

UNION PACIFIC CORP
Form 10-Q
April 26, 2018
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2018

OR

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

For the transition period from _____ to _____

Commission File Number 1-6075

UNION PACIFIC CORPORATION

(Exact name of registrant as specified in its charter)

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| | |
|---|---|
| UTAH | 13-2626465 |
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification No.) |

1400 DOUGLAS STREET, OMAHA, NEBRASKA

(Address of principal executive offices)

68179

(Zip Code)

(402) 544-5000

(Registrant's telephone number, including area code)

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

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act).

Yes No

Indicate by check mark whether the registrant is an emerging growth company as defined in Rule 405 of the Securities Act of 1933 (§230.405 of this chapter) or Rule 12b-2 of the Securities Exchange Act of 1934 (§240.12b-2 of this chapter).

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

As of April 20, 2018, there were 770,245,910 shares of the Registrant's Common Stock outstanding.

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PART I. FINANCIAL INFORMATION

Item 1. Condensed Consolidated Financial Statements

Condensed Consolidated Statements of Income (Unaudited)

Union Pacific Corporation and Subsidiary Companies

Millions, Except Per Share Amounts,

| for the Three Months Ended March 31, | 2018 | 2017 |
|---|----------|----------|
| Operating revenues: | | |
| Freight revenues | \$ 5,122 | \$ 4,794 |
| Other revenues | 353 | 338 |
| Total operating revenues | 5,475 | 5,132 |
| Operating expenses: | | |
| Compensation and benefits | 1,273 | 1,262 |
| Purchased services and materials | 599 | 566 |
| Fuel | 589 | 460 |
| Depreciation | 543 | 520 |
| Equipment and other rents | 266 | 276 |
| Other | 266 | 260 |
| Total operating expenses | 3,536 | 3,344 |
| Operating income | 1,939 | 1,788 |
| Other income/(expense) (Note 7) | (42) | 72 |
| Interest expense | (186) | (172) |
| Income before income taxes | 1,711 | 1,688 |
| Income taxes | (401) | (616) |
| Net income | \$ 1,310 | \$ 1,072 |
| Share and Per Share (Note 9): | | |
| Earnings per share - basic | \$ 1.69 | \$ 1.32 |
| Earnings per share - diluted | \$ 1.68 | \$ 1.32 |
| Weighted average number of shares - basic | 776.4 | 811.5 |
| Weighted average number of shares - diluted | 779.6 | 814.8 |
| Dividends declared per share | \$ 0.73 | \$ 0.605 |

Condensed Consolidated Statements of Comprehensive Income (Unaudited)

Union Pacific Corporation and Subsidiary Companies

| Millions, for the Three Months Ended March 31, | 2018 | 2017 |
|---|----------|----------|
| Net income | \$ 1,310 | \$ 1,072 |
| Other comprehensive income/(loss): | | |
| Defined benefit plans | 19 | 11 |
| Foreign currency translation | - | 9 |
| Total other comprehensive income/(loss) [a] | 19 | 20 |
| Comprehensive income | \$ 1,329 | \$ 1,092 |

[a]Net of deferred taxes of \$(6) million and \$(14) million during the three months ended March 31, 2018, and 2017, respectively.

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

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Condensed Consolidated Statements of Financial Position (Unaudited)

Union Pacific Corporation and Subsidiary Companies

| Millions, Except Share and Per Share Amounts | March 31, 2018 | December 31, 2017 |
|--|-------------------|-------------------------|
| Assets | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 1,048 | \$ 1,275 |
| Short-term investments (Note 14) | 90 | 90 |
| Accounts receivable, net (Note 11) | 1,571 | 1,493 |
| Materials and supplies | 808 | 749 |
| Other current assets | 380 | 399 |
| Total current assets | 3,897 | 4,006 |
| Investments | 1,810 | 1,809 |
| Net properties (Note 12) | 51,696 | 51,605 |
| Other assets | 386 | 386 |
| Total assets | \$ 57,789 | \$ 57,806 |
| Liabilities and Common Shareholders' Equity | | |
| Current liabilities: | | |
| Accounts payable and other current liabilities (Note 13) | \$ 2,855 | \$ 3,139 |
| Debt due within one year (Note 15) | 1,891 | 800 |
| Total current liabilities | 4,746 | 3,939 |
| Debt due after one year (Note 15) | 15,697 | 16,144 |
| Deferred income taxes | 11,050 | 10,936 |
| Other long-term liabilities | 1,907 | 1,931 |
| Commitments and contingencies (Note 17) | | |
| Total liabilities | 33,400 | 32,950 |
| Common shareholders' equity: | | |
| Common shares, \$2.50 par value, 1,400,000,000 authorized; 1,111,814,739 and 1,111,371,304 issued; 772,517,399 and 780,917,756 outstanding, respectively | 2,779 | 2,778 |
| Paid-in-surplus | 4,473 | 4,476 |
| Retained earnings | 42,359 | 41,317 |
| Treasury stock | (23,800) | (22,574) |
| Accumulated other comprehensive loss (Note 10) | (1,422) | (1,141) |
| Total common shareholders' equity | 24,389 | 24,856 |
| Total liabilities and common shareholders' equity | \$ 57,789 | \$ 57,806 |

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

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Condensed Consolidated Statements of Cash Flows (Unaudited)

Union Pacific Corporation and Subsidiary Companies

| Millions, for the Three Months Ended March 31, | 2018 | 2017 |
|---|----------|----------|
| Operating Activities | | |
| Net income | \$ 1,310 | \$ 1,072 |
| Adjustments to reconcile net income to cash provided by operating activities: | | |
| Depreciation | 543 | 520 |
| Deferred and other income taxes | 112 | 145 |
| Other operating activities, net | 339 | 94 |
| Changes in current assets and liabilities: | | |
| Accounts receivable, net | (78) | (21) |
| Materials and supplies | (59) | (43) |
| Other current assets | (112) | (132) |
| Accounts payable and other current liabilities | (379) | (186) |
| Income and other taxes | 225 | 434 |
| Cash provided by operating activities | 1,901 | 1,883 |
| Investing Activities | | |
| Capital investments | (910) | (811) |
| Purchases of short-term investments (Note 14) | (60) | (90) |
| Maturities of short-term investments (Note 14) | 60 | 60 |
| Proceeds from asset sales | 12 | 17 |
| Other investing activities, net | (21) | (19) |
| Cash used in investing activities | (919) | (843) |
| Financing Activities | | |
| Debt issued (Note 15) | 1,706 | 200 |
| Common share repurchases (Note 18) | (1,166) | (759) |
| Debt repaid | (1,157) | (184) |
| Dividends paid | (568) | (492) |
| Other financing activities, net | (24) | (33) |
| Cash used in financing activities | (1,209) | (1,268) |
| Net change in cash and cash equivalents | (227) | (228) |
| Cash and cash equivalents at beginning of year | 1,275 | 1,277 |
| Cash and cash equivalents at end of period | \$ 1,048 | \$ 1,049 |
| Supplemental Cash Flow Information | | |
| Non-cash investing and financing activities: | | |
| Capital investments accrued but not yet paid | \$ 74 | \$ 94 |
| Common shares repurchased but not yet paid | 64 | 43 |
| Cash (paid for)/received from: | | |

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| | | |
|--------------------------------------|-------|--------|
| Income taxes, net of refunds | \$ 2 | \$ (3) |
| Interest, net of amounts capitalized | (230) | (203) |

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

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Condensed Consolidated Statements of Changes in Common Shareholders' Equity (Unaudited)

Union Pacific Corporation and Subsidiary Companies

| Millions | Common Shares | Treasury Shares | Common Shares | Paid-in-Surplus | Retained Earnings | Treasury Stock | AOCI [a] | Total |
|--|------------------|--------------------|------------------|-----------------|----------------------|-------------------|-------------|-----------|
| Balance at January 1, 2017 | 1,111.0 | (295.2) | \$ 2,777 | \$ 4,421 | \$ 32,587 | \$ (18,581) | \$ (1,272) | \$ 19,932 |
| Net income | | | - | - | 1,072 | - | - | 1,072 |
| Other comprehensive income | | | - | - | - | - | 20 | 20 |
| Conversion, stock option exercises, forfeitures, and other | 0.4 | 0.5 | 2 | (15) | - | 6 | - | (7) |
| Share repurchases (Note 18) | - | (7.5) | - | - | - | (802) | - | (802) |
| Cash dividends declared (\$0.605 per share) | - | - | - | - | (492) | - | - | (492) |
| Balance at March 31, 2017 | 1,111.4 | (302.2) | \$ 2,779 | \$ 4,406 | \$ 33,167 | \$ (19,377) | \$ (1,252) | \$ 19,723 |
| Balance at January 1, 2018 | 1,111.4 | (330.5) | \$ 2,778 | \$ 4,476 | \$ 41,317 | \$ (22,574) | \$ (1,141) | \$ 24,856 |
| Net income | | | - | - | 1,310 | - | - | 1,310 |
| Other comprehensive income | | | - | - | - | - | 19 | 19 |
| Conversion, stock option exercises, forfeitures, and other | 0.4 | 0.5 | 1 | (3) | - | 4 | - | 2 |
| Share repurchases (Note 18) | - | (9.3) | - | - | - | (1,230) | - | (1,230) |

| | | | | | | | | |
|---|---------|---------|----------|----------|-----------|-------------|------------|-----------|
| Cash dividends declared (\$0.73 per share) | - | - | - | - | (568) | - | - | (568) |
| Reclassification due to ASU 2018-02 adoption (Note 2) | - | - | - | - | 300 | - | (300) | - |
| Balance at March 31, 2018 | 1,111.8 | (339.3) | \$ 2,779 | \$ 4,473 | \$ 42,359 | \$ (23,800) | \$ (1,422) | \$ 24,389 |

[a]AOCI = Accumulated Other Comprehensive Income/(Loss) (Note 10)

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

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UNION PACIFIC CORPORATION AND SUBSIDIARY COMPANIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

For purposes of this report, unless the context otherwise requires, all references herein to the “Corporation”, “Company”, “UPC”, “we”, “us”, and “our” mean Union Pacific Corporation and its subsidiaries, including Union Pacific Railroad Company, which will be separately referred to herein as “UPRR” or the “Railroad”.

1. Basis of Presentation

Our Condensed Consolidated Financial Statements are unaudited and reflect all adjustments (consisting of normal and recurring adjustments) that are, in the opinion of management, necessary for their fair presentation in conformity with accounting principles generally accepted in the United States of America (GAAP). Pursuant to the rules and regulations of the Securities and Exchange Commission (SEC), certain information and note disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted. Accordingly, this Quarterly Report on Form 10-Q should be read in conjunction with our Consolidated Financial Statements and notes thereto contained in our 2017 Annual Report on Form 10-K. Our Consolidated Statement of Financial Position at December 31, 2017, is derived from audited financial statements. The results of operations for the three months ended March 31, 2018, are not necessarily indicative of the results for the entire year ending December 31, 2018.

The Condensed Consolidated Financial Statements are presented in accordance with GAAP as codified in the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC).

2. Accounting Pronouncements

In May 2014, the FASB issued Accounting Standards Update No. 2014-09 (ASU 2014-09), Revenue from Contracts with Customers (Topic 606). ASU 2014-09 supersedes the revenue recognition guidance in Topic 605, Revenue Recognition. The core principle of the guidance is that an entity should recognize revenue to depict the transfer of promised goods and services to customers in an amount that reflects the consideration to which the entity expects to

be entitled in the exchange for those goods or services. This may require the use of more judgment and estimates in order to correctly recognize the revenue expected as an outcome of each specific performance obligation. Additionally, this guidance will require the disclosure of the nature, amount, and timing of revenue arising from contracts so as to aid in the understanding of the users of financial statements.

