

# FORM 10-Q

## UNITED STATES SECURITIES AND EXCHANGE COMMISSION WASHINGTON, D.C. 20549

(Mark One)

☒ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2003

- OR -

☐ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number 1-6146

### UNION PACIFIC RAILROAD COMPANY

(Exact name of registrant as specified in its charter)

DELAWARE  
(State or other jurisdiction of  
incorporation or organization)

94-6001323  
(I.R.S. Employer  
Identification No.)

1416 DODGE STREET, OMAHA, NEBRASKA  
(Address of principal executive offices)

68179  
(Zip Code)

(402) 271-5000  
(Registrant's telephone number, including area code)

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

YES ☒ NO ☐

Indicate by check mark whether the Registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act).

YES ☐ NO ☒

As of October 31, 2003, the Registrant had outstanding 7,130 shares of Common Stock, \$10 par value, and 620 shares of Class A Stock, \$10 par value.

THE REGISTRANT MEETS THE CONDITIONS SET FORTH IN GENERAL INSTRUCTIONS H(1)(a) AND (b) OF FORM 10-Q AND IS THEREFORE FILING THIS FORM WITH THE REDUCED DISCLOSURE FORMAT.

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## **PART I. FINANCIAL INFORMATION**

### **Item 1. Consolidated Financial Statements**

#### **Consolidated Statements of Income (Unaudited)**

*Union Pacific Railroad Company and Consolidated Subsidiary and Affiliate Companies*

<i>Millions of Dollars, For the Three Months Ended September 30,</i>	<i>2003</i>	<i>2002</i>
Revenues .....	\$2,946	\$2,838
Operating expenses:		
Salaries, wages and employee benefits.....	958	899
Equipment and other rents .....	308	315
Depreciation.....	267	286
Fuel and utilities .....	330	277
Materials and supplies.....	103	117
Casualty costs.....	107	88
Purchased services and other costs.....	279	218
Total operating expenses.....	2,352	2,200
Operating income.....	594	638
Other income .....	29	160
Interest expense .....	(124)	(136)
Income before income taxes .....	499	662
Income taxes .....	(182)	(248)
Net income.....	\$ 317	\$ 414

*The accompanying notes are an integral part of these Consolidated Financial Statements.*

**Consolidated Statements of Income (Unaudited)***Union Pacific Railroad Company and Consolidated Subsidiary and Affiliate Companies*

<i>Millions of Dollars, For the Nine Months Ended September 30,</i>	<i>2003</i>	<i>2002</i>
Revenues .....	\$8,552	\$8,295
Operating expenses:		
Salaries, wages and employee benefits.....	2,831	2,683
Equipment and other rents .....	914	936
Depreciation.....	792	851
Fuel and utilities .....	1,005	770
Materials and supplies.....	304	358
Casualty costs.....	311	269
Purchased services and other costs.....	848	684
Total operating expenses.....	7,005	6,551
Operating income.....	1,547	1,744
Other income .....	61	216
Interest expense .....	(374)	(412)
Income before income taxes .....	1,234	1,548
Income taxes .....	(455)	(575)
Income before cumulative effect of accounting change.....	779	973
Cumulative effect of accounting change, net of tax.....	274	-
Net income.....	\$ 1,053	\$ 973

*The accompanying notes are an integral part of these Consolidated Financial Statements.*

**Consolidated Statements of Financial Position (Unaudited)***Union Pacific Railroad Company and Consolidated Subsidiary and Affiliate Companies*

<i>Millions of Dollars</i>	<i>Sept. 30, 2003</i>	<i>Dec. 31, 2002</i>
<b>Assets</b>		
Current Assets		
Cash and temporary investments .....	\$ 65	\$ 110
Accounts receivable, net.....	523	529
Inventories .....	269	277
Current deferred income taxes .....	281	281
Other current assets.....	233	189
Total current assets.....	1,371	1,386
Investments:		
Investments in and advances to affiliated companies .....	681	649
Other investments .....	40	49
Total investments .....	721	698
Properties:		
Cost .....	37,994	36,821
Accumulated depreciation .....	(7,892)	(7,841)
Net properties.....	30,102	28,980
Other assets.....	296	250
Total assets.....	\$32,490	\$31,314
<b>Liabilities and Common Shareholders' Equity</b>		
Current Liabilities:		
Accounts payable.....	\$ 517	\$ 416
Accrued wages and vacation .....	384	362
Accrued casualty costs.....	389	403
Income and other taxes.....	339	226
Debt due within one year.....	162	275
Interest .....	56	71
Other current liabilities.....	485	537
Total current liabilities.....	2,332	2,290
Intercompany borrowing from UPC .....	4,410	4,464
Third-party debt due after one year .....	2,044	1,984
Deferred income taxes .....	9,208	8,823
Accrued casualty costs.....	619	658
Retiree benefits obligation .....	807	888
Other long-term liabilities .....	328	333
Redeemable Preference Shares .....	17	18
Commitments and contingencies		
Common shareholders' equity .....	12,725	11,856
Total liabilities and common shareholders' equity .....	\$32,490	\$31,314

*The accompanying notes are an integral part of these Consolidated Financial Statements.*

**Consolidated Statements of Cash Flows (Unaudited)**

Union Pacific Railroad Company and Consolidated Subsidiary and Affiliate Companies

<i>Millions of Dollars, For the Nine Months Ended September 30,</i>	<i>2003</i>	<i>2002</i>
<b>Operating Activities</b>		
Net income .....	\$1,053	\$ 973
Adjustments to reconcile net income to net cash provided by operating activities:		
Cumulative effect of accounting change.....	(274)	-
Depreciation .....	792	851
Deferred income taxes .....	224	350
Cash paid to fund pension plan.....	(50)	-
Other, net.....	(346)	(260)
Changes in current assets and liabilities, net .....	125	(173)
Cash provided by operating activities .....	1,524	1,741
<b>Investing Activities</b>		
Capital investments.....	(1,299)	(1,298)
Proceeds from asset sales .....	85	291
Other investing activities, net.....	112	(49)
Cash used in investing activities .....	(1,102)	(1,056)
<b>Financing Activities</b>		
Dividends paid to parent .....	(174)	(150)
Debt repaid .....	(240)	(159)
Advances to affiliated companies .....	(55)	(401)
Financings, net .....	2	-
Cash used in financing activities .....	(467)	(710)
Net change in cash and temporary investments.....	(45)	(25)
Cash and temporary investments at beginning of period.....	110	87
Cash and temporary investments at end of period .....	\$ 65	\$ 62
<b>Changes in Current Assets and Liabilities, Net</b>		
Accounts receivable, net .....	\$ 6	\$(138)
Inventories.....	8	-
Other current assets .....	(44)	(57)
Accounts, wages and vacation payable.....	123	43
Other current liabilities.....	32	(21)
Total.....	\$ 125	\$(173)
Supplemental cash flow information:		
Non-cash locomotive lease financings.....	\$ 188	\$ 126
Cash paid during the period for:		
Interest .....	390	436
Income taxes, net.....	126	200

The accompanying notes are an integral part of these Consolidated Financial Statements.

