Canadian National
Annual Report 1984

C
Eng.

**Time** is a river. The cover picture and the inside photos accompanying the text of this Annual Report are intended to convey an impression of CN people interacting with **Time** to manage change.

Poets, philosophers, scientists and people actively engaged in great enterprises have thought about and tried to define the ways that **Time** influences and changes events and destinies. The Roman Emperor and Philosopher Marcus Aurelius Antoninus said:

"**Time** is a sort of river of passing events, and strong is the current; no sooner is a thing brought to light than it is swept away and another takes its place, and this too will be swept away."

Implicit in that poetic definition is the concept of **Time** as an instrument of change and as a spur and a guide to action. Through the modern medium of the "photo-essay" we have tried to express the significance for the CN Group of Companies of this aspect of **Time.**

La version française du présent rapport
est disponible sur demande
à l'adresse suivante :

Canadien National
Affaires publiques et Publicité
C.P. 8100 Montréal (Québec)
H3C 3N4

# System Highlights

**Five year financial and statistical summary**

| | | 1984 | 1983 | 1982 | 1981 | 1980 |
|---|---|---|---|---|---|---|
| | ($ millions unless otherwise indicated) | | | | | |
| Operations | Revenues | $ 5,002.5 | $ 4,676.9 | $ 4,249.7 | $ 4,357.5 | $ 3,768.4 |
| | Operating income | 552.2 | 465.4 | 97.1 | 358.9 | 277.1 |
| | Interest expense – net | 349.1 | 268.4 | 240.4 | 170.8 | 110.9 |
| | Net income (loss) | 242.0 | 212.3 | (223.0) | 193.2 | 188.2 |
| | Dividend | 48.4 | 42.5 | — | 38.6 | 38.5 |
| | Return on average investment % | 9.2 | 9.1 | 0.3 | 7.8 | 6.8 |
| | Return on average equity % | 7.5 | 7.1 | — | 6.5 | 6.7 |
| Capital Expenditures | Total expended | 713.1 | 714.4 | 648.1 | 662.5 | 558.1 |
| Assets and Working Capital | Current assets | 1,019.9 | 1,035.2 | 1,006.9 | 1,063.4 | 1,018.3 |
| | Working capital (deficiency) | (266.7) | (32.0) | (9.0) | (7.6) | (26.9) |
| | Properties | 5,771.0 | 5,612.2 | 5,193.5 | 4,832.1 | 4,399.0 |
| | Total assets | 7,466.6 | 6,789.7 | 6,336.0 | 6,133.8 | 5,645.7 |
| Capital Structure | Long-term debt (including current portion) | 2,692.4 | 2,357.8 | 2,274.8 | 1,784.2 | 1,637.9 |
| | Equity | 3,324.3 | 3,112.6 | 2,840.9 | 3,059.6 | 2,898.5 |
| | Debt ratio % | 44.7 | 43.1 | 44.5 | 36.8 | 36.1 |
| Traffic | Revenue ton miles freight (billions) | 97.4 | 86.7 | 77.8 | 87.9 | 88.0 |
| Employees | Average number for year | 66,234 | 63,496 | 67,113 | 73,287 | 74,014 |
| | Average annual wage per employee (dollars) | 32,905 | 30,767 | 28,806 | 25,906 | 22,720 |
| | Average annual cost per employee (dollars) | 39,339 | 36,385 | 34,679 | 30,967 | 27,163 |
| Expenditures in Canada | Purchases | 1,295.0 | 1,098.0 | 1,114.2 | 1,195.0 | 968.0 |
| | Wages, salaries and fringe benefits | 2,212.9 | 2,002.5 | 2,035.2 | 1,962.1 | 1,793.9 |
| | Taxes | 343.5 | 300.9 | 286.2 | 277.4 | 232.1 |

# Table of Contents

# Directors

As at December 31, 1984

**E.J. Hewes,**
Chairman
Edmonton, Alberta
(2)

effective May 31, 1984

**J.M. LeClair**
O.C., M.D., LL.D.
President and
Chief Executive Officer
Montreal, Quebec
(2)

**R. Bégin**
Beauport, Quebec

effective June 14, 1984

**G. Di Battista**
Montreal, Quebec
(1) (4)

**C.A. Fagan**
St. John's, Newfoundland
(2) (4)

effective February 23, 1984

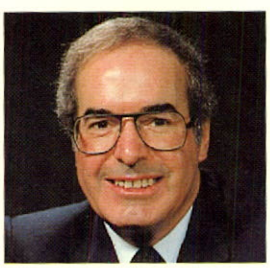
**J.S. Hinds,** Q.C.
Sudbury, Ontario
(2) (3)

**G.D. Mandel**
Toronto, Ontario
(1) (3)

**D.G.A. McLean**
Vancouver, British Columbia
(2) (3)

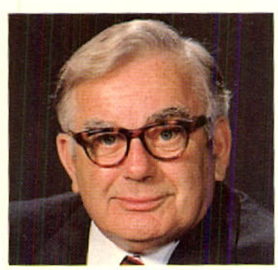
**K.R. Nurse**
Regina, Saskatchewan

effective May 24, 1984



**F.D. Rosebrugh**
Toronto, Ontario
(2) (3)

**J.T. Sears,** D.B.A.
Antigonish, Nova Scotia
(1) (4)



**G.T. Urquhart**
Moncton, New Brunswick
(1)

**Hon. J.H. Horner,** P.C.
end of term, February 29,1984

**Benoit Joncas**
end of term, June 13, 1984

**Ewart A. Pratt**
end of term, February 22, 1984

(1) Member of the Audit Committee
(2) Member of the Compensation Committee
(3) Member of the Investment Committee
(4) Member of the Social Responsibility Committee

# To the Honourable
# The Minister of Transport
# Ottawa

Dear Mr. Minister:

The Board of Directors of the Canadian National system is pleased to submit the Annual Report of the Corporation for 1984.

Since this statement is my first as Chairman of the Board, I am particularly pleased to report that 1984 was a most successful year for Canadian National. The Corporation earned record profits; made significant progress in improving its human resource functions; continued to refine its planning and management procedures; and carried forward the development of a comprehensive five-year corporate plan.

These are indeed impressive achievements and all the people who make up this great Crown corporation can take legitimate pride in them. This pride is shared by the Board of Directors; all the more so because we believe that success in achieving the business objectives of the Corporation has been accompanied by full discharge of CN's historic responsibility to serve the nation as a whole.

But while sharing the pride of all CN people in the accomplishments of 1984, the Board of Directors is not complacent as we look to the future. The Corporation now faces a changing economic environment in which the dual role of having to serve Canada as a competitive business enterprise and as an efficient instrument of public policy is becoming increasingly difficult. We know that this is a problem which cannot be solved by the Corporation alone but must be addressed in consultation and cooperation with the shareholder of CN – that is with the Government of Canada.

While such consultation and cooperation is, of course, an on-going process, there is, within the Corporation, a general sense of urgency in this regard. Meanwhile the Board and management will continue to take a pragmatic approach to the present realities and day-to-day challenges of the Corporation. It is in that spirit that we are proceeding carefully – with thoughtful analysis and planning – in areas such as prudent borrowing for essential capital expenditures; and the introduction of management techniques and new technology aimed at improving the productivity of the Corporation. We believe that the overall result of this policy will be the continued fulfillment of major objectives of both CN and its shareholder.

The commitment of the Board to corporate social responsibility is real and demonstrable. Recent evidence of this is the creation of a Social Responsibility Committee of the Board of Directors. The Committee will review and recommend policies and programs in such areas as technological change, bilingualism, social legislation and the responssibility of the Corporation to minority groups – including the handicapped, the elderly, women and youth. Corporate responsibility to the communities where CN has a presence and enhancement of the work life of CN people also come under the aegis of the Social Responsibility Committee.

As stewards of a great national asset we intend to maintain the flexibility necessary to respond positively to changes in the social as well as the economic environment.

Finally, even in the short time I have been with Canadian National I have been impressed by the loyalty and dedication of the many CN people I have met and by the extent of their contribution to the Corporation. I have been impressed also by the attitudes and the work of the members of the Board who bring very valuable knowledge and experience to collective decision-making. I can assure you, Mr. Minister, on behalf of the Board, that Canadian National is committed to serving Canada as well in the future as it has in the past.

Elizabeth J. Hewes

E.J. Hewes
Chairman

# Officers

as at December 31, 1984

E.J. Hewes
Chairman of the Board

J.M. LeClair
President
and Chief Executive
Officer

R.C. Franklin
Executive
Vice-President

H.J.G. Pye, Q.C.
Vice-President
and Secretary

A.R. Williams
Corporate Vice-President
Western Canada

**Corporate**

Y.H. Masse
Senior Corporate
Vice-President
and Chief Financial Officer

J.P. Laroche
Vice-President
Human Resources -
Corporate

G.C. Church
Treasurer

G. Maroulis
Chief Internal Auditor

E.D. Pinsonnault, Q.C.
Vice-President
Law - Corporate

S.D.H. Thomas
Corporate Comptroller

D.E. Todd
General Manager,
Public Affairs and
Advertising

**Divisions**

CN Rail

R.E. Lawless
President and
Chief Operating Officer

J.L. Cann
Vice-President
Operations

J. Horrocks
Vice-President
Finance and Planning

W.H. Morin
Vice-President
Employee Relations

J.H.D. Sturgess
Vice-President
Marketing

P.A. Clarke
President and
General Manager
TerraTransport

D.L. Fletcher
Vice-President
Prairie Region

J.R. Lagacé
Vice-President
St. Lawrence Region

R.G. Messenger
Vice-President
Atlantic Region

G.A. Van de Water
Vice-President
Great Lakes Region

R.A. Walker
Vice-President
Mountain Region

A.E. Deegan
Vice-President
Administration

R. Boudreau, Q.C.
Vice-President - Law

P.J. Foliot
Vice-President
Purchases and Materials
Management

CN Enterprises

R.C. Franklin
President

D.H. Burstow
President
CN Real Estate

D.C. Campbell
President
CN Communications

J.B. Griffith
President
Transport Route Canada Inc.
and President CNX

C.J. Hudson
President
CNM Inc.

D.S. Oberlander
President
CN Hotels Inc.

M.L. De Pellegrin
President
Canac Consultants Limited

R.J. Tingley
President
CN Marine Inc.

W.H. Waddell
President
CN Exploration Inc.

CN Investment Division

T. Cedraschi
President and
Chief Executive Officer

Grand Trunk Corporation

J.H. Burdakin
President

# Companies

Companies included in the Consolidated Financial Statements
of the Canadian National Railway System
as at December 31, 1984

**Consolidated Companies**

Autoport Limited

Canac Consultants Limited

Canadian National Express Company

Canadian National Hotels (Moncton) Ltd.

Canadian National Railway Company

Canadian National Steamship Company, Limited

Canadian National Telegraph Company

Canadian National Transfer Company Limited

Canadian National Transportation, Limited

Canat Limited

Canaven Limited

Central Vermont Railway, Inc.

Chalut Transport (1974) Inc.

Chapman Transport Limited

CN Exploration Inc.

C.N. (France) S.A.

CN Hotels Inc.

CNM Inc.

CN Tower Limited

CN Transactions Inc.

Coastal Transport Limited

Domestic Four Leasing Corporation

Domestic Three Leasing Corporation

Domestic Two Leasing Corporation

Duluth, Winnipeg and Pacific Railway Company

Empire Freightways Limited

Grand Trunk Corporation

Grand Trunk Land Development Corporation

Grand Trunk Radio Communications, Inc.

Grand Trunk Western Railroad Company

Mount Royal Tunnel and Terminal Company, Limited

Northwestel Inc.

Royal Transportation Limited

Terra Nova Telecommunications Inc.

The Canada and Gulf Terminal Railway Company

The Canadian National Railways Securities Trust

The Canadian Northern Quebec Railway Company

The Great North Western Telegraph Company of Canada

The Minnesota and Manitoba Railroad Company

The Minnesota and Ontario Bridge Company

The Northern Consolidated Holding Company Limited

The Quebec and Lake St. John Railway Company

Transport Husband (Québec) Inc.

Transport Route Canada Inc.

**Jointly-operated and Other Companies in which the System has Investments**

Canaprev Inc.

Chicago and Western Indiana Railroad Company

CN Marine Inc.

Compagnie de gestion de Matane Inc.

Computer Sciences Canada, Ltd.

East Yard Development Ltd.

E I D Electronic Identification Systems Ltd.

Eurocanadian Shipholdings Limited

Fort Point Holdings Ltd.

Halifax Industries (Holdings) Limited

Halterm Limited

Intercast S.A.

Lakespan Marine Inc.

Les Entreprises Bussières Ltée

OCRA Communications Inc.

Seabase Limited

Shawinigan Terminal Railway Company

Société du port ferroviaire de Baie Comeau-Hauterive

Telesat Canada

The Belt Railway Company of Chicago

The Public Markets, Limited

The Toronto Terminals Railway Company

Trailer Train Company

In addition, the property of the Canadian Government Railways is entrusted to the Canadian National Railway Company as part of the System.

# Canadian National
## President's Overview

J. Maurice LeClair
President and
Chief Executive Officer

**Highlights.** Canadian National had a good year in 1984, producing an excellent financial result and a sound operational performance and positioning itself to serve Canada well in what appear to be difficult times immediately ahead.

The Corporation's profits reached $242 million, an improvement of $29.7 million or slightly more than 14 per cent over 1983's record $212.3 million. The actual year-over-year improvement was closer to 45 per cent, but accounting rules introduced in 1984 requiring amortization of the exchange difference on foreign currency borrowing, had the effect of reducing the 1984 income level by $65.4 million.

All of the three major divisions of the Corporation shared in the strong showing. CN Rail increased income by 17 per cent and CN Enterprises by 23 per cent, while Grand Trunk Corporation, Canadian National's U.S. subsidiary, moved from a loss to a profit position.

CN Rail's income exceeded $304 million. Overall freight traffic increased 12.4 per cent compared to 1983 levels, with improvements in coal, potash, sulphur, lumber and intermodal traffic. Grain revenues on a current year basis are up $25 million. There were two reasons for this: CN Rail moved record amounts of grain in the first half of the year; and railways received a phased-in contribution towards fixed costs under the Western Grain Transportation Act. It should be noted, however, that interim payments of some $65 million from the Federal Government for 1982 grain movements were received in 1983 and, therefore, total direct compensation for grain in 1984 was generally comparable to 1983.

Grand Trunk's improved financial performance was also conspicuous in that a $12.2 million loss in 1983 was converted to a $14.3 million profit in 1984. Increases in automotive, coal and coke traffic as well as good management, reflected particularly in effective cost control, were the main reasons for the improvement.

CN Enterprises, in which all non-rail activities are grouped, continued its noteworthy financial progress. Income increased to $89.6 million in 1984 (including $21.9 million for CN Marine) compared to $73 million in 1983. CN Communications, CN Marine, CN Exploration, and CN Real Estate led the way in this advance.

During the year R.C. Franklin, president of CN Enterprises, was appointed executive vice-president of the Corporation. In his new role Mr. Franklin retains responsibility for each of the business units now included in CN Enterprises and assumes additional accountability for corporate staff functions including the overall financial management of the Corporation.

Late in the year the Government of Canada decided to establish CN Marine as a separate Crown corporation, as of January 1, 1985. The financial results of CN Marine for 1984 are therefore shown separately in this report, as an operation being discontinued. Since CN Marine has been making a positive contribution to corporate finances the decision to set up a separate corporation will have some adverse effect on CN's cash flow and on its ability to generate badly needed capital in the immediate future.

**Capital Need and Related Problems.** Lack of capital needed to finance the improvement and expansion of a number of nationally important services, especially railway services in Western Canada, remains the most pressing short-term problem facing Canadian National. This problem is made more acute by a somewhat gloomy economic outlook which foresees a fairly early downturn in the economies of Canada and many other countries, mainly in reflection of the world-wide effect of the U.S. federal deficit situation.

This uncertainty in regard to world economic trends poses problems in predicting the level of earnings of CN over the short term. Even as the present report is being prepared, however, there are some signs of a downturn in the levels of traffic on both major Canadian railways. This could be one of a number of indications that CN's problem of capital shortage will become increasingly serious in the years immediately ahead as the flow of funds from operations stagnates or falls. We will need to be addressing the problem of a falling equity ratio both within the corporation and with our shareholder.

In last year's Annual Report the capital needs of CN during the 1984-88 period were projected at $5.4 billion. The report noted that capital investments of this magnitude required that the Corporation be provided with some means of raising new equity capital. The alternative would be to borrow heavily, thus mortgaging our financial future.

No methods of raising new equity capital have been made available to CN nor does an equity infusion by the shareholder appear to be a national priority in the present economic circumstances. As a consequence, the Corporation has had to revise its five-year plan so as to reduce capital expenditures over the planning period. This decision faces CN with the strong necessity to continue and expand the improvements in productivity which have been achieved in recent years. That necessity has been accepted throughout Canadian National and, despite the reductions in overall capital spending, appropriate productivity programs will be funded in 1985 and subsequent years. This will be done within the framework of corporate policies which emphasize the importance of human values in connection with technological innovation and other productivity improvement programs.

**Human Resources.** Anyone reading these Reports over the past few years realizes that management has made large strides in recognizing its commitments in the area of social issues and in improving the quality of work life of its employees.

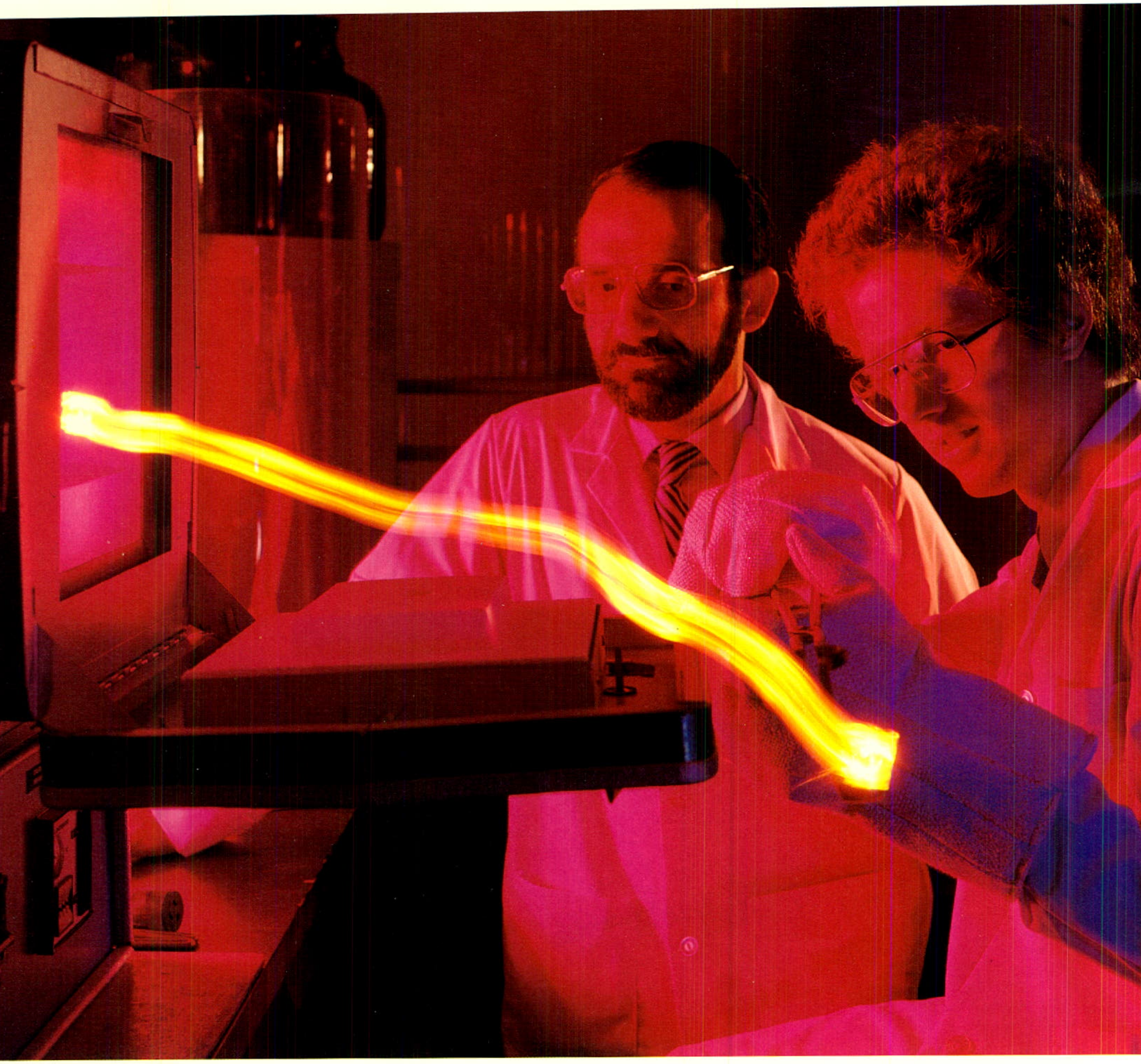
Further advances were registered in 1984 with the introduction of three major initiatives: a five-year national youth employment program; the introduction of the newly-created position, assistant vice-president for equity in employment; and the creation of a social responsibility committee of the Board of Directors of the Corporation.

