NORTH CAROLINA RAILROAD COMPANY

Annual Report

A Norfolk Southern double-stack intermodal train travels through Rowan County on the North Carolina Railroad.

2017

NORTH CAROLINA RAILROAD COMPANY

OUR MISSION

Putting the North Carolina Railroad Company to work for the good of the people of North Carolina.

OUR VISION

To improve our state by:
Enabling freight to grow business;
Expanding rail to move people;
Investing in North Carolina.

Letter

FROM THE CHAIRMAN

The North Carolina Railroad Company is deeply rooted in our state's economic history, and 2017 provided incredible opportunities for the Company to build on nearly 170 years of visionary investments in rail infrastructure.

Our Company continues to play a role in the recruitment and expansion of rail-served business and industry across North Carolina. Through NCRR Invests, we joined with our economic development partners in welcoming eight rail-served companies to the state in 2017, resulting in more than 2,000 jobs.

We are also making further investments in the 317-mile railroad line, initiating and continuing projects in High Point, Morrisville, Selma, Durham and Charlotte. These important infrastructure investments ensure the railroad is ready for the future, accommodating our Class I freight rail provider, Norfolk Southern, as well as the freight rail needs of current and future business and industry served by the North Carolina Railroad line.

Running through 40 municipalities, the North Carolina Railroad has 634 miles of neighbors. As North Carolina grows, preserving the railroad corridor requires significant collaboration with the communities along the line. We work in partnership to accommodate growth, all while protecting the railroad corridor to ensure it can meet current and future needs of rail-served industry.

The North Carolina Railroad connects the state to Class I freight rail service, regional railroads, passenger service and the entire east coast freight railroad network. It is a unique and irreplaceable asset for the state of North Carolina that is impacting the state's economic development now and into the future.

Michael Walters

Chairman, North Carolina Railroad Company Board of Directors

welcoming
8
new rail-served companies

more than
2,000
jobs

more than
$9 MILLION
investment by NCRR

$1.8 BILLION
company investments in NC

NCRR INVESTS 2017

NCRR Invests is a unique economic development initiative that aims to create a competitive advantage for North Carolina in the recruitment of rail-served business and industry. Through NCRR Invests, the North Carolina Railroad Company works with economic development partners at the state and local level to provide assistance to companies that are considering locating or expanding in North Carolina, but require freight rail infrastructure on site.

North Carolina is home to two Class I railroads, Norfolk Southern and CSX, as well as 20 regional railroads. Agriculture, advanced manufacturing, plastics and other industries are demonstrating an increased need for freight rail service, making North Carolina a competitive destination for businesses looking to locate or expand in our state.

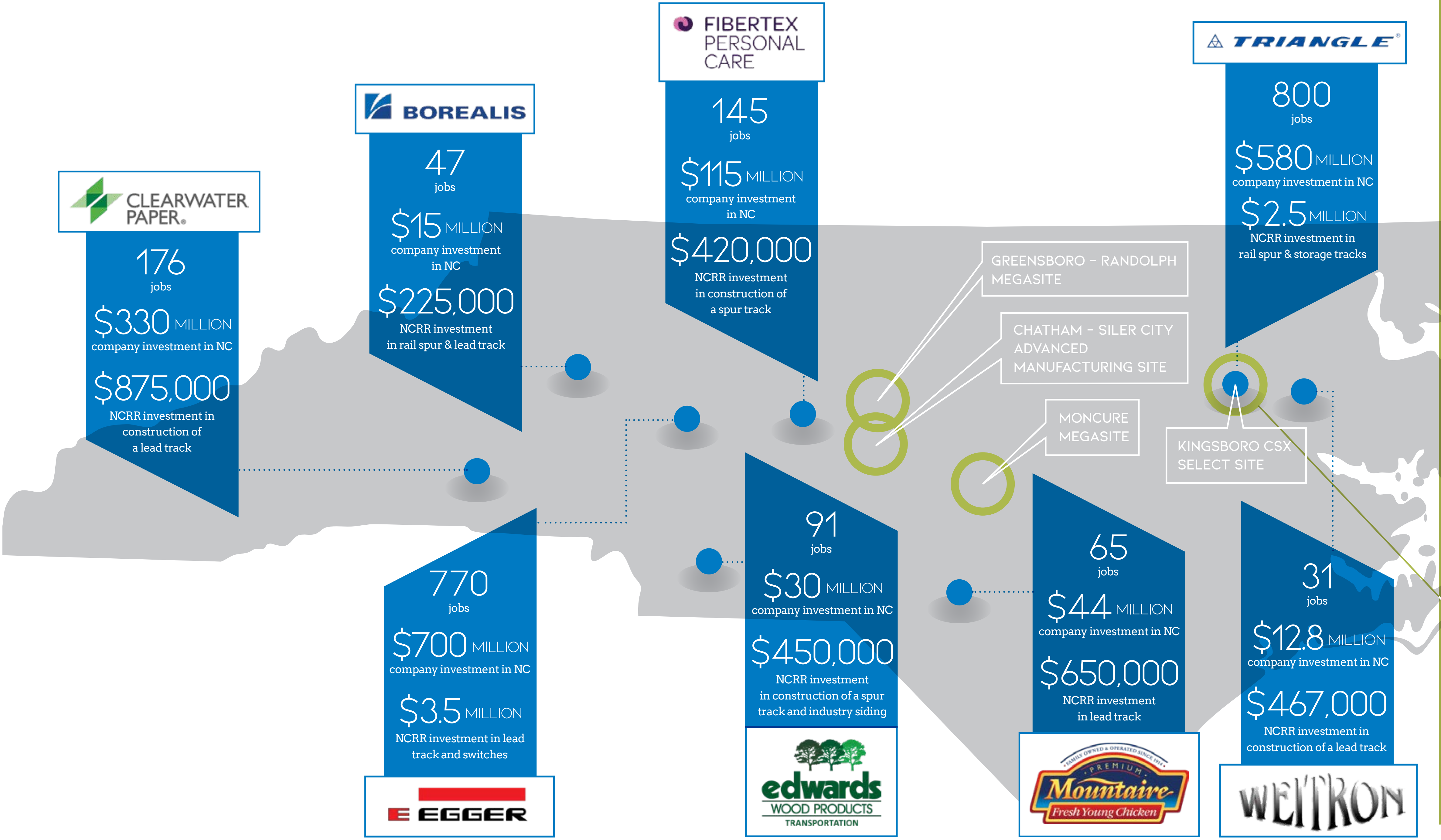
The North Carolina Railroad was created nearly 170 years ago for the purpose of economic development and continues to build on that mission. In 2017, the North Carolina Railroad Company, through NCRR Invests, was a partner on eight economic development announcements, resulting in more than 2000 new jobs in North Carolina.

"If a company requires rail infrastructure to do business, we will work with the Economic Development Partnership, NC Department of Commerce as well as the operating railroads to ensure that North Carolina has a competitive advantage in rail-served business recruitment. Through NCRR Invests, we can assist by investing in the needed infrastructure, whether it's an engineering or design challenge, or building a lead track into an industrial park." Scott Saylor, President

The North Carolina Railroad Company is a unique and irreplaceable asset for the people of North Carolina, and NCRR Invests allows the Company to reinvest the available capital that results from our long-term trackage rights agreement with Norfolk Southern in the 317-mile railroad corridor, as well as rail-served economic development projects across the state.

