

# San Francisco Bay Area Rapid Transit District



**2006  
Annual  
Report**



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Thomas E. Margro



# Message from the General Manager

BART has always been known for its convenient, safe and reliable service and Fiscal Year 2006 was no exception. It was a year of steady ridership growth, diligence in providing safe and secure transportation and a commitment to sound fiscal decisions to maintain the reliable service on which our customers depend.

In FY 2006 BART responded to customer demand by increasing rush hour service to downtown Oakland and San Francisco, implementing a bold new anti-terrorism awareness campaign, advancing the Earthquake Safety Program and taking steps to secure the District's financial future with new labor contracts and a balanced budget.

As BART moves toward its 35th anniversary in September of 2007, steady ridership growth, system safety and reliable service for the Bay Area will remain the District's top priorities.



## Ridership Increases

BART's emphasis on providing safe, reliable and economical transportation continued to result in ridership increases. As the Bay Area experienced a modest economic recovery resulting in worsening traffic, coupled with increased gas prices, and bridge tolls, commuters turned to BART for cost-effective, dependable transportation. The FY06 ridership increases once again proved BART is of utmost importance to the Bay Area economy and quality of life.



SFO Station

## Earthquake Safety



Earthquake Safety Retrofit Construction  
Barge floats over Transbay Tube

With BART as the centerpiece of the regional transportation system, protecting BART's infrastructure against earthquakes is crucial. BART's \$1.3 billion Earthquake Safety Program, which will upgrade the original operating facilities to ensure they can return to operation shortly after a major earthquake, picked up speed as environmental analysis of the Transbay Tube and related work was completed. BART accelerated design of the retrofits to the Transbay Tube and awarded construction-related contracts. Construction work began on the Oakland end of the Transbay Tube in June 2006. Environmental clearance for the remainder of the original system (beyond the Transbay Tube and related work) is nearing completion and preliminary engineering is well underway.

## System Security

Like the March 2004 terror attacks in Madrid, the July 2005 attacks in London reemphasized the importance of securing the system against all threats. BART is ever-vigilant in its efforts to keep our passengers and the system safe. Still, BART needs more help. BART has identified at least \$250 million in unfunded security needs and is working hard to obtain at least a portion of the money. Work is ongoing to make the system more secure in many ways, including:

- ▶ Ongoing public awareness campaigns reminding passengers they are a critical component in keeping BART safe;
- ▶ The addition of three more highly trained, explosive detecting dogs to the BART Police Department's highly acclaimed K9 unit, provided by the Transportation Security Administration;
- ▶ BART's continual assessment and revision of its Emergency Plan and training of staff.



BART K-9 Team

## Labor Contracts

## Financial Responsibility

Maintaining a balanced bottom line is necessary to provide the reliable service our customers depend upon and deserve. In addition to new labor contracts, in June 2006, BART's Board of Directors passed a balanced budget for FY 07. This budget enables the District to continue BART's 95% passenger on-time performance, improve system upkeep and enhance safety and security efforts. In addition:

- ▶ A modest 3.7 percent fare increase went into effect January 1, 2006. This increase was the second in a series of inflation-based fare increases, which the BART Board approved in May 2003.
- ▶ The implementation of daily parking fees at the 10 busiest East Bay stations, which provided revenue enhancement with no significant impact on ridership.



## System Expansion

BART is moving ahead with several capital projects that would eventually expand the 43-station, 104-mile system:

- ▶ The West Dublin/Pleasanton infill station project is underway. This mixed-use development between Castro Valley and Dublin/Pleasanton Stations should open in FY 2009.
- ▶ The Oakland Airport Connector would link the Coliseum/Oakland Airport station to Oakland International Airport. In February 2006, BART issued a Request for Qualifications to interested parties and received responses from a number of highly qualified teams made up of consortiums of contractors, vehicle providers, transit system operators and international financiers.
- ▶ The eBART extension into Eastern Contra Costa County would extend service 21 miles beyond the Pittsburg/Bay Point Station toward Byron.
- ▶ The Warm Springs Extension would add 5.4 miles of new track south of Fremont Station to a new station in the Warm Springs district of Fremont.



*Future station west of Dublin/Pleasanton*

## Capitol Corridor

The Capitol Corridor, which provides inter-city rail service between San Jose and Sacramento, continues to flourish. In March 2006, the Capitol Corridor welcomed its 10 millionth passenger on board. 2006 marked the second year of BART's current five-year term as the Capitol Corridor's managing agency. BART was originally selected as the managing agency in February 1999.

## Always Looking Forward

BART upheld its reputation as one of the world's premier transit agencies with not only its outstanding performance and customer service, but also with its ongoing commitment to being an industry trendsetter.

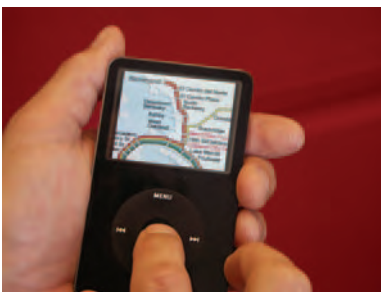
- ▶ The BART Board of Directors unanimously elected two African American women to BART's most powerful posts, making BART the first major transit agency in U.S. History to be led by two Black women. In December 2005 Director Carole Ward Allen, Ed.D., was elected Board President and Director Lynette Sweet was elected Vice President.
- ▶ In October 2005 BART became the first major transit agency in the nation to offer downloadable schedules and maps for the Apple iPod. The free "BART QuickPlanner for Apple iPod" allows customers to look up train departure times, view a color version of the official BART system map and learn general station information. The QuickPlanner for Apple iPod joins BART's QuickPlanners for Palm, Pocket PC and web-enabled mobile devices in the most comprehensive suite of mobile trip planning options in the nation.



*Carole Ward Allen  
Board President*



*Lynette Sweet  
Board Vice President*



*iPod with downloadable BART map and train schedules*

- ▶ The California Council for Environmental and Economic Balance honored BART, along with the Bay Area Air Quality Management District and the Metropolitan Transportation Commission, with the "Edmund G. 'Pat' Brown Award" for balancing environmental and economic principles with the highly successful Spare the Air/Free Morning Commute campaign.

Coming off one of the worst economic downturns in BART's history, FY 2006 was the first year in which we could focus on a budget designed to improve service without making cuts to staff and administrative budgets. As a result, we were able to provide another year of high quality, reliable BART service, steady BART leadership and trend-setting BART innovation. The groundwork is in place for an even more successful 2007, as BART continues to carry the Bay Area into the future.



*Rockridge BART Station*



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To the Board of Directors of the San Francisco Bay Area Rapid Transit District  
Oakland, California

We have audited the accompanying financial statements of the Enterprise Fund and the Retiree Health Benefit Trust Fund of the San Francisco Bay Area Rapid Transit District (the District) as of and for the years ended June 30, 2006 and 2005, which collectively comprise the District's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the District's management. Our responsibility is to express opinions on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the Enterprise Fund and the Retiree Health Benefit Trust Fund of the District, as of June 30, 2006 and 2005 and the respective changes in financial position and cash flows, where applicable, thereof for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated November 29, 2006 on our consideration of the District's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of the District's internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the District'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* and should be considered in assessing the results of our audit.

The management's discussion and analysis, as listed in the table of contents, is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information

*Macias Gini & O'Connell LLP*

Certified Public Accountants

Walnut Creek, California

November 29, 2006

## Introduction

The following discussion and analysis of the financial performance and activity of the San Francisco Bay Area Rapid Transit District (the "District") provide an introduction and understanding of the basic financial statements of the District for the years ended June 30, 2006 and 2005. This discussion was prepared by management and should be read in conjunction with the financial statements and the notes thereto, which follow this section.

The District is an independent agency created in 1957 by the legislature of the State of California for the purpose of providing an adequate, modern, interurban mass rapid transit system in the various portions of the metropolitan area surrounding the San Francisco Bay. The District started its revenue operations in September 1972. It presently owns a 104-mile, 43-station system serving the four counties of Alameda, Contra Costa, San Francisco and San Mateo. The government of the District is vested in a Board of Directors composed of nine members, each representing an election district within the District.

## The Financial Statements

The basic financial statements provide information about the District's Enterprise Fund and the Retiree Health Benefit Trust. The financial statements are prepared in accordance with accounting principles generally accepted in the United States of America as promulgated by the Governmental Accounting Standards Board ("GASB") principles.

## Overview of the Enterprise Fund Financial Statements

The *Statement of Net Assets* reports assets, liabilities and the difference as *net assets*. The entire equity section is combined to report total net assets and is displayed in three components - *invested in capital assets, net of related debt; restricted net assets; and unrestricted net assets*.

The net asset component *invested in capital assets, net of related debt*, consists of capital assets, including restricted capital assets, net of accumulated depreciation and reduced by the outstanding balances of any borrowings attributable to the acquisition, construction or improvements of those assets.

*Restricted net assets* consist of assets where constraints on their use are either (a) externally imposed by creditors (such as debt covenants), grantors, contributors, or laws or regulations of other governments or (b) imposed by law through constitutional provisions or enabling legislation.

*Unrestricted net assets* consist of net assets that do not meet the definition of restricted or invested in capital assets, net of related debt. This net asset component includes net assets that have been designated by management for specific purposes, which in the case of the District include allocations to fund capital projects, and other liabilities, which indicate that management does not consider them to be available for general operations.

The *Statement of Revenues, Expenses and Changes in Net Assets* consists of operating and nonoperating revenues and expenses based upon definitions provided by GASB Statement No. 33, *Accounting and Financial Reporting for Nonexchange Transactions*, as amended by GASB Statement No. 36, *Recipient Reporting for Certain Shared Nonexchange Revenues*, and GASB Statement No. 34, *Basic Financial Statements-and Management's Discussion and Analysis-for State and Local Governments*, as amended by GASB Statement No. 37, *Basic Financial Statements-and Management's Discussion and Analysis for State and Local Governments: Omnibus*. Accordingly, significant recurring sources of the District's revenues, such as capital contributions, are reported separately, after nonoperating revenues and expenses.

*Statement of Cash Flows* is presented using the direct method and includes a reconciliation of operating loss to net cash used in operating activities.

## Financial Highlights

### Statements of Revenues, Expenses and Changes in Net Assets

A summary of the District's *Statements of Revenues, Expenses and Changes in Net Assets* for fiscal years 2006, 2005 and 2004 is as follows (dollar amounts in thousands):

	<u>2006</u>	<u>2005</u>	<u>2004</u>
Operating revenues	\$ 275,124	\$ 248,644	\$ 234,546
Operating expenses, net	<u>(573,187)</u>	<u>(548,197)</u>	<u>(498,503)</u>
Operating loss	(298,063)	(299,553)	(263,957)
Nonoperating revenues, net	232,900	189,059	162,178
Capital contributions	62,487	77,947	75,010
<b>Special item</b>	-	<b>(36,222)</b>	-
Change in net assets	(2,676)	(68,769)	(26,769)
Net assets, beginning of year	<u>4,328,964</u>	<u>4,397,733</u>	<u>4,424,502</u>
Net assets, end of year	<u>\$4,326,288</u>	<u>\$4,328,964</u>	<u>\$4,397,733</u>

### Operating Revenues

The increase of \$26,480,000 in operating revenues in fiscal year 2006 is mainly credited to (1) an increase of \$22,587,000 from passenger fares and (2) a \$3,893,000 increase in concession and other revenues. The increase in passenger fares is due to a 4% increase in weekday passenger trips from 310,717 in fiscal year 2005 to 322,965 in fiscal year 2006 and the 3.7% increase in passenger fare effective January 1, 2006. The increase in concession and other revenues is due to increases in advertising revenue of \$1,528,000, in reimbursements of support costs from telecommunication and other projects of \$1,486,000, and in traffic fine collections and concession revenues from public phones and newsstands of \$963,000.

In fiscal year 2005, the operating revenues increased by \$14,098,000. The increase can be attributed to (1) an increase of 4,148 or 1.4% on the average weekday ridership from 306,569 in 2004 to 310,717 in 2005, and (2) the full year effect on fiscal year 2005 of the 10% fare increase on January 1, 2004, as compared to six months only (January 2004 to June 2004) in fiscal year 2004.

### Operating Expenses

The net operating expenses for fiscal year 2006 increased by \$24,990,000, which is primarily due to an increase in the employer's contribution to CalPERS of \$12,739,000, depreciation expense of \$16,609,000, health insurance premium payments of \$4,889,000, and offset by decrease in other employee and retiree compensation of \$6,188,000 and workers compensation expense accrual (\$3,536,000). The annual required contribution rates to CalPERS increased in 2006 – 8.717% from 2.615% in 2005 for Miscellaneous Employees, and 32.324% from 28.910% in 2005 for Safety Employees.

Net operating expenses increased by \$49,694,000 in fiscal year 2005 which was mainly due to (1) an increase in depreciation expense, a non-cash item, of \$12,129,000; (2) an increase of \$24,550,000 in pension contributions to CalPERS due to the resumption in fiscal year 2005 of the employer contributions for the Miscellaneous Plan and an increase in the required employer contribution rate for the Safety Plan from 2.897% to 28.910%; (3) in fiscal year 2005 the additional 3.5% money purchase pension plan contributions to employees was discontinued which resulted in an expense reduction of \$7,120,000; (4) an increase in the expense accrual for workers' compensation self-insurance reserve of \$4,057,000; (5) increase in the employees salaries and benefits totaling an estimated amount of \$19,000,000 because of the 6% contractual salary increase in fiscal year 2005, accrual of arbitration settlements and severance payments due to position reductions.



## Nonoperating Revenues

The net nonoperating revenues increased by \$43,841,000 in fiscal year 2006. The increase is largely due to an increase in sales tax revenues of \$13,288,000 directly attributable to the strong economy in the District counties, receipt of property tax revenues of \$17,652,000 allocated for debt service payments of the 2005 General Obligation Bonds, the net gain received from the sale of properties of \$11,042,000, and a decrease in interest expense of \$5,110,000 primarily from substantial reduction in the outstanding balance of the FTA Capital Grant Bonds, and offset by a net decrease in investment income of \$4,720,000. The net decrease in investment income is the result of a decrease in the fair value amounting to \$15,189,000 of investments and deposits related to the 2002 lease/leaseback of certain rail traffic control equipment offset by an increase of \$10,469,000 in the interest income from all investments of the general fund, debt service funds and construction funds as a result of better interest rates in fiscal year 2006 and higher investment balances during the year.

Net nonoperating revenues for fiscal year 2005 increased by \$26,881,000. The increase is accounted for as follows: (1) increase of \$7,826,000 in sales tax revenues; (2) an increase of \$13,475,000 in investment income which is mainly due to (a) an increase of \$12,234,000 in interest income recognized from the deposits for sublease obligation related to the lease/leaseback of rail traffic control equipment in 2002 and (b) an increase in the average investment earnings rate from 1.70% in 2004 to 2.26% in 2005; (3) a decrease in interest expense of \$6,902,000 mainly due to the prepayment of a portion of the FTA Capital Grant Bonds, 2001 Series A, with principal amounts totaling \$88,995,000 due in fiscal years 2008 and 2009; (4) the financial assistance received from San Mateo County Transit District (SamTrans) for the net operating expenses of the San Francisco International Airport Extension decreased by \$3,137,000 due to the increase in fare revenues from increased ridership and from cost reduction due to reduced train service and shorter trains.

## Capital Contributions

The revenues from capital contributions relate to grants and other financial assistance received by the District from the federal, state and local agencies to fund capital projects. The District receives reimbursement-type grants on which the District has to first incur eligible costs under the provider's program before qualifying for the grant resources. Revenues from capital contributions are recognized at the time when the eligible project costs are incurred. The capital contributions in fiscal year 2006 showed a decrease of \$15,460,000 and an increase of \$2,937,000 in fiscal year 2005.

## Statements of Net Assets

A comparison of the District's *Statements of Net Assets* as of June 30, 2006, 2005 and 2004 is as follows (dollar amounts in thousands):

	<u>2006</u>	<u>2005</u>	<u>2004</u>
Current assets	\$ 644,290	\$ 525,254	\$ 425,715
Noncurrent assets - capital assets, net	4,944,189	4,997,869	5,009,777
Noncurrent assets - other	353,529	486,394	703,622
Total assets	<u>5,942,008</u>	<u>6,009,517</u>	<u>6,139,114</u>
Current liabilities	358,336	370,415	300,865
Noncurrent liabilities	1,257,384	1,310,138	1,440,516
Total liabilities	<u>1,615,720</u>	<u>1,680,553</u>	<u>1,741,381</u>
Net assets			
Invested in capital assets, net of related debt	4,008,057	4,037,420	3,884,807
Restricted net assets	137,342	180,290	357,343
Unrestricted net assets	180,889	111,254	155,583
Total net assets	<u>\$ 4,326,288</u>	<u>\$ 4,328,964</u>	<u>\$ 4,397,733</u>



In fiscal year 2006, noncurrent assets – other decreased by \$132,865,000, which is mainly due to the decrease in capital grants receivable for the SFO Extension due to the receipt of the federal allocations of \$114,263,000 in fiscal year 2006, the application of a portion (\$42,900,000) of the deposit related to the 2002 lease/leaseback of certain rail traffic control equipment as payment of the sublease obligation, and offset by an increase in deferred changes of \$24,359,000 primarily from deferred interest expense recognized in fiscal year 2006 related to the full defeasance of 1995 and 1999 Sales Tax Revenue Bonds and partial defeasance of 1998 and 2001 Sales Tax Revenue Bonds.

