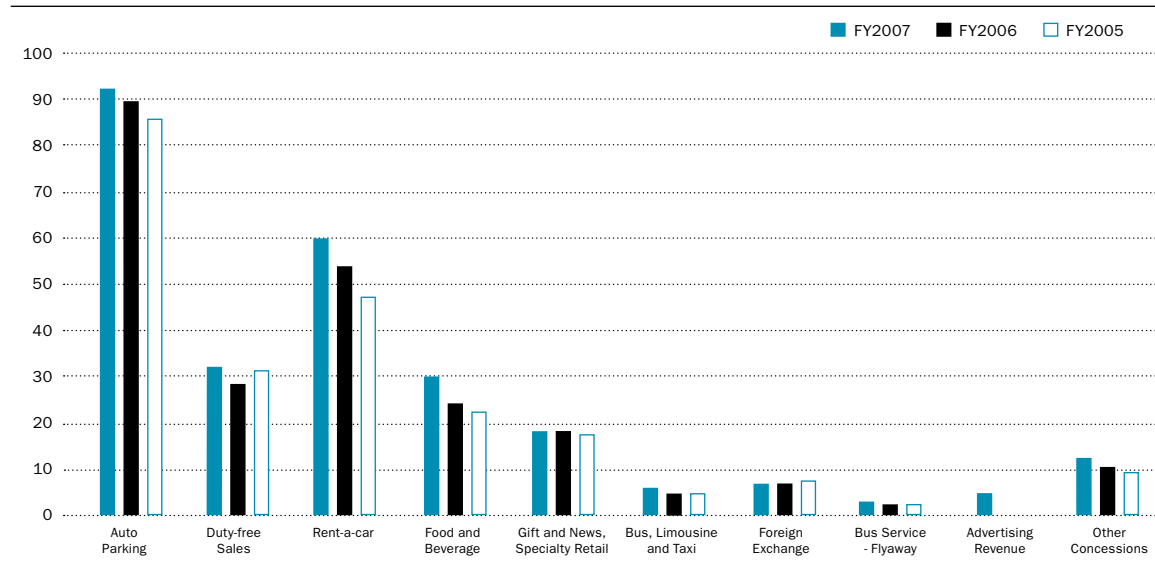
Operating Revenues (continued)

Fiscal Year 2007 Compared to 2006. For fiscal year 2007, LAWA's total operating revenue increased by \$38.3 million, or 6.2%, to \$659.0 million, due primarily to a \$25.1 million or 10.5% increase in LAX concession revenues and from increases in Federal security agreement revenues of \$7.0 million. Additionally, landing fees increased \$10.5 million, or 6.5%. Lastly, LAWA's airport sales and services income jumped 34.2% to \$3.3 million, while miscellaneous revenues, including movie production fees of over \$1.0 million, climbed nearly 29.1% to \$2.5 million.

Fiscal Year 2006 Compared to 2005. During fiscal year 2006, total operating revenue increased by \$47.4 million, or 8.3%, to \$620.7 million, due primarily to increased activity in two categories of aviation revenues: building revenues and landing fees. LAX contributed to LAWA's \$14.7 million increase in building rentals by growing \$18.1 million, or 17.9%, to \$119.3 million. The growth in building rentals at LAX was due to an increase in rental rates. Offsetting the LAX increase was a decline in building revenues at ONT by \$4.8 million, or 16.0% to \$25.2 million.

The following chart illustrates the categories of concession revenues by type for FY2007, FY2006, and FY2005:

Concession Revenues (\$ in millions)



The table on the following page presents concession revenues on a per enplanement basis to indicate spending activity for passengers that pass through LAWA's primary airports. Between fiscal year 2007 to fiscal year 2006, enplanements at LAX grew 6.9%, while growth in concession revenues per enplanement increased 6.0% to \$7.39. In fiscal year 2006, enplanements at LAX were 0.5% over the prior fiscal year, while concession revenues per enplanement grew by 2.7% to \$6.97. These result show that passenger spending has steadily increased at LAX from 2005 through 2007.



Operating Revenues (continued)

At ONT, a slightly different result is shown. Enplanements in 2007 were 2.9% over 2006, while concession revenues decreased 2.3% to \$10.77 per enplaned passenger during this fiscal period. ONT enplanements in 2006 were 1.5% above 2005, while concession revenues per enplanement grew 14.0%. This table indicates that passengers were spending more money on ONT concessions than at LAX on a per enplanement basis.

Los Angeles World Airports Concession Revenues Per Enplanement

	FY2007	FY2006	FY2005
Los Angeles International Airport			
Enplanements	30,751,547	28,777,160	28,639,329
Concession Revenues Per Enplanement	\$ 7.39	\$ 6.97	\$ 6.79
Ontario International Airport			
Enplanements	3,521,926	3,424,025	3,374,445
Concession Revenues Per Enplanement	\$ 10.77	\$ 11.02	\$ 9.67

Operating Expenses

The following table illustrates a comparative summary of operating expenses in FY2007, 2006, and 2005:

Summary of Operating Expenses

(Dollars in Thousands)

	FY2007	FY2006	FY2005
Salaries and benefits	\$ 303,678	\$ 275,031	\$ 237,588
Contractual services	162,826	172,510	156,576
Materials and supplies	50,464	41,261	45,967
Administrative expenses	892	2,103	4,057
Utilities	25,524	28,282	29,023
Advertising and public relations	10,612	10,493	9,613
Other operating expenses	17,091	17,849	16,233
Total operating expenses before depreciation and amortization	571,087	547,529	499,057
Depreciation and amortization	92,230	83,945	76,189
Total operating expenses	\$ 663,317	\$ 631,474	\$ 575,246

Operating Expenses (continued)

Fiscal Year 2007 Compared to 2006. For fiscal year 2007, LAWA's operating expenses before depreciation increased \$23.6 million over fiscal year 2006 to \$571.1 million, or 4.3%. The category that shows the highest operating expense growth is salaries and benefits, which grew \$28.6 million, or 10.4%, to \$303.7 million. Of these two large expense components, salary expense, grew by \$21.2 million, or 10.2%, to \$223.5 million. The second largest component, employee benefits, increased \$7.5 million to \$80.2 million, or 10.2%. The growth to LAWA benefits expense comes largely from a \$4.0 million increase to its workers' compensation claims reserve maintained at an actuarial level relative to LAWA's larger staff size and mix of employee job types. Other significant impacts to employee benefits stem from LAWA's health subsidy and retirement contribution payments to the City, which increased by \$2.6 million, or 11.7%, and \$0.8 million, or 1.8%, respectively. The higher cost of benefits expenses came also as a direct result of increases in both medical and dental insurance that LAWA pays for its larger employee base, growing by 6.3 % to 3,702 full time equivalent employees at June 30, 2007. Of the total LAWA staff, 3,080 full time equivalent personnel are working at LAX, while 499 full time equivalent employees work at ONT.

The operating expense category having the second largest expense growth in fiscal 2007 is materials and supplies, which increased \$9.2 million, or 22.3%, to \$50.5 million. This increase is due largely to the impact of LAWA's personal computer technology upgrade project during fiscal year 2007. This project cost LAWA \$5.3 million to replace the complete desktop configuration for every employee who uses a computer to assist them in their daily assignments. Other substantial increases in materials and supplies expense came from higher fuel costs for LAWA pool vehicles, uniform replacement cost, air conditioning repairs, and automotive repair parts, at \$1.4 million, \$0.8 million, \$0.6 million and \$0.4 million, respectively. In the remaining categories of operating expenses, contractual services expense reflected the largest decline of \$9.7 million, or 5.6%. This decrease is due mainly to reductions in city services of \$5.1 million, environmental contracts for \$2.7 million; systems support services of \$4.5 million and security services of \$3.2 million.

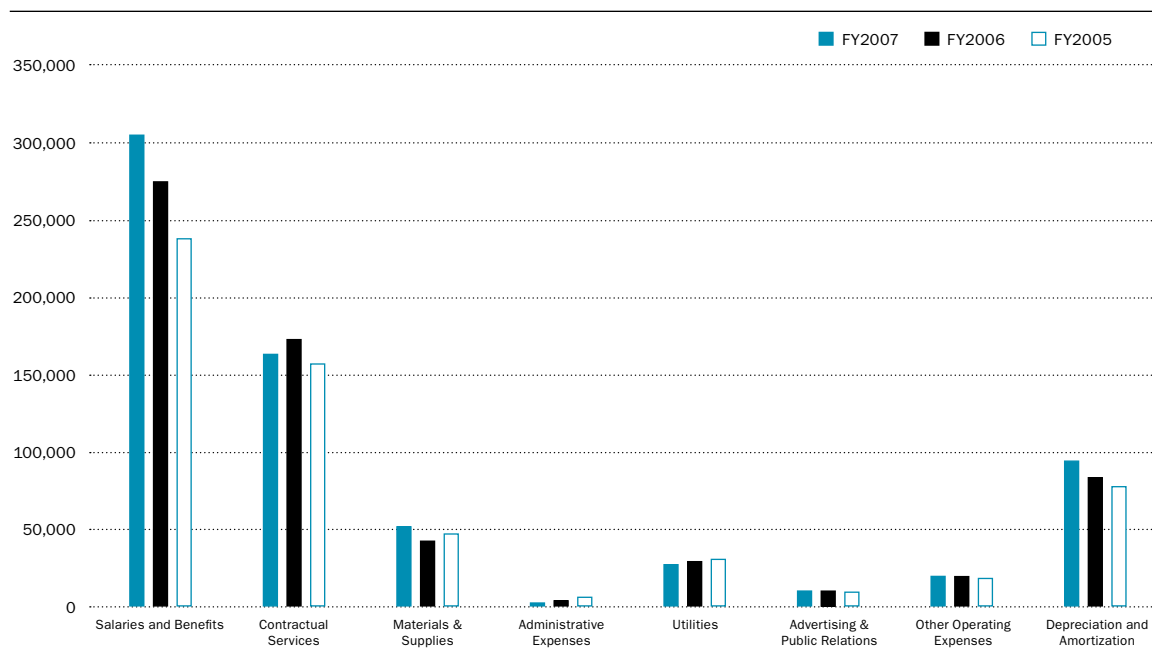
Fiscal Year 2006 Compared to 2005. For fiscal year 2006, LAWA's operating expenses before depreciation increased by \$48.5 million, or 9.7%, over fiscal year 2005 to \$547.5 million. The expense category showing the largest increase is LAWA's salaries and benefits of \$275.0 million, which grew \$37.4 million, or 15.8%, over the previous fiscal year. This growth stems from two factors. Salaries of \$205.0 million grew \$17.8 million, or 9.5%, to \$205.0 million. Also, retirement contributions increased \$18.8 million, or 71.4%, to \$45.1 million. Both of these factors are the result of a 138, or 4.1%, increase in full-time equivalent staff to 3,481, annual salary increases, and retro-active pay for certain employee groups. Also of note is contractual services expense, which grew by \$15.9 million, or 10.2%, due mainly to increases in security services of \$16.4 million and information technology services for \$4.5 million, partially offset by reduction in legal services for \$2.4 million and environmental and engineering consulting services of \$3.7 million.



Operating Expenses (continued)

The following chart illustrates comparative growth in LAWA's operating expenses by category for fiscal years 2007, 2006, and 2005:

LAWA-Operating Expenses (\$ in thousands)



Nonoperating Revenue and Expenses

Nonoperating revenue and expense consist of transactions that are not normally associated with ongoing operations of LAWA, but the impact can be significant to the total change in net assets for the fiscal year. Primary examples of this are collections of FAA-approved Passenger Facilities Charges (PFC), outgoing payments of debt-related interest, and receipts of interest from LAWA investing its idle cash.

