



Alaska Railroad
Corporation

1993

Annual

Report

Like many other businesses around the world, the Alaska Railroad Corporation has to constantly adjust to the marketplace. As competition intensified in 1993, the railroad found itself fighting for market share.

Passenger service and real estate marked an increase in revenues, but the strength of those two segments wasn't enough to offset a decline in freight business. The railroad showed a loss for the second time since its transfer from federal ownership. The loss was \$2.67 million on revenue of \$63.9 million. A one-time charge of \$1.8 million against earnings was taken to finance restructuring in 1994.

Freight revenue was \$47 million, a decrease of 9.8 percent from the previous year. As detailed in the commodities review on the following pages, gravel, coal and pipe showed increases in revenue, while other segments registered declines.

The railroad was looking to the future when it took over rail/barge service between Whittier and the Lower 48. In March 1993, the railroad took over the service after Crowley Marine Services indicated it would discontinue the business. Start-up costs for the barge operation had a significant effect on our performance.

Tourists and local Alaskans continued to be charmed by a trip on the railroad. Revenue from passenger services increased 4 percent over 1992, reaching \$8.8 million.

Real estate revenues continued to climb following the trend of a steady recovery in real estate values since the market bottomed out in 1988. Revenue from leases and permits showed an 8.2 percent increase over 1992 to \$4.4 million.

In 1993, the railroad invested \$8.3 million in capital projects including rails, ties, ballast, locomotives and rail cars. That amount is 32 percent less than was spent in 1992. Projects included:

- 45,094 feet of new rail laid
- 8,400 new cross ties installed
- 313.71 miles of track surfaced (raised, aligned, and tamped)
- upgraded sidings at three locations

Through long- and short-term lease the railroad acquired 50 boxcars, 80 open-top hoppers, 25 bulkhead flatcars and 19 flatcars. Two switch engines were purchased to improve yard operations.

Additionally, upgrades and modifications were begun on more than 100 railcars. Retirement of 200 railcars helped reduce maintenance expenses.

As part of its search for an environmentally sound solution to eliminating vegetation on the right of way, the railroad tested a machine from the Canadian Pacific Railway that uses steam to kill weeds. Plans were made to host an international weed symposium bringing railroad experts from Europe and North America to discuss ways to solve the vegetation problem.

It was a year of transition for the Alaska Railroad Corporation. Though financial results were disappointing, several significant changes were undertaken that will provide exciting opportunities for the future.

First, as of March 1, 1993, the rail/barge operation between Seattle and Whittier came completely under our banner. Prior to March, both Crowley Marine Services and the ARRC were involved in sales, marketing, and administrative activity in support of Alaska HydroTrain. Our unilateral control of what is now called the Alaska Rail Marine Service reduces the overall cost of the operation while at the same time improving customer service and connecting rail interface. Start-up activities for this operation impacted our results.

In June of 1993 the railroad negotiated a new and more comprehensive contract with MAPCO to haul its refined petroleum products between the North Pole Refinery and the Port of Anchorage. Although a change in fuel specifications on the part of the military reduced revenues for hauling jet fuel by over \$2 million, our improved contract with MAPCO bodes well for the corporation as increased export volumes replace the reduction in jet fuel volume.

In October of 1993 the corporation re-examined its position with regard to hauling coal from Healy, Alaska, to the

Port of Seward for export to Korea. Coal shipments were halted for over a month while a new contract to provide the service was negotiated. Though this effort had a negative impact on the 1993 results, revenues for this move in 1994 should be greatly improved.

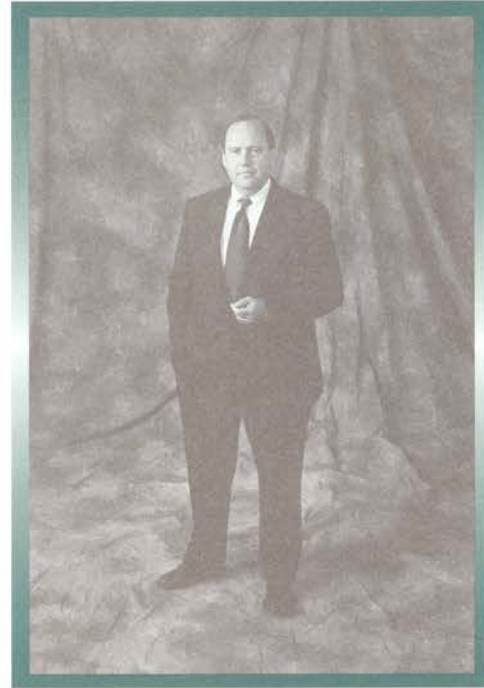
In addition, in the fourth quarter, the corporation posted a \$1.8 million charge to cover the cost of an early retirement and separation program which will be completed in the first half of 1994.

The changes mentioned above, along with efforts to improve customer service, internal communications, and quality control, coupled with significant cost-cutting measures, have resulted in a more efficient railroad.

The Alaska Railroad is determined to provide the best service at the best price operating as a self-sustaining entity in a market-based environment. With the help of our 500 professionals at the Alaska Railroad, I am confident we will succeed.



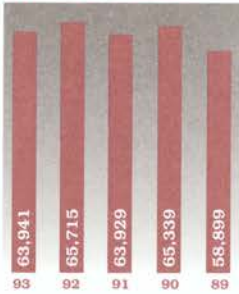
Robert S. Hatfield, Jr.
President & Chief Executive Officer



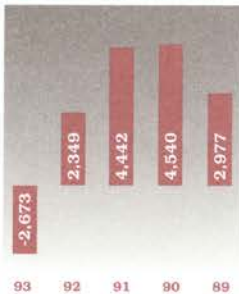
REVENUE (In Thousands)



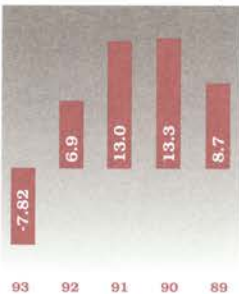
EXPENSES (In Thousands)



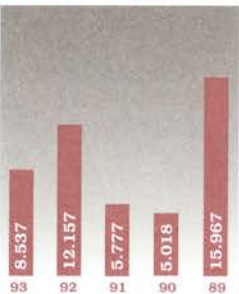
NET INCOME (In Thousands)



RETURN ON ORIGINAL INVESTMENT (Percent Return)



CAPITAL INVESTMENT (In Millions)



The Alaska Railroad Corporation plays a vital role in Alaska's transportation network. Through our freight, passenger and real estate departments, the Alaska Railroad strives to make its services convenient for customers as well as cost-effective for the corporation.

