Chicago Milwaukee Corporation 1972 Annual Report

CHICAGO MILWAUKEE CORPORATION 1972 ANNUAL REPORT

Financial Highlights
CHICAGO MILWAUKEE CORPORATION AND SUBSIDIARIES

	1972	1971
Operating revenues	$319,238,000	$301,569,000
Operating expenses, taxes and rents	325,269,000	298,637,000
Other income, net	13,251,000	9,612,000
Interest expense	6,376,000	9,530,000
Income before extraordinary items	559,000	2,096,000
Extraordinary items	(956,000)	(15,602,000)
Net loss	(397,000)	(13,506,000)
Net current assets	4,345,000	2,553,000

Chicago Milwaukee Corporation

516 West Jackson Boulevard,
Chicago, Illinois 60606

Board of Directors

Terms Expiring:

1973 Ray Garrett, Jr.
Patrick L. O'Malley
Worthington L. Smith

1974 Tilden Cummings
William G. Karnes
Joseph A. Maun

1975 Laurence S. Kaplan
William J. Quinn
Arthur M. Wirtz

Executive Committee

Tilden Cummings
William G. Karnes
Joseph A. Maun
William J. Quinn
Arthur M. Wirtz

Officers

William J. Quinn
Chairman of the Board,
President and Chief Executive Officer

Raymond K. Merrill
Vice President

Richard F. Kratochwill
Treasurer

James T. Taussig
Secretary

Philip W. Pillsbury resigned as a Director, effective July 14, 1972.

To The Shareholders:

1972 was basically a "start-up" and developmental year for Chicago Milwaukee Corporation, which became the holding company of Chicago, Milwaukee, St. Paul and Pacific Railroad Company ("The Milwaukee Road") and its subsidiaries on January 14, 1972. The staff and outside consultants have devoted continued intensive efforts toward the acquisition of profitable companies in keeping with the Corporation's diversification plans.

The careful screening of companies under consideration for acquisition provided a useful base for future decisions and can be expected to reward management's concern for soundness and profitability in the eventual corporate structure. However, during 1972 the only assets and operations of the Corporation were those of the Milwaukee Road and its subsidiaries.

The year 1972 saw sharply higher operating revenues reported by the railroad subsidiary, particularly in the closing months of the year.

Recent favorable developments for the railroad include access to Portland, Oregon, the opening of 11 gateways in the northern tier of states for the interchange of traffic, and the creation of a single-line route connecting Canada and Portland for through movements to and from California. These breakthroughs, which came into being in 1970 and 1971 through the implementation of Interstate Commerce Commission conditions in the merger creating the Burlington Northern, have contributed importantly to the 7.4 per cent increase in Milwaukee Road revenue ton miles in 1972 in comparison with 1971.

Other promising developments during the past year were the unprecedented demand for rail service in the movement of grain and a new concept of the Milwaukee's marketing capability. The latter, largely researched and developed in 1972, resulted in a major realignment of marketing, pricing and sales functions. The form and function of the new Milwaukee Road traffic department organization was announced to shippers and the general public in January, 1973.

Revenues improved $17.7 million in 1972, but failed to keep pace with expenses. Increases in wage rates, fringe benefits, material and supply prices, branch line and other roadway retirement charges, and special track upgrading projects added $23.2 million to railroad expenses on a comparable basis with 1971. The resulting decline in 1972 operating income was overcome to a large extent by improvement in other income and a reduction in interest expense.

The Corporation and its subsidiaries had consolidated income, before extraordinary items, of $559,000, compared to $2,096,000 for 1971. After extraordinary items, there was a net loss of $397,000 for 1972 and a net loss of $13,506,000 for 1971. The extraordinary items referred to are explained in the financial statements.

The narrative section appearing on the following pages of this report relates entirely to the Milwaukee Road and its subsidiaries. Railroad financial statements are available to Chicago Milwaukee Corporation shareholders upon request.

William J. Quinn

The railroad was fortunate in its selection of Worthington L. Smith as president and a director of the railroad and as a director of the holding company effective July 15, 1972. A native of Tacoma, former regional vice president of the Burlington Northern in Seattle and later vice president—market development for that railroad in St. Paul, Mr. Smith brings an intimate knowledge of Milwaukee Road territory and a creative understanding of the Milwaukee's rightful place in the transportation market.

Former President Curtiss E. Crippen, who reached the age of 65 in 1972 and retired at the end of the year, became vice chairman of the company at the time of Mr. Smith's election and worked closely with him in the intervening months. The Board of Directors expresses its gratitude to Mr. Crippen for service marked by exceptional ability and dedication.

Improvement in the national economy and the trend of railroad traffic which became evident late in the year, suggest that a higher level of carloadings and operating revenues will be sustained throughout much of 1973.

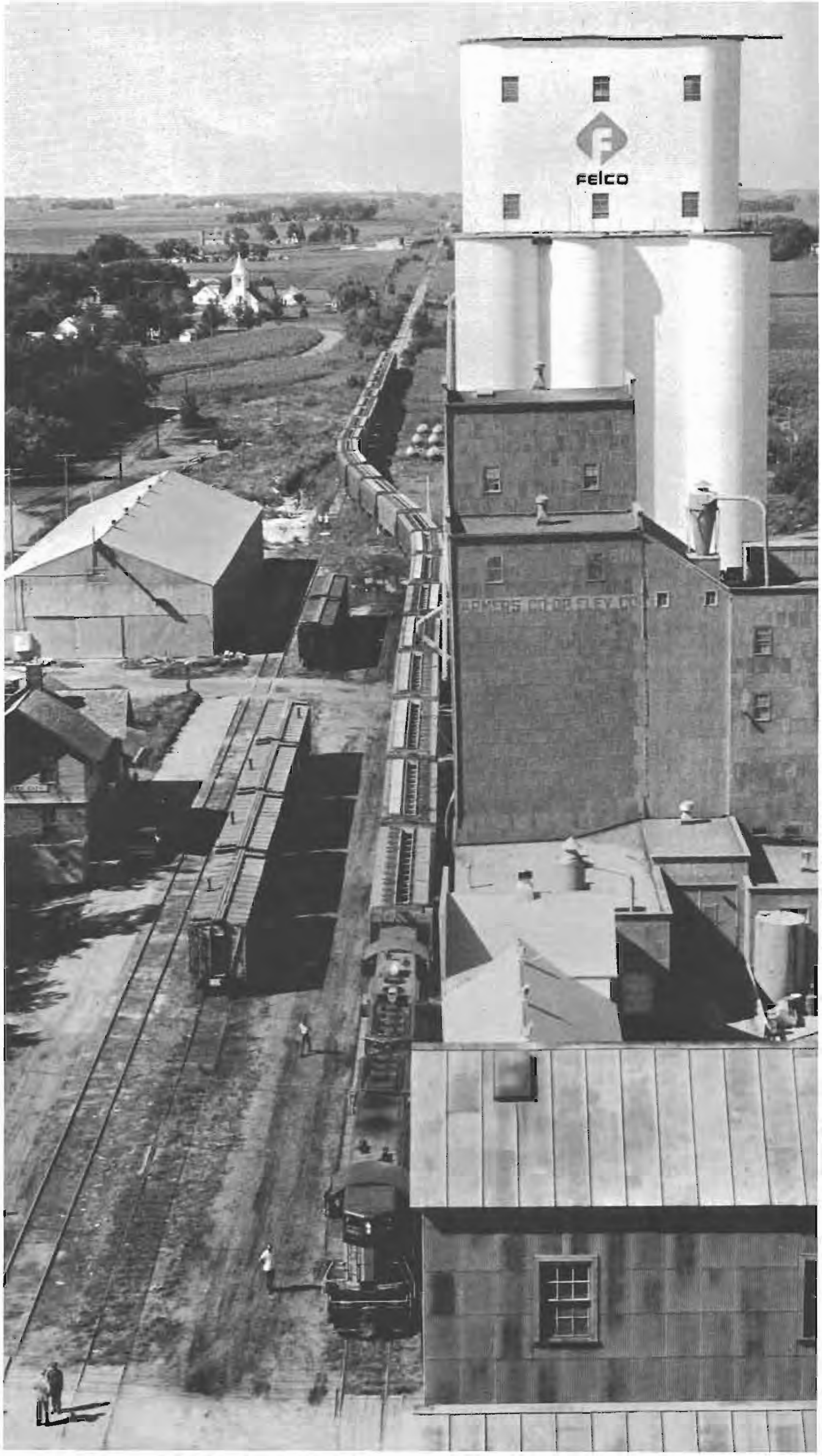
The Milwaukee Road's long-awaited service extension to Louisville, Kentucky, became an accomplished fact with the arrival of the first Milwaukee Road train in that city on March 1. It promises to be a significant breakthrough for the Milwaukee Road and Chicago Milwaukee Corporation in the development of new traffic and longer hauls on existing traffic.

