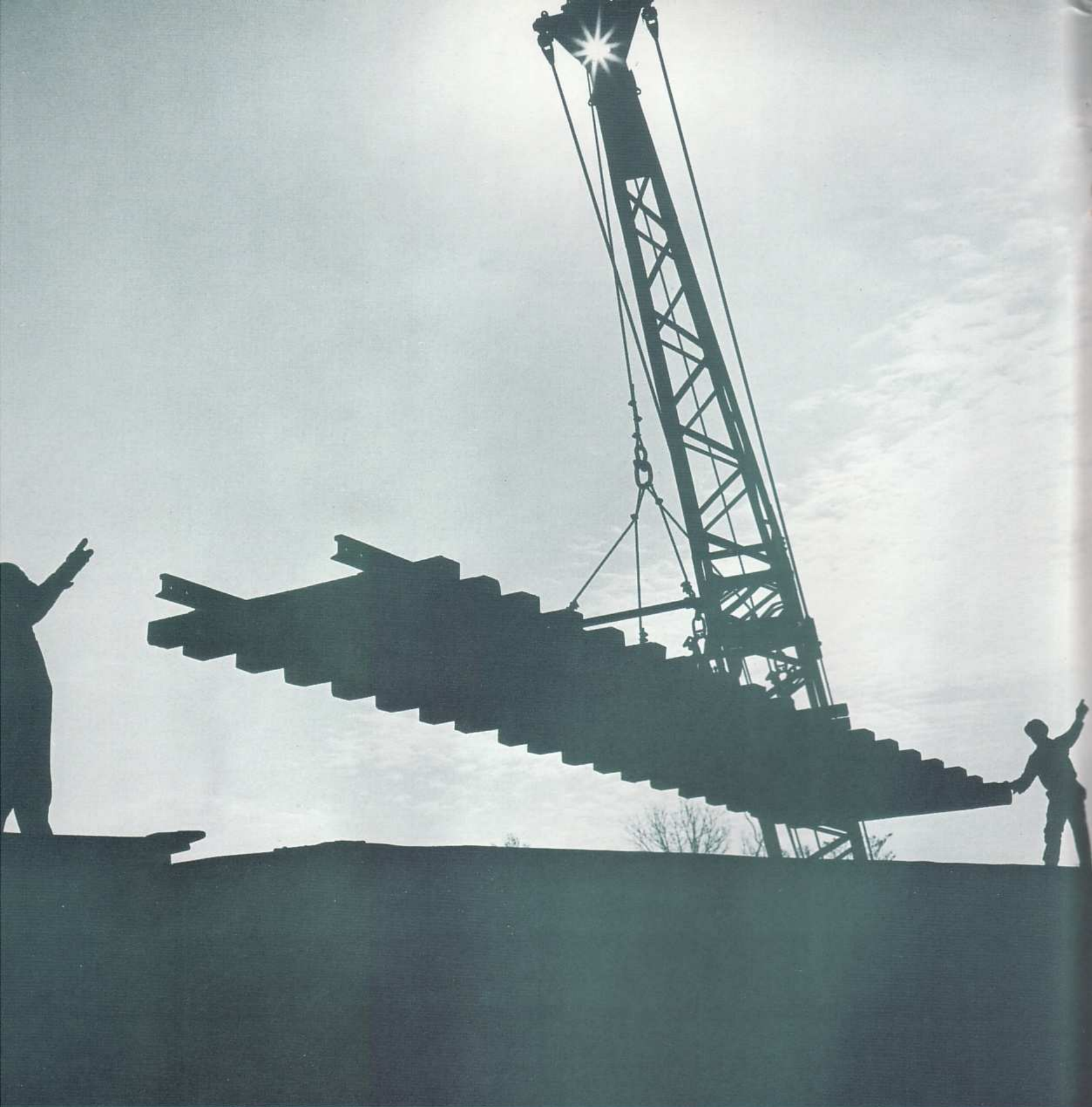




ANNUAL REPORT 1972

ST. LOUIS — SAN FRANCISCO RAILWAY COMPANY



dedicated to service and progress

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St. Louis-San Francisco Railway Company

GENERAL OFFICES: 906 OLIVE STREET ST. LOUIS, MO. 63101



Directors held their July 1972 meeting in Springfield, Missouri, and are pictured in front of Frisco Office Building.

*L to R First Row: Lewis B. Stuart, William A. McDonnell, R. C. Grayson, J. E. Gilliland, Bruce K. Goodman, B. B. Culver, Jr.
Second Row: Lawrason Riggs, III, Elliot H. Stein, Dudley E. Dawson, Jr., C. P. Whitehead, Judson S. Sayre,
Thomas E. Deacy, Jr., Harold F. Ohlendorf. Absent: Edward W. Cook, F. G. McClintock.*

BOARD OF DIRECTORS

• Term Expires 1973

EDWARD W. COOK

President, Cook Industries, Inc., Memphis, Tennessee

* THOMAS E. DEACY, JR.

Attorney, Kansas City, Missouri

*† WILLIAM A. McDONNELL

Chairman of the Finance Committee,
St. Louis-San Francisco Railway Company, St. Louis, Mo.

LAWRASON RIGGS III

Chairman
St. Joe Minerals Corporation, New York, N.Y.

*† ELLIOT H. STEIN

President, Scherck, Stein & Franc, Inc., St. Louis, Mo.

• Term Expires 1974

* B. B. CULVER, JR.

Chairman, Culver Educational Foundation, St. Louis, Mo.

* R. C. GRAYSON

President and Chief Executive Officer,
St. Louis-San Francisco Railway Company, St. Louis, Mo.

JUDSON S. SAYRE

Consultant, Chicago, Illinois

LEWIS B. STUART

Retired Executive Vice President, Ralston Purina Company,
St. Louis, Mo.

† C. P. WHITEHEAD

Retired Chairman of the Board, General Steel Industries,
St. Louis, Mo.

• Term Expires 1975

DUDLEY E. DAWSON, JR.

President and Chief Executive Officer,
Southern Industries Corporation, Mobile, Alabama

* J. E. GILLILAND

Chairman of the Board,
St. Louis-San Francisco Railway Company, Tucson, Arizona

* BRUCE K. GOODMAN

President, Library Plaza Company, Evanston, Illinois

F. G. McCLINTOCK

Chairman and Chief Executive Officer,
The First National Bank & Trust Co. of Tulsa, Tulsa, Okla.

HAROLD F. OHLENDORF

Ohlendorf Farms, Osceola, Arkansas

*Member of Executive Committee

†Member of Finance Committee

#Member of Compensation Committee

OFFICERS

J. E. GILLILAND

Chairman of the Board, Tucson, Arizona

R. C. GRAYSON

President and Chief Executive Officer, St. Louis, Mo.

E. D. GRINNELL, JR.

Vice President-Traffic and Industrial Development,
St. Louis, Mo.

J. H. BROWN

Vice President-Operation, Springfield, Mo.

D. E. ENGLE

Vice President and General Counsel, St. Louis, Mo.

H. B. PARKER

Vice President-Finance and Treasurer, Springfield, Mo.

J. K. BESHEARS

Vice President-Personnel, Springfield, Mo.

G. E. BAILEY

Vice President and Secretary, St. Louis, Mo.

P. E. ODOM

Vice President-Management Services, Springfield, Mo.

J. W. TIPTON

Vice President-Intermodal Services, Springfield, Mo.

TRANSFER AGENTS FOR COMMON STOCK:

First National City Bank, 111 Wall Street, New York, N.Y. 10015

Mercantile Trust Company National Association, 721 Locust Street, St. Louis, Mo. 63101

REGISTRARS FOR COMMON STOCK:

Bankers Trust Company, 16 Wall Street, New York, N.Y. 10015

St. Louis Union Trust Company, 510 Locust Street, St. Louis, Mo. 63101

REGISTRARS FOR BONDS, DEBENTURES AND EQUIPMENT TRUST CERTIFICATES:

First National City Bank, 111 Wall Street, New York, N.Y. 10015

Mercantile Trust Company National Association, 721 Locust Street, St. Louis, Mo. 63101

AUTHENTICATING AGENTS:

First National City Bank, 111 Wall Street, New York, N.Y. 10015 for First Mortgage Bonds, 4% Series A and B, due Jan. 1, 1997 and Sept. 1, 1980, respectively.