# **Consolidated Statement of Changes in Common Shareholders' Equity (Unaudited)**

*Union Pacific Railroad Company and Consolidated Subsidiary and Affiliate Companies*

<i>Millions of Dollars, For the Nine Months Ended September 30, 2003</i>	<i>[a] Common Shares</i>	<i>[b] Class A Shares</i>	<i>Paid- in- Surplus</i>	<i>Retained Earnings</i>	<i>Accumulated Other Comprehensive Income (Loss)</i>				
					<i>Minimum Pension Liability Adjustments</i>	<i>Foreign Currency Translation Adjustments</i>	<i>Derivative Adjustments</i>	<i>Total</i>	<i>Total</i>
Balance at January 1, 2003 .....	\$ -	\$ -	\$4,782	\$7,224	\$(148)	\$ (9)	\$7	\$(150)	\$11,856
Net income.....	-	-	-	1,053	-	-	-	-	1,053
Other comprehensive loss, net of tax[c] .....	-	-	-	-	-	(7)	(3)	(10)	(10)
Comprehensive income .....	-	-	-	(174)	-	-	-	-	1,043
Dividends declared .....	-	-	-	(174)	-	-	-	-	(174)
Balance at September 30, 2003...	\$ -	\$ -	\$4,782	\$8,103	\$(148)	\$(16)	\$4	\$(160)	\$12,725

[a] Common Stock, \$10.00 par value; 9,200 shares authorized; 4,465 outstanding.

[b] Class A Stock, \$10.00 par value; 800 shares authorized; 388 outstanding.

[c] Other comprehensive loss, net of tax of \$6 million.

*The accompanying notes are an integral part of these Consolidated Financial Statements.*

**UNION PACIFIC RAILROAD COMPANY AND CONSOLIDATED SUBSIDIARY AND AFFILIATE  
COMPANIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

(Unaudited)

**1. Responsibilities for Financial Statements** - Union Pacific Railroad Company (the Registrant), a Class I railroad incorporated in Delaware and an indirect wholly owned subsidiary of Union Pacific Corporation (the Corporation or UPC), together with a number of wholly owned and majority owned subsidiaries, certain affiliates and various minority-owned companies (collectively, UPRR, the Company or the Railroad), operates various railroad and railroad-related businesses. The Consolidated Financial Statements of the Company are unaudited and reflect all adjustments (consisting only of normal and recurring adjustments) that are, in the opinion of management, necessary for a fair presentation of the financial position and operating results for the interim periods presented. The Consolidated Statement of Financial Position at December 31, 2002 is derived from audited financial statements. The Consolidated Financial Statements should be read in conjunction with the Consolidated Financial Statements and notes thereto contained in the Company's Annual Report on Form 10-K for the year ended December 31, 2002. The results of operations for the three months and nine months ended September 30, 2003 are not necessarily indicative of the results for the entire year ending December 31, 2003. Certain prior year amounts have been reclassified to conform to the 2003 financial statement presentation.

**2. Stock-Based Compensation** – The Company participates in the Corporation's stock incentive plans. At September 30, 2003, the Corporation had several stock-based employee compensation plans. The Railroad accounts for those plans under the recognition and measurement principles of APB Opinion No. 25, "Accounting for Stock Issued to Employees", and related Interpretations. No stock option expense is reflected in net income as all options granted under those plans had an exercise price equal to the market value of the Union Pacific Corporation common stock on the date of grant. Stock-based employee compensation expense related to restricted stock and other incentive plans is reflected in net income. The following table illustrates the effect on net income if the Company had applied the fair value recognition provisions of FASB Statement No. 123, "Accounting for Stock-Based Compensation", to stock-based employee compensation.

<i>Millions of Dollars</i>	<i>Three Months Ended September 30,</i>		<i>Nine Months Ended September 30,</i>	
	<i>2003</i>	<i>2002</i>	<i>2003</i>	<i>2002</i>
Net income, as reported.....	\$317	\$414	\$1,053	\$973
Stock-based employee compensation expense included in reported net income, net of tax.....	1	2	8	6
Total stock-based employee compensation expense determined under fair value based method for all awards, net of tax.....	(4)	(5)	(18)	(16)
Pro forma net income .....	\$314	\$411	\$1,043	\$963

The fair value of each option grant was estimated on the date of grant using the Black-Scholes option-pricing model. The following were the weighted-average assumptions for options granted during both the three months and nine months ended September 30, 2003: risk-free interest rate of 2.9%; dividend yield of 1.5%; expected lives of 5 years; and volatility of 28.4%. Assumptions for both the three months and nine months ended September 30, 2002 were: risk-free interest rate of 4.4%; dividend yield of 1.3%; expected lives of 5 years; and volatility of 28.8%.

**3. Intercompany Relationship with UPC** - At September 30, 2003 and December 31, 2002, the Railroad had \$961 million and \$904 million working capital deficit balances, respectively, relating to UPC's management of its cash position. As part of UPC's cash management activities, the Railroad advances excess cash (cash available after satisfying all of the Railroad's obligations and paying dividends to UPC) to UPC. Dividends declared and paid to UPC by the Railroad typically approximate the dividends that UPC declares to its shareholders; however, there is no formal requirement to do so. The dividend declaration between the Railroad and UPC is determined solely by the Railroad's Board of Directors. To the extent the Railroad requires additional cash for use in its operations, UPC makes such funds available for borrowing by the Railroad. Transactions between UPC and UPRR are treated as net intercompany borrowings in the Consolidated Statements of Financial Position.



The majority of the Railroad's intercompany borrowings from UPC relate to the acquisitions of the Chicago and North Western Transportation Company and Southern Pacific Rail Corporation which were funded by UPC on behalf of the Railroad. These acquisition costs were assumed by the Railroad in the form of intercompany borrowings from UPC. The intercompany borrowings accrue interest at an annual rate of 7.5%, which may be adjusted from time to time, and are payable on demand. There are no restrictions on the amount the Railroad is able to borrow from UPC. Intercompany borrowings are unsecured and rank equally with all of the Railroad's other unsecured indebtedness.

UPC provides the Company with various services, including strategic planning, legal, treasury, accounting, auditing, insurance, human resources and corporate affairs. In 2003, pursuant to a services agreement, UPC will continue to provide services to the Company, and the Company will pay UPC its share of the costs as determined by an independent review. Billings for these services were \$13 million and \$40 million for the three months and nine months ended September 30, 2003.

#### **4. Financial Instruments**

**Strategy and Risk** - The Company and its subsidiaries use derivative financial instruments in limited instances for other than trading purposes to manage risk related to changes in fuel prices. The Company uses swaps, collars, futures and/or forward contracts to mitigate the downside risk of adverse price movements and hedge the exposure to variable cash flows. The use of these instruments also limits future benefits from favorable movements. The purpose of these programs is to protect the Company's operating margins and overall profitability from adverse fuel price changes.

**Market and Credit Risk** - The Company addresses market risk related to derivative financial instruments by selecting instruments with value fluctuations that highly correlate with the underlying item being hedged. Credit risk related to derivative financial instruments, which is minimal, is managed by requiring high credit standards for counterparties and periodic settlements. At September 30, 2003, the Company has not been required to provide collateral, nor has the Company received collateral relating to its hedging activity.

**Determination of Fair Value** - The fair values of the Company's derivative financial instrument positions at September 30, 2003 and December 31, 2002, detailed below, were determined based upon current fair values as quoted by recognized dealers or developed based upon the present value of expected future cash flows discounted at the applicable swap spread.

**Fuel Strategy** - Fuel costs are a significant portion of the Company's total operating expenses. As a result of the significance of fuel costs and the historical volatility of fuel prices, the Company uses swaps, collars, futures and/or forward contracts to mitigate the impact of adverse fuel price changes.