Of major importance to the future of the Milwaukee Road, a petition was recently filed with the Interstate Commerce Commission requesting inclusion with Burlington Northern Inc. This is consistent with the Administrative Judge's views expressed in the Rock Island merger proceedings that the Milwaukee Road should be included in a Union Pacific, Southern Pacific, Santa Fe, or Burlington Northern System. Milwaukee Road's request for inclusion with the Union Pacific or Southern Pacific, if either acquire any portion of the Rock Island, remains on file with the Commission for possible future action, so that all reasonable options may be kept open.

William J. Quinn
Chairman of the Board

March 23, 1973

Grain traffic, an important source of revenue for the Milwaukee Road since its earliest days, increased significantly in 1972. One of the reasons was the billion-dollar sale of grain to the Soviet Union. A 50-car unit train being loaded with corn bound for Russia is shown here at Albert City, Ia.



The Milwaukee Road in 1972

The continued strengthening of the national economy, a highly active grain industry and a steady growth in traffic moving through Portland and other western gateways all were major factors in the increased volume of freight handled by the Milwaukee Road in 1972 and a substantial rise in revenues during the year. Freight revenues and total operating revenues were the highest in the history of the company.

Revenue ton miles increased again in 1972, posting a heartening 7.4 per cent gain over the previous year. The increase in revenue ton miles reflects a longer average haul due to the growth in traffic through the 11 western gateways opened in 1971, the increased capacity of modern freight cars and an increase in carloadings. For the year, carloadings were up 2.7 per cent, the first year since 1968 that there has been an increase.

Operating revenues up 9% over 1971 level

This increased traffic volume, combined with a rate surcharge in effect for much of the year and selective rate increases granted late in the year, boosted the railroad's operating revenues more than 9 per cent over the 1971 level.

The commodity showing the most significant gain during 1972 was grain. Massive grain sales to Russia negotiated during the summer, the growth of other export grain markets, strong domestic demand for feed grains, a bumper crop and high prices for grain, all combined to bring a tremendous amount of grain onto the market in the last half of 1972. Demand for transportation of this grain has been extremely heavy, and the volume of grain carried by the Milwaukee Road during 1972 was limited by the storage and loading capacities of terminal and port elevators and the availability of cars in which to move the grain. Heavy grain movement has continued into the current year, and projections indicate that present demand levels will continue at least through mid-1973 and possibly through the next harvest season.

Several other commodities which play an important part in the Milwaukee Road's freight traffic picture also registered carloading increases during 1972. Motor vehicles gained 9 per cent, reflecting expanded facilities at marshaling yards, the acquisition of additional specialized equipment and an increase in production by the motor vehicle industry. The other important commodities showing significant increases in carloadings were waste and scrap materials, up 21 per cent, lumber, up 3 per cent, and paper and allied products, up nearly 10 per cent.

Import-export traffic increases

Import-export traffic showed a gratifying increase for the year, with combined revenues increasing 34 per cent over 1971. This increase can be traced to the Milwaukee's continuing emphasis on the solicitation of this type of traffic, favorable labor conditions at Pacific Coast ports and the development of foreign grain markets. Long haul import traffic through the ports of Longview, Seattle and Tacoma, an important segment of traffic in terms of revenue, increased 17 per cent during the past year.

Piggyback and containerized traffic also increased slightly in 1972, after having leveled off somewhat in recent years.

Early in 1972 the Milwaukee Road joined with the Southern Pacific and Rock Island in the operation of unit trains carrying large volumes of coiled steel from a California steel mill to a reprocessing plant in Illinois. Two trains consisting of 50 to 55 specially-equipped gondola cars of 100-ton capacity are in continuous service, each train completing a round trip every ten days.

Another unusual new operation, begun during the past summer, involves the movement of shredded scrap metal (principally "tin" cans) from Chicago, Ill., and Milwaukee and Beloit, Wis., to Butte, Mont., for use in a process which recovers copper from a copper solution. This traffic, moving under annual volume single car rates, is handled exclusively by the Milwaukee Road, which converted 50-foot steel boxcars to "super gondolas" for the purpose.

In 1972 the Milwaukee began moving "minibridge" container shipments between Chicago on the one hand and Portland and Seattle on the other. This traffic is the result of the Milwaukee having joined with major Atlantic and Pacific steamship companies, as well as eastern railroads, in providing through intermodal rates and services between Europe or United Kingdom points via water and land to U.S. points on the Pacific Coast. The same service is available between the Far East and East Coast points in the United States via Pacific Coast ports, the Milwaukee Road and connecting eastern railroads.

Butte, Montana distribution center scheduled for 1973

In 1973 the Milwaukee will start serving an important new facility in Butte, Mont., which is being developed for the movement of imported cargo in containers directly from shipside at Pacific North Coast ports to Butte for storage or for transfer into piggyback trailers and movement to midwestern destinations. Establishing Butte as an inland port and distribution center will enable North Coast ports to extend their consolidation services inland, and will relieve the present shortages of warehouse space and land in the port areas. In addition, the loading of export cargo into containers at Butte instead of the point of export can develop a better balance of empty and loaded container movements from and to the Pacific North Coast ports.

The flooding caused by tropical storm Agnes in late June seriously damaged many industries in the East and greatly reduced the level of business activity throughout a large area. The resulting decrease in carloadings in the East and damage to several eastern railroads reduced the volume of interchange traffic handled by the Milwaukee Road and adversely affected the railroad's revenues.