Fiscal Year 2007 Compared to 2006. For fiscal year 2007, LAWA recorded a substantial 36.9% increase, or \$44.7 million, in net nonoperating revenues to \$165.7 million. This result is due primarily to the positive change of \$30.9 million in the fair value of investments resulting from the City of Los Angeles' pro-rata allocation from its investment pool to LAWA. Also, LAWA's interest income grew by \$6.4 million, or 16.3%, as a result of a positive market impact on its \$1.1 billion of invested cash. A more detailed explanation of the methodology impacting LAWA's investment activity is provided in Note 3 (a) and (c) of the accompanying notes to the financial statements. Additionally, PFC revenue of \$125.5 million increased by \$1.3 million, or 1.0%, over the prior fiscal year results. Of the total PFC's recorded during fiscal year 2007, \$116.1 million were reported by LAX and \$9.4 million were reported by ONT.

Nonoperating Revenue and Expenses (continued)

Fiscal Year 2006 Compared to 2005. For fiscal year 2006, LAWA recorded a decrease in net nonoperating revenues of \$17.0 million to \$121.1 million, compared to \$138.1 million for the prior fiscal period due to a decrease in nonoperating revenues and a slight increase in nonoperating expenses. Fiscal year 2006 gross nonoperating revenues (net of fair value adjustment for investments) of \$147.0 million represented a \$15.3 million, or 9.4% decrease from fiscal year 2005. The reason for this decrease was a \$14.5 million decline in the fair value of LAWA's pooled investments. PFC revenue, which accounted for \$124.2 million of LAWA's \$147.0 million in nonoperating revenue, increased by \$1.9 million, or 1.6%, from the prior fiscal year amount of \$122.3 million. This small increase over the prior fiscal year is merely the result of a very slight growth – 0.5% – in LAWA passenger traffic. Interest income grew by \$6.0 million, or 18.3%, to \$39.2 million.

Gross nonoperating expenses increased by \$1.6 million, or 6.8%, to \$25.9 million. A number of factors contributed to the increase. Interest expense of \$18.9 million was \$5.0 million less than the prior fiscal year because of the advanced refunding of bonds. Counterbalancing this decline was a \$4.8 million write-off of construction costs incurred in prior periods for abandoned projects and a \$1.4 million increase in litigation expense.

Income before Capital Grant Contributions

Fiscal Year 2007 Compared to 2006. Income before capital grant contributions was \$161.5 million for fiscal year 2007, which is 46.4%, or \$51.2 million, higher than the prior fiscal year amount of \$110.3 million. During fiscal year 2007, LAWA received grant contributions for approved capital grant projects in the amount of \$82.1 million, an increase of \$19.5 million, or 31.1%, over the prior year total of \$62.6 million. AIP capital contributions, which are important components of LAWA's grants revenue, grew by \$31.2 million to \$70.1 million. Of this amount, \$62.9 million came in to LAX, while \$6.4 million was reported by ONT and were used mainly for runway improvements. LAWA's change in net assets for fiscal year 2007 of \$243.5 million is 40.9%, or \$70.7 million higher than the change in net assets was for fiscal year 2006. Net Assets increased by 9.2% to \$2.9 billion at the end of 2007.

Fiscal Year 2006 Compared to 2005. Income before capital grant contributions was \$110.3 million for fiscal year 2006, which is 19.5%, or \$26.8 million, below the prior fiscal year amount of \$137.1 million. During fiscal year 2006, LAWA received grant contributions for approved capital grant projects in the amount of \$62.6 million, which is a substantial increase over the prior year's \$1.8 million. TSA capital contributions, which are an important component of capital grants, of \$23.4 million grew by \$21.7 million to \$22.4 million at LAX, and by \$3.6 million to \$3.9 million at ONT. The resulting change in net assets was \$172.9 million, reflecting an increase of \$34.0 million, or 24.5%, over the prior fiscal year change amount of \$138.9 million. Net assets increased by 7.0% to \$2.6 billion at end of fiscal year 2006.



Additional Information

Further information on the results of LAWA is provided in the accompanying audited financial statements and notes thereto for the years ended June 30, 2007 and 2006. This Management Discussion and Analysis (MD&A) is designed to provide LAWA and its customers, investors, and creditors with a general overview of LAWA's financial condition and to present information about the money that it receives and spends for the fiscal years reported. If you have questions about this MD&A, or need additional financial information, please contact the Los Angeles World Airports Financial Reporting Division at 7301 World Way West, 6th Floor, Los Angeles, California 90045. Also, you may find historical and other useful information regarding LAWA and the other LAWA airports from our website at www.lawa.org.

STATEMENT OF NET ASSETS

June 30, 2007 and 2006

ASSETS

(Dollars in Thousands)	2007	2006
Current assets:		
Cash and pooled investments held by the City Treasurer (Note 3)	\$ 431,918	\$ 566,107
Investments with fiscal agents (Note 3)	153,452	—
Accounts receivable, net of allowance for uncollectible accounts of \$2,099 and \$4,063 in 2007 and 2006, respectively	19,250	25,131
Unbilled receivables	33,338	27,228
Accrued interest receivable	6,046	7,330
Prepaid expenses and inventories	3,953	3,256
Total current assets	647,957	629,052
Noncurrent assets:		
Restricted assets:		
Cash and pooled investments held by the City Treasurer (Note 3)	800,818	642,826
Investments with fiscal agents (Note 3)	34,588	37,190
Accrued interest receivable	5,501	4,602
Passenger facility charges receivable (Note 12)	19,863	20,966
Total restricted assets	860,770	705,584
Capital assets (Note 4):		
Land, land clearance, and air easements	751,992	732,643
Buildings, improvements, and equipment	2,141,664	1,896,023
Leased property	184,423	184,423
Less accumulated depreciation and amortization	(1,148,458)	(1,065,538)
Construction work in process	452,102	286,985
Net capital assets	2,381,723	2,034,536
Deferred bond issuance expense	3,732	3,947
Total noncurrent assets	3,246,225	2,744,067
Total assets	\$ 3,894,182	\$ 3,373,119

See accompanying notes to financial statements.

LIABILITIES AND NET ASSETS

(Dollars in Thousands)	2007	2006
Current liabilities:		
Current liabilities payable from unrestricted assets:		
Contracts and accounts payable	\$ 82,083	\$ 58,560
Employee benefits and insurance claims payable (Notes 6)	8,172	7,481
Salaries payable	5,292	4,495
Commercial paper notes payable (Note 5)	178,745	—
Current obligations under capital leases (Notes 6 and 11)	1,140	1,026
Deferred revenue (Note 6)	50	50
Accrued interest payable	1,959	—
Other liabilities (Note 6)	5,319	6,883
Current liabilities payable from unrestricted assets	<u>282,760</u>	<u>78,495</u>
Current liabilities payable from restricted assets:		
Obligations under securities lending transactions	201,835	179,986
Bonds payable, plus net deferred credits of \$958 and \$717 in 2007 and 2006, respectively (Note 5)	16,088	15,332
Contracts and accounts payable	23,995	32,277
Accrued interest payable	1,487	1,846
Current liabilities payable from restricted assets	<u>243,405</u>	<u>229,441</u>
Total current liabilities	<u>526,165</u>	<u>307,936</u>
Long-term liabilities:		
Bonds payable, plus net deferred charges and credits of \$7,286 and \$6,621 in 2007 and 2006, respectively (Note 5)	295,831	329,176
Obligations under capital leases – less current portion (Notes 6 and 11)	50,715	51,855
Employee benefits and insurance claims payable (Notes 6)	31,446	30,246
Deferred revenue (Note 6)	1,121	1,171
Other liabilities (Note 6 and 14)	111,458	18,833
Total long-term liabilities	<u>490,571</u>	<u>431,281</u>
Total liabilities	<u>1,016,736</u>	<u>739,217</u>
Net assets:		
Invested in capital assets, net of related debt	1,992,657	1,637,147
Restricted:		
Capital projects	645	16,040
Debt service	33,231	35,472
Special purpose	599,578	439,963
Unrestricted	251,335	505,280
Total net assets	<u>\$ 2,877,446</u>	<u>\$ 2,633,902</u>

See accompanying notes to financial statements.

STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS

June 30, 2007 and 2006

(Dollars in Thousands)	2007	2006
Operating revenue:		
Aviation revenue:		
Landing fees	\$ 172,495	\$ 162,037
Building rentals	141,521	148,320
Other aviation revenue	74,114	66,024
Concession revenue	265,112	239,936
Airports sales and services	3,306	2,463
Miscellaneous revenue	2,477	1,919
Total operating revenue	659,025	620,699
Operating expenses:		
Salaries and benefits	303,678	275,031
Contractual services	162,826	172,510
Material and supplies	50,464	41,261
Administrative expense	892	2,103
Utilities	25,524	28,282
Advertising and public relations	10,612	10,493
Other operating expenses	17,091	17,849
Total operating expenses before depreciation and amortization	571,087	547,529
Income from operations before depreciation and amortization	87,938	73,170
Depreciation and amortization	(92,230)	(83,945)
Operating loss	(4,292)	(10,775)
Nonoperating revenue (expenses):		
Passenger facility charges (Note 12)	125,515	124,223
Interest income	45,550	39,150
Change in fair value of investments	13,059	(17,847)
Interest expense	(20,922)	(18,861)
Bond expense	(407)	(423)
Gain on sale of securities	1,086	217
Other nonoperating expenses	—	(6,600)
Other nonoperating revenue	1,867	1,218
Total nonoperating revenue, net	165,748	121,077
Income before contributions and transfers	161,456	110,302
Capital grant contributions (Note 13)	70,074	38,834
TSA contributions (Note 13)	12,014	23,756
Change in net assets	243,544	172,892
Net assets, beginning of year	2,633,902	2,461,010
Net assets, end of year	\$ 2,877,446	\$ 2,633,902

See accompanying notes to financial statements.

STATEMENT OF CASH FLOWS

June 30, 2007 and 2006

DEPARTMENT OF AIRPORTS OF THE CITY OF LOS ANGELES, CALIFORNIA



(Dollars in Thousands)	2007	2006
Cash flows from operating activities:		
Receipts from customers	\$ 649,788	\$ 618,309
Cash received in protest from customers	91,680	—
Payments for goods and services	(300,123)	(273,811)
Payments to employees	(300,990)	(269,069)
Other receipts (payments) for operating activities	(38)	(3,898)
Net cash provided by operating activities	<u>140,317</u>	<u>71,531</u>
Cash flows from capital and related financing activities:		
Acquisition and construction of capital assets	(379,222)	(205,973)
Receipts from passenger facility charges	126,618	118,973
Principal payments on bonds	(33,495)	(23,885)
Interest payments on bonds	(19,791)	(17,913)
Bond issuance cost paid	(192)	—
Bond payment liability returned as escheated funds	—	467
Principal payment on capital leases	(1,026)	(912)
Interest payment on capital leases	(2,263)	(1,802)
Commercial paper and issuance/(payments)	178,745	(15,500)
Cash transferred to fiscal agents	2,602	758
Federal grants receipts	82,088	62,590
Net cash used in capital and related financing activities	<u>(45,936)</u>	<u>(83,197)</u>
Cash flows from investing activities:		
Increase (decrease) in fair value of investments	13,059	(17,503)
Investment income receipts	47,966	37,493
Securities lending cash collateral receipt	21,849	12,033
Net cash provided by investing activities	<u>82,874</u>	<u>32,023</u>
Net decrease in cash and cash equivalents	177,255	20,357
Cash and cash equivalents, beginning of year	<u>1,208,933</u>	<u>1,188,576</u>
Cash and cash equivalents, end of year	<u>\$ 1,386,188</u>	<u>\$ 1,208,933</u>

The following is a reconciliation of cash and cash equivalents to the statement of net assets:

Cash and pooled investments held by the City Treasurer – Unrestricted	\$ 431,918	\$ 566,107
Unrestricted investments held with fiscal agents	153,452	—
Cash and pooled investments held by the City Treasurer – Restricted	800,818	642,826
Total	<u>\$ 1,386,188</u>	<u>\$ 1,208,933</u>

See accompanying notes to financial statements.

