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, 2009
AND
INDEPENDENT AUDITORS' REPORT

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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, 2009, and the related statements of revenues, expenses, and changes in fund net assets and cash flows for the year then ended. These basic 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, 2009, 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 January 4, 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 on compliance and the results of that testing, and not to provide an opinion on the 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.

The Management's Discussion and Analysis on pages 3 through 9 is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Gibbons & Kawash

January 4, 2010

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, 2009. 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 $1.2 million 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 $337 thousand during the year ended June 30, 2009 and operating revenues decreased approximately $312 thousand. This resulted in an operating loss decrease of approximately $25 thousand compared to the year ended June 30, 2008. Operating expenses were lower due to a decrease in fuel prices and rail car hire expenses in 2009. Salaries and benefits, car hire, diesel fuel, and liability and property insurance rates are the largest operating expenses. Freight revenue decreased because 410 less revenue cars were handled during the fiscal year ended June 30, 2009. This decrease was due to an overall downturn in the economy. All of our customers experienced a reduction. Our largest customer received 276 less carloads in FY09 than they had in FY08. Even with the decrease in revenue for FY09, by managing expenses, we were still able to reduce our operating loss.

- Non-operating revenues (expenses) were approximately ($78 thousand) in the year ended June 30, 2009 compared to non-operating revenues (expenses) of approximately $392 thousand in the year ended June 30, 2008. The change in total non-operating revenues (expenses) can be attributed to a decrease in interest income, a decrease in funds received for federal assistance for flood mitigation and an increase for loss on disposition of assets.

- The Authority completed approximately $2.4 million in capital improvements in the year ended June 30, 2009 including approximately $1.2 million for SBVR, approximately $1.12 million for the WVCR and approximately $50 thousand for upgrades to the MARC station parking lot at Duffields, WV.

OVERVIEW OF THE FINANCIAL STATEMENTS

This annual report includes management's discussion and analysis report, the independent auditor's report and the basic financial statements of the Authority. The financial statements also include notes that explain in more detail some of the 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 such questions as where did cash come from, what was cash used for, and what was 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 FundNet Assets for the years ended June 30, 2009 and 2008 are as follows:

Condensed Statement of Net Assets

	2009	2008
Current assets	$ 3,352,932	$ 3,529,251
Capital assets, net	37,352,374	36,631,787
Total assets	40,705,306	40,161,038
Current liabilities	133,968	942,640
Noncurrent liabilities	143,073	29,474
Total liabilities	277,041	972,114
Net assets		
Invested in capital assets net of related debt	37,352,374	36,631,787
Unrestricted	3,075,891	2,557,137
Total net assets	$ 40,428,265	$ 39,188,924

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

	2009	2008
Operating revenues		
Freight	$ 1,990,521	$ 2,312,592
Miscellaneous	162,564	152,707
Total operating revenues	2,153,085	2,465,299
Depreciation expense	1,547,468	1,429,698
Other operating expenses	2,434,105	2,889,372
Total operating expenses	3,981,573	4,319,070
Operating loss	(1,828,488)	(1,853,771)
Non-operating revenues (expenses)	(77,978)	391,696
Income (loss) before transfers	(1,906,466)	(1,462,075)
Transfers in	3,145,807	2,816,975
Change in net assets before cumulate effect of adoption of Accounting principles	1,239,341	1,354,900
Cumulative effect of adoption of accounting principles	-	132,913
Total net assets - beginning	39,188,924	37,701,111
Total net assets - ending	$ 40,428,265	$ 39,188,924

FINANCIAL ANALYSIS

- The Authority's budget for the fiscal year ended June 30, 2009 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 $2.8 million appropriation 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 MARC train stations in the eastern panhandle, and the general operation of the Authority. This appropriation is about 53% 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 $2.0 million was earned from the operations of the SBVR which was in line with the year ended June 30, 2009 budgeted projections. Miscellaneous revenues of approximately $163 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 decreased by 13% in the fiscal year ended June 30, 2009.

The following graphs provide a visual representation of the funding (revenue and other income sources) and expenditures (cash outlays) for the fiscal year ended June 30, 2009.