PETROLEUM

The railroad ships bulk petroleum products such as gasoline, heating oil, and aviation and diesel fuels from Fairbanks, bound for markets in and around Anchorage as well as Western Alaska. In 1993, 1.4 million tons of petroleum products were moved south in 16,429 carloads. This generated approximately \$18 million in revenue which accounts for 38 percent of total freight revenue. Results are down about 8.8 percent from 1992, primarily due to a reduction in overseas naphtha shipments by our customers.

COAL

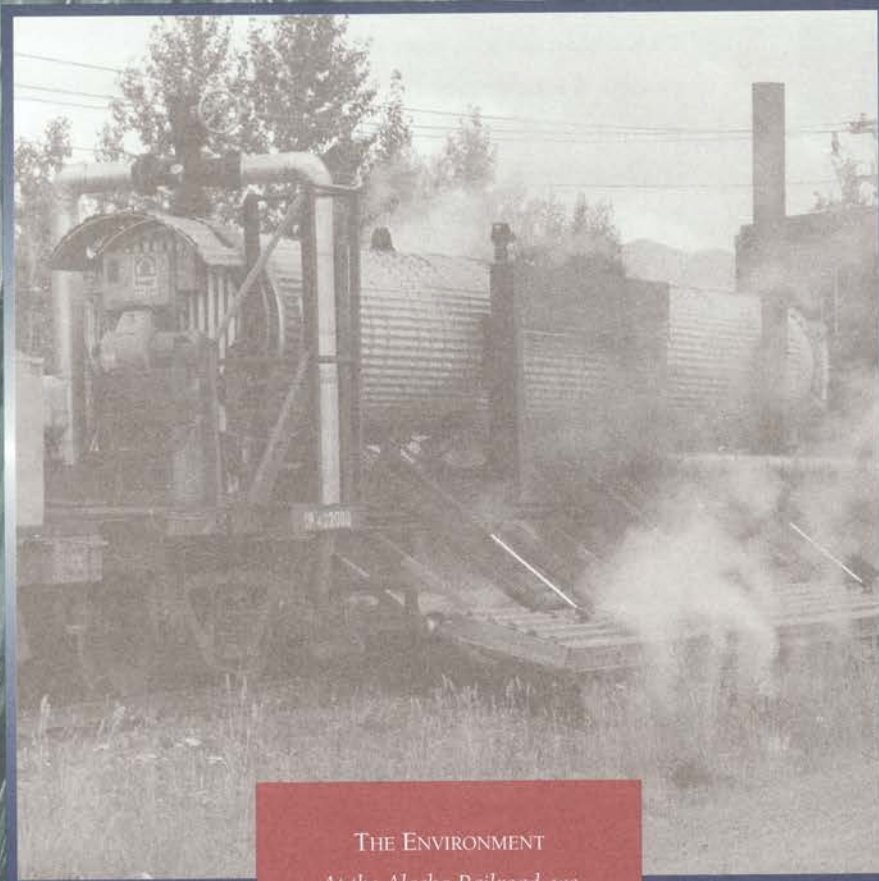
In 1993 the railroad moved nearly 1.4 million tons of coal from Usibelli Coal Mine at Healy. The business generated about \$12 million in revenue which was about equal to 1992 levels. Coal accounted for 25 percent of total freight revenue.

The coal market is composed of two approximately equal segments: domestic and export. Domestic coal involves supplying military and civilian power plants in the Fairbanks area. Export coal is purchased by Sun Eel Shipping Co. Ltd. in Healy and shipped by the railroad to Seward for export to Korean power plants. Late in 1993 the railroad and Sun Eel Shipping Co. Ltd. signed a new three-year contract.

Although export volumes have been relatively stable, lower prices for international coal have kept this business segment from meeting expectations.

GRAVEL

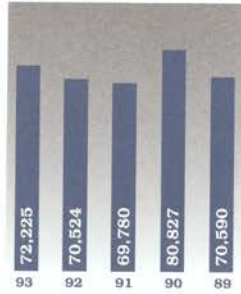
A boom in commercial construction in Anchorage, led by retail expansion, made gravel an important commodity for the railroad in 1993. Gravel represented 10 percent of the railroad's freight business. More than 2.5 million tons of gravel were shipped from the Matanuska Valley to Anchorage between April and October. That amount compared to 1.9 million tons shipped in 1992. Those shipments generated more than \$4.7 million in revenue, the highest level in the past five years.



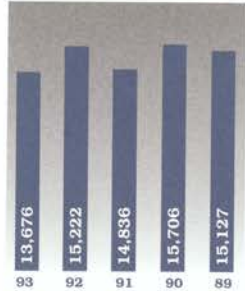
THE ENVIRONMENT

At the Alaska Railroad, we work where we live. Our entire operation revolves around sensitivity to the environment, illustrated through our research for earth-friendly vegetation control projects.

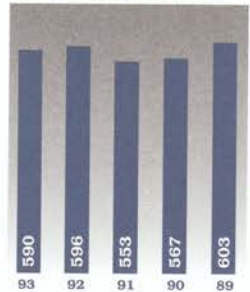
CARLOADS



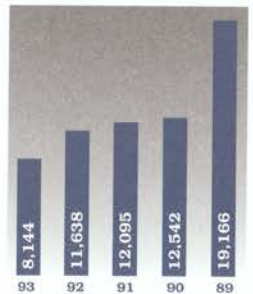
FREIGHT CAR MILES, LOADED (In Thousands)



FREIGHT TRAIN MILES (In Thousands)



INTERMODAL LOADINGS



INTERLINE

Interline traffic involves rail cars that enter and leave the state by a rail-equipped barge through the port of Whittier. Interline accounts generated \$5.4 million in 1993, more than 11 percent of freight revenues. Interline accounts for more than 11 percent of freight revenues. While tonnage and carloads were up from 1992, the start-up of Alaska Rail Marine added additional costs to the service resulting in net revenues below 1992 levels. The railroad took over the marine segment in March 1993 after Crowley Marine indicated it would discontinue the barge service between Alaska and the Lower 48.