Mercantile Trust Company National Association, 721 Locust Street, St. Louis, Mo. 63101 for 5% Income Debentures, Series A, due Jan. 1, 2006.

Annual Meeting of Stockholders second Tuesday in May of each year

TO FRISCO STOCKHOLDERS:

March 5, 1973

Frisco's 1972 earnings were equivalent to \$5.72 per share, up 2.8% from the level of the previous year and second only to the record year of 1952. A new peak in traffic volume, larger tax benefits and higher costs not fully offset by freight rate increases were important factors in our financial results.

Aside from a higher wage-price level, operating expenses reflect a 4.8% increase in revenue ton-miles, sizable expenditures for maintenance and the cost of operating under severe weather conditions in the fourth quarter.

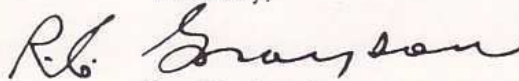
During the year, the Frisco continued to spend liberally to protect the high maintenance standards of both its fixed plant and equipment. More welded rail is being laid every year; in addition, the Company has accelerated its main line bridge renewal program so as to eventually replace wooden bridges and trestles with all-steel or pre-stressed concrete structures. To meet a growing volume, our classification yards are being enlarged at Memphis, Tennessee; Birmingham, Alabama and Springfield, Missouri. To provide us with an improved transcontinental route in connection with the Santa Fe, we also are upgrading our line between Tulsa and Avar, Oklahoma.

At the same time, we continued to search out ways to reduce the burden of maintaining unnecessary trackage. During the year, we received authority to abandon 109 miles of branch lines in Oklahoma, Missouri and Arkansas and are making a careful study of the profitability and potential of other lines.

The pages which follow contain a discussion of the factors affecting the Frisco's operating results. Also of importance to Frisco security holders is the status of legislative proposals to cope with the problems of the whole transportation industry. The Surface Transportation Act, introduced into the 92nd Congress, constituted the most comprehensive piece of transportation legislation considered by Congress in decades. Within its various titles, it contained provisions for attacking many of the ills which currently plague the railroad industry. Congress adjourned before the various bills could be translated into law and we are hopeful that transportation legislation will be among the matters which receive early consideration by the 93rd Congress.

No summary of the year's events would be complete without an acknowledgement of the support and loyalty extended by our stockholders, our customers and our employees. The Directors join me in thanking each of you.

Sincerely,



President and
Chief Executive Officer

FRISCO FACTS

CONSOLIDATED

	1972	1971
Operating revenues	\$238,959,134	\$220,935,474
Operating expenses	\$181,295,041	\$163,361,026
Ratio of expenses to revenues	75.9	73.9
Average number of employees	8,936	8,911
Payroll	\$103,297,500	\$ 93,564,483
Taxes	\$ 18,366,689	\$ 18,232,939
Taxes per share	\$ 7.08	\$ 7.02
Pre-tax Income available for fixed charges	\$ 27,945,325	\$ 27,847,185
Fixed charges	\$ 10,840,796	\$ 10,111,156
Times fixed charges earned — pre-tax	2.6	2.8
Contingent interest	\$ 1,425,725	\$ 1,482,625
Net income	\$ 14,848,804	\$ 14,443,404
Earnings per share	\$ 5.72	\$ 5.56
Dividends per share	\$ 2.475	\$ 2.40

SYSTEM RAIL LINE FREIGHT STATISTICS

Miles of road operated	4,847	4,879
Freight train revenue	\$227,016,878	\$210,288,758
Net ton-miles — revenue (thousands)	14,269,642	13,618,596
Gross ton-miles (thousands)	33,849,541	31,859,649
Train miles	10,557,617	10,124,474
Revenue per ton-mile	1.591¢	1.544¢
Revenue per train mile	\$ 21.50	\$ 20.77
Revenue tons per car	39.2	38.8
Revenue tons per train	1,351.6	1,345.1
Gross tons per train	3,206.2	3,146.8

NET INCOME

Net income of \$14.8 million was up 2.8% from the level of 1971 and equivalent to \$5.72 per share.

The effect of various tax benefits upon net income are discussed on page 10.

DIVIDENDS INCREASE

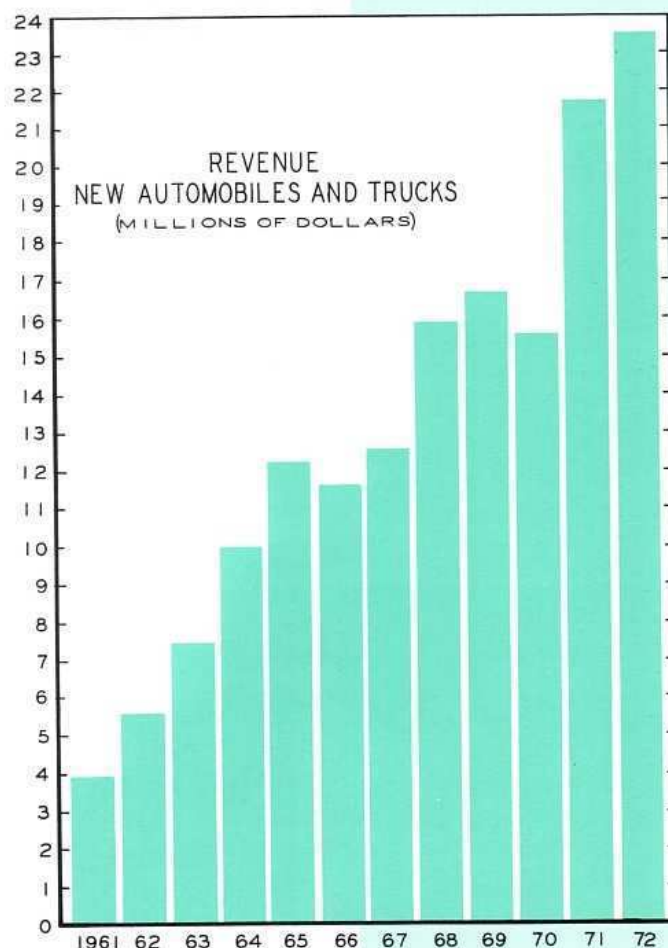
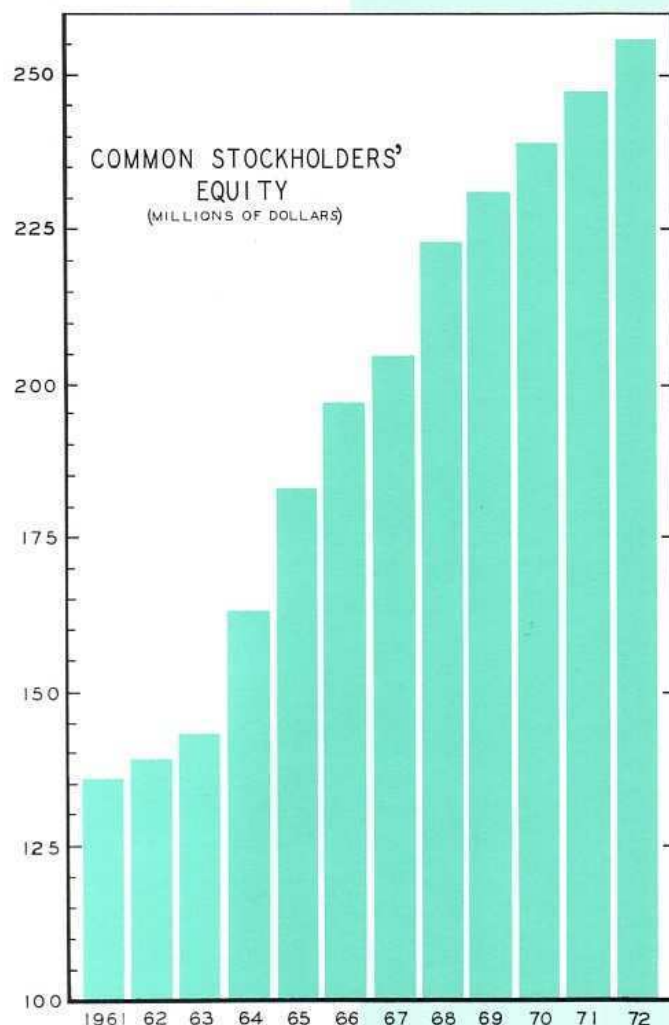
Four dividends totaling \$2.475 were paid in 1972 as follows: 60¢ on March 15 and 62½¢ each on June 15, September 15 and December 15. A total of \$2.40 was paid in 1971.