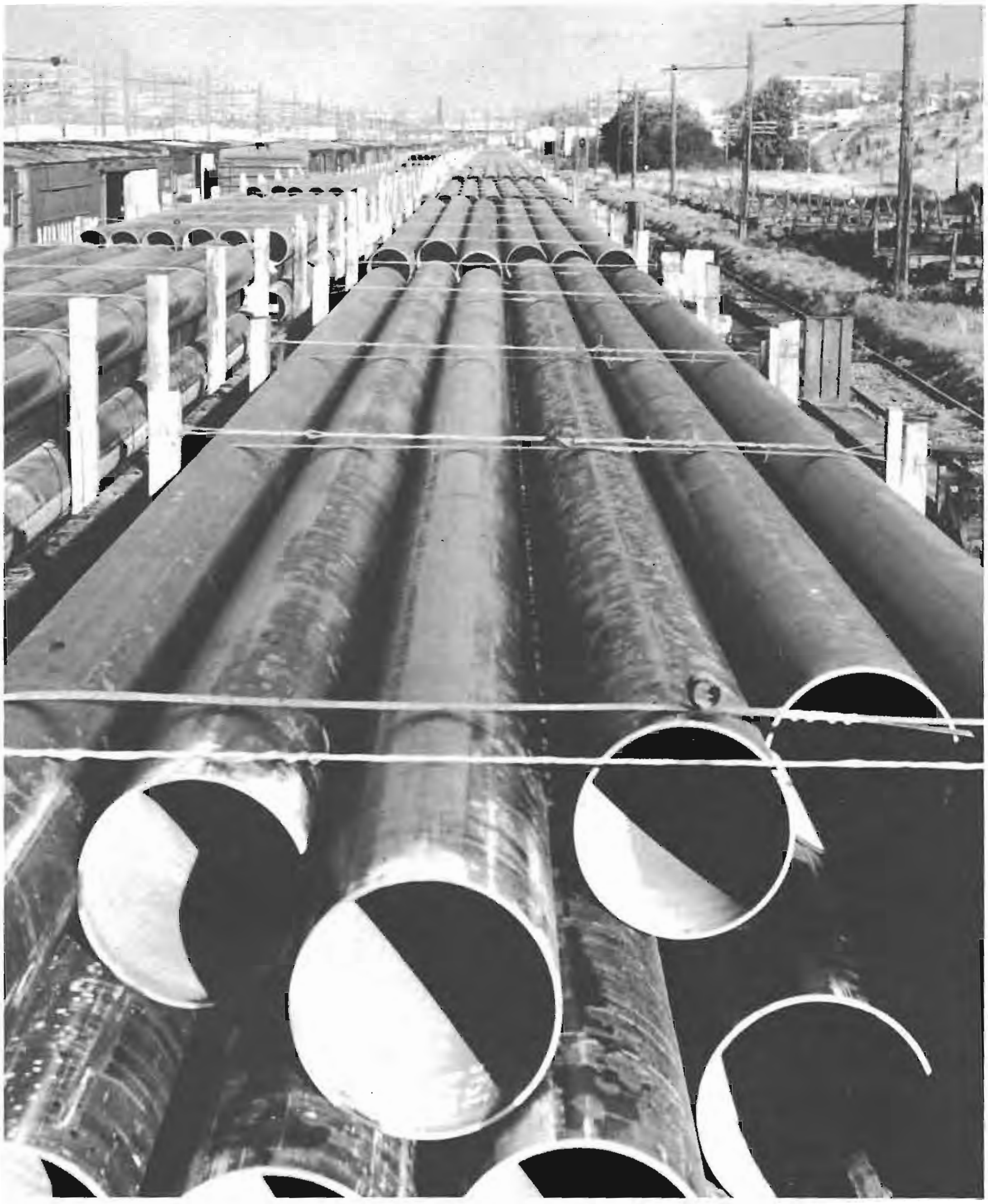
Direct interchanges established with connecting railroads

One of the most important operational improvements made during 1972 was the establishment of direct interchanges with connecting railroads in the terminal areas of Chicago, Kansas City, Mo., and Minneapolis-St. Paul. Direct interchanges, made possible by changes in work rules regarding the use of train and engine crews, speed the movement of cars through these congested terminals, provide faster service to shippers and reduce operating costs.

The Milwaukee Road, jointly with the Burlington Northern, filed two petitions with the Interstate Commerce Commission for the joint use of about 50 miles of branch lines in the State of Washington to reach commonly-served points, thereby eliminating duplicating lines and facilities. These and other similar proposals now under study will allow each company to maintain its competitive posture at the end points of the coordination, while effecting major economies on the lines involved.

As part of its continuing program to economize and to streamline operations throughout 1972, the railroad company was successful in eliminating certain of its unneeded and unprofitable branch line operations. The branch line abandonment program will continue in 1973, as little-used lines still exist and are a drain on the company's resources.

Freight rate increases in 1972 were inadequate to keep pace with the labor and material cost increases sustained during the year. An interim surcharge of 2.5 per cent on all freight became effective in February of 1972, and the



Pipe for an Alaskan natural gas pipeline is pictured in Seattle at the end of its journey from Chicago on the Milwaukee Road. From Seattle the pipe was carried to Cook Inlet, Alaska by ocean barge.

Computers are basic to the Milwaukee Road's daily operation. Used for payroll, accounting, car tracing, billing and many other purposes, computers have aided the flow of information over all parts of the railroad system.

surcharge was replaced in October by selective increases approved by the Interstate Commerce Commission. These increases, with the exceptions imposed by the Commission, failed to produce the gain in revenues anticipated by the nation's rail industry.

As a result, in late 1972, western and southern railroads agreed to seek an across-the-board two per cent emergency surcharge to help offset their still-rising labor and material costs.

Special rates were established to attract additional traffic. Most important of these were export rates applying to five or more shipments of 25- or 50-carloads of grain and soybeans moving from points in Iowa, Minnesota, Illinois, South Dakota and Wisconsin through Great Lakes or Gulf of Mexico ports. In addition, rates on shipments of five-carloads were established for corn and soybeans moving from Iowa stations to barge loading facilities in Iowa on the west side of the Mississippi and to processing facilities at those points and at Cedar Rapids, Ia. These rates have generated traffic from smaller elevators which cannot make use of the rates applying to multiple 25- and 50-carload movements.

Through the acquisition of new motive power and freight cars and the continued upgrading of its existing locomotive and freight car fleet, the Milwaukee Road substantially improved its service to shippers during 1972.

A total of 50 new diesel-electric locomotives were acquired during the year, including four 3,600 h.p. units, 41 3,000 h.p. units and five 2,300 h.p. units.

A program to upgrade 18 1,750 h.p. locomotives to 2,000 h.p. was undertaken and completed at the Milwaukee Shops, further augmenting the motive power fleet.

A vital part of day-to-day operations is the maintenance and repair of freight cars and locomotives. Pictured are wheel assemblies at the Milwaukee Shops, where much of this repair and maintenance work is performed.