Few economic problems have received as much attention as youth unemployment. The reason is simple: a society which is to continue to prosper must be willing to devote a high proportion of its resources to improving the experiences and abilities of its young people, otherwise there can be little change in its economic and social performance in the years ahead. And yet few practical programs to reduce the hardship of youth unemployment have emerged.

The transition from family dependence to personal independence is closely linked to the move towards the job market. If this transition is in doubt because of lack of work, the impact on our youth could determine future patterns of behaviour which would not reflect well on those institutions within society responsible for this transition.

CN's Youth Employment Program is an initative to help alleviate some of this problem. Moreover, it is hoped that it will encourage other organizations to act. The basic objective is to develop marketable and portable job skills for about 600 young Canadians between the ages of 16 and 25, at CN or elsewhere. Its initial duration will be for five years. During each year of the program about 120 young people will be hired and will receive work experience and training for up to three years. The program began September 1, 1984.

The appointment of an assistant vice-president for equity in employment is another way the Corporation is seeking to fulfill a social commitment – this time to equal employment opportunity for women. The newly created position is intended to send a clear signal throughout the organization that equal opportunity is a fundamental operational tenet. The mandate of the position will be to institute permanent, long-term change through programs which eliminate discriminatory practices and encourage the hiring and promotion of women at all levels. The goal is to make equal opportunity an integral part of the normal management process.



Youth Employment: Allan Barney (right), lab technician trainee at CN Rail Research in Montreal, is watched by Chemist Zaven Badiguian as he removes a steel sample from a 1,090 °C oven prior to testing its silicon content. Allan is one of 120 young people hired in 1984 under the Youth Employment Program.

**Management Structure.** The primary responsibility of management remains to preserve and compound the value of the Corporation for the benefit of all Canadians. To accomplish this within today's business environment requires a lean, tough, aggressive, dynamic and innovative management style. Canadian National has, accordingly, developed a management structure and style appropriate for the times.

To remain productive, however, organizations and organizational philosophies must be subjected to continuing review and refinement. The five-year plan which was effective in 1984 reflects this process of examination. It recognizes that significant changes in CN's role have taken place over the years and that further changes are necessary and inevitable. It further recognizes that CN has a dual role to play in fulfilling the policy objectives of government while meeting the requirement to operate with sound business practices in a competitive environment. This means that obstacles which stand in the way of achieving both goals must be identified and solutions discussed and found with CN's shareholder. Since the Corporation has a long history of effective communication and consultation with all levels and types of public authorities regarding these matters, this challenge can and will be met.

**The Fact of Change.** If anything can be said to be certain in these uncertain times, it is that significant changes will continue to be needed in the activities and organization of Canadian National.

The fact of change is not new to the Corporation. Change has been a characteristic of the political, industrial and economic environment in which CN has functioned for many years. But the speed and complexity of the changes which affect us today are truly unprecedented and the task of managing the Corporation has never been more complex or demanding.

It can be said that CN has been responding well to the challenge of the times; and will continue to do so. Much has been happening to and within the Corporation and the response has been quick and imaginative. We have been able to develop suitable organizational mechanisms and provide new and improved services to meet changing demands and circumstances. The successes which are detailed in the financial statements and other parts of this Annual Report are proof that organizations such as CN grow stronger and function better when they are able to adapt in such a fashion.

Signs are now plentiful that CN must begin a new era of organizational development as a national corporation with international responsibilities in an interlinked and competitive world. But CN's service to its customers and the nation cannot be better than the quality of the people who operate the system. Productive people must be motivated by appropriate challenges within an environment that rewards accomplishment. Much of our success in providing these conditions depends upon the relationship that CN has with its shareholder and on the organizational structure which permits this interplay. Management continues to work hard at improving each of these areas and at maintaining excellence within the tradition of national service which has been part of CN's history.

**A Look Ahead.** Last year's Annual Report stressed four major themes: optimism about the financial outlook for 1984; the need for new approaches to the problem of obtaining the equity capital needed to finance improvement and expansion of nationally important services; innovative responses by the corporate human resources function to changes occurring within Canadian society; and continuing efforts to renew and improve management in order to cope with the only constant in the marketplace – change.

Constructive action and advancement in each of these areas was a feature of 1984 and at year-end the Corporation had reason to be confident about its future, its evolving relationship with its shareholder, and its ability to succeed as a business corporation. The general economic outlook had some disturbing features and the problem of insufficient equity capital remained a major one. But, if past is prologue, the events and achievements of 1984 augur well for CN. They demonstrate significant progress towards a number of important goals and hold the promise of further progress in future years.

All in all, this has been a very good year for Canadian National. Everyone who works for the Corporation has a right to be pleased. And a right to sincere thanks for a job well done. Very little would have been accomplished without the individual effort which makes the achievement of shared goals possible. Management recognizes and expresses its gratitude to all for this effort.

J. Maurice LeClair
President and Chief Executive Officer

# Corporate Review

Pavilion at Expo 86: The photo above is of a model of the CN Pavilion designed by Vancouver Architect Peter Cardew. Theme of the pavilion, and of a permanent CN film theatre which is also part of CN's contribution to Expo 86, is "Carrying Things.".

**R.C. Franklin (left) Executive Vice-President and Y.H. Masse Senior Corporate Vice-President and Chief Financial Officer**

**Organization.** The major elements of the new management structure towards which Canadian National has been moving in recent years were in place and working in 1984. The evolution has been from a highly centralized structure to separately managed operating divisions which are able to concentrate on specific business objectives while remaining linked to a central unit, Corporate Management, for policy direction and guidance. This gives the Corporation the flexibility to serve and develop a number of different commercial markets without losing sight of overall corporate objectives and responsibilities.

**Shareholder Relations.** In discharge of its responsibility to act as primary liaison between Canadian National and its sole shareholder, the Federal Government, Corporate Management dealt successfully during 1984 with new requirements for Crown corporations brought about by amendments to the Financial Administration Act. These requirements included more systematic and timely reporting of the Corporation's activities and planning as well as more frequent and extensive contacts with Transport Canada and other departments and agencies of government. In this context, the meeting of a number of objectives of the present government was made easier by the planning process already in place within Canadian National.

**Financial Management.** Economic recovery in 1983 and continued improvement in 1984 have resulted in improved operating income for most of the divisions of CN. This improvement, together with tight cash management and restraint in capital expenditures, has helped to control the borrowing needs of the Corporation. This is reflected in a debt ratio of 43.1 in 1983 compared with 44.5 in 1982. In 1984 the debt ratio was 44.7; but this growth was due entirely to the effect of new Canadian accounting regulations governing the translation of debt denominated mainly in U.S. dollars. These regulations generated an increase in long-term debt of $271.7 million for CN in 1984. Without this effect the debt ratio would have improved to 41.8 in 1984.

The recent behaviour of world currency markets demonstrates the danger to any modern business corporation of uncontrolled growth in long-term debt. It also points to the importance, and the difficulty, of maintaining a balanced financial structure for CN in the years immediately ahead. The Corporation is projecting capital expenditure of $4.6 billion over the period 1985-1989 to maintain and improve transportation services needed in the national interest. Slightly less than 60 per cent of this capital can be generated internally which means that CN must look to external sources for the balance – amounting to about $2 billion. Since CN does not have access to commercial equity markets and since, as noted in the President's Overview, additional equity by the shareholder does not seem to be a priority at this time, the need for new equity capital does indeed remain the most serious short-term financial problem faced by Canadian National.

In planning for the next five years CN will limit both borrowings and capital spending to amounts necessary to hold the debt ratio at about 48 per cent. This will extend by about one year the completion of capital programs originally planned for the period. It is a preferred alternative to more borrowing and higher interest charges.

Within that context, it is clear to management that the contribution to corporate income of profitable business units of CN Enterprises will remain an important source of internal financing.

During 1984, management obtained the right to use "prompt offering prospectuses" for corporate borrowing in Canada. This permits a faster response to financing opportunities, which means the ability to take advantage of the most favourable money market conditions. In October, 1984, the first unguaranteed issue of CN debentures in the Canadian financial market, for $100 million, was offered and sold.

Monitoring of trends in world economies is an important part of the financial management of Canadian National today. Knowledge of flows of commodities and natural resources on a global scale and constant requestioning of major investment decisions are necessary to enable Canada to obtain optimum benefits from long-life railway facilities.

Of particular interest to CN management also is the competitive potential of multimodal transport systems both domestic and international. To meet competition from this source CN will need to maintain the flexibility to become part of such systems through ownership or contractual arrangements.

**Pensions.** Effective January 1, 1984, CN increased its pension payments by an averge of 7.1 per cent for 11,900 pensioners who retired prior to 1975, and by an average of 11.9 per cent for 12,700 survivors and beneficiaries. These increases were higher than current inflation and represented a catch-up over prior years.

CN has granted such voluntary increases for groups of pensioners since 1971 at a total cost of $338.6 million. In 1984 the Corporation continued its policy of allocating these funds to older pensioners, those whose pensions have been most affected by inflation. The amount of increased liability to the pension fund from this action was $45.7 million.

During 1984, $273.3 million was paid to pensioners, survivors and beneficiaries whose numbers totalled 47,300 at the end of the year. There are now close to eight pensioners for every ten active employees.

CN is carefully monitoring the nature and progress of pension reform legislation in Canada in anticipation of changes that may affect its pension plan. In this connection, improved computer systems are being developed to enable CN to provide more and better information to individuals affected by pension reform. This is part of the current "service oriented" approach of CN's pension department.

In February 1984, a representative of the National Council of CN Pensioners' Associations Inc. joined the CN Pension Board. This is the first time the National Council has been represented on the Board.

**Human Resources.** During 1984, a tribunal order under the Canadian Human Rights Act imposed a special program on CN aimed at increasing the representation of women in non-traditional jobs. The Corporation has appealed this decision because of the nature and specificity of the order. It intends, nevertheless, to address the substance of the issue. Steps taken during the year to ensure equal employment opportunity for women, as well as to address other social issues, are set out in the President's Overview.

Among the steps taken was the establishment of an Employment Equity Unit at the Corporate level to develop and ensure the implementation and development of policies designed to increase the representation of women at all levels of the organization.

Also during the year the Corporate Human Resources function managed the introduction of the Youth Employment Program already described by the President.

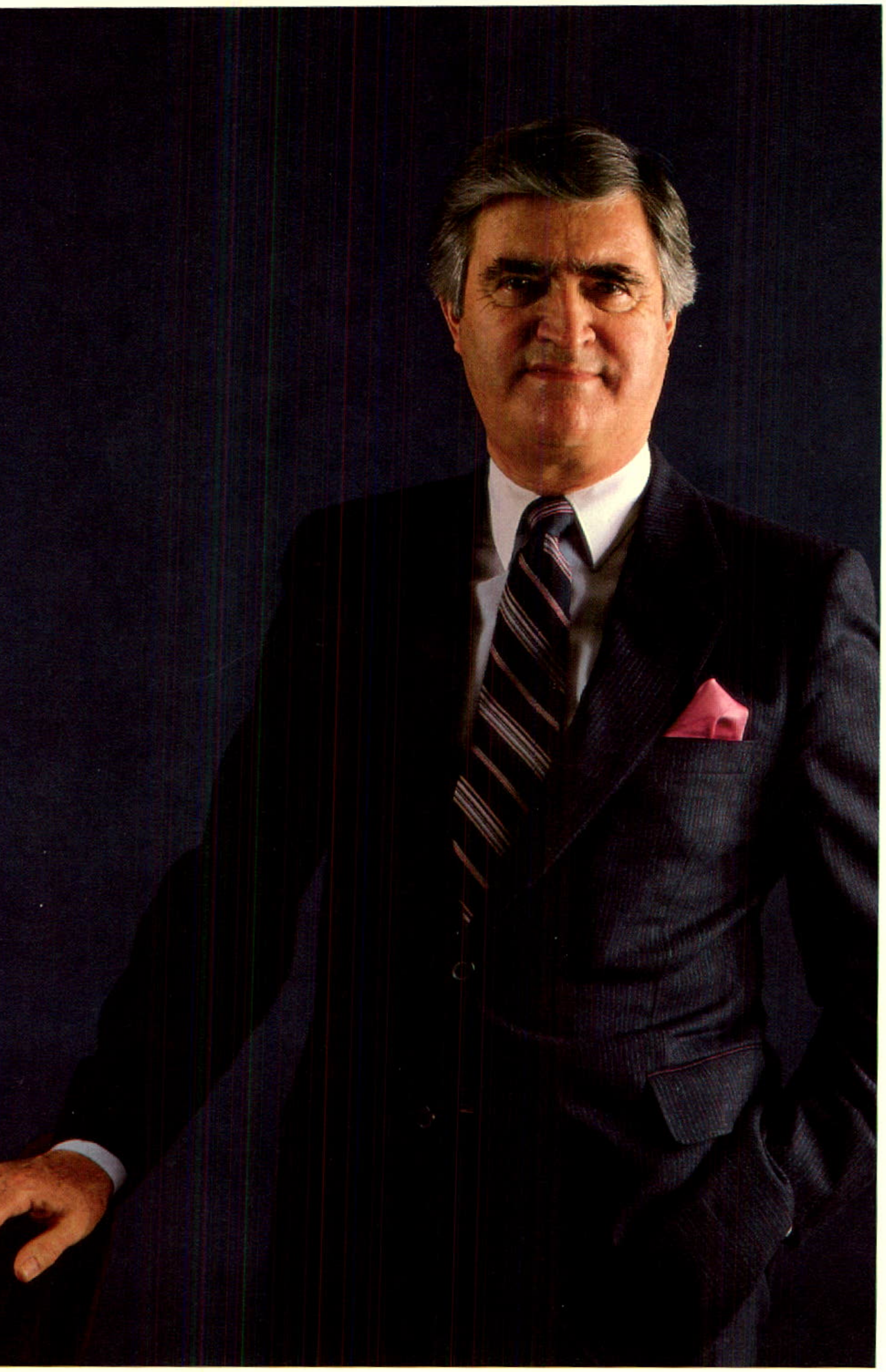
Substantial improvements were made during 1984 to the CN Scholarship Plan for the children of CN employees and pensioners. The number of annual awards was increased from 20 to 50 and the value of each scholarship was increased from $600 to $2,000. Planning for further improvements in the scholarship program continued with recommendations including an earlier closing date for the receipt of documents and a communications program designed to increase the number of applicants. A total of 221 applications was received in 1984 and a target of 400 has been set for 1985.

**Community Affairs.** In accordance with its prominent place in the transportation and communications industries in Canada, CN was busy in 1984 preparing for large scale participation in Expo 86 in Vancouver. The Corporation will be represented on the main exhibition site by a pavilion that will be symbolic of CN's stature, history and use of advanced technology; and at Canada Place by a permanent film theatre showing a unique, IMAX 3-D film produced by the National Film Board.

The theme of both the pavilion and the film will be "Carrying Things" and the intention is to symbolize CN's role as a major Canadian transportation and communications company and also to reflect the growing significance of CN's operations in Western Canada. The combined cost of these exhibits will be $10 million and the CN Theatre will remain as a permanent attraction at Canada Place.

In its role as a responsible corporate citizen, CN gave in excess of $1 million in 1984 to United Appeal campaigns across Canada and to special appeals for universities and hospitals as well as various cultural activities and groups.

# CN Rail
## President's Review



**R.E. Lawless**
**President and**
**Chief Operating Officer**
**CN Rail**

All of us at CN Rail can take pride in the excellent operational and financial performance of 1984. Some of the gains in traffic and earnings which are detailed in this Annual Report are associated with the gradual improvement in the economies of Canada and its trading partners which has been taking place since early 1983. National policies and legislation designed to rationalize methods of compensation to Canadian railways for the carriage of grain have also had a favourable effect on the financial performance of CN Rail.

But substantial credit for the 1984 results must go to the skills, knowledge and creativity of the men and women who manage and operate the great transcontinental and international railway system which is CN Rail today.

As part of the Canadian National system, CN Rail has been very much involved in recent years in the process of planning, adaptation and innovation which is enabling the Corporation to deal with rapid and radical change in the conditions under which it does business. Through this process CN Rail has become a technologically-advanced, market-oriented railway system producing efficient, safe and commercially competitive rail-based transportation and related services in line with the needs of modern Canada. As such we are moving forward into what I believe will be a successful and rewarding future.

Success and reward will not, however, come automatically or easily. The economic outlook is uncertain, with the strong possibility of slowdown in the 1985-86 period. Other factors likely to restrict the earning capacity of CN Rail over the next few years include severe competition within the transportation industry and the effects of deregulation of the industry in the United States. Meantime, the need continues for substantial capital expenditures to improve the capacity and efficiency of CN Rail's physical plant across Canada, and particularly in the West.

The corporate need for more capital and the current approaches to this long-standing problem are discussed elsewhere in this Report. But further improvements in productivity and in the financial performance of CN Rail are certainly an essential part of the solution. In brief, the challenge facing CN Rail is to maintain and build on the substantial achievements of 1984. I am confident that, despite all the difficulties and uncertainties of the times, we can and will meet this challenge.

# CN Rail

CN Rail did a good job for Canada in 1984, improving productivity and earnings while handling a record volume of freight traffic and making the largest contribution among the CN Group of Companies to the overall profitability of the Corporation.

Total traffic handled, as measured in revenue ton miles (RTM's), reached a record level of 89.7 billion. This was 12.4 per cent higher than in 1983 and almost 10 per cent higher than the previous record year of 1980. An increase of 4.4 per cent in CN Rail's workforce was necessary to handle the higher workload.

The major traffic increases were in products destined for export markets - coal, potash, sulphur and lumber. Substantial gains were recorded in intermodal and automotive traffic. Volume of grain traffic rose significantly but revenues received under the new Western Grain Transportation Act were about the same as the total of statutory grain compensation received in 1983, which included about $65 million of interim payments from the Federal government for grain movements in the latter half of 1982.

