



***Central Puget Sound
Regional Transit Authority***

***Financial Statements for the
Years Ended December 31, 2008 and
2007 Independent Auditors' Report***

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STATEMENT OF MANAGEMENT'S RESPONSIBILITY

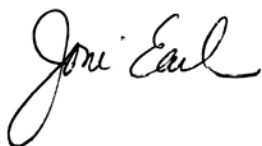
The financial statements of the Central Puget Sound Regional Transit Authority (Sound Transit) have been prepared from the Agency's accounting system in accordance with generally accepted accounting principles. The integrity and objectivity of information in Sound Transit's financial statements, including estimates and judgments, are the responsibility of management.

Sound Transit maintains a system of internal accounting controls designed to provide reasonable assurance as to the integrity and reliability of financial reporting, the safeguarding of assets and the prevention and detection of material errors or fraudulent financial reporting. Monitoring of such systems includes management's responsibility to objectively assess the effectiveness of internal accounting controls and recommend improvements therein.

Limitations exist in any system of internal accounting controls in which the cost of the system being implemented should not exceed the benefits derived. Sound Transit believes that the organization's system does provide reasonable assurance that transactions are executed in accordance with management's general or specific authorizations and is adequate to accomplish the stated objectives.

The independent auditors, whose report is included herein, were engaged to express an opinion on our 2008 financial statements. Their opinion is based on procedures performed in accordance with generally accepted auditing standards, including 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.

In an attempt to assure objectivity, the financial information contained in this report is subject to review by the Board of Directors.



Joni Earl
Chief Executive Officer



Brian McCartan
Chief Financial Officer



Kelly A. Priestley
Controller

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MANAGEMENT'S DISCUSSION AND ANALYSIS

For the years ended December 31, 2008 and 2007

Management's Discussion and Analysis ("MD&A") presents a narrative overview and analysis of the financial activities of the Agency for the years ended December 31, 2008 and 2007. The MD&A is designed to assist readers of financial statements in focusing on significant financial activities and issues and to identify any significant changes. As this information is presented in summary form, it should be read in conjunction with the financial statements and footnotes as a whole.

Central Puget Sound Regional Transit Authority, a public corporation acting under the service name of Sound Transit, is a regional transit authority implementing and providing a high-capacity transportation system throughout parts of King, Pierce and Snohomish counties through commuter rail ("Sounder"), light rail ("Link") and a regional express bus system ("ST Express"). The implementation of the initial phase of the voter-approved regional mass transit system ("*Sound Move*") is scheduled for a 20-year period, ending in 2016. In November, 2008 the voters approved a second phase of expansion of the mass transit system, a 15-year program called ST2. ST2 includes initial investments commencing in 2009 with regional express buses and more commuter trains, as well as mid to longer-term expansion of regional light rail and parking facilities through 2023.

Sound Transit's financial statements have reflected a growth in operating revenues and expenses each year, as well as growth in capital projects in progress and property, vehicles and equipment. The Agency has not reached its full service levels and is in the construction phase on its initial light rail project, with major sources of revenue exceeding expenses resulting in a rising net asset position.

Financial Highlights

- Total operating revenues were \$30.6 million for 2008, an increase of 16.3% from the prior year. Passenger fares increased by \$4.6 million from the prior year with continued large ridership gains on Sounder and ST Express.
- Loss from operations was \$143.6 million for 2008, an increase of 14.5% from the prior year. Operations and maintenance expenses increased by 17.8% reflecting the increased service levels, as well as unit cost increases in the price of fuel and labor and higher maintenance costs. General and administrative expenses, after allocations to capital projects and operations and maintenance, increased by 11.8%, reflecting increased costs in support of facilities, fleet, safety, technology and tax collection.
- Non-operating revenues net of expenses were \$337.5 million, a 4.3% reduction from prior year. Tax revenues decreased by 5.3% as the regional economy slowed in 2008. Interest revenues and non-operating expenses remained comparable to prior year, while other revenues increased by \$7.7 million reflecting the recovery from the State of prior year-impaired costs on the Totem Lake Freeway Station project and recovery of costs through its insurance program for Mercer Island Parking Garage.
- Federal, state and local contributions to Sound Transit of \$175.6 million increased by 49.7 % from the prior year while completed projects transferred to other governments of \$67.8 million decreased by 41.3 %. These changes reflect higher grant and local funds received in the current year, including the new full funding agreement for University Link, Airport Link and Tacoma-to-Lakewood commuter rail.
- Total net assets at December 31, 2008, were \$3.2 billion, an increase of \$301.7 million or 10.5% from 2007. This change was up from 2007, during which net assets increased by \$229 million or 8.7%, which reflected a greater number of projects that were completed and transferred to other governments in the prior year.

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Management's Discussion and Analysis, continued

- Total capital assets, net of accumulated depreciation, were \$3.9 billion at December 31, 2008, an increase of \$466.1 million or 13.5% from 2007. The increase in total capital assets reflects progress on the Central and Airport Link light rail projects, which go into operation in 2009, new activity on the University Link project and related land acquisitions for light rail extension to the University and north, as well as Sounder Commuter rail to Lakewood and several station projects. In 2008, \$168.8 million in expenditures related to completed projects or land acquisitions was transferred to property, vehicles and equipment.

Overview of the Financial Statements

Sound Transit's financial statements are prepared in conformity with United States generally accepted accounting principles ("GAAP") as applied to government units. The 2008 and 2007 financial statements are presented using the economic resource measurement focus and accrual basis of accounting. As Sound Transit comprises a single proprietary fund, no fund level financial statements are shown.

In accordance with GAAP, all revenues are recognized in the period in which they are earned and expenses are recognized in the period in which they are incurred. All assets and liabilities associated with the operation of Sound Transit are included in the Balance Sheets, and depreciation of capital assets is recognized in the Statements of Revenues, Expenses and Changes in Net Assets.

The financial statements provide both long-term and short-term information about Sound Transit's overall financial status as well as Sound Transit's net assets, segregated by invested in capital assets (net of related debt), restricted and unrestricted. Net assets are the difference between Sound Transit's assets and liabilities and over time may serve as a useful indicator of Sound Transit's financial position. The financial statements also include notes that provide additional information that is essential to a full understanding of the information provided.

Financial Analysis

Net Assets

Sound Transit's total net assets at December 31, 2008, were \$3.2 billion, an increase of \$301.7 million or 10.5% from 2007 (see Table A-1). Total assets increased \$272.0 million or 6.2% and total liabilities decreased by \$29.7 million or 2.0%. Assets and liabilities were comparable to prior year as no bonds were issued in 2008 with the balance of the increase in total assets substantially attributable to capital-spending activity. This compares to total net assets of \$2.9 billion at December 31, 2007.

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Management's Discussion and Analysis, continued

Table A-1

Sound Transit Net Assets					
<i>(in millions)</i>					
	As of December 31			% Change	
	2008	2007*	2006*	2008-2007	2007-2006
Current assets, excluding restricted assets	\$ 526.0	\$ 730.3	\$ 587.1	(28.0)	24.4
Restricted assets	124.0	120.2	142.1	3.2	(15.4)
Capital assets	3,917.4	3,451.3	2,868.7	13.5	20.3
Other non-current assets	77.1	70.7	67.9	9.1	4.1
Total Assets	4,644.5	4,372.5	3,665.8	6.2	19.3
Current liabilities, excluding interest payable from restricted assets	174.6	190.6	162.9	(8.4)	17.0
Interest payable from restricted assets	14.0	11.2	10.5	24.4	7.0
Long-term debt	1,204.1	1,226.3	779.8	(1.8)	57.3
Other long-term liabilities	73.8	68.1	65.3	8.4	4.2
Total Liabilities	1,466.5	1,496.2	1,018.5	(2.0)	46.9
Net Assets					
Invested in capital assets, net of related debt	2,701.4	2,216.8	2,085.8	21.9	6.3
Restricted net assets	110.0	109.0	131.6	1.0	(17.2)
Unrestricted net assets	366.6	550.5	429.9	(33.4)	28.1
Total Net Assets	\$ 3,178.0	\$ 2,876.3	\$ 2,647.3	10.5	8.6

* Restated—see *New Accounting Pronouncement*, Note 2

Current assets, excluding restricted assets, decreased in 2008 by 28.0% from 2007. This decrease was due to lower cash and cash equivalent balances on hand, as the agency funded its construction activity. Current assets, excluding restricted assets, increased in 2007 by 24.4% due to higher cash and cash equivalent balances on hand with the receipt of bond proceeds in December 2007, which were considered fully spent on issuance.

Restricted assets were comparable to 2007, however decreased by 15.4% from 2006 as payments were made out of funds restricted under contractual agreement with BNSF for improvements required in the Seattle-to-Tacoma Sounder corridor.

Capital assets increased in 2008 by 13.5% from 2007. Of that, construction in progress increased by \$336.7 million, primarily on the Link light rail projects, the first segments of which are scheduled to go into service in July 2009. In 2008, Sound Transit capitalized \$576.4 million (\$737.6 million in 2007) in design, construction, acquisition, interest and general and administrative costs allocated to capital projects in progress. The Central Link and Airport Link light rail projects are approaching completion of construction, representing \$325.1 million of amounts capitalized in 2008 or 56.4% of total capital spending. Significant activity is also starting to occur on the final Sound Move Link segments, University and North Link with \$114.7 million or 19.9% of total capital spending, bringing total capital spending in 2008 on light rail to \$439.8 million or 76.3% (\$552.4 million in 2007 or 74.9%).

Capital spending on Sounder and ST Express projects as a percentage of total capital spending was 10.4% and 5.8% respectively (13.9% and 10.6% in 2007). Transfers out of capital projects in progress were \$247.3 million (\$302.6 million in 2007) as projects were completed and transferred to property, vehicles and equipment or expensed as follows:

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Management's Discussion and Analysis, continued

(in millions)

	2008	2007
Transferred to property, vehicles and equipment	\$ 168.8	\$ 183.6
Expensed to contributions to other governments	67.6	114.4
Transferred to inventory and prepaid expense	0.7	
Link start-up expenditures	5.4	4.0
Write-off of overhead, discontinued and impaired project costs and loss on disposal of assets	4.8	0.6
	<u>\$ 247.3</u>	<u>\$ 302.6</u>

In 2008, \$4.8 million of costs were written off, substantially all of which related to the Star Lake Freeway Station, a component of a larger state project. The state project was determined to be no longer economically viable and the station project was discontinued. In 2007, write-offs included \$211 thousand related to the Meadowdale dock mitigation project in Shoreline that was not pursued, and \$349 thousand in overhead costs were written off.

Direct additions to property, vehicles or equipment in 2008 were \$1.1 million, including data warehousing, eDiscovery and the ERP systems procurement module. In 2007 direct additions were \$4.7 million, which included the acquisition of seven new 45' diesel buses operated by Pierce Transit.

Offsetting the increase in capital spending were disposals and transfers of \$2.4 million, the most significant of which was a transfer property in the Rainer Valley to land held for resale as well as disposals of 27 Orion buses and various computer and office equipment, which were at the end of their useful life and substantially depreciated. Depreciation increased in 2008 to \$38.2 million. In 2007, disposal and transfers were \$4.6 million, which included land held for resale of \$3.9 million and \$263 thousand related to the replacement of the back office system for the ticket vending machines and depreciation, increased by \$35.1 million.