Customer Service improved through fleet additions

A total of 1,295 additional freight cars, including 656 boxcars of various types, 350 covered hoppers, 284 cars for handling automobiles and automobile parts and five tank cars, were added to the railroad equipment fleet during 1972. Among these are new cars acquired under the company's 1972 budget, as well as others leased from various sources.

A total of 778 freight cars of various types went through the car rebuilding program at Milwaukee during 1972 and returned to service in like-new condition. In addition, major modifications were made on 251 cars during the year to adapt them to special service, and 48 cabooses were completely rebuilt and refurbished.

Milwaukee Road commuter patronage in the Chicago area continued upward in 1972, amounting to an increase of 5.4 per cent for the full year. Despite this increase in ridership, operating costs rose sharply and resulted in a loss for 1972.

In August, a Debt Service Grant in the amount of $538,787 from the State of Illinois Department of Transportation was made to the Milwaukee Road. This grant, with funds from the 1971 State Mass Transportation Assistance Acts and Transportation Bond Fund, was similar to grants made to other mass transit carriers in Illinois. The state program expired on December 31, 1972.

To partially offset the additional expenses, the railroad has proposed an increase in suburban fares in the Chicago area to become effective on March 1, 1973. If the increase requested is approved, it is estimated that additional revenue of $550,000 annually will be generated.

Mass Transit federal and state grants approved

The most significant single development affecting Milwaukee Road commuter service during the year was the approval of the Northwest Suburban Mass Transit District's package of federal and state grant applications. The grants, totaling $26.9 million, include $20.8 million from the Federal Urban Mass Transportation Administration approved on December 16, and $6.1 million from the State of Illinois Department of Transportation approved on November 9. Under the terms of the grants, the Milwaukee Road transferred ownership of its 62 bi-level commuter car fleet to the District late in December.

The grant funds will be used by the NWSMTD for the purpose of capital improvements in the Milwaukee Road's West Line Service and for the retirement of the outstanding obligation on the railroad's 62 bi-level commuter car fleet.

In other mass transit district developments during 1972, the North Suburban Mass Transit District, which was formed on the Milwaukee's North Line late in 1971, has filed a $7.2 million capital grant application with the federal and state agencies for capital improvements on the Milwaukee Road's North Line.

The Greater Lake County Mass Transit District, also on the North Line, was created in early 1972 by the Board of Lake County, Illinois, and concurred in the NSMTD application.

As announced in the railroad's 1971 annual report, the Milwaukee Road was among several major railroads which joined the National Railroad Passenger Corporation (Amtrak) and on May 1, 1971, began the operation of intercity passenger trains on behalf of that corporation.

At the present time, the Milwaukee Road operates seven Amtrak passenger trains daily in each direction between Chicago, Ill., and Milwaukee, Wis. Two of these trains are also operated daily in each direction between Chicago, Ill., and Minneapolis, Minn., en route Seattle, Wash. West of Minneapolis these trains are operated by Burlington Northern. Milwaukee Road on-time performance in the operation of Amtrak trains was the best of any railroad in 1972.

Two money-losing passenger trains operated five days per week between Watertown and Milwaukee, Wis., were discontinued July 31, 1972.

The past year was a period of relative quiet with respect to labor negotiations. National agreements with the United Transportation Union ended the long-standing locomotive fireman dispute and put more efficient work rules into effect for the operation of trains. These and other agreements were reached without disruptive strikes. In addition, a program looking toward better communication between local management officials and union representatives was effectively begun and will continue.

Bensenville Yard, just west of Chicago, is the largest and busiest freight classification yard on the system, with 50 classification tracks in 24-hour-a-day use. Beyond picture range at right is Piggyback Park, the largest piggyback loading, unloading and temporary storage facility on the railroad.

On the other hand, incremental wage increases provided for in agreements reached in 1972 and prior years raised the Milwaukee's 1972 labor costs $17.3 million above those for 1971, including wages, health-welfare benefits and payroll taxes.

The Milwaukee Road's large office building on Fullerton Avenue in Chicago, which for 69 years housed many of the finance and accounting department offices, was closed in 1972. All of the operations and personnel located in that building were transferred to the Chicago Union Station office building where the Railroad Company's other corporate general offices are located, making possible a number of cost savings and operational improvements.

The move also enabled the Milwaukee to consolidate the computer accounting operations previously handled at Fullerton Avenue with the separate computer operations of the transportation department's Carscope offices. The consolida-

ISBN 0-13-171556-7

The Milwaukee Road's extensive commuter operations provide almost 25,000 rides each day on two lines in the Chicago metropolitan area. This commuter train is shown along the Chicago River, just after departing Chicago's Union Station.

ISBN 0-13-171588-7

tion of equipment and operating forces added processing capacity through the joint use of personnel and equipment and also provided further protection to each of the functions through the coordinated use of the two systems.

Industrial development and real estate activity expanding

Industrial development and real estate activity during 1972 continued to expand along all parts of the Milwaukee Road system.

Sixty-four new industries were located along the railroad during the year and 17 existing firms completed expansion programs. Included in this were major expansions of all of the privately-owned industrial districts served by the Milwaukee Road in the metropolitan areas of Chicago, the Twin Cities and Seattle.

Of major importance was the donation to the city of Spokane, Wash., of railroad properties in the downtown area, including the Union Station. The properties which were used in common by the Milwaukee Road and Union Pacific were turned over to Spokane for development in connection with the city's plans for an international exposition in 1974. Authorization from the Interstate Commerce Commission to abandon the tracks on the properties and operations thereover, a prerequisite to retirement of the properties from the Railroad Accounts, was received April 4, 1972. An agreement between the Milwaukee Road and Union Pacific was executed on April 14, 1972, terminating the rights of each company with respect to the tracks. Thereafter train operations ceased and the tracks were removed, permitting the retirement of the properties and the clearing thereof for the international exposition. As part of the agreement, the Milwaukee Road obtained 6.6 acres of land adjacent to its automobile marshaling yard in East Spokane for expansion of that facility. In addition, the Milwaukee Road has been relieved of the obligation to remove certain structures and facilities and to fill certain bridges, thereby avoiding expenditures of approximately $827,000. Further, it is expected that the development of the donated property for the exposition will ultimately enhance the value of other property in the area owned by Milwaukee Road in an estimated amount of $644,000.

