

WEST VIRGINIA STATE RAIL AUTHORITY

A COMPONENT UNIT OF THE STATE OF WEST VIRGINIA
AND THE WEST VIRGINIA DEPARTMENT OF TRANSPORTATION

FINANCIAL STATEMENTS WITH ADDITIONAL INFORMATION

YEAR ENDED JUNE 30, 2010

AND

INDEPENDENT AUDITORS' REPORT

West Virginia State Rail Authority
Year Ended June 30, 2010

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INDEPENDENT AUDITORS' REPORT

To the Members of the
West Virginia State Rail Authority
Moorefield, West Virginia

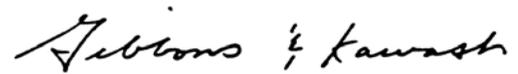
We have audited the accompanying balance sheet of the West Virginia State Rail Authority (the Authority), a component unit of the State of West Virginia and the West Virginia Department of Transportation, as of June 30, 2010, and the related statements of revenues, expenses, and changes in fund net assets and cash flows for the year then ended. These financial statements are the responsibility of the Authority's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the West Virginia State Rail Authority as of June 30, 2010, and the results of its operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 21, 2010, on our consideration of the Authority's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3 through 9 be presented to supplement the financial statements. Such information, although not a part of the financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the financial statements, and other knowledge we obtained during our audit of the financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

A handwritten signature in black ink that reads "Gibson & Kawash". The signature is written in a cursive, flowing style.

October 21, 2010

**WEST VIRGINIA STATE RAIL AUTHORITY
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Unaudited)**

The management of the West Virginia State Rail Authority (Authority) offers readers of our financial statements the following narrative overview and analysis of our financial activities for the year ended June 30, 2010. Please read it in conjunction with the Authority's basic financial statements and notes to the financial statements which follow this section.

FINANCIAL HIGHLIGHTS

- The Authority's net assets increased approximately \$692 thousand as a result of this year's operations. This was due to continual capital improvement projects and upgrades to both the South Branch Valley Railroad (SBVR) and the West Virginia Central Railroad (WVCR) funded through legislative appropriation.
- Operating expenses decreased by approximately \$13 thousand during the year ended June 30, 2010 and operating revenues increased approximately \$120 thousand. This resulted in a reduction in the operating loss of approximately \$133 thousand compared to the year ended June 30, 2009. The expenses that are most responsible for fluctuations in our operations are; salaries and benefits, car hire, diesel fuel, and liability and property insurance. In the current year there was a slight decrease in both diesel fuel and car hire expenses. Freight revenue increased due to the handling of more cars during the fiscal year ended June 30, 2010.
- Non-operating revenues (expenses) were approximately \$2.4 million for the year ended June 30, 2010 compared to non-operating revenues (expenses) of approximately \$3.1 million for the year ended June 30, 2009. The change in total non-operating revenues (expenses) can be attributed to a decrease in intergovernmental revenue, interest income, and a decrease in losses incurred for the disposition of assets.
- The Authority completed approximately \$1.6 million in capital improvements for the year ended June 30, 2010 including approximately \$700 thousand for SBVR track, \$300 thousand for SBVR equipment and approximately \$600 thousand for the WVCR track.

**WEST VIRGINIA STATE RAIL AUTHORITY
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Unaudited)**

OVERVIEW OF THE FINANCIAL STATEMENTS

This annual report includes management's discussion and analysis, the independent auditor's report and the financial statements of the Authority. The financial statements also include notes that explain in more detail the significant information in the financial statements.

The financial statements of the Authority report information using accounting methods similar to those used by private sector companies. These statements offer short and long term financial information about its activities. The Statement of Net Assets includes all of the Authority's assets and liabilities and provides information about the investments in resources (assets) and the obligations to creditors (liabilities). It also provides the basis for evaluating the capital structure of the Authority and assessing the liquidity and financial flexibility of the Authority.

All of the current year's revenues and expenses are accounted for in the Statement of Revenues, Expenses, and Changes in Fund Net Assets. This statement measures the success of the Authority's operations over the past year and can be used to determine whether the Authority's costs are recovered from revenues and how much of the cost is supplemented by appropriations from the State of West Virginia.

The final required financial statement is the Statement of Cash Flows. This statement reports cash receipts, cash payments, and net changes in cash resulting from operating, investing, and financing activities. It provides answers to cash inflows and outflows, supporting the change in the cash balance during the reporting period.

CONDENSED FINANCIAL STATEMENTS

Condensed financial information from the Statements of Net Assets and Statements of Revenues, Expenses and Changes in Fund Net Assets as of and for the years ended June 30, 2010 and 2009 are as follows:

**WEST VIRGINIA STATE RAIL AUTHORITY
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Unaudited)**

Condensed Statement of Net Assets

	<u>2010</u>	<u>2009</u>
Current assets	\$ 4,164,924	\$ 3,352,932
Capital assets, net	<u>37,324,123</u>	<u>37,352,374</u>
Total assets	<u>41,489,047</u>	<u>40,705,306</u>
Current liabilities	98,526	133,968
Noncurrent liabilities	<u>270,746</u>	<u>143,073</u>
Total liabilities	<u>369,272</u>	<u>277,041</u>
Net assets - Invested in capital assets net of related debt	37,324,123	37,352,374
Net assets - Unrestricted	<u>3,795,652</u>	<u>3,075,891</u>
Total net assets	<u>\$ 41,119,775</u>	<u>\$ 40,428,265</u>

