

**LOS ANGELES WORLD AIRPORTS**  
(Department of Airports of the City of Los Angeles, California)

**LOS ANGELES INTERNATIONAL AIRPORT**

Annual Financial Report

For the Years Ended June 30, 2009 and 2008

**LOS ANGELES WORLD AIRPORTS**  
 (Department of Airports of the City of Los Angeles, California)  
**LOS ANGELES INTERNATIONAL AIRPORT**  
 Annual Financial Report  
 For the Years Ended June 30, 2009 and 2008

*Table of Contents*

	<i>Page(s)</i>
<b>FINANCIAL SECTION:</b>	
Independent Auditor’s Report.....	1-2
<b>Financial Statements for the Years Ended June 30, 2009 and 2008:</b>	
Statements of Net Assets.....	3-4
Statements of Revenues, Expenses, and Changes in Net Assets.....	5
Statements of Cash Flows .....	6-7
Notes to Financial Statements .....	8-33
<b>COMPLIANCE SECTION:</b>	
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 <i>Government Auditing Standards</i> .....	34-35



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SACRAMENTO

OAKLAND

WALNUT CREEK

NEWPORT BEACH

SAN DIEGO

## INDEPENDENT AUDITOR'S REPORT

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

We have audited the accompanying basic financial statements of the Los Angeles International Airport (LAX), a department component of Los Angeles World Airports (Department of Airports of the City of Los Angeles, California) (LAWA), an Enterprise Fund of the City of Los Angeles (City), as of and for the years ended June 30, 2009 and 2008, as listed in the 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 LAX'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.

As disclosed in Note 1, the financial statements presents only LAX and do not purport to, and do not, present fairly the financial position of LAWA or the City as of June 30, 2009 and 2008, and the changes in their financial position and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of LAX as of June 30, 2009 and 2008 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 discussed in Note 2 to the basic financial statements, LAX implemented the provisions of Governmental Accounting Standards Board (GASB) Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*, and GASB Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*, during the year ended June 30, 2009.

In accordance with *Government Auditing Standards*, we have also issued our report dated March 12, 2010 on our consideration of LAX'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, 2009. 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.

*Macias Jini & O'Connell LLP*  
Certified Public Accountants

Los Angeles, California  
March 12, 2010

**LOS ANGELES WORLD AIRPORTS**  
 (Department of Airports of the City of Los Angeles, California)  
**LOS ANGELES INTERNATIONAL AIRPORT**  
 Statements of Net Assets  
 June 30, 2009 and 2008  
 (Dollars in thousands)

	<b>2009</b>	<b>2008</b>
<b>ASSETS</b>		
Current assets:		
Cash and pooled investments held by the City Treasurer (Note 3)	\$ 560,759	\$ 432,526
Investments with fiscal agents (Note 3)	101,879	101,780
Accounts receivable, net of allowance for uncollectible accounts of \$308 and \$768 in 2009 and 2008, respectively	8,732	11,041
Unbilled receivables	42,781	21,996
Accrued interest receivable	4,426	4,440
Due from other agencies (Note 8)	45,957	40,083
Prepaid expenses and inventories	5,217	4,806
Total unrestricted current assets	769,751	616,672
Restricted current assets:		
Cash and pooled investments held by the City Treasurer (Note 3)	691,212	791,178
Investments with fiscal agents (Note 3)	186,005	27,470
Accrued interest receivable	3,985	3,945
Passenger facility charges receivable (Note 13)	16,065	16,917
Total restricted current assets	897,267	839,510
Total current assets	1,667,018	1,456,182
Noncurrent assets:		
Capital assets (Note 4 and 12):		
Land and air easements	619,766	619,766
Buildings, improvements, and equipment	1,775,169	1,709,382
Leased property	184,423	184,423
Intangible assets	5,918	-
Less accumulated depreciation and amortization	(1,127,460)	(1,041,491)
Construction work in process	1,223,322	783,332
Net capital assets	2,681,138	2,255,412
Deferred bond issuance expenses	7,001	2,189
Total noncurrent assets	2,688,139	2,257,601
Total assets	\$ 4,355,157	\$ 3,713,783

See accompanying notes to financial statements.

**LOS ANGELES WORLD AIRPORTS**  
 (Department of Airports of the City of Los Angeles, California)  
**LOS ANGELES INTERNATIONAL AIRPORT**  
 Statements of Net Assets (Continued)  
 June 30, 2009 and 2008  
 (Dollars in thousands)

	<b>2009</b>	<b>2008</b>
<b>LIABILITIES AND NET ASSETS</b>		
Current liabilities:		
Current liabilities payable from unrestricted assets:		
Contracts and accounts payable	\$ 91,175	\$ 102,994
Employee benefits and insurance claims payable (Notes 6 and 10)	7,846	5,753
Salaries payable	5,121	5,117
Commercial paper notes payable (Note 5)	96,989	330,228
Current obligations under capital leases (Notes 6 and 12)	1,311	1,197
Accrued interest payable	26	491
Other liabilities (Notes 6 and 15)	1,946	804
Current liabilities payable from unrestricted assets	204,414	446,584
Current liabilities payable from restricted assets:		
Obligations under securities lending transactions	-	165,317
Bonds payable, net of deferred charges and credits of \$565 and \$878 in 2009 and 2008, respectively (Note 5)	99,355	14,158
Contracts and accounts payable	1,749	5,366
Accrued bond interest payable	6,190	877
Current liabilities payable from restricted assets	107,294	185,718
Total current liabilities	311,708	632,302
Long-term liabilities:		
Bonds payable, net of deferred charges and credits of (\$4,615) and \$5,697 in 2009 and 2008, respectively (Note 5)	930,990	198,052
Obligations under capital leases (Notes 6 and 12)	48,207	49,518
Employee benefits and insurance claims payable (Notes 6 and 10)	44,840	41,291
Liability for environmental/hazardous cleanup	12,783	-
Other liabilities (Notes 6 and 15)	56,501	114,384
Total long-term liabilities	1,093,321	403,245
Total liabilities	1,405,029	1,035,547
Net assets:		
Invested in capital assets, net of related debt	1,613,166	1,766,228
Restricted:		
Capital projects	180	174
Debt service	179,816	26,688
Special purpose	669,612	641,089
Central utility plant	39,721	-
Unrestricted	447,633	244,057
Total net assets	\$ 2,950,128	\$ 2,678,236

See accompanying notes to financial statements.