Effective January 1, 2018, the Company adopted ASU 2014-09 using the modified retrospective transition method. The Company analyzed its freight and other revenues and recognizes freight revenues as freight moves from origin to destination and recognizes other revenues as identified performance obligations are satisfied. We also analyzed freight and other revenues in the context of the new guidance on principal versus agent considerations and evaluated the required new disclosures. The ASU did not have an impact on our consolidated financial position, results of operations, or cash flows.

In January 2016, the FASB issued Accounting Standards Update No. 2016-01 (ASU 2016-01), Recognition and Measurement of Financial Assets and Financial Liabilities (Subtopic 825-10). ASU 2016-01 provides guidance for the recognition, measurement, presentation, and disclosure of financial instruments. This guidance is effective for annual and interim periods beginning after December 15, 2017, and early adoption is not permitted. Effective January 1, 2018, the Company adopted the ASU and it did not have an impact on our consolidated financial position, results of operations, or cash flows.

In March 2017, the FASB issued Accounting Standards Update No. 2017-07 (ASU 2017-07), Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost (Topic 715). ASU 2017-07 requires the service cost component be reported separately from the other components of net benefit costs in the income statement, provides explicit guidance on the presentation of the service cost component and the other components of net benefit cost in the income statement, and allows only the service cost component of net benefit cost to be eligible for capitalization. Effective January 1, 2018, we adopted the standard on a retrospective basis. As a result of the adoption, only service costs are recorded within compensation and benefits expense, and the other components of net benefit costs are now recorded

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within other income/(expense). The retrospective adoption of ASU 2017-07 decreased operating income by \$4 million and \$5 million for the three months ended March 31, 2018 and 2017, respectively, and increased other income by \$4 million and \$5 million for the same periods.

On February 14, 2018, the FASB issued Accounting Standards Update 2018-02, (ASU 2018-02), Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income, which allows entities the option to reclassify from accumulated other comprehensive income (“AOCI”) to retained earnings the income tax effects that remain in AOCI resulting from the application of the Tax Act. ASU 2018-02 is effective for fiscal years, and for interim periods within those fiscal years, beginning after December 15, 2018. Early adoption of the ASU is permitted, including adoption in any interim period. We have adopted ASU 2018-02 during the first quarter of 2018. As a result of this adoption, we have elected to reclassify \$300 million from AOCI to retained earnings. UP has adopted the policy that future income tax effects that are stranded in AOCI will be released only when the entire portfolio of the type of item is liquidated.

In February 2016, the FASB issued Accounting Standards Update No. 2016-02 (ASU 2016-02), Leases (Subtopic 842). ASU 2016-02 will require companies to recognize lease assets and lease liabilities on the balance sheet and disclose key information about leasing arrangements. For public companies, this standard is effective for annual reporting periods beginning after December 15, 2018, and early adoption is permitted. Management is currently evaluating the impact of this standard on our consolidated financial position, results of operations, and cash flows, but expects that the adoption will result in an increase in the Company’s assets and liabilities of over \$2 billion.

3. Significant Accounting Policies Update

Our significant accounting policies are detailed in Note 2 of our Annual Report on Form 10-K for the year ended December 31, 2017. Changes to our accounting policies as a result of adopting ASU 2014-09 are discussed below.

Revenue Recognition – Freight revenues are derived from contracts with customers. We account for a contract when it has approval and commitment from both parties, the rights of the parties are identified, payment terms are identified, the contract has commercial substance, and collectability of consideration is probable. Our contracts include private agreements, private rate/letter quotes, public circulars/tariffs, and interline/foreign agreements. The performance obligation in our contracts is typically delivering a specific commodity from a place of origin to a place of destination

and our commitment begins with the tendering and acceptance of a freight bill of lading and is satisfied upon delivery at destination. We consider each freight shipment to be a distinct performance obligation.

We recognize freight revenues over time as freight moves from origin to destination. The allocation of revenue between reporting periods is based on the relative transit time in each reporting period with expenses recognized as incurred. Outstanding performance obligations related to freight moves in transit totaled \$161 million at March 31, 2018 and \$154 million at December 31, 2017 and are expected to be recognized in the next quarter as we satisfy our remaining performance obligations and deliver freight to destination. The transaction price is generally specified in a contract and may be dependent on the commodity, origin/destination, and route. Customer incentives, which are primarily provided for shipping a specified cumulative volume or shipping to/from specific locations, are recorded as a reduction to operating revenues based on actual or projected future customer shipments.

Under typical payment terms, our customers pay us after each performance obligation is satisfied and there are no material contract assets or liabilities associated with our freight revenues. Outstanding freight receivables are presented in our Consolidated Statement of Financial Position as Accounts Receivables, net.

Freight revenue related to interline transportation services that involve other railroads are reported on a net basis. The portion of the gross amount billed to customers that is remitted by the Company to another party is not reflected as freight revenue.

Other revenues consist primarily of revenues earned by our subsidiaries and accessorial revenues. Non-rail subsidiary revenues are generally recognized over time as shipments move from origin to destination. The allocation of revenue between reporting periods is based on the relative transit time in each reporting

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period with expenses recognized as incurred. Accessorial revenues are recognized at a point in time as performance obligations are satisfied.

4. Operations and Segmentation

The Railroad, along with its subsidiaries and rail affiliates, is our one reportable operating segment. Although we provide and analyze revenue by commodity group, we treat the financial results of the Railroad as one segment due to the integrated nature of our rail network. Our operating revenues are primarily derived from contracts with customers for the transportation of freight from origin to destination. The following table represents a disaggregation of our freight and other revenues:

| Millions | Three Months Ended March 31, | |
|--------------------------|------------------------------------|----------|
| | 2018 | 2017 |
| Agricultural Products | \$ 1,098 | \$ 1,094 |
| Energy | 1,173 | 1,024 |
| Industrial | 1,340 | 1,264 |
| Premium | 1,511 | 1,412 |
| Total freight revenues | \$ 5,122 | \$ 4,794 |
| Subsidiary revenues | 217 | 215 |
| Accessorial revenues | 121 | 106 |
| Other revenues | 15 | 17 |
| Total operating revenues | \$ 5,475 | \$ 5,132 |

Although our revenues are principally derived from customers domiciled in the U.S., the ultimate points of origination or destination for some products we transport are outside the U.S. Each of our commodity groups includes revenue from shipments to and from Mexico. Included in the above table are freight revenues from our Mexico business which amounted to \$579 million and \$566 million, respectively, for the three months ended March 31, 2018, and March 31, 2017.

5. Stock-Based Compensation

We have several stock-based compensation plans under which employees and non-employee directors receive stock options, nonvested retention shares, and nonvested stock units. We refer to the nonvested shares and stock units collectively as “retention awards”. We have elected to issue treasury shares to cover option exercises and stock unit vestings, while new shares are issued when retention shares are granted. Information regarding stock-based compensation appears in the table below:

| Millions | Three Months Ended March 31, 2018 2017 | |
|--|--|-------|
| Stock-based compensation, before tax: | | |
| Stock options | \$ 4 | \$ 4 |
| Retention awards | 21 | 22 |
| Total stock-based compensation, before tax | \$ 25 | \$ 26 |
| Excess tax benefits from equity compensation plans | \$ 15 | \$ 22 |

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Stock Options – We estimate the fair value of our stock option awards using the Black-Scholes option pricing model. The table below shows the annual weighted-average assumptions used for valuation purposes:

| | | |
|---|----------|----------|
| Weighted-Average Assumptions | 2018 | 2017 |
| Risk-free interest rate | 2.6% | 2.0% |
| Dividend yield | 2.3% | 2.3% |
| Expected life (years) | 5.3 | 5.3 |
| Volatility | 21.1% | 21.7% |
| Weighted-average grant-date fair value of options granted | \$ 21.70 | \$ 18.19 |

The risk-free rate is based on the U.S. Treasury yield curve in effect at the time of grant; the expected dividend yield is calculated as the ratio of dividends paid per share of common stock to the stock price on the date of grant; the expected life is based on historical and expected exercise behavior; and expected volatility is based on the historical volatility of our stock price over the expected life of the option.

A summary of stock option activity during the three months ended March 31, 2018, is presented below:

| | Options (thous.) | Weighted-Average Exercise Price | Weighted-Average Remaining Contractual Term | Intrinsic Value |
|--|------------------|---------------------------------|---|-----------------|
| Outstanding at January 1, 2018 | 5,630 | \$ 83.37 | 5.8 yrs. | \$ 286 |
| Granted | 800 | 124.86 | N/A | N/A |
| Exercised | (446) | 62.14 | N/A | N/A |
| Forfeited or expired | (8) | 86.57 | N/A | N/A |
| Outstanding at March 31, 2018 | 5,976 | \$ 90.50 | 6.2 yrs. | \$ 263 |
| Vested or expected to vest at March 31, 2018 | 5,918 | \$ 90.33 | 6.2 yrs. | \$ 261 |
| Options exercisable at March 31, 2018 | 4,045 | \$ 82.73 | 5.0 yrs. | \$ 209 |

Stock options are granted at the closing price on the date of grant, have ten-year contractual terms, and vest no later than three years from the date of grant. None of the stock options outstanding at March 31, 2018, are subject to performance or market-based vesting conditions.

At March 31, 2018, there was \$32 million of unrecognized compensation expense related to nonvested stock options, which is expected to be recognized over a weighted-average period of 1.6 years. Additional information regarding

stock option exercises appears in the table below:

| Millions | Three Months Ended March 31, | |
|---|---------------------------------------|-------|
| | 2018 | 2017 |
| Intrinsic value of stock options exercised | \$ 33 | \$ 23 |
| Cash received from option exercises | 26 | 20 |
| Treasury shares repurchased for employee payroll taxes | (8) | (7) |
| Tax benefit realized from option exercises | 8 | 9 |
| Aggregate grant-date fair value of stock options vested | 18 | 19 |

Retention Awards – The fair value of retention awards is based on the closing price of the stock on the grant date. Dividends and dividend equivalents are paid to participants during the vesting periods.

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Changes in our retention awards during the three months ended March 31, 2018, were as follows:

| | Shares | Weighted-Average Grant-Date Fair Value |
|------------------------------|----------|--|
| | (thous.) | |
| Nonvested at January 1, 2018 | 2,313 | \$ 95.04 |
| Granted | 532 | 125.08 |
| Vested | (611) | 87.94 |
| Forfeited | (24) | 97.76 |
| Nonvested at March 31, 2018 | 2,210 | \$ 104.20 |

Retention awards are granted at no cost to the employee or non-employee director and vest over periods lasting up to four years. At March 31, 2018, there was \$133 million of total unrecognized compensation expense related to nonvested retention awards, which is expected to be recognized over a weighted-average period of 2.4 years.

Performance Retention Awards – In February 2018, our Board of Directors approved performance stock unit grants. The basic terms of these performance stock units are identical to those granted in February 2017, except for different annual return on invested capital (ROIC) performance targets. The plan also includes relative operating income growth (OIG) as a modifier compared to the companies included in the S&P 500 Industrials Index. We define ROIC as net operating profit adjusted for interest expense (including interest on the present value of operating leases) and taxes on interest divided by average invested capital adjusted for the present value of operating leases. The modifier can be up to +/- 25% of the award earned based on the ROIC achieved.

Stock units awarded to selected employees under these grants are subject to continued employment for 37 months and the attainment of certain levels of ROIC, modified for the relative OIG. We expense the fair value of the units that are probable of being earned based on our forecasted ROIC over the 3-year performance period, and with respect to the third year of the plan, the relative OIG modifier. We measure the fair value of these performance stock units based upon the closing price of the underlying common stock as of the date of grant, reduced by the present value of estimated future dividends. Dividend equivalents are paid to participants only after the units are earned.

