PRICEWATERHOUSECOOPERS

San Francisco Bay Area Rapid Transit District

Report on Audits of Financial Statements
For the years ended June 30, 2002 and 2001

San Francisco Bay Area Rapid Transit District
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PRICEWATERHOUSECOOPERS

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Report of Independent Accountants

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

In our opinion, the accompanying statements of net assets and the related statements of revenues, expenses and changes in fund net assets, and statements of cash flows present fairly, in all material respects, the financial position of San Francisco Bay Area Rapid Transit District (the "District") at June 30, 2002 and 2001, and the changes in its financial position and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the District's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements 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, which 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 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, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 1 to the financial statements, the District adopted the provisions of the Governmental Accounting Standards Board (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 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*, and Statement No. 38, *Certain Financial Statement Note Disclosure*, effective July 1, 2000.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 6, 2002, 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 grants for the year ended June 30, 2002. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

The Management's Discussion and Analysis on pages 2 through 7 is not a required part of the financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

PricewaterhouseCoopers LLP

December 6, 2002

Management's Discussion and Analysis (unaudited)

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 year ended June 30, 2002 with selected comparative information for the year ended June 30, 2001. This discussion has been 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 and presently owns a 95-mile, 39–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

For the fiscal year ended June 30, 2002, the District adopted Governmental Accounting Standards Board (GASB) Statement No. 34, *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments* as amended by GASB No. 37, *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments: Omnibus and GASB Statement No. 38, Certain Financial Statements Note Disclosures* and has applied those statements on a retroactive basis. GASB Statement No. 34 establishes the accounting and financial reporting standards for state and local governments, including special-purpose governments such as the District. The objective of the GASB in developing the new reporting standards is "to enhance the understandability and usefulness of the general purpose external financial reports of state and local governments to citizenry, legislative and oversight bodies and investors and creditors."

GASB Statement No. 38 modifies, establishes, and rescinds certain financial statement disclosure requirements.

The District's basic financial statements include (1) the *Statement of Net Assets*, (2) the *Statement of Revenues, Expenses and Changes in Fund Net Assets*, and (3) the *Statement of Cash Flows*. 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.

Significant Changes to the Financial Statements

Statement of Net Assets replaces the Balance Sheet

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 through 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 assets allocated to fund capital projects, reserves for liabilities to employees for accrued salaries, benefits and compensated absences, reserves for self-insurance and other liabilities, which indicate that management does not consider them to be available for general operations.

Statement of Revenues, Expenses and Changes in Fund Net Assets replaces the Statement of Revenues and Expenses. Revenues and expenses are now categorized as either operating or nonoperating based upon the definitions provided by GASB Statements No. 33 and No. 34. Significant recurring sources of the District's revenues, such as capital contributions, are reported as nonoperating revenues.

Statement of Cash Flows is presented using the direct method and includes a reconciliation of operating cash flows to operating income.

Financial Highlights

Statement of Revenues, Expenses and Changes in Fund Net Assets

A summary of the District's *Statements of Revenues, Expenses and Changes in Fund Net Assets* for fiscal years 2002 and 2001 is as follows (in thousands):

			Increase (Decrease)	
	2002	2001	Amount	%
Operating revenues	$ 207,608	$ 226,637	$ (19,029)	(8%)
Operating expenses	(432,656)	(414,040)	(18,616)	(4%)
Operating loss	(225,048)	(187,403)	(37,645)	(20%)
Nonoperating revenues (expenses)	184,301	219,180	(34,879)	(16%)
Capital contributions	235,825	278,140	(42,315)	(15%)
Increase in net assets	$ 195,078	$ 309,917	$ (114,839)	(37%)

An increase or decrease in net assets is an indicator of whether the District's financial health is improving or deteriorating. For the fiscal years ended June 30, 2002 and 2001, the District's net assets increased by $195 million and $310 million, respectively.

The rapid decline of the Bay Area economy during fiscal year 2002 had a deep negative impact on the District's two main sources of operating revenues – passenger fare and sales tax. On an overall basis the combined operating and nonoperating revenues for fiscal year 2002 decreased by approximately $54 million or 12% compared to the prior year. The decrease was mainly due to (a) $20 million decrease in passenger revenues from $213 million in 2001 to $193 million in 2002, (b) $19 million decrease in sales tax revenue from $192 million in 2001 to $173 million in 2002 and (c) $15 million decrease in the general fund and capital fund investment earnings. The decrease in passenger revenue is due to the decrease in system ridership, which dropped to an annual total of 91 million in 2002 from 97 million in 2001. The decrease in investment earnings is due to a combination of the drop in interest rates from an average of 6% in 2001 to 4% in 2002 and the reduction in the principal amount invested as funds are expended for the construction and acquisition of capital assets.

The net operating expenses, net of depreciation, for 2002 are $338 million and $334 million for 2001 or a net increase of $4 million. The increase is attributable to a $7 million net increase in employees' salaries, wages and benefits offset by a $3 million decrease in nonlabor and other costs. The net increase in salaries is mainly due to the 6% increase in 2002 given to the employees in compliance with the contractual labor union agreements.

The depreciation expense increased by $14 million from $80 million in 2001 to $94 million in 2002 mostly because of the depreciation on rehabilitated revenue cars put back in operation.

Statement of Net Assets

A comparison of the District's *Statements of Net Assets* as of June 30, 2002 and 2001 is as follows (in thousands):

	2002	**2001**
Current assets	$ 662,999	$ 873,549
Noncurrent assets - capital assets, net	4,817,029	4,383,115
Noncurrent assets - other	682,690	416,219
Total assets	$ 6,162,718	$ 5,672,883
Current liabilities	$ 320,676	$ 291,210
Noncurrent liabilities	1,526,048	1,260,757
Total liabilities	$ 1,846,724	$ 1,551,967
Net assets:		
Invested in capital assets, net of debt	$ 3,715,588	$ 3,531,697
Restricted net assets	467,485	405,433
Unrestricted net assets	132,921	183,786
Total net assets	$ 4,315,994	$ 4,120,916

Capital Assets

As of the end of fiscal year 2002, the District's capital assets, before accumulated depreciation, increased by $523 million. The major additions during the year included capital expenditures for the San Francisco International Airport Extension Project ($249 million), the A&B Car Rehabilitation ($144 million), Systemwide and Basic Line Construction and Improvements ($79 million) and the AFC Equipment Modernization ($17 million).