RECORD REVENUES BUT ADDITIONAL RATE ADJUSTMENTS ARE NEEDED

Under the influence of higher freight rates and a record traffic volume, operating revenues of \$239 million were at an all-time high and 8.2% ahead of the year before.

A 2.5% surcharge became effective on February 5, 1972, and the railroads petitioned the Interstate Commerce Commission to selectively increase rates to a higher level effective May 1, 1972. These increases were not allowed to become effective until October 23, 1972, and then not to the full extent sought. As a result, your Company realized only about \$7.1 million in 1972 from authorized rate increases, which sum was not in and of itself sufficient to offset higher wages and other increased costs. Additional freight rate increases will be necessary in 1973 to help offset known wage and cost increases. On January 22, 1973, your Company joined with other Western and Southern rail carriers in petitioning the Interstate Commerce Commission for a 2% surcharge on freight shipments to more nearly offset higher costs. In denying the petition for an "emergency" surcharge, the Commission stated that the carriers could file for a permanent rate increase. Further action is now being considered by the carriers.

The year began sluggishly. Not until the middle of August did the quality and quantity of Frisco traffic begin to improve noticeably. At that time there was a perceptible pick-up in the movement of the higher-rated commodities. By year-end, Frisco had scored revenue and volume gains in automobiles and trucks, in piggyback and freight forwarder traffic, in food and kindred products, in construction materials, in chemicals, in pulp, paper and related products and in most classifications of freight. While there was a decline in some agricultural crops, the Frisco enjoyed a good winter wheat movement and at year-end was deriving some benefit from the movement of wheat to Russia.





Piggyback traffic a growing part of railway business.

NEW AND ENLARGED PLANTS PROMISE ADDITIONAL TRAFFIC

An important share of Frisco's traffic growth over the years is attributable to new and enlarged plants located along the lines of the Frisco system. During the year, 90 new plants and 19 plant expansions began producing additional freight for the railroad.

One of the largest plant expansions was announced by the Jos. Schlitz Brewing Company for its brewery at Memphis, Tennessee. Originally, this installation was to have had a capacity of 4.4 million barrels per year. The expansion announced in 1972, however, will bring the capacity up to 6 million barrels annually by 1974. Instead of the \$3 million in additional revenues the Frisco originally anticipated, it now appears that revenues will approach \$4 million annually.

Early in the year, Weyerhaeuser Company began operating its 1600-ton, \$150-million pulp mill at Valliant, Oklahoma. That Company also en-

larged and modernized several of its lumber and wall board plants in Southeast Oklahoma and Southwest Arkansas. These installations, while not located on the Frisco proper, are situated on two adjacent short line railroads which are owned by Weyerhaeuser and which jointly interchange traffic with the Frisco at Valliant. The Frisco now hopes to realize from this complex about three times the volume of traffic formerly received.

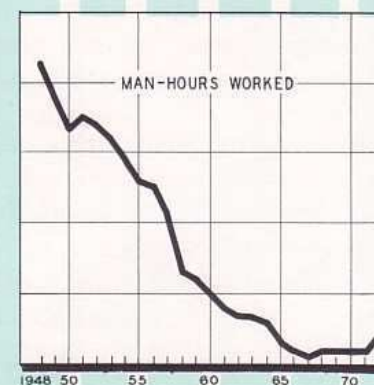
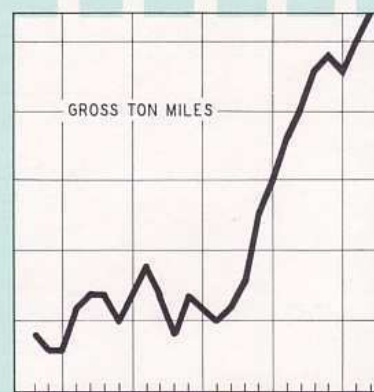
Other sources of additional traffic developed during the year included an expansion of Whirlpool Corporation's window air-conditioner manufacturing plant at Fort Smith, Arkansas; an enlargement of Procter & Gamble's Charmin Paper Products Division plant at Cape Girardeau, Missouri and a new spice and mustard plant of the R. T. French Company in Springfield, Missouri.

OPERATIONS

A record volume of traffic, substantially higher wages and benefits, and heavier maintenance programs described in detail on page 11, pushed operating expenses to \$181.3 million, up 11% from the level of the year before. In the last quarter of the year, severe weather conditions throughout Frisco territory hampered operations and added still further to the expense of operating the property. The effect of these various factors are shown in the following tabulation which compares the number of cents spent from each revenue dollar for all of the major sub-divisions of operating expenses during 1972 and the year before.

	1972	1971
Transportation	37.8	37.0
Maintenance of Way	14.8	13.4
Maintenance of Equipment ..	15.3	15.2
Other	8.0	8.3
Operating Ratio	75.9	73.9

To meet ever-stiffening competition, dependable freight schedules are a requisite. Frisco continues to search for new techniques and methods to expedite train service. These include the computerized monitoring of schedules, the pre-blocking of cars at major terminals to reduce the time and labor required for intermediate switching service and the operation of unit and run-through trains. In cooperation with other railroads, the Frisco currently is offering run-through, expedited service between Florida and the West Coast, between the Carolinas and Kansas City, between the Carolinas and California and between Minneapolis-St. Paul and Texas.

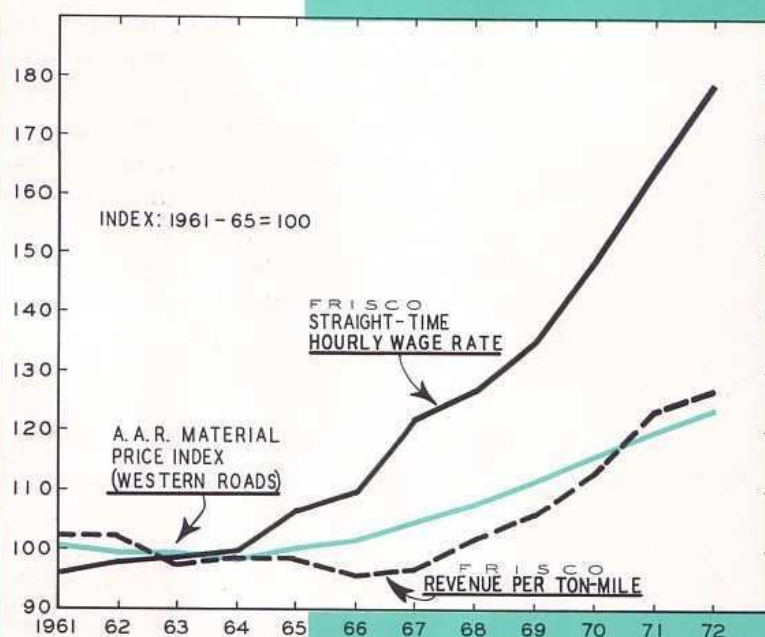


LABOR COSTS UP SHARPLY

Wage costs in 1972 rose \$9.7 million, a full 10%; in addition there were sizable increases in the cost of benefits and, as shown on page 10, in payroll taxes. Under the three-year labor contracts with railway employees, which expire on June 30, 1973, carriers were granted various changes in work rules, some of which are now in effect. The plus and minus effect of implementing the other changes currently is under study to evaluate how much they may affect costs and service.

