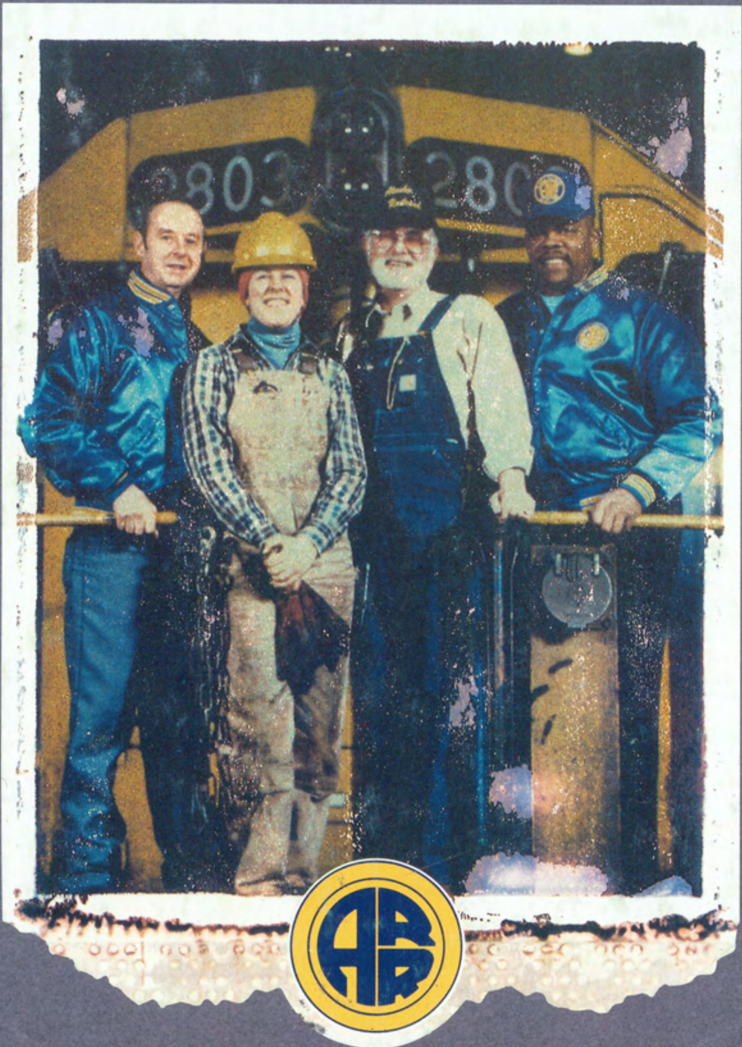
Alaska Railroad Corporation



1991 Annual Report

On Our Cover

The strength of the Alaska Railroad is its people—Alaskans who believe hard work and a common goal have created a model of quality, safety, service and pride

President's Message
1991 Alaska Railroad Annual Report

Terrific things happened at the Alaska Railroad Corporation during 1991.

We made great strides in our continuing effort to improve customer service, we further united our employees in working as a team and we took major steps to broaden our revenue base through real estate development.

As a result, the Alaska Railroad continues to be an exciting place for our employees to work, a quality service for our customers and a diverse transportation and real estate business for the state.

During 1991, our employees in groups or individually discovered new ways to demonstrate to our customers that what we offer is more than a good price for moving freight and passengers. We offer service.

Of course, service has been a watchword for the Railroad since its inception in 1914. However, to compete in today's marketplace, every company must examine the level of service it offers, evaluate whether customers' expectations are being met and determine whether customer benefits can evolve. Frequently price is not at the top of the list for customer needs but, rather, specialized services that make doing business easier for the customer.

Throughout 1991, we asked employees to look at ways they could improve the quality of our services. Can we improve our on-time performance? Can we provide more frequent service? Can we provide more economical means of transportation?

We examined our company's role in the economic development of the state. Can we foster the development of new businesses or make it possible for other businesses to expand? Can we provide a stimulus for new jobs? Can we participate in increasing revenue for sister industries, such as tourism?

In all cases, the answer is yes.

The result of business soul-searching has touched many areas of our company. Employees gained new pride in their jobs and a greater awareness of the role they play in serving our customers. Our customers have welcomed the attention to quality and in some cases have increased their business with us. Some former customers also have resumed relations with us because of our commitment to their needs. Finally, developers and planners have become increasingly aware of the role the Railroad's real estate can have in spurring growth in communities as new businesses start up, such as the new Comfort Inn Hotel in Anchorage.

A positive, can-do attitude has been a hallmark of the Alaska Railroad for years and that is what Alaskans can expect in the future.

Robert S. Hatfield, Jr.
President and Chief Executive Officer

Mission Statement

The mission of the Alaska Railroad Corporation and its employees is to provide quality transportation and real estate services.

Attention to detail is a real attribute for Don Blommer and the other railroad car inspectors, who check each and every rail car before they leave the yard.

The Alaska Railroad Corporation is a full-service transportation and real estate company, offering complete freight and passenger services, and land leasing and development.

During 1991, the corporation earned $68.4 million in revenue, 2 percent below the $69.8 million earned in 1990. The revenue picture was a reflection of the Alaska economy, which remained flat for most of 1991, with little growth in most of the freight commodities hauled by the railroad. Exceptions were a slight increase in the movement of petroleum products refined and marketed in state and a significant decrease in local construction projects from 1990 levels.

Expenses totalled $64 million, including $1.8 million accrued for EPA fines for alleged violations of the Resource Conservation and Recovery Act in relation to storing hazardous wastes at the Anchorage rail yard. No estimate of the ultimate liability can be made until all facts underlying these fines are gathered and negotiations are conducted with the EPA. Without the EPA accrual, 1991 expenses were a marked improvement over the $65.3 million spent in 1990 that also included a one-time expense of $6 million for clean up of a derailment and fuel spill at Dunbar.

Net income for 1991 totalled $4.4 million compared to $4.5 in 1990.

