UNION PACIFIC CORP
Form 10-Q
July 20, 2017
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2017

OR

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

For the transition period from __________ to ____________

Commission File Number 1-6075

UNION PACIFIC CORPORATION

(Exact name of registrant as specified in its charter)

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

1400 DOUGLAS STREET, OMAHA, NEBRASKA

(Address of principal executive offices)

68179

(Zip Code)

(402) 544-5000

(Registrant's telephone number, including area code)

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

Yes No

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

Yes No

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

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

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

Yes No

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

Emerging growth company

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

As of July 14, 2017, there were 800,384,902 shares of the Registrant's Common Stock outstanding.

Table of Contents

TABLE OF CONTENTS

UNION PACIFIC CORPORATION

AND SUBSIDIARY COMPANIES

PART I. FINANCIAL INFORMATION

PART II. OTHER INFORMATION

2

Table of Contents

PART I. FINANCIAL INFORMATION

Item 1. Condensed Consolidated Financial Statements

Condensed Consolidated Statements of Income (Unaudited)

Union Pacific Corporation and Subsidiary Companies

Millions, Except Per Share Amounts, for the Three Months Ended June 30,	2017	2016
Operating revenues:		
Freight revenues	$ 4,906	$ 4,430
Other revenues	344	340
Total operating revenues	5,250	4,770
Operating expenses:		
Compensation and benefits	1,197	1,160
Purchased services and materials	597	570
Depreciation	525	504
Fuel	434	346
Equipment and other rents	273	286
Other	219	244
Total operating expenses	3,245	3,110
Operating income	2,005	1,660
Other income (Note 6)	43	77
Interest expense	(179)	(173)
Income before income taxes	1,869	1,564
Income taxes	(701)	(585)
Net income	$ 1,168	$ 979
Share and Per Share (Note 8):		
Earnings per share - basic	$ 1.45	$ 1.17
Earnings per share - diluted	$ 1.45	$ 1.17
Weighted average number of shares - basic	804.1	837.4
Weighted average number of shares - diluted	807.2	840.1
Dividends declared per share	$ 0.605	$ 0.55

Condensed Consolidated Statements of Comprehensive Income (Unaudited)

Union Pacific Corporation and Subsidiary Companies

Millions, for the Three Months Ended June 30,	2017	2016
Net income	$ 1,168	$ 979
Other comprehensive income/(loss):		
Defined benefit plans	15	13
Foreign currency translation	16	(3)
Total other comprehensive income/(loss) [a]	31	10
Comprehensive income	$ 1,199	$ 989

[a]Net of deferred taxes of $(18) million and $(6) million during the three months ended June 30, 2017, and 2016, respectively.

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

3

Table of Contents

Condensed Consolidated Statements of Income (Unaudited)

Union Pacific Corporation and Subsidiary Companies

Millions, Except Per Share Amounts, for the Six Months Ended June 30,	2017	2016
Operating revenues:		
Freight revenues	$ 9,700	$ 8,932
Other revenues	682	667
Total operating revenues	10,382	9,599
Operating expenses:		
Compensation and benefits	2,454	2,373
Purchased services and materials	1,163	1,139
Depreciation	1,045	1,006
Fuel	894	666
Equipment and other rents	549	575
Other	479	493
Total operating expenses	6,584	6,252
Operating income	3,798	3,347
Other income (Note 6)	110	123
Interest expense	(351)	(340)
Income before income taxes	3,557	3,130
Income taxes	(1,317)	(1,172)
Net income	$ 2,240	$ 1,958
Share and Per Share (Note 8):		
Earnings per share - basic	$ 2.77	$ 2.33
Earnings per share - diluted	$ 2.76	$ 2.32
Weighted average number of shares - basic	807.8	840.7
Weighted average number of shares - diluted	811.0	843.4
Dividends declared per share	$ 1.21	$ 1.10

Condensed Consolidated Statements of Comprehensive Income (Unaudited)

Union Pacific Corporation and Subsidiary Companies

Millions, for the Six Months Ended June 30,	2017	2016
Net income	$ 2,240	$ 1,958
Other comprehensive income/(loss):		
Defined benefit plans	26	21
Foreign currency translation	25	(24)
Total other comprehensive income/(loss) [a]	51	(3)
Comprehensive income	$ 2,291	$ 1,955

[a]Net of deferred taxes of $(32) million and $(1) million during the six months ended June 30, 2017, and 2016, respectively.