STATEMENT OF CASH FLOWS (cont'd)

June 30, 2007 and 2006

(Dollars in Thousands)	2007	2006
Reconciliation of operating loss to net cash provided by operating activities:		
Operating loss	\$ (4,292)	\$ (10,775)
Adjustments to reconcile operating loss to net cash provided by operating activities:		
Depreciation and amortization	92,230	83,945
Change in allowance for uncollectible accounts	(1,964)	(173)
Other revenues (expenses), net	1,335	(5,725)
Changes in operating assets and liabilities:		
Accounts receivable	3,917	389
Unbilled receivables	(6,110)	(2,779)
Prepaid expenses and inventories	(697)	(626)
Contracts and accounts payable	(37,801)	4,295
Employee benefits and insurance claims payable	1,891	4,443
Salaries payable	797	1,519
Deferred revenue	(50)	(50)
Other liabilities	91,061	(2,932)
Total adjustments	144,609	82,306
Net cash provided by operating activities	\$ 140,317	\$ 71,531
Noncash capital, and financing activities:		
Bond proceeds deposited to escrow account for bond refunding	\$ 93,272	\$ —
Acquisition of capital assets	53,042	27,821

See accompanying notes to financial statements.

(1) Reporting Entity and Summary of Significant Accounting Policies**(a) Organization and Reporting Entity**

The financial statements of the Los Angeles World Airports (Department of Airports of the City of Los Angeles, California) (LAWA) have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) as applied to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles.

LAWA is an independent, financially self-sufficient department of the City of Los Angeles (the City) established pursuant to Article XXIV, Section 238 of the City Charter. LAWA operates Los Angeles International Airport (LAX), LA/Ontario International Airport (ONT), Van Nuys Airport (VNY) and LA/Palmdale Regional Airport (PMD) and collectively, the Airport System.

LAWA is under the management and control of a seven-member Board of Airport Commissioners (the Board) appointed by the City Mayor and approved by the City Council. Under the City Charter, the Board has the general power to, among other things: (a) acquire, develop and operate all property, plant and equipment as it may deem necessary or convenient for the promotion and accommodation of air commerce; (b) borrow money to finance the development of airports owned, operated or controlled by the City; and (c) fix, regulate and collect rates and charges for use of the Airport System. An Executive Director administers LAWA and reports to the Board.

The financial statements presented herein represent the financial position and changes in financial position and cash flows of LAWA only and are not intended to present fairly the financial position, changes in financial position, or cash flows of the City in conformity with GAAP.

(b) Basis of Accounting

LAWA is reported as an enterprise fund and maintains its records on the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded when the related liability is incurred. Separate funds are used to account for each airport in the Airport System. Only the funds of LAWA are included in the reporting entity. Bonds issued by LAWA are payable solely from revenues of LAWA and are not general obligations of the City. LAWA applies all applicable GASB pronouncements as well as Financial Accounting Standards Board (FASB) Statements and Interpretations, Accounting Principles Board Opinions, and Accounting Research Bulletins issued on or before November 30, 1989, unless such pronouncements conflict with or contradict GASB pronouncements.

(1) Reporting Entity and Summary of Significant Accounting Policies (continued)

(c) Cash and Pooled Investments

All cash collections are deposited with and all payments are withdrawn from the City Treasurer with the exception of certain bond financing activity of LAWA's outstanding bonds. In order to maximize investment return, LAWA pools its available cash with that of the City, which is invested by the City Treasurer (see Note 3).

LAWA's investments, including its share of the City's pooled investments, are stated at fair value. Fair value is determined based upon market closing prices or bid/asked prices for regularly traded securities. The fair value of mutual funds, government-sponsored investment pools and other similar investments are stated at share value, or appropriate allocation of fair value of the pool, if separately reported. Certain money market investments with initial maturities at the time of purchase of less than one year are recorded at cost.

Interest income arising from such cash and pooled investments is apportioned to LAWA based on the relationship of LAWA's respective daily cash balances to aggregate cash and pooled investments.

(d) Accounts Receivable and Unbilled Receivables

LAWA recognizes revenue in the period earned. Receivables aged beyond 90 days are put into the collection process and then referred after 120 days to LAWA's resident City attorneys for possible write-off. An allowance for uncollectible accounts is set as a reserve by LAWA policy. This policy requires that 2% of outstanding receivables plus all referrals to City Attorney be reserved as uncollectible through a provisional month-end charge to operating expense. Unbilled receivable balances are the result of revenue accrued for services that exceed \$5,000 each, but not yet billed as of year-end. This accrual activity occurs primarily at year-end when services provided in the current fiscal period might not get processed through the billing system for up to sixty days into the next fiscal year.

(e) Contracts Payable, Accounts Payable and Other Liabilities

All transactions for goods and services obtained by LAWA from City-approved contractors and vendors are processed for payment via its automated payment system. This procedure results in the recognition of expense in the period that an invoice for payment is processed through the system, or when a vendor first provided the goods and/or services. If the goods and/or services were received or if the invoice was received but not yet processed in the system, and then an accrual is made manually by journal voucher into the general ledger to reflect the liability to the vendor. When LAWA makes agreements that require customers to make cash deposits, these amounts are then reflected as other current liabilities. Reserves for claims and litigation are recorded as other long-term liabilities.

(1) Reporting Entity and Summary of Significant Accounting Policies (continued)**(f) Securities Lending**

The City Treasurer engages in securities lending activities. LAWA's share of assets and liabilities arising from the reinvested cash collateral has been recognized in the accompanying financial statements (see Note 3).

(g) Investments with Fiscal Agents

LAWA has funds that are held by fiscal agents and pledged to the payment or security of the 1995, 1996, 2002, 2003, and 2006 bonds (see Note 3).

(h) Federal Grants

When a grant agreement is approved and eligible expenditures are incurred, the amount is recorded as a federal grant receivable and as capital grant contributions in the statements of revenues, expenses and changes in net assets.

(i) Capital Assets

All capital assets are carried at cost, or at estimated fair value on the date received in the case of properties acquired by donation or by termination of leases, less allowance for accumulated depreciation. Such cost includes, where appropriate, interest capitalized as part of the cost of construction of capital assets. Maintenance and repairs are charged to operations in the period incurred. Renewals and betterments are capitalized in the asset accounts. LAWA has a capitalization threshold of \$5,000 for all capital assets.

(j) Landing Fees

Landing fee rates are used to determine what fees are to be charged to the airlines each time that a qualified aircraft lands at either LAX or ONT. These fees are calculated using complex and unique allocation methods of relevant operating costs attributable to operational activities approved by the airlines. Two types of landing fee methods are applied by LAWA: compensatory and residual. Under a compensatory fee methodology, the fees charged by LAX for a facility or service are based on costs attributable only to that facility or service. For example, the landing fees charged for using the airfield and apron are based on LAWA's actual costs of operating the airfield and apron. Under a residual fee methodology, ONT sets the airlines' landing fees so that those fees provide the revenue needed to offset the difference between ONT's total expenses and the revenues collected by the airport from other sources, such as concession revenues and persons using its parking lots. For control purposes, the landing fees at LAX and ONT airports are calculated twice each fiscal year.

(k) Concessions Revenue

Concession revenue is generated through LAWA concessionaires or tenants, who pay monthly fees for using airport facilities to offer their goods and services to the general public and air traveling community. Payments to LAWA are based on negotiated agreements with concessionaires to remit amounts based on either a Minimum Annual Guarantee (MAG) or on gross receipts. Amounts recorded to concession revenue are determined by the type of

(1) Reporting Entity and Summary of Significant Accounting Policies (continued)

(k) Concessions Revenue (continued)

revenue category set up in the general ledger system and integrated with the monthly accounts receivable billing process. Concession revenue is recorded as it is earned. Some tenant agreements require self-reporting of concession operations and/or sales. The tenants' operations report and payment are due to LAWA in the month following the activity. The timing of concessionaire reporting and when revenue earned is recorded will determine when accruals are required for each tenant.

(l) Depreciation and Amortization

Depreciation expense includes amortization of assets under capital leases. Depreciation and amortization are computed on a straight-line basis. The estimated useful lives of the major property classifications are as follows: buildings and facilities, 10 to 40 years; landplane ports, 10 to 35 years; and equipment, 5 to 20 years. No depreciation is provided for construction work in process until construction is completed and/or the asset is placed in service.

(m) Preliminary Costs of Capital Projects

Preliminary costs of capital projects incurred prior to the finalization of formal construction contracts are capitalized. In the event the proposed capital projects are abandoned, the associated preliminary costs are charged to expense in the year of abandonment.

(n) Operating and Nonoperating Revenue and Expenses

Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with an enterprise fund's principal ongoing operations. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses. LAWA derives operating revenues primarily from landing fees, terminal space rental, auto parking, and concessions. LAWA's major operating expenses include salaries and employee benefits, fees for contractual services related to security and parking management, and other expenses such as maintenance, insurance, and utilities.

(o) Interest Expense

LAWA capitalizes interest expense (net of interest earnings) for capital projects during construction. Interest expense was \$20,922,000 for the year ended June 30, 2007 and \$18,861,000 for the year ended June 30, 2006. There was no capitalized interest in 2007 and 2006.

(p) Deferred Revenue

Deferred revenue consists of concessionaire rentals and payments received in advance, which will be amortized to revenue on the straight line basis over the applicable period.

(1) Reporting Entity and Summary of Significant Accounting Policies (continued)**(q) Employee Benefits**

LAWA employees accumulate annual vacation and sick leave in varying amounts based on length of service. Vacation and sick leave is recorded as earned. Upon termination or retirement, employees are paid the cash value of their accumulated leave.

(r) Statements of Cash Flows

Cash and cash equivalents as reported in the statements of cash flows include short-term, highly liquid investments that are both readily convertible to known amounts of cash and have maturities of three months or less at the time of purchase. Cash and investments (both restricted and unrestricted) held by the City Treasurer are, in effect, demand deposits and are, therefore, considered to be cash equivalents.

(s) Use of Estimates

The preparation of the financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts in the financial statements and accompanying notes. Actual results could differ from the estimates.

(t) Reclassifications

Certain reclassifications have been made to fiscal year 2006 amounts in order to conform to the fiscal year 2007 presentation.

(u) Inventory

LAWA's inventory consists primarily of general office supplies and is recorded at cost on a first-in, first-out basis.

(v) Bond Premiums, Discounts, and Issuance Costs

Bond premiums, discounts, issuance costs, and gains and losses on extinguishment are deferred and amortized over the life of the bonds. Bonds payable are reported net of the applicable bond premium or discount and deferred losses on extinguishment. Bond issuance costs are reported as deferred charges and amortized over the term of the related debt.

(w) Net Assets

The financial statements utilize a net assets presentation. Net assets are categorized as follows:

- *Invested in Capital Assets, Net of Related Debt* – This category groups all capital assets into one component of net assets. Accumulated depreciation and the outstanding balances of debt that are attributable to the acquisition, construction, or improvement of these assets reduce the balance in this category.

(1) Reporting Entity and Summary of Significant Accounting Policies (continued)

(w) Net Assets (continued)

- *Restricted Net Assets* – This category presents external restrictions imposed by creditors, grantors, contributors, or laws or regulations of other governments and restrictions imposed by law through constitutional provisions or enabling legislation. At June 30, 2007 and 2006, net assets of \$414.9 million and \$365.7 million, respectively, are restricted by enabling legislation.
- *Unrestricted Net Assets* – This category represents net assets of LAWA, not restricted for any project or other purpose.

