

CSX CORP
Form 10-K
February 14, 2017

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-K

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

For the fiscal year ended December 30, 2016

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 1-8022

CSX CORPORATION

(Exact name of registrant as specified in its charter)

Virginia

62-1051971

(State or other jurisdiction of incorporation or organization)

(I.R.S. Employer Identification No.)

500 Water Street, 15th Floor, Jacksonville, FL

32202 (904) 359-3200

(Address of principal executive offices)

(Zip Code) (Telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class

Name of exchange on which registered

Common Stock, \$1 Par Value

Nasdaq Global Select Market

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

Yes No

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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of the registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. (as defined in Exchange Act Rule 12b-2).

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 Exchange Act Rule 12b-2).

Yes () No (X)

On June 24, 2016 (which is the last day of the second quarter and the required date to use), the aggregate market value of the Registrant's voting stock held by non-affiliates was approximately \$24 billion (based on the New York Stock Exchange closing price on such date).

There were 926,446,993 shares of Common Stock outstanding on January 27, 2017 (the latest practicable date that is closest to the filing date).

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant's Definitive Proxy Statement (the "Proxy Statement") to be filed no later than 120 days after the end of the fiscal year with respect to its 2017 annual meeting of shareholders.

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CSX CORPORATION
PART I

Item 1. Business

CSX Corporation (“CSX”), and together with its subsidiaries (the “Company”), based in Jacksonville, Florida, is one of the nation's leading transportation companies. The Company provides rail-based transportation services including traditional rail service and the transport of intermodal containers and trailers.

The Company’s number of employees was approximately 27,000 as of December 2016, which includes approximately 22,000 union employees. Most of the Company’s employees provide or support transportation services.

CSX Transportation, Inc.

CSX’s principal operating subsidiary, CSX Transportation, Inc. (“CSXT”), provides an important link to the transportation supply chain through its approximately 21,000 route mile rail network, which serves major population centers in 23 states east of the Mississippi River, the District of Columbia and the Canadian provinces of Ontario and Quebec. It has access to over 70 ocean, river and lake port terminals along the Atlantic and Gulf Coasts, the Mississippi River, the Great Lakes and the St. Lawrence Seaway. The Company’s intermodal business links customers to railroads via trucks and terminals. CSXT also serves thousands of production and distribution facilities through track connections to approximately 240 short-line and regional railroads.

Lines of Business

During 2016, the Company's services generated \$11.1 billion of revenue and served three primary lines of business:

The merchandise business shipped 2.8 million carloads and generated 64% of revenue and 43% of volume in 2016.

• The Company’s merchandise business is comprised of shipments in the following diverse markets: agricultural and food products, fertilizers, chemicals, automotive, metals and equipment, minerals and forest products.

The coal business shipped 838 thousand carloads and accounted for 17% of revenue and 13% of volume in 2016. The Company transports domestic coal, coke and iron ore to electricity-generating power plants, steel manufacturers and industrial plants as well as export coal to deep-water port facilities. Roughly one-third of export coal and the majority of the domestic coal that the Company transports is used for generating electricity.

The intermodal business accounted for 16% of revenue and 44% of volume in 2016. The intermodal business combines the superior economics of rail transportation with the short-haul flexibility of trucks and offers a cost advantage over long-haul trucking. Through a network of more than 50 terminals, the intermodal business serves all major markets east of the Mississippi River and transports mainly manufactured consumer goods in containers, providing customers with truck-like service for longer shipments.

Other revenue accounted for 3% of the Company’s total revenue in 2016. This category includes revenue from regional subsidiary railroads, demurrage, revenue for customer volume commitments not met, switching, other incidental charges and adjustments to revenue reserves. Revenue from regional railroads includes shipments by railroads that the Company does not directly operate. Demurrage represents charges assessed when freight cars are held beyond a specified period of time. Switching revenue is primarily generated when CSXT switches cars for a customer or another railroad.

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Other Entities

In addition to CSXT, the Company's subsidiaries include CSX Intermodal Terminals, Inc. ("CSX Intermodal Terminals"), Total Distribution Services, Inc. ("TDSI"), Transflo Terminal Services, Inc. ("Transflo"), CSX Technology, Inc. ("CSX Technology") and other subsidiaries. CSX Intermodal Terminals owns and operates a system of intermodal terminals, predominantly in the eastern United States and also performs drayage services (the pickup and delivery of intermodal shipments) for certain customers and trucking dispatch operations. TDSI serves the automotive industry with distribution centers and storage locations. Transflo connects non-rail served customers to the many benefits of rail by transferring products from rail to trucks. The biggest Transflo markets are chemicals and agriculture, which includes shipments of plastics and ethanol. CSX Technology and other subsidiaries provide support services for the Company.

CSX's other holdings include CSX Real Property, Inc., a subsidiary responsible for the Company's operating and non-operating real estate sales, leasing, acquisition and management and development activities. These activities are classified in either operating income or other income - net depending upon the nature of the activity. Results of these activities fluctuate with the timing of real estate transactions.

Financial Information

See Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations for operating revenue, operating income and total assets for each of the last three fiscal years.

Company History

A leader in freight rail transportation for nearly 190 years, the Company's heritage dates back to the early nineteenth century when The Baltimore and Ohio Railroad Company ("B&O") – the nation's first common carrier – was chartered in 1827. Since that time, the Company has built on this foundation to create a railroad that could safely and reliably service the ever-increasing demands of a growing nation.

Since its founding, numerous railroads have combined with the former B&O through merger and consolidation to create what has become CSX. Each of the railroads that combined into the CSX family brought new geographical reach to valuable markets, gateways, cities, ports and transportation corridors.

CSX was incorporated in 1978 under Virginia law. In 1980, the Company completed the merger of the Chessie System and Seaboard Coast Line Industries into CSX. The merger allowed the Company to connect northern population centers and Appalachian coal fields to growing southeastern markets. Later, the Company's acquisition of key portions of Conrail, Inc. ("Conrail") allowed CSXT to link the northeast, including New England and the New York metropolitan area, with Chicago and midwestern markets as well as the growing areas in the Southeast already served by CSXT. This current rail network allows the Company to directly serve every major market in the eastern United States with safe, dependable, environmentally responsible and fuel efficient freight transportation and intermodal service.

Competition

The business environment in which the Company operates is highly competitive. Shippers typically select transportation providers that offer the most compelling combination of service and price. Service requirements, both in terms of transit time and reliability, vary by shipper and commodity. As a result, the Company's primary competition varies by commodity, geographic location and mode of available transportation and includes other railroads, motor carriers that operate similar routes across its service area and, to a less significant extent, barges, ships

and pipelines.

CSXT's primary rail competitor is Norfolk Southern Railway, which operates throughout much of the Company's territory. Other railroads also operate in parts of the Company's territory. Depending on the specific market, competing railroads and deregulated motor carriers may exert pressure on price and service levels. For further discussion on the risk of competition to the Company, see Item 1A. Risk Factors.

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Regulatory Environment

The Company's operations are subject to various federal, state, provincial (Canada) and local laws and regulations generally applicable to businesses operating in the United States and Canada. In the U.S., the railroad operations conducted by the Company's subsidiaries, including CSXT, are subject to the regulatory jurisdiction of the Surface Transportation Board ("STB"), the Federal Railroad Administration ("FRA"), and its sister agency within the U.S. Department of Transportation ("DOT"), the Pipeline and Hazardous Materials Safety Administration ("PHMSA"). Together, FRA and PHMSA have broad jurisdiction over railroad operating standards and practices, including track, freight cars, locomotives and hazardous materials requirements. In addition, the U.S. Environmental Protection Agency ("EPA") has regulatory authority with respect to matters that impact the Company's properties and operations. The EPA is considering regulatory action directed towards the railroad industry governing the disposal of creosote cross-ties and seeking to increase air emission regulations that may impact our operations or increase costs. Similarly, the Transportation Security Administration ("TSA"), a component of the Department of Homeland Security, has broad authority over railroad operating practices that may have homeland security implications. In Canada, the railroad operations conducted by the Company's subsidiaries, including CSXT, are subject to the regulatory jurisdiction of the Canadian Transportation Agency.

Although the Staggers Act of 1980 significantly deregulated the U.S. rail industry, the STB has broad jurisdiction over rail carriers. The STB regulates routes, fuel surcharges, conditions of service, rates for non-exempt traffic, acquisitions of control over rail common carriers and the transfer, extension or abandonment of rail lines, among other railroad activities.

Positive Train Control

In 2008, Congress enacted the Rail Safety Improvement Act (the "RSIA"). The legislation included a mandate that all Class I freight railroads implement an interoperable positive train control system ("PTC") by December 31, 2015. Implementation of a PTC system is designed to prevent train-to-train collisions, over-speed derailments, incursions into established work-zone limits, and train diversions onto another set of tracks. On October 29, 2015, the President of the United States signed the Positive Train Control Enforcement and Implementation Act of 2015 into law extending the deadline. This Act requires the installation of all PTC hardware be completed by December 31, 2018, and, assuming certain conditions are met, requires that the PTC system be fully operational by December 31, 2020.

PTC must be installed on all main lines with passenger and commuter operations as well as most of those over which toxic-by-inhalation hazardous materials are transported. The Company expects to incur significant capital costs in connection with the implementation of PTC as well as related ongoing operating expenses. CSX currently estimates that the total multi-year cost of PTC implementation will be approximately \$2.4 billion for the Company. Total PTC investment through 2016 was \$1.8 billion.

STB Proceedings

In 2012, the STB announced it would accept comments on a proposal by the National Industrial Transportation League that would require Class I railroads to provide a form of "competitive access" to customers served solely by one railroad. Under this proposal, CSX would be required to allow a competing railroad to access certain customers that are currently solely served by CSX's network. In early 2013, shippers, railroads and other parties submitted comments on the proposal, and the STB held a hearing in March 2014 to receive further input from participating parties. Since the hearing, the STB has taken no further action in the proceeding.

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In April 2014, the STB announced it would receive comments to explore its methodology for determining railroad revenue adequacy. The revenue adequacy standard represents the level of profitability for a healthy carrier. Shippers, railroads and other parties filed comments in late 2014. More recently, the STB held a hearing in July 2015 to receive further input from participating parties. Since the hearing, the STB has taken no further action in the proceeding. New rules regarding, among other things, competitive access or revenue adequacy could have a material adverse effect on the Company's financial condition, results of operations and liquidity as well as its ability to invest in enhancing and maintaining vital infrastructure. For further discussion on regulatory risks to the Company, see Item 1A. Risk Factors.

Other Information

CSX makes available on its website www.csx.com, free of charge, its annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and all amendments to those reports as soon as reasonably practicable after such reports are filed with or furnished to the Securities and Exchange Commission ("SEC"). The information on the CSX website is not part of this annual report on Form 10-K. Additionally, the Company has posted its code of ethics on its website, which is also available to any shareholder who requests it. This Form 10-K and other SEC filings made by CSX are also accessible through the SEC's website at www.sec.gov.

CSX has included the certifications of its Chief Executive Officer ("CEO") and the Chief Financial Officer ("CFO") required by Section 302 of the Sarbanes-Oxley Act of 2002 ("the Act") as Exhibit 31, as well as Section 906 of the Act as Exhibit 32 to this Form 10-K report.

The information set forth in Item 6. Selected Financial Data is incorporated herein by reference. For additional information concerning business conducted by the Company during 2016, see Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.

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Item 1A. Risk Factors

The risks set forth in the following risk factors could have a materially adverse effect on the Company's financial condition, results of operations or liquidity, and could cause those results to differ materially from those expressed or implied in the Company's forward-looking statements. Additional risks and uncertainties not currently known to the Company or that the Company currently does not deem to be material also may materially impact the Company's financial condition, results of operations or liquidity.

New legislation or regulatory changes could impact the Company's earnings or restrict its ability to independently negotiate prices.

Legislation passed by Congress, new regulations issued by federal agencies or executive orders issued by the President of the United States could significantly affect the revenues, costs and profitability of the Company's business. For instance, several of the proposals under consideration by the STB could have a significant negative impact on the Company's ability to negotiate prices for the value of rail services provided and meet service standards, which could force a reduction in capital spending. In addition, statutes imposing price constraints or affecting rail-to-rail competition could adversely affect the Company's profitability.

Government regulation and compliance risks may adversely affect the Company's operations and financial results.

The Company is subject to the jurisdiction of various regulatory agencies, including the STB, FRA, PHMSA, TSA, EPA and other state, provincial and federal regulatory agencies for a variety of economic, health, safety, labor, environmental, tax, legal and other matters. New or modified rules or regulations by these agencies could increase the Company's operating costs or reduce operating efficiencies and impact service performance. For example, the RSIA mandates that the installation of PTC hardware be completed by December 31, 2018 and, assuming certain conditions are met, requires that the PTC system be fully operational by December 31, 2020 on main lines that carry certain hazardous materials and on lines that have commuter or passenger operations. Noncompliance with these and other applicable laws or regulations could erode public confidence in the Company and can subject the Company to fines, penalties and other legal or regulatory sanctions.

Failure to complete negotiations on collective bargaining agreements could result in strikes and/or work stoppages.

Most of CSX's employees are represented by labor unions and are covered by collective bargaining agreements. Most of these agreements are bargained for nationally by the National Carriers Conference Committee and negotiated over the course of several years and previously have not resulted in any extended work stoppages. Under the Railway Labor Act's procedures (which include mediation, cooling-off periods and the possibility of an intervention of the U.S. President), during negotiations neither party may take action until the procedures are exhausted. If, however, CSX is unable to negotiate acceptable agreements, or if terms of existing agreements are disputed, the employees covered by the Railway Labor Act could strike, which could result in loss of business and increased operating costs as a result of higher wages or benefits paid to union members.

Capacity constraints could have a negative impact on service and operating efficiency.

CSXT may experience rail network difficulties related to: (i) increased volume; (ii) locomotive or crew shortages; (iii) extreme weather conditions; (iv) increased passenger activities, including high-speed rail; or (v) regulatory changes impacting where and how fast CSXT can transport freight or maintain routes, which could have a negative effect on CSXT's operational fluidity, leading to deterioration of service, asset utilization and overall efficiency.

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Global economic conditions could negatively affect demand for commodities and other freight.

A decline or disruption in general domestic and global economic conditions that affects demand for the commodities and products the Company transports, including import and export volume, could reduce revenues or have other adverse effects on the Company's cost structure and profitability. For example, if the rate of economic growth in Asia slows or if European economies contract, U.S. export coal volume could be adversely impacted resulting in lower revenue for CSX. If the Company experiences significant declines in demand for its transportation services with respect to one or more commodities and products, the Company may experience reduced revenue and increased operating costs associated with the storage of locomotives, railcars and other equipment, workforce adjustments, and other related activities, which could have a material adverse effect on the Company's financial condition, results of operations and liquidity.

Changing dynamics in the U.S. and global energy markets could negatively impact profitability.

Over the past few years, production of natural gas in the U.S. has also increased dramatically, which has resulted in lower natural gas prices. As a result of sustained low natural gas prices, many coal-fired power plants have been displaced by natural gas-fired power generation facilities. If natural gas prices were to remain low, additional coal-fired plants could be displaced, which would likely further reduce the Company's domestic coal volumes and revenues.

Additionally, depressed crude oil prices due to increased supply or lower demand could result in a further decrease in domestic crude oil production, which could have an adverse effect on crude oil volumes for CSX. In addition, new regulations related to the shipment of crude oil by rail, including proposed rail car safety standards, could increase costs for CSX, negatively impact network fluidity or have an adverse impact on customers.

CSXT, as a common carrier by rail, is required by law to transport hazardous materials, which could expose the Company to significant costs and claims.

A train accident involving the transport of hazardous materials could result in significant claims arising from personal injury, property or natural resource damage, environmental penalties and remediation obligations. Such claims, if insured, could exceed existing insurance coverage or insurance may not continue to be available at commercially reasonable rates. Under federal regulations, CSXT is required to transport hazardous materials under the legal duty referred to as the common carrier mandate.

CSXT is also required to comply with regulations regarding the handling of hazardous materials. In November 2008, the TSA issued final rules placing significant new security and safety requirements on passenger and freight railroad carriers, rail transit systems and facilities that ship hazardous materials by rail. Noncompliance with these rules can subject the Company to significant penalties and could be a factor in litigation arising out of a train accident. Finally, legislation preventing the transport of hazardous materials through certain cities could result in network congestion and increase the length of haul for hazardous substances, which could increase operating costs, reduce operating efficiency or increase the risk of an accident involving the transport of hazardous materials.

Climate change and other emissions-related laws and regulations could adversely affect the Company's operations and financial results.

Climate change and other emissions-related laws and regulations have been proposed and, in some cases adopted, on the federal, state, provincial and local levels. These final and proposed laws and regulations take the form of restrictions, caps, taxes or other controls on emissions. In particular, the EPA has issued various regulations and may issue additional regulations targeting emissions, including rules and standards governing emissions from certain

stationary sources and from vehicles.

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Any of these pending or proposed laws or regulations could adversely affect the Company's operations and financial results by, among other things: (i) reducing coal-fired electricity generation due to mandated emission standards; (ii) reducing the consumption of coal as a viable energy resource in the United States and Canada; (iii) increasing the Company's fuel, capital and other operating costs and negatively affecting operating and fuel efficiencies; and (iv) making it difficult for the Company's customers in the U.S. and Canada to produce products in a cost competitive manner. Any of these factors could reduce the amount of shipments the Company handles and have a material adverse effect on the Company's financial condition, results of operations or liquidity.

The Company is subject to environmental laws and regulations that may result in significant costs. The Company is subject to wide-ranging federal, state, provincial and local environmental laws and regulations concerning, among other things, emissions into the air, ground and water; the handling, storage, use, generation, transportation and disposal of waste and other materials; the clean-up of hazardous material and petroleum releases and the health and safety of our employees. If the Company violates or fails to comply with these laws and regulations, CSX could be fined or otherwise sanctioned by regulators. The Company can also be held liable for consequences arising out of human exposure to any hazardous substances for which CSX is responsible. In certain circumstances, environmental liability can extend to formerly owned or operated properties, leased properties, adjacent properties and properties owned by third parties or Company predecessors, as well as to properties currently owned, leased or used by the Company.

The Company has been, and may in the future be, subject to allegations or findings to the effect that it has violated, or is strictly liable under, environmental laws or regulations, and such violations can result in the Company's incurring fines, penalties or costs relating to the clean-up of environmental contamination. Although the Company believes it has appropriately recorded current and long-term liabilities for known and reasonably estimable future environmental costs, it could incur significant costs that exceed reserves or require unanticipated cash expenditures as a result of any of the foregoing. The Company also may be required to incur significant expenses to investigate and remediate known, unknown or future environmental contamination.

The Company relies on the security, stability and availability of its technology systems to operate its business. The Company relies on information technology in all aspects of its business. The performance and reliability of the Company's technology systems are critical to its ability to operate and compete safely and effectively. A cybersecurity attack, which is a deliberate theft of data or impairment of information technology systems, or other significant disruption or failure, could result in a service interruption, train accident, misappropriation of confidential information, process failure, security breach or other operational difficulties. Such an event could result in increased capital, insurance or operating costs, including increased security costs to protect the Company's infrastructure. A disruption or compromise of the Company's information technology systems, even for short periods of time, could have a material adverse effect on the Company.

Disruption of the supply chain could negatively affect operating efficiency and increase costs.

The capital intensive nature and sophistication of core rail equipment (including rolling stock equipment, locomotives, rail, and ties) limits the number of railroad equipment suppliers. If any of the current manufacturers stops production or experiences a supply shortage, CSXT could experience a significant cost increase or material shortage. In addition, a few critical railroad suppliers are foreign and, as such, adverse developments in international relations, new trade regulations, disruptions in international shipping or increases in global demand could make procurement of these supplies more difficult or increase CSXT's operating costs. Additionally, if a fuel supply shortage were to arise, whether due to production restrictions, lower refinery outputs, a disruption of oil imports,

adverse political developments or otherwise, the Company would be negatively impacted.

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The Company faces competition from other transportation providers.

The Company experiences competition in pricing, service, reliability and other factors from various transportation providers including railroads and motor carriers that operate similar routes across its service area and, to a less significant extent, barges, ships and pipelines. Other transportation providers generally use public rights-of-way that are built and maintained by governmental entities, while CSXT and other railroads must build and maintain rail networks largely using internal resources. Any future improvements or expenditures materially increasing the quality or reducing the cost of alternative modes of transportation, or legislation providing for less stringent size or weight restrictions on trucks, could negatively impact the Company's competitive position. Additionally, any future consolidation in the rail industry could materially affect the regulatory and competitive environment in which the Company operates.

Future acts of terrorism, war or regulatory changes to combat the risk of terrorism may cause significant disruptions in the Company's operations.

Terrorist attacks, along with any government response to those attacks, may adversely affect the Company's financial condition, results of operations or liquidity. CSXT's rail lines, other key infrastructure and information technology systems may be direct targets or indirect casualties of acts of terror or war. This risk could cause significant business interruption and result in increased costs and liabilities and decreased revenues. In addition, premiums charged for some or all of the insurance coverage currently maintained by the Company could increase dramatically, or the coverage may no longer be available.

Furthermore, in response to the heightened risk of terrorism, federal, state and local governmental bodies are proposing and, in some cases, have adopted legislation and regulations relating to security issues that impact the transportation industry. For example, the Department of Homeland Security adopted regulations that require freight railroads to implement additional security protocols when transporting hazardous materials. Complying with these or future regulations could continue to increase the Company's operating costs and reduce operating efficiencies.

Severe weather or other natural occurrences could result in significant business interruptions and expenditures in excess of available insurance coverage.

The Company's operations may be affected by external factors such as severe weather and other natural occurrences, including floods, fires, hurricanes and earthquakes. As a result, the Company's rail network may be damaged, its workforce may be unavailable, fuel costs may rise and significant business interruptions could occur. In addition, the performance of locomotives and railcars could be adversely affected by extreme weather conditions. Insurance maintained by the Company to protect against loss of business and other related consequences resulting from these natural occurrences is subject to coverage limitations, depending on the nature of the risk insured. This insurance may not be sufficient to cover all of the Company's damages or damages to others, and this insurance may not continue to be available at commercially reasonable rates. Even with insurance, if any natural occurrence leads to a catastrophic interruption of service, the Company may not be able to restore service without a significant interruption in operations.

The Company could be adversely impacted by actions of activist stockholders, and such activism could impact the value of the Company's securities.

While the Company continually engages with shareholders and considers their views on business and strategy, responding to activist shareholders can be costly and time-consuming, disrupt operations and divert the attention of management and employees. The uncertainties associated with such activities could interfere with the Company's ability to effectively execute its strategic plan, impact customer retention and long-term growth, and limit the

Company's ability to hire and retain personnel. In addition, a proxy contest for the election of directors could require the Company to incur significant legal fees and proxy solicitation expenses and require significant time and attention by management and the board of directors. Uncertainties related to, or the results of, such activism could affect the market price and volatility of the Company's securities.

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The Company may be subject to various claims and lawsuits that could result in significant expenditures.

As part of its railroad and other operations, the Company is subject to various claims and lawsuits related to disputes over commercial practices, labor and unemployment matters, occupational and personal injury claims, property damage, environmental and other matters. The Company may experience material judgments or incur significant costs to defend existing and future lawsuits. Although the Company maintains insurance to cover some of these types of claims and establishes reserves when appropriate, final amounts determined to be due on any outstanding matters may exceed the Company's insurance coverage or differ materially from the recorded reserves.

Additionally, the Company is subject to adverse developments not currently reflected in the Company's reserve estimates.

The unavailability of critical resources could adversely affect the Company's operational efficiency and ability to meet demand.

Marketplace conditions for resources like locomotives as well as the availability of qualified personnel, particularly engineers and trainmen, could each have a negative impact on the Company's ability to meet demand for rail service. Although the Company believes that it has adequate personnel for the current business environment, unpredictable increases in demand for rail services or extreme weather conditions may exacerbate such risks, which could have a negative impact on the Company's operational efficiency and otherwise have a material adverse effect on the Company's financial condition, results of operations, or liquidity in a particular period.

Weaknesses in the capital and credit markets could negatively impact the Company's access to capital.

Due to the significant capital expenditures required to operate and maintain a safe and efficient railroad, the Company regularly relies on capital markets for the issuance of long-term debt instruments as well as on bank financing from time to time. Instability or disruptions of the capital markets, including credit markets, or the deterioration of the Company's financial condition due to internal or external factors, could restrict or prohibit access and could increase the cost of financing sources. A significant deterioration of the Company's financial condition could also reduce credit ratings and could limit or affect its access to external sources of capital and increase the costs of short and long-term debt financing.

Item 1B. Unresolved Staff Comments

None

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Item 2. Properties

The Company's properties primarily consist of track and its related infrastructure, locomotives and freight cars and equipment. These categories and the geography of the network are described below.

Track and Infrastructure

Serving 23 states, the District of Columbia, and the Canadian provinces of Ontario and Quebec, the CSXT rail network serves, among other markets, New York, Philadelphia and Boston in the Northeast and Mid-Atlantic, the southeast markets of Atlanta, Miami and New Orleans, and the midwestern cities of St. Louis, Memphis and Chicago.

CSXT's track structure includes main thoroughfares, connecting terminals and yards (known as mainline track), track within terminals and switching yards, track adjacent to the mainlines used for passing trains, track connecting the mainline track to customer locations and track that diverts trains from one track to another known as turnouts. Total track miles are greater than CSXT's approximately 21,000 route miles, which reflect the size of CSXT's network that connects markets, customers and western railroads. At December 2016, the breakdown of track miles was as follows:

| | Track Miles |
|-------------------------------|----------------|
| Mainline track | 26,530 |
| Terminals and switching yards | 9,396 |
| Passing sidings and turnouts | 937 |
| Total | 36,863 |

In addition to its physical track structure, the Company operates numerous yards and terminals for rail and intermodal service. These serve as hubs between the Company and its local customers and as sorting facilities where railcars and intermodal containers often are received, re-sorted and placed onto new outbound trains. The Company's ten largest yards and terminals based on annual volume (number of railcars or intermodal containers processed) are listed in the table below.

| Yards and Terminals | Annual Volume (number of units processed) |
|---|---|
| Chicago, IL (Bedford Park) - Intermodal | 1,136,124 |
| North Baltimore, OH (Northwest Ohio) - Intermodal | 809,254 |
| Waycross, GA | 677,003 |
| Selkirk, NY | 545,310 |
| Nashville, TN | 539,407 |
| Willard, OH | 515,335 |
| Cincinnati, OH | 496,299 |
| Indianapolis, IN | 496,235 |
| Hamlet, NC | 458,760 |
| Louisville, KY | 417,679 |

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Network Geography

CSXT's operations are primarily focused on four major transportation networks and corridors which are defined geographically and by commodity flows below.

Interstate 90 (I-90) Corridor – This CSXT corridor links Chicago and the Midwest to metropolitan areas in New York and New England. This route, also known as the “waterlevel route,” has minimal hills and grades and nearly all of it has two main tracks (referred to as double track). These superior engineering attributes permit the corridor to support consistent, high-speed intermodal, automotive and merchandise service. This corridor is a primary route for import traffic coming from the far east through western ports moving eastward across the country, through Chicago and into the population centers in the Northeast. The I-90 Corridor is also a critical link between ports in New York, New Jersey, and Pennsylvania and consumption markets in the Midwest. This route carries goods from all three of the Company's major markets – merchandise, coal and intermodal.

Interstate 95 (I-95) Corridor – The CSXT I-95 Corridor connects Charleston, Jacksonville, Miami and many other cities throughout the Southeast with the heavily populated mid-Atlantic and northeastern cities of Baltimore, Philadelphia and New York. CSXT primarily transports food and consumer products, as well as metals and chemicals along this line. It is the leading rail corridor along the eastern seaboard south of the District of Columbia, and provides access to major eastern ports.

Southeastern Corridor – This critical part of the network runs between CSXT's western gateways of Chicago, St. Louis and Memphis through the cities of Nashville, Birmingham, and Atlanta and markets in the Southeast. The Southeastern Corridor is the premier rail route connecting these key cities, gateways, and markets and positions CSXT to efficiently handle projected traffic volumes of intermodal, automotive and general merchandise traffic. The corridor also provides direct rail service between the coal reserves of the southern Illinois basin and the demand for coal in the Southeast.

Coal Network – The CSXT coal network connects the coal mining operations in the Appalachian mountain region and Illinois basin with industrial areas in the Southeast, Northeast and Mid-Atlantic, as well as many river, lake, and deep water port facilities. The domestic coal market has declined significantly over the past several years and export coal remains subject to a high degree of volatility. CSXT's coal network remains well positioned to supply utility markets in both the Northeast and Southeast and to transport coal shipments for export outside of the U.S. Roughly one-third of the tons of export coal and the majority of the domestic coal that the Company transports is used for generating electricity.

See the following pages for maps of the CSX Rail Network and CSX Intermodal Rail Network.

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CSX Rail Network

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CSX Intermodal Rail Network

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Locomotives

At December 2016, CSXT owned 4,400 locomotives. From time to time, the Company also short-term leases locomotives based on business needs. Freight locomotives are the power source used primarily to pull trains. Switching locomotives are used in yards to sort railcars so that the right railcar is attached to the right train in order to deliver it to its final destination. Auxiliary units are typically used to provide extra traction for heavy trains in hilly terrain. At December 2016, CSXT's fleet of owned locomotives consisted of the following types:

| | Locomotives | % | Average Age (years) |
|-----------------|-------------|-------|---------------------------|
| Freight | 3,880 | 88 % | 20 |
| Switching | 311 | 7 % | 37 |
| Auxiliary Units | 209 | 5 % | 24 |
| Total | 4,400 | 100 % | 20 |

Equipment

In 2016, the average daily fleet of cars on line consisted of approximately 208,000 cars. At any time, over half of the railcars on the CSXT system are not owned or leased by the Company. Examples of these include railcars owned by other railroads (which are utilized by CSXT), shipper-furnished or private cars (which are generally used only in that shipper's service), multi-level railcars used to transport automobiles (which are shared between railroads) and doublestack railcars, or well cars (which are industry pooled), that allow for two intermodal containers to be loaded one above the other.

At December 2016, the Company's owned and long-term leased equipment consisted of the following:

| Equipment | Number of Units | % |
|-----------------------|--------------------|-------|
| Gondolas | 23,802 | 37 % |
| Multi-level flat cars | 12,069 | 19 % |
| Open-top hoppers | 11,089 | 17 % |
| Covered hoppers | 10,030 | 15 % |
| Box cars | 7,151 | 11 % |
| Flat cars | 648 | 1 % |
| Other cars | 370 | — % |
| Subtotal freight cars | 65,159 | 100 % |
| Containers | 18,147 | |
| Total equipment | 83,306 | |

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The Company's revenue-generating equipment, either owned or long-term leased, consists of freight cars and containers as described below.

Gondolas – Support CSXT's metals markets and provide transport for woodchips and other bulk commodities. Some gondolas are equipped with special hoods for protecting products like coil and sheet steel.

Multi-level flat cars – Transport finished automobiles and are differentiated by the number of levels: bi-levels for large vehicles such as pickup trucks and SUVs and tri-levels for sedans and smaller automobiles.

Open-top hoppers – Transport heavy dry bulk commodities such as coal, coke, stone, sand, ores and gravel that are resistant to weather conditions.

Covered hoppers – Have a permanent roof and are segregated based upon commodity density. Lighter bulk commodities such as grain, fertilizer, flour, salt, sugar, clay and lime are shipped in large cars called jumbo covered hoppers. Heavier commodities like cement, ground limestone and industrial sand are shipped in small cube covered hoppers.

Box cars – Include a variety of tonnages, sizes, door configurations and heights to accommodate a wide range of finished products, including paper, auto parts, appliances and building materials. Insulated box cars deliver food products, canned goods, beer and wine.

Flat cars – Used for shipping intermodal containers and trailers or bulk and finished goods, such as lumber, pipe, plywood, drywall and pulpwood.

Other cars – Primarily leased refrigerator cars and slab steel cars.

Containers – Weather-proof boxes used for bulk shipment of freight.

Item 3. Legal Proceedings

For further details, please refer to Note 7. Commitments and Contingencies of this annual report on Form 10-K.
Environmental Proceedings That Could Result in Fines Above \$100,000

In connection with a CSXT train derailment in Mount Carbon, West Virginia in February 2015, the Company has entered into discussions with the U.S. Department of Justice and the U.S. Environmental Protection Agency concerning a regulatory penalty related to a release of product into the environment. Although final resolution of this matter is subject to further discussions and potential litigation, the Company does not believe that the outcome will have a material adverse effect on its financial position, results of operations or liquidity.

