



BECOMING A TRUE SUPPLY CHAIN ENABLER

2013 ANNUAL REPORT



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Except where otherwise indicated, all financial information reflected in this document is expressed in Canadian dollars and determined on the basis of United States generally accepted accounting principles (U.S. GAAP).

Certain information included in this annual report constitutes “forward-looking statements” within the meaning of the United States Private Securities Litigation Reform Act of 1995 and under Canadian securities laws. CN cautions that, by their nature, these forward-looking statements involve risks, uncertainties and assumptions. The Company cautions that its assumptions may not materialize and that current economic conditions render such assumptions, although reasonable at the time they were made, subject to greater uncertainty.

Such forward-looking statements are not guarantees of future performance and involve known and unknown risks, uncertainties and other factors which may cause the actual results or performance of the Company or the rail industry to be materially different from the outlook or any future results or performance implied by such statements. Important risk factors that could affect the forward-looking statements include, but are not limited to, the effects of general economic and business conditions, industry competition, inflation, currency and interest rate fluctuations, changes in fuel prices, legislative and/or regulatory developments, compliance with environmental laws and regulations, actions by regulators, various events which could disrupt operations, including natural events such as severe weather, droughts, floods and earthquakes, labor negotiations and disruptions, environmental claims, uncertainties of investigations, proceedings or other types of claims and litigation, risks and liabilities arising from derailments, and other risks detailed from time to time in reports filed by CN with securities regulators in Canada and the United States. Reference should be made to “Management’s Discussion and Analysis” in CN’s annual and interim reports, Annual Information Form and Form 40-F filed with Canadian and U.S. securities regulators, available on CN’s website (www.cn.ca), for a summary of major risks.

CN assumes no obligation to update or revise forward-looking statements to reflect future events, changes in circumstances, or changes in beliefs, unless required by applicable Canadian securities laws. In the event CN does update any forward-looking statement, no inference should be made that CN will make additional updates with respect to that statement, related matters, or any other forward-looking statement.

As used herein, the word “Company” or “CN” means, as the context requires, Canadian National Railway Company and/or its subsidiaries.

A message from the Chairman



Dear fellow shareholders In 2013, CN's outstanding performance further solidified the company's position as the leader of the rail industry. CN not only continued to deliver its customers' goods safely and efficiently, it was also recognized for *Delivering Responsibly* – the term CN uses to describe its sustainability, safety and corporate citizenship activities.

For the fourth consecutive year, CN has earned a position in CDP's Canada 200 Climate Disclosure Leadership Index. As well, CN's sustainability practices earned it a place as the leader in the Transportation and Transportation Infrastructure Industry sector of the Dow Jones Sustainability World Index (DJSI).

This is part of the leadership people have come to expect from CN. Since I became Chairman of CN's Board nearly 20 years ago, the company has made enormous improvements. We embarked on a bold mission to privatize CN and we have become the best in the business.

This will be my last message as CN's Chairman before my retirement. I am proud to say we have continued to raise the bar for our achievements for many years. We have created great value for shareholders while we improved our overall performance. I believe that I leave CN in excellent shape to ensure its continued track record of excellence.

All members of the Board have the fullest confidence in Robert Pace, whom we have selected as the next Chairman of the Board. Robert is a highly respected businessman who is very active in his community, and our shareholders can feel confident about his abilities to help guide CN. He will be supported by a talented team at the Board level, and of course by our President and CEO Claude Mongeau, and the 23,000 railroaders who make CN the leader in the industry.

As I prepare to move on, I want to thank all of our shareholders for the support you have shown me. I am proud to retire knowing the company has everything in place that it needs to keep delivering value for its customers, its shareholders and to continue to play its role as a transportation backbone of the economy for years to come.

Sincerely,

A handwritten signature in black ink that reads "David McLean". The signature is fluid and cursive, with the first letters of the first and last names being capitalized and prominent.

David McLean, O.B.C., LL.D.
Chairman of the Board

A message from Claude Mongeau



BECOMING A TRUE SUPPLY CHAIN ENABLER

Dear fellow shareholders Over the last few years, I've frequently been asked about what the next big step forward would be for railroading. As it turns out, the next leap forward for railroading goes well beyond our tracks and trains.

Of course we're still focussed on improving how our railroad operates. CN has long earned the reputation of being the industry's leader in efficiency, speed and service. And we're not about to let up. We invest more than \$2 billion annually to keep our network safe and fluid, balancing Operational and Service Excellence to serve customers safely and efficiently.

CN's team of dedicated railroaders delivered on our strategic agenda and produced record volumes and revenues in 2013. Our full-year 2013 adjusted diluted EPS increased nine per cent to \$3.06, with adjusted 2013 net income of \$2,582 million versus \$2,456 million in 2012. Key operating and service metrics remained solid, and we continued to drive incremental improvement in our broad safety record. CN reduced its accident rate per million train miles by nine per cent in 2013, an additional indication of long-term gains in safety. In the past 10 years, CN's main-track accidents have declined by approximately 50 per cent despite increased freight volumes.

But CN has also raised its game through a mindset that looks at the entirety of moving goods through the complete supply chain: not just how CN handles its portion of the process.

We are increasingly involved in every step of the way, with all of the players. We are a catalyst for putting partners together in an unprecedented manner, for examining and improving how products and material get from point A to point B. We call this being a Supply Chain enabler.

"We are a catalyst for putting partners together in an unprecedented manner, for examining and improving how products and material get from point A to point B."

Supply Chain mindset

Our aspiration at CN is to become a true Supply Chain enabler, which is to look at things not just as a railroad, but to do so end to end, with a view to driving service and efficiency. It's about helping our customers win in the marketplace, and we're doing that for the benefit of all the supply chain partners that we deal with. We're doing that to improve service in all business segments. We're helping our partners find ways

to save costs while they do likewise for us. We're looking at ways to tactically deploy assets for their benefit and ours. That's what true supply chain engagement is all about.

And why are we doing this? Because we believe that engaging our customers, having a more customer-centric approach, is absolutely essential to help them win in the marketplace and help us grow faster, so that we can all benefit from this success. It's also because when all the players in a supply chain see the world in the same manner, you open up greater opportunities for efficiencies and service improvement.

The first port with which we signed a framework supply chain collaboration agreement a few years ago was the Port of Halifax. It led to service level agreements with the two terminal operators there and the concept caught on quickly with other players. As I've explained before, today we have agreements with ports and terminal operators across Canada.

We measure throughput, slot utilization, and transit time end to end in the same way from every port, and we provide scorecards to our customers about our performance so that we can improve together on an ongoing basis. Those benefits are continuing to help us enhance innovation and productivity throughout the supply chain.

This supply chain mentality is now part of how we approach all areas of our business. As we continue to connect and build trust among customers, shippers, suppliers, and other players, we are keenly aware that a safe supply chain is as important as an efficient one.

"...we believe that engaging our customers, having a more customer-centric approach, is absolutely essential to help them win in the marketplace and help us grow faster..."

Committed to safety

In 2013, CN's main-track accident performance was the best on record, based on statistics established by the Transportation Safety Board in Canada and the Federal Railroad Administration in the U.S. This was the result of CN's comprehensive, integrated safety plan and our ongoing efforts to improve CN's safety culture. CN invests continuously to maintain a safe operation. From track infrastructure, to leading-edge technology, to new training initiatives, this allows us to operate a safe railway and improve the efficiency and fluidity of the network.

In addition to all that we do to improve our safety performance, we are engaging with many other stakeholders, such as shippers, regulators, government officials and other railroads. As an industry leader, CN is committed to playing our role to help ensure goods are moved through communities safely for the benefit of all.



Claude Mongeau
President and CEO

BECOMING A TRUE SUPPLY CHAIN ENABLER

MAKING CONNECTIONS



A fresh approach to the transborder food supply chain

Ensuring perishable food reaches markets on time is challenging, and must be achieved in a way that is cost effective, meets high food safety standards and reduces environmental impact. CN's supply chain efforts, new tools and improved service is making this happen for customers like never before.

CN has undertaken initiatives that include incorporating innovative technology within the CargoCool Program, CN's refrigerated or reefer service. The state-of-the-art remote monitoring technology provides end-to-end visibility with real-time tracking and tracing on CN's network, and even allows remote temperature adjustments. Dedicated reefer customer service personnel execute timely exception management with a sense of urgency that is needed within the food industry. CN's expanded cross-border cold supply chain program helps connect producers from key markets including California, Washington, Oregon and Western Canada to consumer markets in the U.S., Canada and Mexico, making CN the first railroad with this fully containerized Transborder Reefer service. CN's CargoCool Program

allows our customers to grow locally and expand globally. With some of the fastest transit times in the industry, CN is delivering perishable goods in the condition that customers demand: fresh, undamaged and unspoiled.

A cold supply chain must be tight with little room for error. To achieve that, you need a player with enough capacity, not only to meet current market demand but also to respond to growth. With recent investments, including increasing its fleet of reefer containers, CN provides a sustainable transportation solution that is adaptable to growing volumes.

Connecting energy partners and suppliers

Frac sand is used by the oil and gas industry in the process of fracturing shale rock to help the release of hydrocarbons. The process of fracturing, coupled with horizontal drilling, has moved North America to rank among the top world producers of oil and gas. Wisconsin has one of the largest reserves of high-quality frac sand in North America, right in CN's backyard, thanks to the acquisition of the Wisconsin Central in 2001.

CN's unique access to the Wisconsin sand deposits and our direct reach to Western Canada





oil and gas and other key North American shale plays through its connections with all Class I railroads, sets CN apart to benefit from the strong growth in frac sand shipments taking place today. By matching and linking up producers and users of frac sand, CN has been one of the key drivers behind the amazing growth of frac sand along our lines. Matchmaking is being done at all stages of the projects, from the plant design phase, to the building of a customer base for our sand customers, and to the delivery of the sand to oil and gas users. This has benefited our sand customers tremendously, as well as CN, accelerating growth beyond the normal course of doing business.

CN moved over 55,000 carloads in 2013 generating \$200M in revenue, a 50% increase versus 2012. By 2015, we're aiming to achieve annual frac sand revenues of \$300M.

Intermodal: the big picture

CN's supply chain approach is allowing the company to deliver value service as defined by the customer, not just as we see it. We measure end-to-end service for customers from their point of view, which includes the rail portion, but

also goes beyond rail. For overseas intermodal shippers, that means we're paying close attention to the entire roundtrip – from the container's departure overseas, to the waiting time at the port terminal, to the rail transit time, and finally, to the container's return back to the port of entry.

We are actively working to create ecosystems of collaboration, to share information, and to closely monitor the key operating and service metrics that drive a more efficient end-to-end supply chain. It also means we're helping our overseas customers lower their total supply chain costs.

Take for example a loaded container that arrives in Joliet, Illinois. CN is working hard to find opportunities to re-load that container with products destined to Asia. When we can't find an export load, CN seeks to use the empty container in its domestic reposition program (DRP) to deliver goods from greater Chicago to consumers in Western Canada. CN also strives to increase export loads and help our customers leverage their container assets on the sea. At the same time, this helps CN grow its revenues and volumes. That's what we call winning with our customers.

<p>David G.A. McLean, O.B.C., LL.D. Chairman of the Board Canadian National Railway Company Chairman of the Board The McLean Group Committees: 2, 3, 4, 6, 7, 8</p>	<p>Donald J. Carty, O.C., LL.D. Retired Chairman and CEO American Airlines and Retired Vice-Chairman Dell, Inc. Committees: 1, 2, 3, 7, 8</p>	<p>The Honourable Denis Losier, C.M., P.C., LL.D. Retired President and Chief Executive Officer Assumption Life Committees: 1*, 3, 4, 5, 6, 7, 8</p>	<p><i>Directors Emeritus</i> Purdy Crawford J.V. Raymond Cyr James K. Gray Cedric Ritchie</p>
<p>Claude Mongeau President and Chief Executive Officer Canadian National Railway Company Committees: 4*, 7, 8</p>	<p>Ambassador Gordon D. Giffin Senior Partner McKenna Long & Aldridge Committees: 1, 2, 4, 5, 6*, 7, 8</p>	<p>The Honourable Edward C. Lumley, P.C., LL.D. Vice-Chairman BMO Capital Markets Committees: 2, 3, 6, 7, 8*</p>	<p>Committees:</p> <ol style="list-style-type: none"> 1 Audit 2 Finance 3 Corporate governance and nominating 4 Donations and sponsorships 5 Environment, safety and security 6 Human resources and compensation 7 Strategic planning 8 Investment <p>* denotes chairman of the committee</p>
<p>Michael R. Armellino, CFA Retired Partner The Goldman Sachs Group, L.P. Committees: 2, 3*, 5, 6, 7, 8</p>	<p>Edith E. Holiday Corporate Director and Trustee Former General Counsel United States Treasury Department Secretary of the Cabinet The White House Committees: 2, 3, 6, 7, 8</p>	<p>James E. O'Connor Former Chairman and Chief Executive Officer Republic Services, Inc. Committees: 1, 2, 5, 7, 8</p>	
<p>A. Charles Baillie, O.C., LL.D. Former Chairman and Chief Executive Officer The Toronto-Dominion Bank Committees: 2*, 3, 6, 7, 8</p>	<p>V. Maureen Kempston Darkes, O.C., D.Comm., LL.D. Retired Group Vice-President General Motors Corporation and President GM Latin America, Africa and Middle East Committees: 1, 5*, 6, 7, 8</p>	<p>Robert Pace, D.Comm. Vice-Chairman of the Board Canadian National Railway Company President and Chief Executive Officer The Pace Group Committees: 1, 3, 4, 6, 7, 8</p>	
<p>Hugh J. Bolton, FCA Chairman of the Board EPCOR Utilities Inc. Committees: 1, 5, 6, 7*, 8</p>			

Chairman of the Board and Select Senior Officers of the Company As at December 31, 2013

<p>David G.A. McLean Chairman of the Board</p>	<p>Sean Finn Executive Vice-President Corporate Services and Chief Legal Officer</p>	<p>Mike Cory Senior Vice-President Western Region</p>	<p>John Orr Vice-President Eastern Region</p>
<p>Claude Mongeau President and Chief Executive Officer</p>	<p>Luc Jobin Executive Vice-President and Chief Financial Officer</p>	<p>Jeff Liepelt Senior Vice-President Southern Region</p>	<p>Russell Hiscock President and Chief Executive Officer CN Investment Division</p>
	<p>Jean-Jacques Ruest Executive Vice-President and Chief Marketing Officer</p>	<p>Kimberly A. Madigan Vice-President Human Resources</p>	
	<p>Jim Vena Executive Vice-President and Chief Operating Officer</p>	<p>Janet Drysdale Vice-President Investor Relations</p>	

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Selected Railroad Statistics

	Year ended December 31,	2013	2012	2011
Statistical operating data				
Rail freight revenues (\$ millions)		9,587	8,938	8,111
Gross ton miles (GTM) (millions)		401,390	383,754	357,927
Revenue ton miles (RTM) (millions)		210,133	201,496	187,753
Carloads (thousands)		5,190	5,059	4,873
Route miles (includes Canada and the U.S.) ⁽¹⁾		20,000	20,100	20,000
Employees (end of year)		23,721	23,430	23,339
Employees (average for the year)		23,705	23,466	23,079
Productivity				
Operating ratio (%)		63.4	62.9	63.5
Rail freight revenue per RTM (cents)		4.56	4.44	4.32
Rail freight revenue per carload (\$)		1,847	1,767	1,664
Operating expenses per GTM (cents)		1.67	1.62	1.60
Labor and fringe benefits expense per GTM (cents)		0.54	0.51	0.51
GTMs per average number of employees (thousands)		16,933	16,354	15,509
Diesel fuel consumed (US gallons in millions)		403.7	388.7	367.7
Average fuel price (\$/US gallon)		3.55	3.47	3.39
GTMs per US gallon of fuel consumed		994	987	973
Safety indicators				
Injury frequency rate per 200,000 person hours ⁽²⁾		1.69	1.42	1.55
Accident rate per million train miles ⁽²⁾		1.92	2.10	2.25

(1) Rounded to the nearest hundred miles.

(2) Based on Federal Railroad Administration (FRA) reporting criteria.

Statistical data and related productivity measures are based on estimated data available at such time and are subject to change as more complete information becomes available, as such certain of the 2012 and 2011 comparative data and related productivity measures have been restated.

Management's discussion and analysis (MD&A) relates to the financial position and results of operations of Canadian National Railway Company, together with its wholly-owned subsidiaries, collectively "CN" or "the Company." Canadian National Railway Company's common shares are listed on the Toronto and New York stock exchanges. Except where otherwise indicated, all financial information reflected herein is expressed in Canadian dollars and determined on the basis of United States generally accepted accounting principles (U.S. GAAP). The Company's objective is to provide meaningful and relevant information reflecting the Company's financial position and results of operations. In certain instances, the Company may make reference to certain non-GAAP measures that, from management's perspective, are useful measures of performance. The reader is advised to read all information provided in the MD&A in conjunction with the Company's 2013 Annual Consolidated Financial Statements and Notes thereto.

Business profile

CN is engaged in the rail and related transportation business. CN's network of approximately 20,000 route miles of track spans Canada and mid-America, connecting three coasts: the Atlantic, the Pacific and the Gulf of Mexico. CN's extensive network, and its co-production arrangements, routing protocols, marketing alliances, and interline agreements, provide CN customers access to all three North American Free Trade Agreement (NAFTA) nations.

CN's freight revenues are derived from seven commodity groups representing a diversified and balanced portfolio of goods transported between a wide range of origins and destinations. This product and geographic diversity better positions the Company to face economic fluctuations and enhances its potential for growth opportunities. In 2013, no individual commodity group accounted for more than 21% of total revenues. From a geographic standpoint, 16% of revenues relate to United States (U.S.) domestic traffic, 32% transborder traffic, 20% Canadian domestic traffic and 32% overseas traffic. The Company is the originating carrier for approximately 85% of traffic moving along its network, which allows it both to capitalize on service advantages and build on opportunities to efficiently use assets.

Corporate organization

The Company manages its rail operations in Canada and the U.S. as one business segment. Financial information reported at this level, such as revenues, operating income and cash flow from operations, is used by the Company's corporate management in evaluating financial and operational performance and allocating resources across CN's network. The Company's strategic initiatives, which drive its operational direction, are developed and managed centrally by corporate management and are communicated to its regional activity centers (the Western Region, Eastern Region and Southern Region), whose role is to manage the day-to-day service requirements of their respective territories, control direct costs incurred locally, and execute the corporate strategy and operating plan established by corporate management.

See Note 14 – Segmented information to the Company's 2013 Annual Consolidated Financial Statements for additional information on the Company's corporate organization, as well as selected financial information by geographic area.

Strategy overview

CN's focus is on running a safe and efficient railroad. While remaining at the forefront of the rail industry, CN's goal is to be internationally regarded as one of the best-performing transportation companies.

CN's commitment is to create value for both its customers and shareholders. By deepening customer engagement, leveraging the strength of its franchise, and delivering operational and service excellence, the Company seeks to provide quality and cost-effective service that creates value for its customers.

CN's corporate goals are generally based on five key financial performance targets: revenues, operating income, earnings per share, free cash flow and return on invested capital, as well as various key operating and customer service metrics that the Company focuses on to measure efficiency, safety and quality of service. By striving for sustainable financial performance through profitable growth, adequate free cash flow and return on invested capital, CN seeks to deliver increased shareholder value. On October 22, 2013, the Board of Directors of the Company approved a two-for-one common stock split which was effected in the form of a stock dividend of one additional common share of CN for each share outstanding, which was paid on November 29, 2013, to shareholders of record on November 15, 2013. At the effective date of the stock split, all equity-based benefit plans and the share repurchase programs were adjusted to reflect the issuance of additional shares. All share and per share data presented herein reflect the impact of the stock split. In addition, the Company's Board of Directors approved an increase of 16% to the quarterly dividend to common shareholders, from \$0.215 in 2013 to \$0.250 in 2014.

For 2013, the Company's Board of Directors approved share repurchase programs funded mainly from cash generated from operations. The first share repurchase program, which was approved on October 22, 2012, allowed for the repurchase of up to \$1.4 billion in common shares, not to exceed 36.0 million common shares, between October 29, 2012 and October 28, 2013. The Company repurchased a total of 29.4 million common shares under this share repurchase program. On October 22, 2013, the Board of Directors of the Company approved a new share repurchase program which allows for the repurchase of up to 30.0 million common shares, between October 29, 2013 and October 23, 2014. Share repurchases are made pursuant to a normal course issuer bid at prevailing market prices, plus brokerage fees, or such other prices as may be permitted by the Toronto Stock Exchange.

CN's business model is anchored on five core principles: providing quality service, controlling costs, focusing on asset utilization, committing to safety and sustainability, and developing people. For many years, CN has operated with a mindset that drives efficiency. The CN *Precision Railroading* model, which focuses on improving every process that affects delivery of customers' goods, continues to guide the Company's performance. It is a highly disciplined process whereby CN handles individual rail shipments according to a specific trip plan and manages all aspects of railroad operations to meet customer commitments efficiently and profitably. It demands discipline to execute the trip plan, the relentless measurement of results, and the use of such results to generate further execution improvements in the service provided to customers. It also aims to increase velocity, improve reliability, lower costs, enhance asset utilization and, ultimately, help the Company to grow the top line. The Company maintains that philosophy today and works hard to run more efficient trains, reduce dwell times at terminals and improve overall network velocity. With CN's business model, fewer railcars and locomotives are needed to ship the same amount of freight in a tight, reliable and efficient operation. The railroad is run based on a disciplined operating methodology, executing with a sense of urgency and accountability. This philosophy has been a key contributor to CN's earnings growth and improved return on invested capital. The Company has also set its sights on becoming a true supply chain enabler by helping to elevate service performance end-to-end. CN is pursuing better end-to-end service and greater operating efficiencies while helping customers win in their own markets. While CN is a leader in fast and reliable service hub-to-hub, the Company strives to distinguish itself by bringing greater value to the entire range of customer touch points. The Company continues to strengthen its commitment to operational and service excellence through a wide range of innovations anchored on its continuous improvement philosophy. CN's major push in first-mile/last-mile activities is all about quality interaction with customers – from developing a sharper outside-in perspective to better monitoring of traffic forecasts; from the Company's car management distribution activities to higher and more responsive car order fulfillment; and from improving customer communication to iAdvise (proactive customer communication system at the local level). CN's broad-based service innovations benefit customers and support the Company's goal to grow the business faster than the overall economy. CN understands the importance of being the best operator in the business, and being the best service innovator as well. Service excellence means expanding CN's perspective, working more closely, and building on mutual trust, with customers and supply chain customers as well as involving all relevant areas of the Company in the process. The success of the business model is dependent on commercial principles and a supportive regulatory environment, both of which are key to an effective rail transportation marketplace throughout North America.

Providing quality service, controlling costs and focusing on asset utilization

The basic driver of the Company's business is demand for reliable, efficient, and cost effective transportation. As such, the Company's focus is the pursuit of its long-term business plan, delivering operational and service excellence by providing a high level of service to customers while operating safely and efficiently, and meeting short- and long-term financial commitments.

In 2013, the Company benefited from a modest increase in North American industrial production, a significant increase in U.S. housing starts and moderate growth in U.S. automotive sales. In 2014, the Company expects North American industrial production to increase by approximately three percent as well as continued improvements in U.S. housing starts and U.S. automotive sales. For the 2013/2014 crop year, the Company assumes Canadian grain production to be well above the five-year average and U.S. grain production to be above the five-year average. With respect to the 2014/2015 crop year, the Company assumes Canadian and U.S. grain production to be in line with their respective five-year averages.

To meet its business plan objectives, the Company's priority is to grow the business at low incremental cost. The Company's strategy to pursue deeper customer engagement and service improvements is expected to continue to drive growth. Improvements are coming from several key thrusts including first-mile/last-mile initiatives that improve customer service at origin and destination, and a supply chain perspective that emphasizes collaboration and better end-to-end service. The Company sees opportunities for growth across most markets, led by energy-related commodities, particularly crude oil and frac sand; by overseas container traffic; by market share gains against truck in domestic intermodal; by a continued recovery in the U.S. housing market; as well as by strong offshore grain exports due to record western Canadian crop. Longer term, the Company expects continued growth in offshore export markets including metallurgical and thermal coal as well as potash.

To grow the business at low incremental cost and to operate efficiently and safely while maintaining a high level of customer service, the Company continues to invest in capital programs to maintain a safe and fluid railway and pursue strategic initiatives to improve its franchise, as well as undertake productivity initiatives to reduce costs and leverage its assets. Opportunities to improve productivity extend across all functions in the organization. Train productivity is being improved through the acquisition of locomotives that are more fuel-efficient than the ones they replace, which will also improve service reliability for customers and reduce greenhouse gas emissions. In addition, the Company's locomotives are being equipped with distributed power capability, which allows the Company to run longer, more efficient trains, particularly in cold weather conditions, while improving train handling, reducing train separations and improving the overall safety of operations. These initiatives, combined with CN's investments in longer sidings

over the years, offer train-mile savings, allow for efficient long-train operations and reduce wear on rail and wheels. Yard throughput is being improved through SmartYard, an innovative use of real-time traffic information to sequence cars effectively and get them out on the line more quickly in the face of constantly changing conditions. In Engineering, the Company is continuously working to increase the productivity of its field forces, through better use of traffic information and the optimization of work scheduling and as a result, better management of its engineering forces on the track. The Company also intends to continue focusing on the reduction of accidents and related costs, as well as costs for legal claims and health care.

CN's capital expenditure programs support the Company's commitment to its core principles and strategy and its ability to grow the business profitably. In 2014, CN plans to invest approximately \$2.1 billion on capital programs, of which over \$1.2 billion is targeted towards track infrastructure to continue operating a safe railway and improve the productivity and fluidity of the network; and includes the replacement of rail, ties, and other track materials, bridge improvements, as well as various branch line upgrades. This amount also includes funds for strategic initiatives and additional enhancements to the track infrastructure in western and eastern Canada as well as in the U.S. In 2013, the Company invested approximately \$100 million in the Edmonton-Winnipeg corridor in order to increase rail capacity and support strong volumes of grain and other commodities.

In 2014, CN's equipment capital expenditures are targeted to reach approximately \$300 million, allowing the Company to tap growth opportunities and improve the quality of the fleet. In order to handle expected traffic increase and improve operational efficiency, in 2013 CN took delivery of 44 new and 37 second-hand high-horsepower locomotives. In 2014, CN expects to take delivery of an additional 45 new high-horsepower locomotives.

In 2014, CN also expects to spend approximately \$600 million on facilities to grow the business including transloads, distribution centers, and the completion of its Calgary Logistics Park project; on information technology to improve service and operating efficiency; and on other projects to increase productivity.

To meet short- and long-term financial commitments, the Company pursues a solid financial policy framework with the goal of maintaining a strong balance sheet by monitoring its credit ratios and preserving an investment-grade credit rating to be able to maintain access to public financing. The Company's principal source of liquidity is cash generated from operations, which can be supplemented by its commercial paper program and its accounts receivable securitization program to meet short-term liquidity needs. The Company's primary uses of funds are for working capital requirements, including income tax installments, pension contributions, contractual obligations, capital expenditures relating to track infrastructure and other, acquisitions, dividend payouts, and the repurchase of shares through share buyback programs, when applicable. The Company sets priorities on its uses

of available funds based on short-term operational requirements, expenditures to continue to operate a safe railway and pursue strategic initiatives, while also considering its long-term contractual obligations and returning value to its shareholders.

Delivering responsibly

The Company's commitment to safety is reflected in the wide range of initiatives that CN is pursuing and in the size of its capital programs. Comprehensive plans are in place to address safety, security, employee well-being and environmental management. CN's Safety Management Plan is the framework for putting safety at the center of its day-to-day operations. This proactive plan is designed to minimize risk and drive continuous improvement in the reduction of injuries and accidents, and engages employees at all levels of the organization.

The Company has made sustainability an integral part of its business strategy by aligning its sustainability agenda with its business model. As part of the Company's comprehensive sustainability action plan and to comply with the CN Environmental Policy, the Company engages in a number of initiatives, including the use of fuel-efficient locomotives that reduce greenhouse gas emissions; increasing operational and building efficiencies; investing in virtualization technologies, energy-efficient data centers and recycling programs for information technology systems; reducing, recycling and reusing waste at its facilities and on its network; engaging in modal shift agreements that favor low emission transport services; and participating in the Carbon Disclosure Project to gain a more comprehensive view of its carbon footprint.

The CN Environmental Policy aims to minimize the impact of the Company's activities on the environment. The Company strives to contribute to the protection of the environment by integrating environmental priorities into the Company's overall business plan and through the specific monitoring and measurement of such priorities against historical performance and in some cases, specific targets. All employees must demonstrate commitment to the CN Environmental Policy at all times and it is the Environment, Safety and Security Committee of the Board of Directors that has the responsibility of overseeing this policy. This committee's responsibilities, powers and operation are further described in its charter, which is included in the Company's Corporate Governance Manual available on CN's website. Certain risk mitigation strategies, such as periodic audits, employee training programs and emergency plans and procedures, are in place to minimize the environmental risks to the Company.

The CN Environmental Policy, the Company's Carbon Disclosure Project report, and the Corporate Citizenship Report "Delivering Responsibly" are available on CN's website. In 2013, the Company's sustainability practices earned it a place as the leader in the Transportation and Transportation Infrastructure Industry sector of the Dow Jones Sustainability World Index (DJSI). This is also the second consecutive year that the Company has been listed on the DJSI World Index and the fifth straight year on the DJSI North American Index.

Developing people

CN's ability to develop the best railroaders in the industry has been a key contributor to the Company's success. CN recognizes that without the right people – no matter how good a service plan or business model a company may have – it will not be able to fully execute. The Company is focused on recruiting the right people, developing employees with the right skills, motivating them to do the right thing, and training them to be the future leaders of the Company. In 2014, CN expects to open two new state-of-the-art training centers located in Winnipeg, Manitoba and suburban Chicago, Illinois as part of a new revitalized company-wide training program aimed at preparing railroaders to be highly skilled, safety conscious and confident in their work environment. The Company continues to address changes in employee demographics that will span multiple years. The Human Resources and Compensation Committee of the Board of Directors reviews the progress made in developing current and future leaders through the Company's leadership development programs. These programs and initiatives provide a solid platform for the assessment and development of the Company's talent pool. The leadership development programs are tightly integrated with the Company's business strategy.

The forward-looking statements discussed in this MD&A are subject to risks and uncertainties that could cause actual results or performance to differ materially from those expressed or implied in such statements and are based on certain factors and assumptions which the Company considers reasonable, about events, developments, prospects and opportunities that may not materialize or that may be offset entirely or partially by other events and developments. See the section of this MD&A entitled Forward-looking statements for assumptions and risk factors affecting such forward-looking statements.

Impact of foreign currency translation on reported results

Although the Company conducts its business and reports its earnings in Canadian dollars, a large portion of revenues and expenses is denominated in US dollars. As such, the Company's results are affected by exchange rate fluctuations.

Management's discussion and analysis includes reference to "constant currency," which allows the financial results to be viewed without the impact of fluctuations in foreign exchange rates, thereby facilitating period-to-period comparisons in the analysis of trends in business performance. Financial results at constant currency are obtained by translating the current period results denominated in US dollars at the foreign exchange rate of the comparable period of the prior year. The average foreign exchange rate for the year ended December 31, 2013 was \$1.03 per US\$1.00 compared to \$1.00 per US\$1.00 for 2012. Measures at constant currency are considered non-GAAP measures and do not have any standardized meaning prescribed by GAAP and therefore may not be comparable to similar measures presented by other companies.

Forward-looking statements

Certain information included in this MD&A are "forward-looking statements" within the meaning of the United States Private Securities Litigation Reform Act of 1995 and under Canadian securities laws. CN cautions that, by their nature, forward-looking statements involve risks, uncertainties and assumptions. The Company cautions that its assumptions may not materialize and that current economic conditions render such assumptions, although reasonable at the time they were made, subject to greater uncertainty. These forward-looking statements include, but are not limited to, statements with respect to growth opportunities; statements that the Company will benefit from growth in North American and global economies; the anticipation that cash flow from operations and from various sources of financing will be sufficient to meet debt repayments and future obligations in the foreseeable future; statements regarding future payments, including income taxes and pension contributions; as well as the projected capital spending program. Forward-looking statements could further be identified by the use of terminology such as the Company "believes," "expects," "anticipates" or other similar words.

Such forward-looking statements are not guarantees of future performance and involve known and unknown risks, uncertainties and other factors which may cause the actual results or performance of the Company or the rail industry to be materially different from the outlook or any future results or performance implied by such statements. Key assumptions used in determining forward-looking information are set forth below.

Forward-looking statements	Key assumptions or expectations
Statements relating to general economic and business conditions, including those referring to revenue growth opportunities	<ul style="list-style-type: none"> • North American and global economic growth • Long-term growth opportunities being less affected by current economic conditions • Year-over-year carload growth
Statements relating to the Company's ability to meet debt repayments and future obligations in the foreseeable future, including income tax payments, and capital spending	<ul style="list-style-type: none"> • North American and global economic growth • Adequate credit ratios • Investment grade credit rating • Access to capital markets • Adequate cash generated from operations
Statements relating to pension contributions	<ul style="list-style-type: none"> • Adequate cash generated from operations and other sources of financing • Adequate long-term return on investment on pension plan assets • Level of funding as determined by actuarial valuations, particularly influenced by discount rates for funding purposes

Important risk factors that could affect the forward-looking statements include, but are not limited to, the effects of general economic and business conditions; industry competition; inflation, currency and interest rate fluctuations; changes in fuel prices; legislative and/or regulatory developments; compliance with environmental laws and regulations; actions by regulators; various events which could disrupt operations, including natural events such as severe weather, droughts, floods and earthquakes; labor negotiations and disruptions; environmental claims; uncertainties of investigations, proceedings or other types of claims and litigation; risks and liabilities arising from derailments; and other risks detailed from time to time in reports filed by CN with securities regulators in Canada and the U.S. See the section of this MD&A entitled Business risks for detailed information on major risk factors.

CN assumes no obligation to update or revise forward-looking statements to reflect future events, changes in circumstances, or changes in beliefs, unless required by applicable Canadian securities laws. In the event CN does update any forward-looking statement, no inference should be made that CN will make additional updates with respect to that statement, related matters, or any other forward-looking statement.

Financial outlook

During the year, the Company issued and updated its financial outlook. The 2013 actual results are in line with the latest financial outlook as disclosed by the Company.

Financial and statistical highlights

\$ in millions, except per share data, or unless otherwise indicated	2013	2012	2011	Change	
				Favorable/(Unfavorable)	
Financial results					
Revenues	\$ 10,575	\$ 9,920	\$ 9,028	7%	10%
Operating income	\$ 3,873	\$ 3,685	\$ 3,296	5%	12%
Net income ^{(1) (2) (3)}	\$ 2,612	\$ 2,680	\$ 2,457	(3%)	9%
Operating ratio	63.4%	62.9%	63.5%	(0.5)-pts	0.6-pts
Basic earnings per share ^{(1) (2) (3)}	\$ 3.10	\$ 3.08	\$ 2.72	1%	13%
Diluted earnings per share ^{(1) (2) (3)}	\$ 3.09	\$ 3.06	\$ 2.70	1%	13%
Dividend declared per share	\$ 0.86	\$ 0.75	\$ 0.65	15%	15%
Financial position					
Total assets	\$ 30,163	\$ 26,659	\$ 26,026	13%	2%
Total long-term liabilities	\$ 14,712	\$ 13,438	\$ 13,631	(9%)	1%
Statistical operating data and productivity measures ⁽⁴⁾					
Employees (average for the year)	23,705	23,466	23,079	1%	2%
Gross ton miles (GTM) per average number of employees (thousands)	16,933	16,354	15,509	4%	5%
GTMs per US gallon of fuel consumed	994	987	973	1%	1%

(1) The 2013 figures include a gain on exchange of perpetual railroad operating easements on specific rail lines of \$29 million, or \$18 million after-tax (\$0.02 per basic or diluted share); a gain on disposal of a segment of the Oakville subdivision of \$40 million, or \$36 million after-tax (\$0.04 per basic or diluted share); and an income tax expense of \$24 million (\$0.03 per basic or diluted share) resulting from the enactment of higher provincial corporate income tax rates.

(2) The 2012 figures include a gain on disposal of a segment of the Bala and a segment of the Oakville subdivisions of \$281 million, or \$252 million after-tax (\$0.29 per basic share or \$0.28 per diluted share); and a net income tax expense of \$28 million (\$0.03 per basic or diluted share) consisting of a \$35 million income tax expense resulting from the enactment of higher provincial corporate income tax rates that was partly offset by a \$7 million income tax recovery resulting from the recapitalization of a foreign investment.

(3) The 2011 figures include gains on disposal of substantially all of the assets of IC RailMarine Terminal Company of \$60 million, or \$38 million after-tax (\$0.04 per basic or diluted share) and of a segment of the Kingston subdivision known as the Lakeshore East of \$288 million, or \$254 million after-tax (\$0.28 per basic or diluted share). The 2011 figures also included a net income tax expense of \$40 million (\$0.04 per basic or diluted share) resulting from the enactment of state corporate income tax rate changes and other legislated state tax revisions, and an income tax recovery of \$11 million (\$0.01 per basic or diluted share) relating to certain fuel costs attributed to various wholly-owned subsidiaries' fuel consumption in prior periods.

(4) Based on estimated data available at such time and subject to change as more complete information becomes available.

Financial results

2013 compared to 2012

In 2013, net income was \$2,612 million, a decrease of \$68 million, or 3%, when compared to 2012, with diluted earnings per share rising 1% to \$3.09. The \$68 million decrease was mainly due to a reduction in Other income resulting from lower gains on disposal of rail assets that was partly offset by an increase in Operating income.

Included in the 2013 figures was a gain on exchange of perpetual railroad operating easements including the track and roadway assets on specific rail lines (collectively the "exchange of easements"), of \$29 million, or \$18 million after-tax (\$0.02 per diluted share) and a gain on disposal of a segment of the Oakville subdivision, together with the rail fixtures and certain passenger agreements (collectively the "Lakeshore West"), of \$40 million, or \$36 million after-tax (\$0.04 per diluted share). The 2013 figures also included a \$24 million (\$0.03 per diluted share) income tax expense from the enactment of higher provincial corporate income tax rates. Included in the 2012 figures was a gain on disposal of a segment of the Bala and a segment of the Oakville subdivisions, together with the rail fixtures and certain passenger agreements (collectively the "Bala-Oakville"), of \$281 million, or \$252 million after-tax (\$0.28 per diluted share); and a net income tax expense of \$28 million (\$0.03 per diluted share) consisting of a \$35 million income tax expense resulting from the enactment of higher provincial corporate

income tax rates that was partly offset by a \$7 million income tax recovery resulting from the recapitalization of a foreign investment.

Foreign exchange fluctuations have an impact on the comparability of the results of operations. The fluctuation of the Canadian dollar relative to the US dollar, which affects the conversion of the Company's US dollar-denominated revenues and expenses, resulted in a positive impact to net income of \$33 million (\$0.04 per diluted share) in 2013.

Revenues for the year ended December 31, 2013 increased by \$655 million, or 7%, to \$10,575 million, mainly attributable to freight rate increases; higher freight volumes due to strong energy markets, market share gains, as well as growth in the North American economy; the positive translation impact of the weaker Canadian dollar on US dollar-denominated revenues; and the impact of a higher fuel surcharge, mainly as a result of higher volumes.