During the year, Arkansas voters repealed the last Full Crew Law in the country. This statute required railroads to employ extra brakemen on trains of a certain length moving through the State. Under the provisions of a labor agreement, no present employee will lose his job as a result of the repeal of the statute but savings from the gradual discontinuance of the practice will be realized through attrition.

The long-standing firemen-off case was settled nationally between the United Transportation Union and the railroad industry. Through attrition and a procedure whereby firemen will be trained for future engineer job openings, a way has been found to gradually reduce the employment of firemen on Diesel locomotives.



Box car repair program in Frisco's shops.

TAXES

Estimated taxes in 1972 totaled \$18.4 million versus \$18.2 million in 1971.

In 1972, net Federal income tax benefits from accelerated and guideline depreciation, and amortization of defense facilities and rolling stock, were equivalent to \$2.53 per share of Common Stock; in 1971 these benefits were equivalent to \$1.91 per share of Common Stock.

Estimated benefits from allowable investment credit included in net earnings for the year 1972 were \$309,000 compared to \$1.3 million for the year 1971. Carryover of credit to 1973 is estimated to be \$4.3 million.

The minimum tax on certain tax preference items (primarily amortization of rolling stock) is estimated to be \$420,000 for 1972, compared to \$225,000 for the year 1971.

Payroll taxes in 1972 totaled \$10.5 million, an increase of 12.4% from the level of 1971. Following is a statement of Railroad Retirement and Unemployment Tax bases and rates for the years 1972 and 1971:

	1972	1971
Railroad Retirement Tax	9.95%	9.95%
Includes hospital benefits of	0.60%	0.60%
Computed on earnings up to	\$750 per mo.	\$650 per mo.
Additional tax on compensated service	6¾¢ avg. per hr.	6¢ avg. per hr.
Railroad Unemployment Tax	4%	4%
Computed on earnings up to	\$400 per mo.	\$400 per mo.
Total Payroll Taxes	\$10,549,193	\$9,381,491

Effective January 1, 1973 the Railroad Retirement Tax was increased to 10.6% and will be computed on base earnings of \$900.00 per month.

CAPITAL EXPENDITURES—THE COST OF BUYING TRANSPORTATION TOOLS

The changing distribution requirements of the shipping public have accelerated the replacement of Frisco's equipment and facilities. In many instances, the ability to satisfy customer demands depends on the Company's willingness to provide the kind of equipment and services which fit the particular needs of the shipper.

In recent years—between 1968 and 1972, for example—Frisco's capital expenditures for new equipment and facilities have been averaging \$27.5 million annually. In 1972, the Frisco spent \$12.8 million for new cars and locomotives, most of which were financed through Conditional Sale Agreements. The types of cars and locomotives installed may be found on page 27, together with similar data for equipment installed in prior years. In the same year, Frisco spent \$6.1 million on roadway and structures, \$1.3 million on rebuilding freight cars and \$2.9 million on other additions and improvements to its properties.

ROADWAY AND STRUCTURE RENEWAL PROGRAM STEPPED UP

Heavier trains at faster speeds and the changing configuration of equipment have necessitated a stepped-up program of strengthening Frisco's roadway and structures. During the year, a total of 96.5 miles of new 132-pound rail was laid, of which all but 5.4 miles was of the continuously welded type laid in quarter-mile lengths.

A total of 67.6 miles of rail released from the Frisco's primary lines was relaid on secondary lines, some segments of which have enjoyed an encouraging growth of traffic over the years.

Regular maintenance work performed during the year included the insertion of 619,000 new cross ties, as well as the surfacing of 1085 miles of track and the testing of 4315 miles of railroad with electronic detector cars capable of locating hidden internal flaws before they can fail in service.

The year also saw a continuation of an accelerated bridge renewal program: 294 panels of wooden trestles were filled or replaced with culverts and 323 panels of wooden bridges were replaced with permanent steel and concrete structures.

In 1972, work progressed on modernizing and increasing the capacity of the Company's yards at Memphis, Tennessee; Birmingham, Alabama and Springfield, Missouri to permit more efficient switching and classification of freight cars. Planned as a three-year program, the work will be completed during 1973.

EQUIPMENT OBLIGATIONS

Equipment obligations outstanding at year-end, including those due in one year, totaled \$104.7 million, a decrease of \$0.4 million, representing serial maturities of \$10.7 million, less additional obligations of \$10.3 million during 1972.

Installments on our equipment debt due in 1973 will amount to \$10.6 million; equipment depreciation chargeable to operating expenses will approximate \$10.1 million.

LEASED FREIGHT CARS

To augment its ownership of freight-carrying equipment, the Frisco had 2259 freight cars under lease at year-end. It also is a partner to a leasing agreement under which it shares the use of 480 covered hoppers with a major chemical company. Additionally, the Frisco has a stock interest in Trailer Train Company from which it leases flat cars on some of which Frisco-owned automobile racks are mounted.

Weyerhaeuser Company's new and expanded operations in Oklahoma and Arkansas offer a substantial increase in rail traffic.





Revenues from the movement of new motor vehicles reaches a new high.

ABANDONMENT OF UNNEEDED TRACKAGE

Frisco continues its efforts to reduce the burden of maintaining unnecessary branch line mileage which will become even more costly under the new track safety standards promulgated by the Federal Railroad Administration. During the year, regulatory authority was received to abandon some 109 miles of branch lines: 35 miles in East Central Oklahoma, 51 miles in Southeast Missouri and Northeast Arkansas and 23 miles in South Central Missouri. Authority to abandon an additional 5 miles in Southeast Kansas is hoped for at an early date.

In the abandonment of light density lines, Frisco is cooperating with neighboring rail carriers which serve the same communities. In some instances Frisco has been able to abandon its unneeded line into certain communities, allowing a competing road to serve them exclusively, while the competing rail carrier abandons its line into other communities where Frisco's line will remain the survivor. In other instances railroads exchange trackage rights in order to facilitate the abandonment of duplicating lines.



Load testing locomotive to measure its operating efficiency.



Hopper car repair program in Company shops.

MERGERS

In the last several years we have reported the status of the proceeding before the Interstate Commerce Commission whereby various railroads are seeking to acquire all or part of the Rock Island. The Frisco intervened in the proceeding and opposed all of the various acquisition proposals. This proceeding has been pending since 1963. The final volume of the Report of the ICC Administrative Law Judge was issued February 15, 1973. In general terms the report recommends a plan to restructure many of the Western railroads into four basic systems. Frisco was not included within the proposed basic systems and would remain an independent line unless it chose to seek inclusion. It is anticipated

that there will be further ICC proceedings prior to the time the Commission issues its final order. We do not expect a final order to be issued in 1973. The Recommended Report is being studied by your Company and appropriate action will be taken to protect the interests of Frisco stockholders.

The merger of the Illinois Central Railroad and the Gulf, Mobile & Ohio Railroad was approved by the Interstate Commerce Commission and consummated on August 1, 1972. Your Company reached a satisfactory agreement regarding the right of the merged company to use Frisco's facilities at Birmingham, Alabama, and opposition to the merger had been withdrawn.

