MASSACHUSETTS BAY TRANSPORTATION AUTHORITY
(A Component Unit of the Commonwealth of Massachusetts)

Financial Statements and Required Supplementary Information

June 30, 2006 and 2005

(With Independent Auditors' Report Thereon)

MASSACHUSETTS BAY TRANSPORTATION AUTHORITY
(A Component Unit of the Commonwealth of Massachusetts)

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Independent Auditors' Report

The Board of Directors of the
Massachusetts Bay Transportation Authority:

We have audited the accompanying statements of net assets of the Massachusetts Bay Transportation Authority (the Authority or MBTA), a component unit of the Commonwealth of Massachusetts, as of June 30, 2006 and 2005, and the related statements of revenue, expenses, and changes in net assets and cash flows for the years 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 audits.

We conducted our audits 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. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Authority's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Authority as of June 30, 2006 and 2005, and the results of its operations and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

The Management's Discussion and Analysis on pages 2 through 10 and the historical pension information on pages 47 and 48 are not required parts of the financial statements but are supplementary information required by U.S. generally accepted accounting principles. 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.

In accordance with *Government Auditing Standards,* we have also issued a report dated October 24, 2006 on our consideration of the Authority's internal control over financial reporting and on our tests of its compliance with certain provisions of laws and regulations, contracts, 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 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 audits.

KPMG LLP

October 24, 2006

Introduction

The following discussion and analysis of the financial performance and activity of the Massachusetts Bay Transportation Authority (the Authority) is intended to provide an introduction to and an overview and analysis of the basic financial statements of the Authority for the years ended June 30, 2006 (FY06) and June 30, 2005 (FY05). The management of the Authority has prepared this discussion, and it should be read in conjunction with the financial statements and the notes thereto, which follow this section.

The Authority was originally created in 1964 pursuant to Chapter 161A of Massachusetts General Laws, as in effect prior to July 1, 2000 (the Prior Act), as a body politic and corporate and a political subdivision of the Commonwealth to finance and operate mass transportation facilities within (and to a certain extent, outside) its territory. The territorial area of the Authority consisted of 78 cities and towns in the greater Boston metropolitan area. Under the Prior Act, the Commonwealth provided various forms of financial assistance to offset the Authority's operating deficit. In order to finance its capital program, the Authority was authorized to issue indebtedness secured by its general obligation. If the Authority lacked funds to pay such indebtedness, the Commonwealth was obligated to pay such amount, to which obligation the Commonwealth's full faith and credit was pledged.

As part of its Fiscal 2000 annual appropriations act, Chapter 127 of the Acts of 1999 of the Commonwealth, as amended (Chapter 127 or the Forward Funding Legislation), the Commonwealth repealed and restated the Prior Act effective July 1, 2000. The Prior Act as restated by Section 151 of Chapter 127, together with Section 35T of Chapter 10 of Massachusetts General Laws, also enacted as part of Chapter 127, as amended, are collectively referred to herein as the "Enabling Act".

Commencing July 1, 2000, under the Enabling Act, the Authority receives a dedicated revenue stream consisting of the Assessments and the Dedicated Sales Tax (collectively, the Dedicated Revenues). The Dedicated Sales Tax is equal to the greater of the base revenue amount (as defined in the Enabling Act) and the amount raised by a 1% statewide sales tax, which equals 20% of the existing statewide 5% sales tax to be funded from existing sales tax receipts, subject to upward adjustment under certain circumstances set forth in the Enabling Act.

The Enabling Act expanded the territory of the Authority to 175 cities and towns, but aggregate annual Assessments payable by such cities and towns are reduced in five equal amounts from approximately $144 million in Fiscal Year 2001 to approximately $136 million in Fiscal Year 2006. After 2006, aggregate Assessments will be adjusted annually for inflation but will not be permitted to increase by more than 2.5% per year. Under the Enabling Act, the Authority is required to meet all of its operating and capital expenditures from Dedicated Revenues, federal assistance and revenues generated from operation of the Authority's system, including without limitation fare revenues and nonfare revenues (e.g. parking and advertising revenues). However, under the Enabling Act, the Authority's failure to provide transportation services at current levels would not affect the Commonwealth's or the assessed cities' and towns' obligation or ability to provide the Dedicated Revenues.

The MBTA is the oldest and fifth largest transit system in the country, operating subway, trackless trolley, trolley, bus and commuter rail service throughout eastern Massachusetts. The Authority is responsible for an estimated 1.2 million passenger trips every business day and operates over 38 miles of rapid transit heavy rail routes. Service is also provided by trackless trolleys and light rail vehicles on 36 miles of additional routes. The Authority owns more than 1,000 buses which cover routes totaling 740 miles. The MBTA's commuter rail service operates over 460 units of passenger rail equipment and locomotives providing service between Boston and 126 outlying rail stations. In addition, the MBTA provides a broad range of other passenger services including commuter boats, "The Ride" servicing the elderly and the disabled, and express buses.

Under the Enabling Act, the Authority is required to meet all of its expenditures, both operating and capital, from a combination of Dedicated Revenues, federal assistance and revenues generated from operation of the Authority's transportation system.

Financial Statements

Our financial statements are prepared using proprietary fund (enterprise fund) accounting that uses the same basis of accounting as private-sector business enterprises. The Authority is operated under one enterprise fund. Under this method of accounting, an economic resources measurement focus and an accrual basis of accounting is used.

Revenue is recorded when earned and expenses are recorded when incurred. The financial statements include statements of net assets, statements of revenues, expenses and changes in net assets, and statements of cash flows. These are followed by notes to the financial statements. In addition to the financial statements, this report also contains required supplementary information pertaining to the retirement plans of the Authority.

- The statements of net assets present information on the Authority's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the Authority is improving or deteriorating.
- The statements of revenue, expenses and changes in net assets report the operating revenues and expenses and nonoperating revenues and expenses of the Authority for each fiscal year with the difference – the increase in net assets – being combined with any capital grants to determine the net change in assets for the fiscal year. That change combined with the net assets from the end of the previous year equals the net assets at the end of the fiscal year.
- The statements of cash flows report cash and cash equivalent activities for each fiscal year resulting from operating activities, capital and related financing activities, noncapital and related financing activities and investing activities. The net result of these activities added to the beginning of the year balance of cash and cash equivalents total to the cash and cash equivalent balance at the end of the fiscal year.

(Continued)

(Dollars in thousands)

Condensed Financial Information

Condensed financial information as of and for the years ended June 30, 2006, 2005, and 2004 are as follows:

	June 30 2006	2005	2004
Current and other assets	$ 1,881,820	1,313,123	1,344,105
Capital assets, net	7,635,143	7,392,655	7,115,024
Total assets	9,516,963	8,705,778	8,459,129
Current liabilities	508,071	491,206	443,871
Long-term liabilities	5,833,432	5,015,324	4,821,691
Total liabilities	6,341,503	5,506,530	5,265,562
Net assets:			
Invested in capital assets, net of related debt	3,170,007	3,130,920	3,081,213
Restricted	26,953	36,092	31,651
Unrestricted	(21,500)	32,236	80,703
Total net assets	$ 3,175,460	3,199,248	3,193,567
Operating revenue:			
Revenue from transportation	$ 333,096	319,271	295,496
Other	46,864	52,282	49,440
Total operating revenues	379,960	371,553	344,936
Operating expenses:			
Transportation services	534,682	506,503	481,635
Other operating expenses	432,217	416,552	406,678
Total operating expenses, excluding depreciation	966,899	923,055	888,313
Depreciation and amortization	292,633	269,814	249,087
Total operating expenses, including depreciation	1,259,532	1,192,869	1,137,400
Operating loss	(879,572)	(821,316)	(792,464)
Net nonoperating revenue	693,907	644,615	665,739
Loss before capital grants	(185,665)	(176,701)	(126,725)
Capital grants and contributions	161,877	182,382	232,618
Increase (decrease) in net assets	(23,788)	5,681	105,893
Beginning of year net assets	3,199,248	3,193,567	3,087,674
End of year net assets	$ 3,175,460	3,199,248	3,193,567

(Continued)

The information contained in the condensed financial information table is used as the basis for the following discussion regarding the Authority’s financial activities for the fiscal years ended June 30, 2006, 2005, and 2004.

Financial Highlights for the years ended June 30, 2006 and 2005

- The Authority ended the years June 30, 2006 and 2005 with a net asset balance of $3,175,460 and $3,199,248 of which $3,170,007 and $3,130,920 represented the amount invested in capital assets, net of related debt, and $(21,500) and $32,236 was unrestricted, respectively. The net asset balance decreased $23,788 and increased $5,681 in the years ended June 30, 2006 and 2005, respectively. The decrease in net assets is attributable to increased pension and healthcare benefit costs for employees, increased fuel costs for transportation services and only receiving sales tax receipts equal to the base revenue amount.
- The Authority incurred an expected operating loss for the years ended June 30, 2006 and 2005 of $879,572 and $821,316, respectively. The operating losses were offset in accordance with the Commonwealth of Massachusetts Forward Funding Legislation (Chapter 127 of the Acts of 1999 of the Commonwealth or Enabling Act). The legislation allows the Authority to receive a dedicated revenue stream consisting of the assessments on the communities in the Authority’s service area and a Dedicated Sales Tax. For years ended June 30, 2006 and 2005 the Authority recognized $712,586 and $704,809 of sales tax revenues from the Commonwealth of Massachusetts. This amount was the guaranteed full year Base Revenue Amount. Local assessments on cities and towns within the Authority’s service area accounted for $136,027 and $137,732 in nonoperating revenue in 2006 and 2005, respectively. Adding to the operating loss was interest expense, net of investment and other income of $154,706 and $197,926, respectively, in 2006 and 2005.
- The Authority has taken steps to minimize interest expense by reducing the amount of high interest rate debt by refunding outstanding bonds and paying off debt as funds become available.
- The Authority ended the years June 30, 2006 and 2005 with cash and investments of $1,127,813 and $734,879 respectively. However, only $114,559 and $99,994 of this amount at June 30, 2006 and 2005, respectively, is available for operations as the bulk of these assets are restricted for specific purposes and unavailable for the Authority’s general use.
- The statements of cash flows identify the sources and uses of cash for each fiscal year. Cash and cash equivalents increased by $36,645 in fiscal 2006 and decreased by $39,413 in fiscal 2005. The increase in fiscal year 2006 is due to increased transportation revenues. The increase was offset by an increase in health insurance, pension and fuel costs.