Intermodal traffic (in RTM's) increased by about 15 per cent in reflection of the strong merchandising and service effort which is being put into the development of this business by CN Rail Intermodal, the Division's coast-to-coast, door-to-door total distribution system. There is considerable growth potential in intermodal traffic and CN Rail plans to develop this potential through the use of specialized services and cost efficient intermodal/multimodal facilities and trains. Examples are the Montreal/Toronto "LASER" service and the Central Canada/Maritimes "CLIPPER" service. In 1985 CN Rail will begin a major new intermodal service linking Chicago with Montreal and Toronto via the facilities of the Grand Trunk Western. This will tap a large and potentially very profitable market in which head-on competition with the trucking industry will produce substantial benefits for shippers in terms of both price and service.

Improvements in traffic volume, productivity and financial performance were accompanied during the year by substantial progress in CN Rail's on-going program of expansion and modernization of the railway plant. This costly program is of major importance to the economic future of Canada and of particular importance to the increasingly export-based economies of the Western provinces.

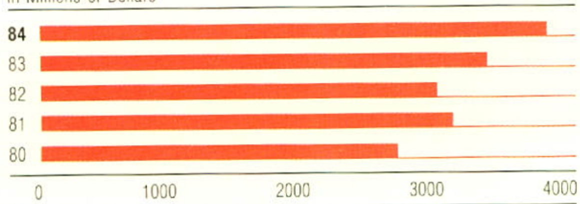
Current economic projection and the present uncomfortably high debt load have brought about some curtailment in the capital expenditures on expansion and modernization planned for 1985. But CN Rail still plans capital investment of about $600 million in 1985 and about two-thirds of this will be invested in Western Canada. Over the 1985-89 period the Division plans capital spending of $3.5 billion and again Western investment will predominate.

These figures reflect the fact that 67 per cent of CN Rail's workload occurred in Western Canada in 1984, and that the ratio is expected to rise to 70 per cent by the end of 1989. Double-tracking and other expansion and upgrading projects created about 3,000 seasonal railway jobs in the West during 1984, not counting the spinoffs to supply and support services across the country. Economic benefits on a similar scale are expected in 1985 and subsequent years as the workload generated by the successful world marketing of grain, coal, forest products, potash, sulphur, petrochemicals and other bulk products continues to increase and the physical plant expands to accommodate it.

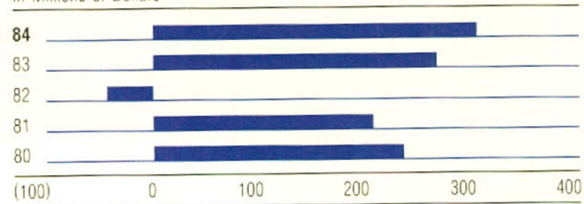
The workload is expected to increase on each region of CN Rail over the 1985-89 planning period, with the highest growth rates, as noted, in the West. Current economic projections indicate, however, that the overall increase will be low-to-moderate - about 1.7 per cent per year. This has led to some downward revision of earlier projections of more than 100 billion RTM's by 1989. The projections now are for a workload of about 98 billion RTM's by the end of 1989. This still represents substantial absolute growth over the 1984 record figure of about 89.7 billion RTM's.

National labour negotiations commenced between CN Rail and a number of different bargaining units during the year. The non-operating and the shop craft unions have joined together under a voluntary Associated Railway Union structure, while the running trades and other unions have elected to negotiate on an individual basis. In total, there are 45,000 unionized employees represented at the various bargaining tables. Some of the key issues relate to job security, wages and rule and benefits improvements.

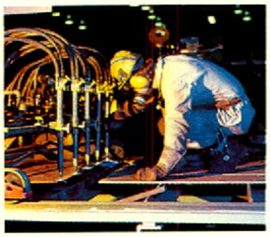
**CN Rail Revenues**
In Millions of Dollars

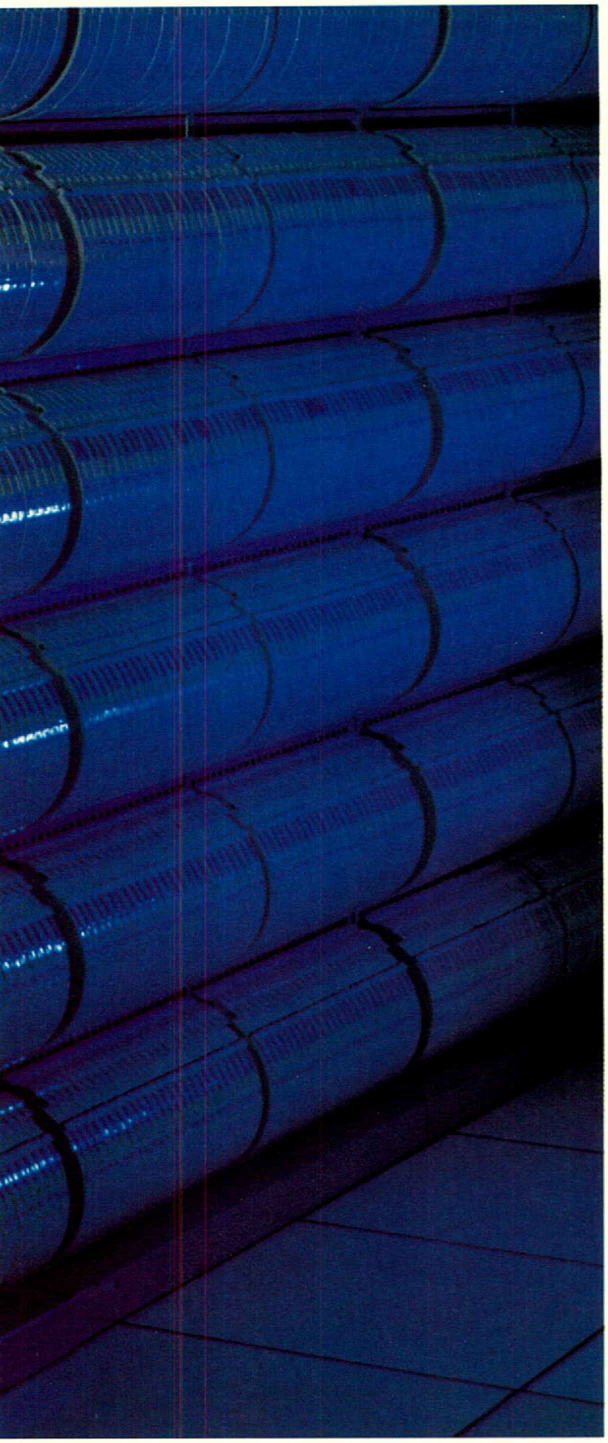



**CN Rail Income (loss)**
In Millions of Dollars



Traditional skills today: Rolling stock has always been repainted as part of normal maintenance schedules, but repainting took on new meaning in 1984 when several CN Rail units (top left), were decorated with colourful designs to promote the Corporation's Expo 86 exhibit about "carrying things."





Lengthy proceedings have recently been concluded before the Canada Labour Relations Board concerning applications made by the shop craft unions for separate certifications which, if approved, will mean they can bargain and deal with CN by craft. The Corporation did not oppose these applications on the understanding that separate certifications will be issued in line with CN's divisionalized organization.

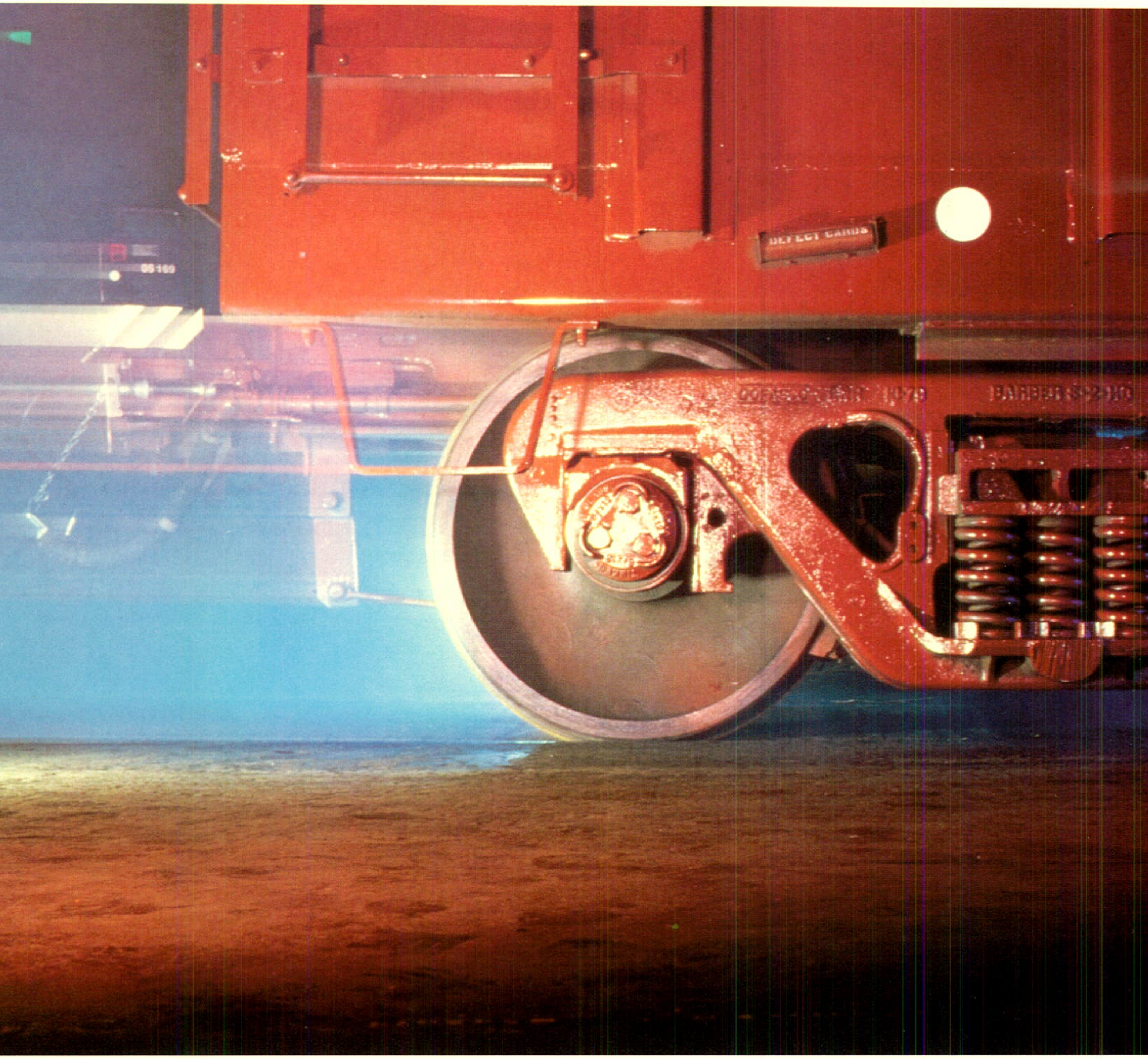
The Public hearings into CN CP purchase of the Canada Southern Railway have ended and the Rail Transport Commission's (RTC's) report approved the purchase; however, the Board also approved the applications for purchase of two other interested parties. A decision by government is expected shortly.

Notice was served upon the United Transportation Union under the appropriate Material Change rule of the Collective Agreements to effect the removal of cabooses from trains. The RTC ordered public hearings across the country in late 1984 and they are continuing into the first part of 1985 on the testing of cabooseless trains.

Despite the somewhat uncertain economic outlook and the problems associated with its debt situation, CN Rail looks forward to an improvement in its financial position in the future. Towards these ends CN Rail will continue to compete for a profitable share of all markets within its sphere of interests, giving particular attention to high-volume bulk commodities, to U.S.-Canada carload and truck-competitive traffic and to domestic Canadian truck-competitive traffic. Recognizing a steady increase in productivity as necessary to improved return on capital, CN Rail will also continue to evaluate and implement productivity improvement programs based on new technology and effective use of the knowledge and skills of all its people.

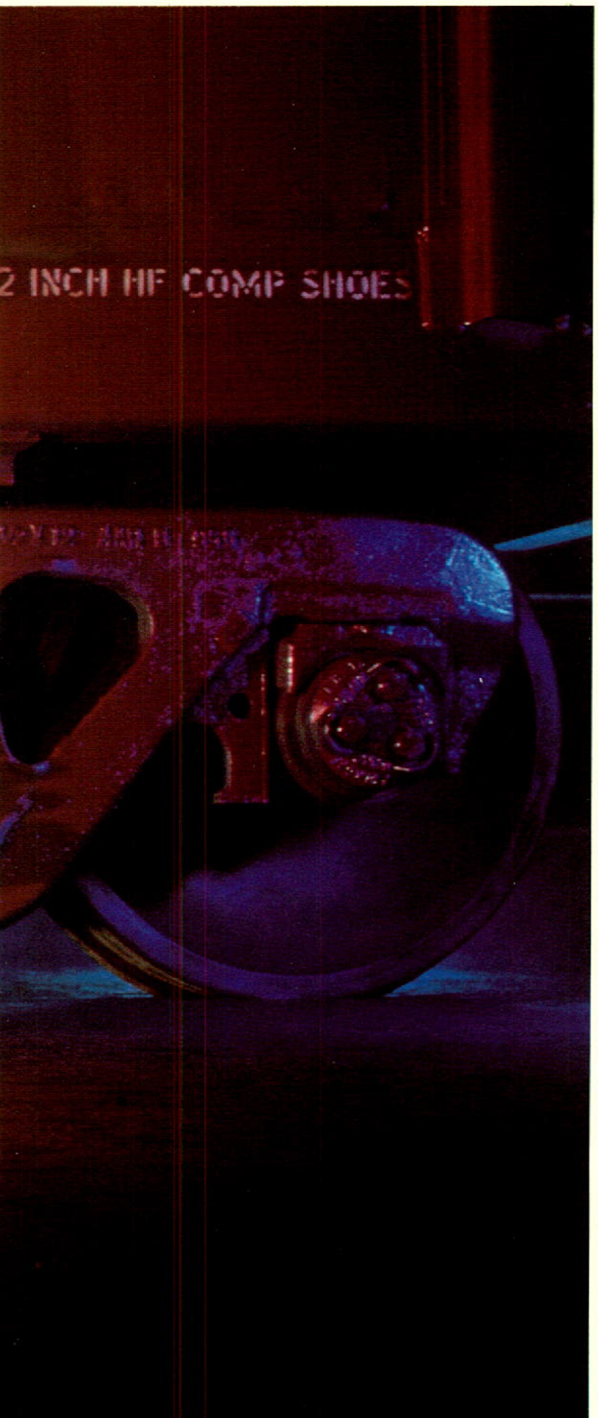
New skills for tomorrow: Apprenticeship and retraining programs were an important part of CN Rail's staff development program during the past year. At top right, a trainee learns how to use a metal cutting machine in the Transcona Shops.

**People make it work: Canadian National runs on technology, but not without constant control and fine-tuning by creative people such as Christine Côté (above), junior computer operator in Montreal. They tell machines what to do, how, and when. Christine is shown with tapes of programs she has retrieved from CN's vast storage system.**




The future: End of Train Information Systems (ETIS) may replace the caboose. The unit shown (top left) attached to the coupler of a freight car monitors brake pipe pressure, senses when the last car begins to move, notes its direction and radios this information to a display in the leading locomotive of the train.

A young snow-fighter: Recycled yard locomotives have been equipped with railmounted snow blowers (top centre), developed by CN Rail especially to cope with snow in congested areas such as rail yards.




## TerraTransport

TerraTransport, which provides rail and highway freight transportation and inter-urban bus passenger services in Newfoundland, remains in a deficit position despite the relative success of a five-year Revitalization Program funded by the Federal Government and scheduled to come to an end in March, 1985. Under the program, TerraTransport has modernized its operations, significantly increased its share of the available market and improved its financial position. The deficit at the end of 1984 was $32.9 million compared with $34.6 million the previous year. This result was strongly influenced by the net benefit (approximately $5.0 million) of government branch line subsidy payments for the years 1978-1984. The efforts of management and employees of TerraTransport have been a key factor in helping to contain the loss incurred since its establishment as a separate division.

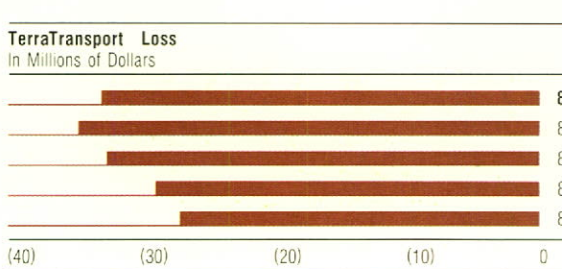
Current projections indicate that the deficit, which is absorbed by Canadian National, will resume an upward movement in 1985 and will reach about $45.0 million in 1989. The Federal Government is now evaluating the costs and benefits of TerraTransport in the context of overall Newfoundland transportation needs. This evaluation will determine the future of TerraTransport and CN is looking forward to a solution that will relieve it of the current financial burden while still providing Newfoundland with efficient and economical freight transportation services. CN is fully prepared to manage the property efficiently under a contract which provides adequate compensation for this important task.

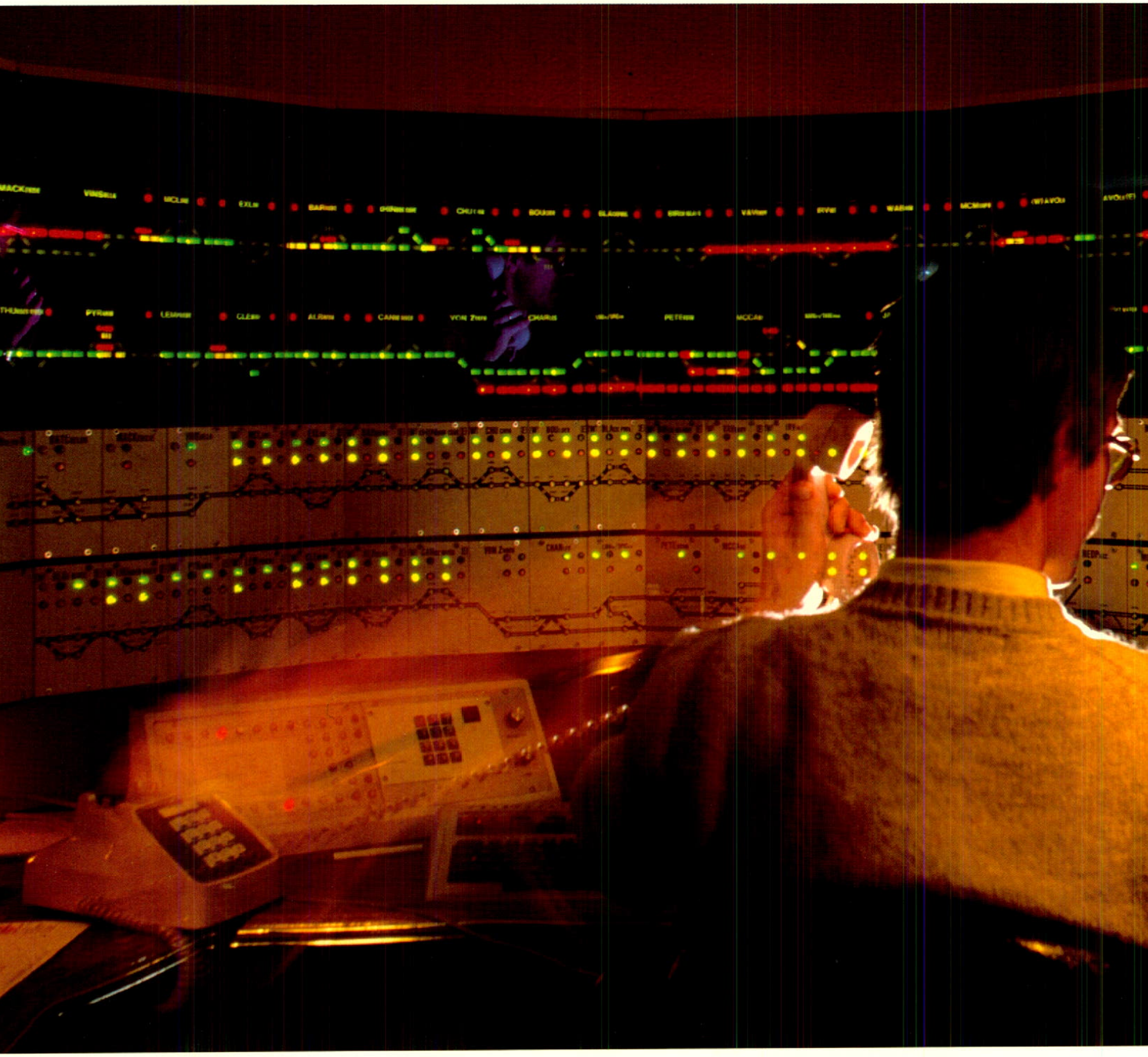
## Grand Trunk Corporation

Grand Trunk Corporation (GTC) had a relatively good year in 1984, increasing its volume of business in the face of strong competition and showing a modest profit after two years in the red. Good work by management and employees played an important part in this improvement. The corporation, which is made up of the Grand Trunk Western Railroad Company (GTW), the Duluth, Winnipeg and Pacific Railway Company (DWP) and the Central Vermont Railway, Inc. (CV), looks forward to another profitable year in 1985 and a steadily improving situation over the 1985-89 planning period.

