A L A S K A   R A I L R O A D   C O R P O R A T I O N

2 0 0 1   A N N U A L   R E P O R T

Building a great railroad in the Great Land

Our Mission:

To be profitable by focusing on safe, high quality service to our freight, passenger, and real estate customers. To foster the development of Alaska's economy by integrating railroad and railbelt community development plans.

CHAIRMAN'S MESSAGE

I have had the pleasure of serving on the Alaska Railroad's board of directors since 1995 and as chairman since 1997. During my tenure, I have gained insight into where the Alaska Railroad has come from and where it plans to go in the future. I am pleased to report that the outlook is extremely bright.

Since the Alaska Railroad was completed in 1923, it has served Alaskans and the nation in a variety of critical roles. The railroad was the catalyst for communities to settle and thrive; it provided an irreplaceable supply route, supported the war effort as well as construction of the Trans-Alaska Pipeline.

Today, this public asset is more valuable to Alaska than ever, thanks to consistent investment in safety, customer service and profitability. In 1984, the railroad was worth $22.3 million; today our equity (net assets) totals over five times this, at $113.6 million. Sixteen years ago, assets were valued at $59.2 million; today, they are worth $306.2 million.

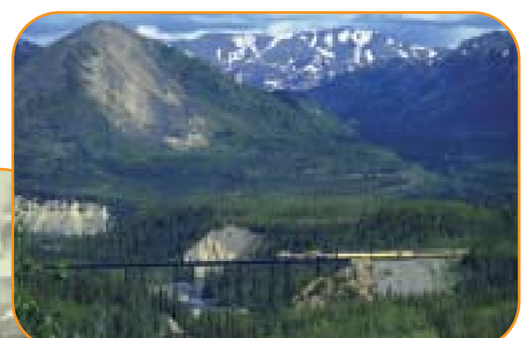
In keeping with the railroad's run on success, 2001 was a banner year. Our vision for modernized infrastructure, made possible through support from our Congressional Delegation, materialized this year with many capital projects going from the drawing board to breaking ground. We emphasized relationships in 2001 and formed key partnerships with a number of community organizations and planning committees. And most important, we made substantial gains in safety, contributing to one of the country's lowest train accident rates.

With 2001 financial statements reflecting record freight and real estate revenues, the railroad's fiscal success and past accomplishments will serve as a springboard to move into new frontiers. Our $6.6 million net earnings in 2001 are being plowed back into the railroad, taking track and train activities to new levels of efficiency and reliability. Technology has been, and will continue to be, a key factor in advancing safety, customer service and profitability goals.

The Alaska Railroad's board of directors is proud of what our employees and customers achieved in 2001. We are determined to set and attain aggressive goals that continue a tradition of support for Alaska's success.

Johne Binkley

Johne Binkley
Chairman of the Board



Passenger train seen approaching the Denali Depot.

Original construction of the railroad took nine years.

PRESIDENT'S MESSAGE

In my first year at the Alaska Railroad, I have acquired a real appreciation for how closely the railroad is tied to the history, culture and economy of the state. This view has been reiterated through employee anecdotes, community feedback, and through the widespread attention given to our accomplishments and activities.

The railroad's essential state role is clearly not lost on the railroad's workforce. Throughout the year, I have been inspired by the pride and commitment Alaska Railroaders demonstrate on the job, day in and day out. In addition to besting our net earning projections, 2001 was marked by solid progress in safety, community relations, revenue growth, environmental response readiness, and modernization.

Communities have quite often been the real benefactors of railroad success. The railroad remains deeply committed to planning and partnering with the communities along the railbelt. We understand how our support of municipal and borough initiatives can translate into a more prosperous Alaska.

Being an effective business partner depends in large part on the condition of our rail infrastructure, and the serviceability of operating and support equipment. We have come far in our efforts to modernize and improve. To keep the momentum going, we are constantly establishing benchmarks and goals as tools to measure productivity and to help flag those areas that need attention.

With excellence in safety and service as top priorities, the Alaska Railroad will remain intricately tied to the success of our people, our communities and our state.

Pat Gamble

Patrick K. Gamble
President & CEO

Railroad employees devote countless hours in their communities.

Railroad personnel participate in dozens of community meetings each year.

The railroad continues to improve reliability of its operating equipment.

Y E A R I N R E V I E W

ARRC prepares to answer the call in Alaska's economic development. The Alaska Railroad spent 2001 demonstrating the kind of partnership the state, communities, and businesses can depend on to support growth and development across Alaska.

We enhanced safety, responsiveness, capacity, and fiscal stewardship. We brought new services online. We improved environmental protection measures, coordinated community planning, and commenced construction on many capital projects. In light of September 11, the railroad also took steps to assess and redress security risks along the Railbelt.

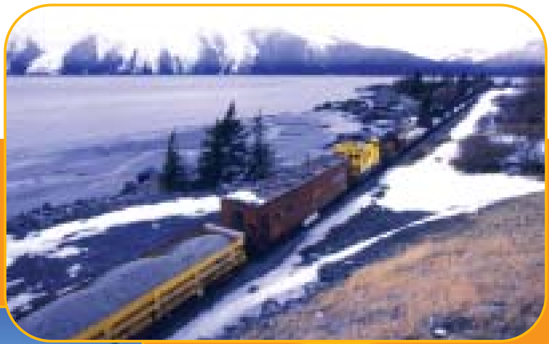
Customers and revenue. With total revenues of $107.3 million and total expenses of $100.7 million, the Alaska Railroad netted $6.6 million in 2001. This was better than expected. Real estate once again proved to be a strong performer with gross revenues reaching $10.57 million – up from $9.28 million last year. Freight revenue also set a record, reaching nearly $80 million. Gravel was up and oil field freight exceeded expectations. A record number of fuel cars were hauled from North Pole, exceeding several daily, weekly and even monthly thresholds. Passenger revenue was up. Collectively, these revenue streams continue to provide the cash flow for our workforce and our railroad services.

New services. Part of the freight success is due to the business relationship established last year to provide barge service between the Lower 48 and our dock in Whittier. On the passenger side, we established direct Seward-Anchorage-Seward service for cruise ship customers. A new passenger reservation system went on-line, and will soon provide Internet convenience for customers, and global exposure for the Alaska Railroad.

Environmental measures. The railroad significantly enhanced emergency and spill response through the purchase of new equipment, extensive employee training, and an overhaul of our spill response plan. Crafted to meet new state regulations, the plan has been filed with the Alaska Department of Environmental Conservation and is available for public review. ARRC also joined Alaska Chadux Corporation, a primary spill response co-op whose considerable experience in Alaska will contribute significantly to our spill response capability.

The railroad's preventative maintenance has resulted in a 32% increase in locomotive reliability.

Construction of the new siding at Pittman was completed in 2001.



General freight revenues continued to climb in 2001.

Y E A R   I N   R E V I E W

Community involvement and planning. Our people have worked hard this year to better coordinate railroad planning efforts with the communities we serve. ARRC anticipates being named as a participant in the Anchorage Metropolitan Area Transportation Study (AMATS) Technical Advisory Committee (TAC) and was named a member of the Fairbanks Metropolitan Area Transportation Study (FMATS) TAC. We are working with several other groups, including the Anchorage and Fairbanks Chambers of Commerce, Anchorage Economic Development Corporation, Seward Centennial Committee, Resource Development Council, and the Alaska 20/20 effort to ensure the railroad's vision complements and supports the overall plans and strategies developed by our State, municipalities and community groups.

Capital improvements. Since 1996, federal funding has laid the financial groundwork to transform the Alaska Railroad into a safer, more reliable rail system. In 2001, we saw years of planning materialize as ground was broken on several capital projects. Some are already completed. The new freight dock in Seward is up and running, track was realigned on Elmendorf Air Force Base, double track will be completed in south Anchorage in 2003, new sidings were constructed at key locations along the rail line, and a state-of-the-art avalanche detection and prevention system was installed south of Anchorage in several slide zones.