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

Table of Contents

Condensed Consolidated Statements of Financial Position (Unaudited)

Union Pacific Corporation and Subsidiary Companies

Millions, Except Share and Per Share Amounts	June 30, 2017	December 31, 2016
Assets		
Current assets:		
Cash and cash equivalents	$ 1,286	$ 1,277
Short-term investments (Note 13)	90	60
Accounts receivable, net (Note 10)	1,357	1,258
Materials and supplies	726	717
Other current assets	410	284
Total current assets	3,869	3,596
Investments	1,504	1,457
Net properties (Note 11)	50,814	50,389
Other assets	291	276
Total assets	$ 56,478	$ 55,718
Liabilities and Common Shareholders' Equity		
Current liabilities:		
Accounts payable and other current liabilities (Note 12)	$ 2,875	$ 2,882
Debt due within one year (Note 14)	531	758
Total current liabilities	3,406	3,640
Debt due after one year (Note 14)	15,229	14,249
Deferred income taxes	16,329	15,996
Other long-term liabilities	1,899	1,901
Commitments and contingencies (Note 16)		
Total liabilities	36,863	35,786
Common shareholders' equity:		
Common shares, $2.50 par value, 1,400,000,000 authorized; 1,111,425,213 and 1,110,986,415 issued; 801,484,015 and 815,824,413 outstanding, respectively	2,778	2,777
Paid-in-surplus	4,431	4,421
Retained earnings	33,847	32,587
Treasury stock	(20,220)	(18,581)
Accumulated other comprehensive loss (Note 9)	(1,221)	(1,272)
Total common shareholders' equity	19,615	19,932
Total liabilities and common shareholders' equity	$ 56,478	$ 55,718

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

Table of Contents

Condensed Consolidated Statements of Cash Flows (Unaudited)

Union Pacific Corporation and Subsidiary Companies

Millions, for the Six Months Ended June 30,	2017	2016
Operating Activities		
Net income	$ 2,240	$ 1,958
Adjustments to reconcile net income to cash provided by operating activities:		
Depreciation	1,045	1,006
Deferred and other income taxes	298	349
Other operating activities, net	119	(190)
Changes in current assets and liabilities:		
Accounts receivable, net	(99)	(17)
Materials and supplies	(9)	76
Other current assets	(114)	(56)
Accounts payable and other current liabilities	(59)	38
Income and other taxes	38	361
Cash provided by operating activities	3,459	3,525
Investing Activities		
Capital investments	(1,589)	(1,590)
Purchases of short-term investments (Note 13)	(90)	(330)
Maturities of short-term investments (Note 13)	60	-
Proceeds from asset sales	70	99
Other investing activities, net	(15)	(17)
Cash used in investing activities	(1,564)	(1,838)
Financing Activities		
Common share repurchases (Note 17)	(1,611)	(1,252)
Debt issued (Note 14)	1,186	1,428
Dividends paid	(980)	(925)
Debt repaid	(444)	(449)
Other financing activities, net	(37)	(50)
Cash used in financing activities	(1,886)	(1,248)
Net change in cash and cash equivalents	9	439
Cash and cash equivalents at beginning of year	1,277	1,391
Cash and cash equivalents at end of period	$ 1,286	$ 1,830
Supplemental Cash Flow Information		
Non-cash investing and financing activities:		
Capital investments accrued but not yet paid	$ 106	$ 97
Common shares repurchased but not yet paid	41	62
Cash (paid for)/received from:		

Income taxes, net of refunds	$ (977)	$ (460)
Interest, net of amounts capitalized	(336)	(349)

