CANADIAN NATIONAL RAILWAY CO
Form 6-K
August 02, 2006

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 August 2006

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 _X_

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 _X_

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 _X_

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 _X_

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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Item 1

News

North America□s Railroad ***FOR IMMEDIATE RELEASE***

Stock symbols: TSX: CNR / NYSE: CNI

www.cn.ca

CN reports record second-quarter 2006 financial results on the strength of solid top line growth

MONTREAL, July 20, 2006 □ CN today reported its financial and operating results for the three-month and six-month periods ended June 30, 2006.

Financial highlights

- Second-quarter net income of C$729 million, or C$1.35 per diluted share, including a deferred income tax recovery of C$250 million (C$0.46 per diluted share) largely attributable to lower corporate tax rates in Canada;
- Excluding this deferred income tax recovery, adjusted net income was C$479 million, or C$0.89 per diluted share, a 22 per cent increase over year-earlier diluted EPS; [1]
- Operating income of C$805 million, up 13 per cent;
- Record quarterly revenues of C$1,946 million and operating ratio of 58.6 per cent, and
- First-half 2006 free cash flow of C$740 million. [1]

E. Hunter Harrison, president and chief executive officer of CN, said: □CN□s excellent financial performance during the quarter demonstrates the power and value of our precision railroading model.

"Precision railroading is grounded in a solid service plan, the relentless pursuit of asset velocity, and a strong focus on safety. This approach to railroading assured a fluid CN network during the quarter and permitted us to grow our business.

"CN maintained a strong free cash flow performance during the quarter, which allows the Company to continue rewarding shareholders through a new share buy-back program authorized by CN's Board of Directors today."

Revenues for the second quarter of 2006 increased six per cent to C$1,946 million, largely due to freight rate increases for all commodity groups, including a higher fuel surcharge resulting from an escalation in crude oil prices, and volume growth led by CN's grain and intermodal commodity groups. Revenue gains were partly offset by the unfavourable C$100-million translation impact of the stronger Canadian dollar on U.S. dollar-denominated revenues.

Five of CN's seven commodity groups registered revenue gains during the second quarter, driven in part by a five per cent increase in the Company's volumes, as measured by revenue ton-miles.

Operating expenses increased by one per cent to C$1,141 million, mainly due to increased fuel costs, purchased services and material expense, and depreciation. Partly offsetting these factors were lower casualty and other expense and equipment rents, as well as the favourable C$55-million translation impact of the stronger Canadian dollar on U.S. dollar-denominated operating expenses.

CN's operating ratio for the second quarter was 58.6 per cent, a 2.6-point improvement.

The continued appreciation of the Canadian dollar relative to the U.S. dollar reduced CN's second-quarter net income by approximately C$25 million.

Intermodal revenues increased 17 per cent during the quarter, benefiting from growth in international container traffic, primarily from Asia, and increased transborder and domestic movements. Grain and fertilizers revenues rose 16 per cent, driven in part by higher shipments to export markets of Canadian wheat, U.S. corn, and Canadian canola and canola meal.

Metals and minerals revenues increased seven per cent, reflecting increased volumes of iron ore, and strong shipments of long steel products and machinery and dimensional loads. Petroleum and chemicals revenues, benefiting from improvements in traffic mix, increased four per cent. Coal revenues grew by two per cent, largely as a result of the expansion of metallurgical coal mines in western Canada, offset partly by lower shipments of U.S. coal and Canadian exports of petroleum coke. Forest products revenues declined one per cent, in part because of reduced shipments of pulp and paper, while automotive revenues declined six per cent on account of production slowdowns by domestic producers, partly offset by higher shipments of import vehicles via CN-served ports.

Six-month 2006 results

Net income for the first six months of 2006 was C$1,091 million, or $C2.01 per diluted share, including the C$250-million (C$0.46 per diluted share) deferred income tax recovery.

Operating income for the six-month period increased 15 per cent to C$1,430 million. Revenues increased seven per cent to C$3,793 million, while operating expenses increased by three per cent to C$2,363 million.

The continued appreciation of the Canadian dollar relative to the U.S. dollar reduced CN's first-half revenues, operating expenses and net income by C$155 million, C$90 million, and C$35 million, respectively.

CN's operating ratio for the first half of 2006 was 62.3 per cent, a 2.7-point improvement.

The financial results in this press release were determined on the basis of U.S. generally accepted accounting principles (U.S. GAAP).

(1) Please see discussion and reconciliation of these non-GAAP adjusted performance measures in the attached supplementary schedule, Non-GAAP Measures.

This news release contains forward-looking statements. CN cautions that, by their nature, forward-looking statements involve risk and uncertainties, including the assumption that the positive economic trends in North America and Asia will continue, and that its results could differ materially from those expressed or implied in such statements. Reference should be made to CN's most recent Form 40-F filed with the United States Securities and Exchange Commission, its Annual Information Form filed with the Canadian securities regulators, its 2005 Annual Consolidated Financial Statements and Notes thereto and Management's Discussion and Analysis (MD&A), as well as its 2006 quarterly consolidated financial statements and MD&A, for a summary of major risks.

CN – Canadian National Railway Company – 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, Ala., and the key cities of Toronto, Buffalo, Chicago, Detroit, Duluth, Minn./Superior, Wis., Green Bay, Wis., Minneapolis/St. Paul, Memphis, St. Louis, and Jackson, Miss., with connections to all points in North America.

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Item 2

CANADIAN NATIONAL RAILWAY COMPANY

CONSOLIDATED STATEMENT OF INCOME *(U.S. GAAP)*

(In millions, except per share data)

	Three months ended June 30		Six months ended June 30	
	2006	2005	**2006**	2005
		(Unaudited)		
Revenues	**$ 1,946**	$ 1,838	**$ 3,793**	$ 3,544
Operating expenses	**1,141**	1,125	**2,363**	2,305
Operating income	**805**	713	**1,430**	1,239
Interest expense	**(75)**	(78)	**(150)**	(153)
Other loss	**(5)**	(5)	**(6)**	(9)
Income before income taxes	**725**	630	**1,274**	1,077
Income tax recovery (expense) *(Note 4)*	**4**	(214)	**(183)**	(362)
Net income	**$ 729**	$ 416	**$ 1,091**	$ 715
Earnings per share *(Notes 8, 9)*				
Basic	**$ 1.38**	$ 0.75	**$ 2.05**	$ 1.28
Diluted	**$ 1.35**	$ 0.73	**$ 2.01**	$ 1.25
Weighted-average number of shares				
Basic	**529.9**	556.1	**533.0**	559.9
Diluted	**538.5**	566.0	**541.8**	570.4

See accompanying notes to consolidated financial statements.

CANADIAN NATIONAL RAILWAY COMPANY

CONSOLIDATED STATEMENT OF OPERATING INCOME *(U.S. GAAP)*

(In millions)

	Three months ended June 30			Six months ended June 30		
	2006	2005	Variance Fav (Unfav)	**2006**	2005	Variance Fav (Unfav)
			(Unaudited)			
Revenues						
Petroleum and chemicals	**$ 282**	$ 271	4%	**$ 574**	$ 546	5%
Metals and minerals	**229**	214	7%	**442**	413	7%
Forest products	**444**	450	(1%)	**882**	854	3%
Coal	**99**	97	2%	**186**	176	6%
Grain and fertilizers	**301**	260	16%	**599**	536	12%
Intermodal	**365**	313	17%	**686**	600	14%
Automotive	**131**	139	(6%)	**263**	261	1%
Other items	**95**	94	1%	**161**	158	2%
	1,946	1,838	6%	**3,793**	3,544	7%
Operating expenses						
Labor and fringe benefits	**430**	436	1%	**918**	935	2%
Purchased services and material	**203**	196	(4%)	**418**	402	(4%)
Depreciation and amortization	**162**	158	(3%)	**326**	314	(4%)
Fuel	**225**	179	(26%)	**428**	345	(24%)
Equipment rents	**38**	53	28%	**85**	100	15%
Casualty and other	**83**	103	19%	**188**	209	10%
	1,141	1,125	(1%)	**2,363**	2,305	(3%)
Operating income	**$ 805**	$ 713	13%	**$ 1,430**	$ 1,239	15%
Operating ratio	**58.6%**	61.2%	2.6	**62.3%**	65.0%	2.7

See accompanying notes to consolidated financial statements.

CANADIAN NATIONAL RAILWAY COMPANY

CONSOLIDATED BALANCE SHEET *(U.S. GAAP)*

(In millions)

	June 30 2006	December 31 2005	June 30 2005
	(Unaudited)		*(Unaudited)*
Assets			
Current assets:			
Cash and cash equivalents	**$ 207**	$ 62	$ 155
Accounts receivable *(Note 2)*	**957**	623	662
Material and supplies	**235**	151	187
Deferred income taxes	**71**	65	181
Other	**118**	248	279
	1,588	1,149	1,464
Properties	**19,924**	20,078	20,057
Intangible and other assets	**970**	961	918
Total assets	**$ 22,482**	$ 22,188	$ 22,439
Liabilities and shareholders' equity			
Current liabilities:			
Accounts payable and accrued charges	**$ 1,511**	$ 1,478	$ 1,577
Current portion of long-term debt *(Note 2)*	**127**	408	83
Other	**77**	72	82
	1,715	1,958	1,742
Deferred income taxes *(Note 4)*	**4,788**	4,817	4,910
Other liabilities and deferred credits	**1,451**	1,487	1,499
Long-term debt *(Note 2)*	**5,294**	4,677	5,034
Shareholders' equity:			
Common shares	**4,543**	4,580	4,640
Accumulated other comprehensive loss	**(521)**	(222)	(106)
Retained earnings	**5,212**	4,891	4,720
	9,234	9,249	9,254

Total liabilities and shareholders' equity	**$ 22,482**	$ 22,188	$ 22,439

See accompanying notes to consolidated financial statements.

CANADIAN NATIONAL RAILWAY COMPANY

CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS EQUITY *(U.S. GAAP)*

(In millions)

	Three months ended June 30		Six months ended June 30	
	2006	2005	**2006**	2005
		(Unaudited)		
Common shares (1)				
Balance, beginning of period	**$ 4,591**	$ 4,715	**$ 4,580**	$ 4,706
Stock options exercised and other	**11**	15	**82**	101
Share repurchase programs *(Note 2)*	**(59)**	(90)	**(119)**	(167)
Balance, end of period	**$ 4,543**	$ 4,640	**$ 4,543**	$ 4,640
Accumulated other comprehensive loss				
Balance, beginning of period	**$ (245)**	$ (91)	**$ (222)**	$ (148)
Other comprehensive income (loss):				
Unrealized foreign exchange gain (loss) on translation of U.S. dollar-denominated long-term debt designated as a hedge of the net investment in U.S. subsidiaries	**201**	(40)	**207**	(77)
Unrealized foreign exchange gain (loss) on translation of the net investment in foreign operations	**(250)**	49	**(264)**	93
Increase (decrease) in unrealized holding gains on fuel derivative instruments *(Note 5)*	**(20)**	(31)	**(47)**	47
Other comprehensive income (loss) before income taxes	**(69)**	(22)	**(104)**	63
Income tax recovery (expense) *(Note 4)*	**(207)**	7	**(195)**	(21)
Other comprehensive income (loss)	**(276)**	(15)	**(299)**	42

Balance, end of period	**$ (521)**	$ (106)	**$ (521)**	$ (106)
Retained earnings				
Balance, beginning of period	**$ 4,856**	$ 4,684	**$ 4,891**	$ 4,726
Net income	**729**	416	**1,091**	715
Share repurchase programs *(Note 2)*	**(288)**	(311)	**(598)**	(581)
Dividends	**(85)**	(69)	**(172)**	(140)
Balance, end of period	**$ 5,212**	$ 4,720	**$ 5,212**	$ 4,720

See accompanying notes to consolidated financial statements.

(1) During the three and six months ended June 30, 2006, the Company issued 0.3 million and 3.2 million common shares, respectively, as a result of stock options exercised. At June 30, 2006, the Company had 526.0 million common shares outstanding (Note 9).