Looking ahead. Expect the railroad to maintain the momentum. New intermodal depots at Denali, Fairbanks and the Anchorage airport will greatly enhance passenger service, security and safety. Ongoing efforts to straighten track and automate train traffic control systems will further increase our efficiency, safety, and our speed. We also continue working on innovative ways to make real estate holdings more attractive to serious investors.

As the railroad modernizes infrastructure and fine-tunes operations, and as we increase our capacity to take on more business challenges, the Alaska Railroad will continue to grow more valuable as a partner upon whom Alaska can depend.

"Our vision for modernized infrastructure, made possible through support from our Congressional Delegation, materialized this year with many capital projects going from the drawing board to breaking ground."

- Johne Binkley

A comprehensive program to rebuild trucks helped increase petroleum car safety.

SAFETY AND RELIABILITY

The Alaska Railroad's continued commitment to safety produced positive results in 2001.

Low train accident rate. For the second consecutive year train accident rates fell well below the national average of 3.8 accidents per million train miles. ARRC's 1.5 accidents per million train miles in 2001 compares with 2000's 1.49 average. Both were well below our historical average of over 4 accidents per million train miles. Success can be attributed to significant investments in mainline infrastructure and employee dedication.

Reduction in derailment risk. Another important safety improvement in 2001 came from a cooperative effort to repair trucks (truck assemblies hold the wheels) on 274 of the 409 tank cars leased by Williams Petroleum Alaska. Repairs significantly reduced the risk of derailment by tank cars transporting fuel from North Pole to Anchorage. The result – the railroad set daily, weekly, monthly and annual records in moving over 31,000 loads (more than 710 million gallons) of petroleum without incident – a remarkable safety achievement. The remainder of Williams' fleet is scheduled for truck upgrades in summer 2002.

Spill contingency plan. The Alaska Railroad submitted a revised, improved Spill Contingency Plan to the Alaska Department of Environmental Conservation in the fall of 2001. After an extensive public comment and review process, we hope to have the plan finalized by mid-2002.

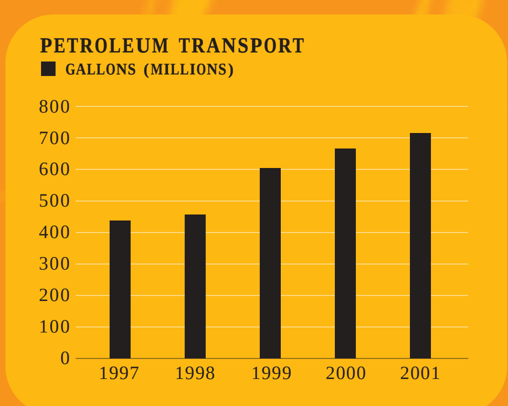
Track improvements. The Maintenance of Way (MOW) department focused on track repair to improve safety. MOW replaced 30,600 crossties, 350 switch ties and 58,000 feet of worn rail. They built nearly 40,000 feet of new track, and resurfaced another 242 track miles. Surfacing is the equivalent of grading a road, accomplished by equipment that lifts the rails and redistributes ballast to smooth out the rail. About 1,800 cars of ballast rock were unloaded in the effort.

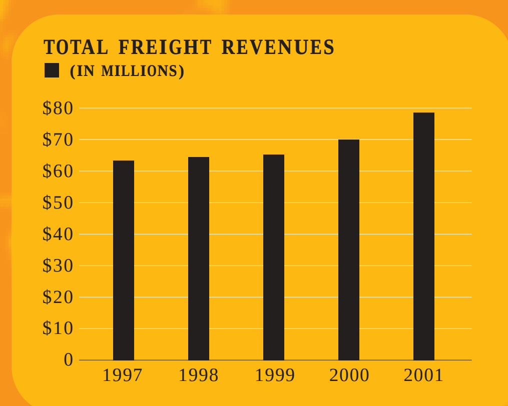
Traffic flow. Other track improvements included major new sidings at Bear Creek (about 15 miles north of Healy) and Pittman (just north of Wasilla) which, along with improvements at existing sidings, helped smooth traffic flow along the track. This improved efficiency played an important part in increasing the number of units moved by 23 percent – to over 96,000 units – and increasing tonnage by 26 percent.

Reliability. During 2001, the mechanical department enhanced reliability of the railroad's locomotive fleet. Their preventative maintenance efforts have resulted in an incredible jump from 65 percent reliability to 97 percent reliability, translating into better, safer customer service.

FREIGHT BUSINESS

In 2001 transportation of commodities generated freight revenues of $79.9 million. Products moved by the railroad include petroleum products, coal, gravel, oilfield and mining supplies, chemicals and consumer goods.





The railroad's new partnership with Lynden, Inc. to operate a rail-barge service from Seattle to Whittier has been successful, giving the railroad a competitive edge with faster turn-around times, shorter cycle times, and improved service quality. In 2001, the railroad initiated design of a new side-unloading facility in Whittier, which should speed unloading time significantly and improve unloading operations' safety.

Fuel transport moved in record numbers on a daily, monthly, and yearly level. This growth held despite the economic slowdown in the aftermath of September 11.

Gravel recovered from the slow activity in 2000, nearly matching record levels achieved in 1999. Robust construction and road-building industries contributed to the movement of 3.54 million tons of gravel in 2001. Projections for 2002 anticipate another year of solid performance in this sector.

Continued resource development on the North Slope and in the Interior also provided a strong market for the railroad. Shipments of pipe, other oilfield supplies, and mining supplies were up from 2000.

Coal shipments, which move south from Usibelli Coal Mine in Healy to Seward for export to Korea, and north to Fairbanks, were steady in 2001.

PASSENGER BUSINESS

The Passenger Services and Marketing & Logistics departments merged in July 2001 to enhance coordination of marketing, transportation services, and sales efforts.

The new division saw passenger travel levels on the Alaska Railroad remain comparable to 2000. Passenger revenues were up slightly. Given the fact that tourism dropped across the state in 2001, it was an accomplishment that the railroad did not experience a significant passenger reduction.

Contributing to passenger success was the continued marketing of a new service begun in late June 2000. The *Grandview* train transports cruise ship passengers from Seward to Anchorage. In Anchorage, the train picks up southbound cruise ship passengers and returns to ships docked in Seward. Almost every seat on the northbound trains was filled in 2001.

In 2001, for the 2002 season, we implemented a new passenger reservations and ticketing system, designed to be more user-friendly for customers and employees alike.

Looking to the future, the railroad plans to seek new opportunities for half- and full-day tours out of Anchorage, aiming towards the 2003 passenger season.

REAL ESTATE BUSINESS

The real estate business continued as a strong performer exceeding 2001 projected revenue by $300,000, generating

Passenger revenues were up slightly in 2001.

Cruise ship passengers enjoy the Grandview Train.

Children from Government Hill Elementary School board a Holiday Train, one of the many activities supported by the railroad as a school-business partner.

$10.57 million – thus breaking the $10 million revenue mark for the first time. New revenues from the Seward freight dock and increased Seward passenger dock activity were instrumental in achieving this new record.

Since re-acquiring the responsibility and general management of the historic Anchorage Depot office building, the ARRC Real Estate Department has been actively involved in the preservation and maintenance of the facility. In line with the corporation's focus on safety, the building has undergone a number of life, health, and safety upgrades. These include the addition of two fire escapes from the second and third floors, new domestic and wastewater plumbing, air conditioning, and the addition of fire alarm pull stations throughout the building. These and other tenant improvements have enhanced the building, resulting in full occupancy while preserving the historic nature of our depot.

An important real estate project involved the successful lease of tidelands from the Municipality of Anchorage and subsequent lease back to Williams Petroleum. This allowed construction of Williams' loop track project in the Anchorage Port area to move forward. When completed in 2002, the new loop track will accommodate entire fuel trains (about 70 cars) proceeding into the offloading area. Previously, trains had to be separated into several sections, causing day-long switching activities and traffic delays at several port and Ship Creek area road crossings.

The project increased lease revenue, contributing positively to the railroad's bottom line by converting tidelands to uplands.

Other tidelands adjacent to Ship Creek Point leased from the railroad now hold a new dock, which is home to tug boats serving Cook Inlet.