"There is no other initiative like this in the U.S. This is another important tool in North Carolina's economic development tool box, with the potential to make our state a destination for rail-served business and industry."
Anna Lea Moore, Vice President of Economic Development

Since launching NCRR Invests in 2016, the North Carolina Railroad Company has partnered on eight economic development announcements resulting in more than 2,000 jobs and $1.8 billion in investments by the companies choosing to locate or expand in North Carolina.



Megasites

Megasites, industrial sites with freight rail access and comprised of 1,000 acres or more, are key to recruiting large scale manufacturers and transformational job growth. North Carolina is home to four rail-served megasites—the Greensboro Randolph Megasite, the Kingsboro CSX Select Site, the Moncure Megasite and the Chatham-Siler City Advanced Manufacturing Site.

Three of these sites will be served via NCRR's connection at Greensboro to Norfolk Southern lines, which reach Randolph, Chatham and Lee Counties.

One of the sites—the Greensboro-Randolph Megasite—faced previous challenges in assembling property. NCRR assisted the Greensboro-Randolph Megasite Foundation in this effort because of the enormous potential of this site to attract industry.

Since announcing its partnership in assembling the Greensboro-Randolph Megasite, NCRR has acquired more than 1,000 acres of the 1,825-acre site, with Randolph County and the Greensboro-Randolph Megasite Foundation acquiring approximately 800 acres. The Greensboro-Randolph Megasite is served by Norfolk Southern and connects to the NCRR line at Greensboro, 12 miles northbound.

We continue to work with our partners to make the megasites in North Carolina as marketable as possible, and in 2017, North Carolina was a top contender for the Toyota-Mazda automotive manufacturing plant. While Toyota-Mazda ultimately chose to locate in another state, the experience resulted in North Carolina becoming top of mind for industrial site selection consultants around the world. NCRR is committed to assisting all of the state's industrial megasites with freight rail infrastructure needs should employers choose to locate in North Carolina.

In late 2017, **TRIANGLE TYRE COMPANY**, a China-based manufacturer of tires for automotive and industrial vehicles announced it would be building its first US manufacturing plant at the Kingsboro CSX Select Site located in Edgecombe County. Triangle Tyre will create up to 800 jobs over five years and invest approximately $580 million. Through the North Carolina Railroad Company's economic development initiative, NCRR Invests, NCRR is investing approximately $2.5 million in design and construction of a rail spur, and storage tracks for the company at the Kingsboro CSX Select Site.

Corridor Management
Real Estate

The 317-mile North Carolina Railroad Corridor is unlike any other infrastructure asset in the state. With 634 miles of neighbors on each side, the corridor runs through four of the state's largest cities, thriving downtown areas, rural communities and growing industrial areas. It's a key route for freight and passenger rail service, connecting to two Class I freight rail networks, short lines, multiple passenger lines, and the entire east coast rail network.

Many of North Carolina's large cities and small towns were formed as a result of the railroad running through that part of the state, bringing jobs to the area. Nearly 170 years later, the population growth and urban development many North Carolina communities are experiencing often puts pressure on the railroad corridor.

317-MILE
corridor

runs through
4
of the state's largest cities

key route for
FREIGHT & PASSENGER
rail service

Through our Real Estate and Corridor Management Departments, we collaborate with the 40 municipalities that the track touches, ensuring that they can plan for growth, while preserving the 200-foot-wide freight rail corridor boundaries to accommodate increased rail capacity needs.

The City of Charlotte and Charlotte Area Transit System (CATS) recently celebrated the opening of the Lynx Blue Line Extension, adding 9.3 miles to the existing light rail service, ultimately connecting UNC Charlotte. As the City of Charlotte and its partners planned this transit expansion, the North Carolina Railroad Company collaborated with them to accommodate the Blue Line Extension route, allowing the light rail extension to operate within the corridor for three miles, while ensuring there is adequate space remaining within the NCRR corridor to address future freight rail needs in a part of the city that will continue to grow.

Cary's Lazy Daze began more than 40 years ago as a one-day arts and crafts fair. Since then, the downtown event has grown into a two-day festival that boasts 300 artists, musical acts and exhibits. The festival has expanded its footprint over the years, intersecting with the North Carolina Railroad Line that runs through the downtown festival area. In recent years, the Company has worked with the Town of Cary and the event planners to address pedestrian concerns raised by a large crowd. (pictured: Lyman Collins, City of Cary Cultural Arts Director; John Spencer, NCRR Director of Corridor Management)

Infrastructure Investment
Capital Improvement

More than 11 million tons of freight traffic is carried on the 317-mile North Carolina Railroad annually. In order to ensure the railroad is at peak condition to meet current and future rail capacity needs, the Company continues its longstanding infrastructure investments. By the close of 2019, we will have made $114 million in improvements and upgrades on the railroad line.

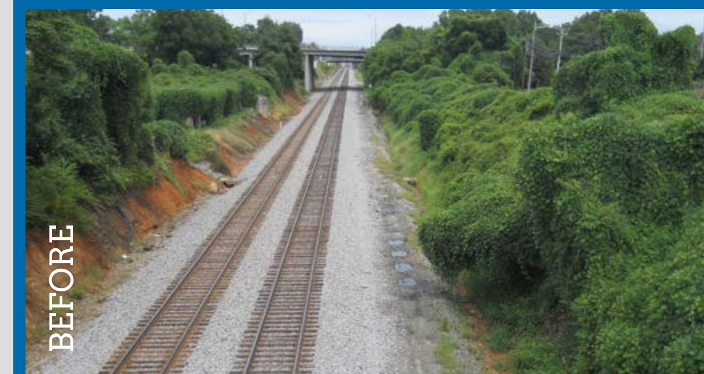
The North Carolina Railroad Company and the City of High Point are partnering on improvements to the railroad corridor and drainage in downtown High Point totaling $5.1 million. The North Carolina Railroad is funding $3.6 million of the total cost.

During the 1930s, the railroad tracks in downtown High Point were lowered to eliminate at-grade crossings and to increase efficiencies on both the roadways and the railroad. Over time, the slopes along the railroad have eroded due to rainfall and storm drainage. The project will include slope and track bed improvements to address drainage and appearance issues.

"More than 40 Norfolk Southern freight trains and Amtrak trains run through High Point each day, moving North Carolina's economy via the North Carolina Railroad," says Saylor. "We are committed to working with community, state and business partners as we plan for long-term freight and passenger growth, and making investments to ensure our rail infrastructure will continue to meet the needs of business and industry and result in job growth for North Carolina."

"The City of High Point enjoys a good working relationship with the North Carolina Railroad," says Keith Pugh, Engineering Services Director for the City of High Point. "We are excited to collaborate on this project which will benefit both our City and NCRR. We look forward to exploring additional opportunities where we can work together to improve the community we serve." Construction is currently underway, with completion slated for mid-2018.

The NCRR line through downtown High Point is located within a cut below street level and includes a number of bridges crossing above the tracks. NCRR is partnering with the City and Norfolk Southern on improvements to the railroad slopes and the storm water drainage on adjacent streets.



