

CANADIAN PACIFIC RAILWAY LTD/CN
Form 6-K
April 28, 2010

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
Form 6-K
Report of Foreign Issuer
Pursuant to Rule 13a-16 or 15d-16 of
the Securities Exchange Act of 1934
For the month of April, 2010

CANADIAN PACIFIC RAILWAY LIMITED
(Commission File No. 1-01342)
CANADIAN PACIFIC RAILWAY COMPANY
(Commission File No. 1-15272)

(translation of each Registrant's name into English)

Suite 500, Gulf Canada Square, 401 9th Avenue, S.W., Calgary, Alberta, Canada, T2P 4Z4

(address of principal executive offices)

Indicate by check mark whether the registrants file or will file annual reports under cover Form 20-F or Form 40-F.
Form 20-F Form 40-F

Indicate by check mark if the registrants are submitting the Form 6-K in paper as permitted by Regulation S-T Rule 101(b)(1):

Indicate by check mark if the registrants are submitting the Form 6-K in paper as permitted by Regulation S-T Rule 101(b)(7):

Indicate by check mark whether the registrants by furnishing the information contained in this Form are also thereby furnishing the information to the Commission pursuant to Rule 12g3-2(b) under the Securities Exchange Act of 1934.

Yes No

If Yes is marked, indicate below the file number assigned to the registrant in connection with Rule 12g3-2(b): 82-

This Report furnished on Form 6-K shall be incorporated by reference into each of the following Registration Statements under the Securities Act of 1933 of the registrant: Form S-8 No. 333-140955 (Canadian Pacific Railway Limited), Form S-8 No. 333-127943 (Canadian Pacific Railway Limited) and Form S-8 No. 333-13962 (Canadian Pacific Railway Limited).

SIGNATURES

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

CANADIAN PACIFIC RAILWAY LIMITED
(Registrant)

Date: April 28, 2010

Signed: Karen L. Fleming

By: Name: Karen L. Fleming
Title: Corporate Secretary

CANADIAN PACIFIC RAILWAY COMPANY
(Registrant)

Date: April 28, 2010

Signed: Karen L. Fleming

By: Name: Karen L. Fleming
Title: Corporate Secretary

Release: Immediate, April 28, 2010

CANADIAN PACIFIC ANNOUNCES FIRST QUARTER RESULTS

CALGARY Canadian Pacific Railway Limited (TSX/NYSE: CP) announced its first-quarter results today. Net income in the first-quarter was \$100 million, an increase of 74 per cent from \$57 million in first-quarter 2009 and diluted earnings per share were \$0.59, up from \$0.36 in first-quarter 2009.

We put in a solid performance this quarter and our results reflect both improvements in the economy and CP's proven ability to rapidly adjust to changes in our customers' demands, said Fred Green, President and CEO. Our ongoing commitment to service reliability, safety and managing our productivity objectives will continue to drive shareholder value.

FIRST-QUARTER 2010 COMPARED WITH FIRST-QUARTER 2009:

Total revenues were \$1.2 billion, up five per cent from \$1.1 billion

Operating expenses were \$962 million, down two per cent from \$977 million

Operating income increased to \$205 million from \$132 million, or 55 per cent

Operating ratio improved 570 basis points to 82.4 per cent

Diluted earnings per share increased to \$0.59 from \$0.36, or 64 per cent

Adjusted diluted earnings per share increased to \$0.60 from \$0.32, or 88 per cent

Presentation of non-GAAP earnings

Diluted earnings per share, excluding foreign exchange gains and losses on long-term debt and other specified items, is also referred to in this news release as adjusted diluted earnings per share.

CP presents non-GAAP earnings measures in this news release to provide an additional basis for evaluating underlying earnings and liquidity trends in its business that can be compared with prior periods' results of operations. When foreign exchange gains and losses on long-term debt and other specified items are excluded from diluted earnings per share, income and income tax expense, these become non-GAAP measures. Capital program is a non-GAAP measure.