The assumptions used to calculate the present value of estimated future dividends related to the February 2018 grant were as follows:

| | |
|--|---------|
| | 2018 |
| Dividend per share per quarter | \$ 0.73 |
| Risk-free interest rate at date of grant | 2.3% |

Changes in our performance retention awards during the three months ended March 31, 2018, were as follows:

| | Shares | Weighted-Average Grant-Date Fair Value |
|------------------------------|----------|--|
| | (thous.) | |
| Nonvested at January 1, 2018 | 1,138 | \$ 92.92 |
| Granted | 348 | 117.80 |
| Vested | (94) | 112.19 |
| Unearned | (201) | 114.97 |
| Forfeited | (5) | 78.20 |
| Nonvested at March 31, 2018 | 1,186 | \$ 95.02 |

At March 31, 2018, there was \$56 million of total unrecognized compensation expense related to nonvested performance retention awards, which is expected to be recognized over a weighted-average period of 1.8 years. This expense is subject to achievement of the performance measures established for the performance stock unit grants.

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6. Retirement Plans

Pension and Other Postretirement Benefits

Pension Plans – We provide defined benefit retirement income to eligible non-union employees through qualified and non-qualified (supplemental) pension plans. Qualified and non-qualified pension benefits are based on years of service and the highest compensation during the latest years of employment, with specific reductions made for early retirements.

Other Postretirement Benefits (OPEB) – We provide medical and life insurance benefits for eligible retirees. These benefits are funded as medical claims and life insurance premiums are paid.

Expense

Both pension and OPEB expense are determined based upon the annual service cost of benefits (the actuarial cost of benefits earned during a period) and the interest cost on those liabilities, less the expected return on plan assets. The expected long-term rate of return on plan assets is applied to a calculated value of plan assets that recognizes changes in fair value over a five-year period. This practice is intended to reduce year-to-year volatility in pension expense, but it can have the effect of delaying the recognition of differences between actual returns on assets and expected returns based on long-term rate of return assumptions. Differences in actual experience in relation to assumptions are not recognized in net income immediately, but are deferred in accumulated other comprehensive income and, if necessary, amortized as pension or OPEB expense.

The components of our net periodic pension and OPEB cost were as follows for the three months ended March 31:

| Millions | Pension | | OPEB | |
|--------------------------------|---------|-------|------|------|
| | 2018 | 2017 | 2018 | 2017 |
| Service cost | \$ 27 | \$ 23 | \$ - | \$ - |
| Interest cost | 36 | 35 | 3 | 3 |
| Expected return on plan assets | (68) | (66) | - | - |
| Amortization of actuarial loss | 23 | 20 | 2 | 3 |

Net periodic benefit cost \$ 18 \$ 12 \$ 5 \$ 6

As a result of the adoption of ASU 2017-07 effective January 1, 2018, only service costs are recorded within compensation and benefits expense, and the other components of net benefit costs are now recorded within other income/(expense).

Cash Contributions

For the three months ended March 31, 2018, we did not make any cash contributions to the qualified pension plan. Any contributions made during 2018 will be based on cash generated from operations and financial market considerations. Our policy with respect to funding the qualified plans is to fund at least the minimum required by law and not more than the maximum amount deductible for tax purposes. At March 31, 2018, we do not have minimum cash funding requirements for 2018.

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7. Other Income / (Expense)

Other income / (expense) included the following:

| Millions | Three Months Ended March 31, | |
|--|---------------------------------------|-------|
| | 2018 | 2017 |
| Early extinguishment of debt [a] | \$ (85) | \$ - |
| Rental income | 28 | 37 |
| Net gain on non-operating asset dispositions [b] | 6 | 34 |
| Interest income | 4 | 2 |
| Net periodic pension and OPEB costs | 4 | 5 |
| Non-operating environmental costs and other | 1 | (6) |
| Total | \$ (42) | \$ 72 |

[a]2018 includes a debt extinguishment charge for the early redemption of certain bonds and debentures (Note 15).

[b]2017 includes \$26 million related to a real estate sale in the first quarter.

8. Income Taxes

On December 22, 2017, The Tax Cuts and Jobs Act (the "Tax Act") was enacted. The Tax Act made significant changes to federal tax law, including a reduction in the federal income tax rate from 35% to 21% effective January 1, 2018, 100% bonus depreciation for certain capital expenditures, stricter limits on deductions for interest and certain executive compensation, and a one-time transition tax on previously deferred earnings of certain foreign subsidiaries. As a result of our initial analysis of the Tax Act and existing implementation guidance, we remeasured our deferred tax assets and liabilities and computed our transition tax liability net of offsetting foreign tax credits. This resulted in a \$5.9 billion reduction in our income tax expense in the fourth quarter of 2017. We also recorded a \$212 million reduction to our operating expense related to income tax adjustments at equity-method affiliates in the fourth quarter of 2017.

The SEC provided guidance in SAB 118 on accounting for the tax effects of the Tax Act. In accordance with that guidance, some of the income tax effects recorded in 2017 are provisional, including those related to our analysis of 100% bonus depreciation for certain capital expenditures, stricter limits on deductions for certain executive compensation, the one-time transition tax, and the reduction to our operating expense related to income tax adjustments at equity-method affiliates. The accounting for the income tax effects may be adjusted during 2018 as a result of continuing analysis of the Tax Act; additional implementation guidance from the IRS, state tax authorities, the SEC, the FASB, or the Joint Committee on Taxation; and new information from domestic or foreign equity affiliates. We had no material adjustments to our initial analysis of the Tax Act during the first quarter of 2018.

UPC is not currently under examination by the Internal Revenue Service. The statute of limitations has run for all years prior to 2014. In 2017, UPC amended its 2013 income tax return, primarily to claim deductions resulting from the resolution of prior year IRS examinations. The IRS and Joint Committee on Taxation have completed their review of this return and we anticipate receiving a refund of \$18 million in the second quarter of 2018.

Several state tax authorities are examining our state tax returns for years 2010 through 2015.

At March 31, 2018, we had a net liability for unrecognized tax benefits of \$182 million.

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9. Earnings Per Share

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

| Millions, Except Per Share Amounts, for the Three Months Ended March 31, | 2018 | 2017 |
|---|----------|----------|
| Net income | \$ 1,310 | \$ 1,072 |
| Weighted-average number of shares outstanding: | | |
| Basic | 776.4 | 811.5 |
| Dilutive effect of stock options | 1.8 | 1.8 |
| Dilutive effect of retention shares and units | 1.4 | 1.5 |
| Diluted | 779.6 | 814.8 |
| Earnings per share – basic | \$ 1.69 | \$ 1.32 |
| Earnings per share – diluted | \$ 1.68 | \$ 1.32 |
| Stock options excluded as their inclusion would be anti-dilutive | 0.5 | 1.6 |

10. Accumulated Other Comprehensive Income/(Loss)

Reclassifications out of accumulated other comprehensive income/(loss) for the three months ended March 31, 2018, and 2017, were as follows (net of tax):

| Millions | Defined benefit plans | Foreign currency translation | Total |
|--|-----------------------------|------------------------------------|------------|
| Balance at January 1, 2018 | \$ (1,029) | \$ (112) | \$ (1,141) |
| Other comprehensive income/(loss) before reclassifications | - | - | - |
| Amounts reclassified from accumulated other comprehensive income/(loss) [a] | 19 | - | 19 |
| Net year-to-date other comprehensive income/(loss), net of taxes of \$(6) million | 19 | - | 19 |
| Reclassification due to ASU 2018-02 adoption (Note 2) | (225) | (75) | (300) |
| Balance at March 31, 2018 | \$ (1,235) | \$ (187) | \$ (1,422) |

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| | | | |
|---|------------|----------|------------|
| Balance at January 1, 2017 | \$ (1,132) | \$ (140) | \$ (1,272) |
| Other comprehensive income/(loss) before reclassifications | (3) | 9 | 6 |
| Amounts reclassified from accumulated other comprehensive income/(loss) [a] | 14 | - | 14 |
| Net year-to-date other comprehensive income/(loss), net of taxes of \$(14) million | 11 | 9 | 20 |
| Balance at March 31, 2017 | \$ (1,121) | \$ (131) | \$ (1,252) |

[a]The accumulated other comprehensive income/(loss) reclassification components are 1) prior service cost/(credit) and 2) net actuarial loss which are both included in the computation of net periodic pension cost. See Note 6 Retirement Plans for additional details.

11. Accounts Receivable

Accounts receivable includes freight and other receivables reduced by an allowance for doubtful accounts. The allowance is based upon historical losses, credit worthiness of customers, and current economic conditions. At both March 31, 2018, and December 31, 2017, our accounts receivable were reduced by \$3 million. Receivables not expected to be collected in one year and the associated allowances are classified as other assets in our Condensed Consolidated Statements of Financial Position. At March 31, 2018, and December 31, 2017, receivables classified as other assets were reduced by allowances of \$19 million and \$17 million, respectively.

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Receivables Securitization Facility – The Railroad maintains a \$650 million, 3-year receivables securitization facility (the Receivables Facility) maturing in July 2019. Under the Receivables Facility, the Railroad sells most of its eligible third-party receivables to Union Pacific Receivables, Inc. (UPRI), a consolidated, wholly-owned, bankruptcy-remote subsidiary that may subsequently transfer, without recourse, an undivided interest in accounts receivable to investors. The investors have no recourse to the Railroad’s other assets except for customary warranty and indemnity claims. Creditors of the Railroad do not have recourse to the assets of UPRI.

The amount outstanding under the Receivables Facility was \$650 million and \$500 at March 31, 2018, and December 31, 2017, respectively. The Receivables Facility was supported by \$1.2 billion and \$1.1 billion of accounts receivable as collateral at March 31, 2018, and December 31, 2017, respectively, which, as a retained interest, is included in accounts receivable, net in our Condensed Consolidated Statements of Financial Position.

The outstanding amount the Railroad is allowed to maintain under the Receivables Facility, with a maximum of \$650 million, may fluctuate based on the availability of eligible receivables and is directly affected by business volumes and credit risks, including receivables payment quality measures such as default and dilution ratios. If default or dilution ratios increase one percent, the allowable outstanding amount under the Receivables Facility would not materially change.

The costs of the Receivables Facility include interest, which will vary based on prevailing benchmark and commercial paper rates, program fees paid to participating banks, commercial paper issuance costs, and fees of participating banks for unused commitment availability. The costs of the Receivables Facility are included in interest expense and were \$4 million and \$1 million for the three months ended March 31, 2018, and 2017, respectively.

12. Properties

The following tables list the major categories of property and equipment, as well as the weighted-average estimated useful life for each category (in years):

| Millions, Except Estimated Useful Life As of March 31, 2018 | Cost | Accumulated Depreciation | Net Book Value | Estimated Useful Life |
|--|----------|--------------------------|----------------|-----------------------|
| Land | \$ 5,271 | \$ N/A | \$ 5,271 | N/A |

Road:

| | | | | |
|-------------------------------|--------|--------|--------|-----|
| Rail and other track material | 16,439 | 5,997 | 10,442 | 43 |
| Ties | 10,227 | 2,935 | 7,292 | 33 |
| Ballast | 5,442 | 1,533 | 3,909 | 34 |
| Other roadway [a] | 19,143 | 3,549 | 15,594 | 47 |
| Total road | 51,251 | 14,014 | 37,237 | N/A |

Equipment:

| | | | | |
|--------------------------|-----------|-----------|-----------|-----|
| Locomotives | 9,667 | 3,737 | 5,930 | 19 |
| Freight cars | 2,295 | 985 | 1,310 | 24 |
| Work equipment and other | 941 | 277 | 664 | 19 |
| Total equipment | 12,903 | 4,999 | 7,904 | N/A |
| Technology and other | 1,099 | 462 | 637 | 11 |
| Construction in progress | 647 | - | 647 | N/A |
| Total | \$ 71,171 | \$ 19,475 | \$ 51,696 | N/A |

[a]Other roadway includes grading, bridges and tunnels, signals, buildings, and other road assets.