High tech switch: The list of high technology pre-assembled track structures now includes switches with concrete ties and continuous welded rail. The photo top right shows the installation of a 77-metre long, 100-tonne switch assembly at Tranquille, just west of Kamloops, B.C.

**A cabooseless train: The striped unit at the end of the train is an important part of the ETIS System designed to result in the removal of cabooses from trains.**

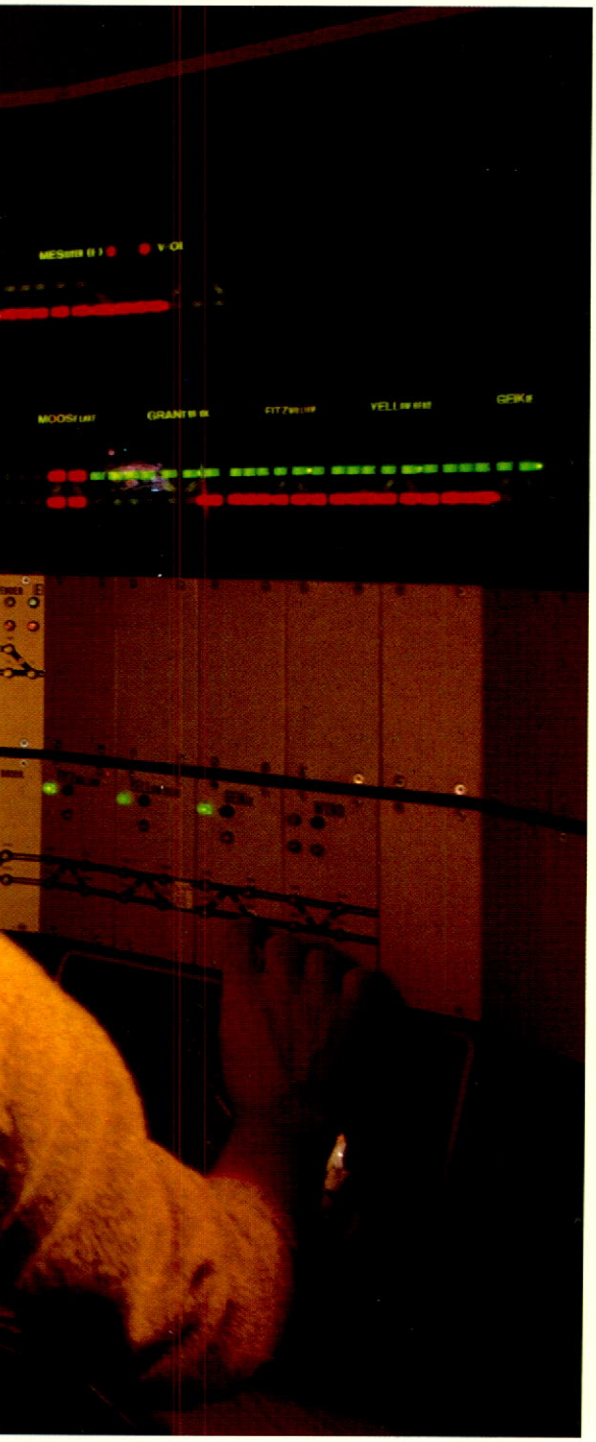




Three in one: The Voluntary Coordination Agreement (VCA) signed in 1984 by Burlington Northern Railroad, Grand Trunk Western, and CN Rail results in better service for all their customers. To symbolize the agreement, a BN diesel (top left) headed a train including units from GTW and CN Rail.

Aquatrain: Another VCA benefit for CN Rail comes from the marketing of CN Rail's barge service (top, second from left), between Prince Rupert, B.C., and Whittier, Alaska, by the BN sales organization.

Prairie grain rolls: Record volumes of grain were moved by CN Rail in 1984 from Prairie elevators such as the one shown (top, second from right), in Saskatchewan.



A major reason for optimism is the signing during 1984 of a voluntary coordination agreement (VCA) with the Burlington Northern Railroad. This agreement, which comes into effect in January, 1985, facilitates coordinated marketing and operations on certain major joint routes of the Burlington Northern, Grand Trunk Corporation and CN Rail. The three railways and their customers in both countries will benefit through increased efficiencies made possible by the creation of run-through train service and improved transit time.

The agreement was negotiated as a major part of GTC's answer to competitive forces created by huge rail mergers facilitated by deregulation of the U.S. railroad industry. It will enable the three railroads to offer their customers access to a 56,300 km track network reaching into 28 states in the busy Central U.S. industrial region and in the Northwest; also into all the Canadian provinces, the Canadian Northwest Territories and Alaska. The agreement promises GTC all the advantages of being part of a major transcontinental and international railway system while retaining the competitive flexibility of its independent status.

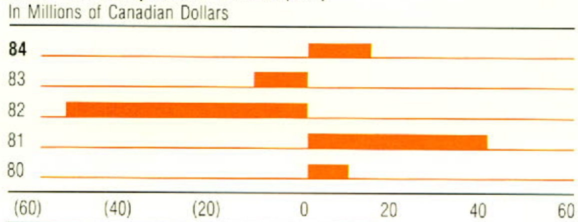
Major problems as well as new opportunities face GTC in the immediate future. The U.S. economy was strong at the end of 1984 although there are some indications of a downturn. Coal and coke and automotive traffic seem to be holding steady. But competitive pressure from large rail systems and from the trucking industry continue to limit traffic growth and revenue per unit handled. GTC is responding with increased productivity, aggressive marketing and the kind of innovation and flexibility represented by the VCA with Burlington Northern.

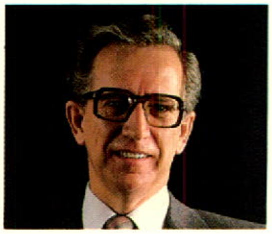
GTC looks forward to a steadily improving financial situation over the next few years, aided substantially by the VCA but resulting also from earnings by a generally leaner and tougher organization. The Grand Trunk Western and the Duluth, Winnipeg and Pacific are expected to contribute to this improvement but the Central Vermont, severely affected by the competitive situation in New England, will probably not be part of the upward trend.

TerraTransport: Efficient handling of containers is a feature of rail operations in Newfoundland. Local delivery (top right), in St. John's is handled by truck.

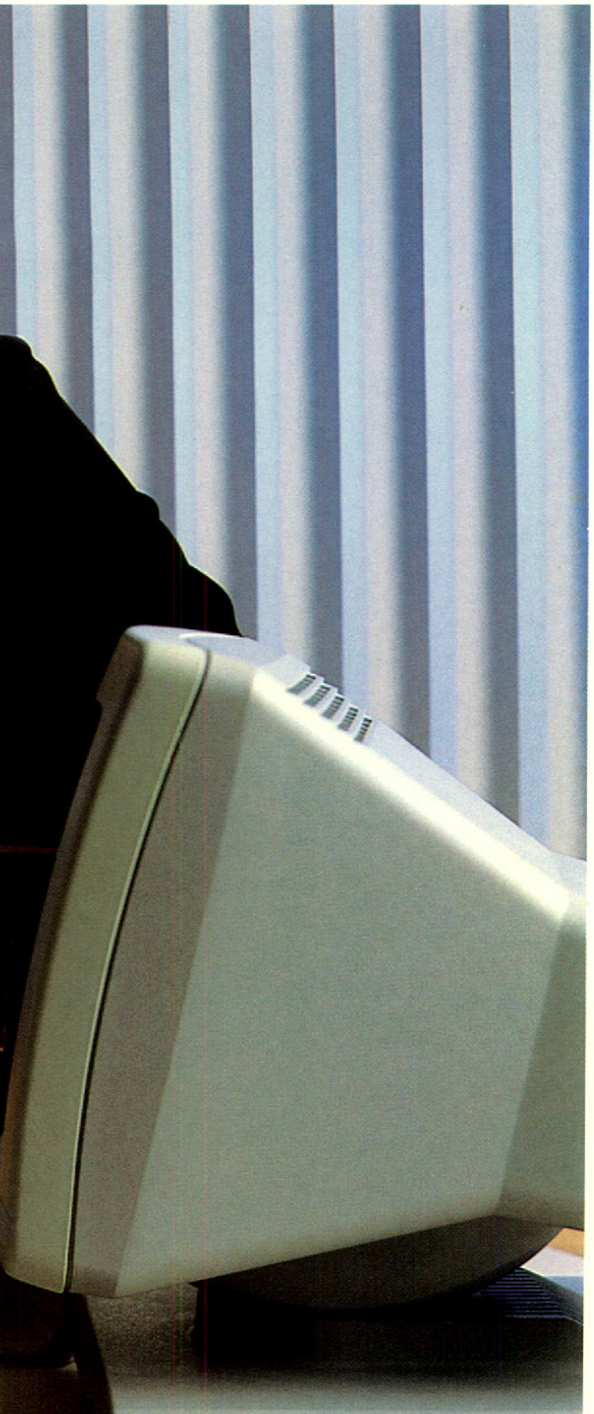
**Electronic Train Control: There is a lot of action on CN Rail's main line between Jasper, Alta. and Kamloops, B.C. but it is under the complete control of Peter VanHoof and the RTC Console at Kamloops. VanHoof can call upon the very latest in electronic equipment to keep the freight moving. But human knowledge and judgment are still the important factors.**

**Grand Trunk Corporation Income (loss)**
In Millions of Canadian Dollars





# CN Enterprises
## President's Review



The business units of Canadian National Enterprises served the corporation and the country well in 1984, providing efficiently a wide variety of services related to the basic activities of the Corporation. All of the services provided by the companies within CN Enterprises are important to the economic health and national prosperity of Canada.

With 1984 profits for the group increasing by 23 per cent to reach $89.6 million (including $21.9 million for CN Marine shown separately in the financial statements) the division made significant progress towards the long-term objective of achieving a commercial return on investment for CN Enterprises as a whole. Total assets including CN Marine Inc. grew to more than $1 billion by year end. In 1984 CN Enterprises' contribution to CN's finances, in terms of cash and additional borrowing capacity beyond its own needs exceeded $125 million.

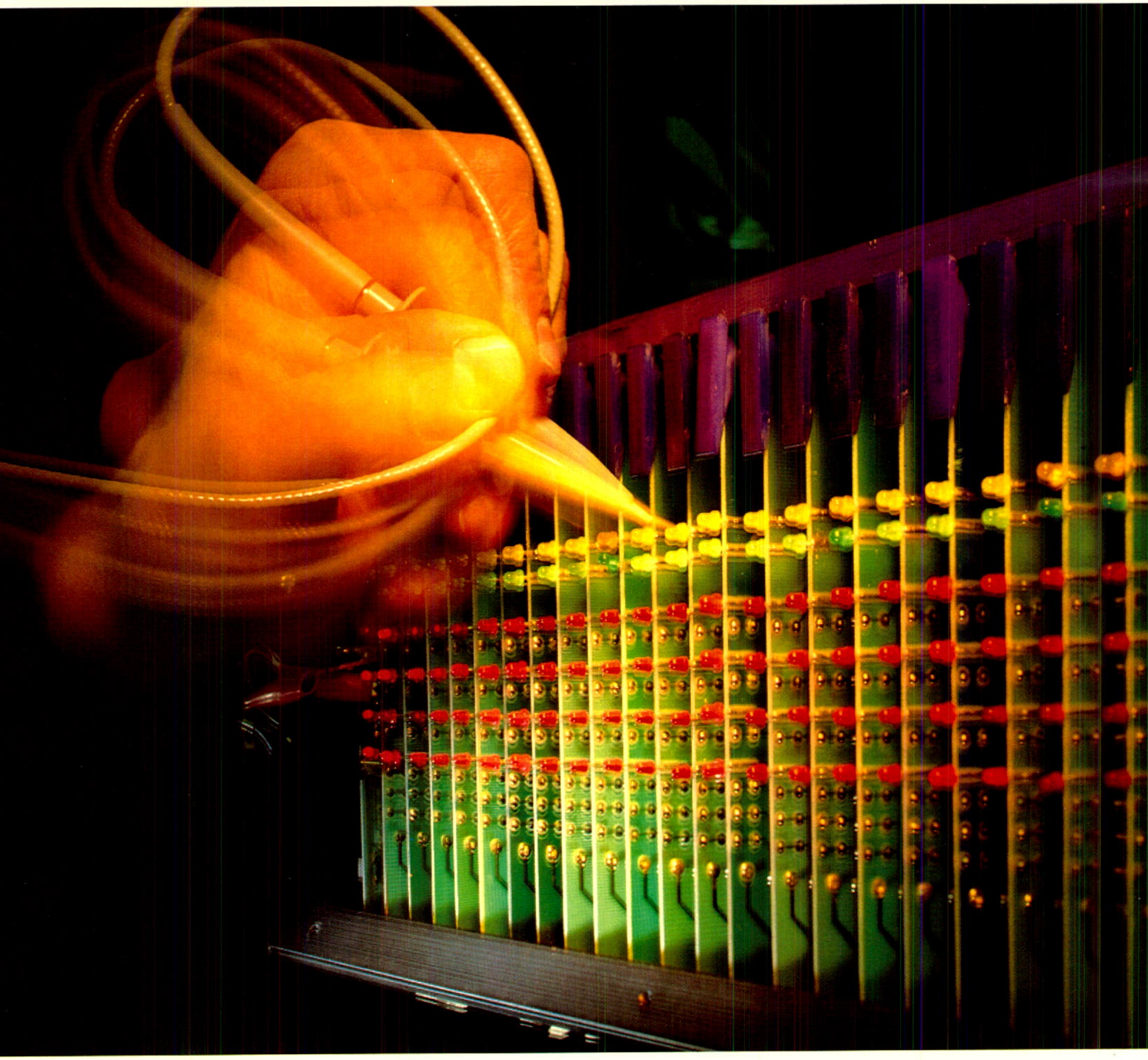
During the year, a number of important events symbolized the evolution of CN Enterprises and its divisions towards a position of maturity and strength within respective industry sectors. An important step was establishment of CN Hotels Inc., a new company with its own board of directors, as the entity responsible for managing the CN hotel chain and for achieving a performance comparable in all respects with that of other national hotels chains. In Toronto, the launching of the Convention Centre, L'Hôtel and the CN office tower by CN Real Estate and CN Hotels represented a major step forward in the urban development and hospitality fields. CN Exploration continued the exploitation of its lands and mineral rights by initiating a new two-year drilling program in the Kerrobert area of Saskatchewan.

The achievements of 1984 were attained primarily through the initiative and drive of employees in all divisions of CN Enterprises. Our objectives for 1985 are even more demanding and, with the Corporation facing severe equity constraints, our success is more critical. With the skills and determination of our people to rely on, I am confident that those objectives wil be met and that CN Enterprises will continue to contribute significantly to the overall success of the CN Group of Companies.

CN Route was formed, and with the granting of common bargaining units for CN Trucking and CNX, the merger of the two highway transport units, begun in 1983, proceeded according to plan and is now near completion. Following an announcement by the federal government in November that CN Marine was to become a separate Crown corporation, steps were taken to have the division managed as such, effective January 1, 1985.

R.C. Franklin
President
CN Enterprises

**Office Automation display: Telecommunications Terminal Systems, a business unit of CN Communications, specializes in new office automation technology for customers in Quebec, Ontario, Alberta and British Columbia. At T.T.S. headquarters in Toronto, Jackie Hing and Murray Smith discuss features of a new office machine.**



The Island's own: Terra Nova Tel is "the phone company" for most Newfoundlanders. At Twillingate, lineman Eugene Anstey (top left) does maintenance on components of a system that's very important to people scattered widely and separated by rugged terrain.

Microwave links: Towers such as the one shown top right in the Yukon connect telephones in the far North with the rest of Canada and the world. The expertise gained by meeting farflung challenges has attracted worldwide attention to CN Communications and Canac Telecom is CN's consulting arm ready to sign up customers.

Switching centre: A technician (above) checks complex circuits at CN Communications headquarters in Toronto. The Company's sophisticated nation-wide network is carefully and constantly monitored here.

## CN Communications

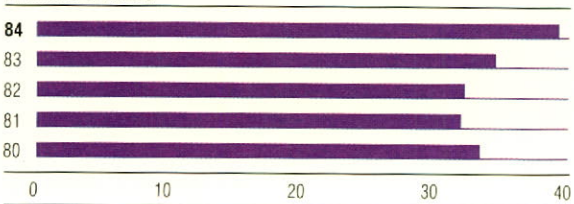
CN Communications – which includes CNCP Telecommunications, NorthwesTel, Terra Nova Telecommunications and Telecommunications Terminal Systems as business units – continued to perform well in a rapidly changing and highly competitive business environment. Business volume and productivity increased and a record profit of $39.3 million was achieved, an improvement of about 14 per cent over the previous year.

A common objective of the business units of CN Communications is a rate of annual growth in revenues and income, as well as rate of return on equity, comparable to rates that are the norms in the industry. Good progress was made towards that objective in 1984.

CNCP Telecommunications, competing strongly with Bell Canada and other members of Telecom Canada, increased revenues by 7.3 per cent through rate increases and greater business volume. CN's share of net income rose 35 per cent to $16.6 million. A seven-week strike by technicians, operators and clerks reduced revenues below anticipated levels, but this was more than offset by a resulting drop in labour costs. Orders were placed for fibre optic communication systems to be brought into service between Toronto, Ottawa and Montreal in 1986, and between Edmonton and Vancouver in 1987. CNCP's application to establish a long distance telephone service in competition with Bell Canada and the British Columbia Telephone Company was the subject of a public hearing held by the Canadian Radio-television and Telecommunications Commission (CRTC) in 1984. Success of this application would improve the competitive position of CNCP. A decision is expected in 1985.