Condensed Statement of Revenues, Expenses, and Changes in Fund Net Assets

	<u>2010</u>	<u>2009</u>
Operating revenues		
Freight	\$ 2,085,610	\$ 1,990,521
Miscellaneous	<u>187,045</u>	<u>162,564</u>
Total operating revenues	<u>2,272,655</u>	<u>2,153,085</u>
Operating expenses		
Depreciation expense	1,591,202	1,547,468
Other operating expenses	<u>2,377,147</u>	<u>2,434,105</u>
Total operating expenses	<u>3,968,349</u>	<u>3,981,573</u>
Operating loss	(1,695,694)	(1,828,488)
Non-operating revenues	<u>2,387,204</u>	<u>3,067,829</u>
Change in net assets	691,510	1,239,341
Total net assets - beginning	<u>40,428,265</u>	<u>39,188,924</u>
Total net assets - ending	<u>\$ 41,119,775</u>	<u>\$ 40,428,265</u>

**WEST VIRGINIA STATE RAIL AUTHORITY
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Unaudited)**

FINANCIAL ANALYSIS

- The Authority's budget for the fiscal year ended June 30, 2010 consisted of funds received from the State of West Virginia General Fund, operating revenues from SBVR, revenues from the operator of the WVCR, and miscellaneous revenues received from the leases and licenses on railroad right-of-ways.

- The Authority received an approximate \$2.4 million appropriation in intergovernmental revenue from the General Fund of the State of West Virginia for capital improvement projects and maintenance projects on the SBVR and WVCR, upkeep of the Maryland Area Rail Commuter (MARC) train stations in the eastern panhandle, and the general operation of the Authority. This appropriation is about 52% of the total funds received. The rehabilitation of the SBVR is planned to be completed in June 2011. After this rehabilitation program is complete, appropriations will be used for continued maintenance projects on the SBVR and more funding will be shifted to projects on the WVCR in order to safely maintain the condition of both railroads.

- Freight revenue of approximately \$2.1 million was earned from the operations of the SBVR which was in line with the year ended June 30, 2010 budgeted projections. Miscellaneous revenues of approximately \$187 thousand were earned in addition to the freight revenue. The miscellaneous revenue is made up of Right of Way leases on the SBVR and income received from the excursion train operators. This revenue is used to pay the operating expenses of the SBVR. Total operating revenues increased by 5% in the fiscal year ended June 30, 2010.

**WEST VIRGINIA STATE RAIL AUTHORITY
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Unaudited)**

The following graphs provide a visual representation of the funding (revenue and other income sources) and expenses for the fiscal year ended June 30, 2010.

Chart 1 - Expense Breakdown - Year Ended June 30, 2010

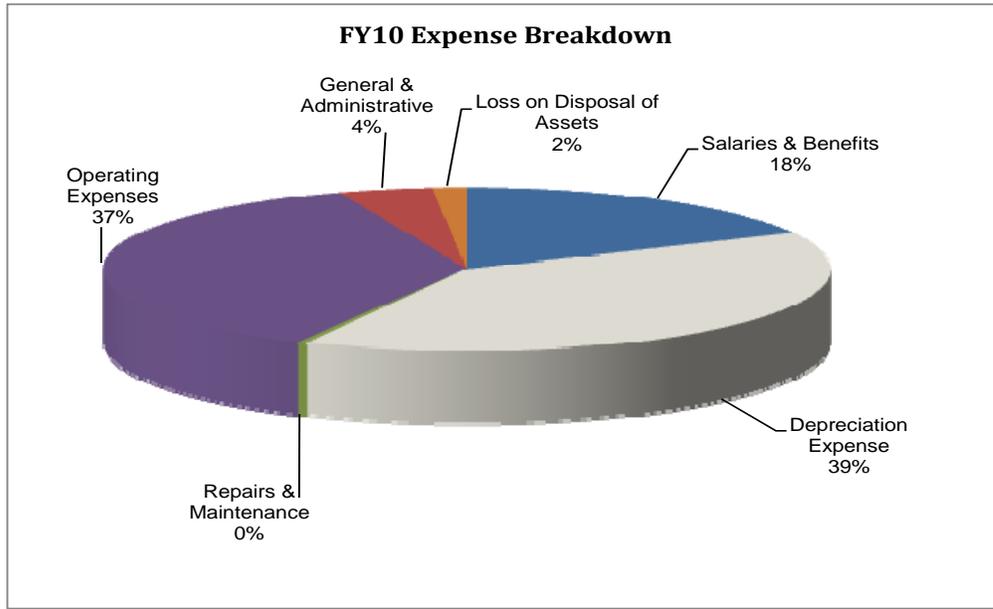
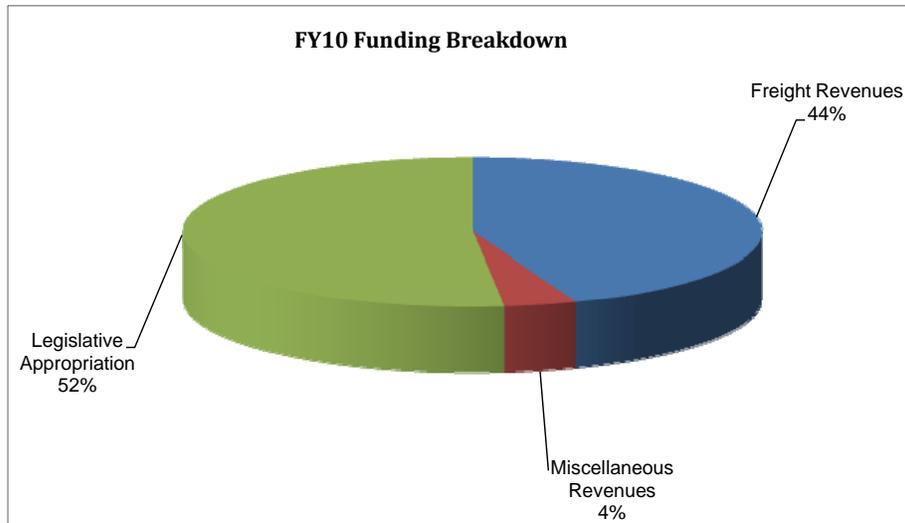


