AIRPORT COMMISSION OF THE CITY AND COUNTY OF SAN FRANCISCO

AUDITED FINANCIAL STATEMENTS

October 27, 2017

The Airport Commission (the "Commission") of the City and County of San Francisco hereby provides its Financial Statements with Schedule of Passenger Facility Charge Revenues and Expenditures June 30, 2017 and 2016 (With Independent Auditors' Report Thereon) (the "Financial Statements").

By providing the Financial Statements, the Commission does not imply or represent: (a) that the information provided is material to investors' decisions regarding the Commission's Airport Revenue Bonds and Airport Revenue Refunding Bonds (the "Bonds"), (b) that no changes, circumstances or events have occurred since the end of the fiscal year ended June 30, 2017 other than what is contained in the Financial Statements, or (c) that there is no other information in existence that may have a bearing on the Commission's financial condition, the security for the Bonds, or an investor's decision to buy, sell or hold the Bonds. The information contained in the Financial Statements has been obtained from officers, employees and records of the Commission and other sources that are believed to be reliable, but such information is not guaranteed as to its accuracy or completeness.

No statement in the Financial Statements should be construed as a prediction or representation about the future operating results or financial performance of the Commission.

AIRPORT COMMISSION OF THE CITY
AND COUNTY OF SAN FRANCISCO

Enclosure: Financial Statements

AIRPORT COMMISSION
CITY AND COUNTY OF SAN FRANCISCO
SAN FRANCISCO INTERNATIONAL AIRPORT

Financial Statements with
Schedule of Passenger Facility Charge Revenues and Expenditures

June 30, 2017 and 2016

(With Independent Auditors’ Report Thereon)

AIRPORT COMMISSION
CITY AND COUNTY OF SAN FRANCISCO
SAN FRANCISCO INTERNATIONAL AIRPORT

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KPMG LLP
Suite 1400
55 Second Street
San Francisco, CA 94105

Independent Auditors' Report

The Honorable Mayor and Board of Supervisors
City and County of San Francisco:

We have audited the accompanying financial statements of the Airport Commission, City and County of San Francisco, San Francisco International Airport (the Airport), an enterprise fund of the City and County of San Francisco, California (the City), as of and for the years ended June 30, 2017 and 2016, and the related notes to the financial statements, as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Airport Commission, City and County of San Francisco, San Francisco International Airport, as of June 30, 2017 and 2016, and the changes in its financial position and its cash flows for the years then ended in accordance with U.S. generally accepted accounting principles.

Emphasis of Matter

As discussed in note 1, the financial statements are intended to present the financial position and the changes in financial position and cash flows of only that portion of the City that is attributable to the transactions of the

Airport. They do not purport to, and do not, present fairly the financial position of the City, as of June 30, 2017 and 2016, the changes in its financial position, or, its cash flows for the years then ended in accordance with U.S. generally accepted accounting principles. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

U.S. generally accepted accounting principles require that the Management's Discussion and Analysis on pages 3–32 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Supplementary and Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Airport's basic financial statements. The accompanying Schedule of Passenger Facility Charge Revenues and Expenditures as specified in the Passenger Facility Charge Audit Guide for Public Agencies, issued by the Federal Aviation Administration are presented for purposes of additional analysis and are not a required part of the basic financial statements.

The Schedule of Passenger Facility Charge Revenues and Expenditures is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the Schedule of Passenger Facility Charge Revenues and Expenditures is fairly stated, in all material respects, in relation to the basic financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated October 20, 2017 on our consideration of the Airport's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely 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 effectiveness of the Airport's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Airport's internal control over financial reporting and compliance.

KPMG LLP

San Francisco, California
October 20, 2017

The management of the Airport Commission, City and County of San Francisco, San Francisco International Airport (the Airport or SFO), an enterprise fund of City and County of San Francisco (the City), presents the following narrative overview and analysis of the financial activities of the Airport for the fiscal years ended June 30, 2017 and 2016.

The Airport's financial statements comprise the following components: (1) Financial Statements and (2) Notes to Financial Statements. The Airport's financial statements include:

Statements of Net Position present information on the Airport's assets, deferred outflows of resources, liabilities, and deferred inflows of resources as of the year end, with the difference between the amounts as net position. Increases or decreases in net position may serve as a useful indicator of whether the financial position of the Airport is improving or weakening.

While the statements of net position provide information about the nature and amount of resources and obligations at the year end, the *Statements of Revenues, Expenses, and Changes in Net Position* present the results of the Airport's operations over the course of the fiscal year and information as to how the net position changed during the fiscal year. These statements can be used as an indicator of the extent to which the Airport has successfully recovered its costs through user fees and other charges. All changes in net position are reported during the period in which the underlying event giving rise to the change occurs, regardless of the timing of the related cash flows.

The *Statements of Cash Flows* present changes in cash and cash equivalents resulting from operating, noncapital financing, capital financing, and investing activities. These statements summarize the annual flow of cash receipts and cash payments, without consideration of the timing of the event giving rise to the obligation or revenue and exclude noncash accounting measures of depreciation or amortization of assets.

The *Notes to Financial Statements* provide information that is not displayed on the face of the financial statements but is essential to a full understanding of the financial statements.

Highlights of Airline Operations at the Airport

Fiscal year 2017 passenger traffic at SFO concluded with 26.9 million enplanements, an increase of 4.9% compared to the prior fiscal year, establishing a new peak for the Airport. Domestic growth was from increased service, mainly by a combination of Low Cost Carriers (LCCs) and legacy carrier United Airlines (United). The international sector also experienced service additions. These included new services commenced by Finnair, Thomas Cook, Virgin Atlantic, Volaris, United and WOW Air, and aircraft size or frequency increases by Air Canada, Air Berlin, KLM, Swiss International, Korean Air, and United. Total cargo and U.S. mail tonnage increased by 18.6% due to increases in both domestic and international shipments.

The 4.9% fiscal year-over-year enplanement increase at SFO compares to increases of 8.3%[1] at Oakland International Airport and 12.8%[2] at Mineta San Jose International Airport, resulting in relatively stable Bay Area passenger market share of 69.1% for SFO, compared to 70.2% in fiscal year 2016.

Passenger and Other Traffic Activity

The number of flight operations (takeoffs and landings) increased by 2.1% fiscal year-over-year. Aircraft revenue landed weight, which affects revenue generated by landing fees, increased by 7.4% above prior fiscal year levels. Total Airport passengers, which comprise enplaned, deplaned and in-transit passengers (defined as passengers who fly into and out of SFO on the same aircraft) were 54.0 million, establishing a new peak for the Airport. Overall enplaned passengers totaled 26.9 million, a 4.9% increase, with 20.5 million domestic and 6.4 million international enplaned passengers, increases of 3.4% and 10.1%, respectively. Cargo and U.S. mail tonnage increased by 18.6%, reflecting a freight increase of 21.8%, and mail increase of 0.7%.

The following table[3] presents a comparative summary of passenger and other traffic at the Airport for the fiscal years ended June 30, 2017, 2016, and 2015:

	FY 2017	FY 2016	FY 2015*	Percentage change FY 2017	Percentage change FY 2016
Flight operations	449,035	439,918	428,171	2.1 %	2.7 %
Landed weight (in 000 lbs.)	37,596,628	35,012,485	32,610,052	7.4	7.4
Total Airport passengers	53,985,826	51,421,348	48,243,910	5.0	6.6
Enplaned passengers	26,871,549	25,621,510	24,023,599	4.9	6.7
Domestic enplaned passengers	20,513,891	19,844,991	18,749,797	3.4	5.8
International enplaned passengers	6,357,658	5,776,519	5,273,802	10.1	9.5
Cargo and U.S. mail tonnage (in metric tons)	535,581	451,501	441,797	18.6	2.2

* Numbers updated to include revised data received subsequent to the 2015 fiscal year end.

Fiscal Year 2017

Passenger Traffic

Compared to fiscal year 2016, passenger enplanements in fiscal year 2017 increased by 4.9% from 25.6 million to 26.9 million passengers. Domestic passenger enplanements increased 3.4%, while international enplanements increased 10.1%. The enplanement increase totaled 1,250,039 passengers, 668,900 of which were domestic and 581,139 were international. The domestic sector grew mostly from service additions by LCCs JetBlue, Frontier and Virgin America, and by legacy carrier United. The international sector had a number of new and added services. Asia had the largest increase in international enplanements with 225,961, followed

[1] Source: Oakland International Airport Traffic Report.

[2] Source: Mineta San Jose International Airport Traffic Report.

[3] Sources: Analysis of Airline Traffic, Fiscal Years 2015, 2016 and 2017.

by Latin America with 153,713, and Europe with 113,378. Growth to Asia was from increased services, including service additions and upgauging and frequency increases by Air China, China Eastern, China Southern, China Airlines, EVA Air, Korean Airlines, and United. New services were also started to Asia by China Eastern to Qingdao, China, and United to Hangzhou, China and nonstop to Singapore. Latin American growth was primarily due to additional service by Copa Airlines and Volaris. Europe growth came from new services by WOW Air to Keflavik, return of Air Berlin service to Dusseldorf as well as new nonstop service to Berlin, new seasonal service to Manchester, UK by Virgin Atlantic and Thomas Cook, as well as frequency increases by KLM to Amsterdam. Canada enplanements increased by 16,780 mainly due to Air Canada service and capacity increase. Australia/Oceania enplanements grew by 82,282 mainly from increased frequency by Qantas Airways, and seasonal services by Fiji Airways to Nadi, and United to Auckland, New Zealand. The Middle East was the only region to experience decline in enplanements by 10,975, mainly due to Etihad Airways reductions to Abu Dhabi that will be fully discontinued in October.

The fiscal year quarterly results outpaced the previous year with strong performance in both domestic and international sectors, with overall enplanement growth rates of 7.1%, 4.9%, 2.5%, and 4.6% in each of the four consecutive quarters. The increases resulted from added frequencies and operations of larger aircraft, and the addition of new services. Airline seat capacity increased by 6.7% during fiscal year 2017, with a domestic increase of 4.9% and an international increase of 12.8%. The overall load factor decreased by 1.4 percentage points to 82.1%. Domestic load factor decreased by 1.2 percentage points to 82.6% and international decreased by 2.0 percentage points to 80.6%.

Flight Operations

During fiscal year 2017, the number of aircraft operations (takeoffs and landings) increased by 9,117 flights (2.1%). Scheduled passenger aircraft arrivals and departures increased by 10,769 flights (2.5%). Civil and military traffic decreased by 1,652 flights (10.3%).

Total scheduled airline passenger and cargo landings increased by 2.6% with an increase in revenue landed weight of 7.4%. Domestic passenger landings increased by 1.2%, while domestic landed weight increased by 5.4%. International passenger landings increased by 11.5%, while international landed weight increased by 12.2%. Average passenger aircraft size increased from approximately 153 to 157 seats per flight. Domestic scheduled seats per flight increased from 138 to 141 while international scheduled seats per flight increased from 245 to 247 in fiscal year 2017. The overall balance between mainline passenger aircraft (wide body and narrow body) and commuters (regional jets and turbo props) continued to shift towards mainline, which increased in share by 1.8 percentage points to 79.5% for domestic and international operations combined. Mainline landings increased by 7,795, and commuter landings decreased by 2,397. Cargo only aircraft landings decreased by 4.2%, while cargo-only landed weight increased by 2.1%.

Cargo Tonnage

Fiscal year 2017 cargo and U.S. mail tonnage increased by 84,080 metric tons (18.6%). Mail increased by 463 metric tons (0.7%), as growth in domestic mail was offset by a decrease in international mail, and cargo volume excluding mail increased by 83,617 metric tons (21.8%), due to increases in both domestic and international shipments. Cargo-only carriers' tonnage share decreased by 3.0 percentage points to 21.1%. Tonnage on cargo-only carriers increased by 3.8%, while those on passenger carriers increased by 23.4%.

Fiscal Year 2016

Passenger Traffic

Compared to fiscal year 2015, passenger enplanements in fiscal year 2016 increased by 6.7% from 24.0 million to 25.6 million passengers. Domestic passenger enplanements increased 5.8%, while international enplanements increased 9.5%. The enplanement increase totaled 1,597,911 passengers, 1,095,194 of which were domestic and 502,717 were international. The domestic sector grew mostly from service additions by LCCs JetBlue, Frontier and Virgin America, and by legacy carrier United. The international sector had a number of new and added services. Europe had the largest increase in international enplanements with 163,745, followed by Asia with 150,396, and Latin America with 81,093. Growth to Europe was from a number of new and increased services, including service additions and upgauging by British Airways, Air France and Virgin Atlantic. Asia growth was also from a number of new services such as Air India to New Delhi and United to Xi'an, China, as well as frequency increases by Cathay Pacific and China Southern. Latin America enplanements increased mainly due to new service by Copa Airlines to Panama City in September 2015. The Middle East which is now served nonstop by 3 carriers, increased in enplanements by 32,186 passengers due to Etihad's increase in frequency to Abu Dhabi and United's new service to Tel Aviv that started in March 2016. Australia/Oceania enplanements increased by 34,226 mainly from the return of Qantas Airways with service to Sydney in December 2015, and the start of seasonal service to Nadi by Fiji Airways in June 2016.

The fiscal year quarterly results outpaced the previous year with strong performance in both domestic and international sectors, with growth rates of 6.5%, 8.9%, 5.6%, and 5.6% in each of the four consecutive quarters. The increases resulted from added frequencies and operations of larger aircraft, and the addition of new services. Airline seat capacity increased by 8.0%, with a domestic increase of 7.0% and an international increase of 11.6%. The overall load factor decreased by 1.0 percentage point to 83.5%. Domestic load factor decreased by 0.9 percentage point to 83.8% and international decreased by 1.5 percentage points to 82.6%.

Flight Operations

During fiscal year 2016, the number of aircraft operations (takeoffs and landings) increased by 11,747 flights (2.7%). Scheduled passenger aircraft arrivals and departures increased by 11,274 flights (2.7%). Civil and military traffic increased by 473 flights (3.0%).

Total scheduled airline passenger and cargo landings increased by 1.9% with an increase in revenue landed weight of 7.4%. Domestic passenger landings increased by 1.4%, while domestic landed weight increased by 5.8%. International passenger landings increased by 6.3%, while international landed weight increased by 11.6%. Average passenger aircraft size increased from approximately 145 to 153 seats per flight. Domestic scheduled seats per flight increased from 131 to 138 while international scheduled seats per flight increased from 233 to 245 in fiscal year 2016. The overall balance between mainline passenger aircraft (wide body and narrow body) and commuters (regional jets and turbo props) continued to shift towards mainline, which increased in share by 3.7 percentage points to 77.7% for domestic and international operations combined. Mainline landings increased by 10,348, and commuter landings decreased by 6,374. Cargo only aircraft landings decreased by 9.4%, while cargo-only landed weight increased by 1.3%.

Cargo Tonnage

Fiscal year 2016 cargo and U.S. mail tonnage increased by 9,704 metric tons (2.2%). Mail increased by 9,749 metric tons (16.7%), and cargo volume excluding mail remained flat at 383,305 metric tons (0.0%), as growth in domestic shipments was offset by a decrease in international shipments. The decrease is from a relatively high base from last year, where shipment volume was high due to labor issues at west coast ports. Cargo-only carriers' tonnage share increased by 3.9 percentage points to 24.2%. Tonnage on cargo-only carriers increased by 22.1%, while those on passenger carriers decreased by 2.9%.

Financial Highlights, Fiscal Year 2017

- Assets and deferred outflows of resources exceeded liabilities and deferred inflows of resources at the close of the fiscal year by $50.2 million.
- Total revenue bonds payable by the Airport increased by $656.0 million.
- Operating revenues were $926.8 million.
- Operating expenses were $808.9 million.
- Nonoperating expenses, net of revenues from nonoperating sources (including revenues of $104.0 million from Passenger Facility Charges) were $201.0 million.
- Capital contributions from the Federal Aviation Administration's (FAA) Airport Improvement Program (AIP) and Air Traffic Control Tower program, and Transportation Security Administration's (TSA) Airport Checked Baggage Screening System were $11.2 million.
- Transfers to the City and County of San Francisco as annual service payment were $45.0 million.
- Net position decreased by $116.9 million due to a significant increase in net pension liability. This increase primarily resulted from updated assumptions about citywide supplemental cost of living adjustments (COLA) for certain retirees. See note 10a.

Financial Highlights, Fiscal Year 2016

- Assets and deferred outflows of resources exceeded liabilities and deferred inflows of resources at the close of the fiscal year by $167.1 million.
- Total revenue bonds payable by the Airport decreased by $235.2 million.
- Operating revenues were $867.0 million.
- Operating expenses were $640.5 million.
- Nonoperating expenses, net of revenues from nonoperating sources (including revenues of $99.1 million from Passenger Facility Charges) were $144.5 million.
- Capital contributions from the Federal Aviation Administration's (FAA) Air Traffic Control Tower, and Transportation Security Administration's (TSA) Airport Checked Baggage Screening System were $10.4 million.
- Transfers to the City and County of San Francisco as annual service payment were $42.5 million.

- Net position increased by $49.9 million due to higher operating income resulting from growth in domestic and international passenger traffic.

Overview of the Airport's Financial Statements

Net Position Summary

A condensed summary of the Airport's net position for the fiscal years 2017, 2016, and 2015 is shown below (in thousands):

SAN FRANCISCO INTERNATIONAL AIRPORT'S NET POSITION

	FY 2017	FY 2016	FY 2015 (as restated)	Percentage increase (decrease) FY 2017	Percentage increase (decrease) FY 2016
Assets:					
Unrestricted current assets	$ 440,930	467,577	450,598	(5.7)%	3.8 %
Restricted current assets	437,934	282,371	245,719	55.1	14.9
Restricted noncurrent assets	726,310	640,970	643,686	13.3	(0.4)
Capital assets, net	4,282,629	4,045,636	3,936,426	5.9	2.8
Total assets	5,887,803	5,436,554	5,276,429	8.3	3.0
Deferred outflows of resources:					
Unamortized loss on refunding of debt	76,789	68,100	78,388	12.8	(13.1)
Deferred outflows on derivative instruments	54,870	83,614	65,408	(34.4)	27.8
Deferred outflows related to pensions	145,743	43,982	37,517	231.4	17.2
Total deferred outflows of resources	277,402	195,696	181,313	41.8	7.9
Liabilities:					
Current liabilities	284,221	309,888	285,929	(8.3)	8.4
Current liabilities payable from restricted assets	356,535	494,128	154,611	(27.8)	219.6
Noncurrent liabilities	5,033,314	4,372,604	4,608,523	15.1	(5.1)
Net pension liability	359,599	144,271	111,932	149.3	28.9
Derivative instruments	65,965	96,132	79,321	(31.4)	21.2
Total liabilities	6,099,634	5,417,023	5,240,316	12.6	3.4
Deferred inflows of resources:					
Deferred inflows related to pensions	15,402	48,154	100,290	(68.0)	(52.0)
Total deferred inflows of resources	15,402	48,154	100,290	(68.0)	(52.0)
Net position:					
Net investment in capital assets	(284,761)	(117,377)	(103,109)	142.6	13.8
Restricted for debt service	109,554	35,462	37,427	208.9	(5.3)
Restricted for capital projects	296,188	212,931	165,224	39.1	28.9
Unrestricted	(70,812)	36,057	17,594	(296.4)	104.9
Total net position	$ 50,169	167,073	117,136	(70.0)%	42.6 %

The Airport adopted the provisions of GASB Statement No. 72 – *Fair Value Measurement and Application* (GASB 72) in fiscal year 2016, which changes how fair value is measured and provides guidance for applying fair value to assets and liabilities, including to investments. As a result, the Airport restated the beginning deferred outflows on derivative instruments and derivative instruments liabilities for fiscal year 2015.

Fiscal Year 2017

Total net position serves as an indicator of the Airport's financial position. The Airport's assets and deferred outflows of resources exceeded liabilities and deferred inflows of resources by $50.2 million and $167.1 million as of June 30, 2017 and 2016, respectively, representing a decrease of $116.9 million (70.0%). Unrestricted net position represented (141.1%) and 21.6% of total net position as of June 30, 2017 and 2016, respectively.

Unrestricted current assets consist primarily of cash and investments available to meet the Airport's current obligations. Unrestricted current assets decreased by $26.6 million (5.7%) as of June 30, 2017, primarily due to decrease in the Airport's cash and investments held in the City Treasury as a result of the transfer of July 2017 debt service deposit in June 2017.

Restricted current assets consist of cash and investments held in the City Treasury, primarily from Passenger Facility Charges (PFC) collected, debt service funds held by the bond trustee, grants receivable and PFC receivable. Restricted current assets increased by $155.6 million (55.1%) as of June 30, 2017. The increase was primarily due to an increase in the Airport's cash and investments held in the City Treasury generated from the growth of passenger traffic and an increase in the Airport's cash and investments held outside the City Treasury in connection with the issuance of the Airport's Second Series Revenue Bonds, Series 2016B/C.

Restricted noncurrent assets increased by $85.3 million (13.3%) as of June 30, 2017. The increase was primarily due to an increase in the Airport's cash and investments held in the City Treasury and outside the City Treasury related to the issuance of the Airport's Second Series Revenue Bonds, Series 2016B/C and the Airport's Second Series Revenue Refunding Bonds, Series 2016D.

Capital assets consist of land, buildings, structures, improvements, equipment, and intangible assets. Capital assets, net of depreciation, increased by $237.0 million (5.9%) as of June 30, 2017, primarily due to the capitalization of capital improvement project costs.

Unamortized loss on refunding of debt increased by $8.7 million (12.8%) as of June 30, 2017. The increase was due to the issuance of the Airport's Second Series Revenue Refunding Bonds, Series 2016D.

Deferred outflows on derivative instruments decreased by $28.7 million (34.4%) as of June 30, 2017, representing deferred outflows of resources offsetting interest rate swap liabilities in accordance with GASB Statement No. 53 – *Accounting and Financial Reporting for Derivative Instruments* (GASB 53) and GASB Statement No. 72 – *Fair Value Measurement and Application* (GASB 72).

Deferred outflows related to pensions increased by $101.8 million (231.4%) primarily due to the change of assumptions and the difference between projected and actual investment earnings on pension plan investments. See additional information in note 10a.

Current liabilities payable from unrestricted assets decreased by $25.7 million (8.3%) as of June 30, 2017, primarily due to the decrease in current maturities of the Airport's long-term debt and unearned aviation revenue.

Current liabilities payable from restricted assets decreased by $137.6 million (27.8%) as of June 30, 2017, primarily due to the take-out of commercial paper notes with the proceeds of the Airport's Second Series Revenue Bonds, Series 2016B/C during fiscal year 2017.

Noncurrent liabilities before net pension liability and derivative instruments increased by $660.7 million (15.1%) as of June 30, 2017, primarily due to the issuance of the Airport's Second Series Revenue Bonds, Series 2016B/C and the Airport's Second Series Revenue Refunding Bonds, Series 2016D during fiscal year 2017.

Net pension liability (NPL) increased by $215.3 million (149.3%) primarily due to the impact of changes in benefits, the updated citywide Supplemental COLA assumptions and amortization of deferred outflows/inflows. See additional information in note 10a.

Derivative instruments liabilities decreased by $30.2 million (31.4%) as of June 30, 2017, due to the change in fair values of interest rate swap contracts per GASB 53 and GASB 72.

Deferred inflows related to pensions decreased by $32.8 million (68.0%) primarily due to the difference between projected and actual investment earnings on pension plan investments. See additional information in note 10a.

The Airport's net investment in capital assets decreased by $167.4 million (142.6%) as of June 30, 2017, primarily due to the residual effect of the Airport depreciating its capital assets faster than repaying its bonded debt.

Net position restricted for debt service increased by $74.1 million (208.9%) as of June 30, 2017, primarily due to an increase in the Airport's cash and investments held outside the City Treasury in connection with the issuance of the Airport's Second Series Revenue Bonds, Series 2016B/C and the Airport's Second Series Revenue Refunding Bonds, Series 2016D.

Net position restricted for capital projects increased by $83.3 million (39.1%) as of June 30, 2017, primarily due to an increase in the Airport's cash and investment held in the City Treasury related to the issuance of the Airport's Second Series Revenue Bonds, Series 2016B/C.

Unrestricted net position decreased by $106.9 million (296.4%) as of June 30, 2017, primarily due to the 149.3% increase in net pension liability related to the impact of changes in benefits, the updated citywide Supplemental COLA assumptions and amortization of deferred outflows/inflows.

Fiscal Year 2016

Total net position serves as an indicator of the Airport's financial position. The Airport's assets and deferred outflows of resources exceeded liabilities and deferred inflows of resources by $167.1 million and $117.1 million as of June 30, 2016 and 2015, respectively, representing an increase of $50.0 million (42.6%).

(Continued)

Unrestricted net position represented 21.6% and 15.0% of total net position as of June 30, 2016 and 2015, respectively.

Unrestricted current assets consist primarily of cash and investments available to meet the Airport's current obligations. Unrestricted current assets increased by $17.0 million (3.8%) as of June 30, 2016, primarily due to the increase in the Airport's cash and investments held in the City Treasury and accounts receivable generated from Airport operations.

Restricted current assets consist of cash and investments held in the City Treasury, primarily from Passenger Facility Charges (PFC) collected, debt service funds held by the bond trustee, grants receivables and PFC receivable. Restricted current assets increased $36.7 million (14.9%) as of June 30, 2016. The increase was primarily due to increase in the Airport's cash and investments held in the City Treasury.

Restricted noncurrent assets decreased by $2.7 million (0.4%) as of June 30, 2016. The decrease was primarily due to the amortization of prepaid bond insurance cost.

Capital assets consist of land, buildings, structures, improvements, equipment, and intangible assets. Capital assets, net of depreciation, increased by $109.2 million (2.8%) as of June 30, 2016, primarily due to the capitalization of capital improvement project costs.

Unamortized loss on refunding of debt decreased by $10.3 million (13.1%) as of June 30, 2016. The decrease was due to the amortization of deferred refunding loss.

Deferred outflows on derivative instruments increased by $18.2 million (27.8%) as of June 30, 2016, representing deferred outflows of resources offsetting interest rate swap liabilities in accordance with GASB Statement No. 53 – *Accounting and Financial Reporting for Derivative Instruments* (GASB 53) and GASB Statement No. 72 – *Fair Value Measurement and Application* (GASB 72).

Deferred outflows related to pensions increased by $6.5 million (17.2%) primarily due to the changes of assumptions. See additional information in note 10a.

Current liabilities payable from unrestricted assets increased by $24.0 million (8.4%) as of June 30, 2016, primarily due to increases in current maturities of the Airport's long-term debt and unearned aviation revenue.

Current liabilities payable from restricted assets increased by $339.5 million (219.6%) as of June 30, 2016, primarily due to the issuance of commercial paper notes to fund capital improvement projects.

Noncurrent liabilities before net pension liability and derivative instruments decreased by $236.0 million (5.1%) as of June 30, 2016, primarily due to redemptions and the refunding of outstanding debt.

Net pension liability (NPL) increased by $32.3 million (28.9%) primarily due to higher service costs and interest costs, and a decrease in the discount rate. See additional information in note 10a.

Derivative instruments liabilities increased by $16.8 million (21.2%) as of June 30, 2016, due to the change in fair values of interest rate swap contracts per GASB 53 and GASB 72.

Deferred inflows related to pensions decreased by $52.1 million (52.0%) primarily due to the difference between projected and actual earnings on pension plan investments. See additional information in note 10a.

The Airport's net investment in capital assets decreased by $14.3 million (13.8%) as of June 30, 2016, primarily due to the residual effect of the Airport depreciating its capital assets faster than repaying its bonded debt.

Net position restricted for debt service decreased $2.0 million (5.3%) as of June 30, 2016, primarily due to a reduction in the bond debt service reserve fund requirement, largely as the result of a bond refunding during fiscal year 2016.

Net position restricted for capital projects increased $47.7 million (28.9%) as of June 30, 2016, primarily due to the issuance of commercial paper notes.

Unrestricted net position increased $18.5 million (104.9%) as of June 30, 2016, primarily due to higher operating income from Airport operations.