CANADIAN NATIONAL RAILWAY COMPANY

CONSOLIDATED STATEMENT OF CASH FLOWS *(U.S. GAAP)*

(In millions)

	Three months ended June 30		Six months ended June 30	
	2006	2005	**2006**	2005
		(Unaudited)		
Operating activities				
Net income	**$ 729**	$ 416	**$ 1,091**	$ 715
Adjustments to reconcile net income to net cash provided from operating activities:				
Depreciation and amortization	**163**	159	**327**	316
Deferred income taxes *(Note 4)*	**(141)**	162	**(94)**	298
Other changes in:				
Accounts receivable *(Note 2)*	**(419)**	70	**(349)**	134
Material and supplies	**(12)**	(8)	**(84)**	(59)
Accounts payable and accrued charges	**35**	(60)	**15**	(81)
Other net current assets and liabilities	**50**	53	**83**	43
Other	**-**	(7)	**35**	2
Cash provided from operating activities	**405**	785	**1,024**	1,368
Investing activities				
Property additions	**(287)**	(318)	**(442)**	(471)
Other, net	**9**	69	**(45)**	73
Cash used by investing activities	**(278)**	(249)	**(487)**	(398)
Financing activities				
Issuance of long-term debt	**2,323**	473	**3,125**	1,093
Reduction of long-term debt	**(1,992)**	(596)	**(2,702)**	(1,247)
Issuance of common shares due to exercise of stock options and related excess tax benefits realized (*Note 3*)	**8**	10	**74**	80
Repurchase of common shares	**(347)**	(401)	**(717)**	(748)
Dividends paid	**(85)**	(69)	**(172)**	(140)
Cash used by financing activities	**(93)**	(583)	**(392)**	(962)

Net increase (decrease) in cash and cash equivalents		**34**		(47)		**145**		8
Cash and cash equivalents, beginning of period		**173**		202		**62**		147
Cash and cash equivalents, end of period	**$**	**207**	$	155	**$**	**207**	$	155
Supplemental cash flow information								
Net cash receipts from customers and other	**$**	**1,547**	$	1,834	**$**	**3,468**	$	3,720
Net cash payments for:								
Employee services, suppliers and other expenses		**(942)**		(892)		**(2,069)**		(2,005)
Interest		**(53)**		(52)		**(141)**		(143)
Workforce reductions		**(11)**		(21)		**(27)**		(52)
Personal injury and other claims		**(16)**		(21)		**(42)**		(48)
Pensions		**(24)**		(52)		**(25)**		(54)
Income taxes		**(96)**		(11)		**(140)**		(50)
Cash provided from operating activities	**$**	**405**	$	785	**$**	**1,024**	$	1,368

See accompanying notes to consolidated financial statements.

Certain of the 2005 comparative figures have been reclassified in order to be consistent with the 2006 presentation.

CANADIAN NATIONAL RAILWAY COMPANY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(U.S. GAAP)*

Note 1 Basis of presentation

In managements opinion, the accompanying unaudited Interim Consolidated Financial Statements and Notes thereto, expressed in Canadian dollars, and prepared in accordance with U.S. generally accepted accounting principles (U.S. GAAP) for interim financial statements, contain all adjustments (consisting of normal recurring accruals) necessary to present fairly Canadian National Railway Companys (the Company) financial position as at June 30, 2006 and December 31 and June 30, 2005, its results of operations, changes in shareholders equity and cash flows for the three and six months ended June 30, 2006 and 2005.

These unaudited Interim Consolidated Financial Statements and Notes thereto have been prepared using accounting policies consistent with those used in preparing the Companys 2005 Annual Consolidated Financial Statements, except for stock-based compensation as explained in Note 3 Stock plans. While management believes that the disclosures presented are adequate to make the information not misleading, these unaudited Interim Consolidated Financial Statements and Notes thereto should be read in conjunction with the Companys Interim Managements Discussion and Analysis and Annual Consolidated Financial Statements and Notes thereto.

Note 2 Financing activities

Shelf prospectus and registration statement

On May 9, 2006, the Company filed a shelf prospectus and registration statement providing for the issuance, from time to time, of up to U.S.$1,500 million of debt securities in one or more offerings. Pursuant to the filing, on May 31, 2006, the Company issued U.S.$250 million (Cdn$275 million) of 5.80% Notes due 2016 and U.S.$450 million (Cdn$495 million) of 6.20% Debentures due 2036. The Company used the net proceeds of U.S.$692 million to reduce its accounts receivable securitization program and to repay a portion of its outstanding commercial paper.

On July 15, 2006, the interest rate on the Companys U.S.$250 million Puttable Reset Securities PURSSM (PURS) was reset at a new rate of 6.71% for the remaining 30-year term ending July 15, 2036. The PURS were originally issued in July 1998 with an option to call the securities on July 15, 2006 (the reset date). The call option holder exercised the call option, which resulted in the remarketing of the original PURS. The new interest rate was determined according to a pre-set mechanism based on prevailing market conditions. The Company did not receive any cash proceeds from the remarketing.

The remarketing did not trigger an extinguishment of debt, as the provisions for the reset of the interest rate were set forth in the original PURS. As such, the original PURS remain outstanding but accrue interest at the new rate until July 2036. Under securities laws, the remarketing required utilization of the Company's shelf prospectus and registration statement.

Following the issuance and remarketing of debt as explained herein, the amount available under the shelf prospectus and registration statement has been reduced to U.S.$550 million.

Revolving credit facility

In January 2006, the Company repaid its borrowings of U.S.$15 million (Cdn$17 million) outstanding at December 31, 2005 under its U.S.$1,000 million revolving credit facility. As at June 30, 2006, the Company had letters of credit drawn on its revolving credit facility of $315 million ($316 million as at December 31, 2005). The Company also had outstanding borrowings of U.S.$117 million (Cdn$130 million) under its commercial paper program at an average interest rate of 5.28% (U.S.$367 million (Cdn$427 million) at an average interest rate of 4.40%, as at December 31, 2005).

CANADIAN NATIONAL RAILWAY COMPANY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(U.S. GAAP)*

Accounts receivable securitization

On May 31, 2006, the Company entered into an agreement, expiring in May 2011, to sell an undivided co-ownership interest of up to a maximum of $600 million in a revolving pool of freight receivables to an unrelated trust. As part of the interest sold, the Company has recorded, in Other current assets, an amount equal to the required reserves stipulated in the agreement. The Company has retained the responsibility for servicing, administering and collecting the receivables sold. At June 30, 2006, the servicing asset and liability were not significant. Costs related to the agreement, which fluctuate with changes in prevailing interest rates, are recorded in Other loss. Subject to customary indemnifications, the trusts recourse to the Company is generally limited to income earned on the receivables.

This new program replaces the Companys previous accounts receivable securitization program that was set to expire in June 2006. Upon termination of the previous program, the receivables sold were repurchased with the funds from the Companys debt issuance in May 2006. Pursuant to the repurchase, receivables in the amount of $535 million were added to the balance sheet and the retained interest that was recorded in Other current assets in the amount of $51 million, was removed.

The Company accounts for the securitization program as a sale, as control over the transferred accounts receivable is relinquished. Due to the relatively short collection period and the high quality of the receivables sold, the fair value of the undivided interest transferred to the trust, net of the retained interest (the required reserves), approximated the book value and there was no gain or loss resulting from the transaction.

At June 30, 2006, the Company had received $100 million under the new accounts receivable securitization program ($489 million at December 31, 2005 under the previous program), and set aside approximately 10% of this amount in Other current assets.

Share repurchase programs

In the second quarter of 2006, under its 32.0 million share repurchase program, the Company repurchased 7.0 million common shares for $347 million, at an average price of $49.57 per share. The Company has now ended this program. Since July 25, 2005, the inception of the program, the Company repurchased a total of 30.0 million common shares for $1,388 million, at an average price of $46.26 per share.

On July 20, 2006, the Board of Directors of the Company approved a new share repurchase program which allows for the repurchase of up to 28.0 million common shares between July 25, 2006 and July 24, 2007 pursuant to a normal course issuer bid, at prevailing market prices.

Note 3 Stock plans

On January 1, 2006, the Company adopted Statement of Financial Accounting Standards (SFAS) No. 123(R), Share-Based Payment, which requires the expensing of all options issued, modified or settled based on the grant date fair value over the period during which an employee is required to provide service (vesting period). The standard also requires that cash settled awards be measured at fair value at each reporting date until ultimate settlement.

The Company adopted SFAS No. 123(R) using the modified prospective approach, which requires application of the standard to all awards granted, modified, repurchased or cancelled on or after January 1, 2006, and to all awards for which the requisite service has not been rendered as at such date. Since January 1, 2003, the Company has been following the fair value based approach prescribed by SFAS No. 123, Accounting for Stock-Based Compensation, as amended by SFAS No. 148, Accounting for Stock-Based Compensation Transition and Disclosure, for stock option awards granted, modified or settled on or after such date, while cash settled awards were measured at their intrinsic value at each reporting period until December 31, 2005. As such, the application of SFAS No. 123(R) on January 1, 2006 to all awards granted prior to its adoption did not have a significant impact on the financial statements. In accordance with the modified prospective approach, prior period financial statements have not been restated to reflect the impact of SFAS No. 123(R).

For the three and six months ended June 30, 2006, the application of SFAS No. 123(R) had the effect of decreasing stock-based compensation expense by $2 million and increasing stock-based compensation expense by $3 million, respectively, and increasing net income by $1 million and decreasing net income by $2 million, respectively. There was no effect on the basic and diluted earnings per share for the three and six months ended June 30, 2006.

CANADIAN NATIONAL RAILWAY COMPANY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(U.S. GAAP)*

The Company has various stock-based incentive plans for eligible employees. A description of the plans is provided herein. For the three and six months ended June 30, 2006, the Company recorded total compensation cost for awards under all plans of $7 million and $41 million, respectively, and $13 million and $41 million, respectively, for the same periods in 2005. The total tax benefit recognized in income in relation to stock-based compensation expense for the three and six months ended June 30, 2006, was $1 million and $11 million, respectively, and $3 million and $10 million, respectively, for the same periods in 2005.

Cash settled awards

A. Restricted share units

The Company has granted restricted share units (RSUs), 0.8 million in 2006 and 0.9 million in 2005, to designated management employees entitling them to receive payout in cash based on the Company's share price. The RSUs granted are generally scheduled for payout after three years and vest upon the attainment of targets relating to return on invested capital over the three-year period and to the Company's share price during the three-month period ending December 31, 2008 for the 2006 grant and December 31, 2007 for the 2005 grant. The Company had granted 2.3 million RSUs in 2004, having the same general terms as the currently outstanding RSUs described, except that the RSUs were subject to accelerated payout if specified targets related to the Company's 20-day average share price were attained during the period ending December 31, 2005. Given that these targets were met, vesting of these units was accelerated and increased to its maximum allowable amount under the plan, resulting in a payout of $105 million. Of this amount, $41 million was converted into deferred share units at December 31, 2005, and the remaining payout of $64 million was paid in cash in January 2006. As at June 30, 2006, a minimal amount of RSUs remained authorized for future issuance under this plan.

B. Vision 2008 Share Unit Plan

The Company has a special share unit plan (Vision), which was approved by the Board of Directors in January 2005, whereby 0.8 million share units were granted to designated senior management employees entitling them to receive a payout in cash, based on the Company's share price, in January 2009. The share units vest conditionally upon the attainment of targets relating to the Company's share price during the six-month period ending December 31, 2008. Payout is conditional upon the attainment of targets relating to return on invested capital over the four-year period and to the Company's share price during the 20-day period ending on December 31, 2008. The award payout will be equal to the number of share units vested on December 31, 2008 multiplied by the Company's 20-day average share price ending on such date. As at June 30, 2006, 0.2 million share units remained authorized for future issuance under this plan.

C. Voluntary Incentive Deferral Plan

The Company has a Voluntary Incentive Deferral Plan (VIDP), providing eligible senior management employees the opportunity to elect to receive their annual incentive bonus payment and other eligible incentive payments in deferred share units (DSUs). A DSU is equivalent to a common share of the Company and also earns dividends when cash dividends are paid on common shares. The number of DSUs received by each participant is established using the average closing price for the 20 trading days prior to and including the date of the incentive payment. For each participant, the Company will grant a further 25% (Company match) of the amount elected in DSUs, which will vest over a period of 4 years. The election to receive eligible incentive payments in DSUs is no longer available to a participant when the value of the participant's vested DSUs is sufficient to meet the Company's stock ownership guidelines. The value of each participant's DSUs is payable in cash at the time of cessation of employment. The Company's liability for DSUs is marked-to-market at each period-end based on the Company's closing stock price.

CANADIAN NATIONAL RAILWAY COMPANY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(U.S. GAAP)*

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

	RSUs		**Vision**		**VIDP**	
In millions	Nonvested	Vested	Nonvested	Vested	Nonvested	Vested
Outstanding at December 31, 2005	1.2	-	0.8	-	0.4	1.7
Granted	0.8	-	-	-	-	-
Forfeited	-	-	-	-	-	-
Vested during period	-	-	-	-	-	-
Conversion into VIDP	-	-	-	-	-	0.1
Outstanding at June 30, 2006	**2.0**	-	**0.8**	**-**	**0.4**	**1.8**

Additional disclosures required under SFAS No. 123(R) for cash settled awards are provided in tabular format herein.