Ship Creek redevelopment in 2001 included the 90 percent completion of a new Plaza Park project across from the headquarters building. The project will be finished in 2002, helping the Ship Creek redevelopment progress.

Further north, previously vacant land in Fairbanks now holds a new building owned and operated by a local artist. The railroad completed the first phase of the Chena Pond excavation in Fairbanks and used extracted gravel to create a new pipe storage pad in the Fairbanks yard. This improvement will aid in moving pipe from tidewater to Fairbanks, its ultimate destination being the North Slope oil fields.

PROJECTS, ENGINEERING, TECHNOLOGY & SIGNALS

In order to more accurately reflect the scope of work conducted by the Capital Projects division, it was renamed Projects, Engineering, Technology & Signals (PETS) in July 2001.

Williams began construction of a loop track in order to accept entire fuel trains.

Increased Seward Dock passenger activity helped grow real estate revenues past $10 million.

The year 2001 was full of accomplishments. On the projects front, the Seward Dock, Whittier Underpass, South Anchorage Double Track, Anchorage Airport Rail Depot, Anchorage-Wasilla Line Changes, Southcentral Commuter Rail Study, and Fairbanks-North Pole Reconnaissance Study all saw significant progress or completion. (Descriptions of the 2001 Program of Projects follow in the next section). The 2002 construction season promises to be busier as we continue to invest in infrastructure in order to provide safer, more reliable service to customers.

The engineering staff met many challenges this year, from meeting complex federal grant regulations to the rigors posed by Alaska's extreme weather. Our engineers are taking lead roles in working directly with communities to resolve road-rail, trail-rail, and rail-river conflicts.

The technology staff made significant progress on upgrading infrastructure. They commenced a three-year plan to upgrade railroad computer systems, and they tapped new technology to move trains more efficiently through use of a computer aided dispatch system.

More sophisticated signalization was installed during the second of a five-year effort by the railroad to more clearly mark road-rail crossings, and to install numerous powered switches. Both efforts, which will continue in 2002, improve safety and increase efficiency.

2001 CAPITAL IMPROVEMENTS PROGRAM REVIEW

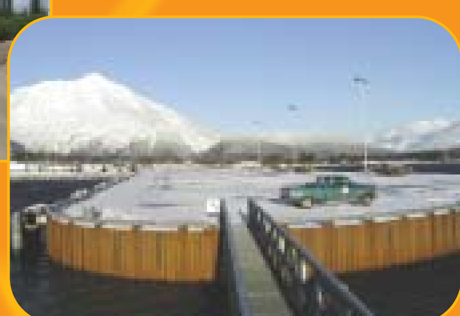
The Alaska Railroad continued to pursue a comprehensive program of capital improvements. The railroad is investing millions on rail, ties and ballast to aggressively upgrade infrastructure. Safety and efficiency improvements include projects to straighten the main track between Anchorage and Wasilla, build longer sidings (railroad "passing" lanes) and add automated and heated switches. The railroad is also capitalizing on opportunities to better serve Alaskans by renovating depots, and modernizing passenger services and equipment. Detailed descriptions of these projects are available on the railroad's website: www.AlaskaRailroad.com.

Funding for much of the capital projects program comes from federal grants received since 1996. Funds have come from the Federal Railroad Administration (FRA), Federal Transit Administration (FTA), Federal Highway Administration (FHWA) and Congressional earmarks through various agencies, such as the U.S. Forest Service. FTA-funded projects require 20 percent railroad matching funds.

SEWARD

Freight dock - In 2001, the railroad finished constructing a new freight dock located just east of the existing dock. The 640-by-200-foot bulkhead fill dock features a low maintenance ship fendering system, a mooring dolphin, and a catwalk at the seaward end. The project was funded by FRA, FHWA and the railroad.

The new Hurricane siding was completed in 2001 and included a powered switch.



The freight dock in Seward was completed in 2001.

Passenger dock - In conjunction with the freight dock project in 2001, the railroad began overhauling the existing dock to serve as a passenger-only facility. This will greatly improve safety and efficiency, and bring the existing facility into compliance with State and Federal regulations. Funded by FRA, FHWA and the railroad, the project included improvements to the passenger dock, including connection to the city sewer service.

Roundhouse - The Seward roundhouse (engine house) was upgraded to accommodate maintenance and custodial services for cruise trains operating between Seward and Anchorage. The project included installation of potable water stations, upgrade of electrical systems, a new office facility, and a train-washing apparatus with wash water collection, cleaning and recirculation. Completed in 2001, the project was funded 80 percent by FTA and 20 percent by the railroad.

WHITTIER

Whittier Intermodal Planning Study - The railroad commissioned an Intermodal Planning Study on improving passenger-related amenities to facilitate tourism growth in Whittier. Goals include better passenger and pedestrian safety, increased passenger service, segregated passenger and freight operations and construction of new passenger and maintenance facilities. Due for completion in 2002, the study and conceptual design is funded 80 percent by FTA and 20 percent by the railroad.

Pedestrian underpass - Part of the Whittier master plan called for a pedestrian underpass that would provide safe passage across the railyard, which lies between the town and the waterfront. Construction on the 300-foot-long, 10-foot-diameter underpass began in spring 2001. Funded 80 percent by FTA and 20 percent by the railroad, the project will be completed in spring 2002.

Equipment maintenance facility - Design was accomplished on a new equipment maintenance building in Whittier to be located in the southeast corner of the railyard. The 4,793-square-foot building will store and maintain heavy equipment, such as graders and bulldozers. Funded 80 percent by the FTA and 20 percent by the railroad, the project will be constructed in 2002.

Barge dock - Design was also completed on a project to accommodate unloading from the side of the railroad's existing barge dock. Construction of two 34-by-60-foot elevated platforms is scheduled to begin in spring 2002. Funded 100 percent by the railroad, the project will significantly improve safety and efficiency of barge operations.

ANCHORAGE

Anchorage airport rail station - Construction is well underway on a new rail terminal at the Ted Stevens Anchorage International Airport. The project includes construction of an elevated track leading to a 17,300-square-foot depot building. Funded 100 percent by FRA, the project is scheduled for completion by fall 2002.

The railroad began renovating the existing Seward general purpose dock into a renovated passenger-only facility.

Construction of the Airport Rail Station continued through 2001.

Anchorage airport spur / south leg of the wye - Construction began on a new "south leg of the wye," at the Airport Spur junction, which will allow southbound travel from the new airport rail station. The project improves the spur leading from Minnesota Drive to the airport. Funded by FRA, the project will be complete by summer 2002.

South Anchorage double track - Construction began on a project to add about five miles of new mainline track between 120th Avenue (near Klatt Road) and the Minnesota Drive overpass, within the railroad's right-of-way. The second track will improve efficiency and safety along the currently congested mainline through Anchorage. Funded 80 percent by FTA and 20 percent by the railroad the project, which includes signalization, will be complete in winter 2003.

North Ship Creek rail yard expansion - The railroad began excavating about 770,000 cubic yards from the North Ship Creek bluff to make room for new and realigned Anchorage Yard tracks. About 220,000 cubic yards of the material was used to fill about 8.5 acres of railroad-owned tideland at the Port of Anchorage to permit construction of the Williams fuel facility loop track. Funded by the railroad, phase one of the yard expansion project will be complete in 2003.

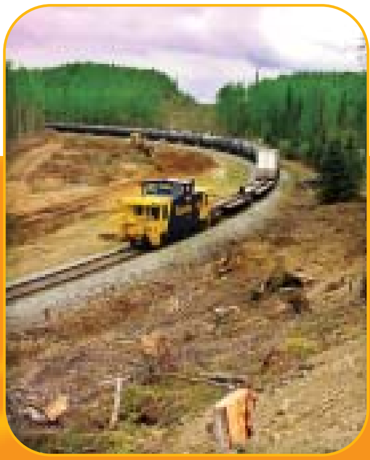
Anchorage yard passenger car shop - Preliminary design began on a new passenger car shop in the Anchorage Yard. The facility will accommodate the railroad's expanded fleet of passenger trains. Funded 80 percent by FTA and 20 percent by the railroad, the design and engineering effort will be complete in 2002.