Highlights of Changes in Net Position

The following table shows a condensed summary of changes in net position for fiscal years 2017, 2016, and 2015 (in thousands):

	FY 2017	FY 2016	FY 2015	FY 2017 percentage increase (decrease)	FY 2016 percentage increase (decrease)
Operating revenues	$ 926,800	866,991	815,364	6.9 %	6.3 %
Operating expenses	(808,860)	(640,473)	(609,029)	26.3	5.2
Operating income	117,940	226,518	206,335	(47.9)	9.8
Nonoperating expenses, net	(201,020)	(144,463)	(141,826)	39.1	1.9
Income (loss) before capital contributions and transfers	(83,080)	82,055	64,509	(201.2)	27.2
Capital contributions	11,212	10,424	32,119	7.6	(67.5)
Transfers to City and County of San Francisco	(45,036)	(42,542)	(40,480)	5.9	5.1
Changes in net position	(116,904)	49,937	56,148	(334.1)	(11.1)
Total net position – beginning of year (as originally reported)	167,073	117,136	266,757	42.6	(56.1)
Restatement due to adoption of GASB 68	—	—	(205,769)	—	(100.0)
Total net position – beginning of year (as restated)	167,073	117,136	60,988	42.6	92.1
Total net position at end of year	$ 50,169	167,073	117,136	(70.0)%	42.6 %

Operating Revenues

The Airport derives its revenues from rates, fees, and charges assessed to the airlines; the operation of public and employee parking facilities; rents and fees assessed to concessionaires and ground transportation operators; and fees assessed for telecommunication access services. Terminal rental rates and landing fees assessed to air carriers are set periodically based on formulas and procedures described in the Lease and Use Agreement (Agreement).[4]

A brief summary of the underlying rate-setting methodology under this Agreement is presented below:

The Agreement establishes a residual rate-setting methodology for the calculation of the landing fees and terminal rental rates using certain cost centers. Under this methodology, landing fees and terminal rentals are established each year to produce projected revenues from the airlines equal to the difference between the Airport's estimated nonairline revenues and the Airport's budgeted total costs, including operating expenses, debt service expenses and the annual service payment to the City for that year. The Agreement provides for matching revenues each fiscal year to the Airport's expenditures by adjusting payments from the airlines. Differences between actual revenues and expenditures and amounts estimated in the calculation of airline fees and charges for that fiscal year result in adjustments of terminal rentals and landing fees in subsequent years. Such differences are recorded on the statements of net position in the financial statements of the Airport in the fiscal year to which such differences pertain. Net overcharges are recorded as liabilities and net undercharges are recorded as assets.

The overcharge balance of $67.6 million as of June 30, 2016, decreased to $54.9 million as of June 30, 2017, and was recorded as unearned aviation revenue in the statements of net position. See note 2j.

[4] In fiscal year 2010, the Airport and airlines reached agreement on a new form of Lease and Use Agreement that became effective on July 1, 2011 and expires June 30, 2021. The Lease and Use Agreements are referred to generally as the "Lease and Use Agreement," and the airlines that are parties to those agreements are referred to as the "Signatory Airlines."

The following table shows the air carriers that served the Airport in fiscal year 2017:

Air Carriers Serving the Airport in Fiscal Year 2017

Domestic passenger air carriers	Foreign flag carriers	Cargo only carriers
Alaska Airlines	Aer Lingus	ABX Air Inc.
American Airlines	Aeromexico	Atlas Air (DHL)
Delta Air Lines	Air Berlin	Federal Express
Frontier Airlines	Air Canada	Kalitta Air
Hawaiian Airlines	Air China	Nippon Cargo Airlines
JetBlue Airways	Air France	Redding Aero Enterprise
Southwest Airlines	Air India Limited	
Sun Country Airlines	Air New Zealand	
United Airlines	Air Pacific Limited dba Fiji Airways	
Virgin America	All Nippon Airways	
	Asiana Airlines	
	British Airways	
	COPA Airlines, Inc.	
	Cathay Pacific	
	China Airlines	
	China Eastern	
	China Southern	
	EVA Airways	
Commuter air carriers	Emirates	
Compass Airlines (American Airlines)	Etihad Airways	
Compass Airlines (Delta Air Lines)	FINNAIR	
Horizon Air (Alaska Airlines)	Japan Airlines	
Jazz Aviation (Air Canada)	KLM Royal Dutch Airlines	
SkyWest Airlines (Alaska Airlines)	Korean Air Lines	
SkyWest Airlines (Delta Air Lines)	Lufthansa German Airlines	
SkyWest Airlines (United Airlines)	Philippine Airlines	
	Qantas Airways	
	SAS Airlines	
	Singapore Airlines	
	Swiss International	
	TACA	
	Thomas Cook Group	
	Turkish Airlines	
	Virgin Atlantic	
	Volaris Airlines	
	WestJet Airlines	
	WOW Air	
	XL Airways France	

The following table shows a comparison of terminal rental rates and airline landing fees for fiscal years 2017, 2016, and 2015:

SAN FRANCISCO INTERNATIONAL AIRPORT TERMINAL RENTAL RATES AND LANDING FEES

		FY 2017	FY 2016	FY 2015
Effective average terminal rental rate (per sq. ft.)	$	161.16	157.18	149.98
Signatory Airline – landing fee rate (per 1,000 lbs.)		4.99	4.87	4.57
General aviation and itinerant aircraft – landing fee rate (per 1,000 lbs.)		5.49	5.36	5.03

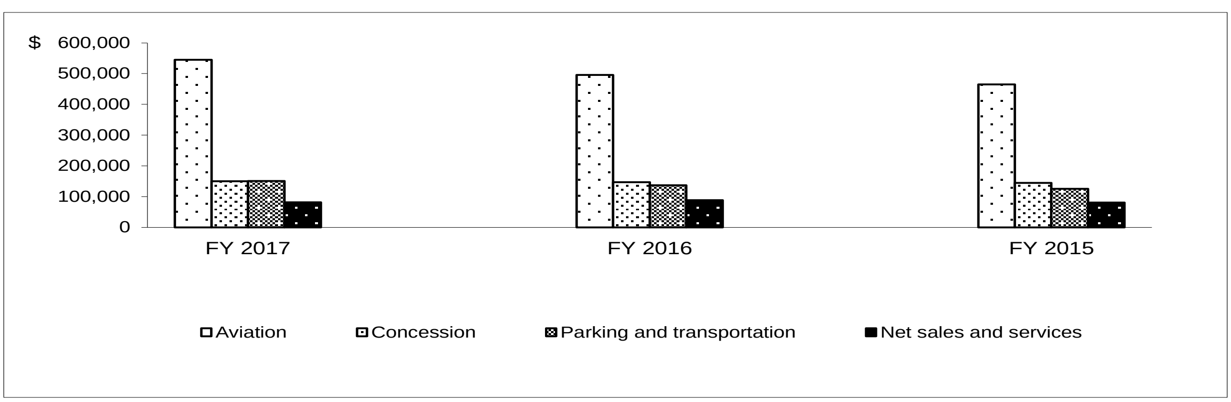
During fiscal years ended June 30, 2017, 2016, and 2015, revenues realized from the following source equaled or exceeded 5% of the Airport's total operating revenues:

	FY 2017	FY 2016	FY 2015
United Airlines	23.9 %	23.5 %	23.5 %

The following shows a comparative summary of operating revenues for fiscal years 2017, 2016, and 2015 (in thousands):

COMPARATIVE SUMMARY OF AIRPORT'S OPERATING REVENUES

		FY 2017	FY 2016	FY 2015	FY 2017 percentage increase (decrease)	FY 2016 percentage increase
Aviation	$	545,310	495,439	464,610	10.1 %	6.6 %
Concession		149,697	146,872	144,781	1.9	1.4
Parking and transportation		150,548	136,743	125,087	10.1	9.3
Net sales and services		81,245	87,937	80,886	(7.6)	8.7
Total operating revenues	$	926,800	866,991	815,364	6.9 %	6.3 %



Fiscal Year 2017

Operating revenues increased by 6.9%, from $867.0 million in fiscal year 2016 to $926.8 million in fiscal year 2017. The Airport experienced increases in aviation revenues, concession revenues, and parking and transportation revenues, which were offset by a decline in net sales and service revenues.

Aviation revenues increased by 10.1%, from $495.4 million in fiscal year 2016 to $545.3 million in fiscal year 2017, due to increases in airline landing fees and passenger traffic, and due to increases in terminal rent partly offset by a net reduction in total rented space. As determined by the calculation method in the Agreement, scheduled airline landing fees per thousand pounds increased 2.5%, from $4.87 in fiscal year 2016 to $4.99 in fiscal year 2017. The airline average annual terminal rent per square foot increased 2.5%, from $157.18 in fiscal year 2016 to $161.16 in fiscal year 2017, partially due to a 3.2% increase in the residual airline terminal rental revenue requirement. Airline leased space increased 0.6% to 1.66 million square feet.

Before the unearned aviation revenue adjustment, revenues from landing fees increased by $16.5 million (9.9%), which reflects the rate increase and a 7.4% increase in airline landed weight. Terminal rentals increased by $3.2 million (1.2%), based on the rate increase partly offset by consolidation of rented space as a result of the US Airways/American Airlines merger which reduced leased space in the Terminal 1. The overcharge balance decreased by $12.7 million, from $67.6 million in fiscal year 2016 to $54.9 million at the end of fiscal year 2017. In aggregate, all other aviation revenues increased by $5.6 million (7.2%), from $78.1 million in fiscal year 2016 to $83.7 million in fiscal year 2017, with net aviation rental revenue and activity-based fees including aircraft parking, common use gates, and employee parking all showing increases.

Concession revenues, consisting of rentals and fees derived from food and beverage concessions, duty free, retail merchandise (gifts, candy, tobacco, and news) and rental car concessions increased by 1.9%, from $146.9 million in fiscal year 2016 to $149.7 million in fiscal year 2017. The higher revenues primarily resulted from a 5.0% increase in airport passengers, and a higher food and beverage spend rate per passenger. Food and beverage revenues increased by $2.1 million (9.9%) due to the commencement of the new International Terminal Food & Beverage program and a 1.5% increase in the passenger food and beverage spend rate. Retail merchandise excluding duty free revenues were slightly higher by $0.03 million (0.2%) despite increases in passenger traffic, as the per passenger spend rate for such merchandise declined from $4.85 to $4.72 (2.7%). Revenues from duty free merchandise sales increased by $0.2 million (0.8%) despite a decline in spend rate per international enplaned passenger departing from the International Terminal of 2.6% from $19.70 to $19.19. On and off-Airport rental car revenues decreased by $1.0 million (1.9%). Other concession revenues increased by $1.5 million (5.0%), primarily from additional jet bridge advertising and a new foreign currency exchange lease that includes a higher Minimum Annual Guarantee (MAG) rent to the Airport.

Public parking and transportation revenues, consisting of rentals and fees derived from parking facilities and ground transportation operations, increased by 10.1%, from $136.7 million in fiscal year 2016 to $150.5 million in fiscal year 2017. Public parking transactions decreased by 7.9% in fiscal year 2017 resulting from the displacement of approximately 600 long-term parking spaces due to the construction of the second long-term garage partly offset by an increase in average ticket price by 12.2%, from $29.12 in fiscal year 2016 to $32.66 in fiscal year 2017. The net result was a parking revenue increase of $3.5 million (3.4%). Ground transportation revenues, including taxi trip fee revenue, increased by $10.3 million (30.7%) in fiscal year 2017 primarily due to both commercial vehicle trip fee rate increases of up to 18.0% and a 58.9% increase in transportation network company (TNC) operations at the Airport (including Uber Technologies Inc., Lyft, Inc., and Tickengo, Inc., d/b/a/ Wingz). TNC Airport pick-ups/drop-offs totaled nearly 7.0 million during the fiscal year resulting in $26.5 million in trip fee revenue. Other modes of transportation also experienced activity increases compared to fiscal year 2016 including door-to-door pre-arranged vans (14.2%), hotel shuttles (5.0%), off-airport parking vans (4.6%), scheduled buses (2.2%) and charter buses (0.7%). Modes that experienced declines compared to the prior year include shared-ride-vans (7.4%), limousines (14.5%) and taxis (18.1%).

Net sales and service revenues consist of revenue derived from utility services, telecommunication access fees, badge and permit fees, rental car facility fees, and cost-based reimbursement of various services. Revenues from net sales and services decreased by 7.6%, from $87.9 million in fiscal year 2016 to $81.2 million in fiscal year 2017. Sales of electricity revenue increased by $0.2 million (2.9%) from utility rate increases. Revenue from the sale of water-sewage disposal increased by $0.3 million (6.4%) from a 10.0% water rate increase in fiscal year 2017 partly offset by a 4.1% decline in tenant usage. Telecommunication fees were higher by $0.4 million (11.7%) from increased demand for telecommunication access services. Licenses and permits fees increased $0.4 million (21.6%) from increased badging activity from tenant employees and contractors. The transportation and facility fee (AirTrain fee charged on rental car contracts) decreased by $4.1 million (10.5%) due to the combination of a $1 per transaction rate deduction and a 5.6% decline in rental car contracts. Fees collected for the cost of the Rental Car Center (RCC) increased $0.5 million (3.3%) due to the Rental Car Center structure and surface rent annual Consumer Price Index (CPI) adjustments. Revenue from penalties resulting from the enforcement of airfield safety rules and regulations decreased by $0.6 million (39.4%). Miscellaneous terminal fees increased by $0.4 million (11.6%) due to the Terminal 2 baggage handling maintenance contract premium increase. Miscellaneous airport revenue decreased by $4.8 million (99.4%) compared to fiscal year 2016, when the Airport recorded payments from certain air carriers and other Airport users under a settlement agreement governing cost sharing for residual contamination. Net revenue from all other sales and services including collection charges, food court infrastructure/cleaning fees, refuse disposal, governmental agency rentals, collection charges and settlements increased $0.6 million (6.5%).

Fiscal Year 2016

Operating revenues increased by 6.3%, from $815.4 million in fiscal year 2015 to $867.0 million in fiscal year 2016. The Airport experienced increases in aviation revenues, concession revenues, parking and transportation revenues, and net sales and services revenues.

Aviation revenues increased by 6.6%, from $464.6 million in fiscal year 2015 to $495.4 million in fiscal year 2016, due to increases in airline landing fees and terminal rent. As determined by the calculation method in the Agreement, scheduled airline landing fees per thousand pounds increased 6.7%, from $4.57 in fiscal year 2015 to $4.87 in fiscal year 2016. The airline average annual terminal rent per square foot increased 4.8%, from $149.98 in fiscal year 2015 to $157.18 in fiscal year 2016, partially due to a 6.9% increase in the residual airline terminal rental revenue requirement. Airline leased space increased 2.0% to 1.65 million square feet.

Before the unearned aviation revenue adjustment, revenues from landing fees increased by $18.5 million (12.5%), which reflects the rate increase and a 7.4% increase in airline landed weight. Terminal rentals increased by $20.6 million (8.5%), based on the rate increase and additional leased space. The overcharge balance increased by $11.9 million, from $55.7 million in fiscal year 2015 to $67.6 million at the end of fiscal year 2016. In aggregate, all other aviation revenues increased by $3.5 million (4.7%), from $74.6 million in fiscal year 2015 to $78.1 million in fiscal year 2016, with net aviation rental revenue and activity-based fees including aircraft parking, jet bridge fees, and employee parking all showing increases.

Concession revenues, consisting of rentals and fees derived from food and beverage concessions, duty free, retail merchandise (gifts, candy, tobacco, and news) and rental car concessions increased by 1.4%, from $144.8 million in fiscal year 2015 to $146.9 million in fiscal year 2016. The higher revenues primarily resulted from a 6.6% increase in passenger enplanements and deplanements, and a higher food and beverage spend rate per passenger. Food and beverage revenues increased by $1.7 million (8.8%) due to the re-opening of Boarding Area E with new concessions on January 28, 2016 and a 1.7% increase in the passenger spend rate. Retail merchandise excluding duty free revenue decreased by $0.1 million (0.7%) despite increases in passenger traffic, as the per passenger spend rate for such merchandise declined from $4.97 to $4.85 (2.4%). Revenues from duty free merchandise sales decreased by $1.6 million (5.2%) with a decline in spend rate per international passenger of 18.4% from $22.14 to $18.07, likely primarily the result of recent global events. On and off-Airport rental car revenues decreased slightly by $0.1 million (0.2%). Other concession revenues increased by $2.2 million (8.1%), primarily from a new foreign currency exchange lease that includes a higher Minimum Annual Guarantee (MAG) rent to the Airport.

Public parking and transportation revenues, consisting of rentals and fees derived from parking facilities and ground transportation operations, increased by 9.3%, from $125.1 million in fiscal year 2015 to $136.7 million in fiscal year 2016. Public parking transactions increased by 1.0% in fiscal year 2016, partly offset by a slight decline in average ticket price by 0.1%, from $29.13 in fiscal year 2015 to $29.12 in fiscal year 2016. The net result was a parking revenue increase of $0.9 million (0.9%). Ground transportation revenues, including taxi trip fee revenue, increased by $10.7 million (47.4%) in fiscal year 2016 primarily due to both commercial vehicle trip fee rate increases of up to 4.7% and a 157.7% increase in the transportation network companies' (TNC) operations at the Airport. TNC Airport pick-ups/drop-offs totaled nearly 4.4 million during the fiscal year resulting in $16.9 million in trip fee revenue. All other modes of transportation experienced activity declines compared to fiscal year 2015 including door-to-door pre-arranged vans (23.9%), shared-ride-vans (21.2%), charter buses (21.2%), taxis (13.2%), limousines (4.3%), hotel shuttles (3.6%) and off-airport parking vans (3.0%).

Net sales and service revenues consist of revenue derived from utility services, telecommunication access fees, badge and permit fees, rental car facility fees, and cost-based reimbursement of various services. Revenues from net sales and services increased by 8.7%, from $80.9 million in fiscal year 2015 to $87.9 million in fiscal year 2016. Sales of electricity revenue increased by $0.8 million (18.9%) from increased usage demand and utility rate increases. Revenue from the sale of water-sewage disposal decreased by $0.2 million (5.2%) from a 17.2% usage decline partly offset by a 13.9% water rate increase in fiscal year 2016. Telecommunication fees were higher by $0.3 million (10.6%) from increased demand for technology services. Licenses and permits fees increased $0.4 million (27.3%) from increased badging activity from tenant employees and contractors. The transportation and facility fee (AirTrain fee charged on rental car contracts) increased $0.1 million (0.2%) due to a 0.9% increase in rental car contracts. The per rental car contract rate of $20 was unchanged in fiscal year 2016. Fees collected for the cost of the Rental Car Center (RCC) increased $0.4 million (3.1%) due to RCC structure and surface rent annual Consumer Price Index (CPI) adjustments. Revenue from penalties increased by $1.3 million (434.8%) resulting from additional revisions to the airfield safety rules and regulations and their enforcement. Miscellaneous airport revenue increased $3.6 million

(Continued)

(292.4%) primarily due to payments from certain air carriers and other Airport users under a settlement agreement governing cost sharing for residual contamination. Net revenue from all other sales and services including collection charges, food court infrastructure/cleaning fees, refuse disposal, miscellaneous terminal fees, and other settlements increased $0.3 million (2.5%).

Operating Expenses

The following table shows a comparative summary of operating expenses for fiscal years 2017, 2016, and 2015 (in thousands):

	FY 2017	FY 2016	FY 2015	Percentage increase (decrease) FY 2017	Percentage increase (decrease) FY 2016
Personnel	$ 364,831	241,162	226,790	51.3 %	6.3 %
Depreciation	265,841	228,359	216,146	16.4	5.7
Contractual services	73,918	68,064	67,491	8.6	0.8
Light, heat and power	23,093	22,925	22,296	0.7	2.8
Services provided by other City departments	21,594	19,946	17,958	8.3	11.1
Repairs and maintenance	34,863	35,839	33,278	(2.7)	7.7
Materials and supplies	16,152	16,419	14,592	(1.6)	12.5
General and administrative	4,360	3,694	5,654	18.0	(34.7)
Environmental remediation	4,208	4,065	4,824	3.5	(15.7)
	$ 808,860	640,473	609,029	26.3 %	5.2 %

Fiscal Year 2017

Operating expenses increased $168.4 million (26.3%), from $640.5 million in fiscal year 2016 to $808.9 million in fiscal year 2017, due to increases in expense for personnel, depreciation, contractual services, services provided by other City departments, general and administrative costs and costs of environmental remediation. The increase was partially offset by a decrease in the cost of repairs and maintenance, and materials and supplies expenses. In fiscal year 2017, the Airport capitalized $18.1 million of indirect costs related to construction of capital projects as overhead, compared to $14.6 million in fiscal year 2016. The variance in the different categories are discussed below.

Personnel expenses increased $123.6 million (51.3%), from $241.2 million in fiscal year 2016 to $364.8 million in fiscal year 2017. The increase was primarily due to a significant pension costs increase, cost of living adjustments, and additional positions added in fiscal year 2017.

Depreciation increased $37.4 million (16.4%), from $228.4 million in fiscal year 2016 to $265.8 million in fiscal year 2017. The increase was primarily due to the addition of completed capital improvement projects such as Terminal 1 Temporary Boarding Area B, Fire House #3 and South Field Checkpoint Relocation, and Terminal 1 Center.

Contractual services increased $5.8 million (8.6%), from $68.1 million in fiscal year 2016 to $73.9 million in fiscal year 2017. The increase was driven by higher software licensing costs and the expansion of information booth services.

Light, heat and power expenses increased $0.2 million (0.7%), from $22.9 million in fiscal year 2016 to $23.1 million in fiscal year 2017. The increase was primarily due to increases in rate and higher consumption.

Expenses of services provided by other City departments increased $1.7 million (8.3%), from $19.9 million in fiscal year 2016 to $21.6 million in fiscal year 2017. The increase was primarily due to costs associated with the implementation of the City's new financial system.

Repairs and maintenance expenses decreased $0.9 million (2.7%), from $35.8 million in fiscal year 2016 to $34.9 million in fiscal year 2017. The decrease was primarily due to lower spending on facilities maintenance projects.

Materials and supplies expenses decreased $0.2 million (1.6%), from $16.4 million in fiscal year 2016 to $16.2 million in fiscal year 2017. This decrease was primarily due to lower spending on electrical supplies.

General and administrative expenses increased $0.7 million (18.0%), from $3.7 million in fiscal year 2016 to $4.4 million in fiscal year 2017. This increase was primarily due to the increase in estimated bad debt expense.

Environmental remediation expenses increased $0.1 million (3.5%), from $4.1 million in fiscal year 2016 to $4.2 million in fiscal year 2017. The increase was primarily due an increase in remediation costs related to capital improvement projects.

Fiscal Year 2016

Operating expenses increased $31.4 million (5.2%), from $609.0 million in fiscal year 2015 to $640.5 million in fiscal year 2016, due to increases in expenses for personnel, depreciation, contractual services, services provided by other City departments, repairs and maintenance, and materials and supplies expenses. The increase was partially offset by a decrease in general and administrative costs, amortization of prepaid bond insurance costs, and costs of environmental remediation. In fiscal year 2016, the Airport capitalized $14.6 million of indirect costs related to construction of capital projects as overhead, compared to $12.7 million in fiscal year 2015. The variance in the different operating expense categories are discussed below.

Personnel costs increased $14.4 million (6.3%), from $226.8 million in fiscal year 2015 to $241.2 million in fiscal year 2016. The increase was primarily due to additional positions and cost of living adjustments included in collective bargaining agreements for Airport employees.

Depreciation increased $12.2 million (5.7%), from $216.1 million in fiscal year 2015 to $228.4 million in fiscal year 2016. The increase was primarily due to the addition of completed capital improvement projects such as Terminal 3 east improvements, the air traffic control tower, and power and water distribution system.

Contractual services increased $0.6 million (0.8%), from $67.5 million in fiscal year 2015 to $68.1 million in fiscal year 2016. This increase was driven by higher costs for curbside management services related to a significant increase in commercial ground transportation activity, particularly from TNCs.

Light, heat, and power expenses increased $0.6 million (2.8%), from $22.3 million in fiscal year 2015 to $22.9 million in fiscal year 2016. The increase was primarily due to an increase in electricity rates and higher consumption.

Services provided by other City departments increased $2.0 million (11.1%), from $18.0 million in fiscal year 2015 to $19.9 million in fiscal year 2016. The increase was primarily due to costs associated with the City's new Financial System Project.

Repairs and maintenance expenses increased $2.6 million (7.7%), from $33.3 million in fiscal year 2015 to $35.8 million in fiscal year 2016. This increase was primarily due to higher costs in information technology & telecommunications support and maintenance of additional networking hardware installed as part of various Airport improvement projects.

Materials and supplies expenses increased $1.8 million (12.5%), from $14.6 million in fiscal year 2015 to $16.4 million in fiscal year 2016. This increase was primarily due to increases in custodial, mechanical, and electrical supplies for the building maintenance.

General and administrative expenses decreased $2.0 million (34.7%), from $5.7 million in fiscal year 2015 to $3.7 million in fiscal year 2016. The decrease was due to lower legal expense and decrease of unamortized prepared bond insurance costs.

Environmental remediation expenses decreased $0.7 million (15.7%), from $4.8 million in fiscal year 2015 to $4.1 million in fiscal year 2016. The decrease was primarily due to the fact that fewer remediation costs were incurred.

Nonoperating Revenues and Expenses

The following summary shows a comparison of nonoperating revenues and expenses in fiscal years 2017, 2016, and 2015 (in thousands):

	FY 2017	FY 2016	FY 2015	FY 2017 percentage increase (decrease)	FY 2016 percentage increase (decrease)
Nonoperating revenues:					
Passenger facility charges (PFC)	$ 103,955	99,131	92,042	4.9 %	7.7 %
Investment income	7,892	13,957	9,118	(43.5)	53.1
Other	1,075	2,597	1,323	(58.6)	96.3
Total nonoperating revenues	112,922	115,685	102,483	(2.4)	12.9
Nonoperating expenses:					
Interest expense	210,415	208,597	210,608	0.9	(1.0)
Write-offs and loss on disposal	21,619	13,091	8,104	65.1	61.5
Other	81,908	38,460	25,597	113.0	50.3
Total nonoperating expenses	313,942	260,148	244,309	20.7	6.5

(Continued)

		FY 2017	FY 2016	FY 2015	FY 2017 percentage increase (decrease)	FY 2016 percentage increase (decrease)
Capital contributions	$	11,212	10,424	32,119	7.6 %	(67.5)%
Transfers to City and County of San Francisco		(45,036)	(42,542)	(40,480)	5.9	5.1
Total	$	(234,844)	(176,581)	(150,187)	33.0 %	17.6 %

Fiscal Year 2017

Nonoperating revenues consist primarily of PFC revenues and investment income, while nonoperating expenses consist of interest expense, write-offs and loss on the disposal of capital assets, and capital improvement costs that did not meet capitalization requirements. PFCs, which became effective in October 2001, generated $104.0 million during fiscal year 2017, an increase of 4.9% compared to the $99.1 million received in fiscal year 2016. The increase in PFC revenues was primarily due to an increase in passenger traffic.

Investment income decreased $6.1 million (43.5%), from $14.0 million in fiscal year 2016 to $7.9 million in fiscal year 2017, primarily due to the net effect of $12.3 million of investment fair value adjustments. Excluding the fair value adjustments, actual investment income increased $6.2 million.

Other nonoperating revenues decreased $1.5 million (58.6%) from $2.6 million in fiscal year 2016 to $1.1 million in fiscal year 2017, primarily due to the decrease in settlement income.

Interest expense increased $1.8 million (0.9%), from $208.6 million in fiscal year 2016 to $210.4 million in fiscal year 2017, primarily due to an increase in financing activities to fund capital improvement projects.

Write-offs and loss on disposal increased $8.5 million (65.1%), from $13.1 million in fiscal year 2016 to $21.6 million in fiscal year 2017, primarily due to the write-offs of the replaced capital assets and assets that did not meet the capitalization threshold.

Other nonoperating expenses increased $43.4 million (113.0%), from $38.5 million in fiscal year 2016 to $81.9 million in fiscal year 2017, primarily due to the higher demolition and capital improvement projects costs that did not meet the capitalization requirement.

Capital contributions received from federal grants increased $0.8 million (7.6%) from $10.4 million in fiscal year 2016 to $11.2 million in fiscal year 2017. The net increase was primarily due to the increase of $10.2 million in the FAA Air Traffic Control Tower and Airport Improvement Program grants, and the decrease of $9.4 million in the TSA's Checked Baggage Screening System grant.

The annual service payments transferred to the City increased $2.5 million (5.9%), from $42.5 million in fiscal year 2016 to $45.0 million in fiscal year 2017. The increase was due to higher concession, parking and transportation revenues during fiscal year 2017.

(Continued)

Fiscal Year 2016

Nonoperating revenues consist primarily of PFC revenues and investment income, while nonoperating expenses consist of interest expense, write-offs and loss on the disposal of capital assets, and capital improvement costs that did not meet the capitalization requirement. PFCs, which became effective in October 2001, generated $99.1 million during fiscal year 2016, an increase of 7.7% compared to the $92.0 million received in fiscal year 2015. The increase in PFC revenues was primarily due to an increase in passenger traffic.

Investment income increased $4.9 million (53.1%), from $9.1 million in fiscal year 2015 to $14.0 million in fiscal year 2016, primarily due to the increase in interest earned and unrealized gains from investments outside the City Treasury.

Other nonoperating revenues were primarily operating grants received during the fiscal year. For fiscal year 2016, other nonoperating revenues increased $1.3 million from $1.3 million in fiscal year 2015 to $2.6 million in fiscal year 2016, primarily due to prior year's cost recovery.

Interest expense decreased $2.0 million (1.0%), from $210.6 million in fiscal year 2015 to $208.6 million in fiscal year 2016, primarily due to decrease in fixed rate bond interest.

Write-offs and loss on disposal increased $5.0 million (61.5%), from $8.1 million in fiscal year 2015 to $13.1 million in fiscal year 2016, primarily due to write-off of capital asset being replaced.

Other nonoperating expenses increased $12.9 million (50.3%), from $25.6 million in fiscal year 2015 to $38.5 million in fiscal year 2016, primarily due to the portion of Terminal 1 capital improvement costs that did not meet the capitalization requirement.