Current liabilities, in 2008, excluding interest payable from restricted assets, decreased by 8.4% as lower amounts were payable at year-end as the initial segment construction approaches completion. The current portion of principal due in 2009 on the 1999 and 2007A bond issues was comparable to the prior year. Interest payable at year-end increased by \$2.7 million, as the 2007A bonds were outstanding for the full year in 2008. Current liabilities, in 2007, excluding interest payable from restricted assets, increased by 17.0% as higher amounts were payable at year-end for the Beacon Hill tunnel and Link vehicle contracts, the construction claim provision was increased and the current portion of long-term debt increased as amounts for principal due in 2008 for the 2007A Bonds.

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Management's Discussion and Analysis, continued

The following table presents the net asset components and their relative percentage to total net assets:

Net Assets <i>(in millions)</i>	As of December 31			% Total Net Assets		
	2008	2007	2006	2008	2007	2006
Invested in capital assets, net of related debt	\$ 2,701.4	\$ 2,216.8	\$ 2,085.8	85.0	77.1	78.8
Restricted net assets	110.0	109.0	131.6	3.5	3.8	5.0
Unrestricted net assets	366.6	550.5	429.9	11.5	19.1	16.2
Total Net Assets	\$ 3,178.0	\$ 2,876.3	\$ 2,647.3	100.0	100.0	100.0

In 2008, the change in the components of Sound Transit's net assets, which represent the cumulative effect of the excess of revenues over expenses, together with the impact of the agency's financing and asset management decisions, reflected the agency's progress on its Sound Move capital program. Unrestricted net assets decreased by 33.4% while invested in capital assets increased by 21.9%. Invested in capital assets reflects investment in property, construction in progress and depreciable net assets used in its operations, while restricted net assets are assets restricted for use by the agency for a specific purpose and unrestricted net assets are the remainder of net assets not invested in capital nor restricted for a specific purpose.

Changes in Net Assets

Changes in net assets reflect the excess of revenue over expenditures for a year. In 2008, the excess of revenues over expenses was \$301.7 million, while in 2007 it was \$229.0 million (see Table A-2). The lower net revenues in 2007 reflect the completion of several significant projects, which were transferred to other local governments or the State, and substantially offset capital contributions received from Federal grants and other funding from state and local agencies.

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Management's Discussion and Analysis, continued

The agency's statement of revenue, expenses and changes in net assets is summarized in the table below:

Table A-2

Changes in Sound Transit Net Assets <i>(in millions)</i>	For the Year Ended December 31			% Change	
	2008	2007	2006	2008-2007	2007-2006
Operating Revenues					
Passenger fares	\$ 26.6	\$ 22.0	\$ 18.1	20.8	22.0
Other	3.9	4.2	3.4	(6.9)	23.4
Total Operating Revenues	30.5	26.2	21.5	16.3	22.3
Operating Expenses					
Total operating expenses, before depreciation and loss on disposal of assets	135.8	116.2	107.6	16.9	8.0
Depreciation and loss on disposal of assets	38.3	35.4	33.5	7.9	6.0
Total operating expenses	174.1	151.6	141.1	14.8	7.5
Loss from operations	(143.6)	(125.4)	(119.6)	14.5	4.8
Non-operating revenues, net of expenses	337.5	352.6	350.4	(4.3)	0.6
Income before capital contributions	193.9	227.2	230.8	(14.6)	(1.5)
Capital contributions	107.8	1.8	71.8	5,953.1	(97.5)
Change in Net Assets	301.7	229.0	302.6	31.8	(24.3)
Total net assets, beginning	2,876.3	2,647.3	2,344.7	8.6	12.9
Total Net Assets, ending	\$ 3,178.0	\$ 2,876.3	\$ 2,647.3	10.5	8.7

Operating Revenues

Operating revenues are composed of passenger fares and other revenue related to operations.

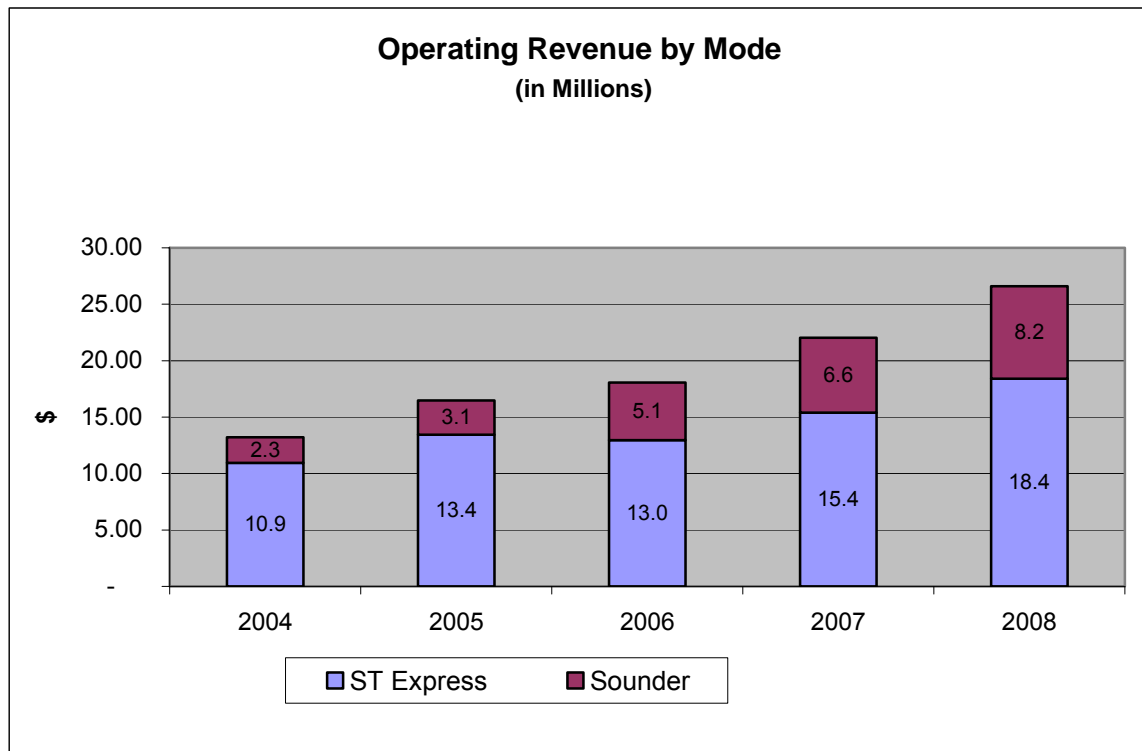
Passenger Fare Revenue

Passenger fare revenue consists of fares earned from the sale of Puget Passes, Sounder tickets and bus farebox receipts from riders on Sounder and ST Express during the year. The agency experienced overall growth in passenger fares revenue of 20.8%, passenger boardings of 17.1% and its average fare per boarding (AFB) of 3.2%.

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Management's Discussion and Analysis, continued

The following chart displays revenue by mode from 2004 to 2008:



Sounder rail passenger revenue increased \$1.6 million or 23.8% in 2008, compared to \$1.5 million or 29.6% in 2007 as ridership continues to grow. The ridership increase in 2008 and 2007 reflects both higher per train ridership and additional round-trip service, the effect of which was an increase in boardings of 23.7% in 2008 and 27.4% in 2007. On the South line, round-trip service was added between Auburn-to-Seattle for the month of August 2007 and between Tacoma-to-Seattle in September 2008 and 2007, as well as reverse commute trips in September 2008 and 2007. On the North line, an additional round trip was added between Everett-to-Seattle in each of September 2008 and 2007.

The average fare per boarding on Sounder in 2008 and 2007 was \$3.07, an increase of \$0.05 from 2006. In June 2007, the agency restructured its fare system to distance based-fares together with a fare increase.

ST Express bus passenger revenue increased by \$3.0 million or 19.5% in 2008 and by \$2.4 million or 19.0% in 2007. The increase in 2008 was driven primarily by growing ridership as well as a slight increase in the average fare per boarding. Ridership on ST Express throughout the system was favorably impacted in both 2008 and 2007, increasing by 1.8 million boardings or 17.2 % in 2008 and 1.0 million boardings or 10.5% in 2007. The rising cost of fuel and increased congestion in the region, continues to make public transportation a more attractive alternative. In addition, service route enhancements were implemented on the Redmond – Seattle route in 2008 and on the Issaquah – Seattle and Lakewood – Seattle routes in 2007. In 2008 and 2007, service hours increased by approximately 2.3% and 4.5%, respectively.

The average fare per boarding on ST Express in 2008 at \$1.47, increased by \$0.03 or 2.0% over 2007; and by \$0.10 or 7.8% in 2007. The last fare increase for ST Express was in 2005 when fare prices were increased by \$0.25, effective in June of that year.

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Management's Discussion and Analysis, continued

Ridership on Tacoma Link, a free fare service, was comparable between 2008 and 2007 and increased slightly from 2006.

Ridership numbers by year and mode of transportation are as follows:

Ridership <i>(in thousands)</i>	% Increase				
	2008	2007	2006	2008-2007	2007-2006
Sounder	2,668.6	2,156.7	1,693.0	23.7	27.4
Link	919.1	919.0	885.6	0.0	3.8
ST Express	12,528.8	10,689.0	9,677.6	17.2	10.5
Total	16,116.5	13,764.7	12,256.2	17.1	12.3

Other Operating Revenues

Other operating revenues consist of vehicle advertising, rental of equipment and facilities and other miscellaneous revenue. Other revenues of \$3.9 million were comparable to prior years.

Operating Expenses

Operating expenses are comprised of operations and maintenance costs, general and administrative expenses and depreciation.

Operations and Maintenance

Operations and maintenance expenses for all transit modes, increased in 2008 by \$17.6 million or 17.8% and by \$10.0 million or 11.2% in 2007. Major expense categories are services, materials, supplies, utilities, insurance, taxes, and purchased transportation, allocated overhead from staff divisions and operating leases and rentals. Purchased transportation represents amounts paid to BNSF, Community Transit, King County Department of Transportation and Pierce Transit who operate Sound Transit's commuter rail and express bus service, accounting for 67% of this category, 70% in 2007. Services are the next largest expenditure in this category and include the Sounder vehicle maintenance contracted to Amtrak and various contracts for facilities maintenance at Sound Transit-owned and shared facilities.

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Management's Discussion and Analysis, continued

Operations and maintenance costs by mode are as follows:

Operations and Maintenance

<i>(in millions)</i>	% Increase				
	2008	2007	2006	2008-2007	2007-2006
Souder	\$ 31.2	\$ 24.8	\$ 22.7	25.9	9.5
Link	3.2	3.2	2.9	1.4	8.6
ST Express	82.3	71.1	63.5	15.7	11.9
Total	\$ 116.7	\$ 99.1	\$ 89.1	17.8	11.2

The operating and maintenance cost increase on Souder was 25.9% in 2008 and 9.5% in 2007 and on ST Express was 15.7% in 2008 and 11.9% in 2007. These increases reflect the service increases and corridor improvements previously described which on Souder equated to a 43.0% increase in trips in 2008 and a 14.6% increase in 2007 and on ST Express a 2.3% increase in hours in 2008 and a 4.5% increase in 2007. Rising fuel costs also contributed to increased costs in both years, as well as higher maintenance costs on ST Express as the fleet ages.

General and Administrative

General and administrative expenses are comprised of Agency staff and administrative costs not allocated to operations and maintenance or to capital projects. Major expense categories include wages, benefits, services, materials, supplies, utilities, insurance, taxes, miscellaneous, lease and rental expenses. In 2008, net general and administrative expenses increased by \$2.0 million or 11.8%, while in 2007, they decreased by \$1.4 million or 7.6%.