Ship Creek intermodal - Planning got underway to conceptualize a Ship Creek area intermodal transportation hub that provides bus and rail facilities, pedestrian improvements, new rail platforms, bus/van stops, retail development, airport accommodations and visitor information. In 2002, the railroad plans to pursue preliminary concept work, organize public and agency scoping meetings, and conduct pre-NEPA studies and documentation. The study is funded 80 percent by FTA and 20 percent by the railroad.

Ship Creek pedestrian amenities - Design was complete and construction began on a pedestrian plaza at the corner of Ship Creek Avenue and North C Street. Funded by the Municipality of Anchorage and the railroad, the plaza project will be complete in spring 2002.

ANCHORAGE TO THE MAT-SU VALLEY

Anchorage to Wasilla track realignment - Efforts to straighten the track from Anchorage to Wasilla got underway in 2001, with the stretch from the Anchorage Yard through Elmendorf Air Force Base completed. When the entire project is done, the line along this stretch will



The railroad continued to realign track between Anchorage and Wasilla.

The railroad installed the first of its new state-of-the-art avalanche detection equipment in 2001.

allow for increased train speeds, and improved efficiency and safety. Administered by FRA, the Anchorage to Eagle River phase started construction in 2001 and should be complete in 2004. Funded 80 percent by FTA and 20 percent by the railroad, the Eagle River to Wasilla phase should enter construction in 2002, with completion in 2004.

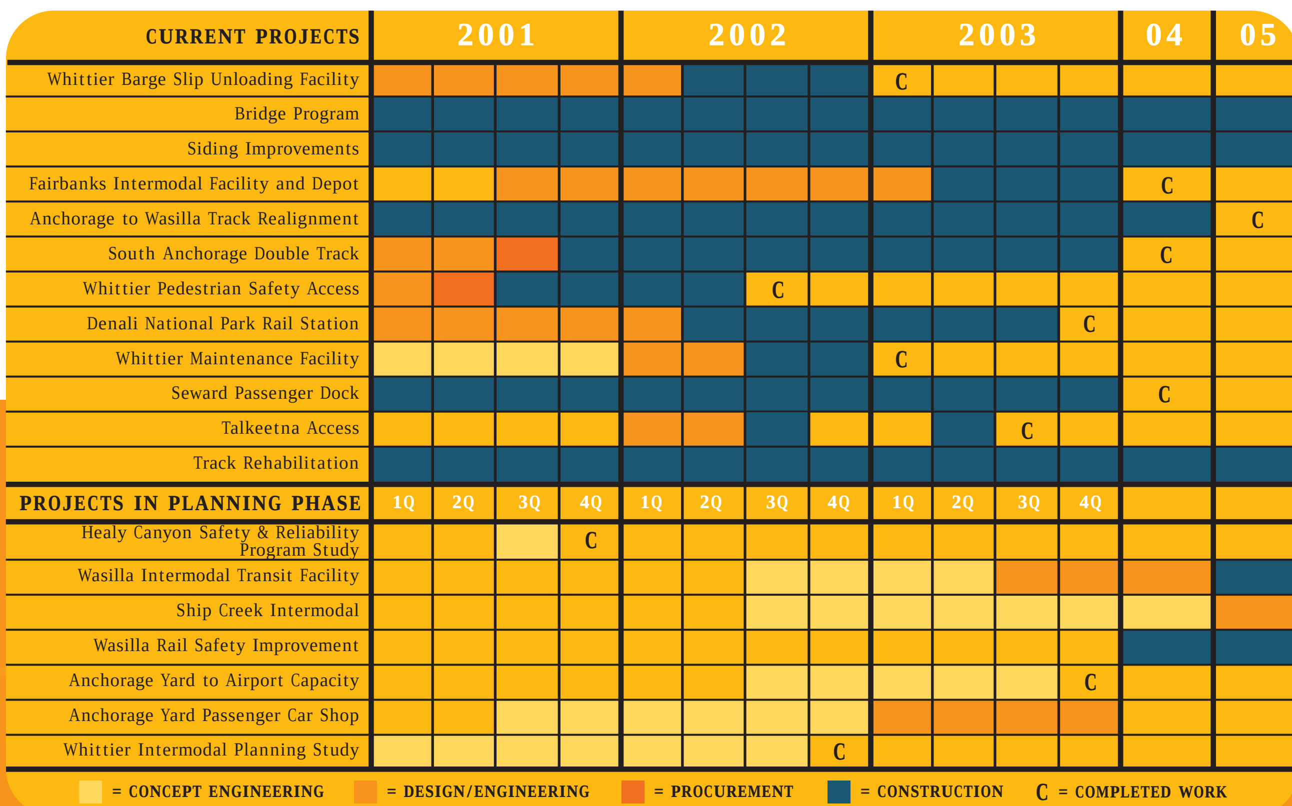
Commuter study - The railroad commissioned the Southcentral Rail Network Commuter Study and Operation Plan in 2000. Completed in 2001, the study creates a blueprint for potential further actions by local and state officials to establish a viable and operational commuter rail system. The study was 80 percent funded by FTA and 20 percent by ARRC. The plan, along with public comments, has been forwarded to FTA.

INTERIOR ALASKA

Denali National Park rail station - Design and engineering are underway to improve the passenger depot and surrounding facilities at Denali National Park. Construction of the project begins in spring 2002, with completion expected in 2004. Funding is 80 percent FTA and 20 percent railroad.

Fairbanks intermodal facility and depot - Preliminary design and engineering was completed on an intermodal facility and depot in Fairbanks. Proposed plans are to locate the new facility on a 32-acre site adjacent to the railroad operations yard, near the intersection of Johansen Expressway and Danby Road. Funded 80 percent by FTA and 20 percent by the railroad, the project will begin construction in 2003, with completion in 2004.

Fairbanks / North Pole Rail Relocation Study - The railroad commissioned a reconnaissance study on relocating the track in Fairbanks and North Pole to eliminate up to 48 rail/road crossings within the two communities. Public meetings to discuss proposed phased options are ongoing in 2002. Funded by FRA, the conceptual study will be complete in 2002. Project construction will depend on the options selected and funding availability.



SYSTEMWIDE SERVICE & EQUIPMENT

Passenger locomotives and car upgrades - Major upgrades to passenger locomotives and cars began in 1999 and continue as funding becomes available. Typical upgrade projects include the repainting and interior restoration of coaches, refurbishment of power generation cars, rehabilitation of railcar trucks, and the rebuild of three passenger locomotives. These projects are funded 80 percent by FTA and 20 percent by the railroad.

Passenger reservation system - In 2001, the Alaska Railroad acquired and installed a computer-based passenger reservations management system that provides integrated, flexible, cost-effective, and automated means of supporting and managing passenger travel. Funded 80 percent by FTA and 20 percent by the railroad, the project can accommodate current and projected needs, and capitalizes on consumer demand for Internet information and transactions. System modifications and personnel training will continue in 2002.

Avalanche program - In 2001, the railroad initiated a three-year program to improve existing avalanche risk management tools and create new control systems. The project involves integrated capital projects to upgrade: a) state-of-the-art detection and data acquisition and management systems, b) explosive delivery systems, c) equipment, and d) joint operations with the Alaska Department of Transportation & Public Facilities. The Avalanche Program is funded in part by a congressional earmark through the U.S. Forest Service.

Yard and terminal plans - During 2001, the railroad commissioned TransSystems and California-based Woodside Consulting Group to update the yard and terminal plans. This effort built on a 1999 Woodside comprehensive plan to improve efficiency, capacity and safety within Anchorage and Fairbanks yards, as well as the main track between the two terminals. Out of this analysis came a prioritized list of capital projects to be undertaken through the year 2005. The plan update is funded by the railroad and is expected to be complete in 2002.

SYSTEMWIDE INFRASTRUCTURE

Siding improvements - In 2001, the railroad continued a five-year Siding Access Plan to place remote control power switches and heaters at about 40 sidings between Seward and Fairbanks, to extend 13 existing sidings and to build seven new sidings. In 2001, FRA grant funds were used to build two new sidings. One was at Pittman – MP 166, just north of Wasilla. The other was at Bear Creek, MP 274, about 15 miles north of Healy.