Stock option awards

The Company has stock option plans for eligible employees to acquire common shares of the Company upon vesting at a price equal to the market value of the common shares at the date of granting. The options are exercisable during a period not exceeding 10 years. The right to exercise options generally accrues over a period of four years of continuous employment. Options are not generally exercisable during the first 12 months after the date of grant. At June 30, 2006, 15.2 million common shares remained authorized for future issuances under these plans.

Options issued by the Company include conventional options, which vest over a period of time, performance options, which vested upon the attainment of Company targets relating to the operating ratio and unlevered return on investment, and performance-accelerated options, which vest on the sixth anniversary of the grant or prior if certain Company targets, relating to return on investment and revenues, are attained.

In the first half of 2006 and 2005, the Company granted approximately 1.0 million and 1.3 million, respectively, of conventional stock options to designated senior management employees that vest over a period of four years of continuous employment. As at June 30, 2006, the Company's performance-based stock options were fully vested and the performance-accelerated options vested in January 2006 given that the specified targets were met.

The total number of options outstanding at June 30, 2006, for conventional, performance, and performance-accelerated options was 13.2 million, 0.8 million and 4.8 million, respectively.

The following table provides the activity of stock option awards during the quarter, and for options outstanding and exercisable at the end of the quarter, the weighted average exercise price, the weighted average years to expiration and the aggregate intrinsic value. The aggregate intrinsic value represents the total pre-tax intrinsic value, based on the Company's closing stock price at June 30, 2006 of $48.76, which would have been received by option holders had they exercised their options on such date.

	Options outstanding						Nonvested options		
	Number of options		Weighted-average exercise price	Weighted-average years to expiration		Aggregate intrinsic value	Number of options		Weighted-average grant date fair value
	In millions					*In millions*	*In millions*		
Outstanding at December 31, 2005 (1)	21.0	$	20.95				5.4	$	8.47
Granted	1.0	$	51.52				1.0	$	13.81
Forfeited	-	$	-				-	$	-
Exercised	(3.2)	$	18.12				N/A		N/A
Vested	N/A		N/A				(4.3)	$	8.30
Outstanding at June 30, 2006 (1)	18.8	$	23.01	5.6	$	484	2.1	$	11.58
Exercisable at June 30, 2006 (1)	16.7	$	20.60	5.2	$	471	N/A		N/A

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

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The following table provides information related to options exercised during the three and six months ended June 30, 2006 and 2005:

	Three months ended June 30		Six months ended June 30	
In millions	**2006**	2005	**2006**	2005
Total intrinsic value	**$ 8**	$ 11	**$ 107**	$ 95
Cash received upon exercise of options	**$ 7**	$ 10	**$ 59**	$ 80
Related tax benefit realized	**$ 1**	$ 1	**$ 15**	$ 15

Prior to January 1, 2006, the Company followed the fair value based approach for stock option awards and had prospectively applied this method of accounting to all awards granted, modified or settled on or after January 1, 2003, and measured cash settled awards at their intrinsic value at period end. For the three and six months ended June 30, 2005, if compensation cost had been determined based upon fair values at the date of grant for awards under all plans, the Company's pro forma net income and earnings per share would have been as follows:

In millions, except per share data	**Three months ended June 30, 2005**	**Six months ended June 30, 2005**
Net income, as reported	$ 416	$ 715
Add (deduct) compensation cost, net of applicable taxes, determined under:		
Fair value method for all awards granted after Jan 1, 2003 (SFAS No. 123)	10	31
Fair value method for all awards (SFAS No. 123)	(16)	(43)
Pro forma net income	$ 410	$ 703
Basic earnings per share, as reported	$ 0.75	$ 1.28
Basic earnings per share, pro forma	$ 0.74	$ 1.26
Diluted earnings per share, as reported	$ 0.73	$ 1.25
Diluted earnings per share, pro forma	$ 0.73	$ 1.23

2006 data is not provided since net income and pro forma net income would be the same given the application of SFAS No. 123(R).

Additional disclosures required under SFAS No. 123(R) for option awards are provided in tabular format herein.

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Additional disclosures required under SFAS No. 123(R) pertaining to all awards

	Cash settled awards					**Stock option awards (3)**		
In millions, unless otherwise indicated	**RSUs (1)**			**Vision (1)**	**VIDP (2)**			
Year of grant	2006	2005	2004	2005	2003 onwards	2006 (8)	2005	Prior to 2005
Stock-based compensation expense recognized over vesting period								
Six months ended June 30, 2006	$ 5	$ 8	$ 3	$ 6	$ 10	$ 5	$ 1	$ 3
Six months ended June 30, 2005	$ -	$ 5	$ 26	$ -	$ -	$ -	$ 1	$ 9
Liability outstanding								
June 30, 2006	$ 5	$ 23	$ 5	$ 6	$ 96	N/A	N/A	N/A
December 31, 2005	$ -	$ 15	$ 66	$ -	$ 83	N/A	N/A	N/A
Fair value per unit								
At period-end *($)*	$ 36.21	$ 47.59	$ 48.76	$ 21.58	$ 48.76	N/A	N/A	N/A
At grant date *($)*	N/A	N/A	N/A	N/A	N/A	$ 13.81	$ 9.24	$ 8.61
Fair value of awards vested during period								
Six months ended June 30, 2006	$ -	$ -	$ -	$ -	$ 2	$ -	$ 3	$ 33
Six months ended June 30, 2005	$ -	$ -	$ -	$ -	$ 1	$ -	$ -	$ 34
Nonvested awards at June 30, 2006								
Unrecognized compensation cost	$ 24	$ 23	$ 11	$ 10	$ 15	$ 8	$ 7	$ -
Remaining recognition period *(years)*	2.5	1.5	2.5	2.5	3.5	3.6	2.6	-
Assumptions (4)								
Stock price *($)*	$ 48.76	$ 48.76	$ 48.76	$ 48.76	$ 48.76	$ 51.52	$ 36.30	$ 23.59
Expected stock price volatility (5)	19%	18%	N/A	20%	N/A	25%	25%	30%
Expected term *(years)* (6)	2.50	1.50	N/A	2.50	N/A	5.17	5.20	6.22
Risk-free interest rate (7)	4.44%	4.40%	N/A	4.84%	N/A	4.04%	3.55%	5.14%
Dividend rate *($)*	$ 0.65	$ 0.65	N/A	$ 0.65	N/A	$ 0.65	$ 0.50	$ 0.30

(1) Beginning in 2006, compensation cost was based on the fair value of the awards at period-end using the lattice-based valuation model that uses the assumptions as presented herein, except for time-vested RSUs. In 2005, compensation cost was measured using intrinsic value.

(2) Compensation cost for all periods presented was based on intrinsic value.

(3) Compensation cost for all periods presented was based on the grant date fair value using the Black-Scholes option-pricing model that uses the assumptions presented herein.

(4) Assumptions used to determine fair value are at period-end for cash settled awards and at grant date for stock option awards.

(5) Based on the historical volatility of the Company's stock.

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

(7) Based on the Treasury rate.

(8) Includes the accelerated recognition of awards granted to retirement-eligible employees. For these individuals, compensation cost is recognized over the period from the grant date to the date the requisite service period has been achieved.

CANADIAN NATIONAL RAILWAY COMPANY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(U.S. GAAP)*

Note 4 Income taxes

In the second quarter of 2006, the Company adjusted its deferred income tax liability mainly due to the enactment of lower federal and provincial corporate tax rates in Canada. As a result, the Company recorded a deferred income tax recovery of $250 million in the Consolidated statement of income.

Also in the second quarter, for certain items reported in Accumulated other comprehensive loss (a separate component of Shareholders equity), the Company adjusted its deferred income tax liability for changes in income tax rates applied to certain temporary differences and also for the income tax effect on the currency translation amount resulting from the difference between the accounting and tax basis of its net investment in foreign subsidiaries. As a result, the Company recorded a net charge for deferred income taxes in Other comprehensive loss of $180 million.

Note 5 Derivative instruments

Fuel

Following the suspension of the Companys fuel hedging program in late 2005, the Companys remaining hedge positions at June 30, 2006 cover approximately 5% of the estimated remaining 2006 fuel consumption, representing approximately 9 million U.S. gallons at an average price of U.S.$0.96 per U.S. gallon. These derivative instruments are carried at market value on the balance sheet and are accounted for as cash flow hedges whereby the effective portion of the cumulative change in the market value of the derivative instruments has been recorded in Other comprehensive income (loss). At June 30, 2006, Accumulated other comprehensive loss included unrealized gains of $10 million, $7 million after tax ($57 million, $39 million after tax at December 31, 2005), which relate to derivative instruments that will mature within the year and are presented in Other current assets.

Interest rate

At June 30, 2006, Accumulated other comprehensive loss included an unamortized gain of $12 million, $8 million after tax.

Note 6 Pensions and other post-retirement benefits

For the three and six months ended June 30, 2006 and 2005, the components of net periodic benefit cost for pensions and other post-retirement benefits were as follows:

(a) **Components of net periodic benefit cost for pensions**

	Three months ended June 30		**Six months ended June 30**	
In millions	**2006**	2005	**2006**	2005
Service cost	**$ 40**	$ 35	**$ 80**	$ 71
Interest cost	**179**	186	**358**	371
Amortization of prior service cost	**5**	5	**9**	10
Expected return on plan assets	**(226)**	(221)	**(453)**	(442)
Amortization of net actuarial loss	**23**	1	**46**	1

Net periodic benefit cost	**$**	**21**	$	6	**$**	**40**	$	11

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(U.S. GAAP)*

(b) **Components of net periodic benefit cost for post-retirement benefits**

	Three months ended June 30		Six months ended June 30	
In millions	**2006**	2005	**2006**	2005
Service cost	**$ 1**	$ 2	**$ 2**	$ 4
Interest cost	**4**	5	**8**	10
Amortization of prior service cost	**-**	1	**-**	1
Recognized net actuarial gain	**(3)**	(1)	**(4)**	(2)
Net periodic benefit cost	**$ 2**	$ 7	**$ 6**	$ 13

For the 2006 funding year, the Company expects to make total contributions of approximately $100 million for all its defined benefit plans of which $25 million was disbursed as at June 30, 2006.

Note 7 Major commitments and contingencies

A. Commitments

As at June 30, 2006, the Company had commitments to acquire railroad ties, rail, freight cars, locomotives and other equipment or services at an aggregate cost of $561 million ($578 million at December 31, 2005). The Company also had outstanding information technology service contracts of $14 million and agreements with fuel suppliers to purchase approximately 75% of the estimated remaining 2006 volume, and 24% of its anticipated 2007 volume at market prices prevailing on the date of the purchase.

B. Contingencies

In the normal course of its operations, the Company becomes involved in various legal actions, including claims relating to personal injuries, occupational disease and damage to property.

In Canada, employee injuries are governed by the workers compensation legislation in each province whereby employees may be awarded either a lump sum or future stream of payments depending on the nature and severity of the injury. Accordingly, 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 administration costs. For all other legal actions, the Company maintains, and regularly updates on a case-by-case basis, provisions for such items when the expected loss is both probable and can be reasonably estimated based on currently available information.

In the United States, employee work-related injuries, including occupational disease claims, are compensated according to the provisions of the Federal Employers Liability Act (FELA), which requires either the finding of fault through the U.S. jury system or individual settlements, and represent a major liability for the railroad industry. The Company follows an actuarial-based approach and accrues the expected cost for personal injury and property damage claims and asserted and unasserted occupational disease claims, based on actuarial estimates of their ultimate cost. A comprehensive actuarial study is conducted on an annual basis by an independent actuarial firm. On an ongoing basis, management reviews and compares the assumptions inherent in the latest actuarial study with the current claim experience and, if required, adjustments to the liability are recorded.