Milwaukee Road enters Louisville

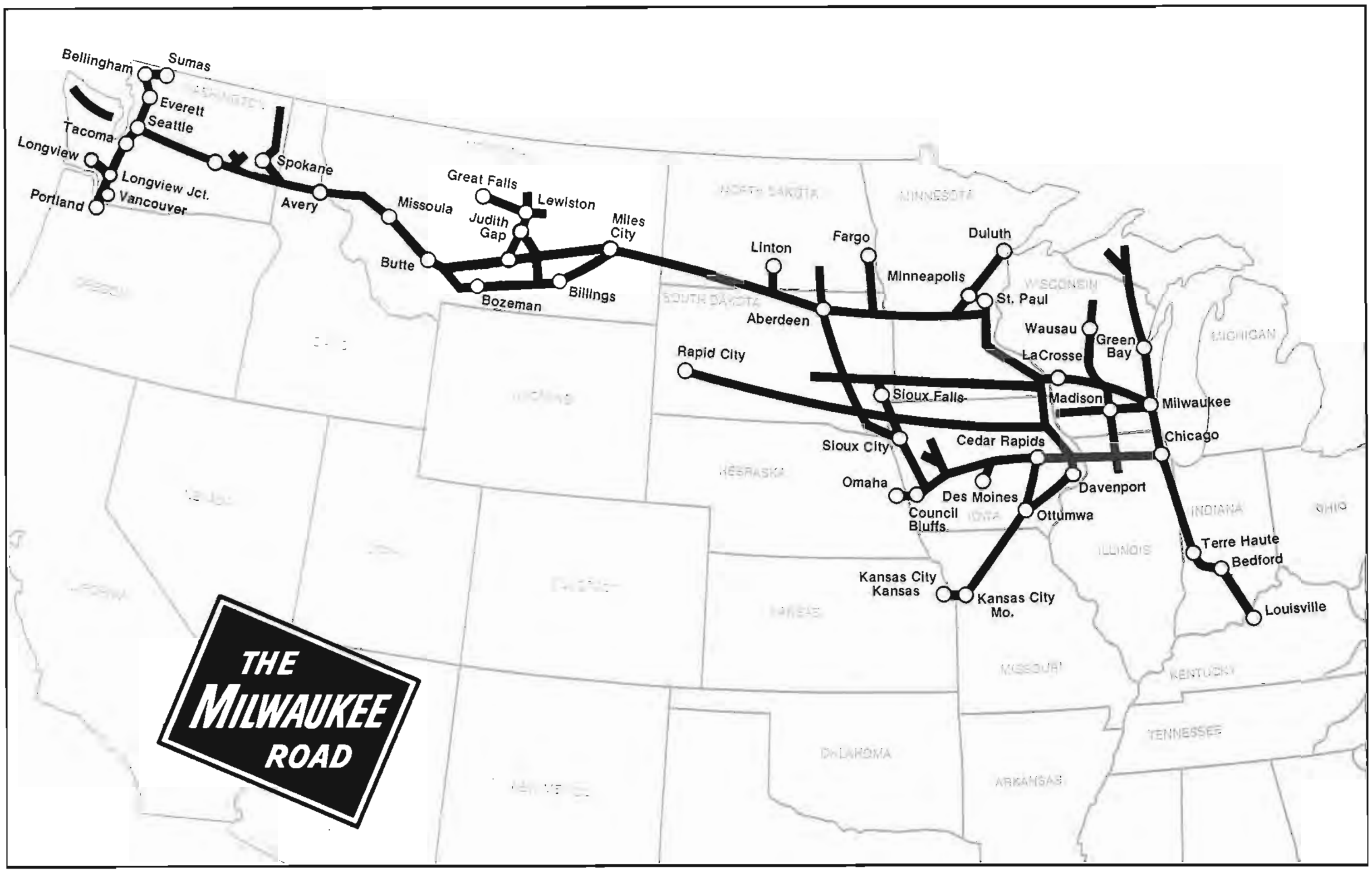
In the railroad's report to shareholders last year, it was anticipated that authorization by the Interstate Commerce Commission and commencement of operations to Louisville, Ky., from Bedford, Ind., would occur by the end of 1972. Authorization by the Commission, however, was not granted until January 10, 1973, and the Commission ordered our operations to begin not later than March 1, 1973. The Louisville and Nashville Railroad Company, over whose tracks the operations will be principally conducted, brought an action in the United States District Court at Louisville to set aside or delay compliance with the Commission's order. After hearing on February 26, 1973, the Court dissolved the temporary restraining order and denied the preliminary injunction which had been sought by the Louisville and Nashville, thereby clearing the way for the Milwaukee Road to start serving Louisville on March 1. Certain issues, including the terms under which trackage rights will be used, are being held under submission for decision by the Court at a later date.

The long awaited final report and recommended order of the hearing judge of the Interstate Commerce Commission in the Union Pacific-Rock Island merger proceeding was released on February 15, 1973. In addition to his recommendation that the Commission authorize the partition of the Rock Island among the Union Pacific, Southern Pacific, and Santa Fe, he recommends that the western railroads be consolidated into four major systems—Union Pacific, Southern Pacific, Santa Fe and Burlington Northern—and that the Milwaukee

Road be included in one of those systems, apparently leaving it to the Milwaukee to choose the system. Consideration is now being given to the next step in protecting the interests of our stockholders and customers.

In 1972, the Full Crew Law of Wisconsin requiring a five-man crew was repealed, and the Indiana Full Crew Law requiring six-man crews on freight trains of 70 cars or more was amended to permit collective bargaining agreements to supersede it. It is estimated that these laws cost the railroads serving Wisconsin and Indiana more than $35.5 million a year. As jobs are vacated by attrition or agreement, the railroads, including the Milwaukee Road, will realize sizeable savings.

During the past year, the railroad industry joined with the American Trucking Association and Water Transport Association in support of the Surface Transportation Act. This proposed legislation, as reported out by a House subcommittee, would, among other things, make available guaranteed loans in the aggregate of up to $2 billion for the acquisition, improvement and maintenance of plant, and up to $3 billion for the acquisition of railroad freight cars. It would also require the Interstate Commerce Commission to adopt procedures to expedite abandonment of non-productive track. Unfortunately, Congress adjourned before the recommended legislation could be enacted. Similar legislation, however, will doubtless be introduced in 1973, and the outlook is favorable for enactment.



One of the many industries recently located along the Milwaukee Road is a food processing plant in Northbrook, Ill. The new facility is served with four tracks capable of handling between 10 and 15 freight cars daily.

Chicago Milwaukee Corporation and Subsidiaries
Consolidated Balance Sheet

December 31, 1972 with comparative figures for 1971

	Assets	
	1972	1971
	(amounts in thousands)	
Current Assets		
Cash and temporary cash investments	$ 13,957	$ 9,917
Accounts receivable	31,040	30,491
Material and supplies	19,095	20,778
Other current assets	4,881	5,343
Total current assets	68,973	66,529
Special Funds	7,023	1,831
Investments (notes 2 and 5)		
Affiliated companies	23,111	22,043
Other companies	1,362	1,454
Total investments	24,473	23,497
Properties (note 3)		
Road	646,132	655,027
Equipment	312,635	332,166
	958,767	987,193
Less allowances for depreciation and amortization	302,423	309,352
Transportation properties	656,344	677,841
Other property, less depreciation	9,311	9,238
Total properties	665,655	687,079
Other Assets and Deferred Charges	10,526	9,310
Total assets	$776,650	$788,246

See accompanying summary of significant accounting policies and notes to consolidated financial statements.