There are also several infrastructure investments planned to kick off in 2018.

Durham is home to several railroad bridges, two of which will undergo improvements. The railroad bridge crossing Gregson Street is nearly 100 years old and was constructed with a roadway clearance of 11' 8". To increase motorists' safety and reduce damage to the bridge structure, the roadway clearance will increase to 12'4".

Modifications are planned to the railroad bridges at Chapel Hill Street which include improvements to one bridge and the removal of a bridge structure that is no longer operational. This project will increase safety in the area and enhance the appearance of an important gateway to downtown Durham.

The at-grade or street level crossing at Sugar Creek Road in Charlotte is the highest traveled crossing along the North Carolina Railroad Line. The Sugar Creek Road Bridge project, initiated in collaboration with NCDOT, replaces the at-grade railroad crossing with an overhead bridge, taking motorists over the railroad tracks and eliminating the at-grade crossing resulting in an immediate impact on safety. Construction began in 2016 and will be completed in 2018. The total cost of the project is $43 million with the North Carolina Railroad Company investing $10 million.

"Progress in Motion" Rail Forum

The North Carolina Railroad Company hosted its seventh Progress in Motion Rail Forum on January 24, 2018. The Forum gathered 300 freight and passenger rail representatives, economic development professionals, engineers, government officials, municipal planners and policymakers to discuss the rail industry and the role of rail infrastructure in economic development and job creation.

Nationally recognized rail industry analyst and president of ABH Consulting, Tony Hatch, provided the opening keynote address and shared insights into the current state of the rail industry.

For the first time, the Rail Forum included breakout sessions. ***Rail Sites: What industrial rail users need in a site and best practices for development*** discussed what industrial users are looking for in a site and how to position a site for success. ***Working with the Railroad: Collaborating with communities to enable growth*** featured panelists from communities along the North Carolina Railroad corridor.

Michael Walters, Chairman, welcomes attendees to the seventh Progress in Motion Rail Forum.

Jason Semple with Martin County Economic Development Corporation and Craig Goodson with Davidson County Economic Development Commission share their experiences recruiting Weitron and EGGER Wood Products to their respective counties and how North Carolina's ability to meet the companies' rail infrastructure needs impacted the projects. (Also pictured: Ben Kinney, Business North Carolina, Emcee; Anna Lea Moore, Vice President for Economic Development)

Christopher Chung, CEO of the Economic Development Partnership of North Carolina, discusses the importance of collaboration in successful economic development.

Christopher Chung, CEO of the Economic Development Partnership of North Carolina offered the lunch address. "The North Carolina Railroad represents a truly unique competitive advantage for our state," says Chung. "They are a key partner in our ability to successfully recruit jobs and industry, and their support and engagement are indispensable to local, regional and state economic development efforts across North Carolina."

Corridor Management Breakout Session: Ben Kinney leads a discussion with John Spencer, Director of Corridor Management, North Carolina Railroad Company; Matt Gedney, Gulf & Ohio Railway; John Hodges, Town of Garner; Jim Westmoreland, City of Greensboro; and Scott Stevens, City of Goldsboro.

Economic Development Breakout Session: Leading industrial rail site development and recruitment consultant Courtney Dunbar discusses rail-served industrial site identification and how to position a site for success.

Scott Saylor, President, shares closing remarks.

North Carolina Railroad Company

Consolidated Financial Statements

Years Ended December 31, 2017 and 2016

DIXON HUGHES GOODMAN LLP

Table of Contents

Independent Auditors' Report 12

Consolidated Financial Statements:

Consolidated Balance Sheets 13

Consolidated Statements of Operations and Comprehensive Income (Loss) 15

Consolidated Statements of Stockholder's Equity 16

Consolidated Statements of Cash Flows 17

Notes to Consolidated Financial Statements 18

DHG
DIXON HUGHES GOODMAN LLP

Independent Auditors' Report

Directors and Stockholder
North Carolina Railroad Company
Raleigh, North Carolina

We have audited the accompanying consolidated financial statements of North Carolina Railroad Company and Subsidiaries, which comprise the consolidated balance sheets as of December 31, 2017 and 2016, and the related consolidated statements of operations and comprehensive income (loss), changes in stockholder's equity, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of North Carolina Railroad Company and Subsidiaries as of December 31, 2017 and 2016, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Dixon Hughes Goodman LLP

Raleigh, North Carolina
May 29, 2018

North Carolina Railroad Company
Consolidated Balance Sheets
December 31, 2017 and 2016

	2017	2016
ASSETS		
Current assets:		
Cash and cash equivalents	$ **4,994,631**	$ 6,644,612
Due from escrow agent	-	1,814,531
Accounts receivable, net of allowance for doubtful accounts of $428,000 and $397,000 for 2017 and 2016	**237,113**	85,761
Prepaid expenses	**50,386**	25,845
Total current assets	**5,282,130**	8,570,749
Property and equipment:		
Roadway and land	**7,848,742**	7,848,742
Tracks, signals and bridges	**400,037,251**	167,652,165
Land	**25,037,187**	19,434,303
Buildings and improvements	**16,344,332**	16,322,189
Equipment and furniture	**2,796,915**	2,662,531
Construction in progress	**1,614,417**	3,128,765
	453,678,844	217,048,695
Less accumulated depreciation	**135,296,320**	113,287,012
Property and equipment, net	**318,382,524**	103,761,683
Other assets:		
Investments reserved for capital projects	**99,647,910**	88,960,404
Long-term receivables	**3,593,622**	3,581,545
Other	**313,037**	28,726
Total other assets	**103,554,569**	92,570,675
Total assets	**$ 427,219,223**	$ 204,903,107

See accompanying notes to consolidated financial statements.

North Carolina Railroad Company
Consolidated Balance Sheets
December 31, 2017 and 2016 **(Continued)**

	2017	2016
LIABILITIES AND STOCKHOLDER'S EQUITY		
Current liabilities:		
Accounts payable and accrued expenses	**$ 1,397,942**	$ 1,040,995
Dividend payable	**3,894,917**	3,848,466
Current portion of unearned rent	**286,780**	287,036
Total current liabilities	**5,579,639**	5,176,497
Long-term liabilities:		
Other liabilities	**337,278**	255,100
Deferred tax liability	**576,000**	928,000
Unearned rent	**10,471,136**	10,692,913
Total long-term liabilities	**11,384,414**	11,876,013
Total liabilities	**16,964,053**	17,052,510
Stockholder's equity:		
Common stock, $0.50 par value; 10,000,000 shares authorized; 317 shares issued and outstanding	**159**	159
Additional paid-in capital	**462,774,353**	230,389,267
Accumulated deficit	**(56,674,080)**	(44,215,560)
Accumulated other comprehensive income:		
Unrealized gain on available-for-sale securities	**4,154,738**	1,676,731
Total stockholder's equity	**410,255,170**	187,850,597
Total liabilites and stockholder's equity	**$ 427,219,223**	$ 204,903,107

See accompanying notes to consolidated financial statements.