(2) Accounting Changes and Recent Accounting Pronouncements

(a) Accounting Changes

The City of Los Angeles early implemented GASB Statements No. 45 and No. 50, accordingly, LAWA also implemented the provisions of these statements to the extent they relate to the department's financial statements:

GASB Statement No. 45, *"Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions."* Issued in June 2004, this statement addresses how state and local governments should account for and report their costs and obligations related to postemployment healthcare and other nonpension benefits, collectively referred to as other postemployment benefits (OPEB). The statement generally requires that state and local governmental employers account for and report the annual cost of OPEB and the outstanding obligations and commitments related to OPEB in essentially the same manner as they currently do for pensions.

GASB Statement No. 50, *"Pension Disclosures- An amendment of GASB Statements No. 25 and No. 27."* Issued in May 2007, the objective of this statement is to amend note disclosure and required supplementary information standards of Statement No. 25, *"Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans,"* and Statement No. 27, *"Accounting for Pensions by State and Local Government Employers,"* to conform with applicable changes adopted in GASB Statement Nos. 43 and 45. GASB 50 is intended to improve transparency and decision usefulness of reported information about pensions by state and local government plans and employers.

(b) Recent Accounting Pronouncements

In December 2006, GASB issued Statement No. 49, *"Accounting and Financial Reporting for Pollution Remediation Obligations."* This statement requires state and local governments to provide the public with better information about the financial impact of environmental cleanup and identifies the circumstances under which a government entity would be required to report a liability related to pollution remediation and how to measure that liability. The statement also requires governments to disclose information about their pollution obligations associated with clean up efforts in the notes to the financial statements. GASB Statement No.

(2) Accounting Changes and Recent Accounting Pronouncements

(b) Recent Accounting Pronouncements (continued)

49 will be effective for financial statements for periods beginning after December 15, 2007, but liabilities will be measured at the beginning of that period so that beginning net assets can be restated. LAWA is required to implement the statement for the fiscal year 2008-09 financial statements.

GASB Statement No. 51, *Accounting and Financial Reporting for Intangible Assets.* Issued in June 2007, this statement establishes standards for accounting and financial reporting for intangible assets, for all state and local governments. Types of assets that may be considered intangible assets include easements, water rights, timber rights, patents, trademarks, and computer software. GASB 51 will be effective for LAWA beginning in fiscal year 2010. Retroactive reporting is required.

(3) Cash and Investments

(a) Cash and Pooled Investments

Cash is deposited with the City Treasurer and generally invested in short-term investments under the City Treasurer's pooled investment program. The Los Angeles City Treasury Investment Procedures and Guidelines, established pursuant to the California Government Code and Los Angeles City Council action, govern the City's investment practices. The primary objectives of the City's investment policy are the safety of capital, the liquidity of the portfolio and the yield on the investments. Investments permitted by the City's investment policy include obligations of the U.S. Government and agencies, certain commercial paper, bankers' acceptances, medium-term corporate notes, negotiable certificates of deposit, repurchase agreements and state and local government pools (e.g., Local Agency Investment Fund) up to certain specified allowable percentages.

The City Treasurer manages the General Pool and Special Investment Pools. The investment disclosure information by pool is not available; accordingly, disclosures provided herein represent the combined General and Special Investment Pools. LAWA is invested only in the General Pool.

(3) Cash and Investments (continued)

(a) Cash and Pooled Investments (continued)

LAWA's equity in the City Treasurer's pooled investment and securities lending programs consists of the following cash and investments, based on the relative percentages of such equity to the General Investment Pool of the City Treasurer's pooled funds and is not necessarily indicative of LAWA's actual investments in the pooled funds (in thousands):

Description	2007	2006
Deposits	\$ 46,844	\$ 6,045
U.S. Treasury securities	357,493	169,251
Federal agency securities	438,854	575,452
Commercial paper	144,230	217,608
Medium-term corporate notes	245,315	240,577
Total	1,232,736	1,208,933
Less restricted portion	(800,818)	(642,826)
Unrestricted portion	\$ 431,918	\$ 566,107

The restricted portion represents cash and investments that are restricted as to use either by bond indenture requirements or the Federal Aviation Administration.

(3) Cash and Investments (continued)

(b) Investments Authorized by the City's Investment Policy

The table below identifies the investment types that are authorized for LAWA by the City's investment policy for the General Pool. The table also identifies certain provisions of the City's investment policy that address interest rate risk, credit risk, and concentration of credit risk.

	Maximum maturities	Maximum concentration
U.S. Treasury and federal agency securities	5 years	100%
Bonds issued by local agencies	5 years	100
Registered state warrants and municipal notes	5 years	100
Bankers' acceptances	180 days	40
Commercial paper	270 days	40
Negotiable certificates of deposit or time deposits	180 days	30
Yankee certificates of deposit	180 days	30
CRA certificates of deposit or time deposits	180 days	30
Repurchase agreements	1 year	100
Reverse repurchase agreements	92 days	5*
Medium-term corporate notes	5 years	30
Shares of a money market mutual fund	N/A	20
Securities lending program	N/A	20
Asset-backed securities	5 years	20**
Collateralized mortgage obligations	5 years	20**
Local agency investment fund (LAIF)		(per state limit)***

* The total of reverse repurchase agreements and the securities subject to a securities lending agreement may not exceed 20% of the total portfolio.

** Combined total for mortgage-backed and asset-backed securities.

*** Current account limit is \$40 million.

At June 30, 2007 and 2006, LAWA has \$1,232,736,000 and \$1,208,933,000, respectively, invested with the City Pool, which represents approximately 21.41% and 21.80%, respectively, of the City Treasury's General Investment Pool.

NOTES TO FINANCIAL STATEMENTS (cont'd)

June 30, 2007 and 2006

(3) Cash and Investments (continued)

(c) City of Los Angeles Investment Pool

At June 30, 2007, the investments held in the City Treasury's General and Special Investment Pool Programs and their maturities are as follows (in thousands):

Type of Investments	Amount	Investment Maturities			
		1 to 30 Days	31 to 60 Days	61 to 365 Days	366 Days To 5 Years
U.S. Treasury Notes	\$1,651,432	\$ —	\$ —	\$ 100,394	\$1,551,038
U.S. Government Agencies	2,588,342	270,397	63,258	267,283	1,987,404
Medium Term Notes	1,135,468	—	—	364,595	770,873
Commercial Paper	900,606	811,138	54,758	34,710	—
Guaranteed Investment Contract	314,860	314,860	—	—	—
State of California LAIF	2,664	2,664	—	—	—
Short Term Investment Funds	7	7	—	—	—
Securities Lending Cash Collateral					
U.S. Treasury Notes	898,087	—	—	5,386	892,701
U.S. Agencies	217,385	—	—	—	217,385
Total General and Special Pools	\$7,708,851	\$1,399,066	\$ 118,016	\$ 772,368	\$5,419,401

At June 30, 2006, the investments held in the City Treasury's General and Special Investment Pool Programs and their maturities are as follows (in thousands):

Type of Investments	Amount	Investment Maturities			
		1 to 30 Days	31 to 60 Days	61 to 365 Days	366 Days To 5 Years
U.S. Treasury Notes	\$ 750,633	\$ —	\$ —	\$ —	\$ 750,633
U.S. Treasury Bills	7,193	7,193	—	—	—
U.S. Government Agencies	3,483,994	229,854	259,964	519,398	2,474,778
Medium Term Notes	1,077,004	—	—	125,689	951,315
Commercial Paper	1,298,356	1,173,459	52,464	72,433	—
State of California LAIF	2,204	2,204	—	—	—
Short Term Investment Funds	13	13	—	—	—
Securities Lending Cash Collateral					
U.S. Treasury Notes	607,597	—	—	—	607,597
U.S. Agencies	344,340	—	—	—	344,340
Total General and Special Pools	\$7,571,334	\$1,412,723	\$ 312,428	\$ 717,520	\$5,128,663

Interest Rate Risk. The City's pooled investment policy limits the maturity of its investments as set forth in 3 (b) above.

Credit Risk. The City's pooled investment policy requires that for all classes of investments, except linked banking program certificates of deposits, the issuers must have minimum credit

(3) Cash and Investments (continued)

(c) City of Los Angeles Investment Pool (continued)

ratings as follows: Standard and Poor's Corporation (S&P) A-1/A; Moody's Investor Services (Moody's) P-1/A2; Fitch Ratings (Fitch), if available, F-1/A. The City's investments in Federal Agency securities were rated AAA by S&P and Aaa by Moody's. In addition medium term notes were rated A+ or better by S&P and A1 or better by Moody's, while investments in commercial paper were rated A-1+/A-1 by S&P, and P-1 by Moody's. As further required by the City's investment policy, issuers of medium-term notes are corporations that have total assets in excess of \$500 million and are operating within the United States. In addition, issuers of commercial paper notes are corporations organized in the United States as special purpose corporations, trust or limited liability companies having program-wide credit enhancements. The State of California Local Agency Investment Fund is not rated.

Concentration of Credit Risk. The City's investment policy does not allow more than 10% of its investment portfolio, except U.S. Treasury and federal agencies, to be invested in securities of a single issuer including its related entities. The City's investment policy further provides for a maximum concentration limit of 30% on any individual federal agency or government-sponsored entity. The City's pooled investments comply with these requirements. GAAP requires disclosure of certain investments in any one issuer that represent 5% or more of total investments, the City does not have such investment.

(d) City of Los Angeles Securities Lending Program

The Securities Lending Program (the SLP) is permitted and limited under provisions of California Government Code Section 53601. The City Council approved the SLP on October 22, 1991 under Council File No. 91-1860, which complies with the California Government Code. The objectives of the SLP in priority order are: safety of loaned securities; and prudent investment of cash collateral to enhance revenue from the investment program. The SLP is governed by a separate policy and guidelines, with oversight responsibility of the Investment Advisory Committee.

The City's custodial bank acts as the securities lending agent. In the event a counterparty defaults by reason of an act of insolvency, the bank shall take all actions which it deems necessary or appropriate to liquidate permitted investment and collateral in connection with such transaction and shall make a reasonable effort for two business days (Replacement Period) to apply the proceeds thereof to the purchase of securities identical to the loaned securities not returned. If during the Replacement Period the collateral liquidation proceeds are insufficient to replace any of the loaned securities not returned, the bank shall, subject to payment by the City of the amount of any losses on any permitted investments, pay such additional amounts as necessary to make such replacement.

Under the provisions of the SLP, and in accordance with the California Government Code, no more than 20% of the market value of the General Investment Pool (the Pool) shall be available for lending. The City receives cash as collateral on loaned securities, which is reinvested in securities permitted under the Policy. In accordance with the California

(3) Cash and Investments (continued)

(d) City of Los Angeles Securities Lending Program (continued)

Government Code, the securities lending agent marks to market the value of both the collateral and the reinvestments daily. Except for open loans where either party can terminate a lending contract on demand, term loans shall have a maximum life of 90 days. Earnings from securities lending shall accrue to the Pool and shall be allocated on a pro-rata basis to all Pool participants.

LAWA's share of cash collateral received and corresponding liability aggregated approximately \$201,835,000 and \$179,986,000 at June 30, 2007 and 2006, respectively. During the fiscal year, collateralizations on all loaned securities were within the required 102% of market value. The City can sell collateral securities only in the event of borrower default. The lending agent provides indemnification for borrower default. There were no violations of legal or contractual provisions and no borrower or lending agent default losses during the year. There was no credit risk exposure to the City because the amounts owed to the borrowers exceeded the amounts borrowed. Loaned securities are held by the City's agents in the City's name and are not subject to custodial credit risk.