Details of the capital assets, net of accumulated depreciation, as of June 30, 2002 and 2001 are as follows (in thousands):

	2002	2001
Land	$ 245,835	$ 243,478
Stations, track, structures and improvements	1,439,955	1,460,259
Buildings	22,346	13,996
Revenue transit vehicles	699,753	568,141
Other	240,034	238,286
Construction in progress	2,169,106	1,858,955
Total	$ 4,817,029	$ 4,383,115

Long-Term Debt

The outstanding balance of long-term debt at the end of fiscal year 2002 shows a net increase of $241 million over prior year. The additional debts in 2002 are the issue of the Series 2001 Sales Tax Revenue Bonds with principal amounts of $168,650 000 and the lease/leaseback payable of $186,616,000 covering rail traffic control equipment. Below is a summary of long-term debt as of June 30, 2002 and 2001 (including portion due in one year but excluding unamortized balance of debt issue costs and bond premium) (in thousands):

	2002	2001
Bonds payable from and collateralized by a pledge of sales tax revenues	$ 762,501	$ 649,361
Bonds payable from and secured by the Federal Full Funding Grant Agreement for the San Francisco International Airport Extension Project	426,655	485,350
Notes payable from bridge toll revenues	53,355	60,345
Construction loans payable from the net operating surplus of the San Francisco International Airport Extension	88,500	88,500
Construction loan for temporary cash flow requirements of the San Francisco International Airport Extension Project	12,325	5,335
Lease/leaseback obligation, including option price, for rail traffic control equipment	186,616	-
Total	$ 1,529,952	$ 1,288,891

In fiscal year 2002, the District issued Series 2001 Sales Tax Revenue Bonds for $168,650,000 to fund certain capital projects and to refund $41,175,000 aggregate principal amount of currently outstanding bonds to achieve cash flow savings. The uninsured portion of Series 2001 Bonds with a principal amount of $2,685,000 was given ratings of AA, Aa3 and AA- by three national rating agencies, while the insured portion with principal amount totaling $165,965,000 received ratings of AAA, Aaa and AAA from the same three national rating agencies.

On March 19, 2002, the District entered into a head lease agreement to lease rail traffic control equipment (the "Network") which include communications, train control, central control equipment and destination sign systems with an aggregate net book value of $203 million. The District simultaneously entered into a sublease agreement to lease the Network back. The head lease has a term of 40 years, which expires on March 19, 2042. The sublease has a term of 15 years and 9 months expiring on January 2, 2018. On the expiration date of the sublease agreement, the District will, in accordance with the sublease contract, purchase from the sublessor the remaining head lease interest at a certain price ("the purchase option"), unless it elects to exercise its "non-purchase option". At the closing date of the head lease agreement, the District received $206 million for basic lease payments, of which $146 million were paid to a Payment Undertaker and $37 million was deposited in a trust to be used to pay the District's lease obligations and the purchase option price if the District elects to do so.

Statement of Cash Flows/Cash and Investments

On an overall basis, the total cash and investments held by the District at the end of the year decreased by $135 million from $871 million in 2001 to $736 million in 2002. The decrease in cash and investments is mainly attributed to the following: (a) $24 million decrease in receipts from ticket sales, and other operating revenues, (b) $15 million decrease in sales tax, property tax and other financial assistance, (c) $21 million decrease in receipts from investment earnings from operating and capital funds, (d) $57 million increase in expenditures, net of capital grants received, for the construction of various capital projects, (e) $61 million increase in principal payments of long term debts, and offset by (f) $60 million increase in cash from the 2002 lease/leaseback of rail traffic control equipment.

A comparative presentation of the major sources and uses of cash for 2002 and 2001 are as follows (in thousands):

	2002	2001
Net cash used in operating activities	$ (123,383)	$ (104,024)
Net cash provided by noncapital financing activities	136,992	160,675
Net cash used by capital and related financing activities	(189,485)	(65,266)
Net cash provided by investing activities	79,136	184,423
Net increase in cash and cash equivalents	(96,740)	175,808
Cash and cash equivalents, beginning of year	528,753	352,945
Cash and cash equivalents, end of year	$ 432,013	$ 528,753

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 San Francisco Bay Area Rapid Transit District's finances and to demonstrate its accountability for funds received. For additional information about this report, please contact Scott Schroeder, Controller-Treasurer, at 800 Madison Street, Oakland, California 94607.

San Francisco Bay Area Rapid Transit District
Statements of Net Assets
June 30, 2002 and 2001
(in thousands)

	2002	2001
Assets		
Current assets:		
Unrestricted assets:		
Cash and cash equivalents	$ 245,677	$ 229,396
Investments	14,662	59,863
Capital grants receivable	49,191	48,490
Other receivables	12,145	14,200
Materials and supplies	24,711	23,691
Total unrestricted current assets	346,386	375,640
Restricted assets:		
Cash and cash equivalents	186,336	299,357
Investments	16,183	112,943
Capital grants receivable	100,000	80,605
Other receivables	10,940	1,850
Current portion of capital lease receivable	3,154	3,154
Total restricted current assets	316,613	497,909
Total current assets	662,999	873,549
Noncurrent assets:		
Capital assets:		
Facilities, property and equipment, net	4,817,029	4,383,115
Investments - restricted	230,446	151,506
Investments - unrestricted	42,210	17,451
Capital grants receivable - restricted	241,640	215,485
Long-term portion of capital lease receivable - restricted	23,659	26,813
Deferred charges - unrestricted	1,473	839
Other receivables - restricted	141,690	-
Other assets - unrestricted	1,572	4,125
Total noncurrent assets	5,499,719	4,799,334
Total assets	6,162,718	5,672,883
Liabilities and Net Assets		
Liabilities:		
Current liabilities:		
Accounts payable and other liabilities	230,007	190,164
Current portion of long-term debt	69,361	81,740
Self-insurance liabilities	10,735	9,466
Deferred revenue	7,419	6,686
Capital lease liability	3,154	3,154
Total current liabilities	320,676	291,210
Noncurrent liabilities:		
Long-term debt, net of current portion	1,448,845	1,200,216
Self-insurance liabilities	17,185	18,644
Deferred revenue	35,809	15,084
Capital lease liability	23,659	26,813
Other noncurrent liabilities	550	-
Total noncurrent liabilities	1,526,048	1,260,757
Total liabilities	1,846,724	1,551,967
Commitments and contingencies (Note 13).		
Net assets		
Invested in capital assets, net of related debt	3,715,588	3,531,697
Restricted net assets	467,485	405,433
Unrestricted net assets	132,921	183,786
Total net assets	$ 4,315,994	$ 4,120,916

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

San Francisco Bay Area Rapid Transit District
Statements of Revenues, Expenses and Changes in Fund Net Assets
For the years ended June 30, 2002 and 2001
(in thousands)