Freight operations earned $51.9 million, a decrease of nearly 3 percent from the previous year, and accounted for the largest share—76 percent—of the Alaska Railroad's 1991 revenue. Revenue carloads totalled 69,780 for 1991 compared to 80,827 the previous year. The Alaska Railroad hauled 5.1 million tons of freight during the year versus 5.9 million in 1990. Revenue ton miles totalled 1 billion for 1991 compared to 1.1 billion last year.

Year-round passenger services earned nearly $8.2 million or about 12 percent of revenue. Tourism throughout the state improved slightly and the Alaska Railroad experienced an 8 percent increase in ridership, hauling 471,217 passengers.

New Comfort Inn At Ship Creek.

Real estate income suffered a slight decline from 1990. Real estate values throughout the state have been slow to recover after the steep decline in property values experienced in 1986. Real estate leases and permits contributed $3.9 million or approximately 6 percent of the Alaska Railroad's 1991 revenue, compared to $4 million in 1990. Despite the slow recovery of real estate values statewide, the Alaska Railroad expects to see significant increases in its real estate income as a result of long-range plans that got underway in 1991 for development of the Ship Creek area in downtown Anchorage.

Reimbursable construction and maintenance projects, wharfage, surplus equipment sales, earned interest, dockage and switching fees contributed the remaining 6 percent of 1991 revenue.

Although owned by the state, the Alaska Railroad receives no state subsidies. Each year, the railroad combines earnings from operations, depreciation and some borrowed money to pay for capital programs to maintain or upgrade the roadbed, physical plant and equipment. During 1991, capital projects totalled $10.1 million, bringing the total capital investment to $86.7 million since state ownership in 1985. That is an average of $12 million per year on capital improvements.

Track programs included surfacing 245 miles of track, relaying 27,000 feet of rail, installing 55,000 cubic yards of new ballast and 5,000 cross ties. Other major projects included replacement of the cathodic protection system on the Seward dock, completion of the line change near Denali Park, installation of additional train defect detectors and continual upgrades of the light vehicle fleet.

Year	Revenue (in Millions)	Expenses (in Millions)	Income (Loss) (in Millions)	Capitol Investments (in Millions)
91	68,371	63,929	4,442	10.1
90	69,879	65,339	4,540	9.9
89	61,876	58,899	2,977	16.9
88	59,053	53,247	5,806	7.9
87	53,703	50,686	3,017	5

PETROLEUM • Alaska petroleum products are the railroad's primary source of freight revenue. These products made up more than 35 percent of total freight revenue for the railroad, totalling nearly $19 million in 1991.

Trains move heating oil, aviation and diesel fuels, lubricants and other petroleum products from a refinery at North Pole, delivering to the Anchorage and Fairbanks international airports, the ports of Anchorage, Whittier and Seward, and to mining areas in the Interior.

Bulk transfer of products by rail between Fairbanks and Anchorage encourages competitive prices for commercial and military aviation fuel, home-heating fuel, automotive gasoline and other refined petroleum products.

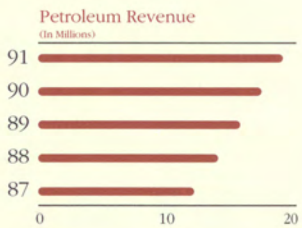
The Alaska Railroad transported more than 20,000 revenue carloads of petroleum products in 1991, weighing 1.5 million tons. Petroleum products increased almost 15 percent from 1990. This growth is a reflection of the increased capacity of the North Pole refinery and increased competition among local gasoline retailers, manifested by both major in-state producers aggressively pursuing combination gasoline and quick-stop-shopping outlets in the Anchorage and Fairbanks areas.

Above: Petroleum products are a major revenue source. Below: Coal is shipped to local and export markets.

COAL • Alaska coal has been a staple of the railroad's freight revenue since Alaska's first coal shipment by rail in 1917. Today, coal shipments continue to provide a regular source of income. The coal is low in sulfur and produces clean energy with little pollution.

In 1991, the railroad continued to move coal from the Usibelli Coal Mine at Healy bound for Korea and for Alaska power generating facilities near Fairbanks. Plans are also on the drawing board for the Japanese firm, Idemitsu Kosan, to re-open a mine near Sutton. However, a legal battle over the state's mental health trust lands, which include the mine site, has stalled the project.

Coal shipments in 1991 totalled 17,000 revenue carloads, or about 25 percent of the freight carloads hauled for the year. The railroad hauled nearly 1.5 million tons of coal during the year, generating nearly $12 million in revenue. This is a decline of about 6 percent in both revenue and tonnage compared to the previous year, reflecting the



Steel fabricator and boilermaker Anne Billman and her coworkers make sure every seam is tight and every weld secure on locomotives and other rail equipment.

Warehouse men and women like Robert "Smitty" Smith ensure the trains keep rolling, by making sure materials and supplies our employees need are delivered efficiently.

extremely competitive world coal market.

Coal is the major international export commodity shipped by the railroad. About half of the coal shipped on the railroad in 1991 was exported to Korea. The railroad hauled the coal in 65-car unit trains, across some of the steepest and most difficult terrain on the Alaska Railroad's route through the Chugach Mountains. From Seward, ships carry the coal to Korea for use by Korea Electric Power Company.

The railroad hauls half of the annual coal tonnage to Fairbanks for use by power generation plants at military installations, the University of Alaska Fairbanks and the Fairbanks Municipal Utility System.

GRAVEL · For nearly 20 years, the Alaska Railroad has been the primary transport mode for gravel and gravel products from the Matanuska-Susitna Valley for use by local road and building construction industries. Despite a modest boom in the construction industry during 1991, gravel shipments decreased 35 percent from 1990, which was the best year for gravel shipments on the Alaska Railroad in five years. In 1991, gravel producers shipped nearly 2 million tons of gravel and gravel products to distribution centers in Anchorage, compared to nearly 3 million tons shipped the previous year. The dramatic drop in gravel requirements is attributable to several major, one-time construction projects built in 1990. In addition, the opening of a new source of gravel near the center of Anchorage introduced significant new competitive forces to the market.