These non-GAAP earnings measures exclude foreign currency translation effects on long-term debt and the tax thereon, which can be volatile and short term. The impact of volatile short-term exchange rate fluctuations on foreign-denominated debt is only realized when long-term debt matures or is settled. In addition, these non-GAAP measures exclude other specified items (described below) that are not a part of CP's normal ongoing revenues and operating expenses. A reconciliation of income, excluding foreign exchange gains and losses on long-term debt and other specified items, to net income as presented in the financial statements is detailed in the attached Summary of Rail Data.

Other specified items are material transactions that may include, but are not limited to, restructuring and asset impairment charges, gains and losses on non-routine sales of assets, unusual income tax adjustments, and other items that do not typify normal business activities.

The non-GAAP earnings measures described in this news release have no standardized meanings and are not defined by accounting principles generally accepted in the United States and, therefore, are unlikely to be comparable to similar measures presented by other companies.

FOREIGN EXCHANGE GAIN AND LOSS ON LONG-TERM DEBT AND OTHER SPECIFIED ITEMS

CP had a net foreign exchange loss after tax of \$3 million on long-term debt in the first quarter of 2010, compared with a gain of \$7 million after tax in first-quarter 2009.

As part of a consolidated financing strategy, CP structures its U.S. dollar long-term debt in different taxing jurisdictions. As well, a portion of this debt is designated as a net investment hedge against the net investment in foreign subsidiaries. Although the taxes on foreign exchange gains and losses on long-term debt generally offset one another, because they may be in different tax jurisdictions, the resulting net tax can vary significantly.

Other specified items in the first quarter of 2010 include an increase to the estimated fair value of the investment in Long-Term Floating Rate Notes of \$1.0 million (\$0.9 million after tax). There were no similar other specified items in the first quarter of 2009.

CP began reporting its financial results in accordance with U.S. GAAP as at January 1, 2010. All prior period comparative numbers contained in this release are to U.S. GAAP. Additional historical U.S. GAAP financial reports can be found at www.cpr.ca.

Note on forward-looking information

This news release contains certain forward-looking statements relating but not limited to our operations, pension obligations and tax rates. Undue reliance should not be placed on forward-looking information as actual results may differ materially.

By its nature, CP's forward-looking information involves numerous assumptions, inherent risks and uncertainties, including, but not limited to, the following factors: changes in business strategies; general North American and global economic, credit and business conditions; risks in agricultural production such as weather conditions and insect populations; the availability and price of energy commodities; the effects of competition and pricing pressures; industry capacity; shifts in market demand; changes in laws and regulations, including regulation of rates; changes in taxes and tax rates; potential increases in maintenance and operating costs; uncertainties of litigation; labour disputes; risks and liabilities arising from derailments; transportation of dangerous goods, timing of completion of capital and maintenance projects; currency and interest rate fluctuations; effects of changes in market conditions and discount rates on the financial position of pension plans and investments; and various events that could disrupt operations, including severe weather conditions, security threats and governmental response to them, and technological changes. There are factors that could cause actual results to differ from those described in the forward-looking statements contained in this news release. These more specific factors are identified and discussed elsewhere in this news release with the particular forward-looking statement in question.

Except as required by law, CP undertakes no obligation to update publicly or otherwise revise any forward-looking information, whether as a result of new information, future events or otherwise.

About Canadian Pacific:

Canadian Pacific, through the ingenuity of its employees located across Canada and in the United States, remains committed to being the safest, most fluid railway in North America. Our people

are the key to delivering innovative transportation solutions to our customers and to ensuring the safe operation of our trains through the more than 1,100 communities where we operate. Come and visit us at www.cpr.ca to see how we can put our ingenuity to work for you.