	2002	2001
Operating revenues:		
Fares	$ 193,701	$ 213,260
Other	13,907	13,377
Total operating revenues	207,608	226,637
Operating expenses:		
Transportation	101,400	100,406
Maintenance	134,275	135,353
Police services	27,446	25,007
Construction and engineering	15,526	15,476
General and administrative	97,708	90,283
Depreciation	94,287	79,956
Total operating expenses	470,642	446,481
Less - capitalized costs	(37,986)	(32,441)
Net operating expenses	432,656	414,040
Operating loss	(225,048)	(187,403)
Nonoperating income (expense):		
Transactions and use tax (sales tax)	172,774	191,648
Property tax	18,713	17,260
State and local financial assistance	1,253	529
Investment income	28,131	43,123
Interest expense	(36,044)	(32,471)
Other expense, net	(526)	(909)
Total nonoperating income, net	184,301	219,180
Income (loss) before capital contributions	(40,747)	31,777
Capital contributions:		
Grants restricted for capital expenditures (Note 1)	235,825	278,140
Net assets		
Increase in net assets	195,078	309,917
Total net assets, beginning of year	4,120,916	3,810,999
Total net assets, end of year	$ 4,315,994	$ 4,120,916

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

San Francisco Bay Area Rapid Transit District
Statements of Cash Flows
For the years ended June 30, 2002 and 2001
(in thousands)

	2002	2001
Cash flows from operating activities		
Receipts from customers	$ 194,998	$ 212,414
Payments to suppliers	(91,862)	(98,978)
Payments to employees	(238,093)	(235,388)
Other operating cash receipts	11,574	17,928
Net cash used by operating activities	(123,383)	(104,024)
Cash flows from noncapital financing activities		
Transactions and use tax (sales tax) received	116,070	143,515
Property tax received	19,140	16,464
Financial assistance received	1,782	696
Net cash provided by noncapital financing activities	136,992	160,675
Cash flows from capital and related financing activities		
Transactions and use tax (sales tax) received	56,704	48,133
Property tax received	-	223
Capital grants received	191,980	207,340
Proceeds from issuance of FTA Capital Grant Bonds	-	485,350
Proceeds from issuance of sales tax revenue bonds	168,650	-
Proceeds from construction loans	10,000	10,000
Expenditures for facilities, property and equipment	(510,269)	(468,202)
Principal paid on long term debt	(122,915)	(20,385)
Proceeds from lease/leaseback of rail traffic control equipment	60,251	-
Payments of long term debt issuance and service costs	(4,837)	(6,270)
Payment of commercial paper notes	-	(300,000)
Premium received from issuance of long term debt	-	15,872
Interest paid on long term debt	(39,202)	(37,484)
Principal payments received from installment receivable	153	157
Net cash used by capital and related financing activities	(189,485)	(65,266)
Cash flows from investing activities		
Proceeds from sale and maturity of investments	343,867	778,094
Purchase of investments	(298,128)	(647,924)
Interest on investments	33,397	54,253
Net cash provided by investing activities	79,136	184,423
Net (decrease) increase in cash and cash equivalents	(96,740)	175,808
Cash and cash equivalents, beginning of year	528,753	352,945
Cash and cash equivalents, end of year	$ 432,013	$ 528,753

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

San Francisco Bay Area Rapid Transit District
Statements of Cash Flows, continued
For the years ended June 30, 2002 and 2001
(in thousands)

	2002	2001
Reconciliation of operating loss to net cash used by operating activities		
Operating loss	$ (225,048)	$ (187,403)
Adjustments to reconcile operating loss to net cash used by operating activities:		
Depreciation	94,287	79,956
Realized gain from deferred revenue	(1,913)	-
Amortization of deferred charges	145	375
Net effect of changes in:		
Decrease (increase) in other receivables	1,520	(4,363)
Decrease (increase) in materials and supplies	(1,018)	172
Increase in other long term receivables	-	(4,500)
Increase in accounts payable and other liabilities	10,271	9,222
Decrease in self-insurance liabilities	(191)	(2,176)
(Decrease) increase in deferred revenue	(1,436)	4,693
Net cash used by operating activities	$ (123,383)	$ (104,024)

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

1. Description of Reporting Entity and 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 disbursements 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 Government Accounting Standards No. 14, 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, the financial statements of the District (the primary government) include those of the Transit Financing Authority (the Authority).

Basis of accounting and presentation

The District is accounted for as a Business Type Activity, as defined by Governmental Accounting Standards Board (GASB) Statement No. 34, *Basic Financial Statements – Management's Discussion & Analysis – for State and Local Governments* and its financial statements are presented on the accrual basis of accounting. Under this method, revenues are recognized when they are earned, and expenses are recognized when they are incurred.

The District adopted GASB Statement No. 34 as amended by GASB statement No. 37, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments: Omnibus*, as of and for the year ended June 30, 2002, and applied those standards on a retroactive basis. GASB Statement No. 34 establishes standards for external financial reporting for state and local governments and requires that resources be classified for accounting and reporting purposes into three net asset categories; namely, those invested in capital assets, net of related debt, restricted net assets and unrestricted net assets.

The District adopted GASB Statement No. 38, *Certain Financial Statement Note Disclosures* for the year ended June 30, 2002, and applied the standard on a retroactive basis. GASB 38 modifies, establishes, and rescinds certain financial statement disclosure requirements.

The following shows the reconciliation of the components of total equity for June 30, 2001 as previously reported to net asset balances for the same period (in thousands):

Fund equity:	
Contributed capital	$ 2,671,802
Reserved retained earnings - capital grants	278,140
Retained earnings	1,170,974
Total fund equity	$ 4,120,916
Fund net assets:	
Invested in capital assets, net of related debt	$ 3,531,697
Restricted net assets	405,433
Unrestricted net assets	183,786
Total fund net assets	$ 4,120,916

Contributed capital/reserved retained earnings

The District receives grants from the Federal Transit Administration ("FTA") and other agencies of the U.S. Department of Transportation, state, and local transportation funds for the acquisition of transit-related equipment and improvements. Prior to July 1, 2000, capital grants were recognized as donated capital to the extent that project costs under the grant have been incurred. Capital grant funds earned, less amortization equal to accumulated depreciation of the related assets, were included in contributed capital. As required by GASB Statement No. 33, *Accounting and Financial Reporting for Nonexchange Transactions*, effective July 1, 2000 the District changed its method of accounting for capital grants from capital contributions to reserved nonoperating revenues. In accordance with GASB No. 33, capital grants are required to be included in the determination of net income resulting in an increase in net revenue of $235,825,000 and $278,140,000 for the fiscal years 2002 and 2001, respectively.

Under GASB Statement No. 34, contributed capital and reserved retained earnings are presented in the net asset section as invested in capital assets, net of related debt.

Retained earnings

Retained earnings which represented the residual value of operations and capital assets constructed with funds other than grants, were restated to reclassify the capital assets to invested in capital assets, net of related debt and the remaining assets resulting from operations as either restricted or unrestricted net assets.

Proprietary accounting and financial reporting

As required under GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, The District will continue to apply 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 Procedure issued on or before November 30, 1989, unless those pronouncements conflict or contradict GASB pronouncements. The District has elected under GASB Statement No. 20 to not apply all FASB Statements and Interpretations issued after November 30, 1989, due to the governmental nature of the District's operations.