The noncurrent assets – other decreased by \$217,228,000 in 2005. The decrease is mainly attributed to (1) a decrease in unrestricted investments of \$35,952,000 due to the use of District funds for operating and capital expenditures; (2) a decrease in restricted cash, cash equivalents and investments amounting to \$23,472,000 due to the use of debt service reserve funds for the payment of long-term debt and the expenditure of bond proceeds for capital projects; and (3) a decrease of \$162,065,000 in 2005 in the receivable from the SFO Federal Full Funding Agreement because of the receipt of the funding allocations for both fiscal years 2004 and 2005.

The current liabilities as of June 30, 2006 decreased by \$12,079,000 which is mainly due to the decrease in the current portion of long-term debt because of the advance refunding of certain sales tax revenue bonds from the proceeds of the 2005 Bonds.

The current liabilities as of June 30, 2005 increased by \$69,550,000. The increase is due to (1) an increase in the current portion of long-term debt totaling \$79,151,000 mainly from the 1998 Sales Tax Revenue Bond, the construction loans and the lease/leaseback obligation; and (2) a decrease of \$10,100,000 in accounts payable and other liabilities due to the timing of payments to vendors and contractors.

## Capital Assets

The District's capital assets, before accumulated depreciation, increased by \$78,869,000 in 2006 and by \$110,693,000 in 2005. The major additions during the years included capital expenditures for the acquisition and/or major improvements on the following assets:

- core system and extensions amounting to \$83,817,000 in 2006 and \$70,797,000 in 2005;
- train control equipment totaling \$20,822,000 in 2006 and \$25,038,000 in 2005;
- revenue transit vehicles in the amount of \$4,498,000 in 2006 and \$9,494,000 in 2005;
- automatic fare collection equipment amounting to \$6,615,000 in 2006 and \$11,488,000 in 2005; and
- Business Advancement Plan (BAP) which is a project to replace the information technology systems supporting the District's administrative business totaling \$2,788,000 in 2006 and \$10,458,000 in 2005.

Details of the capital assets, net of accumulated depreciation, as of June 30, 2006, 2005 and 2004 are as follows (dollar amounts in thousands):

	<u>2006</u>	<u>2005</u>	<u>2004</u>
Land	\$ 524,392	\$ 513,849	\$ 481,466
Stations, track, structures and improvements	2,929,155	2,738,045	2,555,907
Buildings	5,738	18,072	22,409
Revenue transit vehicles	539,634	586,042	628,460
Other	264,325	280,052	288,625
Construction in progress	680,945	861,809	1,032,910
Total capital assets	<u>\$ 4,944,189</u>	<u>\$ 4,997,869</u>	<u>\$ 5,009,777</u>

The District has entered into contracts for the construction of various facilities and equipment totaling approximately \$553,859,000 at June 30, 2006 and \$492,974,000 at June 30, 2005.

## Long-Term Debt

The outstanding balance of long-term debt showed decreases of \$88,589,000 and \$61,054,000 at the end of fiscal years 2006 and 2005, respectively. Below is a summary of long-term debt as of June 30, 2006, 2005 and 2004 (including current portion but excluding unamortized balance of debt issue costs and bond premium/discounts) (dollar amounts in thousands):

	<u>2006</u>	<u>2005</u>	<u>2004</u>
Bonds payable from and collateralized by a pledge of sales tax revenues	\$ 763,875	\$ 714,820	\$ 732,365
Bonds payable from and collateralized by the Federal Full Funding Grant Agreement for the SFO Extension	102,030	197,250	347,540
Notes payable from bridge toll revenues	21,785	30,280	38,355
Construction loans payable from the net operating surplus of the SFO Extension	88,500	88,500	88,500
Construction loan for temporary cash flow requirements of the SFO Extension	40,895	35,400	27,325
Lease/leaseback obligation, including accumulated accretion, for rail traffic control equipment	158,009	197,433	190,652
Bonds payable from the premium fare imposed on the passengers who board on or depart from the San Francisco International Airport Station	56,715	56,715	56,715
General obligation bonds	<u>100,000</u>	<u>100,000</u>	<u>-</u>
Total long-term debt	<u>\$1,331,809</u>	<u>\$1,420,398</u>	<u>\$1,481,452</u>

In fiscal year 2006 the principal payments of the bonds payable from the Federal Full Funding Grant Agreement for the SFO Extension include prepayments of bonds due in fiscal year 2008 amounting to \$5,000,000 (\$1,040,000 in fiscal year 2005) and \$15,710,000 (\$87,955,000 in fiscal year 2005) of the bonds due in fiscal year 2009.

## Additions to Long-Term Debt in Fiscal Year 2006

There were two new bonds issues in fiscal year 2006, which are the Sales Tax Revenue Refunding Bonds, Series 2005 A issued in August 2005 with a principal amount of \$352,095,000 (the "2005 Bonds") and the Sales Tax Revenue Bonds, Series 2006 issued in June 2006 with an aggregate principal amount of \$64,915,000 (the "2006 Bonds"). Both issues are payable from and secured by the District's sales tax revenues.

The proceeds from the 2005 Bonds were mostly used to advance refund certain bonds then outstanding to achieve cash flow savings. Payments of principal of and interest on the 2005 Bonds maturing on or after July 1, 2008 are insured by a financial guaranty insurance policy issued by MBIA Insurance Corporation. The insured 2005 Bonds were rated AAA, Aaa and AAA by Standard & Poor's, Moody's Investors Service and Fitch Ratings, respectively.

The proceeds from the 2006 Bonds are to be used for the construction of a new West Dublin/Pleasanton Station and other related improvements. Payments of principal of and interest on the 2006 Bonds when due are insured by a municipal bond insurance policy issued by Financial Security Assurance. The insured 2006 Bonds were rated AAA, Aaa, and AAA by Standard & Poor's, Moody's Investors Service and Fitch Ratings, respectively.

## Addition to Long-Term Debt in Fiscal Year 2005

On May 13, 2005, the District issued the General Obligation Bonds (Election of 2004), 2005 Series A (2005 GO Bonds) with an aggregate principal amount of \$100,000,000. The 2005 GO Bonds constitute a portion of the total authorized amount of \$980,000,000 of general obligation bonds of the District duly authorized by at least two-thirds of the qualified voters of the District voting on a ballot measure ("Measure AA") at an election held on November 2, 2004. The 2005 GO Bonds were issued to finance earthquake safety improvements to BART facilities and structures. The 2005 GO Bonds are general obligations of the District, payable from and secured solely by property taxes levied by the District, as authorized by Measure AA, upon all property subject to taxation within the three BART Counties of Alameda, Contra Costa and San Francisco. Three national rating agencies have assigned their municipal bond ratings of AAA, Aa1 and AA+ to the 2005 GO Bonds.

## Statements of Cash Flows/Cash, Cash Equivalents and Investments

A comparative presentation of the major sources and uses of cash for 2006, 2005 and 2004 is as follows (dollar amounts in thousands):

	<u>2006</u>	<u>2005</u>	<u>2004</u>
Net cash used in operating activities	\$(150,474)	\$(165,472)	\$(148,899)
Net cash provided by noncapital financing activities	179,431	113,868	152,417
Net cash provided by (used in) capital and related financing activities	72,775	64,898	(65,687)
Net cash provided by (used in) investing activities	<u>(125,409)</u>	<u>107,877</u>	<u>10,157</u>
Net change in cash and cash equivalents	(23,677)	121,171	(52,012)
Cash and cash equivalents, beginning of year	<u>351,922</u>	<u>230,751</u>	<u>282,763</u>
Cash and cash equivalents, end of year	328,245	351,922	230,751
Investments, end of year	<u>404,950</u>	<u>266,664</u>	<u>356,440</u>
Cash, cash equivalents and investments, end of year	<u>\$ 733,195</u>	<u>\$ 618,586</u>	<u>\$ 587,191</u>

The total cash, cash equivalents and investments held by the District and trustee banks at June 30, 2006 amounted to \$733,195,000, an increase of \$114,609,000 compared to \$618,586,000 reported as of June 30, 2005. The increase is primarily due to (1) an increase in cash receipts from passenger fares of \$19,147,000; (2) an increase in cash received from sales tax revenues of \$13,288,000; (3) a receipt of property tax revenues totaling \$17,652,000 for debt service payments of the 2005 General Obligation Bonds; (4) a net cash inflow of \$55,281,000 from the proceeds of the 2006 Bonds issued in late June 2006; and (5) net cash generated of \$22,777,000 from the sale of real properties.

In fiscal year 2005, cash, cash equivalents and investments increased by \$31,395,000. The increase can be mainly attributed to (1) \$100,000,000 from the proceeds of the 2005 General Obligation Bonds received on May 26, 2005; (2) \$36,222,000 cash transferred to the Retiree Health Benefit Trust; (3) an increase of \$55,045,000 in principal and interest payments on long-term debt, particularly because of the prepayment of a portion of the FTA Capital Grant Bonds; and (4) an increase of \$26,716,000 in investment income, fiber optics revenue and other operating revenues.

## Contacting the District's Financial Management

The District's financial report is designed to provide the District's Board of Directors, management, investors, creditors, legislative and oversight agencies, citizens and customers with an overview of the District's finances and to demonstrate its accountability for funds received. For additional information about this report, please contact Scott Schroeder, Controller-Treasurer, at 300 Lakeside Drive, P.O. Box 12688, Oakland, California 94604.

# SAN FRANCISCO BAY AREA RAPID TRANSIT DISTRICT

## Enterprise Fund


### Statements of Net Assets

June 30, 2006 and 2005

(dollar amounts in thousands)

	<u>2006</u>	<u>2005</u>
<b>Assets</b>		
<b>Current assets</b>		
<b>Unrestricted assets</b>		
Cash and cash equivalents	\$ 129,349	\$ 162,404
Investments	167,708	61,048
Capital grants receivable	32,730	29,712
Receivables and other assets	16,722	30,517
Current portion of capital lease receivable	3,154	3,154
Materials and supplies	29,804	27,441
Total unrestricted current assets	<u>379,467</u>	<u>314,276</u>
<b>Restricted assets</b>		
Cash and cash equivalents	198,896	189,518
Investments	65,927	21,460
Total restricted current assets	<u>264,823</u>	<u>210,978</u>
Total current assets	<u>644,290</u>	<u>525,254</u>
<b>Noncurrent assets</b>		
<b>Capital assets</b>		
Nondepreciable	1,205,337	1,375,658
Depreciable, net of accumulated depreciation	3,738,852	3,622,211
<b>Unrestricted assets</b>		
Investments	-	17,793
Long-term portion of capital lease receivable	11,041	14,195
Receivables and other assets	25,478	1,113
<b>Restricted assets</b>		
Investments	171,315	166,363
Capital grants receivable	2,425	115,438
Receivables and other assets	39,923	25,439
Deposits for sublease obligation	103,347	146,053
Total noncurrent assets	<u>5,297,718</u>	<u>5,484,263</u>
Total assets	<u>5,942,008</u>	<u>6,009,517</u>

The accompanying notes are an integral part of these financial statements.



**SAN FRANCISCO  
BAY AREA RAPID TRANSIT DISTRICT  
Enterprise Fund  
Statements of Net Assets (continued)  
June 30, 2006 and 2005**

(dollar amounts in thousands)

	<u>2006</u>	<u>2005</u>
<b>Liabilities and Net Assets</b>		
<b>Liabilities</b>		
Current liabilities		
Accounts payable and other liabilities	\$ 183,369	\$ 175,417
Current portion of long-term debt, net	152,172	172,782
Self-insurance liabilities	9,174	9,340
Deferred revenue	10,467	9,722
Current portion of capital lease liability	3,154	3,154
Total current liabilities	<u>358,336</u>	<u>370,415</u>
Noncurrent liabilities		
Long-term debt, net of current portion	1,187,257	1,233,287
Self-insurance liabilities	19,180	19,300
Deferred revenue	37,789	40,622
Capital lease liability, net of current portion	11,041	14,195
Other liabilities	2,117	2,734
Total noncurrent liabilities	<u>1,257,384</u>	<u>1,310,138</u>
Total liabilities	<u>1,615,720</u>	<u>1,680,553</u>
Net assets		
Invested in capital assets, net of related debt	4,008,057	4,037,420
Restricted net assets		
For debt service and other liabilities	137,342	180,290
Unrestricted net assets	180,889	111,254
Total net assets	<u>\$4,326,288</u>	<u>\$ 4,328,964</u>

*The accompanying notes are an integral part of these financial statements.*

**SAN FRANCISCO**  
**BAY AREA RAPID TRANSIT DISTRICT**  
**Enterprise Fund**  
**Statements of Revenues, Expenses and Changes in Net Assets**  
**For the years ended June 30, 2006 and 2005**  
(dollar amounts in thousands)

	<u>2006</u>	<u>2005</u>
<b>Operating revenues</b>		
Fares	\$ 256,238	\$ 233,651
Other	18,886	14,993
Total operating revenues	<u>275,124</u>	<u>248,644</u>
<b>Operating expenses</b>		
Transportation	125,022	127,391
Maintenance	168,226	163,051
Police services	39,109	37,510
Construction and engineering	17,777	16,030
General and administrative	111,532	109,130
Depreciation	145,306	128,697
Total operating expenses	<u>606,972</u>	<u>581,809</u>
Less - capitalized costs	<u>(33,785)</u>	<u>(33,612)</u>
Net operating expenses	<u>573,187</u>	<u>548,197</u>
Operating loss	<u>(298,063)</u>	<u>(299,553)</u>
<b>Nonoperating revenues (expenses)</b>		
Transactions and use tax (sales tax)	191,680	178,392
Property tax	43,024	22,412
Operating financial assistance	15,749	16,680
Investment income	31,695	36,415
Interest expense	(60,155)	(65,265)
Gain from sale of property, net	11,042	-
Other income (expense), net	(135)	425
Total nonoperating revenues, net	<u>232,900</u>	<u>189,059</u>
Change in net assets before capital contributions and special item	(65,163)	(110,494)
Capital contributions	62,487	77,947
Special item: contributions to Retiree Health Benefit Trust	-	(36,222)
Change in net assets	<u>(2,676)</u>	<u>(68,769)</u>
Net assets, beginning of year	<u>4,328,964</u>	<u>4,397,733</u>
Net assets, end of year	<u>\$4,326,288</u>	<u>\$4,328,964</u>

*The accompanying notes are an integral part of these financial statements.*

**SAN FRANCISCO**  
**BAY AREA RAPID TRANSIT DISTRICT**  
**Enterprise Fund**  
**Statements of Cash Flows**  
**For the years ended June 30, 2006 and 2005**  
(dollar amounts in thousands)

	<u>2006</u>	<u>2005</u>
<b>Cash flows from operating activities</b>		
Receipts from customers	\$ 253,706	\$ 234,559
Payments to suppliers	(110,323)	(125,609)
Payments to employees	(310,764)	(301,485)
Other operating cash receipts	16,907	27,063
Net cash used in operating activities	<u>(150,474)</u>	<u>(165,472)</u>
<b>Cash flows from noncapital financing activities</b>		
Transactions and use tax (sales tax) received	134,790	118,879
Property tax received	24,343	22,280
Financial assistance received	20,298	8,931
Contributions to the Retiree Health Benefit Trust	-	<u>(36,222)</u>
Net cash provided by noncapital financing activities	<u>179,431</u>	<u>113,868</u>
<b>Cash flows from capital and related financing activities</b>		
Transactions and use tax (sales tax) received	56,890	59,513
Property tax received	17,652	-
Capital grants received	179,624	237,225
Proceeds from issuance of 2005 Sales Tax Revenue Bonds	352,095	-
Proceeds from issuance of 2006 Sales Tax Revenue Bonds	64,915	-
Proceeds from issuance of 2005 General Obligation Bonds	-	100,000
Proceeds from construction loans	10,000	10,000
Proceeds from sale of property and equipment	22,777	-
Expenditures for facilities, property and equipment	(109,443)	(112,981)
Principal paid on long-term debt	(475,996)	(175,910)
Payments of long-term debt issuance and service costs	(4,054)	(2,161)
Premium received from issuance of long-term debt	17,773	2,717
Interest paid on long-term debt	(63,812)	(53,611)
Principal payments received from installment receivable	104	106
Advances from local funding agencies	4,250	-
Net cash provided by capital and related financing activities	<u>72,775</u>	<u>64,898</u>

*The accompanying notes are an integral part of these financial statements.*



# SAN FRANCISCO BAY AREA RAPID TRANSIT DISTRICT

## Enterprise Fund

### Statements of Cash Flows (continued)

For the years ended June 30, 2006 and 2005

(dollar amounts in thousands)

	<u>2006</u>	<u>2005</u>
<b>Cash flows from investing activities</b>		
Proceeds from sale and maturity of investments	\$ 360,349	\$ 306,405
Purchase of investments	(509,104)	(217,403)
Investment income	<u>23,346</u>	<u>18,875</u>
Net cash provided by (used in) investing activities	<u>(125,409)</u>	<u>107,877</u>
Net change in cash and cash equivalents	(23,677)	121,171
Cash and cash equivalents, beginning of year	<u>351,922</u>	<u>230,751</u>
Cash and cash equivalents, end of year	<u>\$ 328,245</u>	<u>\$ 351,922</u>

### Reconciliation of cash and cash equivalents to the Statements of Net Assets

Current, unrestricted assets - cash and cash equivalents	\$ 129,349	\$ 162,404
Current, restricted assets - cash and cash equivalents	<u>198,896</u>	<u>189,518</u>
Total cash and cash equivalents	<u>\$ 328,245</u>	<u>\$ 351,922</u>

### Reconciliation of operating loss to net cash used in operating activities

Operating loss	\$(298,063)	\$(299,553)
Adjustments to reconcile operating loss to net cash used in operating activities:		
Depreciation	145,306	128,697
Amortization of deferred charges	112	83
Net effect of changes in		
Decrease in receivables and other assets	3,331	1,414
(Increase) in materials and supplies	(2,363)	(1,749)
Increase (decrease) in accounts payable and other liabilities	2,330	(8,211)
Increase (decrease) in self-insurance liabilities	(286)	1,633
Increase (decrease) in deferred revenue	<u>(841)</u>	<u>12,214</u>
Net cash used in operating activities	<u>\$(150,474)</u>	<u>\$(165,472)</u>

### Noncash transactions

Capital assets acquired with a liability at year-end	\$ 41,771	\$ 39,437
Lease/leaseback obligation additions	9,242	10,837
Lease/leaseback obligation amortization	50,147	6,716
Increase (decrease) in fair value of investments	(8,108)	8,582
Amortization of long-term debt premium, discount and issue costs	(988)	274
Amortization of deferred interest on early debt retirement	931	478
Amortization of deferred gain on lease/leaseback transaction	1,482	1,482

The accompanying notes are an integral part of these financial statements.