INTERMODAL

Increased competition on intra-state movements and the removal of double-deck barge service from Seattle caused an adverse effect on the railroad's intermodal business. TOFC (trailer on flatcar) and COFC (container on flatcar) movements produced \$4.8 million in revenue, down 18 percent from 1992, but still contributing 10 percent of total freight revenues. Movements between

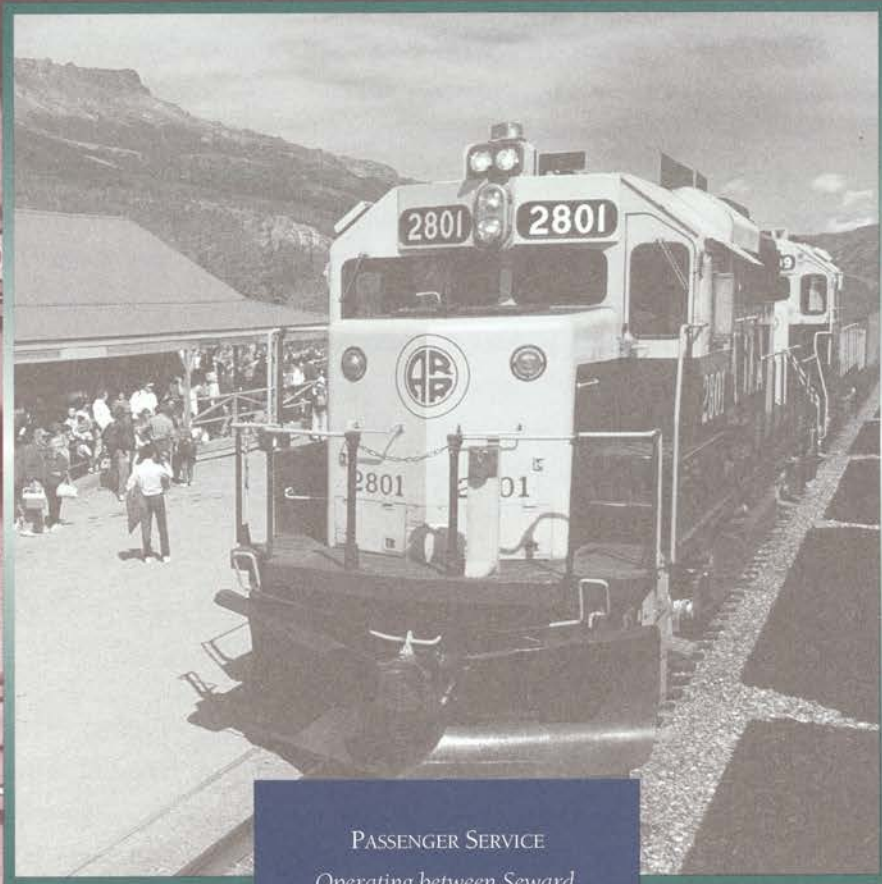
Anchorage and Fairbanks suffered as a result of soft markets in Fairbanks and extreme competitive pressures from the trucking industry.

PIPE

The transportation services of the railroad have played an important role in the oil industry since the discovery of oil at Prudhoe Bay. Pipe arrives from foreign shores by ship at the Port of Seward where it is loaded onto railcars destined for Fairbanks. From Fairbanks, trucks haul the pipe to the North Slope. Revenue from pipe shipments was up 32 percent in 1993 generating \$1.3 million compared to \$1 million in 1992.

ALL OTHER

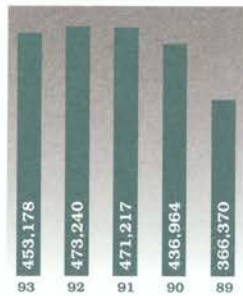
The railroad earned more than \$700,000 in revenue from miscellaneous freight shipments including cement, building materials, and timber bound for Japan. Tonnage for the year totaled 46,000, representing 850 carloads. The railroad also provides vital freight service to smaller communities along the railbelt delivering products to such places as Wasilla, Talkeetna, Nenana and Healy.



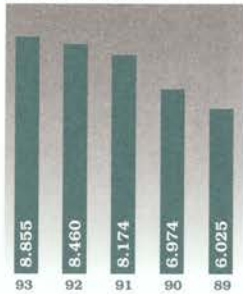
PASSENGER SERVICE

Operating between Seward, Anchorage, Denali Park and Fairbanks since 1923, North America's only full-service railroad continues a rich tradition of passenger service with more than 450,000 passengers in 1993.

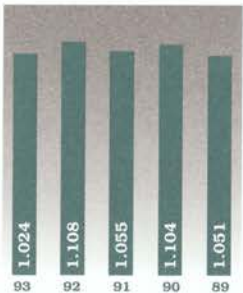
PASSENGER RIDERSHIP



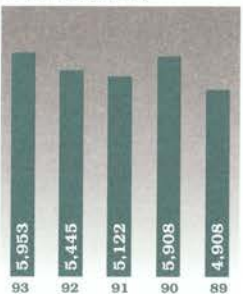
PASSENGER REVENUE (In Millions)



REVENUE TON MILES (in Millions)



REVENUE TONS (in Thousands)



PASSENGER SERVICE

Passenger Services revenue reached \$8.8 million in 1993, a gain of 5 percent over 1992. In the past five years revenues have increased \$2.8 million. Passenger ridership was 453,178 in 1993. In the past five years, passenger ridership has risen by nearly 100,000 passengers.

Passenger season runs mainly from mid-May through mid-September moving locals, tourists from the Lower 48, and an increasing number of international visitors. Winter traffic is primarily composed of the Whittier Shuttle and a local train between Anchorage and Fairbanks that runs weekly.