Net assets

Net assets represent the residual interest in the District's assets after liabilities are deducted. In accordance with GASB Statement No. 34, the Fund Equity section on the Statement of Net Assets was combined to report total net assets and present it in three broad components: invested in capital assets, net of related debt; restricted; and unrestricted. 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. All other net assets are unrestricted.

Cash equivalents

The District considers all highly liquid investments with a maturity of three months or less when purchased to be cash equivalents.

Investments

Investments are stated at fair value, which is based on quoted market price. As a matter of policy, the District 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 or by laws or regulations.

Materials and supplies

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

Facilities, property and equipment

Facilities, property and equipment are stated at cost and depreciated using the straight-line method over the estimated useful lives of the assets. Depreciation expense on assets acquired with capital grant funds is transferred to net assets – invested in capital assets, net of related debt after being charged to operations.

Major improvements and betterments to existing facilities and equipment are capitalized. Costs for maintenance and repairs which 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. The amount capitalized is the difference between the interest revenue and interest expense associated with the applicable tax-free borrowings. Net interest in the amount of $7,739,000 and $6,307,000 was capitalized during the years ended June 30, 2002 and 2001, respectively.

Compensated absences

Compensated absences are accrued and reported as a liability in the period earned.

Fare operating revenue

Fare operating revenues are earned as passengers utilize the train service. Deferred revenue includes an estimate of passenger tickets purchased which have not yet been used as well as 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.

Transactions and use tax (sales tax) revenue

The State of California legislation authorizes the District to impose a ½% transaction and use tax within District boundaries which is collected and administered by the State Board of Equalization. Of amounts available for distribution, 75% is paid directly to the District for the purpose of paying operating expenses, except for a portion which is paid directly to the 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. San Francisco, Alameda and Contra Costa Counties assess properties and bill for, collect, and distribute property taxes. Property taxes are recorded as revenue in the fiscal year of levy.

Financial assistance grants

Financial assistance grants are accrued as other revenue in the period to which the grant applies.

Collective bargaining

Approximately 87% of the District's employees are subject to collective bargaining. The current labor contracts expire on June 30, 2005.

Reclassifications

Certain reclassifications have been made to the prior year financial statements to comply with the retroactive application of GASB Statement No. 34.

Use of estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

2. Cash and Investments

The District maintains a cash and investment pool that includes cash and investments restricted due to externally imposed constraints, available for general use and designated by management for specific purposes.

Deposits

The carrying amount of the District's deposits with banks and cash on hand was $99,420,000 and $51,145,000 at June 30, 2002 and 2001, respectively. The corresponding bank balance was $102,169,000 and $56,078,000 at June 30, 2002 and 2001, respectively. Of the bank balance, $1,900,000 and $1,000,000 for 2002 and 2001, respectively, was insured by federal depository insurance or collateralized by securities held by the District's agent in the District's name, and $100,646,000 (2001-$55,175,000) is required by Section 53652 of the California Government Code to be collateralized 110% by the pledging financial institutions. Such collateral is not required to be in the District's name.

Investments

State of California statutes and District policy authorize the District to invest in obligations of the U.S. Treasury, its agencies and instrumentalities, bankers' acceptances, repurchase and reverse repurchase agreements, and the State Treasurer's investment pool.

The District's investments are categorized below to give an indication of the credit risk assumed by the District at June 30, 2002 and 2001. Category 1 includes investments that are insured or registered or for which the securities are held by the District or its agent in the

District's name. Category 2 includes uninsured and unregistered investments for which the securities are held by the broker's or dealer's trust department or agent in the District's name. The District's investment pools are reported at fair value.

(in thousands)

	2002			2001		
	Category 1	Category 2	Fair Value	Category 1	Category 2	Fair Value
Money market	$ -	$ 5,875	$ 5,875	$ -	$ 19,427	$ 19,427
U.S. Treasury securities	31,872	38,760	70,726	-	32,534	32,534
Federal agency obligations	84,685	116,764	202,643	303,247	153,505	457,532
Repurchase agreements	184,864	147,569	332,433	188,756	106,060	294,816
Corporate obligations	-	8,848	9,417			
Total	$ 301,421	$ 317,816	621,094	$ 492,003	$ 311,526	804,309
Cash on hand			2,415			2,248
Time and demand deposits			97,005			48,959
Investment in California local agency investment fund			15,000			15,000
Total			$ 735,514			$ 870,516
Reported as:	Unrestricted	Restricted		Unrestricted	Restricted	
Current assets:						
Cash and cash equivalents	$ 245,677	$ 186,336	$ 432,013	$ 229,396	$ 299,357	$ 528,753
Investments - current	14,662	16,183	30,845	59,863	112,943	172,806
Noncurrent assets:						
Investments	42,210	230,446	272,656	17,451	151,506	168,957
Total	$ 302,549	$ 432,965	$ 735,514	$ 306,710	$ 563,806	$ 870,516

3. Changes in Capital Assets

Facilities, property and equipment at June 30, 2002 and 2001 are summarized as follows (in thousands):

	Lives (Years)	2001	Additions and Transfers	Retirement and Transfers	2002
Non Depreciated Assets					
Land		$ 243,478	$ 2,357	$ -	$ 245,835
Construction-in-progress		1,858,955	536,957	(226,806)	2,169,106
Total Non Depreciated Assets		2,102,433	539,314	(226,806)	2,414,941
Depreciated Assets					
Stations, track, structures and improvements	80	1,891,883	4,492	(8)	1,896,367
Buildings	80	17,877	8,710	-	26,587
System-wide operation and control	20	397,292	22,625	(633)	419,284
Revenue transit vehicles	30	834,735	174,038	-	1,008,773
Service and miscellaneous equipment	3-20	53,390	2,646	(4,431)	51,605
Capitalized construction and start-up costs	30	98,342	(28)	-	98,314
Repairable property items	30	23,472	858	(149)	24,181
Capital lease - revenue transit vehicles	30	53,366	2,227	-	55,593
Total Depreciated Assets		3,370,357	215,568	(5,221)	3,580,704
Less accumulated depreciation and amortization		(1,089,675)	(94,287)	5,346	(1,178,616)
Depreciated Assets net of accumulated depreciation		2,280,682	121,281	125	2,402,088
Total		$ 4,383,115	$ 660,595	$ (226,681)	$ 4,817,029