Item 4. Mine Safety Disclosure

Not Applicable

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Executive Officers of the Registrant

Executive officers of the Company are elected by the CSX Board of Directors and generally hold office until the next annual election of officers. There are no family relationships or any arrangement or understanding between any officer and any other person pursuant to which such officer was elected. As of the date of this filing, the executive officers' names, ages and business experience are:

| Name and Age | Business Experience During Past Five Years |
|--|--|
| <p>Michael J. Ward, 66 Chairman and Chief Executive Officer</p> | <p>A 39-year veteran of the Company, Ward has served as Chairman and Chief Executive Officer of CSX since January 2003.</p> <p>Ward's distinguished railroad career has included key executive positions in nearly all aspects of the Company's business, including sales and marketing, operations and finance.</p> <p>Clarence Gooden has served as President of CSX since September 2015 with responsibility for operations and sales and marketing. In this role, he is responsible for safe and reliable operations as well as a highly diversified market portfolio serving all facets of the North American economy.</p> |
| <p>Clarence W. Gooden, 65 President</p> | <p>As an employee of the Company for 46 years, Gooden previously served as Executive Vice President and Chief Commercial Officer since 2004 where he was responsible for generating customer revenue, forecasting business trends and developing CSX's model for future revenue growth. Gooden has also held key executive positions in both operations and sales and marketing.</p> <p>Lonegro has served as Executive Vice President and Chief Financial Officer of CSX since September 2015. In this capacity, he directs all financial and strategic planning activities, including accounting, financial planning, purchasing, tax, treasury and investor relations.</p> |
| <p>Frank A. Lonegro, 48 Executive Vice President and Chief Financial Officer</p> | <p>During his 16-year tenure with the Company, Lonegro also served as Vice President Internal Audit, President of CSX Technology, Vice President Mechanical and Vice President Service Design.</p> <p>Additionally, he led development and implementation of Positive Train Control, an advanced train control system, to further enhance the Company's safety performance.</p> <p>Sanborn has served as Executive Vice President and Chief Operating Officer of CSXT since September 2015. In this capacity, she is responsible for all aspects of safe, reliable and cost-effective service delivery. She directs daily train operations, maintains the Company's locomotive and rail car fleet as well as maintains and upgrades the Company's more than 21,000-route-mile network in the eastern United States and two Canadian provinces.</p> |
| <p>Cindy M. Sanborn, 52 Executive Vice President and Chief Operating Officer</p> | <p>Since joining the Company in 1987, she also served as Executive Vice President - Operations, Vice President and Chief Transportation Officer, Vice President of Operations for the Northern Region and various other key roles in network operations, locomotive management and division operations.</p> |

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| Name and Age | Business Experience During Past Five Years |
|---|--|
| <p>Fredrik J. Eliasson, 46 Executive Vice President and Chief Sales and Marketing Officer</p> | <p>Eliasson has served as Executive Vice President and Chief Sales and Marketing Officer of CSX since September 2015. In this capacity, he directs all customer-facing aspects of the Company's business, including market growth, forecasting business trends and development of strategic plans for revenue growth.</p> <p>During his 21-year tenure with the Company, he also served as Executive Vice President and Chief Financial Officer. Prior to becoming CFO, he led development of two of the Company's major markets as Vice President of Chemicals and Fertilizer and Vice President of Emerging Markets. He also supported Sales and Marketing in a previous position as Vice President of Commercial Finance.</p> |
| <p>Ellen M. Fitzsimmons, 56 Executive Vice President of Law and Public Affairs, General Counsel and Corporate Secretary</p> | <p>Fitzsimmons has been the Executive Vice President of Law and Public Affairs, General Counsel, and Corporate Secretary of CSX since December 2003. She serves as the Company's Chief Legal Officer and oversees all government relations and public affairs activities as well as internal audit and other risk management functions.</p> <p>During her 25-year tenure with the Company, her broad responsibilities have included key roles in major risk and corporate governance-related areas.</p> |
| <p>Cressie D. Brown, 55 Senior Vice President and Chief Administrative Officer</p> | <p>Brown has served as Senior Vice President and Chief Administrative Officer since July 2016. She is responsible for human resources, employee compensation and benefits, labor relations, real estate, facilities and aviation.</p> <p>During her 28-year tenure with the Company, Brown previously served as Vice President of Labor Relations and Vice President of Service Design and Advanced Technology. She also has significant experience in technology, finance and customer service.</p> |
| <p>Kathleen Brandt, 53 Senior Vice President and Chief Information Officer</p> | <p>Brandt has been Senior Vice President and Chief Information Officer since July 2016. In this role, she directs the information technology to support the company's strategic objectives and leads the development and application of the tools and information to maximize safety, service excellence, and efficiency.</p> <p>During her 31-year tenure with the Company, she previously served as President CSX Technology and has also made significant contributions to organizational strategy and capital planning.</p> |
| <p>Carolyn T. Sizemore, 54 Vice President and Controller</p> | <p>Sizemore has served as Vice President and Controller of CSX since April 2002. She is responsible for financial and regulatory reporting, freight billing and collections, payroll, accounts payable and various other accounting processes.</p> <p>Sizemore's responsibilities during her 27-year tenure with the Company have included roles in finance and audit-related areas including a variety of positions in accounting, finance strategies, budgets and performance analysis.</p> |

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Item 5. Market for Registrant’s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Market Information

CSX’s common stock is listed on the Nasdaq Global Select Market, which is its principal trading market, and is traded over-the-counter and on exchanges nationwide. The official trading symbol is “CSX.”

Description of Common and Preferred Stock

A total of 1.8 billion shares of common stock are authorized, of which 928,179,723 shares were outstanding as of December 30, 2016. Each share is entitled to one vote in all matters requiring a vote of shareholders. There are no pre-emptive rights, which are privileges extended to select shareholders that would allow them to purchase additional shares before other members of the general public in the event of an offering. At January 27, 2017, the latest practicable date that is closest to the filing date, there were 28,956 common stock shareholders of record. The weighted average of common shares outstanding, which was used in the calculation of diluted earnings per share, was 948 million as of December 30, 2016. (See Note 2, Earnings Per Share.) A total of 25 million shares of preferred stock is authorized, none of which is currently outstanding.

The following table sets forth, for the quarters indicated, the dividends declared and the high and low share prices of CSX common stock.

| | Quarter | | | | |
|--------------------|---------|---------|---------|---------|---------|
| | 1st | 2nd | 3rd | 4th | Year |
| 2016 | | | | | |
| Dividends | \$0.18 | \$0.18 | \$0.18 | \$0.18 | \$0.72 |
| Common Stock Price | | | | | |
| High | \$27.27 | \$27.97 | \$30.11 | \$37.42 | \$37.42 |
| Low | \$21.33 | \$24.36 | \$24.43 | \$29.39 | \$21.33 |
| 2015 | | | | | |
| Dividends | \$0.16 | \$0.18 | \$0.18 | \$0.18 | \$0.70 |
| Common Stock Price | | | | | |
| High | \$36.96 | \$37.67 | \$33.63 | \$30.53 | \$37.67 |
| Low | \$32.71 | \$31.87 | \$24.47 | \$24.58 | \$24.47 |

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Stock Performance Graph

The cumulative shareholder returns, assuming reinvestment of dividends, on \$100 invested at December 31, 2011 are illustrated on the graph below. The Company references the Standard & Poor 500 Stock Index (“S&P 500”), which is a registered trademark of the McGraw-Hill Companies, Inc., and the Dow Jones U.S. Transportation Average Index, which provide comparisons to a broad-based market index and other companies in the transportation industry.

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CSX Purchases of Equity Securities

CSX purchases its own shares for two primary reasons: (1) to further its goals under its share repurchase program and (2) to fund the Company's contribution required to be paid in CSX common stock under a 401(k) plan that covers certain union employees.

In April 2015, the Company announced a \$2 billion share repurchase program, which is expected to be completed by April 2017. Management's assessment of market conditions and other factors guide the timing and volume of repurchases. Future share repurchases are expected to be funded by cash on hand, cash generated from operations and debt issuances. During 2016, 2015, and 2014, CSX repurchased \$1.1 billion or 38 million shares, \$804 million or 26 million shares, and \$517 million or 17 million shares, respectively, of common stock. Shares are retired immediately upon repurchase. In accordance with the Equity Topic in the Accounting Standards Codification ("ASC"), the excess of repurchase price over par value is recorded in retained earnings. Generally, retained earnings are only impacted by net earnings and dividends.

Share repurchase activity of \$278 million for the fourth quarter 2016 was as follows:

CSX Purchases of Equity Securities for the Quarter

| Fourth Quarter (a) | Total Number of Shares Purchased (b) | Average Price Paid per Share | Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs ^(b) | Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs |
|--------------------|--------------------------------------|------------------------------|---|--|
| Beginning Balance | | | | \$ 548,855,151 |
| October | 2,757,869 | \$ 30.39 | 2,736,609 | 465,695,348 |
| November | 3,117,190 | 32.02 | 3,116,900 | 365,903,976 |
| December | 2,634,900 | 36.30 | 2,634,900 | 270,270,134 |
| Ending Balance | 8,509,959 | \$ 32.82 | 8,488,409 | \$ 270,270,134 |

(a) Fourth quarter 2016 consisted of the following fiscal periods: October (September 24, 2016 - October 21, 2016), November (October 22, 2016 - November 25, 2016), and December (November 26, 2015 - December 30, 2016).

(b) The difference of 21,550 shares between the "Total Number of Shares Purchased" and the "Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs" for the quarter represents shares purchased to fund the Company's contribution to a 401(k) plan that covers certain union employees.

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Item 6. Selected Financial Data

Selected financial data related to the Company's financial results for the last five fiscal years are listed below.

| (Dollars and Shares in Millions, Except Per Share Amounts) | Fiscal Years | | | | |
|--|--------------|----------|----------|----------|----------|
| | 2016 | 2015 | 2014 | 2013 | 2012 |
| Financial Performance | | | | | |
| Revenue | \$11,069 | \$11,811 | \$12,669 | \$12,026 | \$11,763 |
| Expense | 7,680 | 8,227 | 9,056 | 8,553 | 8,299 |
| Operating Income | \$3,389 | \$3,584 | \$3,613 | \$3,473 | \$3,464 |
| Net Earnings from Continuing Operations | 1,714 | 1,968 | 1,927 | 1,864 | 1,863 |
| Operating Ratio | 69.4 | % 69.7 | % 71.5 | % 71.1 | % 70.6 |
| Net Earnings Per Share: | | | | | |
| From Continuing Operations, Basic | \$1.81 | \$2.00 | \$1.93 | \$1.83 | \$1.80 |
| From Continuing Operations, Assuming Dilution | 1.81 | 2.00 | 1.92 | 1.83 | 1.79 |
| Average Common Shares Outstanding | | | | | |
| Basic | 947 | 983 | 1,001 | 1,019 | 1,038 |
| Assuming Dilution | 948 | 984 | 1,002 | 1,019 | 1,040 |
| Financial Position | | | | | |
| Cash, Cash Equivalents and Short-term Investments | \$1,020 | \$1,438 | \$961 | \$1,079 | \$1,371 |
| Total Assets | 35,414 | 34,745 | 32,747 | 31,462 | 30,436 |
| Long-term Debt | 10,962 | 10,515 | 9,349 | 8,857 | 8,884 |
| Shareholders' Equity | 11,694 | 11,668 | 11,176 | 10,504 | 9,136 |
| Dividend Per Share | \$0.72 | \$0.70 | \$0.63 | \$0.59 | \$0.54 |
| Additional Data | | | | | |
| Capital Expenditures ^(a) | \$2,705 | \$2,562 | \$2,449 | \$2,313 | \$2,341 |
| Employees -- Annual Averages (estimated) | 27,350 | 31,285 | 31,511 | 31,254 | 32,120 |
| Employees -- Year-end Count (estimated) | 26,628 | 29,410 | 32,287 | 31,413 | 30,787 |

Capital expenditures include investments related to reimbursable public-private partnerships. These partnership investments of \$41 million, \$14 million, \$8 million, \$40 million and \$166 million in 2016, 2015, 2014, 2013 and 2012, respectively, are projects that are partially or wholly reimbursed to CSX through either government grants or other funding sources such as cash received from a property sale. These reimbursements may not be fully received in a given year; therefore, the timing of receipts may differ from the timing of the investment. See the capital expenditures table on page 46 for additional information.

(a)

Certain prior year data has been reclassified to conform to the current presentation.

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Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations
TERMS USED BY CSX

When used in this report, unless otherwise indicated by the context, these terms are used to mean the following:

Car hire - A charge paid by one railroad for its use of cars belonging to another railroad or car owner.

Class I freight railroad - One of the largest line haul freight railroads as determined based on operating revenue; the exact revenue required to be in each class is periodically adjusted for inflation by the Surface Transportation Board. Smaller railroads are classified as Class II or Class III.

Common carrier mandate - A federal mandate that requires U.S. railroads to accommodate reasonable requests from shippers to carry any freight, including hazardous materials.

Demurrage - A charge assessed by railroads for the use of rail cars by shippers or receivers of freight beyond a specified free time.

Department of Transportation ("DOT") - A U.S Government agency with jurisdiction over matters of all modes of transportation.

Depreciation study (also referred to as a "life study") - A periodic statistical analysis of fixed asset service lives, salvage values, accumulated depreciation, and other factors for group assets along with a comparison of similar asset groups at other companies conducted by a third-party specialist.

Double-stack - Stacking containers two-high on specially equipped cars.

Drayage - The pickup or delivery of intermodal shipments by truck.

Federal Railroad Administration ("FRA") - The branch of the DOT that is responsible for developing and enforcing railroad safety regulations, including safety standards for rail infrastructure and equipment.

Free cash flow - The calculation of a non-GAAP measure by using net cash provided by operating activities and adjusting for property additions and certain other investing activities. Free cash flow is a measure of cash available for paying dividends, share repurchases and principal reduction on outstanding debt.

Group-life method - A type of depreciation in which assets with similar useful lives and characteristics are aggregated into groups. Instead of calculating depreciation for individual assets, depreciation is calculated for each group.

Highway-to-rail - An initiative to assist new and existing customers in identifying freight moves that would benefit from converting from a highway-only move to one that utilizes intermodal containers on rail and local drayage by truck.

Incidental revenue - Revenue for switching, demurrage, storage, etc.

Intermodal - A flexible way of transporting freight over water, highway and rail without being removed from the original transportation equipment, namely a container or trailer.

Mainline - The main track thoroughfare, exclusive of terminals, yards, sidings and turnouts.

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National Gateway - A multi-phase construction initiative aimed at increasing intermodal capacity on the CSX network by clearing key corridors between mid-Atlantic ports and the Midwest for double-stack trains. Construction on National Gateway projects is funded by CSX, the federal government, and individual states.

Revenue adequacy - The achievement of a rate of return on investment at least equal to the cost of investment capital, as measured by the STB.

Shipper - A customer shipping freight via rail.

Siding - Track adjacent to the mainline used for passing trains.

Staggers Act of 1980 - Congressional law which significantly deregulated the rail industry, replacing the regulatory structure in existence since the 1887 Interstate Commerce Act. Where previously rates were controlled by the Interstate Commerce Commission, the Staggers Act allowed railroads to establish their own rates for shipments, enhancing their ability to compete with other modes of transportation.

Surface Transportation Board ("STB") - An independent governmental adjudicatory body administratively housed within the DOT, responsible for the economic regulation of interstate surface transportation within the United States.

Switching - Putting cars in a specific order, placing cars for loading, retrieving empty cars or adding or removing cars from a train at an intermediate point.

Terminal - A facility, typically owned by a railroad, for the handling of freight and for the breaking up, making up, forwarding and servicing of trains.

TTX Company ("TTX") - A Company that provides its owner-railroads with standardized fleets of intermodal, automotive and general use railcars at time and mileage rates. CSX owns about 20 percent of TTX's common stock, and the remainder is owned by the other leading North American railroads and their affiliates.

Turnout - A track that diverts trains from one track to another.

Yard - A system of tracks, other than main tracks and sidings, used for making up trains, storing cars and other purposes.

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STRATEGIC OVERVIEW

CSX provides rail-based freight transportation services including traditional rail service, the transport of intermodal containers and trailers, as well as other transportation services such as rail-to-truck transfers and bulk commodity operations. The Company and the rail industry provide customers with access to an expansive and interconnected transportation network that plays a key role in North American commerce and is critical to the long-term economic success and improved global competitiveness of the United States. In addition, freight railroads provide the most economical and environmentally efficient means to transport goods over land.

CSX's transportation solutions connect industries and population centers across the United States with each other and with global markets through access to over 70 port facilities allowing the Company to meet the dynamic transportation needs of manufacturers, industrial producers, construction companies, farmers and feed mills, wholesalers and retailers, energy producers and the U.S. Armed Forces. Through its network, the Company transports a diverse portfolio of commodities and products to meet the country's needs. These products range from agricultural goods, such as grains, to chemicals, automobiles, metals, building materials, paper, consumer products, and energy sources like coal, ethanol and liquefied petroleum gas. The Company categorizes these products into three primary lines of business: merchandise, intermodal and coal.

To support long-term growth and value creation consistent with the evolving trends in freight transportation, CSX has launched a new strategic initiative known as the CSX of Tomorrow: a safe, highly automated, resource-efficient railroad enabling Service Excellence, profitable growth and improved cash flow. The CSX of Tomorrow is comprised of four distinct strategic pillars and builds on the Company's vision, purpose and core values.

CSX of Tomorrow Strategic Initiatives

Network of Tomorrow

The CSX of Tomorrow relies on the reach, capability and efficiency of the Company's rail network to safely and effectively meet the demands of the evolving marketplace and provide increasingly flexible and responsive service to more diverse customers. To facilitate future productivity and growth, CSX is implementing a fundamentally new approach to the network—transforming the railroad into two interconnected networks: a primary network and a local network. The Company is expanding capacity in its primary network to enable increasingly dense traffic while providing improved service for customers and enabling future growth. Further, the Company's capacity investments along the primary network will allow for additional train lengthening, improving efficiency and profitability. The local network will be operated at lower density and speed and will better allow for new customer site development as a result of easier access to the local network and the Company's enhanced focus on local pickup and delivery of freight to customers.

Expanding capacity on U.S. rail networks provides substantial public benefits including job creation, increased business activity at U.S. ports, reduced highway congestion and lower air emissions. Therefore, CSX and its government partners are jointly working to invest in multi-year rail infrastructure projects. These public-private partnerships are a critical part of the Network of Tomorrow strategy for the Company. An example of one of these initiatives is the National Gateway, which is a public-private partnership that will increase intermodal capacity and create substantial environmental and efficiency advantages by clearing key corridors between mid-Atlantic ports and the Midwest for double-stack intermodal trains.

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The modernization of the Virginia Avenue Tunnel in Washington, D.C. is the capstone project for the second, and final phase, of the National Gateway. This project improves the flow of freight traffic through the District of Columbia and eliminates a rail traffic bottleneck that also impacts commuter and passenger trains in the region. CSX completed the first of two new double-stack-cleared tunnels in 2016, and the second tunnel will be finished in late 2018. With the completion of the first tunnel, 95% of CSX intermodal freight now moves in double-stack service. Going forward, CSX will continue to explore other opportunities to partner with the public sector to maximize the many public benefits of freight rail.

Going forward, CSX will continue to explore other opportunities to partner with the public sector to maximize the many public benefits of freight rail. The Network of Tomorrow, along with enhanced operational efficiency, will allow CSX to continue to improve safety, lower the cost structure and provide superior service to customers.

Service Excellence

Service Excellence has long been a core component of CSX's culture that engages all employees to focus on delivering value to customers through improved service levels, communications tools and advanced technologies. As part of the CSX of Tomorrow, the Company will continually strive to consistently meet, or exceed, customer commitments while ensuring all interactions with customers result in a positive experience. Improving the customer experience will allow CSX to continue delivering a safe, reliable and competitive product while enhancing the ability to profitably grow the business and continue to value price its service product. In addition, Service Excellence across the Network of Tomorrow will enable additional volume growth opportunities with new and existing customers, especially in the Company's intermodal and merchandise businesses.

For example, CSX's intermodal network connects all major population centers east of the Mississippi River and positions the Company to capture a significant share of the growing domestic intermodal market opportunity, currently estimated at nine million truckloads in the eastern United States that move over 550 miles. The company's highway-to-rail initiative assists in growing this traffic by helping customers identify new conversion opportunities for both domestic intermodal moves and the U.S. portion of international intermodal moves.

To further enhance the Company's intermodal offering and support future growth, CSX announced a new terminal in eastern North Carolina, known as the Carolina Connector, to capture local, regional, national and international intermodal freight movement opportunities prevalent in the vibrant mid-Atlantic market. This new terminal will be poised to replicate and leverage the success of the Northwest Ohio intermodal terminal by expanding the reach of the Company's hub and spoke network strategy to provide further profitable growth, network connectivity and density, especially in smaller and mid-sized markets.

CSX continues to proactively seek the right opportunities to profitably grow the merchandise business. The Company will continue capitalizing on new opportunities to locate industries on the CSX network, especially on the local network where network connectivity costs will generally be the lowest for customers. Through industrial development, the Company helps new and existing customers grow their business and target new markets by providing access to pre-certified locations as well as project management services.

The Company's coal markets have shifted dramatically over the past several years and continue to rapidly evolve. Domestic utility coal demand decreased again in 2016 relative to previous years while export coal remains subject to a high degree of volatility as a result of changes in the global economy, competition from foreign producers and regulatory impacts on coal mining in the United States. Longer-term, downward pressure on domestic utility coal volumes will likely persist as a result of continued low natural gas prices while global coal demand will likely be mixed as developing countries become more urbanized and industrialized countries continue to use an increasing amount of alternative fuels, other than coal, for electrical power generation. CSX will continue to provide a competitive service product amid coal's market shifts while efficiently capitalizing on short-term demand fluctuations.

CSX CORPORATION
PART II

Highly Automated Railroad

For many years, CSX has utilized technology to enhance operational performance and decision-making. The CSX of Tomorrow will build upon this expertise and increasingly leverage technology (focusing on automation, advanced analytics and the use of mobility tools), innovation and process improvement. CSX is accelerating its technology investments to improve safety, resource efficiency, asset reliability and service levels for customers. Several key initiatives aimed at generating long-term value are focused on automating and optimizing critical operations across the Company. CSX will continue to implement specific workforce and regulatory strategies to ensure the safe, effective adoption of new technologies as the Company progresses towards becoming a Highly Automated Railroad.

Team of Tomorrow

CSX's approximately 27,000 dedicated employees are the driving force behind the CSX of Tomorrow, contributing to the successful development and implementation of all strategic initiatives. As the CSX of Tomorrow requires an increasingly diverse skillset, the Team of Tomorrow will be a highly-capable, flexible, collaborative team, relentlessly focused on safety, service and value creation. To attract, retain and motivate the best talent in the marketplace, CSX will continue to provide a compelling value proposition for its employees. The Company is going to further enhance its investment in employee development, provide career opportunities, have market-competitive employee benefits and continue to reward the creation of customer and employee excellence. Through the Team of Tomorrow initiative, CSX strives to align our people with a culture that embraces the Company's vision, purpose and core values, to safely and efficiently serve our customers and help ensure the successful implementation of the CSX of Tomorrow.

Balanced Approach to Cash Deployment

CSX remains highly committed to delivering value to shareholders through a balanced approach to deploying cash that includes investments in the business, dividend growth and share repurchases. In 2016, the Company invested \$2.7 billion to further enhance the safety, reliability, efficiency, flexibility and capability of its network and its overall business. In addition, during 2016, CSX repaid \$1.4 billion in outstanding debt to capitalize on the lower interest rate environment.

The Company continues to return value to its shareholders in the form of dividends and share repurchases. During 2016, the Company paid a quarterly cash dividend of \$0.18 per common share, with total dividends paid to shareholders of \$680 million for the year. Also in 2016, CSX continued share repurchases under its \$2.0 billion program which began in 2015 and is expected to be completed by April 2017. CSX repurchased \$1.1 billion, or 38 million shares, during 2016 under this program. As part of this balanced approach, the Company is committed to maintaining a credit profile consistent with a BBB+ rating by Standard & Poor's and a Baa1 rating by Moody's Investment Services.

Summary

The strategic initiatives and opportunities, as well as the strategic investments discussed above, provide a foundation for volume growth, continued value pricing, productivity improvement, enhanced customer service and continued advancements in the safety and reliability of operations. To continue these types of investments, the Company must be able to operate in a balanced regulatory environment in which it can generate adequate returns and drive shareholder value. These investments will enable the Company to deliver the CSX of Tomorrow: a safe, highly automated, resource-efficient railroad enabling Service Excellence, profitable growth and improved cash flow.

CSX CORPORATION
PART II

2016 HIGHLIGHTS

- Revenue of \$11.1 billion decreased \$742 million or six percent versus the prior year.
- Expenses of \$7.7 billion decreased \$547 million or seven percent year over year.
- Operating income of \$3.4 billion decreased \$195 million or five percent year over year.
- Operating ratio of 69.4 percent improved 30 basis points from 69.7 percent.

Earnings per diluted share of \$1.81 decreased \$0.19 or 10 percent year over year.

RESULTS OF OPERATIONS

2016 vs. 2015 Results of Operations ^(a)

| | Fiscal Years | | \$ Change | % Change |
|-------------------------------|--------------|----------|--------------|-------------|
| | 2016 | 2015 | | |
| (Dollars in Millions) | | | | |
| Revenue | \$11,069 | \$11,811 | \$(742) | (6)% |
| Expense | | | | |
| Labor and Fringe | 3,159 | 3,290 | 131 | 4 |
| Materials, Supplies and Other | 2,069 | 2,336 | 267 | 11 |
| Fuel | 713 | 957 | 244 | 25 |
| Depreciation | 1,301 | 1,208 | (93) | (8) |
| Equipment and Other Rents | 438 | 436 | (2) | — |
| Total Expense | 7,680 | 8,227 | 547 | 7 |
| Operating Income | 3,389 | 3,584 | (195) | (5) |
| Interest Expense | (579) | (544) | (35) | (6) |
| Debt Repurchase Expense | (115) | — | (115) | (100) |
| Other Income - Net | 46 | 98 | (52) | (53) |
| Income Tax Expense | (1,027) | (1,170) | 143 | 12 |
| Net Earnings | \$1,714 | \$1,968 | \$(254) | (13) |
| Earnings Per Diluted Share: | | | | |
| Net Earnings | \$1.81 | \$2.00 | \$(0.19) | (10)% |
| Operating Ratio | 69.4 | % 69.7 | % | 30 bps |

(a) CSX follows a 52/53 week fiscal reporting calendar. Fiscal year 2016 included 53 weeks and fiscal year 2015 included 52 weeks. All 2016 information presented in Results of Operations is on a 53-week basis, under Generally Accepted Accounting Principles ("GAAP").

CSX CORPORATION
PART II

2016 vs. 2015 Results of Operations, continued

Volume and Revenue (Unaudited) ^(b)

Volume (Thousands of units); Revenue (Dollars in Millions); Revenue Per Unit (Dollars)

| | Volume | | | Revenue | | | Revenue Per Unit | | |
|---|--------|-------|----------|----------|----------|----------|------------------|---------|----------|
| | 2016 | 2015 | % Change | 2016 | 2015 | % Change | 2016 | 2015 | % Change |
| Agricultural | | | | | | | | | |
| Agricultural and Food Products ^(a) | 477 | 503 | (5)% | \$1,286 | \$1,345 | (4)% | \$2,696 | \$2,674 | 1 % |
| Fertilizers ^(a) | 300 | 301 | — | 463 | 489 | (5) | 1,543 | 1,625 | (5) |
| Industrial | | | | | | | | | |
| Chemicals ^(a) | 700 | 726 | (4) | 2,191 | 2,284 | (4) | 3,130 | 3,146 | (1) |
| Automotive | 482 | 450 | 7 | 1,261 | 1,175 | 7 | 2,616 | 2,611 | — |
| Metals and Equipment ^(a) | 259 | 284 | (9) | 704 | 723 | (3) | 2,718 | 2,546 | 7 |
| Housing and Construction | | | | | | | | | |
| Minerals ^(a) | 310 | 306 | 1 | 464 | 459 | 1 | 1,497 | 1,500 | — |
| Forest Products | 274 | 290 | (6) | 773 | 796 | (3) | 2,821 | 2,745 | 3 |
| Total Merchandise | 2,802 | 2,860 | (2) | 7,142 | 7,271 | (2) | 2,549 | 2,542 | — |
| Coal | 838 | 1,063 | (21) | 1,833 | 2,300 | (20) | 2,187 | 2,164 | 1 |
| Intermodal | 2,811 | 2,838 | (1) | 1,726 | 1,762 | (2) | 614 | 621 | (1) |
| Other | — | — | — | 368 | 478 | (23) | — | — | — |
| Total | 6,451 | 6,761 | (5)% | \$11,069 | \$11,811 | (6)% | \$1,716 | \$1,747 | (2)% |

(a) In order to better align markets with the Company's business strategy, changes were made to the categorization of certain lines of business during the third quarter 2016. Prior periods have been reclassified to conform to the current presentation and are posted on the Company's website at csx.com under the investors section.

Agricultural and Food Products includes the combination of the previous Agricultural Products and Food and Consumer markets.

Fertilizers was previously named Phosphates and Fertilizers.

Metals and Equipment includes the Equipment portion of the previous Waste and Equipment market.

Chemicals includes the Waste portion of the previous Waste and Equipment market. Chemicals also includes fly ash for remediation purposes (a form of waste) which was previously included within the Minerals market.

(b) CSX follows a 52/53 week fiscal reporting calendar and 2016 included 53 weeks. The revenue impact of the extra week was \$178 million.

CSX CORPORATION
PART II

Revenue

In 2016, revenue decreased \$742 million, or six percent, due to a five percent decline in volume (including the \$178 million positive impact of an extra week of volume) and a significant decline in fuel recoveries, partially offset by pricing strength.

Merchandise

Agricultural

Agricultural and Food Products - Volume declined as the strong U.S. dollar continued to support import grain and a robust Southeastern crop spurred additional local truck sourcing, displacing grain shipments by rail. Additionally, ethanol market dynamics shifted to favor the Gulf region for storage and export, precluding CSX from participation in shipments from Western origins to the Gulf.

Fertilizers - Volume was flat as the strong U.S. dollar, which drove high levels of imported sulfur, displaced rail transport, and nitrogen demand fell in anticipation of further commodity price deterioration. This offset growth in phosphate rock, driven by operational efficiency that allowed for additional rail traffic conversion that would otherwise move by truck.

Industrial

Chemicals - Volume declined as energy market headwinds significantly reduced crude oil and frac sand shipments. This reduction was partially offset by the ramp up of a fly ash remediation project and a modest increase in core chemical markets.

Automotive - Volume increased as a result of strong North American light vehicle production and growth across several customers. Additionally, movement of trucks and SUVs continued to outpace passenger cars, consistent with customer buying patterns.

Metals and Equipment - Volume was down as the strong U.S. dollar allowed for continued high levels of steel imports, which led to reduced domestic steel production, mill closures and the loss of associated rail moves. These declines were partially offset by strength in the wind-energy and power generation markets.

Housing and Construction

Minerals - Volume was up slightly due to strong gains in aggregates (which include crushed stone, sand and gravel), particularly for highway and non-residential construction in southern markets. The growth was partially offset by headwinds in salt and lime, reflecting mild winter weather and steel production challenges, respectively.

Forest Products - Volume declined as headwinds from electronic substitution and reduced paper products demand drove industry consolidation that reduced rail volume. Further, excess truck capacity in 2016 captured some volume that traditionally moved by rail.

Coal

Domestic - Volume declined as mild winter weather in the beginning of the year and low natural gas prices reduced utility coal burn rates and resulted in inflated coal stockpiles. Further, the weak domestic integrated steel market drove volume decreases in coke.

Export - Volume was down in both metallurgical and thermal coal as a result of the strong U.S. dollar and global oversupply which impacted U.S. competitiveness in the world market, particularly in the first half of the year.

CSX CORPORATION
PART II

Intermodal

Domestic - Volume increased as secular growth from the highway-to-rail conversion program and new service offerings were partially offset by excess truck capacity headwinds and a short-haul competitive loss.

International - Volume declined as headwinds from competitive losses more than offset moderate growth across other customers.

Other

Other revenue decreased \$110 million versus prior year primarily due to payments received in 2015 from customers that did not meet volume commitments. Further decreases in incidental revenue as well as lower coal revenue from affiliates were partially offset by adjustments to revenue reserves.

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CSX CORPORATION
PART II

Expense

In 2016, total expenses decreased \$547 million, or seven percent, compared to prior year. Descriptions of each expense category as well as significant year-over-year changes are described below. Year-over-year changes related to the extra week are estimated incremental expenses of \$116 million incurred for the week of December 24 through December 30, 2016.

Labor and Fringe expenses include employee wages and related payroll taxes, health and welfare costs, pension, other post-retirement benefits and incentive compensation. These expenses decreased \$131 million due to the following items:

- Efficiency savings of \$249 million were driven by lower T&E and operating support costs as a result of structural changes, reduced crew training and the Company's train length initiative that began in the second quarter of 2015.

- Volume-related costs were \$116 million lower.