**LOS ANGELES WORLD AIRPORTS**  
(Department of Airports of the City of Los Angeles, California)  
**LOS ANGELES INTERNATIONAL AIRPORT**  
Statements of Revenues, Expenses, and Changes in Net Assets  
For the years ended June 30, 2009 and 2008  
(Dollars in thousands)

	<u>2009</u>	<u>2008</u>
Operating revenue:		
Aviation revenue:		
Landing fees	\$ 164,489	\$ 171,822
Building rentals	185,457	146,206
Other aviation revenue	59,528	61,932
Concession revenue	265,182	275,659
Airport sales and services	2,229	2,577
Miscellaneous revenue	2,366	2,030
Total operating revenue	<u>679,251</u>	<u>660,226</u>
Operating expenses:		
Salaries and benefits	298,612	291,015
Contractual services	148,627	151,155
Materials and supplies	38,738	37,870
Administrative expense	1,951	1,665
Utilities	29,018	27,674
Advertising and public relations	7,967	8,286
Net other operating expense/(revenue)	<u>(2,002)</u>	<u>67</u>
Total operating expenses before depreciation and amortization	<u>522,911</u>	<u>517,732</u>
Income from operations before depreciation and amortization	156,340	142,494
Depreciation and amortization	<u>(86,927)</u>	<u>(83,908)</u>
Operating income	<u>69,413</u>	<u>58,586</u>
Nonoperating revenue (expenses):		
Passenger facility charges (Note 13)	103,982	116,705
Interest income	53,602	49,477
Change in fair value of investments	2,723	22,207
Interest expense	(20,483)	(18,278)
Bond expense	(455)	(428)
Other nonoperating revenue, net	<u>(24,661)</u>	<u>1,390</u>
Total nonoperating revenue, net	<u>114,708</u>	<u>171,073</u>
Income before contributions and transfers	184,121	229,659
Capital grant contributions (Note 14)	12,457	34,555
TSA contributions (Note 14)	75,784	52,330
Inter-agency transfers	<u>(470)</u>	<u>(7,188)</u>
Change in net assets	271,892	309,356
Net assets, beginning of year	<u>2,678,236</u>	<u>2,368,880</u>
Net assets, end of year	<u>\$ 2,950,128</u>	<u>\$ 2,678,236</u>

See accompanying notes to financial statements.

**LOS ANGELES WORLD AIRPORTS**  
 (Department of Airports of the City of Los Angeles, California)  
**LOS ANGELES INTERNATIONAL AIRPORT**  
 Statements of Cash Flows  
 For the years ended June 30, 2009 and 2008  
 (Dollars in thousands)

	<u>2009</u>	<u>2008</u>
Cash flows from operating activities:		
Receipts from customers	\$ 581,619	\$ 676,397
Cash received in protest from customers	22,322	132
Payments for goods and services	(242,854)	(226,983)
Payments to employees	(292,966)	(275,506)
Other receipts (payments), net	(13,972)	6,633
Net cash provided by operating activities	<u>54,149</u>	<u>180,673</u>
Cash flows from noncapital financing activities:		
Inter-agency transfer out	(470)	(7,188)
Net cash used by noncapital financing activities	<u>(470)</u>	<u>(7,188)</u>
Cash flows from capital and related financing activities:		
Acquisition and construction of capital assets	(505,381)	(476,317)
Receipts from passenger facility charges	104,834	118,086
Net principal received (paid) on bonds	818,792	(12,415)
Interest paid on bonds and commercial paper	(19,328)	(18,993)
Bond and commercial paper issuance cost paid	(5,267)	(112)
Bond payment liability set aside (returned) as escheated funds	94	(19)
Principal paid on capital leases	(1,197)	(1,140)
Interest paid on capital leases	(992)	(1,754)
Cash transferred from (to) fiscal agent	(158,535)	58
Net receipts (payments) for commercial paper	(233,239)	151,483
Federal grants and TSA receipts	84,997	86,885
Net cash provided (used) by capital and related financing activities	<u>84,778</u>	<u>(154,238)</u>
Cash flows from investing activities:		
Increase in fair value of investments	2,723	22,207
Interest received	52,503	53,992
Cash collateral paid under securities lending transactions	(165,317)	(21,016)
Net cash provided (used) by investing activities	<u>(110,091)</u>	<u>55,183</u>
Net increase cash and cash equivalents	28,366	74,430
Cash and cash equivalents, beginning of year	<u>1,325,484</u>	<u>1,251,054</u>
Cash and cash equivalents, end of year	<u>\$ 1,353,850</u>	<u>\$ 1,325,484</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	\$ 560,759	\$ 432,526
Unrestricted investments held with fiscal agents	101,879	101,780
Cash and pooled investments held by the City Treasurer - restricted	691,212	791,178
	<u>\$ 1,353,850</u>	<u>\$ 1,325,484</u>

See accompanying notes to financial statements.

**LOS ANGELES WORLD AIRPORTS**  
 (Department of Airports of the City of Los Angeles, California)  
**LOS ANGELES INTERNATIONAL AIRPORT**  
 Statements of Cash Flows (Continued)  
 For the years ended June 30, 2009 and 2008  
 (Dollars in thousands)

	<b>2009</b>	<b>2008</b>
Reconciliation of operating income to net cash provided by operating activities:		
Operating income	\$ 69,413	\$ 58,586
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation and amortization	86,927	83,908
Change in provision for uncollectible accounts	(460)	(861)
Other expenses, net	(24,682)	(218)
Changes in assets and liabilities:		
Accounts receivable	2,769	4,844
Unbilled receivables	(17,541)	11,327
Due from other agencies	(5,874)	(8,083)
Prepaid expenses and inventories	(411)	(1,165)
Contracts and accounts payable	(18,555)	17,162
Employee benefits and insurance claims payable	5,642	14,609
Salaries payable	4	899
Other liabilities	(43,083)	(335)
Total adjustments	(15,264)	122,087
Net cash provided by operating activities	\$ 54,149	\$ 180,673
Noncash capital and financing activities:		
Acquisition of capital assets included in accounts payable	\$ 47,572	\$ 44,453

See accompanying notes to financial statements.

**LOS ANGELES WORLD AIRPORTS**  
(Department of Airports of the City of Los Angeles, California)  
**LOS ANGELES INTERNATIONAL AIRPORT**

Notes to Financial Statements  
June 30, 2009 and 2008

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

**(a) Organization and Reporting Entity**

The financial statements of the Los Angeles International Airport (LAX) 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.

The Los Angeles World Airports (Department of Airports of the City of Los Angeles, California) (LAWA) operates LAX. 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 LAX only and are not intended to present fairly the financial position, changes in financial position, or cash flows of LAWA or the City in conformity with GAAP.

**(b) Basis of Accounting**

LAX 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 LAX are included in the reporting entity. Bonds issued by LAX are payable solely from revenues of LAX and are not general obligations of the City. LAX 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. LAX has elected not to follow the private sector guidance issued after November 30, 1989.

**LOS ANGELES WORLD AIRPORTS**  
(Department of Airports of the City of Los Angeles, California)  
**LOS ANGELES INTERNATIONAL AIRPORT**

Notes to Financial Statements (Continued)

June 30, 2009 and 2008

**(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 LAX's outstanding bonds. In order to maximize investment return, LAX pools its available cash with that of the City, which is invested by the City Treasurer (see Note 3).

LAX'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 LAX based on the relationship of LAX's respective daily cash balances to aggregate cash and pooled investments.