Chart 2 - Funding Breakdown - Year Ended June 30, 2010



**WEST VIRGINIA STATE RAIL AUTHORITY
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Unaudited)**

CAPITAL ASSETS

The Authority's net capital assets as of June 30, 2010 and 2009 amounted to \$37.3 million and \$37.4 million, respectively. This investment in capital assets includes land, rail properties, transportation and other equipment, and office buildings and equipment.

The Authority primarily acquires its assets with proceeds from the general fund appropriation from the State of West Virginia. Rehabilitation and improvements to the SBVR and WVCR are part of the Authority's capital investment program.

Capital asset additions included the following for the years ended June 30:

	<u>2010</u>	<u>2009</u>
Rail properties	\$ 1,303,375	\$ 2,396,513
Transportation and other equipment	<u>321,251</u>	<u>-</u>
Total	<u>\$ 1,624,626</u>	<u>\$ 2,396,513</u>

Readers interested in more detailed information regarding capital assets should review the accompanying notes to the financial statements.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET

The SBVR's track structure has improved significantly over the past ten years. By establishing a long term capital improvement program, the Authority has been able to increase the weight restrictions on railcars. Track safety has also improved resulting in fewer derailments. Because of the improved track structure, the operating speeds on the SBVR have increased. This has allowed the SBVR to increase the turnaround time for rail cars supplying a significant feed mill enterprise in Moorefield, West Virginia, which is the largest employer in the Potomac Valley. Management believes it is vital that the Authority continue to upgrade the rail infrastructure and maintain the track to promote the economic success of the area it serves. The SBVR capital improvements planned for the fiscal year ending June 30, 2011 include continuing to upgrade and repair bridges, expand the siding at Green Spring, purchase an additional locomotive and replace a highway/railroad grade crossing.

**WEST VIRGINIA STATE RAIL AUTHORITY
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Unaudited)**

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET (Continued)

The Authority's year ending June 30, 2011 budget includes approximately \$2.5 million from the State of West Virginia and approximately \$2.7 million from projected freight revenue. This funding be used to complete the long-term rehabilitation projects started on the SBVR and continue to maintain the WVCR. The capital improvement projects planned on the WVCR for the fiscal year ending June 30, 2011 include tie replacement, ballast spreading, surfacing, replacing culverts and replacing a highway/railroad grade crossing. This railroad has completed eleven years of operations and continues to be a strong economic factor to the areas that it serves.

The Authority will continue to maintain commuter facilities at Harpers Ferry, Duffields and Martinsburg for the MARC train service. This offers West Virginia citizens in the eastern panhandle the advantage of using commuter train service to Washington, DC.

REQUESTS FOR INFORMATION

This financial report is designed to provide an overview of the finances of the Authority for those with an interest in this organization. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the West Virginia State Rail Authority at 120 Water Plant Drive, Moorefield, West Virginia, 26836.

WEST VIRGINIA STATE RAIL AUTHORITY
STATEMENT OF ASSETS
JUNE 30, 2010

ASSETS

Current Assets

Cash and cash equivalents	\$ 4,075,006
Trade receivables	49,680
Inventories	39,579
Other current assets	<u>659</u>

Total current assets 4,164,924

Noncurrent assets

Capital assets	55,396,161
Accumulated depreciation	<u>(18,072,038)</u>

Total noncurrent assets 37,324,123

Total assets \$ 41,489,047

LIABILITIES

Current liabilities

Accounts payable	\$ 640
Accrued expenses	41,626
Compensated absences	49,918
Due to other governmental entities	2,978
Deferred revenue	<u>3,364</u>

Total current liabilities 98,526

Noncurrent liabilities

Other post employment benefits liability	194,083
Deferred revenue	<u>76,663</u>

Total noncurrent liabilities 270,746

Total liabilities 369,272

NET ASSETS

Invested in capital assets	37,324,123
Unrestricted	<u>3,795,652</u>

Total net assets \$ 41,119,775

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

WEST VIRGINIA STATE RAIL AUTHORITY
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET ASSETS
FOR THE YEAR ENDED JUNE 30, 2010