Chart 1 - Expenditures (cash outlays) Breakdown - Year ended June 30, 2009

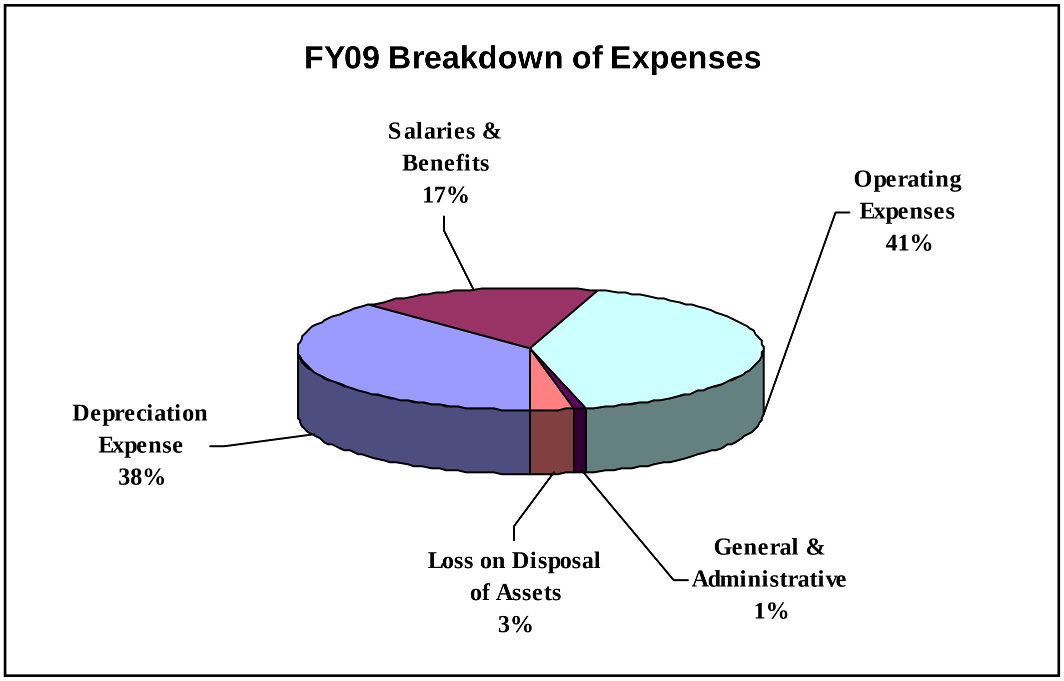
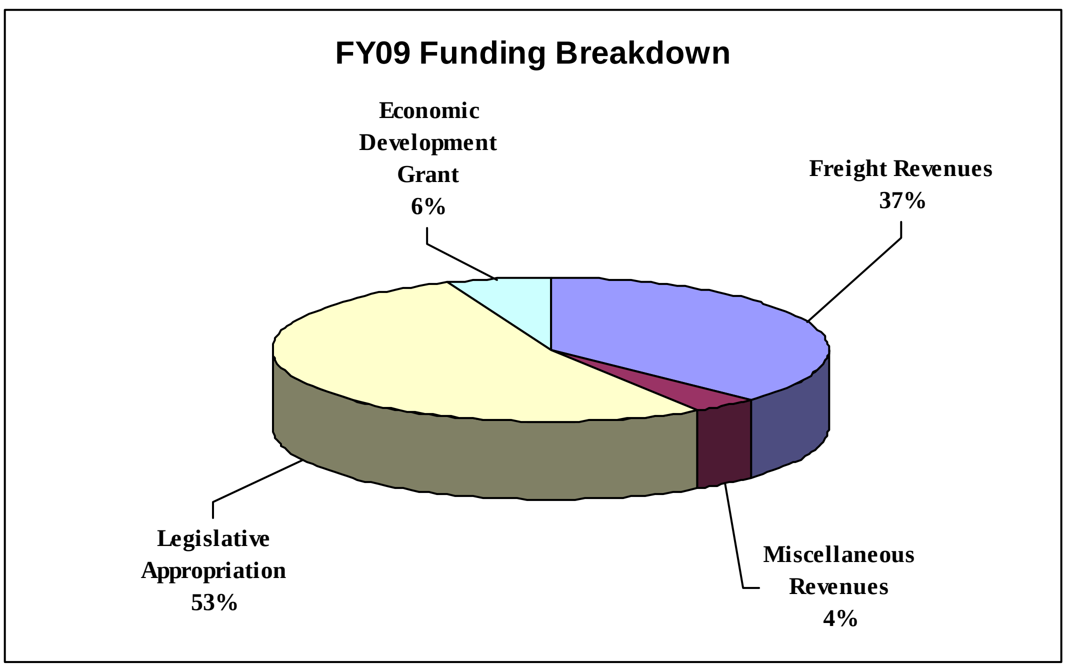