**(d) Accounts Receivable and Unbilled Receivables**

LAX recognizes revenue in the period earned. Receivables aged beyond 90 days are put into the collection process and then referred after 120 days to LAX's resident City attorneys for possible write-off. An allowance for uncollectible accounts is set as a reserve by LAX 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. For fiscal year 2008, certain customer accounts with credit balances were offset to Unbilled Receivables.

**(e) Contracts Payable, Accounts Payable and Other Liabilities**

All transactions for goods and services obtained by LAX 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, an accrual is made manually by journal voucher into the general ledger to reflect the liability to the vendor. When LAX 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.

**LOS ANGELES WORLD AIRPORTS**  
(Department of Airports of the City of Los Angeles, California)  
**LOS ANGELES INTERNATIONAL AIRPORT**

Notes to Financial Statements (Continued)

June 30, 2009 and 2008

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

**(f) *Securities Lending***

The City Treasurer engages in securities lending activities. LAX'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***

LAX has funds that are held by fiscal agents and pledged to the payment or security of the 1995, 2002, 2003 and 2008 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, net 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. LAX 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 LAX. The type of landing fee method applied by LAX is compensatory. Under this 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 LAX's actual costs of operating the airfield and apron. For control purposes, the landing fees are calculated twice each fiscal year.

**(k) *Concession Revenue***

Concession revenue is generated through LAX 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 LAX 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 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 LAX in the month following the activity. The timing of concessionaire reporting determines when accruals are required for each tenant.

**LOS ANGELES WORLD AIRPORTS**  
(Department of Airports of the City of Los Angeles, California)  
**LOS ANGELES INTERNATIONAL AIRPORT**

Notes to Financial Statements (Continued)

June 30, 2009 and 2008

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

**(l) Depreciation and Amortization**

Depreciation expense includes amortization of assets under capital leases. Amortization of assets under capital leases is based on the shorter of the useful life of the asset or the lease term. 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 revenue and expenses generally result from providing services and producing and delivering goods in connection with an enterprise fund's principal ongoing operations. All revenue and expenses not meeting this definition are reported as nonoperating revenue and expenses. LAX derives operating revenue primarily from landing fees, terminal space rental, auto parking, and concessions. LAX's major operating expenses include salaries and employee benefits, fees for contractual services related to security and parking management, and other expenses such as depreciation and amortization, maintenance, insurance, and utilities.

**(o) Interest Expense**

Interest expense was \$20,483,000 for the year ended June 30, 2009 and \$18,278,000 for the year ended June 30, 2008. LAX also capitalizes interest expense (net of interest earnings) for capital projects during construction. In fiscal year 2009, \$28,419,000 interest expense, net of \$581,000 interest earnings, for capital projects was capitalized. There was no capitalized interest expense for fiscal year 2008 because all outstanding bonds then were used for refunding purposes.

**(p) Employee Benefits**

LAX 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.

**(q) Statement 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.

**LOS ANGELES WORLD AIRPORTS**  
(Department of Airports of the City of Los Angeles, California)  
**LOS ANGELES INTERNATIONAL AIRPORT**

Notes to Financial Statements (Continued)

June 30, 2009 and 2008

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

**(r) 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.

**(s) Reclassifications**

Certain reclassifications have been made to fiscal year 2008 amounts in order to conform to the fiscal year 2009 presentation.

**(t) Inventory**

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

**(u) 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.

**(v) 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.
- *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, 2009 and 2008, net assets of \$528.1 million and \$444.2 million, respectively, are restricted by enabling legislation.
- *Unrestricted Net Assets* – This category represents net assets of LAX, not restricted for any project or other purpose.

**LOS ANGELES WORLD AIRPORTS**  
(Department of Airports of the City of Los Angeles, California)  
**LOS ANGELES INTERNATIONAL AIRPORT**

Notes to Financial Statements (Continued)

June 30, 2009 and 2008

**(2) Implementation of New Accounting Standards**

**(a) Governmental Accounting Standards Board (GASB) Statement No. 49 – *Accounting and Financial Reporting for Pollution Remediation Obligations.***

Effective from July 1, 2007, LAX adopted the provisions of GASB Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*. This Statement establishes standards for accounting and financial reporting for pollution remediation obligations. This Statement establishes a framework for recognition and measurement of pollution remediation liabilities that incorporates the following interrelated features:

- Obligating events;
- Components and benchmarks; and
- Measurement, included cash flow technique.

The implementation of GASB 49 did not have a significant impact on LAX as of July 1, 2008 and 2007 or for the fiscal year ended June 30, 2008. For the year ended June 30, 2009, LAX recorded \$12.8 million of pollution remediation obligations and has reported the amount as a liability for environmental/hazardous cleanup.

**(b) 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 states and local governments. Types of assets that may be considered intangible assets include easements, water rights, timber rights, patents, trademarks, and computer software. LAX has early implemented GASB 51 beginning in fiscal year 2009. LAX purchased intangible assets in the amount of \$5.9 million in July 2008.

**LOS ANGELES WORLD AIRPORTS**  
(Department of Airports of the City of Los Angeles, California)  
**LOS ANGELES INTERNATIONAL AIRPORT**

Notes to Financial Statements (Continued)

June 30, 2009 and 2008

**(3) Cash and Investments**

**(a) Cash and Pooled Investments**

The cash balances of substantially all funds on deposit in the City Treasury are pooled and invested by the City Treasurer for the purpose of maximizing interest earnings through pooled investment activities but safety and liquidity still take precedence over return. Interest earned on pooled investments is allocated to the participating funds based on each fund's average daily deposit balance during the allocation period. Investments in the City Treasury are stated at fair value based on quoted market prices except for money market investments that have remaining maturities of one year or less at time of purchase, which are reported at amortized cost.

Pursuant to California Government Code Section 53607 and the Los Angeles City Council File No. 94-2160, the City Treasury provides an Annual Statement of Investment Policy (the Policy) to the City Council. The policy governs the City's pooled investment practices. The Policy addresses soundness of financial institutions in which the Treasurer will deposit funds and types of investment instruments permitted by California Government Code Sections 53600-53636 and 16429.1.

The Investment Advisory Committee (IAC) reviews investment performance and strategy. The IAC is composed of the City Treasurer as chairperson, the Office of the Mayor, City Controller, Chief Legislative Analyst, City Administrative Officer, Director of Office of Finance, and an external investment advisor.

The City Treasurer manages the General and Special Investment Pool. Refer to the City's basic financial statements included in its comprehensive annual financial report for complete disclosures related to the City's General and Special Investment Pools.

**LOS ANGELES WORLD AIRPORTS**  
 (Department of Airports of the City of Los Angeles, California)  
**LOS ANGELES INTERNATIONAL AIRPORT**

Notes to Financial Statements (Continued)

June 30, 2009 and 2008

**(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 LAX 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 and concentration of credit risk.

	<u>Maximum maturities</u>	<u>Maximum concentration</u>
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	32 days	15
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	5 years	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.