Operating revenues	
Freight	\$ 2,085,610
Miscellaneous	<u>187,045</u>
Total operating revenues	<u>2,272,655</u>
 Operating expenses	
Depreciation expense	1,591,202
Other operating expenses	<u>2,377,147</u>
Total operating expenses	<u>3,968,349</u>
Operating loss	<u>(1,695,694)</u>
 Nonoperating revenues (expenses)	
Intergovernmental revenue	2,443,712
Interest income	5,167
Loss on disposition of assets	<u>(61,675)</u>
Total nonoperating revenues	<u>2,387,204</u>
Change in net assets	691,510
Total net assets - beginning	<u>40,428,265</u>
Total net assets - ending	<u>\$ 41,119,775</u>

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

WEST VIRGINIA STATE RAIL AUTHORITY
STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED JUNE 30, 2010

Cash flows from operating activities	
Cash received from customers and government	\$ 2,308,019
Cash paid to employees	(663,448)
Cash paid to suppliers and government	<u>(1,612,787)</u>
Net cash provided by operating activities	<u>31,784</u>
Cash flows from noncapital financing activities	
Receipts of appropriations from State of West Virginia	<u>2,477,163</u>
Cash flows from capital and related financing activities	
Purchase of capital assets	<u>(1,624,626)</u>
Cash flows from investing activities	
Receipts of interest	<u>5,167</u>
Increase in cash and cash equivalents	889,488
Cash and cash equivalents, beginning of year	<u>3,185,518</u>
Cash and cash equivalents, end of year	<u>\$ 4,075,006</u>
Reconciliation of operating income to net cash provided by operating activities	
Operating loss	\$ (1,695,694)
Adjustments to reconcile operating loss to net cash provided by operating activities:	
Depreciation	1,591,202
Changes in operating assets and liabilities	
(Increase) decrease in operating assets:	
Trade receivables	38,728
Inventories	5,236
Increase (decrease) in operating liabilities:	
Other current assets	81
Accounts payable	(33,495)
Accrued expenses	(159)
Employee benefit accruals	128,574
Deferred revenue	(3,364)
Due to other governmental entities	<u>675</u>
Net cash provided by operating activities	<u>\$ 31,784</u>

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

**WEST VIRGINIA STATE RAIL AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
YEAR ENDED JUNE 30, 2010**

NOTE 1: DESCRIPTION OF ORGANIZATION AND FINANCIAL REPORTING ENTITY

In 1975, the West Virginia Legislature created the West Virginia State Rail Authority (the Authority) under the provisions of Chapter 29, Article 18 of the Code of West Virginia, 1931, as amended, known as the “West Virginia Railroad Maintenance Act.” The Authority was created to participate in the rehabilitation, improvement, and restoration of the financial stability of the railway system in the State of West Virginia and enable it to remain viable in the public sector as a mode of transportation. The Authority maintains the South Branch Valley Railroad, and the West Virginia Central Railroad, and is responsible for the rails-to-trails program operation. The Secretary of Transportation serves as a member of the Authority and the remaining six members are appointed by the Governor.

In evaluating how to define the Authority for financial reporting purposes, management has considered all potential component units. The decision to include a potential component unit in the reporting entity is made by applying the criteria set forth in accounting principles generally accepted in the United States of America. Accounting principles generally accepted in the United States of America define component units as those entities which are legally separate governmental organizations for which the appointed members of the Authority are financially accountable, or other organizations for which the nature and significance of their relationship with the Authority are such that exclusion would cause the Authority’s financial statements to be misleading. Since no such organizations exist which meet the above criteria, the Authority has no component units. The Authority is an enterprise fund and a component unit of the West Virginia Department of Transportation and the State of West Virginia. Accordingly, the Authority’s financial statements are discretely presented in the financial statements of the West Virginia Department of Transportation and in the financial statements of the State of West Virginia.

NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

BASIS OF ACCOUNTING - The Authority is considered an enterprise fund and uses the flow of economic resources measurement focus and the accrual basis of accounting. Under this basis, revenues are recorded when earned and expenses are recorded when incurred. Enterprise funds are operated in a manner similar to private business enterprises where the intent of the governing body is that the cost (expense, including depreciation) of providing goods and services to the general public on a continuing basis be financed or recovered primarily through user charges. As permitted by Governmental Accounting Standards Board (GASB) Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting*, the Authority has elected not to adopt Financial Accounting

WEST VIRGINIA STATE RAIL AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
YEAR ENDED JUNE 30, 2010

NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Standards Board (FASB) statements, interpretations and/or Accounting Standards Updates issued after November 30, 1989, unless the GASB specifically adopts such FASB statements, interpretations, and Accounting Standards Updates.

FINANCIAL STATEMENT PRESENTATION - The Authority prepares its financial statements in accordance with GASB Statement No. 34, Basic Financial Statements and Management Discussion and Analysis - for States and Local Governments, as amended.

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 certain estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from management's estimates.

CASH AND CASH EQUIVALENTS - For purposes of the statement of net assets, the Authority considers all highly liquid investments with an original maturity of three months or less to be cash equivalents.

Cash and cash equivalents balances on deposit with the State of West Virginia Treasurer's Office (the "State Treasurer") are pooled by the State Treasurer with other available funds of the State for investment purposes and deposited with the West Virginia Board of Treasury Investments (BTI). The BTI is directed by the State Treasurer to invest the funds in specific investment pools in accordance with West Virginia Code, policies set by the BTI, provisions of bond indentures, and the trust agreements when applicable. Balances in the investment pools are recorded at amortized cost. The BTI was established by the State Legislature and is subject to oversight by the State Legislature. Changes in investment income are allocated to participants in the pools based upon the funds that have been invested. The amounts on deposit are available for immediate withdrawal and, accordingly, are presented as cash and cash equivalents in the accompanying financial statements.