- Incentive compensation was \$111 million higher reflecting the expected award payouts on existing plans.

- Inflation resulted in \$106 million of additional cost driven by increased health and welfare costs.

- The extra week resulted in \$51 million of additional cost.

- Restructuring costs decreased \$37 million due to the 2015 workforce reduction initiatives costs that nearly all occurred in 2015.

- Various other costs increased \$3 million.

Materials, Supplies and Other expenses consist primarily of contracted services to maintain infrastructure and equipment, terminal and coal pier services and professional services. This category also includes costs related to materials, travel, casualty claims, environmental remediation, train accidents, property and sales tax, utilities and other items. Total materials, supplies and other expenses decreased \$267 million driven by the following:

- Real estate gains increased \$98 million primarily related to a current year gain of \$115 million related to the sale of an operating property and other related income partially offset by a prior year real estate gain.

- Efficiency savings of \$95 million were primarily related to lower operating support costs driven by structural changes and broad cost containment.

- Train accident and casualty costs were \$70 million lower due to the continuing declines in the severity of train accidents as well as injuries.

- Inflation resulted in \$34 million of additional costs.

- The extra week resulted in \$18 million of additional cost.

- Volume-related costs were \$11 million lower.

- Various other costs decreased \$45 million.

Fuel expense includes locomotive diesel fuel as well as non-locomotive fuel. This expense is largely driven by the market price and locomotive consumption of diesel fuel. Fuel expense decreased \$244 million driven by the following:

- Average fuel price per gallon decreased 18 percent, from \$1.80 to \$1.48 per gallon versus the prior year, which reduced expenses by \$137 million.

- Efficiency savings of \$60 million were primarily related to locomotive fuel reduction technology and process improvement.

- Volume-related costs were \$58 million lower.

- The extra week resulted in \$15 million of additional cost.

- Various other costs decreased \$4 million.

CSX CORPORATION
PART II

Depreciation expense primarily relates to recognizing the costs of a capital asset, such as locomotives, railcars and track structure, over its useful life. This expense is impacted primarily by the capital expenditures made each year. Depreciation expense increased \$93 million due to a larger asset base and the \$25 million impact of the extra week in 2016.

Equipment and Other expenses include rent paid for freight cars owned by other railroads or private companies, net of rents received by CSXT for use of its equipment. This category of expenses also includes lease expenses for locomotives, railcars, containers and trailers, offices and other rentals. These expenses increased \$2 million driven by the following:

- Inflation resulted in \$18 million of additional cost primarily related to rates on automotive freight cars.
- Volume related costs were \$14 million higher due primarily to growth in automotive volume.
- The extra week resulted in \$7 million of additional cost.
- Efficiency savings of \$23 million were due to improved car cycle times.
- Net other costs decreased \$14 million.

Interest Expense increased \$35 million to \$579 million due to higher average debt balances in addition to \$11 million of additional expense related to the extra week in 2016, partially offset by lower average interest rates.

Debt Repurchase Expense increased to \$115 million due to the repurchase of certain notes that were expected to mature in 2017, 2018 and 2019.

Other Income (Expense) - net decreased \$52 million to \$46 million primarily due to a prior year \$59 million gain on a sale of non-operating easements and reimbursement of environmental costs of \$21 million related to this sale. This decrease was partially offset by other non-operating items, none of which were individually significant.

Income Tax Expense decreased \$143 million to \$1.0 billion primarily due to lower earnings.

Net Earnings decreased \$254 million to \$1.7 billion, and earnings per diluted share decreased \$0.19 to \$1.81 due to the factors mentioned above. Lower average shares outstanding resulting from higher share repurchase activity had a positive impact on earnings per diluted share.

CSX CORPORATION
PART II

2015 vs. 2014 Results of Operations

| | Fiscal Years | | \$ Change | % Change | |
|-------------------------------|--------------|----------|--------------|-------------|-----|
| | 2015 | 2014 | | | |
| (Dollars in Millions) | | | | | |
| Revenue | \$11,811 | \$12,669 | \$ (858) | (7) | % |
| Expense | | | | | |
| Labor and Fringe | 3,290 | 3,377 | 87 | 3 | |
| Materials, Supplies and Other | 2,336 | 2,484 | 148 | 6 | |
| Fuel | 957 | 1,616 | 659 | 41 | |
| Depreciation | 1,208 | 1,151 | (57) | (5) |) |
| Equipment and Other Rents | 436 | 428 | (8) | (2) |) |
| Total Expense | 8,227 | 9,056 | 829 | 9 | |
| Operating Income | 3,584 | 3,613 | (29) | (1) |) |
| Interest Expense | (544) | (545) | 1 | — | |
| Debt Repurchase Expense | — | (16) | 16 | 125 | |
| Other Income - Net | 98 | (8) | 106 | (1,325) | |
| Income Tax Expense | (1,170) | (1,117) | (53) | (5) |) |
| Net Earnings | \$1,968 | \$1,927 | \$41 | 2 | |
| Earnings Per Diluted Share: | | | | | |
| Net Earnings | \$2.00 | \$1.92 | \$0.08 | 4 | % |
| Operating Ratio | 69.7 | % 71.5 | % | 180 | bps |

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CSX CORPORATION
PART II

2015 vs. 2014 Results of Operations, continued

Volume and Revenue (Unaudited)

Volume (Thousands of units); Revenue (Dollars in Millions); Revenue Per Unit (Dollars)

| | Volume | | | Revenue | | | Revenue Per Unit | | |
|---|--------|-------|----------|----------|----------|----------|------------------|---------|----------|
| | 2015 | 2014 | % Change | 2015 | 2014 | % Change | 2015 | 2014 | % Change |
| Agricultural | | | | | | | | | |
| Agricultural and Food Products ^(a) | 503 | 513 | (2)% | \$1,345 | \$1,395 | (4)% | \$2,674 | \$2,719 | (2)% |
| Fertilizers ^(a) | 301 | 330 | (9) | 489 | 534 | (8) | 1,625 | 1,618 | — |
| Industrial | | | | | | | | | |
| Chemicals ^(a) | 726 | 728 | — | 2,284 | 2,375 | (4) | 3,146 | 3,262 | (4) |
| Automotive | 450 | 435 | 3 | 1,175 | 1,213 | (3) | 2,611 | 2,789 | (6) |
| Metals and Equipment ^(a) | 284 | 331 | (14) | 723 | 824 | (12) | 2,546 | 2,489 | 2 |
| Housing and Construction | | | | | | | | | |
| Minerals ^(a) | 306 | 288 | 6 | 459 | 448 | 2 | 1,500 | 1,556 | (4) |
| Forest Products | 290 | 307 | (6) | 796 | 819 | (3) | 2,745 | 2,668 | 3 |
| Total Merchandise | 2,860 | 2,932 | (2) | 7,271 | 7,608 | (4) | 2,542 | 2,595 | (2) |
| Coal | 1,063 | 1,262 | (16) | 2,300 | 2,849 | (19) | 2,164 | 2,258 | (4) |
| Intermodal | 2,838 | 2,728 | 4 | 1,762 | 1,790 | (2) | 621 | 656 | (5) |
| Other | — | — | — | 478 | 422 | 13 | — | — | — |
| Total | 6,761 | 6,922 | (2)% | \$11,811 | \$12,669 | (7)% | \$1,747 | \$1,830 | (5)% |

(a) In order to better align markets with the Company's business strategy, changes were made to the categorization of certain lines of business during the third quarter 2016. Prior periods have been reclassified to conform to the current presentation and are posted on the Company's website at csx.com under the investors section.

Agricultural and Food Products includes the combination of the previous Agricultural Products and Food and Consumer markets.

Fertilizers was previously named Phosphates and Fertilizers.

Metals and Equipment includes the Equipment portion of the previous Waste and Equipment market.

Chemicals includes the Waste portion of the previous Waste and Equipment market. Chemicals also includes fly ash for

remediation purposes (a form of waste) which was previously included within the Minerals market.

CSX CORPORATION
PART II

Revenue

In 2015, revenue decreased \$858 million, or seven percent, mostly due to the decline in fuel surcharge of \$646 million. Additionally, the decline in volume of two percent and unfavorable mix were partially offset by pricing strength.

Merchandise

Agricultural

Agricultural and Food Products - Volume declined due to challenging world market conditions and a strong U.S. dollar. Specifically, high levels of imported ethanol reduced rail moves to Eastern markets and the strong dollar hampered export grain competitiveness. Additionally, excess truck capacity led to lower shipments of food products. These declines were partially offset by strength in feed grain and domestic soybean moves, reflecting the record 2014-2015 harvest.

Fertilizers - Volume was down, reflecting weak demand driven by oversupply of fertilizer, low corn prices and a challenged export market due to strength of the U.S. dollar.

Industrial

Chemicals - Volume was flat as strong gains in LPG and petroleum products were offset by the slowdown in crude oil and frac sand due to low oil prices and the conclusion of major waste remediation projects.

Automotive - Volume increased as gains in auto movement, especially SUVs and trucks, resulted from strong North American light vehicle production and consumer demand.

Metals and Equipment - Volume declined primarily due to high levels of steel imports which resulted from the strength of the U.S. dollar and led to lower production of domestic steel.

Housing and Construction

Minerals - Volume growth reflects strength in aggregates (which include crushed stone, sand and gravel) due to increased highway and non-residential construction activity.

Forest Products - Volume declines reflect high inventories of building products in the housing sector as well as declining demand due to electronic substitution in paper products.

Coal

Domestic - Volume declined as a result of mild weather, high stockpiles and low natural gas prices favoring natural gas power generation.

Export - Reductions in both metallurgical and thermal coal volume resulted from ongoing weak market conditions due to global oversupply and the strength of the U.S. dollar.

Intermodal

Domestic - Domestic volume increased 12 percent due to customer growth, continued success with CSX's highway-to-rail conversion program and new service offerings.

International - Competitive losses resulted in a five percent international volume decline during a volatile year marked by West Coast port disruption, a subsequent volume surge and then a weak peak season.

Other

Other revenue increased \$56 million as a result of higher revenue from customers who did not meet minimum contractual volumes as well as higher incidental revenue.

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CSX CORPORATION
PART II

Expense

In 2015, total expenses decreased \$829 million, or nine percent, compared to prior year. Descriptions of each expense category as well as significant year-over-year changes are described below.

Labor and Fringe expenses include employee wages and related payroll taxes, health and welfare costs, pension, other post-retirement benefits and incentive compensation. These expenses decreased \$87 million due to the following items:

• Inflation resulted in \$128 million of additional cost driven by increased wages partially offset by reduced health and welfare costs.

• Incentive compensation was \$97 million lower reflecting reduced award payouts on existing plans.

• Efficiency savings of \$84 million were primarily a result of reduced crew starts due to the Company's train length initiatives, lower operating support costs and reduced management headcount.

• Volume-related costs were \$66 million lower.

• Restructuring costs were \$2 million higher versus prior year. See Note 1, Nature of Operations and Significant Accounting Policies under the caption, "Workforce Reduction Plans, Separation and Other Costs."

• Various other costs increased \$30 million.

Materials, Supplies and Other expenses consist primarily of contracted services to maintain infrastructure and equipment, terminal services at automotive facilities and professional services. This category also includes costs related to materials, travel, casualty claims, environmental remediation, train accidents, property and sales tax, utilities and other items. Total materials, supplies and other expenses decreased

\$148 million driven by the following:

• Efficiency savings of \$91 million were driven by a reduction in professional costs as well as lower operating support costs.

• Volume-related costs were \$52 million lower.

• Real estate gains were \$23 million higher primarily related to the sale of operating rail corridor.

• Inflation resulted in \$47 million of additional costs.

• Various other costs decreased \$29 million.

Fuel expense includes locomotive diesel fuel as well as non-locomotive fuel. This expense is largely driven by the market price and locomotive consumption of diesel fuel. Fuel expense decreased \$659 million driven by the following:

• Average fuel price per gallon decreased 39 percent, from \$2.95 to \$1.80 per gallon, versus the prior year which reduced expenses by \$560 million.

• Volume-related costs were \$66 million lower.

• Other fuel savings of \$33 million were primarily due to lower non-locomotive fuel price.

Depreciation expense primarily relates to recognizing the costs of a capital asset, such as locomotives, railcars and track structure, over its useful life. This expense is impacted primarily by the capital expenditures made each year. Depreciation expense increased \$57 million due to a larger asset base.

CSX CORPORATION
PART II

Equipment and Other includes rent paid for freight cars owned by other railroads or private companies, net of rents received by CSXT for use of its equipment. This category of expenses also includes lease expenses for locomotives, railcars, containers and trailers, offices and other rentals. These expenses increased \$8 million driven by the following:

- Inflation resulted in \$16 million of additional cost related to rates on automotive and intermodal cars.
- Efficiency savings of \$15 million were due to improved car cycle times.
- Net other costs increased \$7 million.

Interest Expense decreased \$1 million to \$544 million due to lower average interest rates partially offset by higher average debt balances.

Debt Repurchase Expense decreased \$16 million associated with costs incurred in 2014 related to the early redemption of long-term debt did not repeat in the current year.

Other Income (Expense) - net increased \$122 million to \$98 million primarily due to a \$59 million gain on a sale of non-operating easements and a reimbursement of environmental costs of \$21 million related to this sale. Additionally, 2015 environmental costs were \$21 million lower than 2014.

Income Tax Expense increased \$53 million to \$1.2 billion primarily due to higher earnings as well as prior year favorable state legislative changes that did not repeat in the current year.

Net Earnings increased \$41 million to \$2.0 billion, and earnings per diluted share increased \$0.08 to \$2.00 due to the factors mentioned above. Lower average shares outstanding resulting from higher share repurchase activity also had a positive impact on earnings per diluted share.

CSX CORPORATION
PART II

Operating Statistics (Estimated)

| | Fiscal Years | | Improvement/ (Deterioration) |
|-------------------------------------|--------------|---------|---------------------------------|
| | 2016 | 2015 | |
| Safety and Service Measurements | | | |
| FRA Personal Injury Frequency Index | 1.02 | 0.94 | (9)% |
| FRA Train Accident Rate | 2.62 | 2.61 | — |
| On-Time Train Originations | 84 | % 67 | % 25 |
| On-Time Destination Arrivals | 65 | % 51 | % 27 |
| Dwell | 25.7 | 25.8 | — |
| Train Velocity | 20.8 | 20.5 | 1 |
| Cars-On-Line | 207,943 | 206,078 | (1) |

Certain operating statistics are estimated and can continue to be updated as actuals settle.

Key Performance Measures Definitions

FRA Personal Injury Frequency Index - Number of FRA-reportable injuries per 200,000 man-hours.

FRA Train Accident Rate - Number of FRA-reportable train accidents per million train-miles.

On-Time Train Originations - Percent of scheduled road trains that depart the origin yard on-time or ahead of schedule.

On-Time Destination Arrivals - Percent of scheduled road trains that arrive at the destination yard on-time or earlier to two hours late (30 minutes for intermodal trains).

Dwell - Average amount of time in hours between car arrival at and departure from the yard. It does not include cars moving through the yard on the same train.

Train Velocity - Average train speed between terminals in miles per hour (does not include locals, yard jobs, work trains or passenger trains).

Cars-On-Line - An average count of all cars on the network (does not include locomotives, cabooses, trailers, containers or maintenance equipment).

The Company measures and reports safety and service performance. The Company strives for continuous improvement in these measures through training, innovation and investment. CSX's safety and train accident prevention programs rely on the latest tools, programs and employee participation that are designed to continuously strengthen the safety culture. Increased investment in training and technology also is designed to allow CSX employees to have an additional layer of protection that can detect and avoid many types of human factor incidents. The Company's safety programs are designed to prevent incidents that can adversely impact employees, customers and communities.

Continued capital investment in the Company's assets, including track, bridges, signals, equipment and detection technology also supports safety performance. CSX has established formal relationships with industry groups, leading universities and suppliers to develop, implement and deploy the latest technology that can detect infrastructure problems before they happen. To illustrate, through a waiver granted by the FRA, CSX is using advanced continuous rail testing methods that are being adopted by other railroads as the system's value is proven.

The Company constantly collaborates with the FRA and industry organizations as well as federal, state and local governments on safety innovations and initiatives. For example, CSX and other freight railroads have actively worked with the U.S. DOT and other key stakeholders to evaluate and implement far-reaching safety enhancements for transportation of certain flammable materials, including essential energy products, on the nation's freight railroad

network.

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CSX CORPORATION
PART II

At CSX, operational success is built on employee commitment to maintaining a constant focus on safety. Although the number of FRA reportable personal injuries decreased 10 percent year-over-year, the FRA reportable personal injury frequency index increased 9 percent to 1.02 due to a 17 percent decrease in labor hours versus 2015. While the reported FRA train accident frequency rate has remained flat year-over-year at 2.62, both overall FRA train accidents and train miles have decreased 14 percent year-over-year.

The Company made strong improvements to network reliability and service measures in 2016 while delivering a record level of productivity. On-time originations improved 25 percent year-over-year to 84 percent, and on-time arrivals increased 27 percent year-over-year to 65 percent. Terminal dwell remained flat at 25.7 hours versus 2015 and average train velocity increased one percent to 20.8 miles per hour.

LIQUIDITY AND CAPITAL RESOURCES

Liquidity is a company's ability to generate adequate amounts of cash to meet both current and future needs for obligations as they mature and to provide for planned capital expenditures, including those to address regulatory and legislative requirements. To have a complete picture of a company's liquidity, its balance sheet, sources and uses of cash flow and external factors should be reviewed.

Material Changes in the Consolidated Balance Sheets and Significant Cash Flows

Consolidated Balance Sheets

CSX's balance sheet reflects its strong capital base and the impact of CSX's balanced approach in deploying capital for the benefit of its shareholders, which includes investments in infrastructure, dividend payments and share repurchases.

Total assets as well as total liabilities and shareholders' equity increased \$669 million from prior year. The increase in assets was driven by higher net properties of \$976 million resulting from capital investments, partially offset by payments of about \$300 million made on debt related to assets purchased in 2015 under seller financing. The increase in total liabilities and shareholders' equity combined was driven by an increase in net borrowings of about \$450 million (including payments made on debt for assets purchased in 2015 under seller financing) and an increase in deferred income tax liabilities of \$417 million. Partially offsetting these increases was a reduction in other long-term liabilities due to voluntary pension contributions of \$250 million.

Significant cash flows

The following charts present net cash provided by (used in) operating, investing and financing activities for full years 2014, 2015 and 2016.

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Sources of Cash

The Company has multiple sources of cash. First, the Company generates cash from operations. In 2016, the Company generated \$3.0 billion of cash from operating activities which was \$329 million lower than prior year primarily driven by \$250 million in voluntary contributions to the Company's qualified pension plans. In 2015, the Company generated \$3.4 billion of cash from operating activities which was \$27 million higher than 2014 primarily driven by higher collections of freight account receivables.

Second, CSX has access to numerous financing sources including a \$1 billion five-year unsecured revolving credit facility that expires in May 2020. As of the date of this filing, the Company has no outstanding balances under this facility. See Note 9, Debt and Credit Agreements for more information.

Third, CSX filed a new shelf registration statement with the SEC in February 2016 which is unlimited as to amount and may be used to issue debt or equity securities at CSX's discretion, subject to market conditions and CSX Board authorization. While CSX seeks to give itself flexibility with respect to cash requirements, there can be no assurance that market conditions would permit CSX to sell such securities on acceptable terms at any given time, or at all.

Uses of Cash

CSX continued to invest in its business to create long-term value for shareholders. In 2016, net cash used in investing activities was \$1.8 billion, a decrease of \$1.1 billion from the prior year primarily driven by lower net purchases of short-term investments and lower property additions. In 2015, net cash used in investing activities was \$2.9 billion, an increase in net investing of \$709 million from 2014 primarily driven by fewer net sales of short-term investments.

The Company is committed to maintaining and improving its existing infrastructure and to positioning itself for long-term growth through expanding network and terminal capacity. Funds used for property additions are further described below.

| Capital Expenditures (Dollars in Millions) | Fiscal Years | | |
|--|--------------|-------|-------|
| | 2016 | 2015 | 2014 |
| Track | \$714 | \$866 | \$750 |
| Bridges, Signals and Other | 433 | 491 | 538 |
| Total Infrastructure | 1,147 | 1,357 | 1,288 |
| Freight Cars | 82 | 218 | 329 |
| Capacity and Commercial Facilities | 406 | 295 | 452 |
| Regulatory (including PTC) | 313 | 341 | 321 |
| Locomotives | 409 | 337 | 51 |
| Public-Private Partnerships - net ^(a) | 41 | 14 | 8 |
| Total Property Additions | 2,398 | 2,562 | 2,449 |
| Cash paid for new assets using seller financing ^(b) | 307 | \$— | \$— |
| Total Capital Expenditures ^(a) | \$2,705 | 2,562 | 2,449 |

Total capital expenditures shown above include investments related to reimbursable public-private partnerships.

These partnership investments are for projects that are partially or wholly reimbursed to CSX through either (a) government grants or other funding sources such as cash received from a property sale. These reimbursements may not be fully received in a given year; therefore the timing of receipts may differ from the timing of the investment.

(b) In 2016, CSX made payments related to locomotive purchases made in 2015 using seller financing of \$307 million.

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Planned capital investments for 2017 are expected to be \$2.2 billion, including about \$270 million for PTC. This \$2.2 billion excludes investments related to partially or wholly reimbursable public-private partnerships where reimbursements may not be fully received in the year the reimbursement obligation arises. Approximately half of the 2017 investment will be used to sustain the core infrastructure. The remaining amounts will be allocated to locomotives, freight cars and high return projects supporting long-term profitable growth, productivity initiatives and service improvements to optimize performance. CSX intends to fund capital investments through cash generated from operations.

The Company expects to continue incurring significant capital costs in connection with the implementation of PTC. CSX estimates that the total multi-year cost of PTC implementation will be approximately \$2.4 billion. This estimate includes costs for installing the new system along tracks, upgrading locomotives, adding communication equipment and developing new technologies. Total PTC spending through 2016 was \$1.8 billion.

In addition to capital investments, the Company uses cash for scheduled payments of debt and leases, share repurchases and to pay dividends to shareholders. In 2016, net cash used in financing activities was \$1.3 billion, which represents an increase in spending of \$749 million from the prior year primarily driven by the repayment of seller-financed assets, higher share repurchases, and lower net debt issued. In 2015, net cash used in financing activities was \$519 million, which represents a decrease in spending of \$564 million from the prior year primarily driven by higher net long-term debt issued of \$904 million (net of lower debt repayments) partially offset by higher share repurchases of \$287 million.

CSX is continually evaluating market and regulatory conditions that could affect the Company's ability to generate sufficient returns on capital investments. CSX may revise its future estimates for capital spending as a result of changes in business conditions, tax legislation or the enactment of new laws or regulations which could have a material adverse effect on the Company's operations and financial performance in the future (see Risk Factors under Item 1A of this Form 10-K).

Liquidity and Working Capital

Currently, CSX is well positioned from a liquidity standpoint. The Company ended the year with \$1.0 billion of cash, cash equivalents and short-term investments. CSX has a \$1 billion unsecured, revolving credit facility backed by a diverse syndicate of banks. This facility expires in May 2020 and as of the date of this filing, the Company has no outstanding balances under this facility. Additionally in 2016, CSX issued a total of \$2.2 billion of new long-term debt, \$1.4 billion of which was used to repay outstanding debt, to capitalize on the lower interest rate environment. CSX uses current cash balances for general corporate purposes, which may include repayment of additional indebtedness outstanding from time to time, repurchases of CSX's common stock, capital investments, working capital requirements and improvements in productivity and other cost reduction initiatives. See Note 9, Debt and Credit Agreements.

In September 2016, the Company renewed and modified its existing receivables securitization facility. The facility was extended with a three-year term scheduled to expire in September 2019. It was modified to provide liquidity of up to \$200 million, changed from the \$250 million, along with modifications to other terms. The purpose of this facility is to provide an alternative to commercial paper and a low cost source of short-term liquidity. Under the terms of this facility, CSXT transfers eligible third-party receivables to CSX Trade Receivables, a bankruptcy-remote special purpose subsidiary. A separate subsidiary of CSX services the receivables. Upon transfer, the receivables become assets of CSX Trade Receivables and are not available to the creditors of CSX or any of its other subsidiaries. In the event CSX Trade Receivables draws under this facility, the Company will record an equivalent amount of debt on its

consolidated financial statements. As of the date of this filing, the Company has no outstanding balances under this facility.

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Working capital can also be considered a measure of a company's ability to meet its short-term needs. CSX had a working capital surplus of \$447 million at December 2016 and \$888 million (after reclassification of current deferred taxes) at December 2015. This decrease since the prior year end is primarily due to an increase in long-term debt maturing within a year of \$311 million and cash from operations used for property additions, share repurchases and dividend payments.

The Company's working capital balance varies due to factors such as the timing of scheduled debt payments and changes in cash and cash equivalent balances as discussed above. Although the Company currently has a surplus, a working capital deficit is not unusual for CSX or other companies in the industry and does not indicate a lack of liquidity. The Company continues to maintain adequate current assets to satisfy current liabilities and maturing obligations when they come due. Furthermore, CSX has sufficient financial capacity, including its revolving credit facility, trade receivable facility and shelf registration statement to manage its day-to-day cash requirements and any anticipated obligations. The Company from time to time accesses the credit markets for additional liquidity.

Credit Ratings

Credit ratings reflect an independent agency's judgment on the likelihood that a borrower will repay a debt obligation at maturity. The ratings reflect many considerations, such as the nature of the borrower's industry and its competitive position, the size of the company, its liquidity and access to capital and the sensitivity of a company's cash flows to changes in the economy. The two largest rating agencies, Standard & Poor's Ratings Services ("S&P") and Moody's Investors Service ("Moody's"), use alphanumeric codes to designate their ratings. The highest quality rating for long-term credit obligations is AAA and Aaa for S&P and Moody's, respectively. A credit rating is not a recommendation to buy, sell or hold securities and may be subject to revision or withdrawal at any time by the assigning rating agency.

The cost and availability of unsecured financing are materially affected by CSX's long-term credit ratings. CSX's credit ratings remained stable during 2016. As of December 2015 and December 2016, S&P's long-term rating on CSX was BBB+ (Stable), and Moody's was Baa1 (Stable). Ratings of BBB- and Baa3 or better by S&P and Moody's, respectively, reflect ratings on debt obligations that fall within a band of credit quality considered to be investment grade. If CSX's credit ratings were to decline to below investment grade levels, the Company could experience significant increases in its interest cost for new debt. In addition, a decline in CSX's credit ratings to below investment grade levels could adversely affect the market's demand, and thus the Company's ability to readily issue new debt.

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Free Cash Flow (Non-GAAP Measure)

Free cash flow is considered a non-GAAP financial measure under SEC Regulation G and Reg S-K Item 10(e). Management believes that free cash flow is useful to investors as it is important in evaluating the Company's financial performance. More specifically, free cash flow measures cash generated by the business after reinvestment. This measure represents cash available for both equity and bond investors to be used for dividends, share repurchases or principal reduction on outstanding debt. Free cash flow should be considered in addition to, rather than a substitute for, cash provided by operating activities. Free cash flow is calculated by using net cash from operations and adjusting for property additions and certain other investing activities. Free cash flow before dividends decreased \$145 million year-over-year to \$847 million. The decrease in free cash flow from the prior year is primarily due to voluntary contributions to the Company's qualified pension plans of \$250 million in 2016, partially offset by lower property additions of \$164 million.

The following table reconciles cash provided by operating activities (GAAP measure) to free cash flow (non-GAAP measure).

| | Fiscal Years | | |
|--|--------------|----------|----------|
| | 2016 | 2015 | 2014 |
| (Dollars in Millions) | | | |
| Net cash provided by operating activities | \$3,041 | \$3,370 | \$3,343 |
| Property additions ^(a) | (2,398) | (2,562) | (2,449) |
| Proceeds from property dispositions | 195 | 147 | 62 |
| Other investing activities | 9 | 37 | (37) |
| Free Cash Flow (before payment of dividends) | \$847 | \$992 | \$919 |

Property additions include investments related to reimbursable public-private partnerships. These partnership investments of \$41 million, \$14 million and \$8 million in 2016, 2015 and 2014, respectively, are projects that are partially or wholly reimbursed to CSX through either government grants or other funding sources such as cash received from a property sale. These reimbursements may not be fully received in a given year; therefore, the timing of receipts may differ from the timing of the investment. Also, property additions for 2016 above do not include \$307 million for locomotives purchased in 2015 using seller financing with payment made in 2016.

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SCHEDULE OF CONTRACTUAL OBLIGATIONS AND COMMERCIAL COMMITMENTS

The following tables set forth maturities of the Company's contractual obligations and other significant commitments:

| Type of Obligation (Dollars in Millions) (Unaudited) | 2017 | 2018 | 2019 | 2020 | 2021 | Thereafter | Total |
|--|---------|-------|-------|---------|---------|------------|----------|
| Contractual Obligations | | | | | | | |
| Total Debt (See Note 9) | \$331 | \$20 | \$18 | \$745 | \$371 | \$9,808 | \$11,293 |
| Interest on Debt | 539 | 523 | 521 | 509 | 497 | 8,657 | 11,246 |
| Purchase Obligations (See Note 7) | 363 | 336 | 312 | 316 | 310 | 3,943 | 5,580 |
| Other Post-Employment Benefits (See Note 8) ^(a) | 54 | 43 | 41 | 40 | 38 | 165 | 381 |
| Operating Leases - Net (See Note 7) ^(b) | 48 | 36 | 32 | 19 | 10 | 72 | 217 |
| Agreements with Conrail (See Note 12) ^(b) | 27 | 27 | 27 | 27 | 27 | 74 | 209 |
| Total Contractual Obligations | \$1,362 | \$985 | \$951 | \$1,656 | \$1,253 | \$22,719 | \$28,926 |
| Other Commitments ^(c) | \$110 | \$3 | \$2 | \$2 | \$2 | \$2 | \$121 |

Other post-employment benefits include estimated other post-retirement medical and life insurance payments and (a) payments under non-qualified pension plans which are unfunded. No amounts are included for funded pension obligations as no contributions are currently required.

Agreements with Conrail represent minimum future lease payments of \$209 million under the shared asset area (b) agreements (see Note 12, Related Party Transactions). These amounts plus total operating leases-net of \$217 million above equals total net lease commitments of \$426 million disclosed in Note 7, Commitments and Contingencies.

Other commitments of \$121 million consisted of surety bonds, letters of credit, uncertain tax positions and public (c) private partnerships. Surety bonds of \$48 million and letters of credit of \$33 million arise from assurances issued by a third-party that CSX will fulfill certain obligations and are typically a contract, state, federal or court requirement. Uncertain tax positions of \$25 million, which include interest and penalties, are all included in year 2017 as the year of settlement cannot be reasonably estimated. Contractual commitments related to public-private partnerships are \$15 million.

OFF-BALANCE SHEET ARRANGEMENTS

For detailed information about the Company's guarantees, operating leases and purchase obligations, see Note 7, Commitments and Contingencies. There are no off-balance sheet arrangements that are reasonably likely to have a material effect on the Company's financial condition, results of operations or liquidity.

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CRITICAL ACCOUNTING ESTIMATES

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires that management make estimates in reporting the amounts of certain assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and certain revenues and expenses during the reporting period. Actual results may differ from those estimates. These estimates and assumptions are discussed with the Audit Committee of the Board of Directors on a regular basis. Consistent with the prior year, significant estimates using management judgment are made for the following areas:

- casualty, environmental and legal reserves;
- pension and post-retirement medical plan accounting;
- depreciation policies for assets under the group-life method; and
- income taxes.

Casualty, Environmental and Legal Reserves

Casualty

Casualty reserves of \$229 million and \$269 million for 2016 and 2015, respectively, represent accruals for personal injury, occupational disease and occupational injury claims. A majority of the casualty reserves relate to personal injuries. The Company's self-insured retention amount for these claims is \$50 million per occurrence. Currently, no individual claim is expected to exceed the self-insured retention amount. In accordance with the Contingencies Topic in the ASC, to the extent the value of an individual claim exceeds the self-insured retention amount, the Company would present the liability on a gross basis with a corresponding receivable for insurance recoveries. These reserves fluctuate based upon the timing of payments as well as changes in estimate. Actual results may vary from estimates due to the number, type and severity of the injury, costs of medical treatments and uncertainties in litigation. Most of the Company's casualty claims relate to CSXT unless otherwise noted below. Defense and processing costs, which historically have been insignificant and are anticipated to be insignificant in the future, are not included in the recorded liabilities.

Personal Injury

Personal Injury reserves of \$170 million and \$204 million for 2016 and 2015, represent liabilities for employee work-related and third-party injuries. Work-related injuries for CSXT employees are primarily subject to FELA. In addition to FELA liabilities, employees of other current or former CSX subsidiaries are covered by various state workers' compensation laws, the Federal Longshore and Harbor Workers' Compensation Program or the Maritime Jones Act.