**SAN FRANCISCO  
BAY AREA RAPID TRANSIT DISTRICT  
Retiree Health Benefit Trust  
Statements of Trust Net Assets  
June 30, 2006 and 2005**

(dollar amounts in thousands)

	<u>2006</u>	<u>2005</u>
<b>Assets</b>		
Interest receivable and other assets	\$ 222	\$ 187
Pending trades receivable	6,074	5,764
Investments		
Domestic common stocks	24,207	20,605
U.S. Treasury obligations	11,099	9,361
Money market mutual funds	3,455	5,770
Corporate obligations	2,827	3,649
Foreign stocks	428	-
Foreign obligations	336	205
Total investments	<u>42,352</u>	<u>39,590</u>
Total assets	<u>48,648</u>	<u>45,541</u>
<b>Liabilities</b>		
Accounts payable	66	19
Pending trades payable	8,960	8,317
Total liabilities	<u>9,026</u>	<u>8,336</u>
<b>Net assets held in trust for retiree health benefits</b>	<u>\$39,622</u>	<u>\$37,205</u>

*The accompanying notes are an integral part of these financial statements.*

**SAN FRANCISCO**  
**BAY AREA RAPID TRANSIT DISTRICT**  
**Retiree Health Benefit Trust**  
**Statements of Changes in Trust Net Assets**  
**For the years ended June 30, 2006 and 2005**  
(dollar amounts in thousands)

	<u>2006</u>	<u>2005</u>
<b>Additions</b>		
Employer contributions	\$ -	\$36,222
Investment income (expense)		
Interest income	1,099	593
Net appreciation in fair value of investments	1,617	488
Investment expense	<u>(280)</u>	<u>(54)</u>
Net investment income	<u>2,436</u>	<u>1,027</u>
Total additions	<u>2,436</u>	<u>37,249</u>
<b>Deductions</b>		
Legal fees	5	44
Insurance expense	<u>14</u>	<u>-</u>
Total deductions	<u>19</u>	<u>44</u>
Increase in trust net assets	<u>2,417</u>	<u>37,205</u>
<b>Net assets held in trust for retiree health benefits:</b>		
Beginning of year	<u>37,205</u>	<u>-</u>
End of year	<u>\$39,622</u>	<u>\$37,205</u>

*The accompanying notes are an integral part of these financial statements.*

## 1. Reporting Entity and Summary of Significant Accounting Policies

### Description of Reporting Entity

The San Francisco Bay Area Rapid Transit District (the "District") is a public agency created by the legislature of the State of California in 1957 and regulated by the San Francisco Bay Area Rapid Transit District Act, as amended, and subject to transit district law as codified in the California Public Utilities Code. The disbursement of funds received by the District is controlled by statutes and by provisions of various grant contracts entered into with federal, state and local agencies.

The District has defined its financial reporting entity in accordance with the Governmental Accounting Standards Board ("GASB") Statement No. 14, *The Financial Reporting Entity*, which states that the financial reporting entity should consist of (a) the primary government, (b) the organizations for which the primary government is financially accountable, and (c) the other organizations for which the nature and significance of their relationship with the primary government are such that exclusion would cause the reporting entity's financial statements to be misleading or incomplete. Based on this definition, and the fact that the Transit Financing Authority (the "Authority") provides services almost entirely to the District (the "primary government"), the Authority's financial information is presented as a blended component unit of the District's financial statements (See Note 15).

### Basis of Accounting and Presentation

The basic financial statements provide information about the District's Enterprise Fund and the Retiree Health Benefit Trust Fund. Separate statements for each fund category – proprietary and fiduciary – are presented. The basic financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of the related cash flows. On an accrual basis, revenues from operating activities are recognized in the fiscal year that the operations were provided; revenues from property taxes and sales taxes are recognized in the fiscal year for which the taxes are levied; revenue from grants is recognized in the fiscal year in which all eligibility requirements have been satisfied; and revenue from investments is recognized when earned.

The Enterprise Fund, a proprietary fund, distinguishes operating revenues and expenses from nonoperating items. The District's operating revenues are generated directly from its transit operations and consist principally of passenger fares. Operating expenses for the transit operations include all costs related to providing transit services. These costs include labor, fringe benefits, materials, supplies, services, utilities, leases and rentals, and depreciation on capital assets. All other revenues and expenses not meeting these definitions are reported as nonoperating revenues and expenses.

The District applies all applicable GASB pronouncements as well as Financial Accounting Standards Board ("FASB") Statements and Interpretations, Accounting Principles Board ("APB") Opinions and Accounting Research Bulletins ("ARBs") of the Committee on Accounting Procedures issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements. The District has elected under GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, not to apply FASB Statements and Interpretations issued after November 30, 1989, due to the nature of the District's operations.

The Retiree Health Benefit Trust Fund, a fiduciary fund, is used to account for assets held by the District as a trustee to pay retiree health care premiums. The assets of the Trust cannot be used to support the District's programs.

### Cash Equivalents

For purposes of the statements of cash flows, the District considers all highly liquid investments with a maturity of three months or less when purchased to be cash equivalents.

### Investments

The District records investment transactions on the trade date. Investments in nonparticipating interest-earning investment contracts (certificates of deposits and guaranteed investment contracts) are reported at cost and all other investments are at fair value in accordance with GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*. Fair value is defined as the amount that the District could reasonably expect to receive for an investment in a current sale between a willing buyer and a willing seller and is generally measured by quoted market prices. As a matter of policy, the District usually holds investments until their maturity.



## **Restricted Assets**

Certain assets are classified as restricted assets on the statement of net assets because their use is subject to externally imposed stipulations, either by certain bond covenants, laws or regulations or provisions of debt agreements.

## **Capital Grants/Contributions**

The District receives grants from the Federal Transit Administration (“FTA”) and other agencies of the U.S. Department of Transportation, the State of California, and local transportation funds for the acquisition of transit-related equipment and improvements. In accordance with GASB Statement No. 33, *Accounting and Financial Reporting for Nonexchange Transactions*, capital contributions are required to be included in the determination of changes in net assets resulting in an increase in net revenue of \$62,487,000 and \$77,947,000 for fiscal years 2006 and 2005, respectively. Capital grants receivable represent amounts expected from governmental agencies to reimburse the District for costs incurred for capital projects (see Notes 9 and 10).

## **Materials and Supplies**

Materials and supplies consist primarily of replacement parts for the system and rail vehicles, which are stated at cost using the average-cost method. Materials and supplies are expensed as consumed.

## **Bond Issuance Costs, Discounts, Premiums and Deferred Amounts on Refundings**

The bond issuance costs, discounts, premiums and deferred amounts on refundings, are deferred and amortized over the term of the bonds as a component of interest expense. The unamortized portion of these items except the deferred amounts on refundings, which are classified as part of receivables and other assets, are presented as a reduction of the face amount of bonds payable.

## **Capital Assets**

Capital assets are stated at cost and depreciated using the straight-line method over the estimated useful lives of the assets ranging from 3 to 80 years. The District’s policy is to capitalize acquisitions of capital assets with a cost greater than \$5,000 and a useful life of more than one year, and all costs related to capital projects, regardless of amounts.

Major improvements and betterments to existing facilities and equipment are capitalized. Costs for maintenance and repairs that do not extend the useful life of the applicable assets are charged to expense as incurred. Upon disposition, costs and accumulated depreciation are removed from the accounts and resulting gains or losses are included in operations.

The District capitalizes certain interest income and expense related to tax-free borrowings until the assets are ready for their intended use. The amount capitalized is the difference between the interest revenue and interest expense associated with the applicable tax-free borrowings. Amounts capitalized were a net interest income of \$324,000 in fiscal year 2006 and a net interest expense of \$1,789,000 in fiscal year 2005.

## **Deferred Revenue**

Deferred revenue consists principally of the cash gain received by the District from the lease/leaseback of certain rail traffic control equipment in 2002 (see Note 7) and from the sale/leaseback of 25 C-2 rail cars in 1995 (see Note 4). Additionally, deferred revenue includes prepayments of revenues related to license fees paid by telecommunication companies for the use of the District’s right of way for wireless accessibility to their customers and estimated passenger tickets sold but unused.

## **Compensated Absences**

Compensated absences are reported and accrued as a liability in the period incurred. The entire balance of compensated absences in the amounts of \$47,501,000 and \$48,405,000 as of June 30, 2006 and 2005, respectively, is considered short-term and presented as part of accounts payable and other liabilities in the statements of net assets.

## **Net Assets**

Net assets invested in capital assets, net of related debt include capital assets net of accumulated depreciation and outstanding principal balances of debt attributable to the acquisition, construction or improvement of those assets. Net assets are restricted when constraints are imposed by third parties or by law through constitutional provisions or enabling legislation and include amounts restricted for debt service and other liabilities. All other net assets are unrestricted. Generally, the District’s policy is to spend restricted resources first when an expense is incurred for purposes for which both restricted and unrestricted net assets are available.



## Transactions and Use Tax (Sales Tax) Revenues

The State of California legislation authorizes the District to impose a 0.5% transaction and use tax within District boundaries, which is collected and administered by the State Board of Equalization. Of the amounts available for distribution, 75% is paid directly to the District for the purpose of paying operating expenses, except for the portion that is paid directly to trustees to cover principal and interest payments of maturing sales tax revenue bonds and equity reserves. The remaining 25% is allocated by the Metropolitan Transportation Commission ("MTC") to the District, the City and County of San Francisco, and the Alameda-Contra Costa Transit District for transit services. The District records the total transactions and use taxes earned (including amounts paid to the trustee) as revenue.

## Property Taxes, Collection and Maximum Rates

The State of California Constitution Article XIII.A provides that the general purpose maximum property tax rate on any given property may not exceed 1% of its assessed value unless an additional amount for general obligation debt has been approved by voters. Assessed value is calculated at 100% of market value as defined by Article XIII.A and may be adjusted by no more than 2% per year, unless the property is sold or transferred. The State Legislature has determined the method of distribution of receipts from a 1% tax levy among the counties, cities, school districts and other districts, such as the District.

The District receives an allocation of property tax revenues for transit operations. Additionally, beginning in fiscal year 2006, the District received property tax allocations for the debt service payments on the 2005 General Obligation Bonds. As required by the law of the State of California, the District utilizes the services of each of the three BART Counties of Alameda, Contra Costa and San Francisco for the assessment and collection of taxes for District purposes. District taxes are collected at the same time and on the same tax rolls as county, school district and other special district taxes. Property taxes are recorded as revenue in the fiscal year of levy.

## Operating Financial Assistance

Financial assistance grants for operations from federal, state and local agencies are reported as nonoperating revenue in the period to which the grant applies and, for cost reimbursement grants, to the period in which the related expenditures are incurred (see Note 10).

## Collective Bargaining

Approximately 88% of the District's employees are subject to collective bargaining. The current bargaining units consist of the following:

- American Federation of State, County and Municipal Employees (AFSCME), Local 3993
- Amalgamated Transit Union (ATU), Local 1555
- Service Employees International Union (SEIU), Local 790
- BART Police Officers Association (BPOA)
- BART Police Managers Association (BPMA)

## Special Item

Special items are significant transactions or other events within the control of management that are either unusual in nature or infrequent in occurrence. The District normally finances its retiree health benefits on the pay-as-you-go basis. However, in 2005 in anticipation of an upcoming GASB pronouncement that requires these benefits be accounted for on an accrual basis, the District's Board and management decided to make contributions amounting to \$36,222,000 to the Retiree Health Benefit Trust, in an effort to advance fund a portion of its retiree health benefits obligation. Additional discussion is provided at Note 13.

## Capitalized Costs

The District initially charges employee salaries, wages and benefits to operating expenses by functional expense category. Labor costs included in those amounts that are associated with capital projects are subsequently reclassified to be included in the cost of the related capital asset. This reclassification is reflected in the statement of revenues, expenses and changes in net assets as a reduction of operating expenses. The amounts of \$33,785,000 and \$33,612,000 were capitalized during the years ended June 30, 2006 and 2005, respectively.

## Use of Estimates

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

## Recent Accounting Pronouncements

In April of 2004, the GASB issued Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*. This Statement establishes accounting and financial reporting standards for plans that provide postemployment benefits other than pension benefits (known as other postemployment benefits or OPEB). This standard will become effective for the District's Retiree Health Benefit Trust on July 1, 2006.

In June of 2004, the GASB issued Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. This statement establishes standards for the measurement, recognition, and display of OPEB expense and related liabilities (assets), note disclosures, and, if applicable, required supplementary information in the financial reports of state and local government employers. The District is in the process of analyzing the impact that adopting this statement will have on its financial position and results of operations. This standard becomes effective for the District beginning July 1, 2007.

## 2. Cash, Cash Equivalents and Investments

### A. Cash, Cash Equivalents and Investments of the Enterprise Fund

Cash, cash equivalents and investments are reported in the Enterprise Fund as follows (dollar amounts in thousands):

	2006			2005		
	<u>Unrestricted</u>	<u>Restricted</u>	<u>Total</u>	<u>Unrestricted</u>	<u>Restricted</u>	<u>Total</u>
Current assets						
Cash and						
cash equivalents	\$ 129,349	\$ 198,896	\$328,245	\$ 162,404	\$ 189,518	\$351,922
Investments	167,708	65,927	233,635	61,048	21,460	82,508
Noncurrent assets						
Investments	-	171,315	171,315	17,793	166,363	184,156
Total	<u>\$ 297,057</u>	<u>\$ 436,138</u>	<u>\$733,195</u>	<u>\$ 241,245</u>	<u>\$ 377,341</u>	<u>\$618,586</u>

## Investment Policy

The California Public Utilities Code, Section 29100, and the California Government Code, Section 53601, provide the basis for the District's investment policy. To meet the objectives of the investment policy – (1) preservation of capital, (2) liquidity, and (3) yield – the investment policy, approved by the Board of Directors, specifically identifies the types of permitted investments, as well as any maturity limits and other restrictions. The District's investment policy, which is more restrictive than required by law, allows investments in the following:

- Repurchase agreements,
- Reverse repurchase agreements,
- Collateralized time deposits,
- Mutual funds,
- California Local Agency Investment Fund, and
- Securities of the U.S. Government and its agencies.

The District's investments include amounts invested in the State of California Local Agency Investment Fund (LAIF). The total amount invested by all public agencies in LAIF at June 30, 2006 was \$16.4 billion. LAIF is part of the State of California Pooled Money Investment Account (PMIA), whose balance at June 30, 2006 was \$63.3 billion. Of this amount, 2.6% was invested structured notes and asset-backed securities and the remaining balance was invested in non-derivative instruments. PMIA is not SEC-registered, but is required to invest according to the California Government Code. The average maturity of PMIA investments was 152 days as of June 30, 2006. The Local Investment Advisory Board (Board) has oversight responsibility for LAIF. The Board consists of five members as designated by state statute. The value of the pool shares in LAIF, which may be withdrawn, is determined on an amortized cost basis, which is different than the fair value of the pooled treasury's portion in the pool. Withdrawals from LAIF are done on a dollar to dollar basis.