North Carolina Railroad Company
Consolidated Statements of Operations and Comprehensive Income (Loss)
Years Ended December 31, 2017 and 2016

	2017	2016
Income:		
Lease of roadway and land	**$ 15,579,669**	$ 15,393,865
Other lease income	**2,691,174**	2,527,248
Total lease income	**18,270,843**	17,921,113
Expenses:		
Wages and benefits	**3,197,258**	2,491,360
Professional fees	**501,700**	835,205
Contracted services	**790,680**	1,153,258
Franchise and property taxes	**565,068**	537,318
Insurance	**196,629**	195,874
Reporting and public relations	**246,657**	293,602
Depreciation	**22,009,308**	10,522,184
Engineering, surveying and mapping	**1,311,629**	224,376
Property and corridor management	**669,994**	341,143
Bad debts	**77,173**	87,976
General and administrative	**880,879**	975,557
Economic development	**33,266**	68,413
Total expenses	**30,480,241**	17,726,266
Operating income (loss)	**(12,209,398)**	194,847
Other income (expense):		
Investment income, net of expenses	**2,596,170**	1,558,491
Gain on disposition of assets	**-**	13,741,286
Other income	**854,075**	901,802
Total other income	**3,450,245**	16,201,579
Income (loss) before income taxes	**(8,759,153)**	16,396,426
Income tax expense (benefit)	**(195,550)**	138,155
Net income (loss)	**$ (8,563,603)**	$ 16,258,271
Other comprehensive income (loss):		
Unrealized gains on securities:		
Unrealized holding gains arising during the period	**$ 2,909,488**	$ 831,267
Reclassification adjustments for unrealized holding (gains) losses included in net income	**(431,481)**	336,301
Other comprehensive income	**2,478,007**	1,167,568
Comprehensive income (loss)	**$ (6,085,596)**	$ 17,425,839

See accompanying notes to consolidated financial statements.

North Carolina Railroad Company
Consolidated Statements of Changes in Stockholder's Equity
Years Ended December 31, 2017 and 2016

	Common Stock	Additional Paid-in Capital	Accumulated Deficit	Accumulated Other Comprehensive Income	Total Stockholder's Equity
Balance, December 31, 2015	159	$ 204,866,667	$ (56,625,365)	$ 509,163	$ 148,750,624
Capital improvement contributions	-	25,522,600	-	-	25,522,600
Dividends	-	-	(3,848,466)	-	(3,848,466)
Net income	-	-	16,258,271	1,167,568	17,425,839
Balance, December 31, 2016	159	230,389,267	(44,215,560)	1,676,731	187,850,597
Capital improvement contributions	-	232,385,086	-	-	232,385,086
Dividends	-	-	(3,894,917)	-	(3,894,917)
Net income (loss)	-	-	(8,563,603)	2,478,007	(6,085,596)
Balance, December 31, 2017	159	$ 462,774,353	$ (56,674,080)	$ 4,154,738	$ 410,255,170

North Carolina Railroad Company
Consolidated Statements of Cash Flows
Years Ended December 31, 2017 and 2016

	2017	2016
Cash flows from operating activities:		
Net income (loss)	**$ (8,563,603)**	$ 16,258,271
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Provision for bad debts	**(77,173)**	(87,976)
Depreciation	**22,009,308**	10,522,184
Deferred income tax benefit	**(352,000)**	(115,000)
Interest earned by investments reserved for capital projects	**(2,703,412)**	(1,603,831)
Gain on disposal of property and equipment	**-**	(13,741,286)
Changes in operating assets and liabilities:		
Accounts receivable	**(74,179)**	104,577
Long-term receivable	**(12,077)**	992,129
Prepaid expenses	**(24,541)**	(6,347)
Other assets	**(284,311)**	(20,661)
Accounts payable and accrued expenses	**864,589**	(996,616)
Unearned revenues	**(221,777)**	(181,632)
Other liabilities	**82,178**	52,355
Net cash provided by operating activities	**10,643,002**	11,176,167
Cash flows from investing activities:		
Purchase of property and equipment	**(4,752,961)**	(15,033,824)
Proceeds from sale of property	**-**	14,029,940
Due from escrow agent	**1,814,531**	(1,814,531)
Transfer of unrestricted cash and cash equivalents to investments reserved for capital projects	**(10,500,000)**	(16,300,000)
Transfers of investments reserved for capital projects to cash and cash equivalents for capital expenditures	**4,993,913**	12,561,677
Net cash used in investing activities	**(8,444,517)**	(6,556,738)
Cash flows from financing activities:		
Payment of dividend	**(3,848,466)**	(3,779,305)
Net cash used in financing activities	**(3,848,466)**	(3,779,305)
Net increase (decrease) in cash and cash equivalents	**(1,649,981)**	840,124
Cash and cash equivalents at beginning of year	**6,644,612**	5,804,488
Cash and cash equivalents at end of year	**$ 4,994,631**	$ 6,644,612
Supplemental disclosure of cash flow information:		
Cash paid for income taxes	**$ 188,000**	$ 229,509
Supplemental schedule of noncash investing and financing activities:		
Additions to property and equipment contributed by the North Carolina Department of Transportation	**$ 232,385,086**	$ 25,522,600
Property and equipment purchases in accounts payable	**$ 11,177**	$ 519,075
Accrued dividends payable	**$ 3,894,917**	$ 3,848,466

See accompanying notes to consolidated financial statements.

Notes to Consolidated Financial Statements

1. Nature of Business

The North Carolina Railroad Company and Subsidiaries, a North Carolina company, (collectively referred to as the "Company"), owns approximately 317 miles of continuous railroad line extending from Charlotte, North Carolina to Morehead City, North Carolina. The Company's railroad facilities are operated by Norfolk Southern Railway Company ("NSR"). The State of North Carolina is the sole owner of all the common stock of the Company.

N.C. Railroad, Inc. ("NCRI"), a wholly owned subsidiary of the North Carolina Railroad Company ("NCRR"), was formed on December 15, 2006. NCRI conducts certain taxable activities, such as leasing of commercial real estate, while NCRR conducts all tax-exempt activities, such as leasing of railroad facilities and corridor management.

North Carolina Railroad Lessee LLC ("NCRR Lessee"), a wholly owned subsidiary of NCRR, was formed on April 5, 2016. NCRR Lessee manages real estate properties to be used in future economic development projects of NCRR.

North Carolina Railroad Holdings I LLC and North Carolina Railroad Holdings II LLC (collectively "NCRR Holdings"), wholly owned subsidiaries of NCRR, were formed on April 5, 2016, for the purpose of acquiring real estate to be used in future economic development projects of NCRR. Effective April 4, 2017, NCRR Lessee and North Carolina Railroad Holdings II, LLC were merged into North Carolina Railroad Holdings I LLC.

2. Significant Accounting Policies

Basis of Consolidation

The accompanying consolidated financial statements include the accounts of NCRR and its wholly owned subsidiaries, NCRI, NCRR Lessee, and NCRR Holdings. All intercompany transactions and balances have been eliminated in consolidation.

Use of Estimates

In preparing its consolidated financial statements in conformity with accounting principles generally accepted in the United States of America ("GAAP"), management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the consolidated balance sheet date and the reported amounts of revenues and expenses during the reporting period. Significant items subject to such estimates and assumptions include the useful lives of property and equipment. Actual results could differ from those estimates.