Chart 2 - Funding Breakdown - Year ended June 30, 2009



CAPITAL ASSETS

The Authority's net capital assets as of June 30, 2009 and 2008 amounted to $37.4 million and $36.6 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:

	2009	2008
Rail properties	$ 2,396,513	$ 1,951,151
Transportation and other equipment	-	286,931
Total	$ 2,396,513	$ 2,238,082

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 nine 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 the Pilgrim's Pride feed mill in Moorefield. Pilgrim's Pride is the largest employer in the Potomac Valley so 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, 2010 include continuing to upgrade and repair bridges and purchase two additional locomotives to help sustain our aging fleet.

The Authority's year ending June 30, 2010 budget includes approximately $2.7 million from the State of West Virginia and approximately $2.7 million from projected freight revenue. This funding will be used to complete the long-term rehabilitation projects started on the SBVR and also continue to maintain the WVCR. The capital improvement projects planned on the WVCR for the fiscal year ending June 30, 2010 include tie replacement, ballast spreading, surfacing, extending a side track and adding a crossover to assist in train operations and replacing numerous culverts. This railroad has completed ten 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 NET ASSETS
JUNE 30, 2009

ASSETS

Current assets		
Cash and cash equivalents	$	3,185,518
Trade receivables		88,408
Inventories		44,815
Due from other governmental entities		33,451
Other current assets		740
Total current assets		3,352,932
Noncurrent assets		
Capital assets		53,868,655
Accumulated depreciation		(16,516,281)
Total noncurrent assets		37,352,374
Total assets	$	40,705,306

LIABILITIES

Current liabilities		
Accounts payable	$	34,135
Accrued expenses		41,785
Compensated absences		52,381
Due to other governmental entities		2,303
Deferred revenue		3,364
Total current liabilities		133,968
Noncurrent liabilities		
Other post employement benefit liability		63,046
Deferred revenue		80,027
Total noncurrent liabilities		143,073
Total liabilities		277,041

NET ASSETS

Invested in capital assets, net of related debt		37,352,374
Unrestricted		3,075,891
Total net assets	$	40,428,265

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, 2009

Operating revenues	
Freight	$ 1,990,521
Miscellaneous	162,564
Total operating revenues	2,153,085
Depreciation expense	1,547,468
Other operating expenses	2,434,105
Total operating expenses	3,981,573
Operating income (loss)	(1,828,488)
Nonoperating revenues (expenses)	
Interest income	34,059
Federal railroad rehabilitation assistance	6,435
Payment on behalf of WVSRA	9,986
Gain (loss) on disposition of assets	(128,458)
Total nonoperating revenues (expenses)	(77,978)
Income (loss) before transfers	(1,906,466)
Transfers in	3,145,807
Change in net assets	1,239,341
Total net assets - beginning	39,188,924
Total net assets - ending	$ 40,428,265