CSXT retains an independent actuary to assist management in assessing the value of personal injury claims. An analysis is performed by the actuary quarterly and is reviewed by management. The methodology used by the actuary includes a development factor to reflect growth or reduction in the value of these personal injury claims. It is based largely on CSXT's historical claims and settlement experience.

As a direct result of improvements in safety in recent years, the Company has experienced a downward trend in the severity of injuries which has resulted in a decrease in the estimate of costs per incident. During 2016, the Company reduced casualty reserves, primarily personal injury reserves, by \$28 million, resulting in after-tax effect on earnings from continuing operations and net earnings of \$18 million and an after-tax effect on earnings per share of \$0.02. The personal injury reserve reductions were included in materials, supplies and other on the consolidated income statements. During 2015 and 2014, there were no significant changes in estimate recorded to adjust casualty reserves.

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Critical Accounting Estimates, continued

Occupational

Occupational reserves of \$59 million and \$65 million for 2016 and 2015, respectively, represent liabilities for occupational disease claims and occupational injury claims. Occupational disease claims arise primarily from allegations of exposure to asbestos in the workplace. Occupational injury claims arise from allegations of exposure to certain other materials in the workplace, such as solvents, soaps, chemicals (collectively referred to as "irritants") and diesel fuels (like exhaust fumes) or allegations of chronic physical injuries resulting from work conditions, such as repetitive stress injuries. The Company has experienced a downward trend in the number of occupational claims and reserves for these claims have decreased to a level that is no longer material to the Company's financial condition, results of operations or liquidity.

Environmental

Environmental reserves were \$95 million and \$82 million and 2016 and 2015, respectively. The Company is a party to various proceedings related to environmental issues, including administrative and judicial proceedings involving private parties and regulatory agencies. The Company has been identified as a potentially responsible party at approximately 222 environmentally impaired sites. Many of these are, or may be, subject to remedial action under the federal Comprehensive Environmental Response, Compensation and Liability Act of 1980 ("CERCLA"), also known as the Superfund Law, or similar state statutes. Most of these proceedings arose from environmental conditions on properties used for ongoing or discontinued railroad operations. A number of these proceedings, however, are based on allegations that the Company, or its predecessors, sent hazardous substances to facilities owned or operated by others for treatment, recycling or disposal. In addition, some of the Company's land holdings were leased to others for commercial or industrial uses that may have resulted in releases of hazardous substances or other regulated materials onto the property and could give rise to proceedings against the Company.

In any such proceedings, the Company is subject to environmental clean-up and enforcement actions under the Superfund Law, as well as similar state laws that may impose joint and several liability for clean-up and enforcement costs on current and former owners and operators of a site without regard to fault or the legality of the original conduct. These costs could be substantial.

In accordance with the Asset Retirement and Environmental Obligations Topic in the ASC, the Company reviews its role with respect to each site identified at least quarterly, giving consideration to a number of factors such as:

- type of clean-up required;
- nature of the Company's alleged connection to the location (e.g., generator of waste sent to the site or owner or operator of the site);
- extent of the Company's alleged connection (e.g., volume of waste sent to the location and other relevant factors); and
- number, connection and financial viability of other named and unnamed potentially responsible parties at the location.

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PART II

Critical Accounting Estimates, continued

Based on the review process, the Company has recorded amounts to cover contingent anticipated future environmental remediation costs with respect to each site to the extent such costs are reasonably estimable and probable. The recorded liabilities for estimated future environmental costs are undiscounted. The liability includes future costs for remediation and restoration of sites as well as any significant ongoing monitoring costs, but excludes any anticipated insurance recoveries. Payments related to these liabilities are expected to be made over the next several years. Environmental remediation costs are included in materials, supplies and other on the consolidated income statement.

Currently, the Company does not possess sufficient information to reasonably estimate the amounts of additional liabilities, if any, on some sites until completion of future environmental studies. In addition, conditions that are currently unknown could, at any given location, result in additional exposure, the amount and materiality of which cannot presently be reasonably estimated. Based upon information currently available, however, the Company believes its environmental reserves accurately reflect the cost of remedial actions currently required.

Legal

In accordance with the Contingencies Topic in the ASC, an accrual for a loss contingency is established if information available prior to issuance of the financial statements indicates that it is probable that an asset has been impaired or a liability has been incurred at the date of the financial statements, and the amount of loss can be reasonably estimated. If no accrual is made for a loss contingency because one or both of these conditions are not met, or if an exposure to loss exists in excess of the amount accrued, disclosure of the contingency is made when there is at least a reasonable possibility that a loss or an additional loss may have been incurred.

The Company evaluates all exposures relating to legal liabilities at least quarterly and adjusts reserves when appropriate under the guidance noted above. The amount of a particular reserve may be influenced by factors that include official rulings, newly discovered or developed evidence, or changes in laws, regulations and evidentiary standards. See Item 3. Legal Proceedings for further discussion of these items.

Pension and Post-retirement Medical Plan Accounting

The Company sponsors defined benefit pension plans principally for salaried, management personnel. For employees hired prior to 2003, the plans provide eligible employees with retirement benefits based predominantly on years of service and compensation rates near retirement. For employees hired in 2003 or thereafter, benefits are determined based on a cash balance formula, which provides benefits by utilizing interest and pay credits based upon age, service and compensation. As of December 2016, the projected benefit obligation for the Company's pension plans was \$2.9 billion.

In addition to these plans, the Company sponsors a post-retirement medical plan and a life insurance plan that provide certain benefits to full-time, salaried, management employees, hired prior to 2003, upon their retirement if certain eligibility requirements are met. Eligible retirees who are age 65 years or older (Medicare-eligible) are covered by a health reimbursement arrangement, which is an employer-funded account that can be used for reimbursement of eligible medical expenses. Eligible retirees younger than 65 years (non-Medicare eligible) are covered by a self-insured program partially funded by participating retirees. The life insurance plan is non-contributory. As of December 2016, the projected benefit obligation for the Company's other post-retirement benefit plans was \$274 million.

For information related to the funded status of the Company's pension and other post-retirement benefit plans, see Note 8, Employee Benefit Plans.

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Critical Accounting Estimates, continued

The accounting for these plans is subject to the guidance provided in the Compensation-Retirement Benefits Topic in the ASC. This rule requires that management make certain assumptions relating to the following:

- discount rates used to measure future obligations and interest expense;
- long-term rate of return on plan assets;
- salary scale inflation rates; and
- other assumptions.

The Company engages independent actuaries to compute the amounts of liabilities and expenses relating to these plans subject to the assumptions that the Company determines are appropriate based on historical trends, current market rates and future projections. These amounts are reviewed by management.

Discount Rates

Discount rates affect the amount of liability recorded and the interest expense component of pension and post-retirement expense. Discount rates reflect the rates at which pension and other post-retirement benefits could be effectively settled, or in other words, how much it would cost the Company to buy enough high quality bonds to generate cash flow equal to the Company's expected future benefit payments. The Company determines the discount rate based on the market yield as of year-end for high quality corporate bonds whose maturities match the plans' expected benefit payments.

The discount rates used by the Company to value its 2016 pension and post-retirement obligations are 4.08 percent and 3.71 percent, respectively. For 2015, the discount rate used by the Company to value its pension and post-retirement obligations was 4.30 percent and 3.85 percent, respectively. Discount rates may differ for pension and post-retirement benefits due to varying duration of the liabilities for projected payments for each plan. As of December 2016, the estimated duration of pensions and post-retirement benefits is approximately 12 years and eight years, respectively.

Each year, these discount rates are reevaluated and adjusted using the current market interest rates for high quality corporate bonds to reflect the best estimate of the current effective settlement rates. In general, if interest rates decline or rise, the assumed discount rates will change.

Long-term Rate of Return on Plan Assets

The expected long-term average rate of return on plan assets reflects the average rate of earnings expected on the funds invested, or to be invested, to provide for benefits included in the projected benefit obligation. In estimating that rate, the Company gives appropriate consideration to the returns being earned by the plan assets in the funds and the rates of return expected to be available for reinvestment as well as the current and projected asset mix of the funds. Management balances market expectations obtained from various investment managers and economists with both market and actual plan historical returns to develop a reasonable estimate of the expected long-term rate of return on assets. As this assumption is long-term, the annual review may result in less frequent adjustment than other assumptions used in pension accounting. The long-term rate of return on plan assets used by the Company to value its benefit cost for the subsequent plan year was 6.75 percent and 7 percent in 2016 and 2015, respectively.

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PART II

Critical Accounting Estimates, continued

Salary Scale Inflation Rates

Salary scale inflation rates are based on current trends and historical data accumulated by the Company. The Company reviews recent wage increases and management incentive compensation payments over the past five years in its assessment of salary scale inflation rates. The Company used a salary scale rate of 4.60 percent in both 2016 and 2015 to value its pension obligations.

Other Assumptions

The calculations made by the actuaries also include assumptions relating to health care cost trend rates, mortality rates, turnover and retirement age. These assumptions are based upon historical data, recent plan experience and industry trends and are determined by management.

2017 Estimated Pension and Post-retirement Expense

Net pension expense and post-retirement benefits expense for 2017 are each expected to be approximately \$10 million, compared to \$58 million and \$17 million, respectively, in 2016. The decrease in expense is primarily due to a change in approach to measuring service and interest costs, the impact of \$250 million in voluntary pension contributions and other favorable plan experience.

In 2017, the Company will measure the service and interest cost components of the net pension and post-retirement benefits expense by using individual spot rates matched with separate cash flows for each future year instead of a single weighted-average discount rate approach, which has been used in prior years.

The Company made this change to improve the correlation between projected pension and post-retirement benefit liability cash flows and the corresponding spot discount rates and to provide a more precise measurement of service and interest costs. Under the spot rate approach, individual spot discount rates along the same high quality corporate bonds yield curve used to measure the pension and post-retirement benefit liabilities are applied to the relevant projected cash flows at the relevant maturity. The calculated pension and post-retirement benefits liabilities are consistent under both the traditional and spot rate approaches. The Company accounted for this change on a prospective basis as a change in accounting estimate.

The following sensitivity analysis illustrates the effects of a one percent change in certain assumptions like discount rates, long-term rate of return and salaries on the 2017 estimated pension and post-retirement expense:

| (Dollars in Millions) | Pension Expense | Post-Retirement Expense |
|--------------------------|--------------------|----------------------------|
| Discount Rate | \$ 15 | \$ 1 |
| Long-term Rate of Return | \$ 26 | N/A |
| Salary Inflation | \$ 9 | N/A |

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PART II

Critical Accounting Estimates, continued

Depreciation Policies for Assets Utilizing the Group-Life Method

The Company depreciates its rail assets, including main-line track, locomotives and freight cars, using the group-life method of accounting. Assets depreciated under the group-life method comprise 86 percent of total fixed assets of \$43 billion on a gross basis at December 2016. All other assets of the Company are depreciated on a straight-line basis. The group-life method aggregates assets with similar lives and characteristics into groups and depreciates each of these groups as a whole. When using the group-life method, an underlying assumption is that each group of assets, as a whole, is used and depreciated to the end of its recoverable life.

The Company currently utilizes more than 130 different depreciable asset categories to account for depreciation expense for the railroad assets that are depreciated under the group-life method of accounting. Examples of depreciable asset categories include 18 different categories for crossties due to the different combinations of density classifications and asset types. By utilizing various depreciable categories, the Company can more accurately account for the use of its assets. All assets of the Company are depreciated on a time or life basis.

The Company believes the group-life method of depreciation closely approximates the straight-line method of depreciation. Additionally, due to the nature of most of its assets (e.g., track is one contiguous, connected asset), the Company believes that this is the most effective way to properly depreciate its assets.

Management performs a detailed review of depreciation expense and useful lives on a regular basis. Under the group-life method of accounting, the service lives and salvage values for each group of assets are determined by completing periodic depreciation studies and applying management's assumptions regarding the service lives of its properties. A depreciation study (also referred to as a life study) is the periodic review of asset service lives, salvage values, accumulated depreciation, and other related factors for group assets conducted by a third-party specialist, analyzed by the Company's management and approved by the STB, the regulatory board that has broad jurisdiction over railroad practices. The STB requires depreciation studies be performed for equipment assets generally every three years and for road (e.g. bridges and signals) and track (e.g., rail, ties and ballast) assets generally every six years. The Company believes the frequency currently required by the STB provides adequate review of asset service lives and that a more frequent review would not result in a material change due to the long-lived nature of most of the assets. In 2016, the Company completed a depreciation study for its equipment assets. In 2014, the Company completed a depreciation study for its road and track assets. The Company plans to complete the next depreciation study for road and track assets in 2020 and for equipment assets in 2019.

Changes in asset service lives due to the results of the depreciation studies are applied on a prospective basis and could significantly impact future periods' depreciation expense, and thus, the Company's results of operations.

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PART II

Critical Accounting Estimates, continued

There are several factors taken into account during the depreciation study and they include:

- statistical analysis of historical life and salvage data for each group of property;
- statistical analysis of historical retirements for each group of property;
- evaluation of current operations;
- evaluation of technological advances and maintenance schedules;
- previous assessment of the condition of the assets;
- management's outlook on the future use of certain asset groups;
- expected net salvage to be received upon retirement; and
- comparison of assets to the same asset groups with other companies.

Recent experience with depreciation studies has resulted in depreciation rate changes that did not materially affect the Company's annual depreciation expense of \$1.3 billion, \$1.2 billion and \$1.2 billion for 2016, 2015 and 2014 respectively. A 1% change in the average life of all group-life assets would result in an approximate \$12 million change to the Company's annual depreciation expense.

For retirements or disposals of depreciable rail assets that occur in the ordinary course of business, the asset cost (net of salvage value or sales proceeds) is charged to accumulated depreciation and no gain or loss is recognized. As individual assets within a specific group are retired, resulting gains and losses are recorded in accumulated depreciation. This practice is consistent with accounting treatment normally prescribed under the group-life method. As part of the depreciation study, an assessment of the recorded amount of accumulated depreciation is made to determine if it is deficient (or in excess) of the appropriate amount indicated by the study. Any such deficiency (or excess), including any deferred gains or losses, is amortized as a component of depreciation expense over the remaining service life of the asset group until the next required depreciation study. Since the overall assumption with group-life is that the assets within the group on average have the same service life and characteristics, it is therefore concluded that the deferred gains and losses offset over time.

In the event that large groups of assets are removed from service as a result of unusual acts or sales, resulting gains and losses are recognized immediately. These acts are not considered to be in the normal course of business and are therefore recognized when incurred. Examples of such acts would be the major destruction of assets due to significant storm damage (e.g., major hurricanes), the sale of a rail line segment to another railroad or the disposal of an entire class of assets (e.g., disposal of all refrigerated freight cars).

Income Taxes

CSX accounts for income taxes in accordance with the Income Taxes Topic in the ASC that addresses how tax benefits claimed or expected to be claimed on a tax return should be recorded in the financial statements. Under this topic, the Company recognizes the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by the taxing authorities based on the technical merits of the position. The amount recognized in the financial statements from such a position is measured based on the largest benefit that has a greater than 50 percent likelihood of being realized upon ultimate resolution.

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Critical Accounting Estimates, continued

CSX files a consolidated federal income tax return, which includes its principal domestic subsidiaries. Examinations of the federal income tax returns of CSX have been completed through 2015. During 2016, the Company participated in a contemporaneous Internal Revenue Service (“IRS”) audit of tax year 2016. Management believes an adequate provision has been made for any adjustments that might be assessed. While the final outcome of these matters cannot be predicted with certainty, it is the opinion of CSX management that none of these items will have a material adverse effect on the financial condition, results of operations or liquidity of CSX. An unexpected adverse resolution of one or more of these items, however, could have a material adverse effect on the results of operations in a particular fiscal quarter or fiscal year. As of December 2016, the Company’s uncertain tax positions were \$25 million.

New Accounting Pronouncements and Changes in Accounting Policy

See Note 1, Nature of Operations and Significant Accounting Policies under the caption, “New Accounting Pronouncements and Changes in Accounting Policy.”

FORWARD-LOOKING STATEMENTS

Certain statements in this report and in other materials filed with the SEC, as well as information included in oral statements or other written statements made by the Company, are forward-looking statements. The Company intends for all such forward-looking statements to be covered by the safe harbor provisions for forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 and the provisions of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. These forward-looking statements within the meaning of the Private Securities Litigation Reform Act may contain, among others, statements regarding:

projections and estimates of earnings, revenues, margins, volumes, rates, cost-savings, expenses, taxes or other financial items;

expectations as to results of operations and operational initiatives;

expectations as to the effect of claims, lawsuits, environmental costs, commitments, contingent liabilities, labor negotiations or agreements on the Company's financial condition, results of operations or liquidity;

management's plans, strategies and objectives for future operations, capital expenditures, dividends, share

repurchases, safety and service performance, proposed new services and other matters that are not historical facts, and management's expectations as to future performance and operations and the time by which objectives will be achieved; and

future economic, industry or market conditions or performance and their effect on the Company's financial condition, results of operations or liquidity.

Forward-looking statements are typically identified by words or phrases such as "will," "should," "believe," "expect," "anticipate," "project," "estimate," "preliminary" and similar expressions. The Company cautions against placing undue reliance on forward-looking statements, which reflect its good faith beliefs with respect to future events and are based on information currently available to it as of the date the forward-looking statement is made. Forward-looking statements should not be read as a guarantee of future performance or results and will not necessarily be accurate indications of the timing when, or by which, such performance or results will be achieved.

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Forward-looking statements are subject to a number of risks and uncertainties and actual performance or results could differ materially from those anticipated by any forward-looking statements. The Company undertakes no obligation to update or revise any forward-looking statement. If the Company does update any forward-looking statement, no inference should be drawn that the Company will make additional updates with respect to that statement or any other forward-looking statements. The following important factors, in addition to those discussed in Part II, Item 1A (Risk Factors) and elsewhere in this report, may cause actual results to differ materially from those contemplated by any forward-looking statements:

- legislative, regulatory or legal developments involving transportation, including rail or intermodal transportation, the environment, hazardous materials, taxation, international trade and initiatives to further regulate the rail industry;

- the outcome of litigation, claims and other contingent liabilities, including, but not limited to, those related to fuel surcharge, environmental matters, taxes, shipper and rate claims subject to adjudication, personal injuries and occupational illnesses;

- changes in domestic or international economic, political or business conditions, including those affecting the transportation industry (such as the impact of industry competition, conditions, performance and consolidation) and the level of demand for products carried by CSXT;

- natural events such as severe weather conditions, including floods, fire, hurricanes and earthquakes, a pandemic crisis affecting the health of the Company's employees, its shippers or the consumers of goods, or other unforeseen disruptions of the Company's operations, systems, property or equipment;

- competition from other modes of freight transportation, such as trucking and competition and consolidation or financial distress within the transportation industry generally;

- the cost of compliance with laws and regulations that differ from expectations (including those associated with PTC implementation) as well as costs, penalties and operational and liquidity impacts associated with noncompliance with applicable laws or regulations;

- the impact of increased passenger activities in capacity-constrained areas, including potential effects of high speed rail initiatives, or regulatory changes affecting when CSXT can transport freight or service routes;

- unanticipated conditions in the financial markets that may affect timely access to capital markets and the cost of capital, as well as management's decisions regarding share repurchases;

- changes in fuel prices, surcharges for fuel and the availability of fuel;

- the impact of natural gas prices on coal-fired electricity generation;

- availability of insurance coverage at commercially reasonable rates or insufficient insurance coverage to cover claims or damages;

- the inherent business risks associated with safety and security, including the transportation of hazardous materials or a cybersecurity attack which would threaten the availability and vulnerability of information technology;

adverse economic or operational effects from actual or threatened war or terrorist activities and any governmental response;

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• labor and benefit costs and labor difficulties, including stoppages affecting either the Company's operations or customers' ability to deliver goods to the Company for shipment;

• the Company's success in implementing its strategic, financial and operational initiatives;

• changes in operating conditions and costs or commodity concentrations; and

• the inherent uncertainty associated with projecting economic and business conditions.

Other important assumptions and factors that could cause actual results to differ materially from those in the forward-looking statements are specified elsewhere in this report and in CSX's other SEC reports, which are accessible on the SEC's website at www.sec.gov and the Company's website at www.csx.com. The information on the CSX website is not part of this annual report on Form 10-K.

Item 7A. Quantitative and Qualitative Disclosures about Market Risk

CSX does not hold or issue derivative financial instruments for trading purposes. Historically, the Company has used derivative financial instruments to address market risk exposure to fluctuations in interest rates. As of December 2016, CSX does not have a material amount of floating rate debt obligations outstanding, and therefore fluctuations in the interest rate would not have a material impact on the Company's financial condition, results of operations or liquidity.

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Item 8. Financial Statements and Supplementary Data

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Item 8. Financial Statements and Supplementary Data

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Shareholders and Board of Directors of CSX Corporation

We have audited the accompanying consolidated balance sheets of CSX Corporation as of December 30, 2016 and December 25, 2015, and the related consolidated statements of income, comprehensive income, cash flows, and changes in shareholders' equity for each of the three fiscal years in the period ended December 30, 2016. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of CSX Corporation at December 30, 2016 and December 25, 2015, and the consolidated results of its operations and its cash flows for each of the three fiscal years in the period ended December 30, 2016, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), CSX Corporation's internal control over financial reporting as of December 30, 2016, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) and our report dated February 14, 2017 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP
Certified Public Accountants

Jacksonville, Florida
February 14, 2017

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CSX CORPORATION

PART II

Item 8. Financial Statements and Supplementary Data

CONSOLIDATED INCOME STATEMENTS

(Dollars in Millions, Except Per Share Amounts)

| | Fiscal Years | | |
|--|--------------|----------|----------|
| | 2016 | 2015 | 2014 |
| Revenue | \$11,069 | \$11,811 | \$12,669 |
| Expense | | | |
| Labor and Fringe | 3,159 | 3,290 | 3,377 |
| Materials, Supplies and Other | 2,069 | 2,336 | 2,484 |
| Fuel | 713 | 957 | 1,616 |
| Depreciation | 1,301 | 1,208 | 1,151 |
| Equipment and Other Rents | 438 | 436 | 428 |
| Total Expense | 7,680 | 8,227 | 9,056 |
| Operating Income | 3,389 | 3,584 | 3,613 |
| Interest Expense | (579) | (544) | (545) |
| Debt Repurchase Expense | (115) | — | (16) |
| Other Income (Expense) - Net (Note 10) | 46 | 98 | (8) |
| Earnings Before Income Taxes | 2,741 | 3,138 | 3,044 |
| Income Tax Expense (Note 11) | (1,027) | (1,170) | (1,117) |
| Net Earnings | \$1,714 | \$1,968 | \$1,927 |
| Per Common Share (Note 2) | | | |
| Net Earnings Per Share | | | |
| Basic | \$1.81 | \$2.00 | \$1.93 |
| Assuming Dilution | \$1.81 | \$2.00 | \$1.92 |
| Average Common Shares Outstanding (Millions) | | | |
| Basic | 947 | 983 | 1,001 |
| Assuming Dilution | 948 | 984 | 1,002 |
| Cash Dividends Paid Per Common Share | \$0.72 | \$0.70 | \$0.63 |

Certain prior year data has been reclassified to conform to the current presentation.
See accompanying Notes to Consolidated Financial Statements.

CSX CORPORATION

PART II

Item 8. Financial Statements and Supplementary Data

CONSOLIDATED COMPREHENSIVE INCOME STATEMENTS

(Dollars in Millions)

| | Fiscal Years | | |
|---|--------------|---------|---------|
| | 2016 | 2015 | 2014 |
| Net Earnings | \$1,714 | \$1,968 | \$1,927 |
| Other Comprehensive Income (Loss) - Net of Tax: | | | |
| Pension and Other Post-Employment Benefits | 21 | 10 | (149) |
| Other | 4 | (9) | 6 |
| Total Other Comprehensive Income (Loss) | 25 | 1 | (143) |
| Comprehensive Earnings (Note 14) | \$1,739 | \$1,969 | \$1,784 |

See accompanying Notes to Consolidated Financial Statements.

CSX CORPORATION

PART II

Item 8. Financial Statements and Supplementary Data

CONSOLIDATED BALANCE SHEETS

(Dollars in Millions)

| | December 2016 | December 2015 |
|---|------------------|------------------|
| ASSETS | | |
| Current Assets: | | |
| Cash and Cash Equivalents (Note 1) | \$ 603 | \$ 628 |
| Short-term Investments | 417 | 810 |
| Accounts Receivable - Net (Note 1) | 938 | 982 |
| Materials and Supplies | 407 | 350 |
| Other Current Assets | 122 | 70 |
| Total Current Assets | 2,487 | 2,840 |
| Properties | 43,227 | 41,574 |
| Accumulated Depreciation | (12,077) | (11,400) |
| Properties - Net (Note 6) | 31,150 | 30,174 |
| Investment in Conrail (Note 12) | 840 | 803 |
| Affiliates and Other Companies | 619 | 591 |
| Other Long-term Assets | 318 | 337 |
| Total Assets | \$ 35,414 | \$ 34,745 |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | |
| Current Liabilities: | | |
| Accounts Payable | \$ 806 | \$ 764 |
| Labor and Fringe Benefits Payable | 545 | 490 |
| Casualty, Environmental and Other Reserves (Note 5) | 115 | 131 |
| Current Maturities of Long-term Debt (Note 9) | 331 | 20 |
| Income and Other Taxes Payable | 129 | 108 |
| Other Current Liabilities | 114 | 439 |
| Total Current Liabilities | 2,040 | 1,952 |
| Casualty, Environmental and Other Reserves (Note 5) | 259 | 269 |
| Long-term Debt (Note 9) | 10,962 | 10,515 |
| Deferred Income Taxes - Net (Note 11) | 9,596 | 9,179 |
| Other Long-term Liabilities | 863 | 1,162 |
| Total Liabilities | 23,720 | 23,077 |
| Shareholders' Equity: | | |
| Common Stock, \$1 Par Value (Note 3) | 928 | 966 |
| Other Capital | 138 | 113 |
| Retained Earnings (Note 1) | 11,253 | 11,238 |
| Accumulated Other Comprehensive Loss (Note 14) | (640) | (665) |
| Noncontrolling Minority Interest | 15 | 16 |
| Total Shareholders' Equity | 11,694 | 11,668 |
| Total Liabilities and Shareholders' Equity | \$ 35,414 | \$ 34,745 |

Certain prior year data has been reclassified to conform to the current presentation.
See accompanying Notes to Consolidated Financial Statements.

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CSX CORPORATION

PART II

Item 8. Financial Statements and Supplementary Data

CONSOLIDATED CASH FLOW STATEMENTS

(Dollars in Millions)

| | Fiscal Years | | |
|---|--------------|----------|----------|
| | 2016 | 2015 | 2014 |
| OPERATING ACTIVITIES | | | |
| Net Earnings | \$1,714 | \$1,968 | \$1,927 |
| Adjustments to Reconcile Net Earnings to Net Cash Provided by Operating Activities: | | | |
| Depreciation | 1,301 | 1,208 | 1,151 |
| Deferred Income Taxes | 405 | 456 | 298 |
| Contributions to Qualified Pension Plans (Note 8) | (250) | — | — |
| Gain on Property Dispositions | (128) | (90) | (11) |
| Other Operating Activities | (70) | 22 | 14 |
| Changes in Operating Assets and Liabilities: | | | |
| Accounts Receivable | 84 | 149 | (119) |
| Other Current Assets | (113) | (84) | (26) |
| Accounts Payable | 40 | (79) | 1 |
| Income and Other Taxes Payable | 23 | (62) | 74 |
| Other Current Liabilities | 35 | (118) | 34 |
| Net Cash Provided by Operating Activities | 3,041 | 3,370 | 3,343 |
| INVESTING ACTIVITIES | | | |
| Property Additions | (2,398) | (2,562) | (2,449) |
| Purchase of Short-term Investments | (929) | (1,739) | (1,433) |
| Proceeds from Sales of Short-term Investments | 1,325 | 1,225 | 1,674 |
| Proceeds from Property Dispositions | 195 | 147 | 62 |
| Other Investing Activities | 9 | 37 | (37) |
| Net Cash Used in Investing Activities | (1,798) | (2,892) | (2,183) |
| FINANCING ACTIVITIES | | | |
| Long-term Debt Issued (Note 9) | 2,200 | 1,200 | 1,000 |
| Long-term Debt Repaid (Note 9) | (1,419) | (229) | (933) |
| Dividends Paid | (680) | (686) | (629) |
| Shares Repurchased | (1,056) | (804) | (517) |
| Other Financing Activities | (313) | — | (4) |
| Net Cash Used in Financing Activities | (1,268) | (519) | (1,083) |
| Net (Decrease) Increase in Cash and Cash Equivalents | (25) | (41) | 77 |
| CASH AND CASH EQUIVALENTS | | | |
| Cash and Cash Equivalents at Beginning of Period | 628 | 669 | 592 |
| Cash and Cash Equivalents at End of Period | \$603 | \$628 | \$669 |
| SUPPLEMENTAL CASH FLOW INFORMATION | | | |
| Interest Paid - Net of Amounts Capitalized | \$606 | \$566 | \$575 |
| Income Taxes Paid | \$580 | \$768 | \$741 |
| Seller Financed Assets | \$— | \$307 | \$— |

See accompanying Notes to Consolidated Financial Statements.

CSX CORPORATION

PART II

Item 8. Financial Statements and Supplementary Data

CONSOLIDATED STATEMENTS OF CHANGES

IN SHAREHOLDERS' EQUITY

(Dollars in Millions)

| | Common Shares Outstanding (Thousands) | Common Stock and Other Capital | Retained Earnings | Accumulated Other Comprehensive Income (Loss) ^(a) | Non- controlling Interest | Total Shareholders' Equity |
|--|--|--|----------------------|--|---------------------------------|----------------------------------|
| December 27, 2013 | 1,008,860 | \$ 1,070 | \$ 9,936 | \$ (523 |) \$ 21 | \$ 10,504 |
| Comprehensive Earnings: | | | | | | |
| Net Earnings | — | — | 1,927 | — | — | 1,927 |
| Other Comprehensive Loss (Note 14) | — | — | — | (143 |) — | (143 |
| Total Comprehensive Earnings | | | | | | 1,784 |
| Common stock dividends, \$0.63 per share | — | — | (629 |)— | — | (629 |
| Share Repurchases | (17,010 |) (17 |)(500 |)— | — | (517 |
| Bond Conversions | 134 | 1 | — | — | — | 1 |
| Other | (393 |) 30 | — | — | 3 | 33 |
| December 26, 2014 | 991,591 | 1,084 | 10,734 | (666 |) 24 | 11,176 |
| Comprehensive Earnings: | | | | | | |
| Net Earnings | — | — | 1,968 | — | — | 1,968 |
| Other Comprehensive Income (Note 14) | — | — | — | 1 | — | 1 |
| Total Comprehensive Earnings | | | | | | 1,969 |
| Common stock dividends, \$0.70 per share | — | — | (686 |)— | — | (686 |
| Share Repurchases | (26,359 |) (26 |)(778 |)— | — | (804 |
| Bond Conversions | 13 | — | — | — | — | — |
| Other | 269 | 21 | — | — | (8 |) 13 |
| December 25, 2015 | 965,514 | 1,079 | 11,238 | (665 |) 16 | 11,668 |
| Comprehensive Earnings: | | | | | | |
| Net Earnings | — | — | 1,714 | — | — | 1,714 |
| Other Comprehensive Income (Note 14) | — | — | — | 25 | — | 25 |
| Total Comprehensive Earnings | | | | | | 1,739 |
| Common stock dividends, \$0.72 per share | — | — | (680 |)— | — | (680 |
| Share Repurchases | (38,379 |) (38 |)(1,018 |)— | — | (1,056 |
| Bond Conversions | 94 | 1 | — | — | — | 1 |
| Other | 951 | 24 | (1 |)— | (1 |) 22 |
| December 30, 2016 | 928,180 | \$ 1,066 | \$ 11,253 | \$ (640 |) \$ 15 | \$ 11,694 |

(a) Accumulated Other Comprehensive Loss year-end balances shown above are net of tax. The associated taxes were \$354 million, \$347 million and \$335 million for 2014, 2015 and 2016, respectively. For additional information see Note 14, Other Comprehensive Income.

See accompanying Notes to Consolidated Financial Statements.

CSX CORPORATION

PART II

Item 8. Financial Statements and Supplementary Data

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1. Nature of Operations and Significant Accounting Policies

Business

CSX Corporation (“CSX”), together with its subsidiaries (the “Company”), based in Jacksonville, Florida, is one of the nation's leading transportation companies. The Company provides rail-based transportation services including traditional rail service and the transport of intermodal containers and trailers.

The Company's number of employees was approximately 27,000 as of December 2016, which includes approximately 22,000 union employees. Most of the Company's employees provide or support transportation services.

CSX Transportation, Inc.