As at June 30, 2006, the Company had aggregate reserves for personal injury and other claims of $630 million ($657 million at December 31, 2005). Although the Company considers such provisions to be adequate for all its outstanding and pending claims, the final outcome with respect to actions outstanding or pending at June 30, 2006, or with respect to future claims, cannot be predicted with certainty, and therefore there can be no assurance that their resolution will not have a material adverse effect on the Company's financial position or results of operations in a particular quarter or fiscal year.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(U.S. GAAP)*

C. Environmental matters

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

While the Company believes that it has identified the costs likely to be incurred in the next several years, based on known information, for environmental matters, the Companys ongoing efforts to identify potential environmental concerns that may be associated with its properties may lead to future environmental investigations, which may result in the identification of additional environmental costs and liabilities. The magnitude of such additional liabilities and the costs of complying with environmental laws and containing or remediating contamination cannot be reasonably estimated due to:

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

therefore, the likelihood of any such costs being incurred or whether such costs would be material to the Company cannot be determined at this time. There can thus be no assurance that material liabilities or costs related to environmental matters will not be incurred in the future, or will not have a material adverse effect on the Companys financial position or results of operations in a particular quarter or fiscal year, or that the Companys liquidity will not be adversely impacted by such environmental liabilities or costs. Although the effect on operating results and liquidity cannot be reasonably estimated, management believes, based on current information, that environmental matters will not have a material adverse effect on the Companys financial condition or competitive position. Costs related to any future remediation will be accrued in the year in which they become known.

As at June 30, 2006, the Company had aggregate accruals for environmental costs of $127 million ($124 million as at December 31, 2005).

D. Guarantees and indemnifications

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

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

Guarantee of residual values of operating leases

The Company has guaranteed a portion of the residual values of certain of its assets under operating leases with expiry dates between 2007 and 2012, for the benefit of the lessor. If the fair value of the assets, at the end of their respective lease term, is less than the fair value, as estimated at the inception of the lease, then the Company must, under certain conditions, compensate the lessor for the shortfall. As at June 30, 2006, the maximum exposure in respect of these guarantees was $75 million, of which $2 million has been recorded and represents the Company's obligation to stand ready and honor the guarantees that were entered into in accordance with Financial Accounting Standard Board Interpretation No. 45 requirements. There are no recourse provisions to recover any amounts from third parties.

CANADIAN NATIONAL RAILWAY COMPANY

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Other guarantees

The Company, including certain of its subsidiaries, has granted irrevocable standby letters of credit and surety and other bonds, issued by highly rated financial institutions, to third parties to indemnify them in the event the Company does not perform its contractual obligations. As at June 30, 2006, the maximum potential liability under these guarantees was $468 million of which $373 million was for workers compensation and other employee benefits and $95 million was for equipment under leases and other. The Company has granted guarantees for which no liability has been recorded, as they relate to the Companys future performance.

As at June 30, 2006, the Company had not recorded any additional liability with respect to these guarantees, as the Company does not expect to make any additional payments associated with these guarantees. The majority of the guarantee instruments mature at various dates between 2006 and 2010.

CN Pension Plan, CN 1935 Pension Plan and BC Rail Ltd Pension Plan

The Company has indemnified and held harmless the current trustee and the former trustee of the Canadian National Railways Pension Trust Funds, the trustee of the BC Rail Ltd Pension Trust Fund, and the respective officers, directors, employees and agents of such trustees, from any and all taxes, claims, liabilities, damages, costs and expenses arising out of the performance of their obligations under the relevant trust agreements and trust deeds, including in respect of their reliance on authorized instructions of the Company or for failing to act in the absence of authorized instructions. These indemnifications survive the termination of such agreements or trust deeds. As at June 30, 2006, the Company had not recorded a liability associated with these indemnifications, as the Company does not expect to make any payments pertaining to these indemnifications.

General indemnifications

In the normal course of business, the Company has provided indemnifications, customary for the type of transaction or for the railway business, in various agreements with third parties, including indemnification provisions where the Company would be required to indemnify third parties and others. Indemnifications are found in various types of contracts with third parties which include, but are not limited to, (a) contracts granting the Company the right to use or enter upon property owned by third parties such as leases, easements, trackage rights and sidetrack agreements; (b) contracts granting rights to others to use the Companys property, such as leases, licenses and easements; (c) contracts for the sale of assets and securitization of accounts receivable; (d) contracts for the acquisition of services; (e) financing agreements; (f) trust indentures, fiscal agency agreements, underwriting agreements or similar agreements relating to debt or equity securities of the Company and engagement agreements with financial advisors; (g) transfer agent and registrar agreements in respect of the Companys securities; (h) trust and other agreements relating to pension plans and other plans, including those establishing trust funds to secure payment to certain officers and senior employees of special retirement compensation arrangements; (i) pension transfer agreements; (j) master agreements with financial institutions governing derivative transactions; and (k) settlement agreements with insurance companies or other third parties whereby such insurer or third party has been indemnified for any present or future claims relating to insurance policies, incidents or events covered by the settlement agreements. To the extent of any actual claims under these agreements, the Company maintains provisions for such items, which it considers to be adequate. Due to the nature of the indemnification clauses, the maximum exposure for future payments may be material. However, such exposure cannot be determined with certainty.

The Company has entered into various indemnification contracts with third parties for which the maximum exposure for future payments cannot be determined with certainty. As a result, the Company was unable to determine the fair value of these guarantees and accordingly, no liability was recorded. As at June 30, 2006, the carrying value for guarantees for which the Company was able to determine the fair value, was $1 million. There are no recourse provisions to recover any amounts from third parties.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(U.S. GAAP)*

Note 8 Earnings per share

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

	Three months ended June 30		Six months ended June 30	
In millions, except per share data	**2006**	2005	**2006**	2005
		(Unaudited)		
Net income	**$ 729**	$ 416	**$ 1,091**	$ 715
Weighted-average shares outstanding	**529.9**	556.1	**533.0**	559.9
Effect of stock options	**8.6**	9.9	**8.8**	10.5
Weighted-average diluted shares outstanding	**538.5**	566.0	**541.8**	570.4
Basic earnings per share	**$ 1.38**	$ 0.75	**$ 2.05**	$ 1.28
Diluted earnings per share	**$ 1.35**	$ 0.73	**$ 2.01**	$ 1.25

Note 9 Common stock split

On January 24, 2006, the Board of Directors of the Company approved a two-for-one common stock split which was effected in the form of a stock dividend of one additional common share of CN payable for each share held. The stock dividend was paid on February 28, 2006, to shareholders of record on February 22, 2006. All equity-based benefit plans and the current share repurchase program were adjusted to reflect the issuance of additional shares or options due to the stock split. All share and per share data has been adjusted to reflect the stock split.

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SELECTED RAILROAD STATISTICS *(U.S. GAAP)*

	Three months ended June 30		Six months ended June 30	
	2006	2005	**2006**	2005
	(Unaudited)			
Statistical operating data				
Freight revenues ($ millions)	**1,851**	1,744	**3,632**	3,386
Gross ton miles (GTM) (millions)	**89,454**	86,206	**175,685**	170,682
Revenue ton miles (RTM) (millions)	**46,917**	44,757	**92,578**	89,678
Carloads (thousands)	**1,246**	1,225	**2,437**	2,417
Route miles (includes Canada and the U.S.)	**19,908**	19,221	**19,908**	19,221
Employees (end of period)	**21,790**	22,462	**21,790**	22,462
Employees (average during period)	**21,797**	22,519	**21,659**	22,444
Productivity				
Operating ratio (%)	**58.6**	61.2	**62.3**	65.0
Freight revenue per RTM (cents)	**3.95**	3.90	**3.92**	3.78
Freight revenue per carload ($)	**1,486**	1,424	**1,490**	1,401
Operating expenses per GTM (cents)	**1.28**	1.31	**1.35**	1.35
Labor and fringe benefits expense per GTM (cents)	**0.48**	0.51	**0.52**	0.55
GTMs per average number of employees (thousands)	**4,104**	3,828	**8,111**	7,605
Diesel fuel consumed (U.S. gallons in millions)	**100**	102	**204**	206
Average fuel price ($/U.S. gallon) (1)	**2.17**	1.66	**2.02**	1.60
GTMs per U.S. gallon of fuel consumed	**895**	845	**861**	829
Safety indicators				
Injury frequency rate per 200,000 person hours	**1.9**	2.1	**2.1**	2.3
Accident rate per million train miles	**2.5**	1.6	**2.0**	1.4
Financial ratios				
Debt to total capitalization ratio (% at end of period)	**37.0**	35.6	**37.0**	35.6

(1) Includes the impact of the Company's fuel hedging program.

Certain statistical data and related productivity measures are based on estimated data available at such time and are subject to change as more complete information becomes available. As such, certain comparative data have been restated to reflect changes to estimated data previously reported.

CANADIAN NATIONAL RAILWAY COMPANY

SUPPLEMENTARY INFORMATION *(U.S. GAAP)*

	Three months ended June 30			Six months ended June 30		
	2006	2005	Variance Fav (Unfav)	**2006**	2005	Variance Fav (Unfav)
			(Unaudited)			
Revenue ton miles (millions)						
Petroleum and chemicals	**7,762**	7,617	2%	**15,889**	15,675	1%
Metals and minerals	**4,533**	4,104	10%	**8,830**	8,386	5%
Forest products	**10,859**	10,833	-	**21,565**	21,073	2%
Coal	**3,762**	3,803	(1%)	**7,018**	7,213	(3%)
Grain and fertilizers	**10,753**	9,360	15%	**21,466**	19,728	9%
Intermodal	**8,440**	8,199	3%	**16,198**	15,962	1%
Automotive	**808**	841	(4%)	**1,612**	1,641	(2%)
	46,917	44,757	5%	**92,578**	89,678	3%
Freight revenue / RTM (cents)						
Total freight revenue per RTM	**3.95**	3.90	1%	**3.92**	3.78	4%
Commodity groups:						
Petroleum and chemicals	**3.63**	3.56	2%	**3.61**	3.48	4%
Metals and minerals	**5.05**	5.21	(3%)	**5.01**	4.92	2%
Forest products	**4.09**	4.15	(1%)	**4.09**	4.05	1%
Coal	**2.63**	2.55	3%	**2.65**	2.44	9%
Grain and fertilizers	**2.80**	2.78	1%	**2.79**	2.72	3%
Intermodal	**4.32**	3.82	13%	**4.24**	3.76	13%
Automotive	**16.21**	16.53	(2%)	**16.32**	15.90	3%
Carloads (thousands)						
Petroleum and chemicals	**143**	148	(3%)	**293**	302	(3%)
Metals and minerals	**273**	254	7%	**508**	489	4%
Forest products	**171**	182	(6%)	**348**	363	(4%)
Coal	**108**	120	(10%)	**218**	232	(6%)
Grain and fertilizers	**146**	134	9%	**287**	278	3%
Intermodal	**338**	312	8%	**646**	606	7%
Automotive	**67**	75	(11%)	**137**	147	(7%)
	1,246	1,225	2%	**2,437**	2,417	1%

Freight revenue / carload (dollars)						
Total freight revenue per carload	**1,486**	1,424	4%	**1,490**	1,401	6%
Commodity groups:						
Petroleum and chemicals	**1,972**	1,831	8%	**1,959**	1,808	8%
Metals and minerals	**839**	843	-	**870**	845	3%
Forest products	**2,596**	2,473	5%	**2,534**	2,353	8%
Coal	**917**	808	13%	**853**	759	12%
Grain and fertilizers	**2,062**	1,940	6%	**2,087**	1,928	8%
Intermodal	**1,080**	1,003	8%	**1,062**	990	7%
Automotive	**1,955**	1,853	6%	**1,920**	1,776	8%

Such statistical data and related productivity measures are based on estimated data available at such time and are subject to change as more complete information becomes available. As such, certain comparative data have been restated to reflect changes to estimated data previously reported.

CANADIAN NATIONAL RAILWAY COMPANY

NON-GAAP MEASURES - unaudited

Adjusted performance measures

In the second quarter of 2006, the Company reported adjusted net income of $479 million, or $0.89 per diluted share, excluding the impact of a deferred income tax recovery of $250 million ($0.46 per diluted share) that resulted primarily from the enactment of lower federal and provincial corporate tax rates in Canada. Management believes that adjusted net income and adjusted earnings per share are useful measures of performance that can facilitate period-to-period comparisons, as they exclude an item, such as a deferred income tax recovery, that does not necessarily arise as part of the normal day-to-day operations of the Company and could distort the analysis of trends in business performance. The exclusion of such item in adjusted net income and adjusted earnings per share does not, however, imply that such item is necessarily non-recurring. These adjusted measures do not have any standardized meaning prescribed by GAAP and may, therefore, not be comparable to similar measures presented by other companies. The reader is advised to read all information provided in the Company's Interim Consolidated Financial Statements and Notes thereto. The following table provides a reconciliation of net income and earnings per share, as reported for the second quarter and first half of 2006, to the adjusted performance measures presented herein.

