



ANNUAL REPORT 1976

ST. LOUIS - SAN FRANCISCO RAILWAY COMPANY

St. Louis-San Francisco Railway Company

General Offices: 906 Olive Street • St. Louis, Mo. 63101

As shown on the map appearing on the facing page, the St. Louis-San Francisco Railway Company (Frisco) is a 4718-mile line-haul railroad system serving the states of Missouri, Oklahoma, Arkansas, Kansas, Texas, Tennessee, Mississippi, Alabama and Florida. The system mileage includes a wholly-owned subsidiary, the Quanah, Acme & Pacific Railway Company, which operates a 120-mile rail line through the Texas Panhandle to a connection with the Santa Fe Railway at Floydada. The Frisco derives 98% of its earnings from rail operations.

The Frisco's wholly-owned non-rail subsidiaries are: The Frisco Transportation Company, a motor common carrier which operates over routes generally paralleling the Frisco's rail lines in Missouri and which holds rights to operate over other routes in Arkansas, Tennessee, Mississippi, Oklahoma and Texas; two land companies — Clarkland, Inc. and Clarkland Royalty, Inc. — whose primary purpose is to acquire and develop property for the location of traffic-producing industries along the lines of the rail system, and 906 Olive Corporation, which holds the parent company's St. Louis, Mo. headquarters building and the Springfield, Mo. office building.

Frisco stock is listed and traded under the ticker symbol FN on both the New York and Midwest stock exchanges.

	DIVIDENDS PAID ON FRISCO STOCK		PRICE RANGE OF STOCK ON NYSE (As published by Dow Jones)			
	1976	1975	1976		1975	
			High	Low	High	Low
First Quarter	62½ ¢	62½ ¢	33½	23¾	27¾	22¼
Second Quarter	62½ ¢	62½ ¢	38⅝	29	26⅞	21¼
Third Quarter	62½ ¢	62½ ¢	40¾	36½	26⅝	22½
Fourth Quarter	62½ ¢	62½ ¢	41⅞	34	25⅝	21¾

The Frisco also owns approximately 50.78% of the stock of the New Mexico and Arizona Land Company whose financial results are reported in its own annual report but are included in the Frisco's consolidated results on the equity method basis. Anyone desiring a copy of the Land Company's annual report may obtain one by writing to the Secretary of the New Mexico and Arizona Land Company, 4350 East Camelback Road, Phoenix, Arizona 85018.

The financial statements which begin on page 17 are consolidated and have been audited by Price Waterhouse & Co. whose opinion thereon may be found on page 22. Instead of Form 10-K, the Frisco files Form 12-K with the Securities and Exchange Commission; the major portion of the information submitted consists of an appended copy of the R-1 Report filed with the Interstate Commerce Commission. Much of the statistical information contained in the R-1 Report is condensed and reproduced by the Frisco in a Financial and Statistical Report, a copy of which may be obtained without charge by writing to the Secretary of the Company at 906 Olive Street, St. Louis, Mo. 63101. A copy of the 12-K Report also may be obtained without charge, except that a reasonable fee will be imposed if a copy of the R-1 Report is requested.

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March 8, 1977

TO THE STOCKHOLDERS:

It is a pleasure to report that for the Frisco 1976 was a year of recovery and markedly improved profitability. Consolidated earnings per share rose to \$4.61 versus \$3.30 in economically-depressed 1975 when our financial results included extraordinary income of \$1.33 per share from the sale of retired rail facilities.

Frisco's improved performance was made possible by a greater volume of traffic, higher freight rates and prudent cost controls which enabled us to mitigate the ravaging effects of inflation while maintaining high quality service. Important gains in efficiency were achieved in providing transportation services as well as in roadway and equipment maintenance. As a result, our operating ratio — the number of cents spent from each revenue dollar for operation — was reduced from 78.3 in 1975 to 76.2 in 1976. To make further gains possible and to strengthen us competitively, we continued our high standards of maintenance and our investment in new plant and equipment. In addition to almost \$94 million charged to maintenance expenditures during the year, the Company spent a total of \$35 million on capital improvements.

The pickup in traffic volume, which started to accelerate in the third and fourth quarters of 1975, continued throughout the first half of 1976 and helped to produce record revenues and profit in that period. The expansion slowed in the third and fourth quarters of 1976 as a result of a pause in the economic recovery and because we were comparing with the better months of the year before. Throughout 1976 the movement of most of our principal revenue-producing commodities grew in general conformity with the national economic pattern and included traffic from new industries. Despite the decline in outlays for new plants and expansions, we were encouraged by our territory's continued industrial growth and by the resurgence of the coal industry in Frisco's territory and contiguous states. Coal shipments on the Frisco were up 32% from the level of 1975 primarily because of additional unit train movements to electrical utilities. We expect this trend to continue as the nation increasingly converts to the fossil fuel it possesses in greatest abundance.

Because of its traffic growth and profitability, as well as its central location, the Frisco has been considered a likely candidate for a merger or other form of unification. On February 1, 1977 the Burlington Northern and the Frisco announced simultaneously that they were commencing joint studies into the feasibility of unification. The BN was formed in 1970 by a merger of the Great Northern, Northern Pacific and Chicago, Burlington & Quincy railroads. For 1976 the BN reported consolidated revenues of \$1.9 billion and earnings of \$73 million or \$5.69 per share. It is anticipated that these studies will take about six months.

A notable event of 1976 was the enactment of the so-called 4-R Act, the Railroad Revitalization and Regulatory Reform Act. Among its many provisions, it provided for the rescue and rehabilitation of the hardest-pressed railroads in the Northeast and Midwest and hopefully will be of help to viable carriers in solving the industry's more difficult problems, many of them brought on by years of inequitable governmental treatment of the various modes of transport. While the new legislation has some negative aspects — notably increased governmental control and paper work — they have been reluctantly accepted by the industry in the interest of restoring efficient rail service to a large area of the country. A synopsis of the major provisions of the Act can be found elsewhere in this report along with a discussion of other legislative matters of particular importance to the rail industry. This year we expect that tax reform measures enacted in 1976 will afford railroads tangible benefits in improving cash flow and in the formation of internally-generated capital as discussed on page 11.

We enter 1977 with continued confidence in the integrity and strength of Frisco's people and property.

Sincerely,

Chairman and President

Frisco Facts

CONSOLIDATED

	<u>1976</u>	<u>1975</u>
Operating revenues	\$321,512,353	\$280,352,935
Operating expenses	\$244,935,206	\$219,602,430
Ratio of expenses to revenues.....	76.2	78.3
Average number of employes	8,358	8,440
Payroll	\$133,438,753	\$122,327,784
Taxes (including payroll taxes)	\$ 32,594,690	\$ 27,866,698
Taxes per share	\$ 12.51	\$ 10.74
Pre-tax Income available for fixed charges	\$ 29,111,794	\$ 20,370,386
Fixed charges	\$ 12,165,740	\$ 12,238,265
Times fixed charges earned — pre-tax	2.4	1.7
Contingent interest	\$ 1,362,075	\$ 1,414,700
Income before extraordinary item	\$ 12,013,979	\$ 5,117,422
Extraordinary item	\$ —	\$ 3,452,374
Net income	\$ 12,013,979	\$ 8,569,796
Earnings per share on:		
Ordinary income	\$ 4.61	\$ 1.97
Extraordinary income	\$ —	\$ 1.33
Net income	\$ 4.61	\$ 3.30
Dividends per share	\$ 2.50	\$ 2.50

SYSTEM RAIL LINE FREIGHT STATISTICS

Miles of road operated	4,718	4,741
Freight train revenue	\$308,089,972	\$268,081,824
Net ton-miles — revenue (thousands)	14,563,804	13,492,838
Gross ton-miles (thousands)	34,139,270	31,877,433
Train miles	9,446,675	9,060,636
Revenue per ton-mile	2.115¢	1.987¢
Revenue per train mile	\$ 32.61	\$ 29.59
Revenue tons per car	44.5	43.8
Revenue tons per train	1,541.7	1,489.2
Gross tons per train	3,613.9	3,518.2

NET INCOME UP SHARPLY

Reflecting record revenues and improved profitability, net income in 1976 was \$12.0 million versus \$8.6 million in economically-depressed 1975 when earnings were aided by extraordinary income of \$3.5 million, or \$1.33 per share, from the sale of retired rail facilities. Earnings per share in 1976 were \$4.61 versus \$3.30 a year earlier.

1977 DIVIDEND

A dividend of 62½¢ per share of Common was declared payable March 15, 1977 to holders of record February 22. The directors will give further consideration to the subject of dividends at quarterly intervals during the year. Dividends paid during 1976 and 1975 are shown on the inside front cover of this report.

COMPARATIVE QUARTERLY RESULTS

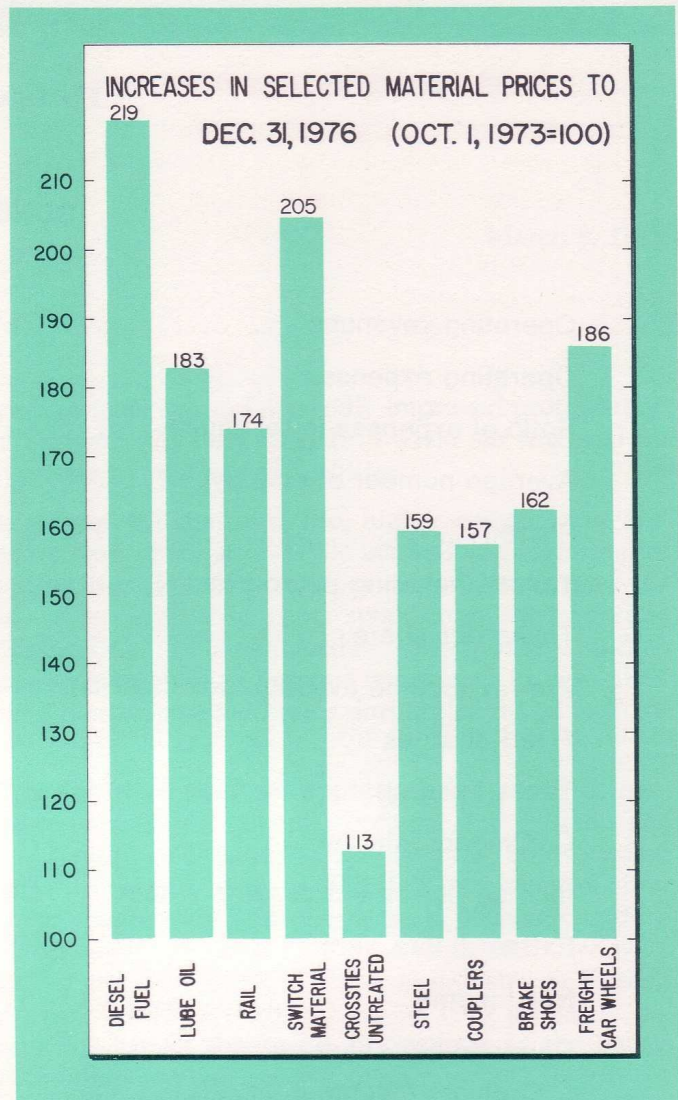
Quarter	Revenues		Net Operating Income		Net Income		Earnings Per Share	
	1976	1975	1976	1975	1976	1975	1976	1975
	(millions)		(millions)		(millions)			
1st	\$79.9	\$64.7	\$7.4	\$2.5	\$3.5	\$0.04	\$1.33	\$0.02
2nd	82.6	68.5	7.3	3.7	3.5	1.4	1.36	0.54
3rd	78.1	72.2	4.6	4.9	1.7	1.7	0.66	0.64
4th	80.9	75.0	6.9	6.6	3.3	5.5*	1.26	2.10*

*Includes Extraordinary Income of \$3.5 Million or \$1.33 Per Share.