The following is a summary of the Company's derivative financial instruments at September 30, 2003 and December 31, 2002:

<i>Millions, Except Average Commodity Prices</i>	<i>Sept. 30, 2003</i>	<i>Dec. 31, 2002</i>
Fuel hedging		
Swaps and swaptions:		
Number of gallons hedged for 2002 [a] .....	-	552
Average price of 2002 hedges (per gallon) [b] .....	\$ -	\$0.56
Number of gallons hedged for the remainder of 2003 [c] .....	79	88
Average price of 2003 hedges outstanding (per gallon) [b] .....	\$0.66	\$0.58
Collars:		
Number of gallons hedged for the remainder of 2003 .....	22	-
Average cap price for 2003 collars outstanding .....	\$0.77	\$ -
Average floor price for 2003 collars outstanding .....	\$0.67	\$ -
Average ceiling price for 2003 collars outstanding .....	\$0.88	\$ -
Number of gallons hedged for 2004 .....	28	-
Average cap price for 2004 collars outstanding .....	\$0.78	\$ -
Average floor price for 2004 collars outstanding .....	\$0.67	\$ -
Average ceiling price for 2004 collars outstanding .....	\$0.88	\$ -

[a] Fuel hedges expired December 31, 2002. Fuel hedges included the swap portion of a swaption with a base term expiring December 31, 2002.

[b] Excluding taxes, transportation costs and regional pricing spreads.

[c] Fuel hedges which are in effect during 2003. These hedges expire December 31, 2003.

The fair value asset positions of the Company's outstanding derivative financial instruments at September 30, 2003 and December 31, 2002 were as follows:

<i>Millions of Dollars</i>	<i>Sept. 30, 2003</i>	<i>Dec. 31, 2002</i>
Fuel hedging:		
Gross fair value asset position .....	\$9	\$12
Gross fair value (liability) position .....	-	-
Total fair value asset position .....	\$9	\$12

Fuel hedging positions will be reclassified from accumulated other comprehensive income to fuel expense over the life of the hedge as fuel is consumed.

The Company's use of derivative financial instruments had the following impact on pre-tax income for the three months and nine months ended September 30, 2003 and 2002:

<i>Millions of Dollars</i>	<i>Three Months Ended September 30,</i>		<i>Nine Months Ended September 30,</i>	
	<i>2003</i>	<i>2002</i>	<i>2003</i>	<i>2002</i>
Decrease in fuel expense from hedging .....	\$4	\$15	\$15	\$15
Decrease in fuel expense from swaptions .....	-	4	-	17
Decrease in operating expenses .....	4	19	15	32
Increase in other income from swaptions .....	-	1	-	4
Increase in pre-tax income .....	\$4	\$20	\$15	\$36

Through September 30, 2003, the Company had recorded less than \$1 million for fuel hedging ineffectiveness.

**Sale of Receivables** - The Railroad has sold, on a 364-day revolving basis, an undivided percentage ownership interest in a designated pool of accounts receivable to third parties through a bankruptcy-remote subsidiary. Receivables are sold at carrying value, which approximates fair value. The third parties have designated the Railroad to service the sold receivables. The amount of receivables sold fluctuates based upon the availability of the designated pool of receivables and is directly affected by changing business volumes and credit risks. Payments

collected from sold receivables can be reinvested in new receivables on behalf of the buyers. Should the Corporation's credit rating fall below investment grade, the amount of receivables sold would be reduced, and in certain cases, the buyers have the right to discontinue this reinvestment, thus requiring the Railroad to fund the receivables. At September 30, 2003 and December 31, 2002, accounts receivable are presented net of \$590 million and \$600 million of receivables sold, respectively. On August 7, 2003, the sale of receivables program was renewed for one year without any significant term changes.

**5. Capital Stock** – The number of shares shown in the Common Stock section of the Consolidated Statement of Changes in Common Shareholders' Equity excludes 2,665 shares of Common Stock and 232 shares of Class A Stock owned by Southern Pacific, an affiliate of the Registrant, whose results are included in the Company's Consolidated Financial Statements.

**6. Other Income** - Other income included the following for the three months and nine months ended September 30, 2003 and 2002:

<i>Millions of Dollars</i>	<i>Three Months Ended Sept. 30,</i>		<i>Nine Months Ended Sept. 30,</i>	
	<i>2003</i>	<i>2002</i>	<i>2003</i>	<i>2002</i>
Net gain on non-operating asset dispositions.....	\$22	\$155	\$46	\$196
Rental income .....	13	12	38	38
Interest income .....	1	1	3	5
Other, net .....	(7)	(8)	(26)	(23)
Total.....	\$29	\$160	\$61	\$216

## **7. Commitments and Contingencies**

**Unasserted Claims** - There are various claims and lawsuits pending against the Company and certain of its subsidiaries, in addition to unasserted claims. It is not possible at this time for the Company to determine fully the effect of all such claims on its consolidated financial condition, results of operations or liquidity; however, to the extent possible, where unasserted claims can be reasonably estimated and where such claims are considered probable, the Company has recorded a liability. The Company does not expect that any known lawsuits or claims, including unasserted claims, will have a material adverse effect on its consolidated financial condition, results of operations or liquidity.

**Personal Injury and Occupational Illness** - The cost of injuries to employees and others related to Railroad activities is charged to expense based on actuarial estimates of the ultimate cost and number of incidents each year. The three month and nine month expenses for the Company's personal injury-related events were \$66 million and \$187 million in 2003 and \$58 million and \$174 million in 2002, respectively. As of September 30, 2003, the Company had a liability of \$630 million accrued for personal injury costs, of which \$272 million was recorded as a current liability. The Railroad has additional amounts accrued for claims related to certain occupational illnesses. Compensation for Railroad work-related accidents is governed by the Federal Employers' Liability Act (FELA). Under FELA, damages are assessed based on a finding of fault through litigation or out-of-court settlements. The Railroad offers a comprehensive variety of services and rehabilitation programs for employees who are injured at work.

**Environmental** - The Company generates and transports hazardous and nonhazardous waste in its current operations and has done so in its former operations, and it is subject to federal, state and local environmental laws and regulations. The Company has identified approximately 417 sites at which it is or may be liable for remediation costs associated with alleged contamination or for violations of environmental requirements. This includes 57 sites that are the subject of actions taken by the U.S. government, 32 of which are currently on the Superfund National Priorities List. Certain federal legislation imposes joint and several liability for the remediation of identified sites; consequently, the Company's ultimate environmental liability may include costs relating to other parties, in addition to costs relating to its own activities at each site.

When an environmental issue has been identified with respect to the property owned, leased or otherwise used in the conduct of the Company's business, the Company and its external consultants perform environmental assessments on such property. The Company expenses the cost of the assessments as incurred. The Company accrues the cost of remediation where its obligation is probable and such costs can be reasonably estimated.

As of September 30, 2003, the Company had a liability of \$195 million accrued for future environmental costs, of which \$59 million was recorded in current liabilities as accrued casualty costs. The liability includes future costs for remediation and restoration of sites, as well as for ongoing monitoring costs, but excludes any anticipated recoveries from third parties. Cost estimates are based on information available for each site, financial viability of other potentially responsible parties and existing technology, laws and regulations. The Company believes that it has adequately accrued for its ultimate share of costs at sites subject to joint and several liability. However, the ultimate liability for remediation is difficult to determine because of the number of potentially responsible parties involved, site-specific cost sharing arrangements with other potentially responsible parties, the degree of contamination by various wastes, the scarcity and quality of volumetric data related to many of the sites and/or the speculative nature of remediation costs. The Company expects to pay out the majority of the September 30, 2003 environmental liability over the next five years, funded by cash generated from operations. The impact of current obligations is not expected to have a material adverse effect on the results of operations, financial condition or liquidity of the Company.