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| Millions, Except Estimated Useful Life As of December 31, 2017 | Cost | Accumulated Depreciation | Net Book Value | Estimated Useful Life |
|---|-----------|-----------------------------|-------------------|--------------------------|
| Land | \$ 5,258 | \$ N/A | \$ 5,258 | N/A |
| Road: | | | | |
| Rail and other track material | 16,327 | 5,929 | 10,398 | 43 |
| Ties | 10,132 | 2,881 | 7,251 | 33 |
| Ballast | 5,406 | 1,509 | 3,897 | 34 |
| Other roadway [a] | 18,972 | 3,482 | 15,490 | 47 |
| Total road | 50,837 | 13,801 | 37,036 | N/A |
| Equipment: | | | | |
| Locomotives | 9,686 | 3,697 | 5,989 | 19 |
| Freight cars | 2,255 | 983 | 1,272 | 24 |
| Work equipment and other | 936 | 267 | 669 | 19 |
| Total equipment | 12,877 | 4,947 | 7,930 | N/A |
| Technology and other | 1,105 | 460 | 645 | 11 |
| Construction in progress | 736 | - | 736 | N/A |
| Total | \$ 70,813 | \$ 19,208 | \$ 51,605 | N/A |

[a]Other roadway includes grading, bridges and tunnels, signals, buildings, and other road assets.

13. Accounts Payable and Other Current Liabilities

| Millions | Mar. 31, Dec. 31, | |
|--|-------------------|----------|
| | 2018 | 2017 |
| Accounts payable | \$ 768 | \$ 1,013 |
| Income and other taxes payable | 641 | 547 |
| Accrued wages and vacation | 388 | 384 |
| Accrued casualty costs | 189 | 194 |
| Interest payable | 165 | 220 |
| Equipment rents payable | 113 | 110 |
| Other | 591 | 671 |
| Total accounts payable and other current liabilities | \$ 2,855 | \$ 3,139 |

14. Financial Instruments

Short-Term Investments – The Company’s short-term investments consist of time deposits (\$90 million as of March 31, 2018). These investments are considered level 2 investments and are valued at amortized cost, which approximates fair value. All short-term investments have a maturity of less than one year and are classified as held-to-maturity. There were no transfers out of Level 2 during the three months ended March 31, 2018.

Fair Value of Financial Instruments – The fair value of our short- and long-term debt was estimated using a market value price model, which utilizes applicable U.S. Treasury rates along with current market quotes on comparable debt securities. All of the inputs used to determine the fair market value of the Corporation’s long-term debt are Level 2 inputs and obtained from an independent source. At March 31, 2018, the fair value of total debt was \$18.0 billion, approximately \$0.4 billion more than the carrying value. At December 31, 2017, the fair value of total debt was \$18.2 billion, approximately \$1.3 billion more than the carrying value. The fair value of the Corporation’s debt is a measure of its current value under present market conditions. It does not impact the financial statements under current accounting rules. At March 31, 2018, and December 31, 2017, approximately \$0 and \$155 million, respectively of debt securities contained call provisions that allow us to retire the debt instruments prior to final maturity, with the payment of fixed call premiums, or in certain cases, at par. The fair value of our cash equivalents approximates their carrying value due to the short-term maturities of these instruments.

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15. Debt

Credit Facilities – At March 31, 2018, we had \$1.7 billion of credit available under our revolving credit facility, which is designated for general corporate purposes and supports the issuance of commercial paper. We did not draw on the facility during the three months ended March 31, 2018. Commitment fees and interest rates payable under the facility are similar to fees and rates available to comparably rated, investment-grade borrowers. The facility allows for borrowings at floating rates based on London Interbank Offered Rates, plus a spread, depending upon credit ratings for our senior unsecured debt. The facility matures in May 2019 under a five-year term and requires UPC to maintain a debt-to-net-worth coverage ratio.

The definition of debt used for purposes of calculating the debt-to-net-worth coverage ratio includes, among other things, certain credit arrangements, capital leases, guarantees and unfunded and vested pension benefits under Title IV of ERISA. At March 31, 2018, the Company was in compliance with the debt-to-net-worth coverage ratio, which allows us to carry up to \$48.8 billion of debt (as defined in the facility), and we had \$17.6 billion of debt (as defined in the facility) outstanding at that date. Under our current financial plans, we expect to continue to satisfy the debt-to-net-worth coverage ratio; however, many factors beyond our reasonable control could affect our ability to comply with this provision in the future. The facility does not include any other financial restrictions, credit rating triggers (other than rating-dependent pricing), or any other provision that could require us to post collateral. The facility also includes a \$125 million cross-default provision and a change-of-control provision.

During the three months ended March 31, 2018, we issued \$1.56 billion and repaid \$920 million of commercial paper with maturities ranging from 1 to 34 days, and at March 31, 2018, we had \$637 million of commercial paper outstanding. Our revolving credit facility supports our outstanding commercial paper balances, and, unless we change the terms of our commercial paper program, our aggregate issuance of commercial paper will not exceed the amount of borrowings available under the facility.

Shelf Registration Statement and Significant New Borrowings – We filed an automatic shelf registration statement with the SEC that became effective on February 12, 2018. The Board of Directors authorized the issuance of up to \$6 billion of debt securities, replacing the prior Board authorization in July 2016, which had \$1.55 billion of authority remaining. Under our shelf registration, we may issue, from time to time, any combination of debt securities, preferred stock, common stock, or warrants for debt securities or preferred stock in one or more offerings.

During the three months ended March 31, 2018, we did not issue any debt securities under this registration statement. At March 31, 2018, we had remaining authority to issue up to \$6 billion of debt securities under our shelf registration.

Receivables Securitization Facility – As of March 31, 2018, and December 31, 2017, we recorded \$650 million and \$500 million, respectively, of borrowings under our Receivables Facility as secured debt. (See further discussion of our receivables securitization facility in Note 11).

Debt Redemption – On March 15, 2018, we effectively redeemed, in entirety, the Missouri Pacific 5% Income Debentures due 2045, the Chicago and Eastern Illinois 5% Income Debentures due 2054, and the Missouri Pacific 4.75% General Mortgage Income Bonds Series A due 2020 and Series B due 2030. The debentures had principal outstanding of \$96 million and \$2 million, respectively, and the bonds had principal outstanding of \$30 million and \$27 million, respectively. The bonds and debentures were assumed by the Railroad in the 1982 acquisition of the Missouri Pacific Railroad Company, with a weighted average interest rate of 4.9%. The carrying value of all four bonds and debentures at the time of redemption was \$70 million, due to fair value purchase accounting adjustments related to the acquisition. The redemption resulted in an early extinguishment charge of \$85 million in the first quarter of 2018.

16. Variable Interest Entities

We have entered into various lease transactions in which the structure of the leases contain variable interest entities (VIEs). These VIEs were created solely for the purpose of doing lease transactions (principally involving railroad equipment and facilities) and have no other activities, assets or liabilities outside of the lease transactions. Within these lease arrangements, we have the right to purchase some or all of the

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assets at fixed prices. Depending on market conditions, fixed-price purchase options available in the leases could potentially provide benefits to us; however, these benefits are not expected to be significant.

We maintain and operate the assets based on contractual obligations within the lease arrangements, which set specific guidelines consistent within the railroad industry. As such, we have no control over activities that could materially impact the fair value of the leased assets. We do not hold the power to direct the activities of the VIEs and, therefore, do not control the ongoing activities that have a significant impact on the economic performance of the VIEs. Additionally, we do not have the obligation to absorb losses of the VIEs or the right to receive benefits of the VIEs that could potentially be significant to the VIEs.

We are not considered to be the primary beneficiary and do not consolidate these VIEs because our actions and decisions do not have the most significant effect on the VIE's performance and our fixed-price purchase options are not considered to be potentially significant to the VIEs. The future minimum lease payments associated with the VIE leases totaled \$1.8 billion as of March 31, 2018.

17. Commitments and Contingencies

Asserted and Unasserted Claims – Various claims and lawsuits are pending against us and certain of our subsidiaries. We cannot fully determine the effect of all asserted and unasserted claims on our consolidated results of operations, financial condition, or liquidity. To the extent possible, we have recorded a liability where asserted and unasserted claims are considered probable and where such claims can be reasonably estimated. We do not expect that any known lawsuits, claims, environmental costs, commitments, contingent liabilities, or guarantees will have a material adverse effect on our consolidated results of operations, financial condition, or liquidity after taking into account liabilities and insurance recoveries previously recorded for these matters.

Personal Injury – The cost of personal injuries to employees and others related to our activities is charged to expense based on estimates of the ultimate cost and number of incidents each year. We use an actuarial analysis to measure the expense and liability, including unasserted claims. The Federal Employers' Liability Act (FELA) governs compensation for work-related accidents. Under FELA, damages are assessed based on a finding of fault through litigation or out-of-court settlements. We offer a comprehensive variety of services and rehabilitation programs for employees who are injured at work.

Our personal injury liability is not discounted to present value due to the uncertainty surrounding the timing of future payments. Approximately 95% of the recorded liability is related to asserted claims and approximately 5% is related to unasserted claims at March 31, 2018. Because of the uncertainty surrounding the ultimate outcome of personal

injury claims, it is reasonably possible that future costs to settle these claims may range from approximately \$272 million to \$296 million. We record an accrual at the low end of the range as no amount of loss within the range is more probable than any other. Estimates can vary over time due to evolving trends in litigation.

Our personal injury liability activity was as follows:

| Millions, for the Three Months Ended March 31, | 2018 | 2017 |
|---|--------|--------|
| Beginning balance | \$ 285 | \$ 290 |
| Current year accruals | 19 | 19 |
| Changes in estimates for prior years | (11) | 4 |
| Payments | (21) | (22) |
| Ending balance at March 31 | \$ 272 | \$ 291 |
| Current portion, ending balance at March 31 | \$ 70 | \$ 65 |

We have insurance coverage for a portion of the costs incurred to resolve personal injury-related claims, and we have recognized an asset for estimated insurance recoveries at March 31, 2018, and December 31, 2017. Any changes to recorded insurance recoveries are included in the above table in the Changes in estimates for prior years category.

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Environmental Costs – We are subject to federal, state, and local environmental laws and regulations. We have identified 310 sites at which we are or may be liable for remediation costs associated with alleged contamination or for violations of environmental requirements. This includes 33 sites that are the subject of actions taken by the U.S. government, 21 of which are currently on the Superfund National Priorities List. Certain federal legislation imposes joint and several liability for the remediation of identified sites; consequently, our ultimate environmental liability may include costs relating to activities of other parties, in addition to costs relating to our own activities at each site.

When we identify an environmental issue with respect to property owned, leased, or otherwise used in our business, we perform, with assistance of our consultants, environmental assessments on the property. We expense the cost of the assessments as incurred. We accrue the cost of remediation where our obligation is probable and such costs can be reasonably estimated. Our environmental liability is not discounted to present value due to the uncertainty surrounding the timing of future payments.

Our environmental liability activity was as follows:

| Millions, for the Three Months Ended March 31, | 2018 | 2017 |
|---|--------|--------|
| Beginning balance | \$ 196 | \$ 212 |
| Accruals | 16 | 2 |
| Payments | (14) | (11) |
| Ending balance at March 31 | \$ 198 | \$ 203 |
| Current portion, ending balance at March 31 | \$ 57 | \$ 53 |

The environmental liability includes future costs for remediation and restoration of sites, as well as ongoing monitoring costs, but excludes any anticipated recoveries from third parties. Cost estimates are based on information available for each site, financial viability of other potentially responsible parties, and existing technology, laws, and regulations. The ultimate liability for remediation is difficult to determine because of the number of potentially responsible parties, site-specific cost sharing arrangements with other potentially responsible parties, the degree of contamination by various wastes, the scarcity and quality of volumetric data related to many of the sites, and the speculative nature of remediation costs. Estimates of liability may vary over time due to changes in federal, state, and local laws governing environmental remediation. Current obligations are not expected to have a material adverse effect on our consolidated results of operations, financial condition, or liquidity.