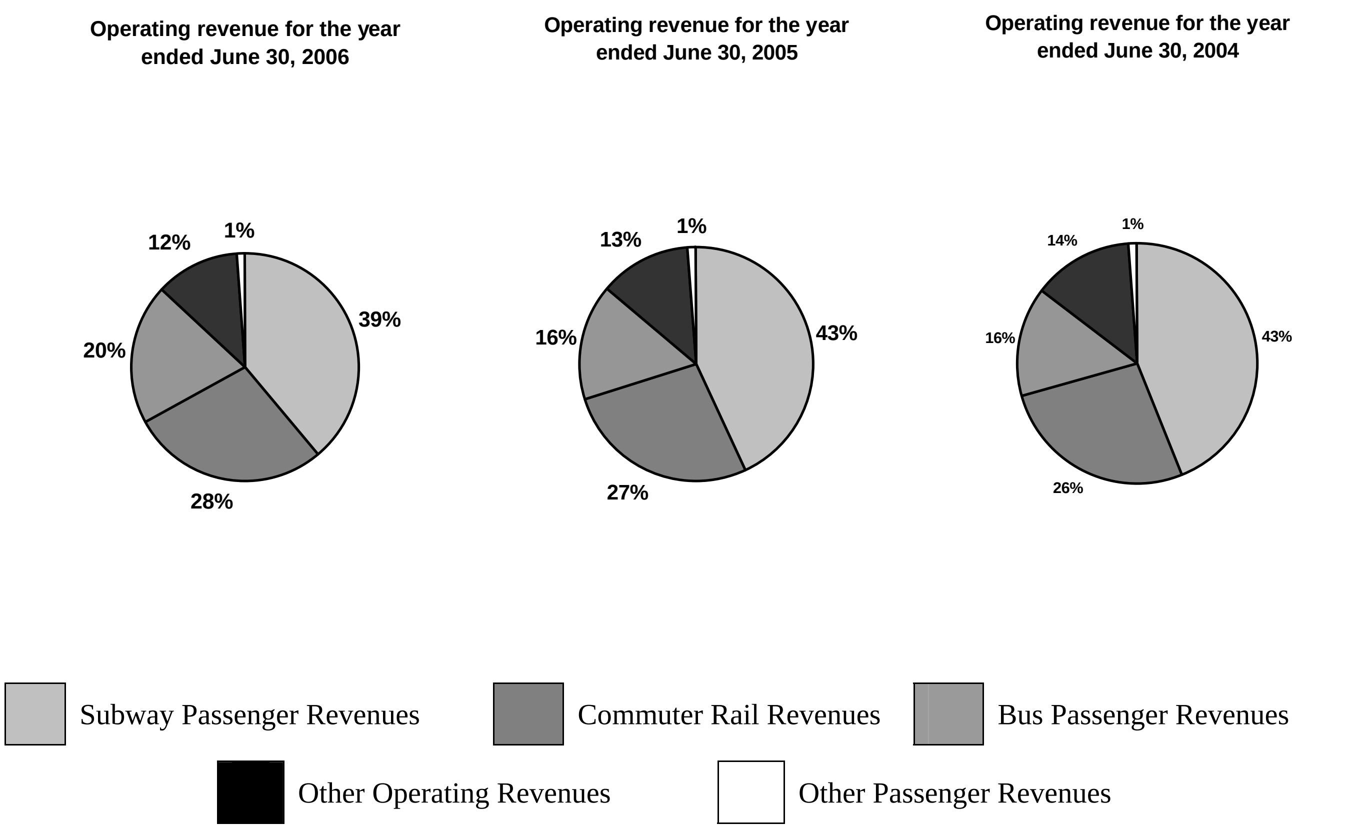
(Continued)

Financial Highlights for the years ended June 30, 2005 and June 30, 2004

- The Authority ended the years June 30, 2005 and 2004 with a net asset balance of $3,199,248 and $3,193,567 of which $3,130,920 and $3,081,213 represented the amount invested in capital assets, net of related debt, and $32,236 and $80,703 was unrestricted, respectively. The net asset balance increased $5,681 and $105,893 in the years ended 2005 and 2004, respectively. The increase in net assets is attributable to increased transportation revenues and increased dedicated sales tax revenue.
- Despite the increase in net assets, the Authority incurred an expected operating loss for the years ended June 30, 2005 and 2004 of $821,316 and $792,464, respectively. The operating losses were offset in accordance with the Commonwealth of Massachusetts Forward Funding Legislation (Chapter 127 of the Acts of 1999 of the Commonwealth or Enabling Act). The legislation allows the Authority to receive a dedicated revenue stream consisting of the assessments on the communities in the Authority's service area and a Dedicated Sales Tax. For years ended June 30, 2005 and 2004 the Authority recognized $704,809 and $684,280 of sales tax revenues from the Commonwealth of Massachusetts. This amount was the guaranteed full year Base Revenue Amount. Local assessments on cities and towns within the Authority's service area accounted for $137,732 and $139,437 in nonoperating revenue in 2005 and 2004, respectively. Adding to the operating loss was interest expense, net of investment and other income of $197,926 and $157,978, respectively, in 2005 and 2004.
- The Authority has taken steps to minimize interest expense by reducing the amount of high interest rate debt by refunding outstanding bonds and paying off debt as funds become available.
- The Authority ended the years June 30, 2005 and 2004 with cash and investments of $734,879 and $779,557 respectively. However, only $99,994 and $146,423 of this amount at June 30, 2005 and 2004, respectively, is available for operations as the bulk of these assets are restricted for specific purposes and unavailable for the Authority's general use.
- The statements of cash flows identify the sources and uses of cash for each fiscal year. Cash and cash equivalents decreased by $39,413 in fiscal 2005 and increased by $61,886 in fiscal 2004. The decrease in fiscal year 2005 is due to the increased cash requirements for operations and increased utilization of cash for capital improvements.

Revenue

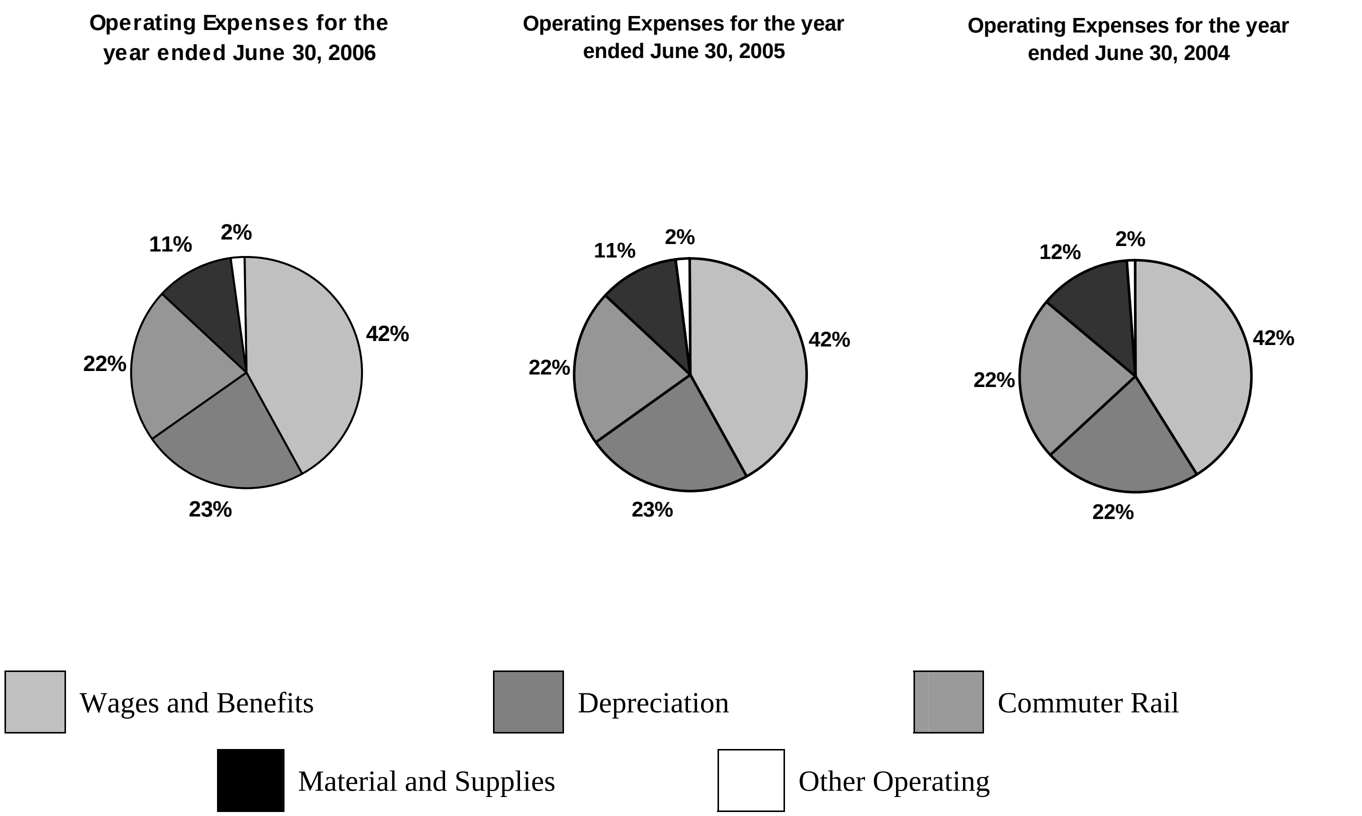
The following charts show the major sources of operating revenue for the years ended June 30, 2006, 2005, and 2004:



As in previous years, the passenger revenues make up over 85% of the total operating revenues. The Authority continues to work on increasing ridership through new equipment purchases, station upgrades and system expansion and will continue to pursue its policy of maximizing nonfare revenue opportunities.

Expenses

The following charts show the major sources of operating expenses for the years ended June 30, 2006, 2005, and 2004:



As in previous years, wages and benefits make up the largest portion of operating expenses. This is common in the public transportation industry as the provision of service is extremely labor intensive. Due to the significant investments the Authority has in capital assets, depreciation continues to be a large operating expense. Unlike the other expenses listed, depreciation is not a cash expense. The Authority has and continues to pursue ways to reduce costs without impacting service. The Authority has taken such measures as bidding and contracting with a new commuter rail provider and utility companies to obtain competitive pricing.

(Dollars in thousands)

Capital Assets

The Authority's capital assets as of June 30, 2006, 2005, and 2004 amounted to $7,635,143 and $7,392,655, and $7,115,024 (net of accumulated depreciation) respectively. This investment in capital assets includes land, construction work in progress, ways and structures and buildings and equipment.

Net capital asset additions (reductions) included the following for the years ended June 30:

	2006	2005	2004
Land	$ 4,135	13,264	37,222
Construction work in progress	(2,007)	(413,686)	243,503
Ways and structures	362,267	738,946	185,133
Buildings and equipment	97,720	181,257	180,972
	$ 462,115	519,781	646,830

The Authority primarily acquires its assets with the proceeds from federal capital grants and revenue bonds. Station improvements, new equipment purchases and system expansion are all part of the Authority's capital investment program. Commitments on approved capital asset construction projects were $286,132 and $319,199, and $368,466 for the years ended June 30, 2006, 2005, and 2004, respectively. Commitments to purchase new transportation equipment were $328,268 and $390,927, and $452,422 as of June 30, 2006, 2005, and 2004, respectively.

Debt

Bonds and notes outstanding for the following years:

	2006	2005	2004
General Transportation System bonds	$ 1,626,960	1,770,835	2,278,390
Revenue bonds	3,414,975	2,665,505	2,200,865
Boston Metropolitan District bonds	19,045	21,000	23,250
Grant Anticipation notes	81,665	81,665	—
Bond Anticipation notes	—	92,800	—
	$ 5,142,645	4,631,805	4,502,505

The total amount for these categories of debt increased by $510,840 and $129,300, and $315,575 for the years ended June 30, 2006, 2005, and 2004, respectively.

The Authority issued $1,018,865 in bonds during the 2006 fiscal year of which, $685,535 were new money bonds and $333,330 were issued to refund higher interest rate debt. The $685,535 in new money bonds were used to finance vehicle replacements, commuter rail expansion, new automated fare collection equipment and other systemwide improvements and to pay off $112,500 in outstanding commercial paper.