## Interest rate risk

Interest rate risk is the risk that changes in market rates will adversely affect the fair value of an investment. One of the District's primary objectives is to provide sufficient liquidity to meet its cash outflow needs, however, the District does not have any policies specifically addressing interest rate risk. A summary of investments by type of investments and by segmented time distribution as of June 30, 2006 and 2005 is as follows (dollar amounts in thousands):

	<u>2006</u>	<u>Investment Maturities (in Years)</u>			
	<u>Fair Value</u>	<u>Less Than 1</u>	<u>1 - 5</u>	<u>6 - 10</u>	<u>More Than 10</u>
Money market mutual funds	\$ 173,076	\$173,076	\$ -	\$ -	\$ -
U.S. government agencies	286,835	233,526	19,744	363	33,202
Repurchase agreements	210,270	-	177,026	33,244	-
Local Agency Investment Fund	20,000	20,000	-	-	-
U.S. Treasury bills	<u>1,132</u>	<u>1,132</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total investments	<u>691,313</u>	<u>427,734</u>	<u>196,770</u>	<u>33,607</u>	<u>33,202</u>
Deposits with banks	40,699	40,699	-	-	-
Certificates of deposit	803	-	803	-	-
Imprest funds	<u>380</u>	<u>380</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total cash and investments	<u>\$ 733,195</u>	<u>\$468,813</u>	<u>\$197,573</u>	<u>\$33,607</u>	<u>\$ 33,202</u>

	<u>2005</u>	<u>Investment Maturities (in Years)</u>			
	<u>Fair Value</u>	<u>Less Than 1</u>	<u>1 - 5</u>	<u>6 - 10</u>	<u>More Than 10</u>
Money market mutual funds	\$ 232,646	\$232,646	\$ -	\$ -	\$ -
U.S. government agencies	207,862	139,323	27,357	402	40,780
Repurchase agreements	100,283	-	67,652	32,631	-
Local Agency Investment Fund	23,758	23,758	-	-	-
U.S. Treasury notes	15,133	-	15,133	-	-
U.S. Treasury bills	<u>2,317</u>	<u>2,317</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total investments	<u>581,999</u>	<u>398,044</u>	<u>110,142</u>	<u>33,033</u>	<u>40,780</u>
Deposits with banks	35,407	35,407	-	-	-
Certificates of deposit	800	-	800	-	-
Imprest funds	<u>380</u>	<u>380</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total cash and investments	<u>\$ 618,586</u>	<u>\$433,831</u>	<u>\$110,942</u>	<u>\$33,033</u>	<u>\$ 40,780</u>

## Credit Risk

The District's credit rating risk is governed by Section 53601 of the California Government Code which, among others, limits investments in money market mutual funds to those funds with the highest evaluations granted by the rating agencies, which is Aaam. The District has investments in U.S. government agencies, bank repurchase agreements (underlying of U.S. Treasury securities) and in money market mutual funds. There are no investment limits on the securities of U.S. Treasury or certain U.S. government agencies as these investments are backed by the full faith and credit of the United States government. The following is a summary of the credit quality distribution for securities with credit exposure as rated by national rating agencies as of June 30, 2006 and 2005 (table on next page - dollar amounts in thousands).





	<u>2006</u>	<u>Credit Ratings</u>			
	<u>Fair Value</u>	<u>AAA</u>	<u>AA</u>	<u>A</u>	<u>Not Rated</u>
Money market mutual funds	\$ 173,076	\$173,076	\$ -	\$ -	\$ -
U.S. Government agencies	286,835	242,955	-	11,017	32,863
Repurchase agreements	210,270	84,762	125,508	-	-
Local Agency Investment Fund	20,000	-	-	-	20,000
U.S. Treasury bills	<u>1,132</u>	-	-	-	<u>1,132</u>
Total investments	<u>691,313</u>	<u>\$500,793</u>	<u>\$125,508</u>	<u>\$11,017</u>	<u>\$ 53,995</u>
Deposits with banks	40,699				
Certificates of deposit	803				
Imprest funds	<u>380</u>				
Total cash and investments	<u>\$ 733,195</u>				

	<u>2005</u>	<u>Credit Ratings</u>			
	<u>Fair Value</u>	<u>AAA</u>	<u>AA</u>	<u>A</u>	<u>Not Rated</u>
Money market mutual funds	\$ 232,646	\$232,646	\$ -	\$ -	\$ -
U.S. Government agencies	207,862	26,241	-	140,179	41,442
Repurchase agreements	100,283	67,652	32,631	-	-
Local Agency Investment Fund	23,758	-	-	-	23,758
U.S. Treasury notes	15,133	15,133	-	-	-
U.S. Treasury bills	<u>2,317</u>	<u>2,317</u>	-	-	-
Total investments	<u>581,999</u>	<u>\$343,989</u>	<u>\$ 32,631</u>	<u>\$140,179</u>	<u>\$ 65,200</u>
Deposits with banks	35,407				
Certificates of deposit	800				
Imprest funds	<u>380</u>				
Total cash and investments	<u>\$ 618,586</u>				

### Concentration of credit risk

The District's investment policies mitigate exposure to concentration of credit risk by diversifying the portfolio and limiting investments in any one issuer to no more than 5% of the total portfolio. Investments issued by or explicitly guaranteed by the U.S. Government and investments in mutual funds, external investment pools, and other pooled investments are exempt from this requirement as they are normally diversified themselves.

### Custodial Credit Risk - Deposits

For deposits, custodial credit risk is the risk that in the event of a bank failure, the District's deposits may not be returned. The California Government Code Section 53652 requires California banks and savings and loan associations to secure governmental deposits by pledging government securities as collateral. The market value of pledged securities must equal at least 110% of the District's deposits. California law also allows financial institutions to secure governmental deposits by pledging first trust deed mortgage notes having a value of 150% of the District's total deposits. Such collateral is considered to be held in the District's name.

## Custodial Credit Risk - Investments

For investments, custodial credit risk is the risk that in the event of a failure of the counterparty, the District may not be able to recover the value of its investments. The exposure to the District is limited as the District's investments are held in the District's name by a third-party safe-keeping custodian that is separate from the counterparty or in the custody of a trust department, as required by bond covenants.

## B. Investments of the Retiree Health Benefit Trust (Trust)

### Investment Policy

The investment objective of the Trust is to achieve consistent long-term growth for the Trust and to maximize income consistent with the preservation of capital for the sole and exclusive purpose of providing benefits to participants and their beneficiaries and defraying reasonable expenses of administering the Trust. The District's Board of Directors establishes the general investment policy and guidelines for the Trust. Allowable investments under the Trust investment guidelines include:

- Cash equivalents such as U.S. Treasury bills, money market trusts, short-term interest fund (STIF) trusts, commercial paper rated A1/P1, banker's acceptances, certificates of deposits and repurchase agreements;
- Fixed income securities which include U.S. agency and corporation bonds (including Yankees) and preferred stock and Rule 144A issues, and mortgage-or-asset-backed securities;
- Equity securities, including U.S. traded common, preferred stocks and convertible stocks and bonds, including American Depository Receipts.

### Interest rate risk

The Trust's investment policies mitigate exposure to changes in interest rates by requiring that the assets of the Trust be invested in accordance with the following asset allocation guidelines:

<u>Asset Class</u>	<u>Minimum</u>	<u>Maximum</u>	<u>Preferred</u>
Equity securities	45%	70%	60%
Fixed income securities	25%	45%	35%
Cash equivalents	3%	10%	5%

A summary of investments by type of investments and by segmented time distribution as of June 30, 2006 and 2005 is as follows (dollar amounts in thousands):

	<u>2006</u>	<u>Investment Maturities (in Years)</u>			
	<u>Fair Value</u>	<u>Less Than 1</u>	<u>1 - 5</u>	<u>6 - 10</u>	<u>More Than 10</u>
U.S. Treasury obligations	\$ 11,099	\$ 901	\$ 787	\$2,587	\$ 6,824
Money market mutual funds	3,455	3,455	-	-	-
Corporate obligations	2,827	15	1,040	522	1,250
Foreign obligations	<u>336</u>	<u>-</u>	<u>43</u>	<u>198</u>	<u>95</u>
Investments subject to interest rate risk	\$17,717	<u>\$ 4,371</u>	<u>\$1,870</u>	<u>\$3,307</u>	<u>\$ 8,169</u>
Domestic common stocks	24,207				
Foreign stocks	<u>428</u>				
Total investments	<u>\$ 42,352</u>				



	<u>2005</u>	<u>Investment Maturities (in Years)</u>			
	<u>Fair Value</u>	<u>Less Than 1</u>	<u>1 - 5</u>	<u>6 - 10</u>	<u>More Than 10</u>
U.S. Treasury obligations	\$ 9,361	\$ 347	\$1,161	\$1,317	\$ 6,536
Money market mutual funds	5,770	5,770	-	-	-
Corporate obligations	3,649	247	1,465	559	1,378
Foreign obligations	<u>205</u>	<u>-</u>	<u>107</u>	<u>69</u>	<u>29</u>
Investments subject to interest rate risk	18,985	<u>\$ 6,364</u>	<u>\$2,733</u>	<u>\$1,945</u>	<u>\$ 7,943</u>
Domestic common stocks	20,605				
Total investments	<u>\$ 39,590</u>				

### Credit Risk

The Trust's credit risk policy is defined in its Statement of Investment Policy approved by the District's Board of Directors. The policy states that the Board recognizes that some risk is necessary to produce long-term investment results that are sufficient to meet the Trust's objectives and that the Trust's investment managers are expected to make reasonable efforts to control risk. The investment policy requires that all of the Trust's assets be invested in liquid securities, defined as securities that can be transacted quickly and efficiently for the Trust, with minimal impact on market prices. The investment policy also demands that no single investment shall exceed five percent of the total Trust assets, at market value, except obligations of the U.S. Government, short-term money market funds, index funds and other diversified commingled accounts; and for actively managed equity accounts, where, for issues that comprise more than 4% of the account's stated benchmark, the limit shall be 125% of the weight of the common stock benchmark. The following is a summary of the credit quality distribution for securities with credit exposure as rated by national rating agencies as of June 30, 2006 and 2005 (dollar amounts in thousands):

	<u>2006</u>	<u>Credit Ratings</u>				
	<u>Fair Value</u>	<u>AAA</u>	<u>AA</u>	<u>A</u>	<u>BBB</u>	<u>Not Rated</u>
US Treasury obligations	\$11,099	\$11,099	\$ -	\$ -	\$ -	\$ -
Money market mutual funds	3,455	-	-	-	-	3,455
Corporate obligations	2,827	1,778	34	408	607	-
Foreign obligations	<u>336</u>	<u>151</u>	<u>-</u>	<u>142</u>	<u>43</u>	<u>-</u>
Investments subject to credit risk	17,717	<u>\$13,028</u>	<u>\$34</u>	<u>\$550</u>	<u>\$650</u>	<u>\$3,455</u>
Domestic common stocks	24,207					
Foreign stocks	428					
Total investments	<u>\$42,352</u>					



	2005	Credit Ratings					
	Fair Value	AAA	AA	A	BBB	BB	Not Rated
US Treasury obligations	\$ 9,361	\$ 9,361	\$ -	\$ -	\$ -	\$ -	\$ -
Money market mutual funds	5,770	-	-	-	-	-	5,770
Corporate obligations	3,649	2,028	218	532	775	96	-
Foreign obligations	205	28	-	42	135	-	-
Investments subject to credit risk	18,985	<u>\$11,417</u>	<u>\$218</u>	<u>\$574</u>	<u>\$910</u>	<u>\$96</u>	<u>\$5,770</u>
Domestic common stocks	<u>20,605</u>						
Total investments	<u>\$39,590</u>						

### Custodial Credit Risk - Investments

For investments, custodial credit risk is the risk that in the event of a failure of the counterparty, the Trust may not be able to recover the value of its investments. The exposure to the Trust is limited as the Trust's investments are in the custody of a third-party custodian that is separate from the counterparty.

### 3. Receivables and Other Assets

The District reports the following aggregated accounts as receivables and other assets in the statements of net assets as of June 30, 2006 and 2005 (dollar amounts in thousands):

	2006	2005
Interest receivable - trust for sublease obligation	\$30,950	\$25,126
Interest receivable - other investments	561	723
Deferred charges - interest on defeased bonds	24,510	38
Deferred charges - other	1,074	1,187
Local financial assistance - SamTrans	8,085	13,092
Deposit for power supply	7,594	-
Ticket vendors	4,407	3,309
Notes receivable	4,184	4,236
Capitol Corridor Joint Powers Authority	2,479	8,262
Property taxes	1,763	734
Prepaid expenses	1,578	2,408
Imprest deposits for self-insurance liabilities	522	1,009
Other	1,987	1,945
Allowance for doubtful accounts - SamTrans	(7,500)	(5,000)
Allowance for doubtful accounts - other	(71)	-
Total receivables and other assets	<u>\$82,123</u>	<u>\$57,069</u>
Current, unrestricted portion	\$16,722	\$30,517
Noncurrent, unrestricted portion	25,478	1,113
Noncurrent, restricted portion	<u>39,923</u>	<u>25,439</u>
Total receivables and other assets, as presented in the basic financial statements	<u>\$82,123</u>	<u>\$57,069</u>

#### 4. Capital Lease Receivable and Liability (Sale/Leaseback – Revenue Transit Vehicles)

On March 30, 1995, the District entered into an agreement with a Swedish corporation to sell 25 newly manufactured C-2 rail cars for \$50,383,000 and simultaneously entered into an agreement to lease them back. The lease agreement was effective on the closing date of September 15, 1995, and continues through January 15, 2011.

The District recorded a gain on the sale of approximately \$2,015,000, which is equal to the amount of cash received on the sale. The gain was deferred and is being amortized over 30 years. In addition, the District recorded a receivable of \$48,368,000 and a capital lease obligation of the same amount. The receivable and the liability will be reduced by a corresponding amount over the term of the lease. At June 30, 2006 and 2005, the balance of the deferred gain was \$1,052,000 and \$1,107,000, respectively. The balance of both the receivable and the liability was \$14,195,000 and \$17,349,000 as of June 30, 2006 and 2005, respectively and is reflected in the statements of net assets as a capital lease receivable and capital lease liability, respectively. Other than the cash received upon the sale, no cash will be exchanged between the parties in settlement of the receivable and liability.

At June 30, 2006 and 2005 the balances of the capital lease receivable and of the capital lease liability related to the sale/leaseback are summarized as follows (dollar amounts in thousands):

	<u>2006</u>	<u>2005</u>
Amounts at beginning of year	\$17,349	\$20,504
Amounts collected/repaid during the year	<u>(3,154)</u>	<u>(3,155)</u>
Balance at end of year	14,195	17,349
Less - current portion	<u>(3,154)</u>	<u>(3,154)</u>
Net noncurrent portion	<u>\$11,041</u>	<u>\$14,195</u>

The District's capital lease receivable and capital lease liability have the following maturities for each of the next five fiscal years, which are summarized as follows (dollar amounts in thousands):

<u>Fiscal Year</u> <u>Year Ending June 30</u>	<u>Annual</u> <u>Installments</u>
2007	\$ 3,154
2008	3,155
2009	3,154
2010	3,155
2011	<u>1,577</u>
	<u>\$ 14,195</u>

Accumulated depreciation related to the C-2 rail cars covered by the sale/leaseback agreement totaled \$20,526,000 and \$18,673,000 as of June 30, 2006 and 2005, respectively.