General and Administration

<i>(in millions)</i>	% Increase				
	2008	2007	2006	2008-2007	2007-2006
Total General and Administrative					
cost before allocations	\$ 52.6	\$ 48.6	\$ 46.0	8.2	5.7
Allocations to Operations	(7.5)	(6.9)	(6.5)	9.0	5.8
Allocations to Capital Projects	(26.8)	(25.0)	(23.4)	7.3	7.0
Project overhead written off	0.8	0.4	2.4	127.6	(85.1)
Net General and Administrative	\$ 19.1	\$ 17.1	\$ 18.5	11.8	(7.6)

Before allocation to capital projects and operations, total agency staff and administrative costs increased by \$4.0 million or 8.2%, primarily in the salary and benefits, services, materials and supplies. Salary and benefit costs represent 75% of the increase, reflecting higher staffing levels in safety, diversity and finance and information technology, as the agency ramps up to support operations, Smart Card fare collection ("ORCA") and Link systems. Also increasing in 2008 were non-revenue vehicle fleet insurance costs and the cost to collect the agency's Motor Vehicle Excise Tax ("MVET"). Total general and administrative expenses in 2007 increased by \$2.6 million or 5.7%, primarily in the salary and benefits, services, materials and supplies.

General and administrative costs allocated to capital projects and transit operations include staff-related costs of those divisions and an allocation of agency overhead. Total general and administrative costs

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Management's Discussion and Analysis, continued

allocated to capital projects and transportation services of \$34.3 million increased in 2008 by \$2.4 million, mostly due to the light rail project, as well as to transportation services reflecting increased operations service. Total general and administrative costs allocated to capital projects in 2007 increased by \$2.0 million, mostly due to the light rail project, which was in its peak construction period, as well as to transportation services reflecting increased operations service.

As projects approach completion, allocated overhead costs are reviewed, and any excess costs or costs with no continuing value are written off. Costs written off in 2008 were comparable to 2007 however, 2006 included \$2.4 million related to the postponement of construction of the Tukwila Sounder Station.

Depreciation

Depreciation expense increased in 2008 by \$3.1 million or 8.8% from the prior year (\$1.9 million in 2007). The increase in 2008 reflects the continued capitalization of the track and facility improvements in the South corridor for Sounder, completion of the Mukilteo North platform, Lakewood Station, the Issaquah Transit Center, Mercer Island Park and Ride and bus fleet replacements. In 2007, the higher depreciation reflects the track and facility improvements in the South corridor, as well as the capitalization of the Link Operations and Maintenance Facility.

Non-Operating Revenues (Expenses)

Non-operating revenues (expenses) are substantially comprised of tax revenues, investment income and certain expenses not related to operation of the agency's three modes of operations. Net non-operating revenues decreased by \$15.1 million or 4.3% in 2008, however were comparable between 2007 and 2006.

Non-operating Revenues and Expenses

<i>(in millions)</i>	% Increase				
	2008	2007	2006	2008-2007	2007-2006
Non-operating revenues					
Sales tax	\$ 265.4	\$ 280.3	\$ 259.2	(5.3)	8.1
Motor vehicle excise tax	68.6	72.4	70.2	(5.2)	3.1
Rental car tax	2.5	2.5	2.4	(1.3)	4.3
Investment income	23.6	25.0	37.3	(5.3)	(33.1)
Other revenues	7.9	0.1	(0.0)	6,577.3	-
Total	\$ 368.0	\$ 380.3	\$ 369.1	(3.2)	3.0
Non-operating Expenses					
Non-operating expense	25.7	27.3	12.4	(5.5)	120.3
Interest expense	0.0	0.2	0.4	(92.8)	(48.7)
Discontinued/impaired projects	4.8	0.2	5.9	2,183.4	(96.5)
Total	30.5	27.7	18.7	10.5	47.6
Non-operating Revenues and Expenses	\$ 337.5	\$ 352.6	\$ 350.4	(4.3)	0.6

The most significant impact on non-operating revenues has been weaker tax revenues, that decreased by \$18.7 million in 2008 compared to an increase of \$23.4 million in 2007. This performance reflects the continued weakening of the regional economy from prior years, as well as a \$4.5 million in over collection of motor vehicle excise tax refunds going back to July 2005. Investment earnings also decreased by \$1.4 million, reflecting lower cash and investment balances on hand in 2008. The higher investment earnings in

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Management's Discussion and Analysis, continued

2006 reflected higher interest rate being generated on funds invested in State and County investment pools and other investments.

Other non-operating expenses include light rail operation start-up costs, east corridor planning, supplemental mitigation in the Rainier Valley, costs not eligible to be capitalized, interest expense and discontinued and impaired project costs. In 2008, preparations for start-up of light rail increased, while east corridor planning, supplemental mitigation and costs related to construction claim support decreased from the prior year. While the Phase II plan went to the ballot in 2008 and 2007, a significant portion Phase II planning costs incurred in preparation for the ballot measure in 2007, together with the start-up activities for light rail resulted in the increase from 2006.

Capital Contributions

Net capital contributions increased in 2008 by \$106.0 million, reflecting a significant increase in federal grant funds received and state contributions, together with a decrease in the number of projects completed in 2008 that were contributed to other governments. In 2007, net capital contributions decreased by \$70.0 million. Capital contributions include federal grant funding, state and local contributions to Sound Transit, as well as contributions from Sound Transit to state and local governments pursuant to capital improvement or funding agreements. The following table summarizes capital contributions by major category:

Capital Contributions <i>(in millions)</i>	% Increase				
	2008	2007	2006	2008-2007	2007-2006
Federal	\$ 161.8	\$ 112.7	\$ 130.5	43.6	(13.6)
State and local governments	13.9	4.7	14.1	197.0	(66.8)
To other governments	(67.9)	(115.6)	(72.8)	(41.3)	58.8
Total	\$ 107.8	\$ 1.8	\$ 71.8	5,953.1	(97.5)

Federal contributions increased in 2008 by \$49.1 million and decreased by \$17.8 million in 2007. The University Link full funding grant agreement was executed in 2008 and \$13.0 million in funds were received. In addition, amounts received in respect of Airport Link increased by \$27.4 million. Grant funds received on Central Link also increased, as well as funding received for Tacoma-to-Lakewood, Everett-to-Seattle and Nisqually Sounder corridor project. In 2007, federal funding on Link and ST Express projects was slightly up, but for Sounder projects were down in 2007 as 2006 included the receipt of \$24.4 million for the Everett-to-Seattle Corridor projects.

State and local government contributions increased by \$9.2 million, however were comparable to 2006. In 2008, grant funding of \$2.6 million was received from the State towards the Mountlake Terrace Freeway Station project and parking expansion for Sounder Commuter parking.

Contributions to other governments decreased in 2008 by \$47.8 million. As contributions are dependent upon the timing and scope of project activities there are significant fluctuations from year to year. In 2008, significant projects completed where Sound Transit does not retain ownership included the South Everett Freeway Station and Phase I of the I90 Two-way Transit and HOV lanes. In 2007, Sound Transit completed the Totem Lake Freeway Station/NE 128th project of which \$67.9 million is included above. Other significant projects included the completion of the Reservation – Freighthouse Square mitigation, Redmond Transit Center/NE 83rd and the SR-522 HOV Enhancements at Kenmore and Bothell. In 2006,

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Management's Discussion and Analysis, continued

project funding provided or projects completed for other governments included: Federal Way HOV Access/317th; Eastgate Transit Access/142nd; and Sammamish Park and Ride/228th SE.

Capital Assets

As of December 31, 2008, Sound Transit had invested \$3.9 billion in capital assets, net of accumulated depreciation, which included \$843.7 million of depreciable assets in service. This represents a \$466.1 million or a 13.5% increase over 2007.

Table A-3

Sound Transit Capital Assets (net of depreciation)

<i>(in millions)</i>	As of December 31			% Change	
	2008	2007*	2006*	2008-2007	2007-2006
Land	\$ 360.2	\$ 326.6	\$ 290.9	10.3	12.3
Permanent easements	282.2	267.2	216.7	5.6	23.3
Capital projects in progress					
Sound Transit	2,414.5	2,040.5	1,556.8	18.3	31.1
Other governments	16.8	54.1	103.8	(68.9)	(47.9)
Total Non-Depreciable Assets	3,073.7	2,688.4	2,168.2	14.3	24.0
Buildings, transit facilities & rail	360.2	290.1	236.2	24.2	22.8
Rail access rights	315.7	305.1	288.9	3.5	5.6
Revenue vehicles	164.2	164.5	172.1	(0.2)	(4.4)
Equipment, vehicles & other	3.6	3.2	3.3	10.7	(2.6)
Total Depreciable Assets	843.7	762.9	700.5	10.6	8.9
Total Net Capital Assets	\$ 3,917.4	\$ 3,451.3	\$ 2,868.7	13.5	20.3

* Restated—see *New Accounting Pronouncement*, Note 2

Land increased by \$33.6 million in 2008, primarily related to acquisitions for the University Link and North Link extension, while in 2007 it increased by \$35.7 million, also related to acquisition for the University Link.

Permanent easements increased in 2008 by \$15.0 million with the acquisition of a permanent easement from the University of Washington. In 2007 the fourth easement from BNSF in the Everett-to-Seattle corridor was acquired for \$50.0 million.

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Management's Discussion and Analysis, continued

Activity on capital projects in progress is summarized in the following table:

Table A-4

Major capital project activities from 2008 and 2007:

	Souder	Link	ST Express
2008	<ul style="list-style-type: none"> ▪ Track and signal projects on Everett to Seattle; Seattle to Auburn; and Auburn to Tacoma ▪ Everett Station ▪ South Tacoma Station ▪ Lakewood Station 	<ul style="list-style-type: none"> ▪ Central Line (CPS to 154th; Beacon Hill tunnel Guideway; and Martin Luther King Way) ▪ Tukwila Roadwork and Parking Lot ▪ Airport Link (154th to 160th; and 160th to 176th) ▪ North Link (PSST to UW Station; and Northgate to 45th) ▪ Beacon Hill Station ▪ Traction Power and other Systems ▪ Light Rail Vehicles 	<ul style="list-style-type: none"> ▪ Issaquah Transit Center ▪ South Everett Freeway Station ▪ I-90 2 Way Transit HOV ▪ Totem Lake Freeway Station/NE128th
2007	<ul style="list-style-type: none"> ▪ Track and signal projects on Everett to Seattle; Seattle to Auburn; and Auburn to Tacoma ▪ Lakewood Station 	<ul style="list-style-type: none"> ▪ Central Line (CPS to 154th; Downtown & Beacon Hill tunnels; Martin Luther King Way) ▪ Tukwila Alignment ▪ Airport Link (154th to 160th; and 160th to 170th) ▪ North Link (PSST to UW Station) ▪ Beacon Hill Station ▪ Traction Power System ▪ Operations and Maintenance Base ▪ Light Rail Vehicles 	<ul style="list-style-type: none"> ▪ Issaquah Transit Center ▪ South Everett Freeway Station ▪ Totem Lake Freeway Station/NE128th

Buildings, transit facilities, and rail, net of depreciation, increased in 2008 by \$70.1 million, primarily related to the capitalization of the Mulkiteo Station North platform, Lakewood Station, Issaquah Transit Center, and the Mercer Island Park & Ride. In 2007 they increased by \$53.9 million with the capitalization of the Link Operations and Maintenance Facility.