REVENUES SET A RECORD

In a strong resurgence from the depressed level of 1975, Frisco's operating revenues climbed 14.7% to a record \$321.5 million versus \$280.4 million a year ago. Traffic growth during the year generally conformed to the pattern of economic recovery in the nation as a whole, with a sharp rise in the first and second quarters, followed by slower growth in the third and fourth quarters. Carloadings were ahead of the year-ago level by 14.2% in the first quarter, 12.8% in the second quarter, 3.6% in the third quarter and 3.3% in the fourth quarter. For the full year, carloadings were up 8.4% from the level of 1975, while revenue ton-miles — a measurement of both tonnage and distance carried — were up 7.9%. For Class I railroads as a group, carloadings were up 1.8% and revenue ton-miles were up 5.4%.

Higher freight rates which yielded the Frisco an increase in revenues of about 0.4% beginning in March and April and a 3.8% increase beginning October 7 — generated an estimated \$18.3 million in additional freight revenue. The additional revenue, however, was more than offset by increased fuel costs, higher prices for other ma-



terials and supplies, as well as two cost-of-living increases for employees plus a 3% wage hike.

Of major consequence to the Frisco's revenue picture in 1976 was the recovery of the automotive industry, the mild upturn in the housing industry and the continuing conversion to coal as a source of industrial energy. These influences are reflected in the carload movement of most of Frisco's principal revenue-producing commodities which account for 80% of all Frisco freight revenue. Volume gains were scored as shown by the following percentages: automobiles and trucks 29%, coal 32%, forest products 22%, pulp and paper 14%, chemicals 13%, construction materials 6%, petroleum and its products 4%, primary metal products 2%, food and kindred products 1% and freight forwarder traffic 8%.

The carload movement of agricultural commodities as a group was down 8% as food and fiber production was hampered during the year by a drought in much of Frisco's wheat-producing territory. Nevertheless, the winter wheat crop as a whole — while below the bumper proportions of 1975 — was among the five largest of all time.

Rail movement of the crop was handicapped by adverse marketing conditions for export sales causing much of the wheat to be held in elevators awaiting more favorable prices. The 1976 cotton crop was larger than in the previous year and the corn harvest was of record proportions.

Volume losses also were registered as shown by the following percentages: iron and steel 26%, machinery 20%, ores and concentrates 10% and fabricated metal products 7%.

DEVELOPING NEW PIGGYBACK MARKETS

Significant strides were made in developing new markets for trailers and containers on flat car (TOFC) traffic, or piggyback. In March, a new TOFC train was put into service between St. Louis and Irving, Texas, to penetrate the ever-growing and highly competitive market of transportation to and from the Dallas area. Nicknamed SUPERHOG, the schedule of the new train was coordinated with those of the Illinois Central Gulf Railroad to reach the Chicago market and of Con Rail and the Chessie System to penetrate the Eastern market.

Aided by SUPERHOG and other piggyback marketing innovations, Frisco's TOFC volume in the last half of 1976 set six consecutive monthly records and enabled the Company to end the year with a full-year increase of 22% over 1975. The fact that a more recognizable amount of this new traffic formerly moved on the highway reinforces the conviction that rail carriers can compete with trucks at a profit by offering the proper price-service package.

FREIGHT RATES RISE 4% EFFECTIVE JANUARY 7, 1977

In December the Interstate Commerce Commission granted a 4% freight rate increase effective January 7, 1977 to partly cover cost escalations not offset by previous rate hikes as well as additional higher costs anticipated during 1977.

NEW REVENUE FROM NEW PLANTS

During 1976 a total of 76 new industries completed construction of their facilities and began generating revenue tonnage. It is anticipated that these new plants will generate in excess of \$5 million in additional freight revenue for the Frisco. Involving an investment in land, building and equipment of \$218 million, the new plants provide employment for more than 3000 persons.

The full impact of the 1974-75 recession is evident in the drop in business outlays for new

plants and equipment. The number of new plants completed in Frisco's territory was the lowest since 1970, even though the capital cost of these facilities remained substantial. The cost of borrowed capital remained high and only showed signs of abatement toward year end.

As many plants operated below capacity levels, interest in expansion was not as prevalent as in other years; nevertheless 13 plants served by the Frisco enlarged their facilities at an investment of more than \$11 million and will produce more than 1700 carloads or trailerloads of additional freight.



Export traffic via Mobile, Alabama.

The new manufacturing plants which went into operation during the year show a healthy diversification: Southwire Company's steel fabricating plant at Osceola, Arkansas; Midland Glass Company's plant for producing beverage bottles at Henryetta, Oklahoma; Boise Cascade's can plant at Memphis, Tennessee and Union Carbide's cellulose casing plant in Osceola, Arkansas.

Entering 1977, 64 new industries are in various stages of planning and construction. Among them is a new \$300 million pulp mill which Parsons & Whittemore announced will be built by its subsidiary, Alabama River Pulp Company, at Fountain, Alabama. The mill will be completed in 1980 and will generate 15,000 carloads of freight per year. Another sizable plant, involving an initial investment of \$95 million, is being built by the Fort Howard Paper Company at Muskogee, Oklahoma. It will be completed in 1978. A second phase costing an additional \$100 million will be completed in 1979. At full capacity the mill will generate 10,000 carloads of freight annually.

The energy crisis continued to influence the industrial development pattern in Frisco's territory. Demands for coal continued to rise. New markets were created not only by new plants utilizing coal for fuel but also by the conversion of existing plants from natural gas to coal. Five new mines were opened on the Frisco, the largest being an installation operated by Carbonex Coal Company at Chelsea, Oklahoma. City Utilities began operating its new \$55 million generating plant at Springfield, Missouri, during the year and will require some 300,000 tons of coal annually. Union Electric is scheduled to start its second generating unit in the Spring of 1977 at Rush Island, Missouri and will require a doubling of the number of unit coal trains presently serving the facility. Several small mines in the Carbon Hill, Alabama, coal district are being purchased and consolidated by two major companies; expanded production from this area should materialize during 1977.

Agriculture remains an important part of the economy of Frisco's territory. Twelve modest-sized fertilizer blending and distribution facilities were opened along the lines of the railroad during the year. Farmland Industries plans to open a second anhydrous ammonia production facility at Enid, Oklahoma, a \$40 million venture, while Agrico Chemical Company plans to construct a second facility at Verdigris, Oklahoma. The multi-million dollar rice mill of Riceland Industries is now undergoing a major expansion at Jonesboro, Arkansas, and will be accessible to the Frisco as a result of negotiations completed during the year.

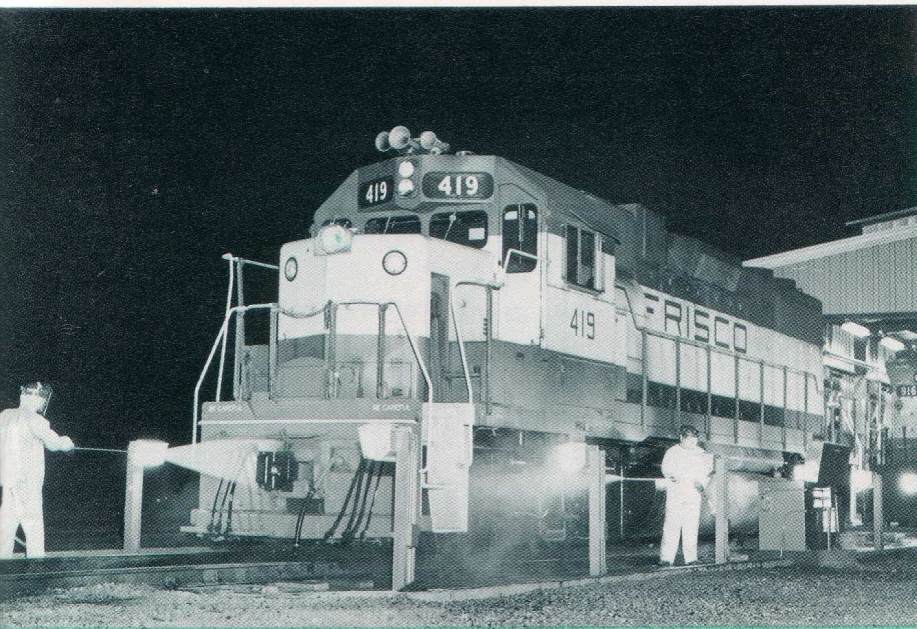
OPERATING EFFICIENCY RISES

Although operating expenses rose 11.5% to \$245 million under the influence of an expanding traffic volume as well as higher payroll costs and material prices, the number of cents spent from each revenue dollar for operation was reduced to 76.2 from 78.3 a year earlier, despite an increase in maintenance expenditures. In the face of a \$2.3 million increase in the cost of fuel, the number of cents spent from each revenue dollar for transportation services was reduced to 39.3 from 41.0 in 1975.

The improvement in freight train performance is shown by the fact that gross ton miles — the total weight of cars and contents in tons, multiplied by miles carried — were 7.1% greater than in 1975, while the freight train miles run in performing this service were only 4.3% greater than the year before. In achieving this result, transportation man-hours were reduced 1.8%, the average train load was increased from 3518 to 3614 gross tons, or 2.7%, and gross ton-miles per train hour from 76,696 in 1975 to 79,640, or 3.8%.



