

**National Railroad Passenger Corporation and Subsidiaries (Amtrak)**

Consolidated Financial Statements

September 30, 2003 and 2002

(With Independent Auditors' Report Thereon)



**National Railroad Passenger Corporation and Subsidiaries (Amtrak)**  
**Consolidated Balance Sheets**  
(In Thousands of Dollars, Except Share Data)

	September 30,	
	<u>2003</u>	<u>2002</u>
<b>ASSETS</b>		
<b>Current Assets:</b>		
Cash and cash equivalents .....	\$ 182,054	\$ 168,806
Receivables, net of allowance for receivable losses of \$33,708 and \$20,041 at September 30, 2003 and 2002, respectively .....	148,394	138,053
Materials and supplies .....	111,720	117,029
Other current assets .....	31,279	25,232
<b>Total current assets</b> .....	<u>473,447</u>	<u>449,120</u>
<b>Property and Equipment:</b>		
Locomotives .....	1,639,375	1,717,078
Passenger cars and other rolling stock .....	2,995,201	3,159,435
Right of way and other properties .....	7,717,900	7,622,528
Leasehold improvements .....	216,807	216,828
<b>Property and equipment, gross</b> .....	<u>12,569,283</u>	<u>12,715,869</u>
Less - Accumulated depreciation and amortization .....	<u>(4,273,951)</u>	<u>(4,091,621)</u>
<b>Total property and equipment, net</b> .....	<u>8,295,332</u>	<u>8,624,248</u>
<b>Other Assets, Deposits, and Deferred Charges:</b>		
Escrowed proceeds on sale-leasebacks .....	836,778	829,161
Deferred charges, deposits, and other .....	336,342	268,466
<b>Total other assets, deposits, and deferred charges</b> .....	<u>1,173,120</u>	<u>1,097,627</u>
<b>Total assets</b> .....	<u>\$ 9,941,899</u>	<u>\$ 10,170,995</u>
<b>LIABILITIES and CAPITALIZATION</b>		
<b>Current liabilities:</b>		
Accounts payable .....	\$ 423,860	\$ 386,881
Accrued expenses and other current liabilities .....	420,321	426,223
Deferred ticket revenue .....	79,942	70,581
Current maturities of long-term debt and lease obligations .....	119,466	90,147
<b>Total current liabilities</b> .....	<u>1,043,589</u>	<u>973,832</u>
<b>Long-Term Debt and Lease Obligations:</b>		
Capital lease obligations .....	3,307,522	3,375,639
Mortgages .....	274,180	304,627
Equipment and other debt .....	191,373	171,979
<b>Total long-term debt and lease obligations</b> .....	<u>3,773,075</u>	<u>3,852,245</u>
<b>Other Liabilities and Deferred Credits:</b>		
Deferred state capital payments .....	335,656	289,251
Casualty reserves .....	217,676	207,606
Deferred gain on sale-leasebacks .....	504,773	526,918
Postretirement employee benefits obligation .....	189,611	157,882
Environmental reserve .....	40,795	43,339
Other .....	13,136	17,584
<b>Total other liabilities and deferred credits</b> .....	<u>1,301,647</u>	<u>1,242,580</u>
<b>Total liabilities</b> .....	<u>6,118,311</u>	<u>6,068,657</u>
<b>Commitments and Contingencies</b>		
<b>Capitalization:</b>		
Preferred stock - \$100 par, 109,396,994 shares authorized, issued and outstanding at September 30, 2003 and 2002 .....	10,939,699	10,939,699
Common stock - \$10 par, 10,000,000 shares authorized, 9,385,694 issued and outstanding at September 30, 2003 and 2002 .....	93,857	93,857
Debt and other paid-in capital .....	11,046,225	10,044,339
Accumulated deficit and comprehensive loss .....	<u>(18,256,193)</u>	<u>(16,975,557)</u>
<b>Total capitalization</b> .....	<u>3,823,588</u>	<u>4,102,338</u>
<b>Total liabilities and capitalization</b> .....	<u>\$ 9,941,899</u>	<u>\$ 10,170,995</u>

*The accompanying Notes are an integral part of these Consolidated Financial Statements*

**National Railroad Passenger Corporation and Subsidiaries (Amtrak)**  
**Consolidated Statements of Operations**  
(In Thousands of Dollars)

	Twelve Months Ended September 30,	
	<u>2003</u>	<u>2002</u>
<b>Revenues:</b>		
Passenger related .....	\$ 1,399,920	\$ 1,468,189
Mail and express .....	77,105	124,753
Commuter .....	269,163	295,225
Other .....	311,763	323,685
State capital payments .....	18,615	16,393
<b>Total revenues</b> .....	<u>2,076,566</u>	<u>2,228,245</u>
<b>Expenses:</b>		
Salaries, wages, and benefits .....	1,556,664	1,617,399
Train operations .....	208,485	247,093
Fuel, power, and utilities .....	188,582	174,952
Materials .....	164,332	141,326
Facility, communication, and office related .....	140,444	154,940
Advertising and sales .....	74,762	98,532
Casualty and other claims .....	119,013	161,458
Depreciation - net of amortization .....	606,068	479,323
Other .....	198,917	206,095
Indirect cost capitalized to property and equipment .....	(50,961)	(57,517)
<b>Total expenses</b> .....	<u>3,206,306</u>	<u>3,223,601</u>
<b>Loss from operations</b> .....	<u>1,129,740</u>	<u>995,356</u>
<b>Other (Income) and Expense:</b>		
Interest income .....	(74,069)	(75,918)
Interest expense .....	218,662	212,458
<b>Other expense - net</b> .....	<u>144,593</u>	<u>136,540</u>
<b>Net loss</b> .....	<u>\$ 1,274,333</u>	<u>\$ 1,131,896</u>

*The accompanying Notes are an integral part of these Consolidated Financial Statements*

**National Railroad Passenger Corporation and Subsidiaries (Amtrak)**  
**Consolidated Statements of Comprehensive Loss**  
(In Thousands of Dollars)

	Twelve Months Ended September 30,	
	<u>2003</u>	<u>2002</u>
<b>Net loss</b> .....	<b>\$ 1,274,333</b>	<b>\$ 1,131,896</b>
<b>Other Comprehensive Loss:</b>		
Unrealized loss on derivatives .....	342	138
Unrealized loss on minimum pension liability adjustment .....	5,961	-
<b>Comprehensive loss</b> .....	<b><u>\$ 1,280,636</u></b>	<b><u>\$ 1,132,034</u></b>

*The accompanying Notes are an integral part of these Consolidated Financial Statements*

**National Railroad Passenger Corporation and Subsidiaries (Amtrak)**  
**Consolidated Statements of Cash Flows**  
(In Thousands of Dollars)