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CANADIAN PACIFIC RAILWAY LIMITED
CONSOLIDATED STATEMENT OF INCOME
(in millions of Canadian dollars, except per share data)
(unaudited)

	For the three months ended March 31	
	2010	2009
Revenues		
Freight	\$ 1,138.2	\$ 1,076.0
Other	28.6	33.6
	1,166.8	1,109.6
Operating expenses		
Compensation and benefits	353.5	342.9
Fuel	181.7	171.0
Materials	63.9	76.6
Equipment rents	49.0	66.4
Depreciation and amortization	125.0	119.7
Purchased services and other	188.7	200.8
	961.8	977.4
Operating income	205.0	132.2
Less:		
Other income and charges	(4.9)	8.5
Interest expense	66.7	71.6
Income before income tax expense	143.2	52.1
Income tax expense (recovery) <i>(Note 4)</i>	43.4	(5.2)
Net income	\$ 99.8	\$ 57.3
Earnings per share <i>(Note 5)</i>		
Basic earnings per share	\$ 0.59	\$ 0.36
Diluted earnings per share	\$ 0.59	\$ 0.36
Weighted average number of shares (millions)		

Basic	168.5	160.9
Diluted	169.1	161.2
Dividends declared per share	\$ 0.2475	\$ 0.2475
See notes to Consolidated Financial Statements.		

CANADIAN PACIFIC RAILWAY LIMITED
CONSOLIDATED BALANCE SHEET
(in millions of Canadian dollars)
(unaudited)

	March 31 2010	December 31 2009
<i>Assets</i>		
Current assets		
Cash and cash equivalents	\$ 723.8	\$ 679.1
Accounts receivable, net	705.8	655.1
Materials and supplies	122.7	132.7
Deferred income taxes	133.6	128.1
Other current assets	57.6	46.5
	1,743.5	1,641.5
Investments	160.5	156.7
Net properties	11,902.6	12,067.5
Goodwill and intangible assets	195.1	202.3
Other assets	172.6	175.8
Total assets	\$14,174.3	\$ 14,243.8
<i>Liabilities and shareholders equity</i>		
Current liabilities		
Accounts payable and accrued liabilities	\$ 900.6	\$ 927.1
Income and other taxes payable	40.3	31.9
Dividends payable	41.7	41.7
Long-term debt maturing within one year	611.9	605.3
	1,594.5	1,606.0
Pension and other benefit liabilities	1,417.7	1,453.9
Other long-term liabilities	477.3	479.9
Long-term debt	4,023.3	4,138.2
Deferred income taxes	1,869.0	1,845.0
Total liabilities	9,381.8	9,523.0
Shareholders equity		
Share capital	1,775.9	1,771.1
Additional paid-in capital	29.5	30.8
Accumulated other comprehensive loss	(1,736.2)	(1,746.3)
Retained earnings	4,723.3	4,665.2

	4,792.5	4,720.8
<i>Total liabilities and shareholders equity</i>	\$14,174.3	\$ 14,243.8

Commitments and contingencies (*Note 10*)
See notes to Consolidated Financial Statements.

CANADIAN PACIFIC RAILWAY LIMITED
CONSOLIDATED STATEMENT OF CASH FLOWS
(in millions of Canadian dollars)
(unaudited)

	For the three months ended March 31	
	2010	2009
Operating activities		
Net income	\$ 99.8	\$ 57.3
Reconciliation of net income to cash provided by operating activities:		
Depreciation and amortization	125.0	119.7
Deferred income taxes (<i>Note 4</i>)	41.1	(10.4)
Foreign exchange (gain) loss on long-term debt	(4.1)	2.4
Restructuring and environmental payments	(5.6)	(8.5)
Pension funding in excess of expense	(9.3)	(15.3)
Other operating activities, net	21.6	1.9
Change in non-cash working capital balances related to operations	(82.0)	(11.9)
Cash provided by operating activities	186.5	135.2
Investing activities		
Additions to properties	(93.0)	(123.1)
Proceeds from the sale of properties and other assets	9.0	8.0
Cash used in investing activities	(84.0)	(115.1)
Financing activities		
Dividends paid	(41.7)	(38.0)
Issuance of CP Common Shares	3.0	495.8
Net decrease in short-term borrowing		(18.1)
Repayment of long-term debt	(9.1)	(13.2)
Cash (used in) provided by financing activities	(47.8)	426.5
Effect of foreign currency fluctuations on U.S. dollar-denominated cash and cash equivalents	(10.0)	2.4
Cash position		
Increase in cash and cash equivalents	44.7	449.0
Cash and cash equivalents at beginning of period	679.1	117.5
Cash and cash equivalents at end of period	\$723.8	\$ 566.5
Supplemental disclosures of cash flow information:		
Income taxes paid	\$ 1.9	\$ 3.3