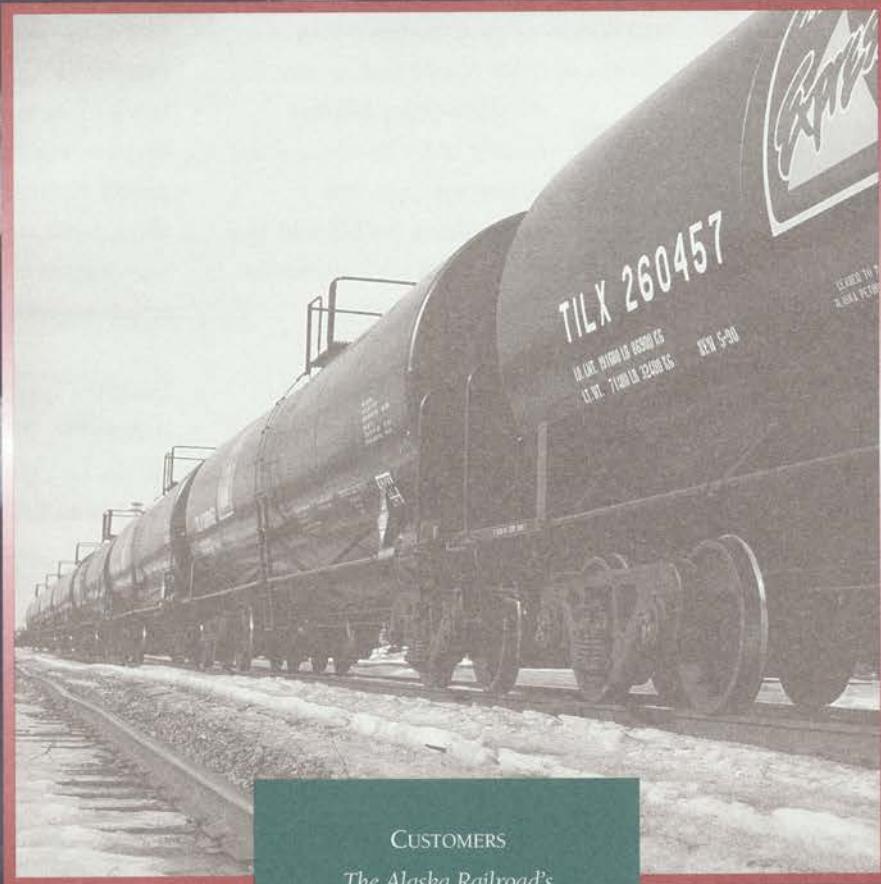
The run between Anchorage and Seward has gained steadily in popularity showing an 11 percent increase in ridership in 1993. Tourists were charmed by Resurrection Bay and the boat tours available out of Seward. The segment between Anchorage and Fairbanks recorded a 9 percent increase in ridership. Ridership was substantially down for charters primarily because of cruise ship operators shifting their port of call from Whittier to Seward, eliminating the need to transport passengers from Whittier to Anchorage.

REAL ESTATE

The railroad owns approximately 36,000 acres of real estate. Some 14,000 acres are right of way and 8,000 acres are 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. Real estate is vital to railroad operations because the revenue it generates is invested in capital projects such as rail, ballast, cross ties, locomotives and freight car programs.

The steady recovery in real estate values is reflected in the revenue derived from railroad real estate. In 1993 revenue totaled \$4.3 million with \$3.7 million from leases, and permits generating \$.6 million.

The Ship Creek Development project being developed in Anchorage by LoPatin & Company has completed the zoning process for its first phase which includes a World Trade Center and a Visitors Center. Approval was delayed for eight months because of local concern regarding height variances for some areas of the project. LoPatin & Company is now pursuing sources of financing for the project.



CUSTOMERS

The Alaska Railroad's connections are pivotal to Alaska's basic industries.

Customers throughout Alaska and the United States depend on the Alaska Railroad year-round for safe, affordable and on-time freight delivery.

Ten years ago the Alaska State Legislature passed legislation accepting the transfer of the Alaska Railroad from the federal government to the state of Alaska. That transaction marked the beginning of a success story for Alaska and its people.

Alaskans enjoy a better quality of life because of the commerce, jobs and competition the railroad has fostered throughout Alaska and North America.

The competitive business market made 1993 a challenging year for the railroad. The board of directors wrestled with many difficult issues to keep the railroad competitive and solvent. All of those decisions were made with

the fiscal and operational soundness of the railroad foremost in our minds. We have a responsibility to the people of the state to protect and enhance the value of their investment in the railroad.

The diversity of our board of directors, who are successful leaders in business, government and labor, helps keep that responsibility in perspective.

Part of our responsibility is ensuring that the railroad is self sustaining. The fact that we must be self sustaining keeps us and the employees of the Alaska Railroad in tune with the market place, business climate and the needs of our customers. It is the guideline by which we make our decisions.

From the beginnings of the Alaska Railroad in 1914 to the start of the Alaska Rail Marine Service in 1993, the Alaska Railroad has come a long way. Our vision is to continue innovation, seek new markets, find ways to better serve our passengers – to make the railroad Alaska's transportation company.

Loren H. Lounsbury
Chairman, Board Of Directors



The 1993 Alaska Railroad Board of Directors (left to right) Frank X. Chapados, Dale R. Lindsey, Loren H. Lounsbury, Michael W. Olson, Robert S. Hatfield, Jr., and Bruce A. Campbell. Not shown: Paul Fuhs

: 1993 Alaska Railroad Board of Directors :

Loren H. Lounsbury

Chairman, International Management Group

- Alaska resident since 1944
- B/S Engineering, Oregon State University
- Serves as chairman for International Management Group, director for Lounsbury & Associates, Inc., Alaska Video Postcards, and First National Bank of Anchorage, Hickel Investment Company, among others
- Professional engineer and land surveyor
- Co-chairman for the Alaska Center for the Performing Arts, director of Commonwealth North
- Chairman of 1994 Alaska Railroad Board of Directors

Robert S. Hatfield, Jr.

President and Chief Executive Officer

Alaska Railroad Corporation

- B/A in Economics, Hobart College
- Began with Southern Pacific, 1973-1990; joined ARRC in 1991
- Background in operations, marketing and management of railroads
- Board of Directors of Commonwealth North, Western Alaska Council Boy Scouts of America, Resource Development Council and on the Executive Committee of Arctic Power. Advisory Board of Enstar Natural Gas Company and the Advanced Information Services Board.

Frank X. Chapados

Retired Business Owner and ARRC Board of Directors

Vice Chair

- On ARRC Board since 1985
- Lifelong Alaskan and former legislator, played key roles in statehood, development and transportation issues
- Board member, Alaska National Bank of the North, Lynden, Inc., Fairbanks Chamber of Commerce (past president)
- Fuel and transportation business owner

Dale R. Lindsey

President & CEO/Harbor Enterprises, Inc.

- Lifelong Alaskan from Seward
- Former ARRC locomotive fireman, commercial fisherman
- Owns Harbor Enterprises, a petroleum-product marketing/distributing firm; president of Forty Niner Transportation, a maritime petroleum supplier; president of Pacesetter Marine, Inc., and Shaman Fisheries
- Serves on boards of Petro-Star Refinery, Northrim Bank
- 30 years of community service

Michael W. Olson

Conductor, Alaska Railroad Corporation

- Began with ARRC in 1971; promoted to conductor in 1975
- Exemplary service includes federal DOT Award of Valor

- History of involvement in labor issues, federal transfer and political issues
- General chairman of the United Transportation Union from 1980-1990
- Appointed to the ARRC Board of Directors in Jan. 1990

Paul Fuhs

Commissioner of the Department of Commerce and Economic Development

- Former legislative liaison to the governor
- Former mayor of Unalaska/Dutch Harbor; instrumental in area growth
- Owned/operated in-state commercial fishing, diving, construction firms

Bruce A. Campbell

Commissioner of the Alaska Department of Transportation and Public Facilities

- B/S in Civil Engineering, Union College
- Served as engineer on Alaska Road Commission in 1952
- Established Campbell and Associates in 1967, designing the standard ferry transfer bridge used by the Alaska Marine Highway System statewide
- Commissioner of Highways and technical advisor to Governor Bill Egan on the trans-Alaska pipeline
- Licensed as a Registered Professional Engineer and Registered Professional Land Surveyor in Alaska

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 judgement of management, present fairly and consistently the Corporation's financial position and the results of operations.

