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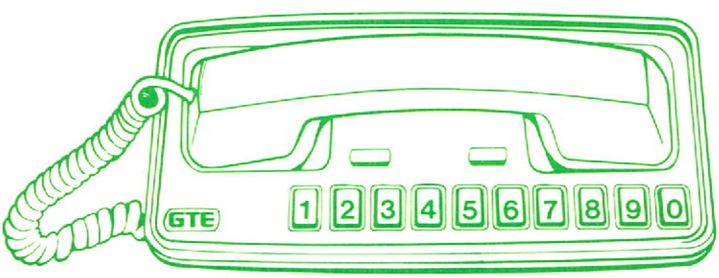
Anglo-Canadian Telephone Company

8750 CÔTE-DE-LIESSE ROAD, SAINT-LAURENT, QUEBEC H4T 1H3



ANNUAL REPORT 1984

ANGLO-CANADIAN TELEPHONE COMPANY

(Incorporated under the Quebec Companies Act)

Directors

ROGER CHARBONNEAU
JOHN H. E. COLBY
WILFRED R. JOYCE
CHARLES R. LEE
JOEL P. MELLIS
TIMOTHY P. MURPHY

Officers

CHARLES R. LEE
President

WILFRED R. JOYCE
Vice-President, Secretary and Treasurer

JOEL P. MELLIS
Assistant Secretary

LYLE E. ORSTAD
Assistant Treasurer

Transfer Agents and Registrars

CUMULATIVE PREFERRED STOCK
The Royal Trust Company, Montreal, Quebec, Canada
Co-Transfer and Co-Registrar Offices at
Toronto, Winnipeg, Vancouver, Saint John, Halifax and Calgary

COMMON STOCK
The Company

Si vous préférez recevoir ce rapport en français, veuillez vous adresser au secrétaire,
La Compagnie de Téléphone Anglo-Canadienne, 8750 Chemin Côte-de-Liesse, Saint-Laurent, Qué. H4T 1H3

To the Shareholders:

March 18th, 1985

Consolidated revenues and sales for 1984 increased to $1,492 million from $1,463 million a year ago, while consolidated net income was $58 million compared with $32 million last year. The increased net income in 1984 reflects the receipt of $15 million of dividends from our unconsolidated telephone subsidiary operating in the Dominican Republic, which was fully reserved in 1983 by an extraordinary charge to income of $13 million.

Income from Canadian operations showed a modest improvement in our telecommunications business. However, this was offset by a decline in manufacturing operations which were adversely affected by lower sales and higher expenses related to the discontinuance of several unprofitable product lines and the introduction of new products offering greater potential for future profit and growth.

Telecommunications revenues increased 5% to $1,322 million from $1,256 million and income from telecommunications operations rose 4% to $127 million. The improvement in operating results reflects increased long-distance calling volumes, rate increases and a modest gain in customer lines, partially offset by higher interest costs. Long-distance calling volumes increased 4.1% this year compared with an increase of 3.3% in 1983. Customer lines grew 2.4% to 1,607,059 by year-end compared with a gain of 2.5% last year.

Manufacturing sales of $170 million declined reflecting the discontinuance of several unprofitable product lines during the year, including single-line telephone sets. The lower sales coupled with costs related to the development of new products and market segments resulted in a net loss for these operations in 1984.

Capital expenditures for expansion and improvement of facilities amounted to $351 million in 1984, 9% lower than the $385 million spent in 1983. Capital expenditures for 1985 are estimated at $396 million.

Financial highlights of our major Canadian subsidiaries are reviewed below.

British Columbia Telephone Company

British Columbia Telephone Company, 40.30% owned by Anglo and 10.08% by Anglo's Parent, GTE Corporation, showed a 4% decline in net income to $102.5 million and earnings per ordinary share were $2.07, 12% lower than 1983 when there were 9% fewer average shares outstanding. The 1984 results reflect a modest increase in telecommunications operations, offset by a decline in manufacturing operations due to lower sales, as well as higher costs due to the factors previously mentioned. Revenues increased to $1,318 million from $1,298 million, reflecting increased long-distance calling, growth in customer lines and an interim rate award, which were partially offset by the lower manufacturing sales.

Net capital expenditures for new plant and equipment during 1984 were $322 million, down 10% from 1983 and total investment in plant at the end of 1984 amounted to $3.7 billion. Long-distance calling increased 3.9% in 1984 compared with a 3% increase last year, and customer lines in service were 1,391,308 at year-end, a gain of 2.3% compared with 2.6% in 1983.