	Three months ended June 30, 2006			**Six months ended June 30, 2006**		
In millions, except per share data	**Reported**	**Rate enactments**	**Adjusted**	**Reported**	**Rate enactments**	**Adjusted**
Revenues	$ 1,946	$ -	$ 1,946	$ 3,793	$ -	$ 3,793
Operating expenses	1,141	-	1,141	2,363	-	2,363
Operating income	805	-	805	1,430	-	1,430
Interest expense	(75)	-	(75)	(150)	-	(150)
Other loss	(5)	-	(5)	(6)	-	(6)
Income before income taxes	725	-	725	1,274	-	1,274
Income tax recovery (expense)	4	(250)	(246)	(183)	(250)	(433)
Net income	**$ 729**	**$ (250)**	**$ 479**	**$ 1,091**	**$ (250)**	**$ 841**
Basic earnings per share	**$ 1.38**	**$ (0.48)**	**$ 0.90**	**$ 2.05**	**$ (0.48)**	**$ 1.57**
Diluted earnings per share	**$ 1.35**	**$ (0.46)**	**$ 0.89**	**$ 2.01**	**$ (0.46)**	**$ 1.55**

Free cash flow

The Company believes that free cash flow is a useful measure of performance as it demonstrates the Company's ability to generate cash after the payment of capital expenditures and dividends. Free cash flow does not have any standardized meaning prescribed by GAAP and may, therefore, not be comparable to similar measures presented by other companies. The Company defines free cash flow as cash provided from operating activities, excluding changes in the level of accounts receivable sold under the securitization program, less investing activities, and after the payment of dividends, calculated as follows:

	Three months ended June 30		**Six months ended June 30**	
In millions	**2006**	2005	**2006**	2005
Cash provided from operating activities	**$ 405**	$ 785	**$ 1,024**	$ 1,368
Less:				
Investing activities	**(278)**	(249)	**(487)**	(398)
Cash provided before financing activities	**127**	536	**537**	970
Adjustments:				
Change in level of accounts receivable sold	**380**	10	**375**	(43)
Dividends paid	**(85)**	(69)	**(172)**	(140)
Free cash flow	**$ 422**	$ 477	**$ 740**	$ 787

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Item 3

CANADIAN NATIONAL RAILWAY COMPANY

MANAGEMENTS DISCUSSION AND ANALYSIS *(U.S. GAAP)*

Managements discussion and analysis (MD&A) relates to the financial condition and results of operations of Canadian National Railway Company (CN) together with its wholly owned subsidiaries. As used herein, the word Company means, as the context requires, CN and its subsidiaries. CNs common shares are listed on the Toronto and New York stock exchanges. Except where otherwise indicated, all financial information reflected herein is expressed in Canadian dollars and determined on the basis of United States generally accepted accounting principles (U.S. GAAP). The Companys objective is to provide meaningful and relevant information reflecting the Companys financial condition and results of operations. In certain instances, the Company may make reference to certain non-GAAP measures that, from managements perspective, are useful measures of performance. The reader is advised to read all information provided in the MD&A in conjunction with the Companys 2006 Interim Consolidated Financial Statements and Notes thereto, as well as the 2005 Annual MD&A.

Business profile

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

CNs freight revenues are derived from seven commodity groups representing a diversified and balanced portfolio of goods transported between diverse origins and destinations. This product and geographic diversity positions the Company well to face economic fluctuations and enhances its potential for growth opportunities. In 2005, no individual commodity group accounted for more than 24% of revenues. From a geographic standpoint, 22% of CNs revenues in 2005 came from U.S. domestic traffic, 33% from transborder traffic, 24% from Canadian domestic traffic and 21% from overseas traffic. The Company originates approximately 88% of traffic moving along its network, which allows it both to capitalize on service advantages and build on opportunities to efficiently use assets.

Corporate organization

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

See Note 16 Segmented information, to the Companys 2005 Annual Consolidated Financial Statements for additional information on the Companys corporate organization, as well as selected financial information by geographic area.

Strategy overview

CNs goal is to remain at the forefront of the rail industry and its challenge is to be regarded as the continents best-performing transportation company.

CN is committed to creating value for both its customers and shareholders. By providing quality and cost-effective service, CN seeks to create value for its customers, which solidifies existing customer relationships, while enabling it to pursue new ones. Sustainable financial performance is a critical element of shareholder value, which CN strives to achieve by pursuing revenue growth, steadily increasing profitability, solid free cash flow generation and an adequate return on investment. CN has a unique business model, which is anchored on five core values: providing good service, controlling costs, focusing on asset utilization, committing to safety and developing employees.

CANADIAN NATIONAL RAILWAY COMPANY

MANAGEMENTS DISCUSSION AND ANALYSIS *(U.S. GAAP)*

The scheduled railroad is the foundation for the Companys business model. For CNs merchandise business, the scheduled railroad, which is defined as a trip plan for every car measured in hours, has reduced transit times, improved the consistency of CNs transportation product, dramatically improved productivity and helped to improve network capacity. In 2003, the Company began to apply the same principles of scheduled railroading to its intermodal business through the Intermodal Excellence (IMX) initiative. IMX is designed to smooth demand and balance the flow of intermodal traffic through pre-defined daily train capacity, slot, gate and equipment reservations, and day-of-the-week pricing. In early 2005, the Company began applying the additional principles learned from IMX to its carload business, launching Carload Excellence (CX), in order to improve asset utilization and optimize capacity. Scheduled railroading has now evolved into precision railroading, in which the focus has become the precise execution of the trip plan.

CNs acquisition and control of Illinois Central and Wisconsin Central, in 1999 and 2001, respectively, extended the Companys reach into the central and southern United States. Among the benefits of single-line service afforded by these transactions are improved transit and cycle times for freight cars and the penetration of new markets.

The acquisition of the railroads and related holdings of Great Lakes Transportation LLC (GLT) in May 2004 has permitted new efficiencies in train operations north of Duluth/Superior in the key Winnipeg-Chicago corridor and positioned CN as a major player in the supply chain for the steel industry in the United States. The purchase of BC Rail in July 2004 not only added to CNs forest products business substantially, but also expanded the railroads capacity in British Columbia.

In 2006, the Company plans to spend approximately $1,550 million on capital programs. Of this, more than $1,000 million is targeted for rail infrastructure integrity and safety maintenance, including rail, tie, ballast, and other track material replacements, as well as bridges and signaling systems upgrades. This allotment also includes strategic initiatives, such as siding extensions in western Canada; the reconfiguration of Johnston Yard in Memphis, Tennessee for increased network fluidity and efficiency; and investments in the Companys Prince Rupert, B.C. corridor, to capitalize on the Port of Prince Ruperts potential as an important traffic gateway between Asia and the North American heartland.

The remaining $500 million is targeted for equipment expenditures, including new locomotive and car purchases, plus existing fleet refurbishments; as well as for facilities, information technology and other projects. These will enable the Company to tap new growth opportunities and improve overall efficiency.

The Company strives to offer transportation services that deliver value to its customers. It does so with the belief that better service benefits customers while improving CNs yields, operating efficiency and earnings. The Company foresees a number of business-growth opportunities. In the intermodal area, there is growth potential in international markets because of increasing North American-Asian container trade, as well as the projected 2007 opening of the Prince Rupert container terminal. In the bulk area, western Canadian growth prospects are enhanced by continued coal mine expansion. In merchandise, the Company sees growth potential for a number of commodities, particularly lumber and metals, and commodities associated with oil and gas developments in Western Canada. The Companys business prospects are based on the continuation of positive economic trends in North America and Asia.

The Company foresees improvements in productivity, particularly in yards and terminals. The Company also intends to pursue further operating efficiencies by continuing to improve labor productivity and to focus on reducing accidents and related costs, legal claims and health care costs. The Company partners with connecting carriers to implement routing protocol agreements and pursues co-production initiatives to further improve service and generally reduce costs.

All forward-looking information provided in this section is based on assumptions about events and developments that may not materialize or that may be offset entirely or partially by other events and developments. See the

Business risks section of this MD&A for a discussion of assumptions and other factors affecting such forward-looking statements.

CANADIAN NATIONAL RAILWAY COMPANY

MANAGEMENT S DISCUSSION AND ANALYSIS *(U.S. GAAP)*

Financial and statistical highlights	**Three months ended June 30**		**Six months ended June 30**	
$ in millions, except per share data, or unless otherwise indicated	**2006**	2005	**2006**	2005
		(Unaudited)		
Financial results				
Revenues	**$ 1,946**	$ 1,838	**$ 3,793**	$ 3,544
Operating income	**$ 805**	$ 713	**$ 1,430**	$ 1,239
Net income (1)	**$ 729**	$ 416	**$ 1,091**	$ 715
Operating ratio	**58.6%**	61.2%	**62.3%**	65.0%
Basic earnings per share (1)	**$ 1.38**	$ 0.75	**$ 2.05**	$ 1.28
Diluted earnings per share (1)	**$ 1.35**	$ 0.73	**$ 2.01**	$ 1.25
Dividend declared per share	**$ 0.1625**	$ 0.1250	**$ 0.3250**	$ 0.2500
Financial position				
Total assets	**$ 22,482**	$ 22,439	**$ 22,482**	$ 22,439
Total long-term financial liabilities	**$ 11,533**	$ 11,443	**$ 11,533**	$ 11,443
Statistical operating data and productivity measures				
Employees (*average during period*)	**21,797**	22,519	**21,659**	22,444
Gross ton miles (GTM) per average number of employees (*thousands*)	**4,104**	3,828	**8,111**	7,605
GTMs per U.S. gallon of fuel consumed	**895**	845	**861**	829

(1) *The 2006 figures include a deferred income tax recovery of $250 million ($0.48 per basic share or $0.46 per diluted share), resulting primarily from the enactment of lower federal and provincial corporate tax rates in Canada.*

Financial results

Second quarter and first half of 2006 compared to corresponding periods in 2005

Second quarter 2006 net income increased by $313 million, or 75%, to $729 million, when compared to the same period in 2005, with diluted earnings per share rising 85%, to $1.35, which includes a deferred income tax recovery of $250 million ($0.46 per diluted share), resulting primarily from the enactment of lower federal and provincial corporate tax rates in Canada. Revenues for the second quarter increased by $108 million, or 6%, to $1,946 million, mainly due to freight rate increases and volume growth, particularly for grain and intermodal, which were partly offset by the translation impact of the stronger Canadian dollar on U.S. dollar-denominated revenues. Operating expenses for the three months ended June 30, 2006 increased by $16 million, or 1%, to $1,141 million, mainly due to increased fuel costs, purchased services and material expense, and depreciation. Partly offsetting these factors was the translation impact of the stronger Canadian dollar on U.S. dollar-denominated expenses, lower U.S. personal injury expense and equipment rents. The operating ratio, defined as operating expenses as a percentage of revenues, was 58.6% in the current quarter compared to 61.2% in the second quarter of 2005, a 2.6-point improvement.

Net income for the six months ended June 30, 2006 increased by $376 million, or 53%, to $1,091 million, when compared to the same period in 2005, with diluted earnings per share rising 61%, to $2.01, which includes the deferred income tax recovery as explained herein. Revenues for the first half of 2006 increased by $249 million, or 7%, to $3,793 million, mainly due to freight rate increases and volume growth, particularly for grain and intermodal, which were partly offset by the translation impact of the stronger Canadian dollar on U.S. dollar-denominated revenues. For the first half of 2006, operating expenses increased by $58 million, or 3%, to $2,363 million, mainly due to increased fuel costs, purchased services and material expenses, and depreciation. Partly offsetting these factors was the translation impact of the stronger Canadian dollar on U.S. dollar-denominated expenses, lower U.S. personal injury expense and equipment rents. The six-month operating ratio was 62.3% compared to 65.0%, a 2.7-point improvement.

Foreign exchange fluctuations have had an impact on the comparability of the results of operations. The continued appreciation in the Canadian dollar relative to the U.S. dollar, which has affected the conversion of the Company's U.S. dollar-denominated revenues and expenses, has resulted in a reduction to net income of approximately $25 million in the second quarter, and approximately $35 million in the first half of 2006.