The Corporation has established and maintained an internal control structure which is designed to provide reasonable assurance that assets are safeguarded and that transactions are properly authorized

by management and recorded in conformance with generally accepted accounting principles. 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.

The Alaska Railroad Board of Directors pursues its oversight responsibilities for the financial statements and corporate conduct through its Audit Committee. The committee 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 KPMG Peat Marwick, 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.



John O'Meara
Vice President, Finance/Administration

**Report of Independent Auditors
: To The Board of Directors of The Alaska Railroad Corporation :**

We have audited the accompanying balance sheet of the Alaska Railroad Corporation (Corporation) as of December 31, 1993, and the related statements of income (loss), equity and cash flows for the year then ended. These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements of the Corporation as of and for the year ended December 31, 1992 were audited by other auditors whose report thereon dated February 8, 1993 had an unqualified opinion.

Except as discussed in the following paragraph, we conducted our audit 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 audit provides a reasonable basis for our opinion.

We were unable to obtain audited financial statements supporting the Corporation's investment in a partnership or its equity in earnings of that partnership as described in Note 13 to the financial statements; nor were we able to satisfy ourselves as to the carrying value

of the investment in the partnership or the equity in its earnings by other auditing procedures.

In our opinion, except for the effects of such adjustments, if any, as might have been determined to be necessary had we been able to examine evidence regarding the partnership investment and earnings, the financial statements referred to in the first paragraph above present fairly, in all material respects, the financial position of the Alaska Railroad Corporation as of December 31, 1993, and the results of its operations and its cash flows for the year then ended in conformity with generally accepted accounting principles.



April 15, 1994
Anchorage, Alaska

	December 31,	
	1993	(In Thousands) 1992
ASSETS		
Current Assets		
Cash and Cash Equivalents	\$ 1,221	\$ 1,492
Temporary Investments (Note 3)	-	543
Accounts Receivable, Net of Allowance for Doubtful Accounts of \$534,000 in 1993 and \$329,000 in 1992	12,007	9,057
Materials and Supplies	3,503	3,753
Other Current Assets	<u>377</u>	<u>560</u>
Total Current Assets	17,107	15,405
Operating Property and Equipment		
Road and Roadway Structures	59,032	52,715
Equipment	42,974	41,206
Road Materials and Supplies	3,072	1,784
Construction in Progress	532	665
Accumulated Depreciation and Amortization	<u>(35,087)</u>	<u>(29,729)</u>
	70,523	66,641
Land (Note 5)	13,850	13,850
Restricted Cash (Note 4)	-	221
Restricted Assets-Wishbone Hill (Note 8)	<u>11,481</u>	<u>10,861</u>
TOTAL ASSETS	<u>\$ 112,961</u>	<u>\$ 106,978</u>
LIABILITIES AND EQUITY		
Current Liabilities		
Notes Payable (Note 6)	\$ 2,900	\$ 3,000
Current Portion of Long-term Debt (Note 6)	5,449	4,047
Current Portion of Capital Lease Obligations (Note 4)	26	1,637
Accounts Payable and Accrued Liabilities	9,201	3,456
Payroll Liabilities	6,177	5,064
Deferred Revenues	<u>329</u>	<u>428</u>
Total Current Liabilities	24,082	17,632
Long-term Debt, Less Current Portion (Note 6)	14,584	12,947
Capital Lease Obligations, Less Current Portion (Note 4)	31	1,089
Accrued Postretirement Benefits (Note 7)	2,003	996
Deferred Revenue-Wishbone Hill (Note 8)	<u>11,481</u>	<u>10,861</u>
Total Liabilities	52,181	43,525
Equity		
Investment by the State of Alaska	34,174	34,174
Retained Earnings	<u>26,606</u>	<u>29,279</u>
Total Equity	60,780	63,453
Commitments and Contingencies (Notes 4,6,7,9,11, and 12)	-----	-----
TOTAL LIABILITIES AND EQUITY	<u>\$ 112,961</u>	<u>\$ 106,978</u>

See Accompanying Notes to Financial Statements

Years Ended December 31,
1993 (In Thousands) 1992

Operating Revenue		
Freight (Note 9)	\$47,066	\$52,208
Passenger	8,855	8,460
Other	<u>3,590</u>	<u>3,181</u>
	59,511	63,849
Operating Expense		
Transportation	20,788	21,317
Engineering	14,303	12,865
Equipment	9,839	11,756
General and Administrative	14,207	13,005
Depreciation and Amortization	<u>5,785</u>	<u>5,157</u>
	64,922	64,100
LOSS FROM OPERATIONS	(5,411)	(251)
Other Income (Expense)		
Real Estate Income, Less Direct Expenses of \$578,000 in 1993 and \$426,000 in 1992	3,799	3,616
Interest Income	53	173
Interest Expense	<u>(1,114)</u>	<u>(1,189)</u>
	2,738	2,600
NET INCOME (LOSS)	\$ <u>(2,673)</u>	\$ <u>2,349</u>

STATEMENTS OF EQUITY

	Investment by the State of Alaska	Retained Earnings	Total Equity
		(In Thousands)	
Balance at December 31, 1991	\$34,174	\$26,930	\$61,104
Net Income for the Year Ended December 31, 1992	-	<u>2,349</u>	<u>2,349</u>
Balance at December 31, 1992	34,174	29,279	63,453
Net Loss for the Year Ended December 31, 1993	-	<u>(2,673)</u>	<u>(2,673)</u>
Balance at December 31, 1993	<u>\$34,174</u>	<u>\$26,606</u>	<u>\$60,780</u>