Rail access rights, net of depreciation, increased by \$10.6 million in 2008 and by \$16.2 million in 2007. Rail access costs reflect the cost of acquiring rights from BNSF for the Tacoma-to-Seattle and Everett-to-Seattle segments. In the Tacoma-to-Seattle corridor, these rights are acquired in an amount equal to the funding of necessary track and signal improvements on the line. Phase 2 of this program was substantially completed at the end of 2008. As the agency is utilizing the rail, these costs are capitalized as charges are incurred.

Revenue vehicles, net of depreciation, and equipment, vehicles and other remained comparable to the prior year of 2007.

More detailed information about Sound Transit's capital assets is presented in Note 5 to the Financial Statements.

Long-Term Debt

The agency issued no debt in 2008. In December 2007, the agency issued sales tax bonds with a par value of \$450.0 million at a premium of \$17.0 million for net proceeds before bond issue costs of \$467.0 million. Total bond issue costs were \$3.1 million.

Under state law, issuance of bonds payable from any type of taxes is subject to statutory debt limitations. Sound Transit is currently authorized to incur debt in an amount equal to 1-1/2 percent of the value of taxable property within the service area, without securing voter approval for bonds. With the approval of

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Management's Discussion and Analysis, continued

60 percent of the region's voters, Sound Transit may incur aggregate indebtedness of up to 5 percent of the value of taxable property within the service area. Based on the 2007 assessed valuations for collection of 2008 taxes, Sound Transit's non-voter approved remaining debt capacity is \$4.4 billion and its voter approved remaining debt capacity is \$17.5 billion.

Economic Conditions

The economic recession has significantly impacted the agency's tax collections, with local tax revenues falling by 5.3% over 2007. Weakness in retail sales and car sales directly impacted the agency's revenue base. The weakness has extended into 2009, with tax revenue still experiencing year-over-year declines.



KPMG LLP
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801 Second Avenue
Seattle, WA 98104

Independent Auditors' Report

Audit and Reporting Subcommittee of the Board of Directors
Central Puget Sound Regional Transit Authority:

We have audited the accompanying basic financial statements of Central Puget Sound Regional Transit Authority (a public corporation acting under the service name Sound Transit) as of and for the years ended December 31, 2008 and 2007, as listed in the table of contents. These financial statements are the responsibility of Sound Transit's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. 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 Sound Transit'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 opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Sound Transit as of December 31, 2008 and 2007, and its changes in financial position and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

As discussed in Note 2, during 2008, Sound Transit adopted Governmental Accounting Standards Board Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*.

The Management's Discussion and Analysis on pages 1 through 14 is not a required part of the basic financial statements of Sound Transit, but is supplementary information required by U.S. generally accepted accounting principles. 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 this information and express no opinion on it.

KPMG LLP

June 19, 2009

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CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Notes to Financial Statements

BALANCE SHEETS

<i>(in thousands)</i>	December 31	
	2008	2007 *
ASSETS		
Current Assets		
Cash and cash equivalents <i>(Note 3)</i>	\$ 144,887	\$ 600,319
Restricted assets <i>(Note 3)</i>	5,238	6,651
Investments <i>(Note 3)</i>	234,683	23,165
Taxes and other receivables <i>(Notes 4)</i>	132,743	96,310
Other	13,690	10,478
Total Current Assets	531,241	736,923
Non-Current Assets		
Capital assets, net of accumulated depreciation <i>(Note 5)</i>	3,917,380	3,451,338
Restricted assets <i>(Note 3)</i>	118,748	113,540
Investment held to pay capital lease obligation <i>(Note 6)</i>	61,617	60,770
Unamortized bond issuance costs	8,025	8,677
Prepaid expense and deposits	7,436	1,228
Total Non-Current Assets	4,113,206	3,635,553
Total Assets	\$ 4,644,447	\$ 4,372,476
LIABILITIES AND EQUITY		
Current Liabilities		
Accounts payable and accrued liabilities <i>(Note 7)</i>	\$ 96,530	\$ 116,436
Deferred receipts	3,377	1,618
Interest payable from restricted assets	13,988	11,245
Current portion, long-term debt <i>(Note 8)</i>	19,810	19,175
Current portion, capital lease obligation <i>(Note 6)</i>	167	228
Other claims and short-term obligations	54,723	50,472
Total Current Liabilities	188,595	199,174
Non-Current Liabilities		
Long-term debt <i>(Note 8)</i>	1,204,052	1,226,285
Capital lease obligations <i>(Note 6)</i>	61,648	60,968
Other long-term obligations <i>(Note 9)</i>	12,171	9,781
Total Non-Current Liabilities	1,277,871	1,297,034
Total Liabilities	1,466,466	1,496,208
Commitments and Contingencies <i>(Notes 6, 9, 11, 12)</i>		
Net Assets		
Invested in capital assets, net of related debt	2,701,345	2,216,783
Restricted for contractual arrangements and other <i>(Note 10)</i>	109,998	108,946
Unrestricted	366,638	550,539
Total Net Assets	3,177,981	2,876,268
Total Liabilities and Net Assets	\$ 4,644,447	\$ 4,372,476

See Notes to Financial Statements.

* Restated—see *New Accounting Pronouncement*, Note 2

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS

<i>(in thousands)</i>	December 31	
	2008	2007
Operating Revenues		
Passenger fares	\$ 26,611	\$ 22,029
Other operating revenue	3,942	4,234
Total Operating Revenues	30,553	26,263
Operating Expenses		
Operations and maintenance	116,748	99,113
General and administrative	19,073	17,060
Loss on disposal of assets	14	309
Depreciation, amortization and accretion	38,282	35,187
Total Operating Expenses	174,117	151,669
Loss from Operations	(143,564)	(125,406)
Non-Operating Revenues (Expenses)		
Sales tax	265,358	280,263
Motor vehicle excise tax	68,621	72,403
Rental car tax	2,498	2,531
Investment income	23,630	24,952
Recovery of prior year and insured losses	7,722	-
Gain on disposal of assets	159	-
Other revenues	65	119
Non-operating expenses	(25,732)	(27,220)
Interest expense	(16)	(224)
Discontinued and impaired projects	(4,818)	(211)
Total Non-Operating Revenues, Net	337,487	352,613
Income Before Capital Contributions	193,923	227,207
Federal capital contributions	161,771	112,668
Other capital contributions	13,867	4,670
Capital contributions to other governments	(67,848)	(115,557)
Net Capital Contributions	107,790	1,781
Change in Net Assets	301,713	228,988
Total Net Assets, Beginning of Year	2,876,268	2,647,280
Total Net Assets, End of Year	\$ 3,177,981	\$ 2,876,268

See Notes to Financial Statements.

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

STATEMENTS OF CASH FLOWS

<i>(in thousands)</i>	December 31	
	2008	2007
Cash Flows from Operating Activities		
Cash receipts from fares	\$ 26,637	\$ 16,265
Cash receipts from other operating revenue	4,112	4,066
Payments to suppliers	(34,852)	(18,876)
Payments to transportation service providers	(60,361)	(73,986)
Payments to employees for wages and benefits	(27,002)	(23,421)
Net Cash Used by Operating Activities	(91,466)	(95,952)
Cash Flows from Non-Capital Financing Activities		
Taxes received	346,767	351,962
Net Cash Provided by Non-Capital Financing Activities	346,767	351,962
Cash Flows from Capital and Related Financing Activities		
Capital contributions from grants	124,575	99,291
Proceeds on issuance of bonds	-	464,236
Proceeds on land sales	580	498
Proceeds for betterments and recoverable costs	1,061	4,499
Purchase of property, vehicles and equipment	(1,317)	(4,642)
Payments in respect of capital projects in progress	(523,473)	(657,518)
Payments to employees capitalized to capital projects in progress	(12,037)	(12,260)
Payments for bond interest, principal and promissory notes	(19,175)	(10,445)
Payments for owner controlled insurance premiums	(9,979)	-
Cash paid for interest	(56,782)	(37,510)
Payments to suppliers for non-operating expenses	(19,762)	(22,396)
Other	(241)	(322)
Net Cash Used by Capital and Related Financing Activities	(516,550)	(176,569)
Cash Flows from Investing Activities		
Purchases of investments	(407,204)	(349,972)
Proceeds from sales or maturities of investments	235,033	589,535
Investment income	18,145	23,209
Net Cash Provided by Investing Activities	(154,026)	262,772
Net (Decrease) Increase in Cash and Cash Equivalents	(415,275)	342,213
Cash and Cash Equivalents		
Beginning of year	646,840	304,627
End of Year	\$ 231,565	\$ 646,840
Cash and Cash Equivalents (Note 3)		
Unrestricted	\$ 144,887	\$ 600,319
Current restricted	2,152	2,432
Non-current restricted	84,526	44,089
	\$ 231,565	\$ 646,840

See Notes to Financial Statements.

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

STATEMENTS OF CASH FLOWS, continued

<i>(in thousands)</i>	December 31	
	2008	2007
Loss from Operations	\$ (143,564)	\$ (125,406)
Adjustments to Reconcile Loss from Operations to Net Cash Used by Operating Activities		
Depreciation, amortization and accretion	38,282	35,187
Loss on disposal of capital assets	14	309
Changes in Operating Assets and Liabilities		
Decrease (increase) in accounts receivable	44	(48)
Decrease (increase) in due from other governments	3,619	(5,224)
(Increase) decrease in materials, parts and supplies	(65)	425
(Increase) decrease in prepaid expenses	(312)	327
(Decrease) increase in accounts payable, accrued and other liabilities	(4,087)	2,596
Increase in salaries, wages and benefits	426	210
Increase (decrease) in deferred pass fare receipts	1,906	(1,249)
Increase (decrease) in due to other governments	12,271	(3,079)
Net Cash Used by Operating Activities	\$ (91,466)	\$ (95,952)

<i>(in thousands)</i>	December 31	
	2008	2007 *
Supplemental Disclosures of Non-Cash Operating, Investing and Financing Activities		
Capital contributions to other governments	\$ (67,848)	\$ (115,557)
Capital contributions from Land Bank	8,119	700
Accounts payable and other liabilities in construction in progress	106,685	133,095
Interest income from investments held to pay capital leases, net	848	844
Interest expense on capital leases	(848)	(844)
Decrease in fair value of investments	(3,177)	(585)

See Notes to Financial Statements.

* Restated—see *New Accounting Pronouncement*, Note 2

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Notes to Financial Statements

NOTES TO FINANCIAL STATEMENTS YEARS ENDED DECEMBER 31, 2008 AND 2007

1. ORGANIZATION AND REPORTING ENTITY

As provided under the Revised Code of Washington (“RCW”) Chapter 81.112 applicable to a regional transit authority, the Central Puget Sound Regional Transit Authority, a public corporation acting under the service name of Sound Transit, was established in 1993. Sound Transit was formed to implement a high-capacity transportation system throughout parts of King, Pierce, and Snohomish counties in the State of Washington through the design, construction, and implementation of a commuter rail (“Sounder”), light rail (“Link”) and regional express bus system (“ST Express”).

Reporting Entity—Sound Transit is a special purpose government supported primarily through sales tax, motor vehicle excise tax and rental car tax in Sound Transit’s operating jurisdiction. In addition, Sound Transit receives capital funding from federal, state and local agencies.

Sound Transit is governed by an 18-member board, seventeen of whom are appointed by the respective member county executives and confirmed by the council of each member county. Membership is based on the population from the portion of each county that lies within Sound Transit’s service area. Representation on the board shall include an elected official representing the largest city in each county and ensures proportional representation from other cities and from unincorporated areas of each county. The final board position is held by the Secretary of Transportation, Washington State Department of Transportation.