Quebec-Telephone

Quebec-Telephone, 50.56% owned by Anglo, earned $19.3 million, essentially the same as last year and earnings per share were $3.71 compared with $3.97 in 1983 when there were 7% fewer average shares outstanding. The results this year reflect a 7% increase in operating revenues to $164 million, offset by higher costs, including increased depreciation rates. The higher revenues in 1984 reflect increased long-distance calling, up 5.4%, and a 3% gain in customer lines, which brought total customer lines in service to 215,751 at year-end.

Net capital expenditures amounted to $29 million in 1984, 4% more than the $28 million spent last year, and total plant investment was $477 million at year-end.

We wish to acknowledge the dedicated efforts of our management and staff and we continue to remain optimistic for the future.

On behalf of the Board of Directors

Charles R. Lee

President

Consolidated Balance Sheets

As at December 31, 1984 and 1983

Assets

	1984	1983
	(Thousands of dollars)	
FIXED ASSETS:		
Telecommunications property, substantially at original cost	$4,173,521	$3,963,951
Accumulated depreciation	(1,270,671)	(1,164,726)
	2,902,850	2,799,225
Manufacturing property, at cost	78,825	69,128
Accumulated depreciation	(34,495)	(32,147)
	44,330	36,981
INVESTMENTS	9,869	6,701
CURRENT ASSETS:		
Cash and short-term deposits	6,779	3,185
Receivables	218,368	235,732
Inventories	60,455	46,370
Other	24,294	11,339
	309,896	296,626
DEFERRED CHARGES:		
Unamortized cost of issuing long-term debt	2,689	2,519
Unamortized loss on foreign exchange	14,439	11,686
Other	666	510
	17,794	14,715
	$3,284,739	$3,154,248

Signed on behalf of the Board:

J. H. E. Bell, Director   Charles R. Lee, Director

The accompanying notes form an integral part of these consolidated financial statements.

Shareholders' Equity and Liabilities

	1984	1983
	(Thousands of dollars)	
SHAREHOLDERS' EQUITY:		
Anglo-Canadian Telephone Company:		
Preferred and preference shares (See page 8)	$ 37,500	$ 37,500
Common shares (Note 2)	12,037	12,037
Premium on common shares	34,218	34,218
Reinvested earnings	321,338	308,073
Contributed surplus	1,538	1,288
	406,631	393,116
Minority interest in consolidated subsidiaries:		
Preferred and preference shares (See page 8)	282,472	293,709
Common shares and reinvested earnings	543,529	458,719
	826,001	752,428
	1,232,632	1,145,544
LONG-TERM DEBT (See page 8)	1,174,337	1,137,598
CURRENT LIABILITIES:		
Loans for construction expected to be refinanced	57,006	47,429
Current portion of long-term debt	3,190	21,508
Accounts payable and accrued liabilities	222,943	184,253
Advance billings and customer deposits	52,384	50,100
Dividends payable	16,230	13,916
Accrued interest	35,814	26,432
Income taxes payable	6,833	49,773
	394,400	393,411
DEFERRED INCOME TAXES	483,370	477,695
COMMITMENTS AND CONTINGENT LIABILITIES (Note 4)		
	$3,284,739	$3,154,248

Consolidated Statements of Income

For the years ended December 31, 1984 and 1983

	1984	1983
	(Thousands of dollars)	
TELECOMMUNICATIONS OPERATIONS		
Operating Revenues:		
Toll service	$ 745,900	$ 698,404
Local service	502,703	495,321
Miscellaneous	73,405	62,542
	1,322,008	1,256,267
Operating Expenses:		
Operations	717,705	670,907
Depreciation	265,248	254,777
Income taxes	104,883	109,500
	1,087,836	1,035,184
Operating Earnings	234,172	221,083
Other income	5,994	7,282
Allowance for funds used during construction	20,145	17,303
Income before interest charges	260,311	245,668
Interest charges	133,668	123,808
Income from telecommunications operations	126,643	121,860
MANUFACTURING OPERATIONS		
Sales	170,400	206,530
Costs and expenses:		
Cost of sales	146,031	170,695
Selling and administrative expenses	28,388	23,581
Interest charges	6,294	4,488
Income taxes (recovery)	(6,773)	1,643
	173,940	200,407
Income (loss) from manufacturing operations	(3,540)	6,123
Combined income before minority interest	123,103	127,983
Minority interest in net income and preferred and preference dividends of subsidiaries	79,340	82,254
Income from Canadian operations	43,763	45,729
Dividends from unconsolidated subsidiary	14,508	—
Consolidated income before extraordinary item	58,271	45,729
Extraordinary item (Note 1)	—	13,301
Consolidated net income	$ 58,271	$ 32,428

The accompanying notes form an integral part of these consolidated financial statements.