CANADIAN NATIONAL RAILWAY COMPANY

MANAGEMENT’S DISCUSSION AND ANALYSIS *(U.S. GAAP)*

Revenues

	Three months ended June 30			Six months ended June 30		
	2006	2005	%Δ	**2006**	2005	%Δ
Total revenues *(millions)*	**$ 1,946**	$ 1,838	6%	**$ 3,793**	$ 3,544	7%
Rail freight:						
Revenues *(millions)*	**$ 1,851**	$ 1,744	6%	**$ 3,632**	$ 3,386	7%
RTMs *(millions)*	**46,917**	44,757	5%	**92,578**	89,678	3%
Revenue/RTM *(cents)*	**3.95**	3.90	1%	**3.92**	3.78	4%

Revenues for the quarter ended June 30, 2006 totaled $1,946 million compared to $1,838 million during the same period in 2005, an increase of $108 million, or 6%. Revenues for the first half of 2006 were $3,793 million, an increase of $249 million, or 7%, from the same period last year. The increases in both the second quarter and first half of the year were mainly due to freight rate increases of approximately $159 million and $292 million, respectively, of which approximately 40% was due to a higher fuel surcharge that mainly resulted from increases in crude oil prices; and volume growth, particularly for grain and intermodal. Partly offsetting these gains was the translation impact of the stronger Canadian dollar on U.S. dollar-denominated revenues of $100 million in the second quarter, and $155 million in the first half of 2006.

Revenue ton miles (RTMs), measuring the volume of rail freight transported by the Company, increased by 5% in the second quarter and 3% in the first half of 2006 when compared to the same periods in 2005. For the second quarter and first half of the year, freight revenue per revenue ton mile, a measurement of yield defined as revenue earned on the movement of a ton of freight over one mile, increased by 1% and 4%, respectively, when compared to the same periods last year, largely due to freight rate increases.

Petroleum and chemicals

	Three months ended June 30			Six months ended June 30		
	2006	2005	%Δ	**2006**	2005	%Δ
Revenues *(millions)*	**$ 282**	$ 271	4%	**$ 574**	$ 546	5%
RTMs *(millions)*	**7,762**	7,617	2%	**15,889**	15,675	1%
Revenue/RTM *(cents)*	**3.63**	3.56	2%	**3.61**	3.48	4%

Petroleum and chemicals comprises a wide range of commodities, including chemicals, sulfur, plastics, petroleum and natural gas products. Although offshore markets have been growing strongly, the primary markets for these commodities are still within North America. As such, the performance of this commodity group is closely correlated with the North American economy. Most of the Company’s petroleum and chemicals shipments originate in the Louisiana petrochemical corridor between New Orleans and Baton Rouge; in northern Alberta, which is a major center for natural gas, feedstock, and world scale petrochemicals and plastics complex derivatives; and in eastern Canadian regional plants. These shipments are destined for customers in Canada, the United States and overseas.

Revenues for this commodity group increased by $11 million, or 4%, for the second quarter and $28 million, or 5%, for the first six months of 2006 when compared to the same periods in 2005. Both the second quarter and first half of 2006 benefited from freight rate increases and overall improvements in traffic mix. These gains were partly offset by the translation impact of the stronger Canadian dollar; soft market conditions for liquefied petroleum gases due to warmer than average weather, particularly in the first quarter; reduced chloralkali shipments due to shipper labor issues and weakness in some end-markets; and lower petroleum products shipments as a result of a temporary refinery shutdown. The revenue per revenue ton mile increase of 2% in the second quarter and 4% in the first half of 2006, was mainly due to freight rate increases that were partly offset by the translation impact of the stronger Canadian dollar and an increase in the average length of haul.

CANADIAN NATIONAL RAILWAY COMPANY

MANAGEMENT S DISCUSSION AND ANALYSIS *(U.S. GAAP)*

Metals and minerals

	Three months ended June 30			Six months ended June 30		
	2006	2005	%Δ	**2006**	2005	%Δ
Revenues *(millions)*	**$ 229**	$ 214	7%	**$ 442**	$ 413	7%
RTMs *(millions)*	**4,533**	4,104	10%	**8,830**	8,386	5%
Revenue/RTM *(cents)*	**5.05**	5.21	(3%)	**5.01**	4.92	2%

The metals and minerals commodity group consists primarily of nonferrous base metals, iron ore, steel, equipment and parts and construction materials. The Company s unique rail access to major mines, ports and smelters throughout North America has made the Company a transportation leader of copper, lead, zinc concentrates, iron ore, refined metals and aluminum. Construction materials are mainly aggregates (stone and sand) and cement. The Company has access to major cement producers and aggregate mines in Canada as well as in the U.S. Metals and minerals traffic is sensitive to fluctuations in the economy. Revenues for this commodity group increased by $15 million, or 7%, for the second quarter and $29 million, or 7%, for the first six months of 2006 when compared to the same periods in 2005. The increases in both the second quarter and first half of 2006 were mainly due to freight rate increases; increased volumes of U.S. iron ore for steel production, particularly in the second quarter; and strong shipments of Canadian long steel products (primarily pipes) and machinery and dimensional loads. Partly offsetting the gains for both the second quarter and first six months of 2006 was the translation impact of the stronger Canadian dollar and reduced shipments of nonferrous commodities. Revenue per revenue ton mile decreased by 3% in the current quarter, mainly due to the translation impact of the stronger Canadian dollar and an increase in the average length of haul. For the first six months of 2006, revenue per revenue ton mile increased by 2%, mainly due to freight rate increases that were partly offset by the translation impact of the stronger Canadian dollar.

Forest products

	Three months ended June 30			Six months ended June 30		
	2006	2005	%Δ	**2006**	2005	%Δ
Revenues *(millions)*	**$ 444**	$ 450	(1%)	**$ 882**	$ 854	3%
RTMs *(millions)*	**10,859**	10,833	-	**21,565**	21,073	2%
Revenue/RTM *(cents)*	**4.09**	4.15	(1%)	**4.09**	4.05	1%

The forest products commodity group includes various types of lumber, panels, wood chips, wood pulp, printing paper, linerboard and newsprint. The Company has superior rail access to the western and eastern Canadian fiber-producing regions, which are among the largest fiber source areas in North America. In the United States, the Company is strategically located to serve both the Midwest and southern U.S. corridors with interline capabilities to other Class I railroads. The key drivers for the various commodities are: for newsprint, advertising lineage and overall economic conditions, primarily in the United States; for fibers (mainly wood pulp), the consumption of paper worldwide; and for lumber and panels, housing starts and renovation activities in the United States. Although demand for forest products can be cyclical, the Company's geographical advantages and product diversity tend to reduce the impact of market fluctuations. Revenues for this commodity group decreased by $6 million, or 1%, for the second quarter and increased by $28 million, or 3%, for the first six months of 2006 when compared to the same periods in 2005. The decrease in the second quarter was driven mainly by the translation impact of the stronger Canadian dollar and a reduction in pulp and paper shipments due to continued weak market conditions. This was partially offset by freight rate increases, improvements in traffic mix and increased lumber shipments originating from western Canada. The increase in the first six months of 2006 was driven mainly by freight rate increases and increased lumber shipments originating from western Canada. Partly offsetting these gains were the translation impact of the stronger Canadian dollar and a reduction in pulp and paper shipments due to continued weak market conditions. The revenue per revenue ton mile decrease of 1% in the second quarter was mainly due to the translation impact of the stronger Canadian dollar. The revenue per revenue ton mile increase of 1% in the first half of 2006 was mainly due to freight rate increases.

CANADIAN NATIONAL RAILWAY COMPANY

MANAGEMENT□S DISCUSSION AND ANALYSIS *(U.S. GAAP)*

Coal

	Three months ended June 30			Six months ended June 30		
	2006	2005	%Δ	**2006**	2005	%Δ
Revenues *(millions)*	**$ 99**	$ 97	2%	**$ 186**	$ 176	6%
RTMs *(millions)*	**3,762**	3,803	(1%)	**7,018**	7,213	(3%)
Revenue/RTM *(cents)*	**2.63**	2.55	3%	**2.65**	2.44	9%

The coal commodity group consists primarily of thermal grades of bituminous coal. Canadian thermal coal is delivered to power utilities primarily in eastern Canada, while in the United States, thermal coal is transported from mines served in southern Illinois, or from western U.S. mines via interchange with other railroads, to major utilities in the Midwest and southeast United States. The coal business also includes the transport of Canadian metallurgical coal, which is largely exported to Asian steel producers. The strong global market for metallurgical coal facilitated the opening of three mines along the Company□s network in late 2004. The renewed strength in this market, which began in 2004, is expected to continue as strong Asian demand for metallurgical coal drives increased Canadian production. Revenues for this commodity group increased by $2 million, or 2%, for the second quarter and $10 million, or 6%, for the first six months of 2006 when compared to the same periods in 2005. The increases were mainly due to the expansion of metallurgical coal mines in western Canada and freight rate increases. Partly offsetting these gains was the translation impact of the stronger Canadian dollar, a decline in CN shipments originating from U.S. coal mines and the loss of export shipments of petroleum coke due to adverse market conditions. The revenue per revenue ton mile increase of 3% in the second quarter and 9% in the first half of 2006 was mainly due to freight rate increases, which were partly offset by the translation impact of the stronger Canadian dollar and an increase in the average length of haul.

Grain and fertilizers

	Three months ended June 30			Six months ended June 30		
	2006	2005	%Δ	**2006**	2005	%Δ
Revenues *(millions)*	**$ 301**	$ 260	16%	**$ 599**	$ 536	12%
RTMs *(millions)*	**10,753**	9,360	15%	**21,466**	19,728	9%
Revenue/RTM *(cents)*	**2.80**	2.78	1%	**2.79**	2.72	3%

The grain and fertilizers commodity group depends primarily on crops grown and fertilizers processed in western Canada and the U.S. Midwest. The grain segment consists of three primary commodities: food grains, mainly wheat; oilseeds and oilseed products, primarily canola seed, oil and meal; and feed grains, including feed barley, feed wheat and corn. Production of grain varies considerably from year to year, affected primarily by weather conditions. Grain exports are sensitive to the size and quality of the crop produced, international market conditions and foreign government policy. The majority of grain produced in western Canada and moved by CN is exported via the ports of Vancouver, Prince Rupert and Thunder Bay. Certain of these rail movements are subject to government regulation and to a □revenue cap,□ which effectively establishes a maximum revenue entitlement that railways can earn. In the U.S., grain grown in Illinois and Iowa is exported, as well as transported to domestic processing facilities and feed markets. The Company also serves major producers of potash in Canada, as well as producers of ammonium nitrate, urea and other fertilizers across Canada and the U.S. Revenues for this commodity group increased by $41 million, or 16%, for the second quarter and $63 million, or 12%, for the first six months of 2006 when compared to the same periods in 2005. The increase in the second quarter was mainly due to freight rate increases and higher shipments to export markets of Canadian wheat, U.S. corn, and Canadian canola and canola meal. These gains were partly offset by the translation impact of the stronger Canadian dollar and decreased shipments of potash and other fertilizers due to soft market conditions. The increase in the first six months of 2006 was mainly driven by freight rate increases and higher shipments to export markets of U.S. corn, Canadian canola, canola meal and wheat. Partly offsetting these gains was the translation impact of the Canadian dollar and decreased shipments of potash and other fertilizers due to soft market conditions. Revenue per revenue ton mile increased by 1% in the second quarter and 3% in the first half of 2006, largely due to freight rate increases that were partly offset by the translation impact of the stronger Canadian dollar and an increase in the average length of haul.

CANADIAN NATIONAL RAILWAY COMPANY

MANAGEMENT□S DISCUSSION AND ANALYSIS *(U.S. GAAP)*

Intermodal

	Three months ended June 30			Six months ended June 30		
	2006	2005	%Δ	**2006**	2005	%Δ
Revenues *(millions)*	**$ 365**	$ 313	17%	**$ 686**	$ 600	14%
RTMs *(millions)*	**8,440**	8,199	3%	**16,198**	15,962	1%
Revenue/RTM *(cents)*	**4.32**	3.82	13%	**4.24**	3.76	13%

The intermodal commodity group is comprised of two segments: domestic and international. The domestic segment is responsible for consumer products and manufactured goods, operating through both retail and wholesale channels while the international segment handles import and export container traffic, directly serving the major ports of Vancouver, Montreal, Halifax and New Orleans. The domestic segment is driven by consumer markets, with growth generally tied to the economy. The international segment is driven by North American economic and trade conditions. Revenues for this commodity group increased by $52 million, or 17%, for the second quarter and $86 million, or 14%, for the first six months of 2006 when compared to the same periods in 2005. The increases were mainly due to freight rate increases; growth in international container traffic, primarily from Asia; an improvement in traffic mix and increased transborder and domestic movements. Partly offsetting these gains was the translation impact of the stronger Canadian dollar. The revenue per revenue ton mile increase of 13% in both the second quarter and first half of 2006 was largely due to freight rate increases and a positive change in traffic mix, which were partly offset by the translation impact of the stronger Canadian dollar.

