

CANADIAN NATIONAL RAILWAY CO
Form 6-K
February 09, 2011

FORM 6-K
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Report of Foreign Issuer

Pursuant to Rule 13a-16 or 15d-16
of the Securities Exchange Act of 1934

For the month of February, 2011

Commission File Number: 001-02413

Canadian National Railway Company
(Translation of registrant's name into English)

935 de la Gauchetiere Street West
Montreal, Quebec
Canada H3B 2M9
(Address of principal executive offices)

Indicate by check mark whether the registrant files or will file annual reports under cover of Form 20-F or Form 40-F:

Form 20-F Form 40-F

Indicate by check mark if the registrant is submitting the Form 6-K in paper as permitted by Regulation S-T Rule 101(b)(1):

Yes No

Indicate by check mark if the registrant is submitting the Form 6-K in paper as permitted by Regulation S-T Rule 101(b)(7):

Yes No

Indicate by check mark whether by furnishing the information contained in this Form, the Registrant is also thereby furnishing the information to the Commission pursuant to Rule 12g3-2(b) under the Securities Exchange Act of 1934:

Yes No

If "Yes" is marked, indicate below the file number assigned to the registrant in connection with Rule 12g3-2(b): N/A

Canadian National Railway Company

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Management's Report on Internal Control over Financial Reporting

Item 1

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, 2010 using the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in Internal Control - Integrated Framework. Based on this assessment, management has determined that the Company's internal control over financial reporting was effective as of December 31, 2010.

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, 2010 and has also expressed an unqualified audit opinion on the Company's 2010 consolidated financial statements as stated in their Reports of Independent Registered Public Accounting Firm dated February 9, 2011.

(s) Claude Mongeau
President and Chief Executive Officer

February 9, 2011

(s) Luc Jobin
Executive Vice-President and Chief Financial Officer

February 9, 2011

Report of Independent Registered Public Accounting Firm

Item 2

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, 2010 and 2009, 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, 2010. 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 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 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 financial position of the Company as of December 31, 2010 and 2009, and the results of its operations and its cash flows for each of the years in the three-year period ended December 31, 2010, in conformity with generally accepted accounting principles in the United States.

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, 2010, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (“COSO”), and our report dated February 9, 2011 expressed an unqualified opinion on the effectiveness of the Company’s internal control over financial reporting.

(s) KPMG LLP*
Chartered Accountants

Montreal, Canada
February 9, 2011

*CA Auditor permit no.
23443

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.

Report of Independent Registered Public Accounting Firm

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, 2010, based on the criteria established in Internal Control—Integrated Framework 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, 2010, based on criteria established in Internal Control—Integrated Framework issued by the COSO.

We also have audited, in accordance with Canadian generally accepted auditing standards and with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of the Company as of December 31, 2010 and 2009, 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, 2010, and our report dated February 9, 2011 expressed an unqualified opinion on those consolidated financial statements.

(s) KPMG LLP*
Chartered Accountants

Montreal, Canada
February 9, 2011

*CA Auditor permit no. 23443

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.

Consolidated Statement of Income

U.S. GAAP

Item 3

In millions, except per share data	Year ended December 31,	2010	2009	2008
Revenues		\$ 8,297	\$ 7,367	\$ 8,482
Operating expenses				
Labor and fringe benefits		1,744	1,696	1,674
Purchased services and material		1,036	1,027	1,137
Fuel		1,048	820	1,456
Depreciation and amortization		834	790	725
Equipment rents		243	284	262
Casualty and other		368	344	334
Total operating expenses		5,273	4,961	5,588
Operating income		3,024	2,406	2,894
Interest expense		(360)	(412)	(375)
Other income (Note 13)		212	267	26
Income before income taxes		2,876	2,261	2,545
Income tax expense (Note 14)		(772)	(407)	(650)
Net income		\$ 2,104	\$ 1,854	\$ 1,895
Earnings per share (Note 16)				
Basic		\$ 4.51	\$ 3.95	\$ 3.99
Diluted		\$ 4.48	\$ 3.92	\$ 3.95
Weighted-average number of shares				
Basic		466.3	469.2	474.7
Diluted		470.1	473.5	480.0

See accompanying notes to consolidated financial statements.