Operating expenses for the year ended December 31, 2013 increased by \$467 million, or 7%, to \$6,702 million, mainly due to higher labor and fringe benefits expense; the negative translation impact of the weaker Canadian dollar on US dollar-denominated expenses; and increased purchased services and material expense, in part due to weather-related conditions. These factors were partly offset by lower casualty and other expense.

The operating ratio, defined as operating expenses as a percentage of revenues, was 63.4% in 2013, compared to 62.9% in 2012, a 0.5-point deterioration.

Revenues

In millions, unless otherwise indicated

<i>Year ended December 31,</i>	2013	2012	% Change	% Change at constant currency
Rail freight revenues	\$ 9,587	\$ 8,938	7%	5%
Other revenues	988	982	1%	(1%)
Total revenues	\$ 10,575	\$ 9,920	7%	5%

Rail freight revenues

Petroleum and chemicals	\$ 1,939	\$ 1,640	18%	16%
Metals and minerals	1,216	1,133	7%	5%
Forest products	1,413	1,331	6%	4%
Coal	693	712	(3%)	(4%)
Grain and fertilizers	1,610	1,590	1%	-
Intermodal	2,167	1,994	9%	8%
Automotive	549	538	2%	-
Total rail freight revenues	\$ 9,587	\$ 8,938	7%	5%
Revenue ton miles (RTM) <i>(millions)</i>	210,133	201,496	4%	4%
Rail freight revenue/RTM <i>(cents)</i>	4.56	4.44	3%	1%
Carloads <i>(thousands)</i>	5,190	5,059	3%	3%
Rail freight revenue/carload <i>(dollars)</i>	1,847	1,767	5%	3%

Revenues for the year ended December 31, 2013 totaled \$10,575 million compared to \$9,920 million in 2012. The increase of \$655 million, or 7%, was mainly attributable to freight rate increases; higher freight volumes due to strong energy markets, market share gains, as well as growth in the North American economy; the positive translation impact of the weaker Canadian dollar on US dollar-denominated revenues; and the impact of a higher fuel surcharge of approximately \$35 million, mainly as a result of higher volumes.

In 2013, revenue ton miles (RTM), measuring the relative weight and distance of rail freight transported by the Company, increased by 4% relative to 2012. Rail freight revenue per revenue ton mile, a measurement of yield defined as revenue earned on the movement of a ton of freight over one mile, increased by 3% when compared to 2012, driven by freight rate increases and the positive translation impact of the weaker Canadian dollar, partly offset by an increase in the average length of haul.



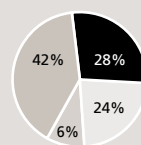
Petroleum and chemicals

<i>Year ended December 31,</i>	2013	2012	% Change	% Change at constant currency
Revenues <i>(millions)</i>	\$ 1,939	\$ 1,640	18%	16%
RTMs <i>(millions)</i>	44,634	37,449	19%	19%
Revenue/RTM <i>(cents)</i>	4.34	4.38	(1%)	(3%)

The petroleum and chemicals commodity group comprises a wide range of commodities, including chemicals and plastics, refined petroleum products, natural gas liquids, crude oil and sulfur. The primary markets for these commodities are within North America, and as such, the performance of this commodity group is closely correlated with the North American economy as well as oil and gas production. Most of the Company's petroleum and chemicals shipments originate in the Louisiana petrochemical corridor between New Orleans and Baton Rouge; in Western Canada, a key oil and gas development area and a major center for natural gas feedstock and world-scale petrochemicals and plastics; and in eastern Canadian regional plants. For the year ended December 31, 2013, revenues for this commodity group increased by \$299 million, or 18%, when compared to 2012. The increase was mainly due to significantly higher crude oil shipments and increased volumes of propane, freight rate increases, the positive translation impact of a weaker Canadian dollar, and a higher fuel surcharge due to longer haul volumes. These factors were partly offset by lower volumes of sulfur and reduced shipments of refined petroleum products due to a customer conversion to pipeline. Revenue per revenue ton mile decreased by 1% in 2013, mainly due to a significant increase in the average length of haul, offset by freight rate increases and the positive translation impact of a weaker Canadian dollar.

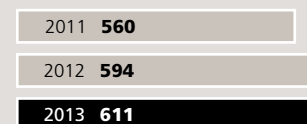
Percentage of revenues

- 42%** Chemicals and plastics
- 28%** Refined petroleum products
- 24%** Crude and condensate
- 6%** Sulfur



Carloads *(thousands)*

Year ended December 31,



Metals and minerals

Year ended December 31,	2013	2012	% Change	% Change at constant currency
Revenues (millions)	\$ 1,216	\$ 1,133	7%	5%
RTMs (millions)	21,342	20,236	5%	5%
Revenue/RTM (cents)	5.70	5.60	2%	(1%)

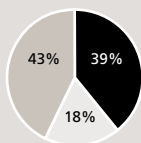


The metals and minerals commodity group consists primarily of materials related to oil and gas development, steel, iron ore, non-ferrous base metals and ores, construction materials and machinery and dimensional (large) loads. The Company provides unique rail access to base metals, iron ore and frac sand mining as well as aluminum and steel producing regions, which are among the most important in North America. This strong origin franchise, coupled with the Company's access to port facilities and the end markets for these commodities, has made CN a leader in the transportation of metals and minerals products. The key drivers for

this market segment are oil and gas development, automotive production, and non-residential construction. For the year ended December 31, 2013, revenues for this commodity group increased by \$83 million, or 7%, when compared to 2012. The increase was mainly due to freight rate increases, higher volumes of frac sand and the positive translation impact of a weaker Canadian dollar. These factors were partly offset by lower shipments of steel products and non-ferrous ores. Revenue per revenue ton mile increased by 2% in 2013, mainly due to freight rate increases and the positive translation impact of a weaker Canadian dollar, partly offset by an increase in the average length of haul, mainly in the fourth quarter.

Percentage of revenues

- 43% Minerals
- 39% Metals
- 18% Iron ore



Carloads (thousands)

Year ended December 31,

2011	1,013
2012	1,024
2013	1,048

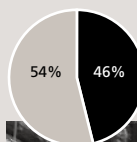
Forest products

Year ended December 31,	2013	2012	% Change	% Change at constant currency
Revenues (millions)	\$ 1,413	\$ 1,331	6%	4%
RTMs (millions)	29,630	29,674	-	-
Revenue/RTM (cents)	4.77	4.49	6%	4%

The forest products commodity group includes various types of lumber, panels, paper, wood pulp and other fibers such as logs, recycled paper, wood chips, and wood pellets. The Company has extensive rail access to the western and eastern Canadian fiber-producing regions, which are among the largest fiber source areas in North America. In the U.S., the Company is strategically located to serve both the midwest and southern U.S. corridors with interline connections to other Class I railroads. The key drivers for the various commodities are: for newsprint, advertising lineage, non-print media and overall economic conditions, primarily in the U.S.; for fibers (mainly wood pulp), the consumption of paper, pulpboard and tissue in North American and offshore markets; and for lumber and panels, housing starts and renovation activities primarily in the U.S. For the year ended December 31, 2013, revenues for this commodity group increased by \$82 million, or 6%, when compared to 2012. The increase was mainly due to freight rate increases, the positive translation impact of a weaker Canadian dollar, and increased shipments of lumber and panels to the U.S. due to an improvement in the housing market. These factors were partly offset by a decrease in shipments of wood pulp, in part due to a mill closure in western Canada. Revenue per revenue ton mile increased by 6% in 2013 mainly due to freight rate increases and the positive translation impact of a weaker Canadian dollar.

Percentage of revenues

- 54% Pulp and paper
- 46% Lumber and panels



Carloads (thousands)

Year ended December 31,

2011	443
2012	445
2013	446





Coal

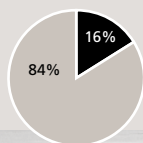
Year ended December 31,	2013	2012	% Change	% Change at constant currency
Revenues (millions)	\$ 693	\$ 712	(3%)	(4%)
RTMs (millions)	22,315	23,570	(5%)	(5%)
Revenue/RTM (cents)	3.11	3.02	3%	2%

The coal commodity group consists of thermal grades of bituminous coal, metallurgical coal and petroleum coke. Canadian thermal and metallurgical coal are largely exported via terminals on the west coast of Canada to offshore markets. In the U.S., thermal coal is transported from mines served in southern Illinois, or from western U.S. mines via interchange with other railroads, to major utilities in the midwest and southeast U.S., as well as offshore markets via terminals in the Gulf and the Port of Prince Rupert. For the year ended December 31, 2013, revenues for this commodity group decreased by \$19 million, or 3%, when compared to 2012. The decrease was mainly due to lower volumes of export thermal coal through west coast ports and reduced shipments of domestic thermal coal to U.S. utilities. These factors were partly offset by higher shipments of export metallurgical coal through west coast ports; freight rate increases; and the positive translation impact of a weaker Canadian dollar. Revenue per revenue ton mile increased by 3% in 2013, mainly due to freight rate increases and the positive translation impact of a weaker Canadian dollar.

Percentage of revenues

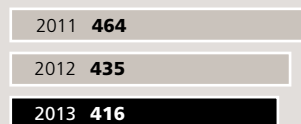
84% Coal

16% Petroleum coke



Carloads (thousands)

Year ended December 31,



Grain and fertilizers

Year ended December 31,	2013	2012	% Change	% Change at constant currency
Revenues (millions)	\$ 1,610	\$ 1,590	1%	-
RTMs (millions)	43,180	45,417	(5%)	(5%)
Revenue/RTM (cents)	3.73	3.50	7%	5%

The grain and fertilizers commodity group depends primarily on crops grown and fertilizers processed in western Canada and the U.S. midwest. The grain segment consists of three primary segments: food grains (mainly wheat, oats and malting barley), feed grains and feed grain products (including feed barley, feed wheat, peas, corn, ethanol and dried distillers grains), and oilseeds and oilseed products (primarily canola seed, oil and meal, and soybeans). Production of grain varies considerably from year to year, affected primarily by weather conditions, seeded and harvested acreage, the mix of grains produced and crop yields. Grain exports are sensitive to the size and quality of the crop produced, international market conditions and foreign government policy. The majority of grain produced in western Canada and moved by CN is exported via the ports of Vancouver, Prince Rupert and Thunder Bay. Certain of these rail movements are subject to government regulation and to a revenue cap, which effectively establishes a maximum revenue entitlement that railways can earn. In the U.S., grain grown in Illinois and Iowa is exported as well as transported to domestic processing facilities and feed markets. The Company also serves major producers of potash in Canada, as well as producers of ammonium nitrate, urea and other fertilizers across Canada and the U.S. For the year ended December 31, 2013, revenues for this commodity group increased by \$20 million, or 1%, when compared to 2012. The increase was mainly due to freight rate increases, greater volumes of potash for offshore export and the positive translation impact of a weaker Canadian dollar. These factors were partly offset by lower shipments of canola and Canadian wheat, mainly for export, and lower volumes of barley. Revenue per revenue ton mile increased by 7% in 2013, mainly due to freight rate increases and the positive translation impact of a weaker Canadian dollar.

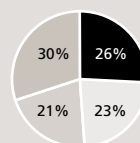
Percentage of revenues

30% Oilseeds

26% Food grains

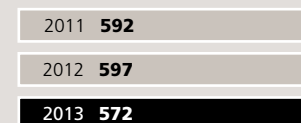
23% Feed grains

21% Fertilizers



Carloads (thousands)

Year ended December 31,





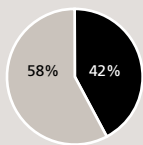
Intermodal

Year ended December 31,	2013	2012	% Change	% Change at constant currency
Revenues (millions)	\$ 2,167	\$ 1,994	9%	8%
RTMs (millions)	46,291	42,396	9%	9%
Revenue/RTM (cents)	4.68	4.70	-	(1%)

The intermodal commodity group is comprised of two segments: domestic and international. The domestic segment transports consumer products and manufactured goods, operating through both retail and wholesale channels, within domestic Canada, domestic U.S., Mexico and transborder, while the international segment handles import and export container traffic, directly serving the major ports of Vancouver, Prince Rupert, Montreal, Halifax and New Orleans. The domestic segment is driven by consumer markets, with growth generally tied to the economy. The international segment is driven by North American economic and trade conditions. For the year ended December 31, 2013, revenues for this commodity group increased by \$173 million, or 9%, when compared to 2012. The increase was mainly due to higher shipments through the Port of Vancouver, in part as a result of new business, and increased volumes of domestic intermodal; the impact of a higher fuel surcharge; the positive translation impact of a weaker Canadian dollar; and freight rate increases. These factors were partly offset by lower volumes through the Port of Prince Rupert. Revenue per revenue ton mile was flat in 2013, mainly due to the positive translation impact of a weaker Canadian dollar and freight rate increases, entirely offset by an increase in the average length of haul.

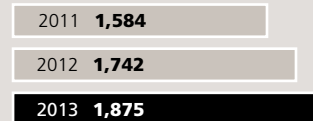
Percentage of revenues

58% International
42% Domestic



Carloads (thousands)

Year ended December 31,



Management's Discussion and Analysis

Automotive

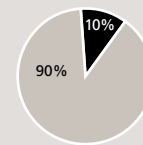
Year ended December 31,	2013	2012	% Change	% Change at constant currency
Revenues (millions)	\$ 549	\$ 538	2%	-
RTMs (millions)	2,741	2,754	-	-
Revenue/RTM (cents)	20.03	19.54	3%	-

The automotive commodity group moves both finished vehicles and parts throughout North America, providing rail access to certain vehicle assembly plants in Canada, and Michigan and Mississippi in the U.S. The Company also serves vehicle distribution facilities in Canada and the U.S., as well as parts production facilities in Michigan and Ontario. The Company serves shippers of import vehicles via the ports of Halifax and Vancouver, and through interchange with other railroads. The Company's automotive revenues are closely correlated to automotive production and sales in North America. For the year ended December 31, 2013, revenues for this commodity group increased by \$11 million, or 2%, when compared to 2012. The increase was mainly due to the positive translation impact of a weaker Canadian dollar and freight rate increases. These factors were partly offset by a non-recurring movement of military equipment in 2012. Revenue per revenue ton mile increased by 3% in 2013, mainly due to the positive translation impact of a weaker Canadian dollar, freight rate increases, and a decrease in the average length of haul.



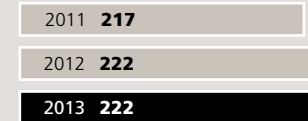
Percentage of revenues

90% Finished vehicles
10% Auto parts



Carloads (thousands)

Year ended December 31,

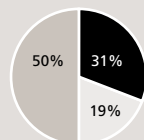


Other revenues

Year ended December 31,	2013	2012	% Change	% Change at constant currency
Revenues (millions)	\$ 988	\$ 982	1%	(1%)

Percentage of revenues

50% Other non-rail services
31% Vessels and docks
19% Interswitching and other revenues



Other revenues are largely derived from non-rail services that support CN's rail business including vessels, docks, warehousing and distribution, automotive logistic services, trucking operations, as well as from other items which include interswitching and commuter train revenues. In 2013, Other revenues amounted to \$988 million, an increase of \$6 million, or 1%, when compared to 2012, mainly due to higher revenues from vessels and docks, partly offset by lower revenues from transportation management services and trucking operations.

Operating expenses

Operating expenses for the year ended December 31, 2013 amounted to \$6,702 million, compared to \$6,235 million in 2012. The increase of \$467 million, or 7%, in 2013 was mainly due to higher labor and fringe benefits expense; the negative translation impact of the weaker Canadian dollar on US dollar-denominated expenses; and increased purchased services and material expense, in part due to weather-related conditions. These factors were partly offset by lower casualty and other expense.

<i>In millions</i>	<i>Year ended December 31,</i>	Percentage of revenues					
		2013	2012	% Change	% Change at constant currency	2013	2012
Labor and fringe benefits		\$ 2,182	\$ 1,952	(12%)	(11%)	20.6%	19.7%
Purchased services and material		1,351	1,248	(8%)	(7%)	12.8%	12.6%
Fuel		1,619	1,524	(6%)	(3%)	15.3%	15.4%
Depreciation and amortization		980	924	(6%)	(5%)	9.3%	9.3%
Equipment rents		275	249	(10%)	(8%)	2.6%	2.5%
Casualty and other		295	338	13%	15%	2.8%	3.4%
<i>Total operating expenses</i>		\$ 6,702	\$ 6,235	(7%)	(6%)	63.4%	62.9%

Labor and fringe benefits: Labor and fringe benefits expense includes wages, payroll taxes, and employee benefits such as incentive compensation, including stock-based compensation; health and welfare; and pension and other postretirement benefits. Certain incentive and stock-based compensation plans are based on financial and market performance targets and the related expense is recorded in relation to the attainment of such targets. Labor and fringe benefits expense increased by \$230 million, or 12%, in 2013 when compared to 2012. The increase was primarily a result of increased pension expense, higher wages due to the impact of a higher workforce level as a result of volume growth and general wage increases, higher incentive compensation, as well as the negative translation impact of the weaker Canadian dollar.

Purchased services and material: Purchased services and material expense primarily includes the cost of services purchased from outside contractors; materials used in the maintenance of the Company's track, facilities and equipment; transportation and lodging for train crew employees; utility costs; and the net costs of operating facilities jointly used by the Company and other railroads. These expenses increased by \$103 million, or 8%, in 2013 when compared to 2012. The increase was mainly due to weather-related conditions impacting materials, crew accommodation and utilities expenses; higher maintenance expenses for track, rolling stock and other equipment; the negative translation impact of the weaker Canadian dollar; and higher costs for third-party non-rail transportation providers.

Fuel: Fuel expense includes fuel consumed by assets, including locomotives, vessels, vehicles and other equipment as well as federal, provincial and state fuel taxes. These expenses increased by \$95 million, or 6%, in 2013 when compared to 2012. The increase was primarily due to higher freight volumes and the negative translation impact of the weaker Canadian dollar. These factors were partly offset by productivity improvements.

Depreciation and amortization: Depreciation and amortization expense relates to the Company's rail and related operations. Depreciation expense is affected by capital additions, railroad property retirements from disposal, sale and/or abandonment and other adjustments including asset impairments. These expenses increased by \$56 million, or 6%, in 2013 when compared to 2012. The increase was mainly due to the impact of net capital additions, some asset impairments, as well as the effect of a depreciation study on certain U.S. track and roadway properties, which were partly offset by the effect of a depreciation study on Canadian track and roadway properties. See the section of this MD&A entitled Critical accounting policies for additional information relating to the depreciation studies.

Equipment rents: Equipment rents expense includes rental expense for the use of freight cars owned by other railroads or private companies and for the short- or long-term lease of freight cars, locomotives and intermodal equipment, net of rental income from other railroads for the use of the Company's cars and locomotives. These expenses increased by \$26 million, or 10%, in 2013 when compared to 2012. The increase was primarily due to higher lease costs for intermodal equipment on account of volume increases, higher net car hire expenses, and the negative translation impact of the weaker Canadian dollar.

Casualty and other: Casualty and other expense includes expenses for personal injuries, environmental, freight and property damage, insurance, bad debt, operating taxes, and travel expenses. These expenses decreased by \$43 million, or 13%, in 2013 when compared to 2012. The decrease was mainly due to a reduction to the liability for U.S. legal claims pursuant to an actuarial valuation, as well as overall lower legal expenses; lower environmental expenses; and lower workers' compensation expenses; that were partly offset by the negative translation impact of the weaker Canadian dollar.

Other

Interest expense: In 2013, interest expense was \$357 million compared to \$342 million in 2012. The increase was mainly due to a higher level of debt and the negative translation impact of the weaker Canadian dollar on US dollar-denominated interest expense, partly offset by a lower weighted-average interest rate.

Other income: In 2013, the Company recorded other income of \$73 million compared to \$315 million in 2012. Included in Other income for 2013 was a gain on exchange of easements in the amount of \$29 million and a gain on disposal of the Lakeshore West of \$40 million. Included in Other income for 2012 was a gain on disposal of the Bala-Oakville of \$281 million.

Income tax expense: The Company recorded income tax expense of \$977 million for the year ended December 31, 2013 compared to \$978 million in 2012. The 2013 figure includes a net income tax recovery of \$7 million which consisted of a \$15 million income tax recovery from the recognition of U.S. state income tax losses and a \$16 million income tax recovery from a revision of the apportionment of U.S. state income taxes which were partly offset by a combined \$24 million income tax expense resulting from the enactment of higher provincial corporate income tax rates. Included in the 2012 figure was a net income tax expense of \$28 million, which consisted of a \$35 million income tax expense resulting from the enactment of higher provincial corporate income tax rates that was partly offset by a \$7 million income tax recovery resulting from the recapitalization of a foreign investment. The effective tax rate for 2013 was 27.2% compared to 26.7% in 2012.

2012 compared to 2011

In 2012, net income was \$2,680 million, an increase of \$223 million, or 9%, when compared to 2011, with diluted earnings per share increasing 13% to \$3.06.

Included in the 2012 figures was a gain on disposal of a segment of the Bala and a segment of the Oakville subdivisions (collectively the "Bala-Oakville") of \$281 million, or \$252 million after-tax (\$0.28 per diluted share); and a net income tax expense of \$28 million (\$0.03 per diluted share) consisting of a \$35 million income tax expense resulting from the enactment of higher provincial corporate income tax rates that was partly offset by a \$7 million income tax recovery resulting from the recapitalization of a foreign investment. Included in the 2011 figures were gains on disposal of substantially all of the assets of IC RailMarine Terminal Company ("IC RailMarine") of \$60 million, or \$38 million after-tax (\$0.04 per diluted share) and of a segment of the Kingston subdivision known as the Lakeshore East of \$288 million, or \$254 million after-tax (\$0.28 per diluted share). The 2011 figures also included a net income tax expense of \$40 million (\$0.04 per diluted share) resulting from the enactment of state corporate income tax rate changes and other legislated state tax revisions and an income tax recovery of \$11 million (\$0.01 per diluted share) relating to certain fuel costs attributed to various wholly-owned subsidiaries' fuel consumption in prior periods.

Foreign exchange fluctuations continue to have an impact on the comparability of the results of operations. The fluctuation of the Canadian dollar relative to the US dollar, which affects the conversion of the Company's US dollar-denominated revenues and expenses, resulted in a positive impact to net income of \$11 million (\$0.01 per diluted share) in 2012.

Revenues for the year ended December 31, 2012 increased by \$892 million, or 10%, to \$9,920 million, mainly attributable to higher freight volumes, due in part to growth in North American and Asian economies, and the Company's performance above market conditions in a number of segments, as well as increased volumes in the second quarter as a result of a labor disruption at a key competitor; freight rate increases; the impact of a higher fuel surcharge as a result of year-over-year increases in applicable fuel prices and higher volumes; and the positive translation impact of the weaker Canadian dollar on US dollar-denominated revenues.

Operating expenses for the year ended December 31, 2012 increased by \$503 million, or 9%, to \$6,235 million, mainly due to higher labor and fringe benefits expense, increased purchased services and material expense, as well as increased fuel costs.

The operating ratio, defined as operating expenses as a percentage of revenues, was 62.9% in 2012, compared to 63.5% in 2011, a 0.6-point improvement.

Revenues
In millions, unless otherwise indicated

<i>Year ended December 31,</i>	2012	2011	% Change	% Change at constant currency
Rail freight revenues	\$ 8,938	\$ 8,111	10%	10%
Other revenues	982	917	7%	6%
Total revenues	\$ 9,920	\$ 9,028	10%	9%
Rail freight revenues				
Petroleum and chemicals	\$ 1,640	\$ 1,420	15%	15%
Metals and minerals	1,133	1,006	13%	12%
Forest products	1,331	1,270	5%	4%
Coal	712	618	15%	15%
Grain and fertilizers	1,590	1,523	4%	4%
Intermodal	1,994	1,790	11%	11%
Automotive	538	484	11%	10%
Total rail freight revenues	\$ 8,938	\$ 8,111	10%	10%
Revenue ton miles (RTM) (millions)	201,496	187,753	7%	7%
Rail freight revenue/RTM (cents)	4.44	4.32	3%	2%
Carloads (thousands)	5,059	4,873	4%	4%
Rail freight revenue/carload (dollars)	1,767	1,664	6%	6%

Revenues for the year ended December 31, 2012 totaled \$9,920 million compared to \$9,028 million in 2011. The increase of \$892 million, or 10%, was mainly attributable to higher freight volumes, due in part to growth in North American and Asian economies, and the Company's performance above market conditions in a number of segments, as well as increased volumes in the second quarter as a result of a labor disruption at a key competitor; freight rate increases; the impact of a higher fuel surcharge of approximately \$140 million, as a result of year-over-year increases in applicable fuel prices and higher volumes; and the positive translation impact of the weaker Canadian dollar on US dollar-denominated revenues.

In 2012, revenue ton miles increased by 7% relative to 2011. Rail freight revenue per revenue ton mile increased by 3% when compared to 2011, driven by freight rate increases, the impact of a higher fuel surcharge, and the positive translation impact of the weaker Canadian dollar. These factors were partly offset by an increase in the average length of haul.

Petroleum and chemicals

<i>Year ended December 31,</i>	2012	2011	% Change	% Change at constant currency
Revenues (millions)	\$ 1,640	\$ 1,420	15%	15%
RTMs (millions)	37,449	32,962	14%	14%
Revenue/RTM (cents)	4.38	4.31	2%	1%

For the year ended December 31, 2012, revenues for this commodity group increased by \$220 million, or 15%, when compared to 2011. The increase was mainly due to higher shipments of crude oil, propane, condensate, petroleum lubricants, and asphalt; freight rate increases; a higher fuel surcharge; and the positive translation impact of a weaker Canadian dollar. These gains were partly offset by lower volumes of molten sulfur to the U.S. market and reduced shipments of gasoline and diesel. Revenue per revenue ton mile increased by 2% in 2012, mainly due to freight rate increases, a higher fuel surcharge and the positive translation impact of a weaker Canadian dollar, partly offset by a significant increase in the average length of haul.

Metals and minerals

<i>Year ended December 31,</i>	2012	2011	% Change	% Change at constant currency
Revenues (millions)	\$ 1,133	\$ 1,006	13%	12%
RTMs (millions)	20,236	18,899	7%	7%
Revenue/RTM (cents)	5.60	5.32	5%	4%

For the year ended December 31, 2012, revenues for this commodity group increased by \$127 million, or 13%, when compared to 2011. The increase was mainly due to greater shipments of materials supporting oil and gas development, increased volumes of machinery and dimensional loads, steel products, and industrial materials; freight rate increases; a higher fuel surcharge; and the positive translation impact of a weaker Canadian dollar. These gains were partly offset by lower volumes of non-ferrous metals and iron ore. Revenue per revenue ton mile increased by 5% in 2012, mainly due to freight rate increases, a higher fuel surcharge, and the positive translation impact of a weaker Canadian dollar, partly offset by an increase in the average length of haul.

Forest products

<i>Year ended December 31,</i>	2012	2011	% Change	% Change at constant currency
Revenues (millions)	\$ 1,331	\$ 1,270	5%	4%
RTMs (millions)	29,674	29,336	1%	1%
Revenue/RTM (cents)	4.49	4.33	4%	3%

For the year ended December 31, 2012, revenues for this commodity group increased by \$61 million, or 5%, when compared to 2011. The increase was mainly due to freight rate increases, a higher fuel surcharge, the positive translation impact of a weaker Canadian dollar and increased shipments of lumber and panels to the U.S. market. These factors were partly offset by reduced

paper shipments due to mill closures and curtailments, as well as decreased shipments of lumber for offshore export. Revenue per revenue ton mile increased by 4% in 2012, mainly due to freight rate increases, a higher fuel surcharge, and the positive translation impact of a weaker Canadian dollar.

Coal

<i>Year ended December 31,</i>	2012	2011	% Change	% Change at constant currency
Revenues (<i>millions</i>)	\$ 712	\$ 618	15%	15%
RTMs (<i>millions</i>)	23,570	19,980	18%	18%
Revenue/RTM (<i>cents</i>)	3.02	3.09	(2%)	(3%)

For the year ended December 31, 2012, revenues for this commodity group increased by \$94 million, or 15%, when compared to 2011. The increase was mainly due to higher volumes of U.S. thermal coal to the Gulf and west coast ports, Canadian petroleum coke and metallurgical coal for offshore export; freight rate increases; a higher fuel surcharge; and the positive translation impact of a weaker Canadian dollar. These factors were partly offset by reduced volumes of thermal coal to U.S. utilities. Revenue per revenue ton mile decreased by 2% in 2012, due to a significant increase in the average length of haul, partly offset by freight rate increases, a higher fuel surcharge and the positive translation impact of a weaker Canadian dollar.

Grain and fertilizers

<i>Year ended December 31,</i>	2012	2011	% Change	% Change at constant currency
Revenues (<i>millions</i>)	\$ 1,590	\$ 1,523	4%	4%
RTMs (<i>millions</i>)	45,417	45,468	-	-
Revenue/RTM (<i>cents</i>)	3.50	3.35	4%	4%

For the year ended December 31, 2012, revenues for this commodity group increased by \$67 million, or 4%, when compared to 2011. The increase was mainly due to freight rate increases; a higher fuel surcharge; higher volumes of Canadian wheat exports, U.S. soybean product exports to the Gulf, and Canadian barley to the U.S.; and the positive translation impact of a weaker Canadian dollar. These gains were partly offset by lower volumes of corn, peas, and ethanol. Revenue per revenue ton mile increased by 4% in 2012, mainly due to freight rate increases, a higher fuel surcharge and the positive translation impact of a weaker Canadian dollar.

Intermodal

<i>Year ended December 31,</i>	2012	2011	% Change	% Change at constant currency
Revenues (<i>millions</i>)	\$ 1,994	\$ 1,790	11%	11%
RTMs (<i>millions</i>)	42,396	38,563	10%	10%
Revenue/RTM (<i>cents</i>)	4.70	4.64	1%	1%

For the year ended December 31, 2012, revenues for this commodity group increased by \$204 million, or 11%, when compared to 2011. The increase was mainly due to higher shipments through the west coast ports and increased volumes of domestic shipments of consumer and industrial products; a higher fuel surcharge; freight rate increases; and the positive translation impact of a weaker Canadian dollar. Revenue per revenue ton mile increased by 1% in 2012, mainly due to a higher fuel surcharge, freight rate increases and the positive translation impact of a weaker Canadian dollar.

Automotive

<i>Year ended December 31,</i>	2012	2011	% Change	% Change at constant currency
Revenues (<i>millions</i>)	\$ 538	\$ 484	11%	10%
RTMs (<i>millions</i>)	2,754	2,545	8%	8%
Revenue/RTM (<i>cents</i>)	19.54	19.02	3%	2%

For the year ended December 31, 2012, revenues for this commodity group increased by \$54 million, or 11%, when compared to 2011. The increase was mainly due to higher volumes of imported finished vehicles via the Port of Vancouver and spot moves of military equipment; freight rate increases; a higher fuel surcharge; and the positive translation impact of a weaker Canadian dollar. Revenue per revenue ton mile increased by 3% in 2012, mainly due to freight rate increases, a higher fuel surcharge and the positive translation impact of a weaker Canadian dollar, partly offset by an increase in the average length of haul.

Other revenues

<i>Year ended December 31,</i>	2012	2011	% Change	% Change at constant currency
Revenues (<i>millions</i>)	\$ 982	\$ 917	7%	6%

In 2012, Other revenues amounted to \$982 million, an increase of \$65 million, or 7%, when compared to 2011, mainly due to higher revenues from freight forwarding and transportation management, vessels and docks, intermodal trucking, and warehousing and distribution, partly offset by the loss of revenues due to the sale of IC RailMarine in August 2011 and lower commuter train revenues.

Operating expenses

Operating expenses for the year ended December 31, 2012 amounted to \$6,235 million, compared to \$5,732 million in 2011. The increase of \$503 million, or 9%, in 2012 was mainly due to higher labor and fringe benefits expense, increased purchased services and material expense, as well as increased fuel costs.

<i>In millions</i>	<i>Year ended December 31,</i>	Percentage of revenues					
		2012	2011	% Change	% Change at constant currency	2012	2011
Labor and fringe benefits		\$ 1,952	\$ 1,812	(8%)	(7%)	19.7%	20.1%
Purchased services and material		1,248	1,120	(11%)	(11%)	12.6%	12.4%
Fuel		1,524	1,412	(8%)	(7%)	15.4%	15.6%
Depreciation and amortization		924	884	(5%)	(4%)	9.3%	9.8%
Equipment rents		249	228	(9%)	(8%)	2.5%	2.5%
Casualty and other		338	276	(22%)	(22%)	3.4%	3.1%
<i>Total operating expenses</i>		\$ 6,235	\$ 5,732	(9%)	(8%)	62.9%	63.5%

Labor and fringe benefits: Labor and fringe benefits expense increased by \$140 million, or 8%, in 2012 when compared to 2011. The increase was primarily a result of the impact of a higher workforce level due to volume growth, and general wage increases; and increased pension expense; which were offset by the recognition of a net settlement gain from the termination of the former Chief Executive Officer's retirement benefit plan in the fourth quarter of 2012.

Purchased services and material: Purchased services and material expense increased by \$128 million, or 11%, in 2012 when compared to 2011. The increase was mainly due to higher expenses for contracted services and for third-party non-rail transportation services as a result of higher volumes; as well as higher maintenance expenses for track, rolling stock and other equipment. These factors were partly offset by lower accident-related expenses; as well as reduced expenses for snow removal and utilities, primarily as a result of milder winter conditions at the beginning of the year.

Fuel: Fuel expense increased by \$112 million, or 8%, in 2012 when compared to 2011. The increase was primarily due to higher freight volumes and a higher average price for fuel, which were partly offset by productivity improvements.

Depreciation and amortization: Depreciation and amortization expense increased by \$40 million, or 5%, in 2012 when compared to 2011. The increase was mainly due to the impact of net capital additions.

Equipment rents: Equipment rents expense increased by \$21 million, or 9%, in 2012 when compared to 2011. The increase was due to increased lease expenses on account of volume increases, as well as higher car hire expenses.

Casualty and other: Casualty and other expense increased by \$62 million, or 22%, in 2012 when compared to 2011. The increase was mainly due to increased provisions for environmental and legal expenses, higher property taxes and workers' compensation expenses pursuant to an actuarial study, which were partly offset by lower expenses for loss and damage claims.

Other

Interest expense: In 2012, interest expense was \$342 million compared to \$341 million in 2011. The increase was mainly due to the issuance of a higher level of debt with a lower interest rate and the negative translation impact of the weaker Canadian dollar on US dollar-denominated interest expense, which were offset by a repayment of debt with a higher interest rate.

Other income: In 2012, the Company recorded other income of \$315 million compared to \$401 million in 2011. Included in Other income for 2012 was a gain on disposal of the Bala-Oakville of \$281 million compared to gains on disposal of substantially all of the assets of IC RailMarine of \$60 million and the Lakeshore East of \$288 million in 2011.

Income tax expense: The Company recorded income tax expense of \$978 million for the year ended December 31, 2012 compared to \$899 million in 2011. The 2012 figure includes a net income tax expense of \$28 million, which consisted of a \$35 million income tax expense resulting from the enactment of higher provincial corporate income tax rates that was partly offset by a \$7 million income tax recovery resulting from the recapitalization of a foreign investment. Included in the 2011 figure was a net income tax expense of \$40 million, resulting from the enactment of state corporate income tax rate changes and other legislated state tax revisions, and an income tax recovery of \$11 million relating to certain fuel costs attributed to various wholly-owned subsidiaries' fuel consumption in prior periods. The effective tax rate for 2012 was 26.7% compared to 26.8% in 2011.

Summary of quarterly financial data

In millions, except per share data

	2013 Quarters				2012 Quarters			
	Fourth	Third	Second	First	Fourth	Third	Second	First
Revenues	\$ 2,745	\$ 2,698	\$ 2,666	\$ 2,466	\$ 2,534	\$ 2,497	\$ 2,543	\$ 2,346
Operating income	\$ 967	\$ 1,084	\$ 1,042	\$ 780	\$ 922	\$ 985	\$ 985	\$ 793
Net income	\$ 635	\$ 705	\$ 717	\$ 555	\$ 610	\$ 664	\$ 631	\$ 775
Basic earnings per share	\$ 0.76	\$ 0.84	\$ 0.85	\$ 0.65	\$ 0.71	\$ 0.77	\$ 0.72	\$ 0.88
Diluted earnings per share	\$ 0.76	\$ 0.84	\$ 0.84	\$ 0.65	\$ 0.71	\$ 0.76	\$ 0.72	\$ 0.87
Dividend declared per share	\$ 0.2150	\$ 0.2150	\$ 0.2150	\$ 0.2150	\$ 0.1875	\$ 0.1875	\$ 0.1875	\$ 0.1875

Revenues generated by the Company during the year are influenced by seasonal weather conditions, general economic conditions, cyclical demand for rail transportation, and competitive forces in the transportation marketplace (see the section of this MD&A entitled Business risks). Operating expenses reflect the impact of freight volumes, seasonal weather conditions, labor costs, fuel prices, and the Company's productivity initiatives. Fluctuations in the Canadian dollar relative to the US dollar have also affected the conversion of the Company's US dollar-denominated revenues and expenses and resulted in fluctuations in net income in the rolling eight quarters presented above.

The Company's quarterly results include items that impacted the quarter-over-quarter comparability of the results of operations as discussed below:

In millions, except per share data

	2013 Quarters				2012 Quarters			
	Fourth	Third	Second	First	Fourth	Third	Second	First
Income tax expenses ⁽¹⁾	\$ -	\$ (19)	\$ (5)	\$ -	\$ -	\$ -	\$ (28)	\$ -
After-tax gain on disposal of property ^{(2) (3) (4)}	-	-	18	36	-	-	-	252
<i>Impact on net income</i>	\$ -	\$ (19)	\$ 13	\$ 36	\$ -	\$ -	\$ (28)	\$ 252
Impact on basic earnings per share	\$ -	\$ (0.02)	\$ 0.01	\$ 0.04	\$ -	\$ -	\$ (0.03)	\$ 0.29
Impact on diluted earnings per share	\$ -	\$ (0.02)	\$ 0.01	\$ 0.04	\$ -	\$ -	\$ (0.03)	\$ 0.28

(1) Income tax expenses resulted mainly from the enactment of provincial corporate income tax rate changes and the recapitalization of a foreign investment.

(2) The Company entered into an exchange of easements without monetary consideration. A gain on disposal of \$29 million (\$18 million after-tax) was recognized in Other income.

(3) The Company sold the Lakeshore West for \$52 million. A gain on disposal of \$40 million (\$36 million after-tax) was recognized in Other income.

(4) The Company sold the Bala-Oakville for \$311 million. A gain on disposal of \$281 million (\$252 million after-tax) was recognized in Other income.

Summary of fourth quarter 2013 compared to corresponding quarter in 2012

Fourth quarter 2013 net income was \$635 million, an increase of \$25 million, or 4%, when compared to the same period in 2012, with diluted earnings per share rising 7% to \$0.76.

Foreign exchange fluctuations have an impact on the comparability of the results of operations. The fluctuation of the Canadian dollar relative to the US dollar, which affects the conversion of the Company's US dollar-denominated revenues and expenses, resulted in a positive impact of \$18 million (\$0.02 per diluted share) to fourth-quarter 2013 net income.

Revenues for the fourth quarter of 2013 increased by \$211 million, or 8%, to \$2,745 million, when compared to the same period in 2012. The increase was mainly attributable to higher freight volumes due to strong energy markets, market share gains, as well as growth in the North American economy; the positive translation impact of the weaker Canadian dollar on US dollar-denominated revenues; freight rate increases; and the impact of a higher fuel surcharge, as a result of higher volumes and year-over-year increases in applicable fuel prices.