Automotive

	Three months ended June 30			Six months ended June 30		
	2006	2005	%Δ	**2006**	2005	%Δ
Revenues *(millions)*	**$ 131**	$ 139	(6%)	**$ 263**	$ 261	1%
RTMs *(millions)*	**808**	841	(4%)	**1,612**	1,641	(2%)
Revenue/RTM *(cents)*	**16.21**	16.53	(2%)	**16.32**	15.90	3%

The automotive commodity group moves both finished vehicles and parts, originating in southern Ontario, Michigan and Mississippi, and destined for the United States, Canada and Mexico. The Company□s broad coverage, including its access to all of the Canadian assembly plants, enables it to consolidate full trainloads of automotive traffic for delivery to connecting railroads at key interchange points. The Company also serves shippers of import vehicles via the ports of Halifax and Vancouver, and through interchange with other railroads. The Company□s automotive revenues are closely correlated to automotive production and sales in North America. Revenues for this commodity group decreased by $8 million, or 6%, for the second quarter and increased by $2 million, or 1%, for the first six months of 2006 when compared to the same periods in 2005. The decrease in the second quarter was driven mainly by reduced shipments from domestic producers mainly due to production slowdowns and the translation impact of the stronger Canadian dollar, that were partly offset by freight rate increases and higher shipments of import vehicles via CN-served ports. For the first six months of 2006, the increase was mainly due to freight rate increases and increased shipments of import vehicles that were partly offset by the translation impact of the Canadian dollar and reduced shipments from domestic producers mainly due to production slowdowns.

Revenue per revenue ton mile decreased by 2% for the second quarter, driven mainly by the translation impact of the stronger Canadian dollar and an increase in the average length of haul that were mostly offset by freight rates increases. Revenue per revenue ton mile increased by 3% for the first half of 2006, largely due to freight rate increases, which were mostly offset by the translation impact of the stronger Canadian dollar and an increase in the average length of haul.

Other

Other revenues increased by $1 million, or 1%, for the second quarter compared to the same period in 2005. For the first six months of 2006, other revenues increased by $3 million, or 2%, when compared to the same period in 2005, mainly due to increased interswitching and commuter traffic revenues.

CANADIAN NATIONAL RAILWAY COMPANY

MANAGEMENT□S DISCUSSION AND ANALYSIS *(U.S. GAAP)*

Operating expenses

In the second quarter of 2006, operating expenses amounted to $1,141 million compared to $1,125 million in the same quarter of 2005. Operating expenses for the first half of 2006 were $2,363 million compared to $2,305 million in the same period of 2005. The increase of $16 million, or 1%, in the second quarter and $58 million, or 3%, in the first half of 2006 were mainly due to increased fuel costs, purchased services and material expense and depreciation. Partly offsetting these factors was the translation impact of the stronger Canadian dollar on U.S. dollar-denominated expenses of $55 million in the second quarter and $90 million in the first half of 2006, lower U.S. personal injury expense and equipment rents.

	Three months ended June 30				Six months ended June 30			
In millions	**2006**		2005		**2006**		2005	
	Amount	**% of revenue**	Amount	% of revenue	**Amount**	**% of revenue**	Amount	% of revenue
Labor and fringe benefits	**$ 430**	**22.1%**	$ 436	23.7%	**$ 918**	**24.2%**	$ 935	26.4%
Purchased services and material	**203**	**10.4%**	196	10.7%	**418**	**11.0%**	402	11.3%
Depreciation and amortization	**162**	**8.3%**	158	8.6%	**326**	**8.6%**	314	8.9%
Fuel	**225**	**11.6%**	179	9.7%	**428**	**11.3%**	345	9.7%
Equipment rents	**38**	**1.9%**	53	2.9%	**85**	**2.2%**	100	2.8%
Casualty and other	**83**	**4.3%**	103	5.6%	**188**	**5.0%**	209	5.9%
Total	**$ 1,141**	**58.6%**	$ 1,125	61.2%	**$ 2,363**	**62.3%**	$ 2,305	65.0%

***Labor and fringe benefits*:** Labor and fringe benefits includes wages, payroll taxes, and employee benefits such as incentive compensation, stock-based compensation, health and welfare, pensions and other post-employment benefits. Certain incentive and stock-based compensation plans are based on financial and market performance targets and the related expense is recorded in relation to the attainment of such targets. Labor and fringe benefits expenses decreased by $6 million, or 1%, for the second quarter and $17 million, or 2%, for the first half of 2006 when compared to the same periods in 2005. The decreases in both the three- and six-month periods were mainly due to the translation impact of the stronger Canadian dollar, the impact of a reduced workforce as a result of synergies following the integration of the GLT and BC Rail acquisitions and ongoing productivity improvements. Also affecting the six-month period was an adjustment in the first quarter of 2005 to the workforce reduction provision for increased health care costs. Partly offsetting these factors were annual wage increases and an increase in net periodic benefit cost for pensions as a result of a decrease in the Company□s discount rate.

Purchased services and material: Purchased services and material primarily includes the costs of services purchased from outside contractors, materials used in the maintenance of the Company□s track, facilities and equipment, transportation and lodging for train crew employees, utility costs and the net costs of operating facilities jointly used by the Company and other railroads. These expenses increased by $7 million, or 4%, for the second quarter and $16 million, or 4%, for the first half of 2006 when compared to the same periods in 2005. The increases were primarily due to higher expenses for services, mainly due to increased prices, higher expenses for locomotive maintenance and lower income from joint facilities. Partly offsetting these factors was the translation impact of the stronger Canadian dollar.

Depreciation and amortization: Depreciation and amortization relates to the Company's rail operations. These expenses increased by $4 million, or 3%, for the second quarter and $12 million, or 4%, for the first half of 2006 when compared to the same periods in 2005. The increases were mainly due to the impact of net capital additions and higher depreciation rates for certain asset classes, which were partly offset by the translation impact of the stronger Canadian dollar.

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Fuel: Fuel expense includes the cost of fuel consumed by locomotives, intermodal equipment and other vehicles. These expenses increased by $46 million, or 26%, for the second quarter and $83 million, or 24%, for the first half of 2006 when compared to the same periods in 2005. The increases were mainly due to a higher average price per U.S. gallon of fuel, net of the benefits from CN□s fuel hedging program: 31% increase in the second quarter, from $1.66 in 2005 to $2.17 in 2006, and 26% increase in the first half, from $1.60 in 2005 to $2.02 in 2006. The increases were also due to higher volumes. Partly offsetting these factors were the translation impact of the stronger Canadian dollar and productivity improvements.

Equipment rents: Equipment rents includes rental expense for the use of freight cars owned by other railroads or private companies and for the short- or long-term lease of freight cars, locomotives and intermodal equipment, net of rental income from other railroads for the use of the Company□s cars and locomotives. These expenses decreased by $15 million, or 28%, for the second quarter and $15 million, or 15%, for the first half of 2006 when compared to the same periods in 2005. The decreases were mainly due to lower car lease expense.

Casualty and other**:** Casualty and other includes expenses for personal injuries, environmental, freight and property damage, insurance, bad debt and operating taxes, as well as travel and travel-related expenses. These expenses decreased by $20 million, or 19%, for the second quarter and $21 million, or 10%, for the first half of 2006 when compared to the same periods in 2005. The decreases were mainly due to a lower expense related to U.S. personal injuries following the latest actuarial valuation that was partly offset by higher derailment-related expenses, particularly late in the second quarter, higher operating taxes and increased Company sponsorships. Also partially offsetting the decrease in the six-month period were higher environmental expenses, particularly for site restoration.

Other

Interest expense: Interest expense decreased by $3 million for both the second quarter and first half of 2006 when compared to the same periods in 2005. The decreases were mainly due to the translation impact of the stronger Canadian dollar that was partly offset by interest on new debt issuances in 2006 and higher interest rates on commercial paper and other borrowings.

Other loss: Other loss for the second quarter of 2006 remained flat at $5 million when compared to the same period in 2005, as lower investment income was offset by realized foreign exchange gains. Other loss for the first half of 2006 was $6 million, compared to $9 million for the same period in 2005, a decrease of $3 million, which was mainly due to higher income from other business activities and realized foreign exchange gains that were partly offset by lower investment income.

Income tax recovery (expense): The Company recorded an income tax recovery of $4 million for the second quarter of 2006 compared to income tax expense of $214 million in the corresponding 2005 period. For the six-month period ended June 30, 2006, income tax expense was $183 million compared to $362 million for the same period in 2005. Included in both the second quarter and first half of 2006 was a deferred income tax recovery of $250 million, mainly due to the enactment of lower tax rates in Canada. Excluding this tax recovery, the effective tax rate for the second quarter and first half of 2006 was 33.9% and 34.0%, respectively. The effective tax rate for the second quarter and first half of 2005 was 34.0% and 33.6%, respectively.

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Summary of quarterly financial data - unaudited

In millions, except per share data

	2006 Quarters		2005 Quarters				2004 Quarters	
	Second	First	Fourth	Third	Second	First	Fourth	Third
Revenues	**$ 1,946**	$ 1,847	$ 1,886	$ 1,810	$ 1,838	$ 1,706	$ 1,736	$ 1,709
Operating income	**$ 805**	$ 625	$ 720	$ 665	$ 713	$ 526	$ 607	$ 591
Net income	**$ 729**	$ 362	$ 430	$ 411	$ 416	$ 299	$ 376	$ 346
Basic earnings per share	**$ 1.38**	$ 0.68	$ 0.80	$ 0.75	$ 0.75	$ 0.53	$ 0.66	$ 0.61
Diluted earnings per share	**$ 1.35**	$ 0.66	$ 0.78	$ 0.74	$ 0.73	$ 0.52	$ 0.65	$ 0.60
Dividend declared per share	**$ 0.1625**	$ 0.1625	$ 0.1250	$ 0.1250	$ 0.1250	$ 0.1250	$ 0.0975	$ 0.0975

Revenues generated by the Company during the year are influenced by seasonal weather conditions, general economic conditions, cyclical demand for rail transportation, and competitive forces in the transportation marketplace. Operating expenses reflect the impact of freight volumes, seasonal weather conditions, labor costs, fuel prices, and the Company□s productivity initiatives.

The Company□s quarterly results included items that affected the quarter-over-quarter comparability of the results of operations: the second quarter of 2006 included a deferred income tax recovery of $250 million ($0.48 per basic share or $0.46 per diluted share), mainly resulting from rate enactments as previously discussed; the Company□s results of operations for 2004 included BC Rail as of July 14, 2004; and the continued appreciation in the Canadian dollar relative to the U.S. dollar has impacted the conversion of the Company□s U.S. dollar-denominated revenues and expenses and resulted in varying reductions in net income in the rolling eight quarters presented above.

Liquidity and capital resources

The Company□s principal source of liquidity is cash generated from operations. The Company also has the ability to fund liquidity requirements through its revolving credit facility, the issuance of debt and/or equity, and the sale of a portion of its accounts receivable through a securitization program. In addition, from time to time, the Company□s liquidity requirements can be supplemented by the disposal of surplus properties and the monetization of assets.

Operating activities: Cash provided from operating activities for the three and six months ended June 30, 2006 was $405 million and $1,024 million, respectively, compared to $785 million and $1,368 million, respectively, for the same periods in 2005. Net cash receipts from customers and other were $3,468 million for the six months ended June 30, 2006 compared to $3,720 million in the same period of 2005, a decrease of $252 million, part of which resulted from a decrease of $375 million in the level of accounts receivable sold under the accounts receivable securitization program. Payments for employee services, suppliers and other expenses were $2,069 million for the six months ended June 30, 2006, an increase of $64 million when compared to the same period in 2005.

Also consuming cash in the first half of 2006, were payments for interest, workforce reductions and personal injury and other claims of $141 million, $27 million and $42 million, respectively, compared to $143 million, $52 million and $48 million, respectively, for the same period in 2005. In the first half of 2006, pension contributions and payments for income taxes were $25 million and $140 million, respectively, compared to $54 million and $50 million, respectively, for the same period in 2005.

