



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

*Financial Statements for the
Years Ended December 31, 2003 and 2002, and
Independent Auditors' Report*

TABLE OF CONTENTS

Statement of Management's Responsibility	i
Independent Auditors' Report	iii
Management's Discussion and Analysis	1
Basic Financial Statements	
Balance Sheets.....	11
Statements of Revenues, Expenses and Changes in Net Assets	12
Statements of Cash Flows.....	13
Notes to Financial Statements	15

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

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 judgements, 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 2003 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



Hugh L. Simpson
Chief Financial Officer



Kelly Priestley
Controller

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KPMG LLP
Suite 900
801 Second Avenue
Seattle, WA 98104

Independent Auditors' Report

Audit and Reporting Subcommittee of the Board
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 of Sound Transit as of and for the year ended December 31, 2003, 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 audit. The accompanying basic financial statements of Sound Transit as of and for the year ended December 31, 2002, were audited by other auditors whose report thereon dated April 24, 2003, expressed an unqualified opinion, which report included an explanatory paragraph that described a change in accounting principle on those statements.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the 2003 financial statements referred to above present fairly, in all material respects, the financial position of Central Puget Sound Regional Transit Authority as of December 31, 2003, and the changes in its financial position and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report dated April 23, 2004 on our consideration of Central Puget Sound Regional Transit Authority internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

The management's discussion and analysis on pages 1 through 10 is not a required part of the financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

KPMG LLP

April 23, 2004



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MANAGEMENT'S DISCUSSION AND ANALYSIS

For the years ended December 31, 2003 and 2002

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, 2003 and 2002. 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 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 ("Regional Express"). The implementation of the initial phase of the voter-approved regional transportation system ("*Sound Move*") is scheduled for a 13-year period, ending in 2009. The agency is seven years into this initial phase and its activities to date have been concentrated on implementing service in all three lines of business and on the design, environmental review and initial construction of Sound Transit's capital projects.

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. As the agency has not reached its full service levels and has not yet entered construction on all of its major projects, major sources of revenue exceed expenses and capital outlays, resulting in a rising net assets position.

Financial Highlights

- Total operating revenues were \$15.0 million for 2003, an increase of 31.6% from the prior year. Passenger fares increased by \$2.4 million from the prior year, as a result of the impact of full-year service increases on the Sounder and Regional Express service as well as higher ridership numbers on Regional Express. Other revenues increased by \$1.2 million relating to leasing additional excess revenue vehicles and a higher number of temporary property rentals related to increased land purchase activity.
- Total operating expenses, excluding depreciation, increased by \$6.5 million or 8.9% from the prior year. Operations and maintenance expenses increased by \$9.4 million. This increase is due to the higher service levels provided in 2003 and the commencement of the no-fare Tacoma Link service in August of 2003. General and administrative expenses decreased by \$2.9 million as more costs were able to be capitalized to projects in 2003. General and administrative expenses before overhead allocation to projects increased by \$3.8 million primarily due to hiring additional full-time equivalent employees as the agency staffed up for increased project activity.
- Non-operating revenues (expenses) decreased by \$17.4 million or 5.7% from the prior year. This decrease is attributable to lower investment income of \$22.9 million, reflecting declining interest rates and the maturing of high rate investments, partially offset by higher tax revenues of \$5.0 million.

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Management's Discussion and Analysis, continued

- Contributions decreased by \$16.2 million or 35.8%. This decrease is due to lower federal capital contributions of \$51.2 million, offset by lower contributions to other governments. Grant contributions in 2003 did not include further appropriations for the Link full-funding grant agreement, while 2002 included an accrual of \$39.5 million of the \$50.0 million Link New Starts funding which was awarded in 2002. In 2003, \$4.4 million in contributions were made to other public agencies, while in 2002 such contributions were \$42.5 million.
- Total net assets at December 31, 2003 were \$1.9 billion, an increase of \$237 million or 14.5% from 2002, as compared to an increase of \$277 million or 20.3% from 2001. The lower increase in net assets in 2003 from 2002 reflects the higher loss from operations of \$6 million, lower investment revenues of \$23 million and the lower contributions of \$16 million.
- Total capital assets, net of depreciation, were \$1.4 billion at December 31, 2003, an increase of \$384 million or 39.0% from 2002. The increase in total capital assets reflects increased land and right of way acquisitions, the most significant of which includes the acquisition of the first of four easements in the Seattle-to-Everett corridor, receipt of the vehicles under the lease agreement with Peninsula Corridor Joint Powers Board ("CalTrain") and an increase in capital projects in progress. Approximately \$161 million in projects, excluding the Seattle-to-Everett corridor easement, were completed during the year and transferred to depreciable assets.

Overview of the Financial Statements

Sound Transit's financial statements are prepared in conformity with accounting principles generally accepted in the United States of America ("GAAP") as applied to government units. The 2003 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, 2003 were \$1.9 billion, an increase of \$237 million or 14.5% from 2002 (see Table A-1). Total assets also increased \$237 million or 11.3%, with total liabilities comparable to 2002, funded through a reduction in current and restricted assets and an excess of revenues over expenses.

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	
	2003	2002	2001	2003 - 2002	2002 - 2001
Current assets, excluding restricted assets	\$ 691.8	\$ 792.9	\$ 686.1	(12.8)	15.6
Restricted assets	217.9	265.8	305.5	(18.0)	(13.0)
Capital assets	1,367.0	983.4	791.5	39.0	24.2
Other non-current assets	<u>69.2</u>	<u>66.4</u>	<u>62.2</u>	<u>4.2</u>	<u>6.8</u>
Total Assets	2,345.9	2,108.5	1,845.3	11.3	14.3
Current liabilities, excluding interest payable from restricted assets	54.3	55.3	72.0	(1.8)	(23.2)
Interest payable from restricted assets	7.2	7.2	7.2	-	-
Long-term debt	347.4	347.5	348.9	(0)	(0)
Other long-term liabilities	<u>58.2</u>	<u>57.1</u>	<u>52.9</u>	<u>1.9</u>	<u>7.9</u>
Total Liabilities	467.1	467.1	481.0	(0.0)	(2.9)
Net Assets					
Invested in capital assets, net of related debt	1,022.5	639.0	447.3	60.0	42.9
Restricted net assets	210.7	258.7	298.4	(18.6)	(13.3)
Unrestricted net assets	<u>645.6</u>	<u>743.7</u>	<u>618.6</u>	<u>(13.2)</u>	<u>20.2</u>
Total Net Assets	<u>\$ 1,878.8</u>	<u>\$ 1,641.4</u>	<u>\$ 1,364.3</u>	14.5	20.3

Current assets, excluding restricted assets, decreased in 2003 by 12.8% from 2002. This decrease reflects payment to Burlington Northern and Santa Fe ("BNSF") for the purchase of the first of four easements in the Seattle-to-Everett corridor, lower accruals for grant contributions and a decrease in lease contract receivable with the receipt by Sound Transit of the cab and coach cars under the lease agreement with CalTrain. In 2002, current assets increased by 15.6% from 2001 due to the accrual of \$39 million in Link New Starts funding and an increase in lease contract receivable with the delivery to CalTrain of the remaining 15 cab and coach cars.

Restricted assets decreased in 2003 by 18.0% from 2002, as payments for construction costs were applied against the investment restricted under contractual agreement with BNSF and state funds restricted for use for commuter rail in Snohomish County were utilized for the BNSF easement acquisition. In 2002, restricted assets decreased by 13.0% related to payments to BNSF.