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

Table of Contents

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

Union Pacific Corporation and Subsidiary Companies

Millions	Common Shares	Treasury Shares	Common Shares	Paid-in-Surplus	Retained Earnings	Treasury Stock	AOCI [a]	Total
Balance at January 1, 2016	1,110.4	(261.2)	$ 2,776	$ 4,417	$ 30,233	$ (15,529)	$ (1,195)	$ 20,702
Net income			-	-	1,958	-	-	1,958
Other comprehensive loss			-	-	-	-	(3)	(3)
Conversion, stock option exercises, forfeitures, and other	0.6	0.6	2	(24)	-	26	-	4
Share repurchases (Note 17)	-	(16.3)	-	-	-	(1,314)	-	(1,314)
Cash dividends declared ($1.10 per share)	-	-	-	-	(925)	-	-	(925)
Balance at June 30, 2016	1,111.0	(276.9)	$ 2,778	$ 4,393	$ 31,266	$ (16,817)	$ (1,198)	$ 20,422
Balance at January 1, 2017	1,111.0	(295.2)	$ 2,777	$ 4,421	$ 32,587	$ (18,581)	$ (1,272)	$ 19,932
Net income			-	-	2,240	-	-	2,240
Other comprehensive income			-	-	-	-	51	51
Conversion, stock option exercises, forfeitures, and other	0.4	0.6	1	10	-	13	-	24
Share repurchases (Note 17)	-	(15.3)	-	-	-	(1,652)	-	(1,652)

Cash dividends declared ($1.21 per share)	-	-	-	-	(980)	-	-	(980)
Balance at June 30, 2017	1,111.4	(309.9)	$ 2,778	$ 4,431	$ 33,847	$ (20,220)	$ (1,221)	$ 19,615

[a]AOCI = Accumulated Other Comprehensive Income/(Loss) (Note 9)

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

7

Table of Contents

UNION PACIFIC CORPORATION AND SUBSIDIARY COMPANIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

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

1. Basis of Presentation

Our Condensed Consolidated Financial Statements are unaudited and reflect all adjustments (consisting of normal and recurring adjustments) that are, in the opinion of management, necessary for their fair presentation in conformity with accounting principles generally accepted in the United States of America (GAAP). Pursuant to the rules and regulations of the Securities and Exchange Commission (SEC), certain information and note disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted. Accordingly, this Quarterly Report on Form 10-Q should be read in conjunction with our Consolidated Financial Statements and notes thereto contained in our 2016 Annual Report on Form 10-K. Our Consolidated Statement of Financial Position at December 31, 2016, is derived from audited financial statements. The results of operations for the six months ended June 30, 2017, are not necessarily indicative of the results for the entire year ending December 31, 2017.

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

2. Accounting Pronouncements

In May 2014, the FASB issued Accounting Standards Update No. 2014-09 (ASU 2014-09), Revenue from Contracts with Customers (Topic 606). ASU 2014-09 supersedes the revenue recognition guidance in Topic 605, Revenue Recognition. The core principle of the guidance is that an entity should recognize revenue to depict the transfer of promised goods and services to customers in an amount that reflects the consideration to which the entity expects to be entitled in the exchange for those goods or services. This may require the use of more judgment and estimates in order to correctly recognize the revenue expected as an outcome of each specific performance obligation. Additionally, this guidance will require the disclosure of the nature, amount, and timing of revenue arising from contracts so as to aid in the understanding of the users of financial statements.

This standard is effective for annual reporting periods beginning after December 15, 2017, and we intend to adopt the standard beginning in 2018 using the modified retrospective transition method. The Company has analyzed a significant proportion of our freight and other revenues and we expect to continue to recognize freight revenues as freight moves from origin to destination and to recognize other revenues as identified performance obligations are satisfied. We are currently analyzing freight and other revenues in the context of the new guidance on principal versus agent considerations and evaluating the required new disclosures. At this time, ASU 2014-09 is not expected to have a material impact on our consolidated financial position, results of operations, or cash flows.

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

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

In March 2017, the FASB issued Accounting Standards Update No. 2017-07 (ASU 2017-07), Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost (Topic 715). ASU 2017-07 requires the service cost component be reported separately from the other components of net benefit costs in the income statement, provides explicit guidance on the presentation of the service cost component and the other components of net benefit cost in the income statement, and allows only the service cost component of net benefit cost to be eligible for capitalization. This standard is effective for annual and interim reporting periods beginning after December 15, 2017, and requires retrospective adoption. Early adoption is permitted. ASU 2017-07 is not expected to have a material impact on our consolidated financial position, results of operations, or cash flows.