Cash and cash equivalents

For purposes of the consolidated statement of cash flows, the Company considers all highly liquid investments with an original maturity of three months or less when purchased to be cash equivalents. Cash equivalents include money market funds. Cash and cash equivalents that are restricted or designated by the Board of Directors for capital projects are reported as investments reserved for capital projects in the accompanying consolidated balance sheets. See Note 5.

At times, the Company places cash and cash equivalents and certificates of deposits with original maturities of three months or more with financial institutions in amounts that are in excess of Federal Deposit Insurance Company insurance limits. The Company has not experienced any losses in such accounts. The financial condition of financial institutions is periodically reassessed, and the Company believes the risk of any loss is minimal.

North Carolina Railroad Company
Notes to Consolidated Financial Statements

Accounts Receivable

Accounts receivable are uncollateralized obligations due under lease agreements. The Company provides an allowance for doubtful accounts equal to the estimated losses that are expected to be incurred in their collection. The allowance is based on historical collection experience and management's review of the current status of the existing receivables. An account receivable is considered to be past due if any portion of the receivable balance is outstanding for more than 30 days.

Property and Equipment

Property and equipment are stated at cost less accumulated depreciation. The Company computes depreciation using the straight-line method over the following estimated useful lives:

	Estimated Useful Lives (Years)
Buildings and building improvements	25
Bridges	25
Track and signals	10
Equipment and furniture	3 - 7

Values of the properties included in Roadway and Land approximate 1916 valuations by the Interstate Commerce Commission. These properties represent fully depreciated roadway or undepreciated land. The Company assesses long-lived assets for impairment whenever events or changes indicate that the carrying amount of the assets may not be recovered based on estimated future undiscounted cash flows. In the event such cash flows are not expected to be sufficient to recover the carrying value of the assets, the useful lives of the assets are revised or the assets are written down to their estimated fair values.

Investments Reserved for Capital Projects

Investments reserved for capital projects consist of investments in marketable equity securities and debt securities. These investments are classified as available-for-sale and are reported at fair value, with changes in net unrealized gains and losses included in other comprehensive income, net of tax, if any. When securities are sold, gains and losses are determined using the specific identification method for all investments except mutual funds which are determined using the average cost method. Investments are classified as noncurrent due to the board designations of investments for capital improvements. The Company reviews securities when quoted market prices are less than cost to determine if the impairment is other than temporary. Declines in the fair value of individual securities below their cost that are other than temporary would result in write-downs of the individual securities to their fair value with such write down being included in earnings as realized losses.

Fair Values

The Company uses market data or assumptions that market participants would use in pricing assets and liabilities at fair value, and establishes a three-tier fair-value hierarchy, which prioritizes the inputs used in measuring fair value. These tiers include values based on quotes in active markets for identical assets (Level 1), values estimated based on other available market information including quoted market prices for similar assets in active and non-active markets and pricing models based on observable inputs (Level 2), and values based on management's estimates using various valuation methods (Level 3).

Revenue Recognition

Lease of Roadway and Land

Revenue received from property that is operated by NSR is reflected in the consolidated statements of income when earned in accordance with the Company's lease arrangements.

Other Lease Income

The Company leases certain property that is not operated by NSR. Revenue is reflected in the consolidated statements of operations when earned. The Company also collects license fee revenue which is recognized when earned. The Company defers recognition of contingent rentals until the requirements are met.

Advertising

The Company incurred $103,593 and $101,665 in advertising costs in 2017 and 2016, respectively.

Income Taxes

Pursuant to Section 11146 of the Safe, Accountable, Flexible, Efficient Transportation Equity Act of 2005 (the "Act"), a substantial portion of the Company's income is exempt from federal and state income taxes. The activities that generate income which is not exempt from federal and state income taxes pursuant to the Act are conducted in NCRI.

Deferred tax assets and liabilities are recognized by NCRI for the estimated future tax consequences attributable to differences between the tax bases of assets and liabilities and their carrying amount for financial reporting purposes. Deferred tax assets and liabilities are measured using enacted tax rates in effect for the year in which the temporary differences are expected to be recovered or settled. Deferred tax assets are reduced by a valuation allowance if it is more likely than not that the tax benefits will not be realized.

3. Investments Reserved for Capital Projects

The following is a summary of the securities portfolio by major classification included in investments reserved for capital projects at December 31, 2017 and 2016:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
December 31, 2017				
Available for Sale:				
U.S. Government and federal agencies	$ 27,853,448	$ 15,541	$ 105,099	$ 27,763,891
Mortgage backed securities	10,303,316	-	180,249	10,123,067
Collateralized mortgage obligations	4,673,359	-	71,252	4,602,107
State and local governments	7,937,873	-	89,967	7,847,906
Corporate debt securities	21,994,911	88,771	-	22,083,682
Mutual funds	15,608,468	4,496,993	-	20,105,461
	$ 88,371,375	$ 4,601,305	$ 446,567	$ 92,526,114

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
December 31, 2016				
Available for Sale:				
Foreign debt instruments	$ 1,739,613	$ 42,011	$ -	$ 1,781,624
U.S. Government and federal agencies	10,217,464	36,572	10,466	10,243,570
Mortgage backed securities	13,615,892	-	253,685	13,362,207
Collateralized mortgage obligations	17,251,810	456	221,363	17,030,903
State and local governments	4,601,915	-	66,544	4,535,371
Corporate debt securities	21,268,650	13,191	73,544	21,208,297
Mutual funds	16,191,391	2,210,103	-	18,401,494
	$ 84,886,735	$ 2,302,333	$ 625,602	$ 86,563,466

Available for sale securities are carried in the consolidated financial statements at fair value. For the year ended December 31, 2017, a net unrealized holding gain on available for sale securities in the amount of $2,909,488 has been included in accumulated other comprehensive income. For the year ended December 31, 2016, a net unrealized holding gain on available for sale securities in the amount of $831,267 has been included in accumulated other comprehensive income.

In addition to the investments disclosed above, investments reserved for capital projects includes cash and cash equivalents totaling $7,100,283 and $2,396,139 and accrued interest receivable totaling $21,513 and $799 at December 31, 2017 and 2016 respectively. Investment management fees, totaling $195,441 and $176,853, respectively, in 2017 and 2016, are netted against investment income.

The fair values of securities carried at fair value in the consolidated financial statements are determined as follows:

	December 31, 2017	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
U.S Government and federal agencies	**$ 27,763,891**	**$ -**	**$ 27,763,891**	**$ -**
Mortgage backed securities	**10,123,067**	**-**	**10,123,067**	**-**
Collateralized mortgage obligations	**4,602,107**	**-**	**4,602,107**	**-**
State and local governments	**7,847,906**	**-**	**7,847,906**	**-**
Corporate debt securities	**22,083,682**	**-**	**22,083,682**	**-**
Mutual funds	**20,105,461**	**20,105,461**	**-**	**-**
	$ 92,526,114	**$ 20,105,461**	**$ 72,420,653**	**$ -**

	December 31, 2016	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Foreign debt instruments	$ 1,781,624	$ -	$ 1,781,624	$ -
U.S Government and federal agencies	10,243,570	-	10,243,570	-
Mortgage backed securities	13,362,207	-	13,362,207	-
Collateralized mortgage obligations	17,030,903	-	17,030,903	-
State and local governments	4,535,371	-	4,535,371	-
Corporate debt securities	21,208,297	-	21,208,297	-
Mutual funds	18,401,494	18,401,494	-	-
	$ 86,563,466	$ 18,401,494	$ 68,161,972	$ -

All assets have been valued using a market approach. Fair values for assets in Level 2 are calculated using quoted market prices for similar assets in markets that are not active.