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Management's Discussion and Analysis, continued

Capital assets increased in 2003 by \$383.6 million from 2002, as compared to an increase of \$191.9 million in 2002 from 2001, reflecting Sound Transit's increased capital program activity as more projects move from design to construction. During the year, Sound Transit capitalized \$371.1 million (\$274.6 million in 2002) in design, construction, acquisition, interest and overhead costs to capital projects in progress and \$243.7 million (\$250.1 million in 2002) in projects were completed and transferred to property, plant and equipment or expensed as follows:

(in millions)

	2003	2002
Transferred to property, vehicles and equipment	\$ 239.9	\$ 174.8
Expensed to contributions to other governments	1.9	41.5
Delivered to CalTrain under capital lease	-	26.7
Transferred to inventory	0.9	1.7
Write-off of overhead, discontinued project costs and loss on disposal of excess materials	1.0	5.4
	<u>\$ 243.7</u>	<u>\$ 250.1</u>

Direct additions, net of disposals, to either property, vehicles or equipment were \$33.9 million (\$6.4 million in 2002), which included delivery to Sound Transit of \$32.4 million in replacement vehicles under the CalTrain lease agreement. Direct additions in 2002 included a \$6.5 million contribution of property from Microsoft Corporation. Offsetting the increase in capital spending, accumulated depreciation increased in 2003 by \$17.6 million from 2002, and by \$13.8 million in 2002 from 2001, reflecting the increased assets put into use.

Current liabilities in 2003, excluding interest payable from restricted assets, are comparable to 2002, decreasing by 1.8%, however 2002 decreased by 23.2% from 2001. The decrease in 2002 from 2001 reflected prompter payments to suppliers, contractors and other governmental agencies. Long-term debt also remains substantially unchanged from 2002 and 2001. Principal payments on the outstanding bonds do not commence until 2006. The increase in other long-term liabilities is due to the lease/leaseback transaction and is offset by an equal increase in the investment held to settle this obligation included in other non-current assets. More detailed information about Sound Transit's long-term liabilities is presented in Notes 9 and 10 to the Financial Statements.

Investment in capital assets, net of related debt represents 54.4% of Sound Transit's total net assets in 2003, 38.9% in 2002 and 32.8% in 2001. The increase in capital asset investment reflects the continued construction of Sound Transit's infrastructure assets for its commuter rail, light rail and express bus system. Sound Transit uses these assets to provide service and consequently these assets are not available to liquidate liabilities or for other expenditures.

Restricted net assets represent 11.2% and unrestricted 34.4% of net assets respectively in 2003, 15.8% and 45.3% in 2002; and 21.9% and 45.3% in 2001. The unrestricted and substantially all of the restricted net assets are available for future expenditures associated with construction projects planned for in *Sound Move*. The decline in the relative proportion of restricted and unrestricted net assets as a percent of total net assets is anticipated as infrastructure assets are constructed.

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Management's Discussion and Analysis, continued

Changes in Net Assets

The increase in net assets in 2003 was \$237.4 million, which was \$39.7 million or 14.3% less than the increase in net assets from 2002 (see Table A-2). The increase in net assets in 2002 of \$277.1 million was \$42.7 million or 13.4% less than the increase in net assets in 2001 of \$319.8 million. Sound Transit's loss from operations increased by 8.0% in 2003 from 2002 and 12.9% in 2002 from 2001 and capital contributions decreased by 35.8% in 2003 from 2002 and 26.0% in 2002 from 2001. In addition, non-operating revenues and expenses decreased by 5.7% and 5.6% from 2002 and 2001 respectively.

The increase in the loss from operations reflects an increase in operating revenues of 31.6% in 2003 from 2002 and 14.0% in 2002 from 2001, however this was more than offset by total operating expenses which increased 11.1% in 2003 from 2002 and 13.0% in 2002 from 2001.

Table A-2

Changes in Sound Transit Net Assets

<i>(in millions)</i>	As of December 31,			% Change	
	2003	2002	2001	2003 - 2002	2002 - 2001
Operating Revenues					
Passenger fares	\$ 11.6	\$ 9.2	\$ 8.8	26.1	4.5
Other	3.4	2.2	1.2	54.5	83.3
Total Operating Revenues	15.0	11.4	10.0	31.6	14.0
Operating Expenses					
Total operating expenses before depreciation	79.6	73.1	66.6	8.9	9.8
Depreciation	17.6	14.4	10.8	22.2	33.3
Total operating expenses	97.2	87.5	77.4	11.1	13.0
Loss from operations	(82.2)	(76.1)	(67.4)	8.0	12.9
Non-operating revenues (expenses)	290.5	307.9	326.0	(5.7)	(5.6)
Income before capital contributions	208.3	231.8	258.6	(10.1)	(10.4)
Capital contributions	29.1	45.3	61.2	(35.8)	(26.0)
Change in Net Assets	237.4	277.1	319.8	(14.3)	(13.4)
Total net assets, beginning	1,641.4	1,364.3	1,044.5	20.3	30.6
Total Net Assets, ending	\$ 1,878.8	\$ 1,641.4	\$ 1,364.3	14.5	20.3

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

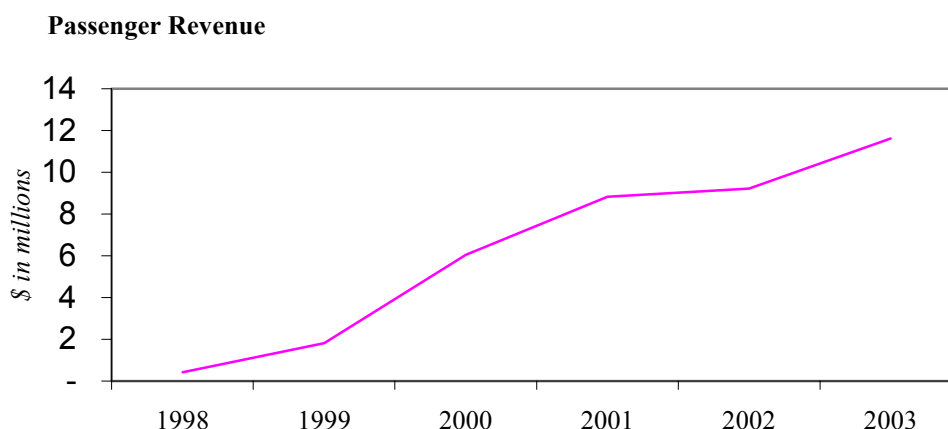
Management's Discussion and Analysis, continued

Operating Revenues

Operating revenues are composed of passenger fares and other revenues.

Passenger Fare Revenue

Passenger fare revenue consists of fares earned from the sale of Puget passes, Sounder tickets and bus farebox receipts and tickets utilized during the year by riders on Sounder and Regional Express.



Sounder rail passenger revenue increased \$267 thousand or 17.0% over 2002 (\$197 thousand or 14.3% in 2002 over 2001), with ridership increasing by 110 thousand boardings in 2003 over 2002 and 94 thousand boardings in 2002 over 2001. Regional Express bus passenger revenue increased by \$2.1 million or 27.9% over 2002 (\$207 thousand or 2.8% in 2002 over 2001), with ridership increasing by 977 thousand boardings in 2003 over 2002 and 752 thousand boardings in 2002 over 2001. In addition to ridership increases, the average fare per boarding increased by \$0.13 in 2003 from 2002 and 2001.

Contributing to the increased ridership was the full-year impact of the additional Sounder Seattle-to-Tacoma train and additional Regional Express routes serving Woodinville to Seattle and Tacoma to the University District, which began in September 2002. Additional ridership in Regional Express is also attributable to service implementation changes in September 2003, whereby Regional Express discontinued a low ridership route serving Everett to Northgate, replacing it with expanded rush hour service covering the same stops. Starting in August 2002, Tacoma Link commenced operations, a free fare service. Sounder also commenced service from Seattle to Everett in late December. This service was provided at no cost until February 1, 2004. Ridership numbers are presented in the following table.

Ridership (in thousands)	% Increase				
	2003	2002	2001	2003 - 2002	2002 - 2001
Sounder	751.2	641.0	547.3	17.2	17.1
Link	266.8	-	-	100.0	-
Regional Express	7,399.9	6,423.3	5,671.2	15.2	13.3
Total Ridership	8,417.9	7,064.3	6,218.5	19.2	13.6

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Management's Discussion and Analysis, continued

Other Revenues

Other revenues consist of vehicle advertising, rental of equipment and facilities and other miscellaneous. The increase in other revenues of \$1.2 million in 2003 over 2002 (\$1.0 million in 2002 over 2001) is due to the leasing of additional Sounder vehicles in 2003 and additional income from short-term property rentals from land acquired for capital projects. The increase in other revenues in 2002 over 2001 reflects the full-year impact in 2002 of vehicles leased in 2001.