See Accompanying Notes to Financial Statements

	Years Ended December 31	
	1993	(In Thousands) 1992
OPERATING ACTIVITIES		
Net Income (Loss)	\$(2,673)	\$ 2,349
Adjustments to Reconcile Net Income (Loss) to Net Cash Provided by Operating Activities:		
Depreciation and Amortization	5,785	5,157
Loss on Disposal of Assets	56	—
(Increase) in Accounts Receivable	(2,949)	(776)
Decrease (Increase) in Operating Material and Supplies	250	(513)
Decrease (Increase) in Other Assets	404	(238)
Increase (Decrease) in Accounts Payable and Payroll Liabilities	7,004	(288)
(Decrease) in Accrued Environmental Claims	(145)	(900)
Increase (Decrease) in Deferred Revenues	(99)	130
Increase in Accrued Postretirement Benefits	1,007	996
NET CASH PROVIDED BY OPERATING ACTIVITIES	<u>8,640</u>	<u>5,917</u>
INVESTING ACTIVITIES		
Net (Purchases of) Proceeds From Temporary Investments	543	(43)
Additions to Property and Equipment, Net of Disposal	(8,537)	(12,157)
(Increase) Decrease in Road Materials and Supplies	(1,288)	53
Net (Increase) Decrease in Construction in Progress	133	(409)
NET CASH USED IN INVESTING ACTIVITIES	<u>(9,149)</u>	<u>(12,556)</u>
FINANCING ACTIVITIES		
Proceeds From Short-Term Notes Payable	4,800	3,000
Payments On Short-Term Notes Payable	(4,900)	(6,000)
Proceeds From Long-Term Debt	12,232	10,455
Payments On Long-Term Debt	(9,194)	(3,326)
Payments On Capital Lease Obligations	(2,700)	(1,432)
NET CASH PROVIDED BY FINANCING ACTIVITIES	<u>238</u>	<u>2,697</u>
DECREASE IN CASH AND CASH EQUIVALENTS	(271)	(3,942)
Cash and Cash Equivalents at Beginning of Year	1,492	5,434
CASH AND CASH EQUIVALENTS AT END OF YEAR	<u>\$ 1,221</u>	<u>\$ 1,492</u>
INTEREST PAID	<u>\$ 1,059</u>	<u>\$ 1,246</u>

See Accompanying Notes to Financial Statements

NOTE 1--ORGANIZATION AND OPERATIONS

Congress authorized construction of the Alaska Railroad (ARR) 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 ARR 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.

The ARRC operates 525 route miles, providing both freight and passenger services. The ARRC serves the 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.

NOTE 2--SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting: The ARRC is subject to the jurisdiction of the Interstate Commerce Commission (ICC). Accordingly, the ARRC has prepared the accompanying financial statements in accordance with the ICC rules and regulations (US CFR Title 49), which are generally consistent with generally accepted accounting principles as promulgated by the Financial Accounting Standards Board.

Materials and Supplies: Materials and supplies inventories are carried at the lower of cost (average cost) or market. Road materials and supplies include rail, ties, ballast, and other track materials. These items will generally be capitalized when placed into service, and accordingly are included in operating property and equipment.

Property and Equipment: Property and equipment are stated at cost. Depreciation and amortization is computed on a straight-line basis over the estimated useful lives of the related assets of 5 to 35 years.

Land: Land is stated at cost.

Capitalized Interest: The ARRC capitalizes interest costs as part of the cost of constructing major facilities and equipment. Interest costs of \$63,000 were capitalized in both 1993 and 1992.

Income Taxes: As a public corporation, the ARRC is exempt from Federal and State income taxes.

Cash and Cash Equivalents: For purposes of the statements of cash flows, cash and cash equivalents include time deposits, money market accounts and repurchase agreements with original maturities of three months or less.

NOTE 3--TEMPORARY INVESTMENTS

U.S. Government obligations are carried at amortized cost. U.S. Government obligations had a market value of \$544,000 at December 31, 1992. The unrealized gain on investments as of December 31, 1992 was \$8,000.

NOTE 4--LEASES

ARRC leases its headquarters and certain operating equipment under operating leases. Operating lease payments totaled \$1,027,000 and \$568,000 in 1993 and 1992, respectively. The ARRC leases certain vehicles under capital leases. Future minimum lease payments as of December 31, 1993 are summarized as follows:

	<u>Capital Leases</u>	<u>Operating Leases</u>
	(in Thousands)	
Year Ending December 31, 1994	\$ 30	\$ 1,049
1995	30	1,049
1996	2	1,015
1997	-	974
1998	-	940
Thereafter	<u>-</u>	<u>5,569</u>
Total minimum lease payments	\$ 62	<u>\$10,595</u>
Less interest	<u>(5)</u>	
Present value of net minimum lease payments (including \$26,000 classified as current)	<u>\$ 57</u>	

The cost of equipment held under capital leases totaled \$103,000 and \$10,246,000 at December 31, 1993 and 1992, respectively. The related accumulated amortization was \$47,000 and \$4,390,000 at December 31, 1993 and 1992, respectively. Amortization expense is included in depreciation expense in the statements of income (loss).

A lease for freight cars required that \$221,000 be kept on deposit with a financial institution for the term of the lease agreement. This lease terminated in June, 1993, ending the restriction on these funds.

NOTE 5--LAND

A significant portion of ARRC's land is leased under agreements, certain of which are cancelable upon 90 days notice by the lessee. The lease terms vary from 2 to 55 years. Annual rental income on these leases was approximately \$4,377,000 in 1993 and \$4,042,000 in 1992.

NOTE 6--LONG-TERM DEBT AND NOTES PAYABLE

Long-term debt at December 31, 1993 and 1992 consists of the following:

	<u>1993</u>	<u>1992</u>
	(In Thousands)	
Note payable, secured by equipment, due in monthly payments of \$132,699 including interest at 4.6%, matures August, 1998. Requires ARRC to meet one debt covenant, ARRC was not in compliance but obtained a waiver from the bank.	\$ 6,675	\$ -
Note payable, secured by equipment, due in semi-annual payments of \$203,397 plus interest at the two year Treasury Note rate of 3.88%, matures April, 2004. ARRC has met all debt covenants.	4,271	4,678
Note payable, secured by various assets, due in monthly payments of \$118,882, including interest at 7.947%, matures July, 1995. Requires ARRC to meet various debt covenants, ARRC is not in compliance with one covenant. The bank has not granted a waiver, therefore the entire balance due has been classified as current.	1,958	3,165
Note payable, secured by equipment, due in monthly payments of \$82,066 including interest at 4.50%, matures October, 1998. Requires ARRC to meet one debt covenant, ARRC was not in compliance but has obtained a waiver from the bank.	4,270	-
Note payable, secured by equipment, due in quarterly payments of \$115,500 plus interest at 68% of the prime rate, matures September, 1997. ARRC has met all debt covenants.	1,387	1,849
Note payable, secured by equipment, due in monthly payments of \$33,008, including interest at 6.22%, matures May, 1997, debt agreement has no debt covenants.	1,196	1,158
Note payable, secured by equipment, due in monthly payments of \$100,000, plus interest at 69% of the prime rate, paid October, 1993.	-	5,300
Other notes payable, secured by equipment, due in annual payments ranging from \$20,965 to \$150,000 maturity dates range from May, 1994 to August, 1997. The agreements have no debt covenants.	276	844
	<u>20,033</u>	<u>16,994</u>
Less Current Portion	<u>(5,449)</u>	<u>(4,047)</u>
	<u>\$14,584</u>	<u>\$12,947</u>