The Authority also sold $224,890 in Senior Sales Tax Bonds that will be issued in December 2006. These bonds will refund $5,500 of the 1997 Series B General Transportation System Bonds and $224,330 of the 1997 Series C General Transportation System Bonds that were pledged under a forward swap that would have commenced in December 2006. The issuance of the $224,890 in Senior Sales Tax bonds effectively terminates the forward swap and the Authority will receive a swap termination payment of $5,675, when the bonds are issued in December 2006.

The Authority issued $1,100,665 in bonds during the 2005 fiscal year. Of the bonds issued, $1,029,625 were used to refund higher interest rate debt. The remainder is being used to finance vehicle replacements and payoff outstanding commercial paper. The Authority issued $1,195,725 in bonds during the 2004 fiscal year. Of the bonds issued, $791,510 were used to refund higher-rate debt, and the remaining $404,215 is being used to finance systemwide improvements, vehicle replacements and a commuter rail expansion project. The Authority issued $727,675 in bonds during the 2003 fiscal year. Of the bonds issued, $303,595 were used to refund higher rate debt with the remainder financing systemwide improvements and a Vehicle Replacement Program. The Authority has also entered into various agreements to help hedge against interest rate changes on certain outstanding debt. These agreements help the Authority better manage the total cost of borrowing and allow for better budgeting of future cash flows. The Authority's Assessment Bonds have a rating of AAA Standard & Poor's and Aa1 by Moody's Investor Services. The Authority's Sales Tax Bonds have a rating of AAA by Standard & Poor's and Aa2 by Moody's Investor Services.

Requests for Information

This financial report is intended to provide an overview of the finances of the Authority for those with an interest in this organization. Questions concerning any information within this report may be directed to the Deputy General Manager and Chief Financial Officer of the Authority.

MASSACHUSETTS BAY TRANSPORTATION AUTHORITY
(A Component Unit of the Commonwealth of Massachusetts)

Statements of Net Assets

June 30, 2006 and 2005

(Dollars in thousands)

Assets		**2006**	**2005**
Current assets:			
Unrestricted cash and temporary cash investments (note 3)	$	114,559	99,994
Restricted cash and temporary cash investments (note 3):			
Bond construction accounts		47,812	11,422
Stabilization accounts		17,420	16,852
Other accounts		64,785	79,663
Lease accounts		19,153	12,768
Accounts receivable:			
Commonwealth of Massachusetts		99,003	97,930
Federal grants		9,533	19,240
Other trade, net		33,545	29,812
Materials and supplies		49,918	42,726
Prepaid expenses		6,208	3,681
Total current assets		461,936	414,088
Restricted cash and investments accounts (note 3):			
Bond construction accounts		289,164	65,300
Lease deposits		208,896	182,242
Bond reserve accounts		385,177	279,406
Total restricted cash and investments accounts		883,237	526,948
Lease accounts		508,476	348,666
Capital assets, at cost (notes 8, 9, and 11):			
Transportation property, being depreciated		9,969,461	9,509,474
Transportation property, not being depreciated		1,170,570	1,168,442
Less accumulated depreciation		(3,504,888)	(3,285,261)
Capital assets, net		7,635,143	7,392,655
Other assets:			
Deferred bond issue costs		28,171	23,421
Total other assets		28,171	23,421
Total non current assets		9,055,027	8,291,690
Total assets	$	9,516,963	8,705,778

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MASSACHUSETTS BAY TRANSPORTATION AUTHORITY
(A Component Unit of the Commonwealth of Massachusetts)

Statements of Net Assets

June 30, 2006 and 2005

(Dollars in thousands)

Liabilities		**2006**	**2005**
Current liabilities:			
Current maturities of bonds and notes payable (note 5)	$	149,415	162,695
Current capital lease and other current obligations (note 8)		21,333	15,490
Accounts payable		131,649	135,284
Accrued liabilities:			
Payroll and vacation		28,547	27,318
Interest		109,856	92,187
Injuries and damage claims, worker’s compensation claims, and other (note 10)		67,271	58,232
Total current liabilities		508,071	491,206
Long-term liabilities, less current maturities:			
Bonds payable, net (note 5)		5,009,268	4,415,847
Obligations under capital leases (note 8)		724,425	533,093
Accrued liabilities (note 10)		40,669	37,696
Pension liability (note 7)		20,429	9,252
Deferred revenue (note 6)		38,641	19,436
Total long-term liabilities		5,833,432	5,015,324
Total liabilities		6,341,503	5,506,530
Net Assets			
Invested in capital assets, net of related debt		3,170,007	3,130,920
Restricted		26,953	36,092
Unrestricted		(21,500)	32,236
Commitments and contingencies (notes 10 and 11)			
Total net assets	$	3,175,460	3,199,248

See accompanying notes to financial statements.

MASSACHUSETTS BAY TRANSPORTATION AUTHORITY
(A Component Unit of the Commonwealth of Massachusetts)

Statements of Revenue, Expenses, and Changes in Net Assets

Years ended June 30, 2006 and 2005

(Dollars in thousands)

		2006	2005
Operating revenue:			
Revenue from transportation	$	333,096	319,271
Other		46,864	52,282
		379,960	371,553
Operating expenses:			
Wages and related employee benefits:			
Wages		347,846	339,760
Medical and dental insurance		112,790	94,035
Pensions		48,387	38,743
Social security taxes		31,264	30,335
Worker's compensation		16,238	20,971
Other		1,963	2,112
Capitalized costs		(23,806)	(19,453)
		534,682	506,503
Other operating expenses:			
Depreciation and amortization		292,633	269,814
Materials, supplies, and services		149,456	136,897
Injuries and damages		14,192	14,673
Commuter railroad and local subsidy expenses (note 4)		266,547	260,448
Other		2,022	4,534
		724,850	686,366
Total operating expenses		1,259,532	1,192,869
Operating loss		(879,572)	(821,316)
Nonoperating revenue (expense):			
Dedicated sales tax revenue		712,586	704,809
Dedicated local assessments		136,027	137,732
Other income		32,458	11,888
Interest income		11,832	5,999
Interest expense		(198,996)	(215,813)
Nonoperating revenue, net		693,907	644,615
Loss before capital grants		(185,665)	(176,701)
Capital grants and contributions		161,877	182,382
(Decrease) increase in net assets		(23,788)	5,681
Beginning of year net assets		3,199,248	3,193,567
End of year net assets	$	3,175,460	3,199,248

See accompanying notes to financial statements.

MASSACHUSETTS BAY TRANSPORTATION AUTHORITY
(A Component Unit of the Commonwealth of Massachusetts)

Statements of Cash Flows

Years ended June 30, 2006 and 2005

(Dollars in thousands)

		2006	2005
Cash flows from operating activities:			
Receipts from transit customers	$	327,835	318,980
Receipts from other operations		99,495	49,330
Payments to suppliers and vendors		(572,882)	(535,440)
Payments to employees		(430,540)	(378,938)
Net cash used for operating activities		(576,092)	(546,068)
Cash flows from capital and related financing activities:			
Cash (used for) provided by:			
Additions to transportation property		(456,588)	(512,694)
Interest paid		(246,876)	(235,733)
Decrease in deferred credits/charges		11,928	(2,482)
Payments on long-term debt		(508,025)	(1,145,830)
Proceeds from bond and note issuances		1,018,865	1,275,130
Payments to bond construction and reserve accounts		(328,996)	—
Proceeds from bond premiums		67,439	66,981
Capital leases		(18,270)	(3,052)
Capital grants		171,583	182,385
Other		16,183	8,978
Net cash used for capital and related financing activities		(272,757)	(366,317)
Cash flows from noncapital and related financing activities:			
Sales tax and local assessment		847,539	842,779
Reimbursable payments		11,932	15,921
Other		13,429	(3,615)
Net cash provided by noncapital and related financing activities		872,900	855,085
Cash flows from investing activities:			
Interest and other income		12,594	17,887
Net cash provided from investing activities		12,594	17,887
Change in cash, temporary cash investments, restricted, and other special accounts		36,645	(39,413)
Cash, restricted cash and temporary cash investments, beginning of year		207,931	247,344
Cash, restricted cash and temporary cash investments, end of year	$	244,576	207,931
Adjustments to reconcile operating loss to net cash used by operating activities:			
Operating loss	$	(879,572)	(821,316)
Charges not requiring current expenditure of cash:			
Depreciation and amortization		292,633	269,814
Changes in all other working capital accounts except cash, temporary cash investments, and short-term debt		10,847	5,434
Net cash used for operating activities	$	(576,092)	(546,068)

See accompanying notes to financial statements.

(1) The Reporting Entity

The Massachusetts Bay Transportation Authority (the Authority) was originally created in 1964 and is body politic and corporate and a political subdivision of the Commonwealth of Massachusetts (the Commonwealth).

The Authority is managed by a board of nine directors. The Secretary of the Executive Office of Transportation of the Commonwealth is the Chairman. The other eight directors are appointed by the Governor of the Commonwealth. All appointments to the Board became effective July 1, 2000. Since this time, six have been reappointed with two new appointments. The Board has the power to appoint and employ a General Manager and other officers. The Advisory Board, consisting of a representative from each of the cities and towns paying Assessments, has the power to approve the Authority's long-term capital program and annual operating budget.

In accordance with the requirements of Statement No. 14, *The Financial Reporting Entity,* of the Governmental Accounting Standards Board (GASB), the financial statements must present the Authority (the primary government) and its component units. Pursuant to this criterion, no component units were identified for inclusion in the accompanying financial statements. Additionally, the accompanying financial statements are incorporated into the financial statements of the Commonwealth as the Authority is a component unit of the Commonwealth.

(2) Summary of Significant Accounting Policies

(a) Funding of Operation

As part of the Commonwealth's Forward Funding Legislation (Chapter 127 of the Acts of 1999 of the Commonwealth or Enabling Act), the Commonwealth's prior funding mechanism was repealed and restated. Effective July 1, 2000, the new legislation allows the Authority to receive a dedicated revenue stream consisting of the assessments on the communities in the Authority's service area (the Assessments) and certain Dedicated Sales Tax. Additionally, the Authority's service territory expanded from 78 to 175 cities and towns. The Authority also funds operations through charges for providing transportation services.

(b) Financial Reporting

The Authority applies U.S. generally accepted accounting principles as prescribed by GASB. The accompanying financial statements have been prepared using the economic resources measurement focus and the accrual basis of accounting and reflect transactions on behalf of the Authority, the reporting entity. The Authority accounts for its operations as an enterprise fund. Operating revenues and expenses result from providing transportation services to member communities. All other revenues and expenses are reported as nonoperating revenues and expenses.

Under GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Government Entities that Use Proprietary Fund Accounting*, the Authority has adopted the option to apply only those Financial Accounting Standards Board (FASB) statements and interpretations issued before November 30, 1989, that do not conflict with or contradict GASB pronouncements. Only GASB pronouncements issued after this date will be followed.

(Dollars in thousands)

(c) Capital Assets

Capital assets over $5,000 are stated at historical cost. These costs include the Authority's labor costs for employees working on capital projects, related fringe benefits, and an allocated share of general and administrative costs.

Depreciation is provided on the straight-line method over its estimated useful life. The major categories of transportation property in service and their estimated useful lives are as follows at June 30, 2006 and 2005:

	Estimated useful life
Ways and structures	10-60 years
Building and equipment	3-25 years

(d) Construction in Progress

During 2006 and 2005, major construction projects aggregating $510,097 and $930,715, respectively, were completed and transferred to the appropriate transportation property accounts. Major projects included transit service extensions, right of way improvements and purchases of new rolling stock and other equipment.