Accounting principles generally accepted in the United States of America require that the reporting entity include the primary government, all organizations for which the primary government is financially accountable and other organizations that, by the nature and significance of their relationship with the primary government, would cause the financial statements to be incomplete or misleading if excluded. Based on these criteria, Sound Transit is considered a primary government and does not have any component unit relationships. Conversely, Sound Transit is not considered a component unit of any primary government.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The following summary of significant accounting policies is presented to assist the reader in interpreting the financial statements and should be considered an integral part of the financial statements.

Basis of Accounting—The accounts are maintained and financial statements prepared using the economic resources measurement focus and accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America and methods prescribed by the State Auditor under the authority of RCW Chapter 43.09 for proprietary funds. The Governmental Accounting Standards Board (“GASB”) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. All applicable GASB pronouncements, as well as all Financial Accounting Standards Board (“FASB”) statements and interpretations have been applied, except for those FASB statements and interpretations that contradict GASB pronouncements.

Tax revenues include taxes on retail sales of goods and services, rental car revenue and a motor vehicle excise tax. These taxes are levied within the district at a rate of 0.4% for sales and use, 0.8% on rental car revenue and 0.3% for motor vehicle excise. In November, 2008 the voters approved a 0.5% increase in the sales and use tax, with collection to commence on April 1, 2009. These taxes are collected on Sound

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Notes to Financial Statements, continued

Transit's behalf by the Department of Revenue and the Department of Licensing of the State of Washington and are recorded in the period when the underlying transaction occurs on which the tax is imposed.

Operating revenues consist primarily of passenger fares, which are recognized in the period in which services are provided and are earned, and expenses are recognized in the period in which they are incurred. All assets and liabilities associated with the operation of Sound Transit are included in the Balance Sheets. Depreciation of capital assets and amortization of deferred revenue is recognized in the Statements of Revenues, Expenses and Changes in Net Assets.

Capital Assets—Capital assets are stated at cost, except for donated capital assets, which are stated at the fair value on the date of donation. Expenditures for additions and improvements with a value in excess of \$5,000 and a useful life of more than one year are capitalized. Expenditures for maintenance, repairs and minor improvements are charged to operations as incurred. Depreciation of capital assets is recorded using the straight-line method over the estimated useful lives of the assets and leasehold improvements over the shorter of the life of the asset or length of the related agreement as follows:

	Estimated Useful Life
Rail access costs	37–40 years
Buildings	8–30 years
Transit facilities, rail, and equipment	4–70 years
Park-and-ride lots and shelters	10 years
Revenue vehicles—Cab cars and coach cars	40 years
Revenue vehicles—Locomotives	29 years
Revenue vehicles—Light rail	25 years
Revenue vehicles—Buses	7–12 years
Furniture and equipment	3–7 years
Administrative vehicles and leasehold improvements	5 years

On an annual basis, Sound Transit evaluates whether events or circumstances have occurred affecting capital assets that are other than temporary in nature and which could result in an impairment of those assets. Impairment is considered to have occurred if there is a decline in the service utility that is large in magnitude and the event or circumstance is outside the normal life cycle of the asset. Impairment losses on assets that will no longer be used are measured based on the lower of carrying value or fair value of the affected asset. Impairment losses on assets that will continue to be used are measured using the best method that reflects the diminished service utility of the related asset.

All costs directly attributable to capital projects, as well as certain indirect costs that are allocated to the projects based on various applicable factors supporting the overhead rates used, are capitalized. Capital projects in progress balances include costs incurred for transportation projects not yet in service and are segregated between assets in which Sound Transit maintains a continuing ownership interest and capital assets that will be transferred to other governments upon completion.

Rail access costs reflect the cost of acquiring rights from BNSF for the Tacoma-to-Seattle and Everett-to-Seattle segments. In the Tacoma-to-Seattle corridor these rights were acquired in an amount equal to the funding of necessary track and signal improvements on the line and in the Everett-to-Seattle corridor through the direct acquisition of easements. In addition, these costs include Sound Transit's direct and indirect costs related to the planning and design, environmental management and permitting. The rail access rights for additional round trip service were acquired incrementally, as certain requirements were met under their

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Notes to Financial Statements, continued

respective agreements. As of December 31, 2008, these improvements have been substantially met and rail access rights have been earned.

Interest costs on funds borrowed through tax-exempt debt to finance the construction or acquisition of certain capital assets are capitalized during the period of construction or acquisition and are depreciated over the life of the related assets once placed into service.

Capital Contributions to Other Governments—Pursuant to capital improvement agreements, Sound Transit has provided funding to or constructed assets for various governments or their wholly owned subsidiaries for transit-related capital improvements. For assets constructed for other governments, these costs are capitalized and included in capital projects in progress until the asset is substantially completed and accepted, at which time it is charged to contributions to other governments.

Cash and Cash Equivalents—Cash and cash equivalents consist of cash on hand, demand deposits and short-term investments with maturities of three months or less when purchased, investments in the Local Government Investment Pool and the King County Investment Pool, which are managed by the Washington State Treasurer's Office and the King County Finance Division, respectively.

Compensated Absences—Vacation leave that has been earned but not paid is accrued. Similarly, sick leave is accrued as the benefits are earned but only to the extent that Sound Transit will compensate the employees through cash payments conditional on the employee's termination, retirement or death. Vacation pay, which may be accumulated up to 50 days, is payable upon termination, retirement or death. Sick leave is payable at the rate of 50% of accrued hours upon resignation, retirement or death for employees hired before January 1, 2004, and 25% thereafter and is limited to 120 days for termination other than for retirement or death.

Environmental Remediation Obligations—Environmental remediation activities are reviewed routinely to determine if whether an obligating event, as defined by GASB statement No. 49, has occurred, when the liability should be accrued and whether the cost should be expensed or capitalized. Generally such costs are incurred with respect to properties that Sound Transit is preparing for its own use or are required in the construction of its projects and subsequently resold. As such these costs are recorded as incurred and capitalized to the project. Cost in excess of the property's fair market value, or that do not meet capitalization criteria under generally accepted accounting principles, are accrued and expensed as soon as a reasonable estimate can be obtained.

Investment Valuation—Investments are generally stated at fair value based on quoted market prices, as available.

New Accounting Pronouncement—In November, 2006 the GASB adopted Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations* and is effective for financial statement periods beginning on or after December 15, 2007. For environmental remediation activities, the new statement establishes when an obligating event has occurred, when a liability should be accrued and whether the costs should be expensed or capitalized. This statement was implemented in 2008 and has been applied retroactively for all periods presented. The effect of the adoption was a decrease to capital assets, construction in progress and a decrease to other liabilities by \$2,653 thousand and \$1,672 thousand as of January 1, 2007 and 2006 respectively.

Parts, Materials and Supplies—Parts, materials and supplies are recorded as inventory at the lower of purchased cost or net realizable value. These assets are reviewed periodically for slow-moving and obsolete items, and any impairment in value is reflected as a charge to operations.

Reclassifications—Certain reclassifications have been made to the 2007 Financial Statements to conform to the current year's presentation.

Restricted Assets—Restricted assets are assets set aside to meet externally imposed legal and contractual obligations. Restricted assets are used in accordance with their requirements and where both restricted and

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Notes to Financial Statements, continued

unrestricted resources are available for use, restricted resources are used first and then unrestricted resources as they are needed. In addition to assets set aside to meet externally imposed legal and contractual obligations, Sound Transit has also set aside two months of average annual operating expenses in cash and cash equivalents and has established an investment fund for capital replacement, as established by resolution of its board in 2007. As these cash and investment reserves are derived from internal restrictions, they are not included in restricted assets.

Revenue and Expense Classification—Sound Transit distinguishes operating revenues and expenses from non-operating items in the preparation of its financial statements. Operating revenues and expenses generally result from providing passenger services in connection with Sound Transit’s principal ongoing operations. The principal operating revenues are passenger fares. Sound Transit’s operating expenses include labor, materials, services, claims, purchased transportation and other expenses related to the delivery of passenger transportation within the Central Puget Sound region. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

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

3. CASH, CASH EQUIVALENTS, INVESTMENTS AND RESTRICTED ASSETS

Sound Transit’s bank deposits are covered by the Federal Deposit Insurance Corporation (“FDIC”) or by collateral held in a multiple financial institution collateral pool administered by the Washington Public Deposit Protection Commission (“PDPC”). All deposits not covered by the FDIC are covered by the PDPC. Cash held in the Local Government Investment Pool and the King County Investment Pool are managed by the Washington State Treasurer’s Office and the King County Finance Division, respectively. These pools represent an interest in a group of securities and have no specific security subject to custodial risk.

All surplus cash is invested in accordance with an investment policy approved by Sound Transit’s Board and certified by the Municipal Treasurer’s Association. Qualifying investments under this policy include obligations of the United States government, Treasury and Agency securities, bankers’ acceptances, certificates of deposit, commercial paper, general obligation municipal bonds and repurchase agreements. Sound Transit investment policy and monitoring program addresses common deposit and investment risks as described below, with detailed information by investment type presented in the tables that follow. Modified duration is presented in years.

Interest Rate Risk—Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. For its internally managed and capital replacement funds, Sound Transit matches its investments to cash flow requirements and manages its exposure to fair value losses using the modified duration method, whereby the modified duration of fixed income securities held in its investment portfolios is compared to established benchmarks. Modified duration estimates the sensitivity of a bond’s price to interest rate changes. Modified duration benchmarks for the internally managed fund was 0.58 and for the capital replacement fund was 1.35. For the 2005A Bond Reserve Fund, interest rate risk is managed by using the specific identification method.

Concentration of Credit Risk—Concentration of credit risk is the risk associated with a lack of diversification or having too much invested in a few individual issues. The investment policy sets forth maximum concentration guidelines whereby no single Agency exceeds 50% of the overall

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Notes to Financial Statements, continued

portfolio, or 25% for repurchase agreements or 10% for certificates of deposit, bankers' acceptances, reverse repurchase agreements, general obligation bonds and A1/P1 commercial paper. Treasury securities may comprise up to 100% of the portfolio, as well as participation in the Washington State Treasurer's Local Government Investment Pool. Agency Securities (combined) may comprise up to 75% of the portfolio. Participation in the King County Investment Pool is limited to 50% of the portfolio.

Credit Risk—Credit risk is the chance that an issuer will fail to pay principal or interest in a timely manner, or that negative perceptions of the issuer's ability to make these payments will cause the price of the investment to decline. All Agency securities in our portfolios are rated AAA and the Certificates of Deposit are covered by the PDPC. The King County Investment Pool's rating of AA+ has been temporarily suspended due to asset-backed commercial paper in their portfolio which is in default. The Washington State Treasurer's Local Government Investment Pool is a 2a7-like pool and is unrated.

Custodial Credit Risk—Custodial credit risk is the risk that, in the event of the failure of the counterparty, Sound Transit would not be able to recover the value of its investment or collateral securities that are in the possession of an outside party. All investments purchased by Sound Transit are held and registered in Sound Transit's name in the Trust Department or safekeeping department of a financial institution as established by a written third party safekeeping agreement between Sound Transit and the financial institution.

In 2007 Sound Transit recorded an estimated loss in the amount of \$209 thousand, which was the expected pro-rata share of the loss on its holdings in the King County Pool based on independent market valuations obtained by the County. In 2008 this estimated loss was increased by \$59 thousand. The ultimate resolution of the impaired investments is expected to take approximately six years.

In 2007, Sound Transit entered into a Forward Purchase and Sale Agreement for funds invested for purposes of its 2005A Bond Reserve. It terminated this agreement in September of 2008 when the counterparty to the transaction, Lehman Brothers, declared bankruptcy. These funds were then invested in a portfolio separately managed by Sound Transit which currently includes municipal bonds and US agency securities.