CSX's principal operating subsidiary, CSX Transportation, Inc. (“CSXT”), provides an important link to the transportation supply chain through its approximately 21,000 route mile rail network, which serves major population centers in 23 states east of the Mississippi River, the District of Columbia and the Canadian provinces of Ontario and Quebec. It has access to over 70 ocean, river and lake port terminals along the Atlantic and Gulf Coasts, the Mississippi River, the Great Lakes and the St. Lawrence Seaway. The Company's intermodal business links customers to railroads via trucks and terminals. CSXT also serves thousands of production and distribution facilities through track connections to approximately 240 short-line and regional railroads.

Lines of Business

During 2016, the Company services generated \$11.1 billion of revenue and served three primary lines of business:

The merchandise business shipped 2.8 million carloads and generated 64% of revenue and 43% of volume in 2016.

The Company's merchandise business is comprised of shipments in the following diverse markets: agricultural and food products, fertilizers, chemicals, automotive, metals and equipment, minerals and forest products.

The coal business shipped about 838 thousand carloads and accounted for 17% of revenue and 13% of volume in 2016. The Company transports domestic coal, coke and iron ore to electricity-generating power plants, steel manufacturers and industrial plants as well as export coal to deep-water port facilities. Roughly one-third of export coal and the majority of the domestic coal that the Company transports is used for generating electricity.

The intermodal business accounted for 16% of revenue and 44% of volume in 2016. The intermodal business combines the superior economics of rail transportation with the short-haul flexibility of trucks and offers a cost advantage over long-haul trucking. Through a network of more than 50 terminals, the intermodal business serves all major markets east of the Mississippi River and transports mainly manufactured consumer goods in containers, providing customers with truck-like service for longer shipments.

Other revenue accounted for 3% of the Company's total revenue in 2016. This revenue category includes revenue from regional subsidiary railroads, demurrage, revenue for customer volume commitments not met, switching, other incidental charges and adjustments to revenue reserves. Revenue from regional railroads includes shipments by railroads that the Company does not directly operate. Demurrage represents charges assessed when freight cars are held beyond a specified period of time. Switching revenue is primarily generated when CSXT switches cars for a customer or another railroad.

CSX CORPORATION

PART II

Item 8. Financial Statements and Supplementary Data

NOTE 1. Nature of Operations and Significant Accounting Policies, continued

Other Entities

In addition to CSXT, the Company's subsidiaries include CSX Intermodal Terminals, Inc. ("CSX Intermodal Terminals"), Total Distribution Services, Inc. ("TDSI"), Transflo Terminal Services, Inc. ("Transflo"), CSX Technology, Inc. ("CSX Technology") and other subsidiaries. CSX Intermodal Terminals owns and operates a system of intermodal terminals, predominantly in the eastern United States and also performs drayage services (the pickup and delivery of intermodal shipments) for certain customers and trucking dispatch operations. TDSI serves the automotive industry with distribution centers and storage locations. Transflo connects non-rail served customers to the many benefits of rail by transferring products from rail to trucks. The biggest Transflo markets are chemicals and agriculture, which includes shipments of plastics and ethanol. CSX Technology and other subsidiaries provide support services for the Company.

CSX's other holdings include CSX Real Property, Inc., a subsidiary responsible for the Company's operating and non-operating real estate sales, leasing, acquisition and management and development activities. These activities are classified in either operating income or other income - net depending upon the nature of the activity. Results of these activities fluctuate with the timing of real estate transactions.

Basis of Presentation

In the opinion of management, the accompanying consolidated financial statements contain all normal, recurring adjustments necessary to fairly present the financial position of CSX and its subsidiaries at December 30, 2016 and December 25, 2015, and the consolidated statements of income, comprehensive income, cash flows and changes in shareholders' equity for fiscal years 2016, 2015 and 2014. In addition, management has evaluated and disclosed all material events occurring subsequent to the date of the financial statements up to the date this annual report is filed on Form 10-K.

Fiscal Year

CSX follows a 52/53 week fiscal reporting calendar. This fiscal calendar allows every quarter to consistently end on a Friday and typically, to be of equal duration (13 weeks), resulting in a 52 week fiscal year. To maintain this type of reporting calendar every fifth or sixth year (depending on the Gregorian calendar and when leap year falls), an extra week will be included in the fourth quarter (a 14-week fiscal quarter) and, therefore, that full fiscal year will have 53 weeks. Fiscal fourth quarter 2016 included an extra week, so the quarter consisted of 14 weeks and fiscal year 2016 consisted of 53 weeks ending on December 30, 2016. Fiscal years 2015 and 2014 each consisted of 52 weeks ending on December 25, 2015 and December 26, 2014, respectively. Except as otherwise specified, references to full years indicate CSX's fiscal periods ended on these dates.

Principles of Consolidation

The consolidated financial statements include results of operations of CSX and subsidiaries over which CSX has majority ownership or financial control. All significant intercompany accounts and transactions have been eliminated. Most investments in companies that were not majority-owned were carried at cost (if less than 20% owned and the Company has no significant influence) or were accounted for under the equity method (if the Company has significant influence but does not have control). These investments are reported within Investment in Conrail or Affiliates and Other Companies on the consolidated balance sheets.

Cash and Cash Equivalents

On a daily basis, cash in excess of current operating requirements is invested in various highly liquid investments having a typical maturity date of three months or less at the date of acquisition. These investments are carried at cost, which approximated market value, and are classified as cash equivalents.

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CSX CORPORATION

PART II

Item 8. Financial Statements and Supplementary Data

NOTE 1. Nature of Operations and Significant Accounting Policies, continued

Investments

Investments in instruments with original maturities greater than three months that will mature in less than one year are classified as short-term investments. Investments with original maturities of one year or greater are classified within other long-term assets.

Allowance for Doubtful Accounts

The Company maintains an allowance for doubtful accounts on uncollectible amounts related to freight receivables, government reimbursement receivables, claims for damages and other various receivables. The allowance is based upon the creditworthiness of customers, historical experience, the age of the receivable and current market and economic conditions. Uncollectible amounts are charged against the allowance account. Allowance for doubtful accounts of \$33 million and \$37 million is included in the consolidated balance sheets as of December 2016 and December 2015, respectively.

Materials and Supplies

Materials and supplies in the consolidated balance sheets are carried at average costs and consist primarily of fuel and parts used in the repair and maintenance of CSXT's freight car and locomotive fleets, equipment and track structure.

Goodwill

Goodwill represents purchase price in excess of fair value and is related to affiliates of CSXT, primarily P&L Transportation, Inc. Goodwill of \$63 million is recorded in other long-term assets in the consolidated balance sheets as of December 2016 and December 2015, respectively.

Revenue and Expense Recognition

The Company recognizes freight revenue using Free-On-Board Origin pursuant to the Revenue Recognition Topic in the Accounting Standards Codification ("ASC"). Accounting guidance in this topic provides for the allocation of revenue between reporting periods based on relative transit time in each reporting period. Expenses are recognized as incurred.

The certain key estimates included in the recognition and measurement of revenue and related accounts receivable under the policies described above are as follows:

- revenue associated with shipments in transit is recognized ratably over transit time and is based on average cycle times to move commodities and products from their origin to their final destination or interchange;
- adjustments to revenue for billing corrections, billing discounts and bad debts or to accounts receivable for allowances for doubtful accounts;
- adjustments to revenue for overcharge claims filed by customers, which are based on historical cash paid to customers for rate overcharges as a percentage of total billing;
- incentive-based refunds to customers, which are primarily based on customers achieving certain volume thresholds, are recorded as a reduction to revenue on the basis of management's best estimate of the projected liability (this estimate is based on historical activity, current volume levels and forecasted future volume).

CSX CORPORATION

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Item 8. Financial Statements and Supplementary Data

NOTE 1. Nature of Operations and Significant Accounting Policies, continued

The Company regularly updates the estimates described above based on historical experience and current conditions. All other revenue, such as demurrage, switching and other incidental charges are recorded upon completion of the service.

New Accounting Pronouncements

In March 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU"), Improvements to Employee Share-based Payment Accounting, which requires excess tax benefits and deficiencies to be recorded as income tax expense or benefit in the income statement rather than being recorded in additional paid-in capital. The Company adopted the provisions of this ASU during the second quarter of 2016 which did not have a material effect on the Company's financial condition, results of operations or liquidity.

In November 2015, the FASB issued ASU, Balance Sheet Classification of Deferred Taxes, which requires that all deferred income taxes be classified as noncurrent in the balance sheet, rather than being separated into current and noncurrent amounts. The Company adopted the provisions of this ASU during second quarter 2016 and applied them retrospectively. Current deferred income tax assets of \$126 million as of December 25, 2015 have been reclassified and reported as a reduction of deferred income tax liabilities on the consolidated balance sheet. Adoption did not have a material effect on the Company's financial condition, results of operations or liquidity

In May 2014, the FASB issued ASU, Revenue from Contracts with Customers, which supersedes previous revenue recognition guidance. The new standard requires that a company recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration the company expects to receive in exchange for those goods or services. Companies will need to use more judgment and estimates than under the guidance currently in effect, including estimating the amount of variable revenue to recognize over each identified performance obligation. Additional disclosures will be required to help users of financial statements understand the nature, amount and timing of revenue and cash flows arising from contracts. This standard will become effective for CSX beginning with the first quarter 2018 and can be adopted either retrospectively to each prior reporting period presented or as a cumulative effect adjustment as of the date of adoption.

The FASB has recently issued several amendments to the revenue standard, including clarification on accounting for principal versus agent considerations (i.e., reporting gross versus net), licenses of intellectual property and identifying performance obligations. These amendments do not change the core principle of the standard, but provide clarity and implementation guidance.

The Company is currently finalizing its review of the impact of adopting this new guidance and developing a comprehensive implementation plan. In-depth reviews of a significant portion of commercial contracts have been completed and changes to processes and internal controls have been identified to meet the standard's reporting and disclosure requirements. At this time, the Company does not believe this standard will have a material effect on the Company's financial condition, results of operations or liquidity.

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Item 8. Financial Statements and Supplementary Data

NOTE 1. Nature of Operations and Significant Accounting Policies, continued

In February 2016, the FASB issued ASU, Leases, which will require lessees to recognize most leases on their balance sheets as a right-of-use asset with a corresponding lease liability, and lessors to recognize a net lease investment. Additional qualitative and quantitative disclosures will also be required. This standard will become effective for CSX beginning with the first quarter 2019 and will be adopted using a modified retrospective method. Changes to processes and internal controls to meet the standard's reporting and disclosure requirements have been identified and are being implemented. For example, software has been implemented that will assist in recognition of additional assets and liabilities to be included on the balance sheet related to operating leases with durations greater than twelve months, with certain allowable exceptions. The Company continues to evaluate the expected financial impact of this standard update.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires that management make estimates in reporting the amounts of certain assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amount of certain revenues and expenses during the reporting period. Actual results may differ from those estimates. Critical accounting estimates using management judgment are made for the following areas:

- casualty, environmental and legal reserves (see Note 5, Casualty, Environmental and Other Reserves);
- pension and post-retirement medical plan accounting (see Note 8, Employee Benefit Plans);
- depreciation policies for assets under the group-life method (see Note 6, Properties); and
- income taxes (see Note 11, Income Taxes).

Other Items

Share Repurchases

In April 2015, the Company announced a \$2 billion share repurchase program, which is expected to be completed by April 2017. Management's assessment of market conditions and other factors guide the timing and volume of repurchases. Future share repurchases are expected to be funded by cash on hand, cash generated from operations and debt issuances. During 2016, 2015 and 2014, CSX repurchased \$1.1 billion, or 38 million shares, \$804 million or 26 million shares, and \$517 million, or 17 million shares, respectively, of common stock. Shares are retired immediately upon repurchase. In accordance with the Equity Topic in the ASC, the Company elected to allocate the excess of repurchase price over par value and record in retained earnings. Generally, retained earnings is only impacted by net earnings and dividends.

Workforce Reduction Plans, Separation & Other Costs

Union agreements, facility closures and management streamlining under workforce reduction plans resulted in payment of separation benefits to employees of \$51 million and \$39 million in 2015 and 2014, respectively. These amounts are recognized in labor and fringe and materials, supplies and other on the consolidated statements of income. Separation benefits incurred in 2016 related to workforce reduction plans were not material.

CSX CORPORATION

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Item 8. Financial Statements and Supplementary Data

NOTE 1. Nature of Operations and Significant Accounting Policies, continued

Union agreements

In November 2015, CSX finalized a union agreement that will improve efficiency across the CSX network. This agreement allowed certain employees impacted by work transitions to voluntarily separate from the Company with enhanced benefits and provided relocation benefits to employees not electing to separate. As a result, approximately 300 union employees were impacted. Separation benefits were paid from general corporate funds.

Facility closures

In October 2015, CSX closed facilities in Erwin, Tennessee and Corbin, Kentucky as a result of the decline in coal movements in these regions. These closures impacted approximately 500 positions. The Company recorded a charge resulting from separation, relocation and furlough costs, as well as asset impairment charges related to the facility closures. Separation benefits were paid from general corporate funds.

Management streamlining

In 2014, the Company announced a workforce reduction plan to streamline the organization. The initiative reduced management workforce by approximately 300 positions through a voluntary separation program with enhanced benefits as well as a subsequent involuntary severance program during the fourth quarter of 2014 and the first quarter of 2015. The majority of separation benefits were paid from CSX's qualified pension plans, while the remainder was paid from general corporate funds.

NOTE 2. Earnings Per Share

The following table sets forth the computation of basic earnings per share and earnings per share, assuming dilution:

| | Fiscal Years | | |
|--|--------------|---------|---------|
| | 2016 | 2015 | 2014 |
| Numerator (Dollars in Millions): | | | |
| Net Earnings | \$1,714 | \$1,968 | \$1,927 |
| Dividend Equivalents on Restricted Stock | (1) | (1) | (1) |
| Net Earnings, Attributable to Common Shareholders | \$1,713 | \$1,967 | \$1,926 |
| Denominator (Units in Millions): | | | |
| Average Common Shares Outstanding | 947 | 983 | 1,001 |
| Other Potentially Dilutive Common Shares | 1 | 1 | 1 |
| Average Common Shares Outstanding, Assuming Dilution | 948 | 984 | 1,002 |
| Net Earnings Per Share, Basic | \$1.81 | \$2.00 | \$1.93 |
| Net Earnings Per Share, Assuming Dilution | \$1.81 | \$2.00 | \$1.92 |

Basic earnings per share is based on the weighted-average number of shares of common stock outstanding. Earnings per share, assuming dilution, is based on the weighted-average number of shares of common stock equivalents outstanding adjusted for the effects of common stock that may be issued as a result of potentially dilutive instruments. CSX's potentially dilutive instruments are made up of equity awards, which include long-term incentive awards and employee stock options.

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Item 8. Financial Statements and Supplementary Data

NOTE 2. Earnings Per Share, continued

The Earnings Per Share Topic in the ASC requires CSX to include additional shares in the computation of earnings per share, assuming dilution. The additional shares included in diluted earnings per share represent the number of shares that would be issued if all of the above potentially dilutive instruments were converted into CSX common stock.

When calculating diluted earnings per share, CSX is required to include the potential shares that would be outstanding if all outstanding stock options were exercised. This number is different from outstanding stock options, which is included in Note 4, Stock Plans and Share-Based Compensation, because it is offset by shares CSX could repurchase using the proceeds from these hypothetical exercises to obtain the common stock equivalent. Approximately 2.8 million and 2.5 million of total average outstanding stock options for 2016 and 2015, respectively, were excluded from the diluted earnings per share calculation because their effect was antidilutive. There were no stock options outstanding for 2014.

NOTE 3. Shareholders' Equity

Common and preferred stock consists of the following:

| | |
|---|--|
| Common Stock, \$1 Par Value | December 2016 (Units in Millions) |
| Common Shares Authorized | 1,800 |
| Common Shares Issued and Outstanding | 928 |
| Preferred Stock | |
| Preferred Shares Authorized | 25 |
| Preferred Shares Issued and Outstanding | — |

Holders of common stock are entitled to one vote on all matters requiring a vote for each share held. Preferred stock is senior to common stock with respect to dividends and upon liquidation of CSX.

CSX CORPORATION

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Item 8. Financial Statements and Supplementary Data

NOTE 4. Stock Plans and Share-Based Compensation

Under CSX's share-based compensation plans, awards consist of performance units, restricted stock units, restricted stock awards and stock options for management and stock grants for directors. Awards granted under the various programs are determined and approved by the Compensation Committee of the Board of Directors or, in certain circumstances, by the Chief Executive Officer for awards to management employees other than senior executives. The Board of Directors approves awards granted to the Company's non-management directors upon recommendation of the Governance Committee.

Share-based compensation expense is measured at fair value of the Company's stock on the grant date and is recognized on a straight-line basis over the service period of the respective award. Forfeitures are recognized as they occur. Total pre-tax expense associated with share-based compensation and its related income tax benefit is shown in the table below.

| (Dollars in Millions) | Fiscal Years | | |
|--|--------------|-------|------|
| | 2016 | 2015 | 2014 |
| Share-Based Compensation Expense | | | |
| Performance Units | \$17 | \$(1) | \$20 |
| Restricted Stock Units and Awards | 11 | 11 | 11 |
| Stock Options | 7 | — | — |
| Stock Awards for Directors | 2 | 2 | 2 |
| Total Share-based Compensation Expense | \$37 | \$12 | \$33 |
| Income Tax Benefit | \$14 | \$4 | \$13 |

Long-term Incentive Plans

The CSX Long-term Incentive Plans ("LTIP") were adopted under the 2010 CSX Stock and Incentive Award Plan. The objective of these plans is to motivate and reward certain employees for achieving and exceeding certain financial and strategic initiatives. Grants were made in performance units, with each unit being equivalent to one share of CSX common stock, and payouts will be made in CSX common stock. The payout range for participants will be between 0% and 200% of the target awards depending on Company performance against predetermined goals for each three-year cycle. In 2014, 2015 and 2016, target performance units were granted to certain employees under three separate LTIP plans covering three-year cycles: the 2014-2016 ("2014-2016 LTIP"), 2015-2017 ("2015-2017 LTIP") and 2016-2018 ("2016-2018 LTIP") plans (collectively, the "plans").

The key financial targets for the plans will be based on the achievement of goals related to both operating ratio and return on assets (tax-adjusted operating income divided by net property) excluding non-recurring items as disclosed in the Company's financial statements. The three-year cumulative operating ratio and average return on assets over the performance period will each comprise 50% of the payout and are measured independently of the other. The plans state that payouts for certain executive officers are subject to downward adjustment by up to 30% based upon total shareholder return relative to specified comparable groups.

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Item 8. Financial Statements and Supplementary Data

NOTE 4. Stock Plans and Share-Based Compensation, continued

Performance unit grant and vesting information is summarized as follows:

| | Fiscal Years | | |
|--|--------------|---------|---------|
| | 2016 | 2015 | 2014 |
| Weighted-average grant date fair value | \$24.17 | \$35.45 | \$28.13 |
| Fair value of units vested in fiscal year ending (in millions) | \$31 | \$34 | \$— |

The performance unit activity related to the outstanding long-term incentive plans and corresponding fair value is summarized as follows:

| | Performance | |
|-------------------------------|----------------------------------|---|
| | Units Outstanding (in Thousands) | Weighted-Average Fair Value at Grant Date |
| Unvested at December 25, 2015 | 1,941 | \$ 31.73 |
| Granted | 852 | 24.17 |
| Forfeited | (118) | 29.22 |
| Vested | (1,094) | 28.60 |
| Unvested at December 30, 2016 | 1,581 | \$ 30.00 |

As of December 2016, there was \$18 million of total unrecognized compensation cost related to performance units that is expected to be recognized over a weighted-average period of approximately two years.

Restricted Stock Grants

Restricted stock grants consist of units and awards, each equivalent to one share of CSX stock. Restricted stock units are issued along with corresponding LTIP plans and vest three years after the date of grant. Separately, restricted stock awards generally vest over an employment period of up to five years. Participants receive cash dividend equivalents on the unvested shares during the restriction period. These awards are time-based and not based upon CSX's attainment of operational targets.

Restricted stock grant and vesting information is summarized as follows:

| | Fiscal Years | | |
|--|--------------|---------|---------|
| | 2016 | 2015 | 2014 |
| Weighted-average grant date fair value | \$24.21 | \$35.94 | \$28.08 |
| Fair value of units and awards vested during fiscal year ended (in millions) | \$14 | \$9 | \$11 |

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Item 8. Financial Statements and Supplementary Data

NOTE 4. Stock Plans and Share-Based Compensation, continued

The restricted stock activity related to the outstanding long-term incentive plans and corresponding fair value is summarized as follows:

| | Restricted Stock Units and Awards Outstanding (in Thousands) | Weighted-Average Fair Value at Grant Date |
|-------------------------------|---|---|
| Unvested at December 25, 2015 | 1,157 | \$ 28.66 |
| Granted | 509 | 24.21 |
| Forfeited | (52) | 28.19 |
| Vested | (538) | 25.44 |
| Unvested at December 30, 2016 | 1,076 | \$ 28.19 |

As of December 2016, unrecognized compensation expense for these restricted stock units and awards was approximately \$13 million, which will be expensed over a weighted-average remaining period of two years.

Stock Options

Stock options were granted in 2016 along with the corresponding LTIP plan and in 2015 to certain members of management. No stock options were granted in 2014. Under this program, an employee receives an award that provides the opportunity in the future to purchase CSX shares at the closing market price of the stock on the date the award is granted (the strike price). The options become exercisable after a three-year vesting period and expire 10 years from the grant date if they are not exercised.

The fair value of stock options granted was estimated as of the dates of grant using the Black-Scholes-Merton option model which uses the following assumptions: dividend yield, risk-free interest rate, annualized volatility and expected life. The annual dividend yield is based on the most recent quarterly CSX dividend payment annualized. The risk-free interest rate is based on U.S. Treasury yield curve in effect at the time of grant. The annualized volatility is based on historical volatility of daily CSX stock price returns over a 6.5year look-back period ending on the grant date. The expected life is calculated using the safe harbor approach due to lack of historical data on CSX options, which is the midpoint between the vesting schedule (three year cliff) and contractual term (10 years).

CSX CORPORATION

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Item 8. Financial Statements and Supplementary Data

NOTE 4. Stock Plans and Share-Based Compensation, continued

Assumptions and inputs used to estimate fair value of stock options are summarized as follows:

| | Fiscal Years | | |
|--|--------------|---------|---|
| | 2016 | 2015 | |
| Weighted-average grant date fair value | \$4.68 | \$5.31 | |
| Stock options valuation assumptions: | | | |
| Annual dividend yield | 3 | % 3 | % |
| Risk-free interest rate | 1 | % 2 | % |
| Annualized volatility | 27 | % 28 | % |
| Expected life (in years) | 6.5 | 6.5 | |
| Other pricing model inputs: | | | |
| Weighted-average grant-date market price of CSX stock (strike price) | \$24.13 | \$24.99 | |

The stock option activity is summarized as follows:

| | Stock Options Outstanding (in Thousands) | Weighted-Average Exercise Price |
|----------------------------------|--|------------------------------------|
| Outstanding at December 25, 2015 | 2,514 | \$ 24.99 |
| Granted | 2,383 | 24.13 |
| Forfeited | (316) | 24.63 |
| Outstanding | 4,582 | \$ 24.57 |
| Exercisable at December 30, 2016 | — | — |

Unrecognized compensation expense related to stock options as of December 2016 was \$15 million and is expected to be recognized over a weighted-average period of approximately two years.

The terms of performance units, restricted stock units and stock options all require participants to be employed through the final day of the respective performance or vesting periods as applicable, except in the case of death, disability or retirement.

Stock Awards for Directors

CSX's non-management directors receive a base annual retainer of \$90,000 to be paid quarterly in cash, unless the director chooses to receive the retainer in the form of CSX common stock. Additionally, non-management directors receive an annual grant of common stock in the amount of approximately \$150,000, with the number of shares to be granted based on the average closing price of CSX stock in the months of November, December and January.

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Item 8. Financial Statements and Supplementary Data

NOTE 5. Casualty, Environmental and Other Reserves

Activity related to casualty, environmental and other reserves is as follows:

| | Casualty | Environmental | Other | Total |
|-----------------------------------|----------|---------------|----------|--------|
| (Dollars in Millions) | Reserves | Reserves | Reserves | |
| December 27, 2013 | \$ 280 | \$ 100 | \$ 71 | \$451 |
| Charged to Expense ^(a) | 89 | 57 | 30 | 176 |
| Payments | (104) | (63) | (42) | (209) |
| December 26, 2014 | 265 | 94 | 59 | 418 |
| Charged to Expense | 60 | 45 | 37 | 142 |
| Payments | (56) | (57) | (47) | (160) |
| December 25, 2015 | 269 | 82 | 49 | 400 |
| Charged to Expense | 52 | 46 | 30 | 128 |
| Change in Estimate ^(b) | (28) | — | — | (28) |
| Payments | (64) | (33) | (29) | (126) |
| December 30, 2016 | \$ 229 | \$ 95 | \$ 50 | \$374 |

^(a) Casualty expense in 2014 was higher due to the resolution of personal injury claims for prior years.

^(b) Changes in estimates are the result of continued safety improvements and a continuing decline in the severity of injuries.

These reserves are considered critical accounting estimates due to the need for significant management judgment. They are provided for in the consolidated balance sheets as shown in the table below.

| | December 2016 | | | December 2015 | | |
|-----------------------------|---------------|-----------|-------|---------------|-----------|-------|
| (Dollars in Millions) | Current | long-term | Total | Current | long-term | Total |
| Casualty: | | | | | | |
| Personal Injury | \$46 | \$ 124 | \$170 | \$57 | \$ 147 | \$204 |
| Occupational ^(a) | 7 | 52 | 59 | 12 | 53 | 65 |
| Total Casualty | \$53 | \$ 176 | \$229 | \$69 | \$ 200 | \$269 |
| Environmental | 42 | 53 | 95 | 42 | 40 | 82 |
| Other | 20 | 30 | 50 | 20 | 29 | 49 |
| Total | \$115 | \$ 259 | \$374 | \$131 | \$ 269 | \$400 |

^(a) Occupational reserves include asbestos-related diseases and occupational injuries.

These liabilities are accrued when reasonably estimable and probable in accordance with the Contingencies Topic in the ASC. Actual settlements and claims received could differ and final outcomes of these matters cannot be predicted with certainty. Considering the legal defenses currently available, the liabilities that have been recorded and other factors, it is the opinion of management that none of these items individually, when finally resolved, will have a material adverse effect on the Company's financial condition, results of operations or liquidity. Should a number of these items occur in the same period, however, their combined effect could be material in that particular period.

CSX CORPORATION

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Item 8. Financial Statements and Supplementary Data

NOTE 5. Casualty, Environmental and Other Reserves, continued

Casualty

Casualty reserves of \$229 million and \$269 million for 2016 and 2015, respectively, represent accruals for personal injury, occupational disease and occupational injury claims. The Company's self-insured retention amount for these claims is \$50 million per occurrence. Currently, no individual claim is expected to exceed the self-insured retention amount. In accordance with the Contingencies Topic in the ASC, to the extent the value of an individual claim exceeds the self-insured retention amount, the Company would present the liability on a gross basis with a corresponding receivable for insurance recoveries. These reserves fluctuate based upon the timing of payments as well as changes in estimate. Actual results may vary from estimates due to the number, type and severity of the injury, costs of medical treatments and uncertainties in litigation. Most of the Company's casualty claims relate to CSXT unless otherwise noted below. Defense and processing costs, which historically have been insignificant and are anticipated to be insignificant in the future, are not included in the recorded liabilities.

Personal Injury

Personal injury reserves represent liabilities for employee work-related and third-party injuries. Work-related injuries for CSXT employees are primarily subject to the Federal Employers' Liability Act ("FELA"). In addition to FELA liabilities, employees of other current or former CSX subsidiaries are covered by various state workers' compensation laws, the Federal Longshore and Harbor Workers' Compensation Program or the Maritime Jones Act.

CSXT retains an independent actuary to assist management in assessing the value of personal injury claims. An analysis is performed by the actuary quarterly and is reviewed by management. The methodology used by the actuary includes a development factor to reflect growth or reduction in the value of these personal injury claims. It is based largely on CSXT's historical claims and settlement experience.

As a direct result of improvements in safety in recent years, the Company has experienced a downward trend in the severity of injuries, which has resulted in a decrease in the estimate of costs per incident. During 2016, the Company reduced casualty reserves, primarily personal injury reserves, by \$28 million, resulting in an after-tax effect on earnings from continuing operations and net earnings of \$18 million and an after-tax effect on earnings per share of \$0.02. The personal injury reserve reductions were included in materials, supplies and other on the consolidated income statements. During 2015 and 2014, there were no significant changes in estimate recorded to adjust casualty reserves.

Occupational

Occupational reserves represent liabilities for occupational disease and injury claims. Occupational disease claims arise primarily from allegations of exposure to asbestos in the workplace. Occupational injury claims arise from allegations of exposure to certain other materials in the workplace, such as solvents, soaps, chemicals (collectively referred to as "irritants") and diesel fuels (like exhaust fumes) or allegations of chronic physical injuries resulting from work conditions, such as repetitive stress injuries.

The greatest possible exposure to asbestos for employees resulted from work conducted in and around steam locomotive engines that were largely phased out beginning around the 1950s. Other types of exposures, however, including exposure from locomotive component parts and building materials, continued until these exposures were substantially eliminated by 1985. Diseases associated with asbestos typically have long latency periods (amount of time between exposure to asbestos and the onset of the disease) which can range from 10 to 40 years after exposure.

CSX CORPORATION

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Item 8. Financial Statements and Supplementary Data

NOTE 5. Casualty, Environmental and Other Reserves, continued

Management reviews asserted asbestos claims quarterly. Unasserted or incurred but not reported ("IBNR") asbestos claims are analyzed by a third-party specialist and reviewed by management annually.

CSXT's historical claim filings, settlement amounts, and dismissal rates are analyzed to determine future anticipated claim filing rates and average settlement values for asbestos claims reserves. The potentially exposed population is estimated by using CSXT's employment records and industry data. From this analysis, the specialist estimates the IBNR claims liabilities.

Environmental

Environmental reserves were \$95 million and \$82 million for 2016 and 2015, respectively. The Company is a party to various proceedings related to environmental issues, including administrative and judicial proceedings involving private parties and regulatory agencies. The Company has been identified as a potentially responsible party at approximately 222 environmentally impaired sites. Many of these are, or may be, subject to remedial action under the federal Comprehensive Environmental Response, Compensation and Liability Act of 1980 ("CERCLA"), also known as the Superfund Law, or similar state statutes. Most of these proceedings arose from environmental conditions on properties used for ongoing or discontinued railroad operations. A number of these proceedings, however, are based on allegations that the Company, or its predecessors, sent hazardous substances to facilities owned or operated by others for treatment, recycling or disposal. In addition, some of the Company's land holdings were leased to others for commercial or industrial uses that may have resulted in releases of hazardous substances or other regulated materials onto the property and could give rise to proceedings against the Company.

In any such proceedings, the Company is subject to environmental clean-up and enforcement actions under the Superfund Law, as well as similar state laws that may impose joint and several liability for clean-up and enforcement costs on current and former owners and operators of a site without regard to fault or the legality of the original conduct. These costs could be substantial.

In accordance with the Asset Retirement and Environmental Obligations Topic in the ASC, the Company reviews its role with respect to each site identified at least quarterly, giving consideration to a number of factors such as:

- type of clean-up required;
- nature of the Company's alleged connection to the location (e.g., generator of waste sent to the site or owner or operator of the site);
- extent of the Company's alleged connection (e.g., volume of waste sent to the location and other relevant factors); and
- number, connection and financial viability of other named and unnamed potentially responsible parties at the location.

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Item 8. Financial Statements and Supplementary Data

NOTE 5. Casualty, Environmental and Other Reserves, continued

Based on the review process, the Company has recorded amounts to cover contingent anticipated future environmental remediation costs with respect to each site to the extent such costs are reasonably estimable and probable. The recorded liabilities for estimated future environmental costs are undiscounted. The liability includes future costs for remediation and restoration of sites as well as any significant ongoing monitoring costs, but excludes any anticipated insurance recoveries. Payments related to these liabilities are expected to be made over the next several years. Environmental remediation costs are included in materials, supplies and other on the consolidated income statements.

Currently, the Company does not possess sufficient information to reasonably estimate the amounts of additional liabilities, if any, on some sites until completion of future environmental studies. In addition, conditions that are currently unknown could, at any given location, result in additional exposure, the amount and materiality of which cannot presently be reasonably estimated. Based upon information currently available, however, the Company believes its environmental reserves accurately reflect the estimated cost of remedial actions currently required.

Other

Other reserves of \$50 million and \$49 million for 2016 and 2015, respectively, include liabilities for various claims, such as property, automobile and general liability. Also included in other reserves are longshoremen disability claims related to a previously owned international shipping business (these claims are in runoff) as well as claims for current port employees.