**Other Matters** - The Company periodically enters into financial and other commitments in connection with its businesses. It is not possible at this time for the Company to determine fully the effect of all unasserted claims on its consolidated financial condition, results of operations or liquidity; however, to the extent possible, where unasserted claims can be reasonably estimated and where such claims are considered probable, the Company has recorded a liability. The Company does not expect that any known lawsuits, claims, environmental costs, commitments, contingent liabilities or guarantees will have a material adverse effect on its consolidated financial condition, results of operations or liquidity.

At September 30, 2003, the Company had unconditional purchase obligations of \$180 million for the acquisition of locomotives as part of the Company's multi-year capital asset acquisition plan. In addition, the Company was contingently liable for \$343 million in guarantees and \$28 million in letters of credit at September 30, 2003. These contingent guarantees were entered into in the normal course of business and include guaranteed obligations of affiliated operations. The Company is not aware of any existing event of default, which would require it to satisfy these guarantees.

As described in note 10 to the Consolidated Financial Statements, Item 8, in the Annual Report on Form 10-K, the Railroad has a synthetic operating lease arrangement to finance a new headquarters building. The Railroad has guaranteed a residual value equal to 85% of the total construction related costs upon completion of the building. During construction, the Railroad guarantees 89.9% of the construction costs incurred. At September 30, 2003, the Railroad's guarantee related to the building was \$92 million. The guarantee will be approximately \$220 million upon completion of the building. At September 30, 2003, the Railroad had a liability recorded of approximately \$7 million related to the fair value of this guarantee.

During May 2003, UPRR entered into a capital lease covering new locomotives. The related capital lease obligation totaled approximately \$188 million and is included in the Consolidated Statements of Financial Position as debt.

**8. Accounting Pronouncements** - In January 2003, the FASB issued Interpretation No. 46, "Consolidation of Variable Interest Entities" (FIN 46). FIN 46 requires a variable interest entity to be consolidated by a company if that company is subject to a majority of the risk of loss from the variable interest entity's activities or entitled to receive a majority of the entity's residual returns or both. FIN 46 also requires disclosures about variable interest entities that a company is not required to consolidate but in which it has a significant variable interest. The consolidation requirements of FIN 46 apply immediately to variable interest entities created after January 31, 2003. As described in note 10 to the Consolidated Financial Statements, Item 8, in the Annual Report on Form 10-K, the Railroad has a synthetic operating lease arrangement to finance a new headquarters building, which falls within the guidance of FIN 46. In June 2003, the Railroad restructured the synthetic lease resulting in no effect to the Consolidated Financial Statements due to the adoption of FIN 46.

In October 2003, the FASB issued FASB Staff Position Number FIN 46-6 (FSP 46-6) which provides public entities an opportunity to delay implementation of FIN 46, for agreements entered into prior to February 1, 2003, until periods ending after December 15, 2003. FSP 46-6 does not impact the Company, as the Company has already adopted FIN 46.

**9. Cumulative Effect of Accounting Change** - Surface Transportation Board (STB) accounting rules require that railroads accrue the cost of removing track structure over the expected useful life of these assets. Railroads historically used this prescribed accounting for reports filed with both the STB and SEC. In August 2001, the FASB issued Statement No. 143, "Accounting for Asset Retirement Obligations" (FAS 143). This statement was effective

for the Company beginning January 1, 2003, and prohibits the accrual of removal costs unless there is a legal obligation to remove the track structure at the end of its life. The Company concluded that it did not have a legal obligation to remove the track structure, and therefore, under generally accepted accounting principles, the Company could not accrue the cost of removal in advance. Reports filed with the SEC will reflect the expense of removing these assets in the period in which they are removed. For STB reporting requirements only, the Company will continue to follow the historical method of accruing in advance, as prescribed by the STB. FAS 143 also requires the Company to record a liability for legally obligated asset retirement costs associated with tangible long-lived assets. In the first quarter of 2003, the Company recorded income from a cumulative effect of accounting change, related to the adoption of FAS 143, of \$274 million, net of tax of \$167 million. The accounting change had no effect on the Company's liquidity. Had the change been retroactively applied, the change would have had an immaterial impact on net income.

## **Item 2. Management's Narrative Analysis of the Results of Operations**

### **UNION PACIFIC RAILROAD COMPANY AND CONSOLIDATED SUBSIDIARY AND AFFILIATE COMPANIES RESULTS OF OPERATIONS**

#### **Three Months and Nine Months Ended September 30, 2003 Compared to Three Months and Nine Months Ended September 30, 2002**

Union Pacific Railroad Company (the Registrant), a Class I railroad incorporated in Delaware and an indirect wholly owned subsidiary of Union Pacific Corporation (the Corporation or UPC), together with a number of wholly owned and majority owned subsidiaries, certain affiliates and various minority-owned companies (collectively, UPRR, the Company or Railroad), operates various railroad and railroad-related businesses.

A copy of this Quarterly Report on Form 10-Q, as well as certain other filings made by the Company, including the Company's 2002 Annual Report on Form 10-K, current reports on Form 8-K and any amendments to such reports are available free of charge on the Internet at Union Pacific Corporation's website at [www.up.com/investors](http://www.up.com/investors). Additionally, the Corporation's corporate governance materials, including Board Committee charters, governance guidelines and policies and codes of conduct and ethics for directors, officers and employees may also be found on the Internet at the Corporation's website at [www.up.com/investors](http://www.up.com/investors).

#### **Critical Accounting Policies and Estimates**

The Company's discussion and analysis of its financial condition and results of operations are based upon its Consolidated Financial Statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires estimation and judgment that affect the reported amounts of revenues, expenses, assets and liabilities. The Company bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. If these estimates differ materially from actual results, the impact on the Consolidated Financial Statements may be material. The Company's critical accounting policies are available in the Company's 2002 Annual Report on Form 10-K, Item 7.

**Net Income** – The Company reported net income of \$317 million in the third quarter of 2003 compared to net income of \$414 million in 2002, a decrease of \$97 million (23%). Year-to-date net income was \$1.1 billion. Year-to-date income before the cumulative effect of accounting change decreased \$194 million (20%) to \$779 million, compared to 2002 net income of \$973 million. The decrease in both periods resulted primarily from higher fuel prices, inflation, volume-related expenses and lower gains from real estate sales. The third quarter decrease in net income was partially offset by 4% operating revenue growth, lower depreciation expense, lower interest expense and cost control efforts. The decrease year-to-date was partially offset by 3% operating revenue growth, lower depreciation expense, lower interest expense and cost control efforts.

**Operating Revenues** – Operating revenue is comprised of rail commodity revenue and other revenues. Other revenues primarily include subsidiary revenue from various companies that are wholly owned or majority owned by the Railroad, revenue from the Chicago commuter rail operations and accessorial revenue earned due to customer detainment of Railroad owned or controlled equipment. Operating revenues increased \$108 million (4%) to \$2.9 billion in the third quarter and \$257 million (3%) to \$8.6 billion in the nine-month period compared to 2002. Commodity revenue increased \$101 million (4%) in the third quarter to \$2.8 billion, led by growth in the Agricultural Products, Energy and Industrial Products commodity groups. Third quarter revenue carloads were essentially flat compared to a year ago. Average revenue per car for the period increased 3% to \$1,195 driven by positive mix, fuel surcharges, pricing gains and index-based contract escalators. Year-to-date rail commodity revenue grew 3% to \$8.2 billion compared to 2002. Revenue carloads were flat and average revenue per car showed a 3% increase to \$1,192 when compared to a year ago. Other revenues increased \$7 million (6%) to \$119 million in the third quarter compared to a year ago and increased \$31 million (10%) year-to-date when compared to 2002 as a result of higher subsidiary revenue and accessorial revenue.