Cash, cash equivalents, investments and restricted assets are as follows:

<i>(in thousands)</i>	2008			2007		
	Fair Value	Maturity	Call Date	Fair Value	Maturity	Call Date
2005A Debt Service Reserve Fund						
Investments						
Municipal Bonds						
Clark County Nevada GO Limited	\$ 17,104	11/1/2027	11/1/2027 *	\$ -	-	-
Georgia State GO Unlimited	6,442	4/1/2026	4/1/2026 *	-	-	-
US Agency Securities						
Federal National Mortgage Association	10,363	4/12/2022	4/12/2022 **	-	-	-
Federal Home Loan Bank	-	-	-	39,892	4/30/2008	-
	<u>33,909</u>			<u>39,892</u>		
Cash and Cash Equivalents						
Washington State Local Government Investment Pool	6,124			-		
	<u>\$ 40,033</u>			<u>\$ 39,892</u>		

* Continuously callable from this date forward

** One-time call

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Notes to Financial Statements, continued

<i>(in thousands)</i>						
	Fair Value	2008 Modified Duration	% of Portfolio	Fair Value	2007 Modified Duration	% of Portfolio
Investments - Internally Managed Fund						
US agency securities:						
Federal Farm Credit Bank	\$ 20,331	0.560	10.79%	\$ -	-	-
Federal Home Loan Bank	76,748	0.650	40.73%	8,034	0.256	27.35%
Federal Home Loan Mortgage Corporation	30,582	0.730	16.23%	9,451	0.372	32.18%
Federal National Mortgage Association	30,525	0.420	16.20%	11,886	0.449	40.47%
US treasury securities	12,856	0.990	6.82%	-	-	-
Municipal Bonds	2,370	0.490	1.26%	-	-	-
Certificate of deposit	15,000	0.000	7.96%	-	-	-
	<u>\$ 188,412</u>	<u>0.636</u>	<u>100.00%</u>	<u>\$ 29,371</u>	<u>0.372</u>	<u>100.00%</u>
Investments - Capital Replacement Fund						
US agency securities:						
Federal Farm Credit Bank	7,855	0.450	16.98%	7,746	1.390	33.44%
Federal Home Loan Bank	27,165	1.510	58.71%	15,419	1.421	66.56%
Federal Home Loan Mortgage Corporation	11,251	1.690	24.32%	-	-	-
	<u>\$ 46,271</u>	<u>1.374</u>	<u>100.00%</u>	<u>\$ 23,165</u>	<u>1.411</u>	<u>100.00%</u>

<i>(in thousands)</i>	December 31	
	2008	2007
Cash and Cash Equivalents		
Investment Pools:		
King County	\$ 145	\$ 181
Washington State Local Government Investment Pool *	181,294	618,794
US discount note:		
Federal Home Loan Bank	-	280
Federal Home Loan Mortgage Corporation	-	-
Certificates of Deposit	8,000	8,000
FDIC or PDPC Insured Bank Deposits	35,819	19,502
Cash on hand	183	83
	<u>225,441</u>	<u>646,840</u>
Other Restricted Assets		
Deductible liability protection policy	3,086	4,219
Interest receivable on restricted investments	313	188
	<u>3,399</u>	<u>4,407</u>
Total Investments, Cash and Cash Equivalents and Other Restricted Assets	<u>\$ 503,556</u>	<u>\$ 743,675</u>

* Portion segregated for the 2005A Debt Reserve. See also table on Page 25.

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Notes to Financial Statements, continued

<i>(in thousands)</i>	December 31	
	2008	2007
Balance Sheet Classifications		
Cash and cash equivalents	\$ 144,887	\$ 600,319
Current restricted assets:		
Cash equivalents	2,152	2,432
Deductible liability protection policy	3,086	4,219
	<u>5,238</u>	<u>6,651</u>
Investments	<u>234,683</u>	<u>23,165</u>
Non-current restricted assets:		
Cash Equivalents	84,526	44,089
Investments	33,909	69,263
Other assets	313	188
	<u>118,748</u>	<u>113,540</u>
	<u>\$ 503,556</u>	<u>\$ 743,675</u>

4. RECEIVABLES

Receivables consist of the following:

<i>(in thousands)</i>	December 31	
	2008	2007
Taxes receivable	\$ 49,251	\$ 57,384
Grants receivable	65,647	22,703
Accounts receivable, net	2,185	139
Due from Other Governments	13,112	14,903
Interest receivable	2,548	1,181
	<u>\$ 132,743</u>	<u>\$ 96,310</u>

Amounts due from other governments include amounts due under the Puget Pass regional fare program, amounts reimbursable under interlocal agreements for operating expenses or capital contributions for transit facilities, and betterments. Payment terms are generally defined in the various agreements with other governments and range from 21 days to 60 days. Where payment terms are not defined by agreement, they are due in accordance with the terms specified in the invoice, which is generally 30 days.

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Notes to Financial Statements, continued

5. CAPITAL ASSETS

Capital assets are summarized as follows:

<i>(in thousands)</i>	Transfers			Transfers			
	December 31	In and	Transfers Out and	December 31	In and	Transfers Out and	December 31
	2006*	Additions*	Retirements	2007*	Additions	Retirements	2008
Non-Depreciable Assets							
Land	\$ 290,876	\$ 39,604	\$ (3,896)	\$ 326,584	\$35,898	\$ (2,300)	\$ 360,182
Permanent easements	216,685	50,491	-	267,176	14,995	-	282,171
Capital Projects in Progress							
Sound Transit	1,556,890	670,192	(186,572)	2,040,510	549,769	(175,747)	2,414,532
Other Governments	103,778	66,399	(116,066)	54,111	34,318	(71,591)	16,838
Total Non-Depreciable Assets	2,168,229	826,686	(306,534)	2,688,381	634,980	(249,638)	3,073,723
Depreciable Assets							
Transit facilities, rail and heavy equipme	265,645	67,620	(575)	332,690	85,430	-	418,120
Rail access rights	304,945	25,181	-	330,126	20,010	-	350,136
Buildings and leasehold improvements	23,168	10	-	23,178	166	-	23,344
Revenue vehicles	231,717	3,881	-	235,598	11,693	(3,430)	243,861
Furniture, equipment and vehicles	14,847	1,558	(479)	15,926	1,650	(2,115)	15,461
Equipment under capital lease	901	170	(131)	940	-	-	940
Total Depreciable Assets	841,223	98,420	(1,185)	938,458	118,949	(5,545)	1,051,862
Accumulated Depreciation							
Transit facilities and heavy equipment	(46,008)	(12,480)	28	(58,460)	(14,656)	-	(73,116)
Rail access rights	(16,047)	(8,942)	-	(24,989)	(9,482)	-	(34,471)
Buildings and leasehold improvements	(6,555)	(776)	-	(7,331)	(793)	-	(8,124)
Revenue vehicles	(59,665)	(11,400)	-	(71,065)	(11,986)	3,403	(79,648)
Furniture, equipment and vehicles	(12,063)	(1,271)	216	(13,118)	(1,057)	2,086	(12,089)
Equipment under capital lease	(389)	(222)	73	(538)	(219)	-	(757)
Total Accumulated Depreciation	(140,727)	(35,091)	317	(175,501)	(38,193)	5,489	(208,205)
Depreciable Assets, Net	700,496	63,329	(868)	762,957	80,756	(56)	843,657
Total Capital Assets, Net	\$ 2,868,725	\$ 890,015	\$ (307,402)	\$ 3,451,338	\$ 715,736	\$ (249,694)	\$ 3,917,380

* Restated—see *New Accounting Pronouncement*, Note 2

During 2008, Sound Transit capitalized \$57.8 million of interest costs, (\$37.3 million in 2007), representing all of the interest, net of premium, discounts and bond issue costs, incurred on its bonds outstanding (see Note 8).

6. CAPITAL AND OPERATING LEASES

Capital lease obligations are comprised of the following:

<i>(in thousands)</i>	2008	2007
Lease/leaseback	\$ 61,617	\$ 60,770
Copier leases	198	426
	61,815	61,196
Less current portion	(167)	(228)
	\$ 61,648	\$ 60,968

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Notes to Financial Statements, continued

Lease/Leaseback—On May 31, 2001, Sound Transit entered into a transaction to lease 22 rail passenger cab and coach cars and 5 locomotives (the “headlease”) to an investor and simultaneously subleased the vehicles back (the “sublease”). Under these transactions, Sound Transit maintains the right to continued use and control of the assets through the end of the leases and is required to insure and maintain the assets. The headlease and sublease have been recorded as capital leases for accounting purposes.

The vehicles had a fair market value of \$61.3 million with a book value of \$37.7 million at closing. Sound Transit received a prepayment equivalent to the net present value of the headlease obligations totaling \$61.3 million. From those proceeds, \$50.4 million was deposited with AIG-FP Special Finance Ltd. to partially meet Sound Transit’s obligations under the sublease payments. In addition, \$5.7 million was deposited with AIG Matched Funding Corp. and invested in securities issued or guaranteed by the United States government to meet the remaining obligations under the sublease. The remaining \$4.9 million (net of closing costs of \$363 thousand) was retained by Sound Transit and recorded as non-operating revenues in the year ended December 31, 2001.

The net present value of the future sublease payments has been recorded as a long-term capital lease obligation. The underlying investments have been structured to meet all future obligations under the sublease when due, and as such, have been recorded to equal the sublease obligations on the accompanying balance sheet.

The lease documentation established minimum credit levels by AIG for the equity and debt defeasance accounts. At the time these transactions closed, AIG was rated “AAA” by S&P and “Aaa” by Moody’s. However, starting in March 2005, AIG suffered a series of credit rating downgrades to reach a level of “A-” by S&P and “A3” by Moody’s by end year 2008. As a result of these rating downgrades under the lease transaction Sound Transit is required to replace AIG for its undertaking agreements and credit enhancements provision in the transaction and AIG is required to post collateral for the debt defeasance accounts.

Through June 30, 2009 Sound Transit has negotiated a standstill agreement with the transaction participants on the requirements to replace the debt defeasance, letter of credits and payment undertaker as required under the transaction. Sound Transit is pursuing options to replace AIG or amend the transaction to the satisfaction of the participants. If Sound Transit does not receive additional standstill agreements or amend the transaction to achieve compliance, the investor has the option to exercise any of several remedies, including termination of the lease in which case investor could request payment of a termination amount. The termination payment, less the accreted value schedule for the equity payment agreement, was \$15.0 million at end year 2008.

Net changes in the sublease are shown in the following table:

<i>(in thousands)</i>	2008	2007
Net sublease, January 1	\$ 60,770	\$ 59,925
Accrued interest	4,548	4,485
Less payment	(3,701)	(3,640)
Net Sublease, December 31	\$ 61,617	\$ 60,770

Amtrak Lease/Sublease—In September 2000, Sound Transit entered into a 40-year agreement to lease its locomotives, passenger coaches and cab cars (“rolling stock”) to the National Railroad Passenger

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Notes to Financial Statements, continued

Corporation (“Amtrak”) for \$1. Under the agreement Amtrak is obligated to repair, maintain and service the rolling stock at Amtrak’s maintenance facility in return for payment by Sound Transit. By separate agreement, Sound Transit assigned to Amtrak its commuter rail operating agreement, which it had entered into with the BNSF Railway Company (“BNSF”) in May 2000 to provide commuter rail service. In order to give BNSF possession and use of the rolling stock for purposes of providing commuter rail service on Amtrak’s behalf for Sound Transit, Amtrak entered into a 40-year sublease of the rolling stock to BNSF for a nominal rental payment of \$1.