Interest on debt used to finance construction that is capitalized as part of the Authority's capital assets is calculated by offsetting interest expense incurred from the date of the borrowing until completion of the project, with interest earned on invested proceeds over the same period. In fiscal years 2006 and 2005, the net interest cost eligible for capitalization was approximately $30,212 and $32,099, ($35,116 and $33,541 of interest expense offset by $4,904 and $1,442 of interest income), respectively.

Additionally, the Authority, under various interagency agreements, performs construction work on behalf of those agencies. Such construction costs are reimbursed upon completion of the work. Costs incurred during 2006 and 2005 were approximately $10,719 and $16,208, respectively. Amounts owed to the Authority for these costs and prior years costs as of June 30, 2006 and 2005 were approximately $4,747 and $4,711, respectively, and are presented in accounts receivable in the accompanying statements of net assets.

(e) Self Insurance

The Authority is fully self-insured for various risks including worker's compensation, injuries and damages and employee health claims. The Authority also self-insures a portion of casualty and liability claims.

(Continued)

(f) Capital Grants and Contributions

The Authority receives capital grants from certain governmental agencies to be used for various purposes connected with the planning, modernization, and expansion of transportation facilities and equipment. Capital grants of the Authority are reported as revenue rather than contributed capital as required by GASB Statement No. 33, *Accounting and Financial Reporting for Nonexchange Transactions*.

(g) Statements of Cash Flows

For purposes of the statements of cash flows, the Authority considers all highly liquid investments purchased with a maturity of three months or less to be temporary cash investments.

(h) Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

(i) Compensated Absences

The Authority accrues for vested vacation pay when it is earned by employees. The amount of vested vacation pay accrued as of June 30, 2006 and 2005 was approximately $16,000 for both years.

(j) Restricted Cash and Investment Accounts

Certain cash and investments are segregated from operating cash due to certain internal or external restrictions. The following are included in restricted and other special accounts:

- Bond Construction Accounts – represents unexpended bond proceeds.
- Lease Deposits – represents cash held by trustees to be used to pay lease payments on the Authority's defeased capital leases.
- Bond Reserve Accounts – represents cash funds required to be maintained by bond indentures.
- Stabilization Account – represents funds held in accordance with statutory requirements to be used when annual revenues are projected to be less than annual expenses, or if the Authority has insufficient funds on hand to pay current expenses.
- Other Accounts – represents funds held in accordance with the Authority's Trust Agreements for capital maintenance, debt service, and other expenses.

(k) Lease accounts

Lease accounts represent amounts required to be used to pay lease payments under payment undertaking agreements on the Authority's capital leases. See footnote 8.

(l) Materials and Supplies

Materials and supplies are stated at average cost and include items to support the Authority's operations.

(m) The Authority accounts for interest rate swaps in accordance with GASB technical bulletin 2003-1.

(n) The Authority adopted the policy of generally utilizing available unrestricted resources prior to restricted resources.

(o) Reclassification

Certain reclassifications were made to the 2005 statements to conform to the current year presentation.

(3) Deposits and Investments

The Authority adopted the Governmental Accounting Standards Board Statement No. 40, *Deposit and Investment Risk Disclosures* effective July 1, 2005. The standard requires that entities disclose essential risk information about deposit and investment requirements addressing common risks of investments.

The Authority's investment policy is to only invest in securities named in the respective trust agreements.

The Authority is authorized by its board of directors to make deposits into checking and savings accounts and to invest in direct obligations of the U.S. Treasury, its agencies and instrumentalities, brokers' acceptances, investment agreements, municipal bonds, repurchase agreements secured by U.S. government and agency obligations, and certain other investments permitted under the trust indentures.

Obligations of any agency or instrumentality of the United States of America, including, but not limited to the following, may be acceptable as collateral to secure certificates of deposit or other instruments:

(A) Federal Home Loan Banks

(B) Federal Land Banks

(C) Federal Intermediate Credit Banks

(D) Bank for Cooperatives

(E) Federal National Mortgage Association

(F) Federal Farm Credit Banks

The Authority may invest in prime commercial paper of corporate issuers with a minimum quality rating of P-1 by Moody's or A-1 by Standard and Poor's. These instruments can vary in maturity; however, no more than ten (10) percent of the investment funds shall be invested in the commercial paper of a single corporation.

(Continued)

(Dollars in thousands)

Additionally, the Authority is authorized to invest in The Massachusetts Municipal Depository Trust (MMDT) established under General Laws, Chapter 29, Section 38 A.

Restricted investments are recorded at fair value. Other investments are recorded at amortized cost, which approximates market, and earn interest and dividends at prevailing rates.

Deposits and investments consisted of the following amounts presented in the accompanying statements of net assets at June 30, 2006 and 2005:

		2006	2005
Construction accounts	$	336,976	76,722
Bond reserve, stabilization and other accounts		467,382	375,921
Lease deposits		208,896	182,242
Cash and temporary cash investments		114,559	99,994
	$	1,127,813	734,879

(a) Custodial Credit Risk – Deposits

The custodial credit risk for deposits is the risk that in the event of a bank failure, the Authority's deposits may not be recovered. The deposits in the bank in excess of the insured amount are uninsured and uncollateralized. The carrying amount of the Authority's deposits at June 30, 2006 and 2005 was $127,783 and $156,174, respectively. The bank balance at June 30, 2006 and 2005 was $128,807 and $156,838, respectively. Of this amount, $22,119 and $30,116, respectively, was exposed to custodial credit risk as uninsured and uncollateralized.

(b) Interest Rate Risk – Investments

Interest rate risk is the risk that changes in interest rates of debt investments will adversely affect the fair value of an investment. The Authority follows the guidelines in the Authority's trust agreements, and does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

(Dollars in thousands)

The Authority's fixed-income investments at June 30, 2006 and 2005 are presented below. All investments are presented by investment type and maturity.

2006

		Investment maturities (in years)			
Investment type	**Fair value**	**Less than 1 year**	**1-3**	**4-8**	**More than 9**
MMDT	$ 50,716	50,716	—	—	—
Guaranteed investment contracts	608,642	55,866	289,164	8,167	255,445
Forward delivery agreements	240,133	240,133	—	—	—
Treasury strips	80,539	3,981	6,572	55,348	14,638
Auction rate securities	20,000	20,000	—	—	—
Investments	$ 1,000,030	370,696	295,736	63,515	270,083

2005

		Investment maturities (in years)			
Investment type	**Fair value**	**Less than 1 year**	**1-3**	**4-8**	**More than 9**
MMDT	$ 16,928	16,928	—	—	—
Guaranteed investment contracts	203,076	1,076	65,300	8,288	128,412
Forward delivery agreements	241,995	241,995	—	—	—
Treasury strips	83,481	527	8,719	58,824	15,411
Auction rate securities	33,225	33,225	—	—	—
Investments	$ 578,705	293,751	74,019	67,112	143,823

The Authority has unrestricted deposits of $55,844 and $59,313 as of June 30, 2006 and 2005, respectively. Restricted deposits held within the Authority's bond construction, stabilization, capital maintenance, compensating and deficiency accounts aggregated $71,939 and $96,861 as of June 30, 2006 and 2005.

(c) Credit Ratings

The Authority holds guaranteed investment contracts and forward delivery agreements with a fair value of $848,775 and $445,071 at June 30, 2006 and 2005, respectively. These investments are not rated.

The Authority holds Auction Rate Securities that are invested in short-term investments that mature every 28 or 32 days. The balance held in these Auction Rate Securities was $20,000 and $33,225 as of June 30, 2006 and 2005 respectively. All of these investments have a rating of AAA by Standard & Poor's.

(Dollars in thousands)

Investments in Treasury Strips are a United States government obligation. The Authority had $80,539 and $83,481 invested in Treasury Strips as of June 30, 2006 and 2005.

The Authority also has $50,716 and $16,928 invested in MMDT as of June 30, 2006 and 2005, a state investment pool managed by Fidelity Investments as agent for the Commonwealth of Massachusetts and shareholders of the MMDT Trust. MMDT is unrated.

(d) Concentration of Credit Risk – Investments

Concentration of credit risk is the risk of loss attributable to the magnitude of a government's investment in a single issuer. The issuers where securities at year-end exceeded 5% of the total investments are as follows:

		2006	% of portfolio
Providers of guaranteed investment contracts and forward delivery agreements:			
IXIS Funding Corp.	$	288,938	28.9%
AMBAC		105,273	10.5
Wachovia Bank		102,599	10.3
AIG Matched Funding		80,173	8.0
Bank of America		73,270	7.3
MBIA		64,973	6.5
FSA Capital		52,797	5.3
	$	768,023	

		2005	% of portfolio
Providers of guaranteed investment contracts and forward delivery agreements:			
AIG Matched Funding Corp.	$	99,925	17.3%
AMBAC		99,288	17.2
Bank of America		78,588	13.6
Wachovia Bank		61,100	10.6
FSA Capital Management		47,015	8.1
	$	385,916	

(e) Foreign Currency Risk

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or a deposit. The Authority was not exposed to foreign currency risk as of June 30, 2006 and 2005.

(4) Commuter Railroad and Local Subsidy

Under General Laws, Chapter 161A, Section 3(f) of the Commonwealth of Massachusetts, the Authority may enter into agreements with private transportation companies, railroads, and other concerns providing for joint or cooperative operation of any mass transportation facility and for operation and use of any mass transportation facility and equipment for the account of the Authority.

On July 1, 2004, the Authority entered into an operating agreement with Massachusetts Bay Commuter Railroad Company (MBCRC) beginning July 1, 2003 for a period of five years to provide commuter railroad service over the Authority's rail lines. The Authority will pay MBCRC a total fixed base contract amount of $1,050,081 over this five-year period.

(5) Long-Term Debt

(a) Bonds Payable

The Enabling Act authorizes the Authority to issue general obligation debt, revenue, or other debt secured by a pledge or conveyance of all or a portion of revenues, receipts or other assets or funds of the Authority beginning July 1, 2000.

Debt issued by the Authority and outstanding at June 30, 2000 (prior obligations) is backed by the full faith and credit of the Commonwealth until the debt is paid off. Principal and interest payments on that debt were also subsidized by the Commonwealth prior to June 30, 2000.

Debt issued by the Authority after June 30, 2000 (new debt) will not be supported by the Commonwealth's guarantee. Additionally, the Authority is not expected to receive any principal or interest subsidies from the Commonwealth for the repayment of the prior obligations or new debt of the Authority, unless authorized by special legislation.

In fiscal 2005, the Authority issued two series of Sales Tax Bonds: 2004 Series C for $323,275 and the 2005 Series A for $777,390. Principal is payable July 1, 2013 through July 1, 2024 on the 2004 Series C and from July 1, 2019 through July 1, 2035 on the 2005 Series A. Interest is payable semiannually on July 1st and January 1st on both series. Both series were used to refinance higher interest rate debt, which is more fully described in footnote 5(b).

Also in fiscal 2005, the Authority issued its first Grant Anticipation Note in the amount of $81,665. The debt service on the 2004 Series A GANS is entirely funded by Section 5307 *FTA Formula Funds*. These notes were issued to fund 175 low floor emission control diesel buses and for improvements to the Fairmount Corridor Commuter Rail line. Principal is payable on March 1, 2006 through March 11, 2011. Interest is paid semiannually on March 1st and September 1st.