Terra Nova Tel, operating in Newfoundland and Labrador, earned net income of $6.6 million, an increase of 29.4 per cent over 1983. Growth in both long distance business and in the subscriber network, combined with a rate increase and productivity enhancement, contributed to the excellent results. Service improvements included installation of a fully automatic mobile telephone system, the upgrading and extension of long distance circuits, and continued expansion of local exchange facilities so that single party service was available to 91 per cent of subscribers by year end.

**CN Communications Income**
In Millions of Dollars




NorthwesTel experienced substantial growth in revenues. Net income of $12.6 million represented a gain of 23.5 per cent over 1983 results. The improvement was due mainly to a significant increase in the volume of long distance business and private line leased services, as well as the full-year impact of a rate increase which went into effect in September 1983. Following a CRTC decision to permit attachment of subscriber-owned terminal equipment after September 1, 1983, NorthwesTel is now marketing residential and business communications terminals in its territory. Modernization and expansion of NorthwesTel operations continued in northern British Columbia, the Yukon, and the western portion of the Northwest Territories. In this context, orders were placed for satellite communication ground stations which, when installed in 1985, will improve service to five remote communities, Pelly Bay, Spence Bay, Gjoa Haven, Fort Franklin, and Telegraph Creek. Installation of a new digital telephone exchange for Yellowknife commenced, with completion expected in March 1985.

Telecommunications Terminal Systems, launched in 1982 as a partnership with Canadian Pacific Limited, had a very busy year in a fiercely competitive interconnect market. Revenues increased by 33.3 per cent but profit margins had to be reduced in order to hold market share. As a result overall earnings of the partnership declined. A new and promising venture was the entry of TTS into the large office automation equipment market during 1984.

Top of Toronto: The ever-popular revolving restaurant in the CN Tower was re-opened (top left) after extensive renovations during 1984.

CN Exploration: The 229 wells providing oil for CN from beneath the wheatfields of Saskatchewan are rigged with pumps such as the one shown at top right, automated, never tiring, working 'round the clock.

**Chanterelles Lounge: The newest member of the CN Hotels family, L'Hotel in Toronto, opened in 1984 and quickly became the first choice of experienced business travellers to Ontario's capital. Karen McPhee, lounge hostess in Chanterelles, serves guests just what they order, and fast!**

## CN Hotels Inc.

The five-year program aimed at integrating all CN Hotel properties into a profitable chain of first-class hotels and associated enterprises was carried forward with drive and enthusiasm in 1984. Steps towards the achievement of long-term objectives include;

- Opening of the new 594-room hotel in Toronto.
- Launching of an innovative product differentiation program - "Entrée" - based on knowledge about consumer demands and preferences and assuring consistent standards of good service to specific groups of customers throughout the hotel chain. The program includes a guest recognition system designed to build "brand loyalty" among frequent travellers.
- Assumption by CN Hotels Inc. of the management of The Queen Elizabeth and the Hotel Vancouver. These properties had formerly been managed for CN by the Hilton organization.
- Conclusion of an agreement with the City of Edmonton regarding redevelopment of the Hotel Macdonald and commencement of major renovation programs at The Queen Elizabeth, Château Laurier and Hotel Vancouver.
- Steps aimed specifically at improving customer services and facilities at CN Tower in Toronto included refurbishing of the revolving restaurant at the top of the tower and an agreement with outside developers for the showing of "Tour of the Universe", an educational and entertainment exhibit, at the base of the Tower.

## CN Exploration

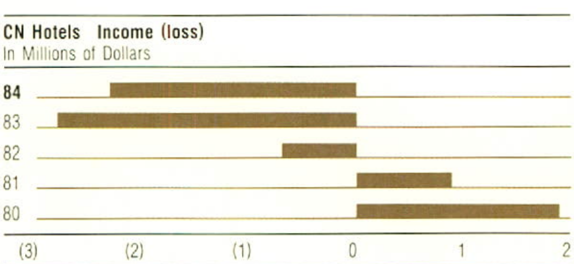
The past year has been an active and profitable one for CN Exploration, and further expansion of activities and earnings is foreseen for 1985.

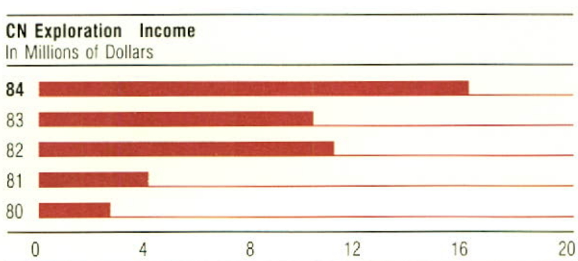
CN Exploration was one of the most active explorers and developers in Saskatchewan during the year, participating in the drilling of 114 wells (111 oil, two gas and one dry hole), an increase of 30 wells from the previous year. At year end, CN Exploration was operating 229 wells from its field office in Kindersley.

The evaluation of a large block of CN lands in the Kerrobert region of Saskatchewan was begun in May of 1984 and it was determined that a significant oil accumulation was present in the area. By the end of the year, 67 wells had been drilled over 180 km$^2$ and plans were underway to develop much of the area by drilling approximately 200 additional wells in 1985. Substantial volumes of oil will be produced from the Kerrobert properties over the next few years, and development plans include commencement of an enhanced oil recovery program in the last half of 1985.

Saskatchewan's Royalty Holiday, initiated in 1982 and extended to the end of 1985, has had a very positive impact on activity in that province. Drilling and provincial land sales income reached record highs during the year and CN Exploration benefited substantially through the elimination of the provincial freehold production tax on wells drilled on its fee simple lands through 1985. Current industry projections are that the record drilling activity of 1984 will be surpassed next year.

CN Exploration experienced a significant increase in production revenues during 1984 and earned a profit of $16.1 million. By year end, daily oil production had reached nearly 2,200 barrels. A further substantial increase is projected for 1985. Of continuing concern, however, is the relative instability of oil prices and markets, transportation bottlenecks and high levels of revenue taxation on the industry.




A night sight. The reflectorized giant maple leaf segment of CN Route's logo on its trailers is highly visible by night. Loading often takes place under lights for overnight delivery, and the top left photo shows a trailer loaded in Vancouver with eastbound merchandise.

On the Ivory Coast: Jacques Desjardins of CN Rail's Taschereau Yard diesel shop in Montreal instructs (top right) employees of Régie du Chemin de fer Abidjan Niger in Africa's legendary Ivory Coast. He was sent by CN's Canac, which offers railway and telecommunications consulting services to industries and governments all over the world.

**Have trucks, will deliver: Driver Rick Merkler of Spruce Grove, Alberta, prepares to take his CN Route rig from Vancouver to Edmonton. The tractor bears CN Route's new livery, now being applied to its nation-wide fleet of tractors, trailers, and city pick-up and delivery trucks.**

## CN Real Estate

CN Real Estate achieved a notable development and construction feat in 1984 with the completion, on time and on budget, of the $180-million Metro Toronto Convention Centre Complex – the largest facility of its kind in Canada. Occupying almost three hectares along Toronto's Front Street West and adjacent to the CN Tower the project was initiated and carried through by CN Real Estate as part of its mandate to develop the maximum commercial potential of CN holdings across Canada. Officially opened by Queen Elizabeth II in October 1984, the project has won recognition for CN Real Estate as an important presence in the development and construction field in Canada.

Other projects and plans on which there was significant action in 1984 included:

- A major mixed-use (residential, commercial and recreational) development of the Toronto railway lands as part of the largest urban redevelopment project in Canada, now to include a domed stadium.
- Completion by a private sector builder of about 700 residential units on land formerly owned by CN in Pointe-aux-Trembles, Montreal, as part of a mixed-use development which will include a major shopping centre.
- An agreement with local builders for the construction of about 800 residential units on about eight hectares of CN's "Bonaventure Lands" in Montreal. Known as "Les Floralies de la Montagne" this project will take four years to complete.
- Development of final plans for the renovation of the Macdonald Hotel in Edmonton. This important project is being managed by CN Real Estate on behalf of CN Hotels, and work will begin in 1985.

CN Real Estate, which reported its fourth consecutive profit ($14.9 million) in 1984, plans to continue to seek out opportunities for the commercial development of surplus railway lands and other properties across Canada. Real Estate also continues to provide its professional services to other companies in the CN Group.

## Canac Consultants Limited

Canac, the domestic and international consulting arm of Canadian National, had a busy and successful year, achieving its 13th consecutive profitable performance, a 23 per cent increase in sales, and a 12 per cent increase in net income over 1983.

This good performance took place in an environment characterized by sharply increased international and domestic competition, delayed or curtailed project funding from national and international lending agencies and high development costs.

Canac's strong marketing drive was reflected in the large number of proposals submitted to potential clients. Good results, including first-time-ever contracts in Madagascar and Mauritania, were produced. Market development efforts were stepped up substantially in South America and in the Far East, where Canac opened a permanent office.

Strong efforts to develop the Chinese market, resulting in a developmental project with the Chinese Railways, were another feature of the year.

Canac's North American operation succeeded in securing a contract in the United States, a market targeted for further development in 1985.

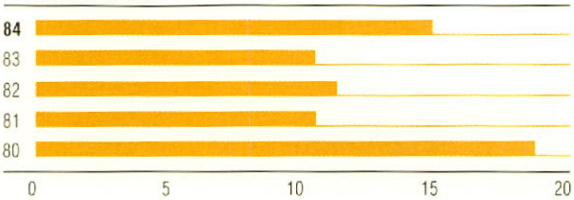
In accordance with Canadian Government guidelines concerning the commercial practices of Crown corporations in international trade, the following are Canadian National's representatives in the consulting field: in Mexico, Amexder, S.A. de C.V.; in Colombia, Antonio Soriano Franco y Compania, S. en C.; in India, C. Desai, I.C. Corporation; in Uruguay, Captain Fernando Garcia; and in Brazil, Suma Representacao Commercial Ltda. A total remuneration of US$500 was paid to these representatives in 1984.

## CN Route

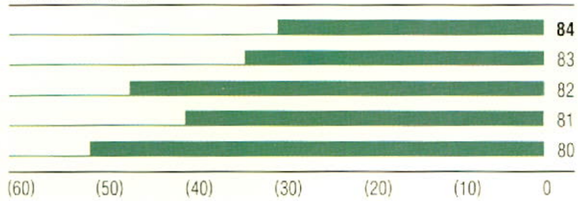
In 1983 the Board of Directors of CN gave authority to consolidate the administration of Express (CNX) and Trucking (CNTL) services in order to create one competitive highway-based unit providing trucking and related physical distribution services at commercial rates of return.

The new unit, then known as CNX/CN Trucking, began the difficult task of forming a single management team to direct the activities of a lean, efficient and commercially viable organization. By mid-1984 the single management team was working well and financial savings and new business opportunities resulting from the integration were becoming apparent. In order to capitalize on these advances a strong promotional program was developed, beginning with a change of name for the organization – to CN Route.

**CN Real Estate Income**
In Millions of Dollars




**CN Route Loss**
In Millions of Dollars



During 1984, compatible accounting and management information systems for the two divisions were established, and offices, terminals and maintenance facilities were rationalized. Following a hearing and a vote conducted by the Canadian Labour Relations Board, the terminal and fleet operations of the two divisions were integrated, providing customers with a single pick-up and delivery service.

Total revenues declined slightly in 1984 but the drop in expenses was proportionately greater, to the extent that the division's deficit was down to $29.8 million from $33.4 million in 1983. With cost savings from the merger expected to become more apparent in 1985, an improved financial performance is foreseen.

CN Route, which now operates 53 terminals across the country, faces a difficult task complicated by increasing competition in its field of activity and by the effects of deregulation on the trucking industry. The new unit has, however, made a good beginning and has good prospects not only for survival but for substantial development in the years ahead.

**CN Marine Inc.**

Continued modernization of ship and shore facilities, increased productivity and significantly improved standards of service characterized the operations of CN Marine Inc. in 1984.

Highlights of operations during 1984 included: a 30 per cent increase in shipment of containers between North Sydney, Nova Scotia, and Port-aux-Basques, Newfoundland; construction of a new ship (the Caribou) for Newfoundland service, proceeding on schedule, within budget and with delivery expected in the fall of 1985; participation by the Gulf ferry Ambrose Shea in the start of the Tall Ships trans-Atlantic race; and acquisition of computer-aided design and drafting terminals to increase the skills and productivity of engineering personnel.

**Results of Operations.** System net income for the year 1984 amounted to $242.0 million, an increase of $29.6 million over 1983. The 1984 net income was a Company record, surpassing the former high of $212.3 million in 1983 by 14%. Income from the railway operating divisions – CN Rail, TerraTransport and Grand Trunk Corporation – improved by $71.9 million or 33.6%. Higher traffic volumes were the principal reason for this improvement. CN Enterprises' income increased by $14.6 million or 27.4%. Tempering this System improvement was the increased interest cost of $80.7 million. Most of this increase arose as a result of the revised accounting requirements relating to the deterioration in the Canadian dollar in the past few years. This change added $65.4 million to the reported expenses.

The main factors accounting for the profit in 1983 compared with the loss in 1982 were a general improvement in economic conditions resulting in higher volumes of business, the 1983 receipt from the Government of Canada of interim grain payments to largely offset revenue shortfalls associated with the cost of carrying grain at uneconomic statutory rates, a decrease in pension costs in 1983 occasioned by an actuarial review of the pension fund and the provision in 1982 for investment impairments.

In accordance with applicable legislation, the Company provided for a dividend of 20% of net income to the Government of Canada. The dividend amounted to $48.4 million in 1984 and $42.5 million in 1983. No dividend was provided for in 1982 because of the loss.

The results for each division, which are discussed below, include the assignment to such divisions of a portion of interest expense. This expense aggregated $349.1 million for the System in 1984, up $80.7 million over 1983 and $108.7 million over 1982. These increases reflect higher borrowings incurred principally to finance capital expenditures and, more significantly, the application in 1984 of the new accounting regulations on the translation of debt denominated in foreign currencies discussed in Note 1 h) of Notes to Consolidated Financial Statements which amounted to $65.4 million of interest expense in 1984. This cost under the new regulations was not assigned to the Divisions in 1984.

**CN Rail.** CN Rail's income for 1984 totalled $304.4 million, as compared with $260.7 million in 1983 and a 1982 loss of $43.3 million. The principal factors accounting for the betterment were traffic volume increases and productivity improvements.

Railway operating revenues amounted to $3,789.2 million in 1984, up $400.7 million from 1983 and $819.9 million from 1982. Freight services revenues were the major factor in both the 1984 and 1983 revenue improvement. In 1984 freight services revenues rose by $508.4 million, mainly because of higher traffic volumes which occurred in most commodity groups, notably fuels and chemicals, intermodal, ores, minerals and metals and forest products, all of which benefited from the improvement in the economic climate in Canada and the U.S.. The other major factor accounting for the 1984 operating revenue increase was revenues earned under the WGTA (Western Grain Transportation Act). However, the adoption of the WGTA resulted in a significant reduction in Government payments for branch lines and the termination of the interim grain payment arrangement. In addition, there was a marked reduction in payments related to prior years. The grain revenue now received under the WGTA exceeds the amounts earned under previous arrangements. All other classes of revenues improved over their 1983 levels as well.

In 1983, freight services revenues, together with interim grain payments from the Government of Canada in anticipation of the WGTA, rose by $452.7 million from the 1982 level. This increase was attributable to higher traffic volumes, which occurred in most commodity groups, and to the interim grain payments. Marginal increases in rates were more than offset by a deterioration in traffic mix. Payments received for prior years' services declined by more than $70 million.

Expenses in 1984 were $3,484.7 million, up $356.9 million from 1983 and $472.1 million from 1982. The 1984 increase was mostly caused by volume increases of more than 11%, wage and material price inflation, and higher pension, tax, depreciation and interest costs, partially offset by improvements in operating efficiency. The 1983 increase was kept below 4% despite inflation and volume increases through management actions to contain expenses by streamlining operations and controlling manpower levels and discretionary work programs. A reduction in pension costs arising from an acturial valuation also helped to keep 1983 expenses down.

**TerraTransport.** TerraTransport's loss in 1984 was $32.9 million, $1.6 million less than in 1983 and $0.5 million higher than the 1982 level. The 1984 improvement was due to net branch line subsidy revenues for 1984 and prior years totalling $5 million and the success of a plan for containerization of Newfoundland traffic, which together exceeded interest and inflation-related cost increases. The higher 1983 loss was attributable to similar cost increases.

**Grand Trunk Corporation.** Grand Trunk Corporation's income amounted to \$14.3 million in 1984 compared with losses of \$12.2 million in 1983 and \$54.5 million in 1982. The strengthened U.S. economy along with specific measures taken to penetrate new markets and reduce the cost structure accounted for the 1984 turnaround. Operating expense savings coupled with the 1982 inclusion of a \$35.9 million write-down of the Central Vermont Railway, Inc. to its estimated realizable value are responsible for the 1983 income improvement.

Revenues amounted to \$524.0 million in 1984, \$436.5 million in 1983 and \$444.3 million in 1982. The 1984 revenue increase reflects higher traffic volumes, particularly in the automotive, coal and coke, intermodal, potash and fertilizer groups. Aggressive marketing practices and the voluntary coordination agreement with the Milwaukee Road (expired January 2, 1985) contributed to the gains achieved in the extremely competitive U.S. transportation market. The 1983 revenue decline was mainly caused by lower rates due to pricing actions required to remain competitive with other rail and motor carriers in the deregulated environment.

Expenses totalled \$509.7 million in 1984, \$448.7 million in 1983 and \$498.8 million in 1982. The 1984 rise was mainly due to higher traffic volumes and moderate inflationary pressures offset to some extent by employee reductions, shop closings, yard consolidations and rail line abandonments. The 1983 cost reduction was mainly attributable to the 1982 Central Vermont provision discussed above and cuts in manpower, programmed maintenance, fuel prices and interest expense.

**CN Enterprises.** CN Enterprises, which includes CN Communications, CN Hotels, CN Exploration, CN Real Estate and Other Businesses, earned income of \$67.7 million in 1984, compared with \$53.2 million in 1983 and \$53.1 million in 1982. Throughout 1984, CN Enterprises continued to manage CN Marine Inc.'s activities and, if its income had been included in CN Enterprises' results instead of being shown separately on the Consolidated Statement of Income, the total income of CN Enterprises would have increased to \$89.6 million for 1984 and \$73.0 million and \$69.6 million in 1983 and 1982 respectively. Details for the individual divisions constituting CN Enterprises are discussed below.

CN Communications. CN Communications' income in 1984 was \$39.3 million, compared with \$34.5 million in 1983 and \$32.1 million in 1982. The \$4.8 million increase in 1984 was mainly due to higher revenues resulting from 1983 and 1984 rate increases and volume growth. The \$2.4 million increase in 1983 was largely due to higher revenues resulting from rate action. Strict expense control was also a factor in both years.

CN Hotels. CN Hotels had losses amounting to \$2.3 million in 1984, \$2.8 million in 1983 and \$0.7 million in 1982. Higher occupancy rates and higher average revenue per room were the principal reasons for the 1984 improvement. Lower occupancy rates at some hotels and the inability to pass on cost increases at others were the most significant factors in the 1983 loss increase. The 1983 results benefited from a municipal tax refund and from an expense accrual adjustment.