The following tables summarize the year-over-year changes in rail commodity revenue, revenue carloads and average revenue per car by commodity type:

<i>Three Months Ended</i> <i>September 30,</i>			<i>%</i> <i>Change</i>	<i>Commodity Revenue</i> <i>Millions of Dollars</i>	<i>Nine Months Ended</i> <i>September 30,</i>		
<i>2003</i>	<i>2002</i>				<i>2003</i>	<i>2002</i>	<i>%</i> <i>Change</i>
\$ 411	\$ 373	10%		Agricultural .....	\$1,158	\$1,096	6%
276	285	(3)		Automotive .....	898	893	1
400	399	-		Chemicals .....	1,187	1,186	-
628	591	6		Energy .....	1,791	1,743	3
572	535	7		Industrial Products .....	1,643	1,542	6
540	543	-		Intermodal .....	1,521	1,512	1
\$2,827	\$2,726	4%		Total .....	\$8,198	\$7,972	3%

  

<i>Three Months Ended</i> <i>September 30,</i>			<i>%</i> <i>Change</i>	<i>Revenue Carloads</i> <i>Thousands</i>	<i>Nine Months Ended</i> <i>September 30,</i>		
<i>2003</i>	<i>2002</i>				<i>2003</i>	<i>2002</i>	<i>%</i> <i>Change</i>
225	215	5%		Agricultural .....	645	642	-
189	193	(2)		Automotive .....	610	605	1
225	231	(3)		Chemicals .....	670	681	(2)
563	540	4		Energy .....	1,621	1,605	1
390	379	3		Industrial Products .....	1,112	1,077	3
775	801	(3)		Intermodal .....	2,220	2,253	(1)
2,367	2,359	-		Total .....	6,878	6,863	-

  

<i>Three Months Ended</i> <i>September 30,</i>			<i>%</i> <i>Change</i>	<i>Average Revenue</i> <i>Per Car</i>	<i>Nine Months Ended</i> <i>September 30,</i>		
<i>2003</i>	<i>2002</i>				<i>2003</i>	<i>2002</i>	<i>%</i> <i>Change</i>
\$1,828	\$1,740	5%		Agricultural .....	\$1,796	\$1,708	5%
1,455	1,479	(2)		Automotive .....	1,471	1,476	-
1,780	1,729	3		Chemicals .....	1,773	1,742	2
1,116	1,095	2		Energy .....	1,105	1,086	2
1,467	1,410	4		Industrial Products .....	1,476	1,432	3
697	667	3		Intermodal .....	685	671	2
\$1,195	\$1,156	3%		Total .....	\$1,192	\$1,162	3%

*Agricultural* - Revenue increased 10% in the third quarter and 6% for the year-to-date period of 2003 over the comparable periods in 2002. Third quarter volume increased 5% while year-to-date volume was flat over last year. Average revenue per car increased 5% in both periods. Demand for domestic wheat and Gulf export wheat led the improvement over 2002. Ethanol shipments also increased due to heightened demand for the fuel additive. Average revenue per car increased due to price increases, the positive mix impact of longer average length of haul shipments and fuel surcharges.

*Automotive* - Revenue declined 3% for the third quarter but increased 1% for the year-to-date period of 2003 over the comparable periods in 2002. The third quarter revenues from domestic manufacturers decreased compared to the same period last year, as the softening economy weakened demand for finished vehicles and forced production cuts. The year-to-date revenue growth was the result of increased volume due to market share gains for materials shipments. Average revenue per car decreased 2% in the third quarter but was flat for the year-to-date period as price increases and fuel surcharges were offset by the mix impact of disproportionate growth in materials shipments, which move at a lower average revenue per car than finished vehicles.

*Chemicals* - Revenue was flat for both the third quarter and year-to-date period of 2003 over the comparable periods of 2002, as declining carloads in both periods were partially offset by an increase in average revenue per car. Reduced plastics volume led the decline in carloads in both periods, as the soft economy combined with higher input costs caused producers to lower inventories and reduce shipments. Increased market demand for domestic and export soda ash partially offset the decline. Average revenue per car increased 3% for the third quarter and 2% year-to-date,

due to a mix shift toward longer average length of haul, price increases, fewer cars in storage in transit and fuel surcharges.

*Energy* - Revenue increased 6% for the third quarter and 3% for the year-to-date period of 2003 over the comparable periods of 2002. First quarter volume was hampered by the absence of export traffic from the Colorado and Utah mining regions, which Japan is now sourcing from other Far Eastern producers. Severe weather in February and March also negatively impacted coal volumes. Strong utility demand due to lower inventories in the second and third quarter resulted in a 1% increase in year-to-date carloads. Average revenue per car increased 2% in both periods, due to index-based contract escalators and longer average length of haul.

*Industrial Products* - Revenue increased 7% for the third quarter and 6% for the year-to-date period of 2003 over the comparable periods of 2002, due to increases in carloads and average revenue per carload. The volume increase was led by lumber, as housing starts and low interest rates continued to drive business. Government shipments of military equipment and ammunition in support of the war effort also contributed to the increase. Steel and scrap shipments increased as the weakening dollar created higher domestic and export demand for U.S. produced steel, augmented by market share gains. Average revenue per car increased 4% in the third quarter and 3% year-to-date, primarily due to positive mix, fuel surcharges and price increases.

*Intermodal* - Revenue was flat for the third quarter and increased 1% for the year-to-date period of 2003 over the comparable periods of 2002, as a decline in carloads in the third quarter was more than offset by an increase in average revenue per car. Domestic carloads were up in both periods while international carloads decreased in the third quarter and year-to-date due to penetration losses, partially offset by strong first quarter market growth. Average revenue per car for the three and nine month periods increased due to fuel surcharges and price increases.

*Mexico Business* - Included in the rail commodity revenue reported above is Mexican related revenue, which increased 1% to \$218 million for the third quarter and was flat at \$650 million for the year-to-date period of 2003 over the comparable periods of 2002. Business growth was led by strong grain export movements and penetration gains from motor carriers in auto part shipments. Reduced steel and scrap along with finished vehicle imports partially offset the increase.

**Operating Expenses** – Operating expenses increased \$152 million (7%) to \$2.4 billion in the third quarter of 2003 and \$454 million (7%) year-to-date when compared to 2002. The increase in operating expenses is due primarily to higher fuel prices, in addition to wage and benefit inflation and volume-related costs as gross ton miles for the quarter and year-to-date periods increased 3% and 2% respectively. A reduction in employment levels, lower depreciation expense (see *Depreciation* discussion) and cost control efforts partially offset the increase. Cost control efforts are defined as focused actions to reduce discretionary spending and failure costs. Expenses in the third quarter were also negatively impacted by increased crew and asset utilization costs.