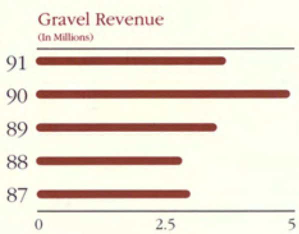
Interline shipments enter Alaska through the Port of Whittier.

Gravel generated revenue of more than $3 million in 1991, accounting for 21,000 carloads, which represents 30 percent of the railroad's total 1991 revenue carloads.

INTERLINE · Interline, made up of rail cars entering and leaving the state through the Port of Whittier, represented more than $10 million in revenue for 1991 or about 20 percent of total freight revenue. Interline revenue decreased 6 percent from 1990, reflecting the flattened economy of 1991 and changes in the marketplace.

Essentially the transfer of rail cars from other railroads, interline involves transport by rail to or from connecting barge services operated by Alaska Hydro-Train operating out of Seattle and Canadian National Aqua-Train through Prince Rupert, British Columbia. The Alaska Railroad hauled 5,300 revenue carloads in interline service in 1991, totalling approximately 320,000 tons.

Products shipped to Alaska in rail cars came from railroads such as



Burlington Northern, Southern Pacific, Union Pacific and Canadian National. Shipments included heavy equipment and machinery, liquefied natural gas, animal feed, automobiles, scrap metal, building supplies, newsprint, foodstuffs and staple goods.

Oil field supplies also are moved by interline, including drag-reducing agent, drilling and anti-freezing compounds, and chemicals essential to Alaska's North Slope oil industry. Domestic pipe enters Alaska by interline connections from the Lower 48 through the Port of Whittier. The railroad hauls the pipe to Fairbanks where it is moved by truck to Prudhoe Bay.

Above: Intermodel freight arrives by barge at the ports of Whittier and Anchorage.
Below: Logs are hauled from interior Alaska.

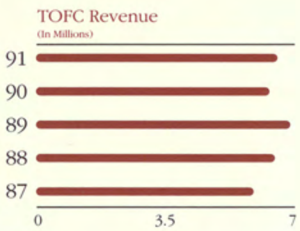
TOFC • Intermodal freight comprises trailers or containers moved by several modes of transportation, such as trains, trucks and barges. Alaska Railroad receives intermodal traffic from barge lines in Whittier and the Port of Anchorage. Also known as TOFC (trailers on flat cars) and COFC (containers on flat cars), these shipments are both inter- and intra-state movements.

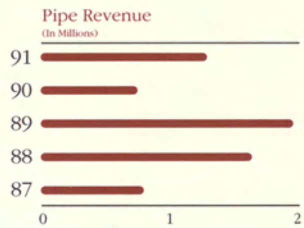
During 1991, revenue from this component of the freight operation reached nearly $6 million, a 3 percent increase over 1990. The railroad hauled approximately 200,000 tons or 6,000 revenue rail car loads of TOFC and COFC freight between Anchorage and Fairbanks in 1991, representing nearly 15 percent of total freight revenue.

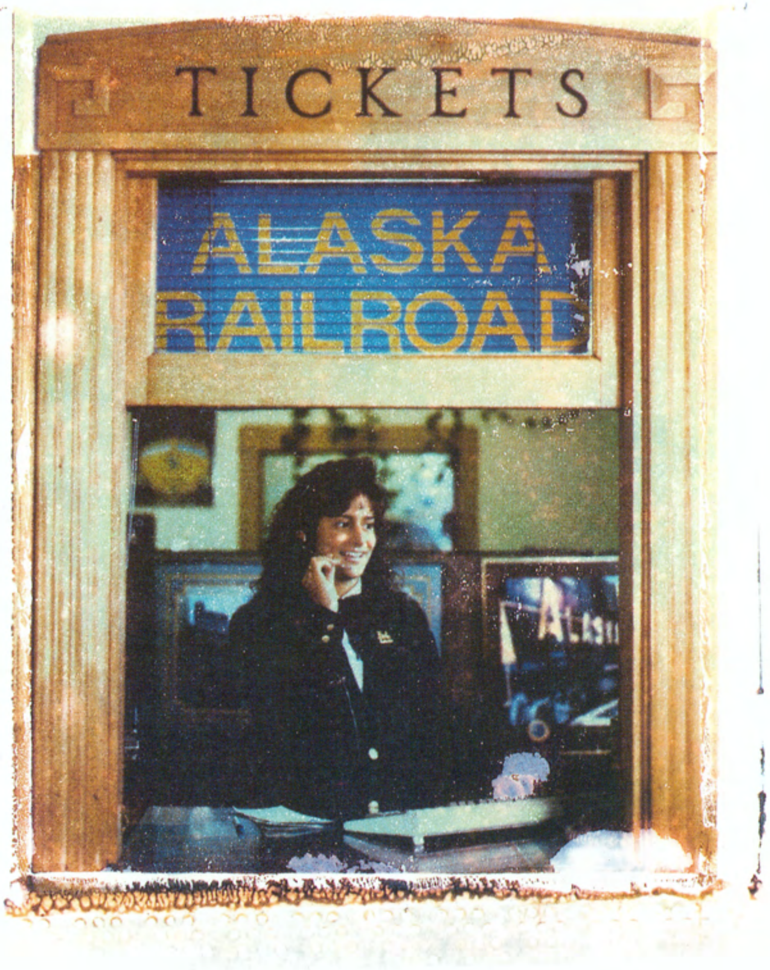
Some North Slope industrial goods and supplies are transported by intermodal service such as chemicals and pipe.

Intermodal freight brings efficiencies in the transportation of foods, beverages, building materials, furniture, appliances, electronic equipment, automotive supplies and other basic, high-use consumer goods to Alaskans well beyond the railbelt area through water, air and highway connections.