CN Exploration. CN Exploration earned income of \$16.1 million in 1984, compared with \$10.3 million in 1983 and \$11.1 million in 1982. The 1984 income improvement was due to increases in oil production sales and royalty income. The 1983 income decline was largely due to lower oil prices coupled with higher operating expenses reflecting increased production and exploration and higher interest costs.

CN Real Estate. Income from CN Real Estate amounted to \$14.9 million in 1984 compared with \$10.5 million in 1983 and \$11.3 million in 1982. In 1984 increased profits from land sales accounted for nearly all of the betterment. In 1983 higher income realized from property management was more than offset by a reduction in profit from land sales.

Other Businesses. Other Businesses had a loss of \$0.3 million in 1984 compared with a profit of \$0.6 million in 1983 and a loss of \$0.6 million in 1982. The 1984 reduction results mainly from the downturn in dockyard business and the disposal in the latter part of 1983 of CN-owned container handling equipment at Task Terminal in Montreal.

**CN Route.** CN Route, the new division integrating the Company's trucking and express operations, had a loss of \$29.8 million in 1984, compared with losses of \$33.4 million in 1983 and \$46.4 million in 1982. Significant factors accounting for the betterment in 1984 were the savings arising from combining the management of CN Trucking and CN Express, the streamlining of operations (including reduced uneconomic services) and a number of miscellaneous improvements. These were partially offset by an increase in the interest charges. A reduction in uneconomic services and a 1982 provision of \$10.8 million for the estimated costs related to the integration of the express and trucking operations accounted for the 1983 improvement.

**Miscellaneous.** The net expense in the Miscellaneous sector in 1984 was \$37.9 million, compared with \$41.3 million in 1983 and \$116.1 million in 1982. Income from the transfer of research and development tax deductions and credits and from the refund of investment tax credits, partially offset by losses on U.S. currency exchange fluctuations, accounted for most of the 1984 improvement. The principal factor in the difference between 1983 and 1982 was the \$61.5 million provision in 1982 for the impairment in the value of an investment. There was also an increase in 1983 interest income and investment tax credits.

**CN Marine Inc.** CN Marine Inc.'s income was \$21.9 million in 1984, \$19.8 million in 1983 and \$16.5 million in 1982. Higher interest income accounted for nearly all of the 1984 improvement. The 1983 increase was largely attributable to greater traffic volumes.

**Income Taxes.** Income taxes otherwise payable with respect to 1984 in the amount of $116.7 million have been eliminated through utilization of tax benefits pertaining to prior years' losses, which reduction was accounted for as an extraordinary item. The corresponding amount for 1983 was $99.4 million. Because of the loss in 1982 there was no income tax expense for that year. See note 10 of Notes to Consolidated Financial Statements which indicates that such benefits are available to reduce taxable income of future years.

**Liquidity and Capital Resources.** As reflected by the Consolidated Statement of Changes in Financial Position, there was a decrease in cash of $150.6 million in 1984 much of which can be attributed to the fact that internally-generated funds were less than the high level of capital expenditures. In 1983, most of the increase in cash was due to improved cash flow from operations, while in 1982 the relatively low level of funds provided from operations was the principal reason for the negative cash flow. Cash deficiencies are financed by short-term bank borrowings. At December 31, 1984, short-term bank loans amounted to Canadian $0.1 million and U.S. $7.0 million. The Company has arrangements with a number of Canadian and U.S. banks which provide lines of credit in excess of the Company's anticipated short-term borrowing requirements.

In November 1984 the Company issued and sold $100 million 13% debentures in the Canadian domestic market. During 1984, the Company issued to the Government of Canada in respect of CN Marine Inc. capital projects, 36,400 common shares for $18,200,000.

In January 1985 the Company repaid $63.2 million outstanding principal balance of its 5 3/4% bonds which matured January 1, 1985. In March 1985 the Company borrowed $42.6 million at a cost of 11.46% by means of a yen syndicated loan and currency swap and arrangements were also made to repay a SFr. 100 million bank loan in April.

The new Canadian accounting regulations on the translation of debt denominated in foreign currencies generated an increase in long-term debt of $271.7 million (see Notes 1 h) and 4 of Notes to Consolidated Financial Statements). As a consequence the Company's year-end debt ratio increased to 44.7% from 43.1%.

As noted elsewhere, effective January 1, 1985, CN Marine Inc. is under the control of the Government of Canada. Negotiations are underway for effecting this divestiture, the financial impact of which has not yet been determined.

Planned capital expenditures for 1985 are approximately $875 million. In addition, the Company anticipates that capital expenditures for 1986 and 1987 will aggregate approximately $2 billion. The capital expenditure program for 1985 to 1989 includes funds required for the expansion of roadway property in Western Canada, renewal of basic plant, purchase of rolling stock and other equipment and improvement of operating efficiency. The Company expects that a significant portion of these expenditures will be funded through borrowings, the timing and amount of which will be subject to market conditions and future operating results.

At December 31, 1984, the Company had commitments to purchase railway ties at an aggregate cost of $124.5 million and rolling stock of $104.9 million.

**Inflation.** For the second consecutive year the annual rate of inflation on CN's wage, fuel and material costs was below the double-digit level. In fact, the Company's rate has been generally in line with the Consumer Price Index increase for the last three years.

There are many factors that help to explain the downtrend in the Company's rate of inflation. In 1983 and 1984, the effect of the Government of Canada's six and five per cent policy guidelines to combat inflation was felt. In addition, fuel prices stabilized, interest rates fell from their record-high levels and the recent economic recession had a dampening effect on prices.

The Government's original guidelines called for a limiting of price increases for goods and services sold by Crown Corporations and federally-regulated industries to 4% for the period from June 1984 to June 1985. However, effective November 8, 1984, the guidelines have been removed and there are now no compulsory Government wage or price guidelines in force.

Notwithstanding the Company's lower inflation rates in 1983 and 1984, there continue to be upward pressures and the effect of many years of rising prices on the Company is pronounced. In recognition of the need to supplement the historical cost information provided in the financial statements, the Canadian Institute of Chartered Accountants, in December 1982, issued recommendations for the reporting of certain effects of changing prices on an enterprise. These recommendations became effective in 1983 and the information for CN is shown following the notes to the Company's financial statements.

# Consolidated Financial Statements

# Consolidated Statement of Income



| | Year ended December 31 | 1984 | 1983 | 1982 |
|---|---|---|---|---|
| | (in thousands) | | | |
| CN Rail | Revenues | $3,789,158 | $3,388,494 | $2,969,291 |
| | Expenses | 3,484,726 | 3,127,800 | 3,012,609 |
| | Income (loss) | 304,432 | 260,694 | (43,318) |
| TerraTransport | Revenues | 53,445 | 47,839 | 46,799 |
| | Expenses | 86,384 | 82,397 | 79,193 |
| | Loss | (32,939) | (34,558) | (32,394) |
| Grand Trunk Corporation | Revenues | 524,035 | 436,464 | 444,272 |
| | Expenses | 509,720 | 448,688 | 498,777 |
| | Income (loss) | 14,315 | (12,224) | (54,505) |
| CN Enterprises | | | | |
| CN Communications | Revenues | 278,887 | 257,883 | 244,016 |
| | Expenses | 239,632 | 223,402 | 211,919 |
| | Income | 39,255 | 34,481 | 32,097 |
| CN Hotels | Revenues | 102,186 | 103,340 | 110,761 |
| | Expenses | 104,500 | 106,107 | 111,476 |
| | Loss | (2,314) | (2,767) | (715) |
| CN Exploration | Revenues | 31,873 | 24,667 | 18,578 |
| | Expenses | 15,729 | 14,349 | 7,474 |
| | Income | 16,144 | 10,318 | 11,104 |
| CN Real Estate | Revenues | 30,544 | 22,701 | 19,711 |
| | Expenses | 15,635 | 12,166 | 8,415 |
| | Income | 14,909 | 10,535 | 11,296 |
| Other Businesses | Income (loss) | (260) | 611 | (649) |
| Total CN Enterprises | Income | 67,734 | 53,178 | 53,133 |
| CN Route | Revenues | 163,427 | 169,656 | 179,769 |
| | Expenses | 193,192 | 203,026 | 226,152 |
| | Loss | (29,765) | (33,370) | (46,383) |
| Miscellaneous | Loss | (37,894) | (41,283) | (116,075) |
| Total Continuing Operations | | 285,883 | 192,437 | (239,542) |
| CN Marine Inc. | Income | 21,888 | 19,803 | 16,507 |
| Income (loss) before amortization of deferred foreign exchange loss, income taxes and extraordinary item | | 307,771 | 212,240 | (223,035) |
| Less: Amortization of deferred foreign exchange loss | | 65,427 | – | – |
| Income taxes | | 117,123 | 99,290 | – |
| Income (loss) before extraordinary item | | 125,221 | 112,950 | (223,035) |
| Reduction in income taxes on application of prior years' losses | | 116,730 | 99,383 | – |
| Net income (loss) | | $ 241,951 | $ 212,333 | $ (223,035) |

See accompanying notes to consolidated financial statements.

# Consolidated Balance Sheet

| | December 31 | | 1984 | | 1983 |
|---|---|---|---|---|---|
| Assets | (in thousands) | | | | |
| Current Assets | Cash | | $ – | | $ 59,544 |
| | Accounts receivable | | 427,622 | | 402,613 |
| | Material and supplies | | 390,362 | | 363,814 |
| | Other current assets | | 201,901 | | 209,269 |
| | | | 1,019,885 | | 1,035,240 |
| Insurance Fund | | | 5,612 | | 5,903 |
| Investments | | | 362,121 | | 36,399 |
| Properties | | | 5,770,982 | | 5,612,173 |
| Other Assets and Deferred Charges | | | 308,011 | | 100,050 |
| | | | $7,466,611 | | $6,789,765 |
| Liabilities | | | | | |
| Current Liabilities | Bank loans and other indebtedness | | $ 91,687 | | $ 600 |
| | Accounts payable | | 645,725 | | 591,210 |
| | Accrued charges | | 261,545 | | 247,930 |
| | Current portion of long-term debt | | 119,773 | | 46,667 |
| | Other current liabilities | | 167,900 | | 180,824 |
| | | | 1,286,630 | | 1,067,231 |
| Provision for Insurance | | | 5,612 | | 5,903 |
| Other Liabilities and Deferred Credits | | | 273,071 | | 288,576 |
| Long-Term Debt | | | 2,572,613 | | 2,311,131 |
| Minority Interest in Subsidiary Companies | | | 4,345 | | 4,345 |
| Shareholder's Equity | Capital stock of Canadian National Railway Company; 6,523,902 (1983 - 6,487,502) common shares of no par value authorized, issued and outstanding | $2,606,425 | | $2,588,225 | |
| | Retained earnings | 717,915 | 3,324,340 | 524,354 | 3,112,579 |
| | | | $7,466,611 | | $6,789,765 |

On behalf of the Board: Elizabeth J. Hewes, Director
J. Maurice LeClair, Director

See accompanying notes to consolidated financial statements.

# Consolidated Statement of Retained Earnings

| Year ended December 31 | 1984 | 1983 | 1982 |
|---|---|---|---|
| (in thousands) | | | |
| Balance, beginning of year | $524,354 | $354,487 | $577,522 |
| Net income (loss) for the year | 241,951 | 212,333 | (223,035) |
| | 766,305 | 566,820 | 354,487 |
| Dividend | 48,390 | 42,466 | – |
| Balance, end of year | $717,915 | $524,354 | $354,487 |

See accompanying notes to consolidated financial statements.

# Consolidated Statement of Changes in Financial Position



| | Year ended December 31 (in thousands) | 1984 | 1983 | 1982 |
|---|---|---|---|---|
| | Cash, beginning of year * | $ 58,944 | $ (114,005) | $ (63,721) |
| Provided from (used for) operations | Sources: | | | |
| | Net income (loss) for the year | 241,951 | 212,333 | (223,035) |
| | Non-cash charges to income: | | | |
| | Depreciation | 260,950 | 254,006 | 240,079 |
| | Amortization of deferred foreign exchange loss | 65,427 | – | – |
| | Other amortization | 494 | 508 | 512 |
| | Loss (income) of equity investees less dividends | (16,207) | 731 | (1,979) |
| | Provision for impairment of investments | – | – | 97,407 |
| | Changes in working capital items ** | 84,123 | 195,906 | (48,878) |
| | Net proceeds from disposal of assets | 31,874 | 41,728 | 16,236 |
| | Other | (37,894) | 54,590 | 24,321 |
| | | 630,718 | 759,802 | 104,663 |
| | Uses: | | | |
| | Additions to properties | 713,149 | 714,413 | 648,100 |
| | Investments | 19,569 | 1,623 | 4,673 |
| | Working capital of previously consolidated subsidiary | 15,855 | – | – |
| | Dividend | 48,390 | 42,466 | – |
| | | 796,963 | 758,502 | 652,773 |
| | Net provided from (used for) operations | (166,245) | 1,300 | (548,110) |
| Provided from (used in) financing activities | Issuance of long-term debt | 132,140 | 124,207 | 536,076 |
| | Reduction of long-term debt | (134,726) | (54,358) | (42,550) |
| | Issuance of capital stock | 18,200 | 101,800 | 4,300 |
| | Net provided from financing activities | 15,614 | 171,649 | 497,826 |
| Net increase (decrease) in cash during the year | | (150,631) | 172,949 | (50,284) |
| | Cash, end of year * | $ (91,687) | $ 58,944 | $ (114,005) |

* Net of current bank loans and other indebtedness
** Excluding cash and current bank loans and other indebtedness

See accompanying notes to consolidated financial statements.

## Note 1: Summary of Significant Accounting Policies

### Introduction

All references in these Notes to the "Company" refer to Canadian National Railway Company which is wholly-owned by the Government of Canada and, unless the context otherwise requires, its consolidated subsidiaries, and all references to the "System" mean Canadian National Railway Company and its consolidated subsidiaries together with the lines of railway, marine, telecommunications and other property entrusted by the Government of Canada to the Company for management and operation.

### a) Principles of Consolidation

The consolidated financial statements include the accounts of all subsidiaries except CN Marine Inc. and also include the Company's share of the assets, liabilities, revenues and expenses of CNCP Telecommunications which is accounted for by the proportionate consolidation method; CN's share in the activities of CNCP Telecommunications represents slightly less than two-thirds of the activities of CN Communications. Also, consistent with the legislation governing the System, the accounts of the Canadian Government Railways entrusted to the Company by the Government of Canada are included in the consolidated financial statements. Since, under Orders in Council issued in December 1984, control of CN Marine Inc. passed to the Government of Canada on January 1, 1985 and as it is intended that ownership thereof be transferred from CN to the Government during 1985, that company's accounts have been deconsolidated effective January 1, 1984 and CN's investment in it has been accounted for by the equity method.

Investments in companies in which the Company has less than a majority interest are accounted for by the equity method, where appropriate.

### b) Reporting by Division

In presenting the results by division and CN Enterprises, charges for services performed by one division for another, which are made generally at market value, have not been eliminated. Consolidated net income is not affected by this practice.

### c) Material and Supplies

The inventory is valued at laid down cost based on weighted average cost for ties and rails, latest invoice price for fuel and new materials in stores, and at estimated utility or sales value for usable second hand, obsolete and scrap materials.

### d) Properties

Properties are carried at cost, which, in the case of properties brought into the system on January 1, 1923, is the aggregate of the values then appearing in the books of the railways now comprised in the System, less a write-down of $262.8 million at the time of capital revision in 1937.

Accounting for railway and telecommunications properties is carried out in accordance with rules issued by the Canadian Transport Commission and the Canadian Radio-television and Telecommunications Commission respectively (Canadian properties), and the Interstate Commerce Commission (United States properties). Generally, major additions and replacements are capitalized and interest costs are charged to expense.

The cost of depreciable assets retired or disposed of, less salvage, is charged to accumulated depreciation, in accordance with the group plan of depreciation except for CN Route and CN Hotels divisions which follow the unit plan whereby gains or losses are taken into income as they occur.

**Note 1: Summary of Significant Accounting Policies** (Cont'd)

e) Depreciation

Depreciation is calculated at rates sufficient to write off properties over their estimated useful lives, generally on a straight-line basis. For railway and telecommunications properties, rates are authorized by the Canadian Transport Commission, the Canadian Radio-television and Telecommunications Commission and the Interstate Commerce Commission. The rates for significant classes of assets are as follows:

| | Annual Rate |
|---|---|
| Ties | 2.89% |
| Rails | 1.87% |
| Other track material | 1.90% |
| Ballast | 2.76% |
| Road locomotives | 5.23% |
| Freight cars | 1.73%-3.18% |
| Commercial communication systems | 6.12% |

Hotel properties are depreciated at annual rates of 2% to 10%.

f) Transportation Revenues

Transportation revenues are generally recognized on completion of movements, with interline movements being treated as complete when the shipment is turned over to the connecting carrier. Costs associated with uncompleted movements are generally deferred.

g) Pensions

Current service costs are charged to operations as they accrue. Past service costs are charged to operations in annual amounts covering principal and interest over varying periods.

The funding payments are determined in accordance with the accrued benefit acturial cost method.

h) Foreign Exchange

Effective January 1, 1984, the Company adopted prospectively the Canadian Institute of Chartered Accountants' recommendations for foreign currency translation. The financial statements and information related to periods prior to 1984 have not been restated for this change in accounting principle.

The Company's foreign operations are classified as integrated and are translated and accounted for on the following bases. Current assets (excluding material and supplies), current liabilities and long-term debt are translated at the rates in effect at the balance sheet date, whereas other assets and other liabilities are translated at historical rates. Revenues and expenses are translated at average rates during the year, except for depreciation which is translated at exchange rates prevailing when the related properties were acquired. Currency gains and losses are reflected in net income for the year except for unrealized foreign currency gains and losses on long-term debt, which are deferred and amortized over the remaining life of the related debt.

The Company's own foreign denominated assets and liabilities are accorded similar treatment. Revenues and expenses are translated at rates prevailing at the time of the transactions.

i) Leases

Leases which satisfy the criteria for capital leases and which have been entered into after 1981 have been capitalized. Other leases have been recorded as operating leases.