(e) Investments with Fiscal Agents

LAWA also maintains investments with fiscal agents that are pledged to the payment or security of LAWA's 1995, 1996, 2002, 2003, and 2006 bonds. In addition to these funds, on February 1, 2007, LAWA deposited approximately \$148.7 million into revocable escrow accounts with a fiscal agent as a result of issuing commercial paper that will be used to finance terminal improvements at LAX. These funds remain in escrow at LAWA's discretion and can be withdrawn in accordance with the escrow agreements. These investments are also generally invested in short-term investments under the control of the fiscal agents.

The investment practices of the fiscal agents are the same as those of the City Treasurer, and have similar investment objectives. These investments are restricted as to their use and have maturities designed to coincide with required bond retirement payments.

These investments are uninsured and unregistered investments for which the securities are held by the counterparty's trust department or agent in LAWA's name.

LAWA's investments with fiscal agents were as follows (in thousands):

Description	FY 2007	FY 2006
Money Market Funds	\$ 161,643	\$ 16,875
U.S. Treasury Securities	26,397	20,315
Total	\$ 188,040	\$ 37,190

(4) Changes in Capital Assets

Capital asset activity for the year ended June 30, 2007 was as follows (in thousands):

	Balance at July 1, 2006	Additions	Deductions	Balance at June 30, 2007
Capital assets, not depreciated:				
Land and land clearance	\$ 685,668	\$ 23,594	\$ (4,245)	\$ 705,017
Air easements	46,975	—	—	46,975
Construction in progress	286,985	444,202	(279,085)	452,102
Total capital assets, not depreciated	1,019,628	467,796	(283,330)	1,204,094
Capital assets, depreciated:				
Buildings	767,950	7,508	—	775,458
Improvements	966,336	271,515	(50,044)	1,187,807
Equipment and vehicles	161,737	16,701	(39)	178,399
Leased property	184,423	—	—	184,423
Total capital assets, depreciated	2,080,446	295,724	(50,083)	2,326,087
Less accumulated depreciation:				
Buildings	(333,620)	(22,234)	2,829	(353,025)
Improvements	(515,861)	(57,336)	—	(573,197)
Equipment and vehicles	(125,243)	(7,869)	6,481	(126,631)
Leased property	(90,814)	(4,791)	—	(95,605)
Total accumulated depreciation	(1,065,538)	(92,230)	9,310	(1,148,458)
Total capital assets depreciation, net	\$ 1,014,908	\$ 203,494	\$ (40,773)	\$ 1,177,629
Total capital assets, net	\$ 2,034,536	\$ 671,290	\$ (324,103)	\$ 2,381,723

NOTES TO FINANCIAL STATEMENTS (cont'd)

June 30, 2007 and 2006

(4) Changes in Capital Assets (continued)

Capital asset activity for the year ended June 30, 2006 was as follows (in thousands):

	Balance at July 1, 2005	Additions	Deductions	Balance at June 30, 2006
Capital assets, not depreciated:				
Land and land clearance	\$ 683,006	\$ 4,929	\$ (2,267)	\$ 685,668
Air easements	46,975	—	—	46,975
Construction in progress	223,565	147,535	(84,115) *	286,985
Total capital assets, not depreciated	953,546	152,464	(86,382)	1,019,628
Capital assets, depreciated:				
Buildings	765,903	2,047	—	767,950
Improvements	837,305	129,031	—	966,336
Equipment and vehicles	152,924	8,813	—	161,737
Leased property	184,423	—	—	184,423
Total capital assets, depreciated	1,940,555	139,891	—	2,080,446
Less accumulated depreciation:				
Buildings	(314,058)	(19,562)	—	(333,620)
Improvements	(463,174)	(52,687)	—	(515,861)
Equipment and vehicles	(118,580)	(6,663)	—	(125,243)
Leased property	(85,781)	(5,033)	—	(90,814)
Total accumulated depreciation	(981,593)	(83,945)	—	(1,065,538)
Total capital assets depreciation, net	958,962	55,946	—	1,014,908
Total capital assets, net	\$ 1,912,508	\$ 208,410	\$ (86,382)	\$ 2,034,536

* Includes write-off of \$4,829 of costs incurred in prior periods for abandoned projects.

(5) Bonds and Commercial Notes Payable

LAWA issued revenue bonds in 1995, 1996, 2002, 2003, and 2006 for various airport improvement projects. LAWA's revenues are pledged as security for the bonds.

The 1995 Revenue Bonds were issued in the amount of \$365,855,000 to finance capital improvements and repay certain indebtedness. The bonds are limited obligations of the Department payable from and secured by a pledge of LAX revenues. The 1996 Series Revenue Bonds were issued in the amount of \$123,075,000 to finance capital improvements of ONT. The bonds were limited obligations of the Department payable from and secured by a pledge of ONT revenues. In fiscal year 2003, LAWA issued \$217,175,000 of revenue bonds to fund LAX airport improvement projects and advance refund a portion of the 1995 bonds. In fiscal year 2007, LAWA issued \$90,155,000 of Refunding Revenue Bonds to refund all of the 1996 Series Revenue Bonds. The refunding of the 1996 Series Revenue Bonds resulted in an economic gain of \$12,519,000 and a reduction of \$47,454,000 in future debt service payments.

During the fiscal year, LAX issued \$178,745,000 in commercial paper for key purposes. A portion of these funds are being used to reimburse the airport for cash used in the construction of improvements on the south airfield. Additionally, these funds are being used to fund deposits that have been placed into revocable escrow accounts used as an interim step toward maintaining the required IRS non-taxable definition for long term financing of defeasing outstanding bonds issued to finance terminal improvements at LAX.

Outstanding revenue bonds at June 30, 2007 mature in varying amounts through 2026. Bond and commercial paper notes activity for the year ended June 30, 2007 was as follows (in thousands):

Debt issue	Interest rate%	Balance at July 1, 2006	Additions	Deductions	Balance at June 30, 2007	Due in one year
Issue of 1995	5.00% to 8.38%	\$ 12,695	\$ —	\$ (2,500)	\$ 10,195	\$ 1,230
Issue of 1996	5.60 to 7.90	107,300	—	(107,300)	—	—
Issue of 2006	4.50 to 5.587	—	90,155	(4,530)	85,625	2,715
Issues of 2002 Series A	4.10 to 5.25	32,450	—	—	32,450	—
Issues of 2002 Series C	3.52*	57,400	—	—	57,400	—
Issues of 2003 Series A	3.58*	23,700	—	—	23,700	—
Issues of 2003 Series B	4.00 to 5.00	103,625	—	(9,320)	94,305	11,185
Subtotal		337,170	90,155	(123,650)	303,675	15,130
Commercial paper Series A	3.68*	—	30,000	—	30,000	30,000
Commercial paper Series B	5.26*	—	148,745	—	148,745	148,745
Deferred charges and credits, net	N/A	7,338	1,679	(773)	8,244	958
Total		\$ 344,508	\$ 270,579	\$ (124,423)	\$ 490,664	\$ 194,833

NOTES TO FINANCIAL STATEMENTS (cont'd)

June 30, 2007 and 2006

(5) Bonds and Commercial Notes Payable (continued)

Bonds and commercial paper notes activity for the year ended June 30, 2006 was as follows (in thousands):

Debt issue	Interest rate%	Balance at July 1, 2005	Additions	Deductions	Balance at June 30, 2006	Due in one year
Issue of 1995	5.00% to 8.38%	\$ 33,935	\$ —	\$ (21,240)	\$ 12,695	\$ 2,500
Issue of 1996	5.60 to 7.90	109,945	—	(2,645)	107,300	2,795
Issues of 2002 Series A	4.10 to 5.25	32,450	—	—	32,450	—
Issues of 2002 Series C	2.93*	57,400	—	—	57,400	—
Issues of 2003 Series A	2.92*	23,700	—	—	23,700	—
Issues of 2003 Series B	4.00 to 5.00	103,625	—	—	103,625	9,320
Subtotal		361,055	—	(23,885)	337,170	14,615
Commercial paper	2.65*	15,500	—	(15,500)	—	—
Deferred charges and credits, net	N/A	8,032	—	(694)	7,338	717
Total		\$ 384,587	\$ —	\$ (40,079)	\$ 344,508	\$ 15,332

* Average variable rate.

Future annual debt service requirements as of June 30, 2007, are as follows (in thousands):

Fiscal year ending June 30:	Principal	Interest ⁽¹⁾	Total
2008	\$ 15,130	\$ 14,150	\$ 29,280
2009	15,905	13,377	29,282
2010	16,705	12,580	29,285
2011	17,565	11,752	29,317
2012	18,435	10,887	29,322
2013 – 2017	107,595	40,091	147,686
2018 – 2022	86,460	15,192	101,652
2023 – 2026	25,880	3,352	29,232
Total	\$ 303,675	\$ 121,381	\$ 425,056

⁽¹⁾ Interest requirements for variable-rate bonds were determined using 3.65%, 3.65%, and 3.85% for 2002 C1, 2002 C2, and 2003 A, respectively, the rates in effect at June 30, 2007.



(6) Other Long-Term Liabilities

Other long-term liabilities' activity for the year ended June 30, 2007 was as follows (in thousands):

	Balance at July 1, 2006	Additions	Deductions	Balance at June 30, 2007	Due in one year
Employee benefits & insurance					
claims payable	\$ 37,727	\$ 13,847	\$ (11,956)	\$ 39,618	\$ 8,172
Deferred revenue	1,221	—	(50)	1,171	50
Obligations under capital leases	52,881	—	(1,026)	51,855	1,140
Other liabilities	25,716	108,239	(17,178)	116,777	5,319
Total	\$ 117,545	\$ 122,086	\$ (30,210)	\$ 209,421	\$ 14,681

Other long-term liabilities' activity for the year ended June 30, 2006 was as follows (in thousands):

	Balance at July 1, 2005	Additions	Deductions	Balance at June 30, 2006	Due in one year
Employee benefits & insurance					
claims payable	\$ 33,284	\$ 14,986	\$ (10,543)	\$ 37,727	\$ 7,481
Deferred revenue	1,271	—	(50)	1,221	50
Obligations under capital leases	53,793	—	(912)	52,881	1,026
Other liabilities	28,181	7,350	(9,815)	25,716	6,883
Total	\$ 116,529	\$ 22,336	\$ (21,320)	\$ 117,545	\$ 15,440

(7) Related Party Transactions

The City provides certain administrative, crash-fire-rescue, police services, and water and power to LAWA. The payments for these services, included in operating expenses for the years ended June 30, 2007 and 2006, were \$46,434,000 and \$50,955,000, respectively. In addition, LAWA collects parking taxes at LAX and ONT on behalf of the cities of Los Angeles and Ontario. Parking taxes collected and remitted to the cities of Los Angeles and Ontario were as follows (in thousands):

	2007	2006
City of Los Angeles	\$ 7,250	\$ 6,913
City of Ontario	4,683	4,866
Total	\$ 11,933	\$ 11,779

(8) Retirement System

(a) Retirement Plan Description

All full-time employees of LAWA are eligible to participate in the Los Angeles City Employees' Retirement System (LACERS) of the City of Los Angeles, California, a single employer defined benefit pension plan. LACERS serves as a common investment and administrative agent for various City departments and agencies that participate in LACERS.

(8) Retirement System (continued)

(a) Retirement Plan Description (continued)

LAWA makes contributions to LACERS for its pro rata share of retirement costs attributable to its employees.