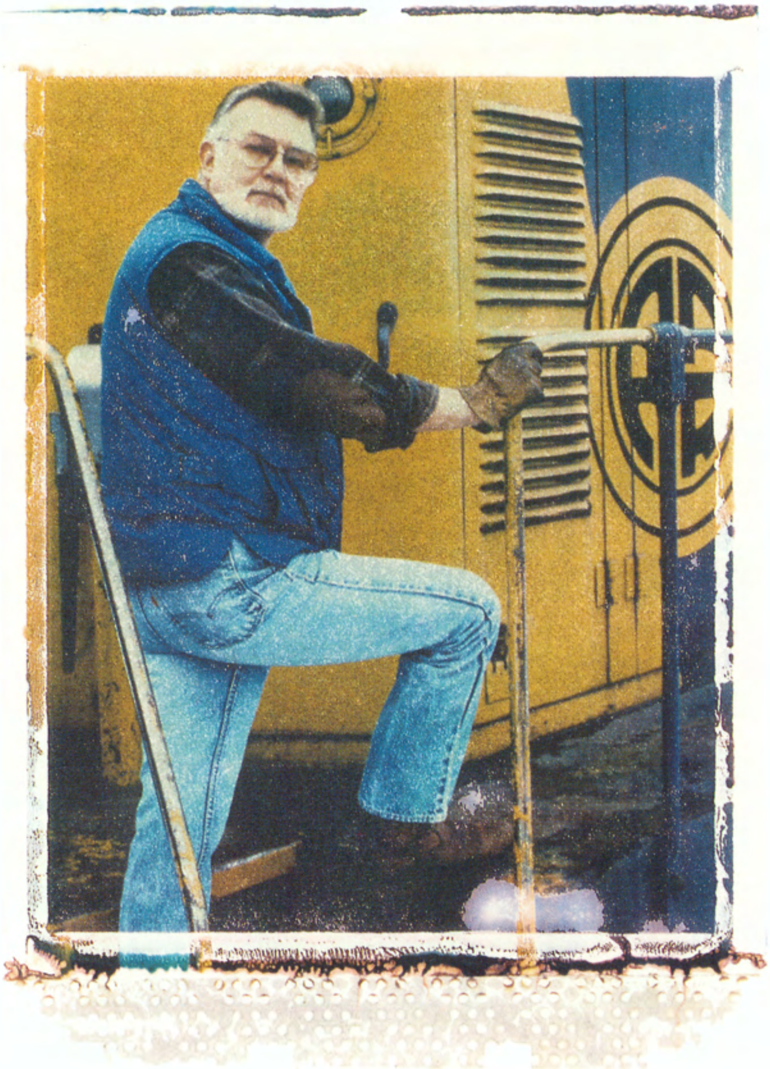
Pipe • The oil industry in Alaska depends heavily on the Alaska Railroad for efficient, cost-effective delivery of pipe and other iron and steel products bound for the North Slope oil fields. In the early days of the oil industry's initial push to develop the Prudhoe Bay fields, the railroad was a primary method of moving pipe and equipment north to pickup points for final delivery. Today, the







On the Alaska Railroad's front lines, ticket and reservations agents like Mia Avila know the secret to our success is service and attention to our customers' needs.



Skilled Locomotive Engineers like Ted Brummond are essential to the safe, timely delivery of our passengers and freight.

railroad is an important link to the ongoing maintenance of oil field equipment and the trans-Alaska pipeline.

A total of 500 revenue carloads representing about 3,000 tons of pipe and related equipment moved by rail from Seward to Fairbanks. Some limited exploration in 1991 caused the 61 percent increase over the dramatically low tonnage moved in 1990. Pipe revenue totalled more than $1 million for 1991, compared to about $650,000 the previous year.

Foreign pipe arrives by ship at the Port of Seward where it is loaded onto rail cars destined for Fairbanks. From Fairbanks, trucks haul the pipe to the North Slope.

MISCELLANEOUS • The railroad earned more than $800,000 in revenue from miscellaneous freight shipments, including timber bound for Japanese markets, cement and other building commodities. Total tonnage for this category exceeded 33,000 tons in 1991 representing 700 revenue carloads.

Revenue from miscellaneous freight dropped 45 percent from 1990, a result in part of the declining building market. More than half of the 1991 miscellaneous freight tonnage was attributable to export log shipments from interior Alaska.

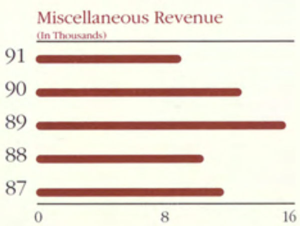
Miscellaneous freight service operates primarily between Anchorage and Fairbanks with deliveries to and from smaller communities such as Nenana, Wasilla and Palmer. The service benefits residents of the state. The railroad is a vital transportation source for efficiently bringing in necessary goods and supplies. It connects with the Yutana Barge Line in interior Alaska to ship goods to communities along the Yukon River. The railroad also helps connect Alaska products to major seaports for shipment to national and international markets.

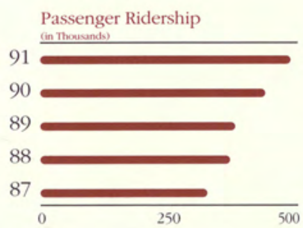
PASSENGER SERVICE • The Alaska Railroad enjoys a high degree of public awareness, primarily due to a very visible passenger service operation. Riders include hundreds of thousands of tourists from the Lower 48, as well as thousands of Alaskans using the railroad for both recreational travel and basic transportation.

Tourism continued to provide most of the $8.1 million generated through passenger service during 1991, an increase of 17 percent. Ridership in 1991 of 471,217 represented an 8 percent increase over the previous year.