Operating expenses for the fourth quarter of 2013 increased by \$166 million, or 10%, to \$1,778 million, when compared to the same period in 2012. The increase was primarily due to higher labor and fringe benefits expense as a result of increased pension expense and higher incentive compensation; the negative translation impact of the weaker Canadian dollar on US dollar-denominated expenses; and increased purchased services and material expense, in part due to weather-related conditions. These factors were partly offset by lower casualty and other expense.

The operating ratio was 64.8% in the fourth quarter of 2013 compared to 63.6% in the fourth quarter of 2012, a 1.2-point deterioration.

Financial position

The following tables provide an analysis of the Company's balance sheet as at December 31, 2013 as compared to 2012. Assets and liabilities denominated in US dollars have been translated to Canadian dollars using the foreign exchange rate in effect at the balance sheet date. As at December 31, 2013 and 2012, the foreign exchange rate was \$1.0636 per US\$1.00 and \$0.9949 per US\$1.00, respectively.

<i>In millions</i>	<i>As at December 31,</i>	2013	2012	Foreign exchange impact	Variance excluding foreign exchange	Explanation of variance, other than foreign exchange impact
Total assets		\$ 30,163	\$ 26,659	\$ 789	\$ 2,715	
Variance mainly due to:						
Properties		\$ 26,227	\$ 24,541	\$ 707	\$ 979	Increase primarily due to gross property additions of \$2,017 million, partly offset by depreciation of \$979 million.
Intangible and other assets		\$ 1,959	\$ 249	\$ 8	\$ 1,702	Increase primarily due to the increase in pension asset of \$1,662 million.
Total liabilities		\$ 17,210	\$ 15,641	\$ 747	\$ 822	
Variance mainly due to:						
Accounts payable and other		\$ 1,477	\$ 1,626	\$ 37	\$ (186)	Decrease primarily due to lower income and other taxes of \$201 million.
Deferred income taxes		\$ 6,537	\$ 5,555	\$ 226	\$ 756	Increase due to deferred income tax expense of \$331 million recorded in Net income excluding recognized tax benefits and deferred income tax expense of \$414 million recorded in Other comprehensive loss.
Pension and other postretirement benefits, net of current portion		\$ 541	\$ 784	\$ 11	\$ (254)	Decrease due primarily to the increase in the year-end discount rate from 4.15% in 2012 to 4.73% in 2013.
Total long-term debt, including the current portion		\$ 7,840	\$ 6,900	\$ 450	\$ 490	Increase primarily due to debt issuances of \$1,850 million, partly offset by debt repayments of \$1,413 million.

<i>In millions</i>	<i>As at December 31,</i>	2013	2012	Variance	Explanation of variance
Total shareholders' equity		\$ 12,953	\$ 11,018	\$ 1,935	
Variance mainly due to:					
Common shares		\$ 4,015	\$ 4,108	\$ (93)	Decrease due to share repurchase programs of \$133 million, partly offset by issuances of common shares of \$40 million upon the exercise of stock options and other.
Accumulated other comprehensive loss		\$ (1,850)	\$ (3,257)	\$ 1,407	Decrease in comprehensive loss due to after-tax amounts of \$1,302 million due to the improvement of the funded status of the Company's pension and other postretirement benefit plans and \$105 million for foreign exchange gains.
Retained earnings		\$ 10,788	\$ 10,167	\$ 621	Increase due to current year net income of \$2,612 million partly offset by share repurchase programs of \$1,267 million and dividends paid of \$724 million.

Liquidity and capital resources

The Company's principal source of liquidity is cash generated from operations and is supplemented by borrowings in the money markets and capital markets. In addition, from time to time, the Company's liquidity requirements can be supplemented by the disposal of surplus properties and the monetization of assets. The strong focus on cash generation from all sources gives the Company increased flexibility in terms of its financing requirements. As part of its financing strategy, the Company regularly reviews its optimal capital structure, cost of capital, and the need for additional debt financing, and considers from time to time the feasibility of dividend increases and share repurchases.

To meet short-term liquidity needs, the Company has a commercial paper program, which is backstopped by its revolving credit facility, expiring on May 5, 2018. Access to commercial paper is dependent on market conditions. If the Company were to lose access to its commercial paper program for an extended period of time, the Company could rely on its \$800 million revolving credit facility to meet its short-term liquidity needs. The Company also has a \$450 million accounts receivable securitization program that can be used to meet its liquidity needs. See the section of this MD&A entitled Available financing arrangements for additional information.

The Company has at times had working capital deficits which are considered common in the rail industry because it is capital-intensive, and such deficits are not an indication of a lack of liquidity. The Company maintains adequate resources to meet daily cash requirements, and has sufficient financial capacity to manage its day-to-day cash requirements and current obligations. As at December 31, 2013 and December 31, 2012, the Company had Cash and cash equivalents of \$214 million and \$155 million, respectively, Restricted cash and cash equivalents of \$448 million and \$521 million, respectively, and a working capital deficit of \$521 million and \$334 million, respectively. The cash and cash equivalents pledged as collateral for a minimum term of one month pursuant to the Company's bilateral letter of credit facilities are recorded as Restricted cash and cash equivalents. See the section of this MD&A entitled Available financing arrangements for additional information. There are currently no specific requirements relating to working capital other than in the normal course of business as discussed herein.

The Company's access to long-term funds in the debt capital markets depends on its credit rating and market conditions. The Company believes that it continues to have access to the long-term debt capital markets. If the Company were unable to borrow funds at acceptable rates in the long-term debt capital markets, the Company could borrow under its revolving credit facility, draw down on its accounts receivable securitization program, raise cash by disposing of surplus properties or otherwise monetizing assets, reduce discretionary spending or take a combination of these measures to assure that it has adequate funding for its business.

The Company's U.S. and other foreign subsidiaries hold cash to meet their respective operational requirements. The Company can decide to repatriate funds associated with either undistributed earnings or the liquidation of its foreign operations, including its U.S. and other foreign subsidiaries. Such repatriation of funds would not cause significant tax implications to the Company under the tax treaties currently in effect between Canada and the U.S. and other foreign tax jurisdictions. Therefore, the impact on liquidity resulting from the repatriation of funds held outside Canada would not be significant.

Operating activities

<i>In millions</i>	<i>Year ended December 31,</i>	2013	2012	Variance
Net cash receipts from customers and other		\$ 10,640	\$ 9,877	\$ 763
Net cash payments for:				
Employee services, suppliers and other expenses		(5,558)	(5,241)	(317)
Interest		(344)	(364)	20
Personal injury and other claims		(61)	(79)	18
Pensions		(239)	(844)	605
Income taxes		(890)	(289)	(601)
Net cash provided by operating activities		\$ 3,548	\$ 3,060	\$ 488

Net cash receipts from customers and other increased mainly due to higher revenues. Payments for employee services, suppliers and other expenses increased principally due to higher payments for labor and fringe benefits and increased fuel costs.

Company contributions to its various pension plans are made in accordance with the applicable legislation in Canada and the U.S. and are determined by actuarial valuations. Actuarial valuations are generally required on an annual basis both in Canada and the U.S. The latest actuarial valuations for funding purposes for the Company's Canadian pension plans, based on a valuation date of December 31, 2012, were filed in June 2013 and identified a going-concern surplus of approximately \$1.4 billion, and a solvency deficit of approximately \$2.1 billion calculated using the three-year average of the Company's hypothetical wind-up ratio in accordance with the *Pension Benefit Standards Regulations, 1985*. The Company's next actuarial valuations required as at December 31, 2013 will be performed in 2014. These actuarial valuations are expected to identify a going-concern surplus of approximately \$1.7 billion, while on a solvency basis a funding deficit of approximately \$1.7 billion is expected due to the level interest rates applicable at their respective measurement dates. Under Canadian

legislation, the solvency deficit is required to be funded through special solvency payments, for which each annual amount is equal to one fifth of the solvency deficit, and is re-established at each valuation date.

In anticipation of its future funding requirements, the Company may occasionally make voluntary contributions in excess of the required contributions mainly to strengthen the financial position of its main pension plan, the CN Pension Plan. The Company has been advised by the Office of the Superintendent of Financial Institutions (OSFI) that voluntary contributions can be treated as a prepayment against the Company's required special solvency payments and as at December 31, 2013, the Company had approximately \$470 million of accumulated prepayments which remain available to offset future required solvency deficit payments. Pension contributions made in 2013 and 2012 of \$226 million and \$833 million, respectively, mainly represent contributions to the Company's main pension plan, the CN Pension Plan and include voluntary contributions of \$100 million and \$700 million, respectively. The pension contributions also include contributions for the current service cost as determined under the Company's current actuarial valuations for funding purposes.

Additional information relating to the pension plans is provided in Note 11 – Pensions and other postretirement benefits to the Company's 2013 Annual Consolidated Financial Statements.

Net income tax payments increased in 2013 mainly due to a higher final payment for the 2012 fiscal year of \$208 million, made in February 2013, and increased installments for the 2013 fiscal year. In 2014, net income tax payments are expected to be approximately \$800 million.

The Company expects cash from operations and its other sources of financing to be sufficient to meet its funding obligations.

Investing activities

<i>In millions</i>	<i>Year ended December 31,</i>	2013	2012	Variance
Net cash used in investing activities		\$ 1,852	\$ 1,421	\$ (431)

The Company's investing activities in 2013 included property additions of \$1,973 million and cash proceeds of \$52 million from the disposal of the Lakeshore West. Investing activities in 2012 included property additions of \$1,731 million and cash proceeds of \$311 million from the disposal of the Bala-Oakville. See the section of this MD&A entitled Disposal of property for additional information.

The following table details property additions for the years ended December 31, 2013 and 2012:

<i>In millions</i>	<i>Year ended December 31,</i>	
	2013	2012
Track and roadway	\$ 1,400	\$ 1,351
Rolling stock	286	206
Buildings	104	66
Information technology	130	125
Other	97	77
Gross property additions	2,017	1,825
Less: Capital leases ⁽¹⁾	44	94
Property additions	\$ 1,973	\$ 1,731

(1) During 2013, the Company recorded \$44 million in assets it acquired through equipment leases (\$94 million in 2012), for which an equivalent amount was recorded in debt.

On an ongoing basis, the Company invests in capital expenditure programs for the renewal of the basic track infrastructure, the acquisition of rolling stock and other investments to take advantage of growth opportunities and to improve the Company's productivity and the fluidity of its network.

Expenditures are generally capitalized if they meet a minimum level of activity, extend the life of the asset or provide future benefits such as increased revenue-generating capacity, functionality, or physical or service capacity. For Track and roadway properties,

expenditures to replace and/or upgrade the basic track infrastructure are generally planned and programmed in advance and carried out by the Company's engineering workforce. In both 2013 and 2012, approximately 90% of the Track and roadway capital expenditures were incurred to renew the basic track infrastructure.

Expenditures relating to the Company's properties that do not meet the Company's capitalization criteria are considered normal repairs and maintenance and are expensed. In 2013, approximately 20% of the Company's total operating expenses were for such expenditures (approximately 20% in both 2012 and 2011). For Track and roadway properties, normal repairs and maintenance include but are not limited to spot tie replacement, spot or broken rail replacement, physical track inspection for detection of rail defects and minor track corrections, and other general maintenance of track structure.

For 2014, the Company expects to invest approximately \$2.1 billion on its capital programs, of which over \$1.2 billion is targeted towards track infrastructure to continue to operate a safe railway and to improve the productivity and fluidity of the network. Implementation costs associated with the U.S. federal government legislative requirement to implement Positive Train Control (PTC) by 2015 will amount to approximately US\$335 million, of which approximately US\$62 million has been spent at the end of 2013.

Free cash flow

Free cash flow does not have any standardized meaning prescribed by GAAP and therefore, may not be comparable to similar measures presented by other companies. The Company believes that free cash flow is a useful measure of performance as it demonstrates the Company's ability to generate cash. In the past, the Company defined free cash flow as the difference between net cash provided by operating activities and net cash used in investing activities; adjusted for changes in restricted cash and cash equivalents, the payment of dividends, changes in cash and cash equivalents resulting from foreign exchange fluctuations, and the impact of major acquisitions, if any.

Beginning with the fourth quarter of 2013, the Company has redefined its free cash flow measure as the difference between net cash provided by operating activities and net cash used in investing activities; adjusted for changes in restricted cash and cash equivalents and the impact of major acquisitions, if any. The Company believes that free cash flow, as redefined, is a better measure of the Company's available cash for debt obligations and for discretionary uses such as payment of dividends and strategic opportunities.

<i>In millions</i>	<i>Year ended December 31,</i>	2013	2012
Net cash provided by operating activities		\$ 3,548	\$ 3,060
Net cash used in investing activities		(1,852)	(1,421)
Net cash provided before financing activities		1,696	1,639
<i>Adjustment:</i>			
Change in restricted cash and cash equivalents		(73)	22
Free cash flow		\$ 1,623	\$ 1,661
Dividends paid		(724)	(652)
Effect of foreign exchange fluctuations on US dollar-denominated cash and cash equivalents		19	(3)
Free cash flow – as previously defined		\$ 918	\$ 1,006

Financing activities

<i>In millions</i>	<i>Year ended December 31,</i>	2013	2012	Variance
Net cash used in financing activities		\$ 1,656	\$ 1,582	\$ (74)

Beginning with the fourth quarter of 2013, in order to better reflect the net cash used in financing activities, the issuances and repayments of commercial paper, all of which have a maturity of three months or less, which were previously reported on a gross basis, are now shown on a net basis.

In 2013, the Company made issuances and repayments of debt of \$1,850 million and \$1,413 million, respectively. In March 2013, the Company, through a wholly-owned subsidiary, repurchased 85% of the 4.40% Notes due March 15, 2013, with a carrying value of US\$340 million pursuant to a tender offer for a total cost of US\$341 million, including consent payments. The remaining 15% of the 4.40% Notes with carrying value of US\$60 million

were paid upon maturity. In November 2013, under its previous shelf prospectus and registration statement, the Company issued US\$350 million (C\$365 million) floating rate Notes due 2015 and US\$250 million (C\$260 million) 4.50% Notes due 2043 in the U.S. capital markets, which resulted in net proceeds of US\$592 million (C\$617 million), intended for general corporate purposes, including the redemption and refinancing of outstanding indebtedness.

In 2012, the Company made issuances and repayments of debt of \$493 million and \$140 million, respectively. In November 2012, under its previous shelf prospectus and registration statement, the Company issued US\$250 million (C\$249 million) 2.25% Notes due 2022 and US\$250 million (C\$249 million) 3.50% Notes due 2042 in the U.S. capital markets, which resulted in net proceeds of US\$494 million (C\$493 million), intended for general corporate purposes, including the redemption and refinancing of outstanding indebtedness.

Cash received from stock options exercised and the related excess tax benefits realized upon exercise during 2013 and 2012 was \$31 million and \$117 million, respectively.

In 2013, the Company repurchased a total of 27.6 million common shares for \$1,400 million (weighted-average price of \$50.65 per share) under its share repurchase programs. In 2012, the Company repurchased a total of 33.8 million common shares for \$1,400 million (weighted-average price of \$41.36 per share) under its share repurchase programs. See the section of this MD&A entitled Common shares for the activity under the 2013 share repurchase programs, as well as the share repurchase programs of the prior years.

During 2013, the Company paid quarterly dividends of \$0.2150 per share amounting to \$724 million, compared to \$652 million, at the rate of \$0.1875 per share, in 2012.

Credit measures

Management believes that the adjusted debt-to-total capitalization ratio is a useful credit measure that aims to show the true leverage of the Company. Similarly, the adjusted debt-to-adjusted earnings before interest, income taxes, depreciation and amortization (EBITDA) multiple is another useful credit measure because it reflects the Company's ability to service its debt. The Company excludes Other income in the calculation of EBITDA. However, since these measures do not have any standardized meaning prescribed by GAAP, they may not be comparable to similar measures presented by other companies and, as such, should not be considered in isolation.

Adjusted debt-to-total capitalization ratio

	December 31, 2013	2012
Debt-to-total capitalization ratio ⁽¹⁾	37.7%	38.5%
Add: Impact of present value of operating lease commitments ⁽²⁾	1.7%	1.9%
Adjusted debt-to-total capitalization ratio	39.4%	40.4%

Adjusted debt-to-adjusted EBITDA

\$ in millions, unless otherwise indicated

	Twelve months ended December 31, 2013	2012
Debt	\$ 7,840	\$ 6,900
Add: Present value of operating lease commitments ⁽²⁾	570	559
Adjusted debt	8,410	7,459
Operating income	3,873	3,685
Add: Depreciation and amortization	980	924
EBITDA (excluding Other income)	4,853	4,609
Add: Deemed interest on operating leases	28	29
Adjusted EBITDA	\$ 4,881	\$ 4,638
Adjusted debt-to-adjusted EBITDA	1.72 times	1.61 times

(1) Debt-to-total capitalization is calculated as total long-term debt plus current portion of long-term debt, divided by the sum of total debt plus total shareholders' equity.

(2) The operating lease commitments have been discounted using the Company's implicit interest rate for each of the periods presented.

The decrease in the Company's adjusted debt-to-total capitalization ratio at December 31, 2013, as compared to 2012, was mainly due to an improvement in the funded status of the Company's pension plans, partly offset by an increased debt level, reflecting the implementation of the accounts receivable securitization program, a higher use of commercial paper and a weaker Canadian-to-US dollar foreign exchange rate in effect at the balance sheet date. This increased debt level as at December 31, 2013, partly offset by a higher operating income earned during 2013, resulted in an increase in the Company's adjusted debt-to-adjusted EBITDA multiple, as compared to 2012.

Available financing arrangements
Revolving credit facility

The Company has an \$800 million revolving credit facility agreement with a consortium of lenders. The agreement, which contains customary terms and conditions, allows for an increase in the facility amount, up to a maximum of \$1.3 billion, as well as the option to extend the term by an additional year at each anniversary date, subject to the consent of individual lenders. The Company exercised such option and on March 22, 2013, the expiry date of the agreement was extended by one year to May 5, 2018. The Company plans to use the credit facility for working capital and general corporate purposes, including backstopping its commercial paper program. As at December 31, 2013 and December 31, 2012, the Company had no outstanding borrowings under its revolving credit facility and there were no draws during the years ended December 31, 2013 and 2012.

Commercial paper

The Company has a commercial paper program, which is backed by its revolving credit facility, enabling it to issue commercial paper up to a maximum aggregate principal amount of \$800 million, or the US dollar equivalent. As at December 31, 2013, the Company had total borrowings of \$273 million presented in Current portion of long-term debt on the Consolidated Balance Sheet (nil as at December 31, 2012). The weighted-average interest rate on these borrowings was 1.14%.

Accounts receivable securitization program

On December 20, 2012, the Company entered into a three-year agreement, commencing on February 1, 2013, to sell an undivided co-ownership interest in a revolving pool of accounts receivable to unrelated trusts for maximum cash proceeds of \$450 million. The trusts are multi-seller trusts and the Company is not the primary beneficiary. Funding for the acquisition of these assets is customarily through the issuance of asset-backed commercial paper notes by the unrelated trusts.

The Company has retained the responsibility for servicing, administering and collecting the receivables sold. The average servicing period is approximately one month. Subject to customary indemnifications, each trust's recourse is limited to the accounts receivable transferred.

The Company is subject to customary reporting requirements for which failure to perform could result in termination of the program. In addition, the program is subject to customary credit rating requirements, which if not met, could also result in termination of the program. The Company monitors the reporting requirements and is currently not aware of any trends, events or conditions that could cause such termination.

The accounts receivable securitization program provides the Company with readily available short-term financing for general corporate use. In the event the program is terminated before its scheduled maturity, the Company expects to meet its future payment obligations through its various sources of financing including its revolving credit facility and commercial paper program, and/or access to capital markets.

The Company accounts for its accounts receivable securitization program under Accounting Standards Codification (ASC) 860, *Transfers and Servicing*. Based on the structure of the program, the Company accounts for the proceeds as a secured borrowing. As such, as at December 31, 2013, the Company recorded \$250 million of proceeds received under the accounts receivable securitization program in the Current portion of long-term debt on the Consolidated Balance Sheet at a weighted-average interest rate of 1.18% which is secured by and limited to \$281 million of accounts receivable.

Bilateral letter of credit facilities and Restricted cash and cash equivalents

The Company has a series of bilateral letter of credit facility agreements with various banks to support its requirements to post letters of credit in the ordinary course of business. On March 22, 2013, the expiry date of these agreements was extended by one year to April 28, 2016. Under these agreements, the Company

has the option from time to time to pledge collateral in the form of cash or cash equivalents, for a minimum term of one month, equal to at least the face value of the letters of credit issued. As at December 31, 2013, the Company had letters of credit drawn of \$481 million (\$551 million as at December 31, 2012) from a total committed amount of \$503 million (\$562 million as at December 31, 2012) by the various banks. As at December 31, 2013, cash and cash equivalents of \$448 million (\$521 million as at December 31, 2012) were pledged as collateral and recorded as Restricted cash and cash equivalents on the Consolidated Balance Sheet.

Shelf prospectus and registration statement

On December 3, 2013, the Company filed a new shelf prospectus with Canadian securities regulators and a registration statement with the United States Securities and Exchange Commission (SEC)

providing for the issuance by CN of up to \$3.0 billion of debt securities in the Canadian and U.S. markets. The current shelf prospectus and registration statement expires January 2, 2016 and replaces CN's previous shelf prospectus and registration statement that was filed on November 4, 2011. Access to capital markets under the shelf prospectus and registration statement is dependent on market conditions at the time of pricing.

All forward-looking information provided in this section is subject to risks and uncertainties and is based on assumptions about events and developments that may not materialize or that may be offset entirely or partially by other events and developments. See the section of this MD&A entitled Forward-looking statements for assumptions and risk factors affecting such forward-looking statements.

Contractual obligations

In the normal course of business, the Company incurs contractual obligations. The following table sets forth the Company's contractual obligations for the following items as at December 31, 2013:

<i>In millions</i>	Total	2014	2015	2016	2017	2018	2019 & thereafter
Debt obligations ⁽¹⁾	\$ 7,058	\$ 868	\$ 369	\$ 582	\$ 263	\$ 556	\$ 4,420
Interest on debt obligations	5,302	326	317	308	296	271	3,784
Capital lease obligations ⁽²⁾	991	209	113	317	154	14	184
Operating lease obligations ⁽³⁾	680	132	111	84	66	56	231
Purchase obligations ⁽⁴⁾	482	397	70	7	4	2	2
Pension contributions ⁽⁵⁾	1,207	3	196	336	336	336	-
Other long-term liabilities reflected on the balance sheet ⁽⁶⁾	754	65	66	44	44	42	493
Other commitments ⁽⁷⁾	363	61	302	-	-	-	-
Total obligations	\$ 16,837	\$ 2,061	\$ 1,544	\$ 1,678	\$ 1,163	\$ 1,277	\$ 9,114

(1) Presented net of unamortized discounts, of which \$833 million relates to non-interest bearing Notes due in 2094, and excludes capital lease obligations of \$782 million which are included in "Capital lease obligations". Also includes \$250 million under the accounts receivable securitization program.

(2) Includes \$782 million of minimum lease payments and \$209 million of imputed interest at rates ranging from 0.7% to 8.5%.

(3) Includes minimum rental payments for operating leases having initial non-cancelable lease terms of one year or more. The Company also has operating lease agreements for its automotive fleet with one-year non-cancelable terms for which its practice is to renew monthly thereafter. The estimated annual rental payments for such leases are approximately \$30 million and generally extend over five years.

(4) Includes commitments for railroad ties, rail, freight cars, locomotives and other equipment and services, and outstanding information technology service contracts and licenses.

(5) The Company's pension contributions are based on actuarial funding valuations. The estimated minimum required payments for pension contributions, excluding current service cost, are based on actuarial funding valuations as at December 31, 2012 that were filed in June 2013. As a result of the voluntary contributions made by the Company of \$100 million and \$700 million in 2013 and 2012, respectively, there are no minimum required payments for pension contributions, excluding current service costs for 2014, for the Company's main pension plan, the CN Pension Plan. Voluntary contributions can be treated as prepayment against the Company's required special solvency payments and as at December 31, 2013 the Company had approximately \$470 million of accumulated prepayments which remain available to offset future required solvency deficit payments. The Company expects to make total contributions in 2014 of approximately \$130 million for all the Company's pension plans and to apply approximately \$335 million from its accumulated prepayments to satisfy its estimated 2014 required solvency deficit payment. Actuarial valuations are required annually and as such, future payments for pension contributions are subject to re-evaluation on an annual basis. See the section of this MD&A entitled Business risks, Other risks – Pensions as well as the section of this MD&A entitled Critical accounting policies – Pensions and other postretirement benefits.

(6) Includes expected payments for workers' compensation, workforce reductions, postretirement benefits other than pensions, net unrecognized tax benefits and environmental liabilities that have been classified as contractual settlement agreements.

(7) Includes estimated remaining commitments of approximately \$291 million (US\$273 million), in relation to the U.S. federal government legislative requirement to implement PTC by 2015. In August 2012, the FRA reported an update of the PTC implementation progress to Congress concluding that the majority of the carriers would be unable to meet the December 31, 2015 implementation deadline. In August 2013, legislation was introduced in the Senate that would delay PTC implementation by five years to the end of 2020, and in the same month, the U.S. Government Accountability Office published a report recommending that Congress give the FRA authority to extend the deadline for individual carriers on a case-by-case basis. It also includes estimated remaining commitments of approximately \$72 million (US\$68 million), in relation to the acquisition of principal lines of the former Elgin, Joliet and Eastern Railway Company, for railroad infrastructure improvements, grade separation projects as well as commitments under a series of agreements with individual communities and a comprehensive voluntary mitigation program established to address surrounding municipalities' concerns.

For 2014 and the foreseeable future, the Company expects cash flow from operations and from its various sources of financing to be sufficient to meet its debt repayments and future obligations, and to fund anticipated capital expenditures.

See the section of this MD&A entitled Forward-looking statements for assumptions and risk factors affecting such forward-looking statements.

Disposal of property**2013***Exchange of easements*

On June 8, 2013, the Company entered into an agreement with another Class I railroad to exchange perpetual railroad operating easements including the track and roadway assets on specific rail lines (collectively the "exchange of easements") without monetary consideration. The Company has accounted for the exchange of easements at fair value pursuant to Financial Accounting Standards Board (FASB) ASC 845, *Nonmonetary Transactions*. The transaction resulted in a gain on exchange of easements of \$29 million (\$18 million after-tax) that was recorded in Other income.

Lakeshore West

On March 19, 2013, the Company entered into an agreement with Metrolinx to sell a segment of the Oakville subdivision in Oakville and Burlington, Ontario, together with the rail fixtures and certain passenger agreements (collectively the "Lakeshore West"), for cash proceeds of \$52 million before transaction costs. Under the agreement, the Company obtained the perpetual right to operate freight trains over the Lakeshore West at its then current level of operating activity, with the possibility of increasing its operating activity for additional consideration. The transaction resulted in a gain on disposal of \$40 million (\$36 million after-tax) that was recorded in Other income under the full accrual method of accounting for real estate transactions.

2012*Bala-Oakville*

On March 23, 2012, the Company entered into an agreement with Metrolinx to sell a segment of the Bala and a segment of the Oakville subdivisions in Toronto, Ontario, together with the rail fixtures and certain passenger agreements (collectively the "Bala-Oakville"), for cash proceeds of \$311 million before transaction costs. Under the agreement, the Company obtained the perpetual right to operate freight trains over the Bala-Oakville at its then current level of operating activity, with the possibility of increasing its operating activity for additional consideration. The transaction resulted in a gain on disposal of \$281 million (\$252 million after-tax) that was recorded in Other income under the full accrual method of accounting for real estate transactions.

2011*IC RailMarine*

On August 1, 2011, the Company sold substantially all of the assets of IC RailMarine Terminal Company ("IC RailMarine"), an indirect subsidiary of the Company, to Raven Energy, LLC, an affiliate of Foresight Energy, LLC ("Foresight") and the Cline Group ("Cline"), for cash proceeds of \$70 million (US\$73 million) before transaction costs. IC RailMarine is located on the east bank of the Mississippi River and stores and transfers bulk commodities and liquids

between rail, ship and barge, serving customers in North American and global markets. Under the sale agreement, the Company will benefit from a 10-year rail transportation agreement with Savatran LLC, an affiliate of Foresight and Cline, to haul a minimum annual volume of coal from four Illinois mines to the IC RailMarine transfer facility. The transaction resulted in a gain on disposal of \$60 million (\$38 million after-tax) that was recorded in Other income.

Lakeshore East

On March 24, 2011, the Company entered into an agreement with Metrolinx to sell a segment of the Kingston subdivision known as the Lakeshore East in Pickering and Toronto, Ontario, together with the rail fixtures and certain passenger agreements (collectively the "Lakeshore East"), for cash proceeds of \$299 million before transaction costs. Under the agreement, the Company obtained the perpetual right to operate freight trains over the Lakeshore East at its then current level of operating activity, with the possibility of increasing its operating activity for additional consideration. The transaction resulted in a gain on disposal of \$288 million (\$254 million after-tax) that was recorded in Other income under the full accrual method of accounting for real estate transactions.

Off balance sheet arrangements*Guarantees and indemnifications*

In the normal course of business, the Company, including certain of its subsidiaries, enters into agreements that may involve providing guarantees or indemnifications to third parties and others, which may extend beyond the term of the agreements. These include, but are not limited to, residual value guarantees on operating leases, standby letters of credit, surety and other bonds, and indemnifications that are customary for the type of transaction or for the railway business.

The Company is required to recognize a liability for the fair value of the obligation undertaken in issuing certain guarantees on the date the guarantee is issued or modified. In addition, where the Company expects to make a payment in respect of a guarantee, a liability will be recognized to the extent that one has not yet been recognized.

The nature of these guarantees or indemnifications, the maximum potential amount of future payments, the carrying amount of the liability, if any, and the nature of any recourse provisions are disclosed in Note 16 – Major commitments and contingencies to the Company's 2013 Annual Consolidated Financial Statements.

Stock plans

The Company has various stock-based incentive plans for eligible employees. All share and per share data for such plans reflect the impact of the stock split (see Note 9 – Capital stock to the Company's 2013 Annual Consolidated Financial Statements). A description of the Company's major plans is provided in Note 10 – Stock plans to the Company's 2013 Annual Consolidated Financial Statements.

The following table provides the total stock-based compensation expense for awards under all plans, as well as the related tax benefit recognized in income, for the years ended December 31, 2013, 2012 and 2011:

<i>In millions</i>	<i>Year ended December 31,</i>	2013	2012	2011
Cash settled awards				
Share Unit Plan		\$ 92	\$ 76	\$ 81
Voluntary Incentive Deferral Plan		35	19	21
		127	95	102
Stock option awards				
		9	10	10
<i>Total stock-based compensation expense</i>		\$ 136	\$ 105	\$ 112
<i>Tax benefit recognized in income</i>		\$ 35	\$ 25	\$ 24

Financial instruments

In the normal course of business, the Company is exposed to various risks such as customer credit risk, commodity price risk, interest rate risk, foreign currency risk, and liquidity risk. To manage these risks, the Company follows a financial risk management framework, which is monitored and approved by the Company's Finance Committee, with a goal of maintaining a strong balance sheet, optimizing earnings per share and free cash flow, financing its operations at an optimal cost of capital and preserving its liquidity. The Company has limited involvement with derivative financial instruments in the management of its risks and does not use them for trading purposes. See Note 17 – Financial instruments to the Company's 2013 Annual Consolidated Financial Statements for a discussion of such risks. At December 31, 2013 and 2012, the Company did not have any significant derivative financial instruments outstanding.

Payments for income taxes

The Company is required to make scheduled installment payments as prescribed by the tax authorities. In Canada, the Company's domestic jurisdiction, tax installments in a given year are generally based on the prior year's taxable income whereas in the U.S., the Company's predominate foreign jurisdiction, they are based on forecasted taxable income of the current year.

In 2013, net income tax payments to Canadian tax authorities were \$610 million (\$138 million in 2012) and net income tax payments to U.S. tax authorities were \$280 million (\$151 million in 2012). For the 2014 fiscal year, the Company's net income tax payments are expected to be approximately \$800 million.

See the section of this MD&A entitled Forward-looking statements for assumptions and risk factors affecting such forward-looking statement.

Common shares

Common stock split

On October 22, 2013, the Board of Directors of the Company approved a two-for-one common stock split in the form of a stock dividend of one additional common share of CN for each share outstanding, which was paid on November 29, 2013, to

shareholders of record on November 15, 2013. All share and per share data presented herein reflect the impact of the stock split.

Share repurchase programs

On October 22, 2012, the Board of Directors of the Company approved a share repurchase program which allowed for the repurchase of up to \$1.4 billion in common shares, not to exceed 36.0 million common shares, between October 29, 2012 and October 28, 2013 pursuant to a normal course issuer bid at prevailing market prices plus brokerage fees, or such other prices as may be permitted by the Toronto Stock Exchange. The Company repurchased a total of 29.4 million common shares for \$1.4 billion under this share repurchase program.

On October 22, 2013, the Board of Directors of the Company approved a new share repurchase program which allows for the repurchase of up to 30.0 million common shares, between October 29, 2013 and October 23, 2014 pursuant to a normal course issuer bid at prevailing market prices plus brokerage fees, or such other prices as may be permitted by the Toronto Stock Exchange.

The following table provides the information related to the share repurchase programs for the years ended December 31, 2013, 2012 and 2011:

In millions, except per share data

<i>Year ended December 31,</i>	2013	2012	2011
October 2013 – October 2014 program			
Number of common shares ⁽¹⁾	5.5	N/A	N/A
Weighted-average price per share ⁽²⁾	\$ 55.25	N/A	N/A
Amount of repurchase	\$ 305	N/A	N/A
October 2012 – October 2013 program			
Number of common shares ⁽¹⁾	22.1	7.2	N/A
Weighted-average price per share ⁽²⁾	\$ 49.51	\$ 42.11	N/A
Amount of repurchase	\$ 1,095	\$ 305	N/A
October 2011 – October 2012 program			
Number of common shares ⁽¹⁾	N/A	26.6	6.8
Weighted-average price per share ⁽²⁾	N/A	\$ 41.16	\$ 37.54
Amount of repurchase	N/A	\$ 1,095	\$ 256
January 2011 – December 2011 program			
Number of common shares ⁽¹⁾	N/A	N/A	33.0
Weighted-average price per share ⁽²⁾	N/A	N/A	\$ 35.28
Amount of repurchase	N/A	N/A	\$ 1,164
Total for the year			
Number of common shares ⁽¹⁾	27.6	33.8	39.8
Weighted-average price per share ⁽²⁾	\$ 50.65	\$ 41.36	\$ 35.67
Amount of repurchase	\$ 1,400	\$ 1,400	\$ 1,420

(1) Includes common shares purchased in the first and fourth quarters of 2013, 2012 and 2011 pursuant to private agreements between the Company and arm's-length third-party sellers.

(2) Includes brokerage fees.

Outstanding share data

As at February 3, 2014, the Company had 829.9 million common shares and 7.7 million stock options outstanding.

Recent accounting pronouncements

In February 2013, the FASB issued Accounting Standards Update (ASU) 2013-02, *Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income*. ASU 2013-02 added new disclosure requirements to ASC 220, *Comprehensive Income*, for items reclassified out of accumulated other comprehensive income (AOCI) effective for reporting periods beginning after December 15, 2012. It requires entities to disclose additional information about amounts reclassified out of AOCI by component including changes in AOCI balances and significant items reclassified out of AOCI by the respective line items of net income. The Company has adopted ASU 2013-02 for the reporting period beginning January 1, 2013 and the prescribed disclosures are presented in Note 18 – Accumulated other comprehensive loss to the Company's 2013 Annual Consolidated Financial Statements.

The Accounting Standards Board of the Canadian Institute of Chartered Accountants required all publicly accountable enterprises to report under International Financial Reporting Standards (IFRS) for the fiscal years beginning on or after January 1, 2011. However, National Instrument 52-107 issued by the Ontario Securities Commission allows SEC issuers, as defined by the SEC, such as CN, to file with Canadian securities regulators financial statements prepared in accordance with U.S. GAAP. As such, the Company decided not to report under IFRS and continues to report under U.S. GAAP. The SEC is currently evaluating the implications of incorporating IFRS into the U.S. financial reporting system. Should the SEC decide it will move forward, the Company will convert its reporting to IFRS when required.

Critical accounting policies

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of revenues and expenses during the period, the reported amounts of assets and liabilities, and the disclosure of contingent assets and liabilities at the date of the financial statements. On an ongoing basis, management reviews its estimates based upon currently available information. Actual results could differ from these estimates. The Company's policies for personal injury and other claims, environmental matters, depreciation, pensions and other postretirement benefits, and income taxes, require management's more significant judgments and estimates in the preparation of the Company's consolidated financial statements and, as such, are considered to be critical. The following information should be read in conjunction with the Company's 2013 Annual Consolidated Financial Statements and Notes thereto.

Management discusses the development and selection of the Company's critical accounting estimates with the Audit Committee of the Company's Board of Directors, and the Audit Committee has reviewed the Company's related disclosures.

Personal injury and other claims

In the normal course of business, the Company becomes involved in various legal actions seeking compensatory and occasionally punitive damages, including actions brought on behalf of various purported classes of claimants and claims relating to employee and third-party personal injuries, occupational disease and property damage, arising out of harm to individuals or property allegedly caused by, but not limited to, derailments or other accidents.

Canada

Employee injuries are governed by the workers' compensation legislation in each province whereby employees may be awarded either a lump sum or a future stream of payments depending on the nature and severity of the injury. As such, the provision for employee injury claims is discounted. In the provinces where the Company is self-insured, costs related to employee work-related injuries are accounted for based on actuarially developed estimates of the ultimate cost associated with such injuries, including compensation, health care and third-party administration costs. A comprehensive actuarial study is generally performed at least on a triennial basis. For all other legal actions, the Company maintains, and regularly updates on a case-by-case basis, provisions for such items when the expected loss is both probable and can be reasonably estimated based on currently available information.

In 2013, the Company recorded a \$1 million increase to its provision for personal injuries and other claims in Canada as a result of a comprehensive actuarial study for employee injury claims as well as various other legal claims.

As at December 31, 2013, 2012 and 2011, the Company's provision for personal injury and other claims in Canada was as follows:

<i>In millions</i>	2013	2012	2011
Balance January 1	\$ 209	\$ 199	\$ 200
Accruals and other	38	55	31
Payments	(37)	(45)	(32)
<i>Balance December 31</i>	\$ 210	\$ 209	\$ 199
<i>Current portion – Balance December 31</i>	\$ 31	\$ 39	\$ 39

The assumptions used in estimating the ultimate costs for Canadian employee injury claims include, among other factors, the discount rate, the rate of inflation, wage increases and health care costs. The Company periodically reviews its assumptions to reflect currently available information. Over the past three years, the Company has not significantly changed any of these assumptions. Changes in any of these assumptions could materially affect Casualty and other expense as reported in the Company's results of operations.

For all other legal claims in Canada, estimates are based on the specifics of the case, trends and judgment.

United States

Personal injury claims by the Company's employees, including claims alleging occupational disease and work-related injuries, are subject to the provisions of the Federal Employers' Liability Act (FELA). Employees are compensated under FELA for damages assessed based on a finding of fault through the U.S. jury system or through individual settlements. As such, the provision is undiscounted. With limited exceptions where claims are evaluated on a case-by-case basis, the Company follows an actuarial-based approach and accrues the expected cost for personal injury, including asserted and unasserted occupational disease claims, and property damage claims, based on actuarial estimates of their ultimate cost. A comprehensive actuarial study is performed annually.