Capital contributions received from federal grants decreased $21.7 million (67.5%), from $32.1 million in fiscal year 2015 to $10.4 million in fiscal year 2016, primarily due to the decrease in grant reimbursable capital improvement projects.

The annual service payments transferred to the City increased $2.0 million (5.1%), from $40.5 million in fiscal year 2015 to $42.5 million in fiscal year 2016. The increase in annual service payments was proportionate to the increase in concession, parking, and transportation revenues during fiscal year 2016.

Capital Acquisitions and Construction

Under the Lease and Use Agreement, the Airport Commission is obligated to use commercially reasonable efforts to finance all capital improvements (above certain de minimis amounts) through the issuance of Airport revenue bonds, grants, TSA funding, and PFCs. The Lease and Use Agreement also provides for airline review of capital projects that exceed the dollar thresholds established in the Agreement.

The Airport has five- and ten-year Capital Plans to build new facilities, improve existing facilities, renovate buildings, repair or replace infrastructure, preserve assets, enhance safety and security, develop systems functionality, and perform needed maintenance.

Fiscal Year 2017

Expenses incurred during fiscal year 2017 with respect to major capital projects are listed below. The figures below do not reflect the total project budget. Most major capital projects at the Airport are implemented over multiple fiscal years.

		Amount
Terminal 1 Redevelopment	$	287,274,333
Runway Improvements		35,839,944
South Field Redevelopment		31,990,680
AirTrain Extension		28,458,188
Consolidated Administration Campus		27,304,929
Additional Long-Term Parking Garage		25,567,160
Airport Traffic Control Tower		20,333,657
Plot 700 Redevelopment		16,057,414
Revenue Enhancement and Customer Hospitality (REACH)		13,752,773
On-Airport Hotel		11,795,966
Security Improvements		8,783,795
Superbay Renovation		7,987,835
Capital Improvement Plan Support		7,076,890
Waste Water System Improvements		6,245,015
Terminal 3 Renovation		5,601,704
Technology Improvement		4,469,897
Parking and Garage Improvements		4,063,867
International Terminal Improvements		3,580,364
Support Facility Improvements		3,547,704
Miscellaneous Terminal Improvements		2,971,747
South McDonnell Road Realignment		2,577,821
Capital Equipment		2,165,901
Shoreline Protection		2,122,848
Miscellaneous Airfield Improvements		1,418,473
Roadway Improvements		1,324,244
Wi-Fi Improvements		1,266,074
Fire Equipment Replacement		1,262,688
Support Facility Improvements		1,152,351
Wayfinding		1,123,892
Gate Capacity Enhancements		1,072,785
Total	$	568,190,939

Significant projects in design or under construction in fiscal year 2018 include the Terminal 1 (T1) Redevelopment Projects, which includes the redevelopment of Boarding Area B and the expansion of the

T1 Central Area, as well as the Terminal 3 (T3) Redevelopment Projects, which will include the redevelopment of the western portion of T3 and a new secure connector and office block between Terminal 2 (T2) and T3. Other notable ongoing projects include a new on-airport hotel, a new consolidated administration campus building, upgrades and enhancements to the International Terminal, a second long-term parking garage, the extension of the AirTrain to the second long-term parking garage, and a new industrial waste treatment plant.

Additional information about the Airport's capital acquisitions and construction is presented in note 5 to the financial statements.

Fiscal Year 2016

Expenses incurred during fiscal year 2016 with respect to major capital projects are listed below. The figures below do not reflect the total project budget. Most major capital projects at the Airport are implemented over multiple fiscal years.

		Amount
Terminal 1 Redevelopment	$	174,361,928
Terminal 3 East Improvements		61,835,219
South Field Redevelopment		25,774,425
Terminal 1 Air Traffic Control Tower Integrated Facilities		13,924,685
Air Traffic Control Tower		7,537,962
Miscellaneous Airfield Improvements		7,461,396
Additional Long-Term Parking Garage		6,406,650
Common Use Self Service		6,016,828
Plot 700 Redevelopment		5,888,892
AirTrain Extension		4,447,992
Consolidated Administration Campus		4,226,134
Ground Transportation Management System		3,783,382
Parking and Garage Improvements		3,509,170
Cargo and Hangar Improvements		3,173,535
Power and Lighting Improvements		3,157,769
On-Airport Hotel		2,995,097
Screening Improvements		2,928,781
Technology Improvement		2,696,033
Wi-Fi Improvements		2,693,263
Revenue Enhancement and Customer Hospitality (REACH)		2,379,012
Capital Improvement Plan Support		2,310,502
International Terminal Improvements		1,693,937
Fire Equipment Replacement		1,309,215
AirTrain Improvements		1,115,552
Total	$	351,627,359

Significant projects in design or under construction in fiscal year 2017 include the Terminal 1 (T1) Redevelopment Program which includes the redevelopment of Boarding Area B, the expansion of the T1 Central Area, and a new baggage handling system, in addition to the Terminal 3 (T3) Redevelopment Program which creates a unified T3 checkpoint and constructs a new secure connector and office block. Other notable ongoing projects include the on-airport hotel, a new consolidated administration campus building, a second long term parking garage, and a new industrial waste treatment plant.

Additional information about the Airport's capital acquisitions and construction is presented in note 5 to the financial statements.

Debt Administration

Fiscal Year 2017

Capital Plan Bonds: During fiscal year 2017, the Airport issued two series of bonds to fund capital projects. On September 29, 2016, the Airport issued its long-term, fixed rate Second Series Revenue Bonds, Series 2016B (AMT) and 2016C (Non-AMT/Governmental Purpose) in the aggregate principal amount of $740.1 million, to finance and refinance (through the repayment of commercial paper notes) the following projects, among others: (a) redevelopment of Terminal 1 including construction of an interim Boarding Area B and the design and construction of a new 24-gate Boarding Area B facility, (b) relocation of a firehouse and vehicle security checkpoint to accommodate the expansion of Boarding Area B and the related realignment of Taxiways H and M, (c) relocation of ground transportation facilities to accommodate the expansion of Boarding Area B, (d) construction of a new administration campus to consolidate some Airport administrative departments, (e) upgrades to operating systems-related components for the AirTrain extension, (f) gate enhancements to accommodate larger aircraft and address demand-driven gate needs, and (g) various technology improvements to upgrade network services.

Refunding Bonds: On September 29, 2016, the Airport issued its Second Series Revenue Refunding Bonds, Series 2016D (Non-AMT/Governmental Purpose) in the principal amount of $147.8 million to refund $42.2 million of its Series 2010C, $39.2 million of its Series 2011D, and $76.5 million of its Series 2011G long-term fixed rate bonds, each of which was refunded for debt service savings.

Cash Defeasance: On June 20, 2017, the Airport legally defeased $12.9 million of its Second Series Revenue Refunding Bonds, Issue 34E (AMT), using available cash on hand together with amounts held by the Trustee for purposes of paying future debt service on such bonds.

Remarketed Bonds: The Airport did not remarket any outstanding bonds during fiscal year 2017.

Subordinate Commercial Paper Notes:

- During fiscal year 2017, the Airport used proceeds of the Series 2016B and Series 2016C Bonds to retire the $343.1 million in commercial paper notes that were outstanding as of July 1, 2016, and subsequently issued $179.0 million in new money commercial paper notes, of which $1.0 million were retired using available cash on hand. As of June 30, 2017, the Airport had $178.0 million in outstanding commercial paper notes.

- On May 4, 2017, the Airport closed an extension of the irrevocable letter of credit issued by Royal Bank of Canada, supporting $200.0 million principal amount of the Airport's subordinate commercial paper notes, Series A-3, Series B-3, and Series C-3. The letter of credit will expire May 1, 2020.
- On June 22, 2017, the Airport closed a $100.0 million expansion of the commercial paper program, increasing the aggregate principal amount of the commercial paper notes that can be outstanding at any one time from $400.0 million to $500.0 million. A five-year irrevocable letter of credit issued by Sumitomo Mitsui Banking Corporation, acting through its New York Branch, supports the additional $100.0 million principal amount of the Airport's subordinate commercial paper notes, reviving the Series A-2, Series B-2 and Series C-2 commercial paper notes that had not been supported by a letter of credit since 2014. The Sumitomo letter of credit will expire June 21, 2022.

Interest Rate Swaps: The Airport ended fiscal year 2017 with six interest rate swaps outstanding with a total notional amount of $462.4 million. The Airport's interest rate swaps are intended as a hedge against the potential volatility of the interest rates on the Airport's variable rate bonds. Under the Airport's swap agreements, the Airport receives a monthly variable rate payment from each counterparty that is intended to approximate the interest payments the Airport makes on the associated variable rate bonds, while the Airport makes a monthly fixed rate payment to the swap counterparties, resulting in a synthetic fixed rate for these bonds. As of June 30, 2017, the Airport's interest rate swaps were associated with the Airport's Issue 36A/B/C, Issue 37C, and Series 2010A Bonds, either directly or indirectly.

More detailed information about the Airport's subordinate commercial paper notes, long-term debt, and interest rate swaps is presented in notes 6 and 7 to the financial statements.

1991 Master Bond Resolution Covenant Compliance: During fiscal year 2017, the Airport's operating revenues, together with the permitted transfers from the Airport's Contingency Account, were sufficient to meet the rate covenant requirements under the Airport's 1991 Master Bond Resolution. See note 7f.

Fiscal Year 2016

Capital Plan Bonds: The Airport did not issue additional bonds to fund new capital projects during fiscal year 2016.

Refunding Bonds: On February 25, 2016, the Airport issued its Second Series Revenue Refunding Bonds, Series 2016A (Non-AMT/Governmental Purpose), in the principal amount of $232.1 million to refund $66.5 million of its Issue 32F, $155.3 million of its Issue 32G and $63.1 million of its Issue 34D long-term fixed rate bonds, which were refunded for debt service savings.

Cash Defeasance: On June 30, 2016 the Airport used available cash on hand to defease a portion of its Second Series Revenue Refunding Bonds, Issue 34E (AMT) ($24.7 million).

Remarketed Bonds: During Fiscal Year 2016, the Airport remarketed two series of outstanding bonds:

- On June 29, 2016 the Airport remarketed its Second Series Variable Rate Revenue Refunding Bonds, Issue 36A (Non-AMT/Private Activity), with a new irrevocable letter of credit from Wells Fargo Bank, National Association, that expires on June 29, 2018. The bonds were previously secured by a letter of credit provided by U.S. Bank, National Association, which was terminated on July 7, 2016, prior to its stated expiration date of October 26, 2016.

- On June 29, 2016 the Airport remarketed its long-term Second Series Variable Rate Revenue Refunding Bonds, Series 2010A (AMT), with a new irrevocable letter of credit from Bank of America, National Association, that expires on June 29, 2020. The bonds were originally secured by a letter of credit provided by JPMorgan Chase Bank, National Association, which was terminated on July 11, 2016, prior to its stated expiration date of December 14, 2016.

Subordinate Commercial Paper Notes:

- During fiscal year 2016, the Airport did not retire any of the $40 million in commercial paper notes that were outstanding as of July 1, 2015 and issued $304.1 million in new money commercial paper notes, of which $1.1 million were retired. As of June 30, 2016, the Airport had $343.1 million in outstanding commercial paper notes.
- On June 2, 2016, the Airport closed a three-year extension of the irrevocable letter of credit issued by Wells Fargo Bank, National Association, supporting $100.0 million of the Airport's subordinate commercial paper notes, Series A-4, Series B-4 and Series C-4. The letter of credit will expire May 31, 2019.

Interest Rate Swaps: The Airport ended fiscal year 2016 with six interest rate swaps outstanding with a total notional amount of $479.5 million. The Airport's interest rate swaps are intended as a hedge against the potential volatility of the interest rates on the Airport's variable rate bonds. Under the Airport's swap agreements, the Airport receives a monthly variable rate payment from each counterparty that is intended to approximate the interest payments the Airport makes on the associated variable rate bonds, while the Airport makes a monthly fixed rate payment to the swap counterparties, resulting in a synthetic fixed rate for these bonds. As of June 30, 2016, the Airport's interest rate swaps were associated with the Airport's Issue 36A/B/C, Issue 37C, and Series 2010A Bonds, either directly or indirectly.

More detailed information about the Airport's subordinate commercial paper notes, long-term debt, and interest rate swaps is presented in notes 6 and 7 to the financial statements.

Master Bond Resolution Covenant Compliance: During fiscal year 2016, the Airport's operating revenues, together with the permitted transfers from the Airport's Contingency Account, were sufficient to meet the rate covenant requirements under the Airport's 1991 Master Bond Resolution.

Credit Ratings and Bond Insurance

Fiscal Year 2017

Credit Ratings: During fiscal year 2017, Moody's Investors Service Inc. (Moody's), Standard & Poor's Ratings Services, a Standard and Poor's Financial Services LLC business (S&P), and Fitch Inc. (Fitch) affirmed their underlying credit ratings on the outstanding debt of the Airport of "A1", "A+", and "A+", respectively, each with stable rating outlooks.

Ratings on each subseries of the Airport's commercial paper notes reflect the short-term credit ratings of the bank whose letter of credit supports that subseries.

As of September 13, 2016, Moody's, S&P, and Fitch assigned credit ratings of "A1", "A+", and "A+", respectively, to the Series 2016B/C/D Bonds, which were issued on September 29, 2016.

Bond Insurance: Prior to fiscal year 2009, the Airport generally purchased municipal bond insurance policies in connection with the issuance of many series of its outstanding revenue bonds from monoline bond insurance companies that enjoyed "AAA" ratings at the time. The insured credit ratings on these Airport bonds declined in tandem with the credit ratings of most bond insurance companies as a result of the global financial crisis that began in fiscal year 2008.

In fiscal year 2017, certain outstanding Airport bonds were supported by Assured Guaranty Corp., Assured Guaranty Municipal Corp., and National Public Finance Guarantee Corp. In fiscal year 2017, the public ratings of Assured Guaranty Corp. were "A3" by Moody's and "AA" by S&P, and the public ratings of Assured Guaranty Municipal Corp. (formerly known as Financial Security Assurance Inc.) were "A2" by Moody's and "AA" by S&P. On June 26, 2017, S&P lowered its financial strength rating on National Public Finance Guarantee Corp. (National) from "AA-" to "A". The Moody's public rating of National (which has assumed the obligations of MBIA Insurance Corporation and Financial Guaranty Insurance Corp.) was "A3" in fiscal year 2017.

Fiscal Year 2016

Credit Ratings: During fiscal year 2016, Moody's Investors Service Inc. (Moody's), Standard & Poor's Ratings Services, a Standard and Poor's Financial Services LLC business (S&P), and Fitch Inc. (Fitch) affirmed their underlying credit ratings on the outstanding debt of the Airport of "A1", "A+", and "A+" with Stable Rating Outlooks, respectively.

On September 11, 2015, Fitch upgraded the credit rating on the Commission's San Francisco International Airport Special Facilities Lease Revenue Bonds (SFO Fuel Company LLC), Series 1997A, and San Francisco International Airport 1997 Special Facilities Lease Revenue Bonds (SFO Fuel Company LLC), Series 2000A, from "BBB+" to "A-" (Stable Outlook).

Ratings on each subseries of the Airport's commercial paper notes reflect the short-term credit ratings of the bank whose letter of credit support that subseries.

On January 20, 2016, Moody's, S&P, and Fitch assigned credit ratings of "A1", "A+", and "A+", respectively, to the Series 2016A Bonds, which were issued on February 25, 2016.

On October 5, 2015, Fitch upgraded the long-term credit rating of U.S. Bank National Association. The Airport's Second Series Variable Rate Revenue Refunding Bonds, Issue 36A, were secured by an irrevocable letter of credit issued by U.S. Bank. As a result, on October 6, 2015, Fitch raised its joint-support, long-term credit rating on the Issue 36A Bonds from "AA+" to "AAA".

On May 23, 2016, S&P applied its updated Methodology and Assumptions for Rating Jointly Supported Financial Obligations criteria to the Airport's Second Series Variable Rate Revenue Bonds, Issues 36A/B/C, Issue 37C, and Series 2010A. As a result, on May 23, 2016, S&P lowered its joint-support, long-term credit rating on those Bonds from "AAA" to "AA+".

On June 29, 2016, the Airport remarketed the Issue 36A Bonds with a new irrevocable letter of credit issued by Wells Fargo Bank, National Association that replaced the prior letter of credit issued by U.S. Bank National Association. In connection with the new letter of credit, the joint-support credit ratings on the Series 36A Bonds were affirmed.

On June 29, 2016, the Airport remarketed the Series 2010A Bonds with a new irrevocable letter of credit issued by Bank of America, National Association that replaced the prior letter of credit issued by JPMorgan Chase Bank, National Association. In connection with the new letter of credit, Moody's downgraded its joint-support credit ratings on the Series 2010A Bonds to "Aa2/VMIG1" and Fitch downgraded its joint-support credit ratings on the Series 2010A Bonds to "AA/F1".

Bond Insurance: Prior to fiscal year 2009, the Airport generally purchased municipal bond insurance policies in connection with the issuance of many series of its outstanding revenue bonds from monoline bond insurance companies that enjoyed "AAA" ratings at the time. The insured credit ratings on these Airport bonds declined in tandem with the credit ratings of most bond insurance companies as a result of the global financial crisis that began in fiscal year 2008.

In fiscal year 2016, the Airport's bond insurance companies' ratings were unchanged. The public ratings of Assured Guaranty Corp. were "A3" by Moody's and "AA" by S&P, and the public ratings of Assured Guaranty Municipal Corp. (formerly known as Financial Security Assurance Inc.) were "A2" by Moody's and "AA" by S&P. The public ratings of National Public Finance Guarantee Corp. (which has assumed the obligations of MBIA Insurance Corporation and Financial Guaranty Insurance Corp.) were "A3" by Moody's and "AA-" by S&P.

Fiscal Year 2018 Airline Rates and Charges

Terminal rental rates and airline landing fees for fiscal year 2018 have been developed as part of the annual budget process that started in October 2016. The Lease and Use Agreement between the Airport and the Signatory Airlines provides the rate-setting methodology for calculating the terminal rental rates and Airline landing fees. Not less than 60 days prior to the start of the fiscal year, the Signatory Airlines are notified of the proposed rates and fees. These fees are subject to review by, but not the approval of, the Signatory Airlines. The terminal rental rates and airline landing fees for fiscal year 2018, which became effective on July 1, 2017, are as follows:

Effective average terminal rental rate (per sq. ft)	$	169.03
Signatory Airline – landing fee rate (per 1,000 lbs.)		5.24
NonSignatory Airline – landing fee rate (per 1,000 lbs.)		6.55
General aviation – landing fee rate (per 1,000 lbs.)		6.55

The effective average terminal rental rate increased by 4.9%, from $161.16 per sq. ft. in fiscal year 2017 to $169.03 per sq. ft. in fiscal year 2018. The fiscal year 2017 landing fee rate for Signatory Airlines increased by 4.9%, from $4.99 per 1,000 pounds in fiscal year 2017 to $5.24 per 1,000 pounds in fiscal year 2018, while the Non-Signatory Airline landing fee rate increased by 4.9%, from $6.24 per 1,000 pounds in fiscal year 2017 to $6.55 per 1,000 pounds in fiscal year 2018. The fiscal year 2017 landing fee rate for general aviation aircraft increased by 19.3%, from $5.49 per 1,000 pounds in fiscal year 2017 to $6.55 per 1,000 pounds in fiscal year 2018.

Requests for Information

This report is designed to provide a general overview of the San Francisco International Airport's finances. Questions concerning any of the information provided in this report or requests for additional information should be addressed to the Chief Business & Finance Officer, San Francisco International Airport, P.O. Box 8097, San Francisco, California 94128.

AIRPORT COMMISSION
CITY AND COUNTY OF SAN FRANCISCO
SAN FRANCISCO INTERNATIONAL AIRPORT

Statements of Net Position

June 30, 2017 and 2016

(In thousands)

		2017	2016
Assets:			
Current assets:			
Cash and investments held in City Treasury	$	375,593	410,358
Cash and investments outside City Treasury		5,854	5,927
Cash – Revolving Fund		10	10
Accounts receivable (net of allowance for doubtful accounts: 2017: $1,807; 2016: $1,214)		53,085	47,851
Accrued interest – City Treasury		513	430
Accrued interest – outside City Treasury		1,572	1,156
Inventories		58	38
Other current assets		4,245	1,807
Restricted assets:			
Cash and investments held in City Treasury		273,106	197,348
Cash and investments outside City Treasury		142,557	63,885
Accounts receivable		—	781
Accrued interest – Other		172	39
Grants receivable		5,083	9,970
Passenger facility charges receivable		17,016	10,348
Total current assets		878,864	749,948
Noncurrent assets:			
Restricted assets:			
Cash and investments held in City Treasury		315,746	259,134
Cash and investments outside City Treasury		409,355	381,237
Accrued interest – City Treasury		924	532
Prepaid bond insurance costs		285	67
Capital assets, net		4,282,629	4,045,636
Total noncurrent assets		5,008,939	4,686,606
Total assets		5,887,803	5,436,554
Deferred outflows of resources:			
Unamortized loss on refunding of debt		76,789	68,100
Deferred outflows on derivative instruments		54,870	83,614
Deferred outflows related to pensions		145,743	43,982
Total deferred outflows of resources	$	277,402	195,696

(Continued)

AIRPORT COMMISSION
CITY AND COUNTY OF SAN FRANCISCO
SAN FRANCISCO INTERNATIONAL AIRPORT

Statements of Net Position

June 30, 2017 and 2016

(In thousands)

		2017	2016
Liabilities:			
Current liabilities:			
Accounts payable	$	54,064	56,483
Accrued payroll		10,477	9,579
Compensated absences		9,845	9,714
Accrued workers’ compensation		1,520	1,413
Estimated claims payable		777	1,346
Unearned aviation revenue		54,853	67,556
Current maturities of long-term debt		152,685	163,797
Payable from restricted assets:			
Accounts payable		90,794	82,720
Accrued payroll		784	467
Grants received in advance		—	6,088
Accrued bond interest payable		36,062	31,475
Commercial paper		178,000	343,050
Current maturities of long-term debt		50,895	30,328
Total current liabilities		640,756	804,016
Noncurrent liabilities:			
Compensated absences, net of current portion		7,172	7,326
Accrued workers’ compensation, net of current portion		5,816	5,244
Estimated claims payable, net of current portion		78	131
Long-term debt, net of current maturities		4,882,080	4,235,551
Other postemployment benefits obligation		138,168	124,352
Net pension liability		359,599	144,271
Derivative instruments		65,965	96,132
Total noncurrent liabilities		5,458,878	4,613,007
Total liabilities		6,099,634	5,417,023
Deferred inflows of resources:			
Deferred inflows related to pensions		15,402	48,154
Total deferred inflows of resources		15,402	48,154
Net position:			
Net investment in capital assets		(284,761)	(117,377)
Restricted for debt service		109,554	35,462
Restricted for capital projects		296,188	212,931
Unrestricted		(70,812)	36,057
Total net position	$	50,169	167,073

See accompanying notes to financial statements.

AIRPORT COMMISSION
CITY AND COUNTY OF SAN FRANCISCO
SAN FRANCISCO INTERNATIONAL AIRPORT

Statements of Revenues, Expenses, and Changes in Net Position

Years ended June 30, 2017 and 2016

(In thousands)

		2017	2016
Operating revenues:			
Aviation	$	545,310	495,439
Concession		149,697	146,872
Parking and transportation		150,548	136,743
Net sales and services		81,245	87,937
Total operating revenues		926,800	866,991
Operating expenses:			
Personnel		364,831	241,162
Depreciation		265,841	228,359
Contractual services		73,918	68,064
Light, heat, and power		23,093	22,925
Services provided by other City departments		21,594	19,946
Repairs and maintenance		34,863	35,839
Materials and supplies		16,152	16,419
General and administrative		4,360	3,694
Environmental remediation		4,208	4,065
Total operating expenses		808,860	640,473
Operating income		117,940	226,518
Nonoperating revenues (expenses):			
Investment income		7,892	13,957
Interest expense		(210,415)	(208,597)
Passenger facility charges		103,955	99,131
Write-offs and loss on disposal		(21,619)	(13,091)
Other nonoperating revenues		1,075	2,597
Other nonoperating expenses		(81,908)	(38,460)
Total nonoperating expenses, net		(201,020)	(144,463)
Income (loss) before capital contributions and transfers		(83,080)	82,055
Capital contributions:			
Grants		11,212	10,424
Transfers to City and County of San Francisco		(45,036)	(42,542)
Changes in net position		(116,904)	49,937
Total net position – beginning of year		167,073	117,136
Total net position – end of year	$	50,169	167,073

See accompanying notes to financial statements.

(Continued)

AIRPORT COMMISSION
CITY AND COUNTY OF SAN FRANCISCO
SAN FRANCISCO INTERNATIONAL AIRPORT

Statements of Cash Flows

Years ended June 30, 2017 and 2016

(In thousands)

		2017	2016
Cash flows from operating activities:			
Cash received from airline carriers, concessionaires, and others	$	931,127	891,569
Cash paid for employees' services		(268,646)	(254,837)
Cash paid to suppliers of goods and services		(204,038)	(194,383)
Net cash provided by operating activities		458,443	442,349
Cash flows from noncapital financing activities:			
Transfers to City and County of San Francisco		(45,036)	(42,542)
Other noncapital financing revenues		1,075	2,597
Other noncapital financing expenses		(81,908)	(38,460)
Net cash used in noncapital financing activities		(125,869)	(78,405)
Cash flows from capital and related financing activities:			
Principal paid on revenue bonds and commercial paper notes		(208,125)	(209,910)
Interest paid on revenue bonds and commercial paper notes		(233,585)	(225,073)
Acquisition and construction of capital assets		(506,508)	(304,421)
Revenues from passenger facility charges		97,287	98,432
Proceeds from sale of revenue bonds		437,465	841
Proceeds from commercial paper notes		179,000	304,100
Capital contributed by federal agencies and others		10,011	20,665
Net cash used in capital and related financing activities		(224,455)	(315,366)
Cash flows from investing activities:			
Sales of investments with Trustee		664,457	635,126
Purchases of investments with Trustee		(689,700)	(624,603)
Interest received on investments		15,235	4,808
Net cash provided (used) in investing activities		(10,008)	15,331
Net increase in cash and cash equivalents		98,111	63,909
Cash and cash equivalents, beginning of year		873,741	809,832
Cash and cash equivalents, end of year	$	971,852	873,741
Reconciliation of cash and cash equivalents to the statements of net position:			
Cash and investments held in City Treasury – unrestricted	$	375,593	410,358
Cash and investments held in City Treasury – restricted		588,852	456,482
Cash and investments outside City Treasury – unrestricted		5,854	5,927
Cash and investments outside City Treasury – restricted		1,123	1,090
Cash – Revolving Fund		10	10
Cash, cash equivalents, and investments		971,432	873,867
Unrealized gain or loss on investments		420	(126)
Cash and cash equivalents, June 30	$	971,852	873,741

(Continued)

AIRPORT COMMISSION
CITY AND COUNTY OF SAN FRANCISCO
SAN FRANCISCO INTERNATIONAL AIRPORT

Statements of Cash Flows

Years ended June 30, 2017 and 2016

(In thousands)

		2017	2016
Reconciliation of operating income to net cash provided by operating activities:			
Operating income	$	117,940	226,518
Adjustments for noncash and other activities:			
Depreciation		265,841	228,359
Allowance for doubtful accounts		593	581
Cost of issuance paid from bond proceeds		1,912	980
Changes in assets and liabilities:			
Accounts receivable		(5,827)	(9,536)
Inventories		(20)	4
Other current assets		(2,438)	(1,188)
Accrued payroll receivable		—	1
Deferred outflows related to pensions		(101,761)	(6,465)
Accounts payable and other liabilities		(3,041)	(1,546)
Accrued payroll		898	2,209
Compensated absences		(22)	746
Accrued workers' compensation		679	576
Other postemployment benefits obligation		13,816	9,055
Unearned aviation revenue		(12,703)	11,852
Deferred inflows related to pensions		(32,752)	(52,136)
Net pension liability		215,328	32,339
Net cash provided by operating activities	$	458,443	442,349
Noncash transactions:			
Accrued capital asset costs	$	91,578	83,187
Bond refunding through fiscal agent		184,536	282,453
Bond proceeds held by fiscal agent		434,287	—
Commercial paper repaid through fiscal agent		343,050	—

See accompanying notes to financial statements.

(Continued)

(1) Definition of Reporting Entity

The accompanying financial statements reflect the net position and changes in net position of the Airport Commission, City and County of San Francisco, San Francisco International Airport (the Airport or SFO), a commercial service airport owned and operated as an enterprise fund of the City and County of San Francisco (the City). The Airport opened in 1927 and for calendar year 2016 was the seventh busiest airport in the United States in terms of passengers and fifteenth in terms of cargo tonnage.[5] The Airport is also a major origin and destination point and one of the nation's principal gateways for Pacific traffic. A five-member Airport Commission is responsible for its operation, development, and maintenance. Airport Commission members are appointed by the City's Mayor for terms of four years.

The Airport is an integral part of the City and is reported as a major enterprise fund in the City's Comprehensive Annual Financial Report. There are no component units considered for inclusion in the Airport's financial reporting entity. The accompanying financial statements present only the financial operations of the Airport and do not purport to, and do not, present the financial position of the City, or the results of its operations and the cash flows of its other proprietary fund types.