Long-term debt maturities are as follows at December 31, 1993 (in Thousands):

<u>Year Ending Dec. 31</u>	<u>Amount</u>
1994	\$ 5,449
1995	3,464
1996	3,611
1997	3,016
1998	2,255
Thereafter	2,238
	<u>\$20,033</u>

ARRC has arrangements for short-term unsecured borrowing up to \$20,000,000 with two banks. Notes payable at December 31, 1993 and 1992, are summarized below:

Description of Line of Credit	<u>Line 1</u>	<u>Line 2</u>	<u>Line 3</u>
	For General Purposes	For General Purposes	For Self-Insurance Purposes Only (Note 12)
Amount Available	\$5,000,000	\$5,000,000	\$10,000,000
Outstanding at Dec. 31, 1993	\$2,900,000	-	-
Outstanding at Dec. 31, 1992	\$3,000,000	-	-
Interest Rate	74% of prime rate of a major bank	74% of prime rate of lending bank	78% of prime rate of lending bank
Covenants	ARRC is not in compliance with a covenant, which was waived.	ARRC is not in compliance with a covenant. ARRC did not receive a waiver.	ARRC is not in compliance with various covenants. ARRC received a waiver through Dec. 31, 1993.
Due Date	July 12, 1994	May 15, 1994	July 12, 1994

NOTE 7--EMPLOYEE BENEFITS

ARRC has a defined benefit pension plan (Plan) that covers all permanent represented and nonrepresented employees who are not covered by the Civil Service Retirement System. Benefits under this Plan are based upon the employee's years of service and final average compensation. The ARRC's funding policy is to contribute each year an amount equal to the net periodic pension cost. Contributions are made continuously throughout the year.

The funded status of the Plan at December 31, 1993 and 1992 is as follows:

	<u>1993</u>	<u>1992</u>
	(In Thousands)	
Actuarial present value of benefit obligations:		
Accumulated benefit obligation-vested	\$ (5,562)	\$(5,442)
Accumulated benefit obligation-nonvested	(6,802)	(1,467)
	<u>\$(12,364)</u>	<u>\$(6,909)</u>
Projected benefit obligation for service rendered to date	\$(11,074)	\$(8,497)
Plan assets at fair value	<u>13,006</u>	<u>10,771</u>
Projected benefit obligation less than Plan assets	1,932	2,274
Unrecognized prior service cost	280	298
Unrecognized net transition obligation	487	547
Unrecognized net gain	<u>(2,566)</u>	<u>(3,025)</u>
Pension prepayment	\$ <u>133</u>	\$ <u>94</u>

Actuarial assumptions used in 1993 and 1992 to measure the projected benefit obligation and the expected return on Plan assets were:

	<u>1993</u>	<u>1992</u>
Assumed discount rate	7.25%	8.00%
Assumed salary increase rate	4.75%	5.50%
Expected long-term rate of investment return	8.00%	8.00%

Net pension costs at December 31, 1993 and 1992 include the following components:

	<u>1993</u>	<u>1992</u>
	(In Thousands)	
Service cost-benefits earned during the period	\$ 249	\$ 248
Interest cost on projected benefit obligation	805	621
Return on plan assets	(1,211)	(735)
Net amortization and deferral	262	(55)
Net periodic pension costs	<u>\$ 105</u>	<u>\$ 69</u>

Actuarial assumptions used in 1993 and 1992 to measure net pension costs were:

	<u>1993</u>	<u>1992</u>
Assumed discount rate	8.00%	8.00%
Assumed salary increase rate	5.50%	5.50%
Expected long-term rate of investment return	8.00%	8.00%

Plan assets are composed of fixed income securities and common stocks.

Federal employees who transferred to the ARRC continue to participate in the Civil Service Retirement System (CSRS). ARRC is required to contribute 7% of the transferred employees' base pay. Pension expense related to CSRS was \$793,000 and \$910,000 for the years ended December 31, 1993 and 1992, respectively.

In addition to the defined benefit pension plan, ARRC sponsors a defined benefit health care plan that provides postretirement medical benefits to employees receiving retirement under the corporate retirement plan, and retired CSRS employees who do not qualify for the federal medical insurance. The plan is contributory, with retiree contributions adjusted annually, and contains other cost-sharing features such as deductibles and coinsurance. The accounting for the plan anticipates future cost-sharing changes to the written plan that are consistent with ARRC's expressed intent to increase the retiree contribution rate by the amount of that year's premium increase. ARRC's policy is to fund the cost of medical benefits in amounts determined at the discretion of management. At December 31, 1993, ARRC has not designated any assets for the funding of these benefit costs.

The following table presents the plan's obligation, at December 31, 1993 and 1992:

	<u>1993</u>	<u>1992</u>
	(In Thousands)	
Accumulated postretirement benefit obligation:		
Retirees	\$ 1,287	\$ 1,111
Fully eligible active plan participants	235	509
Other active employees	4,084	3,093
Total accumulated postretirement benefit obligation	5,606	4,713
Unrecognized transition obligation	(3,481)	(3,675)
Unrecognized net gain	38	-
Accrued postretirement benefit cost	<u>\$ 2,163</u>	<u>\$ 1,038</u>

Net periodic postretirement benefit cost includes the following components:

Service cost	\$ 624	\$ 510
Interest cost	400	348
Amortization of transition obligation over 20 years	193	193
Net periodic postretirement benefit cost	<u>\$ 1,217</u>	<u>\$ 1,051</u>

The weighted average annual assumed rate of increase in the per capita cost of covered benefits (i.e., health care cost trend rate) is 13% for 1994 and is assumed to decrease 1% per year to 5.25% in 2002 and after. The health care cost trend rate assumption has a significant effect on the amounts reported. For example, increasing the assumed health care cost trend rates by one percentage point in each year would increase the accumulated postretirement benefit obligation as of December 31, 1993 by \$159,000, and the aggregate service and interest components of net periodic postretirement benefit cost for 1993 by \$76,000. The assumed discount rate used to measure the accumulated postretirement benefit obligation was 7.25% at December 31, 1993.