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Investing activities: Cash used by investing activities in the quarter and six months ended June 30, 2006 amounted to $278 million and $487 million, respectively, compared to $249 million and $398 million for the comparable periods in 2005. The Company□s investing activities in the first half of 2006 included property additions of $442 million, a decrease of $29 million over the same period in 2005; and $58 million related to two small acquisitions. The following table details property additions for the second quarter and first half of 2006:

	Three months ended June 30		Six months ended June 30	
In millions	**2006**	2005	**2006**	2005
Track and roadway	**$ 231**	$ 249	**$ 343**	$ 361
Rolling stock	**60**	22	**171**	43
Buildings	**-**	20	**5**	20
Information technology	**22**	20	**34**	33
Other	**5**	20	**16**	27
Gross property additions	**318**	331	**569**	484
Less: capital leases	**31**	13	**127**	13
Property additions	**$ 287**	$ 318	**$ 442**	$ 471

The Company expects to spend approximately $1,550 million on capital programs in 2006 due to increased expenditures required for ongoing renewal of the basic plant, the acquisition of rolling stock and other acquisitions and investments required to improve the Company□s operating efficiency and customer service.

Free cash flow

The Company generated $422 million and $740 million of free cash flow for the three and six months ended June 30, 2006, compared to $477 million and $787 million for the same 2005 periods. Free cash flow does not have any standardized meaning prescribed by GAAP and may, therefore, not be comparable to similar measures presented by other companies. The Company believes that free cash flow is a useful measure of performance as it demonstrates the Company□s ability to generate cash after the payment of capital expenditures and dividends. The Company defines free cash flow as cash provided from operating activities, excluding changes in the level of accounts receivable sold under the securitization program, less investing activities, and after the payment of dividends, calculated as follows:

	Three months ended June 30		Six months ended June 30	
In millions	**2006**	2005	**2006**	2005
Cash provided from operating activities	**$ 405**	$ 785	**$ 1,024**	$ 1,368
Less:				
Investing activities	**(278)**	(249)	**(487)**	(398)
Cash provided before financing activities	**127**	536	**537**	970

Adjustments:				
Change in accounts receivable sold	**380**	10	**375**	(43)
Dividends paid	**(85)**	(69)	**(172)**	(140)
Free cash flow	**$ 422**	$ 477	**$ 740**	$ 787

Financing activities: Cash used by financing activities for the second quarter and six months ended June 30, 2006, totaled $93 million and $392 million, respectively, compared to $583 million and $962 million, respectively, for the same 2005 periods. On May 31, 2006, the Company issued U.S.$250 million (Cdn$275 million) of 5.80% Notes due 2016 and U.S.$450 million (Cdn$495 million) of 6.20% Debentures due 2036. The Company used the net proceeds of U.S.$692 million to reduce the Company's accounts receivable securitization program and to repay a portion of its outstanding commercial paper. In 2006 and 2005, issuances and repayments of long-term debt related principally to the Company's commercial paper program.

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During the second quarter and first six months of 2006, the Company recorded $30 million and $128 million, respectively, of assets it acquired through equipment leases ($13 million in both the second quarter and first half of 2005) for which an equivalent amount was recorded in debt.

Cash received from options exercised during the quarters ended June 30, 2006 and 2005 was $7 million and $10 million, respectively, and the related tax benefit realized upon exercise was $1 million in both periods. Cash received from options exercised during the first half of 2006 and 2005 was $59 million and $80 million, respectively, and the related tax benefit realized upon exercise was $15 million in both periods.

In the second quarter and first half of 2006, the Company repurchased 7.0 million and 14.0 million common shares for $347 million (average price per share of $49.57) and $717 million (average price per share of $51.24), respectively, under its normal course issuer bid.

The Company paid a quarterly dividend of $0.1625 per share amounting to $85 million for the second quarter and $172 million for the first six months of 2006 compared to $69 million and $140 million, respectively, at the rate of $0.1250 per share, for the same periods in 2005.

CN□s debt-to-total capitalization ratio was 37.0% at June 30, 2006, compared to 35.6% at June 30, 2005. As at June 30, 2006, the adjusted debt-to-total capitalization ratio was 40.5% compared to 41.1% at June 30, 2005. Management believes that adjusted debt-to-total capitalization is a useful measure of performance and aims to show the true leverage of the Company. However, since this adjusted measure does not have any standardized meaning prescribed by GAAP, it may not be comparable to similar measures presented by other companies and, as such, should not be considered in isolation.

June 30,	**2006**	2005
Debt-to-total capitalization ratio (a)	**37.0%**	35.6%
Add:		
Present value of operating lease commitments plus securitization financing (b)	**3.5%**	5.5%
Adjusted debt-to-total capitalization ratio (c)	**40.5%**	41.1%

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

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

(c) Adjusted debt-to-total capitalization is calculated as adjusted debt (total long-term debt, plus current portion of long-term debt, plus the present value of operating lease commitments, plus securitization financing) divided by the sum of adjusted debt plus total shareholders□ equity.

The Company has access to various financing arrangements:

Shelf prospectus and registration statement

On May 9, 2006, the Company filed a shelf prospectus and registration statement providing for the issuance, from time to time, of up to U.S.$1,500 million of debt securities in one or more offerings. Pursuant to the filing, on May 31, 2006, the Company issued U.S.$250 million (Cdn$275 million) of 5.80% Notes due 2016 and U.S.$450 million (Cdn$495 million) of 6.20% Debentures due 2036. The Company used the net proceeds of U.S.$692 million to reduce its accounts receivable securitization program and to repay a portion of its outstanding commercial paper.

On July 15, 2006, the interest rate on the Companys U.S.$250 million Puttable Reset Securities PURSSM (PURS) was reset at a new rate of 6.71% for the remaining 30-year term ending July 15, 2036. The PURS were originally issued in July 1998 with an option to call the securities on July 15, 2006 (the reset date). The call option holder exercised the call option, which resulted in the remarketing of the original PURS. The new interest rate was determined according to a pre-set mechanism based on prevailing market conditions. The Company did not receive any cash proceeds from the remarketing.

The remarketing did not trigger an extinguishment of debt, as the provisions for the reset of the interest rate were set forth in the original PURS. As such, the original PURS remain outstanding but accrue interest at the new rate until July 2036. Under securities laws, the remarketing required utilization of the Company's shelf prospectus and registration statement.

Following the issuance and remarketing of debt as explained herein, the amount available under the shelf prospectus and registration statement has been reduced to U.S.$550 million.

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MANAGEMENTS DISCUSSION AND ANALYSIS *(U.S. GAAP)*

Revolving credit facility

In January 2006, the Company repaid its borrowings of U.S.$15 million (Cdn$17 million) outstanding at December 31, 2005 under its U.S.$1,000 million revolving credit facility. The credit facility is available for general corporate purposes, including back-stopping the Companys commercial paper program, and provides for borrowings at various interest rates, including the Canadian prime rate, bankers acceptance rates, the U.S. federal funds effective rate and the London Interbank Offer Rate, plus applicable margins. The credit facility agreement has one financial covenant, the customary limitation on debt as a percentage of total capitalization, with which the Company has been in compliance. As at June 30, 2006, the Company had letters of credit drawn on its revolving credit facility of $315 million ($316 million as at December 31, 2005).

Commercial paper

The Company has a commercial paper program, which is backed by a portion of its revolving credit facility, enabling it to issue commercial paper up to a maximum aggregate principal amount of $800 million, or the U.S. dollar equivalent. Commercial paper debt is due within one year but is classified as long-term debt, reflecting the Companys intent and contractual ability to refinance the short-term borrowings through subsequent issuances of commercial paper or drawing down on the long-term revolving credit facility. As at June 30, 2006, the Company had U.S.$117 million (Cdn$130 million) of commercial paper outstanding at an average interest rate of 5.28%, and had U.S.$367 million (Cdn$427 million) at an average interest rate of 4.40%, as at December 31, 2005.

The Companys access to current and alternate sources of financing at competitive costs is dependent on its credit rating. The Company is not currently aware of any adverse trend, event or condition that would affect the Companys credit rating.

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

Contractual obligations

In the normal course of business, the Company incurs contractual obligations. The following table sets forth the Companys contractual obligations for the following items as at June 30, 2006:

In millions	**Total**	2006	2007	2008	2009	2010	2011& thereafter
Long-term debt obligations (a)	**$ 4,503**	$ -	$ 55	$ 192	$ 335	$ 130	$ 3,791
Interest on long-term debt obligations	**5,131**	139	259	250	243	223	4,017
Capital lease obligations (b)	**1,268**	104	160	77	119	61	747
Operating lease obligations	**922**	102	197	165	136	104	218
Purchase obligations (c)	**575**	230	210	66	35	34	-
Other long-term liabilities reflected on the balance sheet (d)	**1,051**	61	75	59	52	48	756
Total obligations	**$ 13,450**	**$ 636**	**$ 956**	**$ 809**	**$ 920**	**$ 600**	**$ 9,529**

(a) Presented net of unamortized discounts, of which $836 million relates to non-interest bearing Notes due in 2094 assumed as part of the BC Rail acquisition in 2004 and excludes capital lease obligations of $918 million which are included in “Capital lease obligations.”

(b) Includes $350 million of imputed interest on capital leases at rates ranging from approximately 3.00% to 11.50%.

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

(d) Includes expected payments for workers’ compensation, workforce reductions, post-retirement benefits and environmental liabilities that have been classified as contractual settlement agreements.

For 2006 and the foreseeable future, the Company expects cash flow from operations and from its various sources of financing to be sufficient to meet its debt repayments and future obligations, and to fund anticipated capital expenditures. See the Business risks section of this MD&A for a discussion of assumptions and other factors affecting such forward-looking statement.

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Off balance sheet arrangements

Accounts receivable securitization

On May 31, 2006, the Company entered into an agreement, expiring in May 2011, to sell an undivided co-ownership interest of up to a maximum of $600 million in a revolving pool of freight receivables to an unrelated trust. As part of the interest sold, the Company has recorded, in Other current assets, an amount equal to the required reserves stipulated in the agreement. The Company has retained the responsibility for servicing, administering and collecting the receivables sold. At June 30, 2006, the servicing asset and liability were not significant. Costs related to the agreement, which fluctuate with changes in prevailing interest rates, are recorded in Other loss. Subject to customary indemnifications, the trust□s recourse to the Company is generally limited to income earned on the receivables.

This new program replaces the Company□s previous accounts receivable securitization program that was set to expire in June 2006. Upon termination of the previous program, the receivables sold were repurchased with the funds from the Company□s debt issuance in May 2006. Pursuant to the repurchase, receivables in the amount of $535 million were added to the balance sheet and the retained interest that was recorded in Other current assets in the amount of $51 million, was removed.

The Company accounts for the securitization program as a sale, as control over the transferred accounts receivable is relinquished. Due to the relatively short collection period and the high quality of the receivables sold, the fair value of the undivided interest transferred to the trust, net of the retained interest (the required reserves), approximated the book value and there was no gain or loss resulting from the transaction.

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

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

At June 30, 2006, the Company had received $100 million under the new accounts receivable securitization program ($489 million at December 31, 2005 under the previous program), and set aside approximately 10% of this amount in Other current assets.

Guarantees and indemnifications

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

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

The nature of these guarantees or indemnifications, the maximum potential amount of future payments, the carrying amount of the liability, if any, and the nature of any recourse provisions are disclosed in Note 7 Major commitments and contingencies, to the Companys Interim Consolidated Financial Statements.

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Stock plans

On January 1, 2006, the Company adopted Statement of Financial Accounting Standards (SFAS) No. 123(R), Share-Based Payment, which requires the expensing of all options issued, modified or settled based on the grant date fair value over the period during which an employee is required to provide service (vesting period). The standard also requires that cash settled awards be measured at fair value at each reporting date until ultimate settlement.

The Company adopted SFAS No. 123(R) using the modified prospective approach, which requires application of the standard to all awards granted, modified, repurchased or cancelled on or after January 1, 2006, and to all awards for which the requisite service has not been rendered as at such date. Since January 1, 2003, the Company has been following the fair value based approach prescribed by SFAS No. 123, Accounting for Stock-Based Compensation, as amended by SFAS No. 148, Accounting for Stock-Based Compensation Transition and Disclosure, for stock option awards granted, modified or settled on or after such date, while cash settled awards were measured at their intrinsic value at each reporting period until December 31, 2005. As such, the application of SFAS No. 123(R) on January 1, 2006 to all awards granted prior to its adoption did not have a significant impact on the financial statements. In accordance with the modified prospective approach, prior period financial statements have not been restated to reflect the impact of SFAS No. 123(R).

For the three and six months ended June 30, 2006, the application of SFAS No. 123(R) had the effect of decreasing stock-based compensation expense by $2 million and increasing stock-based compensation expense by $3 million, respectively, and increasing net income by $1 million and decreasing net income by $2 million, respectively. There was no effect on the basic and diluted earnings per share for the three and six months ended June 30, 2006.

The Company has various stock-based incentive plans for eligible employees. A description of the plans is provided in Note 3 Stock plans, to the Companys Interim Consolidated Financial Statements. For