(2) Significant Accounting Policies

(a) Measurement Focus and Basis of Accounting

The Airport's financial activities are accounted for on a flow of economic resources measurement focus, using the accrual basis of accounting in accordance with U.S. generally accepted accounting principles (GAAP).

The Airport distinguishes operating revenues and expenses from nonoperating revenues and expenses. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with an organization's principal ongoing operations. The principal operating revenues of the Airport are charges to airlines, concessionaires, and parking and transportation charges. Operating expenses of the Airport include personnel costs, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting these definitions are reported as nonoperating revenues and expenses.

As prescribed under GASB Statement No. 68 – *Accounting and Financial Reporting for Pensions* – an amendment of GASB Statement 27, net pension liability, deferred outflows/inflows of resources related to pensions, pension expense, information about the fiduciary net position of the San Francisco Employees Retirement System (SFERS) plan and additions to/deductions from the plan's fiduciary net position have been determined on the same basis as they are reported by the plan. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. Plan member contributions are recognized in the period in which the contributions are due. Investments are reported at fair value and liabilities are based on the results of actuarial calculations.

[5] Source: Airports Council International – North America, 2016 North American Traffic Report.

(b) Implementation of New Governmental Accounting Standards Board (GASB)

Governmental Accounting Standards Board (GASB) Statement No. 73

In June 2015, the GASB issued Statement No. 73 – *Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68*, and Amendments to Certain Provisions of GASB Statements 67 and 68. GASB Statement No. 73 addresses accounting and financial reporting for pensions provided by governments that are not within the scope of GASB 68. The new standard is effective for periods beginning after June 15, 2016. The Airport adopted the provisions of this Statement, which did not have a significant impact on its financial statements.

Governmental Accounting Standards Board (GASB) Statement No. 75

In June 2015, the GASB issued Statement No. 75 – *Accounting and Financial Reporting for Postemployment Benefit Other Than Pension Plans*. GASB Statement No. 75 revises and establishes new accounting and financial reporting requirements for governments that provides their employees with other postemployment benefits other than pensions (OPEB). The new standard is effective for periods beginning after June 15, 2017. The Airport will implement the provisions of Statement No. 75 in fiscal year 2018.

Governmental Accounting Standards Board (GASB) Statement No. 77

In August 2015, the GASB issued Statement No. 77 – *Tax Abatement Disclosures*. GASB Statement No. 77 establishes financial reporting standards for tax abatement agreements entered into by state and local governments. The new standard is effective for periods beginning after December 15, 2015. The Airport adopted the provisions of this Statement, which did not have a significant impact on its financial statements.

Governmental Accounting Standards Board (GASB) Statement No. 78

In December 2015, the GASB issued Statement No. 78 – *Pensions Provided through Certain Multiple-Employer Defined Benefit Pension Plans*. GASB Statement No. 78 establishes accounting and financial reporting standards for defined benefit pensions provided by state or local governments through a cost-sharing plan that meets the criteria of Statement No. 68 and is not a state or local governmental pension plan. The new standard is effective for periods beginning after December 15, 2015. The Airport adopted the provisions of this Statement, which did not have a significant impact on its financial statements.

Governmental Accounting Standards Board (GASB) Statement No. 81

In March 2016, the GASB issued Statement No. 81 – *Irrevocable Split-Interest Agreements*. GASB Statement No. 81 establishes accounting and financial reporting standards for irrevocable split-interest agreement created through trusts in which a donor irrevocably transfers resources to an intermediary. The new standard is effective for periods beginning after December 15, 2016. The Airport will implement the provisions of Statement No. 81 in fiscal year 2018.

Governmental Accounting Standards Board (GASB) Statement No. 82

In March 2016, the GASB issued Statement No. 82 – *Pension Issues*, an amendment of GASB Statements No. 67, No. 68, and No. 73. GASB Statement No. 82 addresses issues regarding (1) the presentation of payroll-related measures in required supplementary information, (2) the selection of assumptions and the treatment of deviations from the guidance in an Actuarial Standard of Practice for financial reporting purposes, and (3) the classification of payments made by employers to satisfy employee (plan member) contribution requirements. The new standard is effective for periods beginning after June 15, 2016. The Airport elected early implementation in fiscal year 2016 and there was no significant impact to its financial statements.

Governmental Accounting Standards Board (GASB) Statement No. 83

In November 2016, the GASB issued Statement No. 83 – *Certain Asset Retirement Obligations*. GASB Statement No. 83 establishes accounting and financial reporting standards for certain asset retirement obligations (AROs). The new standard is effective for periods beginning after June 15, 2018. The Airport will implement the provisions of Statement No. 83 in fiscal year 2019.

Governmental Accounting Standards Board (GASB) Statement No. 84

In January 2017, the GASB issued Statement No. 84 – *Fiduciary Activities*. GASB Statement No. 84 establishes criteria for state and local governments to identify fiduciary activities and how those activities should be reported. The new standard is effective for periods beginning after December 15, 2018. The Airport will implement the provisions of Statement No. 84 in fiscal year 2020.

Governmental Accounting Standards Board (GASB) Statement No. 85

In March 2017, the GASB issued Statement No. 85 – *Omnibus 2017*. GASB Statement No. 85 addresses practice issues identified during the implementation and application of certain GASB Statements. The new standard is effective for periods beginning after June 15, 2017. The Airport will implement the provisions of Statement No. 85 in fiscal year 2018.

Governmental Accounting Standards Board (GASB) Statement No. 86

In May 2017, the GASB issued Statement No. 86 – *Certain Debt Extinguishment Issues*. GASB Statement No. 86 improves accounting and financial reporting for in-substance defeasance of debt using existing resources other than proceeds of refunding debt. The new standard is effective for periods beginning after June 15, 2017. The Airport will implement the provisions of Statement No. 86 in fiscal year 2018.

Governmental Accounting Standards Board (GASB) Statement No. 87

In June 2017, the GASB issued Statement No. 87 – *Leases*. GASB Statement No. 87 establishes a single model for lease accounting and requires reporting of certain lease liabilities that currently are not reported. The new standard is effective for periods beginning after December 15, 2019. The Airport will implement the provisions of Statement No. 87 in fiscal year 2021.

(Continued)

(c) Cash, Cash Equivalents, and Investments

The Airport maintains its cash, cash equivalents, investments, and a significant portion of its restricted cash and investments as part of the City's pool of cash and investments. The Airport's portion of this pool is displayed on the statements of net position as "Cash and investments held in City Treasury." Income earned or losses arising from pooled investments are allocated on a monthly basis to appropriate funds and entities based on their average daily cash balances.

The City reports certain investments at fair value in the statements of net position and recognizes the corresponding change in fair value of investments in the year in which the change occurred.

The Airport considers its pooled deposits held with the City Treasurer to be demand deposits and therefore cash for financial reporting. The City considers highly liquid investments with original maturities of three months or less to be cash equivalents. Restricted cash and investments held by the bond trustees that meet these criteria are considered to be cash and cash equivalents.

The debt service fund, the debt service reserve fund, the costs of issuance fund, the debt service holding fund, and the variable rate demand bond fee account for the Airport's revenue bonds are held and invested at the Airport's direction by an independent bond trustee.

(d) Capital Assets

Capital assets are stated at historical cost, or if donated, at fair value at the date of donation. The capitalization threshold for real property is $100,000 and $5,000 for personal property with a useful life greater than one year.

Depreciation and amortization are computed using the straight-line method over the following estimated useful lives:

	Years
Buildings, structures, and improvements	5–50
Equipment	5–20
Intangible assets	3–20

Maintenance, repairs, and minor replacements are charged against operations in the year performed. Major replacements that extend the useful life of the related assets are capitalized. No depreciation is provided on construction in progress until construction is substantially complete and the asset is placed in service. The Airport begins depreciation on capital assets the month following the date in which assets are placed in service. Additionally, the Airport commenced allocating indirect costs on self-constructed assets starting fiscal year 2007. The indirect cost rate applied is based on a cost allocation plan developed in accordance with the terms of 2 CFR Part 200 *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards (the Uniform Guidance)*, as applicable. See note 5.

(Continued)

(e) Capitalized Interest

Interest cost of debt issued for acquiring a capital asset is capitalized as part of the historical cost of the asset. Interest costs of tax-exempt bond funds used for specified construction purposes, net of interest earned on the temporary investment of the proceeds of such tax-exempt borrowings, are capitalized from the date of borrowings until the asset is ready for its intended use. Interest costs of other borrowings are capitalized based on average accumulated construction expenditures.

(f) Derivative Instruments

The Airport has entered into certain derivative instrument agreements, which it values at fair value, in accordance with GASB Statement No. 53 – *Accounting and Financial Reporting for Derivative Instruments* and GASB Statement No. 72 – *Fair Value Measurement and Application*. The Airport applies hedge accounting for changes in the fair value of hedging derivative instruments, in accordance with GASB Statement No. 64 – *Derivative Instruments: Application of Hedge Accounting Termination Provisions*, an amendment of GASB Statement No. 53. Under hedge accounting, if the derivatives are determined to be effective hedges, the changes in the fair value of hedging derivative instruments are reported as either deferred inflows or deferred outflows in the statements of net position, otherwise changes in fair values are recorded within the investment revenue classification.

(g) Bond Issuance Costs, Discounts, and Premiums

Bond issuance costs related to prepaid insurance costs are capitalized and amortized using the effective interest method. Other bond issuance costs are expensed when incurred. Original issue bond discount or premium are offset against the related debt and are also amortized using the effective interest method. Deferred outflows/inflows of resources from refunding of debt are recognized as a component of interest expense using the effective interest method over the remaining life of the old debt or the life of the new debt, whichever is shorter.

(h) Compensated Absences

Vested vacation, sick leave, and related benefits are accrued when incurred for all Airport employees.

(i) Net Position

Net position consists of the following:

Net Investment in Capital Assets – consists of capital assets, including restricted capital assets, reduced by accumulated depreciation and by any outstanding debt incurred to acquire, construct, or improve those assets (including any unamortized original issue discounts or premiums related to the debt). Deferred outflows of resources that are attributable to the acquisition, construction, or improvement of those assets or related debt (such as deferred losses on advance refundings) are also included in this component of net position.

Restricted for Debt Service and Capital Projects – consists of restricted assets and deferred outflows of resources reduced by liabilities related to those assets and deferred outflows of resources. Restricted assets are those assets with restrictions on their use that are externally imposed (by creditors, grantors, contributors, or the laws or regulations of other governments).

(Continued)

Unrestricted Net Position – consists of the net amount of the assets, deferred outflows of resources, and liabilities, of the Airport that are not restricted for any project or other purpose.

A significant portion of the Airport's net position is restricted by master bond resolutions and the Lease and Use Agreement with the airlines for the purpose of capital improvements and contingencies.

(j) Aviation Revenue and Unearned Aviation Revenue

Aviation revenue is based on reimbursable expenditures as defined in the Lease and Use Agreement with the airlines. Under the Lease and Use Agreement, the airlines are required to pay terminal rents and landing fees in amounts that, when aggregated with certain other Airport revenues, will be equal to the Airport's expenditures for: operating expenses other than depreciation and amortization; principal and interest on outstanding debt; annual service payments to the City; and certain acquisitions of capital assets. Other capital asset additions are funded with proceeds of revenue bonds for which the airlines are required to fund debt service. During fiscal year 2010, the Airport reached an agreement with the airlines on a new 10-year Lease and Use Agreement that became effective on July 1, 2011. Airlines that are not signatories to one of these long-term agreements operate under month-to-month permits.

Amounts billed to airlines are based on budgeted revenues and expenditures, including debt service, pension charges and proportionate payments to such compensation and other insurance or outside reserve funds as the Commission may establish or the Board of Supervisors may require with respect to employees of the Commission. Noncash accrued pension obligations other than those actually paid or budgeted to be paid during the fiscal year are excluded. Aviation revenue collected in advance will be applied to reduce future billings and is recorded as a liability in the financial statements. Aviation revenue due will be reduced by increases in future billings and is recorded as an asset in the financial statements. Pursuant to the terms of the Lease and Use Agreement, the Airport has aviation revenue collected in advance from the airlines of approximately $54.9 million and $67.6 million as of June 30, 2017 and 2016, respectively.

(k) Concession Revenues

Concession revenues consist of rentals and fees derived from food and beverage concessions, duty free, retail merchandise and rental car concessions. Revenues are based on terms of lease agreements entered between the Airport and concessionaires, and are the greater of a percentage of tenant's gross revenues or a minimum annual guarantee (MAG) amount.

(l) Parking and Transportation Revenues

Parking and transportation revenues consist of fees derived from parking facilities and ground transportation operations. Parking revenues are parking fees collected from all public parking facilities at the Airport. Transportation revenues are ground transportation trip fees assessed to commercial vehicles that service the Airport.

(m) Net Sales and Services Revenues

Net sales and services revenues are collected for utility, security, and miscellaneous services provided to the tenants. Utility services are provided by the City. See note 11.

(n) Environmental Remediation Expenses and Recoveries

The Airport incurs costs associated with environmental remediation activities, which arise during the normal course of business. These costs are recorded as a liability when the Airport is required to perform the remediation and if the costs can be reasonably estimated. The Airport records environmental remediation cost recoveries as nonoperating revenues in the financial statements.

(o) Capital Contributions

The Airport receives federal grants for the purpose of acquisition or construction of property and equipment. These grants are recorded as capital contributions when earned generally upon expenditures of the funds.

(p) Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

(q) Reclassification

Certain amounts have been reclassified to conform to the current year presentation.

(3) Cash, Cash Equivalents, and Investments

(a) Pooled Cash and Investments

The Airport maintains operating cash, cash equivalents, investments, and certain restricted cash and investments as part of the City's pool of cash and investments. The City's investment pool is an unrated pool pursuant to investment policy guidelines established by the City Treasurer and is treated as a cash equivalent for financial reporting purposes as the Airport is able to withdraw amounts from the pool on demand without notice or penalty. The objectives of the policy are, in order of priority, preservation of capital, liquidity, and yield. The policy addresses soundness of financial institutions in which the City will deposit funds, types of investment instruments as permitted by the California Government Code and the City Treasurer policy, and the percentage of the portfolio that may be invested in certain instruments with longer terms to maturity. The Airport's unspent bond and commercial paper note proceeds are also generally invested as part of the City's investment pool.

(Continued)

The Airport's cash and investments, at fair value, held in the City's pool as of June 30, 2017 and 2016 are as follows (in thousands):

		2017	2016
Pooled cash and investments:			
Cash and investments held in City Treasury – unrestricted	$	375,593	410,358
Cash and investments held in City Treasury – restricted current		273,106	197,348
Cash and investments held in City Treasury – restricted noncurrent		315,746	259,134
Total cash and investments in City Treasury	$	964,445	866,840

The following table shows the percentage distribution of the City's pooled investments by maturity:

Investment maturities (in months)			
Under 1	**1 – less than 6**	**6 – less than 12**	**12 – 60**
20.1 %	21.2 %	18.0 %	40.7 %

(b) Cash and Investments with Fiscal Agent

The restricted assets for revenue bond reserves, debt service and costs of issuance are held by an independent bond trustee for the Airport's senior lien bonds (the Senior Trustee) and a separate independent bond trustee for the Airport's subordinate lien bonds (the Subordinate Trustee, and collectively with the Senior Trustee, the Trustees). The unrestricted assets in the debt service holding fund and the variable rate demand bond fee account are not pledged to the payment of the Airport Commission's bonds, but are held by the Senior Trustee for the convenience of the Airport Commission in the administration and investment of monies delivered to the Senior Trustee prior to the time the Airport Commission is required to make deposits into the Debt Service Fund or pay the fees of the remarketing agents for the Airport Commission's variable rate bonds, respectively.

As of June 30, 2017 and 2016, the Senior Trustee held investments for the benefit of the Airport with maturities as follows (in thousands):

Investments	Credit ratings June 30, 2017 (S&P/Moody's / Fitch)	June 30, 2017 Maturities	June 30, 2017 Fair value	June 30, 2016 Maturities	June 30, 2016 Fair value
Federal Home Loan Bank Notes	AA+/Aaa/na	—	$ —	May 30, 2017	$ 7,609
Federal Home Loan Bank Notes	AA+/Aaa/NR	October 1, 2018	22,116	—	—
Federal Home Loan Bank Notes	AA+/Aaa/NR	March 18, 2019	12,145	—	—
Federal Home Loan Bank Notes	AA+/Aaa/na	May 28, 2019	5,045	—	—
Federal Home Loan Bank Notes	AA+/Aaa/NR	June 21, 2019	10,441	—	—
Federal Home Loan Bank Notes	AA+/Aaa/NR	August 5, 2019	10,737	—	—
Federal Home Loan Bank Notes	AA+/Aaa/NR	September 26, 2019	9,107	—	—
Federal Home Loan Bank Notes	AA+/Aaa/NR	November 15, 2019	8,514	—	—
Federal National Mortgage Association Notes	AA+/Aaa/AAA	October 26, 2017	12,091	September 27, 2017	13,903
Federal National Mortgage Association Notes	AA+/Aaa/AAA	October 19, 2018	14,604	October 26, 2017	62,617
Federal National Mortgage Association Notes	AA+/Aaa/AAA	February 26, 2019	10,529	October 19, 2018	14,785
Federal National Mortgage Association Notes	AA+/Aaa/AAA	August 28, 2019	17,730	February 26, 2019	10,652
Federal National Mortgage Association Notes	AA+/Aaa/AAA	January 21, 2020	9,906	January 21, 2020	10,113
Federal National Mortgage Association Notes	AA+/Aaa/AAA	February 28, 2020	9,181	June 22, 2020	6,447
Federal National Mortgage Association Notes	AA+/Aaa/AAA	May 6, 2021	11,921	May 6, 2021	12,181
Federal National Mortgage Association Notes	AA+/Aaa/AAA	April 5, 2022	6,400	—	—
U.S. Treasury Notes	AA+/Aaa/AAA	July 31, 2017	1,970	August 31, 2016	165
U.S. Treasury Notes	AA+/Aaa/AAA	August 31, 2017	1,974	October 31, 2016	62,024
U.S. Treasury Notes	AA+/Aaa/AAA	September 30, 2017	1,973	January 31, 2016	100
U.S. Treasury Notes	AA+/Aaa/AAA	October 31, 2017	72,293	May 31, 2017	15,659
U.S. Treasury Notes	AA+/Aaa/AAA	November 30, 2017	1,866	November 30, 2018	16,127
U.S. Treasury Notes	AA+/Aaa/AAA	December 31, 2017	1,859	February 28, 2019	3,497
U.S. Treasury Notes	AA+/Aaa/AAA	January 31, 2018	1,867	April 30, 2019	14,353
U.S. Treasury Notes	AA+/Aaa/AAA	February 28, 2018	1,864	August 31, 2019	29,223
U.S. Treasury Notes	AA+/Aaa/AAA	March 31, 2018	1,865	September 30, 2019	34,042
U.S. Treasury Notes	AA+/Aaa/AAA	April 30, 2018	1,860	November 30, 2019	7,458
U.S. Treasury Notes	AA+/Aaa/AAA	May 31, 2018	1,865	February 29, 2020	18,644
U.S. Treasury Notes	AA+/Aaa/AAA	June 30, 2018	1,571	July 31, 2020	33,464
U.S. Treasury Notes	AA+/Aaa/AAA	July 31, 2018	1,576	November 30, 2020	13,621
U.S. Treasury Notes	AA+/Aaa/AAA	August 31, 2018	1,574	February 28, 2021	20,598
U.S. Treasury Notes	AA+/Aaa/AAA	September 30, 2018	1,574	—	—
U.S. Treasury Notes	AA+/Aaa/AAA	October 31, 2018	1,583	—	—
U.S. Treasury Notes	AA+/Aaa/AAA	November 30, 2018	1,580	—	—
U.S. Treasury Notes	AA+/Aaa/AAA	December 31, 2018	1,568	—	—

Investments	Credit ratings June 30, 2017 (S&P/Moody's / Fitch)	June 30, 2017 Maturities	June 30, 2017 Fair value	June 30, 2016 Maturities	June 30, 2016 Fair value
U.S. Treasury Notes	AA+/Aaa/AAA	January 31, 2019	$ 1,558	—	—
U.S. Treasury Notes	AA+/Aaa/AAA	February 28, 2019	1,558	—	—
U.S. Treasury Notes	AA+/Aaa/AAA	March 31, 2019	1,517	—	—
U.S. Treasury Notes	AA+/Aaa/AAA	May 31, 2019	10,974	—	—
U.S. Treasury Notes	AA+/Aaa/AAA	September 30, 2019	32,485	—	—
U.S. Treasury Notes	AA+/Aaa/AAA	June 30, 2020	6,296	—	—
U.S. Treasury Notes	AA+/Aaa/AAA	July 31, 2020	32,462	—	—
U.S. Treasury Notes	AA+/Aaa/AAA	November 30, 2020	13,188	—	—
U.S. Treasury Notes	AA+/Aaa/AAA	February 28, 2021	10,182	—	—
U.S. Treasury Notes	AA+/Aaa/AAA	March 31, 2021	12,594	—	—
U.S. Treasury Notes	AA+/Aaa/AAA	April 30, 2021	14,512	—	—
U.S. Treasury Notes	AA+/Aaa/AAA	July 31, 2021	5,640	—	—
U.S. Treasury Notes	AA+/Aaa/AAA	August 31, 2021	35,358	—	—
U.S. Treasury Notes	AA+/Aaa/AAA	October 31, 2021	14,359	—	—
Federal Home Loan Mortgage Corp Notes	AA+/Aaa/AAA	January 12, 2018	12,970	February 22, 2017	11,026
Federal Home Loan Mortgage Corp Notes	AA+/Aaa/AAA	July 19, 2019	9,248	January 12, 2018	13,022
Federal Home Loan Mortgage Corp Notes	AA+/Aaa/AAA	April 20, 2020	9,175	May 30, 2019	11,251
Federal Home Loan Mortgage Corp Notes	AA+/Aaa/AAA	August 12, 2021	18,316	—	—
Goldman Sachs Financial Square Treasury Obligations Fund	AAAm/Aaa/NR	—	6,822	—	6,920
Cash			35,803		1,548
Total			$ 557,766		$ 451,049

Fair Value Hierarchy

The City categorizes its fair value measurements within the fair value hierarchy established by GAAP. The hierarchy is based on the valuation inputs used to measure fair value of the assets. The inputs and techniques used for valuing securities are not necessarily an indication of risk associated with investing in those securities.

- Level 1 Inputs: Unadjusted quoted prices in active markets for identical assets or liabilities accessible to the reporting entity at the measurement date.
- Level 2 Inputs: Other than quoted prices included in Level 1 inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the asset or liability.
- Level 3 Inputs: Unobservable inputs for the asset or liability used to measure fair value to the extent that observable inputs are not available, thereby allowing for situations in which there is little, if any, market activity for the asset or liability at measurement date.

The following is a summary of the fair value hierarchy of the Airport's cash and investments with fiscal agent as of June 30, 2017 and June 30, 2016.

	Fiscal year 2017				
			Fair value measurement using		
	Fair value June 30, 2017	Investments exempt from fair value	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Unobservable inputs (Level 3)
Investments outside City Treasury:					
U.S. Treasury securities	$ 294,965	—	294,965	—	—
U.S. agencies	220,176	—	—	220,176	—
Cash and cash equivalents	35,803	35,803	—	—	—
Investments exempt from fair value*	6,822	6,822	—	—	—
Total	$ 557,766	42,625	294,965	220,176	—

* Money market funds

	Fiscal year 2016				
			Fair value measurement using		
	Fair value June 30, 2016	Investments exempt from fair value	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Unobservable inputs (Level 3)
Investments outside City Treasury:					
U.S. Treasury securities	$ 268,975	—	268,975	—	—
U.S. agencies	173,606	—	—	173,606	—
Cash and cash equivalents	1,548	1,548	—	—	—
Investments exempt from fair value*	6,920	6,920	—	—	—
Total	$ 451,049	8,468	268,975	173,606	—

* Money market funds

Investments outside the City Treasury pool consists of U.S. Treasury securities, U.S. Government Agency securities, and Money Market Funds. U.S. Treasury securities are valued using quoted prices in active markets and classified in Level 1 of the fair value hierarchy. U.S. Government Agency securities are valued using mid pricing and classified in Level 2 of the fair value hierarchy. Investments exempt from fair value treatment consist of money market mutual funds with investment holdings having maturities of one year or less at the time of purchase.

The primary objectives of the Airport's policy on investment of debt service reserve funds and debt service funds (including principal and interest accounts) held by the Trustees are safety, liquidity, and yield.

(Continued)

Safety is the foremost objective of the investment program. Investments undertaken seek to ensure the preservation of capital in the overall portfolio, the objective of which is to mitigate credit and interest rate risk.

The term of any investment is based on the cash flow needed to meet the Airport's debt service requirements. Consequently, investment of any debt service reserve funds is limited to seven years or less, and investments in any principal and interest payment accounts are to mature no later than the dates on which the principal or interest payments are due.

The Airport will maximize the retainable earnings of all bond proceeds after meeting the requirements of safety and liquidity. After these objectives are met, the Airport's investment policy will attempt to achieve net investment yield as close as practicable to each bond fund's arbitrage yield.

Funds held by the Senior Trustee in funds and accounts established under the Airport Commission's Resolution No. 91-0210 adopted on December 3, 1991, as amended and supplemented (the 1991 Master Bond Resolution), are invested in "Permitted Investments" as defined in the 1991 Master Bond Resolution.

Funds held by the Subordinate Trustee in funds and accounts established under the Airport Commission's Resolution No. 97-0146 adopted on May 20, 1997 as amended and supplemented (the 1997 Note Resolution) are invested in "Permitted Investments" as defined in the 1997 Note Resolution. Banker's Acceptances are permitted investments only for funds relating to the 1991 Master Bond Resolution. The Airport's policy on Banker's Acceptances of a banking institution requires the highest short-term rating category by at least two Rating Agencies, and Banker's Acceptances must not exceed 270 days maturity or forty percent (40%) of monies invested pursuant to the 1991 Master Bond Resolution. In addition, no more than twenty percent (20%) of monies invested pursuant to the 1991 Master Bond Resolution is to be invested in the Banker's Acceptances of any one commercial bank. The Airport had approximately $557.8 million and $451.0 million in investments held by, and in the name of, the Trustees as of June 30, 2017 and 2016, respectively.

All other funds of the Airport are invested in accordance with the (1) City Treasurer's policy and, if applicable, (2) the 1991 Master Bond Resolution or the 1997 Note Resolution, as appropriate.

(4) Grants Receivable

The Airport receives federal funding from the FAA, the TSA, and other federal agencies. Grants receivable of $5.1 million and $10.0 million as of June 30, 2017 and 2016, respectively, were based on actual costs incurred, subject to federal reimbursement limits.

In making decisions concerning the distribution of discretionary grants to an airport, the Secretary of Transportation may consider, as a militating factor, whether the Airport uses its revenues for purposes other than capital or operating costs, when those revenues exceed the amount used by the Airport for such costs in the base year ending June 30, 1995 as adjusted for inflation. The Airport Commission pays a portion of the Airport's revenues to the City's General Fund as an annual service payment, in part as compensation for all indirect services, management and facilities provided by the City to the Airport. The annual service payment is considered to be a noncapital, nonoperating cost for this purpose. For the past

(Continued)

ten fiscal years, the annual service payment has exceeded the inflation-adjusted base year payment when adjusted for inflation. The Airport Commission uses discretionary grants from the FAA to offset a portion of the costs of various capital projects at the Airport. In the federal fiscal year ended September 30, 2014, the FAA provided discretionary grants of $38.6 million, $11.9 million less than the Airport had requested, as a result of the amount of the annual service payment. In federal fiscal year ended September 30, 2015, the Airport did not apply for any discretionary grants. The Commission received $12.4 million in FAA discretionary grants in the federal fiscal year ended September 30, 2016, $15.3 million less than the Commission requested, as a result of the amount of the annual service payment. The Commission did not receive FAA discretionary grants in the federal fiscal year ending September 30, 2017. The FAA may further reduce discretionary grants in the future. The reduction in discretionary grants awarded to the Airport increases by a corresponding amount the capital expenditures that the Airport Commission needs to fund from other sources, including operating revenues, PFCs and bond proceeds.

Project costs are subject to audit by the funding agencies to ensure that the costs are allowable under the grant agreements. If any project costs are disallowed, amounts recorded as grants receivable will be reduced or refunded to the respective funding agencies.

In fiscal years 2009 and 2010, the Airport was awarded two grants under the American Recovery and Reinvestment Act of 2009 (ARRA) totaling $14.5 million from the FAA in the DOT for runway improvements. The Office of Inspector General (OIG) for the DOT has audited ARRA grants for several airports nationwide, including these two grants received by the Airport.