**Note 2: Investments**

| December 31 (in thousands) | Percentage of Voting Interest | 1984 | 1983 |
|---|---|---|---|
| Companies accounted for by equity method | | | |
| Chicago and Western Indiana Railroad Company | 20% | $ 5,916 | $ 6,010 |
| CN Marine Inc.* | 100% | 324,682 | - |
| The Toronto Terminals Railway Company | 50% | 10,682 | 10,682 |
| Other | | 15,894 | 15,146 |
| | | 357,174 | 31,838 |
| Other companies and investments, at cost less provisions for impairment where applicable | | 4,947 | 4,561 |
| Total | | $362,121 | $36,399 |

* The investment in CN Marine Inc. has replaced the following net assets which were deconsolidated effective January 1, 1984 (see Note 1 a):

| (in thousands) | | |
|---|---|---|
| Net assets January 1, 1984 | | |
| Net current assets | | $ 15,855 |
| Net property investment | | 261,516 |
| Net other assets and deferred charges | | 12,753 |
| | | 290,124 |
| Changes during 1984 | | |
| Investment in capital stock | $ 18,200 | |
| Equity income | 21,888 | |
| | 40,088 | |
| Less Dividend | 5,530 | 34,558 |
| Net assets - Equity at December 31, 1984 | | $324,682 |

**Note 3:
Properties**

| December 31 | | | 1984 | | | 1983 |
|---|---|---|---|---|---|---|
| | Cost | Accumulated Depreciation | Net | Cost | Accumulated Depreciation | Net |
| (in thousands) | | | | | | |
| CN Rail | $7,256,076 | $2,675,878 | $4,580,198 | $6,785,361 | $2,597,619 | $4,187,742 |
| TerraTransport | 100,118 | 54,646 | 45,472 | 98,871 | 50,311 | 48,560 |
| Grand Trunk Corporation | 553,658 | 150,214 | 403,444 | 537,143 | 135,287 | 401,856 |
| CN Enterprises | | | | | | |
| CN Communications | 709,762 | 281,943 | 427,819 | 674,181 | 258,557 | 415,624 |
| CN Hotels | 199,035 | 68,549 | 130,486 | 193,352 | 68,821 | 124,531 |
| CN Exploration | 41,731 | 5,264 | 36,467 | 28,171 | 2,285 | 25,886 |
| CN Real Estate | 66,261 | 17,812 | 48,449 | 54,492 | 11,879 | 42,613 |
| Other Businesses | 33,529 | 1,615 | 31,914 | 31,552 | 26 | 31,526 |
| CN Route | 105,630 | 56,472 | 49,158 | 108,873 | 54,586 | 54,287 |
| Miscellaneous | 28,783 | 11,208 | 17,575 | 27,525 | 9,493 | 18,032 |
| CN Marine Inc.* | – | – | – | 302,721 | 41,205 | 261,516 |
| | $9,094,583 | $3,323,601 | $5,770,982 | $8,842,242 | $3,230,069 | $5,612,173 |
| Amounts included above with respect to Canadian Government Railways entrusted to the Company by the Government of Canada | $ 982,132 | $ 540,085 | $ 442,047 | $ 945,772 | $ 524,886 | $ 420,886 |

At December 31, 1984 the gross value of assets under capital leases included above was $51.3 million (1983 – $38.0 million) and related accumulated amortization thereon amounted to $4.0 million (1983 – $2.7 million).

* See Note 1a).

**Note 4:**
**Long-Term Debt**

| | December 31 | Maturity | Currency in which payable | 1984 | 1983 |
|---|---|---|---|---|---|
| | | | | (in thousands) | |
| Bonds, Debentures and Notes | Canadian National 5 3/4% 25 Year Bonds (a, b) | Jan. 1, 1985 | Canadian | $ 63,211 | $ 64,168 |
| | Canadian National 8 3/8% 10 Year Bonds | Nov. 15, 1986 | United States | 83,232 | 83,232 |
| | Canadian National 8 7/8% 10 Year Bonds (b) | Mar. 1, 1987 | Canadian | 46,157 | 47,924 |
| | Canadian National 5% 27 Year Bonds (a, b) | Oct. 1, 1987 | Canadian | 97,433 | 100,141 |
| | Canadian National 14 5/8% 10 Year Notes | Dec. 1, 1991 | United States | 117,817 | 117,817 |
| | Canadian National 9 1/4% 20 Year Sinking Fund Debentures | Mar. 15, 1998 | United States | 124,631 | 133,533 |
| | Canadian National 8 3/8% 25 Year Sinking Fund Debentures | July 1, 2002 | United States | 95,342 | 100,639 |
| | Canadian National 9 7/10% 25 Year Sinking Fund Debentures | July 15, 2004 | United States | 174,940 | 174,940 |
| | Canadian National 13% 20 Year Sinking Fund Debentures | Nov. 15, 2004 | Canadian | 100,000 | – |
| | Canadian National 14% 25 Year Sinking Fund Debentures | Jan. 15, 2006 | United States | 178,783 | 178,783 |
| | Canadian National 15% 25 Year Sinking Fund Debentures | June 1, 2006 | United States | 181,238 | 181,238 |
| | Canadian National 16 1/4% 25 Year Sinking Fund Debentures | Mar. 1, 2007 | United States | 183,053 | 183,053 |
| | Canadian National 14 3/4% 30 Year Sinking Fund Debentures | Sept. 1, 2012 | United States | 247,984 | 247,984 |
| | Canadian National 12% 30 Year Sinking Fund Debentures | Mar. 15, 2013 | United States | 122,548 | 122,548 |
| | Buffalo and Lake Huron 5 1/2% 1st Mortgage Bonds | Perpetual | Sterling | 795 | 795 |
| | Buffalo and Lake Huron 5 1/2% 2nd Mortgage Bonds | Perpetual | Sterling | 1,228 | 1,228 |
| | Total Bonds, Debentures and Notes | | | 1,818,392 | 1,738,023 |
| Government of Canada Loan and Advances (c) | Government of Canada loan | | Canadian | 260,331 | 268,377 |
| | Canadian Government Railways advances for working capital | | Canadian | 14,075 | 14,075 |
| | Total Government of Canada Loan and Advances | | | 274,406 | 282,452 |
| Other | Amounts owing under equipment purchase agreements (d) | | United States | 160,993 | 183,637 |
| | Swiss borrowings (e) | | Swiss Francs | 129,158 | 129,158 |
| | Capital lease obligations (f) | | Various | 42,509 | 30,297 |
| | Promissory note 9 5/8% (g) | | Canadian | 1,423 | 1,703 |
| | Income debenture (h) | | Canadian | 8,243 | – |
| | Adjustment to current exchange rate (see Note 1h) | | | 271,660 | – |
| | Total Other | | | 613,986 | 344,795 |
| | | | | 2,706,784 | 2,365,270 |
| | Less: | | | | |
| | Current portion of long-term debt (1984 at current exchange rates, 1983 at historical exchange rates) | | | 119,773 | 42,273 |
| | Other | | | 14,398 | 11,866 |
| | | | | 134,171 | 54,139 |
| | **Long-Term Debt** | | | **$2,572,613** | **$2,311,131** |

**Note 4: Long-Term Debt** (Cont'd)

a) Guaranteed by the Government of Canada.

b) These bonds are subject to repurchase arrangements.

c) $213.5 million of the Government of Canada loan bears interest at 8 3/4% per annum and is payable in equal semi-annual payments of $13.63 million covering principal and interest to June 30, 1998. Terms and conditions pertaining to the balance have not yet been finalized. The weighted average interest rate on the $213.5 million loan and the advances outstanding at December 31, 1984 and 1983, was approximately 8.2% per annum.

d) Secured by rolling stock and payable by semi-annual or quarterly instalments over various periods to 1995 at interest rates ranging from 8% to 17 3/4%. As at December 31, 1984, the principal amounts are payable as U.S. $153.0 million (December 31, 1983 - U.S. $174.7 million).

e) A private placement of 100 million Swiss Francs bearing interest at 5 1/8%, repayable on March 16, 1988, and a bank loan of 100 million Swiss Francs bearing interest at 5 1/2% and repayable on April 8, 1988. Both are subject to earlier repayment at the Company's option.

f) Interest rates for these leases range from approximately 10 3/4% to 15 3/4% with expiry dates occurring during the years 1985 through 2003. The imputed interest on these leases amounts to $44.4 million (1983 - $15.1 million).

g) Repayable by semi-annual instalments of $218,503, including principal and interest, to August 1, 1988.

h) Payment of non-cumulative annual interest at 16.55% and repayment of principal during the term and at maturity of the debenture in 2008 is conditional on the annual financial results of one of the Company's operations.

(i) Principal repayments, including sinking fund repayments and repurchase arrangements, on debt outstanding at December 31, 1984, as follows:

| Year ending December 31: | (in thousands) |
|---|---|
| 1985 | $119,773 |
| 1986 | 167,476 |
| 1987 | 205,423 |
| 1988 | 238,529 |
| 1989 | 73,671 |
| 1990 - 1994 | 628,017 |
| 1995 - 1999 | 527,849 |
| 2000 - 2004 | 416,352 |
| 2005 - 2009 | 169,178 |
| 2010 - 2013 | 81,284 |

**Note 5: Shareholder's Equity**

a) Capital Stock

During the year, 36,400 shares (1983 - 203,600) of the no par value common stock of the Company were issued to the Government of Canada at a value of $18,200,000 (1983 - $101,800,000) in completion of an arrangement, whereby the Government purchased shares in the capital stock of the Company as a contribution to the cost of CN Marine Inc.'s capital projects. The aggregate value of shares issued to December 31, 1984 under this arrangement was $157,590,000.

b) Retained Earnings

Under its governing legislation, the Company is required to pay to the Receiver General for Canada a dividend equal to 20% of net income for the year or such greater percentage as the Governor in Council may direct. Accordingly, a dividend representing 20% of the net income for the year has been accrued and is included in Other current liabilities.

**Note 6:**
**Major Commitments**

a) Leases

(i) The Company's commitments as at December 31, 1984,under leases, excluding those which have been capitalized and for which the lease obligations are recorded as long-term debt (see Note 4), are as follows:

| Non-Cancellable Leases | Capital Leases | Operating Leases |
|---|---|---|
| Year ending December 31 | | |
| (in thousands) | | |
| 1985 | $ 50,414 | $ 62,652 |
| 1986 | 45,059 | 55,764 |
| 1987 | 43,302 | 51,974 |
| 1988 | 40,282 | 48,195 |
| 1989 | 32,562 | 44,460 |
| 1990 - 1994 | 28,282 | 97,449 |
| 1995 - 1999 | 4,596 | 44,942 |
| thereafter | 1,891 | 8,133 |
| Total minimum lease payments | 246,388 | $413,569 |
| Less amount representing imputed interest | 60,459 | |
| Present value of net minimum lease payments under capital leases | $185,929 | |

A significant portion of the leases is in respect of railway rolling stock and many of them provide renewal options and an option to purchase the property at fair market value at the end of the lease term.

(ii) Rental expenses under all lease arrangements were:

| Year ended December 31 | 1984 | 1983 | 1982 |
|---|---|---|---|
| (in thousands) | | | |
| Total expenses | $197,041 | $169,328 | $176,073 |
| Expenses under capital leases not included in long-term debt | $ 49,380 | $ 46,899 | $ 47,779 |

**Note 6: Major Commitments** (Cont'd)

(iii) Net change in income and increases in assets and liabilities in the consolidated financial statements, which would have arisen if leases entered into prior to 1982 and which satisfied the criteria for capital leases had been capitalized, are as follows:

| Year ended December 31 | 1984 | 1983 | 1982 |
|---|---|---|---|
| (in thousands) | | | |
| Net increase in income | $ 3,036 | $ 2,272 | $ 596 |
| Increase in Assets | | | |
| Properties | | | |
| Leased properties under capital leases | $293,825 | $295,782 | $296,019 |
| Less accumulated amortization | 193,172 | 172,959 | 152,292 |
| | 100,653 | 122,823 | 143,727 |
| Other assets and deferred charges | | | |
| Unamortized deferred exchange loss | 23,323 | – | – |
| | $123,976 | $122,823 | $143,727 |
| Increase in Current Liabilities | | | |
| Present value of obligations under capital leases | $ 33,954 | $ 28,500 | $ 25,817 |
| Increase in Non-Current Liabilities | | | |
| Present value of obligations under capital leases | $154,832 | $186,288 | $208,292 |
| Adjustment to current exchange rate (see Note 1 h) | 31,097 | – | – |
| | 185,929 | 186,288 | 208,292 |
| Less current portion | 33,954 | 28,500 | 25,817 |
| | $151,975 | $157,788 | $182,475 |

b) Other

The Company has commitments at December 31, 1984, for capital expenditures of $124.5 million for railway ties and $104.9 million for rolling stock.

**Note 7:**
**Subsidies**
Revenues include the following subsidies:

| Year ended December 31 | 1984 | 1983 | 1982 |
|---|---|---|---|
| (in thousands) | | | |
| Government of Canada | | | |
| a. Payments under the Railway Act paid under authority of that Act and the related Appropriation Act in respect of certain uneconomic operations, services and prescribed rates which railways are required by the Railway Act to maintain | $ 48,762* | $205,468 | $229,494 |
| b. Interim payments to partially offset revenue shortfalls associated with the cost of carrying grain at uneconomic statutory rates | 8,660* | 228,452 | — |
| c. Maritime Freight Rates Act and Atlantic Region Freight Assistance Act subsidies | 20,727 | 17,361 | 16,161 |
| d. Other | 2,433 | 6,154 | 6,529 |
| Other | 168 | 168 | 803 |
| | $ 80,750 | $457,603 | $252,987 |

* Effective January 1, 1984, the Western Grain Transportation Act provided for increases in rail freight rates for certain grains and grain products, most of which were previously carried at uneconomic statutory rates. The new rates enable the Company to recover substantially all of the costs of carrying grain traffic through tariff charges being paid partly by the Government of Canada and partly by shippers. Concurrently, apart from a final delayed payment received in 1984, the interim payments referred to in b. above ceased, as did the payments included in a. above for branch lines that ceased to be uneconomic.

**Note 8: Pensions**

The Company has retirement benefit plans covering substantially all its employees under which they are entitled to benefits at retirement age generally based on compensation and length of service and/or contributions. Annual pension costs were as follows:

| Year ended December 31 | 1984 | 1983 | 1982 |
|---|---|---|---|
| (in thousands) | | | |
| | $167,156 | $138,252 | $185,359 |

The effect of the most recent actuarial valuation was a reduction of $46.4 million in 1984 pension costs (1983 – $47.1 million).

The total amount of past service costs remaining to be charged to operations at December 31, 1984, 1983 and 1982 based on the latest actuarial valuation at the time and adjusted for subsequent changes, aggregate:

| At December 31 | 1984 | 1983 | 1982 |
|---|---|---|---|
| (in thousands) | | | |
| Canadian plans | $1,480,297 | $1,415,981 | $1,526,280 |
| U.S. plans | 13,347 | 13,682 | 13,710 |
| | $1,493,644 | $1,429,663 | $1,539,990 |

The past service costs relating to the Canadian plans at December 31, 1984 will be charged to operations in annual amounts, including principal and interest, as follows:

| | Annual Cost (in thousands) | | Annual Cost (in thousands) |
|---|---|---|---|
| 1985 | $ 96,182 | 1996 | $174,200 |
| 1986 | 162,959 | 1997 | 128,463 |
| 1987 | 150,380 | 1998 | 100,047 |
| 1988 | 158,842 | 1999 | 97,367 |
| 1989 | 167,769 | 2000 | 102,722 |
| 1990 | 177,188 | 2001 | 108,372 |
| 1991 | 187,124 | 2002 | 51,882 |
| 1992 | 173,984 | 2003 | 54,735 |
| 1993 | 157,413 | 2004 | 57,746 |
| 1994 | 161,924 | 2005 | 60,922 |
| 1995 | 171,066 | 2006 | 64,273 |

The major portion of the past service costs relating to the U.S. plans at December 31, 1984 will generally be amortized at an annual rate of $1.6 million including principal and interest to 1993 inclusive.

In 1984 and 1983, charges to operations exceeded funding by $36.6 million and $25.4 million respectively whereas for the year 1982 funding exceeded the charge to operations by $4.3 million. The cumulative excess of charges to operations over funding requirements amounts to $118.2 million (1983 – $81.6 million) of which $54.1 million (1983 – nil) is included in Current Liabilities and $64.1 million (1983 – $81.6 million) is included in Other Liabilities and Deferred Credits.

The actuarially-computed value of vested benefits at December 31, 1981, the date of the latest actuarial valuation, exceeded the total of the pension funds at that date by $214.8 million.

**Note 9:**
**Miscellaneous Loss**
Miscellaneous loss consists of the following:

| Year ended December 31 | 1984 | 1983 | 1982 |
|---|---|---|---|
| (in thousands) | | | |
| Miscellaneous revenues | $ 1,887 | $ 1,851 | $ 1,839 |
| Interest | | | |
| Total interest on long-term debt | 281,097 | 274,180 | 236,206 |
| Amortization of foreign exchange on long-term debt | 65,427 | – | – |
| Interest on short-term borrowings | 15,907 | 7,950 | 7,182 |
| Interest on investments | (13,320) | (13,687) | (3,015) |
| Total interest (net) | 349,111 | 268,443 | 240,373 |
| Interest assigned to divisions | (261,407) | (248,507) | (214,169) |
| Amortization shown separately on income statement | (65,427) | – | – |
| | 22,277 | 19,936 | 26,204 |
| Other expense (net)* | 17,504 | 23,198 | 91,710 |
| Total expenses | 39,781 | 43,134 | 117,914 |
| Total miscellaneous loss | $ 37,894 | $ 41,283 | $116,075 |

* Other expense (net) consists of general corporate income and expenses and in 1982 included a provision of $61.5 million for impairment of the value of a portfolio investment.

**Note 10:**
**Income Taxes**

a) The Company has timing differences of approximately $500 million which are available to reduce taxable income of future years. Of that amount, about $200 million is due to the excess of the undepreciated capital cost for income tax purposes over the net book value of depreciable assets.