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NOTE 6. Properties

A detail of the Company's net properties are as follows:

| (Dollars in Millions) | Accumulated | Net | Annual | Estimated | Depreciation | |
|--------------------------|-------------|--------------|----------|---------------|-----------------------|------------------------------|
| December 2016 | Cost | Depreciation | Book | Useful Life | Method ^(a) | |
| Road | | | Value | (Avg. Years) | | |
| Rail and Other Track | \$7,326 | \$ (1,493) | \$5,833 | 2.5% | 40 | Group Life |
| Material | | | | | | |
| Ties | 5,368 | (1,292) | 4,076 | 3.7% | 27 | Group Life |
| Grading | 2,600 | (514) | 2,086 | 1.4% | 90 | Group Life |
| Ballast | 2,897 | (860) | 2,037 | 2.7% | 37 | Group Life |
| Bridges, Trestles, and | | | | | | |
| Culverts | 2,306 | (317) | 1,989 | 1.6% | 70 | Group Life |
| Signals and | | | | | | |
| Interlockers | 2,523 | (496) | 2,027 | 4.0% | 25 | Group Life/ Straight Line |
| Buildings | 1,238 | (447) | 791 | 2.5% | 40 | Group Life |
| Other | 4,566 | (1,905) | 2,661 | 4.2% | 24 | Group Life |
| Total Road | 28,824 | (7,324) | 21,500 | | | |
| Equipment | | | | | | |
| Locomotive | 6,110 | (2,504) | 3,606 | 3.5% | 29 | Group Life |
| Freight Cars | 3,386 | (1,046) | 2,340 | 2.9% | 35 | Group Life |
| Work Equipment and | | | | | | |
| Other | 2,108 | (1,190) | 918 | 7.4% | 14 | Group Life/ Straight Line |
| Total Equipment | 11,604 | (4,740) | 6,864 | | | |
| Land | 1,833 | — | 1,833 | N/A | N/A | N/A |
| Construction In Progress | 913 | — | 913 | N/A | N/A | N/A |
| Other | 53 | (13) | 40 | N/A | 32 | Straight Line |
| Total Properties | \$43,227 | \$ (12,077) | \$31,150 | | | |

(a) For depreciation method, certain asset categories contain technology-related assets, which are depreciated using the straight-line method.

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NOTE 6. Properties, continued

| (Dollars in Millions) | Accumulated | Net | Annual | Estimated | Depreciation | |
|------------------------------------|-------------|--------------|----------|--------------|-----------------------|------------------------------|
| December 2015 | Cost | Depreciation | Book | Useful Life | Method ^(a) | |
| Road | | | Value | (Avg. Years) | | |
| Rail and Other Track | \$7,150 | \$ (1,414) | \$5,736 | 2.5% | 40 | Group Life |
| Material | | | | | | |
| Ties | 5,077 | (1,147) | 3,930 | 3.7% | 27 | Group Life |
| Grading | 2,533 | (479) | 2,054 | 1.4% | 90 | Group Life |
| Ballast | 2,793 | (802) | 1,991 | 2.7% | 37 | Group Life |
| Bridges, Trestles, and Culverts | 2,238 | (283) | 1,955 | 1.6% | 70 | Group Life |
| Signals and Interlockers | 2,315 | (416) | 1,899 | 4.0% | 25 | Group Life/ Straight Line |
| Buildings | 1,152 | (424) | 728 | 2.5% | 40 | Group Life |
| Other | 4,306 | (1,793) | 2,513 | 4.2% | 24 | Group Life |
| Total Road | 27,564 | (6,758) | 20,806 | | | |
| Equipment | | | | | | |
| Locomotive | 5,673 | (2,461) | 3,212 | 3.6% | 28 | Group Life |
| Freight Cars | 3,362 | (1,018) | 2,344 | 3.2% | 31 | Group Life |
| Work Equipment and Other | 2,073 | (1,154) | 919 | 7.1% | 13 | Group Life/ Straight Line |
| Total Equipment | 11,108 | (4,633) | 6,475 | | | |
| Land | 1,858 | — | 1,858 | N/A | N/A | N/A |
| Construction In Progress | 1,003 | — | 1,003 | N/A | N/A | N/A |
| Other | 41 | (9) | 32 | N/A | 32 | Straight Line |
| Total Properties | \$41,574 | \$ (11,400) | \$30,174 | | | |

(a) For depreciation method, certain asset categories contain technology-related assets, which are depreciated using the straight-line method.

Railroad Assets

The Company depreciates its railroad assets, including main-line track, locomotives and freight cars, using the group-life method of accounting. Assets depreciated under the group-life method of accounting comprise 86% of total fixed assets of \$43 billion on a gross basis as of December 2016. The remaining depreciable assets of the Company are depreciated on a straight-line basis. The group-life method aggregates assets with similar lives and characteristics into groups and depreciates each of these groups as a whole. When using the group-life method, an underlying assumption is that each group of assets, as a whole, is used and depreciated to the end of its recoverable life.

The Company currently utilizes more than 130 different depreciable asset categories to account for depreciation expense for the railroad assets that are depreciated under the group-life method of accounting. Examples of depreciable asset categories include 18 different categories for crossties due to the different combinations of density classifications and asset types. By utilizing various depreciable categories, the Company can more accurately account for the use of its assets. All assets of the Company are depreciated on a time or life basis.

CSX CORPORATION

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Item 8. Financial Statements and Supplementary Data

NOTE 6. Properties, continued

The Company believes the group-life method of depreciation closely approximates the straight-line method of depreciation. Additionally, due to the nature of most of its assets (e.g. track is one contiguous, connected asset) the Company believes that this is the most effective way to properly depreciate its assets.

Management performs a detailed review of depreciation expense and useful lives on a regular basis. Under the group-life method of accounting, the service lives and salvage values for each group of assets are determined by completing periodic depreciation studies and applying management's assumptions regarding the service lives of its properties. A depreciation study (also referred to as a life study) is the periodic review of asset service lives, salvage values, accumulated depreciation, and other related factors for group assets conducted by a third-party specialist, analyzed by the Company's management and approved by the STB, the regulatory board that has broad jurisdiction over railroad practices. The STB requires depreciation studies be performed for equipment assets generally every three years and for road (e.g. bridges and signals) and track (e.g. rail, ties and ballast) assets generally every six years. The Company believes the frequency currently required by the STB provides adequate review of asset service lives and that a more frequent review would not result in a material change due to the long-lived nature of most of the assets. In 2016, the Company completed a depreciation study for its equipment assets. In 2014, the Company completed a depreciation study for its road and track assets. The Company plans to complete the next depreciation study for equipment assets in 2019 and road and track assets in 2020.

The results of the depreciation study process determine the service lives for each asset group under the group-life method. Road assets, including main-line track, have estimated service lives ranging from eight years for system roadway machinery to 90 years for grading (construction of protection for the roadway, tracks and embankments). Equipment assets, including locomotives and freight cars, have estimated service lives ranging from four years for technology assets to 40 years for work equipment. Changes in asset service lives due to the results of the depreciation studies are applied on a prospective basis and could significantly impact future periods' depreciation expense, and thus, the Company's results of operations.

There are several factors taken into account during the depreciation study and they include:

- statistical analysis of historical life and salvage data for each group of property;
- statistical analysis of historical retirements for each group of property;
- evaluation of current operations;
- evaluation of technological advances and maintenance schedules;
- previous assessment of the condition of the assets;
- management's outlook on the future use of certain asset groups;
- expected net salvage to be received upon retirement; and
- comparison of assets to the same asset groups with other companies.

Recent experience with depreciation studies has resulted in depreciation rate changes that did not materially affect the Company's annual depreciation expense of \$1.3 billion, \$1.2 billion and \$1.2 billion for 2016, 2015 and 2014, respectively. In general, changes in depreciation rates result from updated average asset service lives as determined during depreciation studies.

CSX CORPORATION

PART II

Item 8. Financial Statements and Supplementary Data

NOTE 6. Properties, continued

For retirements or disposals of depreciable rail assets that occur in the ordinary course of business, the asset cost (net of salvage value or sales proceeds) is charged to accumulated depreciation and no gain or loss is recognized. As individual assets within a specific group are retired or disposed of, resulting gains and losses are recorded in accumulated depreciation. This practice is consistent with accounting treatment normally prescribed under the group-life method. As part of the depreciation study, an assessment of the recorded amount of accumulated depreciation is made to determine if it is deficient (or in excess) of the appropriate amount indicated by the study. Any such deficiency (or excess), including any deferred gains or losses, is amortized as a component of depreciation expense over the remaining service life of the asset group until the next required depreciation study. Since the overall assumption with the group-life method of accounting is that the assets within the group on average have the same service life and characteristics, it is therefore concluded that the deferred gains and losses offset over time.

Since the rail network is one contiguous, connected network it is impractical to maintain specific identification records for these assets. For road assets (such as rail and track related items), CSX utilizes a first-in, first-out approach to asset retirements. The historical cost of these replaced assets is estimated using inflation indices previously published by the Bureau of Labor Statistics, adjusted using Consumer Price Index inflationary figures, applied to the replacement value based on the age of the retired asset. The indices are used because they closely correlate with the major cost of the materials comprising the applicable road assets.

Equipment assets (such as locomotives and freight cars) are specifically identified at retirement. When an equipment asset is retired that has been depreciated using the group-life method, the cost is reduced from the cost base and recorded in accumulated depreciation.

In the event that large groups of assets are removed from service as a result of unusual acts or sales, resulting gains and losses are recognized immediately. These acts are not considered to be in the normal course of business and are therefore recognized when incurred. Examples of such acts would be the major destruction of assets due to significant storm damage (e.g. major hurricanes), the sale of a rail line segment or the disposal of an entire class of assets (e.g. disposal of all refrigerated freight cars). Abnormal operating gains were \$23 million in 2015 primarily related to the sale of an operating rail line segment. There were no abnormal operating gains or losses in 2016 or 2014.

CSX CORPORATION

PART II

Item 8. Financial Statements and Supplementary Data

NOTE 6. Properties, continued

Non-Railroad Assets, Capital Leases and Land

Non-railroad assets and assets under capital leases are not depreciated using the group-life method; rather, they are depreciated using the straight-line method on a per asset basis. The depreciable lives of these assets are periodically reviewed by the Company and any changes are applied on a prospective basis. Amortization expense recorded under capital leases is included in depreciation expense on the consolidated income statements. Land is not depreciated. For retirements or disposals of non-railroad depreciable assets and all dispositions of land, the resulting gains or losses are recognized in earnings at the time of disposal. During 2016, the Company recognized \$115 million of earnings related to a \$110 million gain on the sale of an operating property and a \$5 million reimbursement of environmental costs related to the sale, which is recognized in materials, supplies and other on the consolidated statements of income. During 2015, the Company recognized a gain of \$59 million related to the sale of non-operating easements, which is recognized in other income on the consolidated statements of income. (For additional information regarding cost reimbursements related to this sale, see Note 10, Other Income.) These gains and losses were not material in 2014.

Impairment Review

Properties and other long-lived assets are reviewed for impairment annually or whenever events or business conditions indicate the carrying amount of such assets may not be fully recoverable. Initial assessments of recoverability are based on estimates of undiscounted future net cash flows associated with an asset or a group of assets in accordance with the Property, Plant, and Equipment Topic in the ASC. Where impairment is indicated, the assets are evaluated and their carrying amount is reduced to fair value based on discounted net cash flows or other estimates of fair value.

Capital Expenditures

The Company's capital investment includes purchased and self-constructed assets and property additions that substantially extend the service life or increase the utility of those assets. Indirect costs that can be specifically traced to capital projects are also capitalized. The Company is committed to maintaining and improving its existing infrastructure and expanding its network capacity for long-term growth. Rail operations are capital intensive and CSX accounts for these costs in accordance with GAAP and the Company's capitalization policy. All properties are stated at historical cost less an allowance for accumulated depreciation.

CSX CORPORATION

PART II

Item 8. Financial Statements and Supplementary Data

NOTE 6. Properties, continued

The Company's largest category of capital investment is the replacement of track assets and the acquisition or construction of new assets that enable CSX to enhance its operations or provide new capacity offerings to its customers. These construction projects are primarily completed by CSXT employees. Costs for track asset replacement and capacity projects that are capitalized include:

- labor costs, because many of the assets are self-constructed;
- costs to purchase or construct new track or to prepare ground for the laying of track;
- welding (rail, field and plant) which are processes used to connect segments of rail;
- new ballast, which is gravel and crushed stone that holds track in line;
- fuels and lubricants associated with tie, rail and surfacing work which is the process of raising track to a designated elevation over an extended distance;
- cross, switch and bridge ties which are the braces that support the rails on a track;
- gauging which is the process of standardizing the distance between rails;
- handling costs associated with installing rail, ties or ballast;
- usage charge of machinery and equipment utilized in construction or installation; and
- other track materials.

The primary cost in self-constructed track replacement work is labor. CSXT engineering employees directly charge their labor to the track replacement project (the capitalized depreciable property). These employees concurrently perform deconstruction and installation of track material. Because of this concurrent process, CSX must estimate the amount of labor that is related to deconstruction versus installation. Through analysis of CSXT's track replacement process, CSX determined that approximately 20% of labor costs associated with track material installation is related to the deconstruction of old track and 80% is associated with the installation of new track.

Capital investment related to locomotives and freight cars comprises the second largest category of the Company's capital assets. This category includes purchase costs of locomotives and freight cars as well as certain equipment leases that are considered to be capital leases in accordance with the Leases Topic in the ASC. In addition, costs to modify or rebuild these assets are capitalized if the investment incurred extends the asset's service life or improves utilization. Improvement projects must meet specified dollar thresholds to be capitalized and are reviewed by management to determine proper accounting treatment. Routine repairs and maintenance costs, for all asset categories, are expensed as incurred.

CSX CORPORATION

PART II

Item 8. Financial Statements and Supplementary Data

NOTE 7. Commitments and Contingencies

Lease Commitments

The Company has various lease agreements with other parties with terms up to 30 years. Non-cancelable, long-term leases may include provisions for maintenance, options to purchase and options to extend the terms. Rent expense on operating leases is included in equipment and other rents on the consolidated income statements. The Company uses the straight-line method to recognize rent expense on operating leases that include escalations over their terms. These amounts are shown in the table below.

| (Dollars in Millions) | Fiscal Years | | |
|----------------------------------|--------------|------|------|
| | 2016 | 2015 | 2014 |
| Rent Expense on Operating Leases | \$50 | \$66 | \$61 |

At December 2016, minimum rentals on land, buildings, track and equipment under operating leases are disclosed in the table below. Also, payments to Conrail for leases on shared rail infrastructure are included in these amounts. (See Note 12, Related Party Transactions).

| (Dollars in Millions) | Operating Leases | Sublease Income | Net Lease Commitments |
|-----------------------|------------------|-----------------|-----------------------|
| Years | | | |
| 2017 | \$ 78 | \$ (3) | \$ 75 |
| 2018 | 66 | (3) | 63 |
| 2019 | 62 | (3) | 59 |
| 2020 | 49 | (3) | 46 |
| 2021 | 40 | (3) | 37 |
| Thereafter | 153 | (7) | 146 |
| Total | \$ 448 | \$ (22) | \$ 426 |

Purchase Commitments

CSXT has a commitment under a long-term maintenance program that currently covers 50% of CSXT's fleet of locomotives. The agreement is based on the maintenance cycle for each locomotive. Under CSXT's current obligations, the agreement will expire no earlier than 2031. The costs expected to be incurred throughout the duration of the agreement fluctuate as locomotives are placed into or removed from service, or as required maintenance schedules are revised.

The following table summarizes the number of active and inactive locomotives covered and CSXT's payments under the long-term maintenance program.

| (Dollars in Millions) | Fiscal Years | | |
|-----------------------|--------------|-------|-------|
| | 2016 | 2015 | 2014 |
| Amounts Paid | \$230 | \$233 | \$247 |
| Number of Locomotives | 2,243 | 2,310 | 1,886 |

CSX CORPORATION

PART II

Item 8. Financial Statements and Supplementary Data

NOTE 7. Commitments and Contingencies, continued

As of December 2016, the Company has no outstanding locomotive purchase obligations. Annual payments related to the long-term locomotive maintenance program are estimated in the table below.

Additionally, the Company has various other commitments to purchase technology, communications, railcar maintenance and other services from various suppliers. Total annual payments under all of these purchase commitments are also estimated in the table below.

| (Dollars in Millions) | Locomotive Maintenance Payments | Other Commitments | Total |
|-----------------------|---------------------------------------|----------------------|---------|
| 2017 | \$ 234 | \$ 129 | \$363 |
| 2018 | 244 | 92 | 336 |
| 2019 | 260 | 52 | 312 |
| 2020 | 270 | 46 | 316 |
| 2021 | 274 | 36 | 310 |
| Thereafter | 3,690 | 253 | 3,943 |
| Total | \$ 4,972 | \$ 608 | \$5,580 |

Insurance

The Company maintains numerous insurance programs with substantial limits for property damage (which includes business interruption) and third-party liability. A certain amount of risk is retained by the Company on each of the property and liability programs. The Company has a \$25 million retention per occurrence for the non-catastrophic property program (such as a derailment) and a \$50 million retention per occurrence for the liability and catastrophic property programs (such as hurricanes and floods). While the Company believes its insurance coverage is adequate, future claims could exceed existing insurance coverage or insurance may not continue to be available at commercially reasonable rates.

Legal

The Company is involved in litigation incidental to its business and is a party to a number of legal actions and claims, various governmental proceedings and private civil lawsuits, including, but not limited to, those related to fuel surcharge practices, tax matters, environmental and hazardous material exposure matters, FELA and labor claims by current or former employees, other personal injury or property claims and disputes and complaints involving certain transportation rates and charges. Some of the legal proceedings include claims for compensatory as well as punitive damages and others are, or are purported to be, class actions. While the final outcome of these matters cannot be predicted with certainty, considering, among other things, the legal defenses available and liabilities that have been recorded along with applicable insurance, it is currently the opinion of management that none of these pending items will have a material adverse effect on the Company's financial condition, results of operations or liquidity. An unexpected adverse resolution of one or more of these items, however, could have a material adverse effect on the Company's financial condition, results of operations or liquidity in that particular period.

The Company is able to estimate a range of possible loss for certain legal proceedings for which a loss is reasonably possible in excess of reserves established. The Company has estimated this range to be \$6 million to \$126 million in aggregate at December 30, 2016. This estimated aggregate range is based upon currently available information and is subject to significant judgment and a variety of assumptions. Accordingly, the Company's estimate will change from time to time, and actual losses may vary significantly from the current estimate.

CSX CORPORATION

PART II

Item 8. Financial Statements and Supplementary Data

NOTE 7. Commitments and Contingencies, continued

Fuel Surcharge Antitrust Litigation

In May 2007, class action lawsuits were filed against CSXT and three other U.S.-based Class I railroads alleging that the defendants' fuel surcharge practices relating to contract and unregulated traffic resulted from an illegal conspiracy in violation of antitrust laws. In November 2007, the class action lawsuits were consolidated in federal court in the District of Columbia, where they are now pending. The suit seeks treble damages allegedly sustained by purported class members as well as attorneys' fees and other relief. Plaintiffs are expected to allege damages at least equal to the fuel surcharges at issue.

In June 2012, the District Court certified the case as a class action. The decision was not a ruling on the merits of plaintiffs' claims, but rather a decision to allow the plaintiffs to seek to prove the case as a class. The defendant railroads petitioned the U.S. Court of Appeals for the D.C. Circuit for permission to appeal the District Court's class certification decision. In August 2013, the D.C. Circuit issued a decision vacating the class certification decision and remanded the case to the District Court to reconsider its class certification decision. The District Court remand proceedings are underway and the class certification hearing was held in September 2016. The District Court has delayed proceedings on the merits of the case pending the outcome of the class certification remand proceedings. The court has given no indication of timing on its ruling regarding class certification.

CSXT believes that its fuel surcharge practices were arrived at and applied lawfully and that the case is without merit. Accordingly, the Company intends to defend itself vigorously. However, penalties for violating antitrust laws can be severe, and resolution of this matter or an unexpected adverse decision on the merits could have a material adverse effect on the Company's financial condition, results of operations or liquidity in that particular period.

Environmental

CSXT is indemnifying Pharmacia LLC (formerly known as Monsanto Company) for certain liabilities associated with real estate located in Kearny, New Jersey along the Lower Passaic River (the "Property"). The Property, which was formerly owned by Pharmacia, is now owned by CSXT. CSXT's indemnification and defense duties arise with respect to several matters. The U.S. Environmental Protection Agency ("EPA"), using its CERCLA authority, seeks cleanup and removal costs and other damages associated with the presence of hazardous substances in the 17-mile Lower Passaic River Study Area (the "Study Area"). CSXT, on behalf of Pharmacia, and a significant number of other potentially responsible parties are together conducting a Remedial Investigation and Feasibility Study of the Study Area pursuant to an Administrative Settlement Agreement and Order on Consent with the EPA.

In March 2016, EPA issued its Record of Decision detailing the agency's mandated remedial process for the lower 8 miles of the Study Area, which was based on a Focused Feasibility Study. EPA has estimated that it will take the potentially responsible parties approximately ten years to complete the work. At a later date, EPA will select a remedy for the remainder of the Study Area and is expected to again seek the participation of private parties to implement the selected remedy using EPA's CERCLA authority to compel such participation, if necessary.

CSXT is also defending and indemnifying Pharmacia in a cooperative natural resource damages assessment process related to the Property. Based on currently available information, the Company does not believe any indemnification or remediation costs potentially allocable to CSXT with respect to the Property and the Study Area would be material to the Company's financial condition, results of operations or liquidity.

CSX CORPORATION

PART II

Item 8. Financial Statements and Supplementary Data

NOTE 8. Employee Benefit Plans

The Company sponsors defined benefit pension plans principally for salaried, management personnel. For employees hired prior to 2003, the plans provide eligible employees with retirement benefits based predominantly on years of service and compensation rates near retirement. For employees hired in 2003 or thereafter, benefits are determined based on a cash balance formula, which provides benefits by utilizing interest and pay credits based upon age, service and compensation.

In addition to these plans, the Company sponsors a post-retirement medical plan and a life insurance plan that provide certain benefits to full-time, salaried, management employees hired prior to 2003, upon their retirement if certain eligibility requirements are met. Eligible retirees who are age 65 years or older (Medicare-eligible) are covered by a health reimbursement arrangement, which is an employer-funded account that can be used for reimbursement of eligible medical expenses. Eligible retirees younger than 65 years (non-Medicare eligible) are covered by a self-insured program partially funded by participating retirees. The life insurance plan is non-contributory.

The Company engages independent actuaries to compute the amounts of liabilities and expenses relating to these plans subject to the assumptions that the Company determines are appropriate based on historical trends, current market rates and future projections. These amounts are reviewed by management. In order to perform this valuation, the actuaries are provided with the details of the population covered at the beginning of the year, summarized in the table below, and projects that population forward to the end of the year.

| | Summary of Participants as of January 1, 2016 | |
|----------------------------|---|---------------------------------|
| | Pension Plans | Post-retirement Medical Plan |
| Active Employees | 4,823 | 1,139 |
| Retirees and Beneficiaries | 12,018 | 11,893 |
| Other ^(a) | 3,853 | 54 |
| Total | 20,694 | 13,086 |

(a) For pension plans, the other category consists mostly of terminated but vested former employees. For post-retirement plans, the other category consists of employees on long-term disability that have not yet retired.

The benefit obligation for these plans represents the liability of the Company for current and retired employees and is affected primarily by the following:

- service cost (benefits attributed to employee service during the period);
- interest cost (interest on the liability due to the passage of time);
- actuarial gains/losses (experience during the year different from that assumed and changes in plan assumptions); and
- benefits paid to participants.

CSX CORPORATION

PART II

Item 8. Financial Statements and Supplementary Data

NOTE 8. Employee Benefit Plans, continued

Cash Flows

Plan assets are amounts that have been segregated and restricted to provide qualified pension plan benefits and include amounts contributed by the Company and amounts earned from invested contributions, net of benefits paid. Qualified pension plan obligations are funded in accordance with regulatory requirements and with an objective of meeting or exceeding minimum funding requirements necessary to avoid restrictions on flexibility of plan operation and benefit payments. The Company funds the cost of the post-retirement medical and life insurance benefits as well as nonqualified pension benefits on a pay-as-you go basis. No qualified pension plan contributions were made during 2014 and 2015. Although no contributions to the Company's qualified pension plans were required, CSX made voluntary contributions totaling \$250 million during 2016. No contributions to the Company's qualified pension plans are expected in 2017.

Future expected benefit payments are as follows:

| (Dollars in Millions) | Expected Cash Flows | |
|-----------------------|---------------------|--------------------------|
| | Pension Benefits | Post-retirement Benefits |
| 2017 | \$183 | \$ 39 |
| 2018 | 185 | 28 |
| 2019 | 184 | 26 |
| 2020 | 182 | 24 |
| 2021 | 182 | 22 |
| 2022-2026 | 904 | 86 |
| Total | \$1,820 | \$ 225 |

Plan Assets

The CSX Investment Committee (the "Investment Committee"), whose members were selected by the Chief Financial Officer and approved by the Chief Executive Officer, is responsible for oversight and investment of plan assets. The Investment Committee utilizes an investment asset allocation strategy that is monitored on an ongoing basis and updated periodically in consideration of plan or employee changes, or changing market conditions. Periodic studies provide an extensive modeling of asset investment return in conjunction with projected plan liabilities and seek to evaluate how to maximize return within the constraints of acceptable risk. The current asset allocation targets 70% equity investments and 30% fixed income investments and cash. Within equity, a further target is currently established for 42% of total plan assets in domestic equity and 28% in international equity. Allocations are evaluated for levels within 3% of targeted allocations and are adjusted quarterly as necessary. The distribution of pension plan assets as of the measurement date is shown in the table below, and these assets are netted against the pension liabilities on the balance sheet.

| (Dollars in Millions) | December 2016 | | December 2015 | |
|---------------------------|---------------|-------------------------|---------------|-------------------------|
| | Amount | Percent of Total Assets | Amount | Percent of Total Assets |
| Equity | \$1,806 | 71 % | \$1,626 | 70 % |
| Fixed Income | 665 | 26 | 641 | 28 |
| Cash and Cash Equivalents | 68 | 3 | 42 | 2 |

Total \$2,539 100 % \$2,309 100 %

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Item 8. Financial Statements and Supplementary Data

NOTE 8. Employee Benefit Plans, continued

Under the supervision of the Investment Committee, individual investments or fund managers are selected in accordance with standards of prudence applicable to asset diversification and investment suitability. The Company also selects fund managers with differing investment styles and benchmarks their investment returns against appropriate indices. Fund investment performance is continuously monitored. Acceptable performance is determined in the context of the long-term return objectives of the fund and appropriate asset class benchmarks.

Within the Company's equity funds, the U.S. stock segment includes diversification among large and small capitalization stocks. The international stock segment is diversified in a similar manner as well as in developed versus emerging markets stocks. Guidelines established with individual managers limit investment by industry sectors, individual stock issuer concentration and the use of derivatives and CSX securities.

Fixed income securities guidelines established with individual managers specify the types of allowable investments, such as government, corporate and asset-backed bonds, target certain allocation ranges for domestic and foreign investments and limit the use of certain derivatives. Additionally, guidelines stipulate minimum credit quality constraints and any prohibited securities. For detailed information regarding the fair value of pension assets, see Note 13, Fair Value Measurements.

Benefit Obligation, Plan Assets and Funded Status

Changes in benefit obligation and the fair value of plan assets for the 2016 and 2015 calendar plan years are as follows:

| | Pension Benefits | | Post-retirement Benefits | |
|--|------------------|----------------|--------------------------|----------------|
| | Plan Year 2016 | Plan Year 2015 | Plan Year 2016 | Plan Year 2015 |
| (Dollars in Millions) | | | | |
| Actuarial Present Value of Benefit Obligation | | | | |
| Accumulated Benefit Obligation | \$2,717 | \$2,672 | N/A | N/A |
| Projected Benefit Obligation | 2,871 | 2,860 | \$274 | \$314 |
| Change in Projected Benefit Obligation: | | | | |
| Projected Benefit Obligation at Beginning of Plan Year | \$2,860 | \$3,002 | \$314 | \$340 |
| Service Cost | 48 | 45 | 2 | 2 |
| Interest Cost | 119 | 116 | 12 | 12 |
| Plan Participants' Contributions | — | — | 6 | 7 |
| Workforce Reduction Program/Curtailment | — | 7 | — | — |
| Actuarial Loss (Gain) | 20 | (110) | (22) | (7) |
| Benefits Paid | (176) | (200) | (38) | (40) |
| Benefit Obligation at End of Plan Year | \$2,871 | \$2,860 | \$274 | \$314 |
| Change in Plan Assets: | | | | |
| Fair Value of Plan Assets at Beginning of Plan Year | \$2,309 | \$2,504 | \$— | \$— |
| Actual Return on Plan Assets | 139 | (9) | — | — |
| Qualified Employer Contributions | 250 | — | — | — |

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| | | | | |
|---|----------|----------|----------|---------|
| Non-qualified Employer Contributions | 17 | 14 | 32 | 33 |
| Plan Participants' Contributions | — | — | 6 | 7 |
| Benefits Paid | (176) | (200) | (38) | (40) |
| Fair Value of Plan Assets at End of Plan Year | 2,539 | 2,309 | — | — |
| Funded Status at End of Plan Year | \$(332) | \$(551) | \$(274) | \$(314) |

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CSX CORPORATION

PART II

Item 8. Financial Statements and Supplementary Data

NOTE 8. Employee Benefit Plans, continued

For qualified plan funding purposes, assets and discounted liabilities are measured in accordance with the Employee Retirement Income Security Act ("ERISA"), as well as other related provisions of the IRC and related regulations. Under these funding provisions and the alternative measurements available thereunder, the Company estimates its unfunded obligation for qualified plans on an annual basis.

In accordance with Compensation-Retirement Benefits Topic in the ASC, an employer must recognize the funded status of a pension or other post-retirement benefit plan by recording a liability (underfunded plan) or asset (overfunded plan) for the difference between the projected benefit obligation (or the accumulated post-retirement benefit obligation for a post-retirement benefit plan) and the fair value of plan assets at the plan measurement date. Amounts related to pension and post-retirement benefits recorded in other long-term assets, labor and fringe benefits payable and other long-term liabilities on the balance sheet are as follows:

| (Dollars in Millions) | Pension Benefits | | Post-retirement Benefits | |
|--|------------------|---------------|--------------------------|---------------|
| | December 2016 | December 2015 | December 2016 | December 2015 |
| Amounts Recorded in Consolidated Balance Sheets: | | | | |
| Long-term Assets ^(a) | \$9 | \$ 9 | \$— | \$ — |
| Current Liabilities | (15) | (15) | (39) | (36) |
| Long-term Liabilities | (326) | (545) | (235) | (278) |
| Net Amount Recognized in Consolidated Balance Sheets | \$(332) | \$(551) | \$(274) | \$(314) |

^(a) Long-term assets as of December 2016 and 2015 relate to one of the qualified pension plans whose assets exceed projected benefit obligations.

The funded status, or amount by which the benefit obligation exceeds the fair value of plan assets, represents a liability. At December 2016, the status of CSX plans only with a net liability is disclosed below. The total fair value of all plans as of December 2016 was \$2.5 billion, which includes the qualified pension plans with net assets.

| (Dollars in Millions) | Aggregate Fair Value | |
|--|----------------------|------------------------------|
| | of Plan Assets | Aggregate Benefit Obligation |
| Benefit Obligations in Excess of Plan Assets | | |
| Projected Benefit Obligation | \$ 2,506 | \$ (2,847) |
| Accumulated Benefit Obligation | 2,506 | (2,692) |

CSX CORPORATION

PART II

Item 8. Financial Statements and Supplementary Data

NOTE 8. Employee Benefit Plans, continued

Net Benefit Expense

The following table describes the components of expense/(income) related to net benefit expense recorded in labor and fringe on the income statement.

| (Dollars in Millions) | Pension Benefits Fiscal Years | | | Post-retirement Benefits Fiscal Years | | |
|---|----------------------------------|-------|-------|---|------|------|
| | 2016 | 2015 | 2014 | 2016 | 2015 | 2014 |
| Service Cost | \$48 | \$45 | \$44 | \$2 | \$2 | \$3 |
| Interest Cost | 119 | 116 | 123 | 12 | 12 | 13 |
| Expected Return on Plan Assets | (157) | (162) | (166) | — | — | — |
| Amortization of Net Loss | 48 | 70 | 57 | 3 | 4 | 5 |
| Amortization of Prior Service Cost | — | — | — | — | (1) | (1) |
| Net Periodic Benefit Expense | 58 | 69 | 58 | 17 | 17 | 20 |
| Special Termination Benefits - Workforce Reduction Program/Curtailment ^(a) | — | 7 | 27 | — | — | 8 |
| Settlement Gain ^(b) | (1) | (2) | (1) | — | — | — |
| Total Expense | \$57 | \$74 | \$84 | \$17 | \$17 | \$28 |

Special termination benefits are charges in 2015 and 2014 that resulted from a management workforce reduction (a) program initiated in 2014. For further information regarding the program, see Note 1. Nature of Operations and Significant Accounting Policies.