LITIGATION

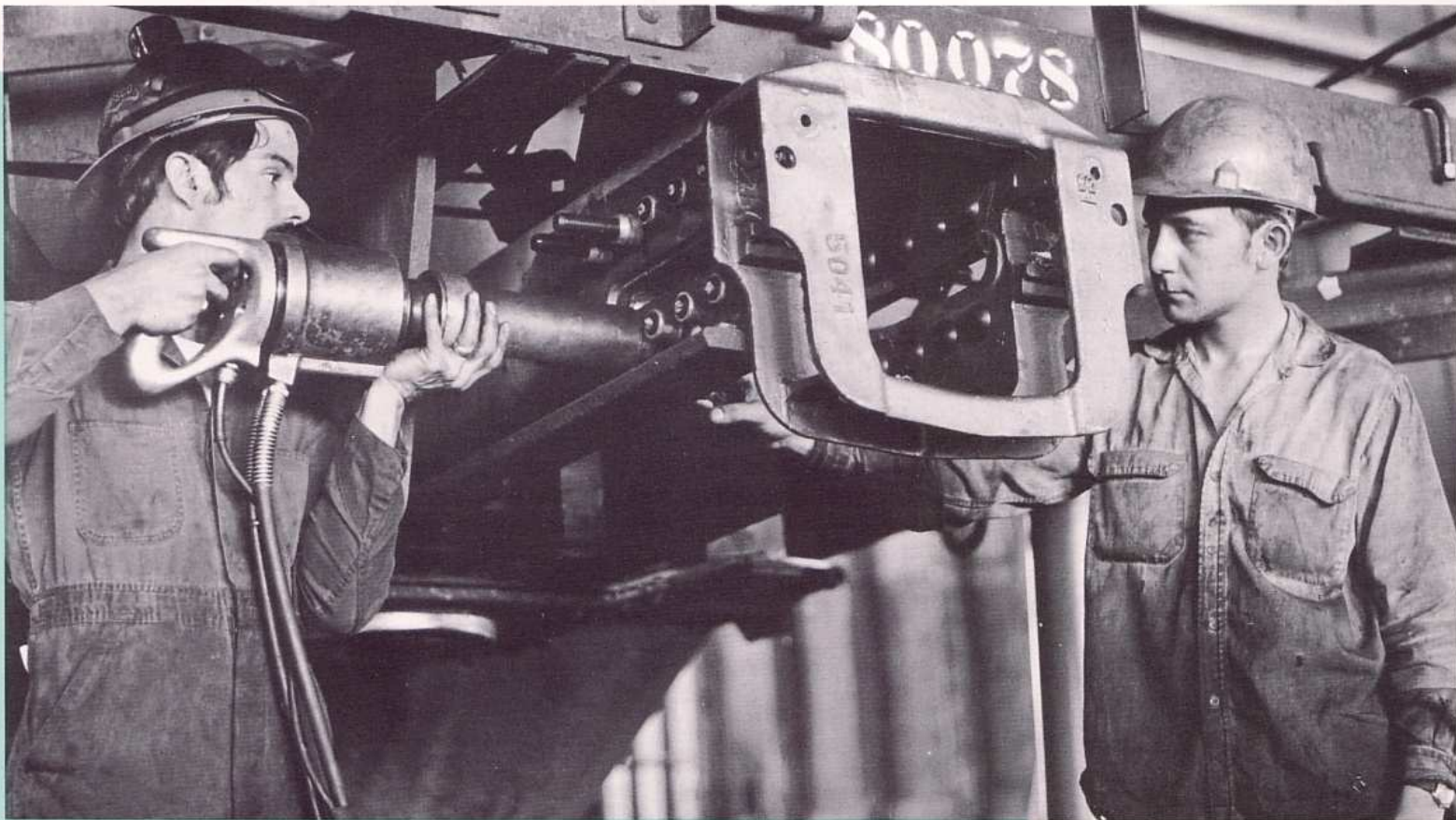
Last year it was reported that the proceeding before the Interstate Commerce Commission involving the divisions of joint revenue on traffic moving in Eastern and Southern territories had been concluded on a favorable basis for your Company. In March, 1972, the Eastern rail carriers again instituted a proceeding before the Interstate Commerce Commission seeking a higher share of the joint revenue on this traffic. It is expected that hearings before the Commission will not begin until sometime in 1974.

REA Express has commenced two lawsuits against Frisco and several other railroads claiming violations of the antitrust laws. In addition, REA seeks the recovery of treble damages for the cancellation of certain REA notes held by Frisco and the other defendants. Frisco is taking appropriate action to defend itself against the alleged claims.

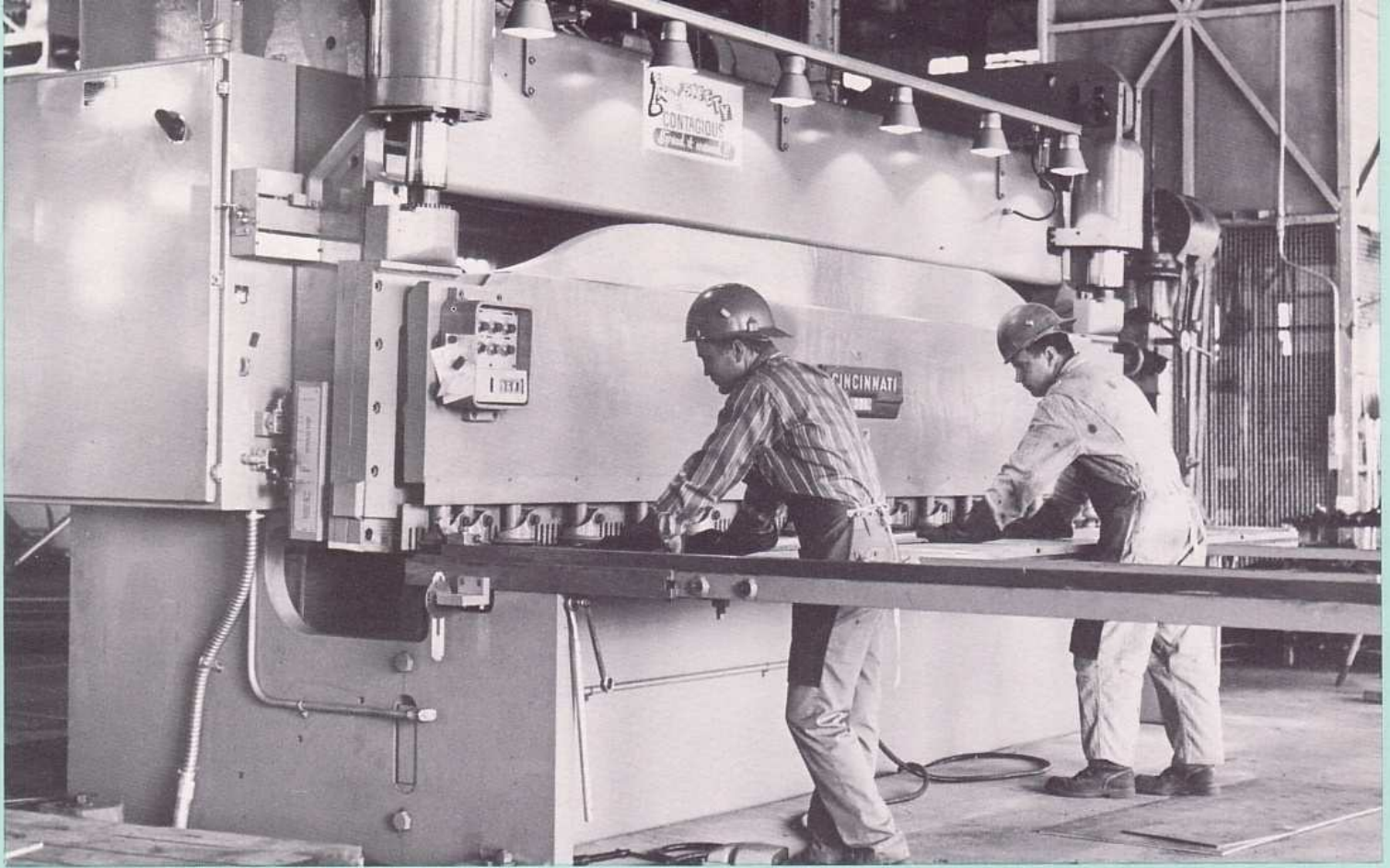
POLLUTION CONTROL

Although railway transportation is not one of the higher pollution industries and is responsible for only about one per cent of emissions from all sources, the Frisco has joined the national move to improve environmental controls. Since 1967, the Company has spent more than \$3.4 million in its efforts to control and, where possible, eliminate pollution. Additional operating expenditures for the control of pollution are continuing at a rate of \$582,000 annually.