Operating Expenses

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

Operations and Maintenance

Operations and maintenance, which increased by \$9.4 million or 18.5% from 2002 (\$3.7 million or 7.9% in 2002 over 2001), includes costs associated with the operation of the Sounder commuter rail, Link light rail in Tacoma and Regional Express bus services. Major expense categories are services, materials, supplies, utilities, insurance, taxes, 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. It is the most significant component of operations and maintenance, accounting for 72% of this category (73% in 2002 and 2001).

As a result of increased service levels in Sounder and Regional Express in 2003, purchased transportation costs increased by \$6.3 million, or 17%, and \$2.9 million in related service payments. In addition, Tacoma Link light rail went into service at the end of August, resulting in a \$1.6 million increase over 2002. Direct operations and maintenance costs were partially offset by lower allocated agency staff overhead due to increased capital spending over operations in 2003. The increase in operations and maintenance in 2002 from 2001 also related to service level increases.

General and Administrative

General and administrative expenses, which decreased in 2003 by \$2.9 million, or 12.9%, from 2002 and increased in 2002 by \$2.8 million, or 14.9%, from 2001, 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.

Total agency staff and administrative costs before allocation to capital projects and operations increased in 2003 by \$3.8 million or 9.3% from 2002, however were comparable between 2002 and 2001. The increase in 2003 general and administrative costs, before allocations, related to higher salary and benefit costs of \$4.1 million as the agency added staff with respect to increased activity in its capital program and operations. Payments to other transit agencies under the Regional Fare Integration Program decreased by \$1 million in 2003 from 2002 while insurance costs increased by \$301 thousand and advertising by \$396 thousand, reflecting increased agency activity. Taxes also were down \$357 thousand as 2002 included \$375 thousand in arbitrage costs related to the Sales Tax and Motor Vehicle Excise Tax Bonds, Series 1999.

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Management's Discussion and Analysis, continued

General and administrative costs are allocated to capital projects and transit operations based on activity drivers and relative level of spending. Costs allocated to capital projects in 2003 were \$22.6 million, up \$3.9 million from \$18.7 million in 2002, which were down \$5.0 million from 2001. Costs allocated to transit operations and maintenance in 2003 were \$3.4 million, down \$1.3 million from \$4.7 million in 2002, which was up \$3.0 million from 2001. Also impacting general and administrative costs is any write-off of overhead from projects. As projects approach completion, allocated overhead costs are reviewed and any excess costs are written off. In 2003, \$704 thousand in excess costs were written off, \$4.7 million in 2002 and \$3.4 million in 2001.

Depreciation

Depreciation expense increased in 2003 by \$3.2 million or 22.2% from 2002 (\$3.6 million or 33.3% in 2002 from 2001), reflecting the increase in depreciable assets put into use in 2003 and 2002. As projects are completed and put into use, the costs of these assets are amortized over their expected useful lives.

Non-Operating Revenues (Expenses)

Non-operating revenues decreased in 2003 by \$17.4 million or 5.7% from 2002. This decrease is attributable to \$22.9 million in lower investment income, reflecting the lower interest rate environment in 2003 and the net decrease in fair value of investments of \$6.6 million. Offsetting the decrease in investment income were higher tax revenues of \$5.0 million, or 1.9%. In 2002, non-operating revenues decreased by \$18.1 million, or 5.6%, from 2001 due to lower investment earnings and tax revenues reflecting the decline in general economic conditions and falling interest rates. In addition, the year 2001 included a one time gain of \$4.9 million on the lease/leaseback transaction described in Note 7 to the Financial Statements.

Capital Contributions

Capital contributions decreased in 2003 by \$16.2 million or 35.8% from 2002 and by \$15.9 million or 26.0% in 2002 from 2001. 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 improvements or funding agreements. The decrease in capital contributions between 2003 and 2002 relates to significantly lower federal capital contributions in 2003, down \$51.2 million from 2002, offset by lower capital contributions to other governments of \$38.1 million. The decrease in capital contributions between 2002 and 2001 relates to the \$42.5 million in contributions to other governments in 2002, offset by higher federal and local capital contributions in 2002, up \$31.5 million from 2001.

Federal capital contributions in 2002 included the accrual of \$39.5 million of the \$50.0 million Link New Starts funding, which was awarded in 2002. No further appropriations under the Link full-funding grant agreement were made in 2003. Capital contributions to other governments are significantly impacted by the timing of completion of related projects. In 2002 several large projects were completed, including the Lynnwood SR-99 Transit Lanes, the Pacific Avenue Overpass, I-90 @ Sunset and the Tacoma Dome Park-and-Ride expansion, whereas in 2003 and 2001 no significant non-Sound Transit-owned projects were completed.

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Management's Discussion and Analysis, continued

Capital Assets

At December 31, 2003, Sound Transit had invested \$1.4 billion in capital assets, net of accumulated depreciation, of which \$437 million of depreciable assets are in service (\$293 million in 2002 and \$214 million in 2001). This represents a net increase of \$144 million or 49.1% over 2002 (\$79 million or 36.9% in 2002 over 2001).

Table A-3

Sound Transit Capital Assets (net of depreciation)

(in millions)	As of December 31,			% Change	
	2003	2002	2001	2003 - 2002	2002 - 2001
Land	\$ 250.9	\$ 121.5	\$ 19.6	106.5	519.9
Capital projects in progress					
Sound Transit	625.0	554.8	503.8	12.7	10.1
Other Governments	104.9	47.7	74.2	119.9	(35.7)
Total Non-Depreciable Assets	980.8	724.0	597.6	35.5	21.2
Buildings & transit facilities	211.7	116.1	71.3	82.3	62.8
Revenue vehicles	171.0	138.8	116.7	23.2	18.9
Equipment, vehicles & other	3.5	4.5	5.9	(22.2)	(23.7)
Total Depreciable Assets	386.2	259.4	193.9	48.9	33.8
Total Net Capital Assets	\$ 1,367.0	\$ 983.4	\$ 791.5	39.0	24.2

Land increased by \$129.4 million in 2003 from 2002, substantially due to the acquisition from BNSF of the first easement in the Seattle-to-Everett corridor for \$79.0 million. Other significant land additions include purchases for the Central Link segment for \$33.2 million, Sounder Everett Station for \$6.7 million and Regional Express Federal Way Transit Center for \$5.6 million. In 2002, land increased by \$101.9 million from 2001, substantially related to the transfer of land from capital projects in progress, including land acquired for Central Link, North Link and Lynnwood Transit Center Park-and-Ride and High Occupancy Vehicle (HOV) Direct Access, as well as a \$6.5 million contribution of land from Microsoft.

Buildings and transit facilities increased by \$95.6 million in 2003 from 2002 due to the completion of Tacoma Dome Station, Tacoma Light Rail Operations and Maintenance Center, Lynnwood Transit Center and DuPont Station. In 2002, buildings and transit facilities increased by \$44.8 million due to the completion of the Auburn and Kent parking garages, as well as the Overlake and Bellevue Transit Centers.

Revenue vehicles increased by \$32.2 million in 2003 from 2002 with the delivery of the replacement cab and coach cars under the CalTrain lease agreement and the delivery of the light rail vehicles for the Tacoma light-rail service. The increase of \$22.1 million in 2002 from 2001 reflects the balance of the delivery of the Sounder vehicles for Phase 1 of *Sound Move*, less those sold and to be replaced under the CalTrain lease agreement.

Equipment, vehicles and other decreased by \$1.0 million in 2003 from 2002 and \$1.4 million in 2002 from 2001 related to depreciation in excess of additions. This category includes office furniture and equipment, as well as agency administrative vehicles.