(b) Settlement gains were recognized as one of the pension plan's lump-sum payments to retirees with insignificant balances exceeded the sum of the service cost and interest cost recognized. The gain is the recognition of a portion of its accumulated other comprehensive income related to that plan.

Pension and Other Post-Employment Benefits Adjustments

The following table shows the pre-tax change in other comprehensive loss (income) attributable to the components of net expense and the change in benefit obligation for CSX for pension and other post-employment benefits.

| (Dollars in Millions) | Pension Benefits | | Post-retirement Benefits | |
|---|---------------------|------------------|-----------------------------|------------------|
| | December 2016 | December 2015 | December 2016 | December 2015 |
| Components of Other Comprehensive Loss (Income) | | | | |
| Recognized in the balance sheet | | | | |
| Losses (Gains) | \$38 | \$ 60 | \$ (22) | \$ (7) |
| Expense (Income) recognized in the income statement | | | | |
| Amortization of net losses ^(a) | \$48 | \$ 70 | \$ 3 | \$ 4 |
| Settlement gain | (1) | (2) | — | — |
| Amortization of prior service costs | — | — | — | (1) |

(a) Amortization of net losses estimated to be expensed for 2017 is approximately \$43 million for pension benefits.

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NOTE 8. Employee Benefit Plans, continued

As of December 2016, the balances of pre-tax amounts to be amortized that are included in accumulated other comprehensive loss (a component of shareholders' equity) are as follows:

| | Pension Benefits | Post-retirement Benefits |
|-------------------------------|---------------------|-----------------------------|
| Losses | \$ 891 | \$ 24 |
| Prior Service Costs (Credits) | — | — |
| Total | \$ 891 | \$ 24 |

Assumptions

The expected long-term average rate of return on plan assets reflects the average rate of earnings expected on the funds invested, or to be invested, to provide for benefits included in the projected benefit obligation. In estimating that rate, the Company gives appropriate consideration to the returns being earned by the plan assets in the funds and the rates of return expected to be available for reinvestment as well as the current and projected asset mix of the funds. Management balances market expectations obtained from various investment managers and economists with both market and actual plan historical returns to develop a reasonable estimate of the expected long-term rate of return on assets. This assumption is reviewed annually and adjusted as deemed appropriate.

In 2017, the Company will measure the service cost and interest cost components of the net pension and post-retirement benefits expense by using individual spot rates matched with separate cash flows for each future year instead of a single weighted-average discount rate approach, which has been used in prior years.

The Company made this change to improve the correlation between projected pension and post-retirement benefit obligation cash flows and the corresponding spot discount rates and to provide a more precise measurement of service and interest costs. Under the spot rate approach, individual spot discount rates along the same high-quality corporate bonds yield curve used to measure the pension and post-retirement benefit obligations are applied to the relevant projected cash flows at the relevant maturity. The use of the spot rate approach does not affect the measurement of the pension and post-retirement benefits obligations. The Company accounted for this change on a prospective basis as a change in accounting estimate. For 2017, the Company estimates the adoption of the spot rate approach will decrease net pension and post-retirement benefits expense by approximately \$25 million compared to the approach applicable in prior years.

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Item 8. Financial Statements and Supplementary Data

NOTE 8. Employee Benefit Plans, continued

The weighted averages of assumptions used by the Company to value its pension and post-retirement obligations were as follows:

| | Pension Benefits | | Post-retirement Benefits | |
|---|-----------------------|--------|--------------------------|--------|
| | 2016 | 2015 | 2016 | 2015 |
| Expected Long-term Return on Plan Assets: | | | | |
| Benefit Cost for Current Plan Year | 7.00 % | 7.25 % | N/A | N/A |
| Benefit Cost for Subsequent Plan Year | 6.75 % | 7.00 % | N/A | N/A |
| Discount Rates: | | | | |
| Benefit Cost for Plan Year | 4.30 % | 4.00 % | 3.85 % | 3.60 % |
| Benefit Obligation at End of Plan Year | 4.08 % ^(a) | 4.30 % | 3.71 % | 3.85 % |
| Salary Scale Inflation | 4.60 % | 4.60 % | N/A | N/A |

This weighted average discount rate represents the single equivalent discount rate that would result in the same (a) projected benefit obligation as calculated under the spot rate approach for all pension plans and is presented for purposes of comparison across years.

The impact of the health care cost trend rate is immaterial to the post-retirement benefit cost and obligation due to the plan's health reimbursement arrangement that covers Medicare-eligible retirees.

Other Plans

Under collective bargaining agreements, the Company participates in a multi-employer benefit plan, which provides certain post-retirement health care and life insurance benefits to eligible contract employees. Premiums under this plan are expensed as incurred and amounted to \$35 million, \$32 million and \$37 million in 2016, 2015 and 2014, respectively.

The Company maintains savings plans for virtually all full-time salaried employees and certain employees covered by collective bargaining agreements. Expense associated with these plans was \$35 million, \$36 million and \$41 million for 2016, 2015 and 2014, respectively.

CSX CORPORATION

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Item 8. Financial Statements and Supplementary Data

NOTE 9. Debt and Credit Agreements

Debt at December 2016 and December 2015 is shown in the table below. For information regarding the fair value of debt, see Note 13, Fair Value Measurements.

| | Maturity at December 2016 | Average | December | |
|---|------------------------------|---------------------------------------|---------------|---------------|
| | | Interest Rates at December 2016 | December 2016 | December 2015 |
| (Dollars in Millions) | 2016 | 2016 | 2016 | 2015 |
| Notes ^(a) | 2017-2066 | 4.5% | \$ 11,055 | \$ 10,277 |
| Equipment Obligations ^(b) | 2016-2023 | 6.3% | 232 | 250 |
| Capital Leases | 2016-2026 | 15.6% | 6 | 7 |
| Convertible Debentures ^(c) | | 1.0% | — | 1 |
| Subtotal Long-term Debt (including current portion) | | | \$ 11,293 | \$ 10,535 |
| Less Debt Due within One Year | | | (331) | (20) |
| Long-term Debt (excluding current portion) | | | \$ 10,962 | \$ 10,515 |

(a) Long-term debt as of December 2015 includes debt issue costs of \$168 million that were reclassified from long-term assets to long-term debt on the consolidated balance sheet as a result of ASU, Interest - Imputation of Interest, which became effective for CSX during first quarter 2016.

(b) Equipment obligations are secured by an interest in certain railroad equipment.

(c) Convertible debentures were fully redeemed during August 2016.

Debt Issuance & Early Redemption of Long-term Debt

During 2016, the Company issued \$2.2 billion of new debt and repurchased \$1.4 billion of certain notes that were expected to mature in 2017, 2018 and 2019 resulting in a net increase in debt of \$800 million related to these transactions. CSX issued \$700 million of 2.60% notes due 2026, \$800 million of 3.80% notes due 2046, and \$700 million of 4.25% notes due 2066 (collectively, the "2016 issuances"). These notes are included in the consolidated balance sheets under long-term debt and may be redeemed by the Company at any time at the applicable redemption premium.

The net proceeds of the 2016 issuances were used to fully redeem \$300 million of 5.60% notes that otherwise would have matured on May 1, 2017; \$600 million of 6.25% notes that otherwise would have matured on March 15, 2018; and \$500 million of 7.375% notes that otherwise would have matured on February 1, 2019. The remaining proceeds have been or will be used for general corporate purposes, which may include repurchases of CSX's common stock, capital investment, pension contributions, working capital requirements, improvements in productivity and other cost reductions at CSX's major transportation units. The transactions noted above were determined to be an extinguishment of the existing debt, resulting in recognition of \$115 million of debt repurchase expense in 2016 related to \$1.4 billion of note repayments.

During 2015, CSX issued \$600 million of 3.95% notes due 2050 and \$600 million of 3.35% notes due 2025. Proceeds were used for general corporate purposes, which may include repurchases of CSX's common stock, capital investment, working capital requirements, improvements in productivity and other cost reductions at CSX's major transportation units.

CSX CORPORATION

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Item 8. Financial Statements and Supplementary Data

NOTE 9. Debt and Credit Agreements, continued

Long-term Debt Maturities (Net of Discounts, Premiums and Issuance Costs)

| (Dollars in Millions) | Maturities as of December 2016 |
|--|---|
| Fiscal Years Ending | |
| 2017 | \$ 331 |
| 2018 | 20 |
| 2019 | 18 |
| 2020 | 745 |
| 2021 | 371 |
| Thereafter | 9,808 |
| Total Long-term Debt Maturities, including current portion | \$ 11,293 |

Credit Facilities

CSX has a \$1 billion unsecured, revolving credit facility backed by a diverse syndicate of banks. This facility expires in May 2020, and as of the date of this filing, the Company has no outstanding balances under this facility. The facility allows borrowings at floating (LIBOR-based) interest rates, plus a spread, depending upon CSX's senior unsecured debt ratings. LIBOR is the London Interbank Offered Rate which is a daily reference rate based on the interest rates at which banks offer to lend unsecured funds.

Commitment fees and interest rates payable under the facility were similar to fees and rates available to comparably rated investment-grade borrowers. At December 2016, CSX was in compliance with all covenant requirements under the facility.

Receivables Securitization Facility

In September 2016, the Company renewed and modified its existing receivables securitization facility. The facility was extended with a three-year term scheduled to expire in September 2019. It was modified to provide liquidity of up to \$200 million, changed from \$250 million, along with modifications to other terms. The purpose of this facility is to provide an alternative to commercial paper and a low cost source of short-term liquidity. Under the terms of this facility, CSXT transfers eligible third-party receivables to CSX Trade Receivables, LLC, a bankruptcy-remote special purpose subsidiary. A separate subsidiary of CSX services the receivables. Upon transfer, the receivables become assets of CSX Trade Receivables and are not available to the creditors of CSX or any of its other subsidiaries. In the event CSX Trade Receivables draws under this facility, the Company will record an equivalent amount of debt on its consolidated financial statements. As of December 30, 2016 and the date of this filing, the Company has no outstanding balances under this facility.

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NOTE 10. Other Income - Net

The Company derives income from items that are not considered operating activities. Income from these items is reported net of related expense. Income from non-operating real estate activities includes the results of the Company's non-operating real estate sales, leasing, acquisition and management and development activities and may fluctuate as a function of timing of real estate sales. Miscellaneous income (expense) includes equity earnings or losses, investment gains and losses and other non-operating activities and may fluctuate due to timing. Other income – net consisted of the following:

| (Dollars in Millions) | Fiscal Years | | |
|--|--------------|-------|-------|
| | 2016 | 2015 | 2014 |
| Interest Income | \$10 | \$6 | \$5 |
| Income from Non-operating Real Estate Activities | 27 | 83 | 23 |
| Miscellaneous Income (Expense) | 9 | 9 | (36) |
| Total Other Income (Expense) - Net | \$46 | \$98 | \$(8) |
| Gross Revenue from Real Estate Operations included above | \$56 | \$104 | \$47 |

Income from non-operating real estate activities decreased from 2015 to 2016 primarily due to a \$59 million gain in 2015 from the sale of non-operating easements. For additional information, see Note 6, Properties. Miscellaneous income increased from 2014 to 2015 related to lower environmental costs as well as the reimbursement of environmental costs related to the sale of non-operating easements. Additionally, miscellaneous income (expense) for 2014 previously included debt repurchase expense, which is now included as a separate line on the income statement.

NOTE 11. Income Taxes

Earnings before income taxes of \$2.7 billion, \$3.1 billion and \$3.0 billion for fiscal years 2016, 2015 and 2014, respectively, represent earnings from domestic operations. The breakdown of income tax expense between current and deferred is as follows:

| (Dollars in Millions) | Fiscal Years | | |
|-----------------------|--------------|---------|---------|
| | 2016 | 2015 | 2014 |
| Current: | | | |
| Federal | \$540 | \$619 | \$729 |
| State | 82 | 95 | 90 |
| Subtotal Current | 622 | 714 | 819 |
| Deferred: | | | |
| Federal | 355 | 414 | 291 |
| State | 50 | 42 | 7 |
| Subtotal Deferred | 405 | 456 | 298 |
| Total | \$1,027 | \$1,170 | \$1,117 |

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Item 8. Financial Statements and Supplementary Data

NOTE 11. Income Taxes, continued

Income tax expense reconciled to the tax computed at statutory rates is presented in the table below. In 2016, the Company recorded an income tax expense adjustment of \$10 million as a result of a change in the apportionment of state income taxes and the related impact on the valuation of deferred taxes. The Company recorded a tax benefit of \$7 million, \$4 million and \$31 million in 2016, 2015 and 2014, respectively, primarily as a result of federal and state legislative changes as well as the resolution of other federal and state tax matters. Each year's benefit is included in the state income tax and other lines in the table below.

| (Dollars In Millions) | Fiscal Years | | | | | |
|-------------------------|--------------|---------|---------|---------|---------|---------|
| | 2016 | | 2015 | | 2014 | |
| Federal Income Taxes | \$959 | 35.0 % | \$1,098 | 35.0 % | \$1,066 | 35.0 % |
| State Income Taxes | 83 | 3.0 % | 86 | 2.7 % | 61 | 2.0 % |
| Other | (15) | (0.5)% | (14) | (0.4)% | (10) | (0.3)% |
| Income Tax Expense/Rate | \$1,027 | 37.5 % | \$1,170 | 37.3 % | \$1,117 | 36.7 % |

In September 2013, the IRS issued final regulations governing the income tax treatment of the acquisition, disposition and repair of tangible property. The regulations were effective beginning in 2014. These new regulations did not have a material impact on the financial statements.

The significant components of deferred income tax assets and liabilities include:

| (Dollars in Millions) | 2016 | | 2015 | |
|-------------------------------------|--------|-------------|--------|-------------|
| | Assets | Liabilities | Assets | Liabilities |
| Pension Plans | \$125 | \$ — | \$207 | \$ — |
| Other Employee Benefit Plans | 272 | — | 258 | — |
| Accelerated Depreciation | — | 9,925 | — | 9,614 |
| Other | 225 | 293 | 261 | 291 |
| Total | \$622 | \$ 10,218 | \$726 | \$ 9,905 |
| Net Deferred Income Tax Liabilities | | \$ 9,596 | | \$ 9,179 |

The primary factors in the change in year-end net deferred income tax liability balances include:

- annual provision for deferred income tax expense and
- accumulated other comprehensive loss.

The Company files a consolidated federal income tax return, which includes its principal domestic subsidiaries. CSX and its subsidiaries are subject to U.S. federal income tax as well as income tax of multiple state jurisdictions. CSX participated in a contemporaneous IRS audit of tax year 2016. Federal examinations of original federal income tax returns for all years through 2015 are resolved.

CSX CORPORATION

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Item 8. Financial Statements and Supplementary Data

NOTE 11. Income Taxes, continued

As of December 2016, 2015 and 2014, the Company had approximately \$25 million, \$23 million and \$21 million, respectively, of total unrecognized tax benefits. Net tax benefits of \$16 million, \$15 million and \$13 million in 2016, 2015 and 2014, respectively, could favorably impact the effective income tax rate in each year. The Company does not expect that unrecognized tax benefits as of December 2016 for various state and federal income tax matters will significantly change over the next 12 months. The final outcome of these uncertain tax positions is not yet determinable. The change to the total gross unrecognized tax benefits and prior year audit resolutions of the Company during the fiscal year ended December 2016 is reconciled in the table below.

| Uncertain Tax Positions: (Dollars in Millions) | Fiscal Year | | |
|--|-------------|------|------|
| | 2016 | 2015 | 2014 |
| Balance at beginning of the year | \$23 | \$21 | \$23 |
| Additions based on tax positions related to current year | 1 | 1 | 2 |
| Additions based on tax positions related to prior years | 4 | 4 | 3 |
| Reductions based on tax positions related to prior years | — | — | — |
| Settlements with taxing authorities | — | 1 | — |
| Lapse of statute of limitations | (3) | (4) | (7) |
| Balance at end of the year | \$25 | \$23 | \$21 |

CSX's continuing practice is to recognize net interest and penalties related to income tax matters in income tax expense. Included in the consolidated income statements are expenses of \$2 million in 2016, \$2 million in 2015 and \$1 million in 2014, respectively, for changes to reserves for interest and penalties for all prior year tax positions. The Company had \$6 million, \$4 million and \$1 million accrued for interest and penalties at 2016, 2015 and 2014, respectively, for all prior year tax positions.

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Item 8. Financial Statements and Supplementary Data

NOTE 12. Related Party Transactions

Conrail

Through a limited liability company, CSX and Norfolk Southern Corporation (“NS”) jointly own Conrail. CSX has a 42% economic interest and 50% voting interest in the jointly-owned entity, and NS has the remainder of the economic and voting interests. Pursuant to the Investments-Equity Method and Joint Venture Topic in the ASC, CSX applies the equity method of accounting to its investment in Conrail.

Conrail owns rail infrastructure and operates for the joint benefit of CSX and NS. This is known as the shared asset area. Conrail charges fees for right-of-way usage, equipment rentals and transportation, switching and terminal service charges in the shared asset area. These expenses are included in materials, supplies and other on the consolidated income statements. Future minimum lease payments due to Conrail under the shared asset area agreements are shown in the table below.

| (Dollars in Millions) | Conrail Shared Asset Agreement |
|-----------------------|---|
| 2017 | \$ 27 |
| 2018 | 27 |
| 2019 | 27 |
| 2020 | 27 |
| 2021 | 27 |
| Thereafter | 74 |
| Total | \$ 209 |

Also, included in materials, supplies and other are CSX’s 42 percent share of Conrail’s income and its amortization of the fair value write-up arising from the acquisition of Conrail and certain other adjustments. The amortization primarily represents the additional after-tax depreciation expense related to the write-up of Conrail’s fixed assets when the original purchase price, from the 1997 acquisition of Conrail, was allocated based on fair value. This write-up of fixed assets resulted in a difference between CSX’s investment in Conrail and its share of Conrail’s underlying net equity, which is \$351 million as of December 2016.

The following table details the related Conrail amounts included in materials, supplies and other in the Company’s consolidated income statements:

| (Dollars in Millions) | Fiscal Years | | |
|---------------------------------------|--------------|-------|-------|
| | 2016 | 2015 | 2014 |
| Rents, fees and services | \$114 | \$123 | \$124 |
| Purchase price amortization and other | 4 | 4 | 4 |
| Equity earnings of Conrail | (37) | (33) | (31) |
| Total Conrail Expense | \$81 | \$94 | \$97 |

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Item 8. Financial Statements and Supplementary Data

NOTE 12. Related Party Transactions, continued

As required by the Related Party Disclosures Topic in the ASC, the Company has identified amounts below owed to Conrail, or its subsidiaries, representing liabilities under the operating, equipment and shared area agreements with Conrail. In 2014, the Company also executed two promissory notes with a subsidiary of Conrail which were included in long-term debt on the consolidated balance sheets. Interest expense from these promissory notes was \$6 million for both 2016 and 2015, and \$3 million for 2014.

| (Dollars in Millions) | December 2016 | December 2015 |
|--|------------------|------------------|
| Balance Sheet Information: | | |
| CSX payable to Conrail | \$ 91 | \$ 65 |
| Promissory notes payable to Conrail subsidiary | | |
| 2.89% CSX promissory note due October 2044 | 73 | 73 |
| 2.89% CSXT promissory note due October 2044 | 151 | 151 |

TTX Company

TTX Company ("TTX") is a privately-held corporation engaged in the business of providing its owner-railroads with standardized fleets of intermodal, automotive and general use railcars at time and mileage rates. CSX owns about 20 percent of TTX's common stock, and the remaining is owned by the other leading North American railroads and their affiliates. CSX's investment in TTX is \$469 million and is included in affiliates and other companies in the consolidated balance sheet. Pursuant to the Investments-Equity Method topic in the ASC, CSX applies the equity method of accounting to its investment in TTX.

As required by the Related Party Disclosures Topic in the ASC, the following table discloses amounts related to TTX that are included in equipment and other rents in the Company's consolidated income statements. Also included below is balance sheet information related to CSX's payable to TTX, which represents car rental liabilities.

| (Dollars in Millions) | Fiscal Years | | |
|-------------------------------|--------------|-------|-------|
| | 2016 | 2015 | 2014 |
| Income statement information: | | | |
| Car hire rents | \$233 | \$218 | \$207 |
| Equity earnings of TTX | (26) | (20) | (21) |
| Total TTX expense | \$207 | \$198 | \$186 |

| | December 2016 | December 2015 |
|----------------------------|------------------|------------------|
| Balance sheet information: | | |
| CSX payable to TTX | \$ 47 | \$ 40 |

CSX CORPORATION

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NOTE 13. Fair Value Measurements

The Financial Instruments Topic in the ASC requires disclosures about fair value of financial instruments in annual reports as well as in quarterly reports. For CSX, this statement applies to certain investments, pension plan assets and long-term debt. Also, the Fair Value Measurements and Disclosures Topic in the ASC clarifies the definition of fair value for financial reporting, establishes a framework for measuring fair value and requires additional disclosures about the use of fair value measurements.

Various inputs are considered when determining the value of the Company's investments, pension plan assets and long-term debt. The inputs or methodologies used for valuing securities are not necessarily an indication of the risk associated with investing in these securities. These inputs are summarized in the three broad levels listed below:

- Level 1 – observable market inputs that are unadjusted quoted prices for identical assets or liabilities in active markets;
- Level 2 – other significant observable inputs (including quoted prices for similar securities, interest rates, credit risk, etc.); and
- Level 3 – significant unobservable inputs (including the Company's own assumptions about the assumptions market participants would use in determining the fair value of investments).

The valuation methods described below may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Company believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

Investments

The Company's investment assets, valued with assistance from a third-party trustee, consist of certificates of deposits, commercial paper, corporate bonds, government securities and auction rate securities and are carried at fair value on the consolidated balance sheet per the Fair Value Measurements and Disclosures Topic in the ASC. There are several valuation methodologies used for those assets as described below:

• Certificates of Deposit and Commercial Paper (Level 2): Valued at amortized cost, which approximates fair value;

• Corporate Bonds and Government Securities (Level 2): Valued using broker quotes that utilize observable market inputs; and

• Auction Rate Securities (Level 3): Valued using pricing models for which the assumptions utilize management's estimates of market participant assumptions, because there is currently no active market for trading.

The Company's investment assets are carried at fair value on the consolidated balance sheets as summarized in the table below. Additionally, the amortized cost basis of these investments was \$500 million and \$920 million as of December 30, 2016 and December 25, 2015, respectively.

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NOTE 13. Fair Value Measurements, continued

| (Dollars in Millions) | Fiscal Years | | | | | | | |
|--|--------------|---------|---------|-------|---------|---------|---------|-------|
| | 2016 | | | 2015 | | | | |
| | Level 1 | Level 2 | Level 3 | Total | Level 1 | Level 2 | Level 3 | Total |
| Certificates of Deposit and Commercial Paper | \$415 | \$— | \$— | \$415 | \$810 | \$— | \$— | \$810 |
| Corporate Bonds | — | 63 | — | 63 | 73 | — | — | 73 |
| Government Securities | — | — | 22 | 22 | 32 | — | — | 32 |
| Auction Rate Securities | — | — | — | — | — | 4 | — | 4 |
| Total investments at fair value | \$500 | \$— | \$— | \$500 | \$915 | \$4 | \$— | \$919 |

These investments have the following maturities and are represented on the consolidated balance sheet within short-term investments for investments with maturities of less than one year, and other long-term assets for investments with maturities of one year and greater:

| (Dollars in Millions) | December | December |
|---------------------------------|----------|----------|
| | 2016 | 2015 |
| Less than 1 year | \$ 417 | \$ 810 |
| 1 - 2 years | 12 | 9 |
| 2 - 5 years | 4 | 27 |
| Greater than 5 years | 67 | 73 |
| Total investments at fair value | \$ 500 | \$ 919 |

Long-term Debt

Long-term debt is reported at carrying amount on the consolidated balance sheets and is the Company's only financial instrument with fair values significantly different from their carrying amounts. The majority of the Company's long-term debt is valued with assistance from a third party that utilizes closing transactions, market quotes or market values of comparable debt. For those instruments not valued by the third party, the fair value has been estimated by applying market rates of similar instruments to the scheduled contractual debt payments and maturities. These market rates are provided by the same third party. All of the inputs used to determine the fair value of the Company's long-term debt are Level 2 inputs.

The fair value of outstanding debt fluctuates with changes in a number of factors. Such factors include, but are not limited to, interest rates, market conditions, credit ratings, values of similar financial instruments, size of the transaction, cash flow projections and comparable trades. Fair value will exceed carrying value when the current market interest rate is lower than the interest rate at which the debt was originally issued. The fair value of a company's debt is a measure of its current value under present market conditions. It does not impact the financial statements under current accounting rules.

CSX CORPORATION

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Item 8. Financial Statements and Supplementary Data

NOTE 13. Fair Value Measurements, continued

The fair value and carrying value of the Company's long-term debt is as follows:

| (Dollars in Millions) | December 2016 | December 2015 |
|--|------------------|------------------|
| Long-term Debt (Including Current Maturities): | | |
| Fair Value | \$ 12,096 | \$ 11,340 |
| Carrying Value | 11,293 | 10,535 |

Pension Plan Assets

Pension plan assets are reported at fair value on the consolidated balance sheet. The Investment Committee targets an allocation of pension assets to be generally 70% equity and 30% fixed income. There are several valuation methodologies used for those assets as described below.

Investments in the fair value hierarchy

Common stock (Level 1): Valued at the closing price reported on the active market on which the individual securities are traded on the last day of the year and classified in level 1 of the fair value hierarchy.

Mutual funds (Level 1): Valued at the net asset value of shares held at year end based on quoted market prices determined in an active market. These assets are classified in level 1 of the fair value hierarchy.

Corporate bonds, government securities, asset-backed securities and derivatives (Level 2): Valued using price evaluations reflecting the bid and/or ask sides of the market for a similar investment at year end. Asset-backed securities include commercial mortgage-backed securities and collateralized mortgage obligations. These assets are classified in level 2 of the fair value hierarchy.

Investments measured at net asset value

Partnerships: Net asset value of private equity is based on the fair market values associated with the underlying investments at year end. These funds have redemption restrictions that require advanced notice of 15 business days.

Common collective trust funds: This class consists of private funds that invest in government and corporate securities and various short-term debt instruments and are measured at net asset value to estimate the fair value of the investments. The net asset value of the investments is determined by reference to the fair value of the underlying securities, which are valued primarily through the use of directly or indirectly observable inputs. These funds have redemption restrictions that require advanced notice of up to 15 business days.

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NOTE 13. Fair Value Measurements, continued

The pension plan assets at fair value by level, within the fair value hierarchy, as of calendar plan years 2016 and 2015 are shown in the table below. For additional information related to pension assets, see Note 8, Employee Benefit Plans.

| (Dollars in Millions) | Fiscal Years | | | | | | | |
|--|--------------|---------|---------|----------|---------|---------|---------|----------|
| | 2016 | | | | 2015 | | | |
| | Level 1 | Level 2 | Level 3 | Total | Level 1 | Level 2 | Level 3 | Total |
| Common Stock | \$940 | \$— | \$— | -\$940 | \$738 | \$— | \$— | -\$738 |
| Mutual funds | 12 | — | — | 12 | 15 | — | — | 15 |
| Cash equivalents | 1 | — | — | 1 | 8 | — | — | 8 |
| Corporate bonds | — | 497 | — | 497 | — | 480 | — | 480 |
| Government securities | — | 141 | — | 141 | — | 132 | — | 132 |
| Asset-backed securities | — | 14 | — | 14 | — | 14 | — | 14 |
| Derivatives and other | — | 11 | — | 11 | — | 6 | — | 6 |
| Total investments in the fair value hierarchy | \$953 | \$663 | \$— | -\$1,616 | \$761 | \$632 | \$— | -\$1,393 |
| Investments measured at net asset value ^(a) | n/a | n/a | n/a | \$923 | n/a | n/a | n/a | \$916 |
| Investments at fair value | \$953 | \$663 | \$— | -\$2,539 | \$761 | \$632 | \$— | -\$2,309 |

(a) Investments measured at net asset value represent certain investments that have been measured at net asset value per share (or its equivalent) and are thus are not classified in the fair value hierarchy. In accordance with ASC 820, Fair Value Measurements, the fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to the pension assets disclosed in Note 8, Employee Benefit Plans.

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Item 8. Financial Statements and Supplementary Data

NOTE 14. Other Comprehensive Income / (Loss)

CSX reports comprehensive earnings or loss in accordance with the Comprehensive Income Topic in the ASC in the Consolidated Comprehensive Income Statement. Total comprehensive earnings are defined as all changes in shareholders' equity during a period, other than those resulting from investments by and distributions to shareholders (e.g. issuance of equity securities and dividends). Generally, for CSX, total comprehensive earnings equal net earnings plus or minus adjustments for pension and other post-retirement liabilities. Total comprehensive earnings represent the activity for a period net of tax and were \$1.7 billion, \$2.0 billion and \$1.8 billion for 2016, 2015 and 2014, respectively.

While total comprehensive earnings is the activity in a period and is largely driven by net earnings in that period, accumulated other comprehensive income or loss ("AOCI") represents the cumulative balance of other comprehensive income, net of tax, as of the balance sheet date. For CSX, AOCI is primarily the cumulative balance related to pension and other post-retirement benefit adjustments and CSX's share of AOCI of equity method investees.

Changes in the AOCI balance by component are shown in the table below. Amounts reclassified in pension and other post-employment benefits to net earnings relate to the amortization of actuarial losses and are included in labor and fringe on the consolidated income statements. See Note 8. Employee Benefit Plans for further information. Other primarily represents CSX's share of AOCI of equity method investees. Amounts reclassified in other to net earnings are included in materials, supplies and other on the consolidated income statements.

| | Pension and Other Post-Employment Benefits | Other | Accumulated Other Comprehensive Income (Loss) |
|---|--|----------|--|
| (Dollars in millions) | | | |
| Balance December 27, 2013 - Net of Tax | \$ (462 |) \$(61) | \$ (523 |
| Other Comprehensive (Loss) Income | | | |
| (Loss) Income Before Reclassifications | (297 |) 4 | (293 |
| Amounts Reclassified to Net Earnings | 60 | 2 | 62 |
| Tax Benefit | 88 | — | 88 |
| Total Other Comprehensive (Loss) Income | (149 |) 6 | (143 |
| Balance December 26, 2014 - Net of Tax | (611 |) (55 |)(666 |
| Other Comprehensive Income (Loss) | | | |
| Loss Before Reclassifications | (53 |) (8 |)(61 |
| Amounts Reclassified to Net Earnings | 71 | (2 |)69 |
| Tax (Expense) Benefit | (8 |) 1 | (7 |
| Total Other Comprehensive Income (Loss) | 10 | (9 |)1 |
| Balance December 25, 2015 - Net of Tax | (601 |) (64 |)(665 |
| Other Comprehensive Income | | | |
| (Loss) Income Before Reclassifications | (16 |) 3 | (13 |
| Amounts Reclassified to Net Earnings | 50 | 1 | 51 |
| Tax Expense | (13 |) — | (13 |
| Total Other Comprehensive Income | 21 | 4 | 25 |
| Balance December 30, 2016 - Net of Tax | \$ (580 |) \$(60) | \$ (640 |

CSX CORPORATION

PART II

Item 8. Financial Statements and Supplementary Data

NOTE 15. Quarterly Financial Data (Unaudited)

Pursuant to Article 3 of the SEC's Regulation S-X, the following are selected quarterly financial data:

| Fiscal Year Ended December 2016 (53 weeks) | Quarters | | | | Full |
|---|----------|---------|---------|---------|----------|
| (Dollars in Millions, Except Per Share Amounts) | 1st | 2nd | 3rd | 4th | Year |
| Revenue | \$2,618 | \$2,704 | \$2,710 | \$3,037 | \$11,069 |
| Operating Income | 704 | 840 | 841 | 1,004 | 3,389 |
| Net Earnings | 356 | 445 | 455 | 458 | 1,714 |
| Earnings Per Share, Basic | \$0.37 | \$0.47 | \$0.48 | \$0.49 | \$1.81 |
| Earnings Per Share, Assuming Dilution | 0.37 | 0.47 | 0.48 | 0.49 | 1.81 |
| Fiscal Year Ended December 2015 (52 weeks) | | | | | |
| Revenue | \$3,027 | \$3,064 | \$2,939 | \$2,781 | \$11,811 |
| Operating Income | 843 | 1,017 | 933 | 791 | 3,584 |
| Net Earnings | 442 | 553 | 507 | 466 | 1,968 |
| Earnings Per Share, Basic | \$0.45 | \$0.56 | \$0.52 | \$0.48 | \$2.00 |
| Earnings Per Share, Assuming Dilution | 0.45 | 0.56 | 0.52 | 0.48 | 2.00 |

NOTE 16. Summarized Consolidating Financial Data

In 2007, CSXT, a wholly-owned subsidiary of CSX Corporation, sold secured equipment notes maturing in 2023 in a registered public offering. CSX has fully and unconditionally guaranteed the notes. In connection with the notes, the Company is providing the following condensed consolidating financial information in accordance with SEC disclosure requirements. Each entity in the consolidating financial information follows the same accounting policies as described in the consolidated financial statements, except for the use of the equity method of accounting to reflect ownership interests in subsidiaries which are eliminated upon consolidation and the allocation of certain expenses of CSX incurred for the benefit of its subsidiaries. Condensed consolidating financial information for the obligor, CSXT, and parent guarantor, CSX, is shown in the tables below.