Modern machinery speeds maintenance-of-way work and provides a better roadway.



RUN-THROUGH TRAINS

The efficiency of train movement has been noticeably enhanced by the operation of run-through trains which by-pass intermediate yards and conserve time once spent on car interchange. Often run-through trains use the same pooled motive power as they proceed from one railroad to another. Frisco now participates with other rail carriers in the movement of ten run-through trains per day.

UNIT TRAIN MOVEMENTS

Still another growing part of railway traffic is the unit train movement of bulk commodities, principally coal. Unit trains shuttle back and forth between origin and destination carrying a single commodity in one direction and returning empty to facilitate a quicker turn-around. Frisco currently operates 12 unit coal trains per week, all of them destined to electrical utilities. Augmented by the coal tonnage hauled in unit trains, Frisco's coal movement now constitutes 8% of total car-loadings, up from 6% in 1975.

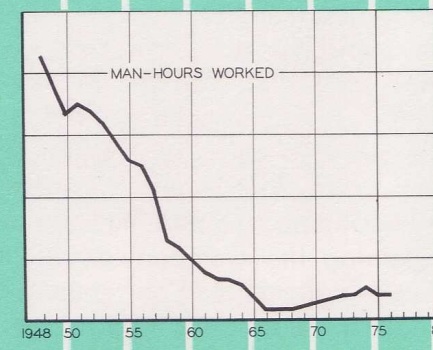
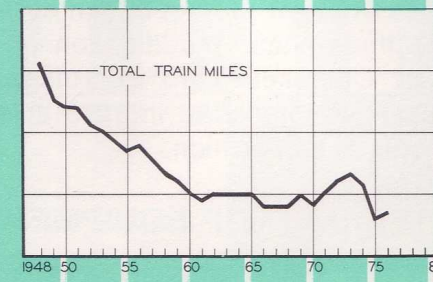
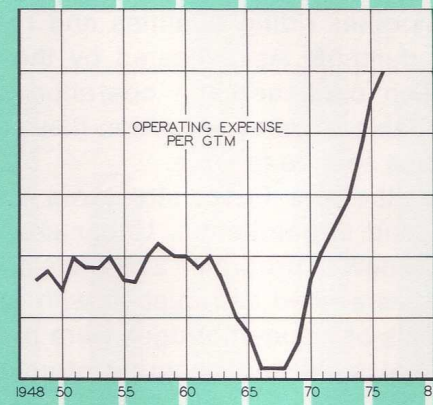
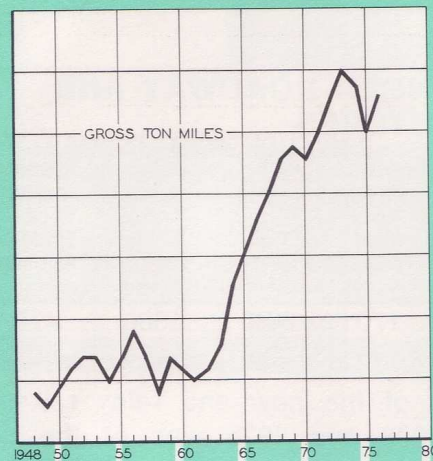
RATIOS

The tabulation which follows shows the amount spent on each of the major subdivisions of operating expenses during 1976 and the year before, together with the ratio of each to total operating revenues.

Transportation	
Maintenance of Way	
Maintenance of Equipment	
Other	
Total Operating Expenses	

1976	
Amount (add 000)	Ratio
\$126,394	39.3
47,229	14.7
46,756	14.5
24,556	7.7
\$244,935	76.2

1975	
Amount (add 000)	Ratio
\$115,008	41.0
42,538	15.2
40,080	14.3
21,976	7.8
\$219,602	78.3



STRONGER ROADWAY AND STRUCTURES

	Miles of Rail (new & relay)	Ties Inserted (add 000)	Track Miles Resurfaced	Cubic Yards of Ballast Applied (add 000)	Track Miles Tested With Detector Cars
1976	170	619	1380	470	4700
1975	146	600	1150	500	4500

Most of the new and relay rail installed in both 1976 and 1975 was of the continuous-welded type laid in quarter-mile lengths to provide smoother riding qualities and reduce joint-related damage. As indicated by the tabulation, the Frisco continued the operation of detector cars capable of locating hidden flaws before they can cause service failures.

During the year, Frisco structures also were upgraded and strengthened. Under an accelerated bridge renewal program, 279 panels of wooden trestles were filled or replaced with culverts and 153 panels of wooden bridges were replaced with permanent steel and concrete structures.

The upgrading of Frisco yards to more efficiently accommodate a growing volume of traffic continues. A major project begun during the year was the three-phase modification and modernization of Cherokee Yard at Tulsa, Oklahoma, which will be completed in 1978 at a total estimated cost of \$4.7 million.

MAINTENANCE OF EQUIPMENT

During the year regular inspection and repair of freight cars and locomotives cost the Frisco \$27.9 million. In a growing number of instances, routine running repairs are being made in train yards to avoid the time and expense of moving equipment into repair shops. Frisco train yards are being modified to accommodate mechanized off-track vehicles carrying mechanics, tools and parts for on-the-spot repair of freight cars often while still coupled in trains. In addition to its role in maintaining the Company's freight car fleet, Frisco's Springfield (Mo.) car shop also added to the Company's coal carrying capacity by the installation of an assembly line to assemble 400 new hopper cars from factory-made kits of component body parts.

More powerful locomotives and better utilization are enabling the Frisco to haul a greater tonnage with fewer units. Greater efficiency in locomotive maintenance also was attained as a result of the installation of an assembly-line type of repair track in our Springfield locomotive shop. As part of its continuing modernization program,

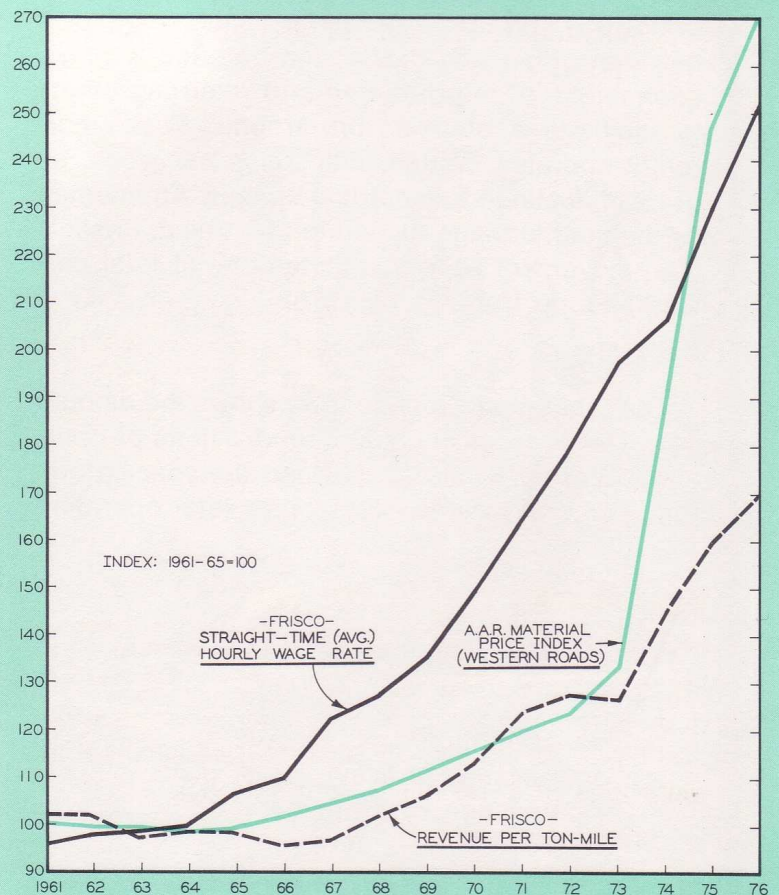
new and more powerful Diesel units are being substituted for old units with lower horsepower ratings.

LABOR COSTS

Under the three-year labor contracts negotiated nationally and due to expire at the end of 1977, union employees were granted two 12¢ per hour cost-of-living adjustments, the first on January 1 and the second on July 1; yardmasters also were granted two cost-of-living adjustments on the same dates, each in the amount of \$24 per month. Additionally, a 3% general wage increase went into effect on April 1 for employees covered by labor contracts.

Under the same contracts, a National Dental Plan for union employees and their dependents was established on March 1. The entire cost is borne by the railroad.

During 1976 the Frisco negotiated a local agreement to establish an interdivisional run which permits the Frisco to operate trains between Tulsa, Oklahoma, and Fort Scott, Kansas, without a crew change at an intermediate terminal. Another agreement negotiated during the year permits trains to move from Amory, Mississippi, to York, Alabama, without a crew change. Interdivisional runs also are operated between St. Louis and Springfield, Missouri.



OPERATING CHARGES UP

Frisco's operating charges during 1976 were up 17% under the influence of a \$2.7 million increase in its payroll taxes and a \$4.7 million increase in the cost of hiring equipment and facilities from others.

PAYROLL TAXES UP

Total payroll taxes in 1976 were \$21.5 million, up 14%. Railroad Retirement Tax payments were \$19.2 million, an increase of 12.1% from the level of the year earlier because of the elevation of the maximum employe earnings base (upon which the tax is calculated) to \$1275 per month, and an increase in the Supplemental Retirement Tax rate from 8.5¢ to 12¢ per hour.

During the year, the Unemployment Tax rate was raised from 4% to 5.5% on an unchanged base of \$400 per month.

On January 1, 1977 the maximum employe earnings base on which the Railroad Retirement Tax is calculated rose to \$1375 per month, the Supplemental Retirement Tax rate rose to 12.5¢ per hour and the Unemployment Tax rate jumped to 8%.