The amortized cost and fair values of available for sale securities at December 31, 2017 and 2016 by contractual maturity are shown below. Actual expected maturities may differ from contractual maturities because issuers may have the right to call or prepay obligations.

	Amortized Cost	Fair Value
December 31, 2017		
Available for sale:		
Due within one year	**$ 9,550,510**	**$ 9,482,270**
Due after one year through five years	**31,815,556**	**31,762,189**
Due after five years through ten years	**19,952,732**	**19,858,529**
Due after 10 years	**11,444,109**	**11,317,665**
Equities	**15,608,468**	**20,105,461**
	$ 88,371,375	**$ 92,526,114**
December 31, 2016		
Available for sale:		
Due within one year	$ 3,894,116	$ 3,840,782
Due after one year through five years	24,396,677	24,279,727
Due after five years through ten years	18,187,406	18,124,252
Due after 10 years	22,217,145	21,917,210
Equities	16,191,391	18,401,494
	$ 84,886,735	$ 86,563,466

North Carolina Railroad Company
Notes to Consolidated Financial Statements

4. Trackage Rights Agreement and Leases on Roadway and Land

Prior to 1999, substantially all of the Company's assets were leased to NSR or its predecessors in two leases originally dating back to 1895 and 1939. The terms of the leases did not require either the Company or Norfolk Southern to renew the leases.

On August 10, 1999, the Board of Directors of the Company approved a Trackage Rights Agreement ("TRA") concurrent with NSR terminating the original leases. The TRA's term is 15 years with two 15-year renewal options by NSR (45 years) for a base annual rental of $11,000,000 (minimum) beginning January 1, 2000, with annual adjustments based upon an inflation index and a 4.5% annual cap (arbitration of cap if it exceeds an average of 4.5% over any 7-year period). The TRA was approved by the Surface Transportation Board on September 1, 1999. During 2012, NSR exercised its option to renew the TRA for the 15 year period beginning January 1, 2015 and ending on December 31, 2029.

The TRA grants exclusive freight trackage rights to NSR to conduct all freight operations over the NCRR railroad line. Under federal law, the National Rail Passenger Corporation ("Amtrak") operates over NSR operated lines under agreements with NSR. NSR is obligated under the TRA to provide rail service to all industries on the NCRR line. NSR is obligated to maintain the NCRR line and any improvements made to the line by NSR for freight operations. Under the TRA, NSR does not have financial responsibility for passenger improvements made by the Company, North Carolina Department of Transportation (NCDOT), Amtrak, or other parties.

Under the TRA, approximately 38 parcels not used in railroad operations have been returned to the Company for separate (non-NSR) management. These noncorridor properties are managed by the Company after transition from NSR management. The TRA contains provisions for responsibility for environmental matters by NSR and the Company.

NSR is responsible for any taxes on its freight operations. A Policy Planning Committee comprised of NCRR and NSR representatives addresses all future planning issues, capital improvements, and any disputes that arise under the TRA. In the event of any disagreements, NCRR and NSR are subject to binding arbitration under the TRA.

A lease of certain properties in Charlotte, North Carolina to NSR (the "1968 Lease") expires on December 31, 2067, and provided for an annual rental of $81,319 through December 2018. The 1968 Lease provides that beginning on January 1, 2019, the annual rental for the remaining term of the 1968 Lease is 6% of the appraised value of the property on that date. Under the terms of the 1968 Lease, all taxes connected with the property, except income taxes, are paid by the lessee. The 1968 Lease was not affected by the TRA. During 2016, the Company sold a portion of the property subject to the 1968 Lease. The 1968 Lease was not affected by the sale.

Pursuant to agreements signed in each year since 2008, NCRR has assigned to NSR all of the NCRR lines that constitute eligible railroad tracks solely for purposes of allowing NSR to qualify as an eligible taxpayer with respect to such track and to claim tax credits under section 45G(a) for qualified railroad track maintenance expenditures it pays or incurs during each year under agreement with respect to such track. In exchange, NSR agrees to pay to NCRR fifty percent of the tax credits NSR claims. Payment of the amount owed under the agreement is not due until the amount of the allowable credit is not subject to further appeal, review or modification through proceedings or otherwise.

The Company has recorded a long-term receivable amounting to $3,585,304, representing $3,405,500 of total tax credit revenue that the Company is due for tax years 2014 to 2017 from NSR, plus accumulated 4% interest of $179,804, as of December 31, 2017. As of December 31, 2016 the long-term receivable amounted to $3,581,545, representing $3,398,500 of total tax credit revenue that the Company was due for tax years 2011 to 2015 from NSR, plus accumulated 4% interest of 183,045.

5. Capital Commitments

Project Agreements and Contracts

As of December 31, 2017, the Company has capital commitments under various individual project agreements and other contracts totaling $51 million. The contractual commitments of the Company consist of certain capital improvement projects set forth in project agreements, other strategic and economic development investments including commitments for the purchase of certain real estate, and ARRA/PRIIA High-Speed Passenger Rail improvement projects. The ARRA/PRIIA High-Speed Passenger Rail improvement commitments are further described in more detail below. The various individual projects, capital improvements and strategic investments to which capital is committed are scheduled for completion between 2018 and 2022.

ARRA/PRIIA High-Speed Passenger Rail Projects

In 2011, the State of North Carolina was selected to receive certain federal grant awards through the American Recovery and Reinvestment Act of 2009 ("ARRA") and the Passenger Rail Investment Act of 2008 ("PRIIA") for the capital funding of certain high speed intercity passenger rail projects, under which NCDOT is the grantee of the awards. On December 15, 2010, the Company, the NCDOT, and NSR entered into an Agreement on Principles ("AOP"), which outlined certain terms for capital improvements within and along the NCRR corridor operated by NSR (Note 4). On March 21, 2011, the Company, NCDOT, NSR and Amtrak entered into a Definitive Service Outcomes Agreement ("DSOA"), clarifying the individual parties' responsibilities and further detailing the projects to be funded by the grants to NCDOT. On March 21, 2012, the Company and the NCDOT entered into a Railroad Corridor Property Acquisition Agreement ("RCPA") regarding rail corridor property, including acquisition of additional railroad corridor property needed in connection with certain projects funded by the grants to NCDOT. As of December 31, 2017, substantially all of the ARRA and PRIIA projects were completed. The Company has recorded capital contributions and related assets for a portion of the improvements made by NCDOT, in addition to the commitment of funds made by the Company described below. Any remaining ARRA and PRIIA projects will be recorded as completed in future years.