Experimentation and research is going forward on Diesel emissions, human waste disposal, smoke abatement, right-of-way clearance and the control of pollutants in and around shop areas.



Bolt application which prevents loosening and eliminates need for riveting.



Hydraulic shearing machine for cutting metal up to $\frac{3}{8}$ " in thickness.

SAFETY IMPROVES

Safety programs continued to further reduce both the frequency and severity of injuries to employees. For the second consecutive year, there were no employee fatalities. The severity ratio, based on injury-caused days lost per million man-hours, was only half of the previous 5-year average.

For the 21st year, the Frisco was recognized by the National Safety Council for promoting public safety through public school programs, news media and civic clubs.

Proposed legislation and policy changes at the Federal level hopefully will result in a higher percentage of Federal and State funding for new installations of active grade crossing warning devices and grade separations. In addition, the Department of Transportation has recommended that Congress provide a \$750-million grade crossing protection fund, to be allocated over a 10-year period. A significant part of this proposal is that it would extend to crossings in both urban and rural areas which are not a part of the Federal Aid Highway System.

HUMAN RESOURCES

While the Frisco has a major investment in the physical tools of transportation, it also has an important investment in human assets: the thousands of men and women who have helped the Company to grow and prosper through the years. To provide a continuing flow of technical talent and skilled managerial personnel, the Frisco has a well-established program of external recruitment and internal training. Specialized job-related courses are given periodically at all levels of employment to upgrade the skills of personnel upon whom the Company must depend in the increasingly competitive struggle for traffic. The hiring of professional and technical talent from the college campus or from other companies has been augmented by a long-range management development program to give the Frisco both quality and depth of management.



MANAGEMENT CHANGES

On May 1, Donald E. Engle was named Vice President and General Counsel, with headquarters at St. Louis, Missouri, succeeding J. E. McCullough who was appointed to serve as Assistant to President until his retirement in April 1973 under the Company's pension plan.

Mr. Engle, a graduate of Macalester College and the University of Minnesota Law School, started his railroad career as an attorney in the Law Department of the Great Northern Railway Company in 1953, following a year in the Attorney General's office of the State of Minnesota. Prior to joining the Frisco, he served in various capacities with both the Great Northern and the newly-merged Burlington Northern.

FINANCIAL STATEMENTS

Included in this report are the consolidated financial statements of the St. Louis-San Francisco Railway Company and its wholly-owned rail and non-rail subsidiaries, together with the opinion thereon of the Company's independent accountants, Price Waterhouse & Co. Frisco's wholly-owned rail subsidiary is the Quanah, Acme & Pacific Railway Company. Non-rail subsidiaries are Frisco Transportation Company, Clarkland, Inc., Clarkland Royalty, Inc. and 906 Olive Corporation.

The financial results of the New Mexico and Arizona Land Company (50.04% owned by the St. Louis-San Francisco Railway Company) are included in the Frisco's consolidated results on an equity method basis. The New Mexico and Arizona Land Company issues its own annual report; anyone desiring a copy may obtain one by writing to the New Mexico and Arizona Land Company, Camel Square, 4350 E. Camelback Road, Phoenix, Arizona 85018.

PRICE WATERHOUSE & CO. ONE MEMORIAL DRIVE ST. LOUIS

March 5, 1973

TO THE BOARD OF DIRECTORS AND STOCKHOLDERS OF
ST. LOUIS-SAN FRANCISCO RAILWAY COMPANY:

We have examined the consolidated balance sheets of the St. Louis-San Francisco Railway Company and its subsidiaries at December 31, 1972 and 1971 and the related consolidated statements of income, retained income and changes in financial position for the years then ended. Our examinations were made in accordance with generally accepted auditing standards and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, except that provision has not been made for the possible increase in income taxes of future periods as set forth in Note 2 to the financial statements, the accompanying statements examined by us present fairly the consolidated financial position of St. Louis-San Francisco Railway Company and its subsidiaries at December 31, 1972 and 1971, the results of their operations and the changes in financial position for the years then ended, in conformity with generally accepted accounting principles consistently applied.

Price Waterhouse & Co.

CONSOLIDATED INCOME STATEMENT

	<u>1972</u>	<u>1971</u>
	<u>(000) omitted</u>	
OPERATING REVENUES:		
Freight	\$230,403	\$212,112
Other	<u>8,556</u>	<u>8,823</u>
Total operating revenues	<u>238,959</u>	<u>220,935</u>
OPERATING EXPENSES:		
Maintenance of way and structures	35,328	29,701
Maintenance of equipment	36,617	33,658
Transportation	90,375	81,681
Other	<u>18,975</u>	<u>18,321</u>
Total operating expenses (includes depreciation of \$12,616,000 and \$12,589,000 respectively)	<u>181,295</u>	<u>163,361</u>
Net operating revenue	<u>57,664</u>	<u>57,574</u>
OPERATING CHARGES:		
Taxes (except federal income taxes)	17,536	16,423
Equipment and joint facility rents	<u>14,400</u>	<u>15,339</u>
Total operating charges	<u>31,936</u>	<u>31,762</u>
Net operating income	<u>25,728</u>	<u>25,812</u>
OTHER INCOME:		
Profit on company bonds purchased	572	54
Other, net	<u>1,645</u>	<u>1,981</u>
Total other income	<u>2,217</u>	<u>2,035</u>
Balance for fixed and contingent charges	<u>27,945</u>	<u>27,847</u>
FIXED AND CONTINGENT CHARGES:		
Interest on long term debt — fixed	10,608	9,896
Other fixed charges	232	215
Interest on long term debt — contingent	<u>1,426</u>	<u>1,483</u>
Total fixed and contingent charges	<u>12,266</u>	<u>11,594</u>
Income before federal income taxes	15,679	16,253
ESTIMATED FEDERAL INCOME TAXES:		
(Note 2, Page 22)	<u>830</u>	<u>1,810</u>
NET INCOME (in conformity with I.C.C. principles)	<u>\$ 14,849</u>	<u>\$ 14,443</u>
EARNINGS PER SHARE	\$ 5.72	\$ 5.56

CONSOLIDATED BALANCE SHEET

	December 31,	
	<u>1972</u>	<u>1971</u>
	<u>(000) omitted</u>	
ASSETS		
CURRENT ASSETS:		
Cash	\$ 3,595	\$ 4,779
Temporary cash investments	14,804	17,416
Cash deposits for interest, dividends, etc.	1,102	1,033
Accounts receivable	23,138	17,037
Material and supplies, at average cost	10,147	10,517
Other current assets	661	645
Total Current Assets	<u>53,447</u>	<u>51,427</u>
SPECIAL DEPOSITS		
	<u>1,998</u>	<u>4,255</u>
INVESTMENTS:		
Securities of and advances to affiliates (Page 25)	5,550	5,317
Other investments	249	1,253
Total Investments	<u>5,799</u>	<u>6,570</u>
PROPERTIES (Note 4, Page 23 and Page 25):		
Roadway and structures	334,335	331,355
Equipment	294,380	286,446
Non-operating property	8,666	8,606
Accrued depreciation — road	(62,038)	(60,983)
Accrued depreciation — equipment	(125,366)	(122,242)
Accrued depreciation — non-operating property	(530)	(479)
Total Properties — Net	<u>449,447</u>	<u>442,703</u>
OTHER ASSETS:		
Unamortized expense on long term debt	1,916	2,043
Miscellaneous	3,838	1,905
Total Other Assets	<u>5,754</u>	<u>3,948</u>
TOTAL ASSETS	\$516,445	\$508,903