	Lives (Years)	2000	Additions and Transfers	Retirement and Transfers	2001
Non Depreciated Assets					
Land		$ 242,188	$ 1,290	$ -	$ 243,478
Construction-in-progress		1,574,942	479,317	(195,304)	1,858,955
Total Non Depreciated Assets		1,817,130	480,607	(195,304)	2,102,433
Depreciated Assets					
Stations, track, structures and improvements	80	1,864,259	27,624	-	1,891,883
Buildings	80	16,880	997	-	17,877
System-wide operation and control	20	391,023	7,029	(760)	397,292
Revenue transit vehicles	30	681,131	153,996	(392)	834,735
Service and miscellaneous equipment	3-20	54,373	5,193	(6,176)	53,390
Capitalized construction and start-up costs	30	98,342	-	-	98,342
Repairable property items	30	23,571	207	(306)	23,472
Capital lease - revenue transit vehicles	30	53,366	-	-	53,366
Total Depreciated Assets		3,182,945	195,046	(7,634)	3,370,357
Less accumulated depreciation and amortization		(1,017,240)	(79,956)	7,521	(1,089,675)
Depreciated Assets net of accumulated depreciation		2,165,705	115,090	(113)	2,280,682
Total		$ 3,982,835	$ 595,697	$ (195,417)	$ 4,383,115

The District is currently involved in construction of Phase 1 of an extension program that will add 38 miles of track and 10 new stations to the system at a total cost of approximately $3,264,000,000. The Dublin/Pleasanton, Pittsburg/Bay Point and Colma station extensions are open and in revenue service. Completion of the San Francisco International Airport extension is anticipated first quarter of calendar year 2003. The funding for Phase 1 comes from the federal government ($877,000,000), State of California ($769,000,000), San Mateo County ($503,000,000), Alameda and Contra Costa Counties ($471,000,000), bridge tolls ($155,000,000), San Francisco International Airport ($200,000,000), and the District ($289,000,000).

The District has entered into contracts for the construction of various facilities and equipment totaling approximately $621,184,000 at June 30, 2002, ($843,523,000 in 2001).

4. Risk Management

The District is partially self-insured for workers' compensation, public liability and property damage claims. The self-insured maximum for workers' compensation is $500,000 for any one accident. The self-insured maximum for public liability and property damage is $2,000,000 for any one occurrence. Claims in excess of self-insured retentions are covered up to a total of $248,000,000 by insurance policies.

The self-insurance programs are administered by independent claims adjustment firms. Liabilities are based, in part, upon the independent adjustment firms' estimate of reserves necessary for the settlement of outstanding claims and related administrative costs, and includes estimates of claims that have been incurred but not yet reported. 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, 2002 is believed to be sufficient to cover any costs arising out of claims filed or to be filed for accidents which occurred through that date.

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. These losses include an estimate of claims that have been incurred but not yet reported.

At June 30, 2002 and 2001, the amount of these liabilities was $27,920,000 and $28,110,000, respectively. Changes in the reported liability since the beginning of the respective fiscal year are as follows (in thousands):

	2002	**2001**
Liability at beginning of year	$ 28,110	$ 30,286
Current year claims and changes in estimates	7,128	6,364
Payments of claims	(7,318)	(8,540)
Liability at end of year	$ 27,920	$ 28,110

5. Joint Exercise of Powers Agreements

Transit Financing Authority

The Joint Exercise of Powers Agreement (the "Agreement"), dated August 1, 1991, between the District and Metropolitan Transportation Commission (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 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 and 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.

The Authority had undertaken a commercial paper program to fund a portion of the costs of acquiring and constructing the District's extension project to the San Francisco International Airport (SFO extension project). Under the program, the Authority issued in December 1998, Commercial Paper Notes Series A and Series B, in October 1999, Series C and Series D, and in March 2000, Series E and Series F, with an aggregate principal amount of $300,000,000. In April 2001, notes with a total principal amount of $30,200,000 were retired. In June 2001, the remaining notes with a total principal amount of $269,800,000 were also retired. The monies used to fully pay and retire all the Commercial Paper Notes came from a portion of the proceeds of the FTA Capital Grant Bonds issued by the Association of Bay Area Governments for the sole benefit of the District's San Francisco Airport Extension Project. (See note number 6 – FTA Capital Grant Bonds). As of June 30, 2002 and June 30, 2001, there are no Commercial Paper Notes outstanding.

During the period when the notes were outstanding, to provide liquidity for the program, the District maintained three lines of credit facilities with commercial banks totaling $309,000,000. Drawing under the agreements was restricted to payment of maturing commercial paper notes and related interest. At June 30, 2001, the lines of credits were closed when the Commercial Paper Notes were fully paid and retired.

In order to fund a portion of the costs of SFO extension project, in September 1999, the Authority issued a limited liability note (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, 2002, the notes outstanding amount to $53,355,000 with interest rates ranging from 4.60% to 5.75% and mature from August 2002 through February 2007.

Capitol Corridor Joint Powers Authority

The Joint Exercise of Powers Agreement (the "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 (the "Authority"), a public instrumentality of the State of California. The Authority 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 the Authority and in that capacity shall provide all necessary administrative support to the Authority. The Authority entered into an Interagency Agreement with the State of California and assumed the administration and operation commencing at the service on July 1, 1998. The initial term of the Interagency Agreement was for three years, from July 1, 1998 and was recently extended for three more years effective July 1, 2001, unless extended or terminated.

The governing board of the Authority 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 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 six participants, and any surplus money on hand shall be returned to these participants in proportion to their respective contributions to the Authority.

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 partially funded under the Technology Reinvestment Project managed by the Advanced Research Projects Agency ("ARPA"). The Federal Transit Administration ("FTA") has agreed to manage and oversee the project on behalf of ARPA.

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 Industries was purchased by GE Transportations Systems, and Harmon became known as GE Transportation Systems, Global Signaling.

The District's participation in this project was in the form of in-kind contributions which consist primarily of labor costs and direct costs that are partially reimbursable by the Alliance. As of June 30, 2002 and 2001, the District had provided the Alliance with approximately $12,758,000 in cumulative in-kind contributions and had incurred $20,890,000 and $20,000,000 of direct costs, respectively, $948,000 of which were reimbursed by the Alliance.

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%/69% between the District and AC Transit, respectively. The District supported the project entirely through its own operating funds and did not receive financial assistance from MTC for fiscal years 2002 and 2001.