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, 2009

Cash flows from operating activities	
Cash received from customers and government	$ 2,213,797
Cash paid to employees	(673,426)
Cash paid to suppliers and government	(2,531,904)
Net cash provided (used) by operating activities	(991,533)
Cash flows from noncapital financing activities	
Transfers in from State of West Virginia	3,840,450
Net cash provided (used) by noncapital financing activities	3,840,450
Cash flows from capital and related financing activities	
Purchase of capital assets	(2,396,513)
Net cash provided (used) by capital and related financing activities	(2,396,513)
Cash flows from investing activities	
Receipts of interest	34,059
Net cash provided (used) by investing activities	34,059
Increase (decrease) in cash and cash equivalents	486,463
Cash and cash equivalents, beginning of year including restricted cash	2,699,055
Cash and cash equivalents, end of year	$ 3,185,518
Reconciliation of operating income to net cash provided (used) by operating activities	
Operating loss	$ (1,828,488)
Adjustments to reconcile operating income to net cash provided by operating activities	
Depreciation	1,547,468
Amortization	
Expenses paid on behalf of entity	
Changes in operating assets and liabilities	
(Increase) decrease in trade receivables	(22,679)
(Increase) decrease in inventories	2,505
(Increase) decrease in other current assets	4,734
Increase (decrease) in operating accounts payable	(383,654)
Increase (decrease) in accrued expenses	(5,190)
Increase (decrease) in compensated absences	18,862
Increase (decrease) in due to other governmental entities	(408,482)
Increase (decrease) in deferred revenue	83,391
Net cash provided (used) by operating activities	$ (991,533)

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

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 Standards Board (FASB) statements and interpretations issued after November 30, 1989, unless

NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

the GASB specifically adopts such FASB statements and interpretations.

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 statements 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 by the West Virginia Board of Treasury Investments (BTI). These funds are transferred to the BTI, and the BTI is directed by the State Treasurer to invest the funds in specific external 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 fair value or amortized cost, which approximates fair value. Fair value is determined by a third-party pricing service based on asset portfolio pricing models and other sources, in accordance with GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments for External Investment Pools*. The BTI was established by the State Legislature and is subject to oversight by the State Legislature. Changes in fair value and 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 or on the first day of each month for the WV Short Term Bond Pool and, accordingly, are presented as cash and cash equivalents in the accompanying financial statements.

NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

The BTI maintains the Consolidated Fund investment fund, which consists of investment pools and participant-directed accounts, three of which the Authority may invest in. These pools have been structured as multiparticipant variable net asset funds to reduce risk and offer investment liquidity diversification to the Fund participants. Funds not required to meet immediate disbursement needs are invested for longer periods. A more detailed discussion of the BTI's investment operations pool 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.wvbti.com.

Permissible investments for all agencies include those guaranteed by the United States of America, its agencies and instrumentalities (U.S. Government obligations); corporate debt obligations, including commercial paper, which meet certain ratings; certain money market funds; repurchase agreements; reverse repurchase agreements; asset-backed securities; certificates of deposit; state and local government securities (SLGS); and other investments. Other investments consist primarily of investments in accordance with the Linked Deposit Program, a program using financial institutions in West Virginia to obtain certificates of deposit, loans approved by the legislature and any other program investments authorized by the legislature.

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, cost is valued 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.

NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

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.com.

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, 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 2009, 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. The liability for post-employment health care benefits is now provided for under the multiple employer cost-sharing plan sponsored by the State of West Virginia.

NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

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.

> **INVESTMENT IN CAPITAL ASSETS, NET OF RELATED DEBT** - 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.
>
> **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, 2009 there were no restricted net assets.
>
> **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.

TRANSFERS - Transfers represent legally authorized appropriations under West Virginia State Code by the West Virginia Legislature.

NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

NEWLY ADOPTED STATEMENTS ISSUED BY THE GASB — During 2009, the Authority adopted GASB Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*. The adoption of this statement had no impact on the financial statements at June 30, 2009.

During 2009, the GASB issued GASB Statement No. 55, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*, effective immediately. This statement identifies the sources of accounting principles and provides the framework for selecting the principles used in the preparation of financial statements of state and local governmental entities that are presented in conformity with generally accepted accounting principles. The Authority adopted GASB Statement No. 55 upon issuance.

During 2009, the GASB also issued GASB Statement No. 56, *Codification of Accounting and Financial Reporting Guidance Contained in the AICPA Statements on Auditing Standards*, effective immediately. This statement establishes accounting and financial reporting standards for related party transactions, subsequent events, and going concern considerations. The Authority adopted GASB Statement No. 56 upon issuance.