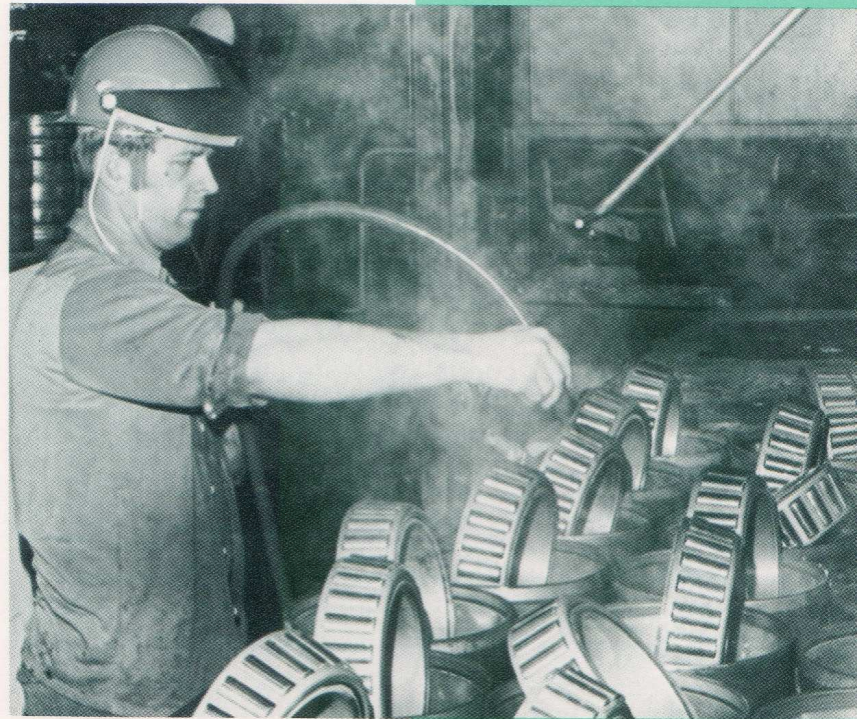
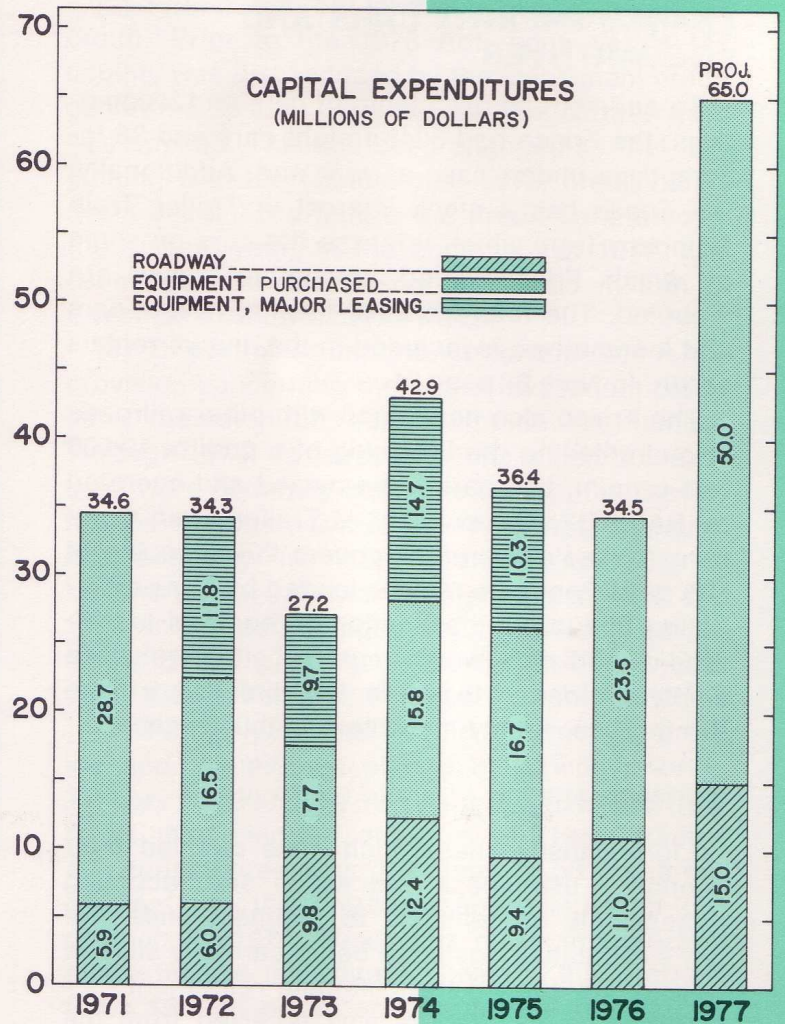
CAPITAL IMPROVEMENTS

As an advancing technology makes available better tools and techniques, their application to railroading has made possible larger and more sophisticated rolling stock as well as sturdier roadways and structures. In addition to \$79.9 million spent on maintenance during the year, Frisco's capital spending program totaled \$34.7 million, of which \$21.8 million went for new cars and locomotives, \$11.1 million went for improved roadway and structures and \$1.8 million went for other additions and improvements to its property.

Included in Frisco's 1976 capital spending program was the acquisition of 20 locomotives and 439 freight cars, all of which were purchased under Conditional Sale Agreements. The types of cars and locomotives purchased may be found on page 25, together with similar data for equipment installed in prior years.

EQUIPMENT OBLIGATIONS

Equipment obligations outstanding at year end, including those due in one year, totaled \$117.2 million, an increase of \$14.3 million, representing additional obligations of \$26.2 million, less serial maturities of \$11.9 million during 1976.



Roller bearings are gradually supplanting friction bearings in freight service.

LEASED FREIGHT CARS AND LOCOMOTIVES

To augment its ownership of cars and locomotives, the Frisco had 3048 freight cars and 36 locomotives under lease at year end. 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. The future cost of leasing freight cars and locomotives is included in the annual rentals shown in Note 5, page 21.

The Frisco also has joined with other railroads in guaranteeing the financing of a pool of 10,000 free-running box cars to be owned and operated by RAILBOX, a subsidiary of Trailer Train Company; Frisco's guarantee covers the financing of 500 cars. Pool cars may be loaded by any participating line to any destination, in contrast to railroad-owned cars which must be either returned empty or loaded to, or in the direction of, the owning line. Empty movement is thus reduced.

RETIREMENTS

Light density lines which have outlived their economic usefulness and which are becoming increasingly burdensome to maintain under today's escalating costs are being carefully studied with a view toward their ultimate retirement.

During 1976 authority was received from the Interstate Commerce Commission to retire 6.7 miles of line between Parsons and Dennis, Kansas, and 14 miles of line between Pittsburg and Mulberry, Kansas. Authority also was received from the Florida Public Service Commission to retire our Bayou Chico Bridge in Pensacola, Florida.

Entering 1977 the Frisco and its rail subsidiary — the Quanah, Acme & Pacific Railway Company — have applications pending before the ICC to retire an additional 204.5 miles of line.

MERGERS

In previous reports you were informed regarding the Rock Island merger proceeding which has been pending before the Commission for over fourteen years. Last year it was noted that the ICC, on January 12, 1976, entered its order dismissing all merger applications filed in these proceedings with the exception of the merger applications of the Southern Pacific and the D&RGW. The Commission provided that these two carriers and other "interested parties" may negotiate with the Rock Island and file appropriate applications with the Commission seeking approval of any negotiations concluded by the

parties. The Southern Pacific filed an application with the ICC for authority to purchase the Rock Island line of railroad between St. Louis, Missouri, and Kansas City, Kansas, and between Santa Rosa, New Mexico, and Topeka, Kansas, on terms to be negotiated. The Commission on February 4, 1977 rejected the Southern Pacific's application and terminated the Rock Island proceedings. Petitions for reconsideration or appeals may be filed.

LITIGATION

In previous Annual Reports you were informed of the existence of two antitrust suits filed by REA Express against the Company and numerous other railroads in which REA is seeking treble damages for actions of the defendants preceding the sale of the stock of REA Express by the railroads. Both of these suits have been dismissed by the trial courts, but appeals are either pending or expected. The Company believes that an unfavorable outcome on appeal is remote.

A SAFER RAILROAD

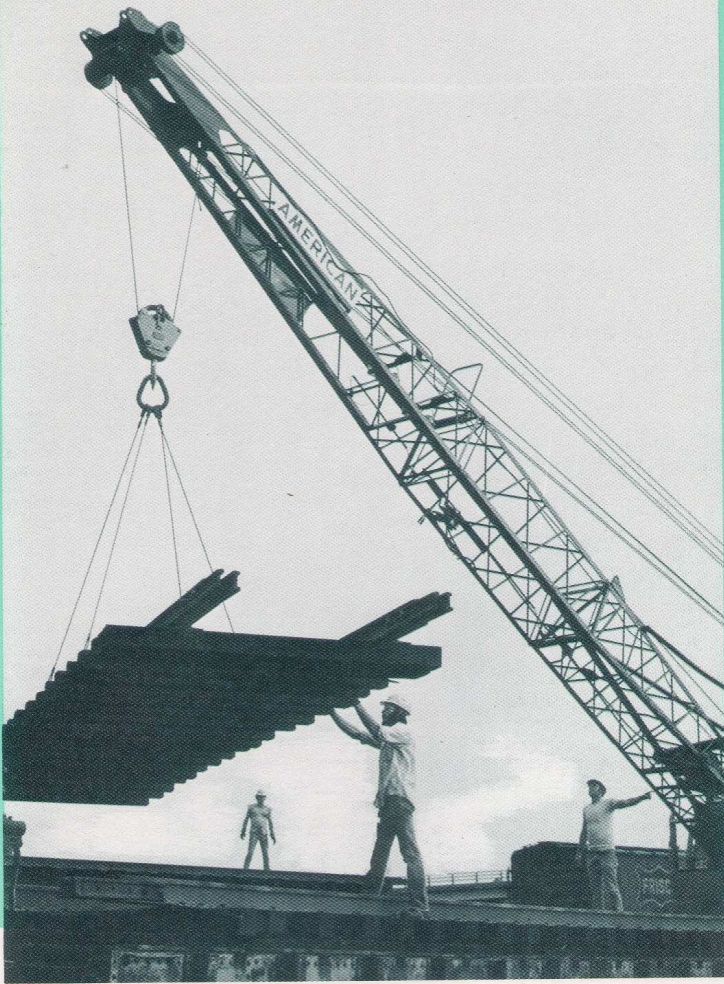
As injuries to employes declined, the number of man-days lost due to accidents was reduced, reflecting a reduction in both the frequency and severity of injuries.

The installation of automatic grade crossing protection devices continued at an accelerated pace, aided by additional federal and state participating funds made available under the Federal Highway Act of 1973.

More stringent federal regulations covering the transportation of hazardous commodities became effective in 1977. Also expected this year are additional environmental regulations concerning noise, water and air pollution.