Insurance – The Company has a consolidated, wholly-owned captive insurance subsidiary (the captive), that provides insurance coverage for certain risks including FELA claims and property coverage which are subject to reinsurance. The captive entered into annual reinsurance treaty agreements that insure workers compensation, general liability, auto

liability and FELA risk. The captive cedes a portion of its FELA exposure through the treaty and assumes a proportionate share of the entire risk. The captive receives direct premiums, which are netted against the Company's premium costs in other expenses in the Condensed Consolidated Statements of Income. The treaty agreements provide for certain protections against the risk of treaty participants' non-performance, and we do not believe our exposure to treaty participants' non-performance is material at this time. In the event the Company leaves the reinsurance program, the Company is not relieved of its primary obligation to the policyholders for activity prior to the termination of the treaty agreements. We record both liabilities and reinsurance receivables using an actuarial analysis based on historical experience in our Condensed Consolidated Statements of Financial Position.

Guarantees – At both March 31, 2018, and December 31, 2017, we were contingently liable for \$33 million in guarantees. The fair value of these obligations as of both March 31, 2018, and December 31, 2017 was \$0. We entered into these contingent guarantees in the normal course of business, and they include guaranteed obligations related to our affiliated operations. The final guarantee expires in 2022. We are not aware of any existing event of default that would require us to satisfy these guarantees. We do not expect that these guarantees will have a material adverse effect on our consolidated financial condition, results of operations, or liquidity.

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Indemnities – We are contingently obligated under a variety of indemnification arrangements, although in some cases the extent of our potential liability is limited, depending on the nature of the transactions and the agreements. Due to uncertainty as to whether claims will be made or how they will be resolved, we cannot reasonably determine the probability of an adverse claim or reasonably estimate any adverse liability or the total maximum exposure under these indemnification arrangements. We do not have any reason to believe that we will be required to make any material payments under these indemnity provisions.

Operating Leases – At March 31, 2018, we had commitments for future minimum lease payments under operating leases with initial or remaining non-cancelable lease terms in excess of one year of approximately \$2.4 billion.

18. Share Repurchase Program

Effective January 1, 2017, our Board of Directors authorized the repurchase of up to 120 million shares of our common stock by December 31, 2020, replacing our previous repurchase program. As of March 31, 2018, we repurchased a total of \$24.4 billion of our common stock since the commencement of our repurchase programs in 2007. The table below represents shares repurchased under this repurchase program during this reporting period.

| | Number of Shares | | Average Price Paid | |
|--|-------------------|-------------------|--------------------|-----------|
| | Purchased 2018 | Purchased 2017 | 2018 | 2017 |
| First quarter | 9,259,004 | 7,531,300 | \$ 132.84 | \$ 106.55 |
| Remaining number of shares that may be repurchased under current authority | | | 74,388,148 | |

Management's assessments of market conditions and other pertinent factors guide the timing and volume of all repurchases. We expect to fund any share repurchases under this program through cash generated from operations, the sale or lease of various operating and non-operating properties, debt issuances, and cash on hand. Repurchased shares are recorded in treasury stock at cost, which includes any applicable commissions and fees.

From April 1, 2018, through April 25, 2018, we repurchased 2.8 million shares at an aggregate cost of approximately \$375 million.

19. Related Parties

UPRR and other North American railroad companies jointly own TTX Company (TTX). UPRR has a 36.79% economic and voting interest in TTX while the other North American railroads own the remaining interest. In accordance with ASC 323 Investments - Equity Method and Joint Venture, UPRR applies the equity method of accounting to our investment in TTX.

TTX is a railcar pooling company that owns railcars and intermodal wells to serve North America's railroads. TTX assists railroads in meeting the needs of their customers by providing railcars in an efficient, pooled environment. All railroads have the ability to utilize TTX railcars through car hire by renting railcars at stated rates.

UPRR had \$1.2 billion recognized as investments related to TTX in our Condensed Consolidated Statements of Financial Position as of both March 31, 2018, and December 31, 2017. TTX car hire expenses of \$105 million and \$86 million for the three months ended March 31, 2018, and 2017, respectively, are included in equipment and other rents in our Condensed Consolidated Statements of Income. In addition, UPRR had accounts payable to TTX of \$68 million and \$69 million as of March 31, 2018, and December 31, 2017, respectively.

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

UNION PACIFIC CORPORATION AND SUBSIDIARY COMPANIES

RESULTS OF OPERATIONS

Three Months Ended March 31, 2018, Compared to

Three Months Ended March 31, 2017

For purposes of this report, unless the context otherwise requires, all references herein to "UPC", "Corporation", "Company", "we", "us", and "our" shall mean Union Pacific Corporation and its subsidiaries, including Union Pacific Railroad Company, which we separately refer to as "UPRR" or the "Railroad".

The following discussion should be read in conjunction with the Condensed Consolidated Financial Statements and applicable notes to the Condensed Consolidated Financial Statements, Item 1, and other information included in this report. Our Condensed Consolidated Financial Statements are unaudited and reflect all adjustments (consisting only of normal and recurring adjustments) that are, in the opinion of management, necessary for their fair presentation in conformity with accounting principles generally accepted in the United States of America (GAAP).

The Railroad, along with its subsidiaries and rail affiliates, is our one reportable business segment. Although we provide and analyze revenue by commodity group, we treat the financial results of the Railroad as one segment due to the integrated nature of our rail network.

Available Information

Our Internet website is www.up.com. We make available free of charge on our website (under the "Investors" caption link) our Annual Reports on Form 10-K; our Quarterly Reports on Form 10-Q; eXtensible Business Reporting Language (XBRL) documents; our current reports on Form 8-K; our proxy statements; Forms 3, 4, and 5, filed on behalf of directors and executive officers; and amendments to any such reports filed or furnished pursuant to the Securities Exchange Act of 1934, as amended (the Exchange Act), as soon as reasonably practicable after such

material is electronically filed with, or furnished to, the Securities and Exchange Commission (SEC). We also make available on our website previously filed SEC reports and exhibits via a link to EDGAR on the SEC's Internet site at www.sec.gov. We provide these previously filed reports as a convenience and their contents reflect only information that was true and correct as of the date of the report. We assume no obligation to update this historical information. Additionally, our corporate governance materials, including By-Laws, Board Committee charters, governance guidelines and policies, and codes of conduct and ethics for directors, officers, and employees are available on our website. From time to time, the corporate governance materials on our website may be updated as necessary to comply with rules issued by the SEC and the New York Stock Exchange or as desirable to promote the effective and efficient governance of our company. Any security holder wishing to receive, without charge, a copy of any of our SEC filings or corporate governance materials should send a written request to: Corporate Secretary, Union Pacific Corporation, 1400 Douglas Street, Omaha, NE 68179.

References to our website address in this report, including references in Management's Discussion and Analysis of Financial Condition and Results of Operations, Item 2, are provided as a convenience and do not constitute, and should not be deemed, an incorporation by reference of the information contained on, or available through, the website. Therefore, such information should not be considered part of this report.

Critical Accounting Policies and Estimates

We base our discussion and analysis of our financial condition and results of operations upon our Condensed Consolidated Financial Statements. The preparation of these financial statements requires estimation and judgment that affect the reported amounts of revenues, expenses, assets, and liabilities. We base our estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. If these estimates differ materially from actual results, the impact on the Condensed Consolidated Financial Statements may be material. Our critical accounting policies are available in Item 7 of our 2017 Annual Report on Form 10-K. In 2018, there were changes to our significant accounting policies as a result of adopting ASU 2014-09

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on January 1, 2018. See Notes 2 and 3 of the Condensed Consolidated Financial Statements for further information.

RESULTS OF OPERATIONS

Quarterly Summary

We reported earnings of \$1.68 per diluted share on net income of \$1.3 billion in the first quarter of 2018 compared to earnings of \$1.32 per diluted share on net income of \$1.1 billion for the first quarter of 2017. Freight revenues increased 7% in the first quarter compared to the same period in 2017 driven by a 5% increase in average revenue per car (ARC) due to higher fuel surcharge revenue and core pricing gains. Volume grew 2%, with increased demand in shale-related frac sand, intermodal, petroleum products, and automotive parts shipments, which more than offset declines in grain, coal, and rock shipments. These top line results contributed to operating income growth of 8% compared to 2017, despite a 22% increase in fuel price. Net income increased 22%, driven by base business operations and a lower federal tax rate, which was implemented on January 1, 2018, resulting from the passage of The Tax Cuts and Jobs Act (the “Tax Act”) in late 2017.

In the first quarter of 2018, our productivity initiatives yielded approximately \$35 million, net of additional expenses due to network operational challenges, including higher labor, equipment rental, locomotive maintenance, and fuel consumption costs. Despite our operational challenges, we handled volume growth of 2% with a 1% decline in work force levels, demonstrating progress in other resource productivity initiatives, including engineering capital projects along with management and administrative reductions. At the end of the first quarter, approximately 300 employees across all crafts were either furloughed or in alternate work status, and approximately 300 high-horsepower, road locomotives were in storage.

As reported to the Association of American Railroads (AAR) in the first quarter 2018, average train speed decreased 4% to 24.8 miles per hour while average terminal dwell time increased 8% to 33.0 hours compared to the same period of 2017. Network congestion on key routes and terminals, created in part by high freight car inventory levels, negatively impacted overall fluidity, average train speed, and terminal dwell. Continued implementation and testing of Positive Train Control across a larger portion of our network also negatively impacted overall average train speed.

Operating Revenues

| Millions, for the Three Months Ended March 31, | 2018 | 2017 | Change | % |
|---|----------|----------|--------|---|
| Freight revenues | \$ 5,122 | \$ 4,794 | 7 | % |
| Subsidiary revenues | 217 | 215 | 1 | |
| Accessorial revenues | 121 | 106 | 14 | |
| Other | 15 | 17 | (12) | |
| Total | \$ 5,475 | \$ 5,132 | 7 | % |

We generate freight revenues by transporting freight or other materials from our four commodity groups. Prior to 2018, we reported on six commodity groups, thus 2017 commodity, average revenue per car, and carloadings have been realigned to the new reporting format. Freight revenues vary with volume (carloads) and ARC. Changes in price, traffic mix and fuel surcharges drive ARC. We provide some of our customers with contractual incentives for meeting or exceeding specified cumulative volumes or shipping to and from specific locations, which we record as reductions to freight revenues based on the actual or projected future shipments. We recognize freight revenues over time as shipments move from origin to destination. The allocation of revenue between reporting periods is based on the relative transit time in each reporting period with expenses recognized as incurred.

Other revenues consist primarily of revenues earned by our subsidiaries and accessorial revenues. Non-rail subsidiary revenues are generally recognized over time as freight moves from origin to destination. The allocation of revenue between reporting periods is based on the relative transit time in each reporting period with expenses recognized as incurred. Accessorial revenues are recognized at a point in time as performance obligations are satisfied.

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Freight revenues increased 7% during the first quarter of 2018 compared to 2017 resulting from higher fuel surcharge revenue, core pricing gains, and 2% volume growth. Growth in frac sand, intermodal, petroleum products, and automotive parts shipments more than offset declines in grain, coal, and rock shipments.

Each of our commodity groups includes revenue from fuel surcharges. Freight revenues from fuel surcharge programs were \$353 million in the first quarter of 2018 compared to \$212 million in the same period of 2017. Higher fuel surcharge revenue resulted from higher year-over-year fuel prices, partially offset by a lag in fuel surcharge recovery due to the sequential increase in fuel price from the fourth quarter of 2017 (it can generally take up to two months for changing fuel prices to affect fuel surcharge recoveries).

Non-freight revenues increased in the first quarter of 2018 compared to 2017 driven primarily by higher accessorial revenues associated with carload and container volume growth.