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Consolidated Statement of Comprehensive Income

U.S. GAAP

In millions	Year ended December 31,	2010	2009	2008
Net income	\$	2,104	\$ 1,854	\$ 1,895
Other comprehensive income (loss) (Note 19)				
Foreign exchange gain (loss) on:				
Translation of the net investment in foreign operations		(330)	(998)	1,259
Translation of US dollar-denominated long-term debt designated as				
a hedge of the net investment in U.S. subsidiaries		315	976	(1,266)
Pension and other postretirement benefit plans (Note 12):				
Net actuarial loss arising during the year		(931)	(868)	(452)
Prior service cost arising during the year		(5)	(2)	(3)
Amortization of net actuarial loss (gain) included in net periodic benefit cost (income)		1	2	(2)
Amortization of prior service cost included in net periodic benefit cost (income)		2	5	21
Derivative instruments (Note 18)		(1)	-	-
Other comprehensive loss before income taxes		(949)	(885)	(443)
Income tax recovery		188	92	319
Other comprehensive loss		(761)	(793)	(124)
Comprehensive income	\$	1,343	\$ 1,061	\$ 1,771

See accompanying notes to consolidated financial statements.

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Consolidated Balance Sheet

U.S. GAAP

In millions	December 31,	2010	2009
Assets			
Current assets			
Cash and cash equivalents	\$	490	\$ 352
Accounts receivable (Note 4)		775	797
Material and supplies		210	170
Deferred income taxes (Note 14)		53	105
Other		62	66
Total current assets		1,590	1,490
Properties (Note 5)		22,917	22,630
Intangible and other assets (Note 6)		699	1,056
Total assets	\$	25,206	\$ 25,176
Liabilities and shareholders' equity			
Current liabilities			
Accounts payable and other (Note 7)	\$	1,366	\$ 1,167
Current portion of long-term debt (Note 9)		540	70
Total current liabilities		1,906	1,237
Deferred income taxes (Note 14)		5,152	5,119
Other liabilities and deferred credits (Note 8)		1,333	1,196
Long-term debt (Note 9)		5,531	6,391
Shareholders' equity			
Common shares (Note 10)		4,252	4,266
Accumulated other comprehensive loss (Note 19)		(1,709)	(948)
Retained earnings		8,741	7,915
Total shareholders' equity		11,284	11,233
Total liabilities and shareholders' equity	\$	25,206	\$ 25,176

On behalf of the Board:

David G. A. McLean

Claude Mongeau

Director

Director

See accompanying notes to consolidated financial statements.

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Consolidated Statement of Changes in Shareholders' Equity

U.S. GAAP

In millions	Issued and outstanding common shares	Common shares	Accumulated other comprehensive loss	Retained earnings	Total shareholders' equity
Balances at December 31, 2007	485.2	\$ 4,283	\$ (31)	\$ 5,925	\$ 10,177
Net income	-	-	-	1,895	1,895
Stock options exercised and other (Notes 10, 11)	2.4	68	-	-	68
Share repurchase programs (Note 10)	(19.4)	(172)	-	(849)	(1,021)
Other comprehensive loss (Note 19)	-	-	(124)	-	(124)
Dividends (\$0.92 per share)	-	-	-	(436)	(436)
Balances at December 31, 2008	468.2	4,179	(155)	6,535	10,559
Net income	-	-	-	1,854	1,854
Stock options exercised and other (Notes 10, 11)	2.8	87	-	-	87
Other comprehensive loss (Note 19)	-	-	(793)	-	(793)
Dividends (\$1.01 per share)	-	-	-	(474)	(474)
Balances at December 31, 2009	471.0	4,266	(948)	7,915	11,233
Net income	-	-	-	2,104	2,104
Stock options exercised and other (Notes 10, 11)	3.4	124	-	-	124
Share repurchase program (Note 10)	(15.0)	(138)	-	(775)	(913)
Other comprehensive loss (Note 19)	-	-	(761)	-	(761)
Dividends (\$1.08 per share)	-	-	-	(503)	(503)
Balances at December 31, 2010	459.4	\$ 4,252	\$ (1,709)	\$ 8,741	\$ 11,284

See accompanying notes to consolidated financial statements.

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Consolidated Statement of Cash Flows