LACERS provides retirement, disability, death benefits, postemployment healthcare benefits and annual cost-of-living adjustments based on the employees' years of service, age and final compensation. Employees with ten or more years of service may retire if they are at least 55 years old, or if the retirement date is between October 2, 1996 and September 30, 1999 at age 50 or older with at least 30 years of service. Normal retirement allowances are reduced for employees under age 60 at the time of retirement, unless they have more than 30 years of service and are age 55 or older. Employees aged 70 or above may retire at any time with no required minimum period of service. LACERS does not have a mandatory retirement age and none of LAWA's employees are required to contribute to LACERS.

(b) Actuarially Determined Contribution Requirements and Contributions Made

The Board of Administration of LACERS establishes and may amend the contribution requirements of System members and the City. Covered employees contribute to LACERS at a rate (8.22% to 13.33%) established through the collective bargaining process for those whose membership began prior to January 1, 1983 and at a fixed rate of 6% of salary for those who entered membership on or after January 1, 1983. The City subsidizes member contributions as determined by the actuarial consultant of LACERS. LAWA's pro rata share of the combined actuarially required contributions (ARC) for pension and postemployment healthcare benefits and actual contributions made to LACERS were approximately \$41,000,000 (100% of ARC), \$39,600,000 (100% of ARC) and \$25,900,000 (86.3% of ARC) for the years ended June 30, 2007, 2006, and 2005, respectively. The allocation of contributions between the pension and postemployment healthcare benefits is not available.



(8) Retirement System (continued)

(b) Actuarially Determined Contribution Requirements and Contributions Made (continued)

LACERS's funding policy provides for actuarially determined periodic contributions at rates such that sufficient assets will be available to pay benefits when due. The current year contribution requirement was determined based on the June 30, 2005 actuarial valuation, using the following actuarial assumptions:

LACERS	
Actuarial valuation date	June 30, 2005
Actuarial cost method	Projected unit credit
Amortization method	Level percent of payroll
Remaining amortization Period	Multiple layers not exceeding 30 years, closed
Asset valuation method	5-year market related
Actuarial assumptions:	
Investment rate of return	8%
Projected salary increases	4.75% - 10%
Inflation rate	3.75%
Cost of living adjustments	3%

(8) Retirement System (continued)

(b) Actuarially Determined Contribution Requirements and Contributions Made (Continued)

The City's and member contribution rates for the year ended June 30, 2007 are as follows:

Contribution Rates:	LACERS
City	14.6 % of covered payroll
Plan Members	8.22% to 13.33% of salaries at entry age with City subsidy for members prior to February 1983; 6% for entry date after January 1983

The City's annual pension cost, the percentage of annual pension cost contributed to the plans, and the net pension obligation for fiscal year 2006-07 and the two preceding years for each of the plans are as follows (in thousands):

	Year Ended	Annual Pension Cost (APC)	Percentage of APC Contributed	Net Pension Obligation
LACERS	06/30/05	\$ 183,242	100%	\$ (83,784)
	06/30/06	227,006	100%	(83,049)
	06/30/07	276,191	86%	(81,723)

The City allocated a pro rata share of its net pension obligation to the LAWA and the amounts recorded at June 30, 2007 and 2006 were \$8,298,000 and \$8,430,000, respectively.

(8) Retirement System (continued)

(c) Funded Status of LACERS

Based upon available data, the following is funded status information for the plan as of June 30, 2007, separate information for LAWA is not available (in thousands):

	LACERS	
Actuarial Accrued Liability (AAL)	\$	10,526,874
Actuarial Value of Assets		8,599,700
Underfunded AAL		1,927,174
Funded Ratio		81.7%
Covered Payroll	\$	1,896,609
Underfunded AAL as a percentage of covered payroll		101.6%

(8) Retirement System (continued)

(c) Funded Status of LACERS (continued)

The funded status of the plan as of June 30, 2007 was based on the following actuarial assumptions:

	LACERS
Actuarial valuation date	June 30, 2007
Actuarial cost method	Projected unit credit
Amortization method	Level percent of payroll
Remaining amortization Period	Multiple layers not exceeding 30 years, closed
Asset valuation method	5-year market related
Actuarial assumptions:	
Investment rate of return	8%
Projected salary increases	4.75% - 10%
Inflation rate	3.75%
Cost of living adjustments	3%

Actuarial valuations involve estimate of the value of reported amounts and assumptions about the probability of events in the future. Amounts determined regarding the funded status of the plans and the annual required contributions of the City are subject to continual revision as actual results are compared to past expectations and new estimates are made about the future.

The required schedule of funding progress, presented as Required Supplementary Information (RSI) in section (d) below, present multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the AAL for benefits.

Other contribution information and ten-year historical trend information can be found in LACERS's Comprehensive Annual Financial Report. Copies of LACERS's Comprehensive Annual Financial Report can be obtained from LACERS, 360 East Second Street, 2nd Floor, Los Angeles, California 90012.



(8) Retirement System (continued)

(d) Required Supplemental Information (Unaudited)

Based upon available data, the following represents the LACERS Schedule of Funding Progress, separate information for LAWA is not available (in thousands):

Schedule of Funding Progress
(in thousands)

Validation date (June 30)	Actuarial accrued liability (AAL)	Actuarial value of assets	Unfunded AAL	Funded ratio	Covered payroll	Unfunded AAL as a % of covered payroll
2005	\$ 9,321,525	\$ 7,193,142	\$ (2,128,383)	77.2%	\$ 1,589,306	(133.9)%
2006	9,870,662	7,674,999	(2,195,663)	77.8%	1,733,340	(126.7)%
2007	10,526,874	8,599,700	(1,927,174)	81.7%	1,896,609	(101.6)%

(e) Other Post-employment Benefits (OPEB)

LAWA, as a participant in LACERS, also provides a Retiree Health Insurance Premium Subsidy. Under Division 4, Chapter 11 of the City's Administrative Code, certain retired employees are eligible for this health insurance premium subsidy. This subsidy is to be funded entirely by the City. Employees with ten or more years of service who retire after age 55, or employees who retire at age 70 with no minimum service requirement, are eligible for a health premium subsidy with a City-approved health carrier. LACERS is advance funding the retiree health benefits on an actuarial-determined basis.

Projections of benefits are based on the substantive plan and include the types of benefits in force at the valuation date. Actuarial calculations reflect a long-term perspective and employ methods and assumptions that are designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial value of assets.

(8) Retirement System (continued)

(e) Other Postemployment Benefits (OPEB) (continued)

The City's annual required contribution rate for OPEB was 6.1% of annual covered payroll and was determined based on the June 30, 2005 actuarial valuation. Significant methods and assumptions are as follows:

LACERS OPEB	
Actuarial valuation date	June 30, 2005
Actuarial cost method	Projected unit credit
Amortization method	Level percent of payroll
Remaining amortization Period	Multiple layers not exceeding 30 years, closed
Asset valuation method	5-year market related
Actuarial assumptions:	
Investment rate of return	8%
Projected salary increases	N/A
Inflation rate	3.75%
Healthcare cost trend rates:	
Medical	12% graded down over 7 years to ultimate rate of 5%
Dental	5%

Amounts contributed specifically to the Retiree Health Insurance Premium Subsidy by LAWA alone are not available.



(8) Retirement System (continued)

(e) Other Postemployment Benefits (OPEB) (continued)

The City's annual pension cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB asset (obligation) for fiscal year 2006-07 and the two preceding years for the plan are as follows (in thousands):

	Year Ended	Annual Pension Cost (APC)	Percentage of APC Contributed	Net Pension Asset Obligation
LACERS	06/30/05	\$ 53,190	100%	—
	06/30/06	76,116	100%	—
	06/30/07	115,233	100%	—

From the most recent data made available by the City, as of June 30, 2007, LACERS membership consists of 30,175 active plan participants and 14,836 retired members. Also as of June 30, 2007, the date of the latest actuarial valuation of the City's Retiree Health Insurance Premium Subsidy, the total underfunded health benefit subsidy applicable to LACERS as a whole was approximately \$545,000,000 as follows (in thousands):

	LACERS
Annual Accrued Liability (AAL)	\$ 1,730,400
Actuarial Value of Assets	1,185,544
Underfunded AAL	544,856
Funded Ratio	68.5%
Covered Payroll	\$ 1,896,609
Underfunded AAL as a percentage of covered payroll	28.7%

(8) Retirement System (continued)

(e) Other Postemployment Benefits (OPEB) (continued)

The funded status of the OPEB plan as of June 30, 2007 was based on the following actuarial assumptions:

LACERS OPEB	
Actuarial validation date	June 30, 2007
Actuarial cost method	Projected unit credit
Amortization method	Level percent of payroll
Remaining amortization Period	Multiple layers not exceeding 30 years, closed
Asset valuation method	5-year market related
Actuarial assumptions:	
Investment rate of return	8%
Projected salary increases	N/A
Inflation rate	3.75%
Healthcare cost trend rates:	
Medical	8.75% decreasing by 0.5% for each year for eight years until it reaches an ultimate rate of 5%
Dental	5%

Actuarial valuations involve estimate of the value of reported amounts and assumptions about the probability of events in the future. Amounts determined regarding the funded status of the plans and the annual required contributions of the City are subject to continual revision as actual results are compared to past expectations and new estimates are made about the future. The require schedule of funding progress, presented as RSI in section (f) below, present multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the AAL for benefits.



(8) Retirement System (continued)

(f) Required Supplementary Information (Unaudited)

Based upon available data, the following represents the LACERS Schedule of Funding Progress for the OPEB plan; separate information for LAWA is not available (in thousands):

**Other Postemployment Benefits Healthcare Plans
Schedule of Funding Progress**
(in thousands)

Validation date (June 30)	Actuarial accrued liability (AAL)	Actuarial value of assets	Unfunded AAL	Funded ratio	Covered payroll	Unfunded AAL as a % of covered payroll
2005	\$ 1,718,899	\$ 893,378	\$ (825,521)	52.0%	\$ 1,589,306	(51.9)%
2006	1,730,799	990,270	(740,529)	57.2%	1,733,340	(42.7)%
2007	1,730,400	1,185,544	(544,856)	68.5%	1,896,609	(28.7)%

(9) Self-Insurance

LAWA is part of the City's self-administered and self-funded workers' compensation system. Claims and judgments are recorded when it is probable that an asset has been impaired or a liability has been incurred and the amount of loss can be reasonably estimated. The liability for workers' compensation claims includes a provision for incurred but not reported claims and loss adjustment expenses. Payment to the Workers' Compensation Division of the City Personnel Department has been made based on cash payments for workers' compensation claims. LAWA's accrued total liability for workers' compensation has been based on the results of an actuarial study. A reconciliation of the accrued workers' compensation liability (included in employee benefits and insurance claims payable) is as follows (in thousands):

Liability at June 30, 2005	\$ 27,578
Provisions for claims	14,701
Claim payments	<u>(7,171)</u>
Liability at June 30, 2006	35,108
Provisions for claims	13,491
Claim payments	<u>(11,600)</u>
Liability at June 30, 2007	36,999
Current portion	<u>(5,553)</u>
Long-term liability at June 30, 2007, net of current portion	<u>\$ 31,446</u>

The LAWA Risk Management Division oversees a sophisticated, self-administered Risk and Claims Management program. Claims are administered in-house by a dedicated team of Analysts who will manage and direct a claim/lawsuit until resolved. LAWA Risk Management (in cooperation with its contracted broker of record) is responsible for placing General Liability insurance policies (including a War & Terrorism policy) up to the policy limits of \$1.0 billion for

(9) Self-Insurance (continued)

General Liability coverage and \$1.25 billion for War and Terrorism coverage. Additional lines of insurance include General Property Insurance, with policy limits of \$1.5 billion, Boiler and Machinery coverage and Earthquake insurance. These insurance limits are in excess of LAWA's self-insured retention (deductible) which for general liability insurance is \$10,000/claim with a \$300,000 annual aggregate and \$125,000 per occurrence and annual aggregate on Property insurance. The self-insured retention for both Property and Liability insurance as well as the purchase of all insurance policies is budgeted and funded annually by the Risk Management Division. Historically, no liability or property claims have reached or exceeded the stated policy limits. LAWA also continues to maintain a catastrophic loss fund that is held in reserve to fund claims or losses that may conceivably breach insurance policy limits. The transference of risk exposure through the procurement of liability and property insurance has proven to be a very effective program for LAWA in its management of risk.