	Twelve Months Ended	
	September 30,	
	<u>2003</u>	<u>2002</u>
<b>Cash Flows From Operating Activities:</b>		
Net loss .....	\$ (1,274,333)	\$ (1,131,896)
Adjustments to reconcile net loss to net cash used in operating activities:		
Gain on sale of subsidiary and air rights .....	(29,815)	(32,847)
Depreciation net of amortization .....	606,068	479,323
Other .....	18,280	(2,271)
Changes in assets and liabilities:		
Receivables .....	(24,007)	(45,177)
Materials and supplies .....	(8,706)	9,204
Other current assets .....	(6,931)	(1,168)
Other assets, deposits, and deferred charges .....	(48,668)	(15,025)
Accounts payable, deferred ticket revenue and other current liabilities .....	46,950	30,354
Deferred federal and state capital payments .....	(2,369)	(12,757)
Other liabilities and deferred credits .....	27,783	102,170
<b>Net cash used in operating activities .....</b>	<b><u>(695,748)</u></b>	<b><u>(620,090)</u></b>
<b>Cash Flows From Investing Activities:</b>		
Purchases and refurbishments of property and equipment .....	(280,544)	(359,216)
Proceeds from disposals of property and equipment .....	25,431	41,122
<b>Net cash used in investing activities .....</b>	<b><u>(255,113)</u></b>	<b><u>(318,094)</u></b>
<b>Cash Flows From Financing Activities:</b>		
Proceeds from federal paid-in capital .....	994,565	1,038,216
Proceeds from federal and state capital payments .....	56,095	65,808
Proceeds from borrowings and lease financings .....	10,303	140,134
Repayments of debt and capital lease obligations .....	(96,854)	(170,230)
<b>Net cash provided by financing activities .....</b>	<b><u>964,109</u></b>	<b><u>1,073,928</u></b>
Net increase in cash and cash equivalents .....	13,248	135,744
Cash and cash equivalents-beginning of period .....	168,806	33,062
Cash and cash equivalents-end of period .....	<u>\$ 182,054</u>	<u>\$ 168,806</u>
<b>Supplemental Disclosure of Cash Payments:</b>		
Interest paid (net of amounts capitalized and non-cash defeased capital lease interest) .....	\$ 163,944	\$ 159,935
<b>Supplemental Disclosure of Noncash Investing and Financing Activities:</b>		
Refinancing of equipment obligations into capital leases .....	\$ 21,282	\$ 259,134
Financed property acquisitions and improvements .....	500	52,682
Property acquired through capital lease obligations .....	11,379	73,555
Debt and capital lease reduction through use of escrow deposits .....	4,258	8,719
Escrowed proceeds received from capital lease and mortgage obligation .....	-	51,047
Property acquired with escrowed deposit .....	16,000	14,829
Debt discharged through sale of subsidiary .....	21,051	-
Other non-cash increases in property, primarily accruals of amounts due for .....	10,154	27,579
Net proceeds from affiliate's bond issuance held in escrow .....	\$ 49,587	\$ -

*The accompanying Notes are an integral part of these Consolidated Financial Statements*

**National Railroad Passenger Corporation and Subsidiaries (Amtrak)**  
**Consolidated Statements of Changes in Capitalization**  
(In Thousands of Dollars)

	Preferred stock	Common stock	Debt and other paid-in capital	Accumulated deficit and comprehensive loss	Totals
<b>Balance at September 30, 2001</b> .....	\$ 10,939,699	\$ 93,857	\$ 8,981,568	\$ (15,843,523)	\$ 4,171,601
Federal paid-in capital .....	-	-	1,038,216	-	1,038,216
Federal capital and other payments .....	-	-	24,555	-	24,555
Net loss .....	-	-	-	(1,131,896)	(1,131,896)
Unrealized loss on derivatives .....	-	-	-	(138)	(138)
<b>Balance at September 30, 2002</b> .....	<u>\$ 10,939,699</u>	<u>\$ 93,857</u>	<u>\$ 10,044,339</u>	<u>\$ (16,975,557)</u>	<u>\$ 4,102,338</u>
Federal paid-in capital .....	-	-	<b>994,565</b>	-	<b>994,565</b>
Federal capital and other payments .....	-	-	<b>7,321</b>	-	<b>7,321</b>
Net loss .....	-	-	-	<b>(1,274,333)</b>	<b>(1,274,333)</b>
Unrealized loss on derivatives and minimum pension liability adjustment ...	-	-	-	<b>(6,303)</b>	<b>(6,303)</b>
<b>Balance at September 30, 2003</b> .....	<u><u>\$ 10,939,699</u></u>	<u><u>\$ 93,857</u></u>	<u><u>\$ 11,046,225</u></u>	<u><u>\$ (18,256,193)</u></u>	<u><u>\$ 3,823,588</u></u>

*The accompanying Notes are an integral part of these Consolidated Financial Statements*

**National Railroad Passenger Corporation and Subsidiaries (Amtrak)**  
**Notes to Consolidated Financial Statements**  
**For the Years Ended September 30, 2003 and 2002**

**NOTE 1: NATURE OF OPERATIONS**

The National Railroad Passenger Corporation (“Amtrak” or the “Company”) is a passenger railroad. All issued and outstanding preferred stock is owned by the United States government (the “Federal Government”) through the United States Department of Transportation (the “DOT”). Its principal business is to provide rail passenger transportation service to the general public in the major intercity travel markets of the United States. The Company also operates commuter rail operations on behalf of several states and transit agencies, provides mail and goods delivery service, provides equipment and right-of-way maintenance services, and has leasing operations.

**NOTE 2: BUSINESS CONDITION AND LIQUIDITY**

**Operations and Liquidity**

Amtrak was incorporated in 1971 pursuant to the Rail Passenger Service Act of 1970 and is authorized to operate a nationwide system of passenger rail transportation. The Company has a history of recurring operating losses and is dependent on subsidies from the Federal Government to operate the national passenger rail system and maintain the underlying infrastructure. These subsidies are usually received through annual appropriations. Amtrak’s ability to continue operating in its current form is dependent upon the continued receipt of subsidies from the Federal Government.

For the fiscal year ending September 30, 2004, Congress has approved an appropriation totaling \$1.225 billion, subject to a 0.59% partial rescission that nets to \$1.218 billion. The DOT may reprogram up to \$2.5 million of the appropriation, at its discretion, and it may reserve \$60 million, as directed by the Surface Transportation Board, to fund costs of commuter rail service should Amtrak cease operations. Both amounts are subject to the partial rescission and may ultimately be made available to Amtrak during the fourth quarter of fiscal year 2004. The \$2.5 million reprogramming is to fund the cost incurred by the Secretary of the United States Department of Transportation (the “Secretary”) to develop and implement a fair competitive bid process to assist states in introducing competition to provide higher quality rail service. In addition to the appropriation, Amtrak is permitted to defer until after fiscal year 2004 the repayment of principal or interest for the \$100 million loan grant by the Federal Railroad Administration (FRA) made in July 2002 (see Note 6). This loan is contingent upon Amtrak's compliance with certain conditions as set forth by the FRA.

The fiscal year 2004 appropriation is in the form of a grant to be administered by the Secretary to provide oversight of the fiscal spending of the Company. House Resolution 2673 (the “2004 Act”) was signed into law on January 23, 2004 as Public Law 108-199 and enables the Secretary to make quarterly grants to the Company, to remain available until September 30, 2004, providing a maximum of \$756 million for operating subsidy grants and \$462 million for capital subsidy grants. The \$2.5 million reprogramming, net of the partial rescission, would directly reduce the operating subsidy, however, the \$60 million reserve, net of the partial rescission, is not subsidy specific and may reduce either or both amounts ultimately available to Amtrak as operating and capital subsidies.

The 2004 Act incorporates certain provisions including that: 1) grant requests be submitted for each specific train route and be accompanied by a detailed financial analysis, revenue projection, and capital expenditure projection justifying the Federal Government support to the Secretary’s satisfaction; 2) Amtrak provide a comprehensive business plan approved by the Board of Directors for fiscal year 2004 within sixty (60) days of enactment of the 2004 Act under section 24104(a) of title 49, United States Code, to the Secretary of Transportation, the House and Senate Committees on Appropriations, the House Committee on Transportation and Infrastructure and the Senate Committee on Commerce, Science, and Transportation; 3) the business plan shall include, as applicable, targets for ridership, revenues, and capital and operating expenses; 4) the plan shall also include a separate accounting of such targets for the

Northeast Corridor, commuter service, long-distance Amtrak service, state-supported service, each intercity train route, including Autotrain and commercial activities including contract operations and mail and express; 5) the business plan shall include a description of the work to be funded, along with cost estimates and an estimated timetable for completion of the projects covered by this business plan; 6) no later than 30 days following the last business day of the previous month, Amtrak shall submit to the Secretary of Transportation and the House and Senate Committees on Appropriations a supplemental report, in electronic format, regarding the pending business plan, which shall describe the work completed to date, any changes to the business plan, and the reasons for such changes; 7) none of the funds in this Act may be used for operating expenses, including advance purchase orders, and capital projects not approved by the Secretary of Transportation nor on the National Railroad Passenger Corporation's fiscal year 2004 business plan; and 8) Amtrak shall display the business plan and all subsequent supplemental plans on the Corporation's website within a reasonable timeframe following their submission to the appropriate entities. In addition, the 2004 Act requires the Company to continue to abide with specified requirements of the \$100 million FRA loan (see Note 6).