RECENT STATEMENTS ISSUED BY THE GASB – The GASB has issued Statement No. 51. *Accounting and Financial Reporting for Intangible Assets*, effective for fiscal years beginning after June 15, 2009. 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 Authority has not yet determined the effect that the adoption of GASB Statement No. 51 may have on the financial statements.

NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

The GASB has issued Statement No. 53 *Accounting and Financial Reporting for Derivative Instruments*, effective for periods beginning after June 15, 2009. 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 Authority has not yet determined the effect that the adoption of GASB Statement No. 53 may have on the financial statements.

NOTE 3: CASH AND CASH EQUIVALENTS

The composition of cash and cash equivalents were as follows at June 30:

	Amortized Cost	Estimated Fair Value
Cash on deposit with State Treasurer	$ 330	$ 330
Cash on deposit with State Treasurer invested in BTI (WV Money Market Pool)	3,185,188	3,185,188
	$ 3,185,518	$ 3,185,518

Amounts with the State Treasurer as of June 30, 2009 are comprised of the following investment pool, which are subject to the following BTI policies and limits.

NOTE 3: CASH AND CASH EQUIVALENTS (Continued)

West Virginia Board of Treasury Investments (BTI) WV 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 Consolidated Fund, 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. Investment policies have been established for each investment pool and account of the BTI's Consolidated Fund. Of the BTI's Consolidated Fund pools and accounts which the Authority may invest in, three are subject to credit risk: WV Money Market Pool, WV Government Money Market Pool, and WV Short Term Bond Pool.

WV Money Market

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, 2009, the WV 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. As this pool has been rated, specific information on the credit ratings of the underlying investments of the pool have not been provided for the year ended June 30, 2009.

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.

NOTE 3: CASH AND CASH EQUIVALENTS (Continued)

At June 30, 2009, the WV Money Market Pool investments had a total carrying value of $2,570,261,000, of which the Authority's ownership represents .12% of these amounts held by the BTI (in thousands).

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. All the BTI's Consolidated Fund pools and accounts are subject to interest rate risk.

The overall weighted average maturity of the investments of the WV 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 WV Money Market Pool:

	2009	
Security Type	**Carrying Value (In Thousands)**	**WAM (Days)**
Repurchase agreements	$ 212,010	1
U.S. Treasury bills	483,714	69
Commercial paper	592,479	32
Certificates of deposit	128,402	56
U.S. agency discount notes	635,602	57
Corporate bonds and notes	73,812	38
U.S. agency bonds/notes	294,019	70
Money market funds	150,223	1
	$ 2,570,261	47

NOTE 3: CASH AND CASH EQUIVALENTS (Continued)

Other Investment Risks

Other investment risks include concentration of credit risk, custodial credit risk, and foreign currency risk. None of the BTI's Consolidated Fund's investment pools or accounts is exposed to these risks as described below.

Concentration of credit risk is the risk of loss attributed to the magnitude of the BTI's Consolidated Fund pool or account's investment in a single corporate issuer. The BTI investment policy prohibits those pools and accounts permitted 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.

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or a deposit. None of the BTI's Consolidated Fund's investment pools or accounts holds 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. None of the above pools 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, 2009 is summarized below:

	June 30, 2008 Balance	Additions	Deletions	June 30, 2009 Balance
Capital assets				
Land	$ 4,835,588	$ -	$ -	$ 4,835,588
Rail Properties	44,929,007	2,396,513	(242,479)	47,083,041
Transportation and other equipment	1,498,656	-	-	1,498,656
Office building and equipment	451,370	-	-	451,370
Total capital assets	$ 51,714,621	$ 2,396,513	$ (242,479)	$53,868,655
Accumulated Depreciation				
Rail Properties	$ 13,899,353	$ 1,407,671	$ (114,021)	$15,193,003
Transportation and other equipment	858,973	128,985	-	987,958
Office building and equipment	324,508	10,812	-	335,320
Total accumulated depreciation	$ 15,082,834	$ 1,547,468	$ (114,021)	$16,516,281

NOTE 5: DUE TO/FROM OTHER GOVERNMENTAL ENTITIES AND TRANSFERS

At June 30, 2009, the Authority had amounts due from the State of West Virginia of $33,451. The Office of the Secretary of Administration, Finance Division transferred from FIMS fund 0506-099 $2,617,287 and FIMS fund 0506-913 $203,520 to the Authority for the year ended June 30, 2009. The Authority received $325,000 in grant monies from the West Virginia Department of Commerce's Development Office for the year ended June 30, 2009.