*Credit Risk.* The City's pooled investment policy requires that for all classes of investments, except linked banking program certificates of deposits, the issuers' minimum credit ratings shall be Standard & Poor's Corporation (S&P) A-1/A or Moody's Investor Services (Moody's) P-1/A2 and, if available, Fitch IBCA F1/A. In addition, domestic banks are limited to those with a current Fitch Ratings BankWatch of "B/C" or better and an A-1 short-term rating.

At June 30, 2009 and 2008, LAX had \$1,251,971,000 and \$1,223,704,000, respectively, invested with the City Pool, which represents approximately 21.50% and 21.42%, respectively, of the City Treasury's General Investment Pool. Refer to the City's basic financial statements for complete disclosures of the investments in the pool and related interest rate risk, credit risk, and concentration of credit risk for the City's General Investment Pool.

**LOS ANGELES WORLD AIRPORTS**  
(Department of Airports of the City of Los Angeles, California)  
**LOS ANGELES INTERNATIONAL AIRPORT**

Notes to Financial Statements (Continued)

June 30, 2009 and 2008

**(3) Cash and Investments (continued)**

**(c) *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 investments 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 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.

Due to the extreme volatility in the financial markets over the past twelve months resulting from the worst global financial crisis, and counterparty risks, the City temporarily suspended its SLP in November 2008. The City, however, continues to monitor the financial markets and will re-enter the SLP market when deemed appropriate.

LAX's share of cash collateral received and corresponding liability aggregated approximately \$0 and \$165,317,000 at June 30, 2009 and 2008, 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.

**LOS ANGELES WORLD AIRPORTS**  
 (Department of Airports of the City of Los Angeles, California)  
**LOS ANGELES INTERNATIONAL AIRPORT**

Notes to Financial Statements (Continued)

June 30, 2009 and 2008

**(3) Cash and Investments (continued)**

**(d) Investments with Fiscal Agents**

LAX also maintains investments with fiscal agents that are pledged to the payment or security of LAX's 1995, 2002, 2003 and 2008 bonds. 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.

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

<u>Description</u>	<u>2009</u>	<u>2008</u>
Money Market Funds	\$ 244,184	\$ 109,696
U.S. Treasury Securities	43,700	19,554
Total	<u>\$ 287,884</u>	<u>\$ 129,250</u>

*Concentration of Credit Risk:* The money market funds are comprised of investments in the First American Treasury Obligation Fund and Federated U.S. Treasury Cash Reserve Fund and the entire U.S. Treasury Securities are invested in U.S. Treasury Bills.

*Interest Rate Risk:* The maturity date of the U.S. Treasury Bills invested is less than one year and the weighted average maturity of the money market funds is as follows:

Federated U.S. Treasury Cash Reserve Fund – 51 days

First American Treasury Obligation Fund – 49 days

*Credit Risk:*

First American Treasury Obligation Fund – Aaa (Moody's) and AAA (Standard & Poor's)

Federated U.S. Treasury Cash Reserve Fund – Aaa (Moody's) and AAA (Standard & Poor's)

**LOS ANGELES WORLD AIRPORTS**  
(Department of Airports of the City of Los Angeles, California)  
**LOS ANGELES INTERNATIONAL AIRPORT**

Notes to Financial Statements (Continued)

June 30, 2009 and 2008

**(4) Changes in Capital Assets**

Capital asset activity for the year ended June 30, 2009 was as follows (in thousands):

	<u>Balance at June 30, 2008</u>	<u>Additions</u>	<u>Deductions</u>	<u>Balance at June 30, 2009</u>
Capital assets, not depreciated:				
Land	\$ 575,420	\$ -	\$ -	\$ 575,420
Air easements	44,346	-	-	44,346
Intangible asset - ERC*	-	5,918	-	5,918
Construction work in process	783,332	457,849	(17,859)	1,223,322
Total capital assets, not depreciated	<u>1,403,098</u>	<u>463,767</u>	<u>(17,859)</u>	<u>1,849,006</u>
Capital assets, depreciated:				
Buildings	521,839	-	-	521,839
Improvements	1,032,936	48,127	-	1,081,063
Equipment and vehicles	154,607	21,304	(3,644)	172,267
Leased property	184,423	-	-	184,423
Total capital assets, depreciated	<u>1,893,805</u>	<u>69,431</u>	<u>(3,644)</u>	<u>1,959,592</u>
Less accumulated depreciation and amortization:				
Buildings	(300,890)	(13,036)	-	(313,926)
Improvements	(528,800)	(60,714)	-	(589,514)
Equipment and vehicles	(111,646)	(8,626)	958	(119,314)
Leased property	(100,155)	(4,551)	-	(104,706)
Total accumulated depreciation and amortization	<u>(1,041,491)</u>	<u>(86,927)</u>	<u>958</u>	<u>(1,127,460)</u>
Total capital assets depreciated, net	<u>852,314</u>	<u>(17,496)</u>	<u>(2,686)</u>	<u>832,132</u>
Total capital assets, net	<u>\$ 2,255,412</u>	<u>\$ 446,271</u>	<u>\$ (20,545)</u>	<u>\$ 2,681,138</u>

\*Environmental Reduction Credits

**LOS ANGELES WORLD AIRPORTS**  
 (Department of Airports of the City of Los Angeles, California)  
**LOS ANGELES INTERNATIONAL AIRPORT**

Notes to Financial Statements (Continued)

June 30, 2009 and 2008

**(4) Changes in Capital Assets (continued)**

Capital asset activity for the year ended June 30, 2008 was as follows (in thousands):

	<b>Balance at July 1, 2007</b>	<b>Additions</b>	<b>Deductions</b>	<b>Balance at June 30, 2008</b>
Capital assets, not depreciated:				
Land	\$ 575,420	\$ -	\$ -	\$ 575,420
Air easements	44,346	-	-	44,346
Construction work in process	<u>355,555</u>	<u>435,395</u>	<u>(7,618)</u>	<u>783,332</u>
Total capital assets, not depreciated	<u>975,321</u>	<u>435,395</u>	<u>(7,618)</u>	<u>1,403,098</u>
Capital assets, depreciated:				
Buildings	521,799	40	-	521,839
Improvements	998,197	34,739	-	1,032,936
Equipment and vehicles	145,784	11,849	(3,026)	154,607
Leased property	<u>184,423</u>	<u>-</u>	<u>-</u>	<u>184,423</u>
Total capital assets, depreciated	<u>1,850,203</u>	<u>46,628</u>	<u>(3,026)</u>	<u>1,893,805</u>
Less accumulated depreciation and amortization:				
Buildings	(287,845)	(13,045)	-	(300,890)
Improvements	(470,150)	(58,650)	-	(528,800)
Equipment and vehicles	(106,212)	(7,663)	2,229	(111,646)
Leased property	<u>(95,605)</u>	<u>(4,550)</u>	<u>-</u>	<u>(100,155)</u>
Total accumulated depreciation and amortization	<u>(959,812)</u>	<u>(83,908)</u>	<u>2,229</u>	<u>(1,041,491)</u>
Total capital assets depreciated, net	<u>890,391</u>	<u>(37,280)</u>	<u>(797)</u>	<u>852,314</u>
Total capital assets, net	<u>\$ 1,865,712</u>	<u>\$ 398,115</u>	<u>\$ (8,415)</u>	<u>\$ 2,255,412</u>