Liabilities and Shareholders' Equity

	1972	1971
	(amounts in thousands)	
Current Liabilities		
Note payable to bank	$ 4,090	$ 4,899
Accounts payable	34,003	31,984
Payroll and vacation pay	15,159	16,695
Accrued taxes	8,157	8,063
Other current liabilities	3,219	2,335
Total current liabilities (exclusive of debt installments due within one year)	64,628	63,976
Debt Installments Due within One Year	10,086	12,141
Long-Term Debt (note 5)		
Mortgage bonds	122,866	122,950
Five per cent income debentures	55,634	55,634
Equipment obligations	42,789	52,409
Other	228	341
Total long-term debt	221,517	231,334
Deferred Federal Income Taxes	32,271	32,910
Reserves and Other Liabilities	28,379	26,550
Total liabilities	356,881	366,911
Minority Interest	18,850	18,855
Shareholders' Equity (notes 1 and 6)		
Capital stock		
$5 Prior Preferred Stock—without par value (stated value $100 per share), nonparticipating, noncumulative. Authorized 518,652 shares, issued and outstanding 477,946	47,795	47,795
Common Stock—$1.00 par value per share. Authorized 15,000,000 shares, issued and outstanding 2,451,708	2,452	2,452
	50,247	50,247
Capital in excess of par value (note 7)	318,551	319,715
Retained earnings	32,121	32,518
Total shareholders' equity	400,919	402,480
Contingent Liabilities (note 8)		
Total liabilities and shareholders' equity	$776,650	$788,246

Chicago Milwaukee Corporation and Subsidiaries
Consolidated Statement of Operations and Retained Earnings

Year ended December 31, 1972 with comparative figures for 1971

	1972	1971
	(amounts in thousands except per share figures)	
Operating Revenues		
Freight	$298,532	$279,620
Passenger, mail and express	6,033	7,777
Other	14,673	14,172
	319,238	301,569
Operating Expenses (including depreciation and retirement charges of $18,780,926 in 1972 and $19,224,261 in 1971)		
Transportation	132,036	121,454
Maintenance of way and structures	57,902	49,517
Maintenance of equipment	52,982	51,728
Traffic	8,669	8,156
General and other	21,322	19,588
	272,911	250,443
Net revenue from operations	46,327	51,126
Taxes and Rents		
Payroll and other taxes	27,177	25,406
Equipment and joint facility rents, net	25,181	22,788
	52,358	48,194
Net operating income (loss)	(6,031)	2,932
Other Income		
Equity in undistributed earnings of affiliates	326	1,126
Gain on sales of properties and timber, net	9,840	6,737
Dividends and interest	857	653
Minority interest	(35)	(87)
Miscellaneous, net	2,263	1,183
	13,251	9,612
	7,220	12,544
Fixed Interest on Long-Term Debt (including amortization of discount)	6,376	6,760
Contingent Interest on Long-Term Debt (note 9)	—	2,770
	6,376	9,530
Income before income taxes and extraordinary items	844	3,014
Deferred Federal Income Taxes (note 4)	285	918
Income before extraordinary items	559	2,096
Extraordinary Items (note 13)—after deducting deferred federal income tax benefit ($924,000 in 1972, $7,944,000 in 1971) and minority interest ($40,000 in 1972, $650,000 in 1971)	(956)	(15,602)
Net loss	(397)	(13,506)
Retained Earnings, beginning of year	32,518	46,024
Retained Earnings, end of year	$ 32,121	$ 32,518
Per Share Loss applicable to common stock		
Income before extraordinary items	$ (.75)	$ (.12)
Extraordinary items	(.39)	(6.36)
Net loss	$ (1.14)	$ (6.48)

See accompanying summary of significant accounting policies and notes to consolidated financial statements.

Chicago Milwaukee Corporation and Subsidiaries
Consolidated Statement of Changes in Financial Position

Year ended December 31, 1972 with comparative figures for 1971

	1972	1971
	(amounts in thousands)	
Source of Funds		
From operations:		
Income before extraordinary items	$ 559	$ 2,096
Add (deduct) items not requiring outlay of working capital in the current period:		
Depreciation and retirement charges	18,955	19,407
Accrual for contingent bond interest	—	2,770
Deferred federal income tax	285	918
Equity in undistributed earnings of affiliates	(326)	(1,126)
Other	806	757
Working capital provided from operations, exclusive of effect of extraordinary items	20,279	24,822
Extraordinary items (note 13)	956	15,602
Less portion not requiring outlay of working capital in the current period	1,920	17,905
Deferred federal income tax and minority interest	(964)	(8,594)
Working capital used by extraordinary items	—	6,291
Working capital provided from operations and extraordinary items	20,279	18,531
Proceeds from sales of properties and timber, less gain reflected in results of operations	806	729
Salvage	4,772	1,702
Equipment and other borrowing	7,795	2,642
Reclassification of casualty reserves from current liabilities	—	942
Drawdown of funds on deposit with mortgage trustee	3,172	2,224
Federal and state mass transit grants (note 14)	2,624	—
	$39,448	$26,770
Application of Funds		
Property additions and betterments	$ 7,469	$ 7,293
Principal payments on equipment debt	15,156	13,362
Other debt retirement	1,230	297
Investment in terminal and other companies	2,373	620
Deposit of property sale and insurance proceeds with mortgage trustee	7,680	2,387
Car-hire funds earmarked per I.C.C. order for investment in equipment	677	617
Organization expenses	1,164	223
Miscellaneous applications, net	1,907	(102)
Increase in working capital	1,792	2,073
	$39,448	$26,770
Analysis of Changes in Working Capital		
Increase (decrease) in current assets:		
Cash and temporary cash investments	$ 4,040	$ (642)
Receivables	549	3,468
Material and supplies	(1,683)	1,662
Other current assets	(462)	1,683
	2,444	6,171
Increase (decrease) in current liabilities:		
Note payable to bank	(809)	—
Accounts payable	2,019	3,004
Payroll and vacation pay	(1,536)	(702)
Accrued taxes	94	(285)
Other current liabilities	884	2,081
	652	4,098
Increase in working capital	$ 1,792	$ 2,073

See accompanying summary of significant accounting policies and notes to consolidated financial statements.

Summary of Significant Accounting Policies

Consolidation

The consolidated financial statements include the accounts of Chicago Milwaukee Corporation and all of its majority owned subsidiaries. All significant intercompany items have been eliminated in consolidation.

Investments

Investments in affiliates (companies in which 20% but not more than 50% of the voting stock is held) are reflected on the equity method of accounting.

Investments in non-affiliates are reflected principally at cost. If the value of an investment becomes permanently impaired, it is written down to estimated realizable value.

Properties

The investment in railroad properties is stated at original cost or estimated original cost, as determined by the Interstate Commerce Commission in 1917 and 1918, with subsequent additions and betterments at cost.

The Corporation follows the policy of providing for depreciation of equipment and certain road properties by charging against earnings amounts sufficient to amortize the cost of properties on a straight-line basis and according to the group plan.

In conformity with Interstate Commerce Commission accounting rules, ratable depreciation provisions are not made in the case of certain roadway properties, principally land, grading and track. Instead, these properties are accounted for by an alternative generally accepted accounting principle whereby replacement costs are recorded as operating expenses and only additions and betterments are capitalized. Gains or losses on sales and retirements of these non-depreciable properties are reflected in current operations. Normal gains or losses on sales and retirements of depreciable properties are reflected as adjustments of accumulated depreciation. Net gains or losses resulting from the sale of leaseback transactions are amortized over the term of the respective leases as an adjustment of the rental cost.