For employee work-related injuries, including asserted occupational disease claims, and third-party claims, including grade crossing, trespasser and property damage claims, the actuarial valuation considers, among other factors, the Company's historical patterns of claims filings and payments. For unasserted occupational disease claims, the actuarial study includes the projection of the Company's experience into the future considering the potentially exposed population. The Company adjusts its liability based upon management's assessment and the results of the study. On an ongoing basis, management reviews and compares the assumptions inherent in the latest actuarial study with the current claim experience and, if required, adjustments to the liability are recorded.

Due to the inherent uncertainty involved in projecting future events, including events related to occupational diseases, which include but are not limited to, the timing and number of actual claims, the average cost per claim and the legislative and judicial environment, the Company's future payments may differ from current amounts recorded.

In 2013, the Company recorded an \$11 million reduction to its provision for U.S. personal injury and other claims attributable to non-occupational disease, third-party and occupational disease claims pursuant to the 2013 external actuarial study. In previous years, external actuarial studies have supported a net increase of \$1 million and a net reduction of \$6 million to the Company's provision for U.S. personal injury and other claims in 2012 and 2011, respectively. The previous years' changes were mainly attributable to changes in the Company's estimates of unasserted claims and costs related to asserted claims as a result of its ongoing risk mitigation strategy focused on reducing the frequency and severity of claims through injury prevention and containment; mitigation of claims; and lower settlements for existing claims.

As at December 31, 2013, 2012 and 2011, the Company's provision for personal injury and other claims in the U.S. was as follows:

<i>In millions</i>	2013	2012	2011
Balance January 1	\$ 105	\$ 111	\$ 146
Accruals and other	25	28	30
Payments	(24)	(34)	(65)
<i>Balance December 31</i>	\$ 106	\$ 105	\$ 111
<i>Current portion – Balance December 31</i>	\$ 14	\$ 43	\$ 45

For the U.S. personal injury and other claims liability, historical claim data is used to formulate assumptions relating to the expected number of claims and average cost per claim (severity) for each year. Changes in any one of these assumptions could materially affect Casualty and other expense as reported in the Company's results of operations. For example, a 5% change in the asbestos average claim cost or a 1% change in the inflation trend rate for all injury types would result in an increase or decrease in the liability recorded of approximately \$1 million.

Environmental matters*Known existing environmental concerns*

The Company has identified approximately 280 sites at which it is or may be liable for remediation costs, in some cases along with other potentially responsible parties, associated with alleged contamination and is subject to environmental clean-up and enforcement actions, including those imposed by the United States Federal Comprehensive Environmental Response, Compensation and Liability Act of 1980 (CERCLA), also known as the Superfund law, or analogous state laws. CERCLA and similar state laws, in addition to other similar Canadian and U.S. laws, generally impose joint and several liability for clean-up and enforcement costs on current and former owners and operators of a site, as well as those whose waste is disposed of at the site, without regard to fault or the legality of the original conduct. The Company has been notified that it is a potentially responsible party for study and clean-up costs at approximately 10 sites governed by the Superfund law (and analogous state laws) for which investigation and remediation payments are or will be made or are yet to be determined and, in many instances, is one of several potentially responsible parties.

The ultimate cost of addressing these known contaminated sites cannot be definitely established given that the estimated environmental liability for any given site may vary depending on the nature and extent of the contamination; the nature of anticipated response actions, taking into account the available clean-up techniques; evolving regulatory standards governing environmental liability; and the number of potentially responsible parties and their financial viability. As a result, liabilities are recorded based on the results of a four-phase assessment conducted on a site-by-site basis. A liability is initially recorded when environmental assessments occur, remedial efforts are probable, and when the

costs, based on a specific plan of action in terms of the technology to be used and the extent of the corrective action required, can be reasonably estimated. The Company estimates the costs related to a particular site using cost scenarios established by external consultants based on the extent of contamination and expected costs for remedial efforts. In the case of multiple parties, the Company accrues its allocable share of liability taking into account the Company's alleged responsibility, the number of potentially responsible parties and their ability to pay their respective share of the liability. Adjustments to initial estimates are recorded as additional information becomes available.

The Company's provision for specific environmental sites is undiscounted and includes costs for remediation and restoration of sites, as well as monitoring costs. Environmental accruals, which are classified as Casualty and other in the Consolidated Statement of Income, include amounts for newly identified sites or contaminants as well as adjustments to initial estimates. Recoveries of environmental remediation costs from other parties are recorded as assets when their receipt is deemed probable.

As at December 31, 2013, 2012 and 2011, the Company's provision for specific environmental sites was as follows:

<i>In millions</i>	2013	2012	2011
Balance January 1	\$ 123	\$ 152	\$ 150
Accruals and other	14	(5)	17
Payments	(18)	(24)	(15)
Balance December 31	\$ 119	\$ 123	\$ 152
<i>Current portion – Balance December 31</i>	\$ 41	\$ 31	\$ 63

The Company anticipates that the majority of the liability at December 31, 2013 will be paid out over the next five years. However, some costs may be paid out over a longer period. Based on the information currently available, the Company considers its provisions to be adequate.

Unknown existing environmental concerns

While the Company believes that it has identified the costs likely to be incurred for environmental matters in the next several years based on known information, the discovery of new facts, future changes in laws, the possibility of releases of hazardous materials into the environment and the Company's ongoing efforts to identify potential environmental liabilities that may be associated with its properties may result in the identification of additional environmental liabilities and related costs. The magnitude of such additional liabilities and the costs of complying with future environmental laws and containing or remediating contamination cannot be reasonably estimated due to many factors, including:

- (i) the lack of specific technical information available with respect to many sites;
- (ii) the absence of any government authority, third-party orders, or claims with respect to particular sites;

- (iii) the potential for new or changed laws and regulations and for development of new remediation technologies and uncertainty regarding the timing of the work with respect to particular sites; and
- (iv) the determination of the Company's liability in proportion to other potentially responsible parties and the ability to recover costs from any third parties with respect to particular sites.

Therefore, the likelihood of any such costs being incurred or whether such costs would be material to the Company cannot be determined at this time. There can thus be no assurance that liabilities or costs related to environmental matters will not be incurred in the future, or will not have a material adverse effect on the Company's financial position or results of operations in a particular quarter or fiscal year, or that the Company's liquidity will not be adversely impacted by such liabilities or costs, although management believes, based on current information, that the costs to address environmental matters will not have a material adverse effect on the Company's financial position or liquidity. Costs related to any unknown existing or future contamination will be accrued in the period in which they become probable and reasonably estimable.

Future occurrences

In railroad and related transportation operations, it is possible that derailments or other accidents, including spills and releases of hazardous materials, may occur that could cause harm to human health or to the environment. As a result, the Company may incur costs in the future, which may be material, to address any such harm, compliance with laws and other risks, including costs relating to the performance of clean-ups, payment of environmental penalties and remediation obligations, and damages relating to harm to individuals or property.

Regulatory compliance

The Company may incur significant capital and operating costs associated with environmental regulatory compliance and clean-up requirements, in its railroad operations and relating to its past and present ownership, operation or control of real property. Environmental expenditures that relate to current operations are expensed unless they relate to an improvement to the property. Expenditures that relate to an existing condition caused by past operations and which are not expected to contribute to current or future operations are expensed. Operating expenses for environmental matters amounted to \$18 million in 2013, \$16 million in 2012 and \$4 million in 2011. For 2014, the Company expects to incur operating expenses relating to environmental matters in the same range as 2013. In addition, based on the results of its operations and maintenance programs, as well as ongoing environmental audits and other factors, the Company plans for specific capital improvements on an annual basis. Certain of these improvements help ensure facilities, such as fuelling stations and

waste water and storm water treatment systems, comply with environmental standards and include new construction and the updating of existing systems and/or processes. Other capital expenditures relate to assessing and remediating certain impaired properties. The Company's environmental capital expenditures amounted to \$10 million in 2013, \$13 million in 2012 and \$11 million in 2011. For 2014, the Company expects to incur capital expenditures relating to environmental matters in the same range as 2013.

Depreciation

Properties are carried at cost less accumulated depreciation including asset impairment write-downs. The cost of properties, including those under capital leases, net of asset impairment write-downs, is depreciated on a straight-line basis over their estimated service lives, measured in years, except for rail which is measured in millions of gross tons per mile. The Company follows the group method of depreciation whereby a single composite depreciation rate is applied to the gross investment in a class of similar assets, despite small differences in the service life or salvage value of individual property units within the same asset class. The Company uses approximately 40 different depreciable asset classes.

For all depreciable assets, the depreciation rate is based on the estimated service lives of the assets. Assessing the reasonableness of the estimated service lives of properties requires judgment and is based on currently available information, including periodic depreciation studies conducted by the Company. The Company's U.S. properties are subject to comprehensive depreciation studies as required by the Surface Transportation Board (STB) and are conducted by external experts. Depreciation studies for Canadian properties are not required by regulation and are conducted internally. Studies are performed on specific asset groups on a periodic basis. Changes in the estimated service lives of the assets and their related composite depreciation rates are implemented prospectively.

The studies consider, among other factors, the analysis of historical retirement data using recognized life analysis techniques, and the forecasting of asset life characteristics. Changes in circumstances, such as technological advances, changes to the Company's business strategy, changes in the Company's capital strategy or changes in regulations can result in the actual service lives differing from the Company's estimates.

A change in the remaining service life of a group of assets, or their estimated net salvage value, will affect the depreciation rate used to amortize the group of assets and thus affect depreciation expense as reported in the Company's results of operations. A change of one year in the composite service life of the Company's fixed asset base would impact annual depreciation expense by approximately \$26 million.

Depreciation studies are a means of ensuring that the assumptions used to estimate the service lives of particular asset groups are still valid and where they are not, they serve as the basis to

establish the new depreciation rates to be used on a prospective basis. In the first quarter of 2013, the Company completed its depreciation study for Canadian track and roadway properties and as a result, the Company changed the estimated service lives for various track and roadway assets and their related composite depreciation rates. This depreciation study resulted in an annualized decrease to depreciation expense of approximately \$25 million. In the fourth quarter of 2013, a depreciation study on U.S. track and roadway properties was completed resulting in an annualized increase to depreciation expense of approximately \$30 million.

In 2013, the Company recorded total depreciation expense of \$979 million (\$923 million in 2012 and \$883 million in 2011). At December 31, 2013, the Company had Properties of \$26,227 million, net of accumulated depreciation of \$10,579 million (\$24,541 million in 2012, net of accumulated depreciation of \$10,181 million). Additional disclosures are provided in Note 4 – Properties to the Company's 2013 Annual Consolidated Financial Statements.

U.S. generally accepted accounting principles require the use of historical cost as the basis of reporting in financial statements. As a result, the cumulative effect of inflation, which has significantly increased asset replacement costs for capital-intensive companies such as CN, is not reflected in operating expenses. Depreciation charges on an inflation-adjusted basis, assuming that all operating assets are replaced at current price levels, would be substantially greater than historically reported amounts.

Pensions and other postretirement benefits

The Company's plans have a measurement date of December 31. The following table shows the Company's pension asset, pension liability and other postretirement benefits liability at December 31, 2013 and December 31, 2012:

<i>In millions</i>	<i>December 31,</i>	2013	2012
Pension asset		\$ 1,662	\$ -
Pension liability		\$ 303	\$ 524
Other postretirement benefits liability		\$ 256	\$ 277

The descriptions in the following paragraphs pertaining to pensions relate generally to the Company's main pension plan, the CN Pension Plan, unless otherwise specified.

Calculation of net periodic benefit cost (income)

The Company accounts for net periodic benefit cost for pensions and other postretirement benefits as required by FASB ASC 715, *Compensation – Retirement Benefits*. Under the standard, assumptions are made regarding the valuation of benefit obligations and performance of plan assets. In the calculation of net periodic benefit cost, the standard allows for a gradual recognition of changes in benefit obligations and fund performance over the expected average remaining service life of the employee group covered by the plans.

In accounting for pensions and other postretirement benefits, assumptions are required for, among other things, the discount rate, the expected long-term rate of return on plan assets, the rate of compensation increase, health care cost trend rates, mortality rates, employee early retirements, terminations and disability. Changes in these assumptions result in actuarial gains or losses, which are recognized in Other comprehensive income (loss). The Company amortizes these gains or losses into net periodic benefit cost over the expected average remaining service life of the employee group covered by the plans only to the extent that the unrecognized net actuarial gains and losses are in excess of the corridor threshold, which is calculated as 10% of the greater of the beginning-of-year balances of the projected benefit obligation or market-related value of plan assets. The Company's net periodic benefit cost for future periods is dependent on demographic experience, economic conditions and investment performance. Recent demographic experience has revealed no material net gains or losses on termination, retirement, disability and mortality. Experience with respect to economic conditions and investment performance is further discussed herein.

For the years ended December 31, 2013, 2012 and 2011, the consolidated net periodic benefit cost (income) for pensions and other postretirement benefits were as follows:

<i>In millions</i>	<i>Year ended December 31,</i>	2013	2012	2011
Net periodic benefit cost (income) for pensions		\$ 90	\$ (9)	\$ (80)
Net periodic benefit cost for other postretirement benefits		\$ 14	\$ 14	\$ 19

At December 31, 2013 and 2012, the projected pension benefit obligation and accumulated other postretirement benefit obligation were as follows:

<i>In millions</i>	<i>December 31,</i>	2013	2012
Projected pension benefit obligation		\$ 15,510	\$ 16,335
Accumulated other postretirement benefit obligation		\$ 256	\$ 277

Discount rate assumption

The Company's discount rate assumption, which is set annually at the end of each year, is used to determine the projected benefit obligation at the end of the year and the net periodic benefit cost for the following year. The discount rate is used to measure the single amount that, if invested at the measurement date in a portfolio of high-quality debt instruments with a rating of AA or better, would provide the necessary cash flows to pay for pension benefits as they become due. The discount rate is determined by management with the aid of third-party actuaries. For the Canadian pension and other postretirement benefit plans, future expected benefit payments at each measurement date are discounted using spot rates from a derived AA corporate bond yield curve. The derived curve is based on observed rates for AA corporate bonds with short term maturities and a projected

AA corporate curve for longer term maturities based on spreads between observed AA corporate bonds and AA provincial bonds. The derived curve is expected to generate cash flows that match the estimated future benefit payments of the plans as the bond rate for each maturity year is applied to the plans' corresponding expected benefit payments of that year. A discount rate of 4.73%, based on bond yields prevailing at December 31, 2013 (4.15% at December 31, 2012) was considered appropriate by the Company to match the approximately 11-year average duration of estimated future benefit payments. The current estimate for the expected average remaining service life of the employee group covered by the plans is approximately 11 years.

The Company amortizes net actuarial gains and losses over the expected average remaining service life of the employee group covered by the plans, only to the extent they are in excess of the corridor threshold. For the year ended December 31, 2013, the Company amortized a net actuarial loss of \$227 million related to the accumulated actuarial losses of its pension plans as part of net periodic benefit cost. The Company also recognized \$5 million of actuarial losses related to settlements in its various pension plans, and recorded a net actuarial gain of \$1,517 million on its pension plans decreasing the net actuarial loss recognized in Accumulated other comprehensive loss to \$1,515 million (\$3,264 million in 2012). The decrease in the net actuarial loss was primarily due to the positive liability experience resulting from the increase in the discount rate from 4.15% to 4.73%, as well as the difference in the actual and expected return on plan assets for the year ended December 31, 2013.

For the year ended December 31, 2013, a 0.25% decrease in the 4.73% discount rate used to determine the projected benefit obligation would have resulted in a decrease of approximately \$440 million to the funded status for pensions and would result in an increase of approximately \$35 million to the 2014 net periodic benefit cost. A 0.25% increase in the discount rate would have resulted in an increase of approximately \$425 million to the funded status for pensions and would result in a decrease of approximately \$35 million to the 2014 net periodic benefit cost.

Expected long-term rate of return assumption

To develop its expected long-term rate of return assumption used in the calculation of net periodic benefit cost applicable to the market-related value of assets, the Company considers multiple factors. The expected long-term rate of return is determined based on expected future performance for each asset class and is weighted based on the current asset portfolio mix. Consideration is taken of the historical performance, the premium return generated from an actively managed portfolio, as well as current and future anticipated asset allocations, economic developments, inflation rates and administrative expenses. Based on these factors, the rate is determined by the Company. For 2013, the Company used a long-term rate of return assumption of 7.00% on the market-related value of plan assets to compute net periodic benefit cost. For

2014, the Company will maintain the expected long-term rate of return on plan assets at 7.00% to reflect management's current view of long-term investment returns. The Company has elected to use a market-related value of assets, whereby realized and unrealized gains/losses and appreciation/depreciation in the value of the investments are recognized over a period of five years, while investment income is recognized immediately. If the Company had elected to use the market value of assets, which for the CN Pension Plan at December 31, 2013 was above the market-related value of assets by \$1,340 million, the projected net periodic benefit cost for 2014 would decrease by approximately \$90 million.

The assets of the Company's various plans are held in separate trust funds which are diversified by asset type, country and investment strategies. Each year, the CN Board of Directors reviews and confirms or amends the Statement of Investment Policies and Procedures (SIPP) which includes the plans' long-term asset mix and related benchmark indices (Policy). This Policy is based on a long-term forward-looking view of the world economy, the dynamics of the plans' benefit liabilities, the market return expectations of each asset class and the current state of financial markets. The target long-term asset mix in 2013 was: 3% cash and short-term investments, 37% bonds and mortgages, 45% equities, 4% real estate, 7% oil and gas and 4% infrastructure assets.

Annually, the CN Investment Division (Investment Manager), a division of the Company created to invest and administer the assets of the plans, proposes a short-term asset mix target (Strategy) for the coming year, which is expected to differ from the Policy, because of current economic and market conditions and expectations. The Investment Committee of the Board (Committee) regularly compares the actual asset mix to the Policy and Strategy and compares the actual performance of the Trusts to the performance of the benchmark indices.

The Committee's approval is required for all major investments in illiquid securities. The SIPP allows for the use of derivative financial instruments to implement strategies or to hedge or adjust existing or anticipated exposures. The SIPP prohibits investments in securities of the Company or its subsidiaries. During the last 10 years ended December 31, 2013, the CN Pension Plan earned an annual average rate of return of 7.56%.

The actual, market-related value, and expected rates of return on plan assets for the last five years were as follows:

Rates of return	2013	2012	2011	2010	2009
Actual	11.2%	7.7%	0.3%	8.7%	10.8%
Market-related value	7.3%	2.3%	3.0%	4.8%	6.5%
Expected	7.00%	7.25%	7.50%	7.75%	7.75%

The Company's expected long-term rate of return on plan assets reflects management's view of long-term investment returns and the effect of a 1% variation in such rate of return would result in a change to the net periodic benefit cost of approximately \$85 million. Management's assumption of the expected long-term

rate of return is subject to risks and uncertainties that could cause the actual rate of return to differ materially from management's assumption. There can be no assurance that the plan assets will be able to earn the expected long-term rate of return on plan assets.

Net periodic benefit cost for pensions for 2014

In 2014, the Company expects a net periodic benefit cost of approximately \$10 million for all its defined benefit pension plans. The favorable variance compared to 2013 is mainly the result of a decrease in the amortization of actuarial losses due to an increase in the discount rate used from 4.15% to 4.73%, partly offset by higher interest costs.

Plan asset allocation

Based on the fair value of the assets held as at December 31, 2013, excluding the economic exposure of derivatives, the assets of the Company's various plans are comprised of 5% in cash and short-term investments, 25% in bonds and mortgages, 41% in equities, 2% in real estate assets, 8% in oil and gas, 5% in infrastructure, 10% in absolute return investments, and 4% in risk-based allocation investments. See Note 11 – Pensions and other postretirement benefits to the Company's 2013 Annual Consolidated Financial Statements for information on the fair value measurements of such assets.

A significant portion of the plans' assets are invested in publicly traded equity securities whose return is primarily driven by stock market performance. Debt securities also account for a significant portion of the plans' investments and provide a partial offset to the variation in the pension benefit obligation that is driven by changes in the discount rate. The funded status of the plan fluctuates with market conditions and impacts funding requirements. The Company will continue to make contributions to the pension plans that as a minimum meet pension legislative requirements.

Rate of compensation increase and health care cost trend rate

The rate of compensation increase is determined by the Company based upon its long-term plans for such increases. For 2013, a rate of compensation increase of 3.00% was used to determine the projected benefit obligation and the net periodic benefit cost.

For postretirement benefits other than pensions, the Company reviews external data and its own historical trends for health care costs to determine the health care cost trend rates. For measurement purposes, the projected health care cost trend rate for prescription drugs was assumed to be 8% in 2013, and it is assumed that the rate will decrease gradually to 4.5% in 2028 and remain at that level thereafter.

For the year ended December 31, 2013, a one-percentage-point change in either the rate of compensation increase or the health care cost trend rate would not cause a material change to the Company's net periodic benefit cost for both pensions and other postretirement benefits.

Funding of pension plans

For accounting purposes, the funded status is calculated under generally accepted accounting principles for all pension plans. For funding purposes, the funded status is also calculated under going-concern and solvency scenarios as prescribed under pension legislation and subject to guidance issued by the Canadian Institute of Actuaries (CIA) for all of the registered Canadian defined benefit pension plans. The Company's funding requirements are determined upon completion of actuarial valuations. Actuarial valuations are generally required on an annual basis for all Canadian plans, or when deemed appropriate by the OSFI.

The Company's latest actuarial valuations for funding purposes conducted as at December 31, 2012 indicated a funding excess on a going-concern basis of approximately \$1.4 billion and a funding deficit on a solvency basis of approximately \$2.1 billion. The Company's next actuarial valuations required as at December 31, 2013 will be performed in 2014. These actuarial valuations are expected to identify a going-concern surplus of approximately \$1.7 billion, while on a solvency basis a funding deficit of approximately \$1.7 billion is expected due to the level of interest rates applicable at their respective measurement dates. The federal pension legislation requires funding deficits, as calculated under

current pension regulations, to be paid over a number of years. Actuarial valuations are also required annually for the Company's U.S. pension plans.

In 2013, in anticipation of its future funding requirements, the Company made voluntary contributions of \$100 million in excess of the required contributions to strengthen the financial position of its main pension plan, the CN Pension Plan. These contributions can be treated as a prepayment against its future required special solvency payments. As at December 31, 2013, the Company had \$470 million of accumulated prepayments which remain available to offset future required solvency deficit payments. The Company expects to use approximately \$335 million of these prepayments to satisfy its 2014 required solvency deficit payment. As a result, the Company's cash contributions for 2014 are expected to be approximately \$130 million, for all the Company's pension plans. The Company expects cash from operations and its other sources of financing to be sufficient to meet its 2014 funding obligations.

Adverse changes to the assumptions used to calculate the Company's funding status, particularly the discount rate, as well as changes to existing federal pension legislation could significantly impact the Company's future contributions.

Information disclosed by major pension plan

The following table provides the Company's plan assets by category, projected benefit obligation at end of year, as well as Company and employee contributions by major defined benefit pension plan:

<i>In millions</i>	<i>December 31, 2013</i>	CN Pension Plan	BC Rail Ltd Pension Plan	U.S. and other plans	Total
Plan assets by category					
Cash and short-term investments		\$ 852	\$ 31	\$ 14	\$ 897
Bonds		3,834	163	88	4,085
Mortgages		160	5	1	166
Equities		6,566	212	110	6,888
Real estate		288	10	1	299
Oil and gas		1,329	46	5	1,380
Infrastructure		758	27	3	788
Absolute return		1,638	53	7	1,698
Risk-based allocation		586	19	2	607
Other ⁽¹⁾		48	2	11	61
Total plan assets		\$ 16,059	\$ 568	\$ 242	\$ 16,869
Projected benefit obligation at end of year		\$ 14,458	\$ 513	\$ 539	\$ 15,510
Company contributions in 2013		\$ 197	\$ 1	\$ 28	\$ 226
Employee contributions in 2013		\$ 56	\$ -	\$ -	\$ 56

(1) Other consists of operating assets of \$85 million (\$94 million in 2012) and liabilities of \$24 million (\$93 million in 2012) required to administer the trust funds' investment assets and the plans' benefit and funding activities.

Additional disclosures are provided in Note 11 – Pensions and other postretirement benefits to the Company's 2013 Annual Consolidated Financial Statements.

Income taxes

The Company follows the asset and liability method of accounting for income taxes. Under the asset and liability method, the change in the net deferred income tax asset or liability is included in the computation of Net income or Other comprehensive income (loss). Deferred income tax assets and liabilities are measured using enacted income tax rates expected to apply to taxable income in the years in which temporary differences are expected to be recovered or settled. As a result, a projection of taxable income is required for those years, as well as an assumption of the ultimate recovery/settlement period for temporary differences. The projection of future taxable income is based on management's best estimate and may vary from actual taxable income. On an annual basis, the Company assesses the need to establish a valuation allowance for its deferred income tax assets, and if it is deemed more likely than not that its deferred income tax assets will not be realized, a valuation allowance is recorded. The ultimate realization of deferred income tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversals of deferred income tax liabilities including the available carryback and carryforward periods, projected future taxable income, and tax planning strategies in making this assessment. As at December 31, 2013, in order to fully realize all of the deferred income tax assets, the Company will need to generate future taxable income of approximately \$1.6 billion and, based upon the level of historical taxable income and projections of future taxable income over the periods in which the deferred income tax assets are deductible, management believes it is more likely than not that the Company will realize the benefits of these deductible differences. Management has assessed the impacts of the current economic environment and concluded there are no significant impacts to its assertions for the realization of deferred income tax assets.

In addition, Canadian, or domestic, tax rules and regulations, as well as those relating to foreign jurisdictions, are subject to interpretation and require judgment by the Company that may be challenged by the taxation authorities upon audit of the filed income tax returns. Tax benefits are recognized if it is more likely than not that the tax position will be sustained on examination by the taxation authorities. As at December 31, 2013, the total amount of gross unrecognized tax benefits was \$30 million before considering tax treaties and other arrangements between taxation authorities. The amount of net unrecognized tax benefits as at December 31, 2013 was \$25 million. If recognized, all of the net unrecognized tax benefits as at December 31, 2013 would affect the effective tax rate. The Company believes that it is reasonably possible that approximately \$8 million of the net unrecognized tax benefits as at December 31, 2013 related to various federal, state, and provincial income tax matters, each of which are individually insignificant, may be recognized over the next twelve months as a result of settlements and a lapse of the applicable statute of limitations. In Canada, the

Company's federal and provincial income tax returns filed for the years 2007 to 2012 remain subject to examination by the taxation authorities. An examination of the Company's federal income tax returns for the 2009 year is currently in progress and is expected to be completed during 2014. Examinations on specific tax positions taken for federal and provincial income tax returns for the years 2007 and 2008 are currently in progress and are also expected to be completed during 2014. In the U.S., the federal income tax returns filed for the year 2007 as well as for the years 2009 to 2012 remain subject to examination by the taxation authorities, and the state income tax returns filed for the years 2009 to 2012 remain subject to examination by the taxation authorities. An examination of the federal income tax returns for the year 2007 as well as for the years 2009 to 2011 is currently in progress. Examinations of certain state income tax returns by the state taxation authorities are currently in progress. The Company does not anticipate any significant impacts to its results of operations or financial position as a result of the final resolutions of such matters.

The Company's deferred income tax assets are mainly composed of temporary differences related to the pension liability, accruals for personal injury claims and other reserves, other postretirement benefits liability, and net operating losses and tax credit carryforwards. The majority of these accruals will be paid out over the next five years. The Company's deferred income tax liabilities are mainly composed of temporary differences related to properties. The reversal of temporary differences is expected at future-enacted income tax rates which could change due to fiscal budget changes and/or changes in income tax laws. As a result, a change in the timing and/or the income tax rate at which the components will reverse, could materially affect deferred income tax expense as recorded in the Company's results of operations. A one-percentage-point change in the Company's reported effective income tax rate would have the effect of changing the income tax expense by \$36 million in 2013.

From time to time, the federal, provincial, and state governments enact new corporate income tax rates resulting in either lower or higher tax liabilities. Such enactments occurred in each of 2013 and 2012 and resulted in an income tax expense of \$24 million and \$35 million, respectively, with corresponding adjustments to the Company's net deferred income tax liability.

For the year ended December 31, 2013, the Company recorded total income tax expense of \$977 million, of which \$331 million was a deferred income tax expense and included a net income tax recovery of \$7 million which consisted of a \$15 million income tax recovery from the recognition of U.S. state income tax losses and a \$16 million income tax recovery from a revision of the apportionment of U.S. state income taxes which were partly offset by a combined \$24 million income tax expense resulting from the enactment of higher provincial corporate income tax rates. For the year ended December 31, 2012, the Company recorded total income tax expense of \$978 million, of which \$451 million of the reported income tax expense was for deferred income taxes,

and included a net income tax expense of \$28 million, which consisted of a \$35 million income tax expense resulting from the enactment of higher provincial corporate income tax rates that was partly offset by a \$7 million income tax recovery resulting from the recapitalization of a foreign investment. For the year ended December 31, 2011, the Company recorded total income tax expense of \$899 million, of which \$531 million of the reported income tax expense was for deferred income taxes, and included a \$40 million net income tax expense resulting from the enactment of state corporate income tax rate changes and other legislated state tax revisions that was partly offset by an income tax recovery of \$11 million relating to certain fuel costs attributed to various wholly-owned subsidiaries' fuel consumption in prior periods. The Company's net deferred income tax liability at December 31, 2013 was \$6,463 million (\$5,512 million at December 31, 2012). Additional disclosures are provided in Note 13 – Income taxes to the Company's 2013 Annual Consolidated Financial Statements.

Business risks

In the normal course of business, the Company is exposed to various business risks and uncertainties that can have an effect on the Company's results of operations, financial position, or liquidity. While some exposures may be reduced by the Company's risk management strategies, many risks are driven by external factors beyond the Company's control or are of a nature which cannot be eliminated. The following is a discussion of key areas of business risks and uncertainties.

Competition

The Company faces significant competition, including from rail carriers and other modes of transportation, and is also affected by its customers' flexibility to select among various origins and destinations, including ports, in getting their products to market. Specifically, the Company faces competition from Canadian Pacific Railway Company (CP), which operates the other major rail system in Canada and services most of the same industrial areas, commodity resources and population centers as the Company; major U.S. railroads and other Canadian and U.S. railroads; long-distance trucking companies, transportation via the St. Lawrence-Great Lakes Seaway and the Mississippi River and transportation via pipelines. In addition, while railroads must build or acquire and maintain their rail systems, motor carriers and barges are able to use public rights-of-way that are built and maintained by public entities without paying fees covering the entire costs of their usage.

Competition is generally based on the quality and the reliability of the service provided, access to markets, as well as price. Factors affecting the competitive position of customers, including exchange rates and energy cost, could materially adversely affect the demand for goods supplied by the sources served by the Company and, therefore, the Company's volumes, revenues and profit margins. Factors affecting the general market conditions

for our customers can result in an imbalance of transportation capacity relative to demand. An extended period of supply/demand imbalance could negatively impact market rate levels for all transportation services, and more specifically the Company's ability to maintain or increase rates. This, in turn, could materially and adversely affect the Company's business, results of operations or financial position.

The level of consolidation of rail systems in the U.S. has resulted in larger rail systems that are able to offer seamless services in larger market areas and, accordingly, compete effectively with the Company in numerous markets. This requires the Company to consider arrangements or other initiatives that would similarly enhance its own service.

On June 27, 2013, the Department of Justice in Canada notified the Company that the Commissioner of Competition had opened an inquiry into allegations that the Company engaged in tied selling and/or abuse of a dominant position in respect of the rail transportation and transloading of lumber products in western Canada. The Commissioner sought the Company's consent to the issuance of an order under the *Competition Act of Canada* to obtain records and information in furtherance of its inquiry. The Company did not object to the issuance of the order and is fully cooperating with the Competition Bureau's inquiry.

There can be no assurance that the Company will be able to compete effectively against current and future competitors in the transportation industry, and that further consolidation within the transportation industry and legislation allowing for more leniency in size and weight for motor carriers will not adversely affect the Company's competitive position. No assurance can be given that competitive pressures will not lead to reduced revenues, profit margins or both.

Environmental matters

The Company's operations are subject to numerous federal, provincial, state, municipal and local environmental laws and regulations in Canada and the U.S. concerning, among other things, emissions into the air; discharges into waters; the generation, handling, storage, transportation, treatment and disposal of waste, hazardous substances and other materials; decommissioning of underground and aboveground storage tanks; and soil and groundwater contamination. A risk of environmental liability is inherent in railroad and related transportation operations; real estate ownership, operation or control; and other commercial activities of the Company with respect to both current and past operations. As a result, the Company incurs significant operating and capital costs, on an ongoing basis, associated with environmental regulatory compliance and clean-up requirements in its railroad operations and relating to its past and present ownership, operation or control of real property.

While the Company believes that it has identified the costs likely to be incurred for environmental matters in the next several years based on known information, the discovery of new facts,

future changes in laws, the possibility of releases of hazardous materials into the environment and the Company's ongoing efforts to identify potential environmental liabilities that may be associated with its properties may result in the identification of additional environmental liabilities and related costs.

In railroad and related transportation operations, it is possible that derailments or other accidents, including spills and releases of hazardous materials, may occur that could cause harm to human health or to the environment. In addition, the Company is also exposed to potential catastrophic liability risk, faced by the railroad industry generally, in connection with the transportation of toxic inhalation hazard materials such as chlorine and anhydrous ammonia, or other dangerous commodities like crude oil and propane that the Company may be required to transport to the extent of its common carrier obligations. As a result, the Company may incur costs in the future, which may be material, to address any such harm, compliance with laws or other risks, including costs relating to the performance of clean-ups, payment of environmental penalties and remediation obligations, and damages relating to harm to individuals or property.

The environmental liability for any given contaminated site varies depending on the nature and extent of the contamination; the available clean-up techniques; evolving regulatory standards governing environmental liability; and the number of potentially responsible parties and their financial viability. As such, the ultimate cost of addressing known contaminated sites cannot be definitively established. Also, additional contaminated sites yet unknown may be discovered or future operations may result in accidental releases.

While some exposures may be reduced by the Company's risk mitigation strategies (including periodic audits, employee training programs and emergency plans and procedures), many environmental risks are driven by external factors beyond the Company's control or are of a nature which cannot be completely eliminated. Therefore, there can be no assurance, notwithstanding the Company's mitigation strategies, that liabilities or costs related to environmental matters will not be incurred in the future or that environmental matters will not have a material adverse effect on the Company's results of operations, financial position or liquidity, and reputation in a particular quarter or fiscal year.

Personal injury and other claims

In the normal course of business, the Company becomes involved in various legal actions seeking compensatory and occasionally punitive damages, including actions brought on behalf of various purported classes of claimants and claims relating to employee and third-party personal injuries, occupational disease, and property damage, arising out of harm to individuals or property allegedly caused by, but not limited to, derailments or other accidents. The Company maintains provisions for such items, which it considers to be adequate for all of its outstanding or pending claims and benefits from insurance coverage for occurrences in excess of

certain amounts. The final outcome with respect to actions outstanding or pending at December 31, 2013, or with respect to future claims, cannot be predicted with certainty, and therefore there can be no assurance that their resolution will not have a material adverse effect on the Company's results of operations, financial position or liquidity, in a particular quarter or fiscal year.

Labor negotiations

Canadian workforce

As at December 31, 2013, CN employed a total of 16,507 employees in Canada, of which 12,337 were unionized employees. From time to time, the Company negotiates to renew collective agreements with various unionized groups of employees.

On January 31, 2013, the tentative agreement reached on December 21, 2012 between CN and the International Brotherhood of Electrical Workers (IBEW), covering approximately 700 signals and communications employees was ratified. The new collective agreement will expire on December 31, 2016.

On October 30, 2013, a tentative agreement was reached between CN and the Teamsters Canada Rail Conference (TCRC) to renew the collective agreements covering approximately 3,000 mainline conductors and yard crews, which expired on July 22, 2013. On January 31, 2014, CN announced that the TCRC advised the Company that the membership did not ratify the tentative agreement. CN and the TCRC will resume discussions during the week of February 3, 2014.

Disputes relating to the renewal of collective agreements could potentially result in strikes, work stoppages, slowdowns and loss of business. Future labor agreements or renegotiated agreements could increase labor and fringe benefits expenses. There can be no assurance that the Company will be able to renew and have its collective agreements ratified without any strikes or lockouts or that the resolution of these collective bargaining negotiations will not have a material adverse effect on the Company's results of operations or financial position.

U.S. workforce

As at December 31, 2013, CN employed a total of 7,214 employees in the U.S., of which 5,725 were unionized employees.

As of February 3, 2014, the Company had in place agreements with bargaining units representing the entire unionized workforce at Grand Trunk Western Railroad Company (GTW), companies owned by Illinois Central Railroad Company (ICRR), companies owned by Wisconsin Central Ltd. (WC), Bessemer & Lake Erie Railroad Company (BLE) and The Pittsburgh and Conneaut Dock Company (PCD). Agreements in place have various moratorium provisions, ranging from 2010 to 2018, which preserve the status quo in respect of the given collective agreement during the terms of such moratoriums. Some of these agreements are currently under renegotiation.

The general approach to labor negotiations by U.S. Class I railroads is to bargain on a collective national basis. GTW, ICRR, WC,

BLE and PCD have bargained on a local basis rather than holding national, industry-wide negotiations because they believe it results in agreements that better address both the employees' concerns and preferences, and the railways' actual operating environment. However, local negotiations may not generate federal intervention in a strike or lockout situation, since a dispute may be localized. The Company believes the potential mutual benefits of local bargaining outweigh the risks.

Where negotiations are ongoing, the terms and conditions of existing agreements generally continue to apply until new agreements are reached or the processes of the Railway Labor Act have been exhausted.

There can be no assurance that there will not be any work action by any of the bargaining units with which the Company is currently in negotiations or that the resolution of these negotiations will not have a material adverse effect on the Company's results of operations or financial position.

Regulation

The Company's rail operations in Canada are subject to (i) economic regulation by the Canadian Transportation Agency under the Canada Transportation Act (CTA), and (ii) safety regulation by the Federal Minister of Transport under the Railway Safety Act and certain other statutes. The Company's U.S. rail operations are subject to (i) economic regulation by the Surface Transportation Board (STB) and (ii) safety regulation by the Federal Railroad Administration (FRA).

Economic regulation – Canada

The CTA provides rate and service remedies, including final offer arbitration (FOA), competitive line rates and compulsory interswitching. The CTA also regulates the maximum revenue entitlement for the movement of grain, charges for railway ancillary services and noise-related disputes. In addition, various Company business transactions must gain prior regulatory approval, with attendant risks and uncertainties.

On June 26, 2013, the Government enacted Bill C-52 which gives shippers a right to an agreement respecting the level of service to be provided by a railway company. Bill C-52 also sets out a process by which the level of service to be provided by the railway company can be established through an arbitration process in the event that the parties cannot reach agreement through their own commercial negotiations. However, the arbitration process will not be available to a shipper in respect of a matter that is governed by a written agreement between the shipper and the railway company or in respect of traffic that is subject to a decision issued under the final arbitration process.

On November 19, 2013, the Canadian Transportation Agency initiated a consultation on the current approach to determining the adequacy of railway third party liability coverage and solicited input on possible improvements to the current regulatory framework.

No assurance can be given that any current or future legislative action by the federal government or other future government initiatives will not materially adversely affect the Company's results of operations or financial position.

Economic regulation – U.S.