NOTE 6: SIGNIFICANT CUSTOMERS AND FUNDING SOURCES

During the year ended June 30, 2009, approximately 92.4% of the Authority's freight traffic was attributable to a single customer. In addition, during the year ended June 30, 2009 the Authority received transfers of $2,820,807 in appropriated funds and a $325,000 grant from the State of West Virginia. 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. In exchange for payment of premiums to PEIA and the third-party insurer, the Authority has transferred its risks related to health, life, prescription drug coverage, and job related injuries. 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.

Workers' Compensation

West Virginia had a single private insurance company, Brickstreet Insurance, which provided workers' compensation coverage to all employers in the state. Other private insurance companies began to offer coverage to private-sector employers on July 1, 2008 and will be allowed to begin offering coverage to government employers beginning July 1, 2012. Nearly every employer in the State, who has a payroll, must have coverage.

In exchange for premiums, the Authority transfers its risk of loss related to employee injuries to Brickstreet.

NOTE 8: OTHER POST EMPLOYMENT BENEFITS

With the adoption of GASB Statement No. 45 for the year ended June 30, 2008, Other Post Employment Benefits (OPEB) costs are accrued based on invoices received from PEIA which uses actuarial determined amounts. At June 30, 2009 and 2008, the noncurrent liability related to OPEB costs was $63,046 and $29,474. For the year ended June 30, 2009, the total of OPEB expense incurred and the amount of OPEB expense that related to retirees was $79,458 and $0. As of the year ended June 30, 2009, there were no retirees receiving these benefits.

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, 2009, 2008, and 2007 were $67,343, $66,589 and $66,393.

NOTE 10: COMMITMENTS & CONTINGENCIES

Periodic Audits – Under the terms of federal 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 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, 2009, and have issued our report thereon dated January 4, 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.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A control deficiency 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 misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the Authority's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the Authority's financial statements that is more than inconsequential will not be prevented or detected by the Authority's internal control. We consider the deficiency described in the accompanying schedule of findings and responses as item 2009-1 to be a significant deficiency in internal control over financial reporting.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in a more than remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the Authority's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, the significant deficiency described above is considered to be material weakness.

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*.

The Authority's response to the finding identified in our audit is described in the accompanying schedule of findings and responses. We did not audit the Authority's response and, accordingly, we express no opinion on it.

This report is intended solely for the information 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.

Gibbons & Kawash

January 4, 2010

2009-1 FINANCIAL REPORTING - CAPITAL ASSETS

Criteria:
Expenditures for capital assets are required by accounting principles generally accepted in the United States of America to be capitalized and depreciated over their estimated useful lives in the Authority's financial statements.

Condition:
The Authority's existing capitalization policy for capital assets is not being consistently applied in a manner that identifies expenditures that should be capitalized in accordance with accounting principles generally accepted in the United States of America.

Cause:
Management has not established appropriate supervisory review and approval procedures to ensure that expenditures are capitalized in accordance with the existing capitalization policy in the year that the expenditure is incurred.

Context:
We noted $381,738 of capital expenditures, incurred in the prior year, that were improperly capitalized during the current fiscal year. The Authority's expenses reported in its financial statements were $3,981,573 for the year ended June 30, 2009.

Effect:
Net assets and capital assets in the unaudited financial statements as of the beginning of the fiscal year ended June 30, 2009 were understated by $381,738, and the current fiscal year's expenses were understated by the same amount.

Recommendation:
Management should ensure that its established capitalization policy for capital assets is properly applied and all expenditures that meet this policy are capitalized in the financial statements in the year that the expenditure is incurred. The Authority should consider changes in supervisory review procedures and account reconciliation procedures to ensure that capital related items are appropriately identified and capitalized.

Views of Responsible Officials:

The State Rail Authority agrees with the finding. We will ensure the capitalization policy is adhered to properly in the future. The review of capital items will be thoroughly monitored and checked by management.