*Salaries, Wages and Employee Benefits* - Salaries, wages and employee benefits increased \$59 million (7%) in the third quarter of 2003 compared to 2002. Year-to-date, wage and benefit expenses rose \$148 million (6%). Increases were driven by the adoption of FAS 143 (see note 10 to the Consolidated Financial Statements), inflation, protection costs, increased crew utilization costs due to a shortage of available crews and increased pension expenses. A 3% and 2% reduction in employee force levels for the third quarter and year-to-date periods, respectively, as well as improvements in productivity partially offset the effects of inflation and protection costs for both periods. Protection cost represents the differential payment when the wage earned for active employment is lower than an employee's "protected" rate of pay. An individual's protected rate is imposed by the Surface Transportation Board for employees adversely affected by a merger or is established by collective bargaining agreements in other cases. The adoption of FAS 143 accounted for \$30 million and \$87 million of the increases for the third quarter and year-to-date, respectively.

*Equipment and Other Rents* - Equipment and other rents primarily includes rental expense UPRR pays for freight cars owned by other railroads or private companies; freight car, intermodal and locomotive leases; other specialty equipped vehicle leases; and office and other rentals. Expenses decreased \$7 million (2%) in the third quarter and \$22 million (2%) year-to-date compared to 2002. The third quarter decrease was due primarily to reduced rental prices for private freight cars, partially offset by increased car cycle times driven by higher inventory levels due to slower network train speed. Equipment and other rents decreased year-to-date due to lower rental prices for private cars and a reduction in lease expenses due to lower car cycle times and lower general car expenses in the first quarter of 2003, partially offset by higher locomotive lease expense. The higher locomotive lease expense is due to UPRR's increased leasing of new, more reliable and fuel efficient locomotives. These new locomotives replaced older, non-leased models in the fleet, which helped reduce expenses for depreciation, labor, materials and fuel during the period.



*Depreciation* - The majority of depreciation expense relates to track structure, including rail, ties and other track material. Depreciation expense decreased \$19 million (7%) in the third quarter and \$59 million (7%) year-to-date over 2002. The adoption of FAS 143 (see note 9 to the Consolidated Financial Statements) decreased depreciation expense in the third quarter by \$24 million and \$73 million year-to-date. Additionally, implementation of the recent depreciation study required and approved by the Surface Transportation Board resulted in lower depreciation expense of \$12 million and \$37 million for the third quarter and first nine months of 2003, respectively, due to a reduction in depreciation rates for certain track assets (effective January 1, 2003), offset by increased rates for locomotives and other assets (effective July 1, 2003). Capital spending in recent years has increased the total value of the Company's depreciable assets. Capital spending totaled \$1.3 billion in both nine month periods ended September 30, 2003 and 2002.

*Fuel and Utilities* - Fuel and utilities is comprised of locomotive fuel, utilities other than telephone, gasoline and other fuels. Expenses increased \$53 million (19%) in the third quarter and \$235 million (31%) year-to-date 2003 compared to a year ago. The increase was driven by higher fuel prices minimally offset by a lower fuel consumption rate, as measured by gallons consumed per thousand gross ton miles. Fuel prices averaged 90 cents per gallon in the third quarter of 2003 compared to 75 cents per gallon in the third quarter of 2002 (price includes taxes and transportation costs). Year-to-date, fuel prices averaged 93 cents per gallon compared to 70 cents per gallon in 2002. Higher fuel prices in 2003 resulted in a \$48 million increase in fuel expense in the third quarter and \$227 million increase year-to-date compared to 2002. The lower consumption rate decreased fuel expense by \$4 million in the third quarter and \$15 million year-to-date. A 3% increase in gross ton miles for the third quarter and a 2% increase year-to-date resulted in additional fuel expense of \$6 million and \$13 million, respectively. The Railroad hedged approximately 7% of its fuel consumption for the third quarter and year-to-date, which decreased fuel costs by \$4 million in the third quarter and \$15 million year-to-date. Gasoline, utilities and propane expenses increased \$3 million in the third quarter and \$10 million year-to-date primarily due to higher fuel prices.

*Materials and Supplies* - Materials used for the maintenance of the Railroad's lines, structures and equipment is the principal component of materials and supplies expense. Office, small tools and other supplies along with the costs of freight services purchased to ship company materials are also included. Expenses decreased \$14 million (12%) in the third quarter and \$54 million (15%) year-to-date, primarily due to the adoption of FAS 143 (see note 10 to the Consolidated Financial Statements), fewer locomotive and freight car repairs, reduced material freight charges, cost control measures and a shift to more contracting of locomotive repairs, which resulted in a corresponding increase to Purchased Services and Other Costs. The decreases were partially offset by increased costs for locomotive materials.

*Casualty Costs* - The largest component of casualty costs is personal injury expense. Freight and property damage, insurance, environmental matters and occupational illness expense are also included in casualty costs. Costs increased \$19 million (22%) in the third quarter compared to 2002 and \$42 million (16%) year-to-date due primarily to higher personal injury expense and insurance costs.

*Purchased Services and Other Costs* - Purchased services and other costs include the costs of services purchased from outside contractors, state and local taxes, net costs of operating facilities jointly used by UPRR and other railroads, transportation and lodging for train crew employees, trucking and contracting costs for intermodal containers, leased automobile maintenance expenses, telephone and cellular expense, employee travel expense and computer and other general expenses. Expenses increased \$61 million (28%) in the third quarter and \$164 million (24%) year-to-date when compared to last year. In the third quarter of 2003, higher expenses were driven by increased state and local taxes, increased spending for contract services and higher expenses for jointly operated facilities. Expenses increased year-to-date primarily due to increased contract services, higher state and local taxes, increased intermodal volume costs, joint facility expenses, and crew transportation costs.

**Operating Income** – Third quarter operating income decreased \$44 million (7%) to \$594 million while operating income year-to-date declined \$197 million (11%) to \$1.5 billion as higher fuel prices, wage and benefit inflation, volume and resource utilization costs offset higher revenues, lower depreciation expense and cost control efforts.

**Non-Operating Items** – Interest expense decreased \$12 million (9%) in the third quarter and \$38 million (9%) year-to-date due to lower interest rates and a lower average debt level in 2003. Other income decreased \$131 million (82%) in the third quarter and \$155 million (72%) year-to-date compared to 2002 due to lower gains from real estate sales (2002 land and track sale to the Utah Transit Authority with a pre-tax value of \$141 million). Income tax expense decreased \$66 million (27%) in the third quarter and \$120 million (21%) year-to-date compared to 2002 due to lower pre-tax income and higher state tax incentives in 2003.

## OTHER MATTERS

**Intercompany Relationship with UPC** - At September 30, 2003 and December 31, 2002, the Railroad had \$961 million and \$904 million working capital deficit balances, respectively, relating to UPC's management of its cash position. As part of UPC's cash management activities, the Railroad advances excess cash (cash available after satisfying all of the Railroad's obligations and paying dividends to UPC) to UPC. Dividends declared and paid to UPC by the Railroad typically approximate the dividends that UPC declares to its shareholders; however, there is no formal requirement to do so. The dividend declaration between the Railroad and UPC is determined solely by the Railroad's Board of Directors. To the extent the Railroad requires additional cash for use in its operations, UPC makes such funds available for borrowing by the Railroad. Transactions between UPC and UPRR are treated as net intercompany borrowings in the Consolidated Statements of Financial Position.

The majority of the Railroad's intercompany borrowings from UPC relate to the acquisitions of the Chicago and North Western Transportation Company and Southern Pacific Rail Corporation which were funded by UPC on behalf of the Railroad. These acquisition costs were assumed by the Railroad in the form of intercompany borrowings from UPC. The intercompany borrowings accrue interest at a rate of 7.5%, which may be adjusted from time to time, and are payable on demand. There are no restrictions on the amount the Railroad is able to borrow from UPC. Intercompany borrowings are unsecured and rank equally with all of the Railroad's other unsecured indebtedness.