6. Long-Term Debt

Long-term debt at June 30, 2002 and 2001 is summarized as follows (in thousands):

	2001	Additions/ Accretion	Payments/ Defeasance and Amortization	2002
1990 Sales Tax Revenue Refunding Bonds	$ 63,326	$ 1,720	$ (9,430)	$ 55,616
1991 Sales Tax Revenue Refunding Bonds	7,410	-	(4,945)	2,465
1995 Sales Tax Revenue Refunding Bonds	95,990	-	(42,010)	53,980
1998 Sales Tax Revenue Refunding Bonds	347,690	-	(845)	346,845
1999 Sales Tax Revenue Refunding Bonds	134,945	-	-	134,945
2001 Sales Tax Revenue Refunding Bonds	-	168,650	-	168,650
TFA Bridge Toll Notes	60,345	-	(6,990)	53,355
Construction Loans	93,835	6,990	-	100,825
FTA Capital Grant Bonds	485,350	-	(58,695)	426,655
Lease/leaseback obligation	-	186,616	-	186,616
	1,288,891	363,976	(122,915)	1,529,952
Less Premium/Discounts	(6,935)	(6,636)	1,825	(11,746)
Long-Term Debt Net of Premium/Discounts	1,281,956	$ 357,340	$ (121,090)	1,518,206
Less Current portion of Long-Term Debt	(81,740)			(69,361)
Net long-term debt	$ 1,200,216			$ 1,448,845

	2000	Additions/ Accretion	Payments/ Defeasance and Amortization	2001
1990 Sales Tax Revenue Refunding Bonds	$ 69,905	$ 2,206	$ (8,785)	$ 63,326
1991 Sales Tax Revenue Refunding Bonds	9,500	-	(2,090)	7,410
1995 Sales Tax Revenue Refunding Bonds	99,345	-	(3,355)	95,990
1998 Sales Tax Revenue Refunding Bonds	348,510	-	(820)	347,690
1999 Sales Tax Revenue Refunding Bonds	134,945	-	-	134,945
TFA Bridge Toll Notes	65,680	-	(5,335)	60,345
Construction Loan	86,699	7,136	-	93,835
FTA Capital Grant Bonds	-	485,350	-	485,350
Commercial Paper Notes Payable	300,000	-	(300,000)	-
	1,114,584	494,692	(320,385)	1,288,891
Less Premium/Discounts	(17,218)	9,641	642	(6,935)
Long-Term Debt Net of Premium/Discounts	1,097,366	$ 504,333	$ (319,743)	1,281,956
Less Current portion of Long-Term Debt	(20,385)			(81,740)
Net long-term debt	$ 1,076,981			$ 1,200,216

Bond and note discount, premium and issuance costs are amortized over the life of the related debt.

1990 Sales Tax Revenue Refunding Bonds (the 1990 Bonds)

In July 1990, the District issued sales tax refunding bonds totaling $158,478,000. The 1990 Bonds are special obligations of the District payable from and collateralized by a pledge of the sales tax revenues. At June 30, 2002, the 1990 Bonds consist of $28,775,000 of current interest serial bonds due from 2010 to 2011 with interest rate of 6.75% and $26,841,000 of capital appreciation serial bonds ($12,206,000 original amount) with yields of 6.65% to 6.75% due from 2002 to 2004. Interest on the capital appreciation bonds is payable at maturity. For financial reporting purposes, accrued interest is added to the principal balance.

1991 Sales Tax Revenue Bonds (the 1991 Bonds)

The 1991 Bonds were issued in August 1991 in the amount of $56,010,000 and 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 $2,675,000 principal amount of term bonds due on July 1, 2003. At June 30, 2002, the 1991 Bonds consist of $2,465,000 of serial bonds due on July 1, 2002 with an interest rate of 6.3%. The outstanding bonds are redeemable at the option of the District at 101%.

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 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 2001 Sales Tax Revenue Bonds to defease $18,585,000 of serial bonds due from 2002 to 2010 and $19,915,000 term bonds due from 2012 to 2015. At

June 30, 2002, the 1995 Bonds consist of $23,620,000 serial bonds due from 2002 to 2011 with interest rates ranging from 4.8% to 5.7% and $30,360,000 of term bonds due from 2012 to 2020 with an interest rate of 5.5%. The District is required to make sinking fund payments on the term bonds beginning on July 1, 2012. In addition, the 1995 Bonds maturing after June 30, 2006 will be redeemable after July 1, 2005 at the option of the District at prices ranging from 100% to 101%.

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 obligation 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 bonds are special obligations of the District payable from and collateralized by a pledge of sales tax revenues. At June 30, 2002, the 1998 Bonds consist of $154,475,000 serial bonds due from 2002 to 2018 with interest rates ranging from 3.85% to 5.50%, $79,105,000 of term bond due July 1, 2023 with interest rate of 4.75% and $113,265,000 of term bond due July 1, 2028 with 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 and 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 bonds are special obligations of the District, payable from and collateralized by a pledge of sales tax revenues. At June 30, 2002, the 1999 Bonds consist of $44,930,000 serial bonds due from 2003 to 2019 with interest rates ranging from 4.15% to 5.25% and three 5.5% term bonds in the amounts of $33,210,000, $18,515,000 and $38,290,000 due in 2026, 2029 and 2034, respectively. The District is required to make sinking fund payments on the term bond due July 1, 2026 beginning on July 1, 2020 and on the term bond due July 1, 2029 beginning on July 1, 2027 and on the term bond due July 1, 2034 beginning on July 1, 2030. In addition, the 1999 bonds maturing on or after July 1, 2010 may be redeemed prior to their respective maturities on or after July 1, 2009 and at the option of the District at prices ranging from 100% to 101%.

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 extension of the System to San Francisco International Airport and to refund certain outstanding bonds with principal amounts of $41,175,000 to achieve cash flow savings. At June 30, 2002, the 2001 Bonds consist of $60,675,000 serial bonds due from 2003 to 2021 with interest rates ranging from 4.375% to 5.25%, $27,420,000 of term bond due July 1, 2026 with an interest rate of 5%, $35,205,000 of term bond due July 1, 2031 with an interest rate of 5%, and $45,350,000 of 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.

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 to the extension project at the San Francisco International Airport.

Pursuant to the MOU, the construction loans as of June 30, 2002, consist of funds received for the SFO Extension project costs from SamTrans for $72,000,000 and MTC for $16,500,000 and $12,325,000 from MTC for the SFO Extension project's temporary cash requirements. The District loaned $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 San Francisco International Airport Extension. Such repayments will commence after SamTrans' capital contribution to the BART system for the Warm Springs extension is fully paid from future net operating surplus. MTC's loan for the project's temporary cash requirements will be repaid from the last federal grant allocations to the SFO Extension project as covered by a Federal Full Funding Grant Agreement.

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 San Francisco International Airport 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. At June 30, 2002, the bonds outstanding amount to $426,655,000, with interest rates ranging from 3.3% to 5.0% with maturities from June 15, 2003 to June 15, 2009.

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 "headlease") and simultaneously sublease the Network back through January 2, 2012 (the "sublease"). At the expiration of the sublease term the District has the option to purchase back the remaining headlease interest.