Interest paid	\$ 45.1	\$ 58.6
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See notes to Consolidated Financial Statements.

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CANADIAN PACIFIC RAILWAY LIMITED
CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS EQUITY
(in millions of Canadian dollars, except common share amounts)
(unaudited)

	Common shares (in millions)	Share capital	Additional paid-in capital	Accumulated other comprehensive loss	Retained earnings	Total shareholders equity
Balance at December 31, 2009	168.5	\$ 1,771.1	\$ 30.8	\$ (1,746.3)	\$ 4,665.2	\$ 4,720.8
Net income					99.8	99.8
Other comprehensive income				10.1		10.1
Comprehensive income				10.1	99.8	109.9
Dividends declared					(41.7)	(41.7)
Stock compensation expense			0.4			0.4
Shares issued under stock option plans	0.1	4.8	(1.7)			3.1
Balance at March 31, 2010	168.6	\$ 1,775.9	\$ 29.5	\$ (1,736.2)	\$ 4,723.3	\$ 4,792.5

See notes to Consolidated Financial Statements.

CANADIAN PACIFIC RAILWAY LIMITED
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2010

(unaudited)

1 Basis of presentation

These unaudited consolidated financial statements of Canadian Pacific Railway Limited (CP , the Company or Canadian Pacific Railway) reflect management 's estimates and assumptions that are necessary for their fair presentation in conformity with accounting principles generally accepted in the United States (GAAP). They do not include all disclosures required under GAAP for annual financial statements and should be read in conjunction with the 2009 U.S. GAAP consolidated financial statements. The policies used are consistent with the policies used in preparing the 2009 U.S. GAAP consolidated financial statements, except as discussed in Note 2. The Company 's investments in which CP has significant influence, which are not consolidated, are accounted for using the equity method.

CP 's operations can be affected by seasonal fluctuations such as changes in customer demand and weather-related issues. This seasonality could impact quarter-over-quarter comparisons. The 2009 global recession has affected financial results such that seasonal fluctuations may not be consistent with those in prior years. The timing of a return to seasonal trends consistent with prior years will depend on the recovery of the economy and the Company 's customers.

2 Accounting changes

Consolidations

In June 2009, the Financial Accounting Standards Board (FASB) issued Amendments to Consolidation of Variable Interest Entities. The guidance retains the scope of the previous guidance with the addition of entities previously considered qualifying special purpose entities. In addition, it replaces the previous quantitative approach with a qualitative analysis approach for determining whether the enterprise 's variable interest or interests give it a controlling financial interest in a variable interest entity. The guidance is further amended to require ongoing reassessments of whether an enterprise is the primary beneficiary of a variable interest entity and requires enhanced disclosures about an enterprise 's involvement in a variable interest entity. The guidance is applicable to all variable interest entities that existed at January 1, 2010, the date of adoption, or are created thereafter. The Company has variable interests in variable interest entities, however, the adoption of the new guidance did not change the previous assessment that the Company is not the primary beneficiary and as such does not consolidate the variable interest entities. Additional note disclosure regarding the nature of the Company 's variable interests and where judgment was required to assess the primary beneficiary of these variable interest entities has been provided in Note 9.