**LOS ANGELES WORLD AIRPORTS**  
(Department of Airports of the City of Los Angeles, California)  
**LOS ANGELES INTERNATIONAL AIRPORT**

Notes to Financial Statements (Continued)

June 30, 2009 and 2008

**(5) Bonds and Commercial Paper Payable**

LAX issued revenue bonds in 1995, 2002, 2003 and 2008 for various airport improvement projects and to refund previously issued debt. LAX's revenues are pledged as security for the bonds. All revenues used specifically for repayment of bonds for LAX are defined in LAWA's Bond Official Statement as Net Pledged Revenues. Net Pledged Revenues means, for any given period, the Pledged Revenues for such period less, for such period, the LAX Maintenance and Operation Expense.

The 1995 Revenue Bonds were issued in the amount of \$365,855,000 to finance capital improvements and to refund previously issued debt. The bonds are limited obligations of LAWA payable from and secured by a pledge of LAX revenues.

In fiscal year 2003, LAX issued a total of \$217,175,000 of revenue bonds to fund LAX airport improvement projects and advance refund a portion of the 1995 bonds.

LAX issued three series of bonds totaling \$853,300,000 in fiscal year 2009. Total bond issuance costs were \$5,375,000 and the net discount amounted to \$9,861,000. The proceeds from the sale of these bonds were used to reimburse LAWA for previous capital expenditures, pay for future capital expenditures, repay outstanding commercial paper notes and refund the balance of the LAX 1995 D bonds. LAX's revenues are pledged as security for the bonds.

LAWA used cash from the LAX revenue fund to defease the balance of the LAX 1995 C bonds on July 15, 2008.

In September of 2008, bond proceeds were used to repay the balance of the Series A and Series B commercial paper notes leaving only the Series C notes outstanding. These Series C commercial paper proceeds 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 airline debt issued to finance terminal improvements at LAX.

As of June 30, 2009, LAX had \$81.1 million outstanding in variable rate bonds. These bonds consisted of the LAX 2002 C1 bonds with a final maturity of 2020, the LAX 2002 C2 bonds with a final maturity of 2020 and the LAX 2003 A bonds with a final maturity of 2016. Pursuant to a Reimbursement Agreement for the LAX 2002 C1 - C2 bonds and the LAX 2003 A bonds, both dated March 1 2005, LAX obtained credit enhancement and liquidity support for these variable rate bonds in the form of irrevocable transferable direct-pay letters of credit issued by BNP Paribas. The liquidity facility provided by BNP Paribas covers a par amount of up to \$81.1 million plus interest. If LAX is unable to repay principal and interest on bonds funded by BNP Paribas, it would extend a term loan to LAX that would be repaid within three years. The facility fee rate is .275% per annum and LAX is required to pay a drawing fee of \$200 for each drawing under the letters of credit. The letters of credit for the bonds expire on March 10, 2010. Accordingly, these bonds are classified as current liabilities in the statement of net assets.

**LOS ANGELES WORLD AIRPORTS**  
(Department of Airports of the City of Los Angeles, California)  
**LOS ANGELES INTERNATIONAL AIRPORT**

Notes to Financial Statements (Continued)

June 30, 2009 and 2008

**(5) Bonds and Commercial Paper Payable (continued)**

Pursuant to a Reimbursement Agreement dated April 1, 2007, LAWA obtained credit enhancement and liquidity support for LAX's \$500 million commercial paper program in the form of an irrevocable transferable direct-pay letter of credit issued by Citibank and State Street Bank and Trust Company. This liquidity facility covers an amount of up to \$500 million plus interest. The letter of credit fee rate is .12% per annum and the commitment fee rate is .10% per annum. LAX is required to pay a drawing fee of \$350 for each draw under the letter of credit. The letter of credit for the commercial paper program expires on April 1, 2012.

Outstanding revenue bonds as of June 30, 2009 mature in varying amounts through 2038. Bond and commercial paper notes activity for the year ended June 30, 2009 was as follows (in thousands):

<u>Debt issue</u>	<u>Interest rate%</u>	<u>Balance at June 30, 2008</u>	<u>Additions</u>	<u>Deductions</u>	<u>Balance at June 30, 2009</u>	<u>Due in one year</u>
Issue of 1995	5.00% to 8.38%	\$ 8,965	\$ -	\$ (8,965)	\$ -	\$ -
Issues of 2002 Series A	4.10 to 5.25	32,450	-	-	32,450	-
Issues of 2002 Series C	1.10 *	57,400	-	-	57,400	57,400
Issues of 2003 Series A	1.01*	23,700	-	-	23,700	23,700
Issues of 2003 Series B	4.00 to 5.00	83,120	-	(11,780)	71,340	12,395
Issues of 2008 Series A	3.75 to 5.50	-	602,075	-	602,075	-
Issues of 2008 Series B	3.00 to 5.00	-	7,875	(595)	7,280	1,070
Issues of 2008 Series C	3.00 to 5.25	-	243,350	(3,200)	240,150	4,225
Subtotal		<u>205,635</u>	<u>853,300</u>	<u>(24,540)</u>	<u>1,034,395</u>	<u>98,790</u>
Commercial paper Series A	1.49 *	158,400	-	(158,400)	-	-
Commercial paper Series B	1.53*	75,000	-	(75,000)	-	-
Commercial paper Series C	1.70*	96,828	161	-	96,989	96,989
Deferred charges and credits, net	N/A	6,575	-	(10,625)	(4,050)	565
Total		<u>\$ 542,438</u>	<u>\$ 853,461</u>	<u>\$ (268,565)</u>	<u>\$ 1,127,334</u>	<u>\$ 196,344</u>

\* Average variable rate.

Bonds and commercial paper notes activity for the year ended June 30, 2008 was as follows (in thousands):

<u>Debt issue</u>	<u>Interest rate%</u>	<u>Balance at July 1, 2007</u>	<u>Additions</u>	<u>Deductions</u>	<u>Balance at June 30, 2008</u>	<u>Due in one year</u>
Issue of 1995	5.00% to 8.38%	\$ 10,195	\$ -	\$ (1,230)	\$ 8,965	\$ 1,500
Issues of 2002 Series A	4.10 to 5.25	32,450	-	-	32,450	-
Issues of 2002 Series C	2.75*	57,400	-	-	57,400	-
Issues of 2003 Series A	2.59*	23,700	-	-	23,700	-
Issues of 2003 Series B	4.00 to 5.00	94,305	-	(11,185)	83,120	11,780
Subtotal		<u>218,050</u>	<u>-</u>	<u>(12,415)</u>	<u>205,635</u>	<u>13,280</u>
Commercial paper Series A	2.01*	30,000	128,400	-	158,400	158,400
Commercial paper Series B	1.41*	-	75,000	-	75,000	75,000
Commercial paper Series C	4.26*	148,745	1,199	(53,116)	96,828	96,828
Deferred charges and credits, net	N/A	7,499	-	(924)	6,575	878
Total		<u>\$ 404,294</u>	<u>\$ 204,599</u>	<u>\$ (66,455)</u>	<u>\$ 542,438</u>	<u>\$ 344,386</u>

\* Average variable rate.