Bridge program - The Alaska Railroad's 500-plus miles of mainline track includes 169 bridges that cross barriers ranging from trickling streams to plunging canyons. Funded by ARRC, the railroad's 2001 Bridge Program included major maintenance, overhaul and replacement projects needed to maintain railroad integrity, safety and efficiency.

BOARD OF DIRECTORS

(L to R back row)
Jack Burton
Track Inspector, Alaska Railroad Corporation

Jacob Adams
President and CEO, Arctic Slope Regional Corporation

Pat Gamble
President and CEO, Alaska Railroad Corporation

Joe Perkins, Vice Chairman
Commissioner of Transportation and Public Facilities

Ed Bauer
Professional Railway Consultant

(L to R front row)
Johne Binkley, Chairman
Chairman and CEO, Alaska Riverways, Inc.

Deborah Sedwick
Commissioner of Community and Economic Development

Carl Marrs
President and CEO, CIRI

MANAGEMENT STATEMENT

The management of the Alaska Railroad Corporation is responsible for the fair statement of the accompanying financial statements and all other information contained in the annual report. The financial statements were prepared in conformity with generally accepted accounting principles and prevailing railroad industry practices and reflect Management's judgments and estimates concerning effects of events and transactions that are accounted for or disclosed. The financial information contained elsewhere in the annual report is consistent with that in financial statements.

The Alaska Railroad Corporation maintains accounting systems that are supported by internal accounting controls. These systems and controls provide reasonable assurance that assets are safeguarded and that transactions are executed in accordance with Management's authorization and recorded properly to permit the preparation of financial statements in accordance with generally accepted accounting principles. The concept of reasonable assurance is based on the recognition that the cost of a system of internal control should not exceed the related benefits. Management believes the company's system provides this appropriate balance in all material respects.

The financial statements have been audited by KPMG LLP, independent certified public accountants, who are appointed by the Board of Directors. Their audit is conducted in accordance with generally accepted auditing standards which include an objective, outside review of operating results, financial condition, and the Corporation's system of internal controls. The opinion of the independent auditors is contained in this annual report.

The audit committee of the board of directors, composed solely of outside directors, meets with independent auditors and management periodically to discuss audit findings and other accounting and financial matters. The committee reviews the scope and results of the audit effort with the independent auditors as well as the annual financial statements and recommends their approval by the board of directors.

Bill O'Leary

Vice President, Finance and Chief Financial Officer

INDEPENDENT AUDITORS' REPORT

The Board of Directors
Alaska Railroad Corporation:

We have audited the accompanying balance sheets of the Alaska Railroad Corporation as of December 31, 2001 and 2000, and the related statements of income, equity and comprehensive income, and cash flows for the years then ended. These financial statements are the responsibility of the Corporation'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. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our 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 Alaska Railroad Corporation as of December 31, 2001 and 2000, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated March 1, 2002 on our consideration of the Alaska Railroad Corporation's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

KPMG LLP

March 1, 2002

ALASKA RAILROAD CORPORATION BALANCE SHEETS

December 31, 2001 and 2000

(In thousands)

Assets	2001	2000
Current assets:		
Cash and cash equivalents	$ 7,279	7,667
Accounts receivable, net of allowance for doubtful accounts of $586 in 2001 and $388 in 2000	10,167	11,378
Materials and supplies	5,013	4,547
Board designated assets (note 3)	—	95
Restricted assets (note 4)	9,454	2,313
Prepaid expenses and other current assets	326	289
Total current assets	32,239	26,289
Property and equipment:		
Road and roadway structures	123,996	115,401
Equipment	107,666	92,726
Road materials and supplies	5,772	4,486
Leasehold improvements (note 10)	1,728	963
Construction in progress	100,539	56,269
Accumulated depreciation and amortization	(88,850)	(76,965)
Total property and equipment, net	250,851	192,880
Land and improvements (note 10)	16,080	16,080
Board designated assets (note 3)	831	944
Restricted assets (note 4)	5,051	13,743
Investments (note 5)	996	1,508
Other assets	194	252
	$ 306,242	251,696

Liabilities and Equity		
Current liabilities:		
Current portion of long-term debt (note 6)	$ 2,242	2,088
Accounts payable and accrued liabilities (note 13)	6,443	8,293
Payroll liabilities	7,734	5,585
Unearned revenues (note 10)	3,295	2,703
Total current liabilities	19,714	18,669
Long-term debt, less current portion (note 6)	18,600	19,963
Accrued postretirement and pension benefits (note 7)	10,121	9,033
Environmental remediation reserve (note 13)	1,341	2,658
Deferred grant revenue (note 8)	141,102	92,104
Deferred revenue (note 4)	1,731	2,136
Total liabilities	192,609	144,563
Equity:		
Investment by the State of Alaska	34,174	34,174
Retained earnings	79,340	72,727
Accumulated other comprehensive income – net unrealized gain on securities available for sale	119	232
Total equity	113,633	107,133
Commitments and contingencies (notes 6, 7, 9, 11, 12 and 13)		
	$ 306,242	251,696

See accompanying notes to financial statements.

ALASKA RAILROAD CORPORATION STATEMENTS OF INCOME

Years ended December 31, 2001 and 2000

(In thousands)

	2001	2000
Operating revenue:		
Freight (note 9)	$ 79,868	70,084
Passenger	13,389	13,163
Other	239	726
	93,496	83,973
Grant revenue (note 8)	2,687	14,448
	96,183	98,421
Operating expense (note 8):		
Transportation	47,776	42,033
Maintenance	23,118	21,010
Mechanical	13,433	12,482
General and administrative	11,819	11,935
	96,146	87,460
Income from operations	37	10,961
Other income (expense):		
Real estate income, less direct expenses of $3,421 in 2001 and $2,915 in 2000 (note 10)	7,150	6,373
Interest income	555	913
Interest expense	(1,129)	(1,563)
	6,576	5,723
Net income	$ 6,613	16,684

See accompanying notes to financial statements.

STATEMENTS OF EQUITY & COMPREHENSIVE INCOME

Years ended December 31, 2001 and 2000

(In thousands)

	Investment by the State of Alaska	Retained earnings	Accumulated other comprehensive income	Total equity
Balance at December 31, 1999	$ 34,174	56,043	332	90,549
Comprehensive income:				
Net income	—	16,684	—	16,684
Change in unrealized holding gain on securities available for sale	—	—	(100)	(100)
Total comprehensive income				16,584
Balance at December 31, 2000	34,174	72,727	232	107,133
Comprehensive income:				
Net income	—	6,613	—	6,613
Change in unrealized holding gain on securities available for sale	—	—	(113)	(113)
Total comprehensive income				6,500
Balance at December 31, 2001	$ 34,174	79,340	119	113,633

See accompanying notes to financial statements.

ALASKA RAILROAD CORPORATION STATEMENTS OF CASH FLOWS

Years ended December 31, 2001 and 2000
(In thousands)

	2001	2000
Operating activities:		
Net income	$ 6,613	16,684
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	12,020	10,303
(Gain) loss on disposal of assets	14	(822)
Changes in assets and liabilities:		
(Increase) decrease in accounts receivable, net of allowance for doubtful accounts	1,211	(2,914)
(Increase) decrease in materials and supplies	(466)	46
Decrease in prepaid expenses and other assets	21	663
Decrease in accounts payable and accrued liabilities	(1,850)	(4,236)
Increase (decrease) in payroll liabilities	2,149	(994)
Increase (decrease) in unearned revenues	(173)	57
Decrease in environmental reserve	(1,317)	(492)
Increase in accrued postretirement and pension benefits	1,088	15
Decrease in deferred revenue	(405)	(13,378)
Net cash provided by operating activities	18,905	4,932
Investing activities:		
Purchases of property and equipment	(69,346)	(78,780)
Purchases of land improvements	—	(201)
Proceeds from sales of property and equipment	106	359
Decrease in board designated assets, net of unrealized gain on available-for-sale securities	95	13,114
(Purchase) sale of investments	512	(1,508)
Decrease in restricted assets	1,551	35,396
Increase in deferred grant revenue	48,998	31,527
Net cash used in investing activities	(18,084)	(93)
Financing activities:		
Payments on long-term debt	(2,209)	(2,018)
Proceeds from long-term debt	1,000	—
Net cash used in financing activities	(1,209)	(2,018)
Net increase (decrease) in cash and cash equivalents	(388)	2,821
Cash and cash equivalents at beginning of year	7,667	4,846
Cash and cash equivalents at end of year	$ 7,279	7,667
Supplemental disclosure of cash activity:		
Interest paid	$ 1,134	1,569
Supplemental disclosure of noncash activity:		
Leasehold improvements provided through rent credits	$ 765	963

See accompanying notes to financial statements.