U.S. GAAP

In millions ended December 31,	Year	2010	2009	2008
Operating activities				
Net income	\$	2,104	\$ 1,854	\$ 1,895
Adjustments to reconcile net income to net cash provided by operating activities:				
Depreciation and amortization		834	790	725
Deferred income taxes (Note 14)		418	138	230
Gain on disposal of property (Notes 5, 13)		(152)	(226)	-
Changes in operating assets and liabilities:				
Accounts receivable (Note 4)		(3)	39	(432)
Material and supplies		(43)	32	(23)
Accounts payable and other		285	(204)	(127)
Other current assets		13	77	37
Other, net		(457)	(221)	(274)
Net cash provided by operating activities		2,999	2,279	2,031
Investing activities				
Property additions		(1,586)	(1,402)	(1,424)
Acquisitions, net of cash acquired (Note 3)		-	(373)	(50)
Disposal of property (Note 5)		168	231	-
Other, net		35	107	74
Net cash used in investing activities		(1,383)	(1,437)	(1,400)
Financing activities				
Issuance of long-term debt		-	1,626	4,433
Repayment of long-term debt		(184)	(2,109)	(3,589)
Issuance of common shares due to exercise of stock options and related excess tax benefits realized (Note 11)		115	73	54
Repurchase of common shares (Note 10)		(913)	-	(1,021)
Dividends paid		(503)	(474)	(436)
Net cash used in financing activities		(1,485)	(884)	(559)
Effect of foreign exchange fluctuations on US dollar-denominated cash and cash equivalents				
		7	(19)	31
Net increase (decrease) in cash and cash equivalents		138	(61)	103
Cash and cash equivalents, beginning of year		352	413	310
Cash and cash equivalents, end of year	\$	490	\$ 352	\$ 413
Supplemental cash flow information				
Net cash receipts from customers and other	\$	8,404	\$ 7,505	\$ 8,012

Net cash payments for:

Employee services, suppliers and other expenses	(4,334)	(4,323)	(4,935)
Interest	(366)	(407)	(396)
Personal injury and other claims (Note 17)	(64)	(112)	(91)
Pensions (Note 12)	(427)	(139)	(134)
Income taxes (Note 14)	(214)	(245)	(425)
Net cash provided by operating activities	\$ 2,999	\$ 2,279	\$ 2,031

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.

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 United States (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) (see Note 19 – 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. 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 the Consolidated Statement of Income. Any gains or losses on the sale of accounts receivable are calculated by comparing the carrying amount of the accounts receivable sold to the total of the cash proceeds

on sale and the fair value of the retained interest in such receivables on the date of transfer. Costs related to the sale of accounts receivable are recognized in earnings in the period incurred.

F. 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.

G. 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 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.

H. 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.

I. Pensions

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

the cost of pension benefits provided in exchange for employees' services rendered during the year;

- (i)
- (ii) the interest cost of pension obligations;
the expected long-term return on pension fund assets;
- (iii)

- the amortization of prior service costs and amendments over the expected average remaining service life of the
- (iv) 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.

Notes to Consolidated Financial Statements

U.S. GAAP

J. 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.

K. 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.

L. 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.

M. 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 tax asset or liability is included in the computation of net income or Other comprehensive income (loss). Deferred 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.

N. 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.

O. 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. 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 11 – Stock plans, for the assumptions used to determine fair value and for other required disclosures.

P. Recent accounting pronouncement

The Accounting Standards Board of the Canadian Institute of Chartered Accountants requires all publicly accountable enterprises to report under International Financial Reporting Standards (IFRS) for the fiscal year beginning on or after January 1, 2011. However, National

Notes to Consolidated Financial Statements

U.S. GAAP

Instrument 52-107 issued by the Ontario Securities Commission allows foreign issuers, as defined by the U.S. Securities and Exchange Commission (SEC), such as CN, to file with Canadian securities regulators financial statements prepared in accordance with U.S. GAAP. As such, the Company has decided not to report under IFRS by 2011 and to continue reporting under U.S. GAAP. The SEC has issued a roadmap for the potential convergence to IFRS for U.S. issuers and foreign issuers which stipulates that the SEC will decide in 2011 whether to move forward with the convergence to IFRS with the transition beginning in 2014. Should the SEC make such a decision, the Company will convert its reporting to IFRS at such time.

2 – Accounting changes

Accounting standard updates effective in 2010 that were issued by the Financial Accounting Standards Board (FASB) had no significant impact on the Company's consolidated financial statements.

2009

Business Combinations

On January 1, 2009, the Company adopted the new requirements of the FASB Accounting Standards Codification (ASC) 805, "Business Combinations," relating to the accounting for business combinations (previously Statement of Financial Accounting Standards (SFAS) No. 141 (R)), which became effective for acquisitions with an acquisition date on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. Until December 31, 2008, the Company was subject to the requirements of SFAS No. 141, "Business Combinations," which required that acquisition-related costs be included as part of the purchase cost of an acquired business. As such, the Company had reported acquisition-related costs in Other current assets pending the closing of its acquisition of the Elgin, Joliet and Eastern Railway Company (EJ&E), which had been subject to an extensive U.S. Surface Transportation Board (STB) approval process. On January 31, 2009, the Company completed its acquisition of the EJ&E and accounted for the acquisition under the revised standard. The Company incurred acquisition-related costs, including costs to obtain regulatory approval of approximately \$49 million, which were expensed and reported in Casualty and other in the Consolidated Statement of Income for the year ended December 31, 2009 pursuant to FASB ASC 805 requirements. At the time of adoption, this change in accounting policy had the effect of decreasing net income by \$28 million (\$0.06 per basic or diluted earnings per share) and Other current assets by \$46 million. This change had no effect on the Consolidated Statement of Cash Flows. Disclosures prescribed by FASB ASC 805 are presented in Note 3 – Acquisitions.