The Company has received \$350.6 million of the fiscal year 2004 appropriation through January 31, 2004. The Company believes that it can achieve its planned results and that it will receive the full amount appropriated under the 2004 Act. To the extent that less than the full appropriation is received from the DOT or the Company's funding needs are greater than \$1.218 billion plus \$182.1 million of cash on hand, due to operating results or the unfavorable resolution of contingencies or other matters, the Company may not have sufficient funds to operate through the end of fiscal year 2004.

Amtrak has indicated that it will require \$1.798 billion in Federal Government funding for fiscal year 2005 to continue operations in its current form, make necessary capital improvements and repay the \$100 million FRA loan. There are currently no Federal Government subsidies authorized or appropriated for years subsequent to September 30, 2004. To the extent that a regular appropriation has not been approved prior to October 1, 2004, the Company expects to receive interim Federal Government funding under a continuing resolution until the fiscal year 2005 funding is approved. There can be no assurances that the Company will receive adequate funding to continue operations in its current form in fiscal year 2005 and beyond. Failure to receive sufficient subsidies may result in severe operational changes and/or restructuring which would likely result in asset impairments and potential bankruptcy or reorganization.

### **NOTE 3: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

#### **Principles of Consolidation**

The Consolidated Financial Statements reflect the consolidated operations of Amtrak: its three wholly owned subsidiaries, Chicago Union Station Company (CUS), Passenger Railroad Insurance, Limited (PRIL), and Penn Station Leasing, LLC (PSL); its 99.7% interest in Washington Terminal Company (WTC); and its 99% interest in 30th Street Limited, L.P. (TSL). In addition, Amtrak has consolidated certain operations owned by the Pennsylvania Economic Development Financing Authority (PEDFA) (see Note 6). All significant intercompany balances and transactions have been eliminated.

#### **Reclassifications**

Certain reclassifications have been made to the prior year's Consolidated Financial Statements and accompanying footnotes to conform to the fiscal year 2003 presentation.

#### **Cash Equivalents**

All temporary investments with original maturities of three months or less are considered cash equivalents.

## **Materials and Supplies**

Materials and supplies, which are stated at the lower of weighted average cost or market, consist primarily of items for maintenance and improvement of property and equipment. An allowance for shrinkage and obsolescence is provided for materials and supplies based on specific identification and turnover rates.

## **Derivative and Hedging Activities**

Amtrak periodically enters into heating oil contracts with durations of 12 months or less to manage a portion of the exposure to fluctuating diesel prices. Changes in the price of heating oil contracts have a high correlation to changes in the price of diesel fuel and therefore, qualify as cash flow hedges under Statement of Financial Accounting Standards (SFAS) No. 133, "Accounting for Derivative Instruments and Certain Hedging Activities" (SFAS 133), as amended.

Amtrak records the fair market value of fuel hedge contracts on the Consolidated Balance Sheets in "Other current assets." On an ongoing basis, Amtrak adjusts the balance sheet to reflect the current fair market value of fuel hedge contracts. The effective portion of the related gains or losses on these contracts is deferred as a component of "Other comprehensive income." These deferred gains and losses are recognized in income in the period in which the related diesel fuel purchases being hedged are consumed and recognized in expense. The ineffective portion of the change in the value of the fuel hedge contracts is immediately recognized in income. Amtrak calculates the ineffective portion of the hedge performance using the dollar offset method. The ineffective portions of the fuel hedge contracts are included in the Consolidated Statements of Operations as a component of "Fuel, power and utilities." If at any time the hedge no longer qualifies for hedge accounting treatment, expires, is sold, terminates, is exercised, or it becomes probable that the forecasted transaction will not occur, the net gain or loss accumulated in "Other comprehensive income" is reclassified into earnings.

For fiscal years 2003 and 2002, pursuant to SFAS 133, as amended, Amtrak recognized increases of \$1,576,000 and \$722,000, respectively, to fuel cost associated with these derivative fuel contracts. At September 30, 2003 and 2002, Amtrak had derivative fuel contracts with fair values of \$1,352,000 and \$1,130,000, respectively. As of September 30, 2003 and 2002, the effective portions of these contracts, which qualify as cash flow hedges, amounted to \$342,000 and \$0, respectively. The effective portion at September 30, 2003 will be reclassified into earnings during fiscal year 2004.

## **Property and Depreciation**

Property and equipment are stated at cost, and are depreciated over their estimated useful lives using the straight-line composite group method. Under this method, gains and losses on ordinary retirements and dispositions are charged to accumulated depreciation. Locomotives, passenger cars and other rolling stock are depreciated using useful lives ranging up to 35 years. Right-of-way and other properties (excluding land) are depreciated using useful lives ranging up to 105 years. Other equipment including computers, office equipment and maintenance equipment is depreciated using useful lives ranging up to 30 years. Property held under capital leases and leasehold improvements are depreciated over the shorter of their estimated useful lives or their respective lease terms. Expenditures that significantly increase asset values or extend useful lives are capitalized. Repair and maintenance expenditures, including preventative maintenance, are charged to operating expense when the work is performed. The cost of internally developed software is capitalized in accordance with Statement of Position 98-1 "Accounting for the Costs of Computer Software Developed or Obtained for Internal Use" and amortized over its estimated useful life which generally does not exceed 5 years. Amtrak capitalizes interest costs in connection with the construction of major facilities, locomotives and passenger cars. Capitalized interest is recorded as part of the asset to which it relates and is depreciated over the asset's useful life. Interest of \$838,000 and \$8,151,000 was capitalized in fiscal years 2003 and 2002, respectively.

### **Impairment of Long-Lived Assets**

Properties and other long-lived assets are reviewed for impairment whenever events or business conditions indicate that the carrying amount of such assets may not be fully recoverable. Initial assessments of recoverability are based on estimates of undiscounted future net cash flows associated with the entire operating network since cash flows generally cannot be attributed to individual assets, and include estimated future operating and capital funding expected to be received from the Federal Government over the expected lives of the assets. Where impairment is indicated, the assets are evaluated for sale or other disposition, and their carrying amount is reduced to fair value based on discounted net cash flows, or other estimates of fair value.

The Company assumes future Federal Government funding at levels consistent with those discussed in Note 2 and historical funding in performing its impairment analysis. At this level of funding, the system-wide carrying amounts of the Company's long-lived assets are recoverable. The Company believes that continued funding at historical levels is their best estimate of the future. If future Federal Government funding levels drop below these levels, substantial impairments may occur.

### **Casualty Losses and Claims**

Provision is made for Amtrak's portion of the estimated actuarial liability for unsettled casualty and other claims. As of September 30, 2003 and 2002, the current claims liability included in "Accrued expenses and other current liabilities" was \$100,800,000 and \$96,200,000, respectively. Included in "Receivables" in the Consolidated Balance Sheets at September 30, 2003 and 2002, are estimated insurance recoveries of \$68,364,000 and \$53,355,000, respectively, which relate to loss events that Amtrak has incurred.

### **Revenue Recognition**

"Passenger related" revenue in the Consolidated Statements of Operations, for fiscal years 2003 and 2002, includes ticket revenue, state contribution revenue associated with requested service provided by Amtrak beyond that included in the basic route system, food and beverage revenue, and other passenger revenue as shown below (in millions):

	<u>2003</u>	<u>2002</u>
Ticket	\$ 1,180.1	\$ 1,250.0
State contribution	136.0	128.5
Food and beverage	78.4	84.1
Other passenger	<u>5.4</u>	<u>5.6</u>
Total Passenger Related Revenue	<u>\$ 1,399.9</u>	<u>\$ 1,468.2</u>

These revenues, as well as "Mail and express" revenues, are recognized as operating revenues when the related services are provided. Tickets that have been sold but not used are reflected as "Deferred ticket revenue" in the Consolidated Balance Sheets.