ALASKA RAILROAD CORPORATION NOTES TO FINANCIAL STATEMENTS

December 31, 2001 and 2000

1. ORGANIZATION AND OPERATIONS

The United States Congress authorized construction of the Alaska Railroad (ARR) in 1914 and operations began in 1923. The federal government operated the railroad until its sale to the State of Alaska in January 1985. The sale of the ARR to the State of Alaska was authorized under the Alaska Railroad Transfer Act of 1982, which was signed into law on January 14, 1983. The Alaska Railroad Corporation (ARRC) is a corporation created by the State of Alaska legislature to own and operate the railroad and manage the railroad's rail, industrial, port and other properties. The ARRC commenced operations on January 6, 1985.

The ARRC operates 525 route miles, providing both freight and passenger services. The ARRC serves the cities of Anchorage and Fairbanks, the ports of Whittier, Seward, and Anchorage as well as Denali National Park and military installations. Vessel and rail barge connections are provided from Seattle, Washington, and Prince Rupert, British Columbia.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

In preparing the financial statements in accordance with accounting principles generally accepted in the United States of America management is required to make a number of estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities as of the date of the financial statements and revenue and expenses for the reporting period. Actual results could differ from these estimates. The more significant accounting and reporting policies and estimates applied in the preparation of the accompanying financial statements are discussed below.

(a) Basis of Accounting

The ARRC is subject to the jurisdiction of the Surface Transportation Board (STB). Accordingly, the ARRC has prepared the accompanying financial statements in accordance with the STB rules and regulations (US CFR Title 49), which are generally consistent with generally accepted accounting principles as promulgated by the Financial Accounting Standards Board.

(b) Cash and Cash Equivalents

For purposes of the statements of cash flows, cash and cash equivalents include time deposits, money market accounts and repurchase agreements with original maturities of three months or less.

(c) Materials and Supplies

Materials and supplies inventories are carried at the lower of average cost or market. Road materials and supplies include rail, ties, ballast, and other track materials. These items will generally be capitalized when placed into service, and accordingly are included in operating property and equipment.

(d) Property and Equipment

Property and equipment is stated at cost. Depreciation and amortization is computed on the straight-line basis over the estimated useful lives of the related assets, ranging from 3 to 32 years.

(e) Board Designated Assets

Board designated assets represent investment securities held by the ARRC in anticipation of funding future postretirement benefits and equipment purchases. Management has both the ability and intent to hold the investment securities designated for equipment purchases to maturity, and accordingly, has elected to account for them at amortized cost under Statement of Financial Accounting Standards (SFAS) No. 115, *Accounting for Certain Investments in Debt*

(Continued)

and Equity Securities. Investment securities designated for postretirement benefits are invested in equity mutual funds and are accounted for as available for sale securities under SFAS No. 115. Available for sale securities are stated at fair value with unrealized holding gains and losses excluded from earnings and reported as a separate component of other comprehensive income.

(f) Restricted Assets

Restricted assets represent investment securities held by the ARRC in anticipation of the approval of future capital projects. Management has both the ability and intent to hold the investment securities to maturity, and accordingly has elected to account for them at amortized cost under SFAS No. 115. Funds received but not yet expended are recorded as deferred revenue.

(g) Investments

Management has both the ability and intent to hold investment securities to maturity and, accordingly, has elected to account for them at amortized cost under SFAS No. 115.

(h) Grants

Grant revenue is recorded in the same period as expenses related to the grant. Grant funds received but not yet expensed are recorded as deferred grant revenue.

(i) Income Taxes

As a corporation owned by the State of Alaska, the ARRC is exempt from Federal and State income taxes.

(j) Environmental Remediation Costs

The Corporation accrues for losses associated with environmental remediation obligations when such losses are probable and reasonably estimable. Costs of future expenditures for environmental remediation liabilities are not discounted to their present value.

(k) Fair Value of Financial Instruments

Fair values of financial instruments, as defined under SFAS No. 107, *Disclosures About Fair Value of Financial Instruments*, are estimated by the ARRC's management. Fair values of restricted assets and related deferred revenue are based on quoted market prices, when available, and quoted market prices of comparable instruments, when not available. Fair values for accounts receivable are estimated using cash flows in comparison to assets with similar estimated average lives but bearing current market interest rates. Fair values of long-term debt are based on the discounted value of contractual cash flows and interest rates being offered for similar debt. ARRC has determined the fair values of financial instruments do not differ significantly from their carrying amounts with the exception of investments which are discussed in notes 3, 4 and 5, and debt, which is estimated to have a fair value of $22,568,000 at December 31, 2001.

(l) Comprehensive Income

Comprehensive income consists of net income and net unrealized gains and losses on securities and is presented in the statement of equity and comprehensive income.

(m) Reclassifications

Certain reclassifications not affecting net income have been made to 2000 numbers in order to conform them to current year presentation.

3. BOARD DESIGNATED ASSETS

Board designated assets at December 31, 2001 and 2000 consist of the following (in thousands):

Description of Security	Amortized cost	Unrealized gains	Unrealized losses	Market value
2001:				
Available for sale –				
Equity mutual fund	$ 712	119	—	831
2000:				
Held to maturity –				
Money market accounts	$ 95	—	—	95
Available for sale –				
Equity mutual fund	$ 712	232	—	944

These assets are designated for postretirement benefits (note 7).

4. RESTRICTED ASSETS

The ARRC received $9,000,000 from the State of Alaska in 1990 for the purchase of locomotives and coal hopper cars for the Wishbone Hill Coal project. Any remaining funds, along with interest earned on the $9,000,000 while in the possession of the ARRC, may be used to purchase other equipment and improvements related to the project. This contribution from the State of Alaska is accounted for as deferred revenue, which will be amortized over the life of the project. During 2000 the ARRC reached an agreement with the State of Alaska where $8,191,000 was returned to the State of Alaska and $5,489,000 was authorized for the purchase of equipment (note 8). The remaining balance and interest thereon totaled $1,495,000 and $1,869,000 at December 31, 2001 and 2000, respectively, and is reported as restricted assets and deferred revenue.

Also included in restricted assets is $259,000 and $267,000 at December 31, 2001 and 2000, respectively, received in 1990 from the Department of Natural Resources. These funds are being managed by the ARRC in anticipation of future capital projects. If no capital projects are undertaken, the funds, including accrued interest, would be returned to the Department of Natural Resources.

As part of the 1997 Taxpayer Relief Act passed by the U.S. Congress, states without Amtrak service are due a benefit to be spent on passenger service improvements in lieu of the tax benefits received through Amtrak subsidies over the years. The ARRC received Alaska's $23,230,000 share of this benefit. The unspent portion of the amount received, along with investment income thereon, is reported as deferred grant revenue (note 8). These restricted assets totaled $10,500,000 and $11,607,000 at December 31, 2001 and 2000, respectively.

ARRC has received grants from the U.S. Department of Interior and the U.S. Department of Agriculture. The amounts received in excess of the amounts spent on the grant programs are reported as deferred grant revenue (note 8). These restricted assets totaled $2,251,000 and $2,313,000 at December 31, 2001 and 2000, respectively.