Consolidated Statements of Reinvested Earnings

For the years ended December 31, 1984 and 1983

	1984	1983
	(Thousands of dollars)	
BALANCE AT BEGINNING OF YEAR	$308,073	$303,042
ADD —		
Consolidated net income	58,271	32,428
	366,344	335,470
DEDUCT —		
Dividends paid on Common Shares	42,500	25,000
Dividends paid on Cumulative Preferred Shares:		
4½% Cumulative Preferred Shares	281	281
$2.90 Cumulative Preferred Shares	363	363
$2.65 Cumulative Preferred Shares	848	848
$3.15 Cumulative Preferred Shares	567	567
Share issue expenses of consolidated subsidiaries	447	338
	45,006	27,397
BALANCE AT END OF YEAR	$321,338	$308,073

Consolidated Statements of Changes in Financial Position

For the years ended December 31, 1984 and 1983

	1984	1983
	(Thousands of dollars)	
CAPITAL EXPENDITURES AND OTHER REQUIREMENTS		
Capital expenditures	$351,413	$385,348
Working capital increase, excluding construction loans	21,858	21,659
Other — net	11,387	(5,175)
Total	384,658	401,832
INTERNAL SOURCES OF FUNDS		
Consolidated income before extraordinary item	58,271	45,729
Depreciation	275,907	260,266
Deferred income taxes	5,675	7,784
Decrease in investment in unconsolidated subsidiary	—	16,502
Other — net	(16,500)	(1,076)
Total funds from internal sources	323,353	329,205
Less — Dividends paid on preferred and common shares	44,559	27,059
Net funds from internal sources	278,794	302,146
EXTERNAL FUNDS REQUIRED	$105,864	$ 99,686
FUNDS FROM FINANCING		
Shares of subsidiaries issued, net of conversions	$ 62,301	$ 38,793
Sale or issuance of long-term debt, net of redemptions and unamortized loss on foreign exchange	33,986	135,296
Increase (decrease) in loans for construction	9,577	(74,403)
Net funds from financing	$105,864	$ 99,686

The accompanying notes form an integral part of these consolidated financial statements.

ANGLO-CANADIAN TELEPHONE COMPANY and Subsidiaries

Summaries of Preferred and Preference Shares and Long-Term Debt

As at December 31, 1984 and 1983

	Shares	1984	1983
		(Thousands of dollars)	
PREFERRED AND PREFERENCE SHARES:			
Anglo-Canadian Preferred shares, par value $50 per share, cumulative dividend. Authorized 1,000,000 shares redeemable at $53 per share; outstanding 750,000 shares:			
4½% Cumulative Preferred shares	125,000	$ 6,250	$ 6,250
$2.90 Cumulative Preferred shares	125,000	6,250	6,250
$2.65 Cumulative Preferred shares	320,000	16,000	16,000
$3.15 Cumulative Preferred shares	180,000	9,000	9,000
		$ 37,500	$ 37,500
Subsidiaries' Preferred and Preference shares:			
British Columbia Telephone Company			
6% Cumulative Redeemable Preferred and Preference shares ($100 par value)		$ 5,500	$ 5,500
4⅜% to 5¾% Cumulative Redeemable Preferred shares ($100 par value)		48,000	48,000
4.84% to 11.24% Cumulative Redeemable Preferred shares ($25 par value)		208,700	218,185
$2.32 Cumulative Redeemable Convertible Subordinate Preferred shares ($25 par value)		700	1,037
Québec-Téléphone			
4¾% to 9¾% Cumulative Redeemable Preferred shares ($20 par value)		19,443	20,836
$1.68 Cumulative Redeemable Convertible Subordinate Preferred shares, Series B ($15 par value)		121	141
Premium on Subordinate Preferred shares		8	10
		$ 282,472	$ 293,709
LONG-TERM DEBT:			
British Columbia Telephone Company and subsidiaries			
First Mortgage Bonds 5⅝% to 17¼%, due 1985 to 2003		$ 908,800	$ 852,643
Promissory notes (Note 3)		140,000	165,000
Notes payable			
Interest rate conversion agreement due 1990 with an effective fixed rate of interest of approximately 12.1%		20,000	20,000
Other at varying rates of interest from 6% to 15.4%		10,200	4,755
Amounts due under capitalized leases		17,500	18,249
Québec-Téléphone			
First Mortgage Redeemable Sinking Fund Bonds 5½% to 11⅞%, due 1987 to 1996		86,306	85,235
Total principal amount		1,182,806	1,145,882
Less - Unamortized discount on long-term debt		8,469	8,284
Total long-term debt		$1,174,337	$1,137,598

The accompanying notes form an integral part of these consolidated financial statements.