A wide array of equipment and services support the passenger service operation, including passenger coaches and dining cars bought two years ago. Various routes and services include the Whittier Shuttle, the Seward excursion aboard rail diesel cars, the summer

Passenger services include a variety of routes through Alaska.





Denali Express between Anchorage and Fairbanks with a stop at Denali National Park and Preserve, and the unique, year-round flag-stop service to rural areas.

The Alaska Railroad also provides service to commercial tour companies, pulling Westours' McKinley Explorer and Princess Tours' Midnight Sun dome cars between Anchorage and Fairbanks with an intermediate stop at Denali, location of North America's tallest peak, Mt. McKinley.

Real Estate • In 1990 the Alaska Railroad began to actively market use of its 36,000 acres of real estate and 1991 marked the beginning of a committed effort to capitalize on real estate opportunities.

Statewide real estate suffered a decline in the late 1980s from which the railroad is gradually recovering; leases issued in recent years are slowly improving in value. Real estate leases and permits resulted in nearly $4 million in revenue in 1991 and have averaged approximately $4.4 million annually for the past five years. Long-term leases to commercial concerns and for industrial uses are expected to provide an ever-increasing source of revenue.

Of all the property owned by the railroad, a 120-acre parcel near the port of Anchorage attracted the most attention in 1991 as the corporation sought a developer to oversee a major land improvement project. The development will focus on the enormous tourism potential of downtown Anchorage, drawing visitors to a waterfront center featuring shops, restaurants, hotels, museums and attractions.

The right of way has been leased for a fiber optic cable, contributing to real estate income.

Construction began in 1991 on a hotel and a new railroad headquarters, launching the first phase of the Ship Creek project. The Alaska Railroad Corporation is a 40-percent partner in the 100-room Comfort Inn. The new headquarters is being built by Railroad Townsite Company, an Alaska owned and operated company. Both buildings were completed in mid-1992.

Railroad land includes 14,000 acres of right of way and 8,000 acres used in operations. Another 12,000 acres are in rural areas with little commercial use or value at this time. The remaining 2,300 acres are leased for industrial, commercial and residential uses. Railbelt communities benefit from the use of railroad land for trails, greenbelts and parks. If leased at fair market value, these leases are estimated to produce as much as $3 million in annual income but are leased at nominal rates as a contribution to local communities.

It takes a skilled Carman Leader Write-Up Man like Melvin Hills to direct the efforts of rail car maintenance crews, changing 1,800-pound train wheels in just 30 minutes.

In many ways, the Alaska Railroad has become all things to Alaskans: transportation, employment and tourism. Indeed, to many, the corporation represents economic prosperity and promise for Alaska. Now we're adding real estate as a new dimension to our business profile.

1991 Alaska Railroad Corporation Board of Directors

Our charter to operate as a business, without state subsidy, is one of the primary reasons we are successful. Since the railroad's purchase by the state, we have seen many changes in Alaska. We have been through a major recession and survived. Freight markets have fluctuated, causing shifts in the products we haul and the schedules we maintain. Tourism has grown and with it the demand for railroad services from passengers, vendors and others who benefit from our operation. The real estate component of our business has gone through similar up-and-down cycles, requiring the company to be flexible and responsive to our customers as well as internally as we work to expand our revenue base.

Our responsibility to be self-sustaining, a mandate from the very beginning, is at the heart of our success. Running a railroad as a business, continuing to do the things that are profitable and eliminating those things that aren't, should forever be the model for the company's future operation.

We have a part to play in economic growth and development of Alaska, but always with the corporation's operational and fiscal soundness in mind.

Projects such as the Ship Creek development, begun in 1991, make economic sense for the railroad as well as the community involved. Should the Alaska Railroad decide to become a participant in other development projects, it will do so with the intent of realizing revenue, making the corporation even stronger as well as benefiting the community in which the development takes place. Operating from that perspective, the benefit to the community and Alaska is twofold. Such developments will attract new businesses and interest to the area and ensure the state's investment remains a viable, financially sound entity providing employment and opportunity to Alaskans for many generations to come.

Anything less would be shortchanging Alaskans who depend on us to manage one of the state's investment success stories — the Alaska Railroad.

Loren H. Lounsbury

LOREN H. LOUNSBURY
Chairman, Board of Directors

Officers

ROBERT S. HATFIELD, JR.
President and Chief Executive Officer

ROBERT E. COX
Vice President, Operations

RICHARD J. KNAPP
Vice President, Marketing

MARVIN J. YETTER
Vice President, Finance

PHYLLIS C. JOHNSON
General Counsel

JAMES B. BLASINGAME
Director, Administration

RONALD W. STOCKER
Director, Personnel

VIVIAN M. HAMILTON
Manager, Corporate Communications

PATRICK C. SHAKE
Superintendent, Transportation

JOHN E. KINCAID
Chief Mechanical Officer

THOMAS E. BROOKS
Chief Engineer

Board Of Directors

SEATED:

FRANK G. TURPIN
Commissioner of Transportation and Public Facilities

LEFT TO RIGHT:

MICHAEL W. OLSON
Conductor, Alaska Railroad Corporation

ROBERT S. HATFIELD, JR.
President and Chief Executive Officer, Alaska Railroad Corporation

LOREN H. LOUNSBURY
Chairman, Board of Directors
Chairman, International Management Group

FRANK X. CHAPADOS
Vice Chairman, Board of Directors
Retired, Business Owner

DALE R. LINDSEY
President, Harbor Enterprises, Inc.

GLENN A. OLDS
Commissioner of Commerce and Economic Development

Management's Statement
1991 Alaska Railroad Annual Report

Management is responsible for the preparation, integrity and objectivity of the Corporation's financial statements and other financial information appearing in this report. The financial statements are prepared in conformity with generally accepted accounting principles and, in the judgment of management, present fairly and consistently the Corporation's financial position and the results of operations.