"Commuter" revenue includes the revenues earned under contractual arrangements to operate various commuter rail services for a cost-based fee.

“Other” revenue, for fiscal years 2003 and 2002, includes revenue associated with performing maintenance of way and maintenance of equipment services for freight railroads and others, fees charged to commuter agencies and freight railroads for the use of Amtrak’s right-of-way, lease rental related revenue, one-time gains, and other miscellaneous services revenue as shown below (in millions):

	<u>2003</u>	<u>2002</u>
Maintenance of way and equipment	\$ 92.1	\$ 97.1
Right-of-way fees	98.5	93.8
Lease rental	55.6	56.6
One-time gains	30.0	32.8
Miscellaneous Services	<u>35.6</u>	<u>43.4</u>
Total	<u>\$ 311.8</u>	<u>\$ 323.7</u>

“State capital payments” includes the amortization of state funds used to acquire depreciable assets. These state capital payments are deferred when received and amortized over the life of the related asset purchased with the funds. The unamortized amounts are included in “Deferred state capital payments” in the Consolidated Balance Sheets.

#### **Income Taxes**

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

Pursuant to the provisions of Title 49 of the United States Code, Section 24-301, Amtrak is exempt from all state and local taxes, including income and franchise taxes that are directly levied against the corporation. Accordingly, there is no provision for state and local income or franchise taxes recorded in the consolidated financial statements for the years ended September 30, 2003 and 2002 (see Note 8).

#### **Use of Estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, 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.

#### **NOTE 4: ACCOUNTING AND REPORTING FOR FEDERAL PAYMENTS**

Certain funds are provided to Amtrak through federal payments for capital and operating expenditures. These federal payments, which are recorded as paid-in capital when received, totaled \$994.6 million and \$1,038.2 million for fiscal years 2003 and 2002, respectively. All of the amount received during fiscal year 2003 was from the fiscal year 2003 appropriation. The remainder of the fiscal year 2003 appropriation in the amount of \$48.6 million was received in October 2003. Of the amount received during fiscal year 2002, \$311.7 million was the remainder of the fiscal year 2001 appropriation, \$521.5 million was the appropriation pursuant to Public Law 107-87 and on August 14, 2002, Amtrak received and recorded into paid-in capital, a supplemental appropriation of \$205 million from the Federal Government (Public Law 107-206) for expenses to ensure the continuation of rail passenger operations.

Certain other federal funds that are provided and restricted for use on designated projects are also recorded as paid-in capital when received, and these totaled \$7.3 million and \$24.5 million for fiscal years 2003 and 2002, respectively.

“Debt and other paid-in capital,” included in the Consolidated Balance Sheets, includes certain funding received from the Federal Government to finance acquisition of and improvements to property and equipment. In exchange for funding, Amtrak issued two promissory notes to the United States. The first note with a balance of \$1.1 billion was issued in 1983 and matures on November 1, 2082, with successive 99-year renewal terms, and is secured by all the rolling stock owned by Amtrak. The second note with a balance of \$4.0 billion was issued in 1976 and matures on December 31, 2975, and is secured by the real and personal property of Amtrak, WTC, CUS, PRIL, and TSL. Neither of the notes bears interest, unless prepaid which Amtrak does not intend to do. The Federal Government's security interest in Amtrak's rolling stock entitles it to repayment plus interest in the event Amtrak ceases operations, is acquired by another entity, or seeks relief under bankruptcy or insolvency laws. The amount due to the Federal Government on the second note may be accelerated by enactment of federal law or upon the occurrence of an event of default under the leases and mortgage entered into by Amtrak and PSL on June 20, 2001 (see Note 6), or upon the occurrence of various actions concerning an Amtrak bankruptcy, reorganization, or assignment for the benefit of creditors.

#### **NOTE 5: PREFERRED AND COMMON STOCK**

For funds received from the Federal Government prior to December 2, 1997, the Rail Passenger Service Act (49 U.S.C. 24304) required Amtrak to issue to the Secretary of Transportation preferred stock equal in par value to all federal operating payments and most federal capital payments received subsequent to October 1, 1981, as well as capital and certain operating payments received prior to that date. At September 30, 2003 and 2002, 109,396,994 shares of \$100 par value preferred stock were authorized, all of which were issued and outstanding. All issued and outstanding preferred shares are held by the Secretary of Transportation for the benefit of the Federal Government. The Amtrak Reform and Accountability Act of 1997 (the Act) resulted in significant modifications to Amtrak's capital structure. Prior to the Act, dividends were to be fixed at a rate not less than 6% per annum, and were cumulative. No dividends were ever declared. The Act abolished the voting rights and the liquidation preference of the preferred stockholder and the 6% minimum annual cumulative preferred stock dividend; and established that no additional preferred stock be issued by Amtrak in exchange for federal grants received. At the time of enactment of the Act, the minimum undeclared cumulative preferred dividend in arrears for all series issued and currently outstanding approximated \$5.8 billion and ranged between \$0.02 and \$97.08 per share.

At September 30, 2003 and 2002, 10,000,000 shares of \$10 par value common stock were authorized, of which 9,385,694 shares were issued and outstanding. The common stockholders, who are the predecessors to the Company, have voting rights for amendments to Amtrak's Articles of Incorporation proposed by the Board of Directors. The Act also required Amtrak to redeem at fair market value the shares of common stock outstanding as of December 2, 1997, by the end of fiscal year 2002.

Amtrak has held meetings with the owners of the common stock to discuss the redemption of their shares, but there has been no resolution of this matter between Amtrak and the owners. Amtrak does not believe that the common stock has value. Nevertheless, in an effort to comply with the Act, Amtrak has made an offer to redeem the stock for cash at a price of \$0.03 per share to the stockholders. By letter dated November 2, 2000, counsel for the four common stockholders responded to Amtrak and rejected the offer as inadequate. Amtrak is considering various courses of action.

**NOTE 6: MORTGAGES AND DEBT**

Total debt in the Consolidated Balance Sheets consisted of the following at September 30, 2003 and 2002 (in thousands):

	2003		2002	
	Current	Long-term	Current	Long-term
Long-term debt:				
FRA loan	\$ -	\$ 100,000	\$ -	\$ 100,000
Mortgages payable	9,518	274,180	9,679	304,627
Equipment obligations	2	500	2	10,402
Notes payable	20,000	-	-	20,000
Bonds	-	79,426	-	30,000
UDAG loan	130	11,447	130	11,577
Total	<u>\$ 29,650</u>	<u>\$ 465,553</u>	<u>\$ 9,811</u>	<u>\$ 476,606</u>

**Credit Facilities**

On September 22, 2003, Amtrak entered into a \$19 million unsecured revolving letter of credit facility that is scheduled to expire on June 27, 2005. Letters of credit issued under this unsecured facility replaced the secured letters of credit that were outstanding at September 30, 2002. At September 30, 2002, Amtrak had a revolving credit facility of \$270 million with a consortium of banks, which expired on November 15, 2002 and was not renewed. Commitment fees and interest rates payable under these credit facilities are similar to fees and rates available to comparably rated investment-grade borrowers. At September 30, 2003 and 2002, there were letters of credit outstanding of \$7,807,000 and \$9,190,000, respectively. As of September 30, 2003 and 2002, there were no borrowings under these facilities.

**Federal Railroad Administration (FRA) Loan**

On July 3, 2002, Amtrak executed a \$100 million interest bearing conditional loan under the Federal Railroad Administration's "Railroad Rehabilitation and Improvement Financing Program" for qualified capital expenditures. The loan currently bears interest at 1.81% per annum, and is secured by various Amtrak-owned right-of-way properties and facilities. The loan was originally scheduled to be repaid on the later of November 15, 2002, or the date Amtrak had access to funds from its fiscal year 2003 appropriation in an amount that exceeds \$100 million. Public Law 108-199 defers repayment of the loan plus accrued interest until after fiscal year 2004. This loan requires Amtrak's compliance with certain conditions which include: improving financial controls and accounting transparency, submission of monthly performance reports and a list of expense reduction options to Congress and the DOT.