The initial OIG audit of the DOT concluded in fiscal year 2012 that several Airport expenditures of the two FAA ARRA grants were questionable because of inadequate documentation, work outside the approved scope for otherwise eligible projects, and nonqualifying expenditures. These Airport expenditures were made on contracts with expenditures that were also reimbursed by two other FAA AIP grants. In fiscal year 2014 and fiscal year 2015, the Airport repaid approximately $1.1 million of the two ARRA grant reimbursements and $0.6 million of other AIP grant reimbursements. Following an internal review, the Airport identified an additional $0.5 million of ineligible ARRA grant reimbursements and an additional $0.4 million of ineligible other AIP grant reimbursements that were repaid to the FAA in December 2015. The Airport received closeout letters from the FAA for the FAA ARRA grants and the other AIP grants in January 2016.

(5) Capital Assets

Capital assets consist of the following (in thousands):

Fiscal Year 2017

		July 1, 2016	Additions	Deletions	June 30, 2017
Capital assets not being depreciated:					
Land	$	3,074	—	—	3,074
Intangible assets		6,881	—	—	6,881
Construction in progress		286,228	398,713	(145,672)	539,269
Total capital assets not being depreciated		296,183	398,713	(145,672)	549,224
Capital assets being depreciated/amortized:					
Buildings, structures, and improvements		6,109,994	219,192	(62,092)	6,267,094
Equipment		290,644	39,067	(11,079)	318,632
Intangible assets		144,982	8,855	(41,900)	111,937
Total capital assets being depreciated/amortized		6,545,620	267,114	(115,071)	6,697,663
Less accumulated depreciation/amortization:					
Buildings, structures, and improvements		(2,518,350)	(226,245)	48,235	(2,696,360)
Equipment		(148,411)	(33,089)	7,646	(173,854)
Intangible assets		(129,406)	(6,507)	41,869	(94,044)
Total accumulated depreciation/amortization		(2,796,167)	(265,841)	97,750	(2,964,258)
Total capital assets being depreciated/amortized, net		3,749,453	1,273	(17,321)	3,733,405
Total capital assets, net	$	4,045,636	399,986	(162,993)	4,282,629

Total interest costs were approximately $219.2 million for fiscal year 2017 and $216.3 million for fiscal year 2016, of which approximately $8.8 million and $7.7 million, respectively, were capitalized.

In fiscal year 2007, the Airport adopted a cost allocation plan to capture indirect costs as a component of a building or other capital asset to reflect the full and true cost of a capital asset. In accordance with the Uniform Guidance, the indirect costs capitalized for the years ended June 30, 2017 and 2016, were $18.1 million and $14.6 million, respectively.

Fiscal Year 2016

	July 1, 2015	Additions	Deletions	June 30, 2016
Capital assets not being depreciated:				
Land	$ 3,074	—	—	3,074
Intangible assets	6,881	—	—	6,881
Construction in progress	359,799	244,488	(318,059)	286,228
Total capital assets not being depreciated	369,754	244,488	(318,059)	296,183
Capital assets being depreciated/amortized:				
Buildings, structures, and improvements	5,743,103	388,378	(21,487)	6,109,994
Equipment	272,083	29,647	(11,086)	290,644
Intangible assets	142,332	2,650	—	144,982
Total capital assets being depreciated/amortized	6,157,518	420,675	(32,573)	6,545,620
Less accumulated depreciation/amortization:				
Buildings, structures, and improvements	(2,339,995)	(190,618)	12,263	(2,518,350)
Equipment	(127,510)	(31,676)	10,775	(148,411)
Intangible assets	(123,341)	(6,065)	—	(129,406)
Total accumulated depreciation/amortization	(2,590,846)	(228,359)	23,038	(2,796,167)
Total capital assets being depreciated/amortized, net	3,566,672	192,316	(9,535)	3,749,453
Total capital assets, net	$ 3,936,426	436,804	(327,594)	4,045,636

(6) Subordinate Commercial Paper Notes

On May 20, 1997, the Airport Commission adopted Resolution No. 97-0146, as amended and supplemented (the 1997 Note Resolution), authorizing the issuance of subordinate commercial paper (CP) notes in an aggregate principal amount not to exceed the lesser of $400.0 million or the stated amount of the letter(s) of credit securing the CP. On November 1, 2016, the Airport Commission adopted Resolution No. 16-0275, which amended the 1997 Note Resolution to increase the authorized maximum aggregate principal amount by $100.0 million, from $400.0 million to $500.0 million.

The Airport issues CP in series based on tax status that are divided into subseries according to the bank providing the applicable direct-pay letter of credit. In addition to the applicable letter of credit, the CP notes are further secured by a pledge of the Net Revenues of the Airport, subject to the prior payment of the Commission’s San Francisco International Airport Second Series Revenue Bonds (the Senior Bonds) outstanding from time to time under Resolution No. 91-0210, adopted by the Commission on December 3, 1991, as amended and supplemented (the 1991 Master Bond Resolution).

Net Revenues are generally defined in the 1997 Note Resolution as all revenues earned by the Commission from or with respect to its construction, possession, management, supervision, maintenance, extension, operation, use and control of the Airport (not including certain amounts specified in the 1997 Note Resolution), less Operation and Maintenance Expenses (as defined in the 1997 Note Resolution). See note 8.

The CP notes are special, limited obligations of the Commission, and the payment of the principal of and interest on the CP notes is secured by a pledge of, lien on and security interest in the Net Revenues and amounts in the funds and accounts as provided in the 1997 Note Resolution, subject to the prior payment of principal of and interest on the Senior Bonds. The CP notes are secured on a parity with any other bonds or other obligations from time to time outstanding under the 1997 Note Resolution.

Fiscal Year 2017

During fiscal year 2017, the CP program was supported by two $100.0 million principal amount direct-pay letters of credit issued by State Street Bank and Trust Company and Wells Fargo Bank, National Association, which, as of June 30, 2017, had expiration dates of May 2, 2019, and May 31, 2019, respectively; a third letter of credit issued by Royal Bank of Canada in the principal amount of $200.0 million that was amended on May 4, 2017, to extend its expiration date from May 19, 2017 to May 1, 2020; and a new letter of credit issued on June 22, 2017, by Sumitomo Mitsui Banking Corporation, acting through its New York Branch, in the principal amount of $100.0 million and with an expiration date of June 21, 2022. Each of the letters of credit supports separate subseries of CP. In the aggregate the letters of credit permit the Airport to issue CP up to a combined maximum principal amount of $500.0 million as of June 30, 2017.

As of June 30, 2017, there were no obligations other than the CP notes outstanding under the 1997 Note Resolution.

During fiscal year 2017, the Airport issued new money CP in the amount of $67.0 million (AMT) and $111.0 million (Non-AMT) to fund capital improvement projects. The Airport also issued and retired $1.0 million of new money CP (taxable) during fiscal year 2017, to fund costs related to various bond and note transactions.

The following table summarizes the activity of CP (excluding refunding CP) during the fiscal year ended June 30, 2017 (in thousands):

	Interest rate	July 1, 2016	Increases	Decreases	June 30, 2017
Commercial paper (Taxable)	0.90 %	$ —	1,000	(1,000)	—
Commercial paper (AMT)	0.36%–1.01%	320,350	67,000	(320,350)	67,000
Commercial paper (Non-AMT)	0.46%–0.99%	22,700	111,000	(22,700)	111,000
Total		$ 343,050	179,000	(344,050)	178,000

Fiscal Year 2016

During fiscal year 2016, the CP program was supported by two $100.0 million principal amount direct-pay letters of credit issued by State Street Bank and Trust Company and Wells Fargo Bank, National Association, which, as of June 30, 2016, had expiration dates of May 2, 2019, and May 31, 2019, respectively, and a third letter of credit issued by Royal Bank of Canada in the principal amount of $200.0 million that, as of June 30, 2016, had an expiration date of May 19, 2017. Each of the letters of credit supports separate subseries of CP and permits the Airport to issue CP up to a combined maximum principal amount of $400.0 million as of June 30, 2016.

As of June 30, 2016, there were no obligations other than the CP notes outstanding under the 1997 Note Resolution.

During fiscal year 2016, the Airport issued $280.4 million of new money CP (AMT) and $22.7 million (Non-AMT) to fund capital improvement projects. The Airport also issued and retired $1.1 million of new money CP (taxable) during fiscal year 2016, to fund costs related to various bond and note transactions.

The following table summarizes the activity of CP (excluding refunding CP) during the fiscal year ended June 30, 2016 (in thousands):

	Interest rate	July 1, 2015	Increases	Decreases	June 30, 2016
Commercial paper (Taxable)	0.55 %	$ —	1,050	(1,050)	—
Commercial paper (AMT)	0.02%–0.58%	40,000	280,350	—	320,350
Commercial paper (Non-AMT)	0.05%–0.52%	—	22,700	—	22,700
Total		$ 40,000	304,100	(1,050)	343,050

(7) Long-Term Obligations

Long-term obligation activity for the years ended June 30, 2017 and 2016, was as follows (in thousands):

	July 1, 2016	Additions	Reductions	June 30, 2017	Due within one year
Revenue bonds payable	$ 4,234,725	887,920	(365,115)	4,757,530	203,580
Less unamortized discounts	(271)	—	9	(262)	—
Add unamortized premiums	195,222	168,368	(35,198)	328,392	—
Total revenue bonds payable	4,429,676	1,056,288	(400,304)	5,085,660	203,580
Compensated absences	17,039	13,525	(13,547)	17,017	9,845
Accrued workers' compensation	6,657	3,095	(2,416)	7,336	1,520
Estimated claims payable	1,477	174	(796)	855	777
Other postemployment benefits obligation	124,352	13,816	—	138,168	—
Net pension liability (see note 10a)	144,271	215,328	—	359,599	—
Derivative instruments	96,132	—	(30,167)	65,965	—
Total	$ 4,819,604	1,302,226	(447,230)	5,674,600	215,722

	July 1, 2015	Additions	Reductions	June 30, 2016	Due within one year
Revenue bonds payable	$ 4,496,390	232,075	(493,740)	4,234,725	194,125
Less unamortized discounts	(279)	—	8	(271)	—
Add unamortized premiums	168,784	51,219	(24,781)	195,222	—
Total revenue bonds payable	4,664,895	283,294	(518,513)	4,429,676	194,125
Compensated absences	16,293	13,493	(12,747)	17,039	9,714
Accrued workers' compensation	6,081	2,654	(2,078)	6,657	1,413
Estimated claims payable	3,772	108	(2,403)	1,477	1,346
Other postemployment benefits obligation	115,297	9,055	—	124,352	—
Net pension liability (see note 10a)	111,932	32,339	—	144,271	—
Derivative instruments	79,321	16,811	—	96,132	—
Total	$ 4,997,591	357,754	(535,741)	4,819,604	206,598

Bond Transactions and Balances

On December 3, 1991, the Commission adopted Resolution No. 91-0210, as amended and supplemented (the 1991 Master Bond Resolution), authorizing the issuance from time to time of San Francisco International Airport Second Series Revenue Bonds to finance capital projects at the Airport. The maximum principal amount of such bonds is not limited by the 1991 Master Bond Resolution, but the Commission must satisfy an additional bonds test prior to the issuance of any such bonds. The 1991 Master Bond Resolution constitutes a contract between the Commission and the registered owners of the bonds under which the Commission has irrevocably pledged the Net Revenues of the Airport to the payment of the principal of and interest on the bonds.

Net Revenues are generally defined in the 1991 Master Bond Resolution as all revenues earned by the Commission from or with respect to its construction, possession, management, supervision, maintenance, extension, operation, use and control of the Airport (not including certain amounts specified in the 1991 Master Bond Resolution), less Operation and Maintenance Expenses (as defined in the 1991 Master Bond Resolution). See note 8.

The bonds are special, limited obligations of the Commission, and the payment of the principal of and interest on the bonds is secured by a pledge of, lien on and security interest in the Net Revenues and amounts in the funds and accounts provided in the 1991 Master Bond Resolution. The payment of the principal of and interest on all previously issued bonds under the 1991 Master Bond Resolution is secured by a pledge of, lien on and security interest in Net Revenues on a parity with the pledge, lien and security interest securing any additional bonds issued thereunder.

As of June 30, 2017 and 2016, long-term revenue bonds consisted of the following (in thousands):

Description	Date of issue	Interest rate	2017	2016
Second Series Revenue Bonds:				
Issue 31F	01/26/05	4.91 %	$ —	6,385
Issue 32F	11/16/06	5.25 %	103,475	134,200
Issue 34C/D/E/F*	03/27/08	5.00%–5.75%	157,800	199,825
Issue 36A	06/03/09	Variable rate	93,130	100,000
Issue 36B	06/03/09	Variable rate	37,820	40,620
Issue 36C	06/03/09	Variable rate	33,655	36,145
Issue 37C	06/03/09	Variable rate	86,930	88,650
Issue 2009A/B	09/03/09	4.90 %	175,000	175,000
Issue 2009C	11/03/09	3.88%–5.00%	40,925	51,295
Issue 2009D	11/04/09	2.50%–4.00%	81,870	83,490
Issue 2009E	11/18/09	4.38%–6.00%	485,800	485,800
Issue 2010A	02/10/10	Variable rate	209,240	212,475
Issue 2010C	04/07/10	3.00%–5.00%	171,545	251,615
Issue 2010D	04/07/10	3.00%–5.00%	55,550	65,390
Issue 2010F	08/05/10	5.00 %	121,360	121,360
Issue 2010G	08/05/10	5.00 %	7,100	7,100
Issue 2011A	02/22/11	5.00%–5.75%	23,915	37,130
Issue 2011B	02/22/11	5.00%–5.50%	24,100	29,295
Issue 2011C	07/21/11	5.00 %	163,720	163,720
Issue 2011D	07/21/11	5.00 %	84,865	124,110
Issue 2011E	07/21/11	3.43%–4.48%	12,760	19,720

Description	Date of issue	Interest rate		2017	2016
Issue 2011F	09/20/11	5.00 %	$	123,325	123,325
Issue 2011G	09/20/11	5.00%–5.25%		29,660	106,195
Issue 2011H	09/20/11	2.74%–4.15%		66,195	88,780
Issue 2012A	03/22/12	5.00 %		208,025	208,025
Issue 2012B	03/22/12	4.00%–5.00%		108,265	108,265
Issue 2013A	07/31/13	5.00%–5.50%		360,785	360,785
Issue 2013B	07/31/13	5.00 %		87,860	87,860
Issue 2013C	07/31/13	2.12%–2.86%		9,350	12,480
Issue 2014A	09/24/14	5.00 %		376,320	376,320
Issue 2014B	09/24/14	5.00 %		97,290	97,290
Issue 2016A	02/25/16	3.00%–5.00%		232,075	232,075
Issue 2016B	09/29/16	5.00 %		574,970	—
Issue 2016C	09/29/16	5.00 %		165,155	—
Issue 2016D	09/29/16	5.00 %		147,695	—
				4,757,530	4,234,725
Unamortized discount				(262)	(271)
Unamortized premium				328,392	195,222
Total revenue bonds payable				5,085,660	4,429,676
Less current portion				(203,580)	(194,125)
Total long-term revenue bonds payable			$	4,882,080	4,235,551

* As of June 30, 2017, Issue 34C/F was no longer outstanding.

Fiscal Year 2017

(a) Second Series Revenue Bonds (Capital Plan Bonds)

Pursuant to resolutions approved in fiscal years 2008, 2012, 2014, 2016, and 2017, the Airport Commission has authorized the issuance of up to $7.8 billion of San Francisco International Airport Second Series Revenue Bonds (Capital Plan Bonds) to finance and refinance the construction, acquisition, equipping, and development of capital projects undertaken by the Airport, including retiring all or a portion of the Airport's outstanding subordinate commercial paper notes issued for capital projects, funding debt service reserves, and for paying costs of issuance. As of June 30, 2017, $5.5 billion of the authorized capital plan bonds remained unissued.

On-Airport Hotel Second Series Revenue Bonds and Related Special Facility Bonds

Pursuant to resolutions adopted in fiscal years 2016 and 2017, the Airport Commission has authorized the issuance of $278.0 million of San Francisco International Airport Second Series Revenue Bonds (Capital Plan Bonds) and $260.0 million of San Francisco International Airport Hotel Special Facility Revenue Bonds to finance the development and construction of a new Airport-owned hotel and related

AirTrain station. The Commission also designated the planned hotel as a “special facility” under the 1991 Master Bond Resolution, which will allow the hotel revenues to be segregated from the Airport’s other revenues and used to pay hotel operating expenses and debt service on the Hotel Special Facility Bonds. In order to obtain the lowest cost of financing, the Commission does not plan to sell the Hotel Special Facility Bonds to investors, but will purchase them itself with a portion of the proceeds of Capital Plan Bonds, which will be sold to investors. The total net proceeds of the two bond issuances are expected to be approximately $278.0 million, which will be applied to the $255.0 million construction costs of the hotel and AirTrain station, capitalized interest on the Hotel Special Facility Bonds and other costs of issuance. In fiscal years 2016 and 2017, the City’s Board of Supervisors authorized the issuance of such Hotel Special Facility Bonds and Capital Plan Bonds for the hotel and AirTrain station. Airport Commission approval of the bond sale is required before such bonds can be issued.

Second Series Revenue Bonds, Series 2016B/C

On September 29, 2016, the Airport issued its long-term, fixed rate Second Series Revenue Bonds (Capital Plan Bonds), Series 2016B (AMT) and 2016C (Non-AMT/Governmental Purpose) in the aggregate principal amount of $740.1 million, to finance and refinance (through the repayment of commercial paper notes) the following projects, among others: (a) redevelopment of Terminal 1 including construction of an interim Boarding Area B and the design and construction of a new 24-gate Boarding Area B facility, (b) relocation of a firehouse and vehicle security checkpoint to accommodate the expansion of Boarding Area B and the related realignment of Taxiways H and M, (c) relocation of ground transportation facilities to accommodate the expansion of Boarding Area B, (d) construction of a new administration campus to consolidate some Airport administrative departments, (e) upgrades to operating systems-related components for the AirTrain extension, (f) gate enhancements to accommodate larger aircraft and address demand-driven gate needs, and (g) various technology improvements to upgrade network services.

(b) Second Series Revenue Refunding Bonds

Pursuant to resolutions adopted between fiscal years 2005 through 2016, the Airport Commission has authorized the issuance of up to $8.4 billion of San Francisco International Airport Second Series Revenue Refunding Bonds for the purposes of refunding outstanding 1991 Master Bond Resolution Bonds and outstanding subordinate commercial paper notes, funding debt service reserves, and paying costs of issuance, including any related bond redemption premiums.

As of June 30, 2017, $1.0 billion of such refunding bonds remained authorized but unissued.

During fiscal year 2017, the Airport issued the following new refunding bonds under the 1991 Master Bond Resolution:

Second Series Revenue Refunding Bonds, Series 2016D

On September 29, 2016, the Airport issued its Second Series Revenue Refunding Bonds, Series 2016D (Non-AMT/Governmental Purpose), in the principal amount of $147.8 million to advance refund and legally defease long-term fixed rate Series 2010C, 2011D, and 2011G bonds. The Series 2016D Bonds bear interest at a fixed rate of 5.0%, and have a final maturity of May 1, 2031.

The net proceeds of $188.1 million (consisting of the $147.8 million par amount of the Series 2016D Bonds, original issue premium of $37.0 million, and $3.3 million accumulated in the debt service fund relating to the refunded bonds) were used to pay $0.3 million underwriter's discount and $0.2 million in costs of issuance and deposit $187.6 million into irrevocable escrow funds with the Senior Trustee to defease and refund $158.0 million in revenue bonds as described below.

		Amount refunded	Interest rate	Redemption price
Second Series Revenue Bond Issue:				
2010C (Non-AMT)	$	42,210,000	4.00%–5.00%	100 %
2011D (Non-AMT)		39,245,000	5.00 %	100 %
2011G (Non-AMT)		76,535,000	5.00%–5.25%	100 %
Total	$	157,990,000		

The refunded bonds were legally defeased and scheduled for redemption on May 1, 2020 (Series 2010C) and May 3, 2021 (Series 2011D and Series 2011G). Accordingly, the liability for these bonds has been removed from the accompanying statements of net assets.

The refunding resulted in the recognition of a deferred accounting gain of $0.2 million for fiscal year ended June 30, 2017. The Airport reduced its aggregate debt service payments by approximately $15.0 million over the next fourteen years and obtained an economic gain (the difference between the present values of the old debt and the new debt) of $13.5 million.

(c) Variable Rate Demand Bonds

As of June 30, 2017, the Airport Commission had outstanding an aggregate principal amount of $460.8 million of Second Series Variable Rate Revenue Refunding Bonds, consisting of Issue 36A/B/C, Issue 37C, and Series 2010A (collectively, the "Variable Rate Bonds"), with final maturity dates of May 1, 2026 (Issue 36A/B/C), May 1, 2029 (Issue 37C), and May 1, 2030 (Series 2010A). The Variable Rate Bonds are long-term, tax-exempt bonds that currently bear interest at a rate that is adjusted weekly, and that are subject to tender at par at the option of the holder thereof on seven days' notice. Any tendered Variable Rate Bonds are remarketed by the applicable remarketing agent in the secondary market to other investors. The interest rate on the Variable Rate Bonds can be converted to other interest rate modes, including a term rate or fixed rates to maturity, upon appropriate notice by the Airport.

The scheduled payment of the principal of and interest on, and payment of purchase price of, the Variable Rate Bonds is secured by separate irrevocable letters of credit issued to the Senior Trustee for the benefit of the applicable bondholders by the banks identified in the table below.

Amounts drawn under a letter of credit that are not reimbursed by the Airport constitute "Repayment Obligations" under the 1991 Master Bond Resolution and are accorded the status of other outstanding bonds to the extent provided in the Resolution. The commitment fees for the letters of credit range between 0.45% and 0.63% per annum. As of June 30, 2017, there were no unreimbursed draws under these facilities.

The letters of credit securing the Variable Rate Bonds included in long-term debt as of June 30, 2017, are as follows:

	Issue 36A	Issue 36B	Issue 36C	Issue 37C	Series 2010A
Principal amount	$ 93,130,000	37,820,000	33,655,000	86,930,000	209,240,000
Expiration date	June 29, 2018	April 25, 2018	April 25, 2018	January 28, 2019	June 29, 2020
Credit provider	Wells Fargo(1)	BTMU(2)	BTMU(2)	MUFG Union Bank (3)	Bank of America(4)

(1) Wells Fargo Bank, National Association
(2) The Bank of Tokyo-Mitsubishi UFJ. Ltd.
(3) Formerly Union Bank, N.A.
(4) Bank of America, National Association

(d) Interest Rate Swaps

Objective and Terms – On December 16, 2004, the Airport entered into seven forward starting interest rate swaps (the 2004 swaps) with an aggregate notional amount of $405.0 million, in connection with the anticipated issuance of Second Series Variable Rate Revenue Refunding Bonds, Issues 32A-E on February 10, 2005, and Second Series Variable Rate Revenue Refunding Bonds, Issue 33 on February 15, 2006. The swap structure was intended as a means to increase the Airport's debt service savings when compared with fixed rate refunding bonds at the time of issuance. The expiration date of the 2004 swaps is May 1, 2026.

On July 26, 2007, the Airport entered into four additional forward starting interest rate swaps in connection with the anticipated issuance of its Second Series Variable Rate Revenue Refunding Bonds, Issue 37B/C, on May 15, 2008 (the 2007 swaps), and Second Series Variable Rate Revenue Refunding Bonds, Series 2010A, on February 10, 2010 (the 2010 swaps). The expiration dates of the 2007 and 2010 swaps are May 1, 2029 and 2030, respectively.

In the spring of 2008, the Airport refunded several issues of auction rate and variable rate bonds, including Issue 32 and Issue 33. The 2004 swaps associated with these issues then became associated with the Second Series Variable Rate Revenue Refunding Bonds, Issues 36A-D, and Issue 37A. Subsequently, on October 30, 2008 and December 3, 2008, the Airport refunded Issue 37A and Issue 37B, respectively. Concurrently with the refunding of Issue 37A, the three associated swaps with an aggregate notional amount of $205.1 million were terminated. The swap associated with Issue 37B was not terminated upon the refunding of Issue 37B.

On December 16, 2010, the Airport terminated a swap with Depfa Bank plc associated with the Series 2010A-3 Bonds, with a notional amount of $72.0 million.

Following the termination of the Depfa swap, the Series 2010A-3 Bonds, which are variable rate, were no longer hedged with an interest rate swap. However, the swap associated with the Issue 37B Bonds is now indirectly hedging the Series 2010A-3 Bonds for accounting purposes. As a practical matter, the swap associated with the Issue 37B Bonds also serves as an indirect hedge on the unhedged portions of the Issue 36B and Issue 36C Bonds, when viewed alongside the Airport's other swaps, and only to the extent that the swap's notional amount exceeds the outstanding amount of the Series 2010A-3 Bonds.

On September 20, 2011, the Airport refunded the Issue 36D Bonds with proceeds of the San Francisco International Airport Second Series Revenue Refunding Bonds, Series 2011H and terminated the swap with JP Morgan Chase Bank, N.A., associated with Issue 36D, which had an initial notional amount of $30.0 million. The Airport paid a termination fee of $4.6 million to the counterparty.

Under the 2004 swaps, the Airport receives a monthly variable rate payment from each counterparty equal to 63.50% of USD-LIBOR-BBA plus 0.29%. Under the 2007 and 2010 swaps, the Airport receives 61.85% of USD-LIBOR-BBA plus 0.34%. These payments are intended to approximate the variable interest rates on the bonds originally hedged by the swaps. The Airport makes a monthly fixed rate payment to the counterparties as set forth below which commenced on the date of issuance of the related bonds. The objective of the swaps is to achieve a synthetic fixed rate with respect to the hedged bonds. All of the outstanding interest rate swaps are terminable at any time upon making a market-based termination payment solely at the option of the Airport.

As of June 30, 2017, the Airport's derivative instruments comprised of six interest rate swaps that the Airport entered into to hedge the interest payments on several series of its variable rate Second Series Revenue Bonds. The Airport determined the hedging relationship between the variable rate bonds and the related interest rate swaps continued to be effective as of June 30, 2017.

No.	Current bonds		Initial notional amount	Notional amount June 30, 2017	Effective date
1	36AB	$	70,000,000	65,170,000	2/10/2005
2	36AB		69,930,000	65,135,000	2/10/2005
3	36C		30,000,000	27,930,000	2/10/2005
4	2010A (37B)*		79,684,000	77,061,000	5/15/2008
5	37C		89,856,000	86,899,000	5/15/2008
6	2010A**		143,947,000	140,230,000	2/1/2010
	Total	$	483,417,000	462,425,000	

* The Issue 37B Bonds that are hedged by this swap agreement were purchased with proceeds of the Series 2008B Notes, which the Commission subsequently refunded, and the Issue 37B Bonds are held in trust. The swap is now indirectly hedging the Series 2010A-3 Bonds for accounting purposes.

** Hedges Series 2010A-1 and 2010A-2.

Fair Value

The fair values take into consideration the prevailing interest rate environment and the specific terms and conditions of each swap. All values were estimated using the zero-coupon discounting method. This method calculates the future payments required by the swap, assuming that the current forward rates implied by the yield curve are the market's best estimate of future spot interest rates. These payments are then discounted using the spot rates implied by the current yield curve for a hypothetical zero-coupon rate bond due on the date of each future net settlement payment on the swaps to arrive at the so-called "settlement amount", i.e., the approximate amount a party would have to pay or would receive if the swap was terminated.

In addition, pursuant to GASB 72, the settlement amounts are then adjusted for the nonperformance risk of each party to the swap to arrive at the fair value. For each swap, the nonperformance risk was computed as the total cost of the transactions required to hedge the default exposure, i.e., a series of European swaptions, exercisable on each of the future payment exchange dates under the swap that are structured to reverse the remaining future cash flow obligations as of such dates, adjusted by probability of default on each future date. Default probabilities were derived from recovery rate adjusted credit default swap quotes or generic ratings based borrowing curves that fall into Level 2 of the GASB 72 fair value hierarchy.

As of June 30, 2017, the fair value of the Airport's six outstanding swaps, counterparty credit ratings, and fixed rate payable by the Airport Commission are as follows:

No.	Current bonds	Counterparty/guarantor*	Counterparty credit ratings (S&P/Moody's/ Fitch)	Fixed rate payable by Commission	Fair value to Commission
1	36AB	J.P. Morgan Chase Bank, N.A.	A+/Aa3/AA-	3.444 %	$ (5,509,894)
2	36AB	J.P. Morgan Chase Bank, N.A.	A+/Aa3/AA-	3.445	(5,513,321)
3	36C	J.P. Morgan Chase Bank, N.A.	A+/Aa3/AA-	3.444	(2,362,561)
4	2010A (37B)**	Merrill Lynch Capital Services, Inc./ Merrill Lynch Derivative Products AG	AA/Aa3/NR*	3.773	(12,652,178)
5	37C	J.P. Morgan Chase Bank, N.A.	A+/Aa3/AA-	3.898	(14,581,404)
6	2010A***	Goldman Sachs Bank USA/ Goldman Sachs Group, Inc.	BBB+/A3/A*	3.925	(25,345,773)
		Total			$ (65,965,131)

* Reflects ratings of the guarantor.

** The Issue 37B Bonds that are hedged by this swap agreement were purchased with proceeds of the Series 2008B Notes, which the Commission subsequently refunded, and the Issue 37B Bonds are held in trust. The swap is now indirectly hedging the Series 2010A-3 Bonds for accounting purposes.