Notes to Consolidated Financial Statements

As at December 31, 1984 and 1983

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

a) Principles of consolidation

All subsidiaries have been included in the consolidated financial statements except a wholly-owned subsidiary in the Dominican Republic.

The consolidated subsidiaries and equity ownership at December 31, 1984, were as follows:

	Percent Owned
British Columbia Telephone Company and subsidiaries	40.30
Dominion Directory Company Limited	100.00
Québec-Téléphone	50.56

GTE Corporation, Stamford, Connecticut, the parent company, also owned 10.08% of the outstanding ordinary shares of British Columbia Telephone Company.

The Company does not consolidate a wholly-owned subsidiary, Compania Dominicana de Telefonos, C. por A. ("Dominicana"), operating in the Dominican Republic, because of severe restrictions which limit the Company's ability to control distribution of earnings from this investment. The Company has not recorded earnings of this subsidiary since 1977, except as dividends were remitted, and elected beginning in 1981 to reduce the book value of its investment by the amount of any cash dividends received. The Company further elected during 1983 to write off this investment due to the uncertainty involved in its ultimate realization. This item was treated as an extraordinary item in the accompanying financial statements.

All significant intercompany transactions have been eliminated, except for purchases of telecommunications equipment and supplies by the telephone subsidiaries from Microtel Limited, a wholly-owned subsidiary of British Columbia Telephone Company, which are reflected in the consolidated financial statements at cost to the telephone subsidiaries, and are included in manufacturing sales in the consolidated statements of income. Intercompany sales for the years 1984 and 1983 totalled $89,900,000 and $113,500,000, respectively. To the extent that any income on these sales has not been offset by depreciation or other operating expenses, it remains in consolidated income and retained earnings. This practice is generally followed in the industry.

b) Depreciation

Depreciation of telecommunications property is provided on the straight-line method, for book purposes, based on engineering studies of the estimated lives and salvage value of the various classes of depreciable property.

Depreciation of the manufacturing property, for book purposes, is provided over the estimated useful lives of the assets using a straight-line basis.

c) Inventories

Inventories held by manufacturing subsidiaries are valued at the lower of cost or net realizable value.

d) Leases

Leases are classified as capital or operating leases depending upon the terms of the contract. Long-term lease rental agreements on equipment leased to customers are accounted for as operating leases. Assets, liabilities and amortization related to these leases are not material in amount.

e) Loans for construction

The loans for construction have been used, principally, to finance the subsidiaries' construction programs, and it is expected that they will in time be refinanced by issues of long-term debt or equity capital.

f) Deferred income taxes

Certain subsidiaries are presently claiming for income tax purposes capital cost allowances in excess of depreciation charged to the accounts and other expenditures which are capitalized in their accounts. The resulting reduction in income taxes is deferred.

Notes to Consolidated Financial Statements (continued)

g) Foreign exchange translation

Debt of consolidated subsidiaries payable in U.S. dollars is reflected in the financial statements at the rate of exchange prevailing at the end of the year. The unrealized loss on long-term debt of $14,439,000 is being amortized over the remaining term of the debt. This amortization amounted to $5,075,000 in 1984 and $1,926,000 in 1983.

2. COMMON SHARES, $10 PAR VALUE

Authorized — 1,700,000 shares

Issued and outstanding — 1,203,685 shares

3. PROMISSORY NOTES

The promissory notes are issued to obtain funds for general corporate purposes including the cost of extension and improvements to the plant and properties of British Columbia Telephone Company. These borrowings will be repaid from the proceeds of long-term financings.

The Company has long-term agreements for revolving loan facilities and at December 31, 1984, the agreements totalled $140,000,000 ($165,000,000 in 1983). Drawdowns under the agreement are by way of promissory notes issued at either fixed or floating interest rates for periods of up to five years. Short-term obligations have been reduced by $140,000,000 ($165,000,000 in 1983) to reflect these arrangements. Interest payable by the subsidiary thereon will be comparable to rates obtained on promissory notes issued on the commercial paper market. To the extent that the promissory notes in total exceed the maximum of the agreement, they are included in short-term obligations.