Throughout 1991, the Corporation maintained a system of internal accounting controls and procedures which are continually reviewed and supported by written policies and guidelines and supplemented by audit review. The system provides reasonable assurance that assets are safeguarded against loss from unauthorized use and that the books and records reflect the transactions of the Corporation and are reliable for the preparation of financial statements. The concept of reasonable assurance recognizes that the cost of a system of internal accounting control should not exceed the benefits derived and also recognizes that the evaluation of these factors necessarily requires estimates and judgments by management.

During 1991, two major projects in support of the Ship Creek redevelopment got underway and opened in the summer of 1992. Both projects, the Alaska Railroad's new headquarters office building and a 100-room Comfort Inn Hotel, provide major anchors for the master developer chosen to coordinate the efforts in the area.

The Board of Directors pursues its oversight responsibilities for the financial statements and corporate conduct through its Audit Committee. It meets regularly with members of management and independent accountants to discuss the adequacy of the Alaska Railroad's internal controls and financial statements.

The Corporation's financial statements are audited by Ernst & Young, independent certified public accountants, who are appointed by the Board of Directors. Their audit is conducted in accordance with generally accepted auditing standards which include a study and evaluation of the Corporation's system of internal accounting controls. The report of the independent accountants is below.

February 25, 1992

Marvin J. Yetter

MARVIN J. YETTER
Vice President, Finance

Independent Auditor's Report

We have audited the accompanying balance sheets of Alaska Railroad Corporation as of December 31, 1991 and 1990, and the related statements of income, equity, and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Alaska Railroad Corporation as of December 31, 1991 and 1990, and the results of its operations and its cash flows for the years then ended in conformity with generally accepted accounting principles.

Ernst & Young

February 14, 1992

Balance Sheets
Alaska Railroad Corporation December 31, 1991 and 1990

	1991	(IN THOUSANDS)	1990
ASSETS			
Current assets:			
Cash and cash equivalents *(Note 3)*	**$ 5,934**		$ 2,346
Accounts receivable, less allowance for bad debts of **$327,000 in 1991** and $368,000 in 1990	**8,281**		9,964
Operating materials and supplies	**3,240**		2,968
Other current assets	**323**		188
Total current assets	**17,778**		15,466
Property and equipment *(Note 4)*:			
Road	**45,609**		41,443
Equipment	**35,943**		34,681
Road materials and supplies	**1,837**		2,651
Construction in progress	**256**		2,269
	83,645		81,044
Less accumulated depreciation and amortization	**(24,572)**		(20,056)
	59,073		60,988
Land *(Note 5)*	**13,850**		13,850
	72,923		74,838
Other assets:			
Restricted lease proceeds *(Note 4)*	**220**		220
Restricted assets—Wishbone Hill *(Note 6)*	**9,798**		9,000
	10,018		9,220
Total assets	**$100,719**		$ 99,524
LIABILITIES AND EQUITY			
Current liabilities:			
Accounts payable	**$ 2,655**		$ 3,274
Payroll liabilities	**4,712**		4,126
Notes payable *(Note 7)*	**6,000**		3,000
Other accrued liabilities	**541**		1,417
Deferred revenues	**298**		578
Environmental claims *(Note 14)*	**1,800**		–
Current portion of capital lease obligations *(Note 4)*	**1,368**		2,733
Current portion of long-term debt *(Note 7)*	**1,677**		1,401
Total current liabilities	**19,051**		16,529
Deferred revenue, Wishbone Hill *(Note 6)*	**9,798**		9,000
Long-term debt, less current portion *(Note 7)*	**8,188**		11,216
Capital lease obligations, less current portion *(Note 4)*	**2,578**		6,117
Equity:			
Contributed capital	**34,174**		34,174
Retained earnings	**26,930**		22,488
Total equity	**61,104**		56,662
Total liabilities and equity	**$100,719**		$ 99,524

See accompanying notes.

Statements of Income

Alaska Railroad Corporation Years Ended December 31, 1991 and 1990

	1991	(IN THOUSANDS)	1990
Operating revenue:			
Freight *(Note 9)*	**$ 51,935**		$ 53,312
Passenger	**8,174**		6,974
Other	**3,919**		5,446
	64,028		65,732
Operating expense:			
Transportation	**16,460**		16,187
Ways and structures	**12,525**		12,357
Equipment	**14,395**		13,928
General and administrative	**13,735**		15,993
Depreciation and amortization	**4,697**		4,490
	61,812		62,955
Income from operations	**2,216**		2,777
Other income (expense):			
Real estate, less direct expenses of **$388,000 in 1991** and $318,000 in 1990	**3,591**		3,718
Interest income	**364**		111
Interest expense	**(1,729)**		(2,066)
	2,226		1,763
Net income	**$ 4,442**		$ 4,540

Statements of Equity

	Contributed Capital	(IN THOUSANDS)	Retained Earnings
Balance at December 31, 1989	**$ 34,174**		$ 17,948
Net income for the year ended December 31, 1990	–		4,540
Balance at December 31, 1990	**34,174**		22,488
Net income for the year ended December 31, 1991	–		4,442
Balance at December 31, 1991	**$ 34,174**		$ 26,930

See accompanying notes.