**LOS ANGELES WORLD AIRPORTS**  
 (Department of Airports of the City of Los Angeles, California)  
**LOS ANGELES INTERNATIONAL AIRPORT**

Notes to Financial Statements (Continued)

June 30, 2009 and 2008

**(5) Bonds and Commercial Paper Payable (continued)**

LAX's future annual debt service requirements as of June 30, 2009, are as follows (in thousands):

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
Fiscal year ending June 30:			
2010	\$ 98,790	\$ 49,625	\$ 148,415
2011	28,585	48,718	77,303
2012	29,880	47,418	77,298
2013	31,270	46,034	77,304
2014	32,760	44,540	77,300
2015–2019	129,165	202,898	332,063
2020–2024	120,950	169,336	290,286
2025 - 2029	156,395	133,891	290,286
2030 - 2034	202,350	87,935	290,285
2035 - 2038	204,250	27,979	232,229
Total	<u>\$ 1,034,395</u>	<u>\$ 858,374</u>	<u>\$ 1,892,769</u>

**(6) Other Long-Term Liabilities**

Other long-term liabilities' activity for the year ended June 30, 2009 was as follows (in thousands):

	<u>Balance at June 30, 2008</u>	<u>Additions</u>	<u>Deductions</u>	<u>Balance at June 30, 2009</u>	<u>Due in one year</u>
Employee benefits & insurance claims payable	\$ 47,044	\$ 5,642	\$ -	\$ 52,686	\$ 7,846
Obligations under capital leases	50,715	1,311	(2,508)	49,518	1,311
Liability for environmental/ hazardous cleanup	-	12,783	-	12,783	-
Other liabilities	115,188	122,532	(179,273)	58,447	1,946
Total	<u>\$ 212,947</u>	<u>\$ 142,268</u>	<u>\$ (181,781)</u>	<u>\$ 173,434</u>	<u>\$ 11,103</u>

**LOS ANGELES WORLD AIRPORTS**  
 (Department of Airports of the City of Los Angeles, California)  
**LOS ANGELES INTERNATIONAL AIRPORT**

Notes to Financial Statements (Continued)  
 June 30, 2009 and 2008

**(6) Other Long-Term Liabilities (continued)**

Other long-term liabilities' activity for the year ended June 30, 2008 was as follows (in thousands):

	<u>Balance at July 1, 2007</u>	<u>Additions</u>	<u>De ductions</u>	<u>Balance at June 30, 2008</u>	<u>Due in one year</u>
Employee benefits & insurance claims payable	\$ 32,435	\$ 14,609	\$ -	\$ 47,044	\$ 5,753
Obligations under capital leases	51,855	-	(1,140)	50,715	1,197
Other liabilities	115,523	2,947	(3,282)	115,188	804
Total	<u>\$ 199,813</u>	<u>\$ 17,556</u>	<u>\$ (4,422)</u>	<u>\$ 212,947</u>	<u>\$ 7,754</u>

**(7) Related Party Transactions**

The City provides certain administrative, crash-fire-rescue, police services, and water and power to LAX. The payments for these services, included in operating expenses for the years ended June 30, 2009 and 2008, were \$52,369,000 and \$51,727,000, respectively. In addition, LAX collects parking taxes on behalf of the City of Los Angeles. For the years ended June 30, 2009 and 2008, parking taxes collected and remitted to the City of Los Angeles were \$6,755,000 and \$7,457,000, respectively.

**(8) Inter-Airport Funding Activity**

LAX controls the expense disbursement process for each of LAWA's other airports: Ontario, Van Nuys and Palmdale. LAX supports the payment activities for these airports by first processing their approved budgeted expenditures and then transferring this impact to the airport that ordered the goods and services in the form of an inter-airport cash transfer. The requesting airport then records the expenditure to the appropriate classification on its books of account at the time it reimburses LAX for the activity. Whenever a specific airport is unable to make a cash transfer to LAX, due to a lack of funds, the amount is then recorded as a Due To Other Agency transaction. Conversely, LAX will record the same amount owed to it as a Due from Other Agency transaction. As a result of this process, Palmdale Airport has accumulated a total of \$45,957,000 and \$40,083,000 in Due To Other Agency balance owed to LAX at June 30, 2009 and 2008, respectively.

Upon combining the statement of net assets of all four airports that comprise LAWA, the Due From Other Agency asset balance on LAX's statement of net assets fully offset against the Due To Other Agency liability on the respective statement of net assets of Palmdale Airport. The amount of elimination for this balance at June 30, 2009 is \$45,957,000. With Palmdale Airport being part of the LAWA airport system, there is no near-term expectation for repayment of the Due To Other Agency balances to LAX.

**(9) Retirement System**

**(a) Retirement Plan Description**

All full-time employees of LAX 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. LAX makes contributions to LACERS for its pro rata share of retirement costs attributable to its employees.

**LOS ANGELES WORLD AIRPORTS**  
 (Department of Airports of the City of Los Angeles, California)  
**LOS ANGELES INTERNATIONAL AIRPORT**

Notes to Financial Statements (Continued)  
 June 30, 2009 and 2008

**(9) Retirement System (continued)**

**(a) Retirement Plan Description (continued)**

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.

**(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. LAX's pro rata share of the combined actuarially required contributions (ARC) for pension and postemployment healthcare benefits and actual contributions made to LACERS, which were based on LAX's salaries relative to total salaries for LAWA as a whole, were approximately \$37,900,000 (100% of ARC), \$39,700,000 (100% of ARC) and \$34,600,000 (100% of ARC) for the years ended June 30, 2009, 2008, and 2007, respectively. The ARCs for the years ended June 30, 2009 and 2008 were based on actuarial valuations performed as of June 30, 2007 and 2006, respectively.

The City's annual pension cost, the percentage of annual pension cost contributed to the plans, and the net pension obligation for fiscal year 2008-09 and the two preceding years for each of the plans are as follows (dollars in thousands):

	Year Ended	Annual Pension Cost (APC)	Percentage of APC Contributed	Net Pension Obligation
LACERS	06/30/07	\$ 276,191	86%	\$ (81,723)
	06/30/08	286,367	100%	(79,972)
	06/30/09	272,331	100%	(77,749)

The City allocated a pro rata share of its net pension obligation to LAWA and the amounts recorded at June 30, 2009 and 2008 were \$10,118,000 and \$9,459,000, respectively. The amounts allocated to LAX equaled the amounts allocated to LAWA.