4. COMMITMENTS AND CONTINGENT LIABILITIES

a) Construction programs

The consolidated telephone subsidiaries' 1985 construction programs, as now planned, approximate $396,000,000 for which substantial purchase commitments have been made. These construction programs will be financed by cash available from operations and loans for construction pending permanent financing.

b) Preferred share redemption requirements

To meet the preferred share redemption requirements, the following payments will have to be made during the next five years:

1985	$ 9,430,000
1986	31,335,000
1987	6,335,000
1988	6,335,000
1989	6,335,000

c) Long-term debt repayment

To meet the sinking fund requirements and the debt retirements, the following payments will have to be made during the next five years:

1985	$ 17,461,000
1986	99,674,000
1987	107,624,000
1988	73,584,000
1989	108,484,000

d) Pension plans

All companies maintain funded pension plans for the benefit of substantially all employees. The actuarially determined aggregate cost of maintaining the pension plans was $34,558,000 in 1984 and $32,000,000 in 1983, respectively, which includes $2,089,000 in 1984 and $1,254,000 in 1983, respectively, for the amortization of past service costs and of experience deficiencies. Such amounts were paid to trustees. Due to the improvements made to certain pension plans during 1984 the present value of the estimated unfunded costs increased to approximately $51,499,000 at December 31, 1984, from $26,263,000 at December 31, 1983.

5. Related Party Transactions

Transactions with related parties (all affiliates of GTE Corporation) for 1984 included purchases and sales of telecommunications equipment and supplies (see Note 1), directory advertising commissions, royalties on equipment manufactured under licence and payments for services rendered under cost-sharing agreements. In 1984, approximately 65% (63% in 1983) of the sales and 14% (14% in 1983) of the purchases of the manufacturing subsidiary, Microtel Limited, were to and from related parties.

6. Segmented Information

The subsidiaries operate principally in two business segments:

1. Telecommunications operations, which includes local exchange and long distance telephone services, teletype, transmission of facsimile data, directory advertising commissions and other telecommunications services; and
2. Telecommunications equipment manufacturing, which includes research and development and sales of telecommunications equipment, training, engineering, installation services and distributed products.

The following table sets forth revenues, income from operations and supplementary data for the years ended December 31, 1984 and 1983 for each of the Company's business segments:

	Telecommunications Operations		Manufacturing Operations		Consolidated Operations	
	1984	1983	1984	1983	1984	1983
			(Millions of dollars)			
Sales to the public	$1,322.0	$1,256.3	$ 80.5	$ 93.0	$1,402.5	$1,349.3
Intersegment sales	—	—	89.9	113.5	89.9	113.5
Total revenues	1,322.0	1,256.3	170.4	206.5	1,492.4	1,462.8
Income from operations	126.6	121.9	(3.5)	6.1	123.1	128.0
Identifiable assets	3,140.3	3,032.0	144.4	122.2	3,284.7	3,154.2
Capital expenditures	337.9	378.7	13.5	6.6	351.4	385.3
Depreciation	265.2	254.8	10.7	5.5	275.9	260.3

Telecommunications operations are conducted in the provinces of British Columbia and Quebec. Manufacturing operations are conducted in the Provinces of British Columbia, Alberta, Saskatchewan, Manitoba and Ontario. Of the total manufacturing sales to the public, 36.5% were to the export market in 1984 and 26% in 1983.

Auditors' Report

TO THE SHAREHOLDERS OF
ANGLO-CANADIAN TELEPHONE COMPANY:

We have examined the consolidated balance sheets and the summaries of preferred and preference shares and long-term debt of Anglo-Canadian Telephone Company (a Quebec company) and subsidiaries as of December 31, 1984 and 1983, and the related consolidated statements of income, reinvested earnings and changes in financial position for the years then ended. Our examinations were made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, the accompanying consolidated financial statements present fairly the financial position of Anglo-Canadian Telephone Company and subsidiaries as of December 31, 1984 and 1983, and the results of their operations and changes in financial position for the years then ended, in accordance with generally accepted accounting principles applied on a consistent basis during the periods.

ARTHUR ANDERSEN & CIE,
Chartered Accountants.

Montreal, January 31, 1985.

GTE

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