In June 2005, the Authority entered into two forward starting swaps with UBS AG in the amount of $248,485 and $47,055, respectively, equal to the approximate par amount of Assessment Bonds needed to current refund portions of the Authority's General Transportation System Bonds, 1997 Series B and C maturing on and after March 1, 2008 and portions of the Series 2000 Assessment Bonds maturing on and after July 1, 2011. The swap on the 1997 Series B and Series C General Transportation System Bonds is effective commencing December 2, 2006. Under this swap agreement, the Authority will receive a variable rate equal to the BMA index and pay a fixed rate of 3.783%. The swap on the 2000 Series A Assessment Bonds is effective April 3, 2010 whereby the MBTA will receive a variable rate equal to the BMA index and pay a fixed rate of 4.132%. Neither swap agreement is a Qualified Hedge under the Assessment Bond Trust Agreement, so payments under each swap agreement are made under the Assessment Bond Trust Agreement from the General Fund, and payments received by the Authority are deposited in the Pledged Revenue Fund.

In fiscal 2006, the Authority issued three series of Sales Tax Bonds: the 2005 Series B for $92,765, the 2006 Series A for $240,565 and the 2006 Series C for $260,535. Principal is payable July 1, 2006 and July 1, 2009 through July 1, 2029 on the 2005 Series B, from July 1, 2006, July 1, 2022 and July 1, 2028 through July 1, 2034 on the 2006 Series A and from July 1, 2007 through July 1, 2034 on the 2006 through July 1, 2034 on the 2006 Series C. Interest is payable semiannually on July 1st and January 1st on all three series. The 2005 Series B Sales Tax Bonds and the 2006 Series A Sales Tax Bonds were used to refinance higher interest rate debt which is more fully described in footnote 5(b). The 2006 Series C Sales Tax Bonds were issued to fund the Authority's capital program.

In March 2006, the Authority sold $224,890 in 2006 Series B Sales Tax Bonds that have a delayed delivery date of December 5, 2006. Principal is payable July 1, 2007 through July 1, 2023. Interest is payable semiannually on July 1st and January 1st on this series. These bonds will refund $5,500 of the 1997 Series B General Transportation System Bonds and $224,330 of the 1997 Series C General Transportation System Bonds that were pledged under a forward swap for $248,485 that the Authority entered into in June 2005 and would have commenced in December 2006. The issuance of the $224,890 in 2006 Series B Sales Tax Bonds will effectively terminate the forward swap and the MBTA is expected to receive a swap termination payment of $5,675.

The Authority also issued the 2005 Series A Assessment bonds for $425,000 in fiscal year 2006. Principal is payable on July 1, 2006 through July 1, 2035. Interest is payable semiannually on July 1st and January 1st. The 2005 Series A Assessment bonds were issued to refund $112,500 in Bond Anticipation Notes (BANS) while the remaining proceeds were used to finance new vehicles, commuter rail expansion, new automated fare collection equipment and other system-wide maintenance projects.

In August 2005, the Authority entered into a forward starting swap with Bear Stearns Financial Products Inc. for a notional amount of $280,000 which is the approximate par amount of Senior Sales Tax Bonds anticipated to be issued by the MBTA in January 2007 to fund a portion of the Authority's capital program. The swap is effective commencing January 10, 2007, and pursuant to the swap the Authority will receive a variable rate equal to BMA Index and pay a fixed rate of 4.168%. In the event that the swap is optionally terminated by the Authority prior to the effective date, the termination payment will be based on the Authority paying a fixed rate of 4.158%. The swap agreement is a qualified hedge under the Sales Tax Bond Trust Agreement. In June 2006, the Authority issued the 2006 Series C Sales Tax Bonds with a par value of $260,535 which effectively terminates the $280,000 forward swap. The MBTA received a swap termination payment of $6,395.

General Transportation System (GTS) Bonds, all issued prior to July 1, 2000, are payable in annual installments on March 1st; interest is payable semiannually on March 1st and September 1st. The GTS bonds were issued to provide funds for the financing of the Authority's transportation property.

Boston Metropolitan District Bonds (BMD) were issued for transit purposes prior to the formation of the Authority in 1964.

In order to take advantage of the low interest rate short-term capital market, the Authority issues commercial paper to raise funds in order to pay its capital costs. The Authority has a $200 million commercial paper program. $100 million is administered by Bear Stearns and $100 million by Lehman Brothers. Authority commercial paper is rated P-1 by Moody's Investor Services and A-1+ by Standard and Poor's. The Authority did not have any outstanding commercial paper as of June 30, 2006.

(Dollars in thousands)

The bonds outstanding are as follows at June 30, 2006:

	Year of maturity	Interest rates	Outstanding principal June 30, 2006	Due in fiscal 2007
General transportation system bonds:				
1974 Series A Bonds dated June 1, 1974	2014	5.0 – 6.6%	$ 12,075	—
1991 Series A Bonds dated November 15, 1991	2021	7.00%	75,000	—
1992 Series C Refunding Bonds dated December 1, 1992	2021	6.20%	125,200	—
1992 Series B Bonds dated November 15, 1992	2023	6.10%	15,575	—
1993 Series A Refunding Bonds dated June 1, 1993	2022	5.4% – 5.5%	169,940	29,540
1994 Series A Refunding Bonds dated June 1, 1994	2019	6.25% – 7.0%	155,725	26,230
1995 Series A Bonds dated April 1, 1995	2025	5.5% – 5.875%	102,180	4,345
1997 Series B Bonds dated August 1, 1997	2014	4.8 – 5.0%	6,145	645
1997 Series C Bonds dated August 1, 1997	2024	5.0 – 6.0%	232,365	8,035
1998 Series A Bonds dated February 15, 1998	2026	4.3% – 5.5%	291,665	1,250
1998 Series C Bonds dated November 1, 1998	2022	5.25% – 5.75	208,205	17,245
1999 Variable Interest Rate Bond dated June 29, 1999	2014	Variable	44,885	4,375
2000 Variable Interest Rate Bond dated March 10, 2000	2030	Variable	188,000	—
			1,626,960	91,665

(Dollars in thousands)

	Year of maturity	Interest rates	Outstanding principal June 30, 2006	Due in fiscal 2007
Boston metropolitan district bonds:				
1998 Series A dated November 1, 1998	2008	4.0% – 4.1%	$ 1,530	470
2002 Series A dated December 1, 2002	2014	5.125% – 5.25%	17,515	1,660
			19,045	2,130
Revenue bonds:				
2000 Series A Assessment Bond dated August 1, 2000	2030	4.9% – 5.75%	81,035	—
2000 Series A Senior Sales Tax Bond dated August 1, 2000	2010	4.7% – 4.8%	28,620	—
2002 Series A Senior Sales Tax Bond dated November 1, 2002	2017	3.0% – 5.0%	36,820	—
2003 Series A Senior Sales Tax Bond dated January 29, 2003	2021	2.25% – 5.25%	218,685	13,305
2003 Series B Senior Sales Tax Bond dated February 26, 2003	2023	Auction Rate	93,375	—
2003 Series C Senior Sales Tax Bond dated February 3, 2004	2023	2.20% – 6.0%	253,455	29,385
2004 Series A Senior Sales Tax Bond dated February 3, 2004	2016	2.20% – 5.25%	16,495	40
2004 Series B Senior Sales Tax Bond dated March 9, 2004	2030	2.0% – 5.25%	511,375	—
2004 Series A Assessment Bond dated June 10, 2004	2021	3.0% – 5.25%	55,585	—
2004 Series C Sales Tax Bond dated December 22, 2004	2024	3.5% – 5.5%	323,275	—
2005 Series A Sales Tax Bond dated March 24, 2005	2035	—	777,390	—
2005 Series A Assessment Bond dated September 8, 2005	2035	3.0% – 5.0%	425,000	900
2005 Series B Sales Tax Bond Bond dated December 21, 2005	2029	3.15% – 5.5%	92,765	445
2006 Series A Sales Tax Bond Bond dated March 2, 2006	2034	4.0% – 5.25°/°	240,565	1,715
2006 Series C Sales Tax Bond Bond dated June 28, 2006	2034	4.0% – 5.0%	260,535	—
			3,414,975	45,790

(Continued)

(Dollars in thousands)

	Year of maturity	Interest rates	Outstanding principal June 30, 2006	Due in fiscal 2007
Grant Anticipation Notes (GANS):				
2004 Series A Grant Anticipation Notes dated August 5, 2004	2011	2.0% – 5.0%	$ 81,665	9,830
Total bond and notes payable			5,142,645	$ 149,415
Less current maturities			149,415	
Total long-term bonds payable			4,993,230	
Plus – unamortized bond premiums			305,718	
Less – unamortized bond discounts/losses on bond refundings, net			(289,680)	
Total long-term bonds payable			$ 5,009,268	

The annual maturities of bonds and notes payable as of June 30, 2006 are as follows:

	Principal	Interest
Fiscal years:		
2007	$ 149,415	262,098
2008	140,915	262,110
2009	159,345	254,040
2010	189,080	245,007
2011	192,435	234,821
2012 – 2016	1,031,685	1,009,616
2017 – 2021	1,080,935	719,971
2022 – 2026	1,003,330	438,001
2027 – 2031	781,545	202,070
2032 – 2036	413,960	44,853
Total	$ 5,142,645	3,672,587

(Dollars in thousands)

A summary rollforward of bonds for 2006 and 2005 is as follows:

	Balance 2005	Additions	Payments	Balance 2006
General Transportation	$ 1,770,835	—	143,875	1,626,960
Boston Metropolitan District	21,000	—	1,955	19,045
Revenue	2,665,505	1,018,865	269,395	3,414,975
Grant Anticipation Notes	81,665	—	—	81,665
Bond Anticipation Notes	92,800	—	92,800	—
	$ 4,631,805	1,018,865	508,025	5,142,645

	Balance 2004	Additions	Payments	Balance 2005
General Transportation	$ 2,278,390	—	507,555	1,770,835
Boston Metropolitan District	23,250	—	2,250	21,000
Revenue	2,200,865	1,100,665	636,025	2,665,505
Grant Anticipation Notes	—	81,665	—	81,665
Bond Anticipation Notes	—	92,800	—	92,800
	$ 4,502,505	1,275,130	1,145,830	4,631,805

The following funds included in restricted assets at June 30, 2006 and 2005 are in connection with the Authority's revenue bond trust agreements:

	2006			2005		
	Assessment bonds	Sales tax bonds	GANs	Assessment bonds	Sales tax bonds	GANs
Debt service	$ 16,817	123,652	—	11,756	82,499	—
Debt service reserve	109,499	131,703	8,288	73,102	103,761	8,288
	$ 126,316	255,355	8,288	84,858	186,260	8,288

The minimum required balances in the debt service reserve funds at June 30, 2006 and 2005 were $48,050 and $23,754 for the assessment bonds and $117,743 and $96,526 for the sales tax bonds, respectively. The minimum required balance in the debt service reserve funds at June 30, 2006 and 2005 for Grant Anticipation Notes is $8,167. In addition, for the year ended 2006 and 2005, the Authority collected $847,539 and $842,779 in pledged revenue ($711,086 and $704,621 in dedicated sales tax receipts and $136,453 and $138,158 in local assessments), respectively. The Authority has complied with its financial bond covenants.

(Continued)

(b) Debt Refundings

In current and prior years, the Authority defeased in-substance several General Transportation System Bonds by placing the proceeds of new bonds in an irrevocable trust fund to provide for future debt service payments on the old debt. Accordingly, the trust account asset and the liability for the defeased bonds are not included in the accompanying financial statements. On June 30, 2006 and 2005, $1,908,410 and $1,940,460 of these bonds, considered defeased in-substance, are still outstanding, respectively.