The STB serves as both an adjudicatory and regulatory body and has jurisdiction over railroad rate and service issues and rail restructuring transactions such as mergers, line sales, line construction and line abandonments. As such, various Company business transactions must gain prior regulatory approval, with attendant risks and uncertainties.

The STB has undertaken proceedings in the past few years in a number of areas. On February 24, 2011, the STB held a hearing to review the commodities and forms of service currently exempt from STB regulation and is considering the comments on these matters and may take further action. On May 7, 2012, the STB proposed new regulations concerning the liability of third parties for rail car demurrage providing that any person receiving rail cars from a carrier for loading or unloading who detains the cars beyond a specified period of time may be held liable for demurrage if that person has actual notice of the carrier's demurrage tariff providing for such liability prior to the carrier's placement of the cars. On July 25, 2012, following hearings in June 2011 on the state of competition in the railroad industry, the STB commenced a proceeding to consider a proposal by the National Industrial Transportation League for competitive switching. In a first phase, parties submitted at STB's request on March 1, 2013, a wide variety of data to assess the scope and potential impact of the proposal and submitted reply comments on May 30, 2013. It is anticipated that the STB will be holding a hearing in early 2014 to further review these matters. On July 18, 2013, the STB issued a decision raising relief caps and making certain other technical changes for rate complaints brought under its simplified rate guidelines. On December 12, 2013, the STB instituted a proceeding to invite comments on how to ensure its rate complaint procedures are accessible to grain shippers and provide effective protection against unreasonable grain rates. On December 20, 2013, the STB instituted a rulemaking proceeding in response to a petition to abolish the use of a multi-stage discounted cash flow model used in part for determining the rail industry's cost of capital and instead rely exclusively on the Capital Asset Pricing model.

As part of the Passenger Rail Investment and Improvement Act of 2008 (PRIIA), the U.S. Congress has authorized the STB to investigate any railroad over whose track Amtrak operates that fails to meet an 80 percent on-time performance standard for Amtrak operations extending over two calendar quarters and to determine the cause of such failures. Compliance with this mandate began with the third quarter of 2010 and is governed by performance metrics and standards jointly issued by the FRA and Amtrak on May 12, 2010. Should the STB commence an investigation and determine that a failure to meet these standards is due to the host

railroad's failure to provide preference to Amtrak, the STB is authorized to assess damages against the host railroad. On January 19, 2012, Amtrak filed a petition with the STB to commence such an investigation, including a request for damages for preference failures, for allegedly sub-standard performance of Amtrak trains on CN's ICRR and GTW lines. CN responded on March 9, 2012 to Amtrak's petition. CN and Amtrak entered into STB-supervised mediation from April 10, 2012 until October 4, 2012 and the proceedings resumed afterwards. On joint motion of the parties, the STB stayed the proceedings until July 31, 2013. The Company participated in a railroad industry challenge to the constitutionality of the joint FRA/Amtrak performance metrics and standards. On July 2, 2013, the U.S. Court of Appeals for the D.C. Circuit reversed a U.S. District Court decision and determined that Congress' delegation to Amtrak of joint legislative authority with the FRA to promulgate the metrics and standards to be unconstitutional. In light of the Court's decision, and on joint motion of the parties, the STB has stayed the proceedings until July 31, 2014, to provide time that may be necessary for a final resolution on the constitutionality of the metrics and standards pending further appeals. On October 11, 2013, the D.C. Circuit denied the Government's petition for hearing en banc. The Government has until February 7, 2014 to seek U.S. Supreme Court review.

On July 30, 2013, Amtrak filed an application with the STB requesting the agency to set terms and compensation for a new CN/Amtrak Operating Agreement to replace the one that was expiring on August 11, 2013. On August 1, 2013, CN agreed to continue to make its facilities available to Amtrak during the STB's consideration under the terms of the expired agreement.

The U.S. Congress has had under consideration for several years various pieces of legislation that would increase federal economic regulation of the railroad industry. In the current session of Congress, legislation to repeal the rail industry's limited antitrust exemptions (Bill S. 638) has been introduced in the Senate, and there is no assurance that this or other legislation to increase federal economic regulation of the railroad industry will not progress through the legislative process.

The acquisition of the Elgin, Joliet and Eastern Railway Company (EJ&E) in 2009 followed an extensive regulatory approval process by the STB, which included an Environmental Impact Statement (EIS) that resulted in conditions imposed to mitigate municipalities' concerns regarding increased rail activity expected along the EJ&E line (see the section of this MD&A entitled Contractual obligations). The Company accepted the STB-imposed conditions with one exception. The Company filed an appeal at the U.S. Court of Appeals for the District of Columbia Circuit challenging the STB's condition requiring the installation of grade separations at two locations along the EJ&E line at Company funding levels significantly beyond prior STB practice. Appeals were also filed by certain communities challenging the sufficiency of the EIS. On March 15, 2011, the Court denied the CN and community appeals. As such, the Company estimates its total remaining commitment related to

the acquisition to be approximately \$72 million (US\$68 million). The commitment for the grade separation projects is based on estimated costs provided by the STB at the time of acquisition and could be subject to adjustment.

The STB also imposed a five-year monitoring and oversight condition, subsequently extended to six years, during which the Company is required to file with the STB monthly operational reports as well as quarterly reports on the implementation status of the STB-imposed mitigation conditions. This permits the STB to take further action if there is a material change in the facts and circumstances upon which it relied in imposing the specific mitigation conditions. On November 8, 2012, the STB denied the request of the Village of Barrington, IL that the STB impose additional mitigation that would require CN to fund the full cost of a grade separation at a location along the EJ&E line in Barrington. On December 26, 2012, the Village appealed the STB's decision to the U.S. Court of Appeals for the D.C. Circuit. Oral arguments were heard on November 15, 2013 and a decision is expected in early 2014.

A first oversight audit of the Company's EJ&E's operational and environmental reporting was completed in April 2010, and after public comment was finalized by the STB in December 2010. In December 2011, the STB directed a second oversight audit that commenced on February 17, 2012, that audit was completed on April 30, 2012, and released publicly by the STB on June 18, 2012.

The resolution of matters that could arise during the STB's remaining oversight of the transaction cannot be predicted with certainty, and therefore, there can be no assurance that their resolution will not have a material adverse effect on the Company's financial position or results of operations.

The Company's ownership of the former Great Lakes Transportation vessels is subject to regulation by the U.S. Coast Guard (USCG) and the Department of Transportation, Maritime Administration, which regulate the ownership and operation of vessels operating on the Great Lakes and in U.S. coastal waters. In addition, the Environmental Protection Agency (EPA) has authority to regulate air emissions from these vessels. Regulatory initiatives of these U.S. government agencies may materially adversely affect the Company's financial position or results of operations.

On November 8, 2011, the Federal Maritime Commission (FMC), which has authority over oceanborne transport of cargo into and out of the U.S., initiated a Notice of Inquiry to examine whether the U.S. Harbor Maintenance Tax (HMT) and other factors may be contributing to the diversion of U.S.-bound cargo to Canadian and Mexican seaports, which could affect CN rail operations. The Company filed comments in this proceeding on January 9, 2012. In July 2012, the FMC issued its study, which found that carriers shipping cargo through Canadian or Mexican ports violate no U.S. law, treaty, agreement, or FMC regulation. The report stated, however, that the HMT is one of many factors affecting the increased use of foreign ports for cargo bound for U.S. destinations and that amendment of the current HMT

structure should be considered so as to assist U.S. seaports. On September 17, 2013, the Maritime Goods Movement Act (Bill S. 1509) was introduced and assigned to a congressional committee for consideration. The bill proposes to replace the HMT with a Maritime Goods Movement Fee which would be imposed on any U.S.-destined cargo regardless of its point of entry into North America. Among the bill's goals is to discourage diversion of U.S.-bound goods through Canadian or Mexican ports.

No assurance can be given that any future regulatory or legislative initiatives by the U.S. federal government related to this inquiry and proposed legislation will not materially adversely affect the Company's results of operations or its competitive and financial position.

Safety regulation – Canada

Rail safety regulation in Canada is the responsibility of Transport Canada, which administers the Canadian Railway Safety Act, as well as the rail portions of other safety-related statutes. On May 1, 2013, Bill S-4 came into force which prohibits anyone from operating a railway without having first obtained a Railway Operating Certificate issued by the Minister. The Bill also includes the ability for the government to establish Administrative Monetary Penalties in the event of contravention of prescribed provisions of the Act or regulations.

On July 23, 2013, following a significant derailment involving a non-related short-line railroad within the Province of Quebec ("Lac-Mégantic derailment"), the Federal Minister of Transport issued an Emergency Directive under the Canada Railway Safety Act to enhance the effectiveness of train securement procedures and safety across the Canadian rail industry and to help reduce the risk of unintended train movements that can lead to catastrophic accidents. CN has reviewed its safety policies for unattended trains and adjusted its safety practices to comply with Transport Canada's order. Transport Canada also issued an order requiring all federal railways to formulate or revise rules, as the case may be, respecting the securement of unattended locomotives and crew size requirements. On November 20, 2013, the Railway Association of Canada filed revised rules on behalf of CN and its other member railway companies in compliance with this order. On December 26, 2013, the Minister issued a notice approving the revised rules.

On November 20, 2013, the Federal Minister of Transport issued Protective Direction No. 32 under the Transportation of Dangerous Goods Act, requiring railway companies to provide designated municipal emergency planning officials with yearly aggregate information on the nature and volume of dangerous goods the company transports by rail through the municipality.

On January 23, 2014, the Transportation Safety Board of Canada (TSB) issued a series of recommendations to Transport Canada to improve the safe transportation of crude oil by rail. The TSB recommendations call for: (1) tougher standards for Class 111

tank cars; (2) route planning and analysis; and (3) emergency response assistance plans.

In 2014, Transport Canada is expected to finalize new regulations for highway-railway crossings. These will specify specific standards for new crossings and require that existing crossings be upgraded to basic safety standards within seven years.

Safety regulation – U.S.

Rail safety regulation in the U.S. is the responsibility of the FRA, which administers the Federal Railroad Safety Act, as well as the rail portions of other safety statutes. In 2008, the U.S. federal government enacted legislation reauthorizing the Federal Railroad Safety Act. This legislation covers a broad range of safety issues, including fatigue management, Positive Train Control (PTC), grade crossings, bridge safety, and other matters. The legislation requires all Class I railroads and intercity passenger and commuter railroads to implement a PTC system by December 31, 2015 on mainline track where intercity passenger railroads and commuter railroads operate and where toxic inhalation hazard materials are transported. PTC is a collision avoidance technology intended to override locomotive controls and stop a train before an accident. The Company is taking steps to ensure implementation of PTC in accordance with the new law, including working with other Class I railroads to satisfy the requirements for U.S. network interoperability. The Company's PTC Implementation Plan, submitted in April 2010, has been approved by the FRA. CN's total implementation costs associated with PTC are estimated to be US\$335 million. The legislation also caps the number of on-duty and limbo time hours for certain rail employees on a monthly basis. The Company is taking appropriate steps and is working with the FRA to ensure that its operations conform to the law's requirements.

In August 2012, the FRA reported an update of the PTC implementation progress to Congress concluding that the majority of the carriers would be unable to meet the December 31, 2015 implementation deadline. In August 2013, legislation was introduced in the Senate that would delay PTC implementation by five years to the end of 2020, and in the same month, the U.S. Government Accountability Office published a report recommending that Congress give the FRA authority to extend the deadline for individual carriers on a case-by-case basis.

The suspension by the Federal Communication Commission (FCC) in May 2013 of its normal processes to review possible impacts to tribal historic and cultural artifacts of the installation of tens of thousands of poles industry-wide that are required to host PTC radio operations, and the uncertainty of yet-to-be determined changes to those procedures needed to accommodate that volume, may further threaten the PTC implementation deadline.

In the aftermath of the July 2013 Lac-Mégantic derailment, the FRA issued Emergency Order No. 28, Notice No. 1 on August 2, 2013 directing that railroads take specific actions regarding unattended trains transporting specified hazardous materials, including securement of these trains. That same day, FRA and the

Pipeline and Hazardous Materials Safety Administration (PHMSA) issued Safety Advisory 2013-06, which made recommendations to railroads on issues including crew staffing practices and operational testing to ensure employees' compliance with securement-related rules, as well as recommendations to shippers of crude oil to be transported by rail. In addition, the railroad industry has acted on its own to enhance rail safety in light of the Lac-Mégantic derailment and fire. Effective August 5, 2013, the Association of American Railroads (AAR) amended the industry's Recommended Railroad Operating Practices for Transportation of Hazardous Materials (Circular No. OT-55-N) by expanding the definition of a "key train" (for which heightened operating safeguards are required) to include trains carrying one tank car load of poison or toxic inhalation hazard, anhydrous ammonia, or ammonia solutions and to include trains carrying 20 car loads or portable tank loads of any combination of hazardous materials (including ethanol and crude oil).

On August 12, 2013, the FRA established the Railroad Safety Advisory Committee (RSAC) to provide advice and recommendations to the FRA on railroad safety matters. The FRA's Emergency Order No. 28 resulted in four new tasks accepted by the RSAC. The four tasks are: train crew size; operational testing for securement; securement; and hazardous material issues. The FRA has asked RSAC's four task groups to conclude meetings by April 2014 and submit their recommendations to the FRA for drafting Emergency Order No. 28 into new regulation. CN is an active participant in all four task groups.

On September 6, 2013, PHMSA published an Advance Notice of Proposed Rulemaking considering improvement of the regulations related to the transportation by rail of hazardous materials in tank cars. On November 14, 2013, CN was a participant in AAR's comments filed with PHMSA in this proceeding, which urged PHMSA to require that all tank cars used to transport flammable liquids be retrofitted or phased out, and that new cars be built to more stringent standards. The AAR comments included specific tank cars safety standard improvements, which AAR maintained will substantially decrease the likelihood of a release if a tank car is involved in an accident.

On January 23, 2014 the National Transportation Safety Board (NTSB) issued a series of recommendations to the U.S. Department of Transportation, to address the safety risk of transporting crude oil by rail. The NTSB's recommendations complement those issued by the TSB and specifically: (1) require expanded hazardous materials route planning for railroads to avoid populated and other sensitive areas; (2) development of an FRA/PHMSA audit program to ensure that railroads carrying petroleum products have adequate emergency response capabilities to address worst-case discharges of the product; and (3) require audits of shippers and railroads to ensure that they are properly classifying hazardous materials being transported and that they have adequate safety and security plans in place.

No assurance can be given that these or any future regulatory initiatives by the Canadian and U.S. federal governments will not materially adversely affect the Company's results of operations, or its competitive and financial position.

Security

The Company is subject to statutory and regulatory directives in the U.S. addressing homeland security concerns. In the U.S., safety matters related to security are overseen by the Transportation Security Administration (TSA), which is part of the U.S. Department of Homeland Security (DHS) and the PHMSA, which, like the FRA, is part of the U.S. Department of Transportation. Border security falls under the jurisdiction of U.S. Customs and Border Protection (CBP), which is part of the DHS. In Canada, the Company is subject to regulation by the Canada Border Services Agency (CBSA). More specifically, the Company is subject to:

- (i) Border security arrangements, pursuant to an agreement the Company and CP entered into with the CBP and the CBSA.
- (ii) The CBP's Customs-Trade Partnership Against Terrorism (C-TPAT) program and designation as a low-risk carrier under CBSA's Customs Self-Assessment (CSA) program.
- (iii) Regulations imposed by the CBP requiring advance notification by all modes of transportation for all shipments into the U.S. The CBSA is also working on similar requirements for Canada-bound traffic.
- (iv) Inspection for imported fruits and vegetables grown in Canada and the agricultural quarantine and inspection (AQI) user fee for all traffic entering the U.S. from Canada.

The Company has worked with the AAR to develop and put in place an extensive industry-wide security plan to address terrorism and security-driven efforts by state and local governments seeking to restrict the routings of certain hazardous materials. If such state and local routing restrictions were to go into force, they would be likely to add to security concerns by foreclosing the Company's most optimal and secure transportation routes, leading to increased yard handling, longer hauls, and the transfer of traffic to lines less suitable for moving hazardous materials, while also infringing upon the exclusive and uniform federal oversight over railroad security matters.

Transportation of hazardous materials

The Company may be required to transport toxic inhalation hazard materials to the extent of its common carrier obligations and, as such, is exposed to additional regulatory oversight.

- (i) The PHMSA requires carriers operating in the U.S. to report annually the volume and route-specific data for cars containing these commodities; conduct a safety and security risk analysis for each used route; identify a commercially practicable alternative route for each used route; and select for use the practical route posing the least safety and security risk.

- (ii) The TSA requires rail carriers to provide upon request, within five minutes for a single car and 30 minutes for multiple cars, location and shipping information on cars on their networks containing toxic inhalation hazard materials and certain radioactive or explosive materials; and ensure the secure, attended transfer of all such cars to and from shippers, receivers and other carriers that will move from, to, or through designated high-threat urban areas.
- (iii) The PHMSA has issued regulations to enhance the crash-worthiness protection of tank cars used to transport toxic inhalation hazard materials and to limit the operating conditions of such cars.
- (iv) In Canada, the Transportation of Dangerous Goods Act establishes the safety requirements for the transportation of goods classified as dangerous and enables the establishment of regulations for security training and screening of personnel working with dangerous goods, as well as the development of a program to require a transportation security clearance for dangerous goods and that dangerous goods be tracked during transport.

While the Company will continue to work closely with the CBSA, CBP, and other Canadian and U.S. agencies, as described above, no assurance can be given that these and future decisions by the U.S., Canadian, provincial, state, or local governments on homeland security matters, legislation on security matters enacted by the U.S. Congress or Parliament, or joint decisions by the industry in response to threats to the North American rail network, will not materially adversely affect the Company's results of operations, or its competitive and financial position.

Radio communications

The Company uses radios for a variety of operational purposes. Licenses for these activities, as well as the transfer or assignment of these licenses, require authorization of the FCC. The Company uncovered a number of instances where such authorization was not obtained and disclosed those instances to the FCC on a voluntary basis. The Company is undertaking a number of corrective actions with the FCC to address the situation, the whole without prejudice to a future FCC enforcement action and the imposition of fines.

Other risks

Economic conditions

The Company, like other railroads, is susceptible to changes in the economic conditions of the industries and geographic areas that produce and consume the freight it transports or the supplies it requires to operate. In addition, many of the goods and commodities carried by the Company experience cyclicity in demand. Many of the bulk commodities the Company transports move offshore and are affected more by global rather than North American economic conditions. Adverse North American and global economic conditions, or economic or industrial restructuring, that affect the producers

and consumers of the commodities carried by the Company, including customer insolvency, may have a material adverse effect on the volume of rail shipments and/or revenues from commodities carried by the Company, and thus materially and negatively affect its results of operations, financial position, or liquidity.

Pensions

Overall returns in the capital markets and the level of interest rates affect the funded status of the Company's defined benefit pension plans.

For accounting purposes, the funded status of all pension plans is calculated at the measurement date, which for the Company is December 31, using generally accepted accounting principles. Adverse changes with respect to pension plan returns and the level of interest rates from the last measurement date may have a material adverse effect on the funded status and significantly impact future pension expense.

For funding purposes, the funded status of the Canadian pension plans is calculated to determine the required level of contributions using going-concern and solvency scenarios as prescribed under pension legislation and subject to guidance issued by the Canadian Institute of Actuaries (CIA). Adverse changes with respect to pension plan returns and the level of interest rates from the date of the last actuarial valuations as well as changes to existing federal pension legislation may significantly impact future pension contributions and have a material adverse effect on the funded status of the plans and the Company's results of operations. The Company's funding requirements are determined upon completion of actuarial valuations which are generally required on an annual basis for all Canadian plans, or when deemed appropriate by the OSFI. The latest actuarial valuations for funding purposes for the Company's Canadian pension plans, based on a valuation date of December 31, 2012, were filed in June 2013 and identified a going-concern surplus of approximately \$1.4 billion and a solvency deficit of approximately \$2.1 billion calculated using the three-year average of the Company's hypothetical wind-up ratio in accordance with the *Pension Benefit Standards Regulations, 1985*. Under Canadian legislation, the solvency deficit is required to be funded through special solvency payments, for which each annual amount is equal to one fifth of the solvency deficit, and is re-established at each valuation date. Actuarial valuations are also required annually for the Company's U.S. pension plans.

In anticipation of its future funding requirements, the Company may occasionally make voluntary contributions in excess of the required contributions mainly to strengthen the financial position of its main pension plan, the CN Pension Plan. The Company has been advised by the OSFI that voluntary contributions can be treated as a prepayment against the Company's required special solvency payments and as at December 31, 2013, the Company had approximately \$470 million of accumulated prepayments which remain available to offset future required solvency deficit payments. Pension contributions made in 2013 and 2012 of

\$226 million and \$833 million, respectively, mainly represent contributions to the Company's main pension plan, the CN Pension Plan and include voluntary contributions of \$100 million and \$700 million, respectively. The pension contributions also include contributions for the current service cost as determined under the Company's current actuarial valuations for funding purposes.

On July 31, 2013, the CIA published a draft report for comment on Canadian Pensioners Mortality. Final guidance on mortality assumptions is expected in early 2014. The report contains proposed Canadian pensioners mortality tables and improvement scales based on experience studies conducted by the CIA. Based on the CIA's report, the overall level of recent mortality experience is significantly lower than that anticipated by the current mortality tables which are commonly used. Furthermore, improvement rates experienced in recent years have been substantially higher than current projections. Based on the draft CIA's report and CN's experience, revised mortality tables and improvement scales that were used for the 2013 year end accounting valuation increased the Company's projected benefit obligation as at December 31, 2013.

The Company expects cash from operations and its other sources of financing to be sufficient to meet its funding obligations.

Trade restrictions

Global as well as North American trade conditions, including trade barriers on certain commodities, may interfere with the free circulation of goods across Canada and the U.S.

Terrorism and international conflicts

Potential terrorist actions can have a direct or indirect impact on the transportation infrastructure, including railway infrastructure in North America, and can interfere with the free flow of goods. Rail lines, facilities and equipment could be directly targeted or become indirect casualties, which could interfere with the free flow of goods. International conflicts can also have an impact on the Company's markets. Government response to such events could adversely affect the Company's operations. Insurance premiums could also increase significantly or coverage could become unavailable.

Customer credit risk

In the normal course of business, the Company monitors the financial condition and credit limits of its customers and reviews the credit history of each new customer. Although the Company believes there are no significant concentrations of credit risk, economic conditions can affect the Company's customers and can result in an increase to the Company's credit risk and exposure to the business failures of its customers. To manage its credit risk on an ongoing basis, the Company's focus is on keeping the average daily sales outstanding within an acceptable range and working with customers to ensure timely payments, and in certain cases, requiring financial security, including letters of credit. A widespread deterioration of customer credit and business failures of

customers could have a material adverse effect on the Company's results of operations, financial position or liquidity.

Liquidity

Disruptions in the financial markets or deterioration of the Company's credit ratings could hinder the Company's access to external sources of funding to meet its liquidity needs. There can be no assurance that changes in the financial markets will not have a negative effect on the Company's liquidity and its access to capital at acceptable rates.

Supplier risk

The Company operates in a capital-intensive industry where the complexity of rail equipment limits the number of suppliers available. The supply market could be disrupted if changes in the economy caused any of the Company's suppliers to cease production or to experience capacity or supply shortages. This could also result in cost increases to the Company and difficulty in obtaining and maintaining the Company's rail equipment and materials. Since the Company also has foreign suppliers, international relations, trade restrictions and global economic and other conditions may potentially interfere with the Company's ability to procure necessary equipment. To manage its supplier risk, it is the Company's long-standing practice to ensure that more than one source of supply for a key product or service, where feasible, is available. Widespread business failures of, or restrictions on suppliers, could have a material adverse effect on the Company's results of operations or financial position.

Availability of qualified personnel

The Company, like other companies in North America, may experience demographic challenges in the employment levels of its workforce. Changes in employee demographics, training requirements and the availability of qualified personnel, particularly locomotive engineers and trainmen, could negatively impact the Company's ability to meet demand for rail service. The Company expects that approximately 40% of its workforce will be eligible to retire or leave through normal attrition (death, termination, resignation) within the next five-year period. The Company monitors employment levels to ensure that there is an adequate supply of personnel to meet rail service requirements. However, the Company's efforts to attract and retain qualified personnel may be hindered by specific conditions in the job market. No assurance can be given that demographic or other challenges will not materially adversely affect the Company's results of operations or its financial position.

Fuel costs

The Company, like other railroads, is susceptible to the volatility of fuel prices due to changes in the economy or supply disruptions. Fuel shortages can occur due to refinery disruptions, production quota restrictions, climate, and labor and political instability. Rising fuel prices could materially adversely affect the Company's expenses. As such, CN has implemented a fuel surcharge program with a

view of offsetting the impact of rising fuel prices. The surcharge applied to customers is determined in the second calendar month prior to the month in which it is applied, and is calculated using the average monthly price of West-Texas Intermediate crude oil (WTI) for revenue-based tariffs and On-Highway Diesel (OHD) for mileage-based tariffs. Increases in fuel prices or supply disruptions may materially adversely affect the Company's results of operations, financial position or liquidity.

Foreign currency

The Company conducts its business in both Canada and the U.S. and as a result, is affected by currency fluctuations. The estimated annual impact on net income of a year-over-year one-cent change in the Canadian dollar relative to the US dollar is in the range of \$10 million to \$15 million. Changes in the exchange rate between the Canadian dollar and other currencies (including the US dollar) make the goods transported by the Company more or less competitive in the world marketplace and thereby may adversely affect the Company's revenues and expenses.

Reliance on technology

The Company relies on information technology in all aspects of its business. While the Company has business continuity and disaster recovery plans, as well as other mitigation programs in place, a cyber security attack and significant disruption or failure of its information technology and communications systems could result in service interruptions, safety failures, security violations, regulatory compliance failures or other operational difficulties and compromise corporate information and assets against intruders and, as such, could adversely affect the Company's results of operations, financial position or liquidity. If the Company is unable to acquire or implement new technology, it may suffer a competitive disadvantage, which could also have an adverse effect on the Company's results of operations, financial position or liquidity.

Transportation network disruptions

Due to the integrated nature of the North American freight transportation infrastructure, the Company's operations may be negatively affected by service disruptions of other transportation links such as ports and other railroads which interchange with the Company. A significant prolonged service disruption of one or more of these entities could have an adverse effect on the Company's results of operations, financial position or liquidity. Furthermore, deterioration in the cooperative relationships with the Company's connecting carriers could directly affect the Company's operations.

Weather and climate change

The Company's success is dependent on its ability to operate its railroad efficiently. Severe weather and natural disasters, such as extreme cold or heat, flooding, drought, hurricanes and earthquakes, can disrupt operations and service for the railroad, affect the performance of locomotives and rolling stock, as well as disrupt operations for both the

Company and its customers. Climate change, including the impact of global warming, has the potential physical risk of increasing the frequency of adverse weather events, which can disrupt the Company's operations, damage its infrastructure or properties, or otherwise have a material adverse effect on the Company's results of operations, financial position or liquidity. In addition, although the Company believes that the growing support for climate change legislation is likely to result in changes to the regulatory framework in Canada and the U.S., it is too early to predict the manner or degree of such impact on the Company at this time. Restrictions, caps, taxes, or other controls on emissions of greenhouse gasses, including diesel exhaust, could significantly increase the Company's capital and operating costs or affect the markets for, or the volume of, the goods the Company carries thereby resulting in a material adverse effect on operations, financial position, results of operations or liquidity. More specifically, climate change legislation and regulation could (a) affect CN's utility coal customers due to coal capacity being replaced with natural gas generation and renewable energy; (b) make it difficult for CN's customers to produce products in a cost-competitive manner due to increased energy costs; and (c) increase legal costs related to defending and resolving legal claims and other litigation related to climate change.

Controls and procedures

The Company's Chief Executive Officer and its Chief Financial Officer, after evaluating the effectiveness of the Company's "disclosure controls and procedures" (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) as of December 31, 2013, have concluded that the Company's disclosure controls and procedures were effective.

During the fourth quarter ended December 31, 2013, there was no change in the Company's internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

As of December 31, 2013, management has assessed the effectiveness of the Company's internal control over financial reporting using the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in Internal Control – Integrated Framework (1992). Based on this assessment, management has determined that the Company's internal control over financial reporting was effective as of December 31, 2013, and issued Management's Report on Internal Control over Financial Reporting dated February 3, 2014 to that effect.

The Company's 2013 Annual Information Form (AIF) and Form 40-F, may be found on SEDAR at www.sedar.com and on EDGAR at www.sec.gov, respectively. Copies of such documents, as well as the Company's Notice of Intention to Make a Normal Course Issuer Bid, may be obtained by contacting the Corporate Secretary's office.

Montreal, Canada
February 3, 2014

Management is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements.

Management has assessed the effectiveness of the Company's internal control over financial reporting as of December 31, 2013 using the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in Internal Control – Integrated Framework (1992). Based on this assessment, management has determined that the Company's internal control over financial reporting was effective as of December 31, 2013.

KPMG LLP, an independent registered public accounting firm, has issued an unqualified audit report on the effectiveness of the Company's internal control over financial reporting as of December 31, 2013 and has also expressed an unqualified audit opinion on the Company's 2013 consolidated financial statements as stated in their Reports of Independent Registered Public Accounting Firm dated February 3, 2014.



Claude Mongeau
President and Chief Executive Officer

February 3, 2014



Luc Jobin
Executive Vice-President and Chief Financial Officer

February 3, 2014

To the Shareholders and Board of Directors of the Canadian National Railway Company

We have audited the accompanying consolidated balance sheets of the Canadian National Railway Company (the "Company") as of December 31, 2013 and 2012, and the related consolidated statements of income, comprehensive income, changes in shareholders' equity and cash flows for each of the years in the three-year period ended December 31, 2013. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company as of December 31, 2013 and 2012, and its consolidated results of operations and its consolidated cash flows for each of the years in the three-year period ended December 31, 2013, in conformity with United States generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company's internal control over financial reporting as of December 31, 2013, based on criteria established in Internal Control – Integrated Framework (1992) issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO"), and our report dated February 3, 2014 expressed an unqualified opinion on the effectiveness of the Company's internal control over financial reporting.



KPMG LLP*

Montreal, Canada
February 3, 2014

* FCPA auditor, FCA, public accountancy permit No. A106087

KPMG LLP is a Canadian limited liability partnership and a member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity.

KPMG Canada provides services to KPMG LLP.

To the Shareholders and Board of Directors of the Canadian National Railway Company

We have audited the Canadian National Railway Company's (the "Company") internal control over financial reporting as of December 31, 2013, based on criteria established in Internal Control – Integrated Framework (1992) issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO"). The Company's management is responsible for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial

reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2013, based on criteria established in Internal Control – Integrated Framework (1992) issued by the COSO.

We also have audited, in accordance with Canadian generally accepted auditing standards and the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of the Company as of December 31, 2013 and 2012, and the related consolidated statements of income, comprehensive income, changes in shareholders' equity and cash flows for each of the years in the three-year period ended December 31, 2013, and our report dated February 3, 2014 expressed an unqualified opinion on those consolidated financial statements.



KPMG LLP*

Montreal, Canada

February 3, 2014

* FCPA auditor, FCA, public accountancy permit No. A106087

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KPMG Canada provides services to KPMG LLP.

Consolidated Statement of Income

<i>In millions, except per share data</i>	<i>Year ended December 31,</i>	2013	2012	2011
Revenues		\$ 10,575	\$ 9,920	\$ 9,028
Operating expenses				
Labor and fringe benefits		2,182	1,952	1,812
Purchased services and material		1,351	1,248	1,120
Fuel		1,619	1,524	1,412
Depreciation and amortization		980	924	884
Equipment rents		275	249	228
Casualty and other		295	338	276
<i>Total operating expenses</i>		6,702	6,235	5,732
<i>Operating income</i>		3,873	3,685	3,296
Interest expense		(357)	(342)	(341)
Other income (Note 12)		73	315	401
<i>Income before income taxes</i>		3,589	3,658	3,356
Income tax expense (Note 13)		(977)	(978)	(899)
<i>Net income</i>		\$ 2,612	\$ 2,680	\$ 2,457
<i>Earnings per share (Note 15)</i>				
Basic		\$ 3.10	\$ 3.08	\$ 2.72
Diluted		\$ 3.09	\$ 3.06	\$ 2.70
<i>Weighted-average number of shares (Note 15)</i>				
Basic		843.1	871.1	902.2
Diluted		846.1	875.4	908.9

See accompanying notes to consolidated financial statements.

Consolidated Statement of Comprehensive Income

<i>In millions</i>	<i>Year ended December 31,</i>	2013	2012	2011
Net income		\$ 2,612	\$ 2,680	\$ 2,457
Other comprehensive income (loss) (Note 18)				
Foreign exchange gain (loss) on:				
Translation of the net investment in foreign operations		440	(128)	130
Translation of US dollar-denominated long-term debt designated as a hedge of the net investment in U.S. subsidiaries		(394)	123	(122)
Pension and other postretirement benefit plans (Note 11):				
Net actuarial gain (loss) arising during the year		1,544	(660)	(1,541)
Prior service cost arising during the year		-	(6)	(28)
Amortization of net actuarial loss included in net periodic benefit cost (income)		226	119	8
Amortization of prior service cost included in net periodic benefit cost (income)		5	7	4
Derivative instruments (Note 17)		-	-	(2)
<i>Other comprehensive income (loss) before income taxes</i>		1,821	(545)	(1,551)
Income tax recovery (expense)		(414)	127	421
<i>Other comprehensive income (loss)</i>		1,407	(418)	(1,130)
<i>Comprehensive income</i>		\$ 4,019	\$ 2,262	\$ 1,327

See accompanying notes to consolidated financial statements.

Consolidated Balance Sheet

<i>In millions</i>	<i>December 31,</i>	2013	2012
Assets			
Current assets			
Cash and cash equivalents	\$	214	\$ 155
Restricted cash and cash equivalents <i>(Note 8)</i>		448	521
Accounts receivable <i>(Note 3)</i>		815	831
Material and supplies		274	230
Deferred and receivable income taxes <i>(Note 13)</i>		137	43
Other		89	89
<i>Total current assets</i>		1,977	1,869
Properties <i>(Note 4)</i>		26,227	24,541
Intangible and other assets <i>(Note 5)</i>		1,959	249
<i>Total assets</i>		\$ 30,163	\$ 26,659
Liabilities and shareholders' equity			
Current liabilities			
Accounts payable and other <i>(Note 6)</i>	\$	1,477	\$ 1,626
Current portion of long-term debt <i>(Note 8)</i>		1,021	577
<i>Total current liabilities</i>		2,498	2,203
Deferred income taxes <i>(Note 13)</i>		6,537	5,555
Pension and other postretirement benefits, net of current portion <i>(Note 11)</i>		541	784
Other liabilities and deferred credits <i>(Note 7)</i>		815	776
Long-term debt <i>(Note 8)</i>		6,819	6,323
Shareholders' equity			
Common shares <i>(Note 9)</i>		4,015	4,108
Accumulated other comprehensive loss <i>(Note 18)</i>		(1,850)	(3,257)
Retained earnings		10,788	10,167
<i>Total shareholders' equity</i>		12,953	11,018
<i>Total liabilities and shareholders' equity</i>		\$ 30,163	\$ 26,659

On behalf of the Board:

David G. A. McLean
Director

Claude Mongeau
Director

See accompanying notes to consolidated financial statements.

Consolidated Statement of Changes in Shareholders' Equity

<i>In millions</i>	Issued and outstanding common shares (Note 9)	Common shares	Accumulated other comprehensive loss	Retained earnings	Total shareholders' equity
<i>Balances at December 31, 2010</i>	918.7	\$ 4,252	\$ (1,709)	\$ 8,741	\$ 11,284
Net income	-	-	-	2,457	2,457
Stock options exercised and other (Notes 9, 10)	5.3	74	-	-	74
Share repurchase programs (Note 9)	(39.8)	(185)	-	(1,235)	(1,420)
Other comprehensive loss (Note 18)	-	-	(1,130)	-	(1,130)
Dividends (\$0.65 per share)	-	-	-	(585)	(585)
<i>Balances at December 31, 2011</i>	884.2	4,141	(2,839)	9,378	10,680
Net income	-	-	-	2,680	2,680
Stock options exercised and other (Notes 9, 10)	6.4	128	-	-	128
Share repurchase programs (Note 9)	(33.8)	(161)	-	(1,239)	(1,400)
Other comprehensive loss (Note 18)	-	-	(418)	-	(418)
Dividends (\$0.75 per share)	-	-	-	(652)	(652)
<i>Balances at December 31, 2012</i>	856.8	4,108	(3,257)	10,167	11,018
Net income	-	-	-	2,612	2,612
Stock options exercised and other (Notes 9, 10)	1.4	40	-	-	40
Share repurchase programs (Note 9)	(27.6)	(133)	-	(1,267)	(1,400)
Other comprehensive income (Note 18)	-	-	1,407	-	1,407
Dividends (\$0.86 per share)	-	-	-	(724)	(724)
<i>Balances at December 31, 2013</i>	830.6	\$ 4,015	\$ (1,850)	\$ 10,788	\$ 12,953

See accompanying notes to consolidated financial statements.

Consolidated Statement of Cash Flows

<i>In millions</i>	<i>Year ended December 31,</i>	2013	2012	2011
Operating activities				
Net income		\$ 2,612	\$ 2,680	\$ 2,457
Adjustments to reconcile net income to net cash provided by operating activities:				
Depreciation and amortization		980	924	884
Deferred income taxes (Note 13)		331	451	531
Gain on disposal of property (Notes 4, 12)		(69)	(281)	(348)
Changes in operating assets and liabilities:				
Accounts receivable		32	(20)	(51)
Material and supplies		(38)	(30)	11
Accounts payable and other		(245)	129	34
Other current assets		13	(13)	(2)
Pensions and other, net		(68)	(780)	(540)
<i>Net cash provided by operating activities</i>		3,548	3,060	2,976
Investing activities				
Property additions		(1,973)	(1,731)	(1,625)
Disposal of property (Note 4)		52	311	369
Change in restricted cash and cash equivalents		73	(22)	(499)
Other, net		(4)	21	26
<i>Net cash used in investing activities</i>		(1,852)	(1,421)	(1,729)
Financing activities				
Issuance of debt (Note 8)		1,850	493	787
Repayment of debt (Note 8)		(1,413)	(140)	(509)
Issuance of common shares due to exercise of stock options and related excess tax benefits realized (Note 10)		31	117	77
Repurchase of common shares (Note 9)		(1,400)	(1,400)	(1,420)
Dividends paid		(724)	(652)	(585)
<i>Net cash used in financing activities</i>		(1,656)	(1,582)	(1,650)
Effect of foreign exchange fluctuations on US dollar-denominated cash and cash equivalents		19	(3)	14
<i>Net increase (decrease) in cash and cash equivalents</i>		59	54	(389)
Cash and cash equivalents, beginning of year		155	101	490
<i>Cash and cash equivalents, end of year</i>		\$ 214	\$ 155	\$ 101
Supplemental cash flow information				
Net cash receipts from customers and other		\$ 10,640	\$ 9,877	\$ 8,995
Net cash payments for:				
Employee services, suppliers and other expenses		(5,558)	(5,241)	(4,643)
Interest		(344)	(364)	(329)
Personal injury and other claims (Note 16)		(61)	(79)	(97)
Pensions (Note 11)		(239)	(844)	(468)
Income taxes (Note 13)		(890)	(289)	(482)
<i>Net cash provided by operating activities</i>		\$ 3,548	\$ 3,060	\$ 2,976

See accompanying notes to consolidated financial statements.