*** Hedges Series 2010A-1 and 2010A-2.

Fair Value Hierarchy

		Fair value June 30, 2017	Fair value measurements using significant other observable inputs (Level 2)
Interest rate swaps	$	(65,965,131)	(65,965,131)

Change in Fair Value

The impact of the interest rate swaps on the financial statements for the year ended June 30, 2017 is as follows (in thousands):

		Deferred outflows on derivative instruments	Derivative instruments
Balance as of June 30, 2016	$	83,614	96,132
Change in fair value to year end		(28,744)	(30,167)
Balance as of June 30, 2017	$	54,870	65,965

The fair value of the interest rate swap portfolio is recorded as a liability (since the Airport would owe a termination payment to the counterparty) in the statements of net position. Unless a swap was determined to be an off-market swap at the inception of its hedging relationship, the fair value of the swap is recorded as a deferred outflow asset (if a termination payment would be due to the counterparty) or inflow liability (if a termination payment would be due to the Airport). The off-market portions of the Airport's swaps are recorded as carrying costs with respect to various refunded bond issues. Unlike fair value and deferred inflow/outflow values, the balance of remaining off-market portions are valued on a present value, or fixed yield, to maturity basis. The difference between the deferred outflows and derivative instruments presented in the table above constitutes the unamortized off-market portions of the swaps as of June 30, 2017.

Risks

Basis Risk – The Airport has chosen a variable rate index based on a percentage of London Interbank Offered Rate (LIBOR) plus a spread, which historically has closely approximated the variable rates payable on the related bonds. However, the Airport is subject to the risk that a change in the relationship between the LIBOR-based swap rate and the variable bond rates would cause a material mismatch between the two rates. Changes that cause the payments received from the counterparty to be insufficient to make the payments due on the associated bonds result in an increase in the synthetic interest rate on the bonds, while changes that cause the counterparty payments to exceed the payments due on the associated bonds result in a decrease in the synthetic interest rate on the bonds.

During the fiscal year ended June 30, 2017, the Airport paid a total of $0.6 million less in interest on its variable rate bonds than the floating-rate payments it received from the swap counterparties, resulting in a decrease in the effective synthetic interest rates on the associated bonds.

Credit Risk – As of June 30, 2017, the Airport is not exposed to credit risk because the swaps have a negative fair value to the Airport. Should long-term interest rates rise and the fair value of the swaps become positive, the Airport would be exposed to credit risk in the amount of the swaps' fair value. Under the terms of the swaps, counterparties are required to post collateral consisting of specified U.S. Treasury and Agency securities in an amount equal to the market value of a swap that exceeds specified thresholds linked to the counterparty's credit ratings. Any such collateral will be held by a custodial bank.

Counterparty Risk – The Airport is exposed to counterparty risk, which is related to credit and termination risk. While the insolvency or bankruptcy of a counterparty, or its failure to perform would be a default under the applicable swap documents, none of the Airport's swaps would automatically terminate. Rather, the Airport would have the option to terminate the affected swap at a market-based termination value, which may result in a payment to or from the counterparty. The Airport may also be exposed to counterparty risk in a high interest rate environment in the event a counterparty is unable to perform its obligations on a swap transaction leaving the Airport exposed to the variable rates on the associated debt. In order to diversify the Airport's swap counterparty credit risk and to limit the Airport's credit exposure to any one counterparty, the Airport's swap policy imposes limits on the maximum net termination exposure to any one counterparty. Maximum net termination exposure is calculated as of the date of execution of each swap and is monitored regularly during the term of the swap. The exposure limits vary for collateralized and noncollateralized swaps based upon the credit rating of the counterparty. If any exposure limit is exceeded by a counterparty during the term of a swap, the Airport Director is required to consult with the Airport's swap advisor and bond counsel regarding appropriate actions to take, if any, to mitigate such increased exposure, including, without limitation, transfer or substitution of a swap. As of June 30, 2017, the fair value of the Airport's swaps was negative to the Airport (representing an amount payable by the Airport to each counterparty in the event the relevant swap was terminated).

(Continued)

Termination Risk – All of the interest rate swaps are terminable at their termination price at any time at the option of the Airport. The Airport has limited termination risk with respect to the interest rate swaps. That risk would arise primarily from certain credit-related events or events of default on the part of the Airport, the municipal swap insurer, or the counterparty. The Airport has secured municipal swap insurance for all its regular payments and some termination payments due under all its interest rate swaps, except the swaps associated with the Series 2010A Bonds, from the following insurers:

No.	Swap	Swap insurer	Insurer credit ratings June 30, 2017 (S&P/Moody's/Fitch)
1	Issue 36AB	FGIC/National Public Finance Guarantee Corporation	A/A3/NR
2	Issue 36AB	FGIC/National Public Finance Guarantee Corporation	A/A3/NR
3	Issue 36C	Assured Guaranty Municipal Corp.	AA/A2/NR
4	Series 2010A (37B)	Assured Guaranty Municipal Corp.	AA/A2/NR
5	Issue 37C	Assured Guaranty Municipal Corp.	AA/A2/NR
6	Series 2010A	None	N/A

If the Airport is rated between Baa1/BBB+ and Baa3/BBB- (Moody's/S&P), and the applicable bond insurer is rated below A3/A- (Moody's/S&P), the counterparties may terminate the swaps and require the Airport to pay the termination value, if any, unless the Airport chooses to provide suitable replacement credit enhancement, assign the Airport's interest in the swaps to a suitable replacement counterparty, or post collateral to secure the swap termination value. If the Airport is rated below Baa3/BBB- (Moody's/S&P) or its ratings are withdrawn or suspended, and the applicable bond insurer is rated below A3/A- (Moody's/S&P), the counterparties may terminate the swaps and require the Airport to pay the termination value, if any. With respect to the Series 2010A swaps with no swap insurance, the counterparty termination provisions and the Airport rating thresholds are the same as described above.

Additional Termination Events under the swap documents with respect to the Airport include an insurer payment default under the applicable swap insurance policy, and certain insurer rating downgrades or specified insurer nonpayment defaults combined with a termination event or event of default on the part of the Airport or a ratings downgrade of the Airport below investment grade. Additional Termination Events under the swap documents with respect to a counterparty and/or its guarantor include a rating downgrade below a specific rating threshold, followed by a failure of the counterparty to assign its rights and obligations under the swap documents to another entity acceptable to the applicable insurer within 15 business days.

On December 16, 2016, S&P upgraded the credit rating of Goldman Sachs Bank USA, the swap counterparty on the Series 2010A Swap, from "A" to "A+".

On December 23, 2016, S&P upgraded the credit rating of Merrill Lynch Derivative Products AG, the guarantor on the Issue 37B (2010A) Swap, from “AA-” to “AA”.

The downgrade of any swap counterparty is indicative of an increased risk to the Airport that such counterparty may become bankrupt or insolvent and not perform under the applicable swap. If a counterparty does not perform under its swap, the Airport may be required to continue making its fixed rate payments to the counterparty even though it does not receive a variable rate payment in return. The Airport may elect to terminate a swap with a nonperforming counterparty and may be required to pay a substantial termination payment related to the fair value of such swap, depending on market conditions at the time. As of June 30, 2017, the fair value of each swap was negative to the Airport as shown above. The risks and termination rights related to the Airport’s swaps are discussed in further detail above.

(e) Special Facilities Lease Revenue Bonds

In addition to the long-term obligations discussed above, the Commission’s San Francisco International Airport Special Facilities Lease Revenue Bonds (SFO Fuel Company LLC), Series 1997A and 2000A, were outstanding in the principal amounts of $68.2 million and $73.2 million, respectively, as of June 30, 2017 and 2016. SFO Fuel Company LLC (SFO Fuel), a special purpose limited liability company formed by certain airlines operating at the Airport, is required to pay facilities rent to the Airport pursuant to a lease agreement between the Commission and SFO Fuel with respect to the on-Airport jet fuel distribution facilities in an amount equal to debt service payments on the bonds and any required bond reserve account deposits. The principal and interest on the bonds are paid solely from the facilities rent payable by SFO Fuel to the Airport. The lease payments, and therefore the SFO Fuel bonds, are payable from charges imposed by SFO Fuel on air carriers for into-plane fueling at the Airport, and are not payable from or secured by the Net Revenues of the Airport. The Airport assigned its right to receive the facilities rent to the bond trustee to pay and secure the payment of the bonds. Neither the Airport nor the City is obligated in any manner for the repayment of the SFO Fuel bonds other than from the facilities rent received from SFO Fuel. The bonds are therefore not reported in the accompanying financial statements.

(f) Debt Service Reserve and Covenants

The Airport Commission issues its senior lien San Francisco International Airport Second Series Revenue Bonds under the 1991 Master Bond Resolution, which provides, among other things, the general terms and conditions of the bonds, the funds and accounts relating to the bonds, and certain covenants made by the Airport Commission for the benefit of bondholders. Such covenants include not creating or allowing creation of liens on its property essential to operations or disposing of any property essential to maintaining revenues or operating the Airport, and maintaining specified levels of insurance or self-insurance. The Airport Commission may also establish one or more reserve accounts with different reserve requirements to secure one or more series of bonds. Accordingly, the Airport Commission has established two reserve accounts in the Reserve Fund: the Issue 1 Reserve Account and the 2009 Reserve Account, both of which are held by the Senior Trustee.

Issue 1 Reserve Account

The Issue 1 Reserve Account is the Airport's original parity reserve account established in connection with the first issuance of bonds under the 1991 Master Bond Resolution and which now secures most of the Airport Commission's outstanding bonds. The Airport Commission may designate any series of bonds as a "participating series" secured by the Issue 1 Reserve Account. The reserve requirement is equal to the maximum annual debt service accruing in any year during the life of all participating series of bonds secured by the Issue 1 Reserve Account. As of June 30, 2017, the reserve requirement was $386.6 million, which was satisfied by $390.9 million of cash and investment securities, and reserve fund surety policies in the initial principal amount of $132.7 million. All of the providers of such reserve policies have one or more credit ratings below the Airport's rating or are no longer rated. In addition, $75.8 million of such surety policies have likely experienced a reduction in value in accordance with their terms.

2009 Reserve Account

The Airport Commission has established an additional pooled reserve account identified as the 2009 Reserve Account in the Reserve Fund, as security for each series of bonds (a 2009 Reserve Series) that is designated as being secured by the 2009 Reserve Account. Currently, only the Series 2009C and 2010D Bonds are secured by the 2009 Reserve Account. The reserve requirement for each 2009 Reserve Series is the lesser of: (i) maximum annual debt service for such series of 2009 Reserve Series Bonds, (ii) 125% of average annual debt service for such series of 2009 Reserve Series Bonds, and (iii) 10% of the outstanding principal amount of such series (or allocable issue price of such series if such series is sold with more than a de minimis (2%) amount of original issue discount), in each case as determined from time to time. With respect to all 2009 Reserve Series, the reserve requirement is the aggregate of such amounts for each individual series. As of June 30, 2017, the reserve requirement for the 2009 Reserve Account was $9.6 million, which was satisfied by $19.6 million in cash and investment securities, and a reserve policy in the principal amount of $3.4 million issued by Financial Security Assurance Inc. (now known as Assured Guaranty Municipal Corp.). The value of this reserve policy may be adjusted downward under certain circumstances and may have experienced a reduction in value.

Series Secured by Other or No Reserve Accounts

As permitted under the 1991 Master Bond Resolution, the Airport Commission may establish separate reserve accounts for individual series of bonds, or may issue bonds without a reserve account.

The Airport Commission does not maintain reserve accounts for its Second Series Variable Rate Revenue Refunding Bonds, Issue 36A/B/C and Series 2010A, all of which are secured by letters of credit.

Reserve Policies

Under the 1991 Master Bond Resolution, the Airport Commission may satisfy a portion of a reserve requirement by depositing with the Senior Trustee one or more reserve policies issued by a credit provider rated in the highest category by at least two rating agencies. However, the 1991 Master Bond Resolution does not require that those ratings be maintained after the date of deposit. Each of the providers of the reserve policies in the reserve accounts was rated “AAA” at the time the policies were deposited. However, as a result of the financial crisis that began in 2007, all of the major municipal bond insurance companies have been downgraded, and several are no longer providing current financial and operating information. In addition, under the terms of several of the reserve policies, the value of the policies may be adjusted downward from time to time as related bonds are refunded and such policies may have experienced a reduction in value. The Airport has periodically deposited additional cash in the Issue 1 Reserve Account to satisfy the reserve requirement and compensate for the diminished value or downgraded providers of these reserve policies, and, as of June 30, 2017, sufficient cash and investments were on deposit in the Issue 1 Reserve Account and the 2009 Reserve Account to satisfy the applicable reserve requirement without the reserve policies.

Rate Covenant

Under the terms of the 1991 Master Bond Resolution, the Airport has covenanted that it will establish and at all times maintain rentals, rates, fees, and charges for the use of the Airport and for services rendered by the Airport so that:

(a) Net Revenues (as defined in the 1991 Master Bond Resolution) in each fiscal year will be at least sufficient (i) to make all required debt service payments and deposits in such fiscal year with respect to the bonds, any subordinate bonds, and any general obligation bonds issued by the City for the benefit of the Airport (there have been no such general obligation bonds outstanding for more than 30 years), and (ii) to make the annual service payment to the City, and

(b) Net Revenues, together with any transfer from the Contingency Account to the Revenue Account (both held by the City Treasurer), in each fiscal year will be at least equal to 125% of aggregate annual debt service with respect to the bonds for such fiscal year.

The methods required by the 1991 Master Bond Resolution for calculating debt service coverage differ from those required under GAAP, which are used to determine amounts reported in the Airport’s financial statements. For example, the 1991 Master Bond Resolution includes in the definition of Operating and Maintenance Expenses (which is used to calculate Net Revenues) “the *payment* of pension charges … with respect to employees of the Commission…” (emphasis added) and excludes a number of noncash accrual items. Accordingly, the Commission excludes from its rate covenant calculations any noncash accrued pension obligations and includes only pension obligations actually paid during the fiscal year.

Revenue bond debt service requirements to maturity are as follows (in thousands):

		Principal	Interest	Total
Fiscal year:				
2018	$	203,580	239,823	443,403
2019		213,255	227,086	440,341
2020		219,630	216,864	436,494
2021		230,735	206,128	436,863
2022		236,280	194,857	431,137
2023–2027		1,185,975	797,622	1,983,597
2028–2032		627,840	538,894	1,166,734
2033–2037		373,020	414,940	787,960
2038–2042		734,755	298,051	1,032,806
2043–2046		732,460	93,790	826,250
Total	$	4,757,530	3,228,055	7,985,585

The table below presents the revenue bond debt service requirements in the event the letters of credit securing the Airport’s outstanding variable rate bonds had to be drawn upon to pay such bonds and the amount drawn had to be repaid by the Airport pursuant to the terms of the related agreements with the banks providing such letters of credit (in thousands):

		Principal	Interest	Total
Fiscal year:				
2018	$	349,500	240,298	589,798
2019		276,185	219,675	495,860
2020		392,040	208,074	600,114
2021		199,965	189,439	389,404
2022		204,110	179,508	383,618
2023–2027		987,330	745,660	1,732,990
2028–2032		508,165	529,699	1,037,864
2033–2037		373,020	414,940	787,960
2038–2042		734,755	298,051	1,032,806
2043–2046		732,460	93,790	826,250
Total	$	4,757,530	3,119,134	7,876,664

(g) Post-Issuance Compliance with Federal Tax Law

The Airport follows certain federal tax law post-issuance compliance procedures that are intended to ensure that proceeds of its tax-exempt bonds are invested and expended consistent with applicable federal tax law, including the Internal Revenue Code of 1986, the Regulations promulgated thereunder, and other applicable guidance from the U.S. Treasury Department and the Internal Revenue Service (IRS).

(h) Cash Defeasance of Bonds

In June 2017, the Airport Commission used cash on hand to legally defease $12.9 million of outstanding Second Series Revenue Refunding Bonds Issue 34E maturing in 2024.

Fiscal Year 2016

(a) Second Series Revenue Bonds (Capital Plan Bonds)

Pursuant to resolutions approved in fiscal years 2008, 2012, 2014 and 2016, the Airport Commission has authorized the issuance of up to $5.0 billion of San Francisco International Airport Second Series Revenue Bonds to finance and refinance the construction, acquisition, equipping, and development of capital projects undertaken by the Airport, including retiring all or a portion of the Airport's outstanding subordinate commercial paper notes issued for capital projects, funding debt service reserves, and for paying costs of issuance. As of June 30, 2016, $3.4 billion of the authorized capital plan bonds remained unissued.

In September 2015, the Airport Commission authorized the issuance of an additional $243.0 million of San Francisco International Airport Second Series Revenue Bonds (Capital Plan Bonds) and $225.0 million of San Francisco International Airport Hotel Special Facility Revenue Bonds to finance the development and construction of a new Airport-owned hotel and related AirTrain station. The Commission also designated the planned hotel as a "special facility" under the 1991 Master Bond Resolution, which will allow the hotel revenues to be segregated from the Airport's other revenues and used to pay hotel operating expenses and debt service on the Hotel Special Facility Bonds. In order to obtain the lowest cost of financing, the Commission does not plan to sell the Hotel Special Facility Bonds to investors, but will purchase them itself with a portion of the proceeds of the Capital Plan Bonds, which will be sold to investors. The total net proceeds of the two bond issuances are expected to be approximately $243.0 million, which will be applied to the $225.0 million construction costs of the hotel and AirTrain station, capitalized interest on the Hotel Special Facility Bonds and other costs of issuance. On December 1, 2015, the City's Board of Supervisors authorized the issuance of such Hotel Special Facility Bonds and Capital Plan Bonds for the hotel and AirTrain station. Airport Commission approval of the bond sale is required before such bonds can be issued.

(b) Second Series Revenue Refunding Bonds

Pursuant to sale resolutions approved between fiscal years 2005 through 2016, the Airport Commission has authorized the issuance of up to $8.4 billion of San Francisco International Airport Second Series Revenue Refunding Bonds for the purposes of refunding outstanding 1991 Master Bond Resolution Bonds and outstanding subordinate commercial paper notes, funding debt service reserves, and paying costs of issuance, including any related bond redemption premiums.

On February 25, 2016 the Airport issued its Second Series Revenue Refunding Bonds, Series 2016A (Non-AMT/Governmental Purpose), in the principal amount of $232.1 million to refund $66.5 million of its Issue 32F, $155.3 million of its Issue 32G and $63.1 million of its Issue 34D long-term fixed rate bonds for debt service savings.

As of June 30, 2016, net of expired sale authorizations, $1.2 billion of such refunding bonds remained authorized but unissued.

(c) Variable Rate Demand Bonds

As of June 30, 2016, the Airport Commission had outstanding an aggregate principal amount of $477.9 million of Second Series Variable Rate Revenue Refunding Bonds, consisting of Issue 36A/B/C and Issue 37C, and Series 2010A (collectively, the "Variable Rate Bonds), with final maturity dates of May 1, 2026 (Issue 36A/B/C), May 1, 2029 (Issue 37C), and May 1, 2030 (Series 2010A). The Variable Rate Bonds are long-term, tax-exempt bonds that currently bear interest at a rate that is adjusted weekly, and that are subject to tender at par at the option of the holder thereof on seven days' notice. Any tendered Variable Rate Bonds are remarketed by the applicable remarketing agent in the secondary market to other investors. The interest rate on the Variable Rate Bonds can be converted to other interest rate modes, including a term rate or fixed rates to maturity, upon appropriate notice by the Airport.

The scheduled payment of the principal and purchase price of and interest on the Variable Rate Bonds is secured by separate irrevocable letters of credit issued to the Senior Trustee for the benefit of the applicable bondholders by the banks identified in the table below.

Amounts drawn under a letter of credit that are not reimbursed by the Airport constitute "Repayment Obligations" under the 1991 Master Bond Resolution and are accorded the status of other outstanding bonds to the extent provided in the Resolution. The commitment fees for the letters of credit range between 0.450% and 0.630% per annum. As of June 30, 2016, there were no unreimbursed draws under these facilities.

On June 29, 2016, the Airport obtained a new irrevocable letter of credit issued by Wells Fargo Bank, National Association, supporting the Second Series Variable Rate Revenue Refunding Bonds, Issue 36A. The letter of credit will expire June 29, 2018.

On June 29, 2016, the Airport obtained a new irrevocable letter of credit issued by Bank of America, National Association, supporting the Second Series Variable Rate Revenue Refunding Bonds Series 2010A. The letter of credit expires June 29, 2020.

The letters of credit securing the Variable Rate Bonds included in long-term debt as of June 30, 2016, are as follows:

	Issue 36A	Issue 36B	Issue 36C	Issue 37C	Series 2010A
Principal amount	$ 100,000,000	40,620,000	36,145,000	88,650,000	212,475,000
Expiration date	June 29, 2018	April 25, 2018	April 25, 2018	January 28, 2019	June 29, 2020
Credit provider	Wells Fargo(1)	BTMU(2)	BTMU(2)	MUFG Union Bank (3)	Bank of America(4)

(1) Wells Fargo Bank, National Association
(2) The Bank of Tokyo-Mitsubishi UFJ. Ltd.
(3) Formerly Union Bank, N.A.
(4) Bank of America, National Association

(d) Interest Rate Swaps

Objective and Terms – On December 16, 2004, the Airport entered into seven forward starting interest rate swaps (the 2004 swaps) with an aggregate notional amount of $405.0 million, in connection with the anticipated issuance of Second Series Variable Rate Revenue Refunding Bonds, Issue 32A-E on February 10, 2005, and Second Series Variable Rate Revenue Refunding Bonds, Issue 33 on February 15, 2006. The swap structure was intended as a means to increase the Airport’s debt service savings when compared with fixed rate refunding bonds at the time of issuance. The expiration date of the 2004 swaps is May 1, 2026.

On July 26, 2007, the Airport entered into four additional forward starting interest rate swaps in connection with the anticipated issuance of its Second Series Variable Rate Revenue Refunding Bonds, Issue 37B/C, on May 15, 2008 (the 2007 swaps), and Second Series Variable Rate Revenue Refunding Bonds, Series 2010A, on February 10, 2010 (the 2010 swaps). The expiration dates of the 2007 and 2010 swaps are May 1, 2029 and 2030, respectively.

In the spring of 2008, the Airport refunded several issues of auction rate and variable rate bonds, including Issue 32 and Issue 33. The 2004 swaps associated with these issues then became associated with the Second Series Variable Rate Revenue Refunding Bonds, Issues 36A-D, and Issue 37A. Subsequently, on October 30, 2008 and December 3, 2008, the Airport refunded Issue 37A and Issue 37B, respectively. Concurrently with the refunding of Issue 37A, the three associated swaps with an aggregate notional amount of $205.1 million were terminated. The swap associated with Issue 37B was not terminated upon the refunding of Issue 37B.

On December 16, 2010, the Airport terminated a swap associated with the Series 2010A-3 Bonds, with a notional amount of $72.0 million. The Airport paid a termination amount of $6.7 million to the counterparty, Depfa Bank plc. The payment was funded with taxable commercial paper, which was subsequently retired with Airport operating funds on March 28, 2011.

Following the termination of the Depfa swap, the Series 2010A-3 Bonds, which are variable rate, were no longer hedged with an interest rate swap. The swap associated with the Issue 37B Bonds, however, is now associated with the Series 2010A-3 Bonds.

On September 20, 2011, the Airport refunded the Issue 36D Bonds with proceeds of the San Francisco International Airport Second Series Revenue Refunding Bonds, Series 2011H and terminated the swap associated with Issue 36D, which had an initial notional amount of $30.0 million and JP Morgan Chase Bank, N.A. as counterparty. The Airport paid a termination fee of $4.6 million to the counterparty.

Under the 2004 swaps, the Airport receives a monthly variable rate payment from each counterparty equal to 63.50% of USD-LIBOR-BBA plus 0.29%. Under the 2007 and 2010 swaps, the Airport receives 61.85% of USD-LIBOR-BBA plus 0.34%. These payments are intended to approximate the variable interest rates on the bonds originally hedged by the swaps. The Airport makes a monthly fixed rate payment to the counterparties as set forth below which commenced on the date of issuance of the related bonds. The objective of the swaps is to achieve a synthetic fixed rate with respect to the hedged bonds. All of the outstanding interest rate swaps are terminable at their market value at any time solely at the option of the Airport.

As of June 30, 2016, the Airport's derivative instruments comprised six interest rate swaps that the Airport entered into to hedge the interest payments on several series of its variable rate Second Series Revenue Bonds. The Airport determined the hedging relationship between the variable rate bonds and the related interest rate swaps to be effective as of June 30, 2016.

No.	Current bonds		Initial notional amount	Notional amount June 30, 2016	Effective date
1	36AB	$	70,000,000	70,000,000	2/10/2005
2	36AB		69,930,000	69,930,000	2/10/2005
3	36C		30,000,000	30,000,000	2/10/2005
4	2010A (37B)*		79,684,000	78,584,000	5/15/2008
5	37C		89,856,000	88,616,000	5/15/2008
6	2010A**		143,947,000	142,383,000	2/1/2010
	Total	$	483,417,000	479,513,000	

* The Issue 37B Bonds that are hedged by this swap agreement were purchased with proceeds of the Series 2008B Notes, which the Commission subsequently refunded, and the Issue 37B Bonds are held in trust. The swap is now indirectly hedging the Series 2010A-3 Bonds for accounting purposes.

** Hedges Series 2010A-1 and 2010A-2.

Fair Value

The fair values take into consideration the prevailing interest rate environment and the specific terms and conditions of each swap. All values were estimated using the zero-coupon discounting method. This method calculates the future payments required by the swap, assuming that the current forward rates implied by the yield curve are the market's best estimate of future spot interest rates. These payments are then discounted using the spot rates implied by the current yield curve for a hypothetical zero-coupon rate bond due on the date of each future net settlement payment on the swaps to arrive at the so-called “settlement amount”, i.e., the approximate amount a party would have to pay or would receive if the swap was terminated.

In addition, pursuant to GASB 72, the settlement amounts are then adjusted for the nonperformance risk of each party to the swap to arrive at the fair value. For each swap, the nonperformance risk was computed as the total cost of the transactions required to hedge the default exposure, i.e., a series of European swaptions, exercisable on each of the future payment exchange dates under the swap that are structured to reverse the remaining future cash flow obligations as of such dates, adjusted by probability of default on each future date. Default probabilities were derived from recovery rate adjusted credit default swap quotes or generic ratings based borrowing curves that fall into Level 2 of the GASB 72 fair value hierarchy.

As of June 30, 2016, the fair value of the Airport’s six outstanding swaps, counterparty credit ratings, and fixed rate payable by the Airport Commission are as follows:

No.	Current bonds	Counterparty/guarantor*	Counterparty credit ratings (S&P/Moody’s/ Fitch)	Fixed rate payable by Commission		Fair value to Commission
1	36AB	J.P. Morgan Chase Bank, N.A.	A+/Aa3/AA-	3.444 %	$	(8,962,694)
2	36AB	J.P. Morgan Chase Bank, N.A.	A+/Aa3/AA-	3.445		(8,965,164)
3	36C	J.P. Morgan Chase Bank, N.A.	A+/Aa3/AA-	3.444		(3,842,002)
4	2010A (37B)**	Merrill Lynch Capital Services, Inc./ Merrill Lynch Derivative Products AG	AA-/Aa3/NR*	3.773		(17,705,290)
5	37C	J.P. Morgan Chase Bank, N.A.	A+/Aa3/AA-	3.898		(20,588,207)
6	2010A***	Goldman Sachs Bank USA/ Goldman Sachs Group, Inc.	BBB+/A3/A*	3.925		(36,068,731)
		Total			$	(96,132,088)

* Reflects ratings of the guarantor.

** The Issue 37B Bonds that are hedged by this swap agreement were purchased with proceeds of the Series 2008B Notes, which the Commission subsequently refunded, and the Issue 37B Bonds are held in trust. The swap is now indirectly hedging the Series 2010A-3 Bonds for accounting purposes.

*** Hedges Series 2010A-1 and 2010A-2.

Fair Value Hierarchy

		Fair value June 30, 2016	Fair value measurements using significant other observable inputs (Level 2)
Interest rate swaps	$	(96,132,088)	(96,132,088)

Change in Fair Value

The impact of the interest rate swaps on the financial statements for the year ended June 30, 2016 is as follows (in thousands):

		Deferred outflows on derivative instruments	Derivative instruments
Balance as of June 30, 2015 (as restated)	$	65,408	79,321
Change in fair value to year end		18,206	16,811
Balance as of June 30, 2016	$	83,614	96,132

The fair value of the interest rate swap portfolio is recorded as a liability (since the Airport would owe a termination payment to the counterparty) in the statements of net position. Unless a swap was determined to be an off-market swap at the inception of its hedging relationship, the fair value of the swap is recorded as a deferred outflow asset (if a termination payment would be due to the counterparty) or inflow liability (if a termination payment would be due to the Airport). The off-market portions of the Airport's swaps are recorded as carrying costs with respect to various refunded bond issues. Unlike fair value and deferred inflow/outflow values, the balance of remaining off-market portions are valued on a present value, or fixed yield, to maturity basis. The difference between the deferred outflows and derivative instruments presented in the table above constitutes the unamortized off-market portions of the swaps as of June 30, 2016.