Under the legal structure of these transactions and pursuant to a Department of Revenue ruling, the equipment is exempted from Washington State sales and use taxes, and Sound Transit and Amtrak have agreed by a Memorandum of Understanding to use funds that would otherwise be payable for projects that mutually benefit Pacific Northwest intercity rail passenger service. Sound Transit maintains title and continuing control of the assets through the end of the lease, upon which the assets will be returned to Sound Transit.

Operating Rentals—Sound Transit has entered into leases of ground, office space, parking, land, storage at various locations, as well as equipment leases under non-cancelable operating leases in excess of one year with lease terms expiring in 2008 and beyond 2010. Significant lease arrangements include office space and parking adjacent to Union Station and a ground lease for the Rider Services Building. Certain of its leases contain one, two or three year extension options as well as a 5-year extension option on the office space adjacent to Union Station.

Minimum lease payments through 2013 are as follows:

Operating Rentals, commitments next 5 years:

(in thousands)

2009	\$	2,224
2010		1,176
2011		301
2012		289
2013		288
	\$	<u>4,278</u>

Total rental expenses for 2008, which include non-cancelable leases as well as other month-to-month rentals, were \$3.0 million, of which \$725 thousand was for capital projects in progress. Total expenses for 2007 were \$2.4 million, of which \$468 thousand was for capital projects in progress.

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Notes to Financial Statements, continued

7. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable and accrued liabilities consist of the following:

<i>(in thousands)</i>	2008	2007
Accounts payable	\$ 35,891	\$ 17,465
Accrued liabilities	7,716	52,769
Due to other governments	50,565	44,268
Accrued salaries, wages and benefits	2,090	1,623
Retainage payable	268	311
	<u>\$ 96,530</u>	<u>\$ 116,436</u>

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Notes to Financial Statements, continued

8. LONG-TERM DEBT

Long-term debt consists of the following:

<i>(in thousands)</i>	2008 Beginning Balance	Additions	Reductions	2008 Ending Balance	Amounts Due within One Year
Bonds payable:					
Series 1999 Bonds, at par	\$ 341,285	-	\$ (4,620)	\$ 336,665	\$ 4,810
Series 2005A Bonds, at par	422,815	-	-	422,815	-
Series 2007A Bonds, at par	450,000	-	(14,555)	435,445	15,000
	1,214,100	-	(19,175)	1,194,925	19,810
Plus unamortized premium	37,708	-	(2,800)	34,908	-
Less unamortized discount	(6,348)	-	377	(5,971)	-
Total Long-Term Debt	\$ 1,245,460	-	\$ (21,598)	\$ 1,223,862	\$ 19,810

<i>(in thousands)</i>	2007 Beginning Balance	Additions	Reductions	2007 Ending Balance	Amounts Due within One Year
Bonds payable:					
Series 1999 Bonds, at par	\$ 345,730	-	\$ (4,445)	\$ 341,285	\$ 4,620
Series 2005A Bonds, at par	422,815	-	-	422,815	-
Series 2007A Bonds, at par	-	450,000	-	450,000	14,555
	768,545	450,000	(4,445)	1,214,100	19,175
Plus unamortized premium	22,460	17,009	(1,761)	37,708	-
Less unamortized discount	(6,732)	-	384	(6,348)	-
Total bonds payable	784,273	467,009	(5,822)	1,245,460	19,175
Promissory notes:					
Lakeview South Line	6,000	-	(6,000)	-	-
Plus (minus) imputed interest	(199)	-	199	-	-
Total Promissory Notes Payable	5,801	-	(5,801)	-	-
Total Long-Term Debt	\$ 790,074	\$ 467,009	\$ (11,623)	\$ 1,245,460	\$ 19,175

Sales Tax and Motor Vehicle Excise Tax Bonds, Series 1999—On January 6, 1999, Sound Transit issued tax-exempt Sales Tax and Motor Vehicle Excise Tax Bonds, Series 1999 dated December 1, 1998 in the amount of \$350 million. The bonds are special limited obligations of Sound Transit payable from and secured solely by a pledge of Sound Transit's sales and use tax, motor vehicle excise tax and rental car tax imposed at the rates of 0.4%, 0.3% and 0.8%, respectively, and are considered senior to the Series 2005A and 2007A subsequently issued.

Sales Tax Bonds, Series 2005A—On March 31, 2005, Sound Transit issued tax-exempt Sales Tax Bonds, Series 2005A dated March 31, 2005 in the amount of \$422.8 million. These bonds were issued on a subordinate basis to the prior bonds issued. These bonds are special limited obligations of Sound Transit payable from and secured solely by a pledge of Sound Transit's sales and use tax and rental car tax.

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Notes to Financial Statements, continued

Sales Tax Bonds, Series 2007A—On December 18, 2007, Sound Transit issued tax-exempt Sales Tax Bonds, Series 2007A dated December 18, 2007 in the amount of \$450.0 million. These bonds were issued on a subordinate basis to prior bonds issued. These bonds are special limited obligations of Sound Transit payable from and secured solely by a pledge of Sound Transit's sales and use tax and rental car tax.

Sound Transit is required to maintain certain minimum deposits as defined in the respective bond resolution for each bond issue to meet debt service requirements. In addition, for the Series 2005A Bonds, the Agency established a \$39.5 million reserve, consistent with the Parity Bond Resolution, which was invested in a Forward Purchase and Sale Agreement in 2007 with a guaranteed yield of 5.18% for the life of the bond reserve. The Purchase and Sale Agreement was terminated in September 2008 (see Note 3). Proceeds from all bond issues have been used for the Agency's capital projects.

The following tables set forward average and effective coupon rates, rating agency information, principal payment commencement, fair value, amounts currently restricted for debt service and debt requirements to maturity.

	Issue Date	Average Rate		Ratings		Principal Payment Commencement
		Coupon	Effective	Moody's (1)	S&P (2)	
Series 1999	Dec 1, 1998	4.88	5.03	Aa2	AAA	Feb 1, 2006
Series 2005A	March 31, 2005	4.95	4.60	Aa3	AAA	Nov 1, 2011
Series 2007A	Dec 18, 2007	4.99	4.76	Aa3	AAA	Nov 1, 2008

December 31					
<i>(in millions)</i>	Fair Value ⁽³⁾		Cash Restricted For Debt Service		
	2008	2007	2008	2007	
Series 1999	308.5	354.7	11.7	11.6	
Series 2005A	377.0	442.5	3.5	3.4	
Series 2007A	371.3	466.7	3.6	0.8	

(1) Moody's Investor Services

(2) Standard and Poor's

(3) Estimated using quoted market prices.

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Notes to Financial Statements, continued

Debt service requirements to maturity for bonds payable.			
Year Ending December 31 2008	Principal	(in thousands) Interest	Total
2009	\$ 19,810	\$ 58,865	\$ 78,675
2010	8,065	57,862	65,927
2011	18,465	57,475	75,940
2012	19,195	56,744	75,939
2013	20,135	55,802	75,937
2014-2018	123,175	262,899	386,074
2019-2023	223,520	219,277	442,797
2024-2028	271,745	159,912	431,657
2029-2033	284,010	95,686	379,696
2034-2036	206,805	21,017	227,822
	<u>\$ 1,194,925</u>	<u>\$ 1,045,539</u>	<u>\$ 2,240,464</u>

9. OTHER LONG-TERM OBLIGATIONS

Other long-term obligations include provisions for asset retirement obligations, uninsured losses related to the agency's risk management program and employee compensated absences as follows:

(in thousands)	2008			2008	Amounts Due
	Beginning	Additions and	Reductions	Ending	within
	Balance	accretion		Balance	One Year
Asset retirement obligations					
Sounder station platforms	\$ 912	\$ 41	\$ -	\$ 953	\$ -
Tacoma Link surface rail	1,332	48	-	1,380	-
Total asset retirement obligations	<u>2,244</u>	<u>89</u>	<u>-</u>	<u>2,333</u>	<u>-</u>
Uninsured Losses					
Owner Controlled Insurance Program	6,297	3,503	(1,278)	8,522	1,909
Transit operations	453	741	-	1,194	252
Total uninsured losses	<u>6,750</u>	<u>4,244</u>	<u>(1,278)</u>	<u>9,716</u>	<u>2,161</u>
Compensated absences	3,119	3,538	(3,213)	3,444	1,161
Total other long-term obligations	<u>\$ 12,113</u>	<u>\$ 7,871</u>	<u>\$ (4,491)</u>	<u>\$ 15,493</u>	<u>\$ 3,322</u>

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Notes to Financial Statements, continued

<i>(in thousands)</i>	2007			2007	Amounts Due
	Beginning	Additions and	Reductions	Ending	within
	Balance	accretion		Balance	One Year
Asset retirement obligations					
Sounder station platforms	\$ 955	\$ (43)	\$ -	\$ 912	\$ -
Tacoma Link surface rail	1,607	(275)	-	1,332	-
Total asset retirement obligations	2,562	(318)	-	2,244	-
Uninsured Losses					
Owner Controlled Insurance Program	2,508	5,040	(1,251)	6,297	1,269
Transit operations	414	721	(682)	453	74
Total uninsured losses	2,922	5,761	(1,933)	6,750	1,343
Compensated absences	2,855	3,370	(3,106)	3,119	989
Total other long-term obligations	\$ 8,339	\$ 8,813	\$ (5,039)	\$ 12,113	\$ 2,332

Asset Retirement Obligations—In the course of entering into agreements with other governments and rail providers to construct the Agency’s capital assets used in providing transportation services, certain of those agreements contain clauses that impose a legal burden on the Agency to remove all or a portion of those constructed assets at the termination of those agreements. FASB 143 and FASB Interpretation 47, require that these costs and related obligations be recognized where they exist.

Risk Management—In the ordinary course of construction of its transit project and agency and rail operations, Sound Transit is exposed to various types of risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; injuries to persons; and natural disasters. Sound Transit has established a comprehensive risk management and insurance program that encompasses risk, safety and security. For its agency and railroad operations a commercial insurance program has been put in place that provides first-level coverage for property, liability, employment practices and crime and fidelity to provide protections from these risks and exposures. For ST Express operations, under Sound Transit’s agreements insurance coverage is provided by its bus partner agencies, however under its agreement for service in Pierce County, Sound Transit reimburses Pierce Transit for the cost of all individual claims paid up to \$1 million.

Sound Transit also utilizes two Owner-Controlled Insurance Programs (“OCIP”) for all general liability claims by third-party injuries and/or property damage related to project construction activities carried out by third-party contractors. Its first program was secured in 2001, primarily for construction of the Central Link Light Rail – Initial Segment and subsequently amended to include the Airport Link light rail segment and provides coverage from January 1, 2001 through December 31, 2009, with the exception of the professional liability and contractor’s pollution liability insurance policy, which provides coverage through December 31, 2016, with an additional 3-year reporting period extending to December 31, 2019.

A second OCIP was secured in October 2008 for the University Link Light rail segment. The funding of the premiums for this program is structured with initial premium payments of \$6.8 million in 2008 followed by premium payments in 2009 and 2010 of \$6.2 million and \$5.8 million respectively, with coverage provided from October 20, 2008 through September 30, 2016.