**Mortgages Payable**

In June 2001, PSL mortgaged a substantial portion of improvements located at Penn Station in New York, New York for \$300 million at a fixed rate of interest of 9.25% per annum, receiving net cash proceeds of \$296,249,000. Of this amount, \$34,280,000 was deposited into escrow for the benefit of the lender and is reflected in "Deferred charges, deposits, and other" in the Consolidated Balance Sheets. Semi-annual principal plus interest payments are due on the mortgage through maturity in June 2017. As provided for under specific covenant provisions between the mortgage lender and investor group providing the mortgage funds, the fixed mortgage rate of 9.25% per annum at September 30, 2002, was increased to 9.50% effective October 2002. At September 30, 2003 and 2002, the outstanding balance due on the mortgage was \$283,440,000 and \$291,900,000, respectively.

In May 2001, CUSCO No. 1, LLC, a limited liability corporation with CUS as its only member, separately mortgaged the property air rights of two real estate sites located in Chicago for \$21,500,000 in total, each at fixed rates of interest of 7.04% per annum. Quarterly principal plus interest payments were

due on each of the two mortgage notes through their maturities in June 2011. On June 2, 2003, CUS sold its membership interest in CUSCO No. 1, LLC, netting proceeds in the amount of \$12,299,000. A condition of the sale was the assumption of CUSCO No. 1, LLC's debt by the purchaser for which the lender's consent was obtained. At September 30, 2002, the total outstanding balance due on the notes was \$21,169,000.

In December 2000, Amtrak acquired land and office facilities located in Connecticut in exchange for \$2,750,000 cash and a \$2,750,000 mortgage note bearing a fixed rate of interest of 9.0% per annum. Monthly principal and interest payments are due through December 2003. The note is secured by the land and office facilities. At September 30, 2003 and 2002, the outstanding balance due on the note was \$258,000 and \$1,237,000, respectively. During November 2003, Amtrak paid the remaining balance due on the mortgage note and obtained a release of mortgage.

### **Equipment Obligations**

Under separate financing arrangements, Amtrak was allowed to borrow up to \$870 million toward the construction and acquisition of high-speed locomotives and trainsets, and related maintenance facilities. As of September 30, 2003 and 2002, the Company had borrowed a total of \$761 million and \$749 million, respectively. Upon delivery of the locomotives and trainsets, and the completion of the maintenance facility, Amtrak has been refinancing the related outstanding advances under capital leasing arrangements. As of September 30, 2003 and 2002 outstanding advances made on Amtrak's behalf under these arrangements totaled \$500,000 and \$10,404,000, respectively. The final two trainsets were delivered during fiscal year 2003, one in October 2002 and the last in June 2003. All outstanding advances at September 30, 2003, are secured by the final two trainsets and have not been refinanced under capital leasing arrangements. Interest charged is based on the London Interbank Offered Rate (LIBOR) and was capitalized during the construction phase.

### **Notes Payable**

Amtrak acquired a parking facility located in Chicago, Illinois in exchange for a \$20 million promissory note due in December 2003 bearing a fixed rate of interest. The seller has secured the note with the parking facility as well as an irrevocable unconditional \$4 million letter of credit as collateral. In December 2003, Amtrak paid the remaining balance due on the promissory note, obtained a lien release and cancelled the letter of credit.

### **Bonds and Grant**

On January 7, 2003, PEDFA issued \$50 million Revenue Bonds (the "PEDFA Garage Bonds") for the purpose of financing the construction and other related costs of a parking garage located at the 30th Street Station in Philadelphia, PA. The bonds have multiple maturities ending on June 1, 2033. Interest on the bonds is payable each June 1 and December 1, and commenced on June 1, 2003. The bonds were issued at a discount of \$588,000 and bear interest, by individual maturities, at fixed rates ranging from 4.500% to 5.875%. The parking garage is being constructed in the air rights owned by Amtrak and on December 15, 2002, Amtrak entered into a lease for the air rights with PEDFA. Also on December 15, 2002, Amtrak entered into a "Pledge and Security Agreement" (the "Pledge") with PEDFA under which Amtrak guarantees the payment of the principal and interest on the PEDFA Garage Bonds which Amtrak's liability is limited to a pledge of: (i) the rent received or receivable by Amtrak under the air rights lease during the fiscal year in which a demand for payment is made, and (ii) the additional parking facilities revenues, as defined in the Pledge. Under these agreements (and certain other related agreements), revenue generated from the parking garage will first be used to fund the operations of the parking garage, second to pay principal and interest payments on the PEDFA Garage Bonds, third to reserve certain amounts for future repairs and maintenance of the parking garage and fourth any excess will be paid to Amtrak subject to amounts that may be owed to the builder of the parking garage as contingent purchase price. Until the PEDFA Garage Bonds are extinguished, the Company has oversight

responsibility of the construction and management of the parking garage and bears the risk of loss (subject to insurance obtained) for the parking garage. When the PEDFA Garage Bonds are extinguished, the Company will be awarded title to and ownership of the parking garage. Accordingly, Amtrak has recognized PEDFA's \$50 million bond obligation on the Consolidated Balance Sheets in "Equipment and other debt." As of September 30, 2003, Amtrak has recorded on the Consolidated Balance Sheets in "Right of way and other properties", capital expenditures in the amount of \$14,740,000 related to the construction of the parking garage, and the remaining net bond proceeds are recorded on the Consolidated Balance Sheets in "Deferred charges, deposits and other" and amount to \$30,920,000 at September 30, 2003.

Included in TSL's long-term debt at September 30, 2003 and 2002, is \$30 million of Philadelphia Authority for Industrial Development (PAID) tax-exempt private-activity bonds (the "PAID Bonds") issued by PAID for the benefit of TSL's rehabilitation of 30th Street Station (the "Station") in the city of Philadelphia (the "City"), Pennsylvania. The PAID Bonds were issued on December 30, 1987, mature on January 1, 2011, and bear interest at a fixed or variable rate payable until maturity at intervals determined under provisions in the bond indenture. No payments of bond principal prior to maturity are required. Amtrak is periodically required to make annual deposits into a sinking fund to be used to pay off the bonds when they mature. As of September 30, 2003 and 2002, Amtrak's aggregate deposits into the fund were \$8,827,000 and \$7,461,000, respectively, which are included in "Deferred charges, deposits, and other" in the Consolidated Balance Sheets. The PAID Bonds are subject to optional tender by the bondholders in the case of significant events, specifically those pertaining to any damage to, destruction of, or condemnation of the Station facilities. TSL has executed a liquidity facility which provides funds to purchase the bonds surrendered under the optional tender provisions.

TSL has a non-interest bearing obligation of \$11,577,000 and \$11,707,000 to the City under an Urban Development Action Grant (UDAG) loan agreement as of September 30, 2003 and 2002, respectively. Principal is being repaid in \$130,000 annual installments each November through 2011, with the balance due in November 2012. The City's rights under the UDAG loan agreement are secured by a leasehold mortgage.

### **Interest Rates**

Per annum weighted average percentage interest rates by debt type for all interest-bearing borrowings at September 30, 2003 and 2002, are shown below (in percentages of 100%):

	<u>2003</u>	<u>2002</u>
FRA loan	1.81	1.81
Mortgages payable	9.50	9.10
Equipment obligations	2.06	3.49
Notes payable	9.00	9.00
Bonds	3.94	1.40

The overall weighted average interest rate on all interest-bearing borrowings is 7.0% per annum at September 30, 2003 and 2002.