Accounting for transfers of financial assets

The FASB has released additional guidance with respect to the accounting and disclosure of transfers of financial assets such as securitized accounts receivable. Although the Company currently does not have an accounts receivable securitization program, the guidance, which includes revisions to the derecognition criteria in a transfer and the treatment of qualifying special purpose entities, would be applicable to any future securitization. The new guidance is effective for the Company from January 1, 2010. The adoption of this guidance had no impact to the Company 's financial statements.

Fair value measurement and disclosure

In January 2010, the FASB amended the disclosure requirements related to fair value measurements. The update provides for new disclosures regarding transfers in and out of Level 1 and Level 2 financial asset and liability categories and expanded disclosures in the Level 3 reconciliation. The update also provides clarification that the level of disaggregation should be at the class level and that disclosures about inputs and valuation techniques are required for both recurring and nonrecurring fair value measurements that fall in either Level 2 or Level 3. New disclosures and clarifications of existing disclosures are effective for interim and annual reporting periods beginning after December 15, 2009, except for the expanded disclosures in the Level 3 reconciliation, which are effective for fiscal years beginning after December 15, 2010. The Company has adopted this guidance resulting in expanded note disclosure (Note 6).

3 Future accounting changes

There have been no new accounting pronouncements issued that are expected to have a significant impact to the Company's financial statements.

CANADIAN PACIFIC RAILWAY LIMITED
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2010

(unaudited)

4 Income taxes

(in millions of Canadian dollars)	For the three months ended March 31	
	2010	2009
Current income tax expense	\$ 2.3	\$ 5.2
Deferred income tax expense (recovery)	41.1	(10.4)
Income tax expense (recovery)	\$43.4	\$ (5.2)

During the first quarter of 2009, legislation was enacted to reduce British Columbia provincial income tax rates. As a result, the Company recorded a \$6.2 million income tax benefit related to the revaluation of its deferred income tax balances as at December 31, 2008. In addition, during the first quarter of 2009 the Company had non-taxable foreign exchange gains which reduced expected income tax expense by approximately \$8 million. In the first quarter of 2010, non-taxable foreign exchange losses increased expected income tax expense by approximately \$6 million.

5 Earnings per share

At March 31, 2010, the number of shares outstanding was 168.6 million (March 31, 2009 168.0 million).

Basic earnings per share have been calculated using net income for the period divided by the weighted average number of Canadian Pacific Railway Limited shares outstanding during the period.

Diluted earnings per share have been calculated using the treasury stock method, which assumes that any proceeds received from the exercise of in-the-money options would be used to purchase Common Shares at the average market price for the period.

The number of shares used in earnings per share calculations is reconciled as follows:

(in millions)	For the three months ended March 31	
	2010	2009
Weighted average shares outstanding	168.5	160.9
Dilutive effect of stock options	0.6	0.3
Weighted average diluted shares outstanding	169.1	161.2

For the three months ended March 31, 2010, 2,529,642 options were excluded from the computation of diluted earnings per share because their effects were not dilutive (three months ended March 31, 2009 3,393,217).

CANADIAN PACIFIC RAILWAY LIMITED
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2010

(unaudited)

6 Financial instruments

A. Fair values of financial instruments

The Company categorizes its financial assets and liabilities measured at fair value into one of three different levels depending on the observability of the inputs employed in the measurement.

Level 1: Unadjusted quoted prices for identical assets and liabilities in active markets that are accessible at the measurement date.

Level 2: Directly or indirectly observable inputs other than quoted prices included within Level 1 or quoted prices for similar assets and liabilities. Derivative instruments in this category are valued using models or other industry standard valuation techniques derived from observable market data.

Level 3: Valuations based on inputs which are less observable, unavailable or where the observable data does not support a significant portion of the instruments' fair value. Generally, Level 3 valuations are longer dated transactions, occur in less active markets, occur at locations where pricing information is not available, or have no binding broker quote to support Level 2 classifications.