Statements of Cash Flows

Alaska Railroad Corporation Years Ended December 31, 1991 and 1990

	1991	(IN THOUSANDS) 1990
OPERATING ACTIVITIES		
Net income	**$ 4,442**	$ 4,540
Adjustments to reconcile net income to net cash provided		
by operating activities:		
Depreciation and amortization	**4,697**	4,490
Accrual of environmental claims	**1,800**	–
Loss on disposal of equipment	**168**	–
Changes in operating assets and liabilities:		
Decrease (increase) in accounts receivable	**1,683**	(3,136)
Increase in operating materials and supplies	**(272)**	(434)
Decrease (increase) in other current assets	**(135)**	121
Increase (decrease) in accounts payable and payroll liabilities	**(33)**	291
Increase (decrease) in other accrued liabilities	**(876)**	(672)
Increase (decrease) in deferred revenues	**(280)**	268
Net cash provided by operating activities	**11,194**	5,468
INVESTING ACTIVITIES		
Increase in road and equipment	**(5,777)**	(5,018)
(Increase) decrease in road materials and supplies	**814**	(360)
(Increase) decrease in construction in progress	**2,013**	(1,053)
Investment of proceeds for Wishbone Hill	**(798)**	(9,000)
Net cash used in investing activities	**(3,748)**	(15,431)
FINANCING ACTIVITIES		
Proceeds from short-term debt	**6,000**	4,000
Payments on short-term debt	**(3,000)**	(4,400)
Proceeds from long-term debt	**–**	6,633
Payments on long-term debt	**(2,752)**	(1,083)
Payments on capital lease obligations	**(4,904)**	(2,655)
Proceeds for Wishbone Hill	**798**	9,000
Net cash provided (used) by financing activities	**(3,858)**	11,495
Increase in cash and cash equivalents	**3,588**	1,532
Cash and cash equivalents at beginning of year	**2,346**	814
Cash and cash equivalents at end of year	**$ 5,934**	$ 2,346

See accompanying notes.

1. Organization and Operations

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

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

2. Significant Accounting Policies

Materials and Supplies Inventory

Operating materials and supplies are carried at the lower of cost (average cost) or market. Road materials and supplies include rail, ties, ballast, and other track materials, and because these items are generally capitalized when placed into service, they are included in property and equipment at cost.

Property and Equipment

Property and equipment are stated at cost. Depreciation and amortization are computed on a straight-line basis over the estimated useful lives of the related assets. Preacquisition depreciable property has been depreciated on a straight-line basis over its estimated original remaining life of five years.

Capitalized Interest

The ARRC capitalizes interest costs as part of the cost of constructing major facilities and equipment. Interest costs of $84,000 and $212,000 were capitalized in 1991 and 1990, respectively.

Income Taxes

As a public corporation, the ARRC is exempt from federal and state income taxes.

3. Cash and Cash Equivalents

For purposes of the statements of cash flows, cash and cash equivalents include time deposits, certificates of deposit, and repurchase agreements with original maturities of three months or less. Temporary investments are carried at cost which approximates market value.

Cash and cash equivalents are summarized at December 31, 1991 as follows:

	Carrying Amount	Bank Statement Balance
	(in thousands)	
Checking accounts and repurchase agreements	**$ 3,566**	$ 4,859
U.S. Government obligations	**500**	500
Time certificates of deposit	**1,868**	1,868
Total cash and temporary investments	**$ 5,934**	$ 7,227
Collateralized by U.S. Government obligations	**$ 4,694**	$ 4,694
Insured by FDIC	**300**	300
Uninsured and uncollateralized	**940**	2,233
Total cash and temporary investments	**$ 5,934**	$ 7,227

U.S. Government obligations, which are carried at cost, had a market value of $528,000 at December 31, 1991.

4. Leases

The ARRC leases certain locomotives, freight cars, computer equipment, and other property under capital leases. Future minimum lease payments for capital leases as of December 31, 1991 are summarized as follows (in thousands):

Year ending December 31,	1992	$ 1,626
	1993	1,776
	1994	871
	1995	85
	1996	43
Total minimum lease payments		4,401
Less interest		455
Present value of net minimum lease payments (including $1,368 classified as current)		$ 3,946

During 1991, the ARRC acquired no additional equipment under capital lease agreements. The cost of equipment held under capital leases aggregated $10,034,000 and $20,032,000 at December 31, 1991 and 1990, respectively. Capital leases on assets with a cost of $9,998,000 and accumulated amortization of $4,167,000 were paid off during 1991. The related accumulated amortization was $3,663,000 and $6,634,000 at December 31, 1991 and 1990, respectively. Amortization expense is included in depreciation expense in the statement of income.

A lease for freight cars requires that $220,000 be kept on deposit with a financial institution for the term of the lease agreement.

5. Land

Certain parcels of land are leased under agreements which are cancelable upon 90 days notice by the lessee. The lease terms vary from 2 to 55 years. Annual rentals on the leases were approximately $3,979,000 in 1991 and $4,036,000 in 1990.

6. Wishbone Hill

The ARRC received $9 million from the State of Alaska in 1990 for the purchase of locomotives and coal hopper cars for the Wishbone Hill Coal project. Any remaining funds, along with interest earned on the $9 million while in the possession of the ARRC, may be used to purchase other equipment and improvements related to the project. This contribution from the State is accounted for as deferred revenue, which will be amortized over the life of the project. During 1991, the $9 million was invested in U.S. Government securities. At December 31, 1991, these investments had a carrying value of $9,798,000 at cost and a market value of $10,102,000. According to the current agreement, ARRC is to refund the $9,000,000 plus interest earned during the holding period if the Wishbone Hill Coal Project is cancelled.

7. Long-Term Debt

Long-term debt at December 31, 1991 consists of the following (in thousands):

Note payable, secured by equipment, due in semi-annual principal payments of $203,397, plus interest, beginning October 1, 1991. Interest is accrued at 9% through September 1991 and thereafter at the two year treasury note rate.	$ 5,085
Note payable, secured by various assets, requires maintenance of a net worth of at least $30 million and a debt service coverage ratio of at least 1.25, due in monthly payments of $118,659, including interest at 8%. The ARRC was in compliance with loan covenants at December 31, 1991.	4,297
Other notes payable, secured by equipment, with varying maturities through 1997 with interest from 7.82% to 8.75%.	483
	9,865
Less current portion	1,677
	$ 8,188

Long-term debt maturities are as follows (in thousands):

Year ending December 31,	1992	$ 1,677
	1993	1,734
	1994	1,814
	1995	1,097
	1996	449
	Thereafter	3,094
		$ 9,865

The ARRC has arrangements for short-term operating borrowing up to $10 million with two banks at December 31, 1991. The amount outstanding on the first line is $3 million at December 31, 1991 with interest at 75 percent of the prime rate of a major bank. The amount outstanding at December 31, 1991 on the second line was $3 million with interest at 74 percent of the prime rate of the bank. In addition, the ARRC has available a line of credit of up to $10 million for the purpose of financing self-insurance claims. There is no outstanding balance on the self-insurance line at December 31, 1991.