For other types of claims, commercial insurance is used when it is either legally or contractually required, or judged to be the most effective way to finance risk. LAWA's Risk Management Division estimates the risk exposure and uses the estimate together with past loss experience to determine maximum insurance coverage. For fiscal years 2007, 2006, and 2005, no claims were in excess of LAWA's insurance coverage. LAWA maintains approximately \$2.5 billion coverage of property, casualty general liability and other lines of insurance. LAWA also maintains an annual budget to fund the deductibles for property damage, general liability, and additionally maintains a catastrophic trust fund for any claims, losses in excess of the stated insurance coverage limits.

(10) Commitments and Contingencies

As of June 30, 2007, a number of claims and lawsuits are pending against LAWA that arose in the normal course of operations. LAWA recognizes a liability for claims and judgments when it is probable that an asset has been impaired or a liability has been incurred and the amount of loss can be reasonably estimated. The following is a summary of certain matters related to LAWA's operations.

(a) Environmental Issues

Through the normal course of operations, LAWA and its facilities are subject to potential environmental contamination and other environmental concerns. Accordingly, LAWA has established a comprehensive hazardous materials management plan for all facilities under its control. This plan calls for the evaluation of all property utilized by LAWA and the environmental cleanup of any sites found to be contaminated. This evaluation has not been completed to date.

(10) Commitments and Contingencies (continued)

(a) Environmental Issues (continued)

LAWA bears the financial responsibility for the cleanup of environmental contamination on property owned by it. However, LAWA believes that if the contamination originated based on contractual arrangements, the primary responsibility for any such cleanup would be borne by the tenants, even if they declare bankruptcy. LAWA, as property owner, however, assumes the ultimate responsibility for cleanup of such contamination in the event that the tenant is unable to make restitution. As a result of the hazardous materials management plan noted above, LAWA has already begun cleanup on several sites, is in the process of implementing additional safeguards to prevent additional hazardous substance contamination and is completing the environmental evaluation of LAWA's facilities. However, the extent of the cleanup and/or the ability of the original tenants to reimburse LAWA for such cleanup cannot be determined at the present time. Therefore, under the circumstances, it is reasonably possible that losses could be incurred; however, until such matters are resolved, the range of loss, if any, cannot be reasonably estimated.

(b) Other

Commitments for construction, the purchase of real property, equipment and materials and supplies amounted to \$53,200,000 and \$50,900,000 as of June 30, 2007 and 2006, respectively. Significant amounts in commitments for fiscal year 2007 are due to the following projects: \$19,200,000 for inspection testing, and surveying for the center taxiway and runway projects; and, \$14,000,000 for land acquisition.

(c) High-Security Environment

LAWA, like the rest of the North American air transportation system, has been adversely affected by the terrorist attacks that occurred in the United States on September 11, 2001 (the September 11 Events). Since the September 11 Events, due in part to the September 11 Events and in part to the slowdown in the national economy, significant declines have been experienced in aviation activity and enplaned passenger traffic, as well as in activity-based revenues consisting primarily of landing fees, passenger facility charges, concession revenues, and parking revenue. During fiscal year 2007, LAWA's passenger volume was 5.7%, or 4.1 million, below its pre-September 11th Events level.

As part of its program of proactively addressing heightened security concerns and requirements, LAWA has engaged in a review of its rates and charges, and has implemented revenue enhancements and expenditure controls that affect a variety of operating expenses. LAWA's capital improvement program was also reevaluated and several planned expenditures were suspended, except where the affected projects were near completion or essential from a security or safety standpoint.

Reductions in operating levels at LAWA from those which existed prior to the September 11 Events may continue for a period of time and to a degree that is uncertain. The future level of aviation activity and enplaned passenger traffic at LAWA will depend upon several factors directly and indirectly related to the September 11 Events, including, among others, the

(10) Commitments and Contingencies (continued)

(c) High-Security Environment (continued)

financial condition of individual airlines and the viability of continued service. A number of airlines are recovering from the economic difficulties they experienced immediately following the September 11 Events.

LAWA is unable to predict (i) the duration of current reduced air traffic volume, (ii) the long-term impact of the above-described events on costs and revenues of LAWA, (iii) the future financial condition of the airlines using LAWA's airports, or (iv) the likelihood of future incidents of terrorism or other air transportation disruptions.

(11) Capital Lease Agreements

LAWA has entered into various lease agreements with certain airlines. These agreements are classified as capital leases and are for certain public areas at LAX. Final terms regarding some of these agreements have not yet been agreed upon. Nonetheless, the agreements generally provide for the payment of amounts over various terms between 27 and 35 years, with interest at the rate incurred by the lessor on their related borrowings, which include improvement bonds. The property capitalized under these lease agreements amounted to \$184,423,000 at June 30, 2007 and 2006. Accumulated depreciation with respect to such property for the respective years was \$95.6 million and \$90.8 million, respectively.

Estimated future minimum lease payments under these agreements are as follows (in thousands):

Fiscal year ending June 30,		
2008	\$	3,061
2009		3,076
2010		3,146
2011		3,268
2012		3,327
2013 - 2017		18,248
2018 - 2022		22,029
2023 - 2026		<u>19,376</u>
Total minimum lease payments		75,531
Less interest portion		<u>(23,676)</u>
Present value of minimum lease payments	\$	<u>51,855</u>

LAWA currently uses rental credits to finance its obligations on capital leases with certain airlines. These rental credits are applied as an offset of amounts owed to LAWA by such airlines for terminal leases and landing fees.

(12) Passenger Facility Charges

In 1990, Congress approved the Aviation Safety and Capacity Expansion Act, which authorized domestic airports to impose a Passenger Facility Charge (PFC) on enplaning passengers. In May 1991, the FAA issued the regulations for the use and reporting of PFC's. PFC's may be used for airport projects that must meet at least one of the following criteria: (1) preserve or enhance safety, security or capacity of the national air transportation system; (2) reduce noise or mitigate noise impacts resulting from an airport; or (3) furnish opportunities for enhanced competition between or among carriers.

Since 1990, the following activities have taken place:

- In April 1993, the FAA granted LAWA's authority to collect PFC's at LAX and ONT in the amount of \$360,000,000 for 5 years for specifically approved airport improvement projects. Effective July 1, 1993, LAWA began collecting PFC's in the amount of \$3 per passenger.
- In 1996, LAWA received approval to transfer a portion of PFC revenue collected at LAX to fund projects at ONT. Effective January 1, 1996, the FAA approved LAWA's amended application to cease PFC collections at LAX after collecting approximately \$152,600,000.
- In May 1996, the FAA approved LAWA's request to transfer a portion of PFC revenues collected at LAX to fund approved projects at ONT. Accordingly, PFC charges totaling \$126,100,000 collected at LAX were transferred.
- In November 1997 and April 1998, the FAA approved LAWA's application to impose \$3 per passenger PFC's at LAX and ONT, respectively, for noise mitigation projects. Approved collections of \$150,000,000 at LAX were to be used for the soundproofing of City of Los Angeles residences and sound insulation of nearby city residences. Approved collections of \$45,700,000 at ONT were to be used for land acquisition and sound insulation of the City of Ontario residences.
- On October 2, 1998, the FAA approved LAWA's application to amend PFC's at LAX for noise mitigation projects. The amendment increased the total approved PFC revenue from \$150,000,000 to \$440,000,000.
- Effective August 1, 2003, the FAA approved an increase to the PFC charge at LAX from \$3.00 to \$4.50.

The PFC funds are recognized on the accrual basis of accounting, and the funds collected are restricted and may be used only on specifically approved projects. Due to their restricted use, PFC's are categorized as nonoperating revenues. All funds collected must be maintained in an interest-bearing account with the City Treasurer prior to disbursement. Cumulative PFC collections and the related interest earned as reported to the FAA were as follows (in thousands):

(12) Passenger Facility Charges (continued)

	2007	2006
Amount collected	\$ 1,090,973	\$ 964,356
Interest received	124,225	108,267
Cumulative PFC collections	<u>\$ 1,215,198</u>	<u>\$ 1,072,623</u>

Collected but unexpended PFC revenue is included on the statement of net assets as restricted cash and pooled investments held by the City Treasurer. Related accrued interest income and PFC receivables are also reported as restricted assets.

(13) Capital Grant Contributions

Contributed capital related to governmental grants and other aid increased by \$19.5 million to \$82.1 million during the year ended June 30, 2007. Capital grant funds were used for projects under the Airport Improvement Program and Transportation Security Administration security-related capital projects.

(14) Terminal Rents

LAWA has lease arrangements at its passenger terminal facilities with American Airlines, Continental Airlines, Delta Air Lines, LAX TWO Corporation, and United Air Lines (collectively, the "Long-term Airlines") that have various terms of up to 40 years. Under these leases, the Long-term Airlines pay various charges, including maintenance and operations rent ("M&O Rent") that reflects the expenses that LAWA incurs in maintaining and operating the terminals. The M&O Rent rates are set each calendar year based on the actual audited M&O expenses for the prior fiscal year ending June 30.

Historically, less than the full amount of M&O Expenses attributable to the airlines has been charged to the terminal tenants as M&O Rent. On December 18, 2006, the Board of Airport Commissioners ("BOAC") approved a resolution setting the M&O Rent rate for 2006, effective January 1, 2006, based upon the full amount of M&O expenses expended in the year ended June 30, 2005 attributable to the airlines for all LAX passenger terminals. These rates remain in effect until changed by board action.

The Long-term Airlines have objected to LAWA's calculation of the M&O Rents as approved by the BOAC for 2006. On January 18, 2007, American, Continental and United Airlines filed a complaint with the United States District Court objecting to the 2006 M&O Rents. Subsequently, Northwest Airlines, as the primary shareholder of LAX TWO, and Delta Air Lines also filed Objections.

Separately, the BOAC approved a new lease form on December 18, 2006 with a subsequent institution of a tariff on January 22, 2007. Certain carriers utilizing terminals 1 and 3 as well as carriers that operate from the Tom Bradley International Terminal objected to the tariff and filed a complaint with the Department of Transportation ("DOT"). The DOT issued its final decision on June 15, 2007. The decision resulted in a refund of portion of the amounts assessed under the tariff



(14) Terminal Rents (continued)

to the complainants. A small number of tenants and sub-tenants were not party to the DOT action and continue to be assessed at the tariff rate. Subsequent to the DOT decision on July 19, 2007, the carriers' party to the DOT complaint filed a Petition to Review at the United States Court of Appeals regarding the DOT ruling.

Pending the resolution of these objections, LAWA has classified the disputed cash portion of the M&O Rent and interest earned as "Cash under Protest" of \$92,625,214 and has not included these amounts as Revenue. The disputed portion of the M&O Rent is classified as "Customer Liability- Protested Revenue" and "Interest Earned under Protest;" both amounts are included as part of other long term liabilities reported in the Statement of Net Assets.