CONSOLIDATED BALANCE SHEET

	December 31,	
	<u>1972</u>	<u>1971</u>
	<u>(000) omitted</u>	
LIABILITIES		
CURRENT LIABILITIES:		
Audited accounts and wages payable	\$ 4,961	\$ 4,653
Accrued and miscellaneous accounts payable	19,441	18,946
Interest and dividends payable	4,375	4,267
Estimated federal taxes on income (Note 5, Page 23)	2,486	3,051
Other accrued taxes	3,768	3,916
Other current liabilities	4,479	3,536
Total Current Liabilities (excluding current portion of long term debt)	<u>39,510</u>	<u>38,369</u>
LONG TERM DEBT (Page 26):		
First Mortgage Bonds, 4% Series A — 1997	61,606	62,468
First Mortgage Bonds, 4% Series B — 1980	14,387	14,388
Income Debentures, 5% Series A — 2006	29,084	29,653
Purchase Money Mortgage Notes, 6¾ % — 1992	6,000	6,000
Equipment obligations	104,713	105,072
Other long term debt	2,937	3,316
Total Long Term Debt (\$11,713,000 payable in 1973 and \$11,188,000 in 1972)	<u>218,727</u>	<u>220,897</u>
OTHER LIABILITIES:		
Estimated casualty and other reserves	735	946
Miscellaneous, including deferred credits	1,447	1,090
Total Other Liabilities	<u>2,182</u>	<u>2,036</u>
STOCKHOLDERS' EQUITY		
CAPITAL STOCK (Note 6, Page 23):		
Common, no par value —		
Authorized 6,000,000 shares, issued 2,595,619 shares, less		
50 shares in treasury	113,565	113,565
CAPITAL SURPLUS	18,935	18,935
RETAINED INCOME (Page 24)	123,526	115,101
Total Stockholders' Equity	<u>256,026</u>	<u>247,601</u>
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	<u>\$516,445</u>	<u>\$508,903</u>

NOTES TO FINANCIAL STATEMENTS

1. **PRINCIPLES OF CONSOLIDATION:** Included in the consolidated financial statements are the accounts of the parent company and wholly-owned rail and non-rail subsidiary companies. 50.04% and 50.03% in 1972 and 1971, respectively, of the net income of partially owned New Mexico and Arizona Land Company has been included in Other Income and the investment has been stated on an equity method basis.

2. **AMORTIZATION, ACCELERATED AND GUIDELINE DEPRECIATION:** The Company and its railroad subsidiaries maintain their books of account, and the accompanying statements have been prepared, in conformity with principles and methods of accounting prescribed or authorized by the Interstate Commerce Commission. These principles and methods do not require a provision for the income tax effect of the excess of tax amortization and depreciation over recorded depreciation as is necessary to conform with generally accepted accounting principles.

The supplementary income information shown below reflects the adjustments necessary to present net income in conformity with generally accepted accounting principles:

	1972	1971
Net income (in conformity with ICC principles) as set forth in the consolidated income statement	\$14,849,000	\$14,443,000
Adjustments to generally accepted accounting principles:		
Provision for income tax effect of —		
Amortization of defense facilities	859,000	920,000
Amortization of rolling stock under 1969 Tax Reform Act	(4,232,000)	(3,542,000)
Accelerated and guideline depreciation	(3,206,000)	(2,340,000)
Net income (as it would be stated in conformity with generally accepted accounting principles) ..	\$ 8,270,000	\$ 9,481,000
Earnings per share	\$ 3.19	\$ 3.65

The cumulative deferred effect on federal income taxes due to the above-mentioned differences, computed at tax rates applicable to the individual years, not reflected in the accompanying balance sheet, amounted to \$62,000,000 at December 31, 1972.

3. **PENSION PLAN:** The Company has a noncontributory pension plan covering officers and supervisory employees. The cost of the plan charged to income was \$1,279,000 in 1972

NOTES TO FINANCIAL STATEMENTS (continued)

and \$1,194,000 in 1971, which amounts include provision for past service costs. The Company's policy is to fund pension costs accrued. Unfunded past service costs of the Company's pension plan amounted to approximately \$4,000,000 at December 31, 1972.

4. **PROPERTIES:** Gross properties are stated at estimated original cost as determined by the Interstate Commerce Commission for reorganizational purposes as of January 1, 1947, plus additions and betterments at cost and less retirements since that date.

The Company uses the straight-line method of depreciation accounting (useful lives of 7 to 75 years) as prescribed by the Interstate Commerce Commission, with respect to equipment and depreciable road properties; however, for rails, ties, and other track materials instead of depreciation accounting, it follows an acceptable alternate accounting practice of "replacement" accounting. Under this method, replacements in kind are charged to expenses, and betterments (improvements) are capitalized. The amounts capitalized are not depreciated and are charged against income only when the related properties are retired.

At December 31, 1972, nondepreciable property, including land and land rights, aggregated approximately \$213,600,000.

5. **FEDERAL INCOME TAXES:** Federal taxes on income for the years 1968 through 1972 are subject to final determination by the Treasury Department. In the opinion of management, the reserve provided for federal taxes on income is adequate. See page 10 for details of investment tax credit.

6. **CAPITAL STOCK:** The Company is authorized to issue 1,500,000 shares of Preferred Stock of \$100.00 par value. None of such stock is outstanding.

7. **CONTINGENT LIABILITIES AND COMMITMENTS:** The Company is guarantor of principal and interest, individually or jointly with other railroads, of obligations of various affiliated companies of which the estimated portion applicable to the Company is approximately \$6,600,000 and \$6,900,000 as of December 31, 1972 and 1971, respectively. The Company is a participant in service interruption policies with The Imperial Insurance Company, Limited. The maximum annual premium under the policies in the event of work stoppages on other participating railroads, is \$5,400,000.

The Company leases equipment under various agreements extending to 1992. Annual rentals under existing leases aggregate approximately \$4,000,000 subject to a partial offset of freight car earnings while equipment is off line.

CONSOLIDATED RETAINED INCOME STATEMENT

	1972 (000)	1971 omitted
Balance at beginning of year	\$115,101	\$106,887
Add:		
Net income for the year	14,849	14,443
Deduct:		
Dividend on Common Stock — Per Share: \$2.475 in 1972 and \$2.40 in 1971.	6,424	6,229
Balance at end of year	<u>\$123,526</u>	<u>\$115,101</u>

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION

	1972 (000)	1971 omitted
SOURCES OF FUNDS:		
Net income	\$ 14,849	\$ 14,443
Depreciation and other non-cash charges	13,579	12,902
Proceeds long term debt	10,499	29,354
Proceeds sale of property and salvage	2,221	1,752
Miscellaneous	1,909	(1,929)
Total	<u>\$ 43,057</u>	<u>\$ 56,522</u>
APPLICATIONS OF FUNDS:		
Additions and betterments — road and equipment	\$ 23,085	\$ 35,302
Long term debt retired	12,669	10,412
Dividends	6,424	6,229
Total	<u>\$ 42,178</u>	<u>\$ 51,943</u>
INCREASE IN WORKING CAPITAL	<u>\$ 879</u>	<u>\$ 4,579</u>
CHANGES IN WORKING CAPITAL:		
Cash and temporary cash investments	\$ (3,796)	\$ 6,050
Accounts receivable	6,101	742
Material and supplies	(370)	338
Accounts payable	(803)	843
Estimated federal taxes on income	565	(2,575)
Other	(818)	(819)
INCREASE IN WORKING CAPITAL	<u>\$ 879</u>	<u>\$ 4,579</u>

**SECURITIES OF AND
ADVANCES TO AFFILIATES**

	Number of Shares	Per Cent Owned	Par Value	Stocks	Notes and Advances	Total Investment
New Mexico and Arizona Land Co.	525,270.48	50.04	\$525,270	\$2,140,644 †	\$	\$2,140,644
Illinois Terminal Railroad Co.	181.82	9.09	1,818	1,818	.....	1,818
Kansas City Terminal Ry. Co.	1,833.33*	8.33	183,333	183,333	1,412,469	1,595,802
Pullman Co., The	8,456.00	1.16	8,456	236,768	.....	236,768
Terminal R. R. Association of St. Louis	2,058.00*	6.25	205,800	1	56,250	56,251
Trailer Train Co.	500.00	2.44	500	50,000	486,000	536,000
Union Terminal Co., The — Dallas	60.00*	12.50	6,000	6,000	207,473	213,473
Wichita Union Terminal Ry. Co.	333.33*	33.33	33,333	12,502	754,289	766,791
Wichita Terminal Association	.....	.....	.....	.....	2,000	2,000
Totals				\$2,631,066	\$2,918,481	\$5,549,547

*Stock Pledged Under First Mortgage.