At closing, the Network had a fair market value of approximately $206 million and a book value of $203 million. Under the terms of the headlease, the District received a prepayment equivalent to the net present value of the headlease obligation totaling approximately $206 million, of which the District paid approximately $146 million 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 headlease interest, if it chooses to do so. Of the remaining headlease proceeds, approximately $37 million 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 headlease interest, if it chooses to do so. The District received cash from the lease/leaseback transaction amounting to approximately $23 million. This 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, the District has recorded the payment to the Payment Undertaker as a receivable 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 is as follows (in thousands):

Debt at the closing	$ 182,958
Interest accrued in 2002	3,658
	186,616
Lease payments due in one year	(5,531)
Net long-term debt at June 30, 2002	$ 181,085

Defeased Bonds

In March 1998, the District defeased several bonds amounting to $155,115,000 by placing part of the proceeds of the 1998 Sales Tax Revenue Bonds in an irrevocable trust to provide for future debt service payments on these bonds. The advance refunding met the requirement of an in substance debt defeasance, and the term bonds were removed from the District's long-term debt. Accordingly, the Trust account assets and liabilities for the defeased bonds are not included in the District's financial statements. As a result of the advance refunding, the District reduced its total debt service requirement by $16,644,000 which resulted in an economic gain (the difference between the present value of the debt service payments on the old and new debt) of $10,721,000.

In July 2001, the District defeased a portion of 1991 and 1995 Sales Tax Revenue Bonds amounting to $41,175,000 by placing part of the proceeds of the 2001 Sales Tax Revenue Bonds in an irrevocable trust to provide for future debt service payments on these bonds. The advance refunding met the requirement of an in substance debt defeasance, and the defeased bonds were removed from the District's long-term debt. Accordingly, the Trust account assets and liabilities for the defeased bonds are not included in the District's financial statements. The advance refunding were made to achieve budgetary savings by extending debt service requirements further into the future and to take advantage of lower interest rates.

The District deferred interest expenses of $9,143,000 related to the defeasance from the proceeds of the 1998 and 2001 Sales Tax Revenue Bonds. These deferred charges are amortized over the life of the defeased bonds. Amortization expense on these deferred charges was $742,000 and $1,337,000 for fiscal years 2002 and 2001, respectively.

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 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, 2002, the District has arbitrage liabilities related to the 1998 Bonds in the amount of $852,000, the 1999 Bonds in the amount of $716,000, TFA Bridge Toll Notes amounting to $689,000, and the San Mateo County Transit District's construction loan in the amount of $306,000. The arbitrage liabilities are payable no later than 60 days after the end of the Fifth Bond/Note Year which is March 12, 2003 for the 1998 Bonds, October 7, 2004 for the 1999 Bonds, September 1, 2004 for the TFA Bridge Toll Notes, and June 1, 2004 for the San Mateo County Transit District's construction loan.

Debt Repayments

The following is a schedule of long-term debt principal payments required as of June 30, 2002 (in thousands):

	1990 Bonds	1991 Bonds	1995 Bonds	1998 Bonds	1999 Bonds	2001 Bonds	TFA Bridge Toll Notes	Construction Loans	FTA Capital Grant Bonds	Lease/ Leaseback Obligation	Total
Year ending June 30:											
2003	$ 9,485	$ 2,465	$ 2,060	$ 880	$ -	$ -	$ 7,320	$ -	$ 41,620	$ 5,531	$ 69,361
2004	9,550	-	2,120	915	1,785	2,685	7,680	-	58,495	17,212	100,442
2005	9,615	-	2,210	3,860	1,860	-	8,075	12,325	61,295	6,716	105,956
2006	-	-	2,315	13,775	1,940	-	8,495	-	64,210	51,473	142,208
2007	-	-	2,435	14,675	2,025	-	21,785	-	46,330	39,362	126,612
2008-2012	26,966	-	12,480	62,860	11,615	-	-	-	154,705	54,684	323,310
2013-2017	-	-	11,095	36,675	14,820	36,650	-	-	-	4,054	103,294
2018-2022	-	-	19,265	61,690	19,140	21,340	-	-	-	163,485	284,920
2023-2027	-	-	-	102,870	24,955	27,420	-	-	-	-	155,245
2028-2032	-	-	-	48,645	32,615	35,205	-	-	-	-	116,465
2033-2037	-	-	-	-	24,190	45,350	-	-	-	-	69,540
Thereafter	-	-	-	-	-	-	-	88,500	-	-	88,500
	$ 55,616	$ 2,465	$ 53,980	$ 346,845	$ 134,945	$ 168,650	$ 53,355	$ 100,825	$ 426,655	$ 342,517	1,685,853
Less:											
Unamortized bond premium											13,467
Unamortized bond discount and issuance cost											(25,213)
Future imputed interest on lease/leaseback											(155,901)
Current portion of long-term debt											(69,361)
Net long-term debt portion											$ 1,448,845

7. Federal Grants

The U.S. Department of Transportation provides financial assistance to the District for capital projects, planning and technical assistance. Grants which were active during the year ended June 30, 2002 are summarized as follows (in thousands):

	San Francisco International Airport Extension Project	Other Capital Projects
Total approved project costs	$ 1,347,230	$ 546,386
Total approved federal funds	$ 373,368	$ 444,412
Less cumulative amounts earned	715,008	357,734
Amounts below (in excess of) approved federal funds	$ (341,640)	$ 86,678

The San Francisco International Airport Extension Project is covered by a Federal Full Funding Grant Agreement 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.

8. Local and State Financial Assistance

The District receives local operating and capital assistance from Transportation Development Act Funds ("TDA"). For the year ended June 30, 2002, TDA operating assistance was $877,000

($529,000 in 2001). These funds were received from the county of Alameda. There was no TDA capital assistance received in fiscal years 2002 and 2001.

The District receives state operating and capital assistance from State Transit Assistance Funds ("STA"). For the year ended June 30, 2002, STA assistance was $376,000, all of which was used for operating assistance. 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 did not receive any STA assistance for the year ended June 30, 2001.

9. Employees' Retirement Plan

Plan Description

All employees are eligible to participate in the Public Employees' Retirement Fund (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 2,504 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 ordinance.

All investments are reported at fair value. The fair value of investments in securities is generally based on published market prices and quotations from major investment firms. Many factors are considered in arriving at fair value. In general, however, corporate bonds are valued based on yields currently available on comparable securities of issuers with similar credit ratings. Investments in certain restricted common stocks are valued at the quoted market price of the issuer's unrestricted common stock less an appropriate discount. Investments held in internal investment pools have been reported at fair value.

Mortgages are valued on the basis of their future principal and interest payments discounted at prevailing interest rates for similar instruments. The fair value of real estate investments, principally rental property subject to long-term net leases, are estimated based on independent appraisals. Short-term investments are reported at fair value, when available, or at cost plus accrued interest, which approximates market value when market values are not available. For investments where no readily ascertainable market value exists, management in consultation with their investment advisors has determined the fair values for the individual investments.

Each plan issues a publicly available financial report that includes financial statements and required supplementary information for that plan. Those reports may be obtained by writing or calling the Plan: California PERS, P.O. Box 942709, Sacramento, CA 94229-2709, (916) 326-3420.

Funding Policy

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 ordinance. The individual entry age normal method is used to determine the normal cost, and 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. District contributions for the year ended June 30, 2002 to cover normal cost and to amortize the unfunded actuarial accrued surplus approximated 7.051% (6.617% in 2001) and 13.557% (14.534% in 2001) of covered payroll for the Miscellaneous Plan and the Safety Plan, respectively.