HONING EMPLOYE SKILLS

Frisco continued to move forward in its personnel training and development programs. These include in-house training of first-line supervisors and mid-managers and executive development programs at several leading universities around the country. In the area of specialized technical training, Frisco's innovative Clerical Training Program continued to prepare newly hired employes and temporarily displaced personnel by teaching proper station accounting procedures as well as station communications functions. Train service personnel likewise benefit from a comprehensive multi-faceted brakeman-switchman training program. Among other efforts to strengthen its competitive position, Frisco advanced its sales,



marketing and sales management training programs. In honing the skills of its men and women, Frisco is preparing them for the challenges that lie ahead.

FRISCO WELCOMES TWO NEW DIRECTORS

At the annual meeting of the stockholders held in St. Louis, Missouri, on May 11, Frank A. Jones, President of Cook Industries, Inc., and Armand C. Stalnaker, Chairman and President of General American Life Insurance Company, were elected Directors for a three-year term expiring in 1979. Mr. Jones succeeded Edward W. Cook who did not stand for re-election because his schedule did not permit regular attendance at Frisco meetings and Mr. Stalnaker succeeded William A. McDonnell who has served with distinction since 1953 and who has reached the age limitation set for Directors. Mr. McDonnell will remain as an Advisory Director.

TAX REFORM ACT OF 1976

Provisions of the Tax Reform Act of 1976 which will be of benefit to your Company and the rail industry are summarized below:

(1) The 10% investment credit, due to return to 7% on December 31, 1976, is extended to January 1, 1981.

(2) First-in-first-out treatment of investment tax credit: Prior to the 1976 Act, each year's tax liability was first reduced by the investment credit generated in that year before the carryforward was applied. This has been changed so that, beginning with the taxable year 1976, credit carryovers are utilized before the credit generated in the current year. At the beginning of 1977, it is estimated that the Frisco had \$16.5 million of investment credit carryforward.

(3) Of particular importance to railroads is the provision concerning the use of investment credit as a reduction of federal income tax liability. Through 1976, investment credits which could be used were generally limited to 50% of tax liability for the tax year. Under the 1976 Act, however, railroads may use their credits up to 100% of tax liability for taxable years ending in 1977 and 1978 and in percentages which are reduced annually by 10 percentage points for later years until 1983 when the limitation returns to 50%.

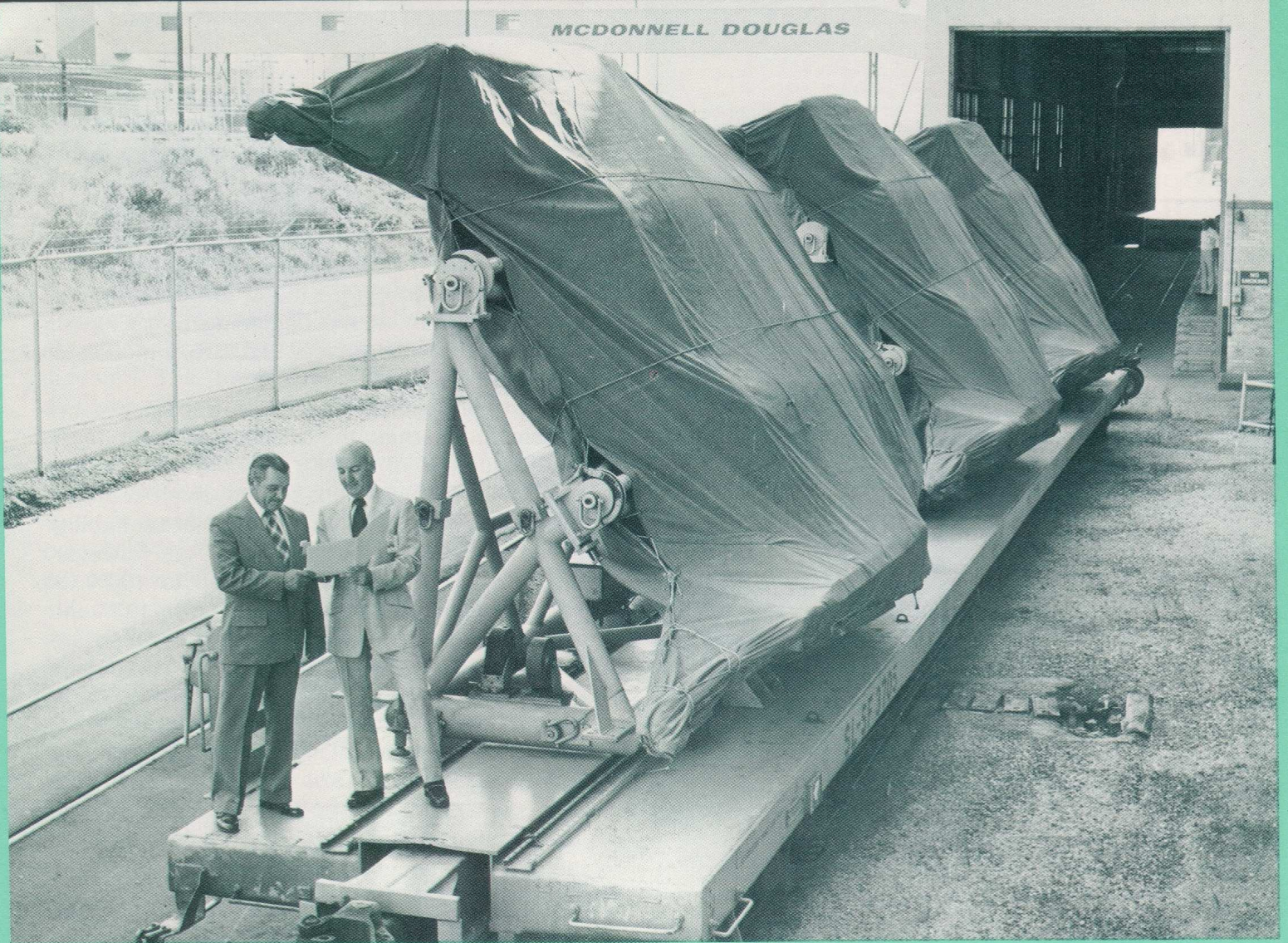
(4) Formerly railroads could not amortize grading and tunnelbores placed in service prior to January 1, 1969. The 1976 Act provides that railroads may elect to amortize pre-1969 grading and tunnelbores over a period of 50 years beginning with the taxable year ending after December 31, 1974. Frisco has made this election and estimates the adjusted basis in this property to be \$50 million, or an estimated additional deduction from taxable income of \$1 million per year.

The above-described benefits will provide an important source of funds for investment in rail property.

SYNOPSIS OF 4R ACT

Some of the more basic provisions of the Railroad Revitalization and Regulatory Reform Act of 1976 call for:

- Making available \$2.1 billion for the Consolidated Rail Corporation to complete the restructuring of the bankrupt railroads in the Northeast and Midwest and \$1.75 billion over the next five years to improve passenger service in the Northeast Corridor.
- Reforming regulations to give railroads new rate-making freedom and impose new procedures on the Interstate Commerce Commission to reduce regulatory lag. Within the next two years rail carriers may adjust individual and joint rates up or down not more than 7 per cent from the prior year without ICC approval. Authority to do this extends only to carriers which do not have a dominant position in their market and when such action cannot be construed as an unfair or predatory competitive practice. General rate



Sections of fighter-plane fuselages, three to each 89' flat car, once moved via highway.

adjustments are not affected by this legislation.

- Assigning to the Secretary of Transportation the task of studying the national rail system and making recommendations for greater efficiency through a restructuring of the industry. This could include the development of plans and recommendations for mergers and other projects at the Secretary's own initiative or at the instigation of any railroad requesting his assistance. The Secretary may recommend but not require mergers and consolidations. Should the Secretary or any railroad propose a merger or coordination prior to December 31, 1981, the ICC shall, after application is made, render a final decision within two years.

- \$360 million to be provided over the next five years for local rail service assistance. The federal government would pay 100 per cent the first year, 90 per cent the second, 80 per cent the third and up to 70 per cent for the next two years to subsidize uneconomic branch lines that railroads want to abandon. The states involved would be required to pay the difference between the federal subsidy and 100 per cent.

- Revision of the abandonment procedures under the Interstate Commerce Act to place the burden of proof on carriers proposing to discontinue service. No abandonment may be permitted where a subsidy is given to offset losses.

- Empowering the Secretary of Transportation to issue loan guarantees up to \$1 billion for equipment and facilities acquisition, rehabilitation or improvement. Certain dividend restrictions would be imposed, and the Secretary would have the right to assure that rail assets and revenues are used for railroad purposes.

- Each railroad to submit to the Secretary of Transportation a traffic density analysis of its system. Such analysis is to be used to classify each segment of the system in terms of usage and contribution to the economic viability of such carrier and other carriers. Each railroad must also submit to the Secretary a statement of deferred maintenance and delayed capital expenditures along with projected amounts needed for maintenance and capital expenditures through 1985. Based upon this, the Secretary will recommend to Congress the amount and type of equity



Employee training sessions hone skills to meet future challenges.

financing needed through 1985 and the means of providing the federal share.

- Making available \$600 million of flexible financing for working capital loans and rehabilitation and plant improvement purposes to qualifying railroads with approval of the Secretary of Transportation. A new financing mechanism, "redeemable preference shares," would be created, with borrowing railroads issuing them to the Rehabilitation and Improvement Fund. Redeemable preference shares would be senior securities and would not pay dividends for ten years. This arrangement is similar to low interest loans but does not require beneficiaries to increase their debt.

- An end — effective three years after enactment of the Act — to discriminatory state taxation with railroads being permitted to seek injunctive relief through federal courts. States are barred from imposing other taxes in lieu of discriminatory property taxes.

- The Secretary of Transportation to complete a study, within one year, of federal aid for railroads and, after comparison with federal aid for

other modes, to determine the impact public assistance for other modes has had on railroads.

LOCKS AND DAM 26

The Frisco, other midwestern railroads and environmentalists stand in strong opposition to the proposed expansion of barge traffic on the Mississippi and Illinois rivers. The proposed construction of a new Alton Locks and Dam 26 on the Mississippi River just north of St. Louis is regarded as the first step in expanding subsidized barge traffic on the upper Mississippi as well as the Illinois rivers through enlargement of the entire locks and dam system. Barges remain the only form of transportation whose right-of-way is 100% built and operated at taxpayer expense. In contrast, railroads must spend between twenty and twenty-five cents out of every revenue dollar to own and maintain their own rights-of-way. Because of this inequity, barges can charge rates which do not come close to covering the true economic cost of providing water service. The effect of such subsidized competition, particularly upon those railroads which

parallel rivers or other waterways, is serious and costly. Waterway interests are expected to renew their push for the Locks and Dam 26 project in the 95th Congress. Rail stockholders can help protect their investments by acquainting their elected representatives with their views and the need for user charges for the use of facilities built at the taxpayers' expense.