## 5. Capital Assets

Changes to capital assets during the year ended June 30, 2006 were as follows (dollar amounts in thousands):

	Lives (Years)	2005	Additions and Transfers	Retirements and Transfers	2006
<b>Capital assets, not being depreciated</b>					
Land	N/A	\$ 513,849	\$ 14,713	\$ (4,170)	\$ 524,392
Construction in progress	N/A	861,809	108,803	(289,667)	680,945
Total capital assets, not being depreciated		<u>1,375,658</u>	<u>123,516</u>	<u>(293,837)</u>	<u>1,205,337</u>
<b>Capital assets, being depreciated</b>					
Stations, track, structures and improvements	80	3,311,632	258,520	(7)	3,570,145
Buildings	80	21,871	-	(14,399)	7,472
System-wide operation and control	20	510,286	9,080	(1,055)	518,311
Revenue transit vehicles	30	1,042,346	-	-	1,042,346
Revenue transit vehicles under capital lease	30	55,593	-	-	55,593
Service and miscellaneous equipment	3-20	61,416	99	(2,066)	59,449
Capitalized construction and start-up costs	30	98,305	-	-	98,305
Repairable property items	30	16,161	-	(982)	15,179
Total capital assets, being depreciated		5,117,610	267,699	(18,509)	5,366,800
Total capital assets, not being depreciated		<u>1,375,658</u>	<u>123,516</u>	<u>(293,837)</u>	<u>1,205,337</u>
Less accumulated depreciation		<u>(1,495,399)</u>	<u>(145,306)</u>	<u>12,757</u>	<u>(1,627,948)</u>
Total capital assets, being depreciated, net		<u>3,622,211</u>	<u>122,393</u>	<u>(5,752)</u>	<u>3,738,852</u>
Total capital assets, net		<u>\$4,997,869</u>	<u>\$245,909</u>	<u>\$(299,589)</u>	<u>\$4,944,189</u>

Changes to capital assets during the year ended June 30, 2005 were as follows (dollar amounts in thousands):

	<b>Lives (Years)</b>	<b>2004</b>	<b>Additions and Transfers</b>	<b>Retirements and Transfers</b>	<b>2005</b>
<b>Capital assets, not being depreciated</b>					
Land	N/A	\$ 481,466	\$ 32,720	\$ (337)	\$ 513,849
Construction in progress	N/A	<u>1,032,910</u>	<u>114,511</u>	<u>(285,612)</u>	<u>861,809</u>
Total capital assets, not being depreciated		<u>1,514,376</u>	<u>147,231</u>	<u>(285,949)</u>	<u>1,375,658</u>
<b>Capital assets, being depreciated</b>					
Stations, track, structures and improvements	80	3,079,442	232,862	(672)	3,311,632
Buildings	80	27,333	-	(5,462)	21,871
System-wide operation and control	20	501,409	9,004	(127)	510,286
Revenue transit vehicles	30	1,037,986	4,364	(4)	1,042,346
Revenue transit vehicles under capital lease	30	55,593	-	-	55,593
Service and miscellaneous equipment	3-20	52,017	13,868	(4,469)	61,416
Capitalized construction and start-up costs	30	98,305	-	-	98,305
Reparable property items	30	<u>16,114</u>	<u>47</u>	<u>-</u>	<u>16,161</u>
Total capital assets, being depreciated		4,868,199	260,145	(10,734)	5,117,610
Less accumulated depreciation		<u>(1,372,798)</u>	<u>(128,697)</u>	<u>6,096</u>	<u>(1,495,399)</u>
Total capital assets, being depreciated, net		<u>3,495,401</u>	<u>131,448</u>	<u>(4,638)</u>	<u>3,622,211</u>
Total capital assets, net		<u>\$5,009,777</u>	<u>\$ 278,679</u>	<u>\$ (290,587)</u>	<u>\$4,997,869</u>

The District has completed construction of Phase 1 of an extension program that added 38 miles of track and 10 new stations to the system at a total cost of approximately \$3,477,127,000. The funding for Phase 1 came from the Federal Government (\$877,634,000), State of California (\$741,770,000), San Mateo County (\$502,719,000), Alameda and Contra Costa Counties (\$505,000,000), bridge tolls (\$279,811,000), San Francisco International Airport (\$200,000,000), and the District (\$370,193,000).

With the completion and pending close out of the project phase of the San Francisco Airport Extension, the District's focus turns to other important projects and cooperative studies. Looking east, the proposed East Contra Costa BART Extension (eBART) in Contra Costa County is moving forward in cooperation with affected jurisdictions, and the West Dublin/Pleasanton Infill Station is moving closer to construction. Projects grappling with funding shortfalls include the Oakland Airport Connector (OAC), for which the District is looking at alternative delivery options to move forward, and the Warm Springs Extension. Additionally, BART is leading the Regional Measure 2 (RM2) funded Regional Rail Study, which will attempt to define the passenger rail network in the Bay Area.

The District has entered into contracts for the construction of various facilities and equipment totaling approximately \$553,859,000 at June 30, 2006, and \$492,974,000 in 2005.

Under the Federal Full Funding Grant Agreement, \$1,347,230,000 was approved for project costs associated with the San Francisco International Airport Extension (“SFO Extension project”) with funding participation from the Federal Government, State of California and certain local agencies. As a local funding participant, the San Francisco International Airport Commission (“SFIA”) pledged to contribute funds to the federally approved project up to \$77,000,000. The District entered into various agreements with the City and County of San Francisco, acting by and through SFIA, which defined the specific project costs that could be funded from the \$77,000,000 contribution. The agreements stated that the contribution would be used for the eligible BART Operating Systems Work on the portion of the project related to the San Francisco International Airport station (“On Airport project”). Eligible project costs include the design, construction, construction support, management and oversight, general and administrative costs and other associated costs of the On Airport project. Based on the agreements between SFIA and the District, SFIA shall own all rights, titles and interest associated with the assets paid from the \$77,000,000 until the end of the projected useful life of each asset at which time, all of SFIA’s rights, titles and interest associated with the assets shall transfer to the District, without payment by the District. The risk of loss on all assets acquired from the SFIA contributions are, at all times, assumed by the District.

The construction of the SFO Extension project was completed in 2003 and revenue operations started on June 22, 2003. All costs incurred as of June 30, 2006, including those paid from and/or incurred against the SFIA contribution, have been capitalized to capital assets and accordingly are subject to depreciation. As of June 30, 2006, the capital assets related to the SFIA contribution amounted to \$61,374,000 with an accumulated depreciation of \$2,712,000.

## 6. Accounts Payable and Other Liabilities

The District reports the following aggregated payables as accounts payable and other liabilities in the statements of net assets as of June 30, 2006 and 2005 (dollar amounts in thousands):

	<u>2006</u>	<u>2005</u>
Payable to vendors and contractors	\$ 77,430	\$ 71,401
Employee salaries and benefits	72,594	70,152
Accrued interest payable	21,123	22,542
MTC advance for debt service	<u>12,480</u>	<u>11,979</u>
Liabilities at the end of year	183,627	176,074
Less noncurrent portion, reported as other liabilities	<u>(258)</u>	<u>(657)</u>
Net current portion	<u>\$183,369</u>	<u>\$175,417</u>



## 7. Long-Term Debt

Long-term debt activity for the years ended June 30, 2006 and 2005 is summarized as follows (dollar amounts in thousands):

	<u>2005</u>	<u>Additions/ Accretion</u>	<u>Payments/ Amortization</u>	<u>2006</u>
1990 Sales Tax Revenue Refunding Bonds	\$ 28,775	\$ -	\$ -	\$ 28,775
1995 Sales Tax Revenue Bonds	47,590	-	(47,590)	-
1998 Sales Tax Revenue Bonds	341,190	-	(169,425)	171,765
1999 Sales Tax Revenue Bonds	131,300	-	(131,300)	-
2001 Sales Tax Revenue Bonds	165,965	-	(19,640)	146,325
2005 Sales Tax Revenue Refunding Bonds	-	352,095	-	352,095
2006 Sales Tax Revenue Bonds	-	64,915	-	64,915
TFA Bridge Toll Notes	30,280	-	(8,495)	21,785
Construction Loans	123,900	8,495	(3,000)	129,395
FTA Capital Grant Bonds	131,250	-	(84,920)	46,330
Lease/Leaseback Obligation	178,879	-	(38,627)	140,252
2002 SFO Extension Premium Fare Bonds	56,715	-	-	56,715
2004 SFO Extension Refunding Bonds	66,000	-	(10,300)	55,700
2005 General Obligation Bonds	100,000	-	-	100,000
	<u>1,401,844</u>	<u>425,505</u>	<u>(513,297)</u>	<u>1,314,052</u>
Add (less):				
Accumulated Accretion on Lease/Leaseback Obligation	18,554	12,049	(12,846)	17,757
Debt related items*	<u>(14,329)</u>	<u>22,936</u>	<u>(987)</u>	<u>7,620</u>
Long-term debt net of accumulated accretion and debt related items	1,406,069	<u>\$ 460,490</u>	<u>\$ (527,130)</u>	1,339,429
Less: current portion of long-term debt	<u>(172,782)</u>			<u>(152,172)</u>
Net long-term debt	<u>\$1,233,287</u>			<u>\$1,187,257</u>

\* Debt related items consist of deferred bond issuance costs, discounts and premiums.

	<u>2004</u>	<u>Additions/ Accretion</u>	<u>Payments/ Amortization</u>	<u>2005</u>
1990 Sales Tax Revenue Refunding Bonds	\$ 38,390	\$ -	\$ (9,615)	\$ 28,775
1995 Sales Tax Revenue Bonds	49,800	-	(2,210)	47,590
1998 Sales Tax Revenue Bonds	345,050	-	(3,860)	341,190
1999 Sales Tax Revenue Bonds	131,160	-	(1,860)	131,300
2001 Sales Tax Revenue Bonds	165,965	-	-	165,965
TFA Bridge Toll Notes	38,355	-	(8,075)	30,280
Construction Loans	115,825	8,075	-	123,900
FTA Capital Grant Bonds	281,540	-	(150,290)	131,250
Lease/Leaseback Obligation	180,207	-	(1,328)	178,879
2002 SFO Extension Premium Fare Bonds	56,715	-	-	56,715
2004 SFO Extension Refunding Bonds	66,000	-	-	66,000
2005 General Obligation Bonds	-	100,000	-	100,000
	<u>1,471,007</u>	<u>108,075</u>	<u>(177,238)</u>	<u>1,401,844</u>
Add (less):				
Accumulated Accretion on Lease/Leaseback Obligation	10,445	13,497	(5,388)	18,554
Debt related items*	<u>(15,392)</u>	<u>789</u>	<u>274</u>	<u>(14,329)</u>
Long-term debt net of accumulated accretion and debt related items	1,466,060	<u>\$ 122,361</u>	<u>\$ (182,352)</u>	1,406,069
Less: current portion of long-term debt	<u>(93,631)</u>			<u>(172,782)</u>
Net long-term debt	<u>\$1,372,429</u>			<u>\$1,233,287</u>

\* Debt related items consist of deferred bond issuance costs, discounts and premiums.



### **1990 Sales Tax Revenue Refunding Bonds (the 1990 Bonds)**

In July 1990, the District issued sales tax revenue refunding bonds totaling \$158,478,000 to refund and defease \$141,045,000 outstanding principal amount of the District's Sales Tax Revenue Bonds, Series 1985. The 1990 Bonds are special obligations of the District payable from and collateralized by a pledge of the sales tax revenues. At June 30, 2006, the 1990 Bonds consist of \$28,775,000 in current interest serial bonds due from 2010 to 2011 with an interest rate of 6.75%. The 1990 Bonds included capital appreciation bonds with an accreted value of \$21,252,000 and the final payment matured on July 1, 2004.

### **1995 Sales Tax Revenue Bonds (the 1995 Bonds)**

In June 1995, the District issued sales tax revenue bonds totaling \$135,000,000 to provide funds for certain capital improvements including rehabilitation of District vehicles and facilities and energy conservation measures. The 1995 Bonds are special obligations of the District payable from and collateralized by a pledge of sales tax revenues. In July 2001, the District used part of the proceeds from the 2001 Sales Tax Revenue Bonds to defease \$18,585,000 in serial bonds due from 2002 to 2010 and \$19,915,000 in term bonds due from 2012 to 2015. In August 2005, 1995 Bonds with a total principal amount of \$45,275,000 were refunded from the proceeds of the 2005 Bonds. At June 30, 2006, there are no outstanding 1995 Bonds.

### **1998 Sales Tax Revenue Bonds (the 1998 Bonds)**

In March 1998, the District issued sales tax revenue bonds totaling \$348,510,000 to provide funds for certain capital improvements, including rehabilitation of the District's vehicles and facilities, to repay obligations of approximately \$49,645,000 related to a lease of certain telecommunications equipment, and to refund certain outstanding bonds with principal amounts of \$155,115,000 to achieve debt service savings. The 1998 Bonds are special obligations of the District payable from and collateralized by a pledge of sales tax revenues. In August 2005, a portion of the 1998 Bonds with an aggregate principal amount of \$155,650,000 were refunded from the proceeds of the 2005 Bonds. At June 30, 2006, the 1998 Bonds consist of \$51,935,000 in serial bonds due from 2006 to 2018 with interest rates ranging from 4.13% to 5.50%, a \$79,105,000 term bond due July 1, 2023 with an interest rate of 4.75% and a \$40,725,000 term bond due July 1, 2028 with an interest rate of 5%. The District is required to make sinking fund payments on the term bond due July 1, 2023 beginning on July 1, 2019 and on the term bond due July 1, 2028 beginning on July 1, 2024. In addition, the 1998 bonds maturing after June 30, 2009 may be redeemed prior to their respective maturities after June 30, 2008 at the option of the District at prices ranging from 100% to 101%.

### **1999 Sales Tax Revenue Bonds (the 1999 Bonds)**

In October 1999, the District issued sales tax revenue bonds totaling \$134,945,000 to provide funds for certain capital improvements including rehabilitation of the District's vehicles, initial deposit to a capital reserve account for the SFO Extension project and rehabilitation of the District's maintenance facility. The 1999 Bonds are special obligations of the District, payable from and collateralized by a pledge of sales tax revenues. In August 2005, the total outstanding principal amount of \$129,360,000 of the 1999 Bonds was refunded from the proceeds of the 2005 Bonds. There are no outstanding 1999 Bonds at June 30, 2006.

### **2001 Sales Tax Revenue Bonds (the 2001 Bonds)**

In July 2001, the District issued sales tax revenue bonds totaling \$168,650,000 to fund the rehabilitation of District rail cars and certain other capital improvements, to fund capital reserves to be utilized in connection with the SFO Extension project and to refund certain outstanding bonds with principal amounts of \$41,175,000 to achieve cash flow savings by extending the debt service requirements further into the future and to take advantage of lower interest rates. In August 2005, 2001 Bonds with principal amounts totaling \$19,640,000 were refunded from the proceeds of the 2005 Bonds. At June 30, 2006, the 2001 Bonds consist of \$38,350,000 in serial bonds due from 2012 to 2021 with interest rates ranging from 4.375% to 5.250%, a \$27,420,000 term bond due July 1, 2026 with an interest rate of 5%, a \$35,205,000 term bond due July 1, 2031 with an interest rate of 5%, and a \$45,350,000 term bond due July 1, 2036 with an interest rate of 5.125%. The District is required to make sinking fund payments on the term bond due July 1, 2026 beginning on July 1, 2022, on the term bond due July 1, 2031 beginning July 1, 2027, and on the term bond due on July 1, 2036 beginning on July 1, 2032. In addition, the 2001 Bonds maturing on or after July 1, 2012 may be redeemed prior to their respective stated maturities, at the option of the District, as a whole or in part, on any date on or after July 1, 2011, at the principal amount called for redemption plus interest accrued thereon to the date fixed for redemption without premium.



## **2005 Sales Tax Revenue Refunding Bonds (the 2005 Bonds)**

In August 2005, the District issued the Sales Tax Revenue Bonds, Refunding Series 2005 A (2005 Bonds) totaling \$352,095,000. The proceeds of the 2005 Bonds, including the net original issue premium of \$17,151,000, were 1) placed into an irrevocable escrow account to advance refund \$349,925,000 in aggregate principal amount of sales tax revenue bonds related to the Sales Tax Revenue Bonds, Series 1995, 1998, 1999, and 2001 to achieve cash flow savings and 2) to pay costs of issuance of the 2005 Bonds. The 2005 Bonds are special obligations of the District, payable from and collateralized by a pledge of sales tax revenues. At June 30, 2006, the 2005 Bonds consist of \$264,625,000 in serial bonds due from 2006 to 2030 with interest rates ranging from 3.00% to 5.00% and two 5.00% term bonds in the amounts of \$55,685,000 and \$31,785,000 due in 2030 and 2034, respectively. This refunding resulted in a cash flow savings of \$19,326,000 and an economic gain of \$16,768,000.

## **2006 Sales Tax Revenue Bonds (the 2006 Bonds)**

In June 2006, the District issued sales tax revenue bonds with an aggregate principal amount of \$64,915,000 to finance a portion of the cost of construction of a new transit station, the West Dublin/Pleasanton Station including two parking facilities, pedestrian bridges, a bus intermodal facility and related improvements. The 2006 Bonds are special obligations of the District payable from and secured by a pledge of sales tax revenues. At June 30, 2006, the 2006 Bonds outstanding consist of \$20,110,000 in serial bonds due from 2014 to 2026 with interest rates ranging from 4.00% to 4.625%, \$17,995,000 in term bonds due July 1, 2031 with 5.000% interest rate and \$26,810,000 in term bonds due July 1, 2036 at 5.000% interest rate. The term bonds are subject to mandatory sinking account payments beginning in 2027 for the term bonds due in 2031 and 2032 for the term bonds due in 2036.

## **Transit Financing Authority (Authority) Bridge Toll Notes**

In order to fund a portion of the costs of the extension project at the San Francisco International Airport (SFO Extension project), in September 1999, the Authority issued a limited liability note (the "Bridge Toll Note") in the amount of \$65,680,000, payable from and collateralized solely by a pledge of certain bridge toll revenues allocated to the District by MTC. At June 30, 2006, the notes outstanding amount to \$21,785,000 with interest rates ranging from 5.00% to 5.75% and mature from August 2006 through February 2007. (For information on the Authority, see Notes 1 and 15.)

## **Construction Loans**

In March 1999, the District, MTC and San Mateo County Transit District ("SamTrans") entered into a Memorandum of Understanding ("MOU"), which provided additional funds for the SFO Extension project.

Pursuant to the MOU, the construction loans as of June 30, 2006, consist of funds received for the SFO Extension project costs from SamTrans for \$72,000,000 and MTC for \$16,500,000 and \$40,895,000 from MTC for the SFO Extension project's temporary cash requirements. The District provided \$50,000,000 of its own funds to assist with the financing of the SFO Extension project costs. The terms and conditions of the MOU provide that the loans for project costs will be repaid, without interest, from the future net operating surplus generated by the SFO Extension. Such repayments of the project cost loans from SamTrans and MTC totaling \$88,500,000 plus the District's \$50,000,000, will commence after SamTrans' capital contribution to the District's Warm Springs Extension project is fully paid from future net operating surplus. Under the terms of the MOU, MTC's loan for the project's temporary cash requirements of \$40,895,000 will be repaid, without interest, when the District receives the last Federal Full Funding Grant allocation for the SFO Extension project, currently expected to be in fiscal year 2007. On June 28, 2006, the District and MTC entered into a Loan Extension and Repayment Agreement, where MTC agreed to extend the repayment period and amortize the principal for the loan over a nine year term, charging 3% simple interest, with final payment due in June 2015. Under the agreement certain STA funds to be received by the District are required to be used to prepay the loan.