**(c) Funded Status of LACERS**

For complete information related to the funded status of LACERS and contribution information, refer to LACERS' basic financial statements. The LACERS' basic financial statements can be obtained from LACERS, 360 East Second Street, 2<sup>nd</sup> Floor, Los Angeles, CA 90012.

**LOS ANGELES WORLD AIRPORTS**  
 (Department of Airports of the City of Los Angeles, California)  
**LOS ANGELES INTERNATIONAL AIRPORT**

Notes to Financial Statements (Continued)

June 30, 2009 and 2008

**(9) Retirement System (continued)**

**(d) Other Postemployment Benefits (OPEB)**

LAX, 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.

The City's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB asset (obligation) for fiscal year 2008-09 and the two preceding years for the plan are as follows (dollars in thousands):

	<u>Year Ended</u>	<u>Annual OPEB Cost</u>	<u>Percentage of OPEB Cost Contributed</u>	<u>Net OPEB Asset (Obligation)</u>
LACERS	06/30/07	\$ 115,233	100%	\$ -
	06/30/08	108,848	100%	-
	06/30/09	95,122	100%	-

For complete information related to the funded status of LACERS and contribution information, refer to LACERS' basic financial statements. The LACERS' basic financial statements can be obtained from LACERS, 360 East Second Street, 2<sup>nd</sup> Floor, Los Angeles, CA 90012.

**LOS ANGELES WORLD AIRPORTS**  
 (Department of Airports of the City of Los Angeles, California)  
**LOS ANGELES INTERNATIONAL AIRPORT**

Notes to Financial Statements (Continued)

June 30, 2009 and 2008

**(10) Self-Insurance**

LAX 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. LAX's accrued total liability for workers' compensation has been based on the results of an actuarial study and has been allocated to LAX based on a ratio of LAX salaries to total LAWA salaries. 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, 2007	\$	30,280
Provisions for claims		5,918
Claim payments		(4,591)
Liability at June 30, 2008		31,607
Provisions for claims		3,862
Claim payments		-
Liability at June 30, 2009		35,469
Current portion		(4,217)
Long-term liability at June 30, 2009, net of current portion	\$	31,252

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 insurance policies up to the policy limits of \$1.0 billion for 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 \$100,000 per occurrence and annual aggregate on Property insurance. The deductible 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 2009, 2008, and 2007, no claims were in

**LOS ANGELES WORLD AIRPORTS**  
(Department of Airports of the City of Los Angeles, California)  
**LOS ANGELES INTERNATIONAL AIRPORT**

Notes to Financial Statements (Continued)

June 30, 2009 and 2008

**(10) Self-Insurance (continued)**

excess of LAWA's insurance coverage. Other claims liabilities are reported in Other Long-Term Liabilities (see Note 6). 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. 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.

**(11) Commitments and Contingencies**

As of June 30, 2009, a number of claims and lawsuits are pending against LAX that arose in the normal course of operations. LAX 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 LAX's operations.

**(a) Environmental Issues**

As discussed in Note 2a, LAWA implemented GASB Statement No. 49 for the year ended June 30, 2009. This Statement establishes accounting and reporting guidelines for the recognition and measurement of pollution remediation liabilities. Through the normal course of operations, LAWA and its facilities are subject to potential environmental contamination and other environmental concerns.

LAWA bears full financial responsibility for the cleanup of environmental contamination on property owned by it. However, if the contamination originated based on contractual arrangements, this means that the primary responsibility for any such cleanup would be borne by the tenants, even if they declare bankruptcy. As property owner, LAWA assumes the ultimate responsibility for cleanup of such contamination in the event that the tenant is unable to make restitution. 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 is an on-going process.

As part of this evaluation, LAWA conducts environmental monitoring to identify potential pollution sites that may require further investigation and remediation. Once LAWA makes a determination of potential remedial action, it commences site assessment, testing and/or clean-up activities. During the year ended June 30, 2009, LAWA identified two sites and began voluntary remediation (asbestos removal in both cases). Further, the Regional Water Quality Board (i.e., regulatory agency) notified LAWA of the need for remediation on groundwater contamination. LAWA is currently performing remediation based on this regulatory order. LAWA accrues pollution remediation liabilities when costs are incurred or amounts can reasonably be estimated. Under LAWA policy, estimated liabilities are determined by the Environmental Services Division based on the expected outlays to settle pollution remediation liabilities. Amounts accrued for LAX at June 30, 2009 totaled \$12.8 million.

**LOS ANGELES WORLD AIRPORTS**  
(Department of Airports of the City of Los Angeles, California)  
**LOS ANGELES INTERNATIONAL AIRPORT**

Notes to Financial Statements (Continued)

June 30, 2009 and 2008

**(11) Commitments and Contingencies (continued)**

**(a) *Environmental Issues (continued)***

At this time, LAWA does not expect any recoveries reducing this particular obligation. For subsequent periods, LAWA will adjust estimated liabilities as new information becomes available, as LAWA's environmental remediation evaluation process is on-going.

**(b) *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 2009, LAWA's passenger volume was 16.6%, or 12.3 million, below its pre-September 11<sup>th</sup> 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 LAX 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 LAX will depend upon several factors directly and indirectly related to the September 11 Events, including, among others, the 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.

LAX 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 LAX, (iii) the future financial condition of the airlines using LAX, or (iv) the likelihood of future incidents of terrorism or other air transportation disruptions.

**(c) *Other***

Commitments for construction, the purchase of real property, equipment and materials and supplies amounted to \$113,800,000 and \$87,500,000 as of June 30, 2009 and 2008, respectively. The change in commitments is due to the following projects: \$36,000,000 for inspection testing, and surveying for the center taxiway, in-line baggage screening, runway projects, TBIT interior improvement projects, and midfield satellite concourse; and, \$30,500,000 for land acquisition.

**LOS ANGELES WORLD AIRPORTS**  
 (Department of Airports of the City of Los Angeles, California)  
**LOS ANGELES INTERNATIONAL AIRPORT**

Notes to Financial Statements (Continued)

June 30, 2009 and 2008

**(12) 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 a remaining term of 27 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 for both June 30, 2009 and 2008. Accumulated depreciation with respect to such property for the respective years was \$104,706,000 million and \$100,155,000 million, respectively.

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

Fiscal year ending June 30,	
2010	\$ 3,146
2011	3,268
2012	3,328
2013	3,439
2014	3,545
2015 – 2019	19,535
2020 – 2024	24,092
2025 – 2026	9,111
Total minimum lease payments	<u>\$ 69,464</u>
Less interest portion	<u>(19,946)</u>
Present value of minimum lease payments	<u><u>\$ 49,518</u></u>

LAX 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 LAX by such airlines for terminal leases and landing fees.