The following tables summarize the year-over-year changes in freight revenues, revenue carloads, and ARC by commodity type:

| Freight Revenues Millions, for the Three Months Ended March 31, | 2018 | 2017 | % Change | |
|---|----------|----------|-------------|---|
| Agricultural Products | \$ 1,098 | \$ 1,094 | - | % |
| Energy | 1,173 | 1,024 | 15 | |
| Industrial | 1,340 | 1,264 | 6 | |
| Premium | 1,511 | 1,412 | 7 | |
| Total | \$ 5,122 | \$ 4,794 | 7 | % |

| Revenue Carloads Thousands, for the Three Months Ended March 31, | 2018 | 2017 | % Change | |
|--|-------|-------|-------------|---|
| Agricultural Products | 279 | 290 | (4) | % |
| Energy | 419 | 395 | 6 | |
| Industrial | 411 | 403 | 2 | |
| Premium | 1,016 | 1,000 | 2 | |

| | | | | |
|-------|-------|-------|---|---|
| Total | 2,125 | 2,088 | 2 | % |
|-------|-------|-------|---|---|

| Average Revenue per Car for the Three Months Ended March 31, | 2018 | 2017 | Change | % |
|---|----------|----------|--------|---|
| Agricultural Products | \$ 3,942 | \$ 3,768 | 5 | % |
| Energy | 2,799 | 2,593 | 8 | |
| Industrial | 3,262 | 3,140 | 4 | |
| Premium | 1,487 | 1,413 | 5 | |
| Average | \$ 2,411 | \$ 2,297 | 5 | % |

Agricultural Products – Freight revenue from agricultural products shipments was flat in the first quarter of 2018 compared to 2017 as core pricing gains and higher fuel surcharge revenue were offset by a 4% decrease in volumes. Grain shipments declined 14% in the first quarter compared to 2017 due to continued weakness in U.S. export competitiveness in the global market. This decrease was partially offset by strength in export fertilizer and ethanol shipments compared to 2017.

Energy – Freight revenue from energy shipments increased 15% in the first quarter of 2018 compared to 2017 due to 6% volume growth, mix of traffic, and higher fuel surcharge revenue. Continued strength in shale drilling activity and increased proppant intensity per drilling well drove substantial volume growth in frac sand shipments. Petroleum products shipments also increased due to stronger year-over-year demand for both crude and refined fuel products. Conversely, coal shipments out of the Powder River Basin (PRB) declined 3% compared to 2017 due to lower natural gas prices and continued market headwinds. Coal shipments out of Colorado and Utah declined 4% as weaker domestic shipments were partially offset by stronger export demand.

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Industrial – Freight revenue from industrial shipments increased 6% in the first quarter of 2018 compared to 2017 due to core pricing gains, higher fuel surcharge revenue, and 2% volume growth. Volume growth was driven by increased metals shipments due to strength in domestic energy markets, as well as increased growth in government, waste, lumber, and plastics shipments. Conversely, rock shipments declined due to weather-related delays in Texas.

Premium – Freight revenue from premium shipments increased 7% in the first quarter compared to 2017 due to higher fuel surcharge revenue, core pricing gains, and 2% volume growth, more than offsetting negative mix of traffic. Domestic intermodal shipments, including containerized automotive parts, grew 5%, driven by tighter truck capacity and continued truck-to-rail conversions. Conversely, international intermodal shipments decreased 2% compared to 2017 due primarily to reduced westbound export shipments. In addition, finished vehicle shipments decreased 2% resulting from lower production levels in response to softer vehicle sales and high inventories.

Mexico Business – Each of our commodity groups includes revenue from shipments to and from Mexico. Revenue from Mexico business increased 2% to \$579 million in the first quarter of 2018 compared to 2017 driven by higher fuel surcharge revenue and core pricing gains. Volume was flat year-over-year as growth in coal and petroleum products shipments were offset by declines in grain and auto parts shipments.

Operating Expenses

| Millions, for the Three Months Ended March 31, | 2018 | 2017 | % Change | |
|---|----------|----------|-------------|---|
| Compensation and benefits | \$ 1,273 | \$ 1,262 | 1 | % |
| Purchased services and materials | 599 | 566 | 6 | |
| Fuel | 589 | 460 | 28 | |
| Depreciation | 543 | 520 | 4 | |
| Equipment and other rents | 266 | 276 | (4) | |
| Other | 266 | 260 | 2 | |
| Total | \$ 3,536 | \$ 3,344 | 6 | % |

Operating expenses increased \$192 million in the first quarter compared to 2017 driven by higher fuel prices, volume-related costs, network operational challenges, depreciation, and increased state and local taxes. Lower management and administrative wage and benefit costs resulting from the carry-over effect of the workforce reduction plan in 2017, lower casualty costs, and locomotive and freight car lease expenses partially offset these increases.

Compensation and Benefits – Compensation and benefits include wages, payroll taxes, health and welfare costs, pension costs, other postretirement benefits, and incentive costs. For the first quarter, expenses increased 1% compared to 2017 due to volume-related costs, network operational challenges, and increased Train, Engine and Yard (TE&Y) training expenses. Lower management and administrative wage and benefit costs partially offset the increases.

Purchased Services and Materials – Expense for purchased services and materials includes the costs of services purchased from outside contractors and other service providers (including equipment maintenance and contract expenses incurred by our subsidiaries for external transportation services); materials used to maintain the Railroad's lines, structures, and equipment; costs of operating facilities jointly used by UPRR and other railroads; transportation and lodging for train crew employees; trucking and contracting costs for intermodal containers; leased automobile maintenance expenses; and tools and supplies. Purchased services and materials increased 6% in the first quarter of 2018 compared to the same period of 2017. Volume-related costs (including higher subsidiary contract services), higher freight car repair expense for leased car expirations, and increased locomotive repair costs to maintain a larger active fleet drove the increase. We also incurred inflationary cost pressures on transportation-related contract services incurred at our subsidiaries that broker intermodal and transload services.

Depreciation – The majority of depreciation relates to road property, including rail, ties, ballast, and other track material. A higher depreciable asset base, reflecting recent years' higher capital spending, increased depreciation expense in the first quarter of 2018 compared to 2017.

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Fuel – Fuel includes locomotive fuel and fuel for highway and non-highway vehicles and heavy equipment. Locomotive diesel fuel prices, which averaged \$2.13 per gallon (including taxes and transportation costs) in the first quarter of 2018, compared to \$1.75 per gallon in the same period in 2017, increased expenses by \$102 million. In addition, fuel costs were higher as gross ton-miles increased 4% compared to the same period in 2017. The fuel consumption rate (c-rate), computed as gallons of fuel consumed divided by gross ton-miles in thousands, increased 2% compared to the first quarter of 2017.

Equipment and Other Rents – Equipment and other rents expense primarily includes rental expense that the Railroad pays for freight cars owned by other railroads or private companies; freight car, intermodal, and locomotive leases; and office and other rentals. Equipment and other rents expense decreased 4% in the first quarter compared to 2017, driven by lower locomotive and freight car lease expenses, combined with higher equity income from certain equity-method affiliates as a result of a legal settlement and the lower federal tax rate implemented January 1, 2018. Increased car rent expense due to volume growth and slower network velocity partially offset these decreases.

Other – Other expenses include state and local taxes; freight, equipment and property damage; utilities, insurance, personal injury, environmental, employee travel, telephone and cellular, computer software, bad debt and other general expenses. Other costs increased 2% in the first quarter compared to 2017 due to higher state and local taxes and environmental expense. Lower personal injury expense due to our continued improvement in employee safety performance, reduced costs for destroyed equipment owned by third parties, and lower freight damage expense partially offset these increases compared to 2017.

Non-Operating Items

| Millions, for the Three Months Ended March 31, | 2018 | 2017 | % | |
|---|---------|-------|--------|---|
| | | | Change | |
| Other income/(expense) | \$ (42) | \$ 72 | U | % |
| Interest expense | (186) | (172) | 8 | |
| Income taxes | (401) | (616) | (35) | |

Other Income/(Expense) – Other income/(expense) decreased in the first quarter of 2018 as a result of an \$85 million expense associated with early-extinguishment of outstanding debentures and mortgage bonds recognized in the first quarter of 2018. Higher real estate sale gains in the first quarter of 2017 also drove the year-over-year decrease.

Interest Expense – Interest expense increased in the first quarter of 2018 compared to 2017 due to an increase in the weighted-average debt level of \$17.1 billion in 2018 compared to \$15.0 billion in 2017. The effective interest rate was 4.4% and 4.6% in the first quarter of 2018 and 2017, respectively.

Income Taxes – Income taxes were lower in the first quarter of 2018 compared to 2017, driven by a lower federal income tax rate due to the enactment of the Tax Act on December 22, 2017. The Tax Act reduced the federal income tax rate from 35% to 21% effective January 1, 2018. Our effective tax rates for the first quarter of 2018 and 2017 were 23.4% and 36.5%, respectively.

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OTHER OPERATING/PERFORMANCE AND FINANCIAL STATISTICS

We report a number of key performance measures weekly to the AAR. We provide this data on our website at www.up.com/investor/aar-stb_reports/index.htm.

Operating/Performance Statistics

Railroad performance measures are included in the table below:

| For the Three Months Ended March 31, | 2018 | 2017 | % Change | |
|--------------------------------------|--------|--------|----------|-----|
| Average train speed (miles per hour) | 24.8 | 25.7 | (4) | % |
| Average terminal dwell time (hours) | 33.0 | 30.6 | 8 | % |
| Gross ton-miles (billions) | 226.9 | 218.9 | 4 | % |
| Revenue ton-miles (billions) | 117.4 | 114.1 | 3 | % |
| Operating ratio | 64.6 | 65.2 | (0.6) | pts |
| Employees (average) | 41,735 | 42,069 | (1) | % |

Average Train Speed – Average train speed is calculated by dividing train miles by hours operated on our main lines between terminals. Average train speed, as reported to the AAR, decreased 4% in the first quarter of 2018 compared to the same period in 2017 largely due to network congestion on key routes and terminals, created in part by high freight car inventory levels and execution challenges. Continued implementation and testing of Positive Train Control across a larger portion of our network also negatively impacted overall average train speed.

Average Terminal Dwell Time – Average terminal dwell time is the average time that a rail car spends at our terminals. Lower average terminal dwell time improves asset utilization and service. Average terminal dwell time in the first quarter of 2018 increased 8%, compared to the same period of 2017 largely due to network congestion on key routes and terminals, created, in part, by high freight car inventory levels and execution challenges.

Gross and Revenue Ton-Miles – Gross ton-miles are calculated by multiplying the weight of loaded and empty freight cars by the number of miles hauled. Revenue ton-miles are calculated by multiplying the weight of freight by the number of tariff miles. Gross ton-miles and revenue ton-miles increased 4% and 3%, respectively, during the first quarter of 2018 compared to 2017, driven by a 2% increase in carloadings. Changes in commodity mix drove the variances in year-over-year increases between gross ton-miles, revenue ton-miles and carloads.

Operating Ratio – Operating ratio is our operating expenses reflected as a percentage of operating revenue. Our first quarter operating ratio of 64.6% improved 0.6 points mainly driven by core pricing gains and volume growth, which more than offset higher fuel prices and other cost hurdles.

Employees – Employee levels decreased 1% in the first quarter of 2018 compared to the same period in 2017 despite a 2% increase in volume levels. A smaller capital workforce and fewer management and administrative personnel drove the reduction and more than offset an increase in TE&Y employees in training.

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Debt to Capital / Adjusted Debt to Capital

| | Mar. 31, | Dec. 31, |
|------------------------------|-----------|-----------|
| Millions, Except Percentages | 2018 | 2017 |
| Debt (a) | \$ 17,588 | \$ 16,944 |
| Equity | 24,389 | 24,856 |
| Capital (b) | \$ 41,977 | \$ 41,800 |
| Debt to capital (a/b) | 41.9% | 40.5% |

| | Mar. 31, | Dec. 31, |
|--|-----------|-----------|
| Millions, Except Percentages | 2018 | 2017 |
| Debt | \$ 17,588 | \$ 16,944 |
| Net present value of operating leases | 1,989 | 2,140 |
| Unfunded pension and OPEB, net of taxes of \$145 and \$238 | 473 | 396 |
| Adjusted debt (a) | 20,050 | 19,480 |
| Equity | 24,389 | 24,856 |
| Adjusted capital (b) | \$ 44,439 | \$ 44,336 |
| Adjusted debt to capital (a/b) | 45.1% | 43.9% |

Adjusted debt to capital is a non-GAAP financial measure under SEC Regulation G and Item 10 of SEC Regulation S-K, and may not be defined and calculated by other companies in the same manner. We believe this measure is important to management and investors in evaluating the total amount of leverage in our capital structure, including off-balance sheet lease obligations, which we generally incur in connection with financing the acquisition of locomotives and freight cars and certain facilities. Operating leases were discounted using 4.4% at March 31, 2018, and 4.6% at December 31, 2017. The discount rate reflects our year-to-date effective interest rate. We monitor the ratio of adjusted debt to capital as we manage our capital structure to balance cost-effective and efficient access to the capital markets with the Corporation's overall cost of capital. Adjusted debt to capital should be considered in addition to, rather than as a substitute for, debt to capital. The tables above provide reconciliations from debt to capital to adjusted debt to capital.