## FTA Capital Grant Bonds

On February 15, 2001, the Association of Bay Area Governments (“ABAG”) issued BART SFO Extension Bonds (FTA Capital Grant), 2001 Series A, in the amount of \$485,350,000. The FTA Capital Grant bonds were issued for the benefit of the District’s SFO Extension project. The proceeds were used mainly to provide additional financing for the SFO Extension and to refund and defease \$300,000,000 aggregate principal amount of the San Francisco Bay Area Transit Financing Authority Commercial Paper Notes, Series A, B, C, D, E and F. The bonds are limited obligations of ABAG and are payable from the monies coming from the Federal Full Funding Grant Agreement between the United States Department of Transportation, Federal Transit Administration and the District for the District’s SFO Extension project. The District’s obligation to make bond payments is not a general obligation of the District. Payment of the principal and interest on the bonds when due are insured by a financial guaranty insurance policy issued by an insurance company. In fiscal year 2006, \$5,000,000 (\$1,040,000 in fiscal year 2005) of the bonds due in fiscal year 2008 and \$15,710,000 (\$87,955,000 in fiscal year 2005) of the bonds due in fiscal year 2009 were paid in advance. At June 30, 2006, the bonds outstanding amount to \$46,330,000 in serial bonds, with interest rates ranging from 3.75% to 5.00% with maturities on June 15, 2007.

## Lease/Leaseback Obligation

On March 19, 2002, the District entered into a transaction to lease rail traffic control equipment (the “Network”) to investors through March 19, 2042 (the “head lease”) and simultaneously sublease the Network back through January 2, 2018 (the “sublease”). At the expiration of the sublease term the District has the option to purchase back the remaining head lease interest.

At closing, the Network had a fair market value of approximately \$206,000,000 and a book value of \$203,000,000. Under the terms of the head lease, the District received a prepayment equivalent to the net present value of the head lease obligation totaling approximately \$206,000,000, of which the District paid approximately \$146,000,000 to a Payment Undertaker. Under the terms of the agreement, the Payment Undertaker committed to pay the debt portion of the District’s sublease obligation and to set aside funds to enable the District to exercise its purchase option of the head lease interest, if it chooses to do so. Of the remaining head lease proceeds, approximately \$37,000,000 was deposited to a trust account to be used to pay the remaining equity portion of the District’s sublease obligation and to set aside additional funds to enable the District to exercise its purchase option of the head lease interest, if it chooses to do so. The District received cash from the lease/leaseback transaction amounting to approximately \$23,000,000. The cash gain was deferred and is being amortized over a period of 15.75 years through January 2, 2018. In accordance with generally accepted accounting principles in the United States of America, the District has reflected this transaction as a financing transaction. The District has recorded the payment to the Payment Undertaker as a deposit for sublease obligation and the deposit to the trust account as investments, and the net present value of the future sublease payments and exercise price of the purchase option as long-term debt.


Under this transaction, the District maintains the right to continued use and control of the Network through the end of the sublease term.

The details of the lease/leaseback obligation, including the accretion of interest, are as follows (dollar amounts in thousands):

	<u>2006</u>	<u>2005</u>
Long-term debt at beginning of year	\$197,433	\$190,652
Interest expense incurred during the year	12,049	13,497
Payments made towards principal	(38,627)	(1,328)
Payments made towards accumulated accretion	<u>(12,846)</u>	<u>(5,388)</u>
	158,009	197,433
Lease payments due in one year	<u>(39,362)</u>	<u>(46,647)</u>
Net long-term debt at end of year	<u>\$118,647</u>	<u>\$150,786</u>

## 2002 SFO Extension Premium Fare Bonds (the Airport Premium Fare Bonds)

On October 1, 2002, the Association of Bay Area Governments (“ABAG”) issued BART SFO Extension Bonds (“Airport Premium Fare Bonds”), 2002 Series, in the amount of \$56,715,000. The Airport Premium Fare Bonds were issued for the benefit of the District’s SFO Extension project. The proceeds were used to finance a portion of the costs of the SFO Extension project, including all system-wide and associated improvements and expenditures related to the extension. The Airport Premium Fare Bonds are limited obligations of ABAG payable solely from and collateralized solely by amounts received from the District pursuant to a Pledge and Contribution Agreement, dated October 1, 2002, between ABAG and the District. The Airport Premium Fare Bonds are not a general obligation of ABAG. The District’s obligation to make payments under the Pledge and Contribution Agreement is limited to and payable solely from



and collateralized solely by a pledge of the premium fare imposed and collected by the District from passengers who board or depart the District's rapid transit system at the San Francisco International Airport station. The District's obligation to make such payments under the Pledge and Contribution Agreement is not a general obligation of the District. The payment of the principal and interest when due are insured by a financial guaranty insurance policy issued by an insurance company. At June 30, 2006, the 2002 Airport Premium Fare Bonds consist of \$21,515,000 in serial bonds due from 2006 to 2022 with interest rates ranging from 2.25% to 5.00%, a \$11,230,000 term bond due August 1, 2026 with an interest rate of 5.00%, and a \$23,970,000 term bond due August 1, 2032 with an interest rate of 5.00%. The District is required to make sinking fund payments on the term bond due August 1, 2026 beginning on August 1, 2023 and on the term bond due August 1, 2032 beginning on August 1, 2027.

### **2004 SFO Extension Refunding Bonds (the Airport Refunding Bonds)**

On June 14, 2004, ABAG issued BART SFO Extension Refunding Bonds (FTA Capital Grant), 2004 Series A (Auction Rate Securities) with an aggregate principal amount of \$66,000,000 for the benefit of the District. The Airport Refunding Bonds were issued in order to refund a portion of the ABAG BART SFO Extension Bonds (FTA Capital Grant), 2001 Series A, to fund the reserve fund deposit with respect to the Airport Refunding Bonds, and to pay certain costs of issuance of the bonds. The issuance of the Airport Refunding Bonds had the effect of freeing up \$14,600,000 from the debt service reserve fund of the BART SFO Extension Bonds (FTA Capital Grant), 2001 Series A, and making the amount available as an additional source of cash for the payment of the SFO Extension Project expenditures. The Airport Refunding Bonds are limited obligations of ABAG payable solely from and collateralized by amounts received from the District pursuant to the Pledge Agreement dated February 1, 2001 between ABAG and the District, amounts on deposit in the funds and accounts established under the Indenture (except the Rebate Fund and any Bond Purchase Fund), and investment earnings thereon. Amounts payable by the District pursuant to the Pledge Agreement are payable solely from and collateralized by amounts received by the District pursuant to a Full Funding Grant Agreement with the United States of America, acting through the Department of Transportation, Federal Transit Administration (the "Grant Agreement") and revenues, if any, under an interest rate cap agreement executed by the District in connection with the Airport Refunding Bonds. The financial obligation of the District under the Pledge Agreement is solely to transfer all receipts under the Grant Agreement to the Trustee. The Airport Refunding Bonds are not a general obligation of ABAG. The Airport Refunding Bonds were issued initially as Auction Rate Securities at an interest rate of 1.05%. Thereafter, the Airport Refunding Bonds will bear interest at the Auction Rate for the Auction Period, until a conversion to a daily, weekly, bond interest term or long-term interest rate period occurs. The initial auction period was on June 21, 2004, with the subsequent auction dates generally scheduled on each Monday of each week. The last auction date in fiscal year 2006 was on June 27, 2006 and the winning interest rate was 3.620%. An auction period generally consists of seven days. Interest payments are payable on the day following the end of each auction period. Payment of the principal and interest when due is insured by a financial guaranty insurance policy issued by an insurance company. The Airport Refunding Bonds are not subject to optional tender for purchase, nor does the District have a commitment to purchase them in the event of a "failed" auction. However, the bonds would be subject to mandatory tender if the District elects to convert the bonds to a different interest rate mode, provided certain conditions regarding the conversion are satisfied. The Airport Refunding Bonds are also subject to redemption prior to their stated maturity in part, by lot, from Mandatory Sinking Account Payments, on any June 15, or on after June 15, 2008, at the principal amount thereof and accrued interest thereon to the date fixed for redemption, without premium.

The interest rate cap has an initial notional amount of \$66,000,000, reducing to \$19,975,000 on June 15, 2008 and maturing on June 15, 2009. The reduction is tied to the principal amount and mandatory sinking fund payment schedule of the Series 2004 Bonds. The cap provides for payments to the District if the BMA Municipal Swap Index™ ("BMA") exceeds 7.00%. The cap effectively limits the amount the District is required to pay pursuant to the Pledge Agreement. Since the interest rate on the Series 2004 Bonds is reset weekly, the District chose to hedge its exposure to high interest rates by the purchase of the interest rate cap.

### **Terms**

Under the interest rate cap agreement, the District will receive, on an annual basis, payments from Citibank N.A. should BMA, or any successor index exceed 7.00%. The District paid \$248,000 upfront to Citibank N.A. for the interest rate cap for the full term of the agreement. The agreement terminates on June 15, 2009, which is the final maturity of the Series 2004 Bonds.

As of June 30, 2006, the notional amount of the rate cap was \$66,000,000, which was \$10,300,000 greater than the amount of outstanding Series 2004 Bonds. This is due to the District's redemption of \$10,300,000 of the Series 2004 Bonds on June 15, 2006. After the redemption \$55,700,000 of the Series 2004 Bonds remained outstanding.

### **Credit Risk**

As of June 30, 2006, the interest rate cap agreement had a fair market value of \$65. Citibank N.A. is rated Aa1 by Moody's Investors Service, AA by Standard & Poor's, and AA+ by Fitch Ratings.



## **Basis Risk**

The interest rate cap agreement exposes the District to basis risk due to any difference between the actual variable interest rate on the Airport Refunding Bonds and BMA. While BMA is a national tax-exempt index commonly used as a proxy for variable rate transactions, there is no guarantee that BMA will perform exactly as the District's variable interest rate. While the District believes BMA is a reasonable proxy for the District's expected variable interest rate, it is possible that the District's variable interest rate could exceed 7.00% while BMA does not. In this case the District would pay interest costs in excess of 7.00%.

## **Termination Risk**

The District retains the right to terminate the interest rate cap prior to maturity. If the interest rate cap agreement is terminated, the interest rate on the Airport Refunding Bonds would no longer be effectively capped at 7.00%.

## **2005 General Obligation Bonds (the 2005 GO Bonds)**

In May 2005, the District issued the General Obligation Bonds (Elections 2004), 2005 Series A (2005 GO Bonds) with an aggregate principal amount of \$100,000,000. The 2005 GO Bonds constitute a portion of the total authorized amount of \$980,000,000 of general obligation bonds of the District duly authorized by at least two-thirds of the qualified voters of the District voting on a ballot measure ("Measure AA") at an election held on November 2, 2004. The 2005 GO Bonds constitute the first issue of general obligation bonds being issued pursuant to the Measure AA authorization. The 2005 GO Bonds were issued to finance earthquake safety improvements to BART facilities, including aerial trackway structures, underground trackway structures, including the Transbay Tube, and at-grade trackway structures, stations, and administrative, maintenance, and operations facilities and to finance additional retrofits to facilitate a rapid return to service after an earthquake or other disasters. The 2005 GO Bonds are general obligations of the District, payable from and secured solely by *ad valorem* taxes upon all property subject to taxation by the District, without limitation as to rate or amount (except for certain personal property which is taxable at limited rates) levied in Alameda and Contra Costa Counties and the City and County of San Francisco. No other revenues of the District are pledged to the payment of the 2005 GO Bonds. At June 30, 2006, the 2005 GO Bonds consist of \$80,385,000 in serial bonds due from 2006 to 2026 with interest ranging from 2.75% to 5.00%, a \$7,720,000 term bond at 4.50% due in 2030 and a \$11,895,000 term bond at 5.00% due in 2035. The District is required to make sinking fund payments on the term bond due in 2030 beginning in 2027 and on the term bond due in 2035 beginning in 2031.

## **Defeased Bonds**

On various dates, the District issued bonds to refund certain outstanding sales tax revenue bonds previously issued by the District. In March 1998, the District used a portion of the proceeds of the 1998 Bonds to defease certain bonds outstanding with principal amounts totaling \$155,115,000. In July 2001, the District issued the 2001 Bonds and used a portion of the proceeds to defease selected bonds outstanding with principal amounts adding up to \$41,175,000. In August 2005, the District refunded \$349,925,000 aggregate principal amount of bonds outstanding from the proceeds of the 2005 Bonds. The bonds refunded in August 2005, consisted of \$45,275,000 of the 1995 Bonds, \$155,650,000 of the 1998 Bonds, \$129,360,000 of the 1999 Bonds and \$19,640,000 of the 2001 Bonds.

On all defeasance, the District placed in irrevocable trusts the required amounts to pay the future debt service payments on the defeased bonds. The advance refunding met the requirement of the in-substance debt defeasance, and the defeased bonds were removed from the District's long-term debt. Accordingly the trust accounts assets and liabilities for the defeased bonds are not included in the District's financial statements.

The outstanding principal balance of the defeased bonds as of June 30, 2006 is \$349,925,000, which relates to the bonds defeased in August 2005. The bonds defeased in March 1998 and July 2001 were all fully paid in fiscal year 2006.

The District deferred, and amortized as a component of interest, the difference between the reacquisition price and the net carrying amount of the old debts which amounted to \$34,547,000 for all defeasance. These deferred charges are amortized over the life of the defeased bonds. Amortization expense on these deferred charges was \$931,000 in fiscal year 2006 and \$478,000 in fiscal year 2005. The deferred charges related to the March 1998 and July 2001 defeasance amounting to \$9,143,000 were fully amortized in fiscal year 2006.

## **Arbitrage Bonds**

The District is subject to certain bond covenants, including the rules set forth by IRS Code Section 148a, which requires that interest earned on the proceeds of a tax exempt bond issuance does not exceed the interest expense related to those bonds, which qualifies those bonds as arbitrage bonds. Any excess interest income is subject to a 100% tax and is payable to the Federal Government. As of June 30, 2006, the District has recorded an estimated arbitrage liability amounting to \$674,000 and \$1,582,000 in 2005, which is included in other liabilities in the statements of net assets.

## Debt Repayments

The following is a schedule of long-term debt principal and interest payments required as of June 30, 2006 (dollar amounts in thousands):

Sales Tax Revenue Bonds											
Year ending June 30:	1990 Bonds		1998 Bonds		2001 Bonds		2005 Bonds		2006 Bonds		
	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest	
2007	\$ -	\$ 1,942	\$ 8,675	\$ 8,038	\$ -	\$ 7,310	\$ 12,655	\$ 16,017	\$ -	\$ 3,148	
2008	-	1,942	5,540	7,734	-	7,310	13,650	15,458	-	3,131	
2009	-	1,942	5,895	7,480	-	7,310	14,295	14,884	-	3,131	
2010	-	1,943	6,205	7,139	-	7,310	14,965	14,227	-	3,131	
2011	13,870	1,006	1,625	7,053	-	7,310	6,840	14,005	-	3,131	
2012-2016	14,905	-	13,040	32,999	18,875	34,083	58,440	62,790	580	15,626	
2017-2021	-	-	33,975	27,936	14,770	30,301	69,285	45,517	6,125	14,848	
2022-2026	-	-	71,190	11,804	26,080	24,672	52,585	34,150	10,645	12,884	
2027-2031	-	-	25,620	1,323	33,490	17,077	77,595	13,621	2,760	9,552	
2032-2036	-	-	-	-	43,090	7,210	31,785	2,481	17,995	4,225	
2037-2041	-	-	-	-	10,020	-	-	-	26,810	-	
	<u>\$ 28,775</u>	<u>\$ 8,775</u>	<u>\$171,765</u>	<u>\$111,506</u>	<u>\$146,325</u>	<u>\$149,893</u>	<u>\$352,095</u>	<u>\$233,150</u>	<u>\$64,915</u>	<u>\$72,807</u>	

Year ending June 30:	TFA Bridge Toll Notes		Construction Loans		FTA Capital Grant Bonds		Lease/ Leaseback Obligation**	
	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest
2007	\$ 21,785	\$ 560	\$ 10,000	\$ 1,410	\$ 46,330	\$ 2,160	\$ 28,826	\$ 10,536
2008	-	-	5,000	1,410	-	-	7,783	5,029
2009	-	-	5,000	1,260	-	-	713	6,586
2010	-	-	8,000	1,110	-	-	17,086	9,116
2011	-	-	8,000	870	-	-	5,192	2,923
2012-2016	-	-	4,895	1,170	-	-	-	3,611
2017-2021	-	-	-	-	-	-	80,652	83,533
2022-2026	-	-	-	-	-	-	-	-
2027-2031	-	-	-	-	-	-	-	-
2032-2036	-	-	-	-	-	-	-	-
2037-3041	-	-	-	-	-	-	-	-
Thereafter	-	-	88,500	-	-	-	-	-
	<u>\$ 21,785</u>	<u>\$ 560</u>	<u>\$129,395</u>	<u>\$ 7,230</u>	<u>\$ 46,330</u>	<u>\$ 2,160</u>	<u>\$140,252</u>	<u>\$121,334</u>

Year ending June 30:	2002 SFO Extension Premium Fare Bonds		2004 SFO Extension Refunding Bonds*		2005 General Obligation Bonds		Total	
	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest
2007	\$ 550	\$ 2,722	\$ -	\$ 2,016	\$ 12,815	\$ 3,660	\$ 141,636	\$ 48,984
2008	570	2,709	46,025	2,017	19,865	2,854	98,433	44,565
2009	640	2,693	9,675	723	25,960	1,955	62,178	45,773
2010	715	2,672	-	-	870	1,856	47,841	48,504
2011	795	2,647	-	-	895	1,829	37,217	40,774
2012-2016	5,345	12,616	-	-	4,915	8,670	120,995	171,565
2017-2021	8,435	10,866	-	-	5,900	7,603	219,142	220,604
2022-2026	12,575	8,177	-	-	7,445	5,953	180,520	97,640
2027-2031	18,010	4,270	-	-	9,440	3,898	166,915	49,741
2032-2036	9,080	273	-	-	11,895	1,297	113,845	15,486
2037-2041	-	-	-	-	-	-	36,830	-
Thereafter	-	-	-	-	-	-	88,500	-
	<u>\$56,715</u>	<u>\$49,645</u>	<u>\$ 55,700</u>	<u>\$ 4,756</u>	<u>\$100,000</u>	<u>\$39,575</u>	<u>\$1,314,052</u>	<u>\$783,636</u>

\* A rate of 3.620%, which was the actual rate as of June 30, 2006, was used for the purposes of calculating the annual interest payment requirements for the 2004 SFO Extension Refunding Bonds.