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Management's Discussion and Analysis, continued

Major capital project activities in 2003 included: in Sounder, track and signal projects (Seattle to Auburn, Auburn to Tacoma Dome, Tacoma Dome to Lakewood and Seattle to Everett); in Link, the Central Line (CPS to 154th, Beacon Hill Tunnel, South Walden St. to South Morgan, 126th St. to 150th St.) and Link Tacoma Link; and in Regional Express, the Lynnwood Transit Center, the Federal Way Transit Center, the Lynnwood HOV Access and the Bellevue HOV Access. In 2002, major project activities in Sounder included: track and signal improvements on all segments; in Link, the operations and maintenance base, as well as Tacoma Line, Link E-3 bus way and Beacon Hill Tunnel; and in Regional Express, the Bellevue and Overlake Transit Centers.

More detailed information about Sound Transit's capital assets is presented in Note 6 to the Financial Statements.

Long-Term Debt

Long-term debt includes sales and motor vehicle excise tax bonds issued in 1999. At December 31, 2003 Sound Transit had \$350 million par value bonds issued and outstanding. These bonds have been rated as A1 by Moody's Investor Services, Inc. and AA by Standard & Poors.

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 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 2001 assessed valuations for collection of 2002 taxes, Sound Transit's non-voted remaining debt capacity is \$3.4 billion and its voted remaining debt capacity is \$12.1 billion.

Economic Factors

With Sound Transit moving into heavy construction over the next four years, it is closely monitoring the current steel price volatility. The average cost of domestic steel has increased by 70% over the last six months. With increasing world demand and short supplies, steel prices are expected to increase and eventually stabilize, but not revert to 2003 market prices. The value of steel in agency construction projects ranges from 4% to 12%. Currently, there are adequate unallocated contingencies included in project budgets for price fluctuations and adequate schedule contingencies to address potential delivery delays.

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

BALANCE SHEETS

<i>(in thousands)</i>	December 31	
	2003	2002
ASSETS		
Current Assets		
Cash and cash equivalents <i>(Note 3)</i>	\$ 358,144	\$ 326,443
Restricted assets <i>(Note 3)</i>	9,674	6,687
Investments <i>(Note 3)</i>	263,926	330,383
Taxes and other receivables <i>(Note 4)</i>	62,231	96,555
Current portion, lease contract receivable <i>(Note 5)</i>	-	32,386
Parts, materials and supplies	2,632	2,404
Prepaid expenses	4,858	4,679
Total Current Assets	<u>701,465</u>	<u>799,537</u>
Non-Current Assets		
Capital assets, net of accumulated depreciation <i>(Note 6)</i>	1,367,005	983,380
Restricted assets <i>(Note 3)</i>	208,189	259,156
Investment held to pay capital lease obligation <i>(Note 7)</i>	56,657	55,542
Advances receivable	95	-
Unamortized bond issuance costs	2,893	3,080
Prepaid expense and deposits	9,585	7,778
Total Non-Current Assets	<u>1,644,424</u>	<u>1,308,936</u>
Total Assets	<u>\$ 2,345,889</u>	<u>\$ 2,108,473</u>
LIABILITIES AND EQUITY		
Current Liabilities		
Accounts payable and accrued liabilities <i>(Note 8)</i>	\$ 50,148	\$ 50,361
Deferred pass revenue	1,865	537
Interest payable from restricted assets	7,152	7,152
Current portion, capital lease obligation <i>(Note 7)</i>	109	73
Current portion, deferred lease revenue <i>(Note 5)</i>	-	1,125
Other	2,172	3,249
Total Current Liabilities	<u>61,446</u>	<u>62,497</u>
Non-Current Liabilities		
Long-term debt <i>(Note 9)</i>	347,391	347,452
Compensated absences <i>(Note 10)</i>	1,463	1,492
Capital lease obligations <i>(Note 7)</i>	56,748	55,628
Total Non-Current Liabilities	<u>405,602</u>	<u>404,572</u>
Total Liabilities	<u>467,048</u>	<u>467,069</u>
Commitments and Contingencies <i>(Notes 7, 13 and 14)</i>		
Net Assets		
Invested in capital assets, net of related debt	1,022,507	639,008
Restricted for contractual arrangements and other <i>(Note 11)</i>	210,712	258,691
Unrestricted	645,622	743,705
Total Net Assets	<u>1,878,841</u>	<u>1,641,404</u>
Total Liabilities and Net Assets	<u>\$ 2,345,889</u>	<u>\$ 2,108,473</u>

See Notes to Financial Statements.

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS

<i>(in thousands)</i>	December 31	
	2003	2002
Operating Revenues		
Passenger fares	\$ 11,625	\$ 9,225
Other operating revenues	3,403	2,146
Total Operating Revenues	15,028	11,371
Operating Expenses		
Operations and maintenance	60,423	51,006
General and administrative	19,274	22,131
Depreciation	17,570	14,352
Total Operating Expenses	97,267	87,489
Loss from Operations	(82,239)	(76,118)
Non-Operating Revenues (Expenses)		
Sales tax	206,665	204,566
Motor vehicle excise tax	61,189	58,319
Rental car tax	2,182	2,151
Investment income	20,020	42,923
Capital lease and other revenues	1,173	802
Interest expense	(203)	(199)
Discontinued projects	(106)	(660)
Loss on disposal of assets	(369)	-
Total Non-Operating Revenues	290,551	307,902
Income Before Capital Contributions	208,312	231,784
Contributions to other governments	(4,443)	(42,536)
Federal capital contributions	26,879	78,088
Other capital contributions	6,689	9,754
Total Capital Contributions	29,125	45,306
Change in Net Assets	237,437	277,090
Total Net Assets, Beginning of Year	1,641,404	1,364,314
Total Net Assets, End of Year	\$ 1,878,841	\$ 1,641,404

See Notes to Financial Statements.

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

STATEMENTS OF CASH FLOWS

<i>(in thousands)</i>	December 31	
	2003	2002
Cash Flows from Operating Activities		
Cash receipts from fares	\$ 12,310	\$ 7,659
Cash receipts from other operating revenues	2,685	2,343
Payments to suppliers	(19,828)	(23,089)
Payments to transportation service providers	(42,214)	(27,910)
Payments to employees for wages and benefits	(17,680)	(16,524)
Net Cash Used by Operating Activities	(64,727)	(57,521)
Cash Flows from Non-Capital Financing Activities		
Taxes received	269,833	264,743
Net Cash Provided by Non-Capital Financing Activities	269,833	264,743
Cash Flows from Capital and Related Financing Activities		
Capital contributions from grants	70,345	59,993
Contribution to other governments	(2,567)	(1,000)
Purchase of properties, vehicles and equipment	(1,346)	(6,970)
Payments for capital projects in progress	(341,152)	(262,905)
Payments to employees capitalized to capital projects in progress	(10,573)	(8,604)
Cash paid for interest	(17,180)	(17,176)
Payments for owner-controlled insurance program	-	(10,550)
Deposit for land	(4,400)	-
Payments for betterments, net of repayments	(1,855)	-
Other	(223)	(89)
Net Cash Used by Capital and Related Financing Activities	(308,951)	(247,301)
Cash Flows from Investing Activities		
Purchases of investments	(379,994)	(243,586)
Proceeds from sales or maturities of investments	497,845	293,705
Investment income	29,105	45,222
Net Cash Provided by Investing Activities	146,956	95,341
Net Increase in Cash and Cash Equivalents	43,112	55,262
Cash and Cash Equivalents		
Beginning of year	352,904	297,642
End of Year	\$ 396,016	\$ 352,904
Cash and Cash Equivalents (Note 3)		
Unrestricted	\$ 358,144	\$ 326,443
Current restricted	2,882	-
Non-current restricted	34,990	26,461
	\$ 396,016	\$ 352,904

See Notes to Financial Statements.

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

STATEMENTS OF CASH FLOWS, *continued*

<i>(in thousands)</i>	December 31	
	2003	2002
Loss from Operations	\$ (82,239)	\$ (76,118)
Adjustments to Reconcile Loss from Operations to Net Cash Used by Operating Activities		
Depreciation	17,570	14,352
Loss (gain) on disposal of capital assets	-	16
Changes in Operating Assets and Liabilities		
Decrease in accounts receivable	120	196
(Increase) decrease in due from other governments	(1,499)	829
Decrease (increase) in materials, parts and supplies	543	(720)
(Increase) in prepaid expenses	(173)	(33)
(Decrease) in accounts payable and accrued liabilities	(2,123)	(3,365)
Increase in salaries, wages and benefits	540	361
Increase in deferred fare pass revenue	1,327	62
Increase in due to other governments	1,319	6,899
Decrease in loss fund	(112)	-
Net Cash Used by Operating Activities	<u>\$ (64,727)</u>	<u>\$ (57,521)</u>

<i>(in thousands)</i>	December 31	
	2003	2002
Supplemental Disclosures of Non-Cash Operating, Investing and Financing Activities		
Transfer of assets under lease contract receivable	\$ 32,386	\$ (29,732)
Capital contributions to other governments	(1,876)	(41,536)
Interest income from investments held to pay capital leases	1,115	2,917
Deferred lease revenue earned during the year	1,125	802
Deferred lease revenue recognized on assets transferred under lease contract receivable	-	1,650
Interest expense on capital leases	(1,115)	(2,917)
Decrease in fair value of investments	(6,656)	(974)

See Notes to Financial Statements.

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

NOTES TO FINANCIAL STATEMENTS YEARS ENDED DECEMBER 31, 2003 AND 2002

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 (“Regional Express”).

Reporting Entity—Sound Transit is a special purpose government supported primarily through sales taxes, state motor vehicle excise taxes and rental car taxes in Sound Transit’s operating jurisdiction. In addition Sound Transit receives capital funding from federal and state 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 revenues and a motor vehicle excise tax. These taxes are collected on Sound 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 and are recognized in the period in which services are provided and are earned; expenses are recognized in the period in which they are incurred. All assets and liabilities associated with the operation of Sound Transit are

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Notes to Financial Statements, continued

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. Upon disposal of capital assets, the accounts are relieved of the related costs and accumulated depreciation and the resulting gains or losses are reflected in the Statements of Revenues, Expenses and Changes in Net Assets. 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 lease, as follows:

	Estimated Useful Life
Buildings	30 years
Transit facilities and equipment	12–30 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

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.

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.

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, money market funds, 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 has been accrued in the accompanying financial statements. 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% upon resignation, retirement or death; however, is limited to 120 days for termination other than retirement or death.

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Notes to Financial Statements, continued

Contributions to Other Governments—Pursuant to capital improvement agreements, Sound Transit has provided funding to or constructed assets for various governments 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 put into use, at which time it is charged to contributions to other governments.

Environmental Reserves—Environmental liabilities are evaluated at the time of purchase of land and are factored into the purchase price. The estimated cost of remediation is accrued at the time of purchase and relieved as remediation costs are incurred.

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

Operating and Contingency Fund—In accordance with Board policy, Sound Transit maintains a cash reserve based on two months of average annual operating expenses, to be used in the event of budget shortfalls. As this is an internally-restricted cash balance, this balance is included in cash and cash equivalents.

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.

Restricted Assets—Restricted assets are assets restricted by the covenants of long-term financial arrangements. Restricted assets are used in accordance with their requirements and where both restricted and unrestricted resources are available for use, restricted resources are used first and then unrestricted resources as they are needed.

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. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

Reclassifications—Certain reclassifications have been made to the 2002 Financial Statements to conform to the current year's presentation.

Risk Management—Risks of loss related to tort; theft of, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters are accrued at estimated award or settlement when it is probable that an asset has been impaired or a liability has been incurred and the amount of the loss can be reasonably estimated.

Subarea Accounting—Sound Transit allocates equity to each of the included jurisdictions in accordance with *Sound Move* and established policies. Presentation of such allocation is not a required disclosure under accounting principles generally accepted in the United States of America. Accordingly, a separate unaudited report and Schedule of Subarea Equity is issued.

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.

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Notes to Financial Statements, continued

New Accounting Pronouncements—

Deposit and Investment Risk Disclosures: In March 2003, the GASB issued Statement No. 40, with an effective date for periods beginning after June 15, 2004. This statement requires governments to present certain disclosures that address common deposit and investment risks related to credit risk, concentration of credit risk, interest rate risk and foreign currency, as well as certain disclosures of investments that have fair values that are highly sensitive to changes in interest rates and requires disclosures of deposit and investment policies related to the risk identified. Sound Transit is currently in the process of evaluating the impact that will result from adopting GASB Statement No. 40 and intends to implement early for the year ended December 31, 2004.

Accounting for Impairment of Capital Assets: In November 2003, the GASB issued Statement No. 42, with an effective date for periods beginning after December 15, 2004. This statement establishes for governments accounting and financial reporting standards for the impairment of capital assets. Sound Transit is currently in the process of evaluating the impact that will result from adopting GASB Statement No. 42 and intends to implement early for the year ended December 31, 2004.

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") and are considered Category 1. 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, together with the qualified money market mutual fund, represent an interest in a group of securities and have no specific security subject to custodial risk and are considered uncategorized.

All short-term cash surplus is invested in accordance with an investment policy certified by the Municipal Treasurer's Association and as required by state law. Qualifying investments include obligations of the United States government, treasury and agency securities, banker's acceptances, certificates of deposit, commercial paper and repurchase agreements.

Sound Transit's investments are categorized to give an indication of the level of custodial credit risk assumed by Sound Transit at December 31, 2003 and 2002. Category 1 includes investments that are insured or registered or for which the securities are held by Sound Transit or its agent, in Sound Transit's name. All of Sound Transit's investments are considered Category 1.

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Notes to Financial Statements, continued

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

<i>(in thousands)</i>	2003		2002	
	Cost	Fair Value	Cost	Fair Value
Categorized Deposits and Investments				
US agency securities	\$ 389,895	\$ 391,575	\$ 298,661	\$ 303,726
US treasury securities	29,973	30,114	20,141	20,355
Certificates of deposits	13,000	13,000	13,000	13,000
Taxable municipal bonds	1,250	1,278	1,250	1,302
Repurchase agreement	-	-	220,572	220,572
FDIC or PDIC insured bank deposits	30,299	30,299	4,687	4,687
	464,417	466,266	558,311	563,642
Uncategorized Cash and Cash Equivalents				
King County Investment Pool	314,900	316,033	285,220	289,527
Washington State Local Government Investment Pool	44,621	44,621	53,553	53,553
Qualified money market fund	5,014	5,014	5,062	5,062
Cash on hand	49	49	75	75
	364,584	365,717	343,910	348,217
Other Restricted Assets				
Deductible liability protection policy	6,792	6,792	6,687	6,687
Interest receivable on restricted investments	1,158	1,158	4,123	4,123
	7,950	7,950	10,810	10,810
Total Cash, Cash Equivalents, Investments and Other Restricted Assets	\$ 836,951	\$ 839,933	\$ 913,031	\$ 922,669
Balance Sheet Classifications:				
Cash and cash equivalents		\$ 358,144		\$ 326,443
Current restricted assets:				
Cash equivalents		2,882		-
Deductible liability protection policy		6,792		6,687
		9,674		6,687
Investments		263,926		330,383
Non-current restricted assets:				
Cash equivalents		34,990		26,461
Investments		172,041		228,572
Other assets		1,158		4,123
		208,189		259,156
		\$ 839,933		\$ 922,669

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Notes to Financial Statements, continued

4. RECEIVABLES

Receivables consist of the following:

<i>(in thousands)</i>	December 31	
	2003	2002
Taxes receivable	\$ 42,393	\$ 42,191
Grants receivable	4,282	46,183
Accounts receivable*	5,545	177
Due from Other Governments	6,382	3,393
Interest receivable	3,629	4,611
	<u>\$ 62,231</u>	<u>\$ 96,555</u>

*Net of allowance for doubtful accounts of \$21 thousand (\$2 thousand in 2002).

Amounts due from other governments include amounts due under the Puget Pass regional fare program, amounts reimbursable under interlocal agreements for operating expense 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.

5. LEASE CONTRACT RECEIVABLE

On December 4, 2001, Sound Transit entered into a lease transaction with the Peninsula Corridor Joint Powers Board ("CalTrain") for 17 commuter rail passenger cab and coach cars. The lease term was for 18 months and included an option to purchase all 17 of the vehicles. The purchase option was exercised by CalTrain and the purchase price of \$32.4 million was deposited into an escrow account. All payments to Sound Transit were applied to the purchase of replacement vehicles. CalTrain received title to the vehicles as Sound Transit received the replacement vehicles from the manufacturer. Payments for Sound Transit's replacement vehicles are paid out of the escrow account.

At December 31, 2002, all 17 cab and coach cars had been delivered to CalTrain and at December 31, 2003, all of the replacement vehicles had been received by Sound Transit. The lease of the cars has been recorded as a capital lease for accounting purposes and was reported in the balance sheet as lease contract receivable. The difference between the value of the new replacement cars and the net book value of the leased cars was recognized as unearned income and was amortized over the 18-month lease term on a straight-line basis, which approximates the effective interest method. In 2002, Sound Transit recorded the remaining \$1.6 million in unearned income on delivery of the vehicles (\$0.3 million in 2001), of which \$1.1 million was earned during 2003 (\$0.8 million in 2002).

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Notes to Financial Statements, continued

6. CAPITAL ASSETS

Capital assets are summarized as follows:

<i>(in thousands)</i>	December 31 2001	Additions	Transfers and Retirements	December 31 2002	Additions	Transfers and Retirements	December 31 2003
Non-Depreciable Assets							
Land	\$ 19,579	\$ 101,936	\$ -	\$ 121,515	\$ 129,401	\$ -	\$ 250,916
Capital Projects in Progress							
Sound Transit	503,797	252,913	(201,889)	554,821	313,565	(243,390)	624,996
Other Governments	74,210	21,670	(48,231)	47,649	57,574	(297)	104,926
Total Non-Depreciable Assets	597,586	376,519	(250,120)	723,985	500,540	(243,687)	980,838
Depreciable Assets							
Transit facilities and heavy equipment	52,525	49,382	-	101,907	103,217	-	205,124
Buildings and leasehold improvements	22,760	-	-	22,760	-	-	22,760
Revenue vehicles	127,717	29,813	-	157,530	40,350	-	197,880
Furniture, equipment and vehicles	10,287	623	(529)	10,381	623	(17)	10,987
Equipment under capital lease	482	-	(12)	470	165	(28)	607
Total Depreciable Assets	213,771	79,818	(541)	293,048	144,355	(45)	437,358
Accumulated Depreciation							
Transit facilities and heavy equipment	(2,214)	(3,681)	-	(5,895)	(6,593)	-	(12,488)
Buildings and leasehold improvements	(1,937)	(974)	-	(2,911)	(974)	-	(3,885)
Revenue vehicles	(11,041)	(7,714)	-	(18,755)	(8,147)	-	(26,902)
Furniture, equipment and vehicles	(4,398)	(1,894)	519	(5,773)	(1,729)	5	(7,497)
Equipment under capital lease	(238)	(87)	6	(319)	(127)	27	(419)
Total Accumulated Depreciation	(19,828)	(14,350)	525	(33,653)	(17,570)	32	(51,191)
Depreciable Assets, Net	193,943	65,468	(16)	259,395	126,785	(13)	386,167
Total Capital Assets, Net	\$ 791,529	\$ 441,987	\$ (250,136)	\$ 983,380	\$ 627,325	\$ (243,700)	\$ 1,367,005

During 2003, Sound Transit relieved capital projects in progress of \$1.9 million with respect to easements to the Kent Station, granted to the City of Kent, and the Link E-3 Busway project, granted to Seattle City Light and City of Seattle, as well as a payment to the City of Lakewood for street improvements around the future Lakewood Station. These amounts have been recorded as contributions to other governments in the Statements of Revenues, Expenses and Changes in Net Assets.

During 2002, Sound Transit substantially completed \$41.5 million in projects which were ultimately owned by other governmental entities pursuant to capital improvement agreements and contributed \$1.0 million to Pierce Transit for maintenance base improvements. Completed projects included Lynnwood SR-99 Transit Lanes, the Pacific Avenue Overpass, I-90 @ Sunset and the Tacoma Dome Park-and-Ride Expansion. The costs of these completed projects are included in contributions to other governments in the Statements of Revenues, Expenses and Changes in Net Assets.

During 2003 and 2002, Sound Transit capitalized \$17.1 million of interest costs, representing all of the interest incurred on its Sales Tax and Motor Vehicle Excise Tax Bonds, Series 1999 (see Note 9).

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Notes to Financial Statements, continued

7. CAPITAL AND OPERATING LEASES

Capital leases are comprised of the following:

<i>(in thousands)</i>	2003	2002
Lease/leaseback	\$ 56,657	\$ 55,542
Copier leases	200	159
	<u>56,857</u>	<u>55,701</u>
Less current portion	(109)	(73)
	<u>\$ 56,748</u>	<u>\$ 55,628</u>

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 \$5.3 million was retained by Sound Transit and recorded as non-operating revenues in the year ended December 31, 2001. The amounts invested are considered uncategorized investments.

Subsequent to the receipt of these funds, certain associated closing costs of \$363 thousand were disbursed, leaving a net benefit to Sound Transit of \$4.9 million, which was included in capital lease revenues in 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.

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

<i>(in thousands)</i>	2003	2002
Net sublease, January 1	\$ 55,542	\$ 52,625
Accrued interest	4,157	3,939
Less payment	(3,042)	(1,022)
Net Sublease, December 31	<u>\$ 56,657</u>	<u>\$ 55,542</u>

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Notes to Financial Statements, continued

Copier Leases—Sound Transit entered into a master lease agreement in 1998 for the acquisition of copiers. The lease is classified as a capital lease for accounting purposes and the copiers were recorded as assets with a corresponding long-term liability, which is equal to the present value of future lease payments. Sound Transit records lease payments as reductions of the long-term liability and as interest expense over the life of the lease.

Future payments under the copier lease obligations are shown in the following table.

<i>(in thousands)</i>	December 31 2003
2004	\$ 119
2005	92
2006	2
Total minimum lease payments	<u>213</u>
Amounts representing interest	<u>(13)</u>
Present value of lease obligations	200
Less current portion	<u>(109)</u>
Long-term portion	<u><u>\$ 91</u></u>

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 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 Burlington Northern & Santa Fe Railroad (“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. See also *Sales Tax Audit* described in Note 14.

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Notes to Financial Statements, continued

Operating Rentals—Sound Transit leases office space adjacent to Union Station, in the Rainier Valley and in Tacoma under noncancelable operating leases with lease terms expiring in 2004 and 2005. Minimum lease payments through 2006 are as follows:

<i>(in thousands)</i>	
2004	\$ 1,538
2005	756
2006	10
	<u>\$ 2,304</u>

Total rental payments for 2003, which include non-cancelable operating leases as well as other month-to-month rentals, was \$2.1 million, of which \$138 thousand was capitalized to capital projects in progress. Total payments for 2002 were \$2.1 million, of which \$100 thousand was capitalized.

8. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable and accrued liabilities consist of the following:

<i>(in thousands)</i>	2003	2002
Accounts payable	\$ 14,937	\$ 26,539
Accrued liabilities	7,355	6,371
Due to other governments	25,116	15,594
Accrued salaried, wages and benefits	2,441	1,550
Retainage payable	299	307
	<u>\$ 50,148</u>	<u>\$ 50,361</u>

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Notes to Financial Statements, continued

9. LONG-TERM DEBT

Long-term debt consists of the following:

<i>(in thousands)</i>	2002 Beginning Balance	Additions	Reductions	2003 Ending Balance	Amounts Due within One Year
Bonds payable:					
Sales Tax and Motor Vehicle Excise Tax Bonds, Series 1999	\$ 350,000	\$ -	\$ -	\$ 350,000	\$ -
Plus unamortized premium	5,640	-	(438)	5,202	-
Less unamortized discount	(8,188)	-	377	(7,811)	-
Total bonds payable	<u>\$ 347,452</u>	<u>\$ -</u>	<u>\$ (61)</u>	<u>\$ 347,391</u>	<u>\$ -</u>

<i>(in thousands)</i>	2001 Beginning Balance	Additions	Reductions	2002 Ending Balance	Amounts Due within One Year
Bonds payable:					
Sales Tax and Motor Vehicle Excise Tax Bonds, Series 1999	\$ 350,000	\$ -	\$ -	\$ 350,000	\$ -
Plus unamortized premium	6,077	-	(437)	5,640	-
Less unamortized discount	(8,565)	-	377	(8,188)	-
Total bonds payable	<u>\$ 347,512</u>	<u>\$ -</u>	<u>\$ (60)</u>	<u>\$ 347,452</u>	<u>\$ -</u>

Sales Tax and Motor Vehicle Excise Tax Bonds, Series 1999—On January 6, 1999, Sound Transit issued Sales Tax and Motor Vehicle Excise Tax Bonds, Series 1999 in the amount of \$350 million. These bonds are dated December 1, 1998, and are tax exempt. The average life of these bonds is 22.5 years with an average coupon rate of 4.88% and an effective rate of 4.87%. Sound Transit is required to maintain certain minimum deposits as defined in the bond resolution to meet debt service requirements. At December 31, 2003 and 2002, cash restricted for debt service totaled \$7.2 million. Principal payments are due February 1 of each year starting February 1, 2006. Proceeds from this bond issue have been used for capital projects in Link, Sounder and Regional Express.

The fair value of long-term debt was \$363.5 million and \$356.6 million as of December 31, 2003 and 2002, respectively. This fair value was estimated using quoted market prices.

At December 31, 2002, Sound Transit had determined that arbitrage rebate payments in the amount of \$375 thousand were due under Section 148 of the Internal Revenue Code of 1986, as amended. This amount was paid in 2003.

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Notes to Financial Statements, continued

Sales Tax and Motor Vehicle Excise Tax Bonds, Series 1999			
Debt service requirements to maturity			
Year Ending		<i>(in thousands)</i>	
December 31	Principal	Interest	Total
2004	\$ -	\$ 17,164	\$ 17,164
2005	-	17,164	17,164
2006	4,270	17,078	21,348
2007	4,445	16,904	21,349
2008	4,620	16,720	21,340
2009-2013	26,680	79,811	106,491
2014-2018	34,395	71,886	106,281
2019-2023	121,510	52,153	173,663
2024-2028	154,080	18,989	173,069
	<u>\$ 350,000</u>	<u>\$ 307,869</u>	<u>\$ 657,869</u>

10. COMPENSATED ABSENCES

Compensated absences are as follows:

<i>(in thousands)</i>	2003	2002
Balance, beginning of year	\$ 1,754	\$ 1,494
Additions	2,141	1,685
Reductions	<u>(1,483)</u>	<u>(1,425)</u>
Balance, end of year	2,412	1,754
Less amounts due within one year	<u>(949)</u>	<u>(262)</u>
Long-term portion	<u>\$ 1,463</u>	<u>\$ 1,492</u>

Amounts due within one year are included in accrued salaries, wages, and benefits (see Note 8).

11. RESTRICTED NET ASSETS

Restricted net assets consist of the following:

<i>(in thousands)</i>	2003	2002
Contractual arrangements	\$ 203,920	\$ 235,455
State contributions	-	16,549
Deductible liability protection policy	<u>6,792</u>	<u>6,687</u>
	<u>\$ 210,712</u>	<u>\$ 258,691</u>

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Notes to Financial Statements, continued

12. 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 either to 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 are eligible to continue their membership in PERS for the duration of their continuous employment with Sound Transit. At December 31, 2003, there were three employees participating in PERS (four employees at December 31, 2002 and five employees at December 31, 2001).

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.

Sound Transit’s actual contribution rates, which were the required contribution rates, are expressed as a percentage of covered payroll. The amount of covered payroll during 2003 and 2002 was \$21.3 million and \$17.9 million, respectively, and total payroll was \$21.8 million and \$18.4 million, respectively. The required contribution rates expressed as a percentage of covered payroll and required Sound Transit contributions during 2003, 2002 and 2001 are as follows:

	Contribution Rate			Contributions (in thousands)		
	2003	2002	2001	2003	2002	2001
Employer	12%	12%	12%	\$2,562	\$2,148	\$1,959
Employee	10%	10%	10%	2,135	1,790	1,632
Total	22%	22%	22%	\$4,697	\$3,938	\$3,591

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Notes to Financial Statements, continued

13. RISK MANAGEMENT

In the ordinary course of its normal operations, Sound Transit is exposed to various 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 program utilizing the purchase of commercial insurance that has in force first-level coverage for property, liability, employment practices and crime and fidelity to provide protections from these exposures. Such coverage includes self-insured per claim retention insignificant to Sound Transit's risk of loss. There have been no changes to the policy since inception and no settlements have exceeded coverage under the plan.

Sound Transit has also established an Owner-Controlled Insurance Program ("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. This commercially-procured insurance program includes a self-insured retention level of \$500 thousand per claim. This program covers construction projects from January 1, 2001, through December 31, 2006, and all premium payments under the policy have been prepaid.

In addition, Sound Transit has also entered into a deductible liability protection policy to supplement the self-insured retention portion of the OCIP. Under this policy the probable maximum claims exposure, estimated at \$6.5 million, has been deposited with the insurer in an interest-bearing loss fund account.

14. COMMITMENTS AND CONTINGENCIES

Operations and Maintenance Agreements—Sound Transit has entered into agreements which expire in September 2004 with Community Transit, King County Department of Transportation and Pierce Transit ("purchased transportation providers") to operate its Regional Express public transportation service within Sound Transit's service area. This service is compensated for based on hourly rates established within the agreements, generally utilizing equipment provided by Sound Transit. In addition, under the King County Department of Transportation agreement, the county will use King County-owned Breda buses for the operation of Sound Transit's express Route 550, which operates in the bus tunnel. An up-front payment of \$2.9 million was paid in 1999 for three years of the Breda bus service. At the end of 2002, this amount was fully amortized, with \$633 thousand expensed to operations and maintenance in the year ended December 31, 2002.

Sound Transit also entered into 40-year agreements in May of 2000 with BNSF and Amtrak for the operations and maintenance of its Sounder commuter rail service. Under the BNSF agreement, Sound Transit pays in accordance with an hourly rate schedule per train mile that is based on the number of trains per day. Under the Amtrak agreement, Sound Transit pays a flat monthly fixed price dependent upon the number of one-way trips. See related agreements described in Note 7: *Amtrak Lease/Sublease*.

Agreements with BNSF for Sounder Commuter Rail Service in the Seattle-to-Everett and Lakewood-to-Tacoma Corridors—On December 18, 2003, Sound Transit entered into a series of agreements with BNSF for the purchase of four perpetual property easements from Seattle to Everett, purchase of property in the Tacoma-to-Nisqually corridor for service and station improvements, conditions for joint use and the purchase of operation services in each corridor.

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Notes to Financial Statements, continued

The acquisition of the easements and property occur over a four-year payment period, with the first easement in the Seattle-to-Everett corridor closing on December 18, 2003, in exchange for a payment of \$79 million and allowing the commencement of train service between Seattle and Everett. In addition, \$3.6 million was paid with respect to the Lakeview Station land parcels and \$4.4 million was paid with respect to a non-refundable deposit for additional land parcels for the Lakeview North and South segments in the Lakewood-to-Tacoma corridor. The easement and the station parcels have been recorded in capital assets as land and the deposit in long-term prepaid expense and deposit.

The acquisition of the remaining easements in the Seattle-to-Everett corridor will close as follows:

	Closing Date	Due on Closing
2nd Easement	December, 2004	\$79 million
3rd Easement	December, 2006	\$50 million
4th Easement	December, 2007	\$50 million

Each of the additional easements allows the addition by Sound Transit of one round trip of commuter train service. Closing by Sound Transit on the second easement is conditioned upon the delivery by BNSF of plan specifications and design documents to 30% for the second through fourth easements, as well as estimates of wetland impacts resulting from those improvements and permitting. Closing by Sound Transit on the third and fourth easements are conditioned upon the lack of a determination that certain permits for improvements that BNSF is designing to construct are highly unlikely to be issued. If these conditions are not met, Sound Transit has the option to not close with no additional payment due and no additional train service beyond that provided by prior accepted easements.

The easement acquisition agreements also contain post-closing options for Sound Transit for the resale of the second, third and fourth easements to BNSF should it appear that permitting will not be allowed. These options may be exercised as follows:

	Earliest Exercise Date	Latest Exercise Date	Exercise Price
2nd Easement	November, 2006	November, 2010	\$27.5 million
3rd Easement	December, 2008	December, 2012	\$50 million
4th Easement	December, 2009	December, 2013	\$50 million

The acquisition of the properties in the Nisqually-to-Tacoma corridor is conditional upon the results of due diligence investigation of the related properties. Subject to acceptable findings, closing dates are as follows:

	Closing Date	Due on Closing	Promissory Note
North Line	September, 2004	\$6 million	\$6 million, due 2006
South Line	September, 2006	\$6 million	\$6 million, due 2007

Should Sound Transit proceed with the acquisition of the Lakewood Station properties and the North and the South line, total payments under the agreement to BNSF are \$32 million, including interest on the promissory notes.

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Notes to Financial Statements, continued

The Joint-Use Agreement for the Seattle-to-Everett corridor defines the periods of operation and compensation for use of the BNSF line and Sound Transit's permitting responsibilities with respect to its operation. The Joint-Use Agreement for the Lakewood-to-Tacoma corridor sets forth BNSF's and Sound Transit's responsibilities for maintenance-of-way and rehabilitation activities and compensation to Sound Transit by BNSF for freight use of the line. Initially, BNSF will retain all maintenance activities associated with the line. However, as Sound Transit incrementally commences construction of the line, Sound Transit will be responsible for maintenance activities on those sections.

The Commuter Rail Service Agreement set forth the terms for the actual operation of the commuter trains by BNSF and the compensation paid to BNSF for train crews, maintenance-of-way and other expenses incurred in the operation of the Sounder service between Seattle and Everett. The compensation is structured to provide flat rates for maintenance and crews with inflation adjusters plus performance incentives after the initial pre-construction period. The term of the agreement is for 12 years with an option of 5 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, contingent upon the Nisqually to Tacoma purchase transactions.

Purchases—At December 31, 2003, and 2002, Sound Transit had outstanding commitments of approximately \$298.5 million and \$205.6 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, 2003, and 2002, may be impaired. In the opinion of management, there are no significant contingent liabilities relating to compliance with the rules and regulations governing the respective grants; therefore, no provision has been recorded in the accompanying financial statements for such contingencies.

Reimbursements Due Under Agreement between Sound Transit and the City of Seattle—Sound Transit and the City of Seattle entered into an agreement to establish, oversee and fund the City of Seattle's portion of the Transit-Oriented Community Development Fund and to provide funding support for certain aspects of the Central Link light rail project. Under the agreement, Sound Transit will be reimbursed within 60 days of invoicing for work performed that would otherwise be the obligation of and/or for the benefit of Seattle Public Utilities and Seattle City Light. As of December 31, 2003, included in accounts receivable is \$888 thousand and \$4.6 million in billed and unbilled costs, respectively.

The City of Seattle is currently involved in a lawsuit brought by ratepayers challenging the use of utility funds to meet the City's funding obligations under the CDF agreement. While the City has acknowledged its responsibilities under this binding agreement, this dispute may result in a deferral of receipt of payment to Sound Transit beyond the 60 day terms of the agreement.

Reservation Junction to Freighthouse Square—Sound Transit completed construction of the Reservation Junction to Freighthouse Square project in September 2003; however, ongoing settlement of the embankment raised stability and safety concerns. Sound Transit retained independent engineers to evaluate the embankment and they recommended remedial measures to stabilize the embankment. In January, Sound Transit relocated commuter rail operations from the Reservation Junction to Freighthouse Square to its temporary platform. The engineer of record has designed remedial pilings to provide additional stability to the foundation, which are being installed by the original contractor.

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Notes to Financial Statements, continued

Sound Transit has reserved its rights to claim for the costs of evaluating the embankment and the remediation work from the responsible parties and will defend any claims brought by the engineering firms.

By letter dated January 23, 2004, the City of Tacoma demanded payment of \$7,500 per day as of January 21, 2004, in liquidated damages for “interruption of service” under the Construction Agreement between the City and Sound Transit. In spite of its claim, the City of Tacoma continues to operate over the segment in question. Sound Transit has rejected the City’s demand.

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 effect, if any, of these matters is not presently determinable, management believes that collectively they will not have a material effect on the results from operations or the Balance Sheet. In addition, Sound Transit has been named in the following legal actions:

Pierce County, City of Tacoma, King County, Sound Transit, et al v. State of Washington, King County Superior Court

The defendant/interveners contend that Sound Transit is not a validly-formed government and is not entitled to impose the 0.3% motor vehicle excise tax authorized and imposed pursuant to RCW 81.104.160 and that Initiative 776 (I-776) repealed Sound Transit’s ability to collect the tax. If the court rejects these claims and finds that Sound Transit is legally entitled to continue to collect the tax through 2028 (because the agency pledged to collect the tax to repay outstanding 30-year bond debt sold before I-776 was enacted), then the defendant/interveners alternatively seek a court order defining what limits apply to Sound Transit’s ability to collect the tax to the extent required to honor Sound Transit’s bond obligations, but has not asserted a position on whether I-776 otherwise limits the agency’s ability to collect or use the tax.

Sound Transit intends to vigorously defend against these claims and believes that defendant/interveners’ claim that Sound Transit cannot collect the tax because it is not a validly-formed government is not likely to prevail. Because none of the opposing parties have articulated a legal basis upon which to argue that I-776 should limit Sound Transit’s ability to collect the tax and in view of inherent uncertainties in the above, we are not able to make a judgment at this time about the outcome of this matter.

Sheehan, et .al., v. Sound Transit and Seattle Popular Monorail Authority, King County Superior Court

Plaintiffs filed suit on March 10, 2004, and contend that the 0.3% motor-vehicle excise tax imposed by Sound Transit and the Seattle Popular Monorail Authority are illegal *ad valorem* property taxes. Plaintiffs seek to enjoin Sound Transit from collecting the tax and seek a refund of prior taxes paid by plaintiffs and other taxpayers. Sound Transit plans to vigorously defend against the lawsuit and is preparing motions to request that the case be dismissed. Based on a Washington Supreme Court precedent finding that the tax is a legally-imposed tax, we do not believe that the plaintiff is likely to prevail.

CENTRAL PUGET SOUND REGIONAL TRANSIT AUTHORITY

Notes to Financial Statements, continued

Sales Tax Audit—The Washington State Department of Revenue (“the Department”) has been conducting a routine tax audit covering the period from June 1, 1998, through June 30, 2002. By letters dated March 27 and April 7, 2003, the Department of Revenue identified two areas that they believe represent taxable issues. This includes certain portions of the operating agreements with Sound Transit’s purchased transportation providers. Sound Transit does not believe any portion of these agreements to be taxable and continues to vigorously oppose the Department should they make such a determination. Should Sound Transit’s position not be upheld, the related sales tax liability, including interest, is estimated to be in the range of \$1.2 million to \$1.8 million.

The Department also reviewed resale certificates for the purchase of rolling stock and various agreements between Sound Transit, Amtrak and BNSF regarding the rolling stock and related maintenance and repairs, which the Department has determined to be invalid. These agreements were entered into in 2000 and provided an exemption from sales tax. Sound Transit sought and received an advance ruling from the Department as to the taxability of these transactions and believes the agreements and related certificates to be valid. The agency intends to vigorously oppose the determination. It is too early for Sound Transit to make any judgment regarding the outcome in this matter; however, should Sound Transit’s position not be upheld, the related sales tax liability, including interest, is estimated to be in the range of \$3.7 million to \$13.1 million. This amount would be reflected in the financial statements as an increase in net assets for the carrying value for materials, parts and supplies and revenue vehicles of \$2.8 million to \$10.9 million, offset by a reduction to net assets from the increase in interest expense and corresponding reduction in the excess of revenues over expenses of \$0.9 million to \$2.2 million.