3. Operations and Segmentation

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

	Three Months Ended June 30,		Six Months Ended June 30,	
Millions	2017	2016	2017	2016
Agricultural Products	$ 907	$ 845	$ 1,849	$ 1,727
Automotive	513	488	1,017	998
Chemicals	898	864	1,783	1,742
Coal	619	494	1,267	1,013
Industrial Products	1,030	830	1,937	1,664
Intermodal	939	909	1,847	1,788
Total freight revenues	$ 4,906	$ 4,430	$ 9,700	$ 8,932
Other revenues	344	340	682	667
Total operating revenues	$ 5,250	$ 4,770	$ 10,382	$ 9,599

Although our revenues are principally derived from customers domiciled in the U.S., the ultimate points of origination or destination for some products we transport are outside the U.S. Each of our commodity groups includes revenue from shipments to and from Mexico. Included in the above table are freight revenues from our Mexico business which amounted to $576 million and $550 million, respectively, for the three months ended June 30, 2017, and June 30, 2016, and $1,142 million and $1,085 million, respectively, for the six months ended June 30, 2017, and June 30, 2016.

4. Stock-Based Compensation

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

Millions	Three Months Ended June 30, 2017	2016	Six Months Ended June 30, 2017	2016
Stock-based compensation, before tax:				
Stock options	$ 5	$ 4	$ 9	$ 8
Retention awards	22	20	44	33
Total stock-based compensation, before tax	$ 27	$ 24	$ 53	$ 41
Excess tax benefits from equity compensation plans	$ 3	$ 6	$ 25	$ 16

Table of Contents

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

Weighted-Average Assumptions	2017	2016
Risk-free interest rate	2.0%	1.3%
Dividend yield	2.3%	2.9%
Expected life (years)	5.3	5.1
Volatility	21.7%	23.2%
Weighted-average grant-date fair value of options granted	$ 18.19	$ 11.36

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

A summary of stock option activity during the six months ended June 30, 2017, is presented below:

	Options (thous.)	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term	Aggregate Intrinsic Value (millions)
Outstanding at January 1, 2017	6,162	$ 73.13	5.9 yrs.	$ 205
Granted	1,086	107.30	N/A	N/A
Exercised	(478)	46.33	N/A	N/A
Forfeited or expired	(90)	91.17	N/A	N/A
Outstanding at June 30, 2017	6,680	$ 80.36	6.2 yrs.	$ 203
Vested or expected to vest at June 30, 2017	6,648	$ 80.22	6.2 yrs.	$ 203
Options exercisable at June 30, 2017	4,288	$ 72.09	4.7 yrs.	$ 166

Stock options are granted at the closing price on the date of grant, have ten-year contractual terms, and vest no later than three years from the date of grant. None of the stock options outstanding at June 30, 2017, are subject to performance or market-based vesting conditions.

At June 30, 2017, there was $28 million of unrecognized compensation expense related to nonvested stock options, which is expected to be recognized over a weighted-average period of 1.6 years. Additional information regarding stock option exercises appears in the table below:

Millions	Three Months Ended June 30, 2017	2016	Six Months Ended June 30, 2017	2016
Intrinsic value of stock options exercised	$ 7	$ 7	$ 30	$ 17
Cash received from option exercises	8	4	28	13
Treasury shares repurchased for employee payroll taxes	(2)	(2)	(9)	(5)
Tax benefit realized from option exercises	2	3	11	7
Aggregate grant-date fair value of stock options vested	-	-	19	19

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

Table of Contents

Changes in our retention awards during the six months ended June 30, 2017, were as follows:

	Shares (thous.)	Weighted-Average Grant-Date Fair Value
Nonvested at January 1, 2017	2,789	$ 84.68
Granted	562	107.30
Vested	(799)	68.06
Forfeited	(67)	92.46
Nonvested at June 30, 2017	2,485	$ 94.93

Retention awards are granted at no cost to the employee or non-employee director and vest over periods lasting up to four years. At June 30, 2017, there was $113 million of total unrecognized compensation expense related to nonvested retention awards, which is expected to be recognized over a weighted-average period of 2.1 years.

Performance Retention Awards – In February 2017, our Board of Directors approved performance stock unit grants. The basic terms of these performance stock units are identical to those granted in February 2016, except for different annual return on invested capital (ROIC) performance targets. The 2016 and 2017 plans also include relative operating income growth (OIG) as a modifier compared to the companies included in the S&P 500 Industrials Index. We define ROIC as net operating profit adjusted for interest expense (including interest on the present value of operating leases) and taxes on interest divided by average invested capital adjusted for the present value of operating leases. The modifier can be up to +/- 25% of the award earned based on the ROIC achieved.