The BTI maintains the Consolidated Fund, which consists of investment pools and participant-directed accounts. These pools have been structured as multiparticipant variable net asset funds to reduce risk and offer investment liquidity diversification to the Consolidated Fund participants. A more detailed discussion of the BTI's permissible investments and operations can be found in its annual report. A copy of that annual report can be obtained from the following address: 1900 Kanawha Blvd. East, Room E-122, Charleston, WV 25305 or <http://www.wvbt.org>.

**WEST VIRGINIA STATE RAIL AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
YEAR ENDED JUNE 30, 2010**

NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

ALLOWANCE FOR DOUBTFUL ACCOUNTS - It is the Authority's policy to provide for future losses on uncollectible accounts, contracts, grants, and loans receivable based on an evaluation of the underlying account, contract, grant and loan balances, the historical collectability experienced by the Authority on such balances and such other factors which, in the Authority's judgment, require consideration in estimating doubtful accounts.

INVENTORIES - Inventories are stated at the lower-of-cost or market, using the weighted average cost method.

CAPITAL ASSETS - Purchases of capital assets are capitalized at cost and, except for land which is not depreciated, are depreciated using the straight-line method over the estimated useful lives of the assets ranging from five to forty years. Buildings and land with an initial cost of \$25,000 or more and furniture and equipment with an initial cost of \$5,000 or more are recorded at cost. When assets are disposed of, the cost and related accumulated depreciation are removed from the accounts and any resulting gain or loss is recognized in operations. The cost of maintenance and repairs is charged to operations as incurred; significant renewals and betterments are capitalized. Capital assets are reviewed annually for impairment.

COMPENSATED ABSENCES AND OTHER POST EMPLOYMENT BENEFITS - Employees fully vest in all earned but unused annual leave and the Authority accrues for obligations that may arise in connection with compensated absences for vacation at the current rate of employee pay. Effective July 1, 2007, the Authority adopted GASB Statement No. 45, Accounting and Financial Reporting by Employers for Postemployment Benefits Other than Pensions. This statement provided standards for the measurement, recognition, and display of other postemployment benefit ("OPEB") expenditures, assets, and liabilities, including applicable note disclosures and required supplementary information. During fiscal year 2006, House Bill No. 4654 was established to create a trust fund for postemployment benefits for the State of West Virginia (the "State"). Effective July 1, 2007, The Authority was required to participate in this multiple employer cost-sharing plan, the West Virginia Retiree Health Benefit Trust Fund sponsored by the State of West Virginia. Details regarding this plan can be obtained by contacting Public Employees Insurance Agency ("PEIA"), 601 57th Street, S.E., Suite 2, Charleston, WV 25304-2345 or <http://www.wvpeia.wv.gov>.

The Authority's full-time employees earn up to two vacation leave days for each month of service and are entitled to compensation for accumulated, unpaid vacation leave upon termination. Full-time employees also earn 1 ½ sick leave days for each month of service and are entitled to extend their health or life insurance coverage upon retirement in lieu of accumulated,

**WEST VIRGINIA STATE RAIL AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
YEAR ENDED JUNE 30, 2010**

NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

unpaid sick leave. Generally, two days of accrued sick leave extend health insurance for one month of single coverage and three days extend health insurance for one month of family coverage. For employees hired after 1988, the employee shares in the cost of the extended benefit coverage to the extent of 50% of the premium required for the extended coverage. Employees hired July 1, 2001, or later are not eligible for these benefits. During 2010, the legislature passed a bill allowing regular full time employees hired before July 1, 2001, having accumulated at least 65 days of sick leave, to be paid, at their option, for a portion of their unused sick leave, not to exceed the number of sick leave days that would reduce the employee's sick leave balance to less than fifty days. The employee shall be paid at a rate equal to one quarter of their usual rate of daily pay during that calendar year. Post-employment health care benefits are now provided through the multiple employer cost-sharing plan sponsored by the State of West Virginia (See Note 8).

OPERATING REVENUES AND EXPENSES - Balances classified as operating revenues and expenses are those which comprise the Authority's ongoing operations. Principal operating revenues are charges to customers for use of the rail lines. Principal operating expenses are the costs of providing the goods and services and include administrative expenses and depreciation of capital assets. Other revenues and expenses are classified as non-operating in the financial statements.

NET ASSETS - As required by GASB 34, the Authority displays net assets in three components, if applicable: invested in capital assets, net of related debt; restricted, and unrestricted.

INVESTED IN CAPITAL ASSETS - This component of net assets consists primarily of capital assets, including restricted capital assets (if any), net of accumulated depreciation and reduced by the outstanding balances of any bonds, mortgages, notes or other borrowings that are attributable to the acquisition, construction, or improvement of those assets, if any.

RESTRICTED NET ASSETS - Restricted net assets are assets whose use or availability has been restricted and the restrictions limit the Authority's ability to use the resources to pay current liabilities. When both restricted and unrestricted resources are available for use, it is the Authority's policy to use restricted resources first, then unrestricted resources as needed. As of June 30, 2010 there were no restricted net assets.