## 8. Risk Management

The District is partially self-insured for workers' compensation, public liability and property damage claims. The self-insured retention for workers' compensation is \$4,000,000. During the year, the self-insured retention for public liability and property damage increased from \$2,000,000 to \$5,000,000 for any one occurrence. Claims in excess of self-insured retentions are covered up to a total of \$95,000,000 by insurance policies. There have been no settlement amounts during the past three years that have exceeded the District's insurance coverage.

The self-insurance programs are administered by independent claims adjustment firms. Claim expenses and liabilities are reported when it is probable that a loss has occurred and the amount of that loss can be reasonably estimated. Liabilities are discounted at a 5% rate and are based, in part, upon the independent adjustment firms' estimate of reserves necessary for the settlement of outstanding claims and related administrative costs, and include estimates of claims that have been incurred but not yet reported, including loss adjustment expenses. Such reserves are reviewed by professional actuaries and are subject to periodic adjustments as conditions warrant.

The estimated liability for insurance claims at June 30, 2006 is believed to be sufficient to cover any costs arising out of claims filed or to be filed for accidents occurring through that date. At June 30, 2006 and 2005, the estimated amounts of these liabilities were \$28,354,000 and \$28,640,000, respectively. Changes in the reported liabilities since the beginning of the respective fiscal year are as follows (dollar amounts in thousands):

	2006	2005
Liabilities at beginning of year	\$28,640	\$27,007
Current year claims and changes in estimates	8,547	11,953
Payments of claims	(8,833)	(10,320)
Liabilities at the end of year	28,354	28,640
Less current portion	(9,174)	(9,340)
Net noncurrent portion	<u>\$19,180</u>	<u>\$19,300</u>



## 9. Federal Capital Financial Assistance

The U.S. Department of Transportation and other Federal agencies provide financial assistance to the District for capital projects, construction, planning and technical assistance. Cumulative information for grants which were active during the year ended June 30, 2006 are summarized as follows (dollar amounts in thousands):

	<b>SFO Extension Projects</b>
Total approved project costs	<u>\$ 1,347,230</u>
Total approved federal allocations received	749,575
Less: cumulative amounts of project costs incurred and earned	<u>(752,000)</u>
Capital grants receivable	<u>\$ (2,425)</u>

	<b>Other Capital Projects</b>
Total approved project costs	<u>\$ 793,340</u>
Total approved federal allocations	641,789
Less: cumulative amounts of project costs incurred and earned	<u>(511,462)</u>
Remaining approved federal allocation	<u>\$ 130,327</u>

The SFO Extension Project is mainly covered by a Federal Full Funding Grant Agreement in the amount of \$750,000,000, which authorizes the District to incur costs or expend local funds prior to an award of federal funding assistance without prejudice to possible future federal participation.

## 10. State and Local Financial Assistance

### Capital Assistance

The District is eligible to receive local operating and capital assistance from the Transportation Development Act Funds ("TDA"). There was no TDA operating or capital assistance received in fiscal years 2006 or 2005.

The District may be entitled to receive state operating and capital assistance from the State Transit Assistance Funds ("STA"). These funds are allocated by MTC based on the ratio of the District's transit operation revenue and local support to the revenue and local support of all state transit agencies. The District received STA operating allocation of \$2,925,000 in fiscal year 2006, and none in fiscal year 2005. The District also received an STA capital allocation amounting to \$1,170,000 in fiscal year 2004, of which \$63,000 was earned during fiscal year 2006 and \$837,000 in fiscal year 2005.

### Operating Assistance

The District receives Paratransit funds provided to cities and transit operators from Alameda County Measure B funds to be used for services aimed at improving mobility for seniors and persons with disabilities. The Alameda County Transportation Improvement Authority ("ACTIA") is the administrator of Measure B funds. A summary of the transactions related to the Measure B funds allocated to the District for fiscal years 2006 and 2005 are as follows (dollar amounts in thousands):

	<u>2006</u>	<u>2005</u>
Prior year allocation received as revenue in the current year	\$ 8	\$ 8
Current year allocation received as revenue in the current year	1,549	1,211
Current year allocation accrued as revenue in the current year	<u>5</u>	<u>240</u>
	<u>\$1,562</u>	<u>\$1,459</u>

The District's revenues in fiscal 2006 and 2005 that relate to the Measure B funds were \$1,562,000 and \$1,459,000, respectively.

The financial assistance from San Mateo County Transit District ("SamTrans") relates to the reimbursement of a portion of the operating costs in excess of fare revenues identified to the SFO Extension, which covers the Colma, South San Francisco, San Bruno, San Francisco International Airport and Millbrae stations. For fiscal year ended June 30, 2006, the District recognized \$10,206,000 and \$14,730,000 in 2005 in operating financial assistance from SamTrans.

## **11. Employees' Retirement Benefits**

### **Plan Description**

All employees are eligible to participate in the Public Employees' Retirement Fund (the "Fund") of the State of California's Public Employees' Retirement System ("CalPERS") under the Miscellaneous Plan and the Safety Plan of the San Francisco Bay Area Rapid Transit District. The Fund is an agent multiple-employer defined-benefit retirement plan that acts as a common investment and administrative agent for 2,582 local public agencies and school districts within the State of California. The Fund provides retirement, disability, and death benefits based on the employee's years of service, age and compensation. Employees vest after five years of service and may receive retirement benefits at age 50. These benefit provisions and all other requirements are established by State statute and District contractual agreements.

Copies of CalPERS' annual financial report may be obtained from their Executive Office - by writing or calling the Plan: California PERS, P.O. Box 942709, Sacramento, CA 94229-2709, (916) 326-3420. A separate report for the District's plan is not available.

### **Funding Policy and Annual Pension Cost**

The Plan's funding policy provides for periodic District contributions at actuarially-determined amounts sufficient to accumulate the necessary assets to pay benefits when due as specified by contractual agreements. The individual entry age normal cost method is used to determine the normal cost. Under this method, projected benefits are determined for all members and the associated liabilities are spread in a manner that produces level annual cost as a percent of pay in each year from the age of hire (entry age) to the assumed retirement age. Beginning on July 1, 1997, the unfunded actuarial accrued surplus or liability (past service liability) is amortized as a level percentage of future covered payroll over 13 years for the Miscellaneous Plan and the Safety Plan.

The District's covered payroll for employees participating in the Fund for the years ended June 30, 2006 and 2005 was \$220,757,000 and \$234,793,000, respectively. The District's 2006 and 2005 payroll for all employees was \$252,919,000 and \$261,269,000, respectively. The District, due to Collective Bargaining Agreements, also reimburses the employees for their contributions, which are 9% for public safety personnel and 7% for miscellaneous covered employees.

The annual required contribution for fiscal year 2006 was determined by an actuarial valuation of the Plans as of June 30, 2003. The contribution rates for fiscal year 2006 were 8.717% and 2.615% in 2005 of covered payroll for the Miscellaneous Plan and 32.324% and 28.910% in 2005 for the Safety Plan. The significant actuarial economic assumptions used in the 2003 valuation to determine the annual required contribution were an investment rate of return of 7.75%, projected salary increases from 3.25% to 14.45% depending on age, service and type of employment, and annual payroll increases of 3.00% attributable to inflation and 0.25% due to production growth.

Since the District has made the actuarially-determined required contributions since 1988, the pension liability or asset was zero at June 30, 2006, in accordance with GASB Statement No. 27, *Accounting for Pensions by State and Local Governmental Employers*.

The three-year trend information for the Fund of the actuarially required employer contribution is as follows (dollar amounts in thousands):

	<b><u>Year Ending</u></b>	<b><u>Annual Pension Cost (APC)</u></b>	<b><u>Percentage of APC Contributed (%)</u></b>	<b><u>Net Pension Obligation</u></b>
Miscellaneous Plan:	June 30, 2004	\$ -	-	\$ -
	June 30, 2005	5,586	100	-
	June 30, 2006	17,849	100	-
Safety Plan:	June 30, 2004	465	100	-
	June 30, 2005	4,534	100	-
	June 30, 2006	4,925	100	-

## Funded Status

The funded status applicable to the District's employee group at June 30, 2005 (the latest available for the Fund) is summarized as follows (dollar amounts in thousands):

### ***Funded Status of the Miscellaneous Plan***

<u>Valuation Date</u>	<u>Entry Age Normal Accrued Liability</u>	<u>Actuarial Value of Assets</u>	<u>Unfunded Liability (Excess Assets)</u>	<u>Funded Status (%)</u>	<u>Annual Covered Payroll</u>	<u>UAAL as a Percentage of Payroll (%)</u>
6/30/03	\$ 939,072	\$ 950,571	\$ (11,499)	101.2	\$202,170	(5.7)
6/30/04	1,023,593	992,217	31,376	96.9	209,675	15.0
6/30/05	1,138,543	1,071,223	67,320	94.1	214,698	31.4

### ***Funded Status of the Safety Plan***

<u>Valuation Date</u>	<u>Entry Age Normal Accrued Liability</u>	<u>Actuarial Value of Assets</u>	<u>Unfunded Liability (Excess Assets)</u>	<u>Funded Status (%)</u>	<u>Annual Covered Payroll</u>	<u>UAAL as a Percentage of Payroll (%)</u>
6/30/03	\$ 100,960	\$ 82,329	\$ 18,631	81.5	\$ 14,277	130.5
6/30/04	113,237	87,575	25,662	77.3	16,040	160.0
6/30/05	129,350	98,677	30,674	76.3	15,221	210.5

## 12. Money Purchase Pension Plan

Most District employees participate in the Money Purchase Pension Plan, which is a supplemental retirement defined contribution plan. In January 1981, the District's employees elected to withdraw from the Federal Social Security System ("FICA") and established the Money Purchase Pension Plan. The District contributes an amount equal to 6.65% of eligible employees' annual compensation (up to \$29,700 after deducting the first \$133 paid during each month) up to a maximum annual contribution of \$1,868. The non-represented employees receive an additional contribution equal to 1.627% of their annual compensation. The annual compensation limit subject to the additional contribution is established by the Internal Revenue Code Section 401(a)(17). For employees hired on or before July 1, 1993, the annual compensation limit is \$315,000 in calendar year 2006 and \$305,000 in calendar year 2005. For employees hired after July 1, 1993, the annual compensation limit is \$220,000 in calendar year 2006 and \$210,000 in calendar year 2005. Each employee's account is available for distribution upon such employee's termination.

The District's total expense and funded contribution for this plan for the years ended June 30, 2006 and 2005 were \$6,805,000 and \$7,050,000, respectively. The Money Purchase Pension Plan assets at June 30, 2006 and 2005 (excluded from the accompanying financial statements) per the plan administrator's unaudited report were \$262,898,000 and \$258,846,000, respectively. At June 30, 2006, there were approximately 304 (274 in 2005) participants receiving benefits under this plan.

The plan issues a publicly available financial report that includes financial statements and required supplementary information. This report may be obtained by writing or calling: BART Investments Plans Committee, 300 Lakeside Drive, Oakland, California 94612, (510) 464-6238.



## **13. Other Postemployment Benefits**

### **Postemployment Health Care Cost**

In addition to the retirement benefits described in Notes 11 and 12, and specified in the District's contractual agreements, the District provides postemployment health care benefits assistance to employees. Most employees who retire directly from the District or their surviving spouses are eligible if the employee retires at or after age 50 with a minimum of 5 years of service with the District, elects to take an annuity from CalPERS and makes a timely election of retiree medical. Currently, 1,226 retirees and surviving spouses (1,061 in 2005) are provided this benefit. The District paid up to \$769,000 and \$655,000 per month for health insurance premiums for the retirees and surviving spouses during fiscal years 2006 and 2005, respectively. These benefits, less a modest premium contribution, are fully paid by the District and accounted for on a pay-as-you-go basis. Cash reimbursements of these benefits totaled \$8,634,000 in 2006 and \$7,124,000 in 2005.

### **Retiree Health Benefit Trust**

In 2004, GASB issued Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. The new GASB statement will require the District to change its accounting for OPEB from pay-as-you-go to an accrual basis. If an employer elects to fund its OPEB liability, GASB 45 requires that for contributions to be recognized as an offset to the employer's actuarial required contribution, the contributions must be paid out in benefits or irrevocably transferred to a trust or an equivalent arrangement, and legally protected from creditors of the employer. The District will be required to implement the requirements of Statement No. 45 beginning in fiscal year 2008.

On May 18, 2004, the District created the Retiree Health Benefit Trust for the San Francisco Bay Area Rapid Transit District (the "Trust"). The purpose of establishing the Trust is to facilitate the provision of medical benefits and other health and welfare benefits for the qualifying retirees of the District; to provide the means for financing the costs and expenses of operating and administering such benefits; to hold Trust assets for the sole and exclusive purpose of providing benefits to participants and beneficiaries; and to defray the reasonable expenses of administering the Trust and designated plans. Assets placed into the Trust cannot be used for any other purposes and are not available to satisfy general creditors of the District. Under California state law, the restrictions on the use of any proceeds from liquidation of the Trust are significant enough to render the Trust effectively irrevocable. The Trust is administered by one or more Trustees appointed by the District's Board of Directors. Currently, the Board has appointed the District's Controller-Treasurer as the Trustee.

In fiscal year 2004, the District sold shares it had received in a transaction involving the demutualization of Principal Life Insurance Company. The demutualization-related cash received was transferred to the Trust in recognition of the District's desire to set aside funds that can be used to satisfy its retiree health benefits funding obligation. In addition to the demutualization-related cash, the District had also contributed in fiscal year 2005 cash proceeds from operations, which brought the total District contributions to the Trust as of June 30, 2006 to \$36,222,000, which is shown as a special item (expense) in the statements of revenues, expenses and changes in net assets. At June 30, 2006, assets held in the Trust included investment in money market, U.S. Treasury obligations, corporate obligations, foreign obligations, foreign stocks, and domestic common stock with an aggregate fair value of \$42,352,000. These investments are included in the District's financial statements and are restricted to use for payment of retiree benefit liabilities that will be recorded when GASB 45 is adopted.

## **14. Board of Directors' Expenses**

Total Directors' expenses, consisting of travel and other business related expenses for the years ended June 30, 2006 and 2005 amounted to \$37,000 and \$28,000, respectively.

## **15. Transit Financing Authority**

The Joint Exercise of Powers Agreement (the "Agreement"), dated August 1, 1991, between the District and MTC provided for the creation of the Transit Financing Authority (the "Authority"), a public instrumentality of the State of California. The initial term of the Agreement was for ten years, unless extended or earlier terminated. On May 1, 1998, the term of the Agreement was extended to August 1, 2010. The Authority was formed for the purpose of providing financing and contracting for public transit improvements, including the refinancing of prior indebtedness and acquiring, selling and financing public capital improvements, working capital, liability and other insurance needs, and for the specific purpose of assisting in financing the District's East-Bay and West-Bay extensions. The Authority's financial information is presented as a blended component unit of the District's financial statements because the Authority provides services almost exclusively to the District.

The governing board of the Authority consists of two members each from the District and MTC. Neither the District nor MTC is responsible for any debt, liabilities or obligations of the Authority.