The District was not required to make contributions to the Fund for covered employees for the fiscal year 2002 due to a surplus of the District's portion of the Fund's net assets over the District's pension benefit obligation caused by a change in 1988 in the actuarial valuation method and an actual rate of return on investment assets that exceeded the assumed rate.

The District's covered payroll for employees participating in the Fund for the years ended June 30, 2002 and 2001 was $210,200,000 and $191,080,000, respectively. The District's 2002 and 2001 payroll for all employees was $229,032,000 and $213,216,000, respectively. The District, due to a Collective Bargaining Agreement, also reimburses the employees for their contributions, which are 9% for public safety personnel and 7% for miscellaneous covered employees. Effective October 1, 2001, due to the 2001 Collective Bargaining Agreements and because of the superfunded status of the Fund, all employees, except sworn police officers, were not required to make contributions to the Fund.

Since the District has made the actuarially-determined required contributions since 1988, the pension liability or asset was zero at June 30, 2002, in accordance with GASB Statement No. 27, *Accounting for Pensions by State and Local Governmental Employers*.

Funding Status and Annual Pension Cost

Three-Year Trend Information for the Fund (in thousands):

	Fiscal Year Ending	Annual Pension Cost (APC)	Percentage of APC Contributed	Net Pension Obligation
Miscellaneous Plan:	June 30, 2000	$ 10,920	100%	$ -
	June 30, 2001	$ 11,370	100%	$ -
	June 30, 2002	$ 12,203	100%	$ -
Safety Plan:	June 30, 2000	$ 1,331	100%	$ -
	June 30, 2001	$ 1,692	100%	$ -
	June 30, 2002	$ 1,803	100%	$ -

The required contribution was determined as part of an actuarial valuation performed as of June 30, 2001, the latest available for the Fund. The significant actuarial assumptions used in the 2001 valuation to compute the pension benefit obligation were an assumed rate of return on investment assets of 8.25%, annual payroll increases of 3.50% attributable to inflation, 3.75% attributable to real salary increases, and merit increases that vary by length of service, and no postretirement benefit increases.

The funding status applicable to the District's employee group at June 30, 2001 (the latest available for the Fund) is summarized as follows:

Funded Status of the Miscellaneous Plan (in thousands):

Valuation Date	Entry Age Normal Accrued Liability	Actuarial Value of Assets	Unfunded Liability (Excess Assets)	Funded Status	Annual Covered Payroll	UAAL as a Percentage of Payroll
6/30/99	$ 587,709	$ 846,793	$ (259,084)	144.1%	$ 164,247	(157.741)%
6/30/00	$ 655,888	$ 947,519	$ (291,631)	144.5%	$ 172,132	(169.423)%
6/30/01	$ 722,298	$ 991,464	$ (269,166)	137.3%	$ 184,513	(149.970)%

Funded Status of the Safety Plan (in thousands):

Valuation Date	Entry Age Normal Accrued Liability	Actuarial Value of Assets	Unfunded Liability (Excess Assets)	Funded Status	Annual Covered Payroll	UAAL as a Percentage of Payroll
6/30/99	$ 56,354	$ 71,453	$ (15,099)	126.8%	$ 11,211	(134.682)%
6/30/00	$ 65,225	$ 79,636	$ (14,411)	122.1%	$ 11,826	(121.868)%
6/30/01	$ 70,958	$ 83,306	$ (12,348)	117.4%	$ 12,385	(99.700)%

Postretirement Health Care Cost

In addition to the retirement benefits described above, as specified in the District's ordinance, the District provides postretirement health care benefits assistance to all employees who retire directly from the District or to their surviving spouses. Substantially all of the District's employees may become eligible for those benefits if they reach age 50 with 5 years of service with the District. Currently, 711 retirees (614 in 2001) are provided this benefit. The District paid up to $264,000 and $155,000 per month for health insurance premiums for the retirees and surviving spouses during fiscal years 2002 and 2001, respectively. These benefits are fully funded by the District and accounted for on a pay-as-you-go basis through payments to the Plan. Cash reimbursements of these benefits totaled $2,468,000 in 2002 ($1,566,000 in 2001).

10. Deferred Compensation Plan

The District offers its employees a deferred compensation plan created in accordance with Internal Revenue Code ("IRC") Section 457. The deferred compensation plan, available to all officers and employees, permits them to defer receipt of a portion of their salary until future years. The deferred compensation is not available to employees until retirement, termination, or certain other covered events.

On January 1, 1997, the District amended the Plan to conform to the Federal Small Business Protection Act of 1996 ("SBPA"). The amendment provided for the creation of a trust for the deferred compensation plan and all income attributable to those amounts. The funds are not subject to the claims of the District's general creditors. The Plan is no longer considered part of the District's assets.

11. Money Purchase Pension Plan

Most District employees participate in the Money Purchase Pension Plan, which is a supplemental retirement program. 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, on a pay-as-you-go basis, an amount equal to 6.65% of covered employee's annual compensation (up to $29,700 after deducting the first $133 paid during each month) up to a maximum annual contribution of $1,868. Non-represented employees receive an additional 1.627% of annual regular earnings up to $160,000. Additionally, effective October 1, 2001, all covered employees, except sworn police officers, receive 3.5% of their wages subject to certain funding thresholds in the CalPers Retirement Plan. 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 year ended June 30, 2002 and 2001 were $7,253,000 and $7,282,000, respectively. Money Purchase Pension Plan assets at June 30, 2002 and 2001 (excluded from the accompanying financial statements) were $221,360,000 and $226,645,000, respectively. At June 30, 2002, there were approximately 177 participants receiving benefits under this plan.

12. Board of Directors' Expenses

In May 2000, the annual reporting for the Board of Directors' travel and other business related expenses (Directors' expenses) was changed from a calendar to a fiscal year cycle. The total Directors' expenses for the fiscal years 2002 and 2001 amount to $32,000 and $31,000, respectively.

13. 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 20 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, 2002 are as follows (in thousands):

	Operating Leases
2003	$ 3,930
2004	678
2005	232
2006	216
2007	119
Thereafter	700
Total minimum payments	$ 5,875

Rent expense under all operating leases was $4,307,000 and $3,260,000 for the years ended June 30, 2002 and 2001, respectively.

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 $2,000,000 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, 2002 and 2001, the balances of the deferred gain were $1,272,000 and $1,327,000, respectively, and the balances of the receivable as well as the liability were $26,812,000 and $29,967,000, respectively. Other than the cash received upon the sale, no cash will be exchanged between the parties in settlement of the receivable and liability.

Accumulated depreciation related to the C-2 rail cars covered by the sale/leaseback agreement totaled $13,114,000 and $10,804,000 as of June 30, 2002 and 2001.