8. Employee Benefits

The ARRC has a defined benefit pension plan (the Plan) that covers all non-represented permanent employees who have not remained in the Civil Service Retirement System and permanent employees who are members of collective bargaining units which have bargained to become covered by this plan. Benefits under this plan are generally based upon the employee's years of service and final average compensation. The ARRC's funding policy is to contribute to the Plan for each year the amount equal to the net periodic pension cost. Contributions are made continually throughout the year.

Note 8 Employee Benefits *(con't.)*

The funded status of the pension plan at December 31, 1991 and 1990 is as follows:

	1991	1990
	(IN THOUSANDS)	
Actuarial present value of benefit obligations:		
Accumulated benefit obligation—vested	**$ (4,109)**	$ (3,200)
Accumulated benefit obligation—nonvested	**(324)**	(200)
	$ (4,433)	$ (3,400)
Projected benefit obligation for service rendered to date	**$ (6,367)**	$ (4,800)
Plan assets at fair value	**8,620**	6,460
Projected benefit obligation less than plan assets	**2,253**	1,660
Unrecognized net transition obligation	**608**	669
Unrecognized net gain	**(3,009)**	(2,329)
Pension liability	**$ (148)**	$ –

Net pension costs at December 31, 1991 and 1990 are included in the following components:

	1991	1990
	(IN THOUSANDS)	
Service cost—benefits earned during the period	**$ 255**	$ 273
Interest cost on projected benefit obligation	**475**	380
Return on plan assets	**(1,347)**	(371)
Net amortization and deferral	**780**	(100)
Net periodic pension costs	**$ 163**	$ 182

Actuarial assumptions used in 1991 and 1990 to develop net periodic pension costs were:

	1991	1990
Assumed discount rate	**8.0%**	8.0%
Assumed salary increase rate	**5.5%**	5.5%
Expected long-term rate of investment return	**8.0%**	8.0%

Assets of the ARRC's pension plan are invested in fixed income securities and common stocks.

Federal employees who transferred to the ARRC will continue participation in the Civil Service Retirement System. The contribution required of the ARRC is 7 percent of the transferred employees' base pay. Pension expense related to the Civil Service Retirement System is $980,380 and $1,001,882 for 1991 and 1990, respectively.

In December 1990 the Financial Accounting Standards Board issued Statement 106 *Employers' Accounting for Postretirement Benefits Other Than Pensions,* with required implementation by 1993. The prevalent current practice of recognizing the cost of postretirement health care benefits when the benefits are paid will be altered under the new statement. The statement requires an actuarial based accrual of the cost of the employees' benefits during the years of service prior to the vestment of the benefits.

The ARRC currently offers continued enrollment in the medical insurance program to qualified retiring employees. The costs of these benefits were $10,000 in 1991 and $9,000 in 1990. The ARRC plans to implement SFAS 106 in 1993. Based on preliminary estimates, the new rules are expected to result in an increase in 1993 net periodic postretirement benefit cost of approximately $1 million including amortization of the expected accumulated postretirement benefit obligation on a straight-line basis over 20 years.

9. Major Customers

Two ARRC customers accounted for 33 percent and 11 percent of freight revenue for the year ended December 31, 1991. In 1990, two customers accounted for 28 percent and 13 percent of freight revenue.

10. Contingencies

In 1990 an action was commenced against the ARRC and several of its present and former officers, alleging that in 1986 the ARRC made a verbal agreement with the plaintiff for very favorable wharfage and transportation rates. The complaint seeks up to $74 million in damages. The Court is currently considering the ARRC's motion to dismiss. Regardless of the Court's action, the ARRC believes that the suit is without merit, and the ARRC intends to vigorously litigate the asserted claims.

During 1991, ARRC was named as a potentially responsible party in a lawsuit brought by the U.S. Environmental Protection Agency (EPA) to recover money spent to date and to be spent in the future cleaning up a superfund site at the Anchorage Terminal Reserve. ARRC believes the contamination occurred prior to the transfer of the Railroad from the federal government to the State of Alaska and will be covered under a pretransfer pollution agreement between the federal government and the State of Alaska.

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

11. Insurance

The ARRC is self-insured to certain limits for employee health benefits, personal property and casualty damage. The ARRC is also self-insured against workers' compensation claims. The ARRC employs a full time "Risk Manager" who monitors all cases involving ARRC liability.

12. Results of 1990 Operations

Net income for the year ended December 31, 1990 includes three items from prior years that increase 1990 net income by $900,000. These items are prior years' wharfage invoiced in 1990, improved freight revenue estimates at year end, and partial reimbursement by a shipper for a prior year's chemical spill cleanup.

13. Investment in Partnership

Effective August 22, 1991, ARRC entered into a general partnership agreement to develop and operate a hotel complex in the Ship Creek area. ARRC agreed to be a 40% participant in the partnership and will account for the investment on the equity method. At December 31, 1991, no investment in the partnership had been made by ARRC. Included in accounts receivable at December 31, 1991, was approximately $500,000 ARRC loaned the partnership until the partnership's bank line-of-credit was funded. This amount has subsequently been repaid to ARRC by the partnership.

14. Subsequent Event

On February 6, 1992, the EPA fined ARRC a total of $1.8 million for alleged violations of the Resource Conservation and Recovery Act in relation to storing hazardous wastes at the Anchorage rail yard. An estimate of the ultimate liability cannot be made until all facts underlying these fines are gathered and negotiations are conducted with the EPA. The entire amount of the fines has been accrued in the 1991 financial statements.

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