LIQUIDITY AND CAPITAL RESOURCES

Financial Condition

Cash Flows

Millions,

| for the Three Months Ended March 31, | 2018 | 2017 |
|---|----------|----------|
| Cash provided by operating activities | \$ 1,901 | \$ 1,883 |
| Cash used in investing activities | (919) | (843) |
| Cash used in financing activities | (1,209) | (1,268) |
| Net change in cash and cash equivalents | \$ (227) | \$ (228) |

Operating Activities

Cash provided by operating activities increased in the first three months of 2018 compared to the same period of 2017 due to higher income, which was partially offset by payments made for past wages as a result of national labor negotiations ratified in late 2017. Although our reported net income in the first quarter of 2018 reflects the lower federal tax effective January 1, 2018, our first quarter estimated tax payment is not paid until the second quarter.

Investing Activities

Increased capital investments drove higher cash used in investing activities in the first three months of 2018 compared to the same period in 2017.

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The table below details cash capital investments:

| Millions, for the Three Months Ended March 31, | 2018 | 2017 |
|---|--------|--------|
| Rail and other track material | \$ 128 | \$ 154 |
| Ties | 114 | 118 |
| Ballast | 45 | 51 |
| Other [a] | 86 | 89 |
| Total road infrastructure replacements | 373 | 412 |
| Line expansion and other capacity projects | 42 | 11 |
| Commercial facilities | 36 | 20 |
| Total capacity and commercial facilities | 78 | 31 |
| Locomotives and freight cars [b] | 300 | 224 |
| Positive train control | 41 | 76 |
| Technology and other | 118 | 68 |
| Total cash capital investments | \$ 910 | \$ 811 |

[a]Other includes bridges and tunnels, signals, other road assets, and road work equipment.

[b]Locomotives and freight cars include lease buyouts of \$210 million in 2018 and \$144 million in 2017.

Capital Plan

As previously stated, we expect our 2018 capital plan to be approximately \$3.3 billion, which may be revised if business conditions or the regulatory environment affect our ability to generate sufficient returns on these investments.

Financing Activities

Cash used in financing activities decreased \$59 million in the first three months of 2018 compared to the same period of 2017 driven by a \$533 million net increase in additional debt, partially offset by a \$407 million increase in shares repurchased and a \$76 million increase in dividends paid.

See Note 15 of the Condensed Consolidated Financial Statements for a description of all our outstanding financing arrangements and significant new borrowings.

Free Cash Flow – Free cash flow is defined as cash provided by operating activities less cash used in investing activities and dividends paid.

Free cash flow is not considered a financial measure under GAAP by SEC Regulation G and Item 10 of SEC Regulation S-K and may not be defined and calculated by other companies in the same manner. We believe free cash flow is important to management and investors in evaluating our financial performance and measures our ability to generate cash without additional external financing. Free cash flow should be considered in addition to, rather than as a substitute for, cash provided by operating activities. The following table reconciles cash provided by operating activities (GAAP measure) to free cash flow (non-GAAP measure):

| Millions, for the Three Months Ended March 31, | 2018 | 2017 |
|---|----------|----------|
| Cash provided by operating activities | \$ 1,901 | \$ 1,883 |
| Cash used in investing activities | (919) | (843) |
| Dividends paid | (568) | (492) |
| Free cash flow | \$ 414 | \$ 548 |

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Share Repurchase Program

Effective January 1, 2017, our Board of Directors authorized the repurchase of up to 120 million shares of our common stock by December 31, 2020, replacing our previous repurchase program. As of March 31, 2018, we repurchased a total of \$24.4 billion of our common stock since the commencement of our repurchase programs in 2007. The table below represents shares repurchased under this repurchase program during this reporting period.

| | Number of Shares | | Average Price Paid | |
|--|-------------------|-------------------|--------------------|-----------|
| | Purchased 2018 | Purchased 2017 | 2018 | 2017 |
| First quarter | 9,259,004 | 7,531,300 | \$ 132.84 | \$ 106.55 |
| Remaining number of shares that may be repurchased under current authority | | | 74,388,148 | |

Management's assessments of market conditions and other pertinent factors guide the timing and volume of all repurchases. We expect to fund any share repurchases under this program through cash generated from operations, the sale or lease of various operating and non-operating properties, debt issuances, and cash on hand. Repurchased shares are recorded in treasury stock at cost, which includes any applicable commissions and fees.

From April 1, 2018, through April 25, 2018, we repurchased 2.8 million shares at an aggregate cost of approximately \$375 million.

Off-Balance Sheet Arrangements, Contractual Obligations, and Commercial Commitments

As described in the notes to the Condensed Consolidated Financial Statements and as referenced in the tables below, we have contractual obligations and commercial commitments that may affect our financial condition. However, based on our assessment of the underlying provisions and circumstances of our contractual obligations and commercial commitments, including material sources of off-balance sheet and structured finance arrangements, there is no known trend, demand, commitment, event, or uncertainty that is reasonably likely to occur that would have a material adverse effect on our consolidated results of operations, financial condition, or liquidity. In addition, our commercial obligations, financings, and commitments are customary transactions that are similar to those of other comparable corporations, particularly within the transportation industry.

The following tables identify material obligations and commitments as of March 31, 2018:

| Contractual Obligations Millions | Total | Apr. 1 Payments Due by Dec. 31, through Dec. 31, | | | | | After | |
|-------------------------------------|-----------|--|----------|----------|----------|----------|-----------|--------|
| | | 2018 | 2019 | 2020 | 2021 | 2022 | 2022 | Other |
| Debt [a] | \$ 29,232 | \$ 1,750 | \$ 1,756 | \$ 1,435 | \$ 1,091 | \$ 1,331 | \$ 21,869 | \$ - |
| Operating leases [b] | 2,450 | 193 | 362 | 298 | 260 | 222 | 1,115 | - |
| Capital lease obligations [c] | 981 | 87 | 152 | 161 | 164 | 147 | 270 | - |
| Purchase obligations [d] | 3,130 | 1,566 | 658 | 462 | 260 | 54 | 98 | 32 |
| Other postretirement benefits [e] | 467 | 38 | 49 | 49 | 48 | 48 | 235 | - |
| Income tax contingencies [f] | 182 | 60 | - | - | - | - | - | 122 |
| Total contractual obligations | \$ 36,442 | \$ 3,694 | \$ 2,977 | \$ 2,405 | \$ 1,823 | \$ 1,802 | \$ 23,587 | \$ 154 |

[a]Excludes capital lease obligations of \$819 million, as well as unamortized discount and deferred issuance costs of (\$793) million. Includes an interest component of \$11,670 million.

[b] Includes leases for locomotives, freight cars, other equipment, and real estate.

[c]Represents total obligations, including interest component of \$162 million.

[d]Purchase obligations include locomotive maintenance contracts; purchase commitments for fuel purchases, locomotives, ties, ballast, and rail; and agreements to purchase other goods and services. For amounts where we cannot reasonably estimate the year of settlement, they are included in the Other column.

[e]Includes estimated other postretirement, medical, and life insurance payments and payments made under the unfunded pension plan for the next ten years.

[f]Future cash flows for income tax contingencies reflect the recorded liabilities and assets for unrecognized tax benefits, including any interest or penalties, as of March 31, 2018. For amounts where the year of settlement is uncertain, they are included in the Other column.

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| Other Commercial Commitments Millions | Total | Amount of Commitment | | | | | |
|--|----------|-------------------------------|------------------------|------|------|------|------|
| | | Apr. 1 through Dec. 31, | Expiration by Dec. 31, | | | | |
| | | 2018 | 2019 | 2020 | 2021 | 2022 | 2022 |
| Credit facilities [a] | \$ 1,700 | \$ - | \$ 1,700 | \$ - | \$ - | \$ - | \$ - |
| Receivables securitization facility [b] | 650 | - | 650 | - | - | - | - |
| Guarantees [c] | 33 | 11 | 7 | 5 | 5 | 5 | - |
| Standby letters of credit [d] | 20 | 12 | 8 | - | - | - | - |
| Total commercial commitments | \$ 2,403 | \$ 23 | \$ 2,365 | \$ 5 | \$ 5 | \$ 5 | \$ - |

[a] None of the credit facility was used as of March 31, 2018.

[b] \$650 million of the receivables securitization facility was utilized as of March 31, 2018, which is accounted for as debt. The full program matures in July 2019.

[c] Includes guaranteed obligations related to our affiliated operations.

[d] None of the letters of credit were drawn upon as of March 31, 2018.

OTHER MATTERS

Asserted and Unasserted Claims – Various claims and lawsuits are pending against us and certain of our subsidiaries. We cannot fully determine the effect of all asserted and unasserted claims on our consolidated results of operations, financial condition, or liquidity. To the extent possible, we have recorded a liability where asserted and unasserted claims are considered probable and where such claims can be reasonably estimated. We do not expect that any known lawsuits, claims, environmental costs, commitments, contingent liabilities, or guarantees will have a material adverse effect on our consolidated results of operations, financial condition, or liquidity after taking into account liabilities and insurance recoveries previously recorded for these matters.

Indemnities – We are contingently obligated under a variety of indemnification arrangements, although in some cases the extent of our potential liability is limited, depending on the nature of the transactions and the agreements. Due to uncertainty as to whether claims will be made or how they will be resolved, we cannot reasonably determine the probability of an adverse claim or reasonably estimate any adverse liability or the total maximum exposure under these indemnification arrangements. We do not have any reason to believe that we will be required to make any material payments under these indemnity provisions.

Accounting Pronouncements – See Note 2 to the Condensed Consolidated Financial Statements.

Labor Agreements – The U.S. Class I railroads have been in collective bargaining with rail labor unions since January 2015. Existing agreements remain in effect until new agreements are ratified or the Railway Labor Act’s (RLA) procedures (which include mediation, potential arbitration, cooling-off periods, and the possibility of Presidential Emergency Boards and Congressional intervention) are exhausted. Through industry and local negotiations, UPRR reached tentative agreements with 12 of our 14 major rail unions. Of those, nine unions (representing nearly 70% of our agreement work force) have ratified the agreements by significant margins. A coalition of two unions (representing about 20% of our agreement work force) has agreed to the wage pattern contained in the tentative agreement, and to pursue final and binding arbitration to decide health plan design. That arbitration is scheduled for early May. Although the tentative agreement failed ratification with three unions, one union has accepted the agreement by executive action and the other two are either out for re-balloting or are in mediation with the National Mediation Board. Under the RLA, the National Mediation Board controls the timing of when to terminate mediation, moving the parties to either arbitration or presentations to a Presidential Emergency Board.