On each of its policies, Sound Transit is responsible for deductibles or self-insured retentions, per occurrence or claim. For its Central and Airport Link Light Rail OCIP general liability policy, Sound Transit also entered into a deductible liability protection policy to supplement the deductible self-insured retention for the probable maximum claims exposure at the inception of the policy, estimated at \$6.5

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Notes to Financial Statements, continued

million. This amount was deposited with the insurer in an interest-bearing loss fund account, of which a balance of \$3.1 million is remaining at December 31, 2008 (see Note 3).

Annually Sound Transit engages an actuary to estimate its total claim exposure under all of these risk management and insurance programs. Claim amounts estimated to be paid within the next year are included in other current liabilities.

Compensated Balances—Amounts estimated to be paid within the next year are included in accrued salaries, wages and benefits.

10. RESTRICTED NET ASSETS

Restricted net assets consist of the following:

<i>(in thousands)</i>	2008	2007
Contractual arrangements	\$ 44,604	\$ 58,063
Debt service, net of related obligations	60,156	44,512
Deductible liability protection policy	3,086	4,219
State appropriation	2,152	2,152
	<u>\$ 109,998</u>	<u>\$ 108,946</u>

11. EMPLOYEE BENEFITS

Sound Transit provides a defined contribution money purchase plan and trust (“401(a) Plan”) to its employees. Prior to December 31, 1999, employees had a choice of participating in either the 401(a) Plan or in the Washington Public Employees’ Retirement System (“PERS”). In 1999, the Washington State Legislature amended the laws governing PERS requiring employers to either terminate their participation in PERS or permit all new employees to participate in PERS regardless of their simultaneous participation in a 401(a) plan. Effective December 31, 1999, Sound Transit terminated its status as a PERS employer with regard to all employees hired after that date. Individuals who were active members at that date were eligible to continue their membership in PERS for the duration of their continuous employment with Sound Transit. At December 31, 2008, 2007 and 2006, there was one remaining employee participating in PERS.

A summary of the 401(a) Plan is as follows:

401(a) Plan—A defined contribution money purchase plan and trust was established for the Agency in 1994 with the adoption of Board Resolution No. 32. This was amended by Resolution No. 100 in 1997 to recognize the contribution made to Sound Transit by its employees. The ICMA Retirement Corporation administers the Central Puget Sound Regional Transit Authority Pension Plan and serves as the plan’s trustee. This plan is a fixed employer system, and membership in the system includes all full-time Sound Transit employees and elected officials. The vesting schedule of the plan is 20% immediately upon employment, 40% after one year of service, 60% after two years, 80% after three years and 100% after four years. Employees are responsible for directing the investment of their contributions and Sound Transit’s contributions.

Any eligible employee who was employed on the effective date of this plan was eligible to participate in the plan. Any other eligible employee shall be eligible to participate on the first day of employment.

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Notes to Financial Statements, continued

Sound Transit's actual contribution rates, which were the required contribution rates, are expressed as a percentage of covered payrolls. The amount of covered payroll during 2008 and 2007 was \$28.6 and \$26.8 million, respectively, and total payroll was \$29.2 and \$27.2 million respectively. The required contribution rates expressed as a percentage of covered payroll and required Sound Transit contributions during 2008, 2007, and 2006 are as follows:

	Contribution Rate			Contributions (in thousands)		
	2008	2007	2006	2008	2007	2006
Employer	12%	12%	12%	\$3,437	\$3,213	\$3,111
Employee	10%	10%	10%	2,864	2,678	2,592
Total	22%	22%	22%	\$6,301	\$5,891	\$5,703

12. COMMITMENTS AND CONTINGENCIES

Operations and Maintenance Agreements—In May, 2000, Sound Transit entered into a 40-year agreement with BNSF for the operation of commuter trains by BNSF between Seattle and Tacoma and the compensation paid to BNSF for train crews, maintenance-of-way and other expenses incurred in the operation of the Sounder service. The compensation is based on the actual costs of crew, dispatch and management, as well as costs for maintenance of way plus performance incentives.

In September, 2000, Sound Transit entered into an agreement with Amtrak for the operations and maintenance of its Sounder commuter rail rolling stock, expiring December 31, 2009 with annual renewal options at the mutual consent of both parties. Under the agreement, Sound Transit pays a flat monthly fixed price dependent upon the number of one-way trips and train sets in operation for a baseline set of operating assumptions. Sound Transit pays a negotiated rate for additional service above this baseline operating plan. See related agreements described in Note 6: *Amtrak Lease/Sublease*. Sound Transit is currently in negotiation with Amtrak for a new contract, however if negotiations are not complete by December 31, 2009 both parties intend to exercise the annual renewal options.

On June, 2002, Sound Transit entered into an agreement with King County to share Downtown Seattle Transit Tunnel ("DSST") maintenance and operation costs in exchange for the right to use the DSST for light rail operations. Sound Transit's obligations include transfer of betterments, reimbursement of costs, and payment of a share of county debt service owed for the original tunnel construction. Sound Transit is also committed under this agreement to share costs for future capital repairs or replacements as they arise. Compensation is calculated as reimbursement of certain county costs based on fixed percentages. The DSST agreement remains in effect indefinitely.

In June, 2003, Sound Transit entered into a Central Link Light Rail system operation and maintenance agreement with King County. The agreement term extends five years beyond the commencement of passenger revenue service. Compensation for this service is based on reimbursement for county expenses based on a fixed amount for a baseline level of service, with additional costs billed for service changes directed by Sound Transit.

In December, 2003, Sound Transit entered into an agreement with BNSF for the operation of the commuter trains by BNSF between Seattle and Everett and the compensation paid to BNSF for train crews, maintenance-of-way and other expenses incurred in the operation of the Sounder service. The compensation is structured as an hourly rate per train mile operated for a baseline service plan, with inflation adjusters

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Notes to Financial Statements, continued

plus performance incentives. The term of the agreement is for 12 years with an option of five additional years that must be agreed to by both parties, for a maximum term of 17 years. In addition, a first amendment was executed to the existing long-term agreement for commuter service from Seattle to Tacoma, covering service for the Lakewood-to-Tacoma corridor, provided Sound Transit eventually operates in the corridor.

In July, 2004, Sound Transit entered into five-year agreements that expire December 2009 with Community Transit, King County Department of Transportation and Pierce Transit (“purchased transportation providers”) to operate its ST Express public transportation service within Sound Transit’s service area. Service is compensated based upon a fixed fee agreed to annually, with certain items subject to variable pricing, such as fuel and special services. Sound Transit is currently in negotiations with its purchased transportation providers with the intention to enter into new multi-year agreements.

Agreements with BNSF for Sounder Commuter Rail Service Easements in the Everett-to-Seattle and Lakewood-to-Tacoma Corridors—On December 18, 2003, Sound Transit entered into a number of agreements with BNSF for, among other things, the purchase of four perpetual easements for commuter rail service between Everett and Seattle, the purchase of railroad right-of-way between Nisqually and Tacoma for service and station improvements, terms for joint use of the railroad right-of-way and the purchase of operation services in each corridor.

The acquisition of the easements and property occurred over a four-year payment period. The first easement in the Everett-to-Seattle corridor closed in December 2003, and the second easement closed in December 2004, each in exchange for a payment of \$79.0 million. The third easement closed in December 2006 and the fourth and final easement closed in December 2007, each in exchange for a payment of \$50 million. Each easement allows the addition by Sound Transit of one round trip commuter train service.

The Joint-Use Agreement for the Everett-to-Seattle corridor provides the mechanism for determining the cost to Sound Transit for the maintenance-of-way and rehabilitation activities on the corridor.

The Joint-Use Agreement for the Lakewood-to-Tacoma corridor sets forth the cost to BNSF for the maintenance-of-way and rehabilitation activities on the corridor and Sound Transit and BNSF’s responsibilities during the interim period before Sound Transit starts operating on each portion of the corridor. However, as Sound Transit incrementally commences construction of the line, Sound Transit will be responsible for maintenance activities on those sections.

Governmental Agreements— In its ordinary course of planning design and construction of its projects, Sound Transit enters into agreements with other governments. These agreements establish the working relationships with the other governmental entities and may obligate Sound Transit to pay for services over the lifecycle of a construction project, and often include provisions to transfer property or property rights upon completion of construction. Significant governmental agreements include:

City of Seattle Construction Services Agreement: Entered into on November 13, 2003, this agreement covers areas including, quality assurance & inspections, emergency services, traffic signal design, and utility work by city crews. The agreement also commits Sound Transit to accomplish certain betterments and utility upgrades, which are to be reimbursed by the city. All commitments under this agreement are anticipated to be completed during 2009.

Port of Seattle Construction Services Agreement: Entered into on April 17, 2006, this agreement provides payment terms and assignments regarding which entity serves as contract administrator, and which serves as construction manager, for the various contract packages making up the Airport Link project. The agreement also stipulates operating terms applicable after construction. The agreement will not expire as long as Sound Transit operates rail transit systems on the segment.

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Notes to Financial Statements, continued

University of Washington Master Implementation Agreement: Entered into on July 2, 2007, this agreement allows Sound Transit entry to the University's Seattle Campus to construct Link light rail; establishes compensation amounts for certain staffing costs, parking mitigation in the amount of \$15.2 million, which was paid in 2007, and consideration for easements granted by the University in the amount of \$20.0 million, paid May 2008. Both parties anticipate additional agreement(s) providing terms for the operation of Link light rail on University property.

Land Bank Agreement—Sound Transit entered into an agreement called the *Land Bank Agreement* with the Washington State Department of Transportation ("WSDOT") in July of 2000 and as restated in December of 2003, the purpose of which is to establish a framework within which WSDOT can from time to time convey portions of WSDOT property to Sound Transit and to make other portions of other WSDOT property available for non-highway use by Sound Transit in consideration for Sound Transit's funding of highway purpose improvements. The value of Land Bank credits at December 31, 2008 was \$141.5 million and is not recorded in the financial statements. The following table provides information on additions to and uses of credits accruing to the benefit of Sound Transit in 2008 and 2007.

	2008	2007
(in millions)		
Balance in Land Bank, beginning of year	\$ 149.6	\$ 150.3
Draws:		
Canyon Park airspace agreement	-	(0.7)
E-3 Busway	(4.3)	-
Issaquah TC	(0.1)	
Resevation-Freighthouse	(0.0)	
Seattle-Auburn Track & Signal	(3.6)	
Totem Lake Fwy Stations/NE 128th	(0.1)	
Balance in Land Bank, end of year	\$ 141.5	\$ 149.6

Purchases—At December 31, 2008 and 2007, Sound Transit had outstanding construction commitments of approximately \$358.3 million and \$398.9 million, respectively.

Grants—Sound Transit participates in several federal grant programs that are governed by various rules and regulations of the grantor agencies. Costs charged to the respective grant programs are subject to audit and adjustment by the grantor agencies; therefore, to the extent that Sound Transit has not complied with the rules and regulations governing the grants, refunds of any money received may be required and the collectibility of any related receivable at December 31, 2008 and 2007 may be impaired. In the opinion of management, there are no significant contingent liabilities relating to non-compliance with the rules and regulations governing the respective grants; therefore, no provision has been recorded in the accompanying financial statements for such contingencies.

Claims—In the ordinary course of business, Sound Transit has been named as a defendant in a number of lawsuits relating to personnel and contractual matters. Although the ultimate outcome, if any, of these matters is presently unknown, management has evaluated all claims and potential claims and where that exposure is probable, has reflected in the accounts of the Agency its best estimate. At December 31, 2008, \$52.0 million has been recorded in construction in progress and a corresponding liability accrued (\$49.0 million at December 31, 2007); however, as these are estimates, these amounts may be subject to change.