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COMBINING STATEMENT OF NET ASSETS

June 30, 2007 and 2006

(With comparative totals at June 30, 2006)

(Dollars in Thousands)	Los Angeles	Ontario	Van Nuys	Palmdale	Eliminations	Totals	
	International Airport	International Airport	Airport	Regional Airport		2007	2006
ASSETS							
Current assets:							
Cash and pooled investments held by the City Treasurer	\$ 383,911	\$ 48,007	\$ —	\$ —	\$ —	\$ 431,918	\$ 566,107
Investments with fiscal agents	153,452	—	—	—	—	153,452	—
Accounts receivable, net of allowance for uncollectible accounts	15,024	2,644	1,384	198	—	19,250	25,131
Unbilled receivable	33,323	—	14	1	—	33,338	27,228
Accrued interest receivable	5,635	411	—	—	—	6,046	7,330
Due from other agencies	32,000	—	—	—	(32,000)	—	—
Prepaid expenses and inventories	3,641	273	39	—	—	3,953	3,256
Total current assets	626,986	51,335	1,437	199	(32,000)	647,957	629,052
Noncurrent assets:							
Restricted assets:							
Cash and pooled investments held by the City Treasurer	713,691	83,626	3,499	2	—	800,818	642,826
Investments with fiscal agents	27,528	7,060	—	—	—	34,588	37,190
Accrued interest receivable	4,842	659	—	—	—	5,501	4,602
Passenger facility charges receivable	18,298	1,565	—	—	—	19,863	20,966
Total restricted assets	764,359	92,910	3,499	2	—	860,770	705,584
Capital assets:							
Land, land clearance, and air easements	619,766	28,291	12,615	91,320	—	751,992	732,643
Buildings, facilities and equipment	1,665,780	405,310	49,282	21,292	—	2,141,664	1,896,023
Leased property	184,423	—	—	—	—	184,423	184,423
Less accumulated depreciation	(959,812)	(153,302)	(27,696)	(7,648)	—	(1,148,458)	(1,065,538)
Construction work in process	355,555	83,551	12,324	672	—	452,102	286,985
Net capital assets	1,865,712	363,850	46,525	105,636	—	2,381,723	2,034,536
Deferred bond issuance expenses	2,504	1,228	—	—	—	3,732	3,947
Total noncurrent assets	2,632,575	457,988	50,024	105,638	—	3,246,225	2,744,067
Total assets	\$ 3,259,561	\$ 509,323	\$ 51,461	\$ 105,837	\$ (32,000)	\$ 3,894,182	\$ 3,373,119

See accompanying independent auditor's report.



(Dollars in Thousands)	Los Angeles	Ontario	Van Nuys	Palmdale	Eliminations	Totals	
	International Airport	International Airport	Airport	Regional Airport		2007	2006
LIABILITIES AND NET ASSETS							
Current liabilities:							
Current liabilities payable from unrestricted assets:							
Contracts and accounts payable	\$ 69,134	\$ 9,746	\$ 2,384	\$ 819	\$ —	\$ 82,083	\$ 58,560
Employee benefits and insurance claims payable	6,365	1,432	266	109	—	8,172	7,481
Salaries payable	4,218	704	343	27	—	5,292	4,495
Commercial paper notes payable	178,745	—	—	—	—	178,745	—
Due to other agencies	—	—	—	32,000	(32,000)	—	—
Current obligations under capital leases	1,140	—	—	—	—	1,140	1,026
Accrued interest payable	1,959	—	—	—	—	1,959	—
Deferred revenue	—	50	—	—	—	50	50
Other liabilities	4,065	554	554	146	—	5,319	6,883
Current liabilities payable from unrestricted assets	265,626	12,486	3,547	33,101	(32,000)	282,760	78,495
Current liabilities payable from restricted assets:							
Obligations under securities lending transactions	186,333	15,502	—	—	—	201,835	179,986
Bonds payable, plus net deferred charges and credits	13,334	2,754	—	—	—	16,088	15,332
Contracts and accounts payable	23,975	20	—	—	—	23,995	32,277
Accrued bond interest payable	955	532	—	—	—	1,487	1,846
Current liabilities payable from restricted assets	224,597	18,808	—	—	—	243,405	229,441
Total current liabilities	490,223	31,294	3,547	33,101	(32,000)	526,165	307,936
Long-term liabilities:							
Bonds payable, plus net deferred charges and credits	212,215	83,616	—	—	—	295,831	329,176
Obligations under capital leases	50,715	—	—	—	—	50,715	51,855
Employee benefits and insurance claims payable	26,070	4,276	650	450	—	31,446	30,246
Deferred revenue	—	1,121	—	—	—	1,121	1,171
Other liabilities	111,458	—	—	—	—	111,458	18,833
Total long-term liabilities	400,458	89,013	650	450	—	490,571	431,281
Total Liabilities	890,681	120,307	4,197	33,551	(32,000)	1,016,736	739,217
Net assets:							
Invested in capital assets, net of related debt	1,563,016	277,480	46,525	105,636	—	1,992,657	1,637,147
Restricted:							
Capital projects	164	481	—	—	—	645	16,040
Debt service	26,667	6,564	—	—	—	33,231	35,472
Special purpose	526,265	69,812	3,499	2	—	599,578	439,963
Unrestricted	252,768	34,679	(2,760)	(33,352)	—	251,335	505,280
Total net assets	\$ 2,368,880	\$ 389,016	\$ 47,264	\$ 72,286	\$ —	\$ 2,877,446	\$ 2,633,902

See accompanying independent auditor's report.

COMBINING STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS

June 30, 2007 and 2006

(With comparative totals at June 30, 2006)

(Dollars in Thousands)	Los Angeles International Airport	Ontario International Airport	Van Nuys Airport	Palmdale Regional Airport	Eliminations	Totals	
						2007	2006
Operating revenue:							
Aviation revenue:							
Landing fees	\$ 148,937	\$ 16,362	\$ 25	\$ —	\$ 7,171	\$ 172,495	\$ 162,037
Building rentals	107,338	28,559	4,741	883	—	141,521	148,320
Other aviation revenue	61,689	4,954	14,179	463	(7,171)	74,114	66,024
Concession revenue	227,177	37,929	3	3	—	265,112	239,936
Airport sales and services	2,824	83	92	307	—	3,306	2,463
Miscellaneous revenue	2,012	359	106	—	—	2,477	1,919
Total operating revenue	<u>549,977</u>	<u>88,246</u>	<u>19,146</u>	<u>1,656</u>	<u>—</u>	659,025	620,699
Operating expenses:							
Salaries and benefits	255,536	39,391	7,917	834	—	303,678	275,031
Contractual services	141,306	18,071	2,066	1,383	—	162,826	172,510
Materials and supplies	43,313	6,070	914	167	—	50,464	41,261
Administrative expenses	725	211	(51)	7	—	892	2,103
Utilities	20,101	4,912	314	197	—	25,524	28,282
Advertising and public relations	10,015	265	264	68	—	10,612	10,493
Other operating expenses	(2,472)	12,579	5,327	1,657	—	17,091	17,849
Total operating expenses							
before depreciation							
and amortization	<u>468,524</u>	<u>81,499</u>	<u>16,751</u>	<u>4,313</u>	<u>—</u>	571,087	547,529
Income (loss) from							
operations before							
depreciation and							
amortization	81,453	6,747	2,395	(2,657)	—	87,938	73,170
Depreciation and amortization	(72,438)	(16,471)	(2,395)	(926)	—	(92,230)	(83,945)
Operating income (loss)	<u>9,015</u>	<u>(9,724)</u>	<u>—</u>	<u>(3,583)</u>	<u>—</u>	(4,292)	(10,775)
Nonoperating revenue (expenses):							
Passenger facility charges	116,083	9,432	—	—	—	125,515	124,223
Interest income	39,502	5,909	139	—	—	45,550	39,150
Change in fair value of							
investments	10,386	2,673	—	—	—	13,059	(17,847)
Interest expense	(15,266)	(5,656)	—	—	—	(20,922)	(18,861)
Bond expense	(345)	(62)	—	—	—	(407)	(423)
Gain on sale of securities	1,082	4	—	—	—	1,086	217
Other nonoperating expenses	—	—	—	—	—	—	(6,600)
Other nonoperating revenue	810	207	850	—	—	1,867	1,218
Total nonoperating							
revenue, net	<u>152,252</u>	<u>12,507</u>	<u>989</u>	<u>—</u>	<u>—</u>	165,748	121,077
Income before							
contributions and							
transfers	161,267	2,783	989	(3,583)	—	161,456	110,302
Capital grant contributions	62,947	6,353	415	359	—	70,074	38,834
TSA contribution	11,094	920	—	—	—	12,014	23,756
Inter-agency transfers	(43,511)	—	43,511	—	—	—	—
Change in net assets	191,797	10,056	44,915	(3,224)	—	243,544	172,892
Net assets, beginning of year	2,177,083	378,960	2,349	75,510	—	2,633,902	2,461,010
Net assets, end of year	<u>\$ 2,368,880</u>	<u>\$ 389,016</u>	<u>\$ 47,264</u>	<u>\$ 72,286</u>	<u>\$ —</u>	\$ 2,877,446	\$ 2,633,902

See accompanying independent auditor's report.

COMPLIANCE SECTION

June 30, 2007 and 2006



DEPARTMENT OF AIRPORTS OF THE CITY OF LOS ANGELES, CALIFORNIA



MACIAS GINI & O'CONNELL LLP
CERTIFIED PUBLIC ACCOUNTANTS & MANAGEMENT CONSULTANTS

3000 S Street, Suite 300
Sacramento, CA 95816
916.928.4600

2175 N. California Boulevard, Suite 645
Walnut Creek, CA 94596
925.274.0190

515 S. Figueroa Street, Suite 325
Los Angeles, CA 90071
213.286.6400

402 West Broadway, Suite 400
San Diego, CA 92101
619.573.1112

The Members of the Board of Airport Commissioners
of the City of Los Angeles, California

**INDEPENDENT AUDITOR'S 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**

We have audited the financial statements of the Los Angeles World Airports (Department of Airports of the City of Los Angeles, California) (LAWA), an Enterprise Fund of the City of Los Angeles, California, as of and for the year ended June 30, 2007, and have issued our report thereon dated December 14, 2007. Our report included an explanatory paragraph regarding LAWA's adoption of Governmental Accounting Standards Board Statement (GASB) No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, and GASB Statement No. 50, *Pension Disclosures – an amendment of GASB Statement No. 25 and 27*, for the year ended June 30, 2007. 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

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

A control deficiency 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 misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects LAWA's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of LAWA's financial statements that is more than inconsequential will not be prevented or detected by LAWA's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by LAWA's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be 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 above.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether LAWA'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 LAWA's Board of Airport Commissioners, management, and federal awarding agencies and pass-through entities, and is not intended to be and should not be used by anyone other than these specified parties.

Macias Jini & O'Connell LLP

Certified Public Accountants

Los Angeles, California
December 14, 2007

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Business and Job Resources

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Bruce Brown
Risk Management



*Los Angeles
World Airports*

TM

LOS ANGELES INTERNATIONAL AIRPORT

One World Way
Los Angeles, CA 90045
Mailing: P.O. Box 92216
Los Angeles, CA 90009-2216
310.646.5252

LA/ONTARIO INTERNATIONAL AIRPORT

1940 East Moore Way
Room 200
Ontario, CA 91761
909.937.2710

LA/PALMDALE REGIONAL AIRPORT

Administrative Office
39516 North 25th Street, East
Palmdale, CA 93550
661.266.7602

VAN NUYS AIRPORT

16461 Sherman Way
Suite 300
Van Nuys, CA 91406
818.785.8838

CITY OF LOS ANGELES

Los Angeles World Airports
Clifton A. Moore Administration Building
One World Way
Los Angeles, CA 90045
Mailing: P.O. Box 92216
Los Angeles, CA 90009-2216
www.lawa.org

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