Regulatory Accounting

The railroad subsidiary is regulated by the Interstate Commerce Commission, which prescribes accounting rules and regulations for reports filed with the Commission. Such reports differ from financial reports to shareholders (which are in accordance with generally accepted accounting principles) in the following respects:

(1) Recognition is given to deferred federal income taxes in financial reports to shareholders but not in reports filed with the Commission.

(2) The account "Other elements of investment" appearing in the Railroad Company balance sheet under "Properties" is included in capital in excess of par value in reports to shareholders.

(3) The accounts of majority owned subsidiaries are consolidated in financial reports to shareholders whereas reports to the Commission reflect only the investments in such subsidiaries carried at cost.

(4) Undistributed earnings of affiliates are included in financial reports to shareholders but not in reports filed with the Commission.

Material and Supplies

Material and supplies are stated at cost which is not in excess of replacement market. Cost is determined generally by the first-in first-out method.

Loss Per Share

Loss per share of common stock is based on the average number of common shares outstanding. Preferred dividend requirements are recognized in computing loss per common share.

Federal Income Taxes

The Corporation follows the practice of providing for income taxes based on income reported for financial statement purposes rather than the amount payable under current tax laws. Deferred federal income taxes result primarily from certain differences (principally depreciation) between the methods used for financial reporting purposes and those used for income tax purposes. Previous tax benefits resulting from the excess of tax over book depreciation are deferred to future periods when book depreciation may exceed amounts claimed for tax purposes. No consideration is given to investment credit carryforwards in computing the foregoing amounts.

1. Acquisition of Railroad Subsidiary

Chicago Milwaukee Corporation was incorporated on June 24, 1971, under the laws of the State of Delaware. It became the parent of Chicago, Milwaukee, St. Paul and Pacific Railroad Company on January 14, 1972, the effective date of its offer to exchange its capital stock for outstanding shares of Railroad Company stock. The Corporation offered one share of its $5 Prior Preferred Stock and 0.75 of a share of its Common Stock for each share of Railroad Company preferred stock, and offered to exchange common stock on a share-for-share basis.

As a result of consummation of the Exchange Offer the Corporation owns 477,946 shares (92.2%) of the preferred stock of the Railroad Company and 2,092,720 shares (96.0%) of its common stock. The Corporation's initial investment has been recorded at the proportionate share of the Railroad Company's underlying net assets, determined on the basis of generally accepted accounting principles, as of December 31, 1971, and is increased or decreased to reflect earnings or losses of the Railroad Company. As of December 31, 1972 the Corporation had no significant assets other than its holdings of Railroad Company capital stock.

The consolidated statement of operations includes the Corporation's proportionate share of Railroad Company's consolidated results for the years ended December 31, 1972 and 1971 with the accounting treatment similar to pooling of interests accounting. This accounting treatment assumes that the Corporation was the parent of the Railroad Company during 1971.

2. Equity in Subsidiary Companies

Equity of the Railroad Company in the underlying net assets of its subsidiaries exceeded the cost of investments therein by $30,583,406 at December 31, 1972 and $21,041,437 at December 31, 1971. This excess consisted of $30,829,800 for 1972 ($21,287,831 for 1971) representing undistributed earnings of the subsidiaries since acquisition, included in consolidated retained earnings, less $246,394 representing excess of the cost of investments over subsidiary net assets at acquisition, included in other assets and deferred charges.

3. Properties

Roadway properties for which ratable depreciation provisions are not made amounted to approximately $403 million at December 31, 1972 and $408 million at December 31, 1971.

4. Federal Income Taxes

Federal income tax liabilities have been settled through the year 1968. Based in part upon unaudited returns and estimated tax data for 1972, the consolidated loss carryforward available as of December 31, 1972 amounted to $30,846,000, which will expire as follows: 1973—$1,848,000, 1974—$2,648,000, 1975—$10,542,000, 1976—$15,808,000.

The available investment credit carryforward as of December 31, 1972 amounted to approximately $13,539,000, which will expire as follows: 1974—$1,474,000, 1975—$1,941,000, 1976—$2,900,000, 1977—$2,861,000, 1978—$1,787,000, 1979—$2,426,000, 1980—$150,000.

5. Long-Term Debt

Long-term debt, exclusive of installments due within one year, is summarized as follows:

	Interest		Principal Amount	
	Fixed	Contingent	Dec. 31, 1972	Dec. 31, 1971
Chicago, Milwaukee, St. Paul and Pacific Railroad Company first mortgage bonds, Series A, 1994 (d)	4%	—	$ 49,235,300	$ 49,235,300
Chicago, Milwaukee, St. Paul and Pacific Railroad Company general mortgage income bonds, Series A, 2019	—	4½% (a)	24,684,700	24,684,700
Chicago, Milwaukee, St. Paul and Pacific Railroad Company general mortgage convertible income bonds, Series B, 2044 (e)	—	4½% (a)	31,127,400	31,127,400
The Bedford Belt Railway Company first mortgage bonds, 1994 (f)	2¾%	1½% (b)	178,000	178,000
The Southern Indiana Railway Co. first mortgage bonds, 1994	2¾%	1½% (b)	5,718,000	5,802,000
Chicago, Terre Haute and Southeastern Railway Company first and refunding mortgage bonds, 1994 (g)	2¾%	1½% (b)	7,184,000	7,184,000
Chicago, Terre Haute and Southeastern Railway Company income mortgage bonds, 1994	2¾%	1½% (b)	4,738,800	4,738,800
Chicago, Milwaukee, St. Paul and Pacific Railroad Company income debentures, Series A, 2055	—	5% (c)	55,634,000	55,634,000
Equipment and other obligations due 1973 to 1982	4-9%	—	43,017,259	52,750,354
Total			$221,517,459	$231,334,554

(a) Cumulative to a maximum of 13½%—See note 9.

(b) Cumulative to a maximum of 4½%—See note 9.

(c) Noncumulative.

(d) Chicago, Milwaukee, St. Paul and Pacific Railroad Company first mortgage Series B bonds in the principal amount of $5,500,000 and Series C bonds in the principal amount of $650,000 have been authenticated and pledged, along with a mortgage note receivable in the principal amount of $1,423,792, as collateral to note payable to bank.

(e) Convertible into Railroad Company common stock on the basis of one share of common stock for each $100 principal amount of bonds.

(f) Bonds held by Railroad Company include $100,000 principal amount pledged under Chicago, Terre Haute and Southeastern Railway Company first and refunding mortgage.

(g) Bonds held by Railroad Company include $1,515,000 principal amount pledged under Chicago, Milwaukee, St. Paul and Pacific Railroad Company first mortgage.

Substantially all of the properties of the Railroad Company and its investments in common stock of certain subsidiaries are pledged under the mortgages and equipment obligations. Investments in affiliated companies include $7,111,574 pledged as collateral to mortgage bonds.

Maturities of long-term debt, exclusive of contingent sinking fund requirements, during each of the years 1973-1977 inclusive are approximately $10,086,000, $8,649,000, $7,420,000, $6,495,000 and $5,402,000.