NOTE 8--WISHBONE HILL

The ARRC received \$9,000,000 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 \$9,000,000 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. Since 1991, the \$9,000,000 has been invested in U.S. Government securities. At December 31, 1993 and 1992, these investments had a carrying value, including accrued interest, of \$11,481,000 and \$10,861,000, respectively, at cost and a market value of \$11,408,000 and \$10,961,000, respectively. 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 canceled.

NOTE 9--MAJOR CUSTOMERS

Two ARRC customers accounted for 38% and 12% of freight revenue for the year ended December 31, 1993. In 1992 two customers accounted for 36% and 11% of freight revenue.

NOTE 10--BUSINESS PROCESS REVIEW

ARRC has incurred a \$5.4 million loss from operations and a \$2.7 million net loss in 1993 and realized a \$4.7 million decrease in working capital. ARRC has determined that fundamental changes are needed in the way the railroad operates. Management is currently redesigning the business practices of the ARRC to enhance revenue and improve operating results sufficient to provide for maintenance of the railroad's property. Part of the redesign process is a voluntary separation and early retirement program which will be followed by an involuntary reduction in force. Management's estimate of the cost of this program is \$1.8 million, which is included in operating expenses in the accompanying financial statements in 1993.

NOTE 11--COMMITMENTS AND CONTINGENCIES

Effective March 1, 1993, ARRC entered into an agreement for rail barge services between Seattle and Alaska and related administrative responsibilities for a period of five years. The agreement provides a substantial minimum level of utilization calculated on an annual basis. The rail barge operation, which is a significant portion of ARRC's interline traffic, becomes profitable for ARRC when they maintain a barge capacity utilization of 66 2/3 percent. The accompanying financial statements reflect payments under this agreement and the prior revenue sharing agreement which are accounted for as a reduction of freight revenue.

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 that liability for contamination will be ultimately imposed on the federal government under the transfer act and a 1990 agreement between the federal government and ARRC.

On February 6, 1992, the EPA filed a complaint seeking to fine ARRC for alleged violations of the Resource Conservation and Recovery Act in relation to storing hazardous wastes at the Anchorage rail yard. A consent agreement was executed on April 14, 1994 settling the alleged violations. The settlement amount has been provided for in the accompanying financial statements.

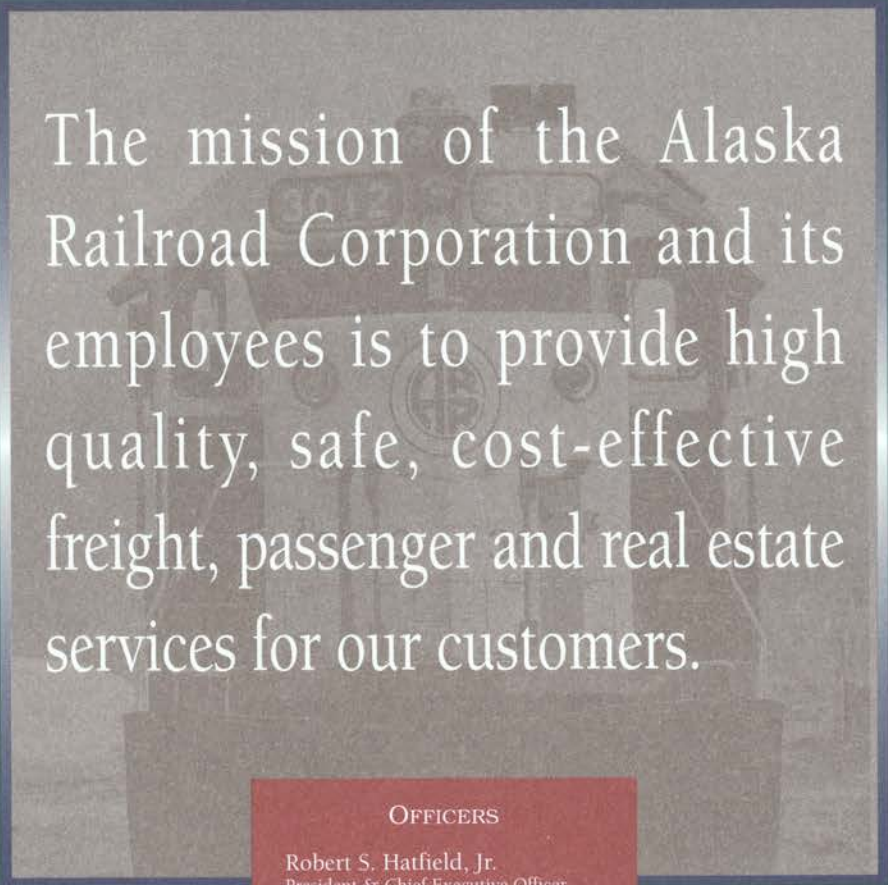
The ARRC is a defendant in various legal proceedings related to the conduct of its business. Provision has been made in the financial statements for possible losses from litigation. In the opinion of management, the outcome of the litigation will not have a material effect on the financial position of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

NOTE 12--INSURANCE

The ARRC is self-insured to certain limits for employee health benefits, personal injury, property and casualty damage claims. The ARRC maintains a line of credit available to finance significant losses, if any (Note 6). 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.

NOTE 13--INVESTMENT IN PARTNERSHIP

Effective August 22, 1992, ARRC entered into a general partnership agreement to develop and operate a hotel complex in the Ship Creek area. ARRC entered into a 35 year lease with the partnership for the land on which the hotel is located for \$1 per year. In return for this, ARRC received a 40% interest in the partnership, which is accounted for on the equity method and carried at (\$1,521) at December 31, 1993. ARRC has no cash investment in the partnership. The railroad's portion of net income of \$139,702 in 1993 is included in real estate income. The ARRC is jointly and severally liable as a partner on a deed of trust loan for \$3.9 million, secured by the hotel building which is due December 31, 1994, and on a \$500,000 line of credit which is renewable annually.



The mission of the Alaska
Railroad Corporation and its
employees is to provide high
quality, safe, cost-effective
freight, passenger and real estate
services for our customers.

OFFICERS

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

Robert E. Cox
Vice President, Operations

Richard J. Knapp
Vice President, Marketing

John O'Meara
Vice President, Finance/Administration

Phyllis C. Johnson
Vice President & General Counsel

James B. Blasingame
Vice President, Corporate Affairs

John G. Burns
Vice President, Real Estate & Facilities

Patrick C. Shake
Superintendent, Transportation

John E. Kincaid
Chief Mechanical Officer

Thomas E. Brooks
Chief Engineer



Corporate Headquarters

Alaska Railroad Corporation

P.O. Box 107500, Anchorage, AK 99510 - 7500

(907) 265-2300