Under the AOP, DSOA, and RCPA, the Company has committed up to a total of $31,000,000 of capital investment toward certain projects in order to assist in completion of certain track capacity improvement projects and engineering. Out of its $31,000,000 commitment, the AOP and DSOA provide that the Company reserve up to $10,000,000 for a Capital Reserve Fund, which is designated by the Company for the purpose of making further capacity improvements to the NCRR line in the future in order to improve passenger and freight train reliability caused by identified unacceptable train delays. Investments by the Company under these agreements are to be applied against and reduce the Company's commitment under the agreements. Through December 31, 2017, the Company has expended approximately $5.6 million of its commitments under these agreements. The Company also has committed use of the Company's rail corridor lands for such capacity and other related improvement projects.

Board Designated Funds

The Board of Directors passed resolutions during 2017 and 2016 to designate $10,500,000 and $16,300,000, respectively, of unrestricted cash for use on future capital improvement projects.

The Company has designated the following amounts (invested in cash, certificates of deposit, debt securities and mutual funds) for capital improvement projects as follows:

	2017	2016
Restricted under contracts	**$ 50,748,153**	$ 34,961,900
Restricted for other capital improvements	**147,436**	147,436
Board designated funds	**48,752,321**	53,851,068
Investments reserved for capital projects	**$ $99,647,910**	$ 88,960,404

6. Employee Benefit Plan

The Company established a Safe Harbor 401(k) Plan effective January 1, 2012 to provide retirement benefits for its employees. All full-time employees who meet certain eligibility requirements are qualified to participate in the 401(k) Plan. Participants may make pre-tax deferrals up to 90% of their compensation subject to Internal Revenue Service limitations. Participants are fully vested in their contributions plus actual earnings thereon and any rollovers into their accounts. The Company contributes 3% of the compensation of all eligible active participants. In addition, the Company may elect each plan year whether to make a discretionary employer contribution on behalf of eligible active participants. Employer contributions for the years ended December 31, 2017 and 2016 were $142,608 and $120,481, respectively, including $81,490 and $68,846, respectively, of discretionary contributions.

In 2013 the Company entered into a deferred compensation agreement with an officer. The deferred compensation liability is fully vested at all times unless the officer is terminated for cause as defined in the plan, at which time the deferred compensation balance would be forfeited in its entirety. The plan is credited on an annual basis for employer contributions equal to a percentage of the officer's compensation plus an earnings component. The Company recognized expense of $82,178 and $52,355 related to the plan in 2017 and 2016, respectively. The resulting deferred compensation liability of $289,764 at December 31, 2017 and $207,586 at December 31, 2016, is included in other liabilities in the accompanying financial statements.

7. Future Minimum Lease Revenue

The Company derives income from leased commercial space and other property under non-cancellable operating leases. Of the non-cancellable leases, one lease, described in Note 4, comprises 85% of the lease income. Rental income received from this lease during 2017 and 2016 was approximately $15.6 million and $15.4 million, respectively. The remaining non-cancellable leases are related to the rental of commercial space. Future minimum rent receipts, excluding renewal periods, on the non-cancellable operating leases are as follows for the years ending December 31:

	Amount
2018	$ 15,497,661
2019	15,178,675
2020	15,166,017
2021	14,991,400
2022	14,963,017
Thereafter	107,600,599
	$ 183,397,369

Minimum lease receipts do not include contingent rentals that may be received under certain leases. The Company's policy is to defer recognition of such contingent rentals until the requirements are met. Contingent rental income earned during the years ended December 31, 2017 and 2016 totaled $22,224 and $58,057, respectively.

City of Charlotte Lease Agreement

The Company and the City of Charlotte ("Charlotte") entered into an agreement ("Lease Agreement") dated May 3, 2012, whereby Charlotte leased a segment of the North Carolina Railroad corridor, approximately 2.7 miles in length parallel to the Company's main line railroad tracks and facilities, for the purpose of the extension of Charlotte's LYNX Blue Line light rail transit system. The Lease Agreement provides for a one time rent payment to be paid to the Company in the amount of $11,760,000 for the 50 year lease term, all of which was received in full on October 16, 2013. The Lease Agreement provides that Charlotte is responsible for all construction, operations, maintenance, taxes, assessments and costs related to Charlotte's use of the segment.

Coincident with the execution of the Lease Agreement, Charlotte entered into a Construction and Reimbursement Agreement and an Operations Agreement with NSR related to Charlotte's use of the segment and the compatibility thereof with NSR's operation and maintenance of the Company's rail line.

The Lease Agreement provides that design and construction is to be provided by Charlotte at its expense, subject to the approval of the Company. The Lease Agreement is subject to early termination, in which event a portion of the lease fee may be refundable. The Lease Agreement contains one renewal term at a rate agreed upon by the parties, or in the absence of agreement, based upon an appraised value.

The Company has recorded an unearned rent liability of $10,757,916 and $10,979,949 at December 31, 2017 and 2016, respectively, of which $286,780 and $287,036 is included in the current portion of unearned rent at December 31, 2017 and 2016, respectively.

8. Income Taxes

The Company's income (loss) before income taxes for the years ended December 31, 2017 and 2016 is as follows:

	2017	2016
Income (loss) before income taxes:		
Nontaxable entities	**$ (9,136,707)**	$ 15,973,394
Taxable entity	**377,554**	423,032
Income (loss) before income taxes	**$ (8,759,153)**	$ 16,396,426

The difference between the federal income tax computed by the statutory federal income tax rate of 34% and NCRI's income tax expense as reflected in the consolidated financial statements is as follows:

	2017	2016
Income tax at statutory federal income tax rates	**$ 128,368**	$ 143,831
Decrease attributable to:		
State income tax, net of federal income tax benefit	**10,896**	21,637
Decrease in federal and state tax rates	**(332,000)**	(19,000)
Other	**(2,814)**	(8,313)
	$ (195,550)	$ 138,155

The Company's taxable subsidiary, NCRI, has deferred income tax balances at December 31, 2017 and 2016 as follows:

	2017	2016
Asset:		
Deferred rent	**$ 32,000**	$ 50,000
Liability:		
Property and equipment	**(608,000)**	(978,000)
Net deferred tax liability	**$ (576,000)**	$ (928,000)

The Company's total tax expense (benefit) for 2017 and 2016 is summarized as follows:

	2017	2016
Current income tax expense	**$ 156,450**	$ 253,155
Deferred income tax benefit	**(352,000)**	(115,000)
Total income tax expense (benefit)	**$ (195,550)**	$ 138,155

9. Commitments and Contingencies

The Company is subject to litigation in the ordinary course of business. Management believes that any potential liability thereto is not material to the Company's financial position and results of operations.

10. Subsequent Events

The Company evaluated the effect subsequent events would have on the consolidated financial statements through May 29, 2018, which is the date the financial statements were available to be issued.