UPC provides the Company with various services, including strategic planning, legal, treasury, accounting, auditing, insurance, human resources and corporate affairs. In 2003, pursuant to a services agreement, UPC will continue to provide services to the Company, and the Company will pay UPC its share of the costs as determined by an independent review. Billings for these services were \$13 million and \$40 million for the three months and nine months ended September 30, 2003.

**Commitments and Contingencies** - There are various claims and lawsuits pending against the Company and certain of its subsidiaries. The Company is also subject to various federal, state and local environmental laws and regulations, pursuant to which it is currently participating in the investigation and remediation of various sites. A discussion of certain claims, lawsuits, contingent liabilities and guarantees is set forth in note 7 to the Consolidated Financial Statements, which discussion is incorporated herein by reference.

**Ratio of Earnings to Fixed Charges** - For the three months and nine months ended September 30, 2003, the Company's ratio of earnings to fixed charges was 4.0 and 3.6, respectively, compared to 5.4 and 4.4 for the three months and nine months ended September 30, 2002. The ratio of earnings to fixed charges has been computed on a consolidated basis. Earnings represent income before cumulative effect of accounting change, less equity in undistributed earnings of unconsolidated affiliates, plus fixed charges and income taxes. Fixed charges represent interest charges, amortization of debt discount and the estimated amount representing the interest portion of rental charges.

**Pensions** - During the first quarter of 2003, the Company decreased its assumed rate of return on pension plan assets from 9% to 8%. This assumption change will result in an increase to 2003 pension expense of \$14 million. During the first nine months of 2003, the Railroad voluntarily contributed \$50 million to its pension plan.

**Network Performance** - The Railroad's operating efficiency has been adversely impacted due to record-level volumes, an expanded summer maintenance program and a shortage of trainmen, engineers and yardmasters. Programs are being put in place which the Railroad believes should remediate the situation by early next year including, among other things, hiring and training additional employees and acquiring additional locomotives.

**Accounting Pronouncements** - In January 2003, the FASB issued Interpretation No. 46, "Consolidation of Variable Interest Entities" (FIN 46). FIN 46 requires a variable interest entity to be consolidated by a company if that company is subject to a majority of the risk of loss from the variable interest entity's activities or entitled to receive a majority of the entity's residual returns or both. FIN 46 also requires disclosures about variable interest entities that a company is not required to consolidate but in which it has a significant variable interest. The consolidation requirements of FIN 46 apply immediately to variable interest entities created after January 31, 2003. As described in note 10 to the Consolidated Financial Statements, Item 8, in the Annual Report on Form 10-K, the Railroad has a synthetic operating lease arrangement to finance a new headquarters building, which falls within the guidance of FIN 46. In June 2003, the Railroad restructured the synthetic lease resulting in no effect to the Consolidated Financial Statements due to the adoption of FIN 46.

In October 2003, the FASB issued FASB Staff Position Number FIN 46-6 (FSP 46-6) which provides public entities an opportunity to delay implementation of FIN 46, for agreements entered into prior to February 1, 2003, until periods ending after December 15, 2003. FSP 46-6 does not impact the Company, as the Company has already adopted FIN 46.

## **CAUTIONARY INFORMATION**

Certain statements in this report are, and statements in other material filed or to be filed with the Securities and Exchange Commission (as well as information included in oral statements or other written statements made or to be made by the Company) are, or will be, forward-looking statements as defined by the Securities Act of 1933 and the Securities Exchange Act of 1934. These forward-looking statements include, without limitation, statements regarding: expectations as to operational improvements; expectations as to cost savings, revenue growth and earnings; the time by which certain objectives will be achieved; estimates of costs relating to environmental remediation and restoration; proposed new products and services; expectations that claims, lawsuits, environmental costs, commitments, contingent liabilities, labor negotiations or agreements, or other matters will not have a material adverse effect on the Company's consolidated financial position, results of operations or liquidity; and statements concerning projections, predictions, expectations, estimates or forecasts as to the Company's business, financial and operational results, and future economic performance, statements of management's goals and objectives and other similar expressions concerning matters that are not historical facts.

Forward-looking statements should not be read as a guarantee of future performance or results, and will not necessarily be accurate indications of the times that, or by which, such performance or results will be achieved. Forward-looking information is based on information available at the time and/or management's good faith belief with respect to future events, and is subject to risks and uncertainties that could cause actual performance or results to differ materially from those expressed in the statements.

Important factors that could affect the Company's future results and could cause those results or other outcomes to differ materially from those expressed or implied in the forward-looking statements include, but are not limited to:

- whether the Company is fully successful in implementing their financial and operational initiatives;
- industry competition, conditions, performance and consolidation;
- legislative and regulatory developments, including possible enactment of new tax rates and possible enactment of initiatives to re-regulate the rail industry;
- natural events such as severe weather, fire, floods and earthquakes;
- the effects of adverse general economic conditions, both within the United States and globally;
- any adverse economic or operational repercussions from terrorist activities and any governmental response thereto;
- war or risk of war;
- changes in fuel prices;
- changes in labor costs;
- labor stoppages; and
- the outcome of claims and litigation, including those related to environmental contamination, personal injuries, and occupational illnesses arising from hearing loss, repetitive motion and exposure to asbestos and diesel fumes.

Forward-looking statements speak only as of the date the statement was made. The Company assumes no obligation to update forward-looking information to reflect actual results, changes in assumptions or changes in other factors affecting forward-looking information. If the Company does update one or more forward-looking

statements, no inference should be drawn that the Company will make additional updates with respect thereto or with respect to other forward-looking statements.

### **Item 3. Quantitative and Qualitative Disclosures About Market Risk**

There have been no material changes in market risk from the information provided in Item 7A. Quantitative and Qualitative Disclosures About Market Risk of the Company's Annual Report on Form 10-K for the year ended December 31, 2002.

### **Item 4. Controls and Procedures**

As of the end of the period covered by this report, the Company carried out an evaluation, under the supervision and with the participation of the Company's management, including the Company's Chief Executive Officer (CEO) and Chief Financial Officer (CFO), of the effectiveness of the design and operation of the Company's disclosure controls and procedures pursuant to Exchange Act Rule 13a-15. Based upon that evaluation, the CEO and the CFO concluded that, as of the end of the period covered by this report, the Company's disclosure controls and procedures are effective in alerting them, in a timely manner, to material information relating to the Company (including its consolidated subsidiaries) required to be included in the Company's periodic SEC filings.

Additionally, as of the end of the period covered by this report, the CEO and CFO determined that there have been no changes to the Company's internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

## **PART II. OTHER INFORMATION**

### **Item 1. Legal Proceedings**

#### **ENVIRONMENTAL MATTERS**

The Company and its affiliates have received notices from the EPA and state environmental agencies alleging that they are or may be liable under certain federal or state environmental laws for remediation costs at various sites throughout the United States, including sites which are on the Superfund National Priorities List or state superfund lists. Although specific claims have been made by the EPA and state regulators with respect to some of these sites, the ultimate impact of these proceedings and suits by third parties cannot be predicted at this time because of the number of potentially responsible parties involved, the degree of contamination by various wastes, the scarcity and quality of volumetric data related to many of the sites and/or the speculative nature of remediation costs. Nevertheless, at many of the superfund sites, the Company believes it will have little or no exposure because no liability should be imposed under applicable law, one or more other financially able parties generated all or most of the contamination, or a settlement of the Company's exposure has been reached although regulatory proceedings at the sites involved have not been formally terminated.