Canadian National Railway Company, together with its wholly-owned subsidiaries, collectively "CN" or "the Company," is engaged in the rail and related transportation business. CN spans Canada and mid-America, from the Atlantic and Pacific oceans to the Gulf of Mexico, serving the ports of Vancouver, Prince Rupert, B.C., Montreal, Halifax, New Orleans and Mobile, Alabama, and the key cities of Toronto, Buffalo, Chicago, Detroit, Duluth, Minnesota/Superior, Wisconsin, Green Bay, Wisconsin, Minneapolis/St. Paul, Memphis, St. Louis, and Jackson, Mississippi, with connections to all points in North America. CN's freight revenues are derived from the movement of a diversified and balanced portfolio of goods, including petroleum and chemicals, grain and fertilizers, coal, metals and minerals, forest products, intermodal and automotive.

1 Summary of significant accounting policies

These consolidated financial statements are expressed in Canadian dollars, except where otherwise indicated, and have been prepared in accordance with United States generally accepted accounting principles (U.S. GAAP). The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of revenues and expenses during the period, the reported amounts of assets and liabilities, and the disclosure of contingent assets and liabilities at the date of the financial statements. On an ongoing basis, management reviews its estimates, including those related to personal injury and other claims, environmental matters, depreciation, pensions and other postretirement benefits, and income taxes, based upon currently available information. Actual results could differ from these estimates.

On October 22, 2013, the Board of Directors of the Company approved a two-for-one common stock split in the form of a stock dividend of one additional common share of CN for each share outstanding, which was paid on November 29, 2013, to shareholders of record on November 15, 2013. All share and per share data presented herein reflect the impact of the stock split.

A. Principles of consolidation

These consolidated financial statements include the accounts of all subsidiaries. The Company's investments in which it has significant influence are accounted for using the equity method and all other investments are accounted for using the cost method.

B. Revenues

Freight revenues are recognized using the percentage of completed service method based on the transit time of freight as it moves from origin to destination. The allocation of revenues between reporting periods is based on the relative transit time in each period with expenses being recorded as incurred. Revenues related to non-rail transportation services are recognized as service is performed or as contractual obligations are met. Revenues are presented net of taxes collected from customers and remitted to governmental authorities.

C. Foreign currency

All of the Company's operations in the United States (U.S.) are self-contained foreign entities with the US dollar as their functional currency. Accordingly, the U.S. operations' assets and liabilities are translated into Canadian dollars at the rate in effect at the balance sheet date and the revenues and expenses are translated at average exchange rates during the year. All adjustments resulting from the translation of the foreign operations are recorded in Other comprehensive income (loss) (see Note 18 – Accumulated other comprehensive loss).

The Company designates the US dollar-denominated long-term debt of the parent company as a foreign currency hedge of its net investment in U.S. subsidiaries. Accordingly, foreign exchange gains and losses, from the dates of designation, on the translation of the US dollar-denominated long-term debt are also included in Other comprehensive income (loss).

D. Cash and cash equivalents

Cash and cash equivalents include highly liquid investments purchased three months or less from maturity and are stated at cost, which approximates market value.

E. Restricted cash and cash equivalents

The Company has the option, under its bilateral letter of credit facility agreements with various banks, to pledge collateral in the form of cash and cash equivalents for a minimum term of one month, equal to at least the face value of the letters of credit issued. Restricted cash and cash equivalents are shown separately on the balance sheet and include highly liquid investments purchased three months or less from maturity and are stated at cost, which approximates market value.

F. Accounts receivable

Accounts receivable are recorded at cost net of billing adjustments and an allowance for doubtful accounts. The allowance for doubtful accounts is based on expected collectability and considers historical experience as well as known trends or uncertainties related to account collectability. When a receivable is deemed uncollectible, it is written off against the allowance for doubtful accounts. Subsequent recoveries of amounts previously written off are credited to the bad debt expense in Casualty and other in the Consolidated Statement of Income.

1 Summary of significant accounting policies

continued

G. Material and supplies

Material and supplies, which consist mainly of rail, ties, and other items for construction and maintenance of property and equipment, as well as diesel fuel, are valued at weighted-average cost.

H. Properties

Railroad properties are carried at cost less accumulated depreciation including asset impairment write-downs. Labor, materials and other costs associated with the installation of rail, ties, ballast and other structures are capitalized to the extent they meet the Company's capitalization criteria. Major overhauls and large refurbishments of equipment are also capitalized when they result in an extension to the service life or increase the functionality of the asset. Repair and maintenance costs are expensed as incurred.

The cost of properties, including those under capital leases, net of asset impairment write-downs, is depreciated on a straight-line basis over their estimated service lives, measured in years, except for rail which is measured in millions of gross tons per mile. The Company follows the group method of depreciation whereby a single composite depreciation rate is applied to the gross investment in a class of similar assets, despite small differences in the service life or salvage value of individual property units within the same asset class.

In accordance with the group method of depreciation, upon sale or retirement of properties in the normal course of business, cost less net salvage value is charged to accumulated depreciation. As a result, no gain or loss is recognized in income under the group method as it is assumed that the assets within the group on average have the same life and characteristics and therefore that gains or losses offset over time. For retirements of depreciable properties that do not occur in the normal course of business, a gain or loss may be recognized if the retirement varies significantly from the retirement pattern identified through depreciation studies. A gain or loss is recognized in Other income for the sale of land or disposal of assets that are not part of railroad operations.

Assets held for sale are measured at the lower of their carrying amount or fair value, less cost to sell. Losses resulting from significant rail line sales are recognized in income when the asset meets the criteria for classification as held for sale, whereas losses resulting from significant rail line abandonments are recognized in the Consolidated Statement of Income when the asset ceases to be used. Gains are recognized in income when they are realized.

The Company reviews the carrying amounts of properties held and used whenever events or changes in circumstances indicate that such carrying amounts may not be recoverable based on future undiscounted cash flows. Assets that are deemed impaired as a result of such review are recorded at the lower of carrying amount or fair value.

I. Intangible assets

Intangible assets consist mainly of customer contracts and relationships assumed through past acquisitions and are being amortized on a straight-line basis over 40 to 50 years.

The Company reviews the carrying amounts of intangible assets held and used whenever events or changes in circumstances indicate that such carrying amounts may not be recoverable based on future undiscounted cash flows. Assets that are deemed impaired as a result of such review are recorded at the lower of carrying amount or fair value.

J. Pensions

Pension costs are determined using actuarial methods. Net periodic benefit cost is charged to income and includes:

- (i) the cost of pension benefits provided in exchange for employees' services rendered during the year;
- (ii) the interest cost of pension obligations;
- (iii) the expected long-term return on pension fund assets;
- (iv) the amortization of prior service costs and amendments over the expected average remaining service life of the employee group covered by the plans; and
- (v) the amortization of cumulative net actuarial gains and losses in excess of 10% of the greater of the beginning of year balances of the projected benefit obligation or market-related value of plan assets, over the expected average remaining service life of the employee group covered by the plans.

The pension plans are funded through contributions determined in accordance with the projected unit credit actuarial cost method.

K. Postretirement benefits other than pensions

The Company accrues the cost of postretirement benefits other than pensions using actuarial methods. These benefits, which are funded as they become due, include life insurance programs, medical benefits and, for a closed group of employees, free rail travel benefits.

The Company amortizes the cumulative net actuarial gains and losses in excess of 10% of the projected benefit obligation at the beginning of the year, over the expected average remaining service life of the employee group covered by the plan.

L. Personal injury and other claims

In Canada, the Company accounts for costs related to employee work-related injuries based on actuarially developed estimates of the ultimate cost associated with such injuries, including compensation, health care and third-party administration costs.

In the U.S., the Company accrues the expected cost for personal injury, property damage and occupational disease claims, based on actuarial estimates of their ultimate cost.

For all other legal actions in Canada and the U.S., the Company maintains, and regularly updates on a case-by-case basis, provisions for such items when the expected loss is both probable and can be reasonably estimated based on currently available information.

M. Environmental expenditures

Environmental expenditures that relate to current operations, or to an existing condition caused by past operations, are expensed unless they can contribute to current or future operations. Environmental liabilities are recorded when environmental assessments occur, remedial efforts are probable, and when the costs, based on a specific plan of action in terms of the technology to be used and the extent of the corrective action required, can be reasonably estimated. The Company accrues its allocable share of liability taking into account the Company's alleged responsibility, the number of potentially responsible parties and their ability to pay their respective shares of the liability. Recoveries of environmental remediation costs from other parties are recorded as assets when their receipt is deemed probable and collectability is reasonably assured.

N. Income taxes

The Company follows the asset and liability method of accounting for income taxes. Under the asset and liability method, the change in the net deferred income tax asset or liability is included in the computation of Net income or Other comprehensive income (loss). Deferred income tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which temporary differences are expected to be recovered or settled.

O. Derivative financial instruments

The Company uses derivative financial instruments from time to time in the management of its interest rate and foreign currency exposures. Derivative instruments are recorded on the balance sheet at fair value and the changes in fair value are recorded in Net income or Other comprehensive income (loss) depending on the nature and effectiveness of the hedge transaction. Income and expense related to hedged derivative financial instruments are recorded in the same category as that generated by the underlying asset or liability.

P. Stock-based compensation

The Company follows the fair value based approach for stock option awards based on the grant-date fair value using the Black-Scholes option-pricing model. The Company expenses the fair value of its stock option awards on a straight-line basis, over the period during which an employee is required to provide service (requisite service period) or until retirement eligibility is attained, whichever is shorter. The Company also follows the fair value based approach for cash settled awards using a lattice-based valuation model. Compensation cost for cash settled awards is based on the fair value of the awards at period-end and is recognized over the period during which an employee is required to provide service (requisite service period) or until retirement eligibility is attained, whichever is shorter. See Note 10 – Stock plans, for the assumptions used to determine fair value and for other required disclosures.

2 Accounting changes

The Company adopts accounting standards that are issued by the Financial Accounting Standards Board (FASB), if applicable. For the years 2013, 2012 and 2011, there were no accounting standard updates issued by FASB that had a significant impact on the Company's consolidated financial statements, except as noted below.

In February 2013, the FASB issued Accounting Standards Update (ASU) 2013-02, *Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income*. ASU 2013-02 added new disclosure requirements to Accounting Standards Codification (ASC) 220, *Comprehensive Income*, for items reclassified out of accumulated other comprehensive income (AOCI) effective for reporting periods beginning after December 15, 2012. It requires entities to disclose additional information about amounts reclassified out of AOCI by component including changes in AOCI balances and significant items reclassified out of AOCI by the respective line items of net income. The Company has adopted ASU 2013-02 for the reporting period beginning January 1, 2013 and the prescribed disclosures are presented in Note 18 – Accumulated other comprehensive loss.

3 Accounts receivable

<i>In millions</i>	<i>December 31,</i>	2013	2012
Freight		\$ 675	\$ 674
Non-freight		147	167
Gross accounts receivable		822	841
Allowance for doubtful accounts		(7)	(10)
<i>Net accounts receivable</i>		\$ 815	\$ 831

4 Properties

In millions	Depreciation rate	December 31, 2013			December 31, 2012		
		Cost	Accumulated depreciation	Net	Cost	Accumulated depreciation	Net
Track and roadway ⁽¹⁾	2%	\$ 27,833	\$ 7,103	\$ 20,730	\$ 26,209	\$ 6,948	\$ 19,261
Rolling stock	4%	5,193	1,894	3,299	4,989	1,785	3,204
Buildings	2%	1,392	521	871	1,275	492	783
Information technology ⁽²⁾	12%	1,000	455	545	976	427	549
Other	6%	1,388	606	782	1,273	529	744
<i>Total properties including capital leases</i>		\$ 36,806	\$ 10,579	\$ 26,227	\$ 34,722	\$ 10,181	\$ 24,541
Capital leases included in properties							
Track and roadway ⁽³⁾		\$ 417	\$ 58	\$ 359	\$ 417	\$ 53	\$ 364
Rolling stock		982	358	624	1,222	353	869
Buildings		109	21	88	109	18	91
Other		102	22	80	91	17	74
<i>Total capital leases included in properties</i>		\$ 1,610	\$ 459	\$ 1,151	\$ 1,839	\$ 441	\$ 1,398

(1) Includes the cost of land of \$1,911 million and \$1,766 million as at December 31, 2013 and December 31, 2012, respectively.

(2) The Company capitalized \$85 million in 2013 and \$93 million in 2012 of internally developed software costs pursuant to FASB ASC 350-40, "Intangibles – Goodwill and Other, Internal – Use Software."

(3) Includes \$108 million of right-of-way access in both years.

Accounting policy for capitalization of costs

The Company's railroad operations are highly capital intensive. The Company's properties consist mainly of a large base of homogeneous or network-type assets such as rail, ties, ballast and other structures, which form the Company's Track and roadway properties, and Rolling stock. The Company's capital expenditures are for the replacement of assets and for the purchase or construction of assets to enhance operations or provide new service offerings to customers. A large portion of the Company's capital expenditures are for self-constructed properties including the replacement of existing track and roadway assets and track line expansion, as well as major overhauls and large refurbishments of rolling stock.

Expenditures are generally capitalized if they extend the life of the asset or provide future benefits such as increased revenue-generating capacity, functionality, or physical or service capacity. The Company has a process in place to determine whether its capital programs qualify for capitalization. For Track and roadway properties, the Company establishes basic capital programs to replace or upgrade the track infrastructure assets which are capitalized if they meet the capitalization criteria. These basic capital programs are planned in advance and carried out by the Company's engineering workforce.

In addition, for Track and roadway properties, expenditures that meet the minimum level of activity as defined by the Company are also capitalized as detailed below:

- *Land*: all purchases of land;
- *Grading*: installation of road bed, retaining walls, drainage structures;
- *Rail and related track material*: installation of 39 or more continuous feet of rail;

- *Ties*: installation of 5 or more ties per 39 feet;
- *Ballast*: installation of 171 cubic yards of ballast per mile.

Expenditures relating to the Company's properties that do not meet the Company's capitalization criteria are considered normal repairs and maintenance and are expensed. For Track and roadway properties, such expenditures include but are not limited to spot tie replacement, spot or broken rail replacement, physical track inspection for detection of rail defects and minor track corrections, and other general maintenance of track infrastructure.

For the ballast asset, the Company also engages in "shoulder ballast undercutting" that consists of removing some or all of the ballast, which has deteriorated over its service life, and replacing it with new ballast. When ballast is installed as part of a shoulder ballast undercutting project, it represents the addition of a new asset and not the repair or maintenance of an existing asset. As such, the Company capitalizes expenditures related to shoulder ballast undercutting given that an existing asset is retired and replaced with a new asset. Under the group method of accounting for properties, the deteriorated ballast is retired at its average cost measured using the quantities of new ballast added.

For purchased assets, the Company capitalizes all costs necessary to make the asset ready for its intended use. Expenditures that are capitalized as part of self-constructed properties include direct material, labor, and contracted services, as well as other allocated costs which are not charged directly to capital projects. These allocated costs include, but are not limited to, fringe benefits, small tools and supplies, machinery used on projects and project supervision. The Company reviews and adjusts its allocations, as required, to reflect the actual costs incurred each year.

Costs of deconstruction and removal of replaced assets, referred to herein as dismantling costs, are distinguished from installation costs for self-constructed properties based on the nature of the related activity. For Track and roadway properties, employees concurrently perform dismantling and installation of new track and roadway assets and, as such, the Company estimates the amount of labor and other costs that are related to dismantling. The Company determines dismantling costs based on an analysis of the track and roadway installation process.

Accounting policy for depreciation

Properties are carried at cost less accumulated depreciation including asset impairment write-downs. The cost of properties, including those under capital leases, net of asset impairment write-downs, is depreciated on a straight-line basis over their estimated service lives, measured in years, except for rail which is measured in millions of gross tons per mile. The Company follows the group method of depreciation whereby a single composite depreciation rate is applied to the gross investment in a class of similar assets, despite small differences in the service life or salvage value of individual property units within the same asset class. The Company uses approximately 40 different depreciable asset classes.

For all depreciable assets, the depreciation rate is based on the estimated service lives of the assets. Assessing the reasonableness of the estimated service lives of properties requires judgment and is based on currently available information, including periodic depreciation studies conducted by the Company. The Company's U.S. properties are subject to comprehensive depreciation studies as required by the Surface Transportation Board (STB) and are conducted by external experts. Depreciation studies for Canadian properties are not required by regulation and are conducted internally. Studies are performed on specific asset groups on a periodic basis. Changes in the estimated service lives of the assets and their related composite depreciation rates are implemented prospectively.

For the rail asset, the estimated service life is measured in millions of gross tons per mile and varies based on rail characteristics such as weight, curvature and metallurgy. The annual composite depreciation rate for rail assets is determined by dividing the estimated annual number of gross tons carried over the rail by the estimated service life of the rail measured in millions of gross tons per mile. For the rail asset, the Company capitalizes the costs of rail grinding which consists of restoring and improving the rail profile and removing irregularities from worn rail to extend the service life. The service life of the rail asset is based on expected future usage of the rail in its existing condition, determined using railroad industry research and testing, less the rail asset's usage to date.

The service life of the rail asset is increased incrementally as rail grinding is performed thereon. As such, the costs incurred for rail grinding are capitalized given that the activity extends the service life of the rail asset beyond its original or current condition as additional gross tons can be carried over the rail for its remaining service life. The Company amortizes the cost of rail grinding over the remaining life of the rail asset, which includes the incremental life extension generated by the rail grinding.

Disposal of property

2013

Exchange of easements

On June 8, 2013, the Company entered into an agreement with another Class I railroad to exchange perpetual railroad operating easements including the track and roadway assets on specific rail lines (collectively the "exchange of easements") without monetary consideration. The Company has accounted for the exchange of easements at fair value pursuant to FASB ASC 845, *Nonmonetary Transactions*. The transaction resulted in a gain on exchange of easements of \$29 million (\$18 million after-tax) that was recorded in Other income.

Lakeshore West

On March 19, 2013, the Company entered into an agreement with Metrolinx to sell a segment of the Oakville subdivision in Oakville and Burlington, Ontario, together with the rail fixtures and certain passenger agreements (collectively the "Lakeshore West"), for cash proceeds of \$52 million before transaction costs. Under the agreement, the Company obtained the perpetual right to operate freight trains over the Lakeshore West at its then current level of operating activity, with the possibility of increasing its operating activity for additional consideration. The transaction resulted in a gain on disposal of \$40 million (\$36 million after-tax) that was recorded in Other income under the full accrual method of accounting for real estate transactions.

2012

Bala-Oakville

On March 23, 2012, the Company entered into an agreement with Metrolinx to sell a segment of the Bala and a segment of the Oakville subdivisions in Toronto, Ontario, together with the rail fixtures and certain passenger agreements (collectively the "Bala-Oakville"), for cash proceeds of \$311 million before transaction costs. Under the agreement, the Company obtained the perpetual right to operate freight trains over the Bala-Oakville at its then current level of operating activity, with the possibility of increasing its operating activity for additional consideration. The transaction resulted in a gain on disposal of \$281 million (\$252 million after-tax) that was recorded in Other income under the full accrual method of accounting for real estate transactions.

4 Properties *continued*

2011

IC RailMarine

On August 1, 2011, the Company sold substantially all of the assets of IC RailMarine Terminal Company ("IC RailMarine"), an indirect subsidiary of the Company, to Raven Energy, LLC, an affiliate of Foresight Energy, LLC ("Foresight") and the Cline Group ("Cline"), for cash proceeds of \$70 million (US\$73 million) before transaction costs. IC RailMarine is located on the east bank of the Mississippi River and stores and transfers bulk commodities and liquids between rail, ship and barge, serving customers in North American and global markets. Under the sale agreement, the Company will benefit from a 10-year rail transportation agreement with Savatran LLC, an affiliate of Foresight and Cline, to haul a minimum annual volume of coal from four Illinois mines to the IC RailMarine transfer facility. The transaction resulted in a gain on disposal of \$60 million (\$38 million after-tax) that was recorded in Other income.

Lakeshore East

On March 24, 2011, the Company entered into an agreement with Metrolinx to sell a segment of the Kingston subdivision known as the Lakeshore East in Pickering and Toronto, Ontario, together with the rail fixtures and certain passenger agreements (collectively the "Lakeshore East"), for cash proceeds of \$299 million before transaction costs. Under the agreement, the Company obtained the perpetual right to operate freight trains over the Lakeshore East at its then current level of operating activity, with the possibility of increasing its operating activity for additional consideration. The transaction resulted in a gain on disposal of \$288 million (\$254 million after-tax) that was recorded in Other income under the full accrual method of accounting for real estate transactions.

5 Intangible and other assets

<i>In millions</i>	<i>December 31,</i>	2013	2012
Pension asset (Note 11)		\$ 1,662	\$ -
Deferred and long-term receivables		109	87
Intangible assets (A)		59	57
Investments (B)		57	30
Other		72	75
<i>Total intangible and other assets</i>		\$ 1,959	\$ 249

A. Intangible assets

Intangible assets consist mainly of customer contracts and relationships assumed through past acquisitions.

B. Investments

As at December 31, 2013, the Company had \$46 million (\$20 million as at December 31, 2012) of investments accounted for under the equity method and \$11 million (\$10 million as at December 31, 2012) of investments accounted for under the cost method.

6 Accounts payable and other

<i>In millions</i>	<i>December 31,</i>	2013	2012
Trade payables		\$ 408	\$ 386
Payroll-related accruals		351	340
Accrued charges		156	135
Accrued interest		125	105
Income and other taxes		96	294
Stock-based incentives liability (Note 10)		80	88
Personal injury and other claims provisions (Note 16)		45	82
Environmental provisions (Note 16)		41	31
Other postretirement benefits liability (Note 11)		18	17
Other		157	148
<i>Total accounts payable and other</i>		\$ 1,477	\$ 1,626

7 Other liabilities and deferred credits

<i>In millions</i>	<i>December 31,</i>	2013	2012
Personal injury and other claims provisions, net of current portion (Note 16)		\$ 271	\$ 232
Stock-based incentives liability, net of current portion (Note 10)		240	203
Environmental provisions, net of current portion (Note 16)		78	92
Deferred credits and other		226	249
<i>Total other liabilities and deferred credits</i>		\$ 815	\$ 776

8 Long-term debt

<i>In millions</i>	Maturity	Outstanding US dollar- denominated amount	December 31,	
			2013	2012
<i>Debentures and notes: (A)</i>				
Canadian National series:				
4.40%	10-year notes (B)	Mar. 15, 2013	\$ -	\$ 398
4.95%	6-year notes (B)	Jan. 15, 2014	325	323
-	2-year floating rate notes (C)	Nov. 6, 2015	350	-
5.80%	10-year notes (B)	June 1, 2016	250	249
1.45%	5-year notes (B)	Dec. 15, 2016	300	298
5.85%	10-year notes (B)	Nov. 15, 2017	250	249
5.55%	10-year notes (B)	May 15, 2018	325	323
6.80%	20-year notes (B)	July 15, 2018	200	199
5.55%	10-year notes (B)	Mar. 1, 2019	550	547
2.85%	10-year notes (B)	Dec. 15, 2021	400	398
2.25%	10-year notes (B)	Nov. 15, 2022	250	249
7.63%	30-year debentures	May 15, 2023	150	149
6.90%	30-year notes (B)	July 15, 2028	475	473
7.38%	30-year debentures (B)	Oct. 15, 2031	200	199
6.25%	30-year notes (B)	Aug. 1, 2034	500	498
6.20%	30-year notes (B)	June 1, 2036	450	448
6.71%	Puttable Reset Securities PURS SM (B)	July 15, 2036	250	249
6.38%	30-year debentures (B)	Nov. 15, 2037	300	298
3.50%	30-year notes (B)	Nov. 15, 2042	250	249
4.50%	30-year notes (B)	Nov. 7, 2043	250	-
Illinois Central series:				
5.00%	99-year income debentures	Dec. 1, 2056	7	7
7.70%	100-year debentures	Sep. 15, 2096	125	124
<i>Total US dollar-denominated debentures and notes</i>			\$ 6,157	5,927
BC Rail series:				
	Non-interest bearing 90-year subordinated notes (D)	July 14, 2094	842	842
<i>Total debentures and notes</i>			7,391	6,769
<i>Other:</i>				
	Commercial paper (E) (F)		273	-
	Accounts receivable securitization (G)		250	-
	Capital lease obligations and other (H)		783	985
<i>Total debt, gross</i>			8,697	7,754
<i>Less:</i>				
	Net unamortized discount		857	854
<i>Total debt (I) ⁽¹⁾</i>			7,840	6,900
<i>Less:</i>				
	Current portion of long-term debt (I)		1,021	577
<i>Total long-term debt</i>			\$ 6,819	\$ 6,323

(1) See Note 17 – Financial instruments, for the fair value of debt.

Footnotes to the table follow on the next page.

8 Long-term debt *continued*

A. The Company's debentures, notes and revolving credit facility are unsecured.

B. These debt securities are redeemable, in whole or in part, at the option of the Company, at any time, at the greater of par and a formula price based on interest rates prevailing at the time of redemption.

C. These floating rate notes bear interest at the three-month London Interbank Offered Rate (LIBOR) plus 0.20%. The interest rate as at December 31, 2013 was 0.44%.

D. The Company records these notes as a discounted debt of \$9 million, using an imputed interest rate of 5.75%. The discount of \$833 million is included in the net unamortized discount.

E. The Company has an \$800 million revolving credit facility agreement with a consortium of lenders. The agreement allows for an increase in the facility amount, up to a maximum of \$1.3 billion, as well as the option to extend the term by an additional year at each anniversary date, subject to the consent of individual lenders. The Company exercised such option and on March 22, 2013, the expiry date of the agreement was extended by one year to May 5, 2018. The credit facility, containing customary terms and conditions, is available for working capital and general corporate purposes, including back-stopping the Company's commercial paper program, and provides for borrowings at various interest rates, including the Canadian prime rate, bankers' acceptance rates, the U.S. federal funds effective rate and the LIBOR, plus applicable margins. The credit facility agreement has one financial covenant, which limits debt as a percentage of total capitalization, and with which the Company is in compliance. As at December 31, 2013 and December 31, 2012, the Company had no outstanding borrowings under its revolving credit facility and there were no draws during the years ended December 31, 2013 and 2012.

F. The Company has a commercial paper program, which is backed by its revolving credit facility, enabling it to issue commercial paper up to a maximum aggregate principal amount of \$800 million, or the US dollar equivalent. As at December 31, 2013, the Company had total borrowings of \$273 million presented in Current portion of long-term debt on the Consolidated Balance Sheet (nil as at December 31, 2012). The weighted-average interest rate on these borrowings was 1.14%.

The Company presents issuances and repayments of commercial paper in the Consolidated Statement of Cash Flows, all of which have a maturity less than 90 days, on a net basis. The following table presents the gross issuances and repayments of commercial paper:

<i>In millions</i>	<i>Year ended December 31,</i>	2013	2012	2011
Issuances of commercial paper		\$ 3,255	\$ 1,861	\$ 659
Repayments of commercial paper		\$ (2,987)	\$ (1,943)	\$ (575)

The Company has revised the Consolidated Statement of Cash Flows for 2012 and 2011 to present the cash flows from the issuances and repayments of commercial paper on a net basis, consistent with the presentation adopted for 2013. The Company chose to present such cash flows on a net basis since the issuance and repayments of commercial paper are part of the Company's cash management activities and this debt matures in less than 90 days.

G. On December 20, 2012, the Company entered into a three-year agreement, commencing on February 1, 2013, to sell an undivided co-ownership interest in a revolving pool of accounts receivable to unrelated trusts for maximum cash proceeds of \$450 million. The trusts are multi-seller trusts and the Company is not the primary beneficiary. Funding for the acquisition of these assets is customarily through the issuance of asset-backed commercial paper notes by the unrelated trusts.

The Company has retained the responsibility for servicing, administering and collecting the receivables sold. The average servicing period is approximately one month. Subject to customary indemnifications, each trust's recourse is limited to the accounts receivable transferred.

The Company is subject to customary reporting requirements for which failure to perform could result in termination of the program. In addition, the program is subject to customary credit rating requirements, which if not met, could also result in termination of the program. The Company monitors the reporting requirements and is currently not aware of any trends, events or conditions that could cause such termination.

The accounts receivable securitization program provides the Company with readily available short-term financing for general corporate use. In the event the program is terminated before its scheduled maturity, the Company expects to meet its future payment obligations through its various sources of financing including its revolving credit facility and commercial paper program, and/or access to capital markets.

The Company accounts for its accounts receivable securitization program under ASC 860, *Transfers and Servicing*. Based on the structure of the program, the Company accounts for the proceeds as a secured borrowing. As such, as at December 31, 2013, the Company recorded \$250 million of proceeds received under the accounts receivable securitization program in the Current portion of long-term debt on the Consolidated Balance Sheet at a weighted-average interest rate of 1.18% which is secured by and limited to \$281 million of accounts receivable.

H. During 2013, the Company recorded \$44 million in assets it acquired through equipment leases (\$94 million in 2012), for which an equivalent amount was recorded in debt.

Interest rates for capital lease obligations range from approximately 0.7% to 8.5% with maturity dates in the years 2014 through 2037. The imputed interest on these leases amounted to \$209 million as at December 31, 2013 and \$249 million as at December 31, 2012.

The capital lease obligations are secured by properties with a net carrying amount of \$779 million as at December 31, 2013 and \$1,021 million as at December 31, 2012.

I. Long-term debt maturities, including repurchase arrangements and capital lease repayments on debt outstanding as at December 31, 2013, for the next five years and thereafter, are as follows:

<i>In millions</i>	Capital leases	Debt	Total
2014 ⁽¹⁾	\$ 153	\$ 868	\$ 1,021
2015	83	369	452
2016	287	582	869
2017	143	263	406
2018	7	556	563
2019 and thereafter	109	4,420	4,529
	\$ 782	\$ 7,058	\$ 7,840

(1) Current portion of long-term debt.

J. The aggregate amount of debt payable in US currency as at December 31, 2013 was US\$6,730 million (C\$7,158 million), including US\$573 million relating to capital leases and other; and US\$6,690 million (C\$6,656 million), including US\$733 million relating to capital leases and other, as at December 31, 2012.

K. The Company has a series of bilateral letter of credit facility agreements with various banks to support its requirements to post letters of credit in the ordinary course of business. On March 22, 2013, the expiry date of these agreements was extended by one year to April 28, 2016. Under these agreements, the Company has the option from time to time to pledge collateral in the form of cash or cash equivalents, for a minimum term of one month, equal to at least the face value of the letters of credit issued. As at December 31, 2013, the Company had letters of credit drawn of \$481 million (\$551 million as at December 31, 2012) from a total committed amount of \$503 million (\$562 million as at December 31, 2012) by the various banks. As at December 31, 2013, cash and cash equivalents of \$448 million (\$521 million as at December 31, 2012) were pledged as collateral and recorded as Restricted cash and cash equivalents on the Consolidated Balance Sheet.

9 Capital stock

A. Authorized capital stock

The authorized capital stock of the Company is as follows:

- Unlimited number of Common Shares, without par value
- Unlimited number of Class A Preferred Shares, without par value, issuable in series
- Unlimited number of Class B Preferred Shares, without par value, issuable in series

B. Issued and outstanding common shares

Common stock split

On October 22, 2013, the Board of Directors of the Company approved a two-for-one common stock split in the form of a stock dividend of one additional common share of CN for each share outstanding, which was paid on November 29, 2013, to shareholders of record on November 15, 2013. All share and per share data presented herein reflect the impact of the stock split.

The following table provides the activity of the issued and outstanding common shares of the Company for the years ended December 31, 2013, 2012 and 2011:

<i>In millions</i>	<i>Year ended December 31,</i>	2013	2012	2011
Issued and outstanding common shares at beginning of year		856.8	884.2	918.7
Number of shares repurchased through buyback programs		(27.6)	(33.8)	(39.8)
Stock options exercised		1.4	6.4	5.3
<i>Issued and outstanding common shares at end of year</i>		830.6	856.8	884.2

Share repurchase programs

On October 22, 2012, the Board of Directors of the Company approved a share repurchase program which allowed for the repurchase of up to \$1.4 billion in common shares, not to exceed 36.0 million common shares, between October 29, 2012 and October 28, 2013 pursuant to a normal course issuer bid at prevailing market prices plus brokerage fees, or such other prices as may be permitted by the Toronto Stock Exchange. The Company repurchased a total of 29.4 million common shares for \$1.4 billion under this share repurchase program.

On October 22, 2013, the Board of Directors of the Company approved a new share repurchase program which allows for the repurchase of up to 30.0 million common shares, between October 29, 2013 and October 23, 2014 pursuant to a normal course issuer bid at prevailing market prices plus brokerage fees, or such other prices as may be permitted by the Toronto Stock Exchange.

9 Capital stock *continued*

The following table provides the information related to the share repurchase programs for the years ended December 31, 2013, 2012 and 2011:

<i>In millions, except per share data</i>			
<i>Year ended December 31,</i>	2013	2012	2011
Number of common shares ⁽¹⁾	27.6	33.8	39.8
Weighted-average price per share ⁽²⁾	\$ 50.65	\$ 41.36	\$ 35.67
Amount of repurchase	\$ 1,400	\$ 1,400	\$ 1,420

(1) Includes common shares purchased in the first and fourth quarters of 2013, 2012 and 2011 pursuant to private agreements between the Company and arm's-length third-party sellers.

(2) Includes brokerage fees.

10 Stock plans

The Company has various stock-based incentive plans for eligible employees. All share and per share data for such plans reflect the impact of the stock split (see Note 9 – Capital stock). A description of the Company's major plans is provided below:

A. Employee Share Investment Plan

The Company has an Employee Share Investment Plan (ESIP) giving eligible employees the opportunity to subscribe for up to 10% of their gross salaries to purchase shares of the Company's common stock on the open market and to have the Company invest, on the employees' behalf, a further 35% of the amount invested by the employees, up to 6% of their gross salaries.

The following table provides the number of participants holding shares, the total number of ESIP shares purchased on behalf of employees, including the Company's contributions, as well as the resulting expense recorded for the years ended December 31, 2013, 2012 and 2011:

<i>Year ended December 31,</i>	2013	2012	2011
Number of participants holding shares	18,488	17,423	16,218
Total number of ESIP shares purchased on behalf of employees (<i>millions</i>)	2.3	2.5	2.6
Expense for Company contribution (<i>millions</i>)	\$ 30	\$ 24	\$ 21

B. Stock-based compensation plans

The following table provides the total stock-based compensation expense for awards under all plans, as well as the related tax benefit recognized in income, for the years ended December 31, 2013, 2012 and 2011:

<i>In millions</i>	<i>Year ended December 31,</i>	2013	2012	2011
Cash settled awards				
Share Unit Plan		\$ 92	\$ 76	\$ 81
Voluntary Incentive Deferral Plan		35	19	21
		127	95	102
Stock option awards				
		9	10	10
<i>Total stock-based compensation expense</i>		\$ 136	\$ 105	\$ 112
<i>Tax benefit recognized in income</i>		\$ 35	\$ 25	\$ 24

(i) *Cash settled awards*

Share Unit Plan

In 2013, the Company granted 0.8 million performance share units (PSUs), previously known as restricted share units (RSUs), (0.9 million in both 2012 and 2011) to designated management employees entitling them to receive payout in cash based on the Company's share price. The PSUs granted are generally scheduled for payout after three years ("plan period") and vest conditionally upon the attainment of a target relating to return on invested capital (ROIC) over the plan period. Such performance vesting criteria results in a performance vesting factor that ranges from 0% to 150% depending on the level of ROIC attained.

Payout is conditional upon the attainment of a minimum share price, calculated using the average of the last three months of the plan period. In addition, commencing at various dates, for senior and executive management employees ("executive employees"), payout for PSUs is also conditional on compliance with the conditions of their benefit plans, award or employment agreements, including but not limited to non-compete, non-solicitation and non-disclosure of confidential information conditions. Current or former executive employees who breach such conditions of their benefit plans, award or employment agreements will forfeit the PSU payout. Should the Company reasonably determine that a current or former executive employee may have violated the conditions of their benefit plans, award or employment agreement, the Company may at its discretion change the manner of vesting of the PSUs to suspend payout on any PSUs pending resolution of such matter.

The value of the payout is equal to the number of PSUs awarded multiplied by the performance vesting factor and by the 20-day average closing share price ending on January 31 of the following year. On December 31, 2013, for the 2011 grant, the level of ROIC attained resulted in a performance vesting factor of 150%. As the minimum share price condition was met, payout under the plan of approximately \$80 million, calculated using the Company's average share price during the 20-day period ending on January 31, 2014, will be paid to employees meeting the conditions of their

benefit plans, award or employment agreements in the first quarter of 2014.

In February 2012, the Company's Board of Directors unanimously voted to forfeit and cancel the PSU payout of approximately \$18 million otherwise due in February 2012 to its former Chief Executive Officer (CEO) after determining that the former CEO was likely in breach of his non-compete and non-disclosure of confidential information conditions contained in the former CEO's employment agreement. On February 4, 2013, the Company's Executive Vice-President and Chief Operating Officer (COO) resigned to join the Company's major competitor in Canada. As a result of the COO's resignation, compensation amounts subject to non-compete, non-solicitation and other applicable terms of his long-term incentive award agreements and related plans, and certain amounts accumulated under non-registered pension plans and arrangements were forfeited. In February 2013, the Company entered into confidential agreements to settle these matters. As a result, in the quarter ended March 31, 2013, the stock-based compensation liability was reduced by approximately \$20 million.

Voluntary Incentive Deferral Plan

The Company has a Voluntary Incentive Deferral Plan (VIDP), providing eligible senior management employees the opportunity to elect to receive their annual incentive bonus payment and other eligible incentive payments in deferred share units (DSUs). A DSU is equivalent to a common share of the Company and also earns dividends when normal cash dividends are paid on common shares. The number of DSUs received by each participant is established using the average closing price for the 20 trading days prior to and including the date of the incentive payment. For each participant, the Company will grant a further 25% of the amount elected in DSUs, which will vest over a period of four years. The election to receive eligible incentive payments in DSUs is no longer available to a participant when the value of the participant's vested DSUs is sufficient to meet the Company's stock ownership guidelines. The value of each participant's DSUs is payable in cash at the time of cessation of employment. The Company's liability for DSUs is marked-to-market at each period-end based on the Company's closing stock price.

The following table provides the 2013 activity for all cash settled awards:

<i>In millions</i>	PSUs		VIDP	
	Nonvested	Vested	Nonvested	Vested
Outstanding at December 31, 2012	1.9	1.4 ⁽¹⁾	-	2.8
Granted (Payout)	0.8	(0.9)	-	(0.6)
Transferred into plan	-	-	-	0.1
Forfeited/Settled	(0.1)	(0.5) ⁽¹⁾	-	-
Vested during year	(0.9)	0.9	-	-
Outstanding at December 31, 2013	1.7	0.9	-	2.3

(1) The balance outstanding at December 31, 2012 included the units of the PSU payout otherwise due to the Company's former CEO that were in dispute which were settled in the first quarter of 2013.