WEST VIRGINIA STATE RAIL AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
YEAR ENDED JUNE 30, 2010

NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

UNRESTRICTED NET ASSETS - Unrestricted net assets consist of net assets that do not meet the definition of “restricted” or “invested in capital assets, net of related debt.” In the governmental environment, net assets are often designated to indicate that management does not consider them to be available for general operations. These types of constraints on resources are internal and management can remove or modify them. Such internal designations are not reported on the face of the statement of net assets.

INTERGOVERNMENTAL REVENUE - Intergovernmental revenue represents legally authorized appropriations under West Virginia State Code by the West Virginia Legislature.

NEWLY ADOPTED STATEMENTS ISSUED BY THE GASB - The Authority adopted GASB Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*, during the year ended June 30, 2010. This statement requires that all intangible assets not specifically excluded by its scope provisions be classified as capital assets. Accordingly, existing authoritative guidance related to the accounting and financial reporting for capital assets should be applied to these intangible assets, as applicable. This statement also provides authoritative guidance that specifically addresses the nature of these intangible assets. Such guidance should be applied in addition to the existing authoritative guidance for capital assets. The adoption of this statement had no impact on the June 30, 2010 financial statements.

The Authority adopted GASB Statement No. 53 *Accounting and Financial Reporting for Derivative Instruments*, during the year ended June 30, 2010. This statement addresses the recognition, measurement, and disclosure of information regarding derivative instruments entered into by state and local governments. Derivative instruments are often complex financial arrangements used by governments to manage specific risks or to make investments. By entering into these arrangements, governments receive and make payments based on market prices without actually entering into the related financial or commodity transactions. Derivative instruments can be used as effective risk management or investment tools. Derivative instruments can also expose governments to significant risks and liabilities. The adoption of this statement had no impact on the June 30, 2010 financial statements.

**WEST VIRGINIA STATE RAIL AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
YEAR ENDED JUNE 30, 2010**

NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

RECENT STATEMENTS ISSUED BY THE GASB - The GASB has issued Statement No. 59, *Financial Instruments Omnibus*, the provisions of this Statement are effective for financial statements for periods beginning after June 15, 2010. The requirements of this Statement will improve financial reporting by providing more complete information, by improving consistency of measurements, and by providing clarifications of existing standards. Applying the reporting provisions of Statement No. 31 for interest-earning investment contracts to unallocated insurance contracts improves consistency of investment measurements that are reported by pension and other postemployment benefit plans. Emphasizing the applicability of SEC requirements to 2a7-like external investment pools provides practitioners with improved guidance. Limiting interest rate risk disclosures for investments in mutual funds, external investment pools, and other pooled investments to debt investment pools provides better guidance regarding the applicability of interest rate risk disclosures. Finally, addressing the applicability of Statement No. 53 to certain financial instruments refines which financial instruments are within the scope of that Statement. The Authority does not anticipate this Statement to have a significant effect on the financial statements.

NOTE 3: CASH AND CASH EQUIVALENTS

Cash and cash equivalents as of June 30, 2010, consisted of deposits with the State Treasurer and investments in the BTI's West Virginia Money Market Pool which amounted to \$4,075,006, and were carried at amortized cost which approximated fair value.

West Virginia Board of Treasury Investments (BTI) West Virginia Money Market Pool

The BTI has adopted an investment policy in accordance with the "Uniform Prudent Investor Act." The "prudent investor rule" guides those with responsibility for investing the money for others. Such fiduciaries must act as a prudent person would be expected to act, with discretion and intelligence, to seek reasonable income; preserve capital; and, in general, avoid speculative investments. The BTI's investment policy to invest assets in a manner that strives for maximum safety, provides adequate liquidity to meet all operating requirements, and achieves the highest possible investment return consistent with the primary objectives of safety and liquidity. The BTI recognizes that risk, volatility, and the possibility of loss in purchasing power are present to some degree in all types of investments. Due to the short-term nature of BTI's Pools, the BTI believes that it is imperative to review and adjust the investment policy in reaction to interest rate market fluctuations/trends on a regular basis and has adopted a formal review schedule.

**WEST VIRGINIA STATE RAIL AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
YEAR ENDED JUNE 30, 2010**

NOTE 3: CASH AND CASH EQUIVALENTS (Continued)

Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. For the year ended June 30, 2010, the West Virginia Money Market Pool has been rated AAAm by Standard & Poor's. A fund rated "AAAm" has extremely strong capacity to maintain principal stability and to limit exposure to principal losses due to credit, market, and/or liquidity risks. "AAAm" is the highest principal stability fund rating assigned by Standard & Poor's. The West Virginia Money Market Pool is subject to credit risk.

The BTI limits the exposure to credit risk in the WV Money Market Pool by requiring all corporate bonds to be rated AA- by Standard & Poor's (or its equivalent) or higher. Commercial paper must be rated at least A-1 by Standard & Poor's and P1 by Moody's. The pool must have at least 15% of its assets in U.S. Treasury issues.

At June 30, 2010, the WV Money Market Pool investments had a total carrying value of \$2,876,711,000, of which the Authority's ownership represents .14% of these amounts held by the BTI.

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The BTI's West Virginia Money Market Pool is subject to interest rate risk.