Information concerning environmental claims and contingencies and estimated remediation costs is set forth in Management's Discussion and Analysis of Financial Condition and Results of Operations - Other Matters - Environmental Costs, Item 2, and in note 7 to the Consolidated Financial Statements, Item 1.

#### **OTHER MATTERS**

As previously reported, Western Resources, Inc. (Western) filed a complaint on January 24, 2000, in the U.S. District Court for the District of Kansas alleging that UPRR and The Burlington Northern and Santa Fe Railway Company (BNSF) materially breached their service obligations under the transportation contract to deliver coal in a timely manner to Western's Jeffrey Energy Center. The original complaint sought recovery of consequential damages and termination of the contract, excusing Western from further performance. In an amended complaint filed September 1, 2000, Western claimed the right to retroactive termination and added a claim for restitution. The matter went to trial before a jury on August 20, 2002. On September 12, 2002, the jury returned a verdict finding that the contract had not been breached by the railroads, and the judgment dismissing the case was entered by the court on September 16, 2002. Western filed a motion for new trial on September 30, 2002, which was denied by the court on March 6, 2003. Western filed notice of its intent to appeal the verdict to the 10<sup>th</sup> Circuit Court of Appeals on April 4, 2003. The parties reached a settlement on October 22, 2003. Western is in the process of dismissing its appeal in return for the payment to Western of \$50,000 by the railroads and waiving their respective rights to recover costs from Western.

### **Item 6. Exhibits and Reports on Form 8-K**

#### **(a) Exhibits**

Exhibits are listed in the exhibit index on page 23.

#### **(b) Reports on Form 8-K**

On October 23, 2003, the Registrant furnished a Current Report on Form 8-K announcing UPC's financial results for the third quarter of 2003.\*

On July 24, 2003, the Registrant furnished a Current Report on Form 8-K announcing UPC's financial results for the second quarter of 2003.\*

\* These reports were furnished under Item 12 of Form 8-K and are referenced herein for informational purposes only. Therefore, they are not, and none of their contents should be deemed, incorporated by reference into any registration statements filed by UPRR with the SEC under the Securities Act of 1933, as amended.

## **SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Dated: November 13, 2003

UNION PACIFIC RAILROAD COMPANY  
(Registrant)

By /s/ James R. Young  
James R. Young,  
Chief Financial Officer  
(Principal Financial Officer)

By /s/ Richard J. Putz  
Richard J. Putz,  
Chief Accounting Officer and Controller  
(Chief Accounting Officer and Duly Authorized  
Officer)

**UNION PACIFIC RAILROAD COMPANY**  
**EXHIBIT INDEX**

Exhibit No.      Description

Exhibits Filed with this Statement

- |       |   |
|-------|---|
| 12(a) | Ratio of Earnings to Fixed Charges for the Three Months Ended September 30, 2003 and 2002.  |
| 12(b) | Ratio of Earnings to Fixed Charges for the Nine Months Ended September 30, 2003 and 2002.   |
| 31(a) | Certification Pursuant to Rule 13a-14(a) of the Exchange Act, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 – Richard K. Davidson.         |
| 31(b) | Certification Pursuant to Rule 13a-14(a) of the Exchange Act, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 – James R. Young.              |
| 32    | Certifications Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 – Richard K. Davidson and James R. Young. |

Exhibits Incorporated by Reference

- |      |   |
|------|---|
| 3(a) | Amended Certificate of Incorporation of the Registrant, effective as of February 1, 1998, is incorporated herein by reference to Exhibit 3(a) to the Company's Annual Report on Form 10-K for the year ended December 31, 1998. |
| 3(b) | By-laws of the Registrant, as amended effective as of November 19, 1998, are incorporated herein by reference to Exhibit 3(b) to the Company's Annual Report on Form 10-K for the year ended December 31, 1998.                 |

**EXHIBIT 12(a)****Ratio of Earnings to Fixed Charges**

*Union Pacific Railroad Company and Consolidated Subsidiary and Affiliate Companies*  
(Unaudited)

<i>Millions of Dollars, Except Ratios</i>	<i>Three Months Ended September 30,</i>	
	<i>2003</i>	<i>2002</i>
Earnings:		
Income before cumulative effect of accounting change.....	\$317	\$414
Undistributed equity earnings .....	(14)	(18)
Total earnings.....	303	396
Income taxes.....	182	248
Fixed charges:		
Interest expense including amortization of debt discount.....	124	136
Portion of rentals representing an interest factor.....	40	11
Total fixed charges .....	164	147
Earnings available for fixed charges .....	\$649	\$791
Ratio of earnings to fixed charges .....	4.0	5.4



**EXHIBIT 12(b)****Ratio of Earnings to Fixed Charges**

*Union Pacific Railroad Company and Consolidated Subsidiary and Affiliate Companies*  
*(Unaudited)*

<i>Millions of Dollars, Except Ratios</i>	<i>Nine Months Ended September 30,</i>	
	<i>2003</i>	<i>2002</i>
Earnings:		
Income before cumulative effect of accounting change.....	\$ 779	\$ 973
Undistributed equity earnings .....	24	(39)
Total earnings.....	803	934
Income taxes.....	455	575
Fixed charges:		
Interest expense including amortization of debt discount.....	374	412
Portion of rentals representing an interest factor.....	117	32
Total fixed charges .....	491	444
Earnings available for fixed charges .....	\$1,749	\$1,953
Ratio of earnings to fixed charges .....	3.6	4.4

**CERTIFICATION  
OF PRINCIPAL EXECUTIVE OFFICER**

I, Richard K. Davidson, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Union Pacific Railroad Company;
2. Based on my knowledge, this report does not contain any untrue statement of material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 13, 2003

/s/ Richard K. Davidson  
Richard K. Davidson  
Chairman and  
Chief Executive Officer  
Union Pacific Railroad Company

**CERTIFICATION  
OF PRINCIPAL FINANCIAL OFFICER**

I, James R. Young, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Union Pacific Railroad Company;
2. Based on my knowledge, this report does not contain any untrue statement of material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 13, 2003

/s/ James R. Young  
James R. Young  
Chief Financial Officer  
Union Pacific Railroad Company

CERTIFICATION OF CHIEF EXECUTIVE OFFICER PURSUANT TO  
18 U.S.C. SECTION 1350,  
AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the accompanying Quarterly Report of Union Pacific Railroad Company (the Company) on Form 10-Q for the period ending September 30, 2003 as filed with the Securities and Exchange Commission on the date hereof (the Report), I, Richard K. Davidson, Chairman and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, to the best of my knowledge, that:

(1) The Report fully complies with the requirements of Section 13(a) of the Securities Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

By: /s/ Richard K. Davidson  
Richard K. Davidson  
Chairman and  
Chief Executive Officer  
Union Pacific Railroad Company

November 13, 2003

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

CERTIFICATION OF CHIEF FINANCIAL OFFICER PURSUANT TO  
18 U.S.C. SECTION 1350,  
AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the accompanying Quarterly Report of Union Pacific Railroad Company (the Company) on Form 10-Q for the period ending September 30, 2003 as filed with the Securities and Exchange Commission on the date hereof (the Report), I, James R. Young, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, to the best of my knowledge, that:

(1) The Report fully complies with the requirements of Section 13(a) of the Securities Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

By: /s/ James R. Young  
James R. Young  
Chief Financial Officer  
Union Pacific Railroad Company

November 13, 2003

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.