Risks

Basis Risk – The Airport has chosen a variable rate index based on a percentage of London Interbank Offered Rate (LIBOR) plus a spread, which historically has closely approximated the variable rates payable on the related bonds. However, the Airport is subject to the risk that a change in the relationship between the LIBOR-based swap rate and the variable bond rates would cause a material mismatch between the two rates. Changes that cause the payments received from the counterparty to be insufficient to make the payments due on the associated bonds result in an increase in the synthetic interest rate on the bonds, while changes that cause the counterparty payments to exceed the payments due on the associated bonds result in a decrease in the synthetic interest rate on the bonds. During the fiscal year ended June 30, 2016, the Airport paid a total of $2.0 million less in interest on its variable rate bonds than the floating-rate payments it received from the swap counterparties, resulting in a decrease in the effective synthetic interest rates on the associated bonds.

Credit Risk – As of June 30, 2016, the Airport is not exposed to credit risk because the swaps have a negative fair value to the Airport. Should long-term interest rates rise and the fair value of the swaps become positive, the Airport would be exposed to credit risk in the amount of the swaps' fair value. Under the terms of the swaps, counterparties are required to post collateral consisting of specified U.S. Treasury and Agency securities in an amount equal to the market value of a swap that exceeds specified thresholds linked to the counterparty's credit ratings. Any such collateral will be held by a custodial bank.

Counterparty Risk – The Airport is exposed to counterparty risk, which is related to credit and termination risk. While the insolvency or bankruptcy of a counterparty, or its failure to perform would be a default under the applicable swap documents, none of the Airport's swaps would automatically terminate. Rather, the Airport would have the option to terminate the affected swap at its fair value, which may result in a payment to or from the counterparty. The Airport may also be exposed to counterparty risk in a high interest rate environment in the event a counterparty is unable to perform its obligations on a swap transaction leaving the Airport exposed to the variable rates on the associated debt. In order to diversify the Airport's swap counterparty credit risk and to limit the Airport's credit exposure to any one counterparty, the Airport's swap policy imposes limits on the maximum net termination exposure to any one counterparty. Maximum net termination exposure is calculated as of the date of execution of each swap and is monitored regularly during the term of the swap. The exposure limits vary for collateralized and noncollateralized swaps based upon the credit rating of the counterparty. If any exposure limit is exceeded by a counterparty during the term of a swap, the Airport Director is required to consult with the Airport's swap advisor and bond counsel regarding appropriate actions to take, if any, to mitigate such increased exposure, including, without limitation, transfer or substitution of a swap. As of June 30, 2016, the fair value of the Airport's swaps was negative to the Airport (representing an amount payable by the Airport to each counterparty in the event the relevant swap was terminated).

Termination Risk – All of the interest rate swaps are terminable at their market value at any time at the option of the Airport. The Airport has limited termination risk with respect to the interest rate swaps. That risk would arise primarily from certain credit-related events or events of default on the part of the Airport, the municipal swap insurer, or the counterparty. The Airport has secured municipal swap insurance for all its regular payments and some termination payments due under all its interest rate swaps, except the swaps associated with the Series 2010A Bonds, from the following insurers:

No.	Swap	Swap insurer	Insurer credit ratings June 30, 2016 (S&P/Moody's /Fitch)
1	Issue 36AB	FGIC/National Public Finance Guarantee Corporation	AA-/A3/NR
2	Issue 36AB	FGIC/National Public Finance Guarantee Corporation	AA-/A3/NR
3	Issue 36C	Assured Guaranty Municipal Corp.	AA/A2/NR
4	Series 2010A (37B)	Assured Guaranty Municipal Corp.	AA/A2/NR
5	Issue 37C	Assured Guaranty Municipal Corp.	AA/A2/NR
6	Series 2010A	None	N/A

If the Airport is rated between Baa1/BBB+/BBB+ and Baa3/BBB-/BBB- (Moody's/S&P/Fitch), and the applicable bond insurer is rated below A3/A- (Moody's/S&P), the counterparties may terminate the swaps and require the Airport to pay the termination value, if any, unless the Airport chooses to provide suitable replacement credit enhancement, assign the Airport's interest in the swaps to a suitable replacement counterparty, or post collateral to secure the swap termination value. If the Airport is rated below Baa3/BBB-/BBB- (Moody’s/S&P/Fitch) or its ratings are withdrawn or suspended, and the applicable bond insurer is rated below A3/A- (Moody’s/S&P), the counterparties may terminate the swaps and require the Airport to pay the termination value, if any. With respect to the Series 2010A swaps with no swap insurance, the counterparty termination provisions and the Airport rating thresholds are the same as described above.

Additional Termination Events under the swap documents with respect to the Airport include an insurer payment default under the applicable swap insurance policy, and certain insurer rating downgrades or specified insurer nonpayment defaults combined with a termination event or event of default on the part of the Airport or a ratings downgrade of the Airport below investment grade. Additional Termination Events under the swap documents with respect to a counterparty or its guarantor include a rating downgrade below A3/A1/A1 (Moody’s/S&P/Fitch), followed by a failure of the counterparty to assign its rights and obligations under the swap documents to another entity acceptable to the applicable insurer within 15 business days.

Goldman Sachs Group, Inc., which is the guarantor of the Airport’s swap counterparty Goldman Sachs Bank USA, was downgraded to BBB+ by S&P during the year ended June 30, 2016.

Merrill Lynch Derivative Products AG, which is the guarantor of the Airport’s swap counterparty Merrill Lynch Capital Services, Inc., was upgraded by one or more of the rating agencies during the year ended June 30, 2016.

The downgrade of any swap counterparty increases the risk to the Airport that such counterparty may become bankrupt or insolvent and not perform under the applicable swap. If a counterparty does not perform under its swap, the Airport may be required to continue making its fixed rate payments to the counterparty even though it does not receive a variable rate payment in return. The Airport may elect to terminate a swap with a nonperforming counterparty and may be required to pay a substantial termination payment approximately equal to the fair value of such swap, depending on market conditions at the time. As of June 30, 2016, the fair value of each swap was negative to the Airport as shown above. The risks and termination rights related to the Airport’s swaps are discussed in further detail above.

(e) Special Facilities Lease Revenue Bonds

In addition to the long-term obligations discussed above, the Commission’s San Francisco International Airport Special Facilities Lease Revenue Bonds (SFO Fuel Company LLC), Series 1997A and 2000A, were outstanding in the principal amounts of $73.2 million and $78.1 million, respectively, as of June 30, 2016 and 2015. SFO Fuel Company LLC (SFO Fuel), a special purpose limited liability company formed by certain airlines operating at the Airport, is required to pay facilities rent to the Airport pursuant to a lease agreement between the Commission and SFO Fuel with respect to the jet fuel distribution facilities in an amount equal to debt service payments on the bonds and any required bond reserve account deposits. The principal and interest on the bonds are paid solely from the facilities rent payable by SFO Fuel to the Airport. The lease payments, and therefore the SFO Fuel bonds, are payable from charges imposed by SFO Fuel on air carriers for into-plane fueling at the Airport, and are not payable from or secured by the Net Revenues of the Airport. The Airport assigned its right to receive the facilities rent to the bond trustee to pay and secure the payment of the bonds. Neither the Airport nor the City is obligated in any manner for the repayment of the SFO Fuel bonds other than from the facilities rent received from SFO Fuel. The bonds are therefore not reported in the accompanying financial statements.

(f) Post-Issuance Compliance with Federal Tax Law

The Airport follows certain federal tax law post-issuance compliance procedures that are intended to ensure that proceeds of its tax-exempt bonds are invested and expended consistent with applicable federal tax law, including the Internal Revenue Code of 1986, the Regulations promulgated thereunder, and other applicable guidance from the U.S. Treasury Department and the IRS.

(g) Cash Defeasance of Bonds

In June 2016, the Airport Commission used cash on hand to defease $24.7 million of outstanding Second Series Revenue Refunding Bonds Issue 34E.

(8) Pledged Revenue

The Airport Commission has pledged all of the Net Revenues of the Airport to repay the following obligations when due, in order of priority, (1) the San Francisco International Airport Second Series Revenue Bonds (Senior Bonds) issued and to be issued under the Commission's Resolution No. 91-0210 adopted on December 3, 1991, as amended and supplemented (1991 Master Bond Resolution), and amounts due under the letters of credit securing the Senior Bonds to the extent provided in the 1991 Master Bond Resolution, (2) the San Francisco International Airport Subordinate Commercial Paper Notes and any other obligations (Subordinate Bonds) issued and to be issued under the Commission's Resolution No. 97-0146 adopted on May 20, 1997, as amended and supplemented (1997 Note Resolution) and amounts due to reimburse drawings under the letters of credit securing the Commercial Paper Notes, (3) remaining amounts due to reimburse drawings under the letters of credit securing the Senior Bonds, and (4) interest rate swap termination payments. The Senior Bonds and Commercial Paper Notes are issued to finance capital projects at the Airport and to refund previously issued Senior Bonds and Commercial Paper Notes. The pledges of Net Revenues described above are in force so long as the secured obligations are outstanding. As of June 30, 2017, the final maturities of the obligations secured by the Net Revenues are Senior Bonds that mature in fiscal year 2046.

Net Revenues are defined in the 1991 Master Bond Resolution and the 1997 Note Resolution as Revenues less Operation and Maintenance Expenses. Revenues are defined to include all revenues earned by the Commission with respect to the Airport, as determined in accordance with GAAP. Revenues do not include: (a) investment income from moneys in (i) the Construction Fund, (ii) the Debt Service Fund which constitute capitalized interest, or (iii) the Reserve Fund if and to the extent there is any deficiency therein; (b) interest income on, and any profit realized from, the investment of the proceeds of any Special Facility Bonds (as defined in the 1991 Master Bond Resolution); (c) Special Facility Revenues (as defined in the 1991 Master Bond Resolution) and any income realized from the investment thereof unless designated as Revenues by the Commission; (d) any passenger facility or similar charge levied by or on behalf of the Commission unless designated as Revenues by the Commission; (e) grants-in-aid, donations and bequests; (f) insurance proceeds not deemed to be Revenues in accordance with GAAP; (g) the proceeds of any condemnation award; (h) the proceeds of any sale of land, buildings or equipment; and (i) any money received by or for the account of the Commission from the levy or collection of taxes upon any property of the City.

Operation and Maintenance Expenses are defined in the 1991 Master Bond Resolution and the 1997 Note Resolution to include all expenses of the Commission incurred for the operation and maintenance of the Airport, as determined in accordance with GAAP. Operation and Maintenance Expenses do not include: (a) the principal of, premium, if any, or interest on the Senior Bonds or Subordinate Bonds (including Commercial Paper Notes); (b) any allowance for amortization, depreciation or obsolescence of the Airport; (c) any expense for which, or to the extent to which, the Commission will be paid or reimbursed from or through any source that is not included or includable as Revenues; (d) any extraordinary items arising from the early extinguishment of debt; (e) Annual Service Payments to the City; (f) any costs, or charges made therefor, for capital additions, replacements or improvements to the Airport which, under GAAP, are properly chargeable to a capital account or reserve for depreciation; and (g) any losses from the sale, abandonment, reclassification, revaluation or other disposition of any Airport properties. Operating and Maintenance Expenses include the payment of pension charges and proportionate payments to such compensation and other insurance or outside reserve funds as the Commission may establish or the Board of Supervisors may require with respect to Commission employees.

During fiscal years 2017 and 2016, the original principal amount of Senior Bonds and Commercial Paper Notes issued, principal and interest remaining due on outstanding Senior Bonds and Commercial Paper Notes, principal and interest paid on such obligations, and applicable Net Revenues are as set forth in the table below (in thousands). There were no unreimbursed drawings under any letter of credit or interest rate swap termination payments due.

		2017	**2016**
Bonds issued with revenue pledge	$	887,920	232,075
Bond principal and interest remaining due at the end of the fiscal year		7,985,585	6,705,026
Commercial paper issued with subordinate revenue pledge		179,000	304,100
Commercial paper principal and interest remaining due at the end of the fiscal year		178,564	343,343
Net revenues		489,378	473,086
Bond principal and interest paid in the fiscal year		408,750	416,610
Commercial paper principal, interest and fees paid in the fiscal year		4,106	3,900

Pledged Facilities Rent from Fuel System Lease with SFO Fuel Company LLC

The Commission entered into a Fuel System Lease dated as of September 1, 1997, with SFO Fuel Company LLC (SFO Fuel), a special purpose limited liability company formed by certain airlines operating at the Airport. The facilities rent payable by SFO Fuel has been pledged and assigned to the bond trustee to secure the repayment of the Commission’s San Francisco International Airport Special Facilities Lease

Revenue Bonds (SFO Fuel Company LLC), Series 1997A and 2000A, which were outstanding in the aggregate principal amounts of $68.2 million and $73.2 million, respectively, as of June 30, 2017 and 2016. The SFO Fuel bonds were issued to finance improvements to the jet fuel storage and distribution system at the Airport. The pledge of the facilities rent will be in effect until the maturity of the SFO Fuel bonds on January 1, 2027, unless this date is extended because additional bonds (including refunding bonds) with a later maturity are issued.

(9) Concession Revenue and Minimum Future Rents

Certain of the Airport's rental agreements with concessionaires specify that rental payments are to be based on a percentage of tenant sales, subject to a minimum amount, known as a Minimum Annual Guarantee (MAG). Concession percentage rents in excess of the applicable MAG were approximately $29.6 million and $26.3 million as of June 30, 2017 and 2016, respectively. Most of these concession agreements provide that the MAG does not apply if the actual enplanements achieved during a one-month period is less than 80% of the actual enplanements of the same reference month in the reference year, and such shortfall continues for three consecutive months. The MAG is reinstated once monthly enplanements equal or exceed 80% of the reference month enplanements for two consecutive months.

A five-year car rental lease agreement option was exercised effective January 1, 2014. Under this agreement, the rental car companies will continue to pay 10% of gross revenues or a minimum guaranteed rent, whichever is higher. The MAG attributable to the rental car companies was approximately $42.5 million and $43.3 million as of June 30, 2017 and 2016, respectively.

Minimum future rents under noncancelable operating leases at the Airport having terms in excess of one year are as follows (in thousands):

Fiscal year ending:		
2018	$	92,170
2019		54,136
2020		26,371
2021		20,021
2022		16,277
2023 and thereafter		16,576
	$	225,551

(10) Employee Benefit Plans

(a) Retirement Plan

The City administers a cost-sharing multiple-employer defined benefit pension Plan (the Plan). The Plan is administered by the San Francisco City and County Employees' Retirement System (the Retirement System). For purposes of measuring the net pension liability, deferred outflows/inflows of resources related to pensions, pension expense, information about the fiduciary net position of the SFERS plans, and additions to/deductions from the Plan's fiduciary net position have been determined on the same basis as they are reported by Cheiron, the consulting actuary for the Plan. Benefit payments (including refunds of employee contributions) are recognized when currently due and payable in accordance with the benefit terms. Investments are reported at fair value.

GASB 68 requires that the reported results must pertain to liability and asset information within certain defined timeframes. For this report, the following timeframes are used:

San Francisco Employers Retirement System (SFERS) – Cost Sharing

Fiscal year 2017	
Valuation Date (VD)	June 30, 2015 updated to June 30, 2016
Measurement Date (MD)	June 30, 2016
Measurement Period (MP)	July 1, 2015 to June 30, 2016
Fiscal year 2016	
Valuation Date (VD)	June 30, 2014 updated to June 30, 2015
Measurement Date (MD)	June 30, 2015
Measurement Period (MP)	July 1, 2014 to June 30, 2015

The City is an employer of the plan with a proportionate share of 94.22% as of June 30, 2016, and 93.90% as of June 30, 2015 (measurement date). The Airport's allocation percentage was determined based on the Airport's employer contributions divided by the City's total employer contributions for fiscal years 2016 and 2015. The net pension liability, deferred outflows/inflows of resources related to pensions, amortization of deferred outflows/inflows and pension expense to each department is based on the Airport's allocated percentage. The Airport's allocation of the City's proportionate share was 6.57% as of June 30, 2016, and 6.64% as of June 30, 2015 (measurement date).

Plan Description

The Plan provides basic service retirement, disability, and death benefits based on specified percentages of defined final average monthly salary and provides annual cost-of-living adjustments after retirement. The Plan also provides pension continuation benefits to qualified survivors. The San Francisco City and County Charter and the Administrative Code are the authorities which establish and amend the benefit provisions and employer obligations of the Plan. The Retirement System issues a publicly available financial report that includes financial statements and required supplementary information for the Plan. That report may be obtained by writing to the San Francisco City and County Employees' Retirement System, 1145 Market Street, 5th Floor, San Francisco, CA 94103 or by calling (415) 487-7000.

(Continued)

Benefits

The Retirement System provides service retirement, disability and death benefits based on specified percentages of defined final average monthly salary and annual cost of living adjustments after retirement. Benefits and refunds are recognized when due and payable in accordance with the terms of the Plan. The Retirement System pays benefits according to the category of employment and the type of benefit coverage provided by the City and County. The four main categories of Plan members are:

- Miscellaneous Non-Safety Members – staff, operational, supervisory, and all other eligible employees who are not in special membership categories.
- Sheriff's Department and Miscellaneous Safety Members – sheriffs assuming office on and after January 7, 2012, and undersheriffs, deputized personnel of the sheriff's department, and miscellaneous safety employees hired on and after January 7, 2012.
- Firefighter Members – firefighters and other employees whose principal duties are in fire prevention and suppression work or who occupy positions designated by law as firefighter member positions.
- Police Members – police officers and other employees whose principal duties are in active law enforcement or who occupy positions designated by law as police member positions.

The membership groups and the related service retirement benefits are included in the Notes to the Basic Financial Statements of the San Francisco Employees Retirement System.

All members are eligible to apply for a disability retirement benefit, regardless of age, when they have 10 or more years of credited service and they sustain an injury or illness that prevents them from performing their duties. Safety members are eligible to apply for an industrial disability retirement benefit from their first day on the job if their disability is caused by an illness or injury that they receive while performing their duties.

All retired members receive a benefit adjustment each July 1, which is the Basic COLA. The majority of adjustments are determined by changes in CPI with increases capped at 2%. The Plan provides for a Supplemental COLA in years when there are sufficient "excess" investment earnings in the Plan. The maximum benefit adjustment each July 1 is 3.5% including the Basic COLA. Effective July 1, 2012, voters approved changes in the criteria for payment of the Supplemental COLA benefit, so that Supplemental COLAs would only be paid when the Plan is also fully funded on a market value of assets basis. Certain provisions of this voter-approved proposition were challenged in the courts. A decision by the California courts modified the interpretation of the proposition. Effective July 1, 2012, members who retired before November 6, 1996, will receive a Supplemental COLA only when the Plan is also fully funded on a market value of assets basis. However, the "full funding" requirement does not apply to members who retired on or after November 6, 1996, and were hired before January 7, 2012. For all members hired before January 7, 2012, all Supplemental COLAs paid to them in retirement benefits will continue into the future even where an additional Supplemental COLA is not payable in any given year. For members hired on and after January 7, 2012, a Supplemental COLA will only be paid to retirees when the Plan is fully funded on a market value of asset basis, and, in addition for these members, Supplemental COLAs will not be permanent adjustments to retirement benefits. That is, in years when a Supplemental COLA is not paid, all previously paid Supplemental COLAs will expire.

Funding and Contribution Policy

Contributions are made to the basic plan by both the City and the participating employees. Employee contributions are mandatory as required by the Charter. Employee contribution rates for fiscal year 2017 varied from 7.5% to 12.0% as a percentage of gross covered salary. Most employee groups agreed through collective bargaining for employees to contribute the full amount of the employee contributions on a pretax basis. The City is required to contribute at an actuarially determined rate. Based on the July 1, 2015 actuarial report, the required employer contribution rate for fiscal year 2017 was 17.90% to 21.40%.

Employer contributions and employee contributions made by the employer to the Plan are recognized when due and the employer has made a formal commitment to provide the contributions. The City's proportionate share of employer contributions recognized by the Retirement System in the fiscal year ended June 30, 2016 (measurement period) was $496.3 million. The Airport's allocation of employer contributions for fiscal year 2016 was $33.0 million.

Pension Liability, Pension Expenses and Deferred Outflows/Inflows of Resources Related to Pensions

Fiscal Year 2017

As of June 30, 2017, the City reported net pension liabilities for its proportionate share of the pension liability of the Plan of $5.48 billion. The City's net pension liability for the Plan is measured as the proportionate share of the net pension liability. The net pension liability of the Plan is measured as of June 30, 2016 (MD), and the total pension liability for the Plan used to calculate the net pension liability was determined by an actuarial valuation as of June 30, 2015 rolled forward to June 30, 2016, using standard update procedures. The City's proportion of the net pension liability was based on a projection of the City's long-term share of contributions to the pension plan relative to the projected contributions of all participating employers, actuarially determined. The Airport's allocation of the City's proportionate share of the net pension liability for each Plan as of June 30, 2016 and 2017 (reporting years) was $144.3 million and $359.6 million respectively. During the measurement year 2016 the increase in service costs, interest costs, change in benefits, change in assumptions, and difference between projected and actual investment earnings increased total pension liability. This was only partially offset by an increase in the discount rate, contributions, investment income, and actuarial experience gains, resulting in an overall increase in net pension liability.

For the year ended June 30, 2017, the City's recognized pension expense was $1.8 billion including amortization of deferred outflow/inflow related pension items. The Airport's allocation of pension expense including amortization of deferred outflow/inflow related pension items was $114.9 million. Pension expense increased significantly, largely due to the impact of changes in benefits, namely the updated Supplemental COLA assumptions and amortization of deferred inflows/outflows.

At June 30, 2017, the Airport’s proportionate share of the City's reported deferred outflows of resources and deferred inflows of resources related to pensions from the sources set forth below (in thousands).

Schedule of Deferred Inflows and Outflows

		Deferred outflows of resources	Deferred inflows of resources
Changes of assumptions	$	61,861	1,814
Net difference between projected and actual earnings on pension plan investments		49,167	—
Change in proportionate share		632	337
Difference between expected and actual experience		—	13,251
Pension contributions subsequent to the measurement date		34,083	—
Total	$	145,743	15,402

Amounts reported as deferred outflows (excluding pension contributions made subsequent to measurement date) and deferred inflows of resources will be amortized annually and recognized as pension expense as follows (in thousands):

		Deferred outflows/ (inflows) of resources
Fiscal year:		
2018	$	14,167
2019		14,167
2020		38,699
2021		29,225
Total	$	96,258

Fiscal Year 2016

As of June 30, 2016, the City reported net pension liabilities for its proportionate share of the pension liability of the Plan of $2.16 billion. The City’s net pension liability for the Plan is measured as the proportionate share of the net pension liability. The net pension liability of the Plan is measured as of June 30, 2015, and the total pension liability for the Plan used to calculate the net pension liability was determined by an actuarial valuation as of June 30, 2014, rolled forward to June 30, 2015, using standard update procedures. The City’s proportion of the net pension liability was based on a projection of the City’s long-term share of contributions to the pension plan relative to the projected contributions of all participating employers, actuarially determined. The Airport's allocation of the City's proportionate share of the net pension liability for each Plan as of June 30, 2015 (MP) and 2014 (MP) was $144.3 million and $111.9 million, respectively. During the measurement period fiscal year 2015, there were no changes to benefits. The increase in service costs, interest costs, and decrease in the discount rate increased total pension liability and were only partially offset by contributions, investment income, and actuarial experience gains, resulting in an overall increase in net pension liability.

For the year ended June 30, 2016, the City's recognized pension expense was $106.5 million including amortization of deferred outflow/inflow related pension items. The Airport's allocation of pension expense including amortization of deferred outflow/inflow related pension items was $6.7 million. At June 30, 2016, the Airport's reported deferred outflows of resources and deferred inflows of resources related to pensions from the sources set forth below (in thousands).

Schedule of Deferred Inflows and Outflows

		Deferred outflows of resources	Deferred inflows of resources
Changes of assumptions	$	10,815	2,785
Net difference between projected and actual earnings on pension plan investments		—	34,976
Change in proportionate share		214	519
Difference between expected and actual experience		—	9,874
Pension contributions subsequent to the measurement date		32,953	—
Total	$	43,982	48,154

Amounts reported as deferred outflows (excluding pension contributions made subsequent to measurement date) and deferred inflows of resources will be amortized annually and recognized as pension expense as follows (in thousands):

		Deferred outflows/ (inflows) of resources
Fiscal year:		
2017	$	(15,557)
2018		(15,557)
2019		(15,557)
2020		9,546
Total	$	(37,125)

Actuarial Assumptions

Fiscal Year 2017

A summary of the actuarial assumptions and methods used to calculate the Total Pension Liability as of June 30, 2016 (measurement period) is provided below, including any assumptions that differ from those used in the July 1, 2015 actuarial valuation. Refer to the July 1, 2015 actuarial valuation report for a complete description of all other assumptions, which can be found on the Retirement System's website http://mysfers.org.

Key actuarial assumptions:	
Inflation	3.25%
Salary increases	3.75% plus merit component based on employee classification and years of service
Valuation date	June 30, 2015 updated to June 30, 2016
Measurement date	June 30, 2016
Actuarial cost method	Entry-Age Normal Cost Method
Expected rate of return	7.50%
Municipal bond yield	3.85% as of June 30, 2015
	2.85% as of June 30, 2016
	Bond Buyer 20-Bond GO Index, July 2, 2015 and June 30, 2016
Discount rate	7.46% as of June 30, 2015
	7.50% as of June 30, 2016
Administrative expenses	0.45% of payroll as of June 30, 2015
	0.60% of payroll as of June 30, 2016

	Old Miscellaneous and all New Plans	Old Police & Fire pre July 1, 1975 Retirements	Old Police & Fire, Charters A8.595 and A8.596	Old Police & Fire, Charters A8.559 and A8.585
Basic COLA:				
June 30, 2015	2.00 %	3.00 %	4.00 %	5.00 %
June 30, 2016	2.00 %	2.70 %	3.30 %	4.40 %

Mortality rates for active members and healthy annuitants were based upon adjusted Employee and Healthy Annuitant CalPERS mortality tables projected generationally from the 2009 base year using a modified version of the MP-2015 projection scale.

Fiscal Year 2016

A summary of the actuarial assumptions and methods used to calculate the Total Pension Liability as of June 30, 2015 is provided below, including any assumptions that differ from those used in the July 1, 2014 actuarial valuation. Refer to the July 1, 2014 actuarial valuation report for a complete description of all other assumptions, which can be found on the Retirement System's website http://mysfers.org/.

Key actuarial assumptions:	
Inflation	3.25%
Salary increases	3.75% plus merit component based on employee classification and years of service
Valuation date	June 30, 2014 updated to June 30, 2015
Measurement date	June 30, 2015
Actuarial cost method	Entry-Age Normal Cost Method
Expected rate of return	7.50%
Municipal bond yield	4.31% as of June 30, 2014
	3.85% as of June 30, 2015
	Bond Buyer 20-Bond GO Index, July 2, 2014 and July 2, 2015
Discount rate	7.58% as of June 30, 2014
	7.46% as of June 30, 2015
Administrative expenses	0.45% of payroll

	Old Miscellaneous and all New Plans	Old Police & Fire pre July 1, 1975 Retirements	Old Police & Fire, Charters A8.595 and A8.596	Old Police & Fire, Charters A8.559 and A8.585
Basic COLA:				
June 30, 2015	2.00 %	3.00 %	4.00 %	5.00 %

Mortality rates for active members were based upon the RP-2000 Employee Tables for Males and Females projected using Scale AA to 2030 for females and to 2005 for males. Mortality rates for healthy annuitants were based upon the RP-2000 Healthy Annuitant Tables for Males and Females projected using Scale AA to 2020.

Discount Rate

Fiscal Year 2017

The beginning and end of year measurements are based on different assumptions and contribution methods that result in different discount rates. The discount rate was 7.46% as of June 30, 2015 (measurement date) and 7.50% as of June 30, 2016 (measurement date).

The discount rate used to measure the Total Pension Liability as of June 30, 2016, was 7.50%. The projection of cash flows used to determine the discount rate assumed that plan member contributions will continue to be made at the rates specified in the Charter. Employer contributions were assumed to be made in accordance with the contribution policy in effect for the July 1, 2015, actuarial valuation. That policy includes contributions equal to the employer portion of the Entry Age normal costs for members as of the valuation date, a payment for expected administrative expenses, and an amortization payment on the unfunded actuarial liability.

The amortization payment is based on closed periods that vary in length depending on the source. Charter amendments prior to July 1, 2014, are amortized over 20 years. After July 1, 2014, any Charter changes to active member benefits are amortized over 15 years and changes to inactive member benefits, including Supplemental COLAs, are amortized over 5 years. The remaining Unfunded Actuarial Liability not attributable to Charter amendments as of July 1, 2013, is amortized over a 19-year period commencing July 1, 2014. Experience gains and losses and assumption or method changes on or after July 1, 2014, are amortized over 20 years. For the July 1, 2016 valuation, the increases in the Unfunded Actuarial Liability attributable to the Supplemental COLAs granted on July 1, 2013 and July 1, 2014, are amortized over 17-years and 5-years, respectively. All amortization schedules are established as a level percentage of payroll so payments increase 3.75% each year. The Unfunded Actuarial Liability is based on an Actuarial Value of Assets that smooths investment gains and losses over five years and a measurement of the Actuarial Liability that excludes the value of any future Supplemental COLAs.