Restricted assets considered held to maturity at December 31, 2001 and 2000 consisted of the following (in thousands):

Description of Security	Amortized cost	Unrealized gains	Unrealized losses	Market value
2001:				
Money market accounts	$ 4,296	—	—	4,296
U.S. Agency notes (maturing within one year)	5,158	77	—	5,235
U.S. Agency notes (maturing in 1-5 years)	5,051	39	—	5,090
Total	$ 14,505	116	—	14,621
2000:				
Money market accounts	$ 4,901	—	—	4,901
U.S. Agency notes (maturing within one year)	7,080	—	(56)	7,024
U.S. Agency notes (maturing in 1-5 years)	4,075	—	(39)	4,036
Total	$ 16,056	—	(95)	15,961

5. INVESTMENTS

Investments considered held to maturity at December 31:

Description of Security	Amortized cost	Unrealized gains	Unrealized losses	Market value
2001:				
U.S. Agency notes (maturing in 1-5 years)	$ 633	19	—	652
Corporate notes (maturing in 1-5 years)	363	2	—	365
Total	$ 996	21	—	1,017
2000:				
U.S. Agency notes (maturing in 1-5 years)	1,136	—	(24)	1,112
Corporate notes (maturing in 1-5 years)	372	18	—	390
Total	$ 1,508	18	(24)	1,502

6. LONG-TERM DEBT AND NOTES PAYABLE

Long-term debt at December 31, 2001 and 2000 consists of the following (in thousands):

	2001	2000
Note payable, secured by equipment, due in monthly payments of $165,936, including interest at 5.38%, matures September 2014.	$ 18,123	19,086
Note payable, secured by equipment, due in monthly payments of $74,173, including interest at 4.28%, matures September 2003.	1,498	2,305
Note payable, secured by equipment, due in monthly payments of $30,603, including interest at 4.28%, matures October 2003.	343	660
Note payable, secured by vehicles and equipment, due in monthly payments of $18,415, including variable interest, matures April 2006.	878	—
	20,842	22,051
Less current portion	2,242	2,088
	$ 18,600	19,963

ARRC has met all debt covenants at December 31, 2001.

Long-term debt maturities are as follows at December 31, 2001 (in thousands):

Year ending December 31	Amount
2002	$ 2,242
2003	2,093
2004	1,343
2005	1,411
2006	1,309
2007 and beyond	12,444
	$ 20,842

The ARRC has arrangements for three short-term unsecured lines of credit. The general purpose line of credit allows borrowing up to $10,000,000 at a rate of 56% of the prime rate of a major bank. The self-insurance line of credit allows borrowing up to $10,000,000 at a rate of 56% of the prime rate of a major bank. The non-revolving equipment line of credit allows borrowing up to $5,000,000, limited to $1,000,000 annually, at a rate of 56% of the prime rate of a major bank. None of the lines of credit had an outstanding balance as of December 31, 2001.

7. EMPLOYEE BENEFITS

(a) Defined Benefit Plan

The ARRC has a defined benefit pension plan (Plan) covering all regular represented and nonrepresented employees who are not covered by the Civil Service Retirement System. Benefits under this Plan are based upon the employee's years of service and final average compensation. The ARRC's funding policy is to contribute each year an amount equal to the net periodic pension cost. In 2001 and 2000, the ARRC contributed an amount for the periodic pension cost which was net of a prepaid pension amount. Employees contribute an amount equal to 9% of compensation. Contributions are made continuously throughout the year. Plan assets are comprised of fixed income securities and common stocks.

The following table sets forth the Plan's funded status at December 31 (in thousands):

	2001	2000
Change in benefit obligation:		
Benefit obligation at beginning of year	$ 28,558	24,072
Service cost	722	379
Interest cost	2,054	1,890
Participant contributions	2,175	1,836
Actuarial loss	418	1,073
Benefits paid	(934)	(692)
Benefit obligation at end of year	32,993	28,558
Change in plan assets:		
Fair value of plan assets at beginning of year	33,924	31,974
Actual return on plan assets	(1,929)	806
Participant contributions	2,175	1,836
Benefits paid	(934)	(692)
Fair value of plan assets at end of year	33,236	33,924
Funded status	243	5,366
Unrecognized net actuarial gain	(1,687)	(7,091)
Unrecognized prior service cost	808	881
Unrecognized transition asset	—	61
Accrued benefit cost	$ (636)	(783)

The following table sets forth the Plan's weighted average assumptions used in determining the actuarial present value of the projected benefit obligation at December 31:

	2001	2000
Discount rate	7.25%	7.50%
Expected return on plan assets	8.00%	8.00%
Rate of compensation increase	4.00%	4.00%

Components of net pension costs are as follows (in thousands):

	2001	2000
Service cost	$ 722	379
Interest cost	2,054	1,890
Expected return on plan assets	(2,758)	(2,602)
Amortization of prior service costs	73	73
Amortization of unrecognized transition obligation	61	61
Recognized net actuarial gain	(300)	(482)
Net periodic benefit cost	$ (148)	(681)

(b) Civil Service Retirement System

Federal employees who transferred to the ARRC continue to participate in the Civil Service Retirement System (CSRS), a multi-employer defined benefit plan. ARRC is required to contribute 8.5% of the transferred employees' base pay. Pension expense related to CSRS was $729,000 and $765,000 for the years ended December 31, 2001 and 2000, respectively.

(c) Postretirement Benefits Other Than Pension

The ARRC sponsors a defined benefit health care plan (Plan) that provides postretirement medical benefits to employees receiving retirement under the corporate retirement plan and retired CSRS employees who do not qualify for the federal medical insurance. The Plan is contributory, with retiree contributions adjusted annually, and contains other cost-sharing features such as deductibles and coinsurance. The accounting for the Plan anticipates future cost-sharing changes to the written plan that are consistent with ARRC's expressed intent to increase the retiree contribution rate by the amount of that year's premium increase. ARRC's policy is to fund the cost of medical benefits in amounts determined at the discretion of management. At December 31, 2001 and 2000, the ARRC has designated assets with a market value of $831,000 and $944,000, respectively, for the funding of these benefits (note 3).

The ARRC accounts for postretirement health care by accruing these benefits over the period in which active employees become eligible for such postretirement benefits. The following table sets forth the Plan's funded status at December 31 (in thousands):

	2001	2000
Change in benefit obligation:		
Benefit obligation at beginning of year	$ 7,055	4,595
Service cost	912	584
Interest cost	550	417
Actuarial loss	819	1,659
Benefits paid	(200)	(200)
Benefit obligation at end of year	9,136	7,055
Funded status	(9,136)	(7,055)
Unamortized prior service costs	(218)	(245)
Unrecognized net actuarial gain	(131)	(950)
Accrued benefit cost	$ (9,485)	(8,250)

The components of net periodic cost for these postretirement benefits are as follows (in thousands):

	2001	2000
Service costs	$ 912	584
Interest costs	550	417
Recognized prior service costs	(27)	(27)
Recognized net actuarial gains	—	(78)
Net periodic cost	$ 1,435	896

For measuring the 2001 expected postretirement benefit obligation, a 9.25% annual rate of increase in the per capita claims cost was utilized. This rate was assumed to decrease over a three-year period to an ultimate rate of 5.50% in 2004.

For measuring the 2000 expected postretirement benefit obligation, a 9.25% annual rate of increase in the per capita claims cost was utilized. This rate was assumed to decrease over a three-year period to an ultimate rate of 5.50% in 2003.