At the end of the term or upon the earlier termination of the Agreement, all assets of the Authority shall be distributed to the two participants, and any surplus money on hand shall be returned to these participants in proportion to their respective contributions to the Authority.

A summary of the amount and percentage of the Authority's total assets, total liabilities and total net assets as compared with the District is as follows (dollar amounts in thousands):

	<u>2006</u>	<u>2005</u>
Authority's total assets		
Amount	\$92,472	\$94,686
As a % of District's total assets	1.6%	1.6%
Authority's total liabilities		
Amount	\$92,472	\$94,686
As a % of District's total liabilities	5.7%	5.6%
Authority's total net assets		
Amount	\$ -	\$ -

The Authority issues a financial report that includes financial statements and required supplementary information. This report may be obtained by contacting the District's Controller-Treasurer at 300 Lakeside Drive, P.O. Box 12688, Oakland, California 94604.

## 16. Related Organizations and Projects

### Capitol Corridor Joint Powers Authority

The Joint Exercise of Powers Agreement dated December 31, 1996, between the District and five other transportation authorities in surrounding counties ("Agencies") provided for the creation of the Capitol Corridor Joint Powers Authority ("Capitol Corridor"), a public instrumentality of the State of California. Capitol Corridor was formed for the purpose of administering and managing the operation of the Capitol Corridor Rail Service as part of the California intercity passenger rail system. The District is the managing agency of Capitol Corridor and in that capacity shall provide all necessary administrative support to Capitol Corridor. Capitol Corridor entered into an Interagency Transfer Agreement with the State of California and assumed administration and operation commencing on July 1, 1998. The initial term of the Interagency Transfer Agreement was for three years beginning July 1, 1998, and was extended for three additional years effective July 1, 2001. In 2004, State legislation was enacted that eliminated the sunset date of the Interagency Transfer Agreement, which now exists indefinitely.

The governing board of Capitol Corridor consists of six members from the District and two members from each of the five other Agencies. Neither the District nor the other Agencies are responsible for any debt, liabilities and obligations of Capitol Corridor and the District would not be entitled to any of Capitol Corridor's net assets should it terminate.

The District charged Capitol Corridor a total of \$3,791,000 for marketing and administrative services during 2006 and \$2,982,000 during 2005. In addition, Capitol Corridor reimburses the District for its advances for capital project expenditures and other operating expenses. Reimbursements for expenses incurred by the District on behalf of and in providing services to Capitol Corridor are netted against the corresponding expense in the statements of revenues, expenses and changes in net assets. At June 30, 2006, unreimbursed expenses from Capitol Corridor amount to \$2,480,000 and \$8,262,000 as of June 30, 2005. All unreimbursed expenses are included as current receivables and other assets in the statements of net assets. As the District has no ownership involvement or ongoing financial interest or responsibility in Capitol Corridor, its financial statements include only amounts related to the services it provides to Capitol Corridor.

## Technology Reinvestment Project

In 1994, The District and the joint venture of Hughes Transportation Control Systems, Inc. (Hughes), and Morrison Knudsen Train Control, Inc. (HMK) entered into a memorandum of understanding (MOU) to form an alliance (Alliance) to develop a cost-effective, highly reliable and safe train control system for passenger and freight-carrying trains. The project is more commonly known as the Advanced Automatic Train Control (AATC) project. During fiscal year 1998, the Alliance was reorganized. Hughes and HMK withdrew and were replaced by Harmon Industries, Inc. (Harmon). In August 1998, a MOU was executed between the District and Harmon which replaced the 1994 MOU between the District and the joint venture of Hughes and HMK. In 2000, Harmon was purchased by GE Transportation Systems, and Harmon became known as GE Transportation Systems, Global Signaling.

The AATC project has three phases which are: Phase 1, the prototype phase, which demonstrates the feasibility of the technical concepts through a demonstration of the technology at BART's Hayward test track; Phase 2, the development phase, which implements the pilot system at two BART train stations and on ten control cars to demonstrate the safety of the system; and Phase 3, the implementation phase, which implements the AATC system on eight additional BART train stations and 289 control cars, including training of BART personnel, creation of manuals and supply of spare parts.

Phase 1 was completed in 1996, while work on Phase 2 and Phase 3 is still in progress. Phase 1 and Phase 2 were partially funded by the Technology Reinvestment Project managed by the Advanced Research Projects Agency (ARPA). The Alliance handled the disbursements for project costs paid out of the ARPA grant. The District's participation in Phase 1 and Phase 2 include in-kind contributions, which consisted primarily of cost of vehicles and infrastructure use and labor and other direct costs, totaling \$25,848,000, of which \$948,000 was reimbursed by the Alliance. Additional funding for Phase 2 and Phase 3 came from the federal allocations of \$66,844,000, State grants of \$4,728,000, local agency contributions of \$2,389,000 and the District's own funds of \$36,859,000. The total project expenditures through June 30, 2006 for Phase 2 and Phase 3 amount to \$79,365,000.

## East Bay Paratransit Consortium

In 1994, the District and the Alameda-Contra Costa Transit District ("AC Transit") executed an agreement establishing the East Bay Paratransit Consortium (the "Consortium"). The purpose of the Consortium is to enable the District and AC Transit to jointly provide paratransit services in the overlapping service area of the District and AC Transit. Revenues and expenditures for the Consortium are split 31% and 69% between the District and AC Transit, respectively, and the District's financial statements reflect its portion of revenues and expenditures as operating activities. The District supported the project primarily through its own operating funds, with some financial assistance from Alameda County Measure B funds (see Note 10). The District has no equity interest in the Consortium.

## 17. Commitments and Contingencies

### Litigation

The District is involved in various lawsuits, claims and disputes, which for the most part are normal to the District's operations. It is the opinion of the District's management that the costs that might be incurred in the disposition of these matters, if any, would not materially affect the District's financial position.

### Lease Commitments

The District leases certain facilities under operating leases with original terms ranging from one to 50 years with options to renew.

Future minimum rental payments under noncancelable operating leases with initial or remaining lease terms of over one year at June 30, 2006 are as follows (dollar amounts in thousands in table to right):

Rent expenses under all operating leases were \$10,504,000 and \$9,127,000 for the years ended June 30, 2006 and 2005, respectively.

<u>Year ending June 30</u>	<u>Operating Leases</u>
2007	\$ 10,250
2008	11,053
2009	10,973
2010	10,873
2011	10,749
2012 - 2016	36,639
2017 - 2021	12,804
2022 - 2026	12,500
2027 - 2031	12,500
2032 - 2036	12,500
2037 - 2041	12,500
2042 - 2046	12,500
2047 - 2051	12,500
Total minimum payments	<u>\$ 178,341</u>



## Fruitvale Development Corp.

On October 1, 2001, the District entered into a ground lease agreement with Fruitvale Development Corp (“FDC”) pertaining to 1.8 acres of land for the purpose of constructing thereon portions of a mixed-use development project commonly known as the Fruitvale Transit Village, which was planned to consist of approximately 250,000 square feet of commercial, community service and residential improvements. The lease agreement was effective December 9, 2003, the regular term date, which was also the opening date, and continues through January 31, 2077.

The terms of the lease require FDC to pay the District a Base Rent and a Percentage Rent. The Base Rent is a fixed amount determined at the inception of the lease subject to periodic CPI adjustments. Percentage Rent is calculated equal to 15% of annual net revenues, as defined in the ground lease agreement.

The District provided FDC a Rent Credit with an initial amount of \$7,247,000, to acknowledge its assistance in obtaining grants for the construction of a Replacement BART Commuter Parking Garage near the Fruitvale Transit Village. The Rent Credit earns interest on the outstanding balance at simple interest based on the prime rate and can only be applied to satisfy the Base Rent. Based on the agreement, FDC shall not be under any obligation to make any cash payment to the District for Base Rent at any time that Rent Credit still has a positive balance. Changes in the Rent Credit for fiscal years 2006 and 2005 are summarized as follows (dollar amounts in thousands):

	<u>2006</u>	<u>2005</u>
Rent Credit at beginning of year	\$7,590	\$7,316
Annual base rent applied against the credit	(98)	(98)
Interest credit during the year	<u>506</u>	<u>372</u>
Rent Credit at end of year	<u>\$7,998</u>	<u>\$7,590</u>

## Sale/Leaseback and Lease/Leaseback Obligations

The District has entered into two leaseback obligations relating to rail traffic control equipment and rail cars.

On March 30, 1995, the District entered into an agreement with a Swedish corporation to sell 25 newly manufactured C-2 rail cars for \$50,383,000 and simultaneously entered into an agreement to lease them back. The lease agreement was effective on the closing date of September 15, 1995 and continues through January 15, 2011. The District recorded a gain on the sale of approximately \$2,015,000, which is equal to the amount of cash received on the sale.

On March 19, 2002, the District entered into a transaction to lease rail traffic control equipment (the “Network”) to investors through March 19, 2042 and simultaneously sublease the Network back through January 2, 2018. The District received a head lease payment of \$206,000,000 which is equivalent to the fair market value of the Network at closing. To fulfill its sublease obligations, the District paid approximately \$146,000,000 to a payment undertaker and deposited \$37,000,000 to a trust account. The District received cash from this lease/leaseback transaction amounting to approximately \$23,000,000.

On May 17, 2006, President Bush signed into law an act entitled the “Tax Increase Prevention and Reconciliation Act of 2005” (the “Tax Act”). Among other provisions, the Tax Act imposes an excise tax on certain types of leasing transactions entered into by tax-exempt entities, including states and their political subdivisions (including the District). The District currently is evaluating this legislation. At this time, it is unclear to what extent the excise tax imposed by the Tax Act is applicable to the District Lease Transactions and, if so, the magnitude of the District’s excise tax liability, if any, with respect to the District Lease Transactions.

# Sources and Uses of Operating Funds

	<b>FY 2006</b>		<b>FY 2005</b>	
	<b>Amount</b> (in thousands)	<b>Percent</b>	<b>Amount</b> (in thousands)	<b>Percent</b>
<b>Sources of Operating Funds</b>				
Transaction & Use Sales Tax	\$ 191,680	35%	\$ 178,392	36%
Passenger Fares	256,238	46%	233,651	47%
Property Tax	24,325	4%	22,412	4%
Other:				
Investment Income & Other Operating Revenues	23,435	4%	17,113	3%
Construction Funds (Capitalized Costs)	33,785	6%	33,612	7%
Financial Assistance	15,749	3%	16,680	3%
Gain From Sale of Property, Net	11,042	2%	0	0%
Total - Other	84,011	15%	67,405	13%
<b>Total Sources of Operating Funds</b>	<b>\$ 556,254</b>	<b>100%</b>	<b>\$ 501,860</b>	<b>100%</b>
<b>Uses of Operating Funds</b>				
Maintenance	\$ 168,226	30%	\$ 163,051	33%
Transportation	125,022	23%	127,391	25%
General Administration	111,532	20%	109,130	22%
Police Services	39,109	7%	37,510	7%
Construction & Engineering	17,777	3%	16,030	3%
Other:				
Capital Designation	28,166	5%	(6,460)	-1%
Debt Service Allocation	62,719	11%	59,513	12%
Increase (Decrease) in Net Assets - General Fund	3,703	1%	(4,305)	-1%
Total - Other	94,588	17%	48,748	10%
<b>Total Uses of Operating Funds</b>	<b>\$ 556,254</b>	<b>100%</b>	<b>\$ 501,860</b>	<b>100%</b>





Sources and Uses of Capital Funds

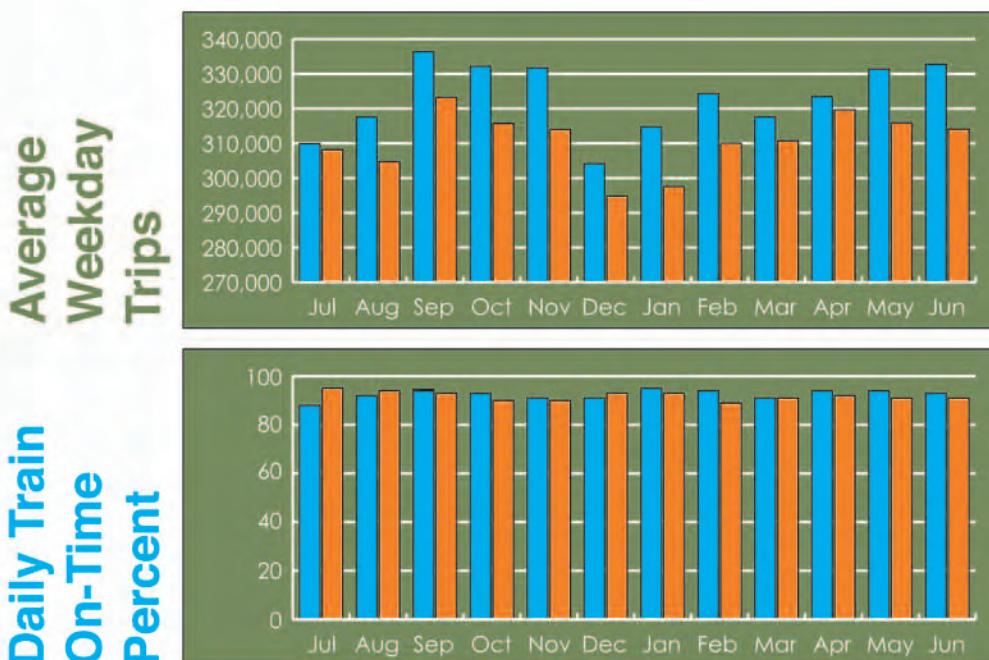
	<u>FY 2006</u>		<u>FY 2005</u>	
	<u>Amount</u> (in thousands)	<u>Percent</u>	<u>Amount</u> (in thousands)	<u>Percent</u>
<b>Sources of Capital Funds</b>				
District	\$ 46,316	43%	\$ 36,564	32%
Federal	37,228	34%	35,951	31%
State	8,148	7%	14,591	13%
Local	17,111	16%	27,405	24%
Total Sources of Capital Funds	<u>\$ 108,803</u>	<u>100%</u>	<u>\$ 114,511</u>	<u>100%</u>
<b>Uses of Capital Funds</b>				
<b>Construction:</b>				
Line	\$ 43,276	40%	\$ 54,388	48%
Systemwide	35,397	33%	16,183	14%
Support Facilities	1,463	1%	365	0%
Total – Construction	80,136	74%	70,936	62%
<b>Equipment:</b>				
Train Control	7,845	7%	7,128	6%
Transit Vehicles	4,498	4%	9,494	8%
Automatic Fare Collections	6,615	6%	11,488	10%
Management Information Systems	2,788	3%	10,457	9%
Other Equipment	2,362	2%	3,215	3%
Total – Equipment	24,108	22%	41,782	36%
<b>Studies &amp; Other</b>	4,559	4%	1,793	2%
Total Uses of Capital Funds	<u>\$ 108,803</u>	<u>100%</u>	<u>\$ 114,511</u>	<u>100%</u>

# Performance Highlights

	<u>FY06</u>	<u>FY05</u>
Annual passenger trips	96,852,220	92,756,099
Average weekday trips	322,965	310,717
Average trip length	13.50	13.54
Annual passenger miles	1,307,104,673	1,255,540,964
Daily train on-time performance	92.45%	91.4%
System utilization	31.4%	31.2%
End-of-period ratios <sup>1</sup>		
Peak patronage	57%	57%
Off-peak patronage	43%	43%
Annual revenue car miles	62,088,502	60,004,354
Unscheduled train removals		
Passenger accidents/million passenger trips	5.76%	5.93%
Passenger crimes/million passenger trips	20.09%	
Net passenger revenue	\$256,238,520	\$233,651,427
Other operating revenue	\$23,434,139	\$17,112,605
Total operating revenue	\$279,672,659	\$250,764,032
Net operating expense, excluding depreciation	\$427,880,784	\$419,499,394
System farebox ratio		
Net passenger revenue/net operating expense	59.9%	55.7%
System operating ratio		
Total operating revenue/total operating expense	65.4%	59.8%
Net rail passenger revenue/passenger mile	\$0.196	\$0.186
Rail operating cost/passenger mile	31.8¢	32.3¢
Net average rail passenger fare	\$2.64	\$2.51
Including FastPass		

Notes:

1. Six hour peak period (three hours a.m. and three hours p.m.)



## BART Board of Directors – Fiscal Year 2006

Carole Ward Allen	President - Oakland
Lynette Sweet	Vice President - San Francisco

## Members of the Board

Gail Murray	District 1	Orinda
Joel Keller	District 2	Antioch
Bob Franklin	District 3	Berkeley
Carole Ward Allen	District 4	Oakland
Zoyd Luce	District 5	Dublin
Thomas M. Blalock	District 6	Fremont
Lynette Sweet	District 7	San Francisco
James Fang	District 8	San Francisco
Tom Radulovich	District 9	San Francisco

## Board Appointed Officers

Thomas E. Margro	General Manager
Sherwood Wakeman	General Counsel
Scott Schroeder	Controller/Treasurer
Ken Duron	District Secretary



- Established in 1957 by the California State Legislature.
- Authorized to plan, finance, construct, and operate a rapid transit system.
- Governed by the Board of Directors elected for four-year terms by voters in nine election districts within the counties of Alameda, Contra Costa and San Francisco.

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