In addition, the following investment tax credits are also available to reduce future income taxes otherwise payable until the related year of expiry:

| Year of Expiry | (in Millions) |
|---|---|
| 1985 | $28.2 |
| 1986 | $35.0 |
| 1987 | $32.0 |
| 1988 | $ 4.2 |
| 1990 | $25.7 |
| 1991 | $35.1 |

The Company is eligible for a refund of 20% of the current year's investment tax credits in respect of qualified expenditures and has recognized the resulting benefit of $8.8 million in "Miscellaneous".

b) The Company's provision for income taxes is made up as follows:

| | 1984 | 1983 |
|---|---|---|
| (in thousands) | | |
| Provision for income taxes based on combined basic Canadian federal and provincial tax rate of 48.0% (1983-48.6%) | $116,325 | $103,149 |
| Increase (decrease) in taxes resulting from: | | |
| Non-allowable scientific research expenditures, net of proceeds from sale of related tax credits | 5,469 | – |
| Refundable investment tax credits | (4,224) | (3,062) |
| Profit on sale of land | (4,076) | (2,221) |
| Other | 3,629 | 1,424 |
| Actual provision for income taxes resulting in an effective tax rate of 48.3% (1983 – 46.9%) | $117,123 | $ 99,290 |

**Note 11:
Segmented Information**

a) Geographic Areas

Virtually all of the System's operations and assets are within Canada with the exception of Grand Trunk Corporation which operates in the United States.

b) International Traffic

In addition to the revenue generated by Grand Trunk Corporation, the System derives revenue from traffic originating or terminating on railroads in the United States. In 1984, such revenues approximated $662 million (1983 - $581 million, 1982 - $528 million).

c) Identifiable Assets by Division

| December 31 | 1984 | 1983 | 1982 |
|---|---|---|---|
| (in thousands) | | | |
| CN Rail | $5,332,545 | $4,886,466 | $4,612,860 |
| TerraTransport | 56,920 | 57,901 | 65,616 |
| Grand Trunk Corporation | 605,774 | 591,851 | 586,727 |
| CN Enterprises | | | |
| CN Communications | 486,828 | 471,750 | 463,827 |
| CN Hotels | 156,482 | 138,783 | 138,781 |
| CN Exploration | 42,035 | 31,111 | 20,845 |
| CN Real Estate | 66,987 | 57,720 | 52,046 |
| Other Businesses | 42,212 | 51,287 | 45,480 |
| CN Route | 87,821 | 90,564 | 92,531 |
| Miscellaneous | 589,007 | 103,149 | 52,596 |
| CN Marine Inc.* | – | 309,183 | 204,662 |
| Total assets per Consolidated Balance Sheet | $7,466,611 | $6,789,765 | $6,335,971 |

d) Capital Expenditures and Depreciation by Division

| | Capital Expenditures** | | | Depreciation | | |
|---|---|---|---|---|---|---|
| | Year ended December 31 | | | Year ended December 31 | | |
| | 1984 | 1983 | 1982 | 1984 | 1983 | 1982 |
| | (in thousands) | | | (in thousands) | | |
| CN Rail | $596,882 | $508,318 | $469,057 | $183,178 | $166,463 | $161,692 |
| TerraTransport | 2,912 | 1,202 | 1,276 | 5,237 | 4,044 | 3,361 |
| Grand Trunk Corporation | 18,231 | 11,264 | 26,161 | 12,772 | 13,366 | 13,553 |
| CN Enterprises | | | | | | |
| CN Communications | 54,061 | 45,631 | 62,260 | 42,323 | 40,679 | 36,374 |
| CN Hotels | 14,728 | 5,074 | 6,168 | 5,725 | 5,748 | 5,932 |
| CN Exploration | 16,987 | 15,216 | 11,988 | 2,992 | 2,028 | — |
| CN Real Estate | 231 | 10,747 | 1,661 | 709 | 637 | 451 |
| Other Businesses | 506 | 8,736 | 34,101 | 1,035 | 822 | 730 |
| CN Route | 8,223 | 8,164 | 4,696 | 5,741 | 7,524 | 8,380 |
| Miscellaneous | 388 | 372 | 280 | 1,238 | 1,093 | 1,089 |
| CN Marine Inc.* | – | 99,689 | 30,452 | – | 11,602 | 8,517 |
| | $713,149 | $714,413 | $648,100 | $260,950 | $254,006 | $240,079 |

* See Note 1 a).
** Represents additions to property, plant and equipment.

| | |
|---|---|
| **Note 12: Other Matters** | a) The Company carries on ordinary business transactions with various entities controlled by the Government of Canada on the same terms and conditions as current transactions with unrelated parties.<br><br>In addition, the Company provides, under contractual arrangements, rail transportation and maintenance and marine services to the Government of Canada and to entities controlled by the latter. The revenue derived from such services rendered in 1984 aggregated $364.8 million (1983 - $462.2 million, 1982 - $487.3 million).<br><br>b) Commencing in 1977, the Government of Canada has agreed to pay to the Company, by way of capital grants not exceeding $557.9 million, certain amounts with respect to expenditures incurred in carrying out rehabilitation programs for branch lines in Western Canada. Total payments received up to December 31, 1984, amounted to $353.2 million of which $64.8 million was received in 1984 (1983 - $50.2 million).<br><br>c) As part of a program commenced in 1981 for the testing and evaluation of railway operations in Newfoundland, the Government of Canada reimbursed CN for certain wage and wage-related costs. Total billings under this program amounted to $4.1 million in 1984 (1983 - $18.4 million). |
| **Note 13: Reclassification of Comparative Figures** | During 1984, changes were made to improve the classification of certain items and for comparative purposes the 1983 and 1982 figures have been reclassified. In the case of the deconsolidation referred to in Note 1 a., the comparative figures have been reclassified in the Consolidated Statement of Income. Other reclassifications have arisen from the combination in 1984 of CN Trucking and CN Express into a new division called CN Route and, in CN Hotels division, the expiry in 1984 of the Hilton contract for management of two major hotels. |

Coopers
&Lybrand

chartered accountants

630 Dorchester Boulevard West
Montreal Quebec Canada
H3B 1W5

telephone (514) 875-5140
cables Colybrand
telex 05-267424

a member firm of
Coopers & Lybrand (International)

February 25, 1985

**Auditors' Report**

To The Minister of Transport
Ottawa, Canada

We have examined the consolidated balance sheets of the Canadian National Railway System as at December 31, 1984 and 1983 and the consolidated statements of income, retained earnings and changes in financial position for each of the years in the three year period ended December 31, 1984. 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, these consolidated financial statements present fairly the financial position of the System as at December 31, 1984 and 1983 and the results of its operations and the changes in its financial position for each of the years in the three year period ended December 31, 1984 in accordance with generally accepted accounting principles applied, except for the change in the method of accounting for foreign exchange translation as set out in Note 1 h) to the consolidated financial statements, on a consistent basis.

Also, in our opinion, the transactions of the corporation and of each subsidiary that have come to our notice in the course of our examination have been within the powers of the System.

Coopers & Lybrand

**Chartered Accountants**

## Supplementary Information Regarding the Effects of Changing Prices (Unaudited)

The financial statements presented in this Annual Report are based on historical prices established in transactions to which the Company was a party. Financial statements prepared on this basis continue to be needed since changes in shareholder's equity in the long run depend on actual transactions and because historical prices based on these transactions generally are the result of arm's length bargaining and provide an objective measure of results that is independently verifiable.

Nevertheless, prolonged periods of significant inflation have resulted in increasing recognition of limitations in the usefulness of conventional historical cost financial statements and of a need for some disclosure about the impact of inflation on the financial position and operating results. Consequently, as recommended by the Canadian Institute of Chartered Accountants (CICA) the Company has set forth supplementary information designed to provide the reader with some insight on the extent to which the Company's capital has been maintained in the inflationary environment.

The CICA recommendations recognize two possible concepts for determining whether the capital has been maintained. The first is the maintenance of operating capability concept, which holds that capital is maintained when the assets of the enterprise remain sufficient to continue the previous level of services. A further refinement of this concept recognizes the extent to which the assets have been financed with borrowed funds and is concerned with the maintenance of the common shareholders' proportionate interest in the operating capability of the entity. The second is the maintenance of financial capital concept which requires that the money amount of the net assets of the company must remain intact.

The elements of the net loss attributable to the shareholder on a current cost basis under an operating capability concept of capital and the items included in Other Supplementary Information disclosed in the 1983 Annual Report have been restated in 1984 average dollars whereas the 1983 figures for properties and net assets have been restated in December 1984 dollars.

Under either concept, the effect of changing prices is determined by using current costs which represent the amount of cash or other consideration that would be needed currently to acquire an asset having the same service potential as embodied by the asset owned. The Company has applied this approach to properties and related depreciation, except that in view of the Government's decision to form a separate Crown Corporation for CN Marine, the net book value of that Division's properties was included in the current costs of properties for 1984. Using current costs as defined above, the properties would be increased by $16,734,455,000 in 1984 (1983 - $17,253,367,000) when compared to their historical cost measured in nominal dollars. Similarly, depreciation for 1984 based on the average current cost of the properties for 1984 would be higher than depreciation based on the historical cost of the properties, by $606,452,000 in 1984 (1983 - $598,607,000). The major explanation for this difference is that many of the Company's properties are old but can still be used because of their long economic life.

The accompanying statement is based on the maintenance of operating capability concept. In addition to the increased depreciation, it includes a financing adjustment which indicates the extent to which increases in the current cost amounts of assets during the year do not, on the basis of the existing relationship between debt and equity, need to be charged against present and future revenues to ensure maintenance of the common shareholder's proportionate interest in the operating capability.

It should be understood that much remains to be learned about reporting the effects of changing prices and a complete assessment of the usefulness of this supplementary information will only be possible after an extended period of preparing and using it. The CICA has recognized that its recommendations do not deal with all practical problems that may be encountered and consequently has provided for flexibility and experimentation in applying them and is planning a comprehensive review of them within five years. These limitations should be recognized in using the supplementary information. In particular, it should not be interpreted as an indication that the Company intends to replace particular assets or that the costs presented represent the costs that would be incurred if the assets were replaced. Therefore, this information should not be used in evaluating the Company's performance until a sufficient period of experimentation has elapsed and conclusive evidence has been obtained regarding its appropriateness.

On the current cost basis the Company incurred a loss in both 1983 and 1984, as compared with a reported income on the historical cost basis. This is mainly due to the higher annual depreciation recognized on the current cost basis. While there can be some question regarding the absolute amounts, it points up the general problem of financing new and replacement assets in an environment which has been affected by the ravages of inflation. In responding to this situation, CN must seek a full commercial return on its services, which return must reflect the cost of maintaining its operating capability. At the same time, management must continue to take full advantage of advances in technology to control the level of future capital and operating expenditures. Over and above this, while there has been increasing recognition by Governments of the need to control inflation, the availability of information regarding the impact of changing prices on enterprises should exert a positive influence on their formulation of economic policies, including taxation.

**Consolidated Statement of Income Adjusted to the Current Cost Basis Under an Operating Capability Concept of Capital**

| Year ended December 31 | 1984 | 1983 |
| --- | --- | --- |
| (Unaudited)<br>(in thousands) | | |
| Net income on an historical cost basis | $ 241,951 | $ 221,573 |
| Depreciation adjustment | (606,452) | (598,607) |
| Financing adjustment | 84,903 | 82,608 |
| Net loss attributable to the shareholder on a current cost basis under an operating capability concept of capital | $ 279,598 | $ 294,426 |

The financing adjustment was based on the current cost adjustment for depreciation made to income. Alternatively, had the financing adjustment been based on the changes in the current cost of properties during 1984 it would have amounted to $135,170,000 (1983 – $204,808,000) and the net loss attributable to the shareholder on a current cost basis under an operating capability concept of capital would have been reduced by $50,267,000 (1983 – $122,200,000).

**Other Supplementary Information**

| Year ended December 31 | 1984 | 1983 |
| --- | --- | --- |
| (Unaudited)<br>(in thousands) | | |
| Increase in current cost of properties | $1,062,110 | $1,484,114 |
| Effect of general inflation | 815,822 | 990,841 |
| Excess of increase in current cost over the effect of general inflation | $ 246,288 | $ 493,273 |
| Gain in general purchasing power from having net monetary liabilities | $ 117,745 | $ 139,240 |

**Schedule of Assets on a Current Cost Basis:**

| December 31 | 1984 | | 1983 | |
| --- | --- | --- | --- | --- |
| | Historical Cost Basis | Current Cost Basis (Unaudited) | Historical Cost Basis | Current Cost Basis (Unaudited) |
| (in thousands) | | | | |
| Properties | $5,770,982 | $22,505,437 | $5,612,173 | $22,865,540 |
| Net assets (shareholder's equity) | $3,324,340 | $20,058,794 | $3,112,579 | $20,271,898 |

The above amounts reflect estimated current costs. There is a continuing need for development of the methods used in determining these costs and we expect to continue our efforts in this regard. The following notes provide a general description of the methods followed in 1984.

**Notes to Supplementary Information Regarding the Effects of Changing Prices**

1. Bases and Methods Used in Determining Current Cost Information

a) Ties

The average current cost per tie applied to the total quantity of ties was obtained by applying the applicable index to the aggregate of the recent current average purchase price for untreated ties and the average treatment cost per tie.

b) Rails

The average current cost per ton applied to the tonnage of rail was determined by applying the applicable index to invoice prices and increased by an estimate for welding costs.

c) Other Track Material and Ballast

The current cost of other track material and ballast was determined using estimates of direct prices.

d) Road Locomotives and Freight Cars including those under Capital Leases and Grading

The current cost of road locomotives and freight cars including those under capital leases and grading was determined by applying the applicable indices obtained from Statistics Canada and the Association of American Railroads.

e) Commercial Communications Systems

There are several sub-categories under this class and for each category the most practical pricing technique has been used in determining current cost. Pricing techniques used include indexing based on indices produced by the Company and Statistics Canada as well as reference pricing and direct pricing.

f) Land and Buildings

The current cost of land is the estimated value determined by appraisals primarily using the "market value for existing use" approach. The current cost of buildings was obtained by applying the applicable index to recently estimated construction costs for buildings with similar service potential.

g) Construction in Progress

The historical cost of assets which are currently being constructed and are not yet in service approximates their current cost and is included on the current cost information.

h) Donations and Grants

The current values for donations and grants were based on the methods employed for the related asset costs.

i) Depreciation Expense

Current cost depreciation expense was calculated by reference to the average current cost of properties.

## 2. Significant Items not Presented on a Current Cost Basis

### a) Material and Supplies

The material and supplies inventory is used by the Company and is not normally available for resale. The amount reported in the historical cost financial statements approximates the amount that would be required to acquire similar items on a current basis.

### b) Unrecorded Capital Leases

In accordance with the transitional provisions regarding lease accounting, financial information related to capital leases entered into prior to 1982 is disclosed in Note 6 to the financial statements. Such information has not been presented on a current cost basis.

# Canadian National Railways Pension Trust Fund Consolidated Statement of Financial Position as at December 31

| | (in thousands) | 1984 | 1983 |
|---|---|---|---|
| Investments | Bonds - quoted market value 1984 - $1,768,735; 1983 - $1,570,168 | $1,744,902 | $1,567,820 |
| | Mortgages | 293,580 | 305,530 |
| | Real estate | 187,761 | 187,125 |
| | Oil and gas | 67,604 | 56,402 |
| | Equities – quoted market value 1984 – $1,561,107; 1983 – $1,478,204 | 1,169,307 | 1,066,217 |
| | Short-term investments | 218,541 | 176,465 |
| | | 3,681,695 | 3,359,559 |
| | Cash | 1,408 | 1,140 |
| | Accounts receivable – Canadian National Railways | 7,584 | 12,309 |
| | Accrued interest and other assets | 58,561 | 49,394 |
| | | 3,749,248 | 3,422,402 |
| Amount to be funded | Amount to be funded by the Company in accordance with the Pension Benefits Standards Act by special payments to December 31, 2006 | | |
| | Balance, beginning of year | 1,497,620 | 1,582,050 |
| | Add increases during year | 115,810 | — |
| | Deduct – Principal payments | (14,945) | (429) |
| | – Decreases during year | — | (84,001) |
| | Balance, end of year | 1,598,485 | 1,497,620 |
| | | $5,347,733 | $4,920,022 |

See accompanying notes to consolidated statement of financial position.

## Auditors' Report

To The Minister of Transport,
Ottawa, Canada

We have examined the consolidated statement of financial position of the Canadian National Railways Pension Trust Fund as at December 31, 1984. Our examination was 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, this consolidated financial statement presents fairly the financial position of the Canadian National Railways Pension Trust Fund as at December 31, 1984 and the results of its operations for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Also, in our opinion, proper books of account have been kept and the transactions that have come under our notice have been within the powers of the Trustee.

Mallette, Benoit, Boulanger, Rondeau & Associés

Mallette, Benoit, Boulanger, Rondeau & Associés
Chartered Accountants
Montreal, February 25, 1985

# Canadian National Railways Pension Trust Fund Consolidated Statement of Financial Position as at December 31

| | (in thousands) | 1984 | 1983 |
|---|---|---|---|
| Actuarial Liability for Pension Benefits | Balance, beginning of year | $4,920,022 | $4,690,278 |
| Additions during year | Increases (decreases) in actuarial liability for pension benefits resulting from | | |
| | – Actuarial valuation | — | (126,759) |
| | – Pension Plan amendments, increases in pension benefits to pensioners, and actuarial liability related to current service | 115,810 | 42,758 |
| | | 115,810 | (84,001) |
| | Contributions by employees on account of | | |
| | – Current service | 89,059 | 82,917 |
| | – Prior years' service | 7,873 | 11,642 |
| | | 96,932 | 94,559 |
| | Contributions by the Company relating to current service and/or amount to be funded | 128,722 | 111,173 |
| | Net earnings on investments | 383,590 | 363,102 |
| | | 609,244 | 568,834 |
| | | 5,645,076 | 5,175,111 |
| Deductions during year | Pension benefits paid | 273,343 | 246,016 |
| | Refunds on termination of service | 7,430 | 8,290 |
| | Principal payments applied to amount to be funded | 14,945 | 429 |
| | Reduction in actuarial liability for pension benefits related to transfer of employees to VIA Rail Canada Inc. and CNCP Telecommunications | 1,625 | 354 |
| | | 297,343 | 255,089 |
| | Balance, end of year | $5,347,733 | $4,920,022 |

On behalf of the board: Elizabeth J. Hewes, Director
J. Maurice LeClair, Director

# Actuarial Certificate

To the Trustee
Canadian National Railways
Pension Trust Fund

I have examined the actuarial liability for pension benefits shown in the consolidated statement of financial position of the Canadian National Railways Pension Trust Fund as at December 31, 1984, and in my opinion the amount of $5,347,733,000 represents adequate provision for the actuarial liabilities for all pension benefits of the 1935 and 1959 Pension Plans and of the Northern Alberta Railways Company Pension Plan.

Geoffrey B. White
Fellow of the Canadian Institute of Actuaries

William M. Mercer Limitée
Montreal, February 18, 1985

Notes to Consolidated Statement of Financial Position

Note 1: Summary of Significant Accounting Policies

a) Pension Plans of Canadian National Railways covered by Statement

The Pension Trust Fund consolidated statement of financial position includes the actuarial liability for pension benefits, the investments and the amount to be funded with respect to the 1935 and 1959 Pension Plans and to the Northern Alberta Railways Company Pension Plan.

These plans under which benefits are generally based on compensation and length of service and/or contributions cover substantially all employees of the Canadian National Railway System.

b) Consolidation of Wholly-owned Companies

The Pension Trust Fund has invested in a number of wholly-owned companies. The accounts of these companies are consolidated with the accounts of the Pension Trust Fund.

c) Investment Valuation

(i) Bonds are carried at their amortized cost, plus deferred amounts arising from exchanges made to improve yields which are written-off over the remaining life of the bonds sold;

(ii) Mortgages are carried at outstanding principal balances and are secured by real estate;

(iii) Real estate consists of land and buildings. Land is carried at the lower of cost and net realizable value less encumbrances, and buildings at the lower of cost and net realizable value less encumbrances and accumulated depreciation;

(iv) Oil and gas properties are carried at cost as determined by the full cost method less depletion except that for properties managed by Dome Petroleum Limited no depletion is provided for as the Fund holds an offer to purchase, effective until January 3, 1999, which it may exercise for a consideration equal to their cost less proceeds on disposal of any portion of such properties;

(v) Equities and short-term investments are carried at cost.

The quoted market value of investments in bonds and equities is based on the closing market quotations as of December 31.

d) Determination of Funding Payments

The funding payments are determined in accordance with the accrued benefit actuarial cost method and are based on the latest actuarial valuation as at December 31, 1981.

The principal assumptions underlying the actuarial computations adopted by the Plans' actuary have been developed from the actual experience of the Plans in regard to the members' mortality, disability, retirement, termination of employment, and merit and periodic increases in earnings.

For purposes of the actuarial computations, the Pension Trust Fund is assumed to have a long-term rate of return of 7% per annum on investments and future increases in members' earnings have been projected using economic assumptions consistent with that projection.

The funding payments, including liquidation of the amount to be funded, meet the requirements of the Pension Benefits Standards Act and regulations thereunder. Consistent with the regulations, the Company is making annual special payments over varying periods to 2006.

e) Accounting for Contributions

Contributions from employees are recorded in the period in which the Company makes payroll deductions.

The contributions by the Company are determined in accordance with the requirements of the Pension Benefits Standards Act and the regulations thereunder and are recorded using the accrual method.

f) Income Determination

Dividend income is recorded as of the ex-dividend date. Income from other investments is recorded as earned on an accrual basis.

Gain or loss on sales of equities is based on the average cost.

g) Foreign Exchange

Investments denominated in foreign currencies other than short-term investments are translated at historical rates of exchange. Short-term investments and the quoted market value of investments denominated in foreign currencies are translated at current rates. Foreign dividends and interest income are translated at the rates prevailing when received.

Note 2: Commitments

Outstanding commitments to purchase oil and gas properties amounted to $33 million as at December 31, 1984.

Production: CN Public Affairs and Advertising
Design: Morin, Lessard, Mc'nnis Inc.
Major Photography: Bernard Bohn / Alain Cornu
Printed in Canada