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

	2001		2000	
	One percentage point increase	One percentage point decrease	One percentage point increase	One percentage point decrease
Effect on total service and interest cost components	$ 411	(308)	260	(197)
Effect on postretirement benefit obligation	2,227	(1,698)	1,719	(1,313)

8. GRANTS

The ARRC has spent grant funding on a variety of operating property and equipment. Grant revenue will be recognized equal to depreciation on these assets each year. The original cost of assets constructed with grant funding as of December 31, 2001 consists of the following (in thousands):

Road and roadway structures	15 – 32 year life	$ 30,261
Equipment	5 – 25 year life	21,936
Construction in process		92,144
		$ 144,341

Deferred grant revenue as of December 31 consists of the following (in thousands):

	2001	2000
Federal Railroad Administration:		
Net book value of assets constructed	$ 25,062	26,533
Construction in process	70,610	32,882
Amount receivable from grantor	(5,300)	(3,362)
Taxpayer Relief Act:		
Net book value of assets purchased and constructed	6,830	5,039
Construction in process	8,368	9,112
Grant funding received in advance	7,496	8,937
Investment earnings on funding	2,729	2,136
Federal Transit Administration:		
Net book value of assets purchased and constructed	8,412	1,782
Construction in process	10,627	6,866
Amount receivable from grantor	(1,691)	(3,458)
Federal Emergency Management Agency:		
Net book value of assets constructed	222	230
Grant funding received in advance	31	31
Department of Interior:		
Grant funding received in advance	1,569	2,313
Accrued derailment expense (note 13)	(1,569)	(2,313)
Department of Agriculture:		
Construction in process	1,492	—
Grant funding received in advance	504	—
State of Alaska Wishbone Hill Coal Project:		
Net book value of assets purchased	5,119	5,376
Construction in process	853	308
Amount receivable from grantor	(456)	(308)
Municipality of Anchorage Ship Creek Economic Development – Construction in process	194	—
	$ 141,102	92,104

The ARRC recognized the following grant revenue during the years ended December 31 (in thousands):

		2001	2000
Federal Railroad Administration –			
Depreciation on assets constructed	$	1,471	1,472
Taxpayer Relief Act:			
Depreciation on assets purchased and constructed		364	141
Grant funded project planning expense		4	1
Federal Transit Administration –			
Depreciation on assets purchased and constructed		603	96
Federal Emergency Management Agency:			
Depreciation on assets constructed		8	8
Grant funding of 1999 derailment expense (note 13)		—	3,323
Department of Interior:			
Grant funding of 1999 derailment expense (note 13)		—	6,981
Grant reduction		(20)	—
Grant funding of accrued derailment expense (note 13)		(724)	2,313
Derailment expense paid in current year		724	—
State of Alaska Wishbone Hill Coal Project –			
Depreciation on assets purchased		257	113
	$	2,687	14,448

9. MAJOR CUSTOMER

One ARRC customer accounted for 45% and 48% of freight revenue in 2001 and 2000 respectively.

10. LAND

The ARRC leases a significant portion of its land to various parties under long-term agreements. Rental income on these leases, which is included in Real Estate income, was $8,553,000 and $7,831,000 in 2001 and 2000, respectively. The following table summarizes future minimum lease payments receivable as of December 31, 2001 (in thousands):

Year ending December 31		Amount
2002	$	7,918
2003		7,429
2004		7,272
2005		7,162
2006		7,064
Thereafter		128,693
	$	165,538

The ARRC has $1,676,000 in rent credits outstanding on these leases at December 31, 2001. The assets provided by tenants in exchange for the rent credits are included in property and equipment and are depreciated over their useful lives. The balance of the rent credits is included in unearned revenue.

11. OPERATING LEASES AND AGREEMENTS

The ARRC leases its headquarters, certain operating equipment, and barge services under operating leases and agreements. Payments under the leases and agreements totaled $12,629,000 and $15,355,000 in 2001 and 2000, respectively. Future minimum lease payments as of December 31, 2001 are summarized as follows (in thousands):

Year ending December 31	Amount
2002	$ 11,730
2003	10,570
2004	10,447
2005	10,414
2006	10,405
Thereafter	43,965
	97,531
Amounts to be received under non-cancelable sub-leases	4,798
	$ 92,733

12. INSURANCE

The ARRC is self-insured to certain limits for employee health benefits, personal injury, property and casualty damage claims and establishes reserves for the estimated losses of such claims. The ARRC is also self-insured against workers' compensation claims. The ARRC carries commercial insurance policies limiting ARRC's exposure for health benefits to $4.6 million, for casualty/liability to $5 million and for property to $10 million at December 31, 2001.

13. COMMITMENTS AND CONTINGENCIES

During 1992, the EPA filed a complaint seeking to fine the ARRC for alleged violations of the Resource Conservation and Recovery Act in relation to storing hazardous wastes at the Anchorage rail yard. A consent agreement was executed during 1994 settling the alleged violations. The accrual included in the financial statements does not reflect any costs to clean up any contamination in the area covered by the settlement. No contamination has been discovered, but the ARRC believes most, if not all, contamination in this area would have occurred prior to the transfer of the ARRC from the federal government to the State of Alaska. That liability for contamination will be ultimately imposed on the federal government under the transfer act and a 1990 agreement between the federal government and the ARRC.

During 1999, two derailments resulted in fuel spills along the ARRC tracks at Canyon and at Gold Creek. The ARRC is responsible for the remediation, restoration and monitoring of environmental contamination at these sites. The ARRC has accrued its best estimate of its remaining obligation with respect to the sites which was $2,104,000 and $5,067,000 at December 31, 2001 and 2000, respectively. Of the amount accrued at December 31, 2001, $763,000 is expected to be paid during 2002 and is included in accounts payable and accrued liabilities. The remaining $1,341,000 is expected to be incurred through 2004 and is reported as environmental remediation reserve. The total expense relating to these derailments and reflected in the statement of operations was $12,853,000 during 1999. During 2000 management reviewed the reasonableness of the estimated remaining obligation and recorded additional expense of $2,313,000. During 2001 management reviewed the reasonableness of the estimated remaining obligation and reduced expense by $659,000. Also during 2000 the ARRC received two federal grants to cover costs associated with the Gold Creek derailment and the 1999/2000 winter storm disaster. These grants, totaling $12,647,000, are reflected in the 2000 statement of operations as grant revenue. One of these grants was reduced by $20,000 during 2001. As of December 31, 2001, $11,058,000 of these grants have been used to reimburse ARRC for 1999 and 2000 expenses and the remaining $1,569,000 is reserved to cover a portion of the ARRC's remaining obligation. The aggregate undiscounted amount has been recorded since it represents management's best estimate of the cost, but the payments are not considered to be fixed and reliably determinable. The estimate of costs and their timing of payment could change as a result of changes to the remediation plan, changes in technology available to treat the site and unforeseen circumstances existing at the site. It is not possible to estimate the amount losses may exceed amounts accrued at this time as a result of these factors.

The ARRC has entered into permit agreements allowing the installation of fiber optic cables along the ARRC right-of-way corridor in exchange for payments over a 35-year period. The lessee under these agreements has claimed that pursuant to the federal Telecommunications Act of 1996 the ARRC may only charge the actual costs it incurs as a result of having the fiber optic cable on the right-of-way. Legal counsel and management of the ARRC believe the ultimate outcome, if the claim is determined to be valid, will not have a material adverse impact on the ARRC's financial position. At this point in time, it is not possible to assess the validity of the claim, or to estimate the amount of loss, if any.

Approximately 79% of the ARRC's labor force is subject to one of five collective bargaining agreements. One of the agreements, representing 25% of the labor force, expired on December 31, 2000 and is being renegotiated. Another agreement, representing 2% of the labor force, expires in 2002.

The ARRC is a defendant in various legal proceedings related to the conduct of its business. Provision has been made in the financial statements for probable losses, if any, from such litigation. In the opinion of management, the outcome of the litigation will not have a material effect on the financial position of the ARRC.

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Yard Office	1888 Fox Avenue	(907) 458-6022	(907) 458-6052
Freight House	1888 Fox Avenue	(907) 458-6048	(907) 458-6061

Seward, Alaska

913 Port Avenue, P.O. Box 95, Seward, Alaska 99664
Telephone: (907) 224-5552 or 265-2696
Fax: (907) 265-2660

Seattle, Washington

5615 W. Marginal Way S.W., Seattle, WA 98106
Telephone: (206) 767-1100
Fax; (206) 767-1112

800 Numbers	Within Alaska (Outside Anchorage)	From Lower 48
Freight Customer Service	1-800-478-2442	1-800-247-3153
Freight Marketing	1-800-321-6518	1-800-321-6518
Passenger Service	1-800-544-0552	1-800-544-0552
Seattle Office	1-800-843-2772	1-800-843-2772

The Alaska Railroad Corporation has not received any bona-fide offers of a sale arrangement within the calendar year of 2001, nor is the Corporation aware of any potential sales that require analysis under AS 42.40.260

ALASKA RAILROAD CORPORATION

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907.265.2300
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