10 Stock plans *continued*

The following table provides valuation and expense information for all cash settled awards:

<i>In millions, unless otherwise indicated</i>	PSUs ⁽¹⁾					VIDP ⁽²⁾	Total
Year of grant	2013	2012	2011	2010	2009		
Stock-based compensation expense (recovery) recognized over requisite service period							
Year ended December 31, 2013 ⁽³⁾	\$ 34	\$ 37	\$ 34	\$ (4)	\$ (9)	\$ 35	\$ 127
Year ended December 31, 2012	N/A	\$ 24	\$ 26	\$ 26	\$ -	\$ 19	\$ 95
Year ended December 31, 2011	N/A	N/A	\$ 19	\$ 27	\$ 35	\$ 21	\$ 102
Liability outstanding							
December 31, 2013	\$ 34	\$ 61	\$ 80	\$ -	\$ -	\$ 145	\$ 320
December 31, 2012	N/A	\$ 24	\$ 45	\$ 70	\$ 18	\$ 134	\$ 291
Fair value per unit							
December 31, 2013 (\$)	\$ 55.12	\$ 59.66	\$ 60.56	N/A	N/A	\$ 60.56	N/A
Fair value of awards vested during the year							
Year ended December 31, 2013	\$ -	\$ -	\$ 80	N/A	N/A	\$ 1	\$ 81
Year ended December 31, 2012	N/A	\$ -	\$ -	\$ 70	N/A	\$ 1	\$ 71
Year ended December 31, 2011	N/A	N/A	\$ -	\$ -	\$ 82	\$ 1	\$ 83
Nonvested awards at December 31, 2013							
Unrecognized compensation cost	\$ 26	\$ 15	\$ -	N/A	N/A	\$ 1	\$ 42
Remaining recognition period (years)	2.0	1.0	N/A	N/A	N/A	N/A ⁽⁴⁾	N/A
Assumptions ⁽⁵⁾							
Stock price (\$)	\$ 60.56	\$ 60.56	\$ 60.56	N/A	N/A	\$ 60.56	N/A
Expected stock price volatility ⁽⁶⁾	14%	14%	N/A	N/A	N/A	N/A	N/A
Expected term (years) ⁽⁷⁾	2.0	1.0	N/A	N/A	N/A	N/A	N/A
Risk-free interest rate ⁽⁸⁾	1.13%	0.99%	N/A	N/A	N/A	N/A	N/A
Dividend rate (\$) ⁽⁹⁾	\$ 0.86	\$ 0.86	N/A	N/A	N/A	N/A	N/A

(1) Compensation cost is based on the fair value of the awards at period-end using the lattice-based valuation model that uses the assumptions as presented herein.

(2) Compensation cost is based on intrinsic value.

(3) Includes the reversal of stock-based compensation expense related to the forfeiture of PSUs by the Company's former CEO and COO.

(4) The remaining recognition period has not been quantified as it relates solely to the 25% Company grant and the dividends earned thereon, representing a minimal number of units.

(5) Assumptions used to determine fair value are at December 31, 2013.

(6) Based on the historical volatility of the Company's stock over a period commensurate with the expected term of the award.

(7) Represents the remaining period of time that awards are expected to be outstanding.

(8) Based on the implied yield available on zero-coupon government issues with an equivalent term commensurate with the expected term of the awards.

(9) Based on the annualized dividend rate.

(ii) Stock option awards

The Company has stock option plans for eligible employees to acquire common shares of the Company upon vesting at a price equal to the market value of the common shares at the date of granting. The options issued by the Company are conventional options that vest over a period of time. The right to exercise options generally accrues over a period of four years of continuous employment. Options are not generally exercisable during the first 12 months after the date of grant and expire after 10 years. At

December 31, 2013, 20.2 million common shares remained authorized for future issuances under these plans.

For 2013, 2012 and 2011, the Company granted 1.1 million, 1.2 million and 1.3 million, respectively, of conventional stock options to designated senior management employees that vest over a period of four years of continuous employment.

The total number of conventional options outstanding at December 31, 2013 was 7.7 million.

The following table provides the activity of stock option awards during 2013, and for options outstanding and exercisable at December 31, 2013, the weighted-average exercise price:

	Options outstanding		Nonvested options	
	Number of options <i>In millions</i>	Weighted-average exercise price	Number of options <i>In millions</i>	Weighted-average grant date fair value
Outstanding at December 31, 2012 ⁽¹⁾	8.5	\$ 26.05	3.4	\$ 7.28
Granted	1.1	\$ 47.47	1.1	\$ 8.52
Forfeited	(0.5)	\$ 36.06	(0.2)	\$ 7.93
Exercised	(1.4)	\$ 19.54	N/A	N/A
Vested	N/A	N/A	(1.6)	\$ 6.95
Outstanding at December 31, 2013 ⁽¹⁾	7.7	\$ 30.97	2.7	\$ 7.89
Exercisable at December 31, 2013 ⁽¹⁾	5.0	\$ 25.58	N/A	N/A

⁽¹⁾ Stock options with a US dollar exercise price have been translated to Canadian dollars using the foreign exchange rate in effect at the balance sheet date.

The following table provides the number of stock options outstanding and exercisable as at December 31, 2013 by range of exercise price and their related intrinsic value, and for options outstanding, the weighted-average years to expiration. The table also provides the aggregate intrinsic value for in-the-money stock options, which represents the value that would have been received by option holders had they exercised their options on December 31, 2013 at the Company's closing stock price of \$60.56.

Range of exercise prices	Options outstanding				Options exercisable		
	Number of options <i>In millions</i>	Weighted-average years to expiration	Weighted-average exercise price	Aggregate intrinsic value <i>In millions</i>	Number of options <i>In millions</i>	Weighted-average exercise price	Aggregate intrinsic value <i>In millions</i>
\$15.52 – \$18.17	0.9	2.8	\$ 17.47	\$ 40	0.9	\$ 17.47	\$ 40
\$18.18 – \$23.76	0.8	4.5	\$ 21.96	31	0.8	\$ 21.96	31
\$23.77 – \$30.79	2.8	4.4	\$ 26.18	95	2.4	\$ 26.03	84
\$30.80 – \$40.61	2.2	7.6	\$ 37.79	50	0.8	\$ 37.19	19
\$40.62 – \$53.34	1.0	9.1	\$ 49.13	11	0.1	\$ 42.25	-
Balance at December 31, 2013 ⁽¹⁾	7.7	5.7	\$ 30.97	\$ 227	5.0	\$ 25.58	\$ 174

⁽¹⁾ Stock options with a US dollar exercise price have been translated to Canadian dollars using the foreign exchange rate in effect at the balance sheet date. As at December 31, 2013, all stock options outstanding were in-the-money. The weighted-average years to expiration of exercisable stock options was 4.5 years.

10 Stock plans *continued*

The following table provides valuation and expense information for all stock option awards:

In millions, unless otherwise indicated

Year of grant	2013	2012	2011	2010	2009	2008	2007	Total
Stock-based compensation expense recognized over requisite service period ⁽¹⁾								
Year ended December 31, 2013	\$ 5	\$ 2	\$ 1	\$ 1	\$ -	N/A	N/A	\$ 9
Year ended December 31, 2012	N/A	\$ 4	\$ 2	\$ 2	\$ 2	\$ -	N/A	\$ 10
Year ended December 31, 2011	N/A	N/A	\$ 5	\$ 2	\$ 2	\$ 1	\$ -	\$ 10
Fair value per unit								
At grant date (\$)	\$ 8.52	\$ 7.74	\$ 7.83	\$ 6.55	\$ 6.30	\$ 6.22	\$ 6.68	N/A
Fair value of awards vested during the year								
Year ended December 31, 2013	\$ -	\$ 2	\$ 3	\$ 2	\$ 4	N/A	N/A	\$ 11
Year ended December 31, 2012	N/A	\$ -	\$ 2	\$ 2	\$ 4	\$ 3	N/A	\$ 11
Year ended December 31, 2011	N/A	N/A	\$ -	\$ 2	\$ 4	\$ 3	\$ 3	\$ 12
Nonvested awards at December 31, 2013								
Unrecognized compensation cost	\$ 3	\$ 2	\$ 1	\$ -	\$ -	N/A	N/A	\$ 6
Remaining recognition period (years)	3.0	2.0	1.0	-	-	N/A	N/A	N/A
Assumptions								
Grant price (\$)	\$ 47.47	\$ 38.35	\$ 34.47	\$ 27.38	\$ 21.07	\$ 24.25	\$ 26.40	N/A
Expected stock price volatility ⁽²⁾	23%	26%	26%	28%	39%	27%	24%	N/A
Expected term (years) ⁽³⁾	5.4	5.4	5.3	5.4	5.3	5.3	5.2	N/A
Risk-free interest rate ⁽⁴⁾	1.41%	1.33%	2.53%	2.44%	1.97%	3.58%	4.12%	N/A
Dividend rate (\$) ⁽⁵⁾	\$ 0.86	\$ 0.75	\$ 0.65	\$ 0.54	\$ 0.51	\$ 0.46	\$ 0.42	N/A

(1) Compensation cost is based on the grant date fair value using the Black-Scholes option-pricing model that uses the assumptions at the grant date.

(2) Based on the average of the historical volatility of the Company's stock over a period commensurate with the expected term of the award and the implied volatility from traded options on the Company's stock.

(3) Represents the period of time that awards are expected to be outstanding. The Company uses historical data to estimate option exercise and employee termination, and groups of employees that have similar historical exercise behavior are considered separately.

(4) Based on the implied yield available on zero-coupon government issues with an equivalent term commensurate with the expected term of the awards.

(5) Based on the annualized dividend rate.

The following table provides information related to stock options exercised for the years ended December 31, 2013, 2012 and 2011:

<i>In millions</i>	<i>Year ended December 31,</i>	2013	2012	2011
Total intrinsic value		\$ 45	\$ 167	\$ 122
Cash received upon exercise of options		\$ 28	\$ 101	\$ 68
Related excess tax benefit realized		\$ 3	\$ 16	\$ 9

(iii) Stock price volatility

Compensation cost for the Company's Share Unit Plan is based on the fair value of the awards at period end using the lattice-based valuation model for which a primary assumption is the Company's share price. In addition, the Company's liability for the VIDP is marked-to-market at period-end and, as such, is also reliant on the Company's share price. Fluctuations in the Company's share price cause volatility to stock-based compensation expense as recorded in net income. The Company does not currently hold any derivative financial instruments to manage this exposure. A \$1 increase in the Company's share price at December 31, 2013 would have increased stock-based compensation expense by \$6 million, whereas a \$1 decrease in the price would have reduced it by \$5 million.

11 Pensions and other postretirement benefits

The Company has various retirement benefit plans under which substantially all of its employees are entitled to benefits at retirement age, generally based on compensation and length of service and/or contributions. Senior and executive management employees ("executive employees") subject to certain minimum service and age requirements, are also eligible for an additional retirement benefit under their Special Retirement Stipend Agreements (SRS), the Supplemental Executive Retirement Plan (SERP) or the Defined Contribution Supplemental Executive Retirement Plan (DC SERP). Executive employees who breach the non-compete, non-solicitation and non-disclosure of confidential information conditions of the SRS, SERP or DC SERP plans or other employment agreement will forfeit the retirement benefit under these plans. Should the Company reasonably determine that a current or former executive employee may have violated the conditions of their SRS, SERP, or DC SERP plan or other employment agreement, the Company may at its discretion withhold or suspend payout of the retirement benefit pending resolution of such matter.

On February 4, 2013, the Company's COO resigned to join the Company's major competitor in Canada. As a result, compensation amounts accumulated under the non-registered pension plans subject to non-compete and non-solicitation agreements were forfeited. The Company has recorded an actuarial gain related to the amounts forfeited. In 2012, the Company cancelled the \$1.5 million annual retirement benefit otherwise due to its former CEO after determining that the former CEO was likely in breach of the non-compete, non-solicitation and non-disclosure of confidential information conditions contained in the former CEO's employment agreement. The Company recorded a settlement gain of \$20 million from the termination of the former CEO's retirement benefit plan for the period beyond June 28, 2012, which was partially offset by the recognition of past accumulated actuarial losses of approximately \$4 million. In February 2013, the Company entered into confidential agreements to settle these matters.

The Company also offers postretirement benefits to certain employees providing life insurance, medical benefits and, for a closed group of employees, free rail travel benefits during retirement. These postretirement benefits are funded as they become due. The information in the tables that follow pertains to all of the Company's defined benefit plans. However, the following descriptions relate solely to the Company's main pension plan, the CN Pension Plan, unless otherwise specified.

A. Description of the CN Pension Plan

The CN Pension Plan is a contributory defined benefit pension plan that covers the majority of CN employees. It provides for pensions based mainly on years of service and final average pensionable earnings and is generally applicable from the first day of employment. Indexation of pensions is provided after retirement through a gain/

loss sharing mechanism, subject to guaranteed minimum increases. An independent trust company is the Trustee of the Company's pension trust funds (including the CN Pension Trust Fund). As Trustee, the trust company performs certain duties, which include holding legal title to the assets of the CN Pension Trust Fund and ensuring that the Company, as Administrator, complies with the provisions of the CN Pension Plan and the related legislation. The Company utilizes a measurement date of December 31 for the CN Pension Plan.

B. Funding policy

Employee contributions to the CN Pension Plan are determined by the plan rules. Company contributions are in accordance with the requirements of the Government of Canada legislation, *The Pension Benefits Standards Act, 1985*, including amendments and regulations thereto, and are determined by actuarial valuations. Actuarial valuations are generally required on an annual basis for all Canadian plans, or when deemed appropriate by the Office of the Superintendent of Financial Institutions (OSFI). These actuarial valuations are prepared in accordance with legislative requirements and with the recommendations of the Canadian Institute of Actuaries for the valuation of pension plans. The Company's most recently filed actuarial valuations conducted as at December 31, 2012 indicated a funding excess on a going-concern basis of approximately \$1.4 billion and a funding deficit on a solvency basis of approximately \$2.1 billion calculated using the three-year average of the Company's hypothetical wind-up ratio in accordance with the *Pension Benefit Standards Regulations, 1985*. The Company's next actuarial valuations required as at December 31, 2013 will be performed in 2014. These actuarial valuations are expected to identify a going-concern surplus of approximately \$1.7 billion, while on a solvency basis a funding deficit of approximately \$1.7 billion is expected due to the level of interest rates applicable at their respective measurement dates. The federal pension legislation requires funding deficits, as calculated under current pension regulations, to be paid over a number of years. Actuarial valuations are also required annually for the Company's U.S. pension plans.

In 2013, in anticipation of its future funding requirements, the Company made voluntary contributions of \$100 million in excess of the required contributions mainly to strengthen the financial position of its main pension plan, the CN Pension Plan. These voluntary contributions can be treated as a prepayment against its future required special solvency deficit payments. As at December 31, 2013, the Company had \$470 million of accumulated prepayments which remain available to offset future required solvency deficit payments. The Company expects to use approximately \$335 million of these prepayments to satisfy its 2014 required solvency deficit payment. As a result, the Company's cash contributions for 2014 are expected to be \$130 million, for all the Company's pension plans. As at February 3, 2014, the Company contributed \$89 million to its defined benefit pension plans for 2014.

11 Pensions and other postretirement benefits

continued

C. Plan assets

The assets of the Company's various Canadian defined benefit pension plans are held in separate trust funds (Trusts) which are diversified by asset type, country and investment strategies. Each year, the CN Board of Directors reviews and confirms or amends the Statement of Investment Policies and Procedures (SIPP) which includes the plans' long-term asset mix and related benchmark indices (Policy). This Policy is based on a long-term forward-looking view of the world economy, the dynamics of the plans' benefit liabilities, the market return expectations of each asset class and the current state of financial markets.

Annually, the CN Investment Division (Investment Manager), a division of the Company created to invest and administer the assets of the plans, proposes a short-term asset mix target (Strategy) for the coming year, which is expected to differ from the Policy, because of current economic and market conditions and expectations. The Investment Committee of the Board (Committee) regularly compares the actual asset mix to the Policy and Strategy and compares the actual performance of the Trusts to the performance of the benchmark indices.

The Company's 2013 target long-term asset mix and actual asset allocation for the Company's pension plans based on fair value, are as follows:

Asset allocation	Target long-term asset mix	Percentage of plan assets	
		2013	2012
Cash and short-term investments	3%	5%	4%
Bonds and mortgages	37%	25%	28%
Equities	45%	41%	41%
Real estate	4%	2%	2%
Oil and gas	7%	8%	8%
Infrastructure	4%	5%	4%
Absolute return	-	10%	9%
Risk-based allocation	-	4%	4%
<i>Total</i>	100%	100%	100%

The Committee's approval is required for all major investments in illiquid securities. The SIPP allows for the use of derivative financial instruments to implement strategies, hedge, and adjust existing or anticipated exposures. The SIPP prohibits investments in securities of the Company or its subsidiaries. Investments held in the Trusts consist mainly of the following:

- (i) Cash and short-term investments consist primarily of highly liquid investments which ensure adequate cash flows are available to cover near-term benefit payments. Short-term investments are mainly obligations issued by Canadian chartered banks.
- (ii) Bonds include bond instruments, issued or guaranteed by governments and corporate entities, as well as corporate notes. As at December 31, 2013, 91% of bonds were issued or guaranteed by Canadian, U.S. or other governments. Mortgages consist of mortgage products which are primarily conventional or participating loans secured by commercial properties.
- (iii) Equity investments are primarily publicly traded securities, well diversified by country, issuer and industry sector. In 2013, the most significant allocation to an individual issuer was approximately 2% and the most significant allocation to an industry sector was approximately 25%.
- (iv) Real estate is a diversified portfolio of Canadian land and commercial properties held by the Trusts' wholly-owned subsidiaries.
- (v) Oil and gas investments include petroleum and natural gas properties operated by the Trusts' wholly-owned subsidiaries and listed and non-listed Canadian securities of oil and gas companies.
- (vi) Infrastructure investments include participations in private infrastructure funds, public and private debt and publicly traded equity securities of infrastructure and utility companies. Some of these investments are held by the Trusts' wholly-owned subsidiaries.
- (vii) Absolute return investments are a portfolio of units of externally managed hedge funds, which are invested in various long/short strategies within fixed income, commodities, equities, global macro and multi-strategy funds, as presented in the table of fair value measurement. External managers are monitored on a continuous basis through investment and operational due diligence.
- (viii) Risk-based allocation is a portfolio of externally managed funds where each asset class contributes equally to the overall risk of the portfolio in order to capture over time different asset classes risk premiums. Some of these investments are held by the Trusts' wholly-owned subsidiaries.

The plans' Investment Manager monitors market events and exposures to markets, currencies and interest rates daily. When investing in foreign securities, the plans are exposed to foreign currency risk that may be adjusted or hedged; the effect of which is included in the valuation of the foreign securities. Net of the effects mentioned above, the plans were 66% exposed to the Canadian dollar, 14% to the US dollar, 8% to European currencies, and 12% to various other currencies as at December 31, 2013. Interest rate risk represents the risk that the fair value of the investments will fluctuate due to changes in market interest rates. Sensitivity to interest rates is a function of the timing and amount of cash flows of the assets and liabilities of the plans. To manage credit risk, established policies require dealing with counterparties considered to be of high credit quality. Derivatives are used from time to time to adjust asset mix or exposures to foreign currencies, interest rate or market risks of the portfolio or anticipated transactions. Derivatives are contractual agreements whose value is derived from interest rates, foreign exchange rates, and equity or commodity prices. They include forwards, futures, options and swaps and are included in investment categories based on their underlying exposure. When derivatives are used for hedging purposes, the gains or losses on the derivatives are offset by a corresponding change in the value of the hedged assets.

The tables on the following page present the fair value of plan assets as at December 31, 2013 and 2012 by asset class, their level within the fair value hierarchy and the valuation techniques and inputs used to measure such fair value.

<i>In millions</i>		Fair value measurements at December 31, 2013			
Asset class	Total	Level 1	Level 2	Level 3	
Cash and short-term investments ⁽¹⁾	\$ 897	\$ 16	\$ 881	\$ -	
Bonds ⁽²⁾					
Canada, U.S. and supranational	1,416	-	1,416	-	
Provinces of Canada and municipalities	2,297	-	2,297	-	
Corporate	111	-	111	-	
Emerging market debt	261	-	261	-	
Mortgages ⁽³⁾	166	-	166	-	
Equities ⁽⁴⁾					
Canadian	2,160	2,138	-	22	
U.S.	1,307	1,307	-	-	
International	3,421	3,421	-	-	
Real estate ⁽⁵⁾	299	-	-	299	
Oil and gas ⁽⁶⁾	1,380	379	40	961	
Infrastructure ⁽⁷⁾	788	10	115	663	
Absolute return funds ⁽⁸⁾					
Multi-strategy	460	-	460	-	
Fixed income	519	-	486	33	
Equity	391	2	389	-	
Global macro	328	-	328	-	
Risk-based allocation ⁽⁹⁾	607	-	607	-	
	\$ 16,808	\$ 7,273	\$ 7,557	\$ 1,978	
Other ⁽¹⁰⁾	61				
Total plan assets	\$ 16,869				

<i>In millions</i>		Fair value measurements at December 31, 2012			
Asset class	Total	Level 1	Level 2	Level 3	
Cash and short-term investments ⁽¹⁾	\$ 615	\$ 13	\$ 602	\$ -	
Bonds ⁽²⁾					
Canada, U.S. and supranational	1,735	-	1,735	-	
Provinces of Canada and municipalities	2,152	-	2,152	-	
Corporate	35	-	35	-	
Emerging market debt	353	-	353	-	
Mortgages ⁽³⁾	133	-	133	-	
Equities ⁽⁴⁾					
Canadian	2,220	2,198	-	22	
U.S.	1,121	1,121	-	-	
International	3,082	3,082	-	-	
Real estate ⁽⁵⁾	279	-	-	279	
Oil and gas ⁽⁶⁾	1,339	370	29	940	
Infrastructure ⁽⁷⁾	679	8	94	577	
Absolute return funds ⁽⁸⁾					
Multi-strategy	410	-	410	-	
Fixed income	425	-	415	10	
Commodity	91	-	91	-	
Equity	259	-	259	-	
Global macro	296	-	296	-	
Risk-based allocation ⁽⁹⁾	586	-	586	-	
	\$ 15,810	\$ 6,792	\$ 7,190	\$ 1,828	
Other ⁽¹⁰⁾	1				
Total plan assets	\$ 15,811				

Level 1: Fair value based on quoted prices in active markets for identical assets.

Level 2: Fair value based on significant observable inputs.

Level 3: Fair value based on significant unobservable inputs.

Footnotes to the table follow on the next page.

11 Pensions and other postretirement benefits *continued*

The following table reconciles the beginning and ending balances of the fair value of investments classified as Level 3:

<i>In millions</i>	Fair value measurements based on significant unobservable inputs (Level 3)				Absolute return ⁽⁸⁾	Total
	Equities ⁽⁴⁾	Real estate ⁽⁵⁾	Oil and gas ⁽⁶⁾	Infrastructure ⁽⁷⁾		
<i>Beginning balance at December 31, 2011</i>	\$ 22	\$ 214	\$ 889	\$ 619	\$ -	\$ 1,744
Actual return relating to assets still held at the reporting date	2	68	90	(13)	-	147
Purchases, sales and settlements	(2)	(3)	(39)	(29)	10	(63)
<i>Balance at December 31, 2012</i>	\$ 22	\$ 279	\$ 940	\$ 577	\$ 10	\$ 1,828
Actual return relating to assets still held at the reporting date	2	26	72	43	3	146
Purchases, sales and settlements	(2)	(6)	(51)	43	20	4
<i>Ending balance at December 31, 2013</i>	\$ 22	\$ 299	\$ 961	\$ 663	\$ 33	\$ 1,978

- (1) Cash and short-term investments are valued at cost, which approximates fair value, and are categorized as Level 1 for cash and Level 2 for short-term investments.
- (2) Bonds are valued using mid-price bids obtained from independent pricing data suppliers, predominantly TMX Group Inc. When prices are not available from independent sources, the fair value is based on the present value of future cash flows using current market yields for comparable instruments. All bonds are categorized as Level 2.
- (3) Mortgages are secured by real estate. The fair value of \$166 million (\$133 million in 2012) of mortgages categorized as Level 2 is based on the present value of future cash flows using current market yields for comparable instruments.
- (4) The fair value of equity investments categorized as Level 1 is based on quoted prices in active markets. The fair value of equity investments of \$22 million (\$22 million in 2012) categorized as Level 3 represent units in private equity funds which are valued by their independent administrators.
- (5) The fair value of real estate investments of \$299 million (\$279 million in 2012) includes land and buildings classified as Level 3 and is presented net of related mortgage debt of \$41 million (\$48 million in 2012). Land is valued based on the fair value of comparable assets, and buildings are valued based on the present value of estimated future net cash flows or the fair value of comparable assets. Independent valuations of land and buildings are performed triennially on a rotational basis.
- (6) Oil and gas investments categorized as Level 1 are valued based on quoted prices in active markets. Investments in oil and gas equities traded on a secondary market are valued based on the most recent transaction price and are categorized as Level 2. Investments of \$961 million (\$940 million in 2012) classified as Level 3 consist of operating oil and gas properties and the fair value is based on estimated future net cash flows that are discounted using prevailing market rates for transactions in similar assets. The future net cash flows are based on forecasted oil and gas prices and projected future annual production and costs.
- (7) Infrastructure investments consist of \$10 million (\$8 million in 2012) of publicly traded equity securities of infrastructure companies classified as Level 1, \$115 million (\$94 million in 2012) of public and private debt issued by infrastructure companies classified as Level 2 and \$663 million (\$577 million in 2012) of infrastructure funds that are classified as Level 3 and are valued based on discounted cash flows or earnings multiples. Infrastructure funds cannot be redeemed; distributions will be received from the funds as the underlying investments are liquidated.
- (8) Absolute return investments are valued using the net asset value as reported by the independent fund administrators. All absolute return investments have contractual redemption frequencies, ranging from monthly to annually, and redemption notice periods varying from 5 to 90 days. Absolute return investments that have redemption dates less frequent than every four months or that have restrictions on contractual redemption features at the reporting date are classified as Level 3.
- (9) Risk-based allocation investments are valued using the net asset value as reported by the independent fund administrators and are classified as Level 2. All funds have contractual redemption frequencies ranging from daily to annually, and redemption notice periods varying from 5 to 60 days.
- (10) Other consists of operating assets of \$85 million (\$94 million in 2012) and liabilities of \$24 million (\$93 million in 2012) required to administer the Trusts' investment assets and the plans' benefit and funding activities. Such assets are valued at cost and have not been assigned to a fair value category.

D. Additional disclosures*(i) Obligations and funded status*

<i>In millions</i>	<i>Year ended December 31,</i>	Pensions		Other postretirement benefits	
		2013	2012	2013	2012
Change in benefit obligation					
Projected benefit obligation at beginning of year		\$ 16,335	\$ 15,548	\$ 277	\$ 284
Amendments		-	-	-	6
Interest cost		658	740	11	13
Actuarial loss (gain)		(747)	812	(22)	(3)
Service cost		155	134	3	4
Curtailement gain		-	-	-	(6)
Plan participants' contributions		56	55	-	-
Foreign currency changes		16	(5)	5	(3)
Benefit payments, settlements and transfers ⁽¹⁾		(963)	(949)	(18)	(18)
<i>Projected benefit obligation at end of year</i>		\$ 15,510	\$ 16,335	\$ 256	\$ 277
Component representing future salary increases		(344)	(443)	-	-
Accumulated benefit obligation at end of year		\$ 15,166	\$ 15,892	\$ 256	\$ 277
Change in plan assets					
Fair value of plan assets at beginning of year		\$ 15,811	\$ 14,719	\$ -	\$ -
Employer contributions		226	833	-	-
Plan participants' contributions		56	55	-	-
Foreign currency changes		10	(2)	-	-
Actual return on plan assets		1,728	1,135	-	-
Benefit payments, settlements and transfers		(962)	(929)	-	-
<i>Fair value of plan assets at end of year</i>		\$ 16,869	\$ 15,811	\$ -	\$ -
<i>Funded status (Excess (deficiency) of fair value of plan assets over projected benefit obligation at end of year)</i>		\$ 1,359	\$ (524)	\$ (256)	\$ (277)

(1) Includes the settlement gain related to the termination of the former CEO's retirement benefit plan in 2012.

Measurement date for all plans is December 31.

The projected benefit obligation and fair value of plan assets for the CN Pension Plan at December 31, 2013 were \$14,458 million and \$16,059 million, respectively (\$15,247 million and \$15,042 million, respectively, at December 31, 2012).

(ii) Amounts recognized in the Consolidated Balance Sheet

<i>In millions</i>	<i>December 31,</i>	Pensions		Other postretirement benefits	
		2013	2012	2013	2012
Noncurrent assets (Note 5)		\$ 1,662	\$ -	\$ -	\$ -
Current liabilities (Note 6)		-	-	(18)	(17)
Noncurrent liabilities		(303)	(524)	(238)	(260)
<i>Total amount recognized</i>		\$ 1,359	\$ (524)	\$ (256)	\$ (277)

(iii) Amounts recognized in Accumulated other comprehensive loss (Note 18)

<i>In millions</i>	<i>December 31,</i>	Pensions		Other postretirement benefits	
		2013	2012	2013	2012
Net actuarial gain (loss)		\$ (1,515)	\$ (3,264)	\$ 27	\$ 6
Prior service cost		\$ (22)	\$ (26)	\$ (5)	\$ (6)

11 Pensions and other postretirement benefits *continued*

(iv) Information for the pension plans with an accumulated benefit obligation in excess of plan assets

In millions	December 31,	Pensions		Other postretirement benefits	
		2013	2012	2013	2012
Projected benefit obligation		\$ 527	\$ 526	N/A	N/A
Accumulated benefit obligation		\$ 475	\$ 461	N/A	N/A
Fair value of plan assets		\$ 224	\$ 201	N/A	N/A

(v) Components of net periodic benefit cost (income)

In millions	Year ended December 31,	Pensions			Other postretirement benefits		
		2013	2012	2011	2013	2012	2011
Service cost		\$ 155	\$ 134	\$ 124	\$ 3	\$ 4	\$ 4
Interest cost		658	740	788	11	13	14
Curtailment gain		-	-	-	-	(6)	(1)
Settlement loss (gain) ⁽¹⁾		4	(12)	3	-	-	-
Expected return on plan assets		(958)	(994)	(1,005)	-	-	-
Amortization of prior service cost		4	4	2	1	3	2
Amortization of net actuarial loss (gain)		227	119	8	(1)	-	-
Net periodic benefit cost (income)		\$ 90	\$ (9)	\$ (80)	\$ 14	\$ 14	\$ 19

(1) Includes the settlement gain related to the termination of the former CEO's retirement benefit plan in 2012.

The estimated prior service cost and net actuarial loss for defined benefit pension plans that will be amortized from Accumulated other comprehensive loss into net periodic benefit cost (income) over the next fiscal year are \$4 million and \$129 million, respectively.

The estimated prior service cost and net actuarial gain for other postretirement benefits that will be amortized from Accumulated other comprehensive loss into net periodic benefit cost (income) over the next fiscal year are \$2 million and \$4 million, respectively.

(vi) Weighted-average assumptions used in accounting for pensions and other postretirement benefits

	December 31,	Pensions			Other postretirement benefits		
		2013	2012	2011	2013	2012	2011
<i>To determine projected benefit obligation</i>							
Discount rate ⁽¹⁾		4.73%	4.15%	4.84%	4.69%	4.01%	4.70%
Rate of compensation increase ⁽²⁾		3.00%	3.00%	3.25%	3.00%	3.00%	3.25%
<i>To determine net periodic benefit cost</i>							
Discount rate ⁽¹⁾		4.15%	4.84%	5.32%	4.01%	4.70%	5.29%
Rate of compensation increase ⁽²⁾		3.00%	3.25%	3.50%	3.00%	3.25%	3.50%
Expected return on plan assets ⁽³⁾		7.00%	7.25%	7.50%	N/A	N/A	N/A

(1) The Company's discount rate assumption, which is set annually at the end of each year, is used to determine the projected benefit obligation at the end of the year and the net periodic benefit cost for the following year. The discount rate is used to measure the single amount that, if invested at the measurement date in a portfolio of high-quality debt instruments with a rating of AA or better, would provide the necessary cash flows to pay for pension benefits as they become due. The discount rate is determined by management with the aid of third-party actuaries. For the Canadian pension and other postretirement benefit plans, future expected benefit payments at each measurement date are discounted using spot rates from a derived AA corporate bond yield curve. The derived curve is based on observed rates for AA corporate bonds with short-term maturities and a projected AA corporate curve for longer term maturities based on spreads between observed AA corporate bonds and AA provincial bonds. The derived curve is expected to generate cash flows that match the estimated future benefit payments of the plans as the bond rate for each maturity year is applied to the plans' corresponding expected benefit payments of that year.

(2) The rate of compensation increase is determined by the Company based upon its long-term plans for such increases.

(3) To develop its expected long-term rate of return assumption used in the calculation of net periodic benefit cost applicable to the market-related value of assets, the Company considers multiple factors. The expected long-term rate of return is determined based on expected future performance for each asset class and is weighted based on the current asset portfolio mix. Consideration is taken of the historical performance, the premium return generated from an actively managed portfolio, as well as current and future anticipated asset allocations, economic developments, inflation rates and administrative expenses. Based on these factors, the rate is determined by the Company. For 2013, the Company used a long-term rate of return assumption of 7.00% on the market-related value of plan assets to compute net periodic benefit cost. The Company has elected to use a market-related value of assets, whereby realized and unrealized gains/losses and appreciation/depreciation in the value of the investments are recognized over a period of five years, while investment income is recognized immediately. In 2014, the Company will maintain the expected long-term rate of return on plan assets at 7.00% to reflect management's current view of long-term investment returns.

(vii) Health care cost trend rate for other postretirement benefits

For measurement purposes, increases in the per capita cost of covered health care benefits were assumed to be 8% for 2013 and 2014. It is assumed that the rate will decrease gradually to 4.5% in 2028 and remain at that level thereafter.

Assumed health care costs have a significant effect on the amounts reported for the health care plan. A one-percentage-point change in the assumed health care cost trend rate would have the following effect:

<i>In millions</i>	One-percentage-point	
	Increase	Decrease
Effect on total service and interest costs	\$ 1	\$ -
Effect on benefit obligation	\$ 10	\$ (9)

(viii) Estimated future benefit payments

<i>In millions</i>	Pensions	Other postretirement benefits
2014	\$ 991	\$ 18
2015	\$ 1,011	\$ 19
2016	\$ 1,033	\$ 19
2017	\$ 1,048	\$ 19
2018	\$ 1,058	\$ 19
Years 2019 to 2023	\$ 5,367	\$ 95

E. Defined contribution and other plans

The Company maintains defined contribution pension plans for certain salaried employees as well as certain employees covered by collective bargaining agreements. The Company also maintains other plans including Section 401(k) savings plans for certain U.S. based employees. The Company's contributions under these plans are expensed as incurred and amounted to \$13 million, \$11 million and \$10 million for 2013, 2012 and 2011, respectively.

F. Contributions to multi-employer plan

Under collective bargaining agreements, the Company participates in a multi-employer benefit plan named the Railroad Employees National Early Retirement Major Medical Benefit Plan which is administered by the National Carriers' Conference Committee (NCCC), and provides certain postretirement health care benefits to certain retirees. The Company's contributions under this plan are expensed as incurred and amounted to \$10 million, \$11 million and \$11 million in 2013, 2012 and 2011, respectively. The annual contribution rate for the plan is determined by the NCCC and for 2013 was \$143.21 per month per active employee (\$154.49 in 2012). The plan covered 867 retirees in 2013 (874 in 2012).

12 Other income

<i>In millions</i>	Year ended December 31,	2013	2012	2011
Gain on disposals of properties ⁽¹⁾		\$ 64	\$ 295	\$ 348
Gain on disposal of land		19	20	30
Other		(10)	-	23
Total other income		\$ 73	\$ 315	\$ 401

(1) 2013 includes \$29 million and \$40 million for the exchange of easements and the disposal of the Lakeshore West, respectively; 2012 includes \$281 million for the disposal of the Bala-Oakville; and 2011 includes \$60 million and \$288 million for the disposal of substantially all of the assets of IC RailMarine and the Lakeshore East, respectively. See Note 4 – Properties.

13 Income taxes

As at December 31, 2013, Deferred and receivable income taxes include a net deferred income tax asset of \$74 million (\$43 million as at December 31, 2012) and an income tax receivable of \$63 million (nil as at December 31, 2012).

The Company's consolidated effective income tax rate differs from the Canadian, or domestic, statutory Federal tax rate. The effective tax rate is affected by recurring items such as tax rates in provincial, U.S. federal, state and other foreign jurisdictions and the proportion of income earned in those jurisdictions. The effective tax rate is also affected by discrete items such as income tax rate enactments and lower tax rates on capital dispositions that may occur in any given year. The following table provides a reconciliation of income tax expense:

<i>In millions</i>	<i>Year ended December 31,</i>	2013	2012	2011
Federal tax rate		15.0%	15.0%	16.5%
Income tax expense at the statutory Federal tax rate		\$ (538)	\$ (549)	\$ (554)
Income tax recovery (expense) resulting from:				
Provincial and foreign taxes		(423)	(425)	(360)
Deferred income tax adjustments due to rate enactments		(24)	(35)	(40)
Gain on disposals		9	44	62
Other ⁽¹⁾		(1)	(13)	(7)
Income tax expense		\$ (977)	\$ (978)	\$ (899)
Cash payments for income taxes		\$ 890	\$ 289	\$ 482

(1) Comprises of adjustments relating to the resolution of matters pertaining to prior years' income taxes, including net recognized tax benefits, and other items.

The following table provides tax information on a domestic and foreign basis:

<i>In millions</i>	<i>Year ended December 31,</i>	2013	2012	2011
<i>Income before income taxes</i>				
Domestic		\$ 2,445	\$ 2,656	\$ 2,464
Foreign		1,144	1,002	892
		\$ 3,589	\$ 3,658	\$ 3,356
<i>Current income tax expense</i>				
Domestic		\$ (404)	\$ (314)	\$ (340)
Foreign		(242)	(213)	(28)
		\$ (646)	\$ (527)	\$ (368)
<i>Deferred income tax expense</i>				
Domestic		\$ (279)	\$ (370)	\$ (288)
Foreign		(52)	(81)	(243)
		\$ (331)	\$ (451)	\$ (531)

The following table provides the significant components of deferred income tax assets and liabilities:

<i>In millions</i>	<i>December 31,</i>	2013	2012
<i>Deferred income tax assets</i>			
Pension liability		\$ 89	\$ 149
Personal injury and legal claims		64	64
Environmental and other reserves		171	130
Other postretirement benefits liability		77	80
Net operating losses and tax credit carryforwards ⁽¹⁾		19	4
Total deferred income tax assets		420	427
<i>Deferred income tax liabilities</i>			
Properties		6,232	5,686
Net pension asset		438	-
Other		213	253
Total deferred income tax liabilities		6,883	5,939
Total net deferred income tax liability		\$ 6,463	\$ 5,512
<i>Total net deferred income tax liability</i>			
Domestic		\$ 2,920	\$ 2,267
Foreign		3,543	3,245
		\$ 6,463	\$ 5,512
Total net deferred income tax liability		\$ 6,463	\$ 5,512
Net current deferred income tax asset		74	43
Net noncurrent deferred income tax liability		\$ 6,537	\$ 5,555

(1) Net operating losses and tax credit carryforwards will expire between the years 2014 and 2033.

On an annual basis, the Company assesses the need to establish a valuation allowance for its deferred income tax assets, and if it is deemed more likely than not that its deferred income tax assets will not be realized, a valuation allowance is recorded. The ultimate realization of deferred income tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversals of deferred income tax liabilities including the available carryback and carryforward periods, projected future taxable income, and tax planning strategies in making this assessment. As at December 31, 2013, in order to fully realize all of the deferred income tax assets, the Company will need to generate future taxable income of approximately \$1.6 billion and, based upon the level of historical taxable income and projections of future taxable income over the periods in which the deferred income tax assets are deductible, management believes it is more likely than not that the Company will realize the benefits of these deductible differences. Management has assessed the impacts of the current economic environment and concluded there are no significant impacts to its assertions for the realization of deferred income tax assets. The Company has not recognized a deferred income tax asset (\$243 million as at December 31, 2013) on the unrealized foreign exchange loss recorded in Accumulated

other comprehensive loss relating to its net investment in foreign subsidiaries, as the Company does not expect this temporary difference to reverse in the foreseeable future.