CAUTIONARY INFORMATION

Certain statements in this report, and statements in other reports or information filed or to be filed with the SEC (as well as information included in oral statements or other written statements made or to be made by us), are, or will be, forward-looking statements as defined by the Securities Act of 1933 and the Exchange Act. These forward-looking statements and information include, without limitation, the statements and information set forth under the caption “Liquidity and Capital Resources” in Item 2 regarding our capital plan and statements under the caption “Off-Balance Sheet Arrangements, Contractual Obligations, and

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Commercial Commitments.” Forward-looking statements and information also include any other statements or information in this report regarding: expectations as to operational or service improvements; expectations regarding the effectiveness of steps taken or to be taken to improve operations, service, infrastructure improvements, and transportation plan modifications; expectations as to cost savings, revenue growth, and earnings; the time by which goals, targets, or objectives will be achieved; projections, predictions, expectations, estimates, or forecasts as to our business, financial and operational results, future economic performance, and general economic conditions; proposed new products and services; estimates of costs relating to environmental remediation and restoration; estimates and expectations regarding tax matters, expectations that claims, litigation, environmental costs, commitments, contingent liabilities, labor negotiations or agreements, or other matters will not have a material adverse effect on our consolidated results of operations, financial condition, or liquidity and any other similar expressions concerning matters that are not historical facts.

Forward-looking statements and information reflect the good faith consideration by management of currently available information, and may be based on underlying assumptions believed to be reasonable under the circumstances. However, such information and assumptions (and, therefore, such forward-looking statements and information) are or may be subject to variables or unknown or unforeseeable events or circumstances over which management has little or no influence or control. The Risk Factors in Item 1A of our 2017 Annual Report on Form 10-K, filed February 9, 2018, could affect our future results and could cause those results or other outcomes to differ materially from those expressed or implied in the forward-looking statements, and this report, including this Item 2, should be read in conjunction with these Risk Factors. To the extent circumstances require or we deem it otherwise necessary, we will update or amend these risk factors in a Form 10-Q or Form 8-K. Information regarding new risk factors or material changes to our risk factors, if any, is set forth in Item 1A of Part II of this report. Forward-looking statements should not be read as a guarantee of future performance or results, and will not necessarily be accurate indications of the times that, or by which, such performance or results will be achieved. Forward-looking information is subject to risks and uncertainties that could cause actual performance or results to differ materially from those expressed in the statements.

Forward-looking statements speak only as of the date the statement was made. We assume no obligation to update forward-looking information to reflect actual results, changes in assumptions or changes in other factors affecting forward-looking information. If we do update one or more forward-looking statements, no inference should be drawn that we will make additional updates with respect thereto or with respect to other forward-looking statements.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

There were no material changes to the Quantitative and Qualitative Disclosures About Market Risk previously disclosed in our 2017 Annual Report on Form 10-K.

Item 4. Controls and Procedures

As of the end of the period covered by this report, the Corporation carried out an evaluation, under the supervision and with the participation of the Corporation's management, including the Corporation's Chief Executive Officer (CEO) and Executive Vice President and Chief Financial Officer (CFO), of the effectiveness of the design and operation of the Corporation's disclosure controls and procedures pursuant to Exchange Act Rules 13a-15 and 15d-15. In designing and evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives. Based upon that evaluation, the CEO and the CFO concluded that, as of the end of the period covered by this report, the Corporation's disclosure controls and procedures were effective to provide reasonable assurance that information required to be disclosed in our Exchange Act reports is recorded, processed, summarized and reported within the time periods specified by the SEC, and that such information is accumulated and communicated to management, including the CEO and CFO, as appropriate, to allow timely decisions regarding required disclosure.

Additionally, the CEO and CFO determined that there were no changes to the Corporation's internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) during the last fiscal quarter that materially affected, or are reasonably likely to materially affect, the Corporation's internal control over financial reporting.

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PART II. OTHER INFORMATION

Item 1. Legal Proceedings

From time to time, we are involved in legal proceedings, claims, and litigation that occur in connection with our business. We routinely assess our liabilities and contingencies in connection with these matters based upon the latest available information and, when necessary, we seek input from our third-party advisors when making these assessments. Consistent with SEC rules and requirements, we describe below material pending legal proceedings (other than ordinary routine litigation incidental to our business), material proceedings known to be contemplated by governmental authorities, other proceedings arising under federal, state, or local environmental laws and regulations (including governmental proceedings involving potential fines, penalties, or other monetary sanctions in excess of \$100,000), and such other pending matters that we may determine to be appropriate.

Environmental Matters

We receive notices from the EPA and state environmental agencies alleging that we are or may be liable under federal or state environmental laws for remediation costs at various sites throughout the U.S., including sites on the Superfund National Priorities List or state superfund lists. We cannot predict the ultimate impact of these proceedings and suits because of the number of potentially responsible parties involved, the degree of contamination by various wastes, the scarcity and quality of volumetric data related to many of the sites, and the speculative nature of remediation costs.

On May 2, 2015, a UPRR train en route from Chicago, Illinois to St. Louis, Missouri experienced an accidental release of diesel fuel in the vicinity of Sidney, Illinois. On May 29, 2015, the Railroad entered into an agreed-upon interim order to perform a comprehensive site investigation and remedial measures at the release site. On March 13, 2017, the State of Illinois issued a demand for \$125,000 in civil penalties as part of the ongoing enforcement action. UPRR entered into a settlement agreement with the State on March 2, 2018, to resolve this matter. Under the terms of the agreement, UPRR agreed to pay a \$70,000 penalty and \$17,659 to reimburse the State for its investigation and enforcement costs.

Certain California District Attorneys' sent a notice letter to UPRR of various environmental compliance violations beginning in 2010 in five counties in California. The Railroad has been involved in discussions with the district attorneys of Placer, Butte, Nevada, San Joaquin and San Bernardino counties (District Attorneys) regarding the various alleged environmental violations. The Railroad is currently in settlement negotiations with the District Attorneys with respect to the alleged violations. The District Attorneys are seeking penalties that may exceed the reporting threshold.

Information concerning environmental claims and contingencies and estimated remediation costs is set forth in Management's Discussion and Analysis of Financial Condition and Results of Operations – Critical Accounting Policies – Environmental, Item 7 of our 2017 Annual Report on Form 10-K.

Other Matters

Antitrust Litigation - As we reported in our Quarterly Report on Form 10-Q for the quarter ended June 30, 2007, 20 rail shippers (many of whom are represented by the same law firms) filed virtually identical antitrust lawsuits in various federal district courts against us and four other Class I railroads in the U.S. Currently, UPRR and three other Class I railroads are the named defendants in the lawsuit. For additional information on this lawsuit, please refer to Item 3. Legal Proceedings, under Other Matters, Antitrust Litigation in our most recently filed Annual Report on Form 10-K for the year ended December 31, 2017.

As we reported in our Current Report on Form 8-K, filed on June 10, 2011, the Railroad received a complaint filed in the U.S. District Court for the District of Columbia on June 7, 2011, by Oxbow Carbon & Minerals LLC and related entities (Oxbow). The parties are currently conducting discovery in this matter. For additional information on Oxbow, please refer to Item 3. Legal Proceedings, under Other Matters, Antitrust Litigation in our most recently filed Annual Report on Form 10-K for the year ended December 31, 2017.

We continue to deny the allegations that our fuel surcharge programs violate the antitrust laws or any other laws. We believe that these lawsuits are without merit, and we will vigorously defend our actions. Therefore,

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we currently believe that these matters will not have a material adverse effect on any of our results of operations, financial condition, and liquidity.

Item 1A. Risk Factors

There were no material changes from the risk factors previously disclosed in our 2017 Annual Report on Form 10-K.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

Purchases of Equity Securities – The following table presents common stock repurchases during each month for the first quarter of 2018:

| Period | Total Number of Shares Purchased [a] | Average Price Paid Per Share or Program [b] | Total Number of Shares Purchased as Part of a Publicly Announced Plan | Maximum Number of Shares That May Be Purchased Under Current Authority [b] |
|------------------------|--------------------------------------|---|---|--|
| Jan. 1 through Jan. 31 | 1,562,752 | \$ 136.25 | 1,511,102 | 82,136,050 |
| Feb. 1 through Feb. 28 | 4,058,578 | 130.35 | 3,783,000 | 78,353,050 |
| Mar. 1 through Mar. 31 | 3,974,621 | 134.00 | 3,964,902 | 74,388,148 |
| Total | 9,595,951 | \$ 132.82 | 9,259,004 | N/A |

[a] Total number of shares purchased during the quarter includes 336,947 shares delivered or attested to UPC by employees to pay stock option exercise prices, satisfy excess tax withholding obligations for stock option exercises or vesting of retention units, and pay withholding obligations for vesting of retention shares.

[b] Effective January 1, 2017, our Board of Directors authorized the repurchase of up to 120 million shares of our common stock by December 31, 2020, replacing our previous repurchase program. These repurchases may be made on the open market or through other transactions. Our management has sole discretion with respect to determining the timing and amount of these transactions.

Dividend Restrictions – Our revolving credit facility includes a debt-to-net worth covenant (discussed in Note 15 of the Condensed Consolidated Financial Statements) that, under certain circumstances, restricts the payment of cash

dividends to our shareholders. The amount of retained earnings available for dividends was \$15.6 billion and \$16.4 billion at March 31, 2018, and December 31, 2017, respectively.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Mine Safety Disclosures

Not Applicable.

Item 5. Other Information

None.

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Item 6. Exhibits

| Exhibit No. | Description |
|---------------------------------|---|
| Filed with this Statement | |
| 12 | <u>Ratio of Earnings to Fixed Charges for the Three Months Ended March 31, 2018 and 2017.</u> |
| 31(a) | <u>Certifications Pursuant to Rule 13a-14(a), of the Exchange Act, as Adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 – Lance M. Fritz.</u> |
| 31(b) | <u>Certifications Pursuant to Rule 13a-14(a), of the Exchange Act, as Adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 - Robert M. Knight, Jr.</u> |
| 32 | <u>Certifications Pursuant to 18</u> |

101

U.S.C. Section
1350, as
Adopted
pursuant to
Section 906 of
the
Sarbanes-Oxley
Act of 2002 –
Lance M. Fritz
and Robert M.
Knight, Jr.
eXtensible
Business
Reporting
Language
(XBRL)
documents
submitted
electronically:
101.INS (XBRL
Instance
Document),
101.SCH
(XBRL
Taxonomy
Extension
Schema
Document),
101.CAL
(XBRL
Calculation
Linkbase
Document),
101.LAB
(XBRL
Taxonomy
Label Linkbase
Document),
101.DEF
(XBRL
Taxonomy
Definition
Linkbase
Document) and
101.PRE
(XBRL
Taxonomy
Presentation
Linkbase
Document). The
following

financial and related information from Union Pacific Corporation's Quarterly Report on Form 10-Q for the period ended March 31, 2018 (filed with the SEC on April 26, 2018), is formatted in XBRL and submitted electronically herewith: (i) Condensed Consolidated Statements of Income for the periods ended March 31, 2018 and 2017, (ii) Condensed Consolidated Statements of Comprehensive Income for the periods ended March 31, 2018 and 2017, (iii) Condensed Consolidated Statements of Financial Position at March 31, 2018 and December 31, 2017, (iv) Condensed Consolidated Statements of Cash Flows for the periods ended March 31, 2018 and 2017, (v) Condensed

Consolidated
Statements of
Changes in
Common
Shareholders'
Equity for the
periods ended
March 31, 2018
and 2017, and
(vi) the Notes to
the Condensed
Consolidated
Financial
Statements.

Incorporated by Reference

3(a) Restated
Articles of
Incorporation of
UPC, as
amended and
restated through
June 27, 2011,
and as further
amended May
15, 2014, are
incorporated
herein by
reference to
Exhibit 3(a) to
the Corporation's
Quarterly
Report on Form
10-Q for the
quarter ended
June 30, 2014.

3(b) By-Laws of
UPC, as
amended,
effective
November 19,
2015, are
incorporated
herein by
reference to
Exhibit 3.2 to
the Corporation's
Current Report
on Form 8-K
dated November
19, 2015.

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SIGNATURES

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

Dated: April 26, 2018

UNION PACIFIC CORPORATION (Registrant)

By /s/ Robert M. Knight, Jr.
Robert M. Knight, Jr.
Executive Vice President and
Chief Financial Officer
(Principal Financial Officer)

By /s/ Todd M. Rynaski
Todd M. Rynaski
Vice President and Controller
(Principal Accounting Officer)