3 – Acquisitions

2009

On January 31, 2009, the Company acquired the principal rail lines of the EJ&E, a short-line railway that operated over 198 miles of track in and around Chicago, for a total cash consideration of US\$300 million (C\$373 million), paid with cash on hand. The Company accounted for the acquisition using the acquisition method of accounting pursuant to FASB ASC 805, "Business Combinations," which the Company adopted on January 1, 2009. As such, the consolidated financial statements of the Company include the assets, liabilities and results of operations of EJ&E as of January 31, 2009, the date of acquisition. The costs incurred to acquire the EJ&E of approximately \$49 million were expensed and reported in Casualty and other in the Consolidated Statement of Income for the year ended December 31, 2009 (see Note 2 – Accounting changes).

Notes to Consolidated Financial Statements

U.S. GAAP

The following table summarizes the consideration paid for EJ&E and the fair value of the assets acquired and liabilities assumed that were recognized at the acquisition date:

In US millions	At January 31, 2009
Consideration	
Cash	\$ 300
Fair value of total consideration transferred	\$ 300
Recognized amounts of identifiable assets acquired and liabilities assumed	
Current assets	\$ 4
Properties	310
Current liabilities	(4)
Other noncurrent liabilities	(10)
Total identifiable net assets	\$ 300

The 2009 revenues and net income of EJ&E included in the Company's Consolidated Statement of Income from the acquisition date to December 31, 2009, were \$74 million and \$12 million, respectively.

2008

The Company acquired the three principal railway subsidiaries of the Quebec Railway Corp. (QRC) and a QRC rail-freight ferry operation for a total acquisition cost of \$50 million, paid with cash on hand. The acquisition included:

- (i) Chemin de fer de la Matapedia et du Golfe, a 221-mile short-line railway;
- (ii) New Brunswick East Coast Railway, a 196-mile short-line railway;
- (iii) Ottawa Central Railway, a 123-mile short-line railway; and
- (iv) Compagnie de gestion de Matane Inc., a rail ferry which provides shuttle boat-rail freight service.

This acquisition was accounted for using the purchase method of accounting pursuant to SFAS No. 141, "Business Combinations." As such, the Company's consolidated financial statements include the assets, liabilities and results of operations of the acquired entities from the date of acquisition.

4 – Accounts receivable

In millions	December 31,	2010	2009
Freight	\$	585	\$ 567
Non-freight		211	264
Gross accounts receivable		796	831
Allowance for doubtful accounts		(21)	(34)
Net accounts receivable	\$	775	\$ 797

The Company has a five-year agreement, expiring in May 2011, to sell an undivided co-ownership interest in a revolving pool of freight receivables to an unrelated trust for maximum cash proceeds of \$600 million. Since the fourth quarter of 2009, the Company has gradually reduced the program limit, which will stand at \$100 million until

the expiry of the program, to reflect the anticipated reduction in the use of the program. The trust is a multi-seller trust and the Company is not the primary beneficiary. The trust was established in Ontario, Canada by a Canadian bank to acquire receivables and interests in other financial assets from a variety of originators. Funding for the acquisition of these assets is customarily through the issuance of asset-backed commercial paper notes. The notes are secured by, and recourse is limited to, the assets purchased using the proceeds of the notes.

Pursuant to the agreement, the Company sells an interest in its receivables and receives proceeds net of the required reserve as stipulated in the agreement. The required reserve represents an amount set aside to allow for possible credit losses and is recognized by the Company as a retained interest and recorded in Other current assets in its Consolidated Balance Sheet.

The Company retains the responsibility for servicing, administering and collecting the receivables sold and receives no fee for such ongoing servicing responsibilities. The average servicing period is approximately one month. During 2010, there were no proceeds from collections reinvested in the securitization program as there was no activity under the program. During 2009, \$151 million of proceeds from collections was reinvested in the securitization program and \$4 million of previously transferred accounts receivable was purchased. Subject to customary indemnifications, the trust's recourse is generally limited to the receivables.

As at December 31, 2010, the Company had no receivables sold under this program. As at December 31, 2009, the Company had sold receivables that resulted in proceeds of \$2 million and recorded retained interest of approximately 10% in Other current assets.

Other income included nil in 2010, \$1 million in 2009 and \$10 million in 2008, for costs related to the agreement, which fluctuate with changes in prevailing interest rates (see Note 13 – Other income). These costs include interest, program fees and fees for unused committed availability.

5 – Properties