The overall weighted average maturity of the investments of the West Virginia Money Market Pool cannot exceed 60 days. Maximum maturity of individual securities cannot exceed 397 days from date of purchase. The following table provides information on the weighted average maturities for the various asset types in the West Virginia Money Market Pool:

**WEST VIRGINIA STATE RAIL AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
YEAR ENDED JUNE 30, 2010**

NOTE 3: CASH AND CASH EQUIVALENTS (Continued)

Security Type	2010	
	Carrying Value (In Thousands)	Weighted Average Maturity (Days)
Repurchase agreements	\$ 174,980	1
U.S. Treasury notes	65,153	140
U.S. Treasury bills	476,670	35
Commercial paper	855,844	18
Certificates of deposit	281,000	45
U.S. agency discount notes	606,048	52
Corporate bonds and notes	20,000	19
U.S. agency bonds/notes	246,990	55
Money market funds	150,026	1
	\$ 2,876,711	33

Other Risks of Investing

Other risks of investing can include concentration of credit risk, custodial credit risk, and foreign currency risk. The West Virginia Money Market Pool is not exposed to these risks as described below.

Concentration of credit risk is the risk of loss attributed to the magnitude of the pool or in a single corporate issuer. The BTI investment policy prohibits the pool to hold corporate securities from investing more than 5% of their assets in any one corporate name of one corporate issue.

The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, the BTI will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. Repurchase agreements are required to be collateralized by at least 102% of their value, and the collateral is held in the name of the BTI. Securities lending collateral that is reported on the BTI's Statement of Fiduciary Net Assets is invested in the lending agent's money market fund in the BTI's name. In all transactions, the BTI or its agent does not release cash or securities until the counterparty delivers its side of the transaction.

**WEST VIRGINIA STATE RAIL AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
YEAR ENDED JUNE 30, 2010**

NOTE 3: CASH AND CASH EQUIVALENTS (Continued)

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or a deposit. The West Virginia Money Market Pool does not hold interests in foreign currency or interests valued in foreign currency.

Deposits

Custodial credit risk of deposits is the risk that in the event of failure of a depository financial institution, a government will not be able to recover deposits or will not be able to recover collateral securities that are in the possession of an outside party. Deposits include nonnegotiable certificates of deposit. The West Virginia Money Market Pool does not contain non-negotiable certificates of deposit. The BTI does not have a deposit policy for custodial credit risk.

NOTE 4: CAPITAL ASSETS

Capital assets balances and the activity for the year ended June 30, 2010 is summarized below:

	June 30, 2009			June 30, 2010	
	<u>Balance</u>	<u>Additions</u>	<u>Deletions</u>	<u>Balance</u>	
Capital assets					
Land	\$ 4,835,588	\$ -	\$ -	\$ 4,835,588	
Rail properties	47,083,041	1,303,375	97,120	48,289,296	
Transportation and other equipment	1,498,656	321,251	-	1,819,907	
Office buliding and equipment	<u>451,370</u>	<u>-</u>	<u>-</u>	<u>451,370</u>	
Total capital assets	<u>\$ 53,868,655</u>	<u>\$ 1,624,626</u>	<u>\$ 97,120</u>	<u>\$ 55,396,161</u>	
Accumulated depreciation					
Rail properties	\$ 15,193,003	\$ 1,466,530	\$ 35,445	\$ 16,624,088	
Transportation and other equipment	987,958	114,006	-	1,101,964	
Office building and equipment	<u>335,320</u>	<u>10,666</u>	<u>-</u>	<u>345,986</u>	
Total accumulated depreciation	<u>\$ 16,516,281</u>	<u>\$ 1,591,202</u>	<u>\$ 35,445</u>	<u>\$ 18,072,038</u>	

NOTE 5: TRANSACTIONS WITH OTHER WEST VIRGINIA GOVERNMENTAL ENTITIES

The West Virginia Office of the Secretary of Administration, Finance Division distributed from the West Virginia Financial Information Management System (FIMS) fund 0506 \$2,443,712 to the Authority for the year ended June 30, 2010.

**WEST VIRGINIA STATE RAIL AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
YEAR ENDED JUNE 30, 2010**

NOTE 6: SIGNIFICANT CUSTOMERS AND FUNDING SOURCES

During the year ended June 30, 2010, approximately 91.8% of the Authority's freight traffic was attributable to a single customer. In addition, during the year ended June 30, 2010 the Authority received distributions of \$2,443,712 in appropriated funds. A significant decrease in this revenue or assistance would have a significant effect on the operations of the Authority.

The credit and liquidity crisis in the United States and throughout the global financial system triggered significant events and substantial volatility in world financial markets and the banking system that have had a significant negative impact on foreign and domestic financial markets. If the aforementioned single customer is affected it could have a significant impact on the future operations of the Authority.

NOTE 7: RISK MANAGEMENT

The Authority is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; employee health and life coverage; and natural disasters. The State of West Virginia established the Board of Risk and Insurance Management (BRIM) and the Public Employees Insurance Agency (PEIA) public entity risk pools to account for and finance uninsured risks of losses for state agencies, institutions of higher education, and component units.

BRIM is a public entity risk pool that provides coverage for general, liability and property damage in the amount of \$1,000,000 per occurrence. Such coverage may be provided to the Authority by BRIM through self-insurance programs maintained by BRIM or policies underwritten by BRIM that may involve experience – related premiums or adjustments to BRIM. BRIM engages an independent actuary to assist in the determination of its premiums so as to minimize the likelihood of premium adjustments to the Authority or other participants in BRIM'S insurance program. As a result, management does not expect significant differences between the premiums the Authority is currently charged by BRIM and the ultimate cost of that insurance based on the Authority's actual loss experience. Furthermore, there have been no settlements that have exceeded this coverage in the last three years.