The Company recognized tax credits of nil in 2013, and \$1 million in each of 2012 and 2011 for eligible research and development expenditures, which reduced the cost of properties.

The following table provides a reconciliation of unrecognized tax benefits on the Company's domestic and foreign tax positions:

<i>In millions</i>	<i>Year ended December 31,</i>	2013	2012	2011
Gross unrecognized tax benefits at beginning of year		\$ 36	\$ 46	\$ 57
<i>Increases for:</i>				
Tax positions related to the current year		2	1	1
Tax positions related to prior years		4	3	11
<i>Decreases for:</i>				
Tax positions related to prior years		(4)	-	-
Settlements		(8)	(13)	(21)
Lapse of the applicable statute of limitations		-	(1)	(2)
<i>Gross unrecognized tax benefits at end of year</i>		\$ 30	\$ 36	\$ 46
Adjustments to reflect tax treaties and other arrangements		(5)	(6)	(11)
<i>Net unrecognized tax benefits at end of year</i>		\$ 25	\$ 30	\$ 35

As at December 31, 2013, the total amount of gross unrecognized tax benefits was \$30 million, before considering tax treaties and other arrangements between taxation authorities. The amount of net unrecognized tax benefits as at December 31, 2013 was \$25 million. If recognized, all of the net unrecognized tax benefits as at December 31, 2013 would affect the effective tax rate. The Company believes that it is reasonably possible that approximately \$8 million of the net unrecognized tax benefits as at December 31, 2013 related to various federal, state, and provincial income tax matters, each of which are individually insignificant, may be recognized over the next twelve months as a result of settlements and a lapse of the applicable statute of limitations.

The Company recognizes accrued interest and penalties related to gross unrecognized tax benefits in Income tax expense in the Company's Consolidated Statement of Income. The Company recognized approximately \$2 million, \$3 million and \$4 million in accrued interest and penalties during the years ended December 31, 2013, 2012 and 2011, respectively. The Company had approximately \$5 million and \$9 million of accrued interest and penalties as at December 31, 2013 and 2012, respectively.

In Canada, the Company's federal and provincial income tax returns filed for the years 2007 to 2012 remain subject to examination by the taxation authorities. An examination of the Company's federal income tax returns for the 2009 year is currently in progress and is expected to be completed during 2014. Examinations on specific tax positions taken for federal and provincial income tax returns for the 2007 and 2008 year are currently in progress and are also expected to be completed during 2014. In the U.S., the

federal income tax returns filed for the year 2007 as well as 2009 to 2012 remain subject to examination by the taxation authorities, and the state income tax returns filed for the years 2009 to 2012 remain subject to examination by the taxation authorities. An examination of the federal income tax returns for the year 2007 as well as 2009 to 2011 is currently in progress. Examinations of certain state income tax returns by the state taxation authorities are currently in progress. The Company does not anticipate any significant impacts to its results of operations or financial position as a result of the final resolutions of such matters.

14 Segmented information

The Company manages its operations as one business segment over a single network that spans vast geographic distances and territories, with operations in Canada and the United States. Financial information reported at this level, such as revenues, operating income, and cash flow from operations, is used by corporate management, including the Company's chief operating decision-maker, in evaluating financial and operational performance and allocating resources across CN's network.

The Company's strategic initiatives, which drive its operational direction, are developed and managed centrally by corporate management and are communicated to its regional activity centers (the Western Region, Eastern Region and Southern Region). Corporate management is responsible for, among others, CN's marketing strategy, the management of large customer accounts, overall planning and control of infrastructure and rolling stock, the allocation of resources, and other functions such as financial planning, accounting and treasury.

The role of each region is to manage the day-to-day service requirements within their respective territories and control direct costs incurred locally. Such cost control is required to ensure that pre-established efficiency standards set at the corporate level are met. The regions execute the overall corporate strategy and operating plan established by corporate management, as their management of throughput and control of direct costs does not serve as the platform for the Company's decision-making process. Approximately 95% of the Company's freight revenues are from national accounts for which freight traffic spans North America and touches various commodity groups. As a result, the Company does not manage revenues on a regional basis since a large number of the movements originate in one region and pass through and/or terminate in another region.

The regions also demonstrate common characteristics in each of the following areas:

- (i) each region's sole business activity is the transportation of freight over the Company's extensive rail network;
- (ii) the regions service national accounts that extend over the Company's various commodity groups and across its rail network;

14 Segmented information *continued*

- (iii) the services offered by the Company stem predominantly from the transportation of freight by rail with the goal of optimizing the rail network as a whole;
- (iv) the Company and its subsidiaries, not its regions, are subject to single regulatory regimes in both Canada and the U.S.

For the years ended December 31, 2013, 2012, and 2011, no major customer accounted for more than 10% of total revenues and the largest rail freight customer represented approximately 2%, 2%, and 3%, respectively, of total rail freight revenues.

For the reasons mentioned herein, the Company reports as one operating segment.

The following tables provide information by geographic area:

<i>In millions</i>	<i>Year ended December 31,</i>	2013	2012	2011
<i>Revenues</i>				
Canada		\$ 7,149	\$ 6,770	\$ 6,169
U.S.		3,426	3,150	2,859
		\$ 10,575	\$ 9,920	\$ 9,028

<i>In millions</i>	<i>Year ended December 31,</i>	2013	2012	2011
<i>Net income</i>				
Canada		\$ 1,762	\$ 1,972	\$ 1,836
U.S.		850	708	621
		\$ 2,612	\$ 2,680	\$ 2,457

<i>In millions</i>	<i>December 31,</i>	2013	2012
<i>Properties</i>			
Canada		\$ 15,056	\$ 14,406
U.S.		11,171	10,135
		\$ 26,227	\$ 24,541

15 Earnings per share

On October 22, 2013, the Board of Directors of the Company approved a two-for-one common stock split in the form of a stock dividend of one additional common share of CN for each share outstanding, which was paid on November 29, 2013, to shareholders of record on November 15, 2013. All share and per share data presented herein reflect the impact of the stock split.

The following table provides a reconciliation between basic and diluted earnings per share:

<i>In millions, except per share data</i>	<i>Year ended December 31,</i>	2013	2012	2011
Net income		\$ 2,612	\$ 2,680	\$ 2,457
Weighted-average shares outstanding		843.1	871.1	902.2
Effect of stock options		3.0	4.3	6.7
Weighted-average diluted shares outstanding		846.1	875.4	908.9
Basic earnings per share		\$ 3.10	\$ 3.08	\$ 2.72
Diluted earnings per share		\$ 3.09	\$ 3.06	\$ 2.70

Basic earnings per share are calculated based on the weighted-average number of common shares outstanding over each period. Diluted earnings per share are calculated based on the weighted-average diluted shares outstanding using the treasury stock method, which assumes that any proceeds received from the exercise of in-the-money stock options would be used to purchase common shares at the average market price for the period.

16 Major commitments and contingencies

A. Leases

The Company has operating and capital leases, mainly for locomotives, freight cars and intermodal equipment. Of the capital leases, many provide the option to purchase the leased items at fixed values during or at the end of the lease term. As at December 31, 2013, the Company's commitments under these operating and capital leases were \$680 million and \$991 million, respectively. Minimum rental payments for operating leases having initial non-cancelable lease terms of more than one year and minimum lease payments for capital leases for the next five years and thereafter, are as follows:

<i>In millions</i>	Operating	Capital
2014	\$ 132	\$ 209
2015	111	113
2016	84	317
2017	66	154
2018	56	14
2019 and thereafter	231	184
	\$ 680	991
Less: Imputed interest on capital leases at rates ranging from approximately 0.7% to 8.5%		209
Present value of minimum lease payments included in debt		\$ 782

The Company also has operating lease agreements for its automotive fleet with one-year non-cancelable terms for which its practice is to renew monthly thereafter. The estimated annual

rental payments for such leases are approximately \$30 million and generally extend over five years.

Rent expense for all operating leases was \$179 million, \$162 million and \$143 million for the years ended December 31, 2013, 2012 and 2011, respectively. Contingent rentals and sub-lease rentals were not significant.

B. Commitments

As at December 31, 2013, the Company had commitments to acquire railroad ties, rail, freight cars, locomotives, and other equipment and services, as well as outstanding information technology service contracts and licenses, at an aggregate cost of \$482 million (\$735 million as at December 31, 2012). The Company also has estimated remaining commitments of approximately \$291 million (US\$273 million), in relation to the U.S. federal government legislative requirement to implement Positive Train Control (PTC) by 2015. In addition, it has estimated remaining commitments of approximately \$72 million (US\$68 million), in relation to the acquisition of the principal lines of the former Elgin, Joliet and Eastern Railway Company, for railroad infrastructure improvements, grade separation projects as well as commitments under a series of agreements with individual communities and a comprehensive voluntary mitigation program established to address surrounding municipalities' concerns. The Company also has agreements with fuel suppliers which allow but do not require the Company to purchase approximately 85% of its estimated 2014 volume, 60% of its anticipated 2015 volume, 55% of its anticipated 2016 volume and 20% of its anticipated 2017 volume at market prices prevailing on the date of the purchase.

C. Contingencies

In the normal course of business, the Company becomes involved in various legal actions seeking compensatory and occasionally punitive damages, including actions brought on behalf of various purported classes of claimants and claims relating to employee and third-party personal injuries, occupational disease and property damage, arising out of harm to individuals or property allegedly caused by, but not limited to, derailments or other accidents.

Canada

Employee injuries are governed by the workers' compensation legislation in each province whereby employees may be awarded either a lump sum or a future stream of payments depending on the nature and severity of the injury. As such, the provision for employee injury claims is discounted. In the provinces where the Company is self-insured, costs related to employee work-related injuries are accounted for based on actuarially developed estimates of the ultimate cost associated with such injuries, including compensation, health care and third-party administration costs. A comprehensive actuarial study is generally performed at least on a triennial basis. For all other legal actions, the Company maintains, and regularly updates on a case-by-case basis, provisions for such

items when the expected loss is both probable and can be reasonably estimated based on currently available information.

In 2013, the Company recorded a \$1 million increase to its provision for personal injuries and other claims in Canada as a result of a comprehensive actuarial study for employee injury claims as well as various other legal claims.

As at December 31, 2013, 2012 and 2011, the Company's provision for personal injury and other claims in Canada was as follows:

<i>In millions</i>	2013	2012	2011
Balance January 1	\$ 209	\$ 199	\$ 200
Accruals and other	38	55	31
Payments	(37)	(45)	(32)
<i>Balance December 31</i>	\$ 210	\$ 209	\$ 199
<i>Current portion – Balance December 31</i>	\$ 31	\$ 39	\$ 39

United States

Personal injury claims by the Company's employees, including claims alleging occupational disease and work-related injuries, are subject to the provisions of the Federal Employers' Liability Act (FELA). Employees are compensated under FELA for damages assessed based on a finding of fault through the U.S. jury system or through individual settlements. As such, the provision is undiscounted. With limited exceptions where claims are evaluated on a case-by-case basis, the Company follows an actuarial-based approach and accrues the expected cost for personal injury, including asserted and unasserted occupational disease claims, and property damage claims, based on actuarial estimates of their ultimate cost. A comprehensive actuarial study is performed annually.

For employee work-related injuries, including asserted occupational disease claims, and third-party claims, including grade crossing, trespasser and property damage claims, the actuarial valuation considers, among other factors, the Company's historical patterns of claims filings and payments. For unasserted occupational disease claims, the actuarial study includes the projection of the Company's experience into the future considering the potentially exposed population. The Company adjusts its liability based upon management's assessment and the results of the study. On an ongoing basis, management reviews and compares the assumptions inherent in the latest actuarial study with the current claim experience and, if required, adjustments to the liability are recorded.

Due to the inherent uncertainty involved in projecting future events, including events related to occupational diseases, which include but are not limited to, the timing and number of actual claims, the average cost per claim and the legislative and judicial environment, the Company's future payments may differ from current amounts recorded.

16 Major commitments and contingencies

continued

In 2013, the Company recorded an \$11 million reduction to its provision for U.S. personal injury and other claims attributable to non-occupational disease, third-party and occupational disease claims pursuant to the 2013 external actuarial study. In previous years, external actuarial studies have supported a net increase of \$1 million and a net reduction of \$6 million to the Company's provision for U.S. personal injury and other claims in 2012 and 2011, respectively. The previous years' changes were mainly attributable to changes in the Company's estimates of unasserted claims and costs related to asserted claims as a result of its ongoing risk mitigation strategy focused on reducing the frequency and severity of claims through injury prevention and containment; mitigation of claims; and lower settlements for existing claims.

As at December 31, 2013, 2012 and 2011, the Company's provision for personal injury and other claims in the U.S. was as follows:

<i>In millions</i>	2013	2012	2011
Balance January 1	\$ 105	\$ 111	\$ 146
Accruals and other	25	28	30
Payments	(24)	(34)	(65)
Balance December 31	\$ 106	\$ 105	\$ 111
<i>Current portion – Balance December 31</i>	\$ 14	\$ 43	\$ 45

Although the Company considers such provisions to be adequate for all its outstanding and pending claims, the final outcome with respect to actions outstanding or pending at December 31, 2013, or with respect to future claims, cannot be reasonably determined. When establishing provisions for contingent liabilities the Company considers, where a probable loss estimate cannot be made with reasonable certainty, a range of potential probable losses for each such matter, and records the amount it considers the most reasonable estimate within the range. However, when no amount within the range is a better estimate than any other amount, the minimum amount in the range is accrued. For matters where a loss is reasonably possible but not probable, a range of potential losses cannot be estimated due to various factors which may include the limited availability of facts, the lack of demand for specific damages and the fact that proceedings were at an early stage. Based on information currently available, the Company believes that the eventual outcome of the actions against the Company will not, individually or in the aggregate, have a material adverse effect on the Company's consolidated financial position. However, due to the inherent inability to predict with certainty unforeseeable future developments, there can be no assurance that the ultimate resolution of these actions will not have a material adverse effect on the Company's results of operations, financial position or liquidity in a particular quarter or fiscal year.

D. Environmental matters

The Company's operations are subject to numerous federal, provincial, state, municipal and local environmental laws and regulations in Canada and the U.S. concerning, among other things, emissions into the air; discharges into waters; the generation, handling, storage, transportation, treatment and disposal of waste, hazardous substances, and other materials; decommissioning of underground and aboveground storage tanks; and soil and groundwater contamination. A risk of environmental liability is inherent in railroad and related transportation operations; real estate ownership, operation or control; and other commercial activities of the Company with respect to both current and past operations.

Known existing environmental concerns

The Company has identified approximately 280 sites at which it is or may be liable for remediation costs, in some cases along with other potentially responsible parties, associated with alleged contamination and is subject to environmental clean-up and enforcement actions, including those imposed by the United States Federal Comprehensive Environmental Response, Compensation and Liability Act of 1980 (CERCLA), also known as the Superfund law, or analogous state laws. CERCLA and similar state laws, in addition to other similar Canadian and U.S. laws, generally impose joint and several liability for clean-up and enforcement costs on current and former owners and operators of a site, as well as those whose waste is disposed of at the site, without regard to fault or the legality of the original conduct. The Company has been notified that it is a potentially responsible party for study and clean-up costs at approximately 10 sites governed by the Superfund law (and analogous state laws) for which investigation and remediation payments are or will be made or are yet to be determined and, in many instances, is one of several potentially responsible parties.

The ultimate cost of addressing these known contaminated sites cannot be definitely established given that the estimated environmental liability for any given site may vary depending on the nature and extent of the contamination; the nature of anticipated response actions, taking into account the available clean-up techniques; evolving regulatory standards governing environmental liability; and the number of potentially responsible parties and their financial viability. As a result, liabilities are recorded based on the results of a four-phase assessment conducted on a site-by-site basis. A liability is initially recorded when environmental assessments occur, remedial efforts are probable, and when the costs, based on a specific plan of action in terms of the technology to be used and the extent of the corrective action required, can be reasonably estimated. The Company estimates the costs related to a particular site using cost scenarios established by external consultants based on the extent of contamination and expected costs for remedial efforts. In the case of multiple parties, the Company accrues its allocable share of liability taking into account the Company's alleged responsibility, the number of potentially responsible parties and their ability to pay their respective share of

the liability. Adjustments to initial estimates are recorded as additional information becomes available.

The Company's provision for specific environmental sites is undiscounted and includes costs for remediation and restoration of sites, as well as monitoring costs. Environmental accruals, which are classified as Casualty and other in the Consolidated Statement of Income, include amounts for newly identified sites or contaminants as well as adjustments to initial estimates. Recoveries of environmental remediation costs from other parties are recorded as assets when their receipt is deemed probable.

As at December 31, 2013, 2012 and 2011, the Company's provision for specific environmental sites was as follows:

<i>In millions</i>	2013	2012	2011
Balance January 1	\$ 123	\$ 152	\$ 150
Accruals and other	14	(5)	17
Payments	(18)	(24)	(15)
<i>Balance December 31</i>	\$ 119	\$ 123	\$ 152
<i>Current portion – Balance December 31</i>	\$ 41	\$ 31	\$ 63

The Company anticipates that the majority of the liability at December 31, 2013 will be paid out over the next five years. However, some costs may be paid out over a longer period. Based on the information currently available, the Company considers its provisions to be adequate.

Unknown existing environmental concerns

While the Company believes that it has identified the costs likely to be incurred for environmental matters in the next several years based on known information, the discovery of new facts, future changes in laws, the possibility of releases of hazardous materials into the environment and the Company's ongoing efforts to identify potential environmental liabilities that may be associated with its properties may result in the identification of additional environmental liabilities and related costs. The magnitude of such additional liabilities and the costs of complying with future environmental laws and containing or remediating contamination cannot be reasonably estimated due to many factors, including:

- (i) the lack of specific technical information available with respect to many sites;
- (ii) the absence of any government authority, third-party orders, or claims with respect to particular sites;
- (iii) the potential for new or changed laws and regulations and for development of new remediation technologies and uncertainty regarding the timing of the work with respect to particular sites; and
- (iv) the determination of the Company's liability in proportion to other potentially responsible parties and the ability to recover costs from any third parties with respect to particular sites.

Therefore, the likelihood of any such costs being incurred or whether such costs would be material to the Company cannot be determined at this time. There can thus be no assurance that liabilities or costs related to environmental matters will not be incurred in the future, or will not have a material adverse effect on the Company's financial position or results of operations in a particular quarter or fiscal year, or that the Company's liquidity will not be adversely impacted by such liabilities or costs, although management believes, based on current information, that the costs to address environmental matters will not have a material adverse effect on the Company's financial position or liquidity. Costs related to any unknown existing or future contamination will be accrued in the period in which they become probable and reasonably estimable.

Future occurrences

In railroad and related transportation operations, it is possible that derailments or other accidents, including spills and releases of hazardous materials, may occur that could cause harm to human health or to the environment. As a result, the Company may incur costs in the future, which may be material, to address any such harm, compliance with laws and other risks, including costs relating to the performance of clean-ups, payment of environmental penalties and remediation obligations, and damages relating to harm to individuals or property.

Regulatory compliance

The Company may incur significant capital and operating costs associated with environmental regulatory compliance and clean-up requirements, in its railroad operations and relating to its past and present ownership, operation or control of real property. Operating expenses for environmental matters amounted to \$18 million in 2013, \$16 million in 2012 and \$4 million in 2011. In addition, based on the results of its operations and maintenance programs, as well as ongoing environmental audits and other factors, the Company plans for specific capital improvements on an annual basis. Certain of these improvements help ensure facilities, such as fuelling stations and waste water and storm water treatment systems, comply with environmental standards and include new construction and the updating of existing systems and/or processes. Other capital expenditures relate to assessing and remediating certain impaired properties. The Company's environmental capital expenditures amounted to \$10 million in 2013, \$13 million in 2012 and \$11 million in 2011.

E. Guarantees and indemnifications

In the normal course of business, the Company, including certain of its subsidiaries, enters into agreements that may involve providing guarantees or indemnifications to third parties and others, which may extend beyond the term of the agreements. These include, but are not limited to, residual value guarantees on operating leases, standby letters of credit, surety and other bonds, and indemnifications that are customary for the type of transaction or for the railway business.

16 Major commitments and contingencies

continued

The Company is required to recognize a liability for the fair value of the obligation undertaken in issuing certain guarantees on the date the guarantee is issued or modified. In addition, where the Company expects to make a payment in respect of a guarantee, a liability will be recognized to the extent that one has not yet been recognized.

(i) Guarantee of residual values of operating leases

The Company has guaranteed a portion of the residual values of certain of its assets under operating leases with expiry dates between 2014 and 2021, for the benefit of the lessor. If the fair value of the assets at the end of their respective lease term is less than the fair value, as estimated at the inception of the lease, then the Company must, under certain conditions, compensate the lessor for the shortfall. As at December 31, 2013, the maximum exposure in respect of these guarantees was \$160 million. There are no recourse provisions to recover any amounts from third parties.

(ii) Other guarantees

As at December 31, 2013, the Company, including certain of its subsidiaries, had granted \$481 million of irrevocable standby letters of credit and \$90 million of surety and other bonds, issued by highly rated financial institutions, to third parties to indemnify them in the event the Company does not perform its contractual obligations. As at December 31, 2013, the maximum potential liability under these guarantee instruments was \$571 million, of which \$528 million related to workers' compensation and other employee benefit liabilities and \$43 million related to other liabilities. The letters of credit were drawn on the Company's bilateral letter of credit facilities. The Company had not recorded a liability as at December 31, 2013 with respect to these guarantee instruments as they related to the Company's future performance and the Company did not expect to make any payments under these guarantee instruments. The majority of the guarantee instruments mature at various dates between 2014 and 2016.

(iii) General indemnifications

In the normal course of business, the Company has provided indemnifications, customary for the type of transaction or for the railway business, in various agreements with third parties, including indemnification provisions where the Company would be required to indemnify third parties and others. Indemnifications are found in various types of contracts with third parties which include, but are not limited to:

- (a) contracts granting the Company the right to use or enter upon property owned by third parties such as leases, easements, trackage rights and sidetrack agreements;
- (b) contracts granting rights to others to use the Company's property, such as leases, licenses and easements;

- (c) contracts for the sale of assets;
- (d) contracts for the acquisition of services;
- (e) financing agreements;
- (f) trust indentures, fiscal agency agreements, underwriting agreements or similar agreements relating to debt or equity securities of the Company and engagement agreements with financial advisors;
- (g) transfer agent and registrar agreements in respect of the Company's securities;
- (h) trust and other agreements relating to pension plans and other plans, including those establishing trust funds to secure payment to certain officers and senior employees of special retirement compensation arrangements;
- (i) pension transfer agreements;
- (j) master agreements with financial institutions governing derivative transactions;
- (k) settlement agreements with insurance companies or other third parties whereby such insurer or third-party has been indemnified for any present or future claims relating to insurance policies, incidents or events covered by the settlement agreements; and
- (l) acquisition agreements.

To the extent of any actual claims under these agreements, the Company maintains provisions for such items, which it considers to be adequate. Due to the nature of the indemnification clauses, the maximum exposure for future payments may be material. However, such exposure cannot be reasonably determined.

During the year, the Company entered into various indemnification contracts with third parties for which the maximum exposure for future payments cannot be reasonably determined. As a result, the Company was unable to determine the fair value of these guarantees and accordingly, no liability was recorded. There are no recourse provisions to recover any amounts from third parties.

17 Financial instruments

A. Risk management

In the normal course of business, the Company is exposed to various risks such as customer credit risk, commodity price risk, interest rate risk, foreign currency risk, and liquidity risk. To manage these risks, the Company follows a financial risk management framework, which is monitored and approved by the Company's Finance Committee, with a goal of maintaining a strong balance sheet, optimizing earnings per share and free cash flow, financing its operations at an optimal cost of capital and preserving its liquidity. The Company has limited involvement with derivative financial instruments in the management of its risks and does not use them for trading purposes. At December 31, 2013 and 2012, the Company did not have any significant derivative financial instruments outstanding.

(i) Customer credit risk

In the normal course of business, the Company monitors the financial condition and credit limits of its customers and reviews the credit history of each new customer. Although the Company believes there are no significant concentrations of credit risk, economic conditions can affect the Company's customers and can result in an increase to the Company's credit risk and exposure to business failures of its customers. To manage its credit risk, on an ongoing basis, the Company's focus is on keeping the average daily sales outstanding within an acceptable range and working with customers to ensure timely payments, and in certain cases, requiring financial security, including letters of credit.

(ii) Fuel

The Company is exposed to commodity price risk related to purchases of fuel and the potential reduction in net income due to increases in the price of diesel. The impact of variable fuel expense is mitigated substantially through the Company's fuel surcharge program which apportions incremental changes in fuel prices to shippers within agreed upon guidelines. While this program provides effective coverage, residual exposure remains given that fuel price risk cannot be completely mitigated due to timing and given the volatility in the market. As such, the Company may enter into derivative instruments to mitigate such risk when considered appropriate.

(iii) Interest rate

The Company is exposed to interest rate risk, which is the risk that the fair value or future cash flows of a financial instrument will vary as a result of changes in market interest rates.

Such risk exists in relation to the Company's pension and postretirement plans and to its long-term debt. Overall return in the capital markets and the level of interest rates affect the funded status of the Company's pension plans, particularly the Company's main Canadian pension plan. Adverse changes with respect to pension plan returns and the level of interest rates from the date of the last actuarial valuations may have a material adverse effect on the funded status of the plans and on the Company's results of operations.

The Company mainly issues fixed-rate debt, which exposes the Company to variability in the fair value of the debt. The Company also issues debt with variable interest rates which exposes the Company to variability in interest expense. To manage its interest rate exposure, the Company manages its borrowings in line with liquidity needs, maturity schedule, and currency and interest rate profile. In anticipation of future debt issuances, the Company may enter into forward rate agreements. The Company does not currently hold any significant derivative financial instruments to manage its interest rate risk. At December 31, 2013, Accumulated other comprehensive loss included an unamortized gain of \$8 million, \$6 million after-tax (\$8 million, \$6 million after-tax at December 31, 2012) relating to treasury lock transactions settled in a prior year, which are being amortized over the term of the related debt.

(iv) Foreign currency

The Company conducts its business in both Canada and the U.S. and as a result, is affected by currency fluctuations. Changes in the exchange rate between the Canadian dollar and other currencies (including the US dollar) make the goods transported by the Company more or less competitive in the world marketplace and thereby further affect the Company's revenues and expenses.

All of the Company's U.S. operations are self-contained foreign entities with the US dollar as their functional currency. Accordingly, the U.S. operations' assets and liabilities are translated into Canadian dollars at the rate in effect at the balance sheet date and the revenues and expenses are translated at average exchange rates during the year. All adjustments resulting from the translation of the foreign operations are recorded in Other comprehensive income (loss). For the purpose of minimizing volatility of earnings resulting from the conversion of US dollar-denominated long-term debt into the Canadian dollar, the Company designates the US dollar-denominated long-term debt of the parent company as a foreign currency hedge of its net investment in U.S. subsidiaries. As a result, from the dates of designation, foreign exchange gains and losses on translation of the Company's US dollar-denominated long-term debt are recorded in Accumulated other comprehensive loss.

Occasionally, the Company enters into short-term foreign exchange contracts as part of its cash management strategy. The Company does not hold or issue derivative financial instruments for trading or speculative purposes. Changes in the fair value of forward contracts, resulting from changes in foreign exchange rates, are recognized in the Consolidated Statement of Income as they occur. As at December 31, 2013, a gain of \$6 million, before tax, related to the fair value of the foreign exchange forward contracts of US\$325 million, was recorded in Other income on the Consolidated Statement of Income.

(v) Liquidity risk

The Company monitors and manages its cash requirements to ensure sufficient access to funds to meet operational and investing requirements. The Company pursues a solid financial policy framework with the goal of maintaining a strong balance sheet, by monitoring its adjusted debt-to-total capitalization ratio and its adjusted debt-to-adjusted earnings before interest, income taxes, depreciation and amortization (EBITDA) multiple, and preserving an investment grade credit rating to be able to maintain access to public financing.

The Company's principal source of liquidity is cash generated from operations, which is supplemented by its commercial paper program to meet short-term liquidity needs. If the Company were to lose access to the program for an extended period of time, the Company could rely on its \$800 million revolving credit facility. The Company's primary uses of funds are for working capital requirements, including income tax installments as they become due and pension contributions, contractual obligations, capital expenditures relating to track infrastructure and other, acquisitions, dividend payouts, and the repurchase of shares through a share buyback program, when applicable.

17 Financial instruments *continued*

The Company sets priorities on its uses of available funds based on short-term operational requirements, expenditures to maintain a safe railway and strategic initiatives, while also considering its long-term contractual obligations and returning value to its shareholders.

B. Fair value of financial instruments

For financial assets and liabilities measured at fair value on a recurring basis, fair value is the price the Company would receive to sell an asset or pay to transfer a liability in an orderly transaction with a market participant at the measurement date. In the absence of active markets for identical assets or liabilities, such measurements involve developing assumptions based on market observable data and, in the absence of such data, internal information that is believed to be consistent with what market participants would use in a hypothetical transaction that occurs at the measurement date. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect the Company's market assumptions. Preference is given to observable inputs. These two types of inputs create the following fair value hierarchy:

Level 1: Quoted prices for identical instruments in active markets.

Level 2: Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations whose inputs are observable or whose significant value drivers are observable.

Level 3: Significant inputs to the valuation model are unobservable.

The following table provides the carrying amounts and estimated fair values of the Company's financial instruments as at December 31, 2013 and December 31, 2012 for which the carrying values on the Consolidated Balance Sheet are different from their fair values:

<i>In millions</i>	December 31, 2013		December 31, 2012	
	Carrying amount	Fair value	Carrying amount	Fair value
<i>Financial assets</i>				
Investments (Note 5)	\$ 57	\$ 164	\$ 30	\$ 125
<i>Financial liabilities</i>				
Total debt (Note 8)	\$ 7,840	\$ 8,683	\$ 6,900	\$ 8,379

The Company uses the following methods and assumptions to estimate the fair value of each class of financial instruments for which the carrying amounts are included in the Consolidated Balance Sheet under the following captions:

(i) *Cash and cash equivalents, Restricted cash and cash equivalents, Accounts receivable, Other current assets, Accounts payable and other:*

The carrying amounts approximate fair value because of the short maturity of these instruments. Cash and cash equivalents and Restricted cash and cash equivalents include highly liquid investments purchased three months or less from maturity and are classified as Level 1. Accounts receivable, Other current assets, and Accounts payable and other are classified as Level 2 as they may not be priced using quoted prices, but rather determined from market observable information.

(ii) *Intangible and other assets:*

Included in Intangible and other assets are equity investments for which the carrying value approximates the fair value, with the exception of certain cost investments for which the fair value is estimated based on the Company's proportionate share of the underlying net assets. Investments are classified as Level 3 as their fair value is based on significant unobservable inputs.

(iii) *Debt:*

The fair value of the Company's debt is estimated based on the quoted market prices for the same or similar debt instruments, as well as discounted cash flows using current interest rates for debt with similar terms, company rating, and remaining maturity. The Company's debt is classified as Level 2.

18 Accumulated other comprehensive loss

The components of Accumulated other comprehensive loss are as follows:

<i>In millions</i>	Pension and other postretirement benefit plans	Foreign currency items	Derivative instruments	Total before tax	Tax recovery (expense)	Total net of tax
<i>Beginning balance at December 31, 2010</i>	\$ (1,193)	\$ (582)	\$ 10	\$ (1,765)	\$ 56	\$ (1,709)
Other comprehensive income (loss) before reclassifications:						
Foreign currency translation adjustments	-	8	-	8	19	27
Actuarial loss arising during the year	(1,541)	-	-	(1,541)	397	(1,144)
Prior service cost from plan amendment arising during the year	(28)	-	-	(28)	7	(21)
Amounts reclassified from accumulated other comprehensive income (loss):						
Amortization of net actuarial loss	8	-	-	8 ⁽¹⁾	(2) ⁽³⁾	6
Amortization of prior service cost	4	-	-	4 ⁽¹⁾	(1) ⁽³⁾	3
Amortization of gain on treasury lock	-	-	(2)	(2) ⁽²⁾	1 ⁽³⁾	(1)
Other comprehensive income (loss)	(1,557)	8	(2)	(1,551)	421	(1,130)
<i>Ending balance at December 31, 2011</i>	\$ (2,750)	\$ (574)	\$ 8	\$ (3,316)	\$ 477	\$ (2,839)
Other comprehensive income (loss) before reclassifications:						
Foreign currency translation adjustments	-	(5)	-	(5)	(17)	(22)
Actuarial loss arising during the year	(660)	-	-	(660)	176	(484)
Prior service cost from plan amendment arising during the year	(6)	-	-	(6)	2	(4)
Amounts reclassified from accumulated other comprehensive income (loss):						
Amortization of net actuarial loss	119	-	-	119 ⁽¹⁾	(32) ⁽³⁾	87
Amortization of prior service cost	7	-	-	7 ⁽¹⁾	(2) ⁽³⁾	5
Other comprehensive income (loss)	(540)	(5)	-	(545)	127	(418)
<i>Ending balance at December 31, 2012</i>	\$ (3,290)	\$ (579)	\$ 8	\$ (3,861)	\$ 604	\$ (3,257)
Other comprehensive income (loss) before reclassifications:						
Foreign currency translation adjustments	-	46	-	46	59	105
Actuarial gain arising during the year	1,544	-	-	1,544	(412)	1,132
Amounts reclassified from accumulated other comprehensive income (loss):						
Amortization of net actuarial loss	226	-	-	226 ⁽¹⁾	(60) ⁽³⁾	166
Amortization of prior service cost	5	-	-	5 ⁽¹⁾	(1) ⁽³⁾	4
Other comprehensive income (loss)	1,775	46	-	1,821	(414)	1,407
<i>Ending balance at December 31, 2013</i>	\$ (1,515)	\$ (533)	\$ 8	\$ (2,040)	\$ 190	\$ (1,850)

(1) Reclassified to Labor and fringe benefits on the Consolidated Statement of Income and included in components of net periodic benefit cost. See Note 11 – Pensions and other postretirement benefits.

(2) Reclassified to Other income on the Consolidated Statement of Income.

(3) Included in Income tax expense on the Consolidated Statement of Income.

CN is committed to being a good corporate citizen. At CN, sound corporate citizenship touches nearly every aspect of what we do, from governance to business ethics, from safety to environmental protection. Central to this comprehensive approach is our strong belief that good corporate citizenship is simply good business.

CN has always recognized the importance of good governance. As it evolved from a Canadian institution to a North American publicly traded company, CN voluntarily followed certain corporate governance requirements that, as a company based in Canada, it was not technically compelled to follow. We continue to do so today. Since many of our peers – and shareholders – are based in the United States, we want to provide the same assurances of sound practices as our U.S. competitors.

Hence, we adopt and adhere to corporate governance practices that either meet or exceed applicable Canadian and U.S. corporate governance standards. As a Canadian reporting issuer with securities listed on the Toronto Stock Exchange (TSX) and the New York Stock Exchange (NYSE), CN complies with applicable rules adopted by the Canadian Securities Administrators and the rules of the U.S. Securities and Exchange Commission giving effect to the provisions of the U.S. Sarbanes-Oxley Act of 2002.

As a Canadian company, we are not required to comply with many of the NYSE corporate governance rules, and instead may comply with Canadian governance practices. However, except as summarized on our website (www.cn.ca in the Delivering Responsibly – Governance section), our governance practices comply with the NYSE corporate governance rules in all significant respects.

Consistent with the belief that ethical conduct goes beyond compliance and resides in a solid governance culture, the Delivering Responsibly – Governance section on the CN website contains CN's Corporate Governance Manual (including the charters of our Board and of our Board committees) and CN's Code of Business Conduct. Printed versions of these documents are also available upon request to CN's Corporate Secretary.

Because it is important to CN to uphold the highest standards in corporate governance and that any potential or real wrongdoings be reported, CN has also adopted methods allowing employees and third parties to report accounting, auditing and other concerns, as more fully described on our website.

We are proud of our corporate governance practices. For more information on these practices, please refer to our website, as well as to our proxy circular – mailed to our shareholders and also available on our website. CN understands that our long-term success is connected to our contribution to a sustainable future. That is why we are committed to the safety of our employees, the public and the environment; delivering reliable, efficient service so our customers succeed in global markets; building stronger communities; and providing a great place to work. Our sustainability activities are outlined in our *Delivering Responsibly* report, which can be found on our website: www.cn.ca

For the second straight year, CN's practices have earned it a place on the Dow Jones Sustainability World Index (DJSI), which includes an assessment of CN's governance practices, in addition to being named to the DJSI North America index for the fifth consecutive year. CN was also recognized for climate change transparency for the fourth year in a row by earning a position in CDP's Canada 200 Climate Disclosure Leadership Index.

CN received the Best Corporate Governance Award from IR Magazine in 2009, 2010 and 2014. As well, in 2011 we received the Canadian Coalition for Good Governance (CCGG) Award for Best Disclosure of Board Governance Practices and Director Qualifications; and in 2012 the CCGG Award for Best Disclosure of Approach to Executive Compensation.

Shareholder and Investor Information

Annual meeting

The annual meeting of shareholders will be held at 9:00 a.m. PDT on April 23, 2014 at:

The Westin Bayshore
Bayshore Grand Ballroom
1601 Bayshore Drive
Vancouver, British Columbia, Canada

Annual information form

The annual information form may be obtained by writing to:

The Corporate Secretary
Canadian National Railway Company
935 de La Gauchetière Street West
Montreal, Quebec H3B 2M9

It is also available on CN's website.

Transfer agent and registrar

Computershare Trust Company of Canada

Offices in:
Montreal, Quebec;
Toronto, Ontario;
Calgary, Alberta;
Vancouver, British Columbia

Telephone: 1-800-564-6253
www.investorcentre.com

Co-transfer agent and co-registrar

Computershare Trust Company N.A.
Att: Stock Transfer Department

Overnight Mail Delivery:
250 Royall Street, Canton MA 02021

Regular Mail Delivery: P.O. Box 43078,
Providence, RI 02940-3078

Telephone: 1-800-962-4284

Additional copies of this report are available from:

CN Public Affairs

935 de La Gauchetière Street West
Montreal, Quebec H3B 2M9
Telephone: 1-888-888-5909
Email: contact@cn.ca

Shareholder services

Shareholders having inquiries concerning their shares, wishing to obtain information about CN, or to receive dividends by direct deposit or in U.S. dollars may obtain detailed information by communicating with:

Computershare Trust Company of Canada
Shareholder Services
100 University Avenue, 8th Floor
Toronto, Ontario M5J 2Y1

Telephone: 1-800-564-6253
www.investorcentre.com

Stock exchanges

CN common shares are listed on the Toronto and New York stock exchanges.

Ticker symbols:

CNR (Toronto Stock Exchange)
CNI (New York Stock Exchange)

Investor relations

Janet Drysdale
Vice-President, Investor Relations
Telephone: 514-399-0052

Head office

Canadian National Railway Company
935 de La Gauchetière Street West
Montreal, Quebec H3B 2M9

P.O. Box 8100
Montreal, Quebec H3C 3N4

La version française du présent rapport est disponible à l'adresse suivante :

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