When possible the estimated fair value is based on quoted market prices and, if not available, estimates from third party brokers. For non exchange traded derivatives classified in Level 2, the Company uses standard valuation techniques to calculate fair value. These methods include discounted mark to market for forwards, futures and swaps. Primary inputs to these techniques include observable market prices (interest, foreign exchange and commodity) and volatility, depending on the type of derivative and nature of the underlying risk. The Company uses inputs and data used by willing market participants when valuing derivatives and considers its own credit default swap spread as well as those of its counterparties in its determination of fair value. Wherever possible the Company uses observable inputs. All derivatives are classified as Level 2. A detailed analysis of the techniques used to value long-term floating rate notes, which are classified as Level 3, is discussed below.

Gain/loss in fair value of long-term floating rate notes

At March 31, 2010 and December 31, 2009, the Company held long-term floating rate notes with a total settlement value of \$129.0 million and \$129.1 million, respectively, and carrying values of \$71.8 million and \$69.3 million, respectively. The carrying values, being the estimated fair values, are reported in Investments .

The Company received the long-term floating rate notes as part of a Canadian Court sanctioned restructuring plan completed on January 21, 2009. The notes were in replacement for previously held Canadian third-party asset backed commercial paper (ABCP).

During the first quarter of 2010 the Company received \$0.1 million in partial redemption, at par, of certain of the notes held. At March 31, 2010 the Company held long-term floating rate notes with settlement value, as follows:

\$116.7 million Master Asset Vehicle (MAV) 2 notes with eligible assets;

\$12.1 million MAV 2 Ineligible Asset (IA) Tracking notes; and

\$0.2 million MAV 3 Class 9 Traditional Asset (TA) Tracking notes.

The valuation technique used by the Company to estimate the fair value of its investment in long-term floating rate notes at March 31, 2010 and December 31, 2009, incorporates probability weighted discounted cash flows considering the best available public information regarding market conditions and other factors that a market participant would consider for such investments. The above noted redemption of notes, accretion and other minor changes in assumptions have resulted in a gain of \$2.5 million in the first quarter of 2010 (first quarter 2009 no gain or loss). The interest rates and maturities of the various long-term floating rate notes, discount rates and credit losses modelled at March 31, 2010 and December 31, 2009, respectively, are:

CANADIAN PACIFIC RAILWAY LIMITED
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2010

(unaudited)

6 Financial instruments (continued)

	March 31, 2010	December 31, 2009
Probability weighted average coupon interest rate	0.1%	Nil
Weighted average discount rate	7.6%	7.9%
Expected repayments of long-term floating rate notes	Three to 19 years	Three and a half to 19 years
Credit losses	MAV 2 eligible asset notes: nil to 100%	MAV 2 eligible asset notes: nil to 100%
	MAV 2 IA Tracking notes: 25%	MAV 2 IA Tracking notes: 25%
	MAV 3 Class 9 TA Tracking notes: nil	MAV 3 Class 9 TA Tracking notes: nil

The probability weighted discounted cash flows resulted in an estimated fair value of the Company's long-term floating rate notes of \$71.8 million at March 31, 2010 (December 31, 2009 \$69.3 million). The change in the original cost and estimated fair value of the Company's long-term floating rate notes is as follows (representing a roll-forward of assets measured at fair value using Level 3 inputs):

(in millions of Canadian dollars)	Original cost	Estimated fair value
As at January 1, 2010	\$ 129.1	\$ 69.3
Redemption of notes	(0.1)	
Accretion		1.5
Change in market assumptions		1.0
As at March 31, 2010	\$ 129.0	\$ 71.8

Accretion and gains and losses from the redemption of notes and change in market assumptions are reported in Other income and charges .

CANADIAN PACIFIC RAILWAY LIMITED
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2010

(unaudited)

6 Financial instruments (continued)

B. Financial risk management

The Company's policy with respect to using derivative financial instruments is to selectively reduce volatility associated with fluctuations in interest rates, foreign exchange (FX) rates, the price of fuel and stock-based compensation expense. Where derivatives are designated as hedging instruments, the relationship between the hedging instruments and their associated hedged items is documented, as well as the risk management objective and strategy for the use of the hedging instruments. This documentation includes linking the derivatives that are designated as fair value or cash flow hedges to specific assets or liabilities on the Consolidated Balance Sheet, commitments or forecasted transactions. At the time a derivative contract is entered into, and at least quarterly thereafter, an assessment is made whether the derivative item is effective in offsetting the changes in fair value or cash flows of the hedged items. The derivative qualifies for hedge accounting treatment if it is effective in substantially mitigating the risk it was designed to address.