Stock units awarded to selected employees under these grants are subject to continued employment for 37 months and the attainment of certain levels of ROIC, and for the 2016 and 2017 plans, modified for the relative OIG. We expense the fair value of the units that are probable of being earned based on our forecasted ROIC over the 3-year performance period, and with respect to the third year of the 2016 and 2017 plans, the relative OIG modifier. We measure the fair value of these performance stock units based upon the closing price of the underlying common stock as of the date of grant, reduced by the present value of estimated future dividends. Dividend equivalents are paid to participants only after the units are earned.

The assumptions used to calculate the present value of estimated future dividends related to the February 2017 grant were as follows:

	2017
Dividend per share per quarter	$ 0.605
Risk-free interest rate at date of grant	1.5%

Changes in our performance retention awards during the six months ended June 30, 2017, were as follows:

	Shares (thous.)	Weighted-Average Grant-Date Fair Value
Nonvested at January 1, 2017	1,145	$ 86.23
Granted	461	101.38
Vested	(255)	83.06
Unearned	(110)	83.06
Forfeited	(52)	92.20
Nonvested at June 30, 2017	1,189	$ 92.82

At June 30, 2017, there was $55 million of total unrecognized compensation expense related to nonvested performance retention awards, which is expected to be recognized over a weighted-average period of 2.0 years. This expense is subject to achievement of the performance measures established for the performance stock unit grants.

Table of Contents

5. Retirement Plans

Pension and Other Postretirement Benefits

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

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

Expense

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

The components of our net periodic pension cost were as follows:

	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
Millions	2017	2016	2017	2016
Service cost	$ 22	$ 21	$ 45	$ 43

Interest cost	36	36	71	71
Expected return on plan assets	(66)	(67)	(132)	(134)
Amortization of:				
Actuarial loss	19	21	39	41
Net periodic pension cost	$ 11	$ 11	$ 23	$ 21

The components of our net periodic OPEB cost were as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
Millions	2017	2016	2017	2016
Service cost	$ 1	$ -	$ 1	$ 1
Interest cost	2	3	5	6
Amortization of:				
Prior service credit	-	(3)	-	(5)
Actuarial loss	2	3	5	5
Net periodic OPEB cost	$ 5	$ 3	$ 11	$ 7

Cash Contributions

For the six months ended June 30, 2017, we did not make any cash contributions to the qualified pension plan. Any contributions made during 2017 will be based on cash generated from operations and financial market considerations. Our policy with respect to funding the qualified plans is to fund at least the minimum required by law and not more than the maximum amount deductible for tax purposes. At June 30, 2017, we do not have minimum cash funding requirements for 2017.

Table of Contents

6. Other Income

Other income included the following:

Millions	Three Months Ended June 30, 2017	Three Months Ended June 30, 2016	Six Months Ended June 30, 2017	Six Months Ended June 30, 2016
Rental income	$ 26	$ 23	$ 63	$ 48
Net gain on non-operating asset dispositions [a] [b]	11	63	45	88
Interest income	4	3	6	5
Non-operating environmental costs and other	2	(12)	(4)	(18)
Total	$ 43	$ 77	$ 110	$ 123

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

[b]2016 includes $17 million related to a real estate sale in the first quarter and $50 million related to a real estate sale in the second quarter.

7. Income Taxes

Internal Revenue Service (IRS) examinations have been completed and settled for all years prior to 2011, and UPC is not currently under examination by the IRS. In 2016, UPC amended its 2011 and 2012 income tax returns to claim deductions resulting from the resolution of IRS examinations for years prior to 2011. The IRS has completed its review of these amended returns, and because the returns request refunds, they are currently being reviewed by the Joint Committee on Taxation.

Several state tax authorities are examining our state tax returns for years 2006 through 2014.

At June 30, 2017, we had a net liability for unrecognized tax benefits of $122 million.

On July 6, 2017, the State of Illinois increased its corporate income tax rate effective July 1, 2017. In the third quarter of 2017, we will increase our deferred tax expense by approximately $33 million to reflect the increased tax rate.

8. Earnings Per Share

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