During fiscal 2006, the Authority refunded $90,120 in General Transportation System Bonds with the issuance of the 2005 Series B Sales Tax Bonds. The refunding qualified as an "in-substance defeasance". The difference in cash flows between the prior debt service and the new debt service is approximately $13,972. The net present value or economic gain on the refunding is $11,321. The accounting loss of $7,169 has been presented as a reduction in the amount of outstanding debt and will be amortized over the life of the 2005 Series B Sales Tax Bonds.

In March 2006, the Authority refunded $135,440 in 2004 Series A Assessment Bonds and $119,770 in 2002 Series A Sales Tax Bonds with the issuance of the 2006 Series A Sales Tax Bonds. The difference in cash flows between the prior debt service and the new debt service is approximately $25,672. The net present value or economic gain on the refunding is $13,808. The accounting loss of $10,562 has been presented as a reduction in the amount of outstanding debt and will be amortized over the life of the 2006 Series A Sales Tax Bonds.

During fiscal 2006, the Authority priced the 2006 Series B Sales Tax Bonds which will be delivered in December 2006. The issuance of the 2006 Series B Sales Tax bonds will refund $5,500 of the 1997 Series B General Transportation System Bonds and $224,330 of the 1997 Series C General Transportation System bonds which were pledged under a forward swap commencing in December 2006. The issuance of these bonds will effectively terminate the forward swap. The MBTA will also receive a swap termination payment of $5,675 in December 2006. The difference in cash flows between the prior debt service and the new debt service is approximately $25,328. The net present value or economic gain on the refunding will be $15,569. The accounting loss will not be calculated until the bonds are delivered in December 2006.

During fiscal 2005, the Authority refunded $222,215 in General Transportation System Bonds, $14,900 of 2000 Series A Sales Tax Bonds, $7,145 of 2002 Sales Tax Bonds and $41,985 of 2004 Series A Assessment Bonds with the issuance of the 2004 Series C Senior Sales Tax Bonds. The 2004 Series C Sales Tax Bonds also funded $20,649 of the $23,575 in swap termination payments while the Authority funded the balance of $2,926. The refunding qualified as an "in-substance defeasance." The difference in cash flows between the prior debt service and new debt service is approximately $21,476. The net present value or economic gain on the refunding is $3,117. The accounting loss of $19,842 has been presented as a reduction in the amount of outstanding debt and will be amortized over the life of the refunded bonds.

(Dollars in thousands)

Additionally, the Authority refunded $197,015 in General Transportation System Bonds, $246,715 of 2000 Series A Assessment Bonds, $16,155 of 2000 Series A Sales Tax Bonds, $113,290 of 2002 Sales Tax Bonds and $170,205 of 2004 Series A Assessment Bonds with the issuance of the 2005 Series A Senior Sales Tax Bonds. The refunding qualified as an "in-substance defeasance". The difference in cash flows between the prior debt service and new debt service is approximately $57,282. The net present value or economic gain on the refunding is $51,167. The accounting loss of $47,138 has been presented as a reduction in the amount of outstanding debt and will be amortized over the life of the refunded bonds.

(c) Certificates of Participation

Outstanding Certificates of Participation (COPs) of the Authority totaled $0 and $1,135 at June 30, 2006 and 2005, respectively. Under the Forward Funding legislation effective July 1, 2000, these COP payments are not reimbursable from the Commonwealth. However, the Commonwealth will continue to guarantee the debt until it is repaid.

A rollforward of the COPs for the years ended June 30, 2006 and 2005 is as follows:

Outstanding – June 30, 2004	$	2,270
Payments		(1,135)
Outstanding – June 30, 2005		1,135
Payments		(1,135)
Outstanding – June 30, 2006	$	—

The remaining outstanding principal balance of COPs that were defeased in-substance in prior years is $9,075 at June 30, 2006.

(d) Derivative Investments

The Authority has entered into interest rate swaps and swaptions (referred to herein collectively as Swaps) in order to lower its cost of capital, protect against rising interest rates, lock in interest rate savings, realize refinancing savings according to schedules that suit the Authority's needs, and to provide the Authority with a stable and predictable cost of fuel. When the Authority has entered into Swaps, the Authority has done so in order to: (1) provide lower cost fixed rate financing for its capital needs through synthetic fixed rate structures; (2) lock in long-term fixed rate returns on invested assets in its required reserve funds; (3) create synthetic refinancing with cash flow savings realized as the Authority designates; or (4) create a synthetic fixed rate for the purchase of vehicular fuel for fixed periods of time rather than being exposed to unpredictable variations in fuel prices on the spot market. All premiums received by the Authority in connection with the swaps/swaptions are deferred and amortized into income over the life of the swap/swaption. Should a swap/swaption be terminated, any unamortized premiums are recognized as income in the period the termination occurs. In addition, any termination fees will be recorded as interest or other expense.

(Dollars in thousands)

Summary of Swap Transactions by Category

Synthetic Fixed Rate Swap Transactions

Date of execution	Notional amount	Termination date	Associated bonds	Fixed payable swap rate	Variable receivable swap rate	Lump-sum payment from counterparty	Counterparty credit rating at June 30, 2006	Fair value appreciation (depreciation) at June 30, 2006
July 2001	$ 188,000	2030	GTS Series 2000 VRDO	5.00%	67% of Libor	$ 12,230 (August 2005)	A2/AA+	$ (23,835)
December 2001	87,805	2022	Senior Sales Tax Series 2003 B	5.20	BMA	4,546 (June 2007)	Aaa/AAA	(2,928)
February 2004	25,005	2020	*Senior Sales Tax Series 2003 C	4.13	CPI+79 basis points	N/A	Aa3/A+	(623)

* This swap relates only to the July 1, 2020 maturity which has a variable rate of interest.

Swap Payments and Associated Debt. As of June 30, 2006, debt service requirements of the GTS Series 2000 VRDO (2000 Bonds) bonds and net swap payments, applying the fixed rate on the swap of 5.0% and assuming the 67% of Libor rate is 3.58% and the variable rate on the 2000 Bonds is 3.96% through the term of the swap, were as follows. As rates vary, variable rate interest rate payments on the 2000 Bonds and net swap payments will vary.

Fiscal year ending June 30	2000 Bonds principal	2000 Bonds interest	Interest rate swap, net	Total
2007	$ —	7,445	2,666	10,111
2008	—	7,445	2,666	10,111
2009	—	7,445	2,666	10,111
2010	—	7,445	2,666	10,111
2011	—	7,445	2,666	10,111
2012 – 2016	26,580	35,495	12,710	74,785
2017 – 2021	41,170	28,921	10,356	80,447
2022 – 2026	57,735	19,546	6,999	84,280
2027 – 2030	62,515	6,398	2,291	71,204
Totals	$ 188,000	127,585	45,686	361,271

As of June 30, 2006, debt service requirements of the 2003 B-1 and 2003 B-2 hedged bonds and net swap payments, applying the fixed rate on the swap of 5.2% and assuming the BMA rate is 3.97% and the variable rate on the 2003 B-1 bonds is 3.80% and 2003 B-2 bonds is 3.50% through the term of the swap, were as follows. As rates vary, variable rate interest rate payments on the 2003 bonds and net swap payments will vary.

(Dollars in thousands)

Fiscal year ending June 30		2003 B Bonds principal	2003 B Bonds interest	Interest rate swap, net	Total
2007	$	—	3,216	1,080	4,296
2008		—	3,216	1,080	4,296
2009		—	3,216	1,080	4,296
2010		—	3,216	1,080	4,296
2011		—	3,216	1,080	4,296
2012-2016		26,075	14,714	4,941	45,730
2017-2021		42,075	8,353	2,807	53,235
2022		19,655	723	243	20,621
	$	87,805	39,870	13,391	141,066

As of June 30, 2006, debt service requirements on the 2003 Series C Sales Tax bonds and net swap payments, applying the fixed rate on the swap of 4.13% and assuming the CPI rate of 2.33% plus 79 basis points through the term of the swap, were as follows. As rates vary, variable interest rate payments on the 2003 Series C bonds and net swap payments will vary.

Fiscal year ending June 30		2003 C Bonds principal	2003 C Bonds interest	Interest rate swap, net	Total
2007	$	—	582	253	835
2008		—	582	253	835
2009		—	582	253	835
2010		—	582	253	835
2011		—	582	253	835
2012-2016		—	2,911	1,265	4,176
2017-2020		25,005	2,183	949	28,137
	$	25,005	8,004	3,479	36,488

(Dollars in thousands)

Swaptions for Forward Refundings

Date of execution of swaption	Notional amount	Lump-sum payment from counter-party	Counter-party option exercise date	Term of swap	Associated bonds	Fixed payable swap rate	Variable receivable swap rate	Counter-party credit rating at June 30, 2006	Fair value appreciation (depreciation) at June 30, 2006
December 2001	79,645	4,140 (August 2005)	Each March and September from 2009 through and including 2011	2030	GTS Bonds, 1999 Series A maturing 2026 and 2030	5.610%	BMA	Aaa/AAA	(8,578)
June 2005	47,055	N/A	Forward swap effective commencing April 3, 2010 through July 1, 2030	2030	2000 Series A Assessment Bonds	4.130	BMA	(Aa2/AA+)	1,411

These two swaptions are generally exercisable from September 2009 through March 2011.

Asset-Side Swaption for Reserve Investment

Date of execution of swaption	Notional amount	Lump-sum payment from counter-party	Counter-party option exercise date	Term of swap	Associated bonds	Fixed payable swap rate	Variable receivable swap rate	Counter-party credit rating at June 30, 2006	Fair value appreciation (depreciation) at June 30, 2006
December 2000	$ 49,123	$ 1,265 (July 2001)	January 1st and July 1st from July 2010 through July 2030	2030	Debt Service Reserve Fund for 2000 Assessment and Sales Tax Bonds	5.60%	BMA	Aa2/AA+	$ (1,986)

Risk Disclosure

Credit Risk – Because all of the Authority's Swaps rely upon the performance of the third parties who serve as swap counterparties, the Authority is exposed to credit risk, or the risk that a swap counterparty fails to perform according to its contractual obligations. The appropriate measurement of this risk at the reporting date is the fair value of the swaps, as shown in the columns labeled Fair Value in the tables above. All Fair Values have been calculated using the Mark to Market. To mitigate credit risk, the Authority maintains strict credit standards for swap counterparties. All swap counterparties for longer term swaps are rated in the double-A category by both Moody's and Standard & Poor's. On the Authority's shorter term swap that expired in September 2005, the counterparty is rated in the single-A category by both rating agencies. To further mitigate credit risk, the Authority's swap documents require counterparties to post collateral for the Authority's benefit if they are downgraded below a designated threshold.

Basis Risk – The Authority is exposed to basis risk if the relationship between the floating index the Authority receives on the swaps (BMA, CPI plus 79 basis points, or 67% of LIBOR) falls short of the variable rate on the associated bonds. Should this occur, the expected savings may not be realized. As of June 30, 2006, the 67% of Libor was 3.58%, while the variable rate on the 2000 Bonds was 3.96% and the variable rates on the 2003 B-1 hedged bonds and 2003 B-2 hedged bonds were 3.80% and 3.50%, respectively. For the Series 2003 C in the amount of $25,005, the Authority has basis risk should CPI plus 79 basis points fall below the 4.13%. CPI plus 79 basis points as of June 30, 2006 was 3.12%.