†Equity of New Mexico and Arizona Land Company at December 31, 1972 (Note 1, Page 22).

**PROPERTY CHANGES DURING
THE YEAR 1972**

	Balance Dec. 31, 1971	Additions and Betterments	Retirements	Balance Dec. 31, 1972
Roadway and Structures	\$ 331,354,384	\$ 6,123,009	\$ 3,142,857	\$334,334,536
Equipment (Page 27):				
Diesel Locomotives	73,605,269	10,477,925	2,703,581	81,379,613
Freight-Train Cars	198,578,214	4,276,985	4,991,116	197,864,083
Work and Miscellaneous	12,739,133	1,784,341	1,123,819	13,399,655
Motor Carrier Equipment	1,523,702	268,957	55,700	1,736,959
Total Equipment	286,446,318	16,808,208	8,874,216	294,380,310
Total Transportation Property	617,800,702	22,931,217	12,017,073	628,714,846
Non-Operating Property	8,605,744	153,456	93,593	8,665,607
Total Properties	\$626,406,446	\$23,084,673	\$12,110,666	\$637,380,453

LONG TERM DEBT

	Date of Maturity	Outstanding Dec. 31, 1972		Fixed and Contingent Interest	
		Due After 1973	Due in 1973	Rate	Expense for 1972
FUNDED DEBT UNMATURED:					
First Mortgage Series A	1-1-97	\$ 61,606,200†	*	4.00	\$ 2,481,753
First Mortgage Series B	9-1-80	14,387,000†	*	4.00	575,476
Income Debentures Series A	1-1-06	29,083,500†	*	5.00	1,425,725
Purchase Money Mortgage Notes.	8-1-92	6,000,000	*	6.75	405,000
		111,076,700			4,887,954
EQUIPMENT OBLIGATIONS#:					
Trust Certificates:	Serially to				
Series N	3-15-80	1,953,000	\$ 279,000	4.25	97,330
Series O	5-15-80	2,205,000	315,000	4.38	115,417
Conditional Sale Agreements:					
Numbers:					
10	2-10-74	30,833	61,667	4.75	5,452
11	2-1-75	102,450	68,300	5.63	10,885
12	3-1-75	345,644	320,000	5.75	45,941
13	8-1-75	369,320	208,000	5.25	33,949
14	6-1-76	270,333	117,400	4.75	22,135
15/16	1-1-77	455,100	152,400	4.75	34,286
17	11-1-77	364,950	101,758	5.00	26,303
18/22	8-1-78	1,667,179	350,783	4.50	96,070
23/27	1-15-79	3,282,167	596,758	4.45	181,315
28/29	3-15-79	437,130	79,478	4.45	24,610
30	9-1-75	369,799	184,899	4.75	30,008
31/39	1-15-81	6,004,538	800,605	5.25	369,529
40	4-1-76	248,665	99,466	5.60	22,280
41/43	3-1-82	2,294,178	269,903	6.25	167,284
44/45	3-1-82	2,000,360	235,336	5.75	134,191
46/50	7-1-82	4,974,149	552,683	6.25	362,698
51/56	1-1-83	8,422,500	935,833	6.70	694,856
57/58	10-1-80	2,333,310	333,330	6.00	152,246
59/64	12-15-83	6,660,000	666,000	7.25	577,408
65	8-15-84	2,750,000	250,000	8.25	260,391
66/67	1-15-85	4,521,000	376,750	9.38	460,636
68/70	2-1-85	4,536,000	378,000	9.50	469,822
71	7-1-85	3,454,843	287,904	9.75	373,917
72	11-15-82	4,500,000	500,000	6.00	285,948
73/74 & 76/77	7-1-86	7,711,991	593,417	7.75	657,024
75	5-15-83	2,654,797	265,480	6.00	157,700
78/80	10-1-86	9,373,894	721,069	8.25	857,919
81	3-1-84	5,579,588	507,235	6.00	223,987
82	3-1-88	4,231,904		5.75	14,195
Matured During Year					13,883
		94,104,622	10,608,454		6,979,615
Other Long Term Debt		1,832,754	1,104,587		166,748
Totals		\$207,014,076	\$11,713,041		\$12,034,317

†Excludes bonds held in treasury as follows:

First Mortgage Series A	\$1,014,000
First Mortgage Series B	1,132,000
Income Debentures Series A .	379,000

*Subject to sinking fund provisions under mortgage indentures in 1973:

First Mortgage Series A	\$571,498
First Mortgage Series B	195,000
Income Debentures Series A ..	165,645
Purchase Money Mortgage Notes	150,000

#Equipment obligations maturing in future years are:

1973 ...	\$10,608,454	1978 ...	\$9,489,794	1983 ...	\$4,327,819
1974 ...	10,859,261	1979 ...	8,887,629	1984 ...	3,396,340
1975 ...	10,453,567	1980 ...	8,549,511	1985 ...	2,639,104
1976 ...	9,913,853	1981 ...	7,221,878	1986 ...	1,596,451
1977 ...	9,636,205	1982 ...	6,568,956	1987/88	564,254

EQUIPMENT OWNED

DESCRIPTION	Owned Dec. 31, 1971	Changes During 1972			Owned Dec. 31, 1972
		Purchased	Reclas- sified	Retired	
DIESEL LOCOMOTIVES:					
Freight 3600 H.P. (A Units)	49	...	...	...	49
Freight 3000 H.P. (A Units)	12	...	...	...	12
Freight 2500 H.P. (A Units)	65	...	...	...	65
Freight 2000 H.P. (A Units)	30	37	...	...	67
Freight 1750 H.P. (A Units)	2	...	...	...	2
Freight 1750 H.P. (B Units)	13	...	...	...	13
Freight 1500 H.P. (A Units)	12	...	...	3	9
Freight 1500 H.P. (B Units)	11	...	...	5	6
All Purpose 1500 H.P.	128	...	...	4	124
Switch 1500 H.P.	32	6	...	...	38
Switch 1200 H.P.	19	...	...	...	19
Switch 1000 H.P.	47	...	...	9	38
Switch 44 Ton	3	...	...	2	1
Total	423	43	...	23	443
FREIGHT-TRAIN CARS:					
Box-Plain	3,934	100	...	297	3,737
Box-Equipped-Non-Insulated	2,519	...	1	11	2,509
Box-Equipped-Insulated	1,121	...	...	9	1,112
Gondola	2,477	...	...	23	2,454
Hopper-Open Top	3,374	...	...	149	3,225
Hopper-Covered	2,431	6	...	45	2,392
Flat-Including Special Equipped	561	...	47	229	379
Wood Rack and Bulkhead Flat	844	35	...	5	874
Multi-Level Auto Transport	185	...	...	...	185
Mechanical Refrigerators	100	...	...	...	100
Caboose	237	1	...	12	226
Total	17,783	142	48	780	17,193
WORK EQUIPMENT:					
Tool and Material	586	...	176	65	697
Ballast	215	...	...	52	163
Boarding	76	...	6	8	74
Tank	129	...	...	3	126
Other	44	2	...	8	38
Total	1,050	2	182	136	1,098
MISCELLANEOUS EQUIPMENT:					
Motor Trucks	388	72	...	57	403
Automobiles	308	91	...	98	301
Airplane	1	...	...	...	1
Other	47	...	...	2	45
Total	744	163	...	157	750
FLOATING EQUIPMENT:					
Car Ferry	2	...	...	...	2
MOTOR CARRIER EQUIPMENT:					
Trucks	25	2	...	6	21
Tractors	82	15	...	4	93
Semitrailers	141	1	140
Service Cars	6	6
Total	254	17	...	11	260



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