Board of Directors and Management Team

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Cameron Kidd
Land Manager

William C. Miller
Property Manager

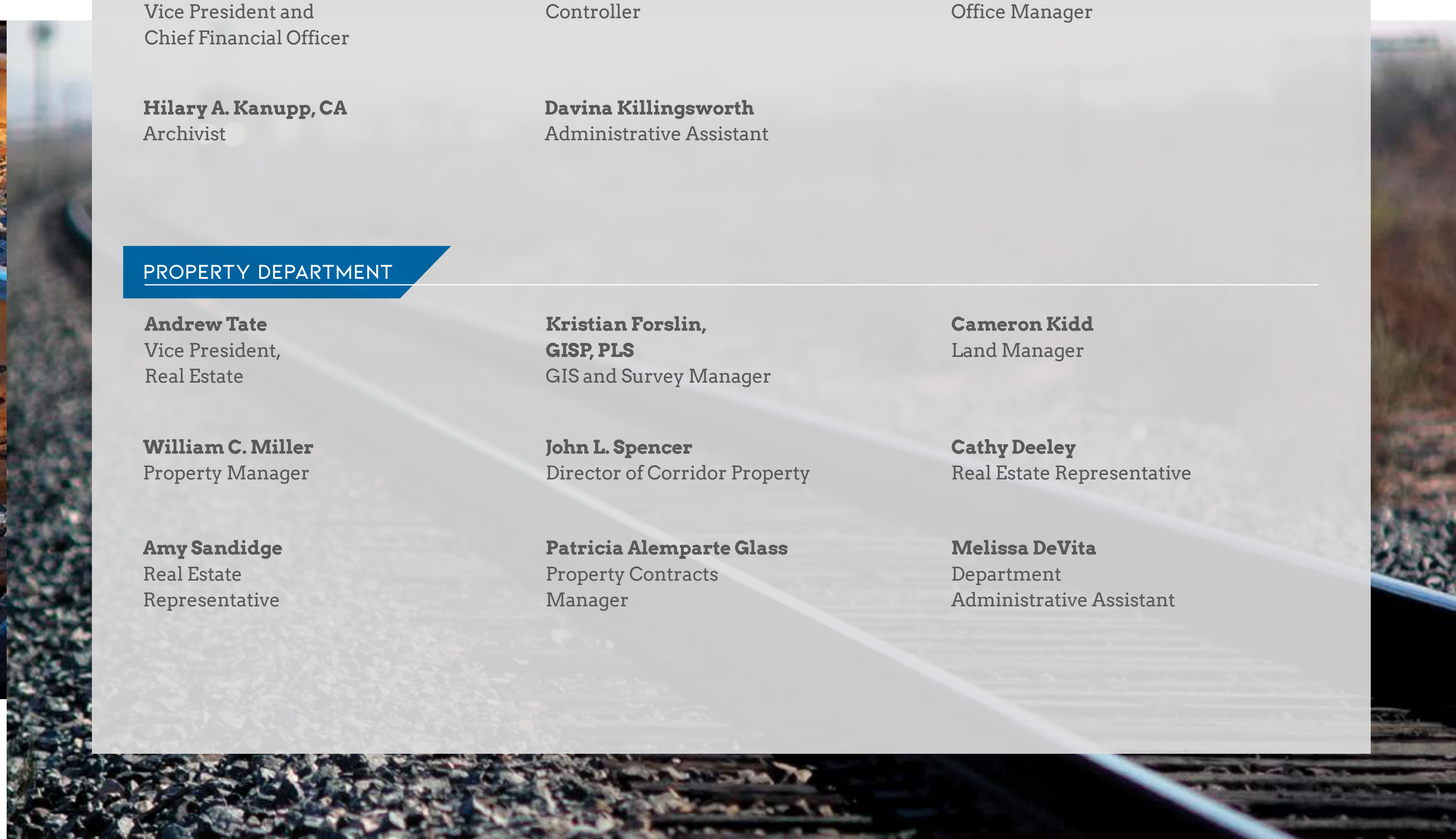
John L. Spencer
Director of Corridor Property

Cathy Deeley
Real Estate Representative

Amy Sandidge
Real Estate Representative

Patricia Alemparte Glass
Property Contracts Manager

Melissa DeVita
Department Administrative Assistant



Freight Routes

- North Carolina Railroad Company
  *Norfolk Southern Class I Freight Service
- Norfolk Southern
- CSX Transportation
- Various Shortlines

Passenger Routes

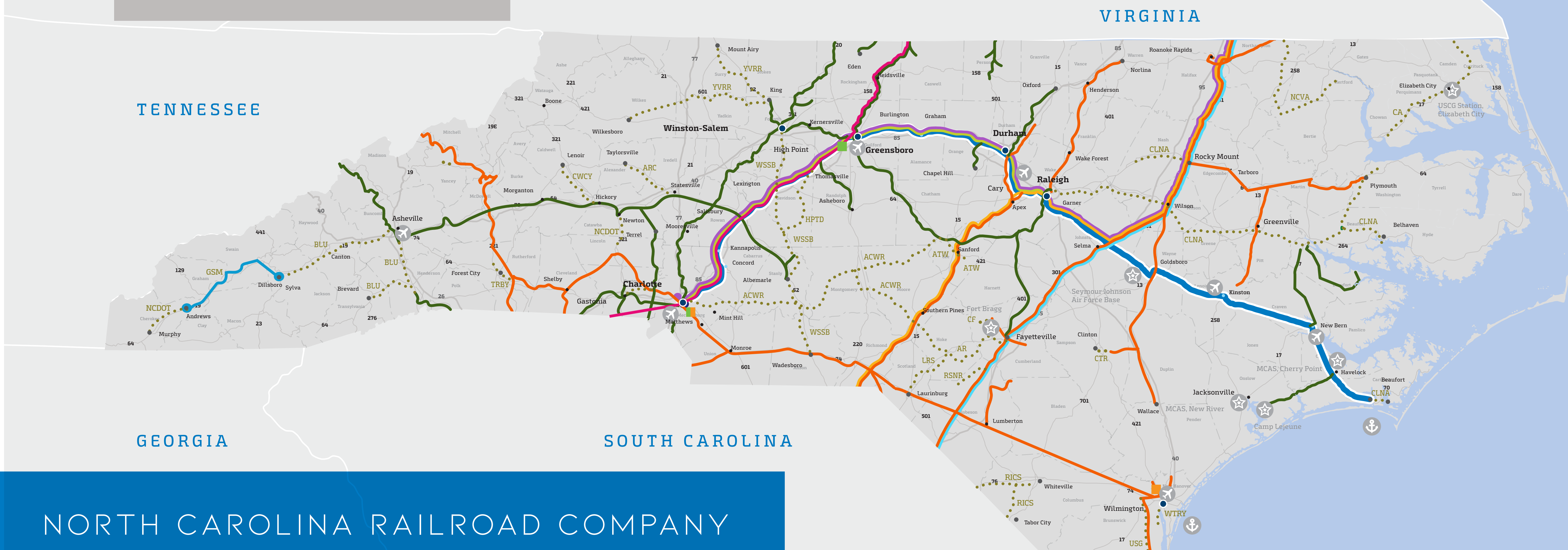
- Carolinian
- Crescent
- Piedmont
- Palmetto/Silver Meteor
- Silver Star
- Great Smoky Mountains Railroad

Intermodal Terminals

- Norfolk Southern
- CSX Transportation

Logistical Centers

- Military Bases
- Seaports
- Airports



NORTH CAROLINA RAILROAD COMPANY

Corridor Map

Putting the North Carolina Railroad Company to work for the good of the people of North Carolina.

2017

Annual Report

NORTH CAROLINA RAILROAD COMPANY

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