COAL SLURRY PIPELINE

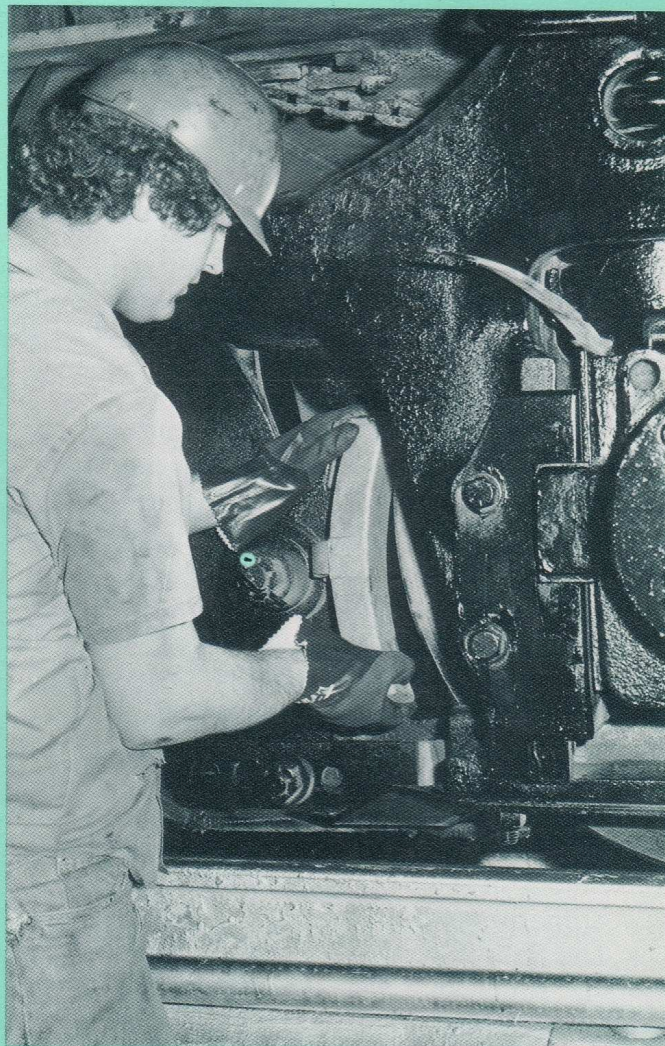
Several federal and state proposals to give the power of eminent domain to coal slurry pipelines are pending. Railroads stand in strong opposition to the adoption of such legislation and take the position that it would not be in accord with sound transportation policy. Railroads *already in place* are capable of substantial expansion to accommodate new coal traffic. Today the volume of coal moved by rail far exceeds the volume of any other commodity. In 1976 coal constituted almost 26% of all tonnage carried by the American railway system and 13% of total revenues. To deprive rail carriers of this source of revenue would be to burden other commodities moving by rail with a greater proportion of overall transportation costs. Railroads and their employees are jointly opposing these proposals in cooperation with environmental, agricultural and other groups interested in the conservation of scarce water that would have to be used for the transmission of the coal particles through pipelines. Letters to Congress from railroad shareholders would be of great assistance.

MANAGEMENT'S DISCUSSION OF YEARS 1975 TO 1973

1975 versus 1974

Net income in 1975 was \$8.6 million versus \$13.2 million in 1974 when the Frisco enjoyed one of its most profitable years. Adversely affected by a steep drop in traffic brought on by the most severe economic downturn since the 1930's and by the inability to apply timely rate increases to offset inflationary pressures, Frisco's depressed 1975 earnings were aided by extraordinary income of \$3.5 million from the sale of retired rail facilities. Earnings per share in 1975 were \$3.30 versus \$5.08 in 1974. Included in earnings for the year 1975 was \$1.6 million of estimated benefits from allowable investment credit on the Company's Federal Income Tax; the comparable figure for 1974 was \$4.1 million, during which year the Company's earnings were also benefited by a refund of approximately \$700,000

in Federal Income Tax as a result of a carry-back of a 1973 net operating loss. Operating revenues in 1975 were 3.5% behind those of the preceding year despite higher freight charges, as rate increases proved too little, too late to offset a substantial reduction in traffic volume and spiraling costs of operation. Higher freight charges generated an estimated \$26.5 million in revenue during 1975. Operating expenses in 1975 were \$219.6 million, down 0.3% from the level of the year before as operations were measurably curtailed to conform to a lower traffic volume. The reduction was achieved in the face of greatly increased payroll costs which had to be applied under the three-year labor contracts negotiated nationally by the industry as a whole and an unremitting rise in the price of everything required to provide transportation service, particularly fuel, the cost of which was up more than \$2.5 million from the year-earlier level. Income derived from other than railway operations during 1975 declined 34% chiefly as a result of a drop in the sale of land to industries for plant sites and a reduction in the interest received from short term investments.



1974 versus 1973

Net income in 1974, under Generally Accepted Accounting Principles, was \$13.2 million versus \$8.2 million in flood-ravaged 1973 restated to conform to GAAP. Under GAAP, there was a reduction of net income by increasing deferred Federal Income Tax accruals \$1.9 million in 1974 and \$4.1 million in 1973. Earnings in 1974 were benefited by a refund of approximately \$700,000 in Federal Income Tax as a result of a carry-back of a 1973 net operating loss, while earnings in 1973 were benefited by a refund of \$1.2 million in Federal Income Tax as a result of flood disaster losses in that year. Operating revenues in 1974 were up 10.1% from the level of the previous year under the influence of higher freight charges authorized by the ICC to help offset inflationary cost increases which included higher Railroad Retirement tax payments and soaring fuel prices. Freight rate increases in 1974 ac-

counted for about \$35.3 million of operating revenues. Operating expenses in 1974 rose 8.4% from the level of the year before under the influence of higher wage and fringe benefits and inflationary increases in the cost of materials and supplies, particularly fuel, the price of which surged more than 70% in one year's time; greater expenditures for maintenance during 1974 also were a factor. Operating charges during 1974 rose \$3.2 million from the level of the year before because of a \$5.5 million increase in payroll taxes, partially offset by a \$2.3 million reduction in the cost of hiring equipment from others. During 1974, there was a decrease of \$1.3 million in income from other than railway operations; a major influence was the downward revaluation of second-hand relay rail inventory at the insistence of the ICC to partially offset the upward revaluation undertaken in 1973.



St. Louis-San Francisco Railway Company
Consolidated Five-Year Summary of Operations

CONDENSED INCOME ACCOUNT

(000) omitted

	1976	1975	1974	1973	1972
Operating revenues	\$321,512	\$280,353	\$290,573	\$263,886	\$238,959
Operating expenses	244,935	219,602	220,353	203,245	181,295
Net operating revenue	76,577	60,751	70,220	60,641	57,664
Operating charges	50,432	43,022	44,552	41,338	31,936
Net operating income	26,145	17,729	25,668	19,303	25,728
Other income, net	2,967	2,642	4,030	5,292	2,217
Balance for fixed and contingent charges	29,112	20,371	29,698	24,595	27,945
Fixed and contingent charges ...	13,528	13,653	13,201	12,664	12,266
Income before federal income taxes	15,584	6,718	16,497	11,931	15,679
Estimated federal income taxes:					
Current	1,935	(200)	1,384	(350)	830
Deferred	1,635	1,800	1,940	4,120	3,730
Income before extraordinary item	12,014	5,118	13,173	8,161	11,119
Extraordinary item	—	3,452	—	—	—
Net income	\$ 12,014	\$ 8,570	\$ 13,173	\$ 8,161	\$ 11,119
Earnings per share on:					
Ordinary income	\$ 4.61	\$ 1.97	\$ 5.08	\$ 3.14	\$ 4.28
Extraordinary income	—	1.33	—	—	—
Net income	\$ 4.61	\$ 3.30	\$ 5.08	\$ 3.14	\$ 4.28

Two Decade Comparison of Selected Statistics
(Rail System)

	1976	% Change 1976 vs.			% Change 1966 vs.		
		1966	1956	1966	1956	1956	
Total operating revenues (000)	\$316,879	108.0	130.9	\$152,357	11.0	\$137,251	
Revenue ton-miles (millions)	14,564	21.4	53.2	11,995	26.2	9,504	
Freight train miles (000)	9,447	9.8	15.3	8,605	5.0	8,196	
Average number of employes	8,196	(2.5)	(41.2)	8,405	(39.7)	13,936	
Man-hours paid (000)	18,723	(8.2)	(43.1)	20,388	(38.0)	32,890	
Total payroll#	\$130,645	107.4	87.7	\$ 62,991	(9.5)	\$ 69,614	
Average hourly rate	\$ 8.5700	145.0	276.7	\$ 3.4974	53.7	\$ 2.2750	
(incl. fringe benefits)†							
Western RR Material Price Index	261.7	169.5	198.4	97.1	10.7	87.7	
Including fuel. (1967 = 100)							

Includes accruals

† Includes payroll tax and health & welfare benefits

Consolidated Income Statement

	<u>1976</u>	<u>1975</u>
	(000)	omitted
OPERATING REVENUES:		
Freight	\$312,556	\$272,004
Other	8,956	8,349
Total operating revenues	321,512	280,353
OPERATING EXPENSES:		
Maintenance of way and structures	47,229	42,538
Maintenance of equipment	46,756	40,080
Transportation	126,394	115,008
Other	24,556	21,976
Total operating expenses (includes depreciation of \$14,100,000 and \$14,075,000, respectively)	244,935	219,602
Net operating revenue	76,577	60,751
OPERATING CHARGES:		
Payroll taxes	21,483	18,820
Property and other taxes	7,541	7,447
Equipment and joint facility rents	21,408	16,755
Total operating charges	50,432	43,022
Net operating income	26,145	17,729
OTHER INCOME:		
Profit on Company bonds purchased	954	572
Other, net	2,013	2,070
Total other income	2,967	2,642
Balance for fixed and contingent charges	29,112	20,371
FIXED AND CONTINGENT CHARGES (Page 24):		
Interest on long term debt — fixed	11,858	11,789
Other fixed charges	308	449
Interest on long term debt — contingent	1,362	1,415
Total fixed and contingent charges	13,528	13,653
Income before federal income taxes	15,584	6,718
ESTIMATED FEDERAL INCOME TAXES:		
Current	1,935	(200)
Deferred	1,635	1,800
Total estimated federal income taxes (Notes 1 and 3, Page 20)	3,570	1,600
Income before extraordinary item	12,014	5,118
Extraordinary item (Note 7, Page 22):		
Retirement and sale of rail facilities under threat of condemnation ..	—	3,452
NET INCOME	\$ 12,014	\$ 8,570
EARNINGS PER SHARE:		
Ordinary income	\$ 4.61	\$ 1.97
Extraordinary income	—	1.33
NET INCOME	\$ 4.61	\$ 3.30