6. Stock Options and Incentives

On May 9, 1972, the stockholders approved a Long-Range Incentive Program, which became effective August 1, 1972 and consists of an Incentive Stock Compensation Plan and a Stock Option Plan. Under the Incentive Stock Compensation Plan selected employees may be awarded incentive stock compensation units which qualify them to receive cash and/or shares of the Corporation's Common Stock upon termination of employment. The amounts which accrue to grantees under the incentive plan are based upon dividends paid by the Corporation on its Common Stock and the increase in market value of the Common Stock subsequent to the time the units were awarded.

Under the Stock Option Plan key officers of the Corporation or its subsidiaries may be awarded qualified and non-qualified options to purchase an aggregate of 150,000 shares of Common Stock at prices not less than 100% of the fair market value at date of grant. Options were granted in 1972 for the purchase of 27,500 shares at $9.75 a share. At December 31, 1972, these options were outstanding but not exercisable, and 122,500 shares were available for option.

Proceeds from the sale of stock under options are credited to Common Stock at par value and the excess of the option price over par value is credited to capital in excess of par value. No charges are made against operations in respect of stock options.

7. Capital in Excess of Par Value

Capital in excess of par value arose in connection with the Exchange Offer as outlined in Note 1, and is summarized as follows:

	1972	1971
	(amounts in thousands)	
Excess of par value of Railroad Company common stock received ($100) over par value of Corporation common stock issued ($1)	$206,820	$206,820
Other elements of investment arising from 1944 reorganization of the Railroad Company	117,830	117,830
Minority interest (3.999%) in other elements of investment	(4,712)	(4,712)
Write-off of Corporation organization expenses	(1,387)	(223)
	$318,551	$319,715

8. Contingent Liabilities and Long-Term Leases

The Railroad Company is liable, jointly with other railroads, as guarantor of certain obligations of affiliated companies amounting to $64,780,400 at December 31, 1972. Also, the Railroad Company is contingently liable as guarantor along with other railroads for its proportion (2.44%), and its proportionate share of any contingent obligations not met by other railroad participants, of obligations of Trailer Train Company aggregating $32,011,244.

Under long-term noncancelable equipment leases expiring in 1973 through 1989, the Railroad Company and subsidiaries are obligated as of December 31, 1972 to pay rentals of $133,246,507, of which $14,732,556 is payable within one year.

The Railroad Company carries a service interruption policy under which it may be obligated to pay additional premiums up to a maximum of $7,814,200 for certain work stoppages.

The Railroad Company is a defendant in lawsuits brought by REA Express, Inc. against a number of railroads and other companies seeking monetary damages and other relief. In the opinion of counsel for the Railroad Company the suits are without merit.

9. Contingent Interest

Contingent interest is payable only to the extent of applicable "available net income" as defined in the debt indentures. While the amount of such available net income was negative in both 1972 and 1971, provision was made in 1971 for contingent interest on mortgage bonds as required by the respective railroad mortgage indentures calling for accumulation up to a maximum of three years' interest (see note 5). This maximum was reached in 1971 and accordingly no provision was made in 1972. Provision was not made in either 1972 or 1971 for interest on the Five Per Cent Income Debentures, which interest is contingent but not cumulative.

10. Railroad Company Dividends

Under its debt indentures the Railroad Company may pay dividends on its capital stock from available net income, as defined, only to the extent there is available net income remaining after specified requirements. The major requirements having priority under the indentures are current contingent interest, accumulated contingent interest, and available net income deficit carryforwards. As of December 31, 1972 these three requirements amounted to $5,561,000, $8,399,000 and $26,802,000, respectively.

11. Pensions

Pension expense amounted to $1,403,363 in 1972 and $1,416,639 in 1971. The actuarially computed value of vested benefits was approximately $17,539,000 as of August 1, 1971.

12. Interstate Commerce Commission Reporting

The following table summarizes the differences between results of consolidated operations as reported herein and results as reported by the Corporation's railroad subsidiary to the Interstate Commerce Commission (see "Regulatory Accounting" section of Summary of Significant Accounting Policies):

	1972	1971
	(amounts in thousands)	
Net loss per reports to the Interstate Commerce Commission	$(8,643)	$(22,196)
Undistributed earnings of consolidated subsidiaries	9,541	6,346
Equity in undistributed earnings of affiliates	326	1,126
Amtrak participation fee, included herein as a part of the 1971 extraordinary item but treated as an investment in reports to the Interstate Commerce Commission	—	(5,943)
Deferred federal income tax benefit	639	7,026
Amortization of other elements of investment	(1,976)	(428)
Chicago Milwaukee Corporation pre-tax net loss	(289)	—
Minority interest	5	563
Net loss per accompanying consolidated statement of operations	$ (397)	$(13,506)

13. Extraordinary Items

The 1972 extraordinary item is a charge from retirement during the year of certain railroad properties, principally land, located in downtown Spokane, Washington, in connection with that city's "Expo '74" riverfront development project. The 1971 extraordinary item consists of one-time costs and losses resulting from the take-over by National Railroad Passenger Corporation (Amtrak) of intercity rail passenger service effective May 1, 1971.

14. Mass Transit Capital Grants

Commuter operations of the Railroad Company are expected to benefit starting in 1973 from capital improvement grants approved in December 1972 by the Federal Urban Mass Transportation Administration and the State of Illinois. Recipient of the grants, totaling $26.9 million, is Northwest Suburban Mass Transit District formed by communities along the railroad's West (Chicago area) commuter line. Funds are to be used principally to purchase new locomotives and coaches, which the District will lease to the railroad for 25 years at an annual rental of $45,100. This lease and rental will also include the existing commuter fleet of 62 bi-level coaches, which was transferred in December 1972 to the District for a consideration of $2,624,472 as the railroad's participation in the project. The $2,624,472, which was used to retire the outstanding equipment debt on the bi-level fleet, was taken into account as a reduction of the railroad's carrying value of such equipment property on its balance sheet. The remaining book carrying value of $4,264,575 will be amortized over a period approximately equal to the lease term.

Accountants' Report

The Board of Directors
Chicago Milwaukee Corporation:

We have examined the consolidated balance sheet of Chicago Milwaukee Corporation and subsidiaries as of December 31, 1972 and 1971, and the related consolidated statements of operations and retained earnings and changes in financial position for the years then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the aforementioned financial statements present fairly the consolidated financial position of Chicago Milwaukee Corporation and subsidiaries at December 31, 1972 and 1971, and the results of their operations and changes in financial position for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis.

PEAT, MARWICK, MITCHELL & CO.

Chicago, Illinois
February 16, 1973

Stock Transfer Offices

The Chase Manhattan Bank, New York, N.Y. 10015
The First National Bank of Chicago, Chicago, Illinois 60670

Registrars

The First National City Bank of New York, New York, N.Y. 10022
Continental Illinois National Bank and Trust Company of Chicago, Chicago, Illinois 60690

Annual Meeting
May 8, 1973,
Chicago, Illinois

This Annual Report is not and must not be considered as proxy soliciting material, or as a report or document filed pursuant to the Securities Exchange Act, or any rule or regulation thereunder.