CSX CORPORATION

PART II

Item 8. Financial Statements and Supplementary Data

NOTE 16. Summarized Consolidating Financial Data, continued

Consolidating Income Statements

(Dollars in Millions)

| Fiscal Year Ended December 2016 | CSX Corporation | CSX Transportation | Eliminations and Other | CSX Consolidated |
|-------------------------------------|--------------------|-----------------------|---------------------------|---------------------|
| Revenue | \$ — | \$ 10,991 | \$ 78 | \$ 11,069 |
| Expense | (265) | 8,100 | (155) | 7,680 |
| Operating Income | 265 | 2,891 | 233 | 3,389 |
| Equity in Earnings of Subsidiaries | 1,997 | 2 | (1,999) | — |
| Interest Expense | (583) | (35) | 39 | (579) |
| Other Income - Net | (112) | 44 | (1) | (69) |
| Earnings Before Income Taxes | 1,567 | 2,902 | (1,728) | 2,741 |
| Income Tax Benefit (Expense) | 147 | (1,081) | (93) | (1,027) |
| Net Earnings | \$ 1,714 | \$ 1,821 | \$ (1,821) | \$ 1,714 |
| Total Comprehensive Earnings | \$ 1,739 | \$ 1,833 | \$ (1,833) | \$ 1,739 |
| Fiscal Year Ended December 2015 | | | | |
| Revenue | \$ — | \$ 11,733 | \$ 78 | \$ 11,811 |
| Expense | (589) | 8,922 | (106) | 8,227 |
| Operating Income | 589 | 2,811 | 184 | 3,584 |
| Equity in Earnings of Subsidiaries | 1,949 | — | (1,949) | — |
| Interest Expense | (539) | (33) | 28 | (544) |
| Other Income - Net | (4) | 111 | (9) | 98 |
| Earnings Before Income Taxes | 1,995 | 2,889 | (1,746) | 3,138 |
| Income Tax Expense | (27) | (1,083) | (60) | (1,170) |
| Net Earnings | \$ 1,968 | \$ 1,806 | \$ (1,806) | \$ 1,968 |
| Total Comprehensive Earnings | \$ 1,969 | \$ 1,806 | \$ (1,806) | \$ 1,969 |
| Fiscal Year Ended December 2014 | | | | |
| Revenue | \$ — | \$ 12,590 | \$ 79 | \$ 12,669 |
| Expense | (427) | 9,585 | (102) | 9,056 |
| Operating Income | 427 | 3,005 | 181 | 3,613 |
| Equity in Earnings of Subsidiaries | 1,996 | 1 | (1,997) | — |
| Interest Expense | (520) | (46) | 21 | (545) |
| Other Income - Net | (19) | (4) | (1) | (24) |
| Earnings Before Income Taxes | 1,884 | 2,956 | (1,796) | 3,044 |
| Income Tax Benefit (Expense) | 43 | (1,093) | (67) | (1,117) |
| Net Earnings | \$ 1,927 | \$ 1,863 | \$ (1,863) | \$ 1,927 |
| Total Comprehensive Earnings | \$ 1,784 | \$ 1,875 | \$ (1,875) | \$ 1,784 |

CSX CORPORATION

PART II

Item 8. Financial Statements and Supplementary Data

NOTE 16. Summarized Consolidating Financial Data, continued

Consolidating Balance Sheets

(Dollars in Millions)

| As of December 30, 2016 | CSX Corporation | CSX Transportation | Eliminations and Other | CSX Consolidated |
|---|--------------------|-----------------------|---------------------------|---------------------|
| ASSETS | | | | |
| Current Assets: | | | | |
| Cash and Cash Equivalents | \$ 305 | \$ 281 | \$ 17 | \$ 603 |
| Short-term Investments | 415 | — | 2 | 417 |
| Accounts Receivable - Net | 2 | 215 | 721 | 938 |
| Receivable from Affiliates | 1,157 | 2,351 | (3,508) |) — |
| Materials and Supplies | — | 407 | — | 407 |
| Other Current Assets | — | 106 | 16 | 122 |
| Total Current Assets | 1,879 | 3,360 | (2,752) |) 2,487 |
| Properties | 1 | 40,518 | 2,708 | 43,227 |
| Accumulated Depreciation | (1 |) (10,634 |) (1,442 |) (12,077 |
| Properties - Net | — | 29,884 | 1,266 | 31,150 |
| Investments in Conrail | — | — | 840 | 840 |
| Affiliates and Other Companies | (39 |) 643 | 15 | 619 |
| Investment in Consolidated Subsidiaries | 24,179 | — | (24,179) |) — |
| Other Long-term Assets | 2 | 607 | (291) |) 318 |
| Total Assets | \$ 26,021 | \$ 34,494 | \$ (25,101) |) \$ 35,414 |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | | | |
| Current Liabilities: | | | | |
| Accounts Payable | \$ 95 | \$ 678 | \$ 33 | \$ 806 |
| Labor and Fringe Benefits Payable | 40 | 440 | 65 | 545 |
| Payable to Affiliates | 3,457 | 500 | (3,957) |) — |
| Casualty, Environmental and Other Reserves | — | 102 | 13 | 115 |
| Current Maturities of Long-term Debt | 313 | 19 | (1) |) 331 |
| Income and Other Taxes Payable | (346 |) 459 | 16 | 129 |
| Other Current Liabilities | — | 112 | 2 | 114 |
| Total Current Liabilities | 3,559 | 2,310 | (3,829) |) 2,040 |
| Casualty, Environmental and Other Reserves | — | 208 | 51 | 259 |
| Long-term Debt | 10,203 | 759 | — | 10,962 |
| Deferred Income Taxes - Net | (203 |) 9,541 | 258 | 9,596 |
| Other Long-term Liabilities | 783 | 410 | (330) |) 863 |
| Total Liabilities | 14,342 | 13,228 | (3,850) |) 23,720 |
| Shareholders' Equity: | | | | |
| Common Stock, \$1 Par Value | 928 | 181 | (181) |) 928 |
| Other Capital | 138 | 5,095 | (5,095) |) 138 |
| Retained Earnings | 11,253 | 15,994 | (15,994) |) 11,253 |
| Accumulated Other Comprehensive Loss | (640 |) (19 |) 19 | (640 |
| Noncontrolling Minority Interest | — | 15 | — | 15 |
| Total Shareholders' Equity | 11,679 | 21,266 | (21,251) |) 11,694 |
| Total Liabilities and Shareholders' Equity | \$ 26,021 | \$ 34,494 | \$ (25,101) |) \$ 35,414 |

CSX CORPORATION

PART II

Item 8. Financial Statements and Supplementary Data

NOTE 16. Summarized Consolidating Financial Data, continued

Consolidating Balance Sheets

(Dollars in Millions)

| As of December 25, 2015 | CSX Corporation | CSX Transportation | Eliminations and Other | CSX Consolidated |
|---|--------------------|-----------------------|---------------------------|---------------------|
| ASSETS | | | | |
| Current Assets | | | | |
| Cash and Cash Equivalents | \$ 444 | \$ 175 | \$ 9 | \$ 628 |
| Short-term Investments | 810 | — | — | 810 |
| Accounts Receivable - Net | 1 | 198 | 783 | 982 |
| Receivable from Affiliates | 1,092 | 2,038 | (3,130) | — |
| Materials and Supplies | — | 350 | — | 350 |
| Other Current Assets | (59) |) 120 | 9 | 70 |
| Total Current Assets | 2,288 | 2,881 | (2,329) |) 2,840 |
| Properties | 1 | 38,964 | 2,609 | 41,574 |
| Accumulated Depreciation | (1) |) (10,016) |) (1,383) |) (11,400) |
| Properties - Net | — | 28,948 | 1,226 | 30,174 |
| Investments in Conrail | — | — | 803 | 803 |
| Affiliates and Other Companies | (39) |) 658 | (28) |) 591 |
| Investment in Consolidated Subsidiaries | 22,755 | — | (22,755) | — |
| Other Long-term Assets | 8 | 399 | (70) |) 337 |
| Total Assets | \$ 25,012 | \$ 32,886 | \$ (23,153) |) \$ 34,745 |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | | | |
| Current Liabilities | | | | |
| Accounts Payable | \$ 108 | \$ 626 | \$ 30 | \$ 764 |
| Labor and Fringe Benefits Payable | 36 | 407 | 47 | 490 |
| Payable to Affiliates | 2,954 | 437 | (3,391) | — |
| Casualty, Environmental and Other Reserves | — | 115 | 16 | 131 |
| Current Maturities of Long-term Debt | 1 | 19 | — | 20 |
| Income and Other Taxes Payable | (87) |) 183 | 12 | 108 |
| Other Current Liabilities | — | 437 | 2 | 439 |
| Total Current Liabilities | 3,012 | 2,224 | (3,284) |) 1,952 |
| Casualty, Environmental and Other Reserves | — | 219 | 50 | 269 |
| Long-term Debt | 9,732 | 783 | — | 10,515 |
| Deferred Income Taxes - Net | (188) |) 9,141 | 226 | 9,179 |
| Other Long-term Liabilities | 804 | 484 | (126) |) 1,162 |
| Total Liabilities | 13,360 | 12,851 | (3,134) |) 23,077 |
| Shareholders' Equity | | | | |
| Common Stock, \$1 Par Value | 966 | 181 | (181) |) 966 |
| Other Capital | 113 | 5,091 | (5,091) |) 113 |
| Retained Earnings | 11,238 | 14,774 | (14,774) |) 11,238 |
| Accumulated Other Comprehensive Loss | (665) |) (31) |) 31 |) (665) |
| Noncontrolling Minority Interest | — | 20 | (4) |) 16 |
| Total Shareholders' Equity | 11,652 | 20,035 | (20,019) |) 11,668 |
| Total Liabilities and Shareholders' Equity | \$ 25,012 | \$ 32,886 | \$ (23,153) |) \$ 34,745 |

Certain prior year data has been reclassified to conform to the current presentation.

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PART II

Item 8. Financial Statements and Supplementary Data

NOTE 16. Summarized Consolidating Financial Data, continued

Consolidating Cash Flow Statements

(Dollars in Millions)

| Fiscal Year Ended December 2016 | CSX Corporation | CSX Transportation | Eliminations and Other | CSX Consolidated |
|---|--------------------|-----------------------|---------------------------|---------------------|
| Operating Activities | | | | |
| Net Cash Provided by (Used in) Operating Activities | \$ 453 | \$ 2,950 | \$ (362) | \$ 3,041 |
| Investing Activities | | | | |
| Property Additions | — | (2,208) | (190) | (2,398) |
| Purchases of Short-term Investments | (929) | — | — | (929) |
| Proceeds from Sales of Short-term Investments | 1,325 | — | — | 1,325 |
| Proceeds from Property Dispositions | — | 195 | — | 195 |
| Other Investing Activities | (41) | 91 | (41) | 9 |
| Net Cash Provided by (Used in) Investing Activities | 355 | (1,922) | (231) | (1,798) |
| Financing Activities | | | | |
| Long-term Debt Issued | 2,200 | — | — | 2,200 |
| Long-term Debt Repaid | (1,400) | (19) | — | (1,419) |
| Dividends Paid | (680) | (600) | 600 | (680) |
| Shares Repurchased | (1,056) | — | — | (1,056) |
| Other Financing Activities | (11) | (303) | 1 | (313) |
| Net Cash Provided by (Used in) Financing Activities | (947) | (922) | 601 | (1,268) |
| Net Decrease in Cash and Cash Equivalents | (139) | 106 | 8 | (25) |
| Cash and Cash Equivalents at Beginning of Period | 444 | 175 | 9 | 628 |
| Cash and Cash Equivalents at End of Period | \$ 305 | \$ 281 | \$ 17 | \$ 603 |

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CSX CORPORATION

PART II

Item 8. Financial Statements and Supplementary Data

NOTE 16. Summarized Consolidating Financial Data, continued

Consolidating Cash Flow Statements

(Dollars in Millions)

| Fiscal Year Ended December 2015 | CSX Corporation | CSX Transportation | Eliminations and Other | CSX Consolidated |
|---|--------------------|-----------------------|---------------------------|---------------------|
| Operating Activities | | | | |
| Net Cash Provided by (Used in) Operating Activities | \$ 983 | \$ 2,974 | \$ (587) | \$ 3,370 |
| Investing Activities | | | | |
| Property Additions | — | (2,400) | (162) | (2,562) |
| Purchases of Short-term Investments | (1,734) | — | (5) | (1,739) |
| Proceeds from Sales of Short-term Investments | 1,175 | — | 50 | 1,225 |
| Proceeds from Property Dispositions | — | 147 | — | 147 |
| Other Investing Activities | (10) | 132 | (85) | 37 |
| Net Cash Provided by (Used in) Investing Activities | (569) | (2,121) | (202) | (2,892) |
| Financing Activities | | | | |
| Long-term Debt Issued | 1,200 | — | — | 1,200 |
| Long-term Debt Repaid | (200) | (29) | — | (229) |
| Dividends Paid | (686) | (750) | 750 | (686) |
| Shares Repurchased | (804) | — | — | (804) |
| Other Financing Activities | 10 | 1 | (11) | — |
| Net Cash Provided by (Used in) Financing Activities | (480) | (778) | 739 | (519) |
| Net (Decrease) Increase in Cash and Cash Equivalents | (66) | 75 | (50) | (41) |
| Cash and Cash Equivalents at Beginning of Period | 510 | 100 | 59 | 669 |
| Cash and Cash Equivalents at End of Period | \$ 444 | \$ 175 | \$ 9 | \$ 628 |

CSX CORPORATION

PART II

Item 8. Financial Statements and Supplementary Data

NOTE 16. Summarized Consolidating Financial Data, continued

Consolidating Cash Flow Statements

(Dollars in Millions)

| Fiscal Year Ended December 2014 | CSX Corporation | CSX Transportation | Eliminations and Other | CSX Consolidated |
|---|--------------------|-----------------------|---------------------------|---------------------|
| Operating Activities | | | | |
| Net Cash Provided by (Used in) Operating Activities | \$ 583 | \$ 3,278 | \$ (518) | \$ 3,343 |
| Investing Activities | | | | |
| Property Additions | — | (2,192) | (257) | (2,449) |
| Purchases of Short-term Investments | (1,419) | — | (14) | (1,433) |
| Proceeds from Sales of Short-term Investments | 1,642 | — | 32 | 1,674 |
| Proceeds from Property Dispositions | — | 62 | — | 62 |
| Other Investing Activities | — | (128) | 91 | (37) |
| Net Cash Provided by (Used in) Investing Activities | 223 | (2,258) | (148) | (2,183) |
| Financing Activities | | | | |
| Long-term Debt Issued | 1,000 | — | — | 1,000 |
| Long-term Debt Repaid | (600) | (333) | — | (933) |
| Dividends Paid | (629) | (660) | 660 | (629) |
| Shares Repurchased | (517) | — | — | (517) |
| Other Financing Activities | 11 | (18) | 3 | (4) |
| Net Cash Provided by (Used in) Financing Activities | (735) | (1,011) | 663 | (1,083) |
| Net (Decrease) Increase in Cash and Cash Equivalents | 71 | 9 | (3) | 77 |
| Cash and Cash Equivalents at Beginning of Period | 439 | 91 | 62 | 592 |
| Cash and Cash Equivalents at End of Period | \$ 510 | \$ 100 | \$ 59 | \$ 669 |

CSX CORPORATION
PART II

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure
None.

Item 9A. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

As of December 30, 2016, under the supervision and with the participation of CSX's Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO"), management has evaluated the effectiveness of the design and operation of the Company's disclosure controls and procedures. Based on that evaluation, the CEO and CFO concluded that, as of December 30, 2016, the Company's disclosure controls and procedures were effective at the reasonable assurance level in timely alerting them to material information required to be included in CSX's periodic SEC reports.

Management's Report on Internal Control over Financial Reporting

CSX's management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rules 13a-15(f) and 15d-15(f). Under the supervision and with the participation of the management of CSX, including CSX's CEO and CFO, CSX conducted an evaluation of the effectiveness of the Company's internal control over financial reporting as of December 30, 2016 based on the 2013 framework in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission which is also referred to as COSO. Based on that evaluation, management of CSX concluded that the Company's internal control over financial reporting was effective as of December 30, 2016. Management's assessment of the effectiveness of internal control over financial reporting is expressed at the level of reasonable assurance because a control system, no matter how well designed and operated, can provide only reasonable, but not absolute, assurance that the control system's objectives will be met.

The Company's internal control over financial reporting as of December 30, 2016 has been audited by Ernst & Young LLP, an independent registered public accounting firm, as stated in their report which is included elsewhere herein.

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CSX CORPORATION
PART II

Report of Independent Registered Public Accounting Firm
The Board of Directors and Shareholders of CSX Corporation

We have audited CSX Corporation's (CSX) internal control over financial reporting as of December 30, 2016, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) (the COSO criteria). CSX's management is responsible for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

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

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

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

In our opinion, CSX maintained, in all material respects, effective internal control over financial reporting as of December 30, 2016, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the 2016 consolidated financial statements of CSX and our report dated February 14, 2017 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP
Certified Public Accountants

Jacksonville, Florida

February 14, 2017

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CSX CORPORATION
PART II

Changes in Internal Control over Financial Reporting

There were no material changes in the Company's internal control over financial reporting.

Item 9B. Other Information

None

PART III

Item 10. Directors, Executive Officers of the Registrant and Corporate Governance

In accordance with Instruction G(3) of Form 10-K, the information required by this item is incorporated herein by reference to the Proxy Statement. The Proxy Statement will be filed not later than April 29, 2017 with respect to its 2017 annual meeting of shareholders, except for the information regarding the executive officers of the Company. Information regarding executive officers is included in Part I of this report under the caption "Executive Officers of the Registrant."

Item 11. Executive Compensation

In accordance with Instruction G(3) of Form 10-K, the information required by this Item is incorporated herein by reference to the Proxy Statement (see Item 10 above).

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

In accordance with Instruction G(3) of Form 10-K, the information required by this Item is incorporated herein by reference to the Proxy Statement (see Item 10 above).

Item 13. Certain Relationships and Related Transactions, and Director Independence

In accordance with Instruction G(3) of Form 10-K, the information required by this Item is incorporated herein by reference to the Proxy Statement (see Item 10 above).

Item 14. Principal Accounting Fees and Services

In accordance with Instruction G(3) of Form 10-K, the information required by this Item is incorporated herein by reference to the Proxy Statement (see Item 10 above).

Item 15. Exhibits, Financial Statement Schedules

(a)(1) Financial Statements

See Index to Consolidated Financial Statements on page 57.

(2) Financial Statement Schedules

The information required by Schedule II, Valuation and Qualifying Accounts, is included in Note 5 to the Consolidated Financial Statements, Casualty, Environmental and Other Reserves. All other financial statement schedules are not applicable.

(3) Exhibits

The documents listed below are being filed or have previously been filed on behalf of CSX and are incorporated herein by reference from the documents indicated and made a part hereof. Exhibits not previously filed are filed herewith.

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Pursuant to Regulation S-K, Item 601(b)(4)(iii), instruments that define the rights of holders of the Registrant's long-term debt securities, where the long-term debt securities authorized under each such instrument do not exceed 10% of the Registrant's total assets, have been omitted and will be furnished to the Commission upon request.

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CSX CORPORATION
PART IV

| Exhibit designation | Nature of exhibit | Previously filed as exhibit to |
|--|---|--|
| 2.1 | Distribution Agreement, dated as of July 26, 2004, by and among CSX Corporation, CSX Transportation, Inc., CSX Rail Holding Corporation, CSX Northeast Holding Corporation, Norfolk Southern Corporation, Norfolk Southern Railway Company, CRR Holdings LLC, Green Acquisition Corp., Conrail Inc., Consolidated Rail Corporation, New York Central Lines LLC, Pennsylvania Lines LLC, NYC Newco, Inc. and PRR Newco, Inc. | September 2, 2004, Exhibit 2.1, Form 8-K |
| 3.1 | Amended and Restated Articles of Incorporation of the Registrant, effective as of October 7, 2015 | October 9, 2015, Exhibit 3.1, Form 8-K |
| 3.2 | Amended and Restated Bylaws of the Registrant, amended effective as of February 8, 2017 | February 10, 2017, Exhibit 3.1, Form 8-K |
| Instruments Defining the Rights of Security Holders, Including Debentures: | | |
| 4.1(a) | Indenture, dated August 1, 1990, between the Registrant and The Chase Manhattan Bank, as Trustee | September 7, 1990, Form SE |
| 4.1(b) | First Supplemental Indenture, dated as of June 15, 1991, between the Registrant and The Chase Manhattan Bank, as Trustee | May 28, 1992, Exhibit 4(c), Form SE |
| 4.1(c) | Second Supplemental Indenture, dated as of May 6, 1997, between the Registrant and The Chase Manhattan Bank, as Trustee | June 5, 1997, Exhibit 4.3, Form S-4 (Registration No. 333-28523) |
| 4.1(d) | Third Supplemental Indenture, dated as of April 22, 1998, between the Registrant and The Chase Manhattan Bank, as Trustee | May 12, 1998, Exhibit 4.2, Form 8-K |
| 4.1(e) | Fourth Supplemental Indenture, dated as of October 30, 2001, between the Registrant and The Chase Manhattan Bank, as Trustee | November 7, 2001, Exhibit 4.1, Form 10-Q |
| 4.1(f) | Fifth Supplemental Indenture, dated as of October 27, 2003 between the Registrant and The Chase Manhattan Bank, as Trustee | October 27, 2003, Exhibit 4.1, Form 8-K |
| 4.1(g) | Sixth Supplemental Indenture, dated as of September 23, 2004 between the Registrant and JP Morgan Chase Bank, formerly The Chase Manhattan Bank, as Trustee | November 3, 2004, Exhibit 4.1, Form 10-Q |

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| 4.1(h) | Seventh Supplemental Indenture, dated as of April 25, 2007, between the Registrant and The Bank of New York (as successor to JP Morgan Chase Bank), as Trustee | April 26, 2007, Exhibit 4.4, Form 8-K |
| 4.1(i) | Eighth Supplemental Indenture, dated as of March 24, 2010, between the Registrant and The Bank of New York Mellon(as successor to JP Morgan Chase Bank), as Trustee | April 19, 2010, Exhibit 4.1, Form 10-Q |
| Material Contracts: | | |
| 10.2** | CSX Directors' Pre-2005 Deferred Compensation Plan (as amended through January 8, 2008) | February 22, 2008, Exhibit 10.2, Form 10-K |
| 10.3** | CSX Directors' Deferred Compensation Plan effective January 1, 2005 | February 22, 2008, Exhibit 10.3, Form 10-K |
| 10.4** | CSX Directors' Charitable Gift Plan, as amended | March 4, 1994, Exhibit 10.4, Form 10-K |
| 10.5** | CSX Directors' Matching Gift Plan (as amended through February 9, 2011) | February 26, 2003, Exhibit 10.13, Form 10-K |
| 10.6** | Railroad Retirement Benefits Agreement with Michael J. Ward | February 26, 2003, Exhibit 10.13, Form 10-K |

CSX CORPORATION
PART IV

| Exhibit designation | Nature of exhibit | Previously filed as exhibit to |
|---------------------|---|--|
| 10.12** | Special Retirement Plan of CSX Corporation and Affiliated Companies (as amended through February 14, 2001) | March 4, 2002, Exhibit 10.23, Form 10-K |
| 10.13** | Supplemental Retirement Benefit Plan of CSX Corporation and Affiliated Companies (as amended through February 14, 2001) | March 4, 2002, Exhibit 10.24, Form 10-K |
| 10.14** | Senior Executive Incentive Compensation Plan | March 17, 2000, Appendix B, Definitive Proxy Statement |
| 10.16 | Transaction Agreement, dated as of June 10, 1997, by and among CSX Corporation, CSX Transportation, Inc., Norfolk Southern Corporation, Norfolk Southern Railway Company, Conrail Inc., Consolidated Rail Corporation and CRR Holdings LLC, with certain schedules thereto | July 8, 1997, Exhibit 10, Form 8-K |
| 10.17 | Amendment No. 1, dated as of August 22, 1998, to the Transaction Agreement, dated as of June 10, 1997, by and among CSX Corporation, CSX Transportation, Inc., Norfolk Southern Corporation, Norfolk Southern Railway Company, Conrail Inc., Consolidated Rail Corporation and CRR Holdings, LLC | June 11, 1999, Exhibit 10.1, Form 8-K |
| 10.18 | Amendment No. 2, dated as of June 1, 1999, to the Transaction Agreement, dated as of June 10, 1997, by and among CSX Corporation, CSX Transportation, Inc., Norfolk Southern Corporation, Norfolk Southern Railway Company, Conrail Inc., Consolidated Rail Corporation and CRR Holdings, LLC | June 11, 1999, Exhibit 10.2, Form 8-K |
| 10.19 | Amendment No. 3, dated as of August 1, 2000, to the Transaction Agreement by and among CSX Corporation, CSX Transportation, Inc., Norfolk Southern Corporation, Norfolk Southern Railway Company, Conrail Inc., Consolidated Rail Corporation, and CRR Holdings, LLC. | March 1, 2001, Exhibit 10.34, Form 10-K |
| 10.20 | Amendment No. 4, dated and effective as of June 1, 1999, and executed in April 2004, to the Transaction Agreement, dated as of June 10, 1997, by and among CSX Corporation, CSX Transportation, Inc., Norfolk Southern Corporation, Norfolk Southern Railway Company, Conrail Inc., Consolidated Rail Corporation and CRR Holdings, LLC | August 6, 2004, Exhibit 99.1, Form 8-K |
| 10.21 | Amendment No. 5, dated as of August 27, 2004, to the Transaction Agreement, dated as of June 10, 1997, by and among CSX Corporation, CSX Transportation, Inc., Norfolk Southern Corporation, Norfolk Southern Railway Company, Conrail Inc., Consolidated Rail Corporation and CRR Holdings LLC | September 2, 2004, Exhibit 10.1, Form 8-K |
| 10.22 | Shared Assets Area Operating Agreement for Detroit, dated as of June 1, 1999, by and among Consolidated Rail Corporation, CSX Transportation, Inc. and Norfolk Southern Railway Corporation, with exhibit thereto | June 11, 1999, Exhibit 10.6, Form 8-K, |
| 10.23 | Shared Assets Area Operating Agreement for North Jersey, dated as of June 1, 1999, by and among Consolidated Rail Corporation, CSX Transportation, Inc. and Norfolk Southern Railway Company, with exhibit thereto | June 11, 1999, Exhibit 10.4, Form 8-K |

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10.24 Shared Assets Area Operating Agreement for South Jersey/Philadelphia, dated as of June 1, 1999, by and among Consolidated Rail Corporation, CSX Transportation, Inc. and Norfolk Southern Railway Company, with exhibit thereto June 11, 1999, Exhibit 10.5, Form 8-K

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CSX CORPORATION
PART IV

| Exhibit designation | Nature of exhibit | Previously filed as exhibit to |
|---------------------|--|---|
| 10.25 | Monongahela Usage Agreement, dated as of June 1, 1999, by and among CSX Transportation, Inc., Norfolk Southern Railway Company, Pennsylvania Lines LLC and New York Central Lines LLC, with exhibit thereto | June 11, 1999, Exhibit 10.7, Form 8-K |
| 10.26 | Tax Allocation Agreement, dated as of August 27, 2004, by and among CSX Corporation, Norfolk Southern Corporation, Green Acquisition Corp., Conrail Inc., Consolidated Rail Corporation, New York Central Lines LLC and Pennsylvania Lines LLC | September 2, 2004, Exhibit 10.2, Form 8-K |
| 10.27** | Restricted Stock Award Agreement with Fredrik J. Eliasson | February 12, 2014, Exhibit 10.29, Form 10-K |
| 10.28** | Long-term Incentive Plan, dated May 6, 2014 | May 8, 2014, Exhibit 10.1, Form 8-K |
| 10.29** | Form of Change of Control Agreement | May 8, 2014, Exhibit 10.2, Form 8-K |
| 10.30 | Revolving Credit Agreement, dated May 21, 2015 | May 28, 2015, Exhibit 10.1, Form 8-K |
| 10.31** | Long-term Incentive Plan, dated February 11, 2015 | February 13, 2015, Exhibit 10.1, Form 8-K |
| 10.32** | CSX Stock and Incentive Award Plan | May 7, 2010, Exhibit 10.1, Form 8-K |
| 10.33** | Long-term Incentive Plan, dated February 10, 2016 | February 16, 2016, Exhibit 10.1, Form 8-K |
| 10.34** | Form of Restricted Stock Unit Agreement | February 16, 2016, Exhibit 10.2, Form 10-K |
| 10.35** | Form of Stock Option Agreement | February 16, 2016, Exhibit 10.3, Form 10-K |
| 10.36** | Restricted Stock Award Agreement with Fredrik J. Eliasson | February 16, 2016, Exhibit 10.5, Form 10-K |

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| 10.37** | Restricted Stock Award Agreement with Frank A. Lonegro | February 16, 2016, Exhibit 10.5, Form 10-K |
| 10.38** | Restricted Stock Award Agreement with Cynthia M. Sanborn | February 16, 2016, Exhibit 10.5, Form 10-K |
| 10.39** | CSX Executives' Deferred Compensation Plan (as amended and restated effective January 1, 2017) | October 12, 2016, Exhibit 10.1, Form 10-Q |

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CSX CORPORATION
PART IV

| Exhibit designation | Nature of exhibit | Previously filed as exhibit to |
|-------------------------|--|--------------------------------|
| Officer certifications: | | |
| 31* | Rule 13a-14(a) Certifications | |
| 32* | Section 1350 Certifications | |
| Interactive data files: | | |
| | The following financial information from CSX Corporation's Annual Report on Form 10-K for the year ended December 30, 2016 filed with the SEC on February 14, 2017, formatted in XBRL includes: (i) Consolidated Income Statements for the fiscal periods ended December 30, 2016, December 25, 2015 and December 26, 2014, (ii) Consolidated Comprehensive | |
| 101* | Income Statements for the fiscal periods ended December 30, 2016, December 25, 2015 and December 26, 2014, (iii) Consolidated Balance Sheets at December 30, 2016 and December 25, 2015, (iv) Consolidated Cash Flow Statements for the fiscal periods ended December 30, 2016, December 25, 2015 and December 26, 2014, and (v) the Notes to Consolidated Financial Statements. | |
| Other exhibits: | | |
| 21* | Subsidiaries of the Registrant | |
| 23* | Consent of Independent Registered Public Accounting Firm | |
| 24* | Powers of Attorney | |
| | * Filed herewith | |
| | ** Management Contract or Compensatory Plan or Arrangement | |
| | Note: Items not filed herewith have been submitted in previous SEC filings. | |

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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.

CSX CORPORATION

(Registrant)

By: /s/ CAROLYN T. SIZEMORE

Carolyn T. Sizemore

Vice President and Controller

(Principal Accounting Officer)

Dated: February 14, 2017

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities indicated on February 14, 2017.

| Signature | Title |
|---|---|
| /s/ MICHAEL J. WARD Michael J. Ward | Chairman of the Board, Chief Executive Officer and Director (Principal Executive Officer) |
| /s/ FRANK A. LONEGRO Frank A. Lonegro | Executive Vice President and Chief Financial Officer (Principal Financial Officer) |
| /s/ CAROLYN T. SIZEMORE Carolyn T. Sizemore | Vice President and Controller (Principal Accounting Officer) |
| /s/ ELLEN M. FITZSIMMONS Ellen M. Fitzsimmons | Executive Vice President of Law and Public Affairs, General Counsel and Corporate Secretary *Attorney-in-Fact |

SIGNATURES

| Signature | Title |
|---------------------------|----------|
| * Donna M. Alvarado | Director |
| * John B. Breaux | Director |
| * Pamela L. Carter | Director |
| * Steven T. Halverson | Director |
| * Edward J. Kelly, III | Director |
| * John D. McPherson | Director |
| * David M. Moffett | Director |
| * Timothy T. O'Toole | Director |
| * David M. Ratcliffe | Director |
| * Donald J. Shepard | Director |
| * J. Steven Whisler | Director |

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