Financial derivatives or commodity instruments are used to mitigate financial risk and are not for trading or speculative purposes.

Foreign exchange management

The Company is exposed to fluctuations of financial commitments, assets, liabilities, income or cash flows due to changes in FX rates. The Company conducts business transactions and owns assets in Canada, the United States and other countries; as a result, revenues and expenses are incurred in both Canadian and U.S. dollars. The Company enters into foreign exchange risk management transactions primarily to manage fluctuations in the exchange rate between Canadian and U.S. currencies. In terms of net income, excluding FX on long-term debt, mitigation of U.S. dollar FX exposure is provided primarily through offsets created by revenues and expenses incurred in the same currency.

The FX gains and losses on long-term debt are mainly unrealized and can only be realized when U.S. dollar denominated long-term debt matures or is settled. The Company also has long-term FX exposure on its investment in U.S. affiliates. A portion of the Company's U.S. dollar denominated long-term debt has been designated as a hedge of the net investment in foreign subsidiaries. This designation has the effect of mitigating volatility on net income by offsetting long-term FX gains and losses on long-term debt against gains and losses on its net investment. In addition, the Company may enter into FX forward contracts to lock in the amount of Canadian dollars it has to pay on its U.S. denominated debt maturities.

Occasionally the Company will enter into short-term FX forward contracts as part of its cash management strategy.

Foreign exchange forward contracts

In 2007, the Company entered into a FX forward contract to fix the exchange rate on US\$400 million 6.250% Notes due 2011. This derivative guaranteed the amount of Canadian dollars that the Company will repay when its US\$400 million 6.250% Notes mature in October 2011. This derivative is not designated as a hedge and changes in fair value are recognized in net income in the period in which the change occurs. During the three months ended March 31, 2009, CP unwound US\$25 million of the US\$400 million for total proceeds of \$4.5 million, which was settled in the second quarter of 2009. During the remainder of 2009, CP unwound a further US\$305 million for total proceeds of \$29.6 million.

During the three months ended March 31, 2010, the Company recorded an unrealized foreign exchange loss on long-term debt of \$1.9 million to Other income and charges related to the currency forward. For the same period in 2009, the Company recorded a net gain of \$14.1 million, which was inclusive of both realized and unrealized gains.

At March 31, 2010, the unrealized loss of \$1.7 million on the remaining FX forward of US\$70 million was included in Other long-term liabilities. At December 31, 2009, the unrealized gain on the remaining FX forward of \$0.2 million was included in Other assets.

CANADIAN PACIFIC RAILWAY LIMITED
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2010

(unaudited)

6 Financial instruments (continued)

Interest rate management

The Company is exposed to interest rate risk, which is the risk that the fair value or future cash flows of a financial instrument will vary as a result of changes in market interest rates. In order to manage funding needs or capital structure goals, the Company enters into debt or capital lease agreements that are subject to either fixed market interest rates set at the time of issue or floating rates determined by on-going market conditions. Debt subject to variable interest rates exposes the Company to variability in interest expense, while debt subject to fixed interest rates exposes the Company to variability in the fair value of debt.

To manage interest rate exposure, the Company accesses diverse sources of financing and manages borrowings in line with a targeted range of capital structure, debt ratings, liquidity needs, maturity schedule, and currency and interest rate profiles. In anticipation of future debt issuances, the Company may enter into forward rate agreements such as treasury rate locks, bond forwards or forward starting swaps, designated as cash flow hedges, to substantially lock in all or a portion of the effective future interest expense. The Company may also enter into swap agreements to manage the mix of fