

New York City Transit Authority

**Consolidated Financial Statements
Management's Discussion and Analysis
December 31, 2003 and 2002**

New York City Transit Authority

Index

December 31, 2003 and 2002

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Report of Independent Auditors

Members of the Board
Metropolitan Transportation Authority

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of revenues, expenses and changes in net assets, and of cash flows present fairly, in all material respects, the financial position of the New York City Transit Authority (the Authority) at December 31, 2003 and 2002, and changes in its financial position and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America. These consolidated financial statements are the responsibility of the Authority's management; our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits of the statements in accordance with auditing standards generally accepted in the United States of America, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As described in the notes to the consolidated financial statements, the Authority is a public benefit corporation that receives a significant portion of its operating and capital financing requirements from the City of New York, the State of New York, federal and regional governmental entities and from the sale of bonds to the public. Also, the Authority has material transactions with affiliated agencies and other public transportation agencies.

The Management's Discussion and Analysis for the years ended December 31, 2003 and 2002 on pages 2 through 13 and the required supplementary information on page 48 are not required parts of the basic financial statements but are supplementary information required by the accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consist 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.

PricewaterhouseCoopers LLP

March 12, 2004, except as to Note 12 for which
the date is April 8, 2004

**NEW YORK CITY TRANSIT AUTHORITY
MANAGEMENT'S DISCUSSION AND ANALYSIS (Unaudited)
For the Years Ended December 31, 2003 and 2002**

OVERVIEW OF THE FINANCIAL STATEMENTS

Introduction to the Annual Report

This annual report consists of three parts: Management's Discussion and Analysis, Financial Statements and Notes to the Financial Statements and Supplementary Information.

The Financial Statements Include:

The Consolidated Balance Sheets provide information about the nature and amounts of investments in resources (assets) and the obligations to New York City Transit Authority's (the Authority's) creditors (liabilities), with the difference between the two reported as net assets.

The Consolidated Statements of Revenues, Expenses and Changes in Net Assets show how the Authority's net assets changed during each year. It accounts for all of the current year's revenues and expenses, measures the financial results of the Authority's operations over the past year and can be used to determine how the Authority has funded its costs.

The Consolidated Statements of Cash Flows provide information about the Authority's cash receipts, cash payments and net changes in cash resulting from operations, non-capital financing, capital and related financing and investing activities.

The Notes to the Financial Statements and Supplementary Information Provide:

Information that is essential to understanding the basic financial statements, such as the Authority's accounting methods and policies.

Details of cash and investments, capital assets, employee benefits, long-term debt, lease transactions and future commitments and contingencies of the Authority.

Any other events or developing situations that could materially affect the Authority's financial position, results of operations and cash flows.

The Required Supplementary Information provides information concerning the Authority's progress in funding its obligation to provide pension benefits to its employees.

Management's Discussion and Analysis:

The following is a narrative overview and analysis of the financial activities of the Authority for the years ended December 31, 2003 and 2002. This management discussion and analysis (MD&A) is intended to serve as an introduction to the Authority's basic financial statements. It provides an assessment of how the Authority's position has improved or deteriorated and identifies the factors that, in management's view, significantly affected the Authority's overall financial position. It may contain opinions, assumptions or conclusions by the Authority's management that should not be considered a replacement for, and must be read in conjunction with, the financial statements described above.

CONDENSED FINANCIAL INFORMATION (CONTINUED)

Financial Reporting Entity

The New York City Transit Authority and its subsidiary, Manhattan and Bronx Surface Transit Operating Authority (MaBSTOA) (collectively, the Authority) are public benefit corporations established pursuant to the New York State (the State) Public Authorities Law, to operate public subway, bus and paratransit services within the City of New York (the City). The Authority is a part of the financial reporting group of the Metropolitan Transportation Authority (MTA), which is a component unit of the State and whose mission is to continue, develop and improve public transportation and to develop and implement a unified public transportation policy in the New York Metropolitan area.

CONDENSED FINANCIAL INFORMATION

All amounts are in millions, except as noted.

The following sections will discuss the significant changes in the Authority's financial position for the years ended December 31, 2003 and 2002. Additionally, an examination of major economic factors and industry trends that have contributed to these changes is provided. It should be noted that for purposes of the MD&A, summaries of the financial statements and the various exhibits presented are in conformity with the Authority's financial statements, which are presented in accordance with Generally Accepted Accounting Principles.

Operating Expenses

The format for reporting operating expenses in 2003 was revised resulting in an improved presentation. Operating expenses for 2002 and 2001 have been reclassified to be consistent with the revised 2003 format.

Debt Restructuring-2002

Substantially all of the outstanding debt of MTA, Triborough Bridge and Tunnel Authority (TBTA) and the Authority was restructured during 2002 by consolidating most existing credits into four principal new credits: (1) MTA Transportation Revenue Bonds; (2) MTA State Service Contract Bonds; (3) MTA Dedicated Tax Fund Bonds and TBTA General Revenue and Subordinate Revenue Bonds. In connection with the debt restructuring, the following MTA and Authority bonds and notes that were secured by the Authority's operating revenues were paid or defeased with the proceeds of MTA's Transportation Revenue Bonds: MTA Transit Facilities Revenue Bonds and Bond Anticipation Notes and Transit Authority Subordinated Transit Facilities Revenue Bonds (Livingston Plaza Project).

The Transportation Revenue Bonds are special obligations of the MTA, payable from, and secured by a pledge of: the gross operating revenues of Long Island Rail Road, Metro-North Commuter Railroad Company and the Authority and its subsidiary, MaBSTOA, until monthly deposits of principal and interest are satisfied under the Transportation Revenue Bond Resolution; TBTA's operating surplus; general operating subsidies from the State and local governments; special tax-supported operating subsidies and station maintenance and service reimbursements.

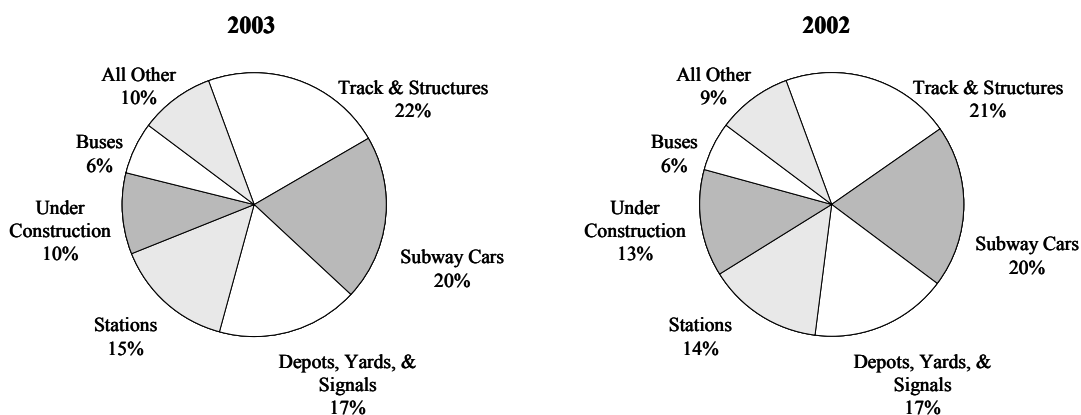
In addition, as part of the debt restructuring, the Dedicated Tax Fund Bonds and the TBTA Mortgage Recording Tax Special Obligation Bonds, which were apportioned to the Authority, were paid or defeased with the proceeds of the MTA Dedicated Tax Fund Bonds and TBTA General Revenue and Subordinate Revenue Bonds, respectively. In a separate transaction, on December 19, 2002, MTA defeased the MTA Excess Loss Fund Special Obligation Bonds, Series 1998, thereby defeasing the Authority's payment obligations with respect thereto. Assumption of the debt by the MTA converted the Authority's debt into a capital contribution from the MTA.

CONDENSED FINANCIAL INFORMATION (CONTINUED)

Total Assets, Distinguishing Between Capital and Other Assets

	2003	2002	2001	Increase/(Decrease)	
				2003-2002	2002-2001
Gross Capital Assets	\$ 27,939	\$ 25,517	\$ 22,894	\$ 2,422	\$ 2,623
Allowance For Depreciation	(7,169)	(6,394)	(5,702)	(775)	(692)
Net Capital Assets	20,770	19,123	17,192	1,647	1,931
Other Assets	1,891	1,970	2,327	(79)	(357)
Total Assets	\$ 22,661	\$ 21,093	\$ 19,519	\$ 1,568	\$ 1,574

Gross Capital Assets



The Authority's Gross Capital Assets totaled almost \$28 billion at year-end 2003. Of the total, stations/depots and yards were 32%, subway cars and buses accounted for 26%, and track/structures were 22%. The majority of assets under construction consist of subway cars, track and structures, and stations' improvements.

Significant changes in assets include:

December 31, 2003 versus 2002

Net Capital Assets increased from December 31, 2002 to December 31, 2003 by \$1,647, or 8.6%. The net increase is due primarily to capital asset additions of \$2,486. Significant additions include track & structures (\$939), new subway cars (\$581) and station rehabilitations (\$497). The additions are partially offset by the disposal of 296 "redbird" subway cars (\$64) and two buses, as well as annual depreciation of \$829. The Authority completed the disposal of "redbird" subway cars through 2003, which resulted in a \$31 loss on disposal in 2003. The Redbird fleet has been in the process of replacement with new subway cars and the principal method of disposal is "reefing" of the cars off the coasts of some states to enhance sea life.

Other Assets decreased by \$79, or 4.0%, as compared with the prior year. This decrease is mostly attributable to a decrease in funds held in the MTA investment pool of \$79, due to the timing of receipts and expenditures.

CONDENSED FINANCIAL INFORMATION (CONTINUED)

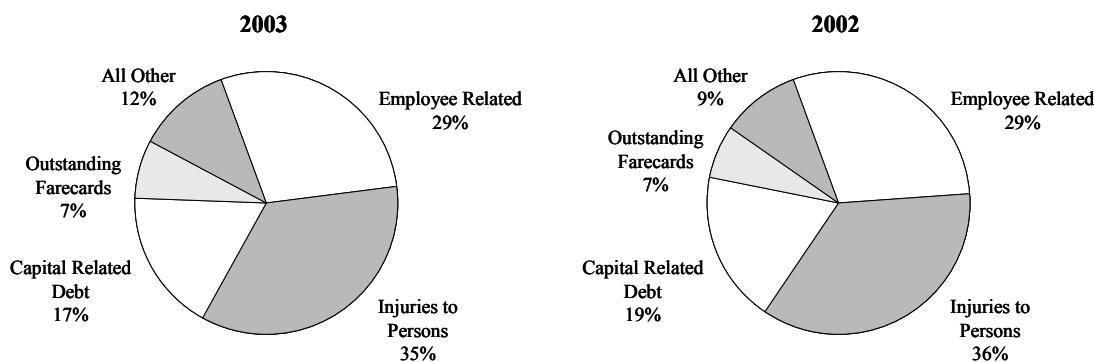
December 31, 2002 versus 2001

Net capital assets increased from December 31, 2001 to December 31, 2002 by \$1,931, or 11.2%. The net increase was due primarily to additions of capital assets, including new subway cars (\$1,086), infrastructure work under construction (\$492), track & structures (\$380) and station re-habilitations (\$331), partially offset by the disposal of 405 "redbird" subway cars and three buses (\$108). Other Assets decreased by \$357, or 15.3%, due mostly to a reduction in subsidy receivables of \$235 caused by the timing of subsidy receipts. The impact of the Debt Restructuring Program served to reduce other assets by \$218.

Total Liabilities, Distinguishing Between Long-Term Liabilities and Current Liabilities

	2003	2002	2001	Increase/(Decrease)	
				2003-2002	2002-2001
Current Liabilities	\$ 1,075	\$ 968	\$ 1,006	\$ 107	\$ (38)
Long-Term Liabilities	1,098	1,088	5,542	10	(4,454)
Total Liabilities	\$ 2,173	\$ 2,056	\$ 6,548	\$ 117	\$ (4,492)

Total Liabilities



At the end of 2003, the Authority's liabilities consist primarily of Injuries to Persons (public liability), 35% and employee related liabilities (for pensions, health and other benefits), 29%.

Significant changes in liabilities include:

December 31, 2003 versus 2002

Total Liabilities increased from December 31, 2002 to December 31, 2003 by \$117, or 5.7%. Current Liabilities increased \$107, or 11.1%, while Long-Term Liabilities increased \$10, or 0.9%.

The increase in Current Liabilities was due primarily to an increase in bank overdrafts payable of \$56, accrued expenses of \$41 and to the increase in unredeemed farecards of \$40, partly offset by a \$16 write-off of token liabilities. The bank overdrafts payable increase was due to the timing of payroll and other expense checks issued at the end of the year but not as yet funded by the bank. Total accrued expenses increased primarily due to the effect of the Authority assuming responsibility, in July, 2003, for providing health benefits to its employees who are members of TWU Local 100, as well as to retirees who were members of TWU local 100 at the time of retirement. Prior to this assumption of responsibility, the TWU Health Benefit Trust was financed by the Authority.

CONDENSED FINANCIAL INFORMATION (CONTINUED)

In addition, accrued retirement and death benefits increased due to higher NYCERS 2004 pension funding requirements. Accrued salaries, wages and payroll taxes decreased due to the timing of year-end payrolls. The unredeemed farecard liability increase was the result of the May, 2003 fare increase.

The increase in Long-Term Liabilities was due largely to an increase in liabilities associated with injuries to persons. This increase is attributable to changes in actuarial experience based on the claims history. Obligations under capital leases decreased \$10 due to settlement with the lessor resulting in rent credits, which will be applied against annual lease payments over the next thirty years.

December 31, 2002 versus 2001

Total Liabilities decreased from December 31, 2001 to December 31, 2002 by \$4,492, or 68.6%. The decrease in Current Liabilities of \$38, or 3.8%, and the decrease in Long-Term Liabilities of \$4,454, or 80.4%, were due primarily to the impact of the MTA Debt Restructuring Program.

Total Net Assets, Distinguishing Among Amounts Invested in Capital Assets, Net of Related Debt; Restricted Amounts and Unrestricted Amounts

	2003	2002	2001	Increase/(Decrease)	
				2003-2002	2002-2001
Investment in Capital Assets, Net of Related Debt	\$ 20,718	\$ 19,088	\$ 12,580	\$ 1,630	\$ 6,508
Restricted	-	19	32	(19)	(13)
Unrestricted	(230)	(70)	359	(160)	(429)
Total Net Assets	\$ 20,488	\$ 19,037	\$ 12,971	\$ 1,451	\$ 6,066

Net assets represent the residual interest in the Authority's assets after liabilities are deducted and consist of three sections: Invested in capital assets, net of related debt, restricted and unrestricted. Net assets invested in capital assets, net of related debt include capital assets, net of accumulated depreciation and outstanding principal balances of debt attributable to the acquisition, construction or improvement of those assets. Net assets are reported as restricted when constraints are imposed by third parties or enabling legislation. All other net assets are unrestricted.

December 31, 2003 versus 2002

Total net assets reached \$20,488 at the end of 2003, a net increase of \$1,451 from the end of 2002. The net increase was comprised of capital contributions from the MTA of \$1,945, non-operating income of \$1,888, partially offset by operating losses of \$2,382.

- The operating losses and non-operating income results are addressed in the following section.
- Restricted assets consisted of unused bond proceeds, which were restricted and utilized by the MTA for debt service in 2003.
- Unrestricted assets reflect non-capital assets and liabilities. Assets that decreased include the MTA investment pool, receivables from the MTA for purchase of capital assets, investments restricted for debt service and deferred expenses. Liabilities that increased include bank overdrafts, employee health benefits, unredeemed farecards and injuries to persons accounts.

CONDENSED FINANCIAL INFORMATION (CONTINUED)

December 31, 2002 versus 2001

Total net assets reached \$19,037 at the end of 2002, a net increase of \$6,066 from the end of 2001. The net increase was comprised of capital contributions from the MTA of \$7,068, and non-operating income of \$1,304, partially offset by operating losses of \$2,306. Investments in Capital Assets net of related debt increased by \$6,508 to \$19,088, due primarily to the MTA Debt Restructuring Program. Unrestricted assets that decreased include subsidy receivables, receivables from the MTA for purchase of capital assets and deferred expenses. Liabilities that increased include personnel-related and injuries to persons accounts.

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

	<u>Year Ended December 31,</u>		
	<u>2003</u>	<u>2002</u>	<u>2001</u>
Operating Revenues	\$ 2,583	\$ 2,334	\$ 2,336
Operating Expenses	<u>(4,965)</u>	<u>(4,640)</u>	<u>(4,483)</u>
Operating Loss	<u>(2,382)</u>	<u>(2,306)</u>	<u>(2,147)</u>
Non-operating Revenues (Expenses)			
Subsidies-New York State & City	1,461	1,349	1,264
Triborough Bridge & Tunnel Authority	242	100	133
Insurance Recovery Related to World Trade Center Settlement	245	-	-
Interest Expense	(29)	(87)	(153)
Loss on Impairment of Capital Assets	-	-	(173)
Loss on Disposal of Subway Cars	<u>(31)</u>	<u>(58)</u>	<u>(58)</u>
Total Non-operating Revenues (Expenses)	1,888	1,304	1,013
Loss before Capital Contributions	<u>(494)</u>	<u>(1,002)</u>	<u>(1,134)</u>
Capital Contributions	1,945	7,068	1,935
Change in Net Assets	<u>1,451</u>	<u>6,066</u>	<u>801</u>
Total Net Assets - Beginning of Year	<u>19,037</u>	<u>12,971</u>	<u>12,170</u>
Total Net Assets - End of Year	<u><u>\$ 20,488</u></u>	<u><u>\$ 19,037</u></u>	<u><u>\$ 12,971</u></u>

CONDENSED FINANCIAL INFORMATION (CONTINUED)

Operating Revenues, by Major Source

	2003	2002	2001	Increase/(Decrease)	
				2003-2002	2002-2001
Rapid Transit Revenue	\$ 1,673	\$ 1,503	\$ 1,524	\$ 170	\$ (21)
Surface Transit Revenue	704	632	613	72	19
Total Revenue from Fares	2,377	2,135	2,137	242	(2)
Total Ridership (millions of riders)	2,120	2,175	2,145	(55)	30
Non-Student Average Fare	\$ 1.19	\$ 1.04	\$ 1.06	\$ 0.15	\$ (0.02)

2003 versus 2002

Total revenue from fares was \$2,377 in 2003, an increase of \$242, or 11.3%, from the prior year. Ridership in 2003 was 2,120, a decrease of 55, or 2.6%, from 2002. The increase in revenue was largely due to the May 2003 fare increase, partially offset by the impact of the August 2003 blackout and the continuation of an adverse ridership trend caused by economic factors that preceded the fare increase. The non-student average fare increased by 15 cents or 14.4%, due to the fare increase.

Rapid (subway) revenue from fares was \$1,673 in 2003, an increase of \$170, or 11.3%, from 2002. Ridership in 2003 was 1,385, a decrease of 28, or 2.0%. The increase in revenue was mostly due to the fare increase, partly offset by the effect of ridership losses from the pre-fare increase adverse ridership trend and the blackout.

Surface (bus) revenue from fares was \$704 in 2003, an increase of \$72, or 11.4%, from 2002, principally due to the fare increase. Ridership in 2003 was 735 in 2003, a decrease of 27, or 3.5%.

Fare evasion (turnstile/gate evasion) was estimated to be 0.38% in 2003, slightly above the 2002 level of 0.36% (0.32% in 2001). This is an improvement from 1996 when fare evasion was estimated to be 1.45% and from the 1991 high of 5.91%.

2002 versus 2001

Total revenue from fares was \$2,135 in 2002, a decrease of \$2, or 0.1% from the prior year. Ridership in 2002 was 2,175, the highest annual ridership since 1970 and up \$30, or 1.4% from 2001. The increase from 2001 was largely due to depressed ridership during the last four months of 2001 following the WTC attack. Revenue from fares declined from 2001 despite the higher ridership in 2002 because more customers took advantage of discounted fare media, resulting in a reduction in the non-student average fare from \$1.06 in 2001 to \$1.04 in 2002.

Rapid revenue from fares was \$1,503 in 2002, a decrease of \$21, or 1.4%, from 2001. Ridership reached 1,413 in 2002, an increase of 8, or 0.6%, from 2001, the highest annual ridership since 1953.

Surface revenue from fares was \$632 in 2002, an increase of \$19, or 3.0%, from 2001. Ridership totaled 762 in 2002, an increase of 22, or 3.1%, from 2001, the highest annual ridership since 1975.

CONDENSED FINANCIAL INFORMATION (CONTINUED)

Operating Expenses, by Major Function

	2003	2002	2001	Increase/(Decrease)	
				2003-2002	2002-2001
Salaries & Wages	\$ 2,497	\$ 2,434	\$ 2,389	\$ 63	\$ 45
Retirement & Death Benefits	361	278	263	83	15
Other Employee Benefits	557	488	435	69	53
Materials & Supplies	234	243	274	(9)	(31)
Fuel and Power	195	184	182	11	2
Outside Services	250	234	224	16	10
Public Liability	81	73	49	8	24
Depreciation	829	761	727	68	34
Other Expenses	122	111	83	11	28
Reimbursed Overhead Expenses	(161)	(166)	(143)	5	(23)
Total Expenses	\$ 4,965	\$ 4,640	\$ 4,483	\$ 325	\$ 157

2003 versus 2002

Salaries & wages increased \$63, or 2.6%, over 2002. Significant factors included a one-time TWU lump sum bonus agreed to in the collective bargaining process, which was paid in 2003 at the rate of one thousand dollars per eligible employee or \$33. Unscheduled overtime and bonus expenses increased by \$18 largely to support additional work requirements for bus depot maintenance, shop programs and shuttles. Bus and subway overtime also increased to compensate for unfilled positions, and due to the impact of the August 2003 blackout. Sick and vacation expenses increased by \$17 due to a higher workforce eligibility mix and the effect of some labor enhancements agreed to in the collective bargaining process.

Retirement and death benefit expenses increased by \$83, or 29.9%. Increased pension costs (NYCERS and MaBSTOA) amounted to \$45, while escalating health benefit costs for retirees increased \$38.

Other employee benefits increased by \$69, or 14.1%, due principally to the effect of the Authority assuming the responsibilities of the TWU Health Benefit Trust during 2003 and escalating health benefit costs for active employees.

Depreciation expense in 2003 was \$68, or 8.9% higher than 2002. This increase was due mostly to capitalization of new subway cars, track and structures, station rehabilitations and other infrastructure enhancements. New subway cars are depreciated over fewer years than the other capitalization categories.

Reimbursed overhead expenses represent those expenses that are incurred as part of labor support for capital program work and are therefore eligible for reimbursement by the MTA through the Capital Program.

CONDENSED FINANCIAL INFORMATION (CONTINUED)

2002 versus 2001

Salaries & wages were \$2,434 in 2002, an increase of \$45, or 1.9%, from 2001 principally due to contractual wage rate increases. Represented personnel (mostly Transportation Workers Union members) received a 4% increase as of December 15, 2001 based upon the contract in effect at that time. Non-represented personnel received a 3% increase during 2002.

Other employee benefits increased by \$53, or 12.2%, due mostly to higher Workers Compensation reserve requirements and increased health & welfare costs relating to active personnel.

Public liability expenses increased by \$24, or 49.0%, due in large part to a significant favorable reserve adjustment in 2001, not recurring in 2002.

Depreciation expense in 2002 increased by \$34, or 4.7%, due mostly to capitalization of new subway cars, station rehabilitations and other infrastructure enhancements.

Non-Operating Revenues and Expenses

The Authority receives a variety of tax-supported subsidies from New York State and New York City. These subsidies represent corporate franchise, sales, energy, mortgage recording (through the MTA) and real estate taxes and are sensitive to the strength of the local economy and prevailing interest rates.

Operating assistance subsidies from New York State and New York City have been maintained at the same level each year.

The TBTA, another affiliate of the MTA, distributes to the Authority each year surplus funds that vary based upon its level of operation. Subsidies from the TBTA increased primarily because of the 2003 increase in the toll fare structure. Included as well in 2003 was the benefit resulting from the TBTA prior year debt restructuring.

In April 2004, the MTA settled claims with its property insurance carriers for damage caused as a result of the September 11, 2001 terrorist attack. The Authority's portion of the MTA global settlement was \$245 representing the settlement of claims for losses related to physical damage of property. In addition, as part of the global settlement, MTA has received funds relating to claims for lost revenues, increased operating expenses and other expenses associated with the cleanup of its facilities. In the future, the MTA may choose to distribute a portion of these additional funds to the Authority.

The 2003 capital contributions from the MTA of \$1,945 represent capital program funding from several sources including bonds, Federal, State and City funding. In 2002, capital contributions of \$7,068 included \$4,567 to replace debt extinguished and deferred debt expense, as a result of the MTA Debt Restructuring Program. The remaining capital contributions of \$2,501 represent capital program funding from Federal, State and City sources as well as Mortgage Recording Tax and Petroleum Business Tax debt service contributions.

Changes in Net Assets

In 2003 and 2002, the change in net assets represents the excess of capital contributions over the loss before capital contributions. In 2003, the net assets increased by \$1,451 due mostly to capital contributions. In 2002, net assets increased by \$6,066, due primarily to the MTA Debt Restructuring Program.

CONDENSED FINANCIAL INFORMATION (CONTINUED)

Budget Highlights

Total revenue from fares was less than budget by 1.4%. Rapid (subway) revenue was less than budget by 1.8% and surface (bus) revenue was less than budget by 0.4%. The total unfavorable variance to budget was due largely to the impact of the August, 2003 blackout and a reduction in NYC employment as the budget assumed employment levels would remain unchanged. The revenue impact of the fare increase was on budget, as a result of two offsetting factors: (1) a greater-than-anticipated shift to the 30 day unlimited ride pass, reducing the average fare to below budget, and (2) a smaller-than-anticipated loss of riders. Because of the second factor, total ridership was 0.4% above budget, despite the negative impact of the blackout and the economy.

Total 2003 operating expenses of \$4,136 (excluding depreciation), were essentially on budget.

GOVERNMENT'S OVERALL FINANCIAL POSITION, RESULTS OF OPERATIONS AND IMPORTANT ECONOMIC CONDITIONS

Important Economic Conditions

Metropolitan New York is the most transit-intensive region in the United States. A financially sound and reliable transportation system is critical to the region's economic well-being.

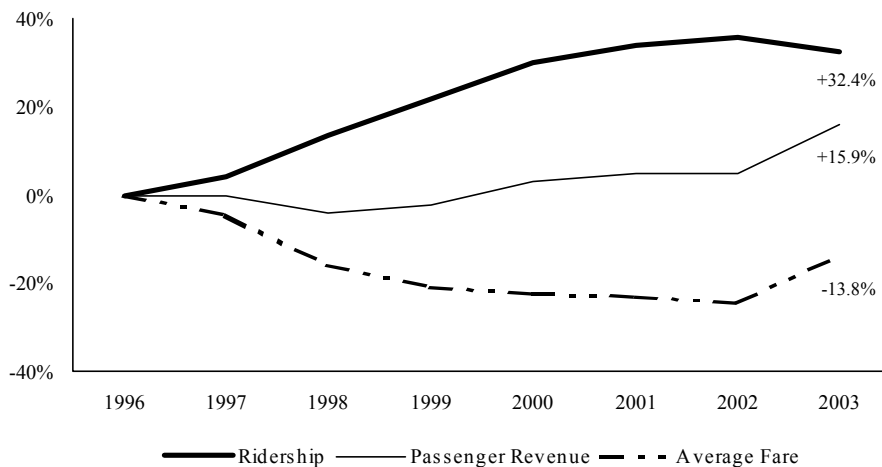
The Authority's overall ridership continues to be affected by adverse economic factors including employment levels in the City. Additionally, severe State and City budget constraints remain.

The Authority expects that, over time, federal and state economic stimulus measures and the rebuilding of the downtown infrastructure will improve the New York City economy.

Results of Operations and Overall Financial Position

Since the introduction of the MetroCard and related fare incentives and unlimited-ride passes, operating revenues of the Authority have remained essentially level (excluding the May, 2003 fare increase). Fare revenues from significant ridership increases during this period have been offset by the effect of riders taking advantage of MetroCard incentives and unlimited-ride passes, thus reducing the non-student average fare from \$1.38 in 1996 to \$1.19 in 2003.

Ridership, Passenger Revenue, and Average Fare



GOVERNMENT'S OVERALL FINANCIAL POSITION, RESULTS OF OPERATIONS AND IMPORTANT ECONOMIC CONDITIONS (CONTINUED)

At the same time, operating expenses have grown annually, mostly due to general wage and benefit increases and service increases in subways, buses and paratransit to meet demand from increased ridership.

The effect of the above is an ongoing deterioration in operating results, which have been offset during the 1996 through 2002 period by operating and tax-based subsidies combined with operating expense control in non-service and maintenance areas. The tax-based subsidies are contingent upon the local economic employment environment. In 2003, the operating deterioration was offset by the May 2003 fare increase.

On March 6, 2003, the MTA Board voted to increase the Authority's subway and bus fares effective May 4, 2003. This fare increase should enable the Authority, as required by law, to be self sustaining on a cash basis through 2004. The basic MetroCard, cash or single-ride ticket fare increased from \$1.50 to \$2.00. The bonus percentage increased from ten percent to twenty percent and the minimum purchase required to receive the bonus decreased from \$15.00 to \$10.00. In the previous fare structure, a customer received eleven rides for the price of ten rides, while under the new fare structure the customer receives six rides for the price of five. The sale of tokens ended on April 12, 2003, token usage on subways ended May 4, 2003 and token usage on buses ended at the end of the year. MetroCard seven-day passes increased from \$17 to \$21, and MetroCard thirty-day passes increased from \$63 to \$70. The approximate increase in passenger revenue resulting from the fare increase was \$290 for 2003 (partial year, May-December) and is projected to be \$420 in 2004 (full year).

Subsequent to 2004, the deterioration in operating results is anticipated to continue due to escalating pension and health & welfare costs and inflation-level wage increases, while operating revenues are expected to be relatively unchanged. Additionally, debt service costs are projected to grow annually while subsidies are assumed to remain relatively level.

SIGNIFICANT CAPITAL ASSET ACTIVITY

Capital Program

The Authority's portion of the current MTA Capital Program for 2000-2004 totals \$10.1 billion. As of December 31, 2003, \$8.7 billion has been committed under the five-year plan, of which \$4.2 billion has been expended. Funding sources for the Capital Program come mostly from new money bonds, federal funds, money made available through debt restructuring and City capital funding.

Among the projects included in the 2000-2004 Transit Capital Program and subsequent amendments are the following: rebuilding the 1/9 line track and structures destroyed by the September 11, 2001 attacks on the World Trade Center, design and initiation of construction of the full-length Second Avenue Subway, acquisition of 1,130 new subway cars, replacing 927 existing cars and expanding the fleet by 203 cars, acquisition of 1,065 new buses, including 300 clean fuel buses, rehabilitation of 64 stations, provision for full Americans with Disability Act (ADA) accessibility at 26 stations, replacement of 32 escalators at various stations, replacement of approximately 40 miles of mainline track, signal modernization, communications improvements and improvements to shops, yards and depots.

CURRENTLY KNOWN FACTS, DECISIONS, OR CONDITIONS

In July 2003, the MTA Capital Construction Company was created by action of the MTA Board of Directors as a public benefit corporation subsidiary of the MTA under section 1266(s) of the Public Authorities Law. The mission of the new subsidiary company is to plan, design and construct current and future major MTA system expansion projects. Projects currently underway include all activities associated with Long Island Rail Road East Side Access, the #7 Line Extension, the Lower Manhattan Fulton Transit Center, the new South Ferry station complex, system-wide capital Security Projects and the Second Avenue Subway, which are consolidated under the management of the MTA Capital Construction Company.

The possible inclusion of non-MTA bus transportation providers is still under consideration.

New York City Transit Authority
Consolidated Balance Sheets
December 31, 2003 and 2002
(In thousands)

	<u>2003</u>	<u>2002</u>
Assets		
Current assets:		
Cash (note 3)	\$ 36,847	\$ 36,109
MTA Investment Pool (note 4)	220,857	299,896
Receivables:		
Billed and unbilled charges due from New York City	23,728	22,857
Accrued subsidies	89,804	65,417
Due from MTA and constituent Authorities	404,437	131,121
Other	57,712	51,370
Less allowance for doubtful accounts	<u>(26,368)</u>	<u>(23,683)</u>
Net receivables	549,313	247,082
Investments - restricted for debt service (note 3)	-	19,539
Materials and supplies	155,134	156,849
Prepaid pension expenses (note 6)	114,388	72,029
Prepaid expenses and other current assets	<u>24,192</u>	<u>15,154</u>
Total current assets	<u>1,100,731</u>	<u>846,658</u>
Due from New York City for capital cost reimbursement (note 1)	-	265
Due from MTA for purchase of capital assets	469,077	771,064
Capital assets, net of accumulated depreciation (note 5)	20,769,963	19,123,455
Leased property under capital lease, net of accumulated amortization (note 5)	102,923	119,515
Leasehold improvements on property, net of accumulated depreciation (note 5)	202,663	215,601
Deferred expenses related to issuance of debt	14,945	15,513
Restricted deposits and other escrow funds	<u>771</u>	<u>708</u>
Total assets	<u>\$ 22,661,073</u>	<u>\$ 21,092,779</u>

(Continued)

See accompanying notes to consolidated financial statements.

New York City Transit Authority
Consolidated Balance Sheets
December 31, 2003 and 2002
(In thousands)

	<u>2003</u>	<u>2002</u>
Liabilities and Net Assets		
Current liabilities:		
Bank overdrafts payable	\$ 89,048	\$ 33,409
Accounts payable	66,237	79,485
Accrued expenses:		
Salaries, wages, and payroll taxes	89,542	147,983
Vacation, sick pay and other benefits	436,243	387,183
Retirement and death benefits (note 6)	41,107	8,985
Estimated liability arising from injuries to persons (note 10)	108,192	107,143
Other	67,896	50,394
Total accrued expenses	742,980	701,688
Car overhaul program	5,218	5,351
Due to MTA for repayment of debt, current portion (note 7)	6,430	6,197
Unredeemed farecards and tokens	158,421	134,558
Deferred subsidy revenue	6,885	6,885
Total current liabilities	1,075,219	967,573
Due to MTA for repayment of Certificates of Participation (note 7)	226,124	229,600
Obligations under capital lease, long-term (note 5)	124,678	134,749
Accrued retirement and death benefits (note 6)	58,931	60,790
Estimated liability arising from injuries to persons (note 10)	656,302	626,460
Restricted deposits and other escrow funds	771	708
Other long-term liabilities	30,996	35,659
Total liabilities	2,173,021	2,055,539
Net assets:		
Invested in capital assets, net of related debt	20,718,317	19,088,025
Restricted	-	19,539
Unrestricted	(230,265)	(70,324)
Total net assets	20,488,052	19,037,240
Commitments and contingencies (notes 1, 10, and 11)	-	-
Total liabilities and net assets	\$ 22,661,073	\$ 21,092,779

See accompanying notes to consolidated financial statements.

New York City Transit Authority
Consolidated Statements of Revenues, Expenses and Changes in Net Assets
Years Ended December 31, 2003 and 2002
(In thousands)

	<u>2003</u>	<u>2002</u>
Revenues:		
Operating revenues:		
Rapid transit	\$ 1,673,175	\$ 1,502,811
Surface transit	703,574	631,563
School, elderly, and paratransit reimbursement	124,355	120,924
Advertising and other	82,104	78,675
	<u>2,583,208</u>	<u>2,333,973</u>
Expenses:		
Salaries and wages	2,496,944	2,433,862
Retirement and death benefits	360,869	277,512
Other employee benefits	557,394	487,931
Materials and supplies	233,734	243,103
Fuel and power	195,460	183,503
Outside computer, engineering, and other services	250,405	233,791
Public liability	80,528	73,275
Depreciation	828,957	760,868
Other expenses	121,978	111,467
Reimbursed overhead expenses	(160,683)	(165,712)
	<u>4,965,586</u>	<u>4,639,600</u>
Operating loss	(2,382,378)	(2,305,627)
Nonoperating revenues:		
Tax-supported subsidies:		
New York State	973,141	855,710
New York City	173,103	178,687
Operating Assistance subsidies:		
New York State	158,672	158,672
New York City	158,672	158,672
Triborough Bridge and Tunnel Authority	242,501	100,101
World Trade Center disaster insurance recovery	244,500	-
Less: Amounts provided to Staten Island Rapid Transit Operating Authority	(2,475)	(2,945)
	<u>1,948,114</u>	<u>1,448,897</u>
Total nonoperating revenues	<u>1,948,114</u>	<u>1,448,897</u>
Interest expense	(29,433)	(86,548)
Loss on disposal of subway cars (note 5)	(30,749)	(58,287)
	<u>1,887,932</u>	<u>1,304,062</u>
Total nonoperating income	<u>1,887,932</u>	<u>1,304,062</u>
Loss before capital contributions	(494,446)	(1,001,565)
Capital contributions (note 2)	1,945,258	7,067,738
	<u>1,450,812</u>	<u>6,066,173</u>
Change in net assets	<u>1,450,812</u>	<u>6,066,173</u>
Net assets:		
Beginning of year	19,037,240	12,971,067
End of year	<u>\$ 20,488,052</u>	<u>\$ 19,037,240</u>

See accompanying notes to consolidated financial statements.

New York City Transit Authority
Consolidated Statements of Cash Flows
Years Ended December 31, 2003 and 2002
(In thousands)

	<u>2003</u>	<u>2002</u>
Cash flows from operating activities:		
Cash received from passengers, tenants, advertisers, and others	\$ 2,499,979	\$ 2,375,433
Cash payments for payroll and related employee costs	(3,417,342)	(3,129,786)
Cash payments to suppliers for goods and services	<u>(717,674)</u>	<u>(684,407)</u>
Net cash used in operating activities	<u>(1,635,037)</u>	<u>(1,438,760)</u>
Cash flows from noncapital financing activities:		
Subsidies received	1,659,094	1,686,406
Increase in bank overdraft	<u>55,639</u>	<u>8,463</u>
Net cash provided by noncapital financing activities	<u>1,714,733</u>	<u>1,694,869</u>
Cash flows from capital and related financing activities:		
Principal payments	(7,028)	(6,795)
Interest paid	(17,195)	(307,646)
Payments on MTA Transportation bonds issued to fund capital assets	(323,829)	-
Subsidies designated for debt service payments	119,218	200,341
Capital project costs incurred for capital program	(746,169)	(734,397)
Reimbursement of capital project costs from MTA	<u>795,592</u>	<u>721,581</u>
Net cash used in capital and related financing activities	<u>(179,411)</u>	<u>(126,916)</u>
Cash flows from investing activities:		
Purchase of investment securities	(3,146)	(9,674)
Proceeds from sale and maturities of investments	22,071	21,839
Decrease (increase) in MTA Investment Pool	79,039	(139,826)
Interest on investments	<u>2,489</u>	<u>3,172</u>
Net cash provided by (used in) investing activities	<u>100,453</u>	<u>(124,489)</u>
Net increase in cash	738	4,704
Cash at:		
Beginning of year	<u>36,109</u>	<u>31,405</u>
End of year	<u>\$ 36,847</u>	<u>\$ 36,109</u>

(Continued)

See accompanying notes to consolidated financial statements.

New York City Transit Authority
Consolidated Statements of Cash Flows
Years Ended December 31, 2003 and 2002
(In thousands)

	<u>2003</u>	<u>2002</u>
Reconciliation of cash flows from operating activities:		
Operating loss	\$ (2,382,378)	\$ (2,305,627)
Adjustments to reconcile operating loss to net cash used in operating activities		
Interest income	(2,277)	(3,337)
Depreciation	<u>828,957</u>	<u>760,868</u>
	(1,555,698)	(1,548,096)
Changes in operating assets and liabilities:		
Increase in farecard and token liability	23,863	21,984
(Decrease) increase in accrued salaries, wages, and payroll taxes	(58,441)	13,046
Decrease in accounts payable and other accrued liabilities	(346)	(11,975)
Increase in accrued vacation and sick pay benefits	49,060	15,096
Increase (decrease) in accrued retirement and death benefits	30,263	(2,833)
Increase in estimated liability and arising from injuries to persons	30,892	41,755
(Increase) decrease in operating receivables	(104,815)	22,813
(Increase) decrease in prepaid expenses and other current assets	(9,038)	7,279
(Increase) decrease in prepaid pension expense	(42,359)	11,501
Decrease (increase) in materials and supplies and change in car overhaul program liability	<u>1,582</u>	<u>(9,330)</u>
Net cash used in operating activities	<u>\$ (1,635,037)</u>	<u>\$ (1,438,760)</u>
Supplemental schedule of noncash capital and related financing activities:		
Fair value of assets contributed	\$ 1,352,782	\$ 1,055,962
Debt issued by affiliated agency for capital assets	-	247,072

See accompanying notes to consolidated financial statements.

New York City Transit Authority

Notes to Consolidated Financial Statements

December 31, 2003 and 2002

1. Financial Statements

Reporting Entity

The accompanying consolidated financial statements include the accounts of the New York City Transit Authority (Transit Authority), and its subsidiary, the Manhattan and Bronx Surface Transit Operating Authority (MaBSTOA) (collectively, the Authority), which are public benefit corporations created pursuant to the Public Authorities Law (the Act) of the State of New York (the State) to operate public subway and bus services within the City of New York (the City).

MaBSTOA is a subsidiary of the Transit Authority and, therefore, the financial results of MaBSTOA are combined with those of the Transit Authority in the consolidated financial statements. The MaBSTOA Pension Plan (the Plan) is not a component unit of the Transit Authority, in accordance with Governmental Accounting Standards Board (GASB) Statement No. 14, *The Financial Reporting Entity*, and, therefore, the financial results of the Plan are not included in the Authority's consolidated financial statements.

The Authority has material transactions with affiliated agencies included in the Metropolitan Transportation Authority (MTA) financial reporting group. Such agencies include the MTA, Triborough Bridge and Tunnel Authority (TBTA), Metro North Commuter Railroad (MNCR), Long Island Rail Road (LIRR), Metropolitan Suburban Bus Authority (MSBA or LIB), and the Staten Island Rapid Transit Operating Authority (SIRTOA).

The Authority is a part of the financial reporting group of the MTA and is included in the combined financial statements of the MTA in accordance with GASB Statement No. 14. The MTA is a component unit of the State and is included in the State of New York Comprehensive Annual Financial Report of the State Comptroller as a public benefit corporation.

In July 2003, the MTA Capital Construction Company was created by action of the MTA Board of Directors as a public benefit corporation subsidiary of the MTA under section 1266(s) of the Public Authorities Law. The mission of this new subsidiary company is to plan, design and construct current and future major MTA system expansion projects. Projects currently underway, include all activities associated with Long Island Rail Road East side access, the #7 Line Extension, the Lower Manhattan Fulton Transit Center, the new South Ferry station complex, system-wide capital Security Projects, and the Second Avenue Subway which are consolidated under the management of the MTA Capital Construction Company.

The possible inclusion of non-MTA bus transportation providers is still under consideration.

Operations

Operations are conducted pursuant to leases with the City which expired on November 1, 1989, except that the terms of the leases continue so long as any financing agreement between the Authority and the MTA and any MTA Transportation Revenue Bonds remain outstanding (see note 7). The City has the option to terminate the leases at any time. In the event of termination, the City is required to assume the assets and liabilities of the Authority and must pay or make provision for the payment of any debt incurred pursuant to financing agreements of the Authority.

New York City Transit Authority

Notes to Consolidated Financial Statements

December 31, 2003 and 2002

Substantial operating deficits (the difference between operating revenues and expenses) result from the essential services that the Authority provides; such operating deficits will continue in the foreseeable future. To meet the funding requirements of these operating deficits, the Authority receives subsidies from:

- (a) The State in the form of annual subsidies of special State and regional tax revenues, operating assistance, and reimbursement of certain expenses;
- (b) The City in the form of operating assistance, tax revenues, and reimbursement of certain expenses; and
- (c) An affiliated agency (TBTA), in the form of a portion of its operating surplus.

The New York State Public Authorities Law and the financing agreement between the Authority and the MTA provide that the Authority shall establish fares, tolls, and other fees for the use of its facilities as may be necessary to maintain its combined operations on a self-sustaining basis as defined in such law. It is the opinion of management that the Authority is in compliance with these requirements. The Authority is not liable for real estate taxes, franchise taxes, or sales taxes on substantially all of its purchases or other excise taxes on its properties.

Capital Financing

1992-1999 Capital Programs

The MTA has ongoing programs on behalf of the Authority and other affiliated agencies, subject to approval by the New York State Metropolitan Transportation Authority Capital Program Review Board (the State Review Board), which are intended to improve public transportation in the New York Metropolitan area. The 1992-1999 Capital Programs (the Capital Programs) totaled \$18.1 billion, of which the Authority's portion amounted to \$12.6 billion. The Capital Programs are, and are expected to continue to be, funded by federal capital grants, City capital funds, MTA bonds secured by system revenues and other sources, bonds issued and to be issued by the TBTA, proceeds from the sale of tax benefits on leasing transactions, and by direct transfers of operating budget revenues raised expressly for the purpose of supporting the Capital Programs.

At December 31, 2003, \$12.6 billion has been committed to Authority projects from the 1992-1999 approved plan, of which approximately \$12.0 billion has been expended.

Approved 2000-2004 Capital Program

The 2000-2004 Capital Program, which was approved by the State Review Board in May 2000, provided for \$18.1 billion in capital expenditures, of which the Authority's portion was \$10.3 billion. In May and December of 2002, the MTA Board approved amendments to the program reflecting changes to budgets, schedules, funding and added to the infrastructure and facilities security programs. Subsequently, the program has evolved as capital work has been awarded, investment strategies modified and the mix of funding has changed. In December 2003, the MTA Board approved a general update to the plan to incorporate changes and authorized its submission to the MTA Capital Program Review Board (CPRB). In January 2004, the MTA Board approved a further modification to that program to support the accelerated purchase of additional commuter railcars. The current MTA approved plan is now \$19.3 billion, of which the Authority's share is

New York City Transit Authority

Notes to Consolidated Financial Statements

December 31, 2003 and 2002

\$10.1 billion. Among the projects included in the 2000-2004 Transit Capital Program and subsequent amendments are the following: rebuilding the 1/9 line track and structures destroyed by the September 11, 2001 attacks on the World Trade Center, design and initiation of construction of the full-length Second Avenue Subway, acquisition of 1,130 new subway cars, replacing 927 existing cars and expanding the fleet by 203 cars, acquisition of 1,065 new buses, including 300 clean fuel buses, rehabilitation of 64 stations, provision of full Americans with Disability Act (ADA) accessibility at 26 stations, replacement of 32 escalators at various stations, replacement of approximately 40 miles of mainline track, signal modernization, communications improvements, and improvements to shops, yards, and depots.

The combined funding sources for the 2000-2004 Capital Program include \$7.0 billion in new money bonds, \$6.2 billion in federal funds, \$4.5 billion from debt restructuring, \$0.5 billion in City capital funding, \$0.3 billion from sale and leasing of assets and \$0.8 billion from other sources.

As part of the 2000-2004 Capital Program, the MTA, the TBTA and the Authority have refunded and defeased substantially all of their outstanding debt and consolidated most of their existing credits.

While the 2000-2004 Capital Program has been approved by the State legislature, there can be no assurance that the funding sources identified will be available in the amounts and at the times contemplated or that the Capital Program will not be delayed or reduced. If the implementation of the 2000-2004 Capital Program is significantly delayed, the Authority's efforts to bring the entire transit system to a state of good repair and to prevent deterioration of portions of the transit system which have already reached a state of good repair may be impeded, with potential negative effects on ridership and fare revenues.

At December 31, 2003, \$8.7 billion has been committed to Authority projects from the 2000-2004 approved plan, of which approximately \$4.2 billion has been expended.

Pursuant to a Memorandum of Understanding (MOU) dated May 20, 1996, by and among the MTA, the Authority, and the City, the Authority was authorized, and made grant transfers to the City totaling \$250 million through 1997. In exchange, the City agreed to pay \$500 million from its capital budget to fund the Authority's capital program. The intent of the MOU was to provide additional capital funding to the Authority which did not require the issuance of bonds supported by Authority revenues, including fare receipts. As of December 31, 2003, the receivable due from the City for the first \$250 million has been fully recovered. The second \$250 million is recognized as capital contributions when the City reimburses the Authority for the costs of certain capital projects. As of December 31, 2003, the City has reimbursed the Authority \$221.8 million for capital projects included in the second \$250 million amount.

2. Accounting Policies

Basis of Accounting

In accordance with GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, the Authority applies all applicable GASB pronouncements, as well as all Financial Accounting Standards Board (FASB) Statements and Interpretations issued on or before November 30, 1989 that do not conflict

New York City Transit Authority

Notes to Consolidated Financial Statements

December 31, 2003 and 2002

with GASB pronouncements. Subsequent to November 30, 1989, the Authority exclusively applies all applicable GASB pronouncements.

These financial statements have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America.

New Accounting Standards

In March 2003, the Governmental Accounting Standards Board (“GASB”) issued GASB Statement No. 40, Deposit and Investment Risk Disclosures, an Amendment of GASB Statement No. 3. The Statement establishes more comprehensive disclosure requirements addressing common risks of the deposits and investments of state and local governments. The Statement is effective for financial statements for periods beginning after June 15, 2004. Adoption of this Statement is not expected to have a material impact on the Authority’s consolidated financial statements.

In November 2003, the GASB issued Statement No. 42, Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries. The Statement defines and establishes new guidance for accounting and reporting for the impairment of capital assets and for insurance recoveries. The Statement is effective for financial statement periods beginning after December 15, 2004. We are evaluating the impact the adoption of GASB 42 may have on the Authority’s consolidated financial statements.

During 2002, the Authority adopted GASB Statement No. 34, Basic Financial Statements – and Management’s Discussion and Analysis – for State and Local Governments (GASB34) as amended by GASB Statement No 37, Basic Financial Statements – and Management’s Discussion and Analysis – for State and Local Governments: Omnibus, and GASB Statement No. 38, Certain Financial Statement Note Disclosures. The Authority follows the “business type” activity requirements of GASB 34 which requires that resources be classified for accounting and reporting purposes into the following three net asset categories:

- Invested in capital assets, net of related debt: Capital assets, net of accumulated depreciation and outstanding principal balances of debt attributable to the acquisition, construction or improvement of those assets.
- Restricted:

Nonexpendable – Net assets subject to externally imposed stipulations such that the Authority maintains them permanently. For the years ended December 31, 2003 and 2002, the Authority did not have nonexpendable net assets.

Expendable – Net assets whose use by the Authority is subject to externally imposed stipulations that can be fulfilled by actions of the Authority pursuant to those stipulations or that expire by the passage of time.

- Unrestricted: Net assets that are not subject to externally imposed stipulations. Unrestricted net assets may be designated for specific purposes by actions of management or the Board of Directors or may otherwise be limited by contractual agreements with outside parties.

New York City Transit Authority

Notes to Consolidated Financial Statements

December 31, 2003 and 2002

Subsidies

The Authority receives subsidies from various sources including the State and the City. In general, these subsidies are subject to annual appropriations by the governmental units and periodic approval of the continuation of the taxes supporting the subsidies.

The principal funding sources for the Authority are as follows:

Operating Assistance Appropriations and Grants

The Authority receives, subject to annual appropriations, State and City operating assistance funds. The funds received under the State transit operating assistance program are fully matched by contributions from the City. State and City operating assistance subsidies are recognized as non-operating revenue in the amount of the respective annual appropriation when such appropriation becomes effective.

Triborough Bridge and Tunnel Authority

The New York State Public Authorities law requires the TBTA to transfer its annual operating surplus, as defined, to the Authority and the MTA. The initial \$24 million of the operating surplus is provided to the Authority and the balance is divided equally between the Authority and the MTA. However, the amounts transferred to the Authority and the MTA are net of a provision for debt service on TBTA bonds issued to finance the acquisition of facilities under their respective portions of the Capital Program. For the years ended December 31, 2003 and 2002, \$171.0 million and \$161.0 million, respectively, were paid from the operating surplus of the TBTA to satisfy the Authority's portion of debt service requirements. Included in the 2003 TBTA operating surplus is \$64.0 million representing amounts received related to 2002 TBTA excess debt service funds. Additionally, in 2002, the Authority reduced the amount of TBTA operating surplus recognized by \$3.9 million to reimburse the MTA for the MTA's portion of the allocation of debt service on TBTA Beneficial Interest Certificates.

Mortgage Recording Taxes

Under New York State law, the MTA receives operating and capital assistance from the State Mortgage Recording Tax, which is collected by the City and the seven counties within the MTA transportation region, at the rate of one-quarter of 1% of the debt secured by certain real estate mortgages. Such legislation governs the use of the funds from this revenue source whereby the proceeds of this tax are first used by the MTA to meet the operating costs of the MTA headquarters, with the remaining funds allocated 55% to the Authority and 45% to the commuter railroads for their capital and operating needs. The Authority recognizes such sources of funds when designated by the MTA for the Authority's use. The portion of this subsidy attributable to the Authority is reported in "tax-supported subsidies: New York State" in the accompanying consolidated statements of operations and surplus. The Authority records the portion of its State Mortgage Recording Tax subsidy which funds principal and interest payments on long-term debt, net of investment earnings on unexpended proceeds, used to construct capital assets as capital contributions.

New York City Transit Authority

Notes to Consolidated Financial Statements

December 31, 2003 and 2002

In addition, the State designated for the MTA's use an additional mortgage recording tax (the Additional Mortgage Recording Tax) of one-quarter of 1% of mortgages secured by real estate improved or to be improved by structures containing one to six dwelling units in the MTA transportation region. The funds from this additional tax are available, after satisfying debt service requirements, to meet the capital and operating needs of the Authority and the commuter railroads.

The Authority recognizes such sources of funds when designated by the MTA for the Authority's use. The MTA designated \$0 million in 2003 and \$113.9 million in 2002 for the Authority's debt service requirements. In addition, in 2003 the MTA disbursed \$178.6 million of available funds from the Additional Mortgage Recording Tax (after satisfying debt service requirements) to the Authority. The Authority has utilized these funds to meet capital and operating needs.

The Authority receives operating assistance directly from the City through the City Mortgage Recording Tax at the rate of five-eighths of 1% of the debt secured by certain real estate mortgages and through the Real Property Transfer Tax at the rate of 1% of certain properties' assessed value (collectively referred to as Urban Tax Subsidies). These Urban Tax Subsidies are reflected in tax supported subsidies: New York City in the accompanying consolidated statements of operations and surplus. These funds are recognized as revenue, based upon the reported amount of taxes collected by the City from underlying transactions, within the Authority's fiscal year.

New York State Regional Mass Transit Taxes

The Authority receives, subject to annual appropriations, revenues from taxes enacted by the State legislature from various taxing sources.

In 1980, the State enacted a series of taxes, portions of which are deposited in the Metro Mass Transportation Operating Account (MMTOA), to fund the operating deficits of State mass transportation systems. MMTOA taxes currently include a business privilege tax imposed on petroleum business in the State, a one-quarter of 1% sales and use tax on certain personal property and services, a corporate franchise tax imposed on transportation and transmission companies, and a temporary franchise tax surcharge on certain corporations, banks, insurance, utility, and transportation companies attributable to business activity carried on in the State. MMTOA taxes are subject to annual appropriation, availability of sufficient tax collections, and determination of operating need by the State for the MTA. They are recognized as revenue in the amount of the annual appropriation when such appropriation becomes effective.

Under New York State law, subject to annual appropriation, the MTA receives operating and capital assistance through a portion of petroleum business tax receipts, certain motor fuel taxes, and certain motor vehicle fees, which are collected by the State. Such assistance is required by law to be allocated, after provision for debt service on any bonds secured by such taxes, 85% to the Authority and 15% to the commuter railroads for their operating and capital needs. MTA Dedicated Tax Fund Bonds (DFT Bonds), Series 2002A, Series 2002B, and Series 2001A, are secured by certain petroleum business tax receipts. The Authority recognizes such sources of funds when designated by the MTA for the Authority's use. A portion of the petroleum business tax receipts collected by the MTA is used to satisfy the debt service requirements for the DTF Bonds and is recorded as capital contributions.

New York City Transit Authority
Notes to Consolidated Financial Statements
December 31, 2003 and 2002

The composition of New York State tax-supported subsidies for 2003 and 2002 is as follows:

	2003		2002	
	Accrued Revenue	Cash	Accrued Revenue	Cash
	(In thousands)			
Petroleum business tax (a)	\$ 293,564	\$ 276,607	\$ 280,468	\$ 371,072
Metro mass tax	463,242	463,242	575,242	791,184
Mortgage recording taxes (b)	216,335	196,381	-	-
	\$ 973,141	\$ 936,230	\$ 855,710	\$ 1,162,256

(a) Net of \$119,218 and \$86,402 for debt service payments in 2003 and 2002, respectively.

(b) Net of \$0 and \$113,939 for debt service payments in 2003 and 2002, respectively.

Paratransit

Pursuant to an agreement between the City and the MTA, the Authority, effective July 1, 1993, assumed operating responsibility for all paratransit service required by the Americans with Disability Act of 1990. Services are provided by private vendors under contract with the Authority. The City reimburses the Authority for the lesser of 33% of net paratransit operating expenses defined as labor, transportation, and administrative costs less fare revenues and 6% of gross urban tax proceeds as described above or, an amount that is 20% greater than the amount paid by the City for the preceding calendar year. Fare revenues and the City reimbursement aggregated approximately \$36.5 million in 2003 and \$32.0 million in 2002. Total paratransit expenses were \$144.3 million and \$129.9 million in 2003 and 2002, respectively.

Reimbursement of Expenditures

Engineering and labor costs incurred by the Authority for capital projects are reimbursed under the capital program by the MTA to the extent that they relate to approved expenditures applicable to capital projects primarily initiated after April 1, 1982. They are reimbursed by the City to the extent they relate to amounts approved for prior projects. In 2003 and 2002, reimbursements were netted against gross operating expenses on the statements of Revenues, Expenses and Changes in Net Assets.

Fare and Service Reimbursement from the State and City

The City no longer fully reimburses the Authority for costs of the free fare program for students; however, pursuant to a 1995 agreement with the State and the City, the Authority continued the student program beginning with the 1995-1996 school year, with the State and the City each agreeing to pay \$45 million per annum. The estimated cost of this program is approximately \$154 million for the 2003-2004 school year. It is believed the City will continue to provide for the continuation of the City's \$45 million contribution for the 2003-2004 school year, of which \$15 million was received in December 2003. The Authority's approved 2004 Adopted Budget assumes that the remaining \$30 million from the City will be received in 2004. It also assumes that the State's full \$45 million for the 2003-2004 school year will be received in 2004. The Authority's

New York City Transit Authority

Notes to Consolidated Financial Statements

December 31, 2003 and 2002

2004-2007 Financial Plan assumes the continuation of the joint funding of the free fare program for students.

Prior to April 1995, the City was obligated to reimburse the Authority for the transit police force. As a result of the April 1995 merger of the transit police force into the New York City Police Department, the City no longer reimburses the Authority for the costs of policing the Transit System on an ongoing basis since policing of the Transit System is being carried out by the New York City Police Department at the City's expense. The Authority continues to be responsible for certain capital costs and support services related to such police activities, a portion of which is reimbursed by the City. The Authority received approximately \$4.2 million in 2003 and 2002 for the reimbursement of transit police costs (see note 11).

Due from MTA and Constituent Authorities

Due from MTA and constituent authorities consists of reimbursements due from the MTA Capital Program for billed and unbilled charges relating to capital projects, farecards and tokens on consignment with sister agencies, and intercompany operating receivables, payables, and inter agency loan transactions.

Prepaid Expenses and Other Current Assets

The Authority prepaid \$8.0 million to the New York State Health Insurance Plan (NYSHIP) and \$16.1 million for insurance coverage during 2003. In 2002, \$15.1 million was paid towards insurance coverage. The various policies cover environmental liability, sabotage and terrorism, property and excess liability.

Due from MTA for Purchase of Capital Assets

Due from MTA for purchase of capital assets consists of funds held by the MTA which are restricted for capital asset acquisitions by the Authority pursuant to the 1982 Transit Facility Special Obligation Bond Resolution. This capital program pool is comprised of non-bond proceed funds derived from safe harbor and sale/leaseback transactions, operating fund transfers, legal settlements, TBTA bond purchase rights and swap option agreements, and interest earnings on these pooled funds.

Capital Assets

Capital assets acquired prior to April 1982 were funded primarily by the City, with capital grants made available to the Authority. The City has title to a substantial portion of such assets and, accordingly, these assets are not recorded on the books of the Authority. Subsequent acquisitions, which are part of the capital program, are recorded at cost by the Authority. Funding sources for the acquisition of these capital assets include federal, State, and City capital grants, grants from the Port Authority of New York and New Jersey, the proceeds from the issuance of Transportation Revenue Bonds, and various TBTA bonding and other sources. Capital assets are recorded at cost and are depreciated on a straight-line basis over 25 or 35 years for subway cars, 12 years for buses, and lives generally ranging from 10 years to 60 years for the other capital assets. Cost includes capitalized interest apportioned to assets during construction. For the purposes of this calculation, interest expense is reported net of investment income.

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Contributed Capital

For fiscal year 2001, with the implementation of GASB Statements No. 33 and No. 36, capital assets contributed by the MTA and restricted funds due from the MTA for the purchase of capital assets are recorded as capital contributions on the consolidated statement of revenues, expenses and changes in net assets. In fiscal year 2000 and prior, such items were recorded as additions to contributed capital in the consolidated balance sheets. Capital contributions for the years ended December 31, 2003 and 2002 consist of the following:

	<u>2003</u>	<u>2002</u>
	(In thousands)	
Capital assets contributed by MTA from:		
Federal grants	\$ 389,051	\$ 353,064
Other than federal grants	1,631,027	1,334,031
Capital assets contributed by MTA for WTC disaster replacement	(31,472)	103,900
Capital assets contributed by New York City for grant transfers	26,966	31,324
New York State mortgage recording taxes received for principal and interest payments on debt	-	113,939
Petroleum business taxes received for principal and interest payments on debt	119,218	86,402
Principal and interest payments on MTA Transportation bonds issued to fund capital assets	(103,179)	-
(Decrease) increase in restricted funds due from MTA for purchase of capital assets	(66,671)	477,885
Extinguishment of debt issued to fund capital assets (note 7)	(19,682)	4,567,193
	<u>\$ 1,945,258</u>	<u>\$ 7,067,738</u>
Total capital contributions		

Passenger Revenue

Revenues from the sale of farecards and tokens are recognized as income as the farecards and tokens are used and are reported as operating income.

Materials and Supplies

Materials and supplies are recorded at average cost net of a reserve for obsolescence.

Staten Island Rapid Transit Operating Authority

The Staten Island Rapid Transit Operating Authority (SIRTOA) is a wholly owned subsidiary of the MTA and provides transportation service on Staten Island. SIRTOA is managed by the Authority on behalf of the City under a contract which provides that the City fund SIRTOA's deficit. The Authority has no responsibility for the operating deficit of SIRTOA. The Authority collects on SIRTOA's behalf its share of certain operating assistance subsidies determined by formula and transfers such subsidies to SIRTOA. The amount of subsidy funds to which SIRTOA is entitled is recorded as a reduction of the subsidy revenues of the Authority. Separate financial

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statements are issued by SIRTOA and may be obtained by writing to SIRTOA, 60 Bay Street, 5th Floor, Staten Island, New York 10301.

Employee Benefits

Pension cost is required to be measured and disclosed using the accrual basis of accounting. Annual pension cost should be equal to the annual required contributions (ARC) to the pension plan, calculated in accordance with certain parameters.

In 2003, and as a result of the most recent collective bargaining agreement, the Authority assumed responsibility for providing health benefits to its employees who are members of the TWU Local 100 as well as to retirees who were members of the TWU Local 100 and reach normal retirement age while working for the Authority. Previously, these benefits were being provided by the TWU Health Benefits Trust (the Trust) with the Authority required to make monthly contributions to the Trust on behalf of the participants on a 'pay as you go' basis. The majority of the benefits provided under the plan are self insured with administrative services provided by various health insurance companies.

The Authority has therefore recorded a liability for claims incurred but not reported (IBNR). The liability represents those estimated future payments that are attributable, under the plan's provisions, to services rendered to participants prior to year end. The estimated liability of claims includes benefits expected to be paid to retired or terminated employees or their beneficiaries and present employees or their beneficiaries, as applicable. The estimated liability for claims incurred but not reported or paid is \$37 million as of December 31, 2003.

Investments

Investments maturing and expected to be liquidated within a year of December 31 have been classified as current assets in the consolidated financial statements. Investments included in the debt service reserve funds pursuant to the Authority's various bond resolutions are recorded at amounts which approximate fair value.

Receivables

Receivables are recorded as amounts due to the Authority, reduced by an allowance for doubtful accounts to report the receivables at net realizable value.

Reclassifications

Reclassification of certain prior year amounts have been made to conform to the current year presentation.

Accounting Estimates

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

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3. Cash and Investments

Cash consists of the following as of December 31:

	2003		2002	
	Book Balance	Bank Balance	Book Balance	Bank Balance
	(In thousands)			
Insured (FDIC) and collateralized deposits	\$ 4,066	\$ 3,632	\$ 3,696	\$ 3,376
Less escrow and other restricted deposits	(1,054)	(1,074)	(791)	(806)
Insured funds on-hand and in-transit	33,835	-	33,204	-
	<u>\$ 36,847</u>	<u>\$ 2,558</u>	<u>\$ 36,109</u>	<u>\$ 2,570</u>

The on-hand and in-transit funds consist primarily of passenger revenue funds collected but not yet deposited.

The Authority invests the unused proceeds from the Transit Facilities Revenue Bonds, Series 1990 and Transit Facilities Refunding Revenue Bonds, Series 1993 (see note 8), held for debt service accounts and debt service reserve accounts, in repurchase agreements collateralized by U.S. Treasury securities, U.S. Treasury bills, and U.S. Treasury notes as permitted by the State Public Authorities Law. All investments are held by the Authority's agent in custody accounts in the name of the Authority. During 2002, the MTA issued the Transportation Bonds, Series 2002 A, B, C, D and E. A portion of the proceeds were applied to refund all of the outstanding Transit Facilities Refunding Revenue Bonds, Series 1990 and 1993.

As of December 31, 2003 and 2002, the cost and market values of these restricted investments consist of the following:

	2003		2002	
	Cost	Fair Value	Cost	Fair Value
	(In thousands)			
Investments - short-term				
U.S. Treasury notes	\$ -	\$ -	\$ 18,146	\$ 18,758
U.S. Treasury bills	-	-	780	781
	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 18,926</u>	<u>\$ 19,539</u>

Earnings on these investments, which were liquidated and used to pay debt service in February 2003, amounted to \$0.7 million and \$1.0 million in 2003 and 2002, respectively.

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4. MTA Investment Pool

The MTA, on behalf of the Authority, invests funds which are not immediately required for the Authority's operations in securities permitted by the State Public Authorities Law, including repurchase agreements collateralized by U.S. Treasury securities, U.S. Treasury notes, and U.S. Treasury zero coupon bonds. All investments are held by the MTA's agent in custody accounts in the name of the MTA. The Authority's earnings from short-term investments approximated \$1.6 million and \$2.4 million for the years ended December 31, 2003 and 2002, respectively. Approximately \$221.0 million of funds are included in the MTA investment pool in the consolidated balance sheet as of December 31, 2003.

In December 1998, the MTA Board approved the establishment of the MTA New York City Transit General Reserve Fund in the amount of \$113.0 million. Funds held therein including interest earned, shall be expended per MTA Board approval to stabilize the Authority's cash flow requirements as needed. The balance in the reserve fund was approximately \$10.8 million and \$240.3 million for the years ended December 31, 2003 and 2002, respectively. These funds are included in the MTA Investment Pool in the accompanying consolidated balance sheets.

5. Capital Assets

Capital assets, at December 31, consist of the following:

	December 2002	Additions	Scrap Buses/ Subway Cars	December 2003
	(In thousands)			
Subway cars	\$ 5,168,532	\$ 580,843	\$ (63,170)	\$ 5,686,205
Buses	1,572,765	165,367	(419)	1,737,713
Track and structures	5,283,469	939,281	-	6,222,750
Depots and yards	2,658,040	211,699	-	2,869,739
Stations	3,630,602	497,401	-	4,128,003
Signals	1,555,382	325,913	-	1,881,295
Service vehicles	188,098	875	-	188,973
Building	169,584	-	-	169,584
Other	1,987,731	234,457	-	2,222,188
Under construction	3,302,989	(470,268)	-	2,832,721
	<u>25,517,192</u>	<u>2,485,568</u>	<u>(63,589)</u>	<u>27,939,171</u>
Less: Allowance for depreciation	<u>(6,393,737)</u>	<u>(808,311)</u>	<u>32,840</u>	<u>(7,169,208)</u>
	<u>\$ 19,123,455</u>	<u>\$ 1,677,257</u>	<u>\$ (30,749)</u>	<u>\$ 20,769,963</u>

Due to the terrorist attacks on September 11, 2001, the Authority recorded a loss on impairment of capital assets of approximately \$172.6 million during 2001. Refer to note 11 in the consolidated financial statements for a further discussion of the impact of the World Trade Center disaster.

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During 2001, the Authority began replacement of certain subway car fleets. The Authority scrapped 296 and 405 cars in 2003 and 2002, respectively. Loss on disposal of capital assets of \$30.7 million and \$58.3 million were recorded for the years ended December 31, 2003 and 2002, respectively. The Authority, to a large extent, concluded the fleet disposal program in 2003.

In 1990, the Authority issued approximately \$202.8 million of Transit Facility Revenue Bonds, Series 1990 to fund the acquisition of an office building located in Brooklyn, New York. The bonds were subsequently defeased in May 2002 by the MTA Transportation bonds. The property is located on land owned by the New York City Economic Development Corporation, as trustee for the City, with whom the Authority has entered into a 99-year ground lease. Rent expense, on a cash basis, under the lease for 2003 and 2002, was approximately \$566,000 each year.

Capitalized interest totaled \$23.5 million and \$70.8 million in 2003 and 2002, respectively. This included \$0 million and \$31.9 million in noncash capitalized interest transfers from the TBTA recorded by the Authority in 2003 and 2002, respectively, on capital program expenditures funded by TBTA debt.

Lease Transaction

In July 1998, the MTA, the Authority and TBTA authorized and entered into a lease and related agreements whereby each agency, as a sublessee, rents office space at Two Broadway in lower Manhattan. The triple-net-lease has an initial stated term of approximately 50 years; with the right to extend the lease for two successive 15-year periods at a rental of at least 95% of fair market rent. Remaining payments under the lease approximate \$1.5 billion. Under the subleases, the lease is apportioned as follows: the Authority, 68.7%, MTA, 21%; and TBTA, 10.3%. However, the involved agencies have agreed to sub-sublease space from one another as necessary to satisfy actual occupancy needs. The agencies will be responsible for obligations under the lease based on such actual occupancy percentages. Projected occupancy percentages at December 31, 2003 for the Authority and TBTA were 75.6% and 25.4%, respectively. The Authority's sublease is for a year-to-year term, automatically extended, except upon the giving of a nonextension notice by the Authority.

The lease is comprised of both operating and capital elements, with the portion of the lease attributable to the land recorded as an operating lease, and the portion of the lease attributable to the building recorded as a capital lease. Operating rent expenses under the Authority's sublease amounted to \$7.5 million in both 2003 and 2002.

Additionally, MTA entered into a Coordination and Monitoring Agreement with the lessor, Two Broadway LLC. As part of this agreement, \$68.3 million was advanced to the lessor, as of December 31, 1999, to finance contracted base building improvements from proceeds of the 1999 Certificates of Participation. Under the agreement, the lessor was to reimburse the advance with 1.25% interest, primarily through rent credits during the lease term. The obligation to pay these rent credits had been disputed by the lessor. Given the uncertainty of the collectibility of the advance through rent credits, the Authority's portion of the net discounted advance at December 31, 2000 of \$30.5 million was reclassified to base building improvements during fiscal year 2001. Amounts expended in fiscal years 2003 and 2002 have also been recorded as base building improvements.

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In November 2003, the MTA and its affiliates and subsidiaries entered into a settlement agreement with the lessor. As part of the settlement, the MTA received rent credits against the ground lease rent totaling \$45.0 million that will be credited over the next 30 years at 1.25% interest. As a result of the settlement, the Authority reduced its "Obligations under capital lease" and the corresponding "Leased property under capital lease" asset by \$14.0 million in the consolidated 2003 balance sheet, which represents the Authority's portion of the discounted rent credits.

Assuming the projected occupancy percentage at December 31, 2003 will continue, the revised future minimum lease payments under the Authority's sublease, as affected by the rent credits, are as follows:

Year Ending December 31:	<u>Operating</u>	<u>Capital</u>
	(In thousands)	
2004	\$ 7,452	\$ 8,454
2005	7,452	8,454
2006	7,452	8,454
2007	7,452	8,454
2008	7,452	8,454
2009-2013	37,260	50,106
2014-2018	37,260	58,571
2019-2023	37,260	67,713
2024-2028	37,260	77,586
2029-2033	37,260	98,121
2034-2038	37,260	116,440
2039-2043	37,260	128,878
2044-2048	33,530	128,076
	<u>\$ 331,610</u>	<u>767,761</u>
Total minimum lease payments		
Less imputed interest		<u>(643,083)</u>
Present value of net minimum lease payments		<u>\$ 124,678</u>

The adjusted capital lease for the aforementioned building is being amortized over the remaining life of the lease. The cost of the building and related accumulated amortization at December 31, 2003 and 2002 is as follows:

	<u>2003</u>	<u>2002</u>
	(In thousands)	
Capital lease - building	\$ 114,489	\$ 128,510
Less accumulated amortization	<u>(11,566)</u>	<u>(8,995)</u>
Capital lease - building, net	<u>\$ 102,923</u>	<u>\$ 119,515</u>

In July 1999 and July 2000, the MTA issued Certificates of Participation in the amount of \$328.2 million and \$121.2 million, respectively, to finance the renovation of the building and certain other tenant improvements (see note 7).

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The amount of such improvements apportioned to the Authority as of December 31, 2003 and 2002 is as follows:

	<u>2003</u>	<u>2002</u>
	(In thousands)	
Base building improvements	\$ 131,738	\$ 129,790
Tenant improvements	99,623	99,039
Furniture and fixtures	11,434	11,434
Computers and equipment	7,789	6,028
Development fees	6,893	6,866
Capitalized interest	9,289	9,237
	<u>266,766</u>	<u>262,394</u>
Less: Accumulated depreciation	<u>(64,103)</u>	<u>(46,793)</u>
Total leasehold improvements	<u>\$ 202,663</u>	<u>\$ 215,601</u>

6. Employee Benefits

New York City Employee's Retirement System

Plan Description

The Authority contributes to the New York City Employees' Retirement System (NYCERS), a cost-sharing, multiple-employer public employee retirement system (PERS) for employees of the City and certain other governmental units whose employees are not otherwise members of the City's four other main pension systems. The NYCERS plan combines features of a defined benefit pension plan with those of a defined contribution pension plan. NYCERS provides pension benefits to retired employees based on salary and length of service. In addition, NYCERS provides disability benefits, accident benefits, cost-of-living adjustments, and death benefits subject to satisfaction of certain service requirements and other provisions. The NYCERS plan functions in accordance with existing New York State statutes and New York City laws and may be amended by action of the State legislature. NYCERS issues a publicly available comprehensive annual financial report that includes financial statements and required supplementary information. That report may be obtained by writing to the New York City Employees' Retirement System, 335 Adams Street, Suite 2300, Brooklyn, NY 11201-3751.

Funding Policy

The contribution requirements of Plan members and the Authority are established and amended by law. The Authority's contribution to NYCERS is actuarially determined. The current rate is 1.2% of annual covered payroll. The Authority's contribution to NYCERS for the Authority's fiscal years ending December 31, 2003, 2002, and 2001 were \$68.8, \$30.7 and \$19.5 million, respectively. These amounts cover the Authority's annual required contributions for the NYCERS 2003 and 2002 fiscal years ended June 30, as well as a portion of the annual required contribution for the 2004 NYCERS fiscal year. The remainder of the 2004 annual required contribution is expected to be paid subsequent to year-end within the NYCERS fiscal year. In 2003, the Authority

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received a refund from NYCERS of \$6.3 million related to the overpayment of the annual required contribution recorded in fiscal 2002.

For most Transit Authority employees hired prior to July 27, 1976, NYCERS is noncontributory. Certain employees who entered qualifying service after July 27, 1976, commonly referred to as Tier 4, contributed 3% of their salary (see chapter 10 and 126 of the laws of 2000 below).

55/25 and Age 57 Pension Elections

In 1994, hourly employees and certain operating supervisors participating in the NYCERS plan were given the opportunity to elect the Transit 55/25 option, which enabled such employees to become eligible for pension benefits upon reaching 25 years of service and at least 55 years of age. Employees hired after July 26, 1994 in the above titles are mandated into the Transit 55/25 option. All participants were required to make an additional employee contribution of 2.3%.

In 1995, managerial employees and certain other employees participating in the NYCERS plan were given the opportunity to elect a 25 Year Early Retirement plan, which enabled such employees to become eligible for pension benefits upon reaching 25 years of service and at least 55 years of age. Managerial and certain other employees entering after June 28, 1995 were mandated into the Age 57 option. Legislation finalized in 2000 changed the 57/10 plan to allow service retirement after age 57 and completion of five years of service (five-year vesting). Employees electing these options must contribute an additional 2.85% of their gross salary.

Legislation passed in 1999 enabled elective participants in the Transit 55/25 and the 25 Year Early Retirement plans who, by age 62 would not have 25 years of allowable service with the Authority, to withdraw from the applicable plan and revert back to their previous plan.

Amendments enacted by State legislation in 2000 reflect the most recent significant changes to the plan and are summarized as follows:

For operating employees (Chapter 10 of the Laws of 2000)

- All operating employees are automatically included in the Transit 55/25 plan except those who are in the Age 57 plan who elect to remain in that plan.
- Elimination of the 2.3% additional employees contributions applicable to members of the Transit 55/25 plan.
- Reduction in the Tier 3 and 4 employee contribution rate from 3.0% to 2.0%.

For nonoperating employees (Chapter 126 of the Laws of 2000):

- Vesting under the Age 57 plan requires only five years of service.
- As of October 1, 2000, regular Tier 3 and 4 employee contributions cease after the completion of ten years of credited service.

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For retired members (Chapter 125 of the Laws of 2000):

- Automatic COLAs. The COLAs apply to retired members as follows:

<u>Retirees at Least Age</u>	<u>Retired or Receiving Benefits for at least</u>
62	5 years
65	10
Disabled retirees	5
Accidental death beneficiaries	5

- Initial COLA payable September 30, 2000 based on the first \$18,000 of the maximum retirement allowance.
- Thereafter, annual COLAs of 50% of the increase in the consumer price index (CPI) but not less than 1% or more than 3%, of the first \$18,000 of maximum retirement allowance will be payable.

These benefit enhancements, as well as the automatic COLA for retirees, were reflected in the actuarial valuation beginning with the June 30, 2000 valuation.

The Plan adopted several amendments during 2002 as a result of State Legislation. Amendments include changes to the definition of active service for Tier 1 and Tier 2 members, extension of the phase in period from five years to ten years for funding liabilities created by Chapter 125 of the Laws of 2000 and increases in accidental disability benefits for Tier 3 and Tier 4 members.

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Actuarial Assumptions

The more significant actuarial assumptions and methods used in the calculation of employer contributions to NYCERS for the plan's fiscal years ended June 30, 2003 and 2002 are as follows:

<u>Valuation dates</u>	<u>June 30, 2003</u>	<u>June 30, 2002</u>
Actuarial cost method	Frozen initial liability ⁽¹⁾	Frozen initial liability ⁽¹⁾
Amortization method for Unfunded Actuarial Accrued Liabilities (UAAL)	Level dollar for UAAL attributable to Early Retirement Incentive (ERI) 1999. All outstanding components of UAAL are being amortized over closed periods.	Level dollar for UAAL attributable to Early Retirement Incentive (ERI) 1999. All outstanding components of UAAL are being amortized over closed periods.
Remaining amortization period	3 years for 1999 ERI and 4 years for 2000 ERI. 5 years for 2002 ERI	4 years for 1999 ERI and 5 years for 2000 ERI.
Actuarial Asset Valuation Method (AAVM)	Modified five-year moving average of market values with Market Value Restart as of June 30, 1999. As of June 30 thereafter, the AAVM recognizes investment returns greater or less than expected over a period of 5 years.	Modified five-year moving average of market values with Market Value Restart as of June 30, 1999. As of June 30 thereafter, the AAVM recognizes investment returns greater or less than expected over a period of 5 years.
Assumed rate of return on investments	8.0% per annum ⁽²⁾	8.0% per annum ⁽²⁾
Postretirement mortality	Tables based on recent experience	Tables based on recent experience
Active service, withdrawal, death, disability, service retirement	Tables based on recent experience	Tables based on recent experience
Salary increases	In general, merit and promotion increase including an assumed general wage increase of 3.0% per year ⁽²⁾	In general, merit and promotion increase including an assumed general wage increase of 3.0% per year ⁽²⁾
Cost-of-living adjustments	1.3% per annum ⁽²⁾	1.3% per annum ⁽²⁾

(1) Under this actuarial cost method, the initial liability has been established by the Entry Age Actuarial Cost Method but with the UAAL not less than zero.

(2) Developed assuming a long-term consumer price inflation assumption of 2.5% per year.

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Manhattan and Bronx Surface Transit Operating Authority

Plan Description

The Authority contributes to the Manhattan and Bronx Surface Transit Operating Authority (MaBSTOA) Plan, a single employer governmental retirement plan. MaBSTOA provides retirement, disability, and death benefits to plan members and beneficiaries which are similar to those benefits provided by NYCERS to similarly situated Transit Authority employees. Article 12.08 of the MaBSTOA Plan assigns the authority to establish and amend the benefit provisions to the MaBSTOA Board. MaBSTOA issues a publicly available financial report that includes financial statements and required supplementary information for the plan. That report may be obtained by writing to MaBSTOA Pension Plan, New York City Transit Authority, Operations Accounting, 130 Livingston Street, 8th Floor, Brooklyn, NY 11201.

Funding Policy

The contribution requirements of plan members are established and may be amended only by the MaBSTOA Board in accordance with Article 10.01 of the MaBSTOA Plan. MaBSTOA's funding policy for periodic employer contributions is to provide for actuarially determined amounts that are designed to accumulate sufficient assets to pay benefits when due. It is MaBSTOA's policy to fund, at a minimum, the current year's normal pension cost plus amortization of the unfunded actuarial accrued liability.

The Authority's contributions to the MaBSTOA Plan for the years ended December 31, 2003, 2002, and 2001 were \$137.0 million, \$123.5 million and \$116.1 million, respectively, equal to the annual required contributions for each year. During 2003 and 2002, the Authority made advance payments of \$114.4 million and \$72.0 million, respectively, resulting in the recognition of a pension asset in the accompanying consolidated balance sheets.

For employees, the Plan has both contributory and noncontributory requirements depending on the date of entry into service. Employees entering qualifying service on or before July 26, 1976 are non-contributing. Certain employees entering qualifying service on or after July 27, 1976 are required to contribute 3% of their salary (see 2000 Plan Amendments).

The MaBSTOA Pension Plan includes the Transit 55/25 Plan, the 25 Year Early Retirement Plan, the Age 57 Plan, and the 2000 amendments under the same terms and conditions as NYCERS.

The cost of additional benefit enhancements to the Plan will be funded by an increase in the employer's normal contribution rate. The cost of the above Plan amendments was reflected in the January 1, 2000 and January 1, 2001 actuarial valuations and increased the Plan's UAAL by approximately \$67.9 million and \$75.2 million, respectively.

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Annual Pension Cost and Net Pension Obligation

The Authority's annual pension cost and net pension obligation for MaBSTOA for the years ended December 31, 2003, 2002, and 2001 were as follows:

	<u>2003</u>	<u>2002</u>	<u>2001</u>
	(In thousands)		
Annual required contribution	\$ 137,012	\$ 123,501	\$ 116,080
Interest on net pension obligation	5,015	5,167	5,319
Adjustment to annual required contribution	<u>(6,874)</u>	<u>(7,008)</u>	<u>(7,166)</u>
Annual pension cost	135,153	121,660	114,233
Contributions made	<u>(137,012)</u>	<u>(123,501)</u>	<u>(116,080)</u>
Decrease in net pension obligation	(1,859)	(1,841)	(1,847)
Net pension obligation at beginning of year	<u>60,790</u>	<u>62,631</u>	<u>64,478</u>
Net pension obligation at end of year	<u>\$ 58,931</u>	<u>\$ 60,790</u>	<u>\$ 62,631</u>

Actuarial Assumptions

Several changes in actuarial assumptions were made by the Plan, effective with the January 1, 2001 actuarial valuation. These changes in assumptions decreased the Plan's UAAL by approximately \$16.9 million. There have been no changes to the actuarial assumptions since the January 1, 2001 valuation. The more significant actuarial assumptions and methods used in the calculation of employer contributions to the MaBSTOA Plan for the years ended December 31, 2003 and 2002 are as follows:

<u>Valuation dates</u>	<u>January 1, 2003</u>	<u>January 1, 2002</u>
Actuarial cost method	Frozen initial liability ⁽¹⁾	Frozen initial liability ⁽¹⁾
Amortization method for UAAL	30-year level dollar	30-year level dollar
Actuarial asset valuation method	Market value restart as of 1/1/96, then five-year moving average of market values	Market value restart as of 1/1/96, then five-year moving average of market values
Interest rate	8.25% per annum ⁽²⁾ , prior to expenses	8.25% per annum ⁽²⁾ , prior to expenses
Provision for expenses	0.35% of market value of assets plus two-year average of administrative charges	0.35% of market value of assets plus two-year average of administrative charges
Deaths after retirement	Tables based on recent experience	Tables based on recent experience

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<u>Valuation dates</u>	<u>January 1, 2003</u>	<u>January 1, 2002</u>
Separations other than for normal retirement	Tables based on recent experience	Tables based on recent experience
Rates of normal retirement	Tables based on recent experience	Tables based on recent experience
Salary increases	In general, merit and promotion increases plus assumed general wage increases of 3.5% to 18.0% for operating employees and 4.5% to 7.0% for nonoperating employees per year, depending on years of service	In general, merit and promotion increases plus assumed general wage increases of 3.5% to 18.0% for operating employees and 4.5% to 7.0% for nonoperating employees per year, depending on years of service
Overtime	Except for managerial employees, 8.5% of base salary for operating employees and 3.0% of base salary for nonoperating employees, with different assumptions used in the year before retirement	Except for managerial employees, 8.5% of base salary for operating employees and 3.0% of base salary for nonoperating employees, with different assumptions used in the year before retirement
Cost-of-living adjustments	1.3% per annum ⁽²⁾	1.3% per annum ⁽²⁾

(1) Under this actuarial method, the initial liability has been established by the Entry Age Actuarial Cost Method but with the UAAL not less than zero.

(2) Assumes a long-term consumer price inflation assumption of 2.5% per annum.

Deferred Compensation Plans

Certain Authority employees are eligible to participate in a deferred compensation plan established in 1985 in accordance with Internal Revenue Code (IRC) Section 457. On August 20, 1996, the IRC Section 457 guidelines were amended requiring governmental entities to place Section 457 deferred compensation plan assets in a trust for the benefit of the plan's members. GASB Statement No. 32, *Accounting and Financial Reporting for IRC Section 457 Deferred Compensation Plans*, was issued effectively requiring that once plan assets are placed into trust they be removed from the financial statements of the entity. The assets in the plan which have been excluded from the consolidated balance sheets at December 31, 2003 and 2002 totaled \$297.3 million and \$240.0 million, respectively.

Beginning in 1988, the MTA and its affiliated agencies' employees are participants in a second deferred compensation plan established in accordance with IRC Section 401(k). All amounts of compensation deferred under this plan, and all income attributable to such compensation, are solely the property of the participants and thus this plan is not reflected in the accompanying consolidated balance sheets.

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Postretirement Benefits

In addition to providing pension benefits, the Authority provides certain health care and life insurance benefits for retired employees. Substantially all of the Authority's employees may become eligible for those benefits if they reach normal retirement age while working for the Authority. The Authority recognizes the costs of providing those benefits by expensing the contributions to the Transport Workers Union (TWU) Health & Welfare Trust Fund and other funds, and the annual insurance premiums for retiree benefits, which aggregated \$162.6 million and \$124.4 million for the years ended December 31, 2003 and 2002, respectively. At December 31, 2003 and 2002, there were 30,846 and 31,350 retired employees, respectively. In 2003 and as a result of the most recent collective bargaining agreement, the Authority assumed responsibility for directly providing health care benefits to TWU retirees rather than via the TWU Health & Welfare Trust Fund.

7. Due to MTA for Repayment of Debt

Transit Facilities Revenue Bonds

Pursuant to state legislation, the MTA is currently authorized to issue on behalf of the MTA, the Authority, and the TBTA (net of statutory exclusions) revenue bonds and parity obligations to finance capital improvements as contemplated by the MTA Capital Program. The revenue bonds are special obligations of the MTA, payable solely from and collateralized by a pledge of all of the gross operating revenue and operating subsidies of the Authority, excluding reimbursements for project labor and engineering costs.

Substantially all of the outstanding debt of MTA, Triborough Bridge and Tunnel Authority ("TBTA") and the Authority was restructured during 2002 by consolidating most existing credits into four principal new credits:

- MTA Transportation Revenue Bonds,
- MTA State Service Contract Bonds,
- MTA Dedicated Tax Fund Bonds, and
- TBTA General Revenue Bonds and TBTA Subordinate Revenue Bonds.

In connection with the debt restructuring, the following MTA and Authority bonds and notes that were secured by Authority operating revenues were paid or defeased with the proceeds of MTA's Transportation Revenue Bonds:

- MTA Transit Facilities Revenue Bonds and Bond Anticipation Notes, and
- Transit Authority Subordinated Transit Facilities Revenue Bonds (Livingston Plaza Project).

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The Transportation Revenue Bonds are special obligations of MTA, payable from, and secured by a pledge of:

- The gross operating revenues of Long Island Rail Road, Metro-North Commuter Railroad Company, and the Authority and its subsidiary, MaBSTOA, until monthly deposits of principal and interest are satisfied under the Transportation Revenue Bond Resolution,
- TBTA's operating surplus,
- General operating subsidies from the State and local governments,
- Special tax-supported operating subsidies, and
- Station maintenance and service reimbursements.

In addition, as part of the debt restructuring, the Dedicated Tax Fund (DTF) Bonds and the TBTA Mortgage Recording Tax Special Obligation Bond, which were apportioned to the Authority, were paid or defeased with the proceeds of the MTA Dedicated Tax Fund Bonds and TBTA General Revenue Bonds and TBTA Subordinate Revenue Bonds, respectively.

In a separate transaction, on December 19, 2002, MTA defeased the MTA Excess Loss Fund Special Obligation Bonds, Series 1998, thereby defeasing the Authority's payment obligations with respect thereto.

The MTA's approved 2000-2004 Capital Program anticipates funding \$7.0 billion of the cost of the plan with the proceeds from DTF Bonds, Transportation Revenue Bonds, and TBTA bonds. A portion of the proceeds will be used to finance the Authority's \$10.1 billion portion of the Capital Program.

The Authority is required to deposit all of its pledged revenues with a trustee for the bondholders. Such funds are first applied to meet all obligations under the revenue bonds, and the remainder is returned to the Authority for its operating needs.

The MTA is responsible for all payments from these bond proceeds and for administering the debt service reserve funds and the unexpended bond funds and has recorded the liability for these bonds. Prior to the debt restructuring, the Authority had recorded a liability to the MTA to the extent of the Authority's expenditure of such bond proceeds. Debt service paid by the Authority is net of the amount provided from the MTA's investment of the unexpended bond funds.

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Summary of Amounts Due to MTA for Repayment of Debt

Prior to December 31, 2002, the Authority recognized as a liability in the accompanying consolidated balance sheets the portion of the bond proceeds pledged to the Authority by the MTA for the acquisition of capital assets to the extent of the Authority's expenditure of such bond proceeds. As a result of the MTA's bond restructuring during fiscal year 2002 and except for the Authority's portion of the Certificates of Participation, the Authority no longer records a liability to the MTA for the portion of the bonds utilized to fund the Authority's capital program. Amounts due to the MTA for repayment of debt at December 31, 2003 and 2002 consist of the following:

	<u>December 31,</u> <u>2002</u>	<u>Refunded</u>	<u>Issued</u> <u>(In thousands)</u>	<u>Principal</u> <u>Payments</u>	<u>December 31,</u> <u>2003</u>
Certificates of Participation					
Series 1999A: 4.50% - 5.63%, due through 2029	\$ 216,641	\$ -	\$ -	\$ 3,858	\$ 212,783
Series 2000A: 4.85% - 5.88%, due through 2030	79,291	-	-	2,339	76,952
	<u>295,932</u>	<u>-</u>	<u>-</u>	<u>6,197</u>	<u>289,735</u>
Less: Unamortized discount	-	-	-	-	-
	295,932	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 6,197</u>	289,735
Payment due in one year	(6,197)				(6,430)
Debt service reserve funds and unexpended proceeds held by affiliates	<u>(60,135)</u>				<u>(57,181)</u>
Total long term	<u>\$ 229,600</u>				<u>\$ 226,124</u>

In June 1999 and June 2000, the MTA issued approximately \$328.2 million and \$121.2 million, respectively, of its Series 1999A and Series 2000A Certificates of Participation. The proceeds from these issuances were used to finance certain building and leasehold improvements to an office building at Two Broadway to be occupied by the Authority, the MTA or its subsidiaries, and the TBTA. Both series represent proportionate interests in the principal and interest components of base rent paid severally, but not jointly, by the Authority, the MTA, and the TBTA pursuant to a Leasehold Improvement Sublease Agreement dated as of June 1, 1999. The Authority, the MTA, and the TBTA are obligated to pay 68.7%, 21.0%, and 10.3%, respectively, of the base rent under the Leasehold Improvement Sublease. The principal amounts of the Series 1999A and Series 2000A certificates are payable in various installments and in various amounts beginning January 1, 2000 and 2001, respectively, through January 1, 2029 and 2030, respectively. Interest was paid on January 1, 2001 and 2002 and is payable each January 1 and July 1, thereafter, until maturity, at rates ranging from 4.50% to 5.63% and 4.85% to 5.88% for the Series 1999A and Series 2000A, respectively. In addition, each issuance is subject to prepayment prior to maturity, as defined.

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Future debt service payments including interest, at December 31, 2003 are as follows:

	<u>Interest</u>	<u>Principal</u> <u>(In thousands)</u>	<u>Total</u>
Year ending December 31:			
2004	\$ 15,433	\$ 6,430	\$ 21,863
2005	15,127	6,678	21,805
2006	14,803	6,942	21,745
2007	14,489	6,073	20,562
2008	14,174	6,368	20,542
2009 - 2013	65,238	37,297	102,535
2014 - 2018	53,385	48,822	102,207
2019 - 2023	38,112	63,723	101,835
2024 - 2028	18,417	82,904	101,321
2029	976	24,498	25,474
	<u>\$ 250,154</u>	<u>\$ 289,735</u>	<u>\$ 539,889</u>

Interest paid on the Series 2000A and Series 1999A Certificates of Participation amounted to \$17.2 million in 2003 and \$17.5 million in 2002.

In November 2002, TBTA defeased the Mortgage Recording Tax Special Obligation bonds, therefore the Authority no longer records a liability to the MTA for the portion of the bonds utilized to fund the Authority's capital program.

In April 2000 and November 2001, respectively, the MTA issued approximately \$344.6 million and \$544.1 million of its Series 2000A and Series 2001A DTF Bonds. The proceeds of the DTF Bonds were used to fund the projects in the Transit and Commuter Rail Capital Programs and to fund debt service requirements. The DTF Bonds are special obligations of the MTA payable from, and secured by, certain petroleum business tax receipts, certain motor fuel taxes, and certain motor vehicle fees held in the MTA Dedicated Tax Fund. The MTA is responsible for all payments from the bond proceeds and for administering the debt service reserve funds and the unexpended bond funds and has recorded the liability for these bonds. Prior to December 31, 2002, the Authority had recorded a liability to the MTA to the extent of the Authority's expenditure of such bond proceeds. As a result of the MTA's debt restructuring during fiscal year 2002, the Authority no longer records a liability to the MTA for the portion of the DTF bonds utilized to fund the Authority's capital program.

The interest portion of debt service payments on the Transportation Revenue Bonds and the MTA DTF Bonds amounted to \$168.8 million in 2003 and \$276.7 million in 2002.

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8. Advertising and Other Income

Advertising and other income for the years ended December 31, 2003 and 2002 consist of:

	<u>2003</u>	<u>2002</u>
	(In thousands)	
Advertising revenue	\$ 59,877	\$ 55,122
Interest income	2,277	3,337
Transit Adjudication Bureau collections	6,479	6,218
Station income	9,028	8,590
Rental income	2,723	2,357
All other	1,720	3,051
	<u>\$ 82,104</u>	<u>\$ 78,675</u>

9. Other Expenses

Other expenses for the years ended December 31, 2003 and 2002 consist of:

	<u>2003</u>	<u>2002</u>
	(In thousands)	
Rentals	\$ 31,168	\$ 28,869
Insurance premiums	25,457	16,484
Heating fuel	15,224	10,204
Miscellaneous electric	10,087	9,918
Telephone and telecommunications	7,192	10,524
Allowance for (recovery) of uncollectible accounts	6,141	(1,132)
Data communications	4,726	4,589
Water and sewage	3,375	5,507
Insurance recoveries	(558)	(8,903)
Other miscellaneous expenses	19,166	35,407
	<u>\$ 121,978</u>	<u>\$ 111,467</u>

10. Risk Management

The Authority is exposed to various risks of loss related to torts; theft of, damage to, and destruction of its assets; injuries to persons, including employees; and natural disasters.

The Authority is self-insured up to certain per occurrence limits for liability claims arising from injuries to persons, excluding employees. Claims arising prior to November 1, 1995 are subject to a \$5 million per occurrence limit; claims arising between November 1, 1996 and October 31, 2001 are subject to a \$6 million per occurrence limit; and claims arising after October 31, 2001 are subject to a \$7 million per occurrence limit. The Authority is self-insured for work-related injuries to employees. The annual cost associated with injuries to persons, other than employees, and damage to third-party property, is reflected as expenses: public liability in the accompanying consolidated statements of operations and change in net assets.

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The Authority establishes its liability for injuries to employees and to the general public on the basis of independent actuarial estimates of future liability.

A summary of activity in estimated liability arising from injuries to persons, including employees, and damage to third-party property, for the years ended December 31, 2003 and 2002, is as follows:

	<u>2003</u>	<u>2002</u>
	<u>(In thousands)</u>	
Balance at beginning of year	\$ 733,603	\$ 691,847
Activity during the year:		
Current year claims and changes in estimates	147,864	148,565
Claims paid	<u>(116,973)</u>	<u>(106,809)</u>
Balance at end of year	764,494	733,603
Less: Current portion	<u>(108,192)</u>	<u>(107,143)</u>
Long-term liability	<u>\$ 656,302</u>	<u>\$ 626,460</u>

Through October 31, 2003, claims over the applicable per occurrence limits up to the lesser of the assets available for claims or \$50 million were insured by the Excess Loss Fund (ELF) maintained and managed by the MTA on behalf of itself and its affiliates. The ELF covered the Authority and other MTA subsidiaries and affiliated agencies. Contributions to ELF were not required in 2003 or 2002. On October 31, 2003, First Mutual Transportation Assurance Company ("FMTAC"), a subsidiary of MTA, assumed the existing ELF program on both a retrospective and prospective basis. The retrospective portion contains the same insurance agreements, participant retentions and limits as existed under the ELF program for occurrences happening on or before October 30, 2003. The coverage limit will remain \$50 million per occurrence or the proceeds of the program whichever is less. On a prospective basis, FMTAC will issue insurance policies indemnifying the MTA, its subsidiaries and affiliates above their specifically assigned Self-Insured Retention with a limit of \$50 million per occurrence with \$50 million annual aggregate. On December 12, 2003, the ELF transferred all net assets (\$77.7 million) to FMTAC in order to secure any claims assumed from the ELF, as well as to capitalize the prospective programs and insure current and future claims. FMTAC will charge appropriate annual premiums based on loss experience and exposure analysis to maintain the fiscal viability of the program.

Effective October 31, 2003, an All-Agency Excess Liability Insurance Policy was renewed. This coverage affords the MTA and its subsidiaries and affiliates an additional limit of \$150 million, for a total limit of \$200 million (\$150 million in excess of \$50 million). In certain circumstances, when FMTAC's assets are exhausted due to payment of claims, the All-Agency Excess Liability Insurance will assume FMTAC's coverage position of \$50 million.

There are currently two accidents with outstanding claims which have breached the \$5 million per occurrence limit. In 1990, a fire occurred in a subway tunnel at Clark Street operated by the Authority, resulting in passenger injuries on a subway train passing through the same tunnel. Additionally, in 1991, a subway train operated by the Authority, which derailed at Union Square, resulted in injuries to passengers who were aboard the train.

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In accordance with the terms of the ELF and its successor, FMTAC, the Authority had requested cumulative reimbursement of \$15.0 million for the net losses paid in excess of the per occurrence limits. As of December 31, 2003, this amount has been paid to the Authority.

First Mutual Transportation Assurance Company

The First Mutual Transportation Assurance Company (FMTAC) was established as a captive insurance company on December 5, 1997 and provides reinsurance coverage for property and primary insurance coverage for station liability and force account liability. FMTAC insured property damages or loss exposures in excess of \$15 million per occurrence, \$30 million annual aggregate, for claims brought by the MTA and its subsidiaries and affiliates until October 30, 2001. From October 31, 2001 to January 31, 2002 coverage units were \$500 million per occurrence. By February 1, 2002, coverage limits were increased to \$900 million. This policy excludes coverage for acts of terrorism. Effective November 1, 2001, a stand-alone policy was purchased to cover sabotage and terrorism up to \$70 million in excess of a \$30 million self-insured retention.

Effective October 31, 2003, FMTAC insures property damages or loss exposures in excess of \$25 million per occurrence, \$75 million annual aggregate, up to a limit of \$1 billion for claims brought by the MTA and its subsidiaries and affiliates. This policy excludes acts of terrorism. Effective November 1, 2003, a stand-alone policy was purchased to cover sabotage and terrorism up to \$100 million in excess of a \$25 million self-insured retention. On November 26, 2002, with the enactment of the Terrorism Risk Insurance Act ("TRIA") of 2002, any endorsements, excluding certified acts of terrorism, were void if the act of terrorism is covered by TRIA. The stand-alone terrorism policy is structured to provide \$100 million of coverage in excess of the \$25 million self-insured retention for all acts of terrorism or 10 percent of \$1 billion for those acts covered by TRIA. FMTAC reinsures the majority of its property risks above the \$25 million retention.

At December 31, 2003, the Authority has four outstanding claims covered by FMTAC, with a total exposure of \$9 million (excluding World Trade Center). At December 31, 2003, FMTAC had \$852.2 million of assets to insure current and future claims. The Authority paid premiums of approximately \$11.1 million and \$7.8 million to FMTAC for the policy years November 1, 2003 through October 31, 2004 and November 1, 2002 through October 31, 2003, respectively.

11. Contingencies

The authority is involved in various litigation and claims involving personal liability claims and certain other matters. The ultimate outcome of these claims and suits cannot be predicted at this time. Nevertheless, management does not believe that the ultimate outcome of these matters will have a material effect on the consolidated financial position of the Authority.

The Authority was cited in 1991 by the New York State Department of Environmental Conservation (NYSDEC) for not complying with state requirement for tightness testing of underground storage tanks and for failure to notify NYSDEC of leaking tanks. The Authority is obligated to remediate contaminated soil and groundwater. In 2003 and 2002, the Authority expended \$3.7 million and \$5.9 million, respectively, on such cleanup efforts. Expenditures exclude the cost of capital improvements. Although there were no new incidents requiring accruals during 2003, in 2002 an additional \$6 million in spills and remediation reserves were accrued. At December 31, 2003, the Authority believes that its remaining accrued liability of \$24.3 million is sufficient to cover future costs associated with this cleanup. Also, in 2001, in settlement of

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allegations of noncompliance with various provisions of the Environmental Conservation Law and related regulations concerning petroleum and chemical bulk handling and storage, underground storage tanks, tidal wetlands, and air emission requirements, the Authority and NYSDEC entered into a global consent order resolving the outstanding environmental issues. The financial terms of the global consent required the payment of a \$400,000 penalty and the commitment of \$2.0 million toward implementation of an environmental benefits program. There were no findings of this nature during 2003 or 2002.

On March 31, 1995, the MTA Board agreed to a merger of the transit police with the New York City Police Department, in accordance with a memorandum of understanding between the Authority and the City. Pursuant to the terms of the merger, the Authority's operation of the transit police and the City's obligation to reimburse the cost of operating the transit police terminated, effective April 2, 1995. Additionally, the City has assumed the liability for substantially all past and future costs associated with operating the transit police, including, but not limited to all future pension costs. The Authority has asserted a claim of approximately \$92 million against the City relating to reimbursement of costs incurred in the operation of the transit police. The Authority claims that the City underpaid these amounts in the period from 1988 through December 1994. In January 1995, the Authority filed a demand for arbitration pursuant to the lease governing the overall relationship between the Authority and the City to pursue, among other matters, payment of these arrearages. The arbitration matter has been held in abeyance pending a possible resolution of the matter.

12. Subsequent Events

In April 2004, the MTA settled claims with its property insurance carriers for damage caused as a result of the September 11, 2001 terrorist attack. The Authority's portion of the MTA global settlement was \$244.5 million representing the settlement of claims for losses related to physical damage of property.

In addition, as part of the global settlement, MTA has received funds relating to claims for lost revenues, increased operating expenses, and other expenses associated with the cleanup of its facilities. In the future, the MTA may choose to distribute a portion of these additional funds to the Authority.

**New York City Transit Authority
Required Supplementary Information
Schedule of Funding Progress for the MaBSTOA Pension Plan
(Unaudited)
(In millions)**

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Liability (AAL) Initial Entry Age (b)	Unfunded (AAL) (UAAL) (b-a)	Funded Ratio ((a/b)	Covered Payroll (c)	(UAAL) As a Percentage of Covered Payroll ((b-a)/c)
1/1/96 (1)	316.0	1,188.3	872.3	26.59	321.3	271.5
1/1/97	355.4	1,232.4	877.0	28.84	322.5	271.9
1/1/98 (2)	404.5	1,286.2	881.7	31.45	343.3	256.8
1/1/99	467.6	1,342.0	874.4	34.84	362.0	241.5
1/1/00 (3)	540.1	1,471.8	931.7	36.70	378.9	245.9
1/1/01 (4)	611.5	1,592.5	981.0	38.40	400.5	244.9
1/1/02	656.4	1,614.9	958.6	40.60	432.7	221.5
1/1/03 (5)	629.8	1,564.6	934.8	40.30	450.6	207.5

- (1) Certain actuarial assumptions, including the interest rate and the amortization period of the unfunded actuarial accrued liability, were changed.
- (2) The method for determining valuation compensation and the use of the overtime assumption were changed.
- (3) Pension supplementation payable on September 30, 2000 increased the Plan's UAAL by \$67.9 million.
- (4) Automatic COLA adjustment for 2001 increased the Plan's UAAL by \$75.2 million. This increase was offset, in part, by changes in certain actuarial assumptions, which decreased the Plan's UAAL by \$16.9 million.
- (5) Increased employer contributions in 2003 have resulted in a decrease in the Plan's UAAL.