While the contributions and measure of Actuarial Liability in the valuation do not anticipate any future Supplemental COLAs, the projected contributions for the determination of the discount rate include the anticipated future amortization payments on future Supplemental COLAs for current members when they are expected to be granted. For members who worked after November 6, 1996 and before Proposition C passed, a Supplemental COLA is granted if the actual investment earnings during the year exceed the expected investment earnings on the Actuarial Value of Assets. For members who did not work after November 6, 1996 and before Proposition C passed, the Market Value of Assets must also exceed the actuarial liability at the beginning of the year for a Supplemental COLA to be granted. When a Supplemental COLA is granted, the amount depends on the amount of excess earnings and the basic COLA amount for each membership group. The large majority of members receive a 1.50% Supplemental COLA when granted.

(Continued)

Because the probability of a Supplemental COLA depends on the current funded level of the System for certain members, Cheiron developed an assumption as of June 30, 2016 for the probability and amount of Supplemental COLA for each future year. The table below shows the net assumed Supplemental COLA for members with a 2.00% Basic COLA for sample years.

Assumed Supplemental COLA for Members with a 2.00% Basic COLA

	1996 – Prop C	Before November 6, 1996 or after Prop C
Fiscal year:		
2018	0.750 %	— %
2023	0.750	0.220
2028	0.750	0.322
2033	0.750	0.370
2038+	0.750	0.375

The projection of benefit payments to current members for determining the discount rate includes the payment of anticipated future Supplemental COLAs.

Based on these assumptions, the System's fiduciary net position was projected to be available to make projected future benefit payments for current members until fiscal year end 2093 when only a portion of the projected benefit payments can be made from the projected fiduciary net position. Projected benefit payments are discounted at the long-term expected return on assets of 7.50% to the extent the fiduciary net position is available to make the payments and at the municipal bond rate of 2.85% to the extent they are not available. The single equivalent rate used to determine the Total Pension Liability as of June 30, 2016, is 7.50%.

The long-term expected rate of return on pension plan investments was 7.50%. It was set by the Retirement Board after consideration of both expected future returns and historical returns experienced by the Retirement System. Expected future returns were determined by using a building-block method in which best-estimate ranges of expected future real rates of return were developed for each major asset class. These ranges were combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. Target allocation and best estimates of geometric long-term expected real rates of return (net of pension plan investment expense and inflation) for each major asset class are summarized in the following table:

Asset class	Target allocation	Long-term expected real rate of return
Global equity	40 %	5.1 %
Fixed income	20	1.1
Private equity	18	6.3
Real assets	17	4.3
Hedge funds/absolute return	5	3.3
	100 %	

Fiscal Year 2016

The beginning and end of year measurements are based on different assumptions and contribution methods that result in different discount rates. The discount rate was 7.58% as of June 30, 2014, and 7.46% as of June 30, 2015.

The discount rate used to measure the total pension liability as of June 30, 2015, was 7.46%. The projection of cash flows used to determine the discount rate assumed that plan member contributions will continue to be made at the rates specified in the Charter. Employer contributions were assumed to be made in accordance with the contribution policy in effect for July 1, 2014 actuarial valuation. That policy includes contributions equal to the employer portion of the Entry Age normal costs for members as of the valuation date, a payment for the expected administrative expenses, and an amortization payment on the unfunded actuarial liability. The amortization payment is based on closed periods that vary in length depending on the source. Charter amendments prior to July 1, 2014, are amortized over 20 years. After July 1, 2014, any Charter changes to active member benefits are amortized over 15 years and changes to inactive member benefits, including Supplemental COLAs, are amortized over 5 years. The remaining unfunded actuarial liability not attributable to Charter amendments as of July 1, 2013, is amortized over a 19-year period commencing July 1, 2014. Experience gains and losses and assumption or method changes on or after July 1, 2014, are amortized over 20 years. All amortization schedules are established as a level percentage of payroll so payments increase 3.75% each year. The unfunded actuarial liability is based on an actuarial value of assets that smooths investment gains and losses over five years and a measurement of the actuarial liability that excludes the value of any future Supplemental COLAs.

While the contributions and measure of actuarial liability in the valuation do not anticipate any Supplemental COLAs, the projected contributions for the determination of the discount rate include the anticipated future amortization payments on future Supplemental COLA's for current members when they are expected to be granted. For a Supplemental COLA to be granted the market value of assets must exceed the actuarial liability at the beginning of the year and the actual investment earnings during the year must exceed the expected investment earnings on the actuarial value of assets. When a Supplemental COLA is granted, the amount depends on the amount of excess earnings and the basic COLA amount for each membership group. In most cases, the large majority of members receive a 1.50% Supplemental COLA.

Because the probability of a Supplemental COLA depends on the current funded level of the System, we developed an assumption as of June 30, 2015, of the probability and amount of Supplemental COLA for each future year. The table below shows the net assumed Supplemental COLAs for members with a 2.00% basic COLA for sample years.

Assumed Supplemental COLA for Members with a 2.00% Basic COLA

	Assumption
Fiscal year:	
2016	— %
2021	0.345
2026	0.375
2031	0.375
2036+	0.375

The projection of benefit payments to current members for determining the discount rate includes the payment of anticipated future Supplemental COLAs.

Based on these assumptions, the Retirement System's fiduciary net position was projected to be available to make projected future benefit payments for current members until fiscal year end 2076 when only a portion of the projected benefit payments can be made from the projected fiduciary net position. Projected benefit payments are discounted at the long-term expected return on assets of 7.50% to the extent the fiduciary net position is available to make the payments and at the municipal bond rate of 3.85% to the extent they are not available. The single equivalent rate used to determine the Total Pension Liability as of June 30, 2015, is 7.46%.

The long-term expected rate of return on pension plan investments was 7.50%. It was set by the Retirement Board after consideration of both expected future returns and historical returns experienced by the Retirement System. Expected future returns were determined by using a building-block method in which best-estimate ranges of expected future real rates of return were developed for each major asset class. These ranges were combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. Target allocation and best estimates of geometric long-term expected real rates of return (net of pension plan investment expense and inflation) for each major asset class are summarized in the following table:

Asset class	Target allocation	Long-term expected real rate of return
Global equity	40 %	5.1 %
Fixed income	20	1.2
Private equity	18	7.5
Real assets	17	4.1
Hedge funds/absolute return	5	3.5
	100 %	

Sensitivity of Proportionate Share of the Net Pension Liability to Changes in the Discount Rate

The following presents the Airport’s allocation of the employer’s proportionate share of the net pension liability for the Plan, calculated using the discount rate, as well as what the Airport’s allocation of the employer’s proportionate share of the net pension liability would be if it were calculated using a discount rate that is 1% lower or 1% higher than the current rate (in thousands):

Fiscal Year 2017

Employer	1% decrease share of NPL @ 6.50%	Share of NPL @ 7.50%	1% increase share of NPL @ 8.50%
Airport	$ 569,852	359,599	185,694

Fiscal Year 2016

Employer	1% decrease share of NPL @ 6.46%	Share of NPL @ 7.46%	1% increase share of NPL @ 8.46%
Airport	$ 319,033	144,271	(2,294)

(b) Health Care Benefits

Health care benefits of Airport employees, retired employees, and surviving spouses are financed by beneficiaries and by the City through the City and County of San Francisco Health Service System (the Health Service System). The Airport's annual contribution, which amounted to approximately $39.7 million and $36.7 million in fiscal years 2017 and 2016, respectively, is determined by a Charter provision based on similar contributions made by the 10 most populous counties in California.

Included in these amounts are $10.9 million and $10.3 million for fiscal years 2017 and 2016, respectively, to provide postretirement benefits for retired Airport employees on a pay-as-you-go basis, as well as $1.0 million and $0.5 million for fiscal years 2017 and 2016, respectively, to fund the Airport's share of the City's retiree health care trust fund. The City did not allocate to the Airport any additional share of the payments made by the City's Health Service System for postretirement health benefits in fiscal years 2017 and 2016.

The City has determined a Citywide annual required contribution (ARC), interest on net other postemployment benefits other than pensions (OPEB), ARC adjustment, and OPEB cost based upon an actuarial valuation performed in accordance with GASB 45, by the City's actuaries. The City's allocation of the OPEB-related costs to Airport for the years ended June 30, 2017 and 2016, based upon its percentage of Citywide payroll costs is presented below.

The following table shows the components of the City's annual OPEB allocations for the Airport for the fiscal year, the amount contributed to the plan, and changes in the net OPEB obligation (in thousands):

		2017	2016
Annual required contribution	$	22,129	18,797
Interest on net OPEB obligation		6,013	5,969
Adjustment to ARC		(2,432)	(4,853)
Annual OPEB cost		25,710	19,913
Contribution made		(11,894)	(10,858)
Increase in net OPEB obligation		13,816	9,055
Net OPEB obligation – beginning of year		124,352	115,297
Net OPEB obligation – end of year	$	138,168	124,352

As of June 30, 2017, the Airport has set aside $115.5 million in a separate fund for purposes of the OPEB obligations and such amount is included in Unrestricted Cash and Investments in the accompanying statements of net position. The disposition of this fund is under management's discretion and has not been placed in a trust fund.

The City issues a publicly available financial report for Citywide level that includes the complete note disclosures and required supplementary information related to the City's postretirement health care obligations. The report may be obtained by writing to City and County of San Francisco, Office of the Controller, 1 Dr. Carlton B. Goodlett Place, Room 316, San Francisco, California 94102, or by calling (415) 554-7500.

(11) Related-Party Transactions

The Airport receives services from various other City departments that are categorized in the various operating expense line items in the statements of revenues, expenses, and changes in net position. These services include utilities provided to tenants (see note 2m) and the Airport. The cost of all services provided to the Airport by the City work order system totaled approximately $147.4 million and $140.7 million in fiscal years 2017 and 2016, respectively. Included in personnel operating expenses are approximately $74.6 million and $70.5 million in fiscal years 2017 and 2016, respectively, related to police and fire services.

The Lease and Use Agreement with the airlines provides for continuing annual service payments to the City equal to 15% of concession revenues (net of certain adjustments), but not less than $5.0 million per fiscal year. Annual service payments to the City were $45.0 million and $42.5 million in fiscal years 2017 and 2016, respectively. The annual service payments are reported as transfers in the statements of revenues, expenses, and changes in net position.

(12) Passenger Facility Charges

As of June 30, 2017, the FAA has approved several Airport applications to collect and use PFCs (from PFC #2 to PFC #7) in a total cumulative collection amount of $2.0 billion and the cumulative use amount of $1.7 billion, with a final charge expiration date estimated to be February 1, 2030. During the fiscal years ended June 30, 2014, 2015 and 2017, the following changes occurred to the Airport's PFC collection authorizations.

In October 2013, the FAA approved the Airport's fifth application (PFC #5) for $610.5 million to pay for debt service related costs associated with the reconstruction and reopening of Terminal 2 and Boarding Area D renovations. The earliest charge effective date is January 1, 2017 and is based upon the estimated charge expiration date of PFC #3. The FAA estimates the charge expiration date for PFC #5 to be June 1, 2023. In November 2014, the FAA approved an amendment to PFC #5 that increased the imposition and use authority by $131.3 million from $610.5 million to $741.7 million. The estimated expiration date for PFC #5 was changed from June 1, 2023 to October 1, 2024. The Airport is working with the FAA to change the expiration date for PFC #3 and the charge effective date for PFC #5 from January 1, 2017 to November 1, 2013, because PFC #3 was fully collected earlier than originally anticipated due to increased passenger levels.

In June 2015, the FAA approved the Airport's sixth PFC application (PFC #6) for $141.1 million to pay for debt service related to the Runway Safety Area Program and the installation of ten passenger boarding bridges at Boarding Area E. The FAA estimates the charge expiration date for PFC #6 to be March 1, 2026.

In May 2017, the FAA approved the Airport's seventh PFC application (PFC #7) for collection of $319.7 million to pay for debt service associated with the AirTrain Extension and Improvements Project at the Airport. The approval of PFC #7 for use is pending. FAA estimates the charge expiration date for PFC #7 to be February 1, 2030.

PFC collections and related interest earned for the years ended June 30, 2017 and 2016, are as follows (in thousands):

		2017	2016
Amount collected	$	103,955	99,131
Interest earned		1,972	1,070
Total	$	105,927	100,201

Interest earned on PFC revenues is included in investment income in the accompanying financial statements.

(13) Commitments, Litigation, and Contingencies

(a) Commitments

Purchase commitments for construction, material, and services as of June 30, 2017 are as follows (in thousands):

Construction	$	188,826
Operating		28,896
Total	$	217,722

The Airport's Noise Insulation Program was implemented to mitigate the aircraft noise impact in the surrounding communities. This involved execution of a Memorandum of Understanding in 1992 with neighboring communities to insulate eligible properties and acquire easements for noise, vibration, and other effects resulting from aircraft operations at the Airport, and implementation of a supplemental program in 2000 to complete the work. This program was managed by the local communities with Airport funds (using bond proceeds, operating and other internally generated funds), as well as federal grants.

In fiscal year 2008, these components of the program were finalized and a new phase was started, with the Airport managing all new noise insulation work directly. In fiscal year 2017, the Airport disbursed approximately $77,000 in this new phase of the program ($50,000 in federal grants and $27,000 in Airport funds). In fiscal year 2016, the Airport disbursed approximately $33,000 in this phase of the program ($300 in federal grants and $32,700 in Airport funds). As of June 30, 2017, the cumulative disbursements of Airport funds under this program were approximately $122.3 million.

(Continued)

(b) Security Deposits

Airline leases and permits require airlines to deliver a security deposit to the Airport prior to the effective date of the lease or permit. Such deposits are either in the form of (a) a surety bond payable to the City or (b) a letter of credit naming the City as a beneficiary. Under the 2011 Lease and Use Agreement, security deposits are renewed and increased annually in order to equal to two months of fees, as established by the Airport Director each fiscal year in accordance with Rates and Charges. Under most other leases and permits at the Airport, a deposit equal to six months is required.

The bonds or letters of credit are required to be kept in full force and effect at all times to ensure the faithful performance by the respective lessee or permittee of all covenants, terms, and conditions of the leases or permits, including payment of the monthly fees.

(c) Litigation

The Airport is a defendant in various legal actions and claims that arise during the normal course of business. Insurance policies cover certain actions, claims, and defense costs. Only those items not covered by insurance are included in the financial statements. The Airport's potential liabilities have been estimated and reported in the financial statements, in conformity with GAAP.

(d) Risk Management

Under the 1991 Master Bond Resolution, the Airport is required to procure or provide and maintain insurance, or to self-insure, against such risks as are usually insured by other major airports in amounts adequate for the risk insured against, as determined by the Airport, and to file with the Trustee each year a written summary of all insurance coverage then in effect. The Airport is not required to nor does it carry insurance or self-insure against any risks due to land movement or seismic activity.

The Airport has an ongoing loss prevention program, a safety officer, property loss control, and ongoing employee training programs. The Airport has instituted an Enterprise Risk Management Program by implementing a comprehensive risk identification, assessment, and treatment protocol to address key risks that may adversely affect the Airport's ability to meet its business goals and objectives. The Airport carries general liability insurance coverage of $1.0 billion with $250.0 million in War Perils Liability, subject to a deductible of $10,000 per single occurrence. The Airport also carries commercial property insurance coverage for full replacement value on all facilities at the Airport owned by the Airport, subject to a limit of $1.0 billion per single occurrence and a deductible of $500,000 per single occurrence.

Additionally, tenants and contractors on all contracts are required to carry commercial general and automobile liability insurance in various amounts, naming the Airport as additional insured. The Airport is self-insured as part of the City's workers' compensation program. From current revenues, the Airport pays losses from workers' compensation claims of Airport employees, the deductible portion of insured losses, and losses from other uninsured risks. The Airport carries public officials' liability and employment practices liability coverage of $5.0 million, subject to a deductible of $100,000 per single occurrence for each wrongful act other than employment practices' violations, and $250,000 per each occurrence for each employment practices' violation. The Airport also carries insurance for public employee dishonesty, fine arts, electronic data processing equipment, and watercraft liability for Airport

(Continued)

fire and rescue vessels and Target Range Liability for the San Francisco Police Department's firearms range located at the Airport.

Prior to September 11, 2001, the Airport had liability insurance coverage in the amount of $750.0 million per occurrence for war, terrorism, and hijacking. Immediately following the events of September 11, 2001, insurers canceled the coverage for war, terrorism, and hijacking for all airports, including the Airport, and for all airlines around the country. A number of insurers now provide this coverage through the Terrorism Risk Insurance Program Reauthorization Act (TRIPA) of 2015. However, the scope of the coverage is limited and the premiums are high. Due to these factors, the Airport, in consultation with the City's Director of Risk Management, has elected not to secure such coverage.

The estimated claims payable are actuarially determined as part of the City's self-insurance program. Changes in the reported amount resulted from the following activity (in thousands):

Balance as of June 30, 2015	$	3,772
Claim payments		(2,403)
Claims and changes in estimates		108
Balance as of June 30, 2016		1,477
Claim payments		(796)
Claims and changes in estimates		174
Balance as of June 30, 2017	$	855

The Airport is self-insured as part of the City's program for workers' compensation. All self-insurance claims are processed by the City. Liability and risk are retained by the Airport. Accrued workers' compensation includes provisions for claims reported and claims incurred but not reported. This accrued workers' compensation liability is actuarially determined as part of the City's program and is as follows (in thousands):

Balance as of June 30, 2015	$	6,081
Claim payments		(2,078)
Claims and changes in estimates		2,654
Balance as of June 30, 2016		6,657
Claim payments		(2,416)
Claims and changes in estimates		3,095
Balance as of June 30, 2017	$	7,336

(e) Grants

Grants that the Airport receives are subject to audit and final acceptance by the granting agency. Current and prior year costs of such grants are subject to adjustment upon audit.

(f) Financial Guarantees

The Airport participates in the City and County of San Francisco's surety bond program which provides training, support and City-funded surety bond guaranties for local business enterprise (LBE) contractors who want to bid on construction contracts for City departments (including the Airport), but cannot qualify for the required surety bonds on their own. If program parameters are met, the Airport may guaranty the lesser of $750,000 or 40% of the face amount of the surety bond, which would enable the LBE contractor to bid on Airport construction work. There were no outstanding Airport guaranties under the program as of June 30, 2017.

(g) Concentration of Credit Risk

The Airport leases facilities to the airlines pursuant to the Lease and Use Agreement (see note 2j) and to other businesses to operate concessions at the Airport. For fiscal years ended June 30, 2017 and 2016, revenues realized from the following source exceeded 5% of the Airport's total operating revenues:

	2017	2016
United Airlines	23.9 %	23.5 %

(h) Noncancelable Operating Leases

The Airport has noncancelable operating leases for certain buildings and equipment that require the following minimum annual payments, net of sublease income (in thousands):

Fiscal year ending:		
2018	$	148
2019		—
Total	$	148

Net operating lease expense incurred for the fiscal year ended 2017 was the same as 2016 at approximately $0.2 million.

(14) Subsequent Events

(a) Credit Rating Changes

On October 3, 2017 Fitch downgraded the long-term credit rating of Wells Fargo Bank, N.A. (Wells Fargo), which provides a $100 million principal amount irrevocable letter of credit in support of the Commission's Second Series Variable Rate Revenue Refunding Bonds, Issue 36A. As a result, on October 4, 2017, Fitch lowered its long-term jointly supported rating on the Issue 36A Bonds from "AAA" to "AA+." Fitch's short-term rating on the Issue 36A Bonds (F1+) remained unchanged. Fitch's underlying long-term rating on the Issue 36A Bonds (A+) also remained unchanged.

(b) Issuance of Capital Plan Bonds and Refunding Bonds and Swaps Termination

On October 11, 2017, the Commission priced and expects to issue on October 31, 2017 approximately $571.6 million in Second Series Revenue Bonds, Series 2017A and 2017B, a portion of which will be used to finance and refinance (through the repayment of $300.5 million of commercial paper notes) a portion of the costs of capital improvements to the Airport; $45.1 million in Second Series Revenue Refunding Bonds, Series 2017C, to fund a deposit to the Contingency Account, to finance a $12.6 million termination payment on a portion of the interest rate swaps associated with the Second Series Revenue Refunding Bonds, Issue 36A, 36B, and 36C, and to pay costs of issuance of its Second Series Revenue Refunding Bonds, Series 2017D; and $144.8 million in Second Series Revenue Refunding Bonds, Series 2017D, to current refund the remaining $164.6 million principal amount of the Second Series Revenue Refunding Bonds, Issue 36A, 36B, and 36C. The Commission also expects to issue on February 1, 2018, $115.4 million in Second Series Revenue Refunding Bonds, Series 2018A, under a forward purchase agreement executed on October 11, 2017, for the purpose of current refunding $140.1 million in outstanding Second Series Revenue Refunding Bonds, Issue 34E. Moody's, S&P, and Fitch assigned credit ratings of "A1", "A+", and "A+" to these bonds.

The Commission issued an additional $152.4 million in subordinate commercial paper notes on July 27, 2017, for a total of $330.4 million subordinate commercial paper notes outstanding. On November 2, 2017, the Commission expects proceeds of the Series 2017A and 2017B Bonds to be used to repay $300.5 million in subordinate commercial paper notes, leaving a total of $29.8 million subordinate commercial paper notes outstanding.

(c) Interest Rate Swaps – LIBOR

In July 2017, the United Kingdom (UK) Financial Conduct Authority, the UK markets regulator, indicated that the London Interbank Overnight Rate (LIBOR) would be phased out by the end of 2021. The Commission's interest rate swap agreements calculate the variable rate payment owed from each counterparty to the Airport each month using LIBOR plus a certain spread. At least a portion of the Airport's swaps are not scheduled to terminate until May 1, 2030. The Commission expects its interest rate swap agreements to be modified to reflect the permanent discontinuation of LIBOR and its substitution with a new variable rate benchmark or variable rate-setting mechanism.

SCHEDULE OF PASSENGER FACILITY CHARGE REVENUES AND EXPENDITURES

AIRPORT COMMISSION
CITY AND COUNTY OF SAN FRANCISCO
SAN FRANCISCO INTERNATIONAL AIRPORT

Schedule of Passenger Facility Charge Revenues and Expenditures

Years ended June 30, 2017 and 2016

(In thousands)

	Passenger Facility Charge revenues	Interest earned	Total revenues	Expenditures on approved projects	Revenues over (under) expenditures on approved projects
Program to date as of June 30, 2015	$ 971,217	17,251	988,468	(837,629)	150,839
Fiscal year 2015 – 2016 transactions:					
Reversal of prior year passenger facility charges accrual	(9,649)	—	(9,649)	—	(9,649)
Quarter ended September 30, 2015	24,574	243	24,817	—	24,817
Quarter ended December 31, 2015	22,457	212	22,669	—	22,669
Quarter ended March 31, 2016	23,977	305	24,282	—	24,282
Quarter ended June 30, 2016	27,424	360	27,784	(43,110)	(15,326)
Unrealized loss on investments	—	(50)	(50)	—	(50)
Passenger facility charges accrual	10,348	—	10,348	—	10,348
Total fiscal year 2015 – 2016 transactions	99,131	1,070	100,201	(43,110)	57,091
Program to date as of June 30, 2016	1,070,348	18,321	1,088,669	(880,739)	207,930
Fiscal year 2016 – 2017 transactions:					
Reversal of prior year passenger facility charges accrual	(10,348)	—	(10,348)	—	(10,348)
Quarter ended September 30, 2016	25,802	414	26,216	—	26,216
Quarter ended December 31, 2016	24,041	421	24,462	—	24,462
Quarter ended March 31, 2017	20,150	553	20,703	—	20,703
Quarter ended June 30, 2017	27,294	731	28,025	(23,363)	4,662
Unrealized loss on investments	—	(147)	(147)	—	(147)
Passenger facility charges accrual	17,016	—	17,016	—	17,016
Total fiscal year 2016 – 2017 transactions	103,955	1,972	105,927	(23,363)	82,564
Program to date as of June 30, 2017	$ 1,174,303	20,293	1,194,596	(904,102)	290,494

See accompanying independent auditors’ report and notes to schedule of passenger facility charge revenues and expenditures.

AIRPORT COMMISSION
CITY AND COUNTY OF SAN FRANCISCO
SAN FRANCISCO INTERNATIONAL AIRPORT

Notes to Schedule of Passenger Facility Charge Revenues and Expenditures

Year ended June 30, 2017

(1) General

The accompanying schedule of Passenger Facility Charge (PFC) revenues and expenditures includes activities related to applications 02-02-C-00-SFO, 03-03-C-01-SFO, 11-05-C-01-SFO, 13-06-C-00-SFO and 17-07-I-00-SFO of the PFC program of the Airport Commission, City and County of San Francisco, San Francisco International Airport (the Airport). The level of PFCs authorized, charge effective dates, and approved collection amounts of the Airport's PFC program are as follows:

Application number		Level of PFCs authorized	Charge effective date for collection		Amounts approved for collection (in thousands)
02-02-C-00-SFO	$	4.50	October 1, 2001	$	224,035
03-03-C-01-SFO		4.50	November 1, 2005		609,108
11-05-C-01-SFO		4.50	January 1, 2017		741,744
13-06-C-00-SFO		4.50	October 1, 2024		141,076
17-07-I-00-SFO		3.00	March 1, 2026		319,711
Total				$	2,035,674

(2) Basis of Accounting – Schedule of Passenger Facility Charge Revenues and Expenditures

The accompanying Schedule of Passenger Facility Charge Revenues and Expenditures (the Schedule) has been prepared on the accrual basis of accounting which is described in note 2a of the Airport's basic financial statements.

KPMG LLP
Suite 1400
55 Second Street
San Francisco, CA 94105

Independent Auditors' Report on Internal Control over Financial Reporting Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

The Honorable Mayor and Board of Supervisors
City and County of San Francisco:

We have audited, 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, the financial statements of the Airport Commission, City and County of San Francisco, San Francisco International Airport (the Airport), an enterprise fund of the City and County of San Francisco, California (the City), which comprise the statement of financial position as of and for the year ended June 30, 2017, and the related statements of revenues, expenses, and changes in financial position, and cash flows for the year then ended, and the related notes to the financial statements, and have issued a report thereon dated October 20, 2017.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Airport's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Airport's internal control. Accordingly, we do not express an opinion on the effectiveness of the Airport's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Airport's financial statements are free from 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*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Airport's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Airport's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

KPMG LLP

San Francisco, California
October 20, 2017

PASSENGER FACILITY CHARGE PROGRAM AUDIT REPORT

KPMG LLP
Suite 1400
55 Second Street
San Francisco, CA 94105

Independent Auditors' Report on Compliance with Requirements That Could Have a Direct and Material Effect on the Passenger Facility Charge Program and on Internal Control over Compliance in Accordance with the Passenger Facility Charge Audit Guide for Public Agencies

The Honorable Mayor and Board of Supervisors
City and County of San Francisco:

Report on Compliance for Passenger Facility Charge Program

We have audited the Airport Commission, City and County of San Francisco, San Francisco International Airport's (the Airport) compliance with the types of compliance requirements described in the Passenger Facility Charge Audit Guide for Public Agencies, issued by the Federal Aviation Administration (the Guide) that could have a direct and material effect on the Airport's passenger facility charge program for the year ended June 30, 2017.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to the passenger facility charge program.

Auditors' Responsibility

Our responsibility is to express an opinion on compliance for the Airport's passenger facility charge program based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the Guide. Those standards and the Guide require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on passenger facility charge occurred. An audit includes examining, on a test basis, evidence about the Airport's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for the passenger facility charge program. However, our audit does not provide a legal determination of the Airport's compliance.

Opinion

In our opinion, the Airport complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on the passenger facility charge program for the year ended June 30, 2017.

Report on Internal Control over Compliance

Management of the Airport is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the Airport's internal control over compliance with the types of requirements that could have a direct and material effect on the passenger facility charge program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance and to test and report on internal control over compliance in accordance with the Guide, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Airport's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A material weakness in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. A significant deficiency in internal control over compliance is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Guide. Accordingly, this report is not suitable for any other purpose.

KPMG LLP

San Francisco, California
October 20, 2017

AIRPORT COMMISSION
CITY AND COUNTY OF SAN FRANCISCO
SAN FRANCISCO INTERNATIONAL AIRPORT

Schedule of Findings and Responses

Year ended June 30, 2017

I. Summary of Auditors' Results

1. The type of report issued on whether the financial statements were prepared in accordance with generally accepted accounting principles: **Unmodified opinion**

2. Internal control deficiencies over financial reporting disclosed by the audit of the financial statements:

   - Material weaknesses: **No**
   - Significant deficiencies: **None Reported**

3. Noncompliance which is material to the financial statements: **No**

4. Internal control deficiencies over the passenger facility charge program:

   - Material weaknesses: **No**
   - Significant deficiencies: **None Reported**

5. The type of report issued on compliance for the passenger facility charge program: **Unmodified opinion**

6. Any audit findings: **No**

II. Findings and Responses Related to the Passenger Facility Charge Program

None