Consolidated Balance Sheet

	December 31,	
	1976	1975
	(000) omitted	
ASSETS		
CURRENT ASSETS:		
Cash	\$ 3,656	\$ 2,296
Temporary cash investments	3,536	3,536
Cash deposits for interest, dividends, etc.	902	891
Accounts receivable	27,190	27,347
Material and supplies, at average cost	24,569	20,239
Other current assets	846	840
Total current assets	60,699	55,149
SPECIAL DEPOSITS	7,898	2,503
INVESTMENTS:		
Securities of and advances to affiliates (Page 26)	7,106	6,509
Other investments	250	251
Total investments	7,356	6,760
PROPERTIES (Note 1, Page 20 and Page 26):		
Roadway and structures	367,265	359,123
Equipment	318,345	308,547
Non-operating property	8,034	8,166
Accumulated depreciation — road	(69,823)	(67,817)
Accumulated depreciation — equipment	(138,074)	(137,364)
Accumulated depreciation — non-operating property	(356)	(301)
Total properties — net	485,391	470,354
OTHER ASSETS:		
Unamortized expense on long term debt	1,767	1,848
Miscellaneous	4,711	4,536
Total other assets	6,478	6,384
TOTAL ASSETS	\$567,822	\$541,150

Consolidated Balance Sheet

	December 31,	
	1976	1975
	(000) omitted	
LIABILITIES		
CURRENT LIABILITIES:		
Audited accounts and wages payable	\$ 11,518	\$ 6,876
Accrued and miscellaneous accounts payable	26,277	24,892
Interest and dividends payable	4,409	4,422
Estimated federal taxes on income (Note 3, Page 20)	2,106	100
Other accrued taxes	4,609	4,010
Other current liabilities	6,697	5,867
Total current liabilities (excluding current portion of long term debt)	55,616	46,167
LONG TERM DEBT (Page 24):		
First Mortgage Bonds, 4% Series A — 1997	57,391	58,952
First Mortgage Bonds, 4% Series B — 1980	13,902	14,312
Income Debentures, 5% Series A — 2006	27,656	28,336
Purchase Money Mortgage Notes, 6¾% — 1992	5,400	5,550
Equipment obligations	117,167	102,872
Other long term debt	3,296	4,313
Total long term debt (\$14,080,000 payable in 1977 and \$13,020,000 in 1976)	224,812	214,335
OTHER LIABILITIES:		
Deferred federal income taxes (Notes 1 and 3, Page 20)	59,983	59,542
Estimated casualty and other reserves	1,719	1,275
Miscellaneous, including other deferred credits	2,398	2,438
Total other liabilities	64,100	63,255
STOCKHOLDERS' EQUITY		
CAPITAL STOCK		
Preferred, \$100 par value — Authorized 1,500,000 shares, none issued.		
Common, no par value — Authorized 6,000,000 shares, issued: 1976 — 2,611,436 shares and 1975 — 2,595,619 shares, less 50 shares in treasury 1976 and 1975	113,967	113,565
CAPITAL SURPLUS	18,935	18,935
RETAINED INCOME (Page 23)	90,392	84,893
Total stockholders' equity	223,294	217,393
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$567,822	\$541,150

Notes to Financial Statements

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

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. 50.78% 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 the equity method basis.

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, 1976 nondepreciable property, including land and land rights, aggregated approximately \$236,700,000.

INCOME TAXES: The provision for income taxes includes amounts for deferred income taxes resulting from the excess of tax amortization and depreciation (except pre-1969 grading amortization) over recorded book depreciation. Investment tax credit is accounted for under the flow-through method.

2. PENSION PLAN:

The Company has a noncontributory pension plan covering officers and supervisory employees. The cost of the plan charged to income was \$1,614,000 in 1976 and \$1,340,000 in 1975 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 were approximately \$1,700,000 at December 31, 1976.

3. FEDERAL INCOME TAXES:

Federal taxes on income for the years 1974 through 1976 are subject to final determination by the Treasury Department. In the opinion of management, the reserve provided for federal taxes on income is adequate. Estimated benefits from allowable investment credit included in earnings for the year 1976 were \$3.6 million compared to \$1.6 million in 1975. At the end of 1976 there was an estimated \$16.5 million in unused investment credit, most of which has been offset against deferred income taxes.

4. STOCK OPTIONS:

The Company has granted options to purchase shares of its common stock to certain officers and key employees under a nonqualified stock option plan adopted in 1975. Options on 100,000 shares may be granted under the plan at purchase prices not less than 100% of the fair market value of the shares on the date of grant. Options are exercisable in cumulative annual instalments and expire over a five-year period ending in 1985. Funds received for exercised options are credited to the capital stock account.

A committee of the Board of Directors may allow optionees, who so request, the alternative of receiving stock appreciation rights in lieu of exercising their stock options. If approved, payment shall be, at the discretion of the committee, in cash or in shares of common stock valued at the fair market value or as a combination thereof. The recording of stock appreciation rights results

Notes to Financial Statements (continued)

in a charge to compensation expense and a credit to capital stock and/or cash for the excess of the market price over the option price.

	Number	Option Price
Shares subject to option:		
Outstanding at beginning of 1976	95,380	
Exercised	(13,584)	\$23.44
Stock appreciation rights	(7,793)	23.44
Canceled	(1,928)	
Outstanding at end of 1976	72,075	\$23.44
Exercisable at end of 1976	18,647	
Become exercisable during 1977	18,575	
Shares reserved for future options:		
Beginning of 1976	4,620	
End of 1976	12,108	

5. LEASE COMMITMENTS:

As of December 31, 1976, minimum rental commitments under long term leases, subject to partial offset for freight car earnings while offline, were as follows, (000) omitted:

Year	Lease Rentals			Portion Classified as Capital Leases
	Trans- portation Equipment	Other	Total	
1977	\$ 5,693	\$1,495	\$ 7,188	\$ 1,943
1978	5,693	1,270	6,963	1,943
1979	5,498	786	6,284	1,828
1980	5,017	441	5,458	1,483
1981	5,017	343	5,360	1,483
After 1981	41,399	1,778	43,177	12,750
Total	\$68,317	\$6,113	\$74,430	\$21,430

The Financial Accounting Standards Board (FASB) has recently established new standards of financial accounting and reporting for leases, including capital leases which functionally finance the acquisition or use of assets. Capital leases entered into after December 31, 1976 must be recorded as depreciable assets and as liabilities. By 1981 all capital leases, including pre-1977 capital leases, must be recorded in accordance with FASB standards. The minimum capital lease rentals include \$8,193,000 of imputed interest, generally determined using the Company's incremental borrowing rate. If the Company had adopted the new standards in 1976, the year-end accounts would have increased as follows, (000) omitted:

Equipment	\$14,528	Current lease liability	\$ 950
Accumulated depreciation	2,839	Non-current lease liability	12,287
	\$11,689		\$13,237

Notes to Financial Statements (continued)

Capitalization of these leases would not have had a material effect upon net income for 1976. Most capital leases have options allowing the Company to renew the lease at the fair rental value or purchase the asset at the fair market value when the lease expires. Rental expense for operating leases in 1976 was approximately \$5,400,000.

6. CONTINGENT LIABILITIES:

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 \$15,000,000 as of December 31, 1976. The Company is a participant in service interruption policies with The Imperial Insurance Company (Cayman Islands) Limited. The maximum annual premium under the policies in the event of work stoppages on other participating railroads is \$7,045,000.

7. EXTRAORDINARY ITEM:

During 1975 the Company recorded extraordinary income of \$3,452,000 as a result of the retirement and sale of rail facilities near Cochrane, Alabama, under threat of condemnation by the United States Corps of Engineers. The funds received were reinvested in non-depreciable road properties, and consequently there was no tax effect.

Report of Independent Accountants

Price
Waterhouse & Co.

ONE MEMORIAL DRIVE, ST. LOUIS, MISSOURI 63102-314-425-0500

February 28, 1977

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

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of income, retained income and changes in financial position present fairly the consolidated financial position of the St. Louis-San Francisco Railway Company and its subsidiaries at December 31, 1976 and 1975, and the results of their operations and the changes in their financial position for the years then ended, in conformity with generally accepted accounting principles consistently applied. Our examinations of these statements 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.

Price Waterhouse & Co.

Consolidated Retained Income Statement

	1976	1975
	(000) omitted	
Balance at beginning of year	\$ 84,893	\$ 82,812
Add:		
Net income for the year	12,014	8,570
Deduct:		
Dividend on Common Stock — Per Share \$2.50 in 1976 and 1975 ..	6,515	6,489
Balance at end of year	\$ 90,392	\$ 84,893

Consolidated Statement of Changes in Financial Position

	1976	1975
	(000) omitted	
SOURCES OF FUNDS:		
Income before extraordinary item	\$ 12,014	\$ 5,118
Depreciation and other non-cash charges	15,030	14,590
Deferred federal income tax	1,635	1,800
Funds provided from operations	28,679	21,508
Extraordinary income	—	3,452
Proceeds long term debt	26,303	14,957
Stock options and stock appreciation rights	402	—
Proceeds sale of property and salvage	4,694	4,172
Miscellaneous	(2,008)	899
Total	58,070	44,988
APPLICATIONS OF FUNDS:		
Additions and betterments — road and equipment	34,708	26,112
Deposit-undelivered equipment financed	4,920	—
Long term debt retired	15,826	14,133
Dividends	6,515	6,489
Total	61,969	46,734
DECREASE IN WORKING CAPITAL (Excluding current portion of long term debt)	\$ 3,899	\$ 1,746
CHANGES IN WORKING CAPITAL:		
Cash and temporary cash investments	\$ 1,360	\$ (4,173)
Accounts receivable	(157)	1,230
Material and supplies	4,330	1,742
Accounts payable	(6,027)	(2,500)
Estimated federal taxes on income	(2,006)	2,025
Other	(1,399)	(70)
DECREASE IN WORKING CAPITAL (Excluding current portion of long term debt)	\$ 3,899	\$ 1,746