Termination Risk – The Authority's swap agreements do not contain any out-of-the-ordinary termination events that would expose it to significant termination risk. In keeping with market standards the authority or the counterparty may terminate each swap if the other party fails to perform under the terms of the contract. In addition, the swap documents allow either party to terminate in the event of a significant loss of creditworthiness. The Authority views such events to be remote at this time. If at the time of the termination a swap has a negative value, the Authority would be liable to the counterparty for a payment equal to the fair value of such swap.

Rollover Risk – Upon the termination of the swap, the Authority will no longer realize the synthetic rate on the 2000 bonds and will be exposed to floating rate risk on the underlying bonds if no new hedge is put in place.

Market Access Risk and Potential Basis Risk – In the case of the swaptions, if any option is exercised and refunding bonds are not issued, the bonds expected to be refunded would not be refunded and the Authority would make net swap payments as required by the terms of each contract, as set forth above. If the option is exercised (and assuming the variable rate bonds are issued in the case of these transactions), the actual savings ultimately recognized by the transaction will be affected by the relationship between the interest rate terms of the variable rate bonds versus the variable payment on the swap.

(6) Deferred Revenue

The deferred revenue amount relates principally to a settlement received from a supplier of green line cars which will be amortized over a remaining life of 5 years and the deferral of swap premiums received which will be amortized over the applicable swap term.

(7) Retirement Plans

The Authority provides retirement benefits to employees through four defined benefit retirement plans and one defined contribution plan: The MBTA Retirement Plan, the MBTA Police Association Plan, the MBTA Deferred Compensation Plan, the MBTA Qualified Deferred Compensation Plan, and the MBTA Deferred Compensation Savings Plan. The Authority also provides supplemental pension benefits after retirement.

The MBTA Retirement Plan, a single-employer plan, covers all employees except the MBTA police, who are covered separately, and certain executives who elect coverage under an alternate plan. This retirement plan and the MBTA Police Association Plan, a single-employer plan, provide retirement, disability, and death benefits. Both plans issue a publicly available financial report that includes financial statements and required supplementary information for that plan. The MBTA Retirement Plan report may be obtained by writing to One Washington Mall, Boston, Massachusetts 02108, or by calling (617) 316-3800. The MBTA Police Association Plan may be obtained by writing to P.O. Box 6807, Boston, MA 02102 or by calling 1-800-281-0063.

The MBTA Deferred Compensation Plan, a single-employer plan, provides supplemental pension benefits for certain executive and Local 453 (collective bargaining unit) employees after retirement. Employees may participate in both the MBTA Retirement Plan and the MBTA Deferred Compensation Plan.

The Authority created a new Qualified Deferred Compensation Plan effective January 1, 2001. The Plan is designed to supplement the Authority's Retirement Plan (Main Fund). Covered employees include all actively employed nonunion employees who are participating in the Authority Main Fund or the Police Association Retirement Plan. Employees are eligible after five years with the Authority, if they have reached age 30 and are paid as part of the executive payroll. The Plan currently provides benefits for 187 retirees. An actuarial valuation was performed on this plan; however, the cost of this plan to the Authority for fiscal 2006 was minimal and no contributions were made to this Plan in fiscal 2006. In addition, the net pension obligation is considered immaterial.

(a) Funding Policy and Annual Pension Cost

The board of trustees of each plan establishes the contribution requirements; however, the Authority may amend these requirements. The MBTA Retirement Plan requires members to contribute 4% with the Authority currently paying an amount equal to approximately 10.10% of total payroll. The actuarial required contribution rate for the Authority was 10.47%. The contribution requirements for the Police Association Plan were 13.27% for the Authority and 7.44% for employees. Both were determined in accordance with actuarial valuations. Actual contributions made to this Plan in 2006 and 2005 were in accordance with these contribution requirements.

(Dollars in thousands)

Deferred Compensation contributions are made on a "pay-as-you-go" basis. The Authority's annual pension cost for the years ended June 30, 2006 and 2005 and related information for each plan is as follows:

		2006		
Pension		**MBTA Retirement Plan**	**MBTA Police Association Plan**	**Deferred Compensation Plan**
Annual pension cost – Authority	$	35,350	1,970	4,609
Contributions made – Authority		34,104	1,632	4,293
Actuarial valuation date/update		6/30/2006	6/30/2006	6/30/2006
Actuarial cost method		Entry age	Entry age	Entry age
Amortization method		Level dollar	Level dollar	Level dollar
Amortization period remaining		30 years	9 years	30 years
Asset valuation method		5 year moving	4 year smoothing	Fair value
Actuarial assumptions:				
Interest rate		7.25%	7.00%	8.00%
Projected salary increases		5.00	4.50	5.00

		2005		
Pension		**MBTA Retirement Plan**	**MBTA Police Association Plan**	**Deferred Compensation Plan**
Annual pension cost – Authority	$	30,160	1,686	4,531
Contributions made – Authority		34,201	1,734	4,057
Actuarial valuation date/update		6/30/2005	6/30/2005	7/1/2004
Actuarial cost method		Entry age	Entry age	Entry age
Amortization method		Level dollar	Level dollar	Level dollar
Amortization period remaining		31 years	10 years	31 years
Asset valuation method		5-year moving	4-year smoothing	Fair value
Actuarial assumptions:				
Interest rate		7.25%	7.00%	8.00%
Projected salary increases		5.00	5.50	5.00

(Dollars in thousands)

Changes in the net pension assets (obligation) for these plans for the years ended June 30, 2006 and 2005 are as follows:

		2006		
Pension		**MBTA Retirement Plan**	**MBTA Police Association Plan**	**Deferred Compensation Plan**
Net pension obligation – beginning of year	$	(2,483)	(95)	(6,674)
Annual pension cost		(35,350)	(1,970)	(4,609)
Contributions and other adjustments		24,827	1,632	4,293
Net pension obligation – end of year	$	(13,006)	(433)	(6,990)

		2005		
Pension		**MBTA Retirement Plan**	**MBTA Police Association Plan**	**Deferred Compensation Plan**
Net pension obligation – beginning of year	$	(6,524)	(143)	(6,200)
Annual pension cost		(30,160)	(1,686)	(4,531)
Contributions		34,201	1,734	4,057
Net pension obligation – end of year	$	(2,483)	(95)	(6,674)

(Continued)

(Dollars in thousands)

(b) Three-Year Trend Information

	Year ending		Annual pension cost (APC)	Percentage of APC contributed	Net pension asset (obligation)
MBTA Retirement Plan					
	06/30/04	$	34,847	61%	(6,524)
	06/30/05		30,160	113	(2,483)
	06/30/06		35,350	96	(13,006)
MBTA Police Association Plan					
	06/30/04		1,636	92%	(143)
	06/30/05		1,686	103	(95)
	06/30/06		1,970	83	(433)
MBTA Deferred Compensation Plan					
	06/30/04		4,392	89%	(6,200)
	06/30/05		4,531	90	(6,674)
	06/30/06		4,609	93	(6,990)

(c) The MBTA Deferred Compensation Savings Plan

The Authority provides a defined contribution retirement plan for nonunion and grandfathered union management not participating in the MBTA Retirement Plan. Authority employee trustees administer the Plan and recommend benefit amendments which require approval from the Authority's General Manager. The Plan requires members to contribute 4% of total covered payroll with the Authority contributing 8%. The Plan has approximately 267 and 261 members at June 30, 2006 and 2005, respectively, and the cost of the Plan to the Authority was $701 and $787 for fiscal years 2006 and 2005, respectively. Member contributions vest to Plan members immediately, while contributions made by the Authority vest to Plan members as follows: 50% after three years; 75% after four years; and 100% after five years of credited service.

(d) Other Post-Employment Benefits

The Authority pays 100% of health insurance to retired employees eligible under the Deferred Compensation Savings Plan, MBTA Retirement Plan and MBTA Police Association Plan. These benefits are expensed on a current (pay-as-you-go) basis. There were approximately 6,104 and 6,296 retired employees eligible to receive post-retirement benefits at June 30, 2006 and 2005, respectively. The cost of these benefits was approximately $50,182 and $47,880 in fiscal years 2006 and 2005, respectively.

(8) Lease Obligations

(a) Lease-In/Lease-Out

In prior years the Authority entered into various lease/sublease financing arrangements for heavy rail, commuter rail cars and buildings. These agreements provide for the lease of the property and equipment owned by the Authority to a financial party lessee and the sublease of such equipment back to the Authority for various periods. At the time of these transactions, the Authority deposited funds with a financial institution sufficient to meet all of its payment obligations under the terms of the lease and acquired United States Treasury Strips which would mature to an amount sufficient to satisfy each agreement's purchase option provided for in the leases. Because these transactions do not meet the criteria for an "in-substance defeasance," the funds on deposit, United States Treasury Strips, and the related lease liability have been included in the accompanying financial statements.

(b) Sale-In/Lease-Out

In fiscal 2006, the Authority entered into a Sale-in / Lease out (SILO) lease transaction involving 80 commuter rail cars. The transaction consists of an owner participant, creating a business trust with a third-party trust company acting as trustee. The trust is used in part to help insulate other parties to the transaction from risks associated with a bankruptcy by the owner participant. The majority investor lends up to 90% of the loan portion to the trust for payment of acquiring the equipment. The minority investor lends up to 10% of the loan portion to the trust for payment of the equipment. Guaranteed Debt and Equity Payment Undertaking Agreements are in place at AAA / Aaa rated financial institutions. The agreement provides for the lease of the rolling stock owned by the Authority for a period of 23 years on 48 of the cars and 29 years on the remaining 32 cars. The fair market value of the 80 cars under the lease agreement is $220,198. The present value of the remaining rents and purchase option is $202,083 at June 30, 2006. Because this transaction does not meet the criteria for an "in-substance defeasance", the undertaking agreements and related lease liability have been included in the accompanying financial statements. The Authority has recorded a net gain on this lease transaction of $16,183 in 2006.

(c) Cross-Border Leases and Other Capital Lease Arrangements

In prior years, the Authority entered into several cross-border leases related to the financing of certain buses and heavy rail cars. The leases provide for the Authority to sell and lease back the equipment over a period of years. Additionally, there is a purchase option at the end of the lease terms. The Authority has deposited funds with financial institutions sufficient to meet all of its payment obligations under the terms of the leases. Because the transaction does not meet the criteria for an "in-substance defeasance," funds on deposit and the related lease liability have been included in the accompanying financial statements.

(Dollars in thousands)

Transportation property and facilities under capital leases is summarized as follows and is included in capital assets (see note 9) at June 30, 2006 and 2005:

		2006	2005
Ways and structures	$	298,168	298,168
Rail cars		443,708	293,526
Equipment		15,722	8,324
		757,598	600,018
Less accumulated depreciation		(285,181)	(202,658)
Net transportation property in service under capital lease	$	472,417	397,360

The following is a schedule by year of future minimum lease payments under the lease-in/lease-out, cross-border and other capital lease arrangements together with the present value of net minimum lease payments as of June 30, 2006:

Fiscal years:		
2007	$	49,779
2008		124,014
2009		153,118
2010		42,449
2011		81,751
2012 – 2016		350,727
2017 – 2020		150,069
		951,907
Less amount representing interest		(206,149)
Present value of net minimum lease payments		745,758
Less current principal maturities		(21,333)
Obligations under capital leases	$	724,425

(Continued)

(Dollars in thousands)

The liability for these leases changed for 2006 and 2005 as follows:

Outstanding – June 30, 2004	$	538,098
Net change in obligation		10,485
Outstanding – June 30, 2005		548,583
Net change in obligation		197,175
Outstanding – June 30, 2006	$	745,758

(d) Operating Leases

The Authority has entered into several sale-leaseback agreements with major financial institutions (the lessors) covering equipment and rolling stock. The leases mature through 2013. At the end of the lease terms, the Authority may purchase the vehicles at prices equal to the lesser of a stated percentage (40% – 70%) of the lessors' original purchase price or residual fair market value, as defined.