### Scheduled Debt Maturities

At September 30, 2003, scheduled maturities of debt over the next five years and thereafter are as follows (in thousands):

2004	\$ 29,650
2005	110,920
2006	11,920
2007	13,030
2008	14,230
Thereafter	<u>316,027</u>
Total	<u>\$ 495,777</u>

Amtrak is subject to various covenants and restrictions under its borrowing arrangements. A default by Amtrak or acceleration of Amtrak's indebtedness may result in cross-default to other Amtrak indebtedness, and may have a material adverse effect on the Company. Most of Amtrak's financing transactions require that Amtrak deliver its audited annual financial statements within 90 to 120 days of the end of its fiscal year. Amtrak has not delivered within this timeframe its audited financial statements for fiscal year 2003. Amtrak has at least a 30-day grace period which commences on written notice to Amtrak of its breach. Amtrak may cure the technical default and avoid a defined Event of Default, by delivering the statements and certificates prior to lapse of this grace period. To date, Amtrak has not received any written notice of its breach. Excluding the foregoing, Amtrak is in compliance with all of its covenants.

### NOTE 7: LEASING ARRANGEMENTS

#### Facilities

During fiscal year 2001, the Pennsylvania Economic Development Financing Authority (PEDFA) completed two separate issues of exempt facilities revenue bonds, the net proceeds of which were used to finance a portion of the costs associated with Amtrak's construction of a frequency converter facility (the facility). The first series (Series A) totaling \$110,795,000 was issued in February 2001 at a \$795,000 discount, netting \$110 million. The second series (Series B) totaling \$45 million was issued in April 2001 at par. Amtrak procured the bond proceeds of each issue through a lease and leaseback arrangement with PEDFA. Under this arrangement, Amtrak awarded title to and ownership of the facility to PEDFA until November 2041 under a ground lease, in exchange for the total net proceeds. Simultaneously, Amtrak is leasing back from PEDFA the facility through June 2033, with an option to extend this term through November 2041. PEDFA also has the right to extend Amtrak's leaseback term through November 2041. At the conclusion of the ground lease, title to and ownership of the facility will revert to Amtrak. Amtrak's leaseback rentals are funding PEDFA's debt service requirements for both the Series A and Series B bonds. Amtrak's rentals are due semi-annually for the Series A bonds, and monthly for the Series B bonds. With the bond proceeds, Amtrak used \$3,343,000 toward financing arrangement costs, and discharged \$85,453,000 of interim debt associated with the facility's construction. The remaining \$66,204,000 of proceeds remained on deposit with the bond trustee and was earmarked for use toward Amtrak's leaseback payments, further facility construction costs, and additional financing arrangement costs. Since Amtrak is maintaining continuing involvement with the facility, assuming the true risks of ownership, and eventually resuming legal title to and ownership of the facility upon termination of the ground lease, the lease and leaseback were accounted for as a capital lease. Accordingly, Amtrak recorded a \$155 million capital lease obligation, \$3,343,000 of deferred financing costs, and \$66,204,000 of deferred deposits. Amtrak's sublease rentals consist of an interest and principal portion, with the latter scheduled to pay down this capital lease obligation over the sublease's initial and option terms.

## Equipment

Amtrak leases equipment, primarily passenger cars and locomotives, under capital leasing arrangements. At September 30, 2003 and 2002, the gross amount of assets recorded under capital leases was \$3,672,521,000 (37% for locomotives, 60% for passenger cars, and 3% for other assets), and \$3,628,205,000 (38% for locomotives, 59% for passenger cars, and 3% for other assets), respectively, with accumulated amortization of \$974,742,000 and \$744,850,000, respectively.

During 2000, Amtrak entered into four separate defeased sale and leaseback transactions involving passenger cars. In exchange for \$915,155,000 consisting of net cash proceeds and set-aside assets in the form of defeasance instruments, Amtrak sold the cars having a net book value of \$334,690,000, resulting in a deferred gain of \$580,465,000. The defeasance instruments are held by the buyers, and Amtrak accretes value at fixed interest rates of approximately 6.8% to 8.8% per annum. Simultaneously, Amtrak is leasing back the cars, that are included in the capital lease amounts above, over terms ranging from 23 to 28 years. The leasebacks are accounted for as capital leases. In addition, the set-aside assets together with future accreted interest are designated toward satisfying Amtrak's rent payment obligations under the capital leaseback arrangements. The assets economically defease, but do not legally defease Amtrak's obligations under the leasebacks. Consequently, the set-aside assets plus accreted interest are not netted against the capital lease obligations, but instead are presented as "Escrowed proceeds on sale-leasebacks" in the Consolidated Balance Sheets. The \$580,465,000 gain on the sales was deferred and is being amortized into income as a reduction to depreciation expense over the terms of the capital leasebacks. During fiscal years 2003 and 2002, \$22,145,000 and \$22,150,000 of deferred gains on these transactions were amortized, respectively.

At September 30, 2003, future minimum lease payments under capital leases including amounts from defeasance trusts were as follows (in thousands):

2004	\$ 273,762
2005	276,374
2006	276,011
2007	276,969
2008	284,465
Thereafter	<u>4,068,696</u>
Total payments	5,456,277
Less amount representing interest	<u>2,058,939</u>
Present value of minimum lease payments at September 30, 2003	<u><u>\$3,397,338</u></u>

The current portion of capital lease obligations at September 30, 2003 and 2002 was \$89,816,000 and \$80,336,000, respectively, and is included in "Current maturities of long-term debt and capital lease obligations" in the Consolidated Balance Sheets.

The Company had wrecked and damaged leased equipment as of September 30, 2003 and 2002. Certain lease agreements require that this equipment be restored to its original condition, like equipment be substituted, or the lessor be reimbursed for the equipment loss. The liability for the wrecked and damaged equipment was estimated to be \$38,078,000 and \$34,979,000 as of September 30, 2003 and 2002, respectively, and is recorded in the Consolidated Balance Sheets in "Accrued expenses and other current liabilities." The amounts expensed relating to these items are reflected in the "Materials" line item in the Consolidated Statements of Operations. Amtrak is subject to various covenants including acceleration clauses and restrictions under its capital lease arrangements. A default by Amtrak or acceleration of Amtrak's indebtedness under a leasing arrangement may result in a cross-default to other Amtrak indebtedness, and may have a material adverse effect on the Company.

### **Operating Rights and Leases**

At September 30, 2003, Amtrak was obligated for the following minimum rental payments, principally for station and office space, under operating leases that have initial or remaining non-cancellable lease terms in excess of one year (in thousands):

2004	\$ 13,110
2005	12,375
2006	10,652
2007	10,166
2008	7,862
Thereafter	<u>30,089</u>
Total	<u>\$ 84,254</u>

Rent expense for the years ended September 30, 2003 and 2002 was \$41,388,000 and \$41,302,000, respectively, and it is expected that future rent expense will be comparable.

Most of the rights-of-way over which Amtrak operates are owned by other railroads some of which own Amtrak's common stock. Amtrak uses such trackage under contracts with these railroads. The terms of the agreements range from 5 to 15 years and costs incurred are based on usage. The total amount paid to the railroads for use of their rights-of-way in 2003 and 2002 totaled \$96.2 million and \$103.9 million, respectively.

### **NOTE 8: INCOME TAXES**

No provision for federal taxes has been recorded as the Company incurred net operating losses for the years ended September 30, 2003 and 2002. As of September 30, 2003, the Company had net operating loss carry-forwards of approximately \$7.4 billion, which begin to expire January 1, 2010.

The provision for income taxes differed from the income tax benefit which would be computed based upon the statutory federal tax rates as a result of the recording of a valuation allowance equal to the increase in net deferred tax assets.

Net operating losses are the main component of net deferred tax assets. Based upon the Company's history of operating losses, it is management's judgment that it is not likely that the net deferred tax assets will be realized in future years. As a result, management has applied a full valuation allowance against the net deferred tax assets at September 30, 2003 and 2002.

### **NOTE 9: COMMITMENTS AND CONTINGENCIES**

#### **Insurance Claims**

Amtrak maintains various insurance policies to cover its liability to employees and other parties for injury or damage resulting from accidents and to cover Amtrak's loss resulting from damage to Amtrak property. The insurance policies contain large deductibles; losses within the deductibles are self-insured by Amtrak.

The Amtrak Reform and Accountability Act of 1997 limits the amount railroad passengers may recover from a single accident to an aggregate of \$200 million. Since non-passenger liability is not so limited, Amtrak purchases excess liability insurance limits beyond this statutory cap.

Amtrak operates a majority of its long distance passenger rail service on tracks owned by freight railroads. Amtrak indemnifies these railroads for certain liabilities that arise as a result of its operations on freight tracks. Its indemnity applies to bodily injury and property damage claims made by its employees and passengers; and third parties struck by its trains, and for damage to its equipment. The freight railroads indemnify Amtrak for bodily injury and property damage claims made by freight railroad

employees and third parties off railroad property; and for damage to freight railroad equipment, lading and property.

### **Labor Agreements**

Approximately 90% of Amtrak's labor force is covered by labor agreements. During fiscal year 2003, Amtrak reached an agreement on a new labor contract with one of the 13 labor organizations and joint councils representing Amtrak workers. The new contract affects approximately 5,000 employees, or 25 percent of Amtrak's labor force and covers the period of January 1, 2000 through December 31, 2004. All other labor agreements currently in force were amendable as of January 1, 2000, and will remain in effect until new agreements are reached or the Railway Labor Act's procedures are exhausted.

### **Legal Proceedings**

In December 1995, Amtrak entered into a \$321 million fixed-price contract with a joint venture consisting of Balfour Beatty Construction, Inc. and Mass. Electric Construction Co. ("BBC/MEC") for the design and construction of an electrified catenary system along Amtrak's Northeast Corridor right-of-way between New Haven, Connecticut and Boston, Massachusetts. To date BBC/MEC has made various claims alleging, among other things, problems with site conditions, design, owner-directed changes, work interference, and work schedule acceleration. The value of the claims total approximately \$112 million, of which Amtrak has already paid \$35 million. Amtrak is vigorously defending the remaining \$77 million in claims, a process that is likely to take several years. Amtrak is asserting its own claims against BBC/MEC for a variety of contract non-compliance issues and is holding \$11 million in retainage against Amtrak's claims. In addition, the United States Department of Justice has undertaken investigations of BBC/MEC that may result in additional claims against it. The total value of claims against BBC/MEC is substantial but cannot be estimated with accuracy at this time. No provision for claims against Amtrak is reflected in the accompanying Consolidated Financial Statements.

On November 8, 2001, Bombardier Corporation ("Bombardier") filed a complaint in the United States District Court for the District of Columbia against Amtrak alleging that Amtrak through various actions and failures caused Bombardier (as partner to a consortium along with Alstom Transportation, Inc., hereinafter, the "Consortium") to incur substantial additional costs related to the contracts for design and manufacture of high-speed electric trainsets and locomotives, and the related maintenance facilities (the "Contracts"). Bombardier's complaint claims entitlement to recovery and requests an award of damages of not less than \$200 million. Bombardier filed an amended complaint on November 16, 2001. In its amended complaint, Bombardier alleges Amtrak breached its Contracts with the Consortium, and violated other legal obligations Amtrak allegedly owed Bombardier, thereby interfering with these Contracts. In its amended complaint, Bombardier seeks damages of not less than \$200 million. On December 3, 2001, Amtrak filed a motion to dismiss Bombardier's complaint on the basis that Bombardier had not complied with the Contracts' dispute resolution provisions and that compliance with these provisions was a prerequisite to filing suit. The District Court denied Amtrak's motion on September 30, 2002. The United States Court of Appeals for the District of Columbia Circuit dismissed Amtrak's appeal on jurisdictional grounds on July 1, 2003. Amtrak filed a counterclaim against Bombardier, Alstom and their sureties on November 14, 2003, seeking approximately \$200 million in damages. Amtrak and Bombardier (the "Parties") have reached a tentative settlement that is subject to completion and execution of a final settlement agreement. Based on the terms of the tentative settlement agreement, Amtrak would make payments to the Consortium from amounts previously withheld under the terms of the Contracts. The Parties have agreed to a stay of the litigation through April 15, 2004.

On October 23, 2003, ERC Frankona Ruckversicherungs-AG ("Frankona"), a reinsurer of portions of the excess liability and property insurance coverage which PRIL provides to Amtrak, filed suit against PRIL in the New York Supreme Court alleging that PRIL made material misrepresentations and omissions regarding Amtrak's loss history and seeking an order declaring the contracts null, void and rescinded. Subsequently, Frankona agreed to dismiss its New York action without prejudice. On

November 21, 2003, PRIL and Amtrak filed suit against Frankona in the United States District Court for the District of Columbia for a declaratory judgment, breach of contract, bad faith, and other relief against Frankona resulting from its claim that the reinsurance contracts are rescinded, and Frankona filed a counterclaim seeking substantially the same recovery as in its New York action. If the contracts are declared null, void and rescinded, Amtrak would have additional uninsured liability and property claims of up to \$34 million and \$10.3 million, respectively, for certain accidents which occurred during the policy periods from October 1, 1998 to December 31, 2002 for liability, and from December 1, 1998 to December 1, 2002 for property coverage. At this stage of the litigation, it is Amtrak's assessment that an outcome adverse to its interest, while possible, is not probable.

On August 19, 2003, former employees filed a class action lawsuit involving Amtrak's 2001 Voluntary Early Retirement Plan (VERP) in the United States District Court for the District of Columbia seeking to void a September 2001 amendment to the Amtrak Pension Plan that eliminated a monthly Railroad Retirement Supplement and replaced it with a one-time lump sum payment of \$15,000 per eligible employee. Additionally, the complaint seeks to "reopen" the window period to allow eligible employees to apply for the original benefits. Amtrak, the Retirement Plan Committee, and the Retirement Income Plan are also named as defendants. The ultimate outcome of this matter cannot be determined at this time.

Amtrak is involved in various other litigation and arbitration proceedings in the normal course of business. While the outcome of these matters cannot be predicted with certainty, it is the opinion of management and counsel that the disposition of these matters will not materially affect Amtrak's Consolidated Financial Statements.

### **Commitments**

Amtrak has entered into various agreements with States, cities and other local transportation authorities and private companies for railroad facility and infrastructure improvements and for the remanufacture and supply of railroad passenger equipment. The largest commitments arise from agreements with two Northeastern States. Under these contracts, Amtrak agreed to fund a portion of the costs with a remaining scope of work at September 30, 2003 of approximately \$132 million. Amtrak has the right to terminate future work contemplated by the contracts. Amtrak is discussing with the States a number of contract scope changes that would result in a reduction in the overall cost. In addition to the foregoing, Amtrak has a commitment of approximately \$39 million for infrastructure improvements whose term extends through project completion.

### **NOTE 10: ENVIRONMENTAL MATTERS**

Some of Amtrak's past and present operations involve activities which are subject to extensive and changing federal and state environmental regulations which can give rise to environmental issues. As a result of its operations and acquired properties, Amtrak is from time to time involved in administrative and judicial proceedings and administrative inquiries related to environmental matters.

In 1976, Amtrak acquired its Northeast Corridor properties. It is Amtrak's policy to accrue estimated liabilities and capitalize such amounts of remediation costs relating to properties acquired with existing environmental conditions (not to exceed the net realizable value of the related property), and to expense remediation costs incurred on properties for environmental clean-up matters occurring after acquisition. The liability is periodically adjusted based on Amtrak's present estimate of the costs it will incur related to these sites and/or actual expenditures made. At September 30, 2003 and 2002, the reserve was \$40,795,000 and \$43,339,000, respectively. Of these amounts, \$34,588,000 and \$37,437,000 relate to estimated capitalizable costs to be incurred as of September 30, 2003 and 2002, respectively. Costs of future expenditures for environmental remediation obligations are not discounted to their present value. At September 30, 2003 and 2002, a deferred charge for each amount is included in the Consolidated Balance Sheets under "Deferred charges, deposits, and other." Amtrak has not recorded any receivables for recoveries from other parties or from insurance because such recoveries are not sufficiently certain.

The ultimate liability for remediation is difficult to determine with certainty due to, among other factors, the number of potentially responsible parties, site-specific cost sharing arrangements, the degree and types of contamination, potentially unidentified contamination, developing remediation technology, and evolving statutory and regulatory standards. Amtrak's management and counsel believe that additional future remedial actions for known environmental matters will not have a material adverse effect on the results of operations or financial condition.

**NOTE 11: RETIREMENT BENEFITS**

Amtrak has a qualified noncontributory defined benefit retirement plan whose assets are held in trust covering nonunion employees and certain union employees who at one time held nonunion positions. Amtrak provides medical benefits to its qualifying retirees and life insurance to some retirees in limited circumstances under its postretirement benefits program. Railroad agreement employees' life insurance benefits are covered by a separate policy purchased by Amtrak. As a result of a voluntary separation plan offered to qualified nonunion employees in late fiscal year 2001 with acceptances received and the plan finalized in early fiscal year 2002, a curtailment loss and termination benefits are included as a component of the fiscal year 2002 net periodic pension benefit cost. The following tables provide a reconciliation of the changes in the plans' benefit obligations and fair value of assets over the two-year period ending September 30, 2003, and a statement of the funded status as of September 30, 2003 and 2002 (in thousands):

	Pension Benefits		Other Benefits	
	2003	2002	2003	2002
Reconciliation of projected benefit obligation:				
Obligation at October 1,	\$ 164,738	\$ 155,157	\$ 228,478	\$ 170,562
Service cost	6,330	6,425	8,053	6,810
Interest cost	11,723	10,824	16,295	14,397
Actuarial loss (gain)	18,698	(2,392)	164,225	48,726
Effect of curtailment	(774)	(262)	(12,221)	(5,013)
Benefit payments	(6,205)	(5,014)	(7,286)	(7,004)
Obligation at September 30,	\$ 194,510	\$ 164,738	\$ 397,544	\$ 228,478
Reconciliation of fair value of plan assets:				
Fair value of plan assets at October 1,	\$ 157,470	\$ 175,344	\$ -	\$ -
Actual gain (loss) on plan assets	6,808	(11,167)	-	-
Employer contributions	-	4	7,286	7,004
Effect of curtailment	-	(1,697)	-	-
Benefit payments	(6,205)	(5,014)	(7,286)	(7,004)
Fair value of plan assets at September 30,	\$ 158,073	\$ 157,470	\$ -	\$ -

	Pension Benefits		Other Benefits	
	2003	2002	2003	2002
Funded status:				
Funded status at September 30,	\$ (36,437)	\$ (7,268)	\$ (397,544)	\$ (228,478)
Unrecognized prior service cost	1,061	1,292	15,977	18,272
Unrecognized loss	30,917	7,446	196,438	46,124
Additional minimum liability	(7,022)	-	-	-
Net asset (liability) recognized in Consolidated Balance Sheets	\$ (11,481)	\$ 1,470	\$ (185,129)	\$ (164,082)
Accumulated benefit obligation (ABO) at September 30,	\$ 169,554	\$ 137,326	\$ 397,544	\$ 228,478

Amtrak recorded an additional minimum liability of \$7,022,000 to other long-term liabilities as the result of the ABO exceeding the fair value of plan assets at September 30, 2003. Offsetting this liability are \$1,061,000 of unrecognized prior service cost recorded as deferred charge, and \$5,961,000 of unrealized comprehensive loss recorded as a reduction to equity.

	Pension Benefits		Other Benefits	
	2003	2002	2003	2002
Weighted average assumptions as of September 30, (in percentages of 100%):				
Discount rate	6.00	7.25	6.00	7.25
Expected return on plan assets	8.00	8.00	N/A	N/A
Rate of compensation increase	4.00	4.00	N/A	N/A

The pension plan's assets consist primarily of U.S equity investments, fixed income investments, and international equity investments. The postretirement benefits program has no plan assets. Amtrak funds this program on a pay-as-you-go basis.

For measurement purposes, a 12.0% and 9.0% annual rate of increase in the per capita cost of covered healthcare benefits was assumed for fiscal years 2003 and 2002, respectively. For fiscal year 2003, the rate was assumed to gradually decrease to 5.0% by 2011, and remain at that level thereafter. For fiscal year 2002, the rate was assumed to gradually decrease to 4.5% by 2008, and remain at that level thereafter.

The following table provides the components of net periodic benefit cost for the plans for fiscal years 2003 and 2002 (in thousands):

	Pension Benefits		Other Benefits	
	2003	2002	2003	2002
Service cost	\$ 6,330	\$ 6,425	\$ 8,053	\$ 6,810
Interest cost	11,723	10,824	16,295	14,397
Expected return on plan assets	(12,354)	(13,805)	-	-
Amortization of prior service cost	203	206	1,203	1,203
Amortization of net (gain) loss	-	(294)	1,690	713
Curtailement loss	28	20	1,093	-
Termination benefits	-	3,689	-	-
Other	-	(2)	-	-
Net periodic benefit cost	<u>\$ 5,930</u>	<u>\$ 7,063</u>	<u>\$ 28,334</u>	<u>\$ 23,123</u>

The prior service costs are amortized on a straight-line basis over the average remaining service period of active participants for both plans. Gains and losses in excess of 10% of the greater of the benefit obligation and the market-related value of assets are amortized over the average remaining service period of active participants.

Under Amtrak's postretirement benefits program, substantially all salaried employees may become eligible for medical benefits if they meet the service requirement and reach age 55 while they are working for Amtrak. Company-provided medical benefits are reduced when covered individuals become eligible for Medicare benefits or reach age 65, whichever comes first. Medical benefits are subject to co-payment provisions and other limitations.

On December 8, 2003, the Medicare Prescription Drug, Improvement, and Modernization Act of 2003 (the "Medicare Act") was signed into law as Public Law 108-173. The Medicare Act introduced a prescription drug benefit under Medicare (Medicare Part D) as well as a federal subsidy to sponsors of retiree health care benefit plans that provide a benefit that is at least actuarially equivalent to Medicare Part D. Amtrak has not determined what impact, if any, the Medicare Act will have on its postretirement benefit programs.

Assumed healthcare cost trend rates have a significant effect on the amounts reported for the healthcare plan. A one-percentage-point change in assumed healthcare cost trend rates would have the following effects (in thousands):

	1% Increase	1% Decrease
Effect on total of service and interest cost component	\$ 4,112	\$ (3,385)
Effect on postretirement benefit obligation	\$ 51,990	\$ (44,681)

Amtrak provides a 401(k) savings plan for nonunion employees. Under the plan, Amtrak matches a portion of employee contributions up to five percent of the participant's salary, subject to applicable limitations. Amtrak's expenses under this plan were \$6,192,000 and \$6,996,000 for the years ended September 30, 2003 and 2002, respectively.

**NOTE 12: FAIR VALUE OF FINANCIAL INSTRUMENTS**

For cash and cash equivalents, accounts receivable, accounts payable and accrued expenses and other current liabilities, the carrying amounts approximate fair value because of the short maturities of these instruments. The carrying amounts of the revolving credit facilities, a portion of bonds, and equipment obligations also approximate fair value. All charge interest at rates that are periodically adjusted to market.

The estimated fair values of the mortgage obligations, remaining bonds, and notes payable were based upon discounted cash flow analyses using interest rates available to Amtrak at September 30, 2003 and 2002 for debt with the same remaining maturities. Although interest free, the UDAG loan was also valued based upon a discounted cash flow analysis using September 30, 2003 and 2002 market interest rates. The estimated fair values of these financial instruments are as follows (in thousands):

	2003		2002	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Mortgage obligations	\$ 283,698	\$ 324,797	\$ 314,306	\$ 356,316
Equipment obligations	502	502	10,404	10,405
Notes payable	20,000	20,000	20,000	18,916
Bonds	79,426	84,969	30,000	30,000
UDAG loan	\$ 11,577	\$ 10,629	\$ 11,707	\$ 10,266