SEE NOTES TO FINANCIAL STATEMENTS

Long Term Debt

	Date of Maturity	Outstanding Dec. 31, 1976		Fixed and Contingent Interest	
		Due After 1977	Due in 1977	Rate	Expense for 1976
FUNDED DEBT UNMATURED:					
First Mortgage Series A	1-1-97	\$ 57,391,000†	*	4.00	\$ 2,320,428
First Mortgage Series B	9-1-80	13,902,000†	*	4.00	566,580
Income Debentures Series A	1-1-06	27,656,500†	*	5.00	1,362,075
Purchase Money Mortgage Notes	8-1-92	5,400,000	*	6.75	370,406
		<u>104,349,500</u>			<u>4,619,489</u>
EQUIPMENT OBLIGATIONS‡:					
Trust Certificates:	Serially to				
Series N	3-15-80	837,000	\$ 279,000	4.25	49,900
Series O	5-15-80	945,000	315,000	4.38	60,292
Conditional Sale Agreements:					
Numbers:					
17	11-1-77	—	59,676	5.00	5,954
18/22	8-1-78	264,047	350,783	4.50	32,929
23/27	1-15-79	895,136	596,758	4.45	74,968
28/29	3-15-79	119,218	79,478	4.45	10,463
31/39	1-15-81	2,802,118	800,605	5.25	201,402
41/43	3-1-82	1,214,565	269,903	6.25	99,808
44/45	3-1-82	1,059,014	235,336	5.75	80,063
46/50	7-1-82	2,763,416	552,683	6.25	224,528
51/56	1-1-83	4,679,167	935,833	6.75	442,181
57/58	10-1-80	999,990	333,330	6.25	108,591
59/64	12-15-83	3,996,000	666,000	7.25	384,268
65	8-15-84	1,750,000	250,000	8.25	177,891
66/67	1-15-85	3,014,000	376,750	9.38	319,354
68/70	2-1-85	3,024,000	378,000	9.50	326,183
71	7-1-85	2,303,229	287,903	9.75	266,671
72	11-15-82	2,500,000	500,000	6.50	248,986
73/74 & 76/77	7-1-86	5,339,295	593,255	7.75	482,761
75	5-15-83	1,592,878	265,480	6.50	138,791
78/80	10-1-86	6,489,619	721,069	8.25	638,146
81	3-1-84	3,550,647	507,235	6.50	293,855
82/83	3-1-88	6,074,080	552,189	7.62	510,545
84/87	5-1-89	10,040,445	836,704	8.63	960,815
ACF, et al	4-1-90	11,432,602	879,431	10.00	1,253,189
88/90	4-1-91	3,227,890	230,564	10.25	345,592
91/92	4-1-91	5,686,185	406,156	9.87	437,692
93/94	11-1-91	5,486,133	391,867	9.00	150,361
95/96	3-1-92	12,015,667	414,333	8.64	44,726
Matured During Year		—	—	—	6,729
		<u>104,101,341</u>	<u>13,065,321</u>		<u>8,377,634</u>
Other Long Term Debt		2,281,259	1,014,572		222,828
Totals		<u>\$210,732,100</u>	<u>\$14,079,893</u>		<u>\$13,219,951</u>

†Excludes bonds held in treasury as follows:

First Mortgage Series A	\$1,561,000
First Mortgage Series B	410,000
Income Debentures Series A	680,000

*Subject to sinking fund provisions under mortgage indentures in 1977.

First Mortgage Series A	\$738,084
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:

1977	\$13,065,321	1982	\$10,412,406	1987	\$4,125,577
1978	13,333,244	1983	8,171,269	1988	4,125,577
1979	12,731,078	1984	7,239,789	1989	3,573,388
1980	12,392,960	1985	6,482,554	1990	2,736,684
1981	11,065,328	1986	5,439,901	1991	1,857,253
				1992	414,333

Equipment Owned

DESCRIPTION	Owned Dec. 31, 1975	Changes During 1976			Owned Dec. 31, 1976
		Purchased	Reclas- sified	Retired	
DIESEL LOCOMOTIVES:					
Freight 3600 H.P. (A Units)	49	...	...	...	49
Freight 3000 H.P. (A Units)	21	...	...	1	20
Freight 2500 H.P. (A Units)	65	...	...	...	65
Freight 2000 H.P. (A Units)	99	20	...	...	119
All Purpose 1500 H.P.	100	...	...	50	50
Switch 1500 H.P.	51	...	...	...	51
Switch 1200 H.P.	15	...	...	...	15
Switch 1000 H.P.	25	...	...	...	25
Switch 44 Ton	1	...	...	...	1
Total	426	20	...	51	395
FREIGHT TRAIN CARS:					
Box-Plain	3,230	...	...	163	3,067
Box-Equipped-Non-Insulated	2,725	25	87	32	2,805
Box-Equipped-Insulated	1,297	...	...	...	1,297
Gondola	2,445	5	...	30	2,420
Hopper-Open Top	2,248	400	...	447	2,201
Hopper-Covered	2,424	...	...	90	2,334
Flat-Including Special Equipped	257	...	...	12	245
Wood Rack & Bulkhead Flat	855	...	...	1	854
Multi-Level Auto Transport	178	...	...	1	177
Mechanical Refrigerators	100	...	...	...	100
Caboose	228	9	...	31	206
Total	15,987	439	87	807	15,706
WORK EQUIPMENT:					
Tool and Material	601	...	16	21	596
Ballast	162	...	...	3	159
Boarding	67	...	4	4	67
Tank	118	...	...	3	115
Other	40	1	...	2	39
Total	988	1	20	33	976
MISCELLANEOUS EQUIPMENT:					
Motor Trucks	466	81	...	88	459
Automobiles	70	11	...	24	57
Airplane	1	...	...	...	1
Other	27	...	...	3	24
Total	564	92	...	115	541
FLOATING EQUIPMENT:					
Car Ferry	2	...	...	...	2
MOTOR CARRIER EQUIPMENT:					
Trucks	23	...	...	1	22
Tractors	90	...	...	2	88
Semitrailers	105	1	...	11	95
Service Cars	13	1	...	...	14
Total	231	2	...	14	219

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.	533,770.48‡	50.78	\$533,770	\$2,914,478†	\$	\$2,914,478
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	1,966,357	2,149,690
Pullman Co., The	8,456.00	1.16	169	109,928	.....	109,928
Terminal R. R. Association of St. Louis	2,058.00*	6.25	205,800	1	625,467	625,468
Trailer Train Co.	500.00	2.44	500	50,000	486,000	536,000
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				\$3,272,060	\$3,834,113	\$7,106,173

‡200,000 shares pledged under loan agreement.

†Equity of New Mexico and Arizona Land Company at December 31, 1976 (Note 1, Page 20).

*Stock pledged under First Mortgage.

Property Changes during the Year 1976

	Balance Dec. 31, 1975	Additions and Betterments	Retirements	Balance Dec. 31, 1976
Roadway and Structures	\$359,123,440	\$11,104,606	\$ 2,963,009	\$367,265,037
Equipment (Page 25):				
Diesel Locomotives	86,321,687	8,272,898	7,863,194	86,731,391
Freight Train Cars	204,981,664	13,576,503	4,766,154	213,792,013
Work and Miscellaneous	15,541,523	1,620,108	984,155	16,177,476
Motor Carrier Equipment	1,701,611	13,054	70,906	1,643,759
Total Equipment	308,546,485	23,482,563	13,684,409	318,344,639
Total Transportation Property	667,669,925	34,587,169	16,647,418	685,609,676
Non-Operating Property	8,166,080	120,938	252,788	8,034,230
Total Properties	\$675,836,005	\$34,708,107	\$16,900,206	\$693,643,906

OFFICERS

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Senior Vice President-Marketing, St. Louis, Mo.

W. F. THOMPSON

Senior Vice President-Operations, Springfield, Mo.

J. H. BROWN

Vice President-Corporate Affairs, St. Louis, Mo.

D. E. ENGLE

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

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N. A. KIRCHOFF

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

TRANSFER AGENTS FOR COMMON STOCK:

Citibank, N.A., 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:

Citibank, N.A., 111 Wall Street, New York, N.Y. 10015
Mercantile Trust Company National Association, 721 Locust Street, St. Louis, Mo. 63101

AUTHENTICATING AGENT:

Citibank, N.A., 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.

Annual Meeting of Stockholders second Tuesday
in May of each year

BOARD OF DIRECTORS



Lawrason Riggs III



Harold F. Ohlendorf



R. C. Grayson



F. A. Jones



A. C. Stalnaker



*W. A. McDonnell
(Advisory Director)*



Z. E. Barnes



Elliot H. Stein



Bruce K. Goodman



E. D. Grinnell



J. E. Gilliland



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B. B. Culver, Jr.



R. Hal Dean



Dudley E. Dawson, Jr.

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St. Louis, Missouri
(Real estate and investment firm)

R. HAL DEAN ^{1,2}
Chairman and Chief Executive Officer
Ralston Purina Company
St. Louis, Missouri

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Chairman and President
St. Louis-San Francisco Railway Company
St. Louis, Missouri

E. D. GRINNELL ¹
Senior Vice President-Marketing
St. Louis-San Francisco Railway Company
St. Louis, Missouri

TERM EXPIRES 1978

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Tucson, Arizona

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Tulsa, Oklahoma

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Planter
Ohlendorf Farms
Osceola, Arkansas

TERM EXPIRES 1979

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Partner, Deacy & Deacy
Kansas City, Missouri

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Cook Industries, Inc. *
Memphis, Tennessee

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Trustee
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New York, N. Y.

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Chairman and President
General American Life Insurance Company
St. Louis, Missouri

ELLIOT H. STEIN ^{1,2}
President
Scherck, Stein & Franc, Inc.
St. Louis, Missouri
(member firm N. Y. Stock Exchange)

¹ Member of the Executive Committee

² Member of the Finance and Compensation Committee

³ Member of the Audit Committee

* Merchants & exporters of agricultural commodities, agricultural chemical distributors, specialty hardwood floor mfrs., pest control services, insurance agency-brokerage business.

† Holding company (banking, loans, investments, leasing, mortgages)

‡ Holding company (production and sale of cane sugar, road & construction materials, lime, poultry feed supplement, wholesale hardware, industrial & construction machinery)

St. Louis-San Francisco Railway Company
906 Olive Street
St. Louis, Missouri 63101

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