The leases have been accounted for as operating leases. Prior to July 1, 2000, these lease payments were eligible for 90% reimbursement from the Commonwealth. After July 1, 2000, the Authority is no longer entitled to and has not received any of this assistance from the Commonwealth. However, these leases will continue to be guaranteed by the Commonwealth.

Future minimum operating lease payments at June 30, 2006 are as follows:

Fiscal years:		
2007	$	17,757
2008		13,787
2009		13,515
2010		13,218
2011		11,082
2012-2013		16,344
	$	85,703

(Dollars in thousands)

(9) Capital Assets

Capital assets at June 30, 2006 and 2005 are as follows:

	Beginning balance June 30, 2005	Increases	Decreases	Ending balance June 30, 2006
Capital assets not being depreciated:				
Land	$ 320,101	4,135	—	324,236
Construction work in progress	848,341	508,090	510,097	846,334
Total capital assets not being depreciated	1,168,442	512,225	510,097	1,170,570
Other capital assets:				
Ways and structures	7,332,495	362,267	—	7,694,762
Buildings and equipment	2,176,979	166,644	68,924	2,274,699
Total other capital assets at historical cost	9,509,474	528,911	68,924	9,969,461
Less accumulated depreciation for:				
Ways and structures	2,226,063	170,622	—	2,396,685
Buildings and equipment	1,059,198	117,929	68,924	1,108,203
Total accumulated depreciation	3,285,261	288,551	68,924	3,504,888
Other capital assets, net	6,224,213	240,360	—	6,464,573
Capital assets, net	$ 7,392,655	752,585	510,097	7,635,143

(Continued)

(Dollars in thousands)

	Beginning balance June 30, 2004	Increases	Decreases	Ending balance June 30, 2005
Capital assets not being depreciated:				
Land	$ 306,837	13,264	—	320,101
Construction work in progress	1,262,027	517,029	930,715	848,341
Total capital assets not being depreciated	1,568,864	530,293	930,715	1,168,442
Other capital assets:				
Ways and structures	6,593,549	738,946	—	7,332,495
Buildings and equipment	1,995,722	201,845	20,588	2,176,979
Total other capital assets at historical cost	8,589,271	940,791	20,588	9,509,474
Less accumulated depreciation for:				
Ways and structures	2,066,543	159,520	—	2,226,063
Buildings and equipment	976,568	103,218	20,588	1,059,198
Total accumulated depreciation	3,043,111	262,738	20,588	3,285,261
Other capital assets, net	5,546,160	678,053	—	6,224,213
Capital assets, net	$ 7,115,024	1,208,346	930,715	7,392,655

(10) Risk Management

The Authority is exposed to various risks of loss related to general liability, property and casualty, worker's compensation, unemployment, and employee health insurance claims.

Buildings are fully insured to the extent that losses exceed $350 per incident. The Authority is self-insured for workers' compensation, unemployment claims, vehicle damage and loss, and health insurance. The Authority pays 85% of all health premiums up to a maximum of $200 per individual for all Blue Cross plans and $100 per individual for Harvard and Tufts plans. Stop loss insurance is carried on health insurance claims in excess of these amounts per individual per illness.

The Authority self-funds a $7,500 per occurrence deductible for general liability. The Authority has a program of excess public liability insurance to provide for $67,500 of layered coverage on a per occurrence and annual aggregate basis. In the opinion of the General Counsel to the Authority, payments of claims by the Authority for amounts not covered by insurance, in the aggregate, are not expected to have a material adverse effect on the Authority's financial position.

(Dollars in thousands)

During fiscal 2006 and 2005, expenditures for claims and judgments, excluding worker's compensation, and health and life, were $14,192 and $14,673, respectively. Expenditures for claims related to worker's compensation were $16,238 and $20,971, and expenditures for the self-insured health plans were $112,790 and $94,035 for the years ended June 30, 2006 and 2005, respectively.

GASB Statement No. 10 requires that liabilities for self-insured claims be reported if it is probable that a loss has been incurred and the amount can be reasonably estimated. These losses include an estimate of claims that have been incurred but not reported. The Authority reserves such liabilities, which consist of workers' compensation, health claims and injuries and damages (legal claims), as accrued expenses as of June 30, 2006, 2005, and 2004. Changes in the self-insurance liabilities in fiscal 2006, 2005, and 2004 were as follows:

		2006	2005	2004
Liability, beginning of year	$	95,928	89,106	73,931
Provisions for claims		143,220	129,679	128,281
Payments		(131,208)	(122,857)	(113,106)
Liability, end of year	$	107,940	95,928	89,106

(11) Commitments and Contingencies

(a) Capital Investment Program

The Authority's capital investment continuing program for mass transportation development has projects in service and in various stages of approval, planning, and implementation. The following table shows, as of June 30, 2006 and 2005, capital project costs approved, expenditures against these projects, and estimated costs to complete these projects, as well as the major funding sources:

Funding source		Approved project costs	Expenditures through June 30, 2006	Unexpended costs
Federal grants	$	5,273,519	5,149,201	124,318
State and local sources		1,433,260	1,348,620	84,640
Authority bonds		4,988,840	4,583,398	405,442
Total	$	11,695,619	11,081,219	614,400

(Dollars in thousands)

Funding source		Approved project costs	Expenditures through June 30, 2005	Unexpended costs
Federal grants	$	5,178,405	5,013,558	164,847
State and local sources		1,356,067	1,292,417	63,650
Authority bonds		4,753,075	4,271,446	481,629
Total	$	11,287,547	10,577,421	710,126

The Authority is presently authorized by law to issue bonds for capital purposes other than refunding, to an amount not exceeding $5,256,300 outstanding at any time. Such bonds outstanding as of June 30, 2006 amounted to $3,330,000.

The terms of the federal grant contracts require the Authority to, in part, utilize the equipment and facilities for the purposes specified in the grant agreement, maintain these items in operation for a specified time period, which normally approximates the useful life of the equipment, and to comply with the Equal Employment Opportunity and Affirmative Action programs required by the Transportation Equity Act for the 21st Century. Failure to comply with these terms may jeopardize future funding and require the Authority to refund a portion of these grants to the Federal Transit Administration (FTA). In management's opinion, no events have occurred that would result in the termination of these grants or require the refund of a significant amount of funds received under these grants.

Other cases and claims include disputes with contractors and others arising out of the Authority's capital construction program. In the opinion of the General Counsel to the Authority, amounts reasonably expected to be paid by the Authority would be within the scope of grant funds and other funds available to the Authority for the respective projects.

The Authority has entered into several long-term contracts to purchase coaches, locomotives, buses, rapid transit cars and other transportation equipment. Unpaid amounts under these contracts total approximately $328,268 and $390,927 at June 30, 2006 and 2005, respectively.

(b) Legal and Other

The Authority is involved in numerous lawsuits, claims, and grievances arising in the normal course of business, including claims for personal injury and personnel practices, property damage, and disputes over eminent domain proceedings. In the opinion of the General Counsel to the Authority, payment of claims by the Authority, for amounts not covered by insurance, in the aggregate, are not expected to have a material adverse effect on the Authority's financial position.

The Authority participates in a number of federally assisted grant programs. These programs are subject to financial and compliance audits by the grantors or their representatives. In the opinion of Authority Management, liabilities resulting from such disallowed expenditures, if any, will not be material to the accompanying financial statements.

(Continued)

(12) Subsequent Events

In September 2006, the Authority refunded $169,550 of its 2005 Series A Assessment Bonds and $2,355 of its 2005 Series A Sales Tax Bonds with the issuance of the 2006 Series A Assessment Bonds with a par value of $163,145. The refunding qualified as an "in-substance defeasance". The difference in cash flows between the prior debt service and the new debt service is approximately $15,205. The net present value or economic gain on the refunding is $6,435. Principal is payable July 1, 2007, July 1, 2024 through July 1, 2031 and July 1, 2035 on the 2006 Series A Assessment Bonds. Interest is payable semiannually on July 1st and January 1st. This series also included $24,260 of variable rate bonds based the on MUNI-CPI rate.

(Dollars in thousands)

MBTA Retirement Plan

Valuation date		Actuarial value of assets (a)	Actuarial accrued liability (AAL) (b)	(Funded) unfunded AAL (UAAL) (b-a)	Funded ratio (a/b)	Covered payroll (c)	UAAL as a percentage of covered payroll ((b-a)/c)
Year ended December 31:							
1999	$	1,578,162	1,477,993	(100,169)	106.78	284,677	(35.19)
2000		1,757,327	1,533,284	(224,043)	114.61	301,132	(74.40)
2001		1,889,500	1,626,998	(262,502)	116.13	316,403	(82.96)
2002		1,701,048	1,871,543	170,495	90.89	318,824	53.48
2003		1,834,834	1,881,974	47,140	97.50	317,598	14.84
2004		1,772,612	1,854,264	81,652	95.60	321,397	25.41

Deferred Compensation Plan

The Deferred Compensation Plan is not currently funded; however, management intends to start funding the plan. As a result, the normal Schedule of Funding Progress would show no provision having been made for the cost of this plan.

In the table below, Column (b) which normally would have contained the Plan's assets, contains instead the Net Pension Obligation (amounts previously charged against operations but not yet contributed to the Plan). This alternative presentation shows how much of the cost of the program has been charged against operations in prior years.

Valuation date		Actuarial accrued liability (a)	Net pension obligation (b)	Unrecognized actuarial accrued liability (c) (a)-(b)	Recognized ratio (d) (b)/(a)	Unrecognized ratio (e) (c)/(a)	Covered payroll (f)
07/01/00	$	28,357	5,688	22,669	20.1	79.9	34,507
07/01/01		40,509	4,708	35,801	11.6	88.4	34,590
07/01/02		41,094	5,211	35,883	12.7	87.3	36,319
07/01/03		41,865	5,734	36,131	13.7	86.3	31,787
07/01/04		42,254	6,200	36,054	14.7	85.3	33,376
07/01/05		43,014	6,991	36,023	16.3	83.7	27,495

See accompanying independent auditors' report.

MASSACHUSETTS BAY TRANSPORTATION AUTHORITY
(A Component Unit of the Commonwealth of Massachusetts)

Required Supplementary Information

June 30, 2006

(Unaudited)

(Dollars in thousands)

Police Association Retirement Plan

Valuation date		Actuarial value of assets (a)	Actuarial accrued liability (b)	(Funded) unfunded actuarial accrued liability (c) (b)-(a)	(Unfunded) funded ratio (d) (a)/(b)	Covered payroll (e)	UAAL as a percentage of covered payroll (c)/(e)
12/31/99	$	30,078	22,511	(7,567)	133.6%	8,391	(90.2)%
12/31/00		28,962	31,971	3,009	90.6	10,351	29.1
12/31/01		31,282	35,447	4,165	88.3	10,814	38.5
12/31/02		31,377	40,852	9,475	76.8	11,598	81.7
12/31/03		32,263	41,373	9,110	78.0	12,485	73.0
12/31/04		34,427	43,634	9,207	78.9	12,882	71.5

See accompanying independent auditors' report.