Through its participation in the PEIA, the Authority has obtained health, life and prescription drug coverage for all its employees. The Authority, through a third-party insurer has obtained coverage for job related injuries for its employees. The commercial insurance carrier is paid a monthly rated premium to provide compensation for injuries sustained in the course of employment. In exchange for payment of premiums to PEIA and the third-party insurer, the Authority has transferred its risks related to health, life, and prescription drug coverage.

**WEST VIRGINIA STATE RAIL AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
YEAR ENDED JUNE 30, 2010**

NOTE 7: RISK MANAGEMENT (Continued)

PEIA issues publicly available financial reports that include financial statements and required supplementary information, these reports may be obtained by writing to West Virginia Public Employees Insurance Agency, 601 57th Street, Charleston, WV 25304 or by calling 1-888-680-7342.

NOTE 8: OTHER POST EMPLOYMENT BENEFITS

Plan Description - The Authority participates in the West Virginia Other Postemployment Benefits Plan (OPEB Plan) of the West Virginia Retiree Health Benefit Trust Fund, a cost-sharing multiple-employer defined benefit postemployment healthcare plan administered by the West Virginia Public Employees Insurance Agency (WVPEIA). The OPEB Plan provides retiree post-employment health care benefits for participating state and local government employers. The provisions of the Code of West Virginia, 1931, as amended (the Code), assigns the authority to establish and amend benefit provisions to the WVPEIA board of trustees. The WVPEIA issues a publicly available financial report that includes financial statements and required supplementary information for the OPEB Plan. That report may be obtained by writing to Public Employees Insurance Agency, 601 57th Street, S.E., Suite 2, Charleston, WV 25304-2345, or by calling 1-888-680-7342.

Funding Policy - The Code requires the OPEB Plan bill the participating employers 100% of the annual required contributions (ARC), an amount actuarially determined in accordance with the parameters of GASB Statement 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities (or funding excess) of the plan over a period not to exceed thirty years. State of West Virginia plan employers are billed per active health policy per month.

The ARC rate is \$901 per employee per month for the year ending June 30, 2010. The Authority's ARC was \$145,642, \$84,630, and \$94,056 and the Authority has paid premiums of \$26,871, \$26,301, and \$18,674, which represent 18.5%, 31.1%, and 19.9% of the ARC, respectively, for the years ending June 30, 2010, 2009, and 2008. At June 30, 2010, the liability related to OPEB costs was \$194,083.

**WEST VIRGINIA STATE RAIL AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
YEAR ENDED JUNE 30, 2010**

NOTE 9: RETIREMENT PLAN

Plan Description - The Authority contributes to the West Virginia Public Employees' Retirement System (PERS), a cost-sharing multiple-employer defined benefit pension plan administered by the West Virginia Consolidated Public Retirement Board. Chapter 5, Article 10 of the West Virginia State Code assigns the authority to establish and amend benefits provisions to the PERS Board of Trustees. Employees who retire at or after age 60 with five or more years of contributory service or who retire at or after age 55 and have completed 25 years of credited service are eligible for retirement benefits as established by State statute. Retirement benefits are payable monthly for life, in the form of a straight- line annuity equal to two percent of the employee's final average salary multiplied by the number of years of the employee's credited service at the time of retirement. PERS also provides deferred retirement, early retirement, death and disability benefits to plan members and beneficiaries. The West Virginia Consolidated Public Retirement Board issues a publicly available financial report that includes financial statements and required supplementary information for PERS. That report may be obtained by writing to the West Virginia Consolidated Public Retirement Board, 4101 MacCorkle Avenue, SE Charleston, West Virginia 25304-1636 or by calling (304) 558-3570.

Funding Policy - The PERS funding policy has been established by action of the State Legislature. State statute requires that plan participants contribute 4.5% of compensation. The current combined contribution rate is 15% of annual covered payroll, including the Authority's contribution of 10.5% which is established by PERS. The Authority's contributions to PERS for the years ended June 30, 2010, 2009, and 2008 were \$62,365, \$67,343 and \$66,589.

NOTE 10: COMMITMENTS & CONTINGENCIES

Periodic Audits – Under the terms of grants, periodic audits are required and certain costs may be questioned as not being appropriate expenditures under the terms of the grants. Such audits could lead to reimbursement to the grantor agencies. The Authority's management believes disallowances, if any, will not have a significant financial impact on the Authority's financial position.

Litigation – Periodically, there are various claims and legal proceedings against the Authority arising from the normal course of business. Currently there are no pending claims or legal proceedings against the Authority.

**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON
COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF
FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH
GOVERNMENT AUDITING STANDARDS**

To the Members of the
West Virginia State Rail Authority

We have audited the financial statements of the West Virginia State Rail Authority (the Authority) as of and for the year ended June 30, 2010, and have issued our report thereon dated October 21, 2010. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Authority's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Authority's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Authority's internal control over financial reporting.

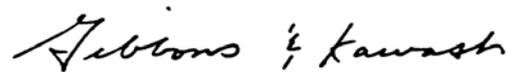
A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Authority's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of management, the Members of the Authority, the Members of the West Virginia Legislature, the West Virginia Department of Transportation, and the West Virginia Department of Administration and is not intended to be and should not be used by anyone other than these specified parties.

A handwritten signature in cursive script that reads "Gibson & Kawash".

October 21, 2010