**LOS ANGELES WORLD AIRPORTS**  
(Department of Airports of the City of Los Angeles, California)  
**LOS ANGELES INTERNATIONAL AIRPORT**

Notes to Financial Statements (Continued)

June 30, 2009 and 2008

**(13) 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 PFCs. PFCs 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 PFCs at LAX in the amount of \$360,000,000 for 5 years for specifically approved airport improvement projects. Effective July 1, 1993, LAWA began collecting PFCs 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, the FAA approved LAWA's application to impose \$3 per passenger PFCs at LAX, 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.
- On October 2, 1998, the FAA approved LAWA's application to amend PFCs 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, PFCs are categorized as nonoperating revenues. All funds collected must be maintained in an interest-bearing account with the City Treasurer prior to disbursement.

**LOS ANGELES WORLD AIRPORTS**  
 (Department of Airports of the City of Los Angeles, California)  
**LOS ANGELES INTERNATIONAL AIRPORT**

Notes to Financial Statements (Continued)

June 30, 2009 and 2008

**(13) Passenger Facility Charges (continued)**

Cumulative PFC collections and the related interest earned as reported to the FAA were as follows (in thousands):

	<b>2009</b>	<b>2008</b>
Amount collected	\$ 1,206,532	\$ 1,101,698
Interest received	129,147	107,918
Cumulative PFC collections	\$ 1,335,679	\$ 1,209,616

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.

**(14) Capital Grant Contributions**

Contributed capital related to governmental grants and other aid increased by \$1.0 million to \$88.2 million during the year ended June 30, 2009. Capital grant funds were used for projects under the Airport Improvement Program and Transportation Security Administration security-related capital projects. During fiscal year 2008, capital grant contributions increased from fiscal year 2007 by \$13.0 million to \$87.0 million.

**(15) Terminal Rents**

LAX has lease arrangements at its passenger terminal facilities with American Airlines, Continental Airlines, Delta Air Lines, LAX TWO Corporation, and United Airlines (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 LAX 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.

The Long-term Airlines have objected to LAX’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. In February of 2008 and January of 2009, LAWA entered into interim settlement agreements and amendments to the interim settlement agreements with each of the Long-term Airlines resolving all disputed charges between January 1, 2006 and April 30, 2009. The agreements resulted in the issuance of credits for a portion of the amounts assessed to date. As part of these agreements, the Long-Term Airlines and LAWA agreed to work together to reach an agreement on future charges

**LOS ANGELES WORLD AIRPORTS**  
(Department of Airports of the City of Los Angeles, California)  
**LOS ANGELES INTERNATIONAL AIRPORT**

Notes to Financial Statements (Continued)

June 30, 2009 and 2008

**(15) Terminal Rents (continued)**

by April 30, 2009. Subsequently, Continental and American entered into additional amendments to the interim settlement agreements which resulted in an resolution of M&O Rents between May 1, 2009 and December 31, 2009 and an agreement to work together to reach an agreement on future M&O Rents by December 31, 2009. On February 18, 2009, LAWA reached an agreement with United Airlines to terminate their long term lease in terminal 6 and part of terminal 7 and now has the right to recover full M&O expenses attributable to that space. Negotiations have continued with all other parties.

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 a portion of the amounts assessed under the tariff 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 Supplemental Order on July 13, 2007, the carriers that were party to the DOT complaint filed a Petition to Review at the United States Court of Appeals regarding the DOT ruling.

On July 24, 2008, the BOAC approved a partial settlement agreement with the carriers operating in the Tom Bradley International Terminal resolving all disputed charges between January 1, 2006 and December 31, 2009. The agreement resulted in the issuance of credits for portions of the amounts that had been charged to date and created a framework for future negotiations on rates beyond December 31, 2009. On October 20, 2008, the BOAC authorized the executive director to enter into binding letter agreements with all current and new entrant carriers subject to the LAX Passenger Terminal Tariff offering interim rates and charges similar to the partial settlement agreement rates and charges framework pending the outcome of the DOT litigation. The agreements resulted in credits for portions of the amounts that had been charged to date.

Pending the resolution of these objections, LAX has classified the disputed cash portion of the M&O Rent and interest earned as “Cash under Protest” of \$33,548,000 as of June 30, 2009 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.

**LOS ANGELES WORLD AIRPORTS**  
(Department of Airports of the City of Los Angeles, California)  
**LOS ANGELES INTERNATIONAL AIRPORT**

Notes to Financial Statements (Continued)

June 30, 2009 and 2008

**(16) Subsequent Events**

**(a) *Bond Issuance***

In July 2009, LAX issued \$85,000,000 in commercial paper notes to partially finance the acquisition of the Park One Property. A total of \$126,563,000, which included the purchase price of \$125,000,000 plus closing costs, was spent on acquiring the 20-acre property.

LAX issued four series of bonds totaling \$689,325,000 in December 2009. The proceeds from the sale of these bonds will be used to reimburse LAX for previous capital expenditure, pay for future capital expenditures, repay the outstanding Series B (tax-exempt non-AMT) commercial paper notes, refund the LAX 2002 C1 bonds and purchase a portion of the LAX 2008 A bonds.

The LAX 2002 C1 bonds were redeemed on January 4, 2010. LAX 2002 C2 and LAX 2003A bonds were redeemed on March 1, 2010. The letters of credit terminated upon redemption of the variable rate bonds.

**(b) *Terminal Rents***

On August 7, 2009, the Court of Appeals issued its opinion on the U.S. DOT Decision regarding the complaint filed by the carriers operating in terminals 1 and 3 at LAX. The Court's opinion generally affirmed some of LAWA's positions, but in any case, remanded the majority of the items under dispute back to the U.S. DOT for further review. LAWA is unable to predict whether any further review of the Court of Appeals' ruling will be sought in the Supreme Court or how the U.S. DOT will rule on the issues remanded.

On November 6, 2009, City Council approved an amended and restated lease between United Airlines and LAWA covering terminal space leased by United in terminals 7 and 8. The amended and restated lease resolved all previous disputes between the parties over terminal rates and charges at LAX in terminals 7 and 8.

**COMPLIANCE SECTION**



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SACRAMENTO

OAKLAND

WALNUT CREEK

NEWPORT BEACH

SAN DIEGO

**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**

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

We have audited the accompanying basic financial statements of the Los Angeles International Airport (LAX), a departmental component of 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, 2009, and have issued our report thereon dated March 12, 2010, which included an explanatory paragraph describing LAX's implementation of Governmental Accounting Standards Board (GASB) Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*, and GASB Statement No. 51, *Accounting and Financial Reporting for Intangible Assets* during the current fiscal year. 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 LAX's internal control over financial reporting in order to determine 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 LAX's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of LAX'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 the entity'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 the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity'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 the entity's internal control.

Our consideration of the 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 LAX'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*.

We noted certain matters that we reported to management of LAX in a separate letter dated December 30, 2009.

This report is intended solely for the information and use of LAWA's management, Board of Airport Commissioners, others within the entity, 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 Fini & O'Connell LLP*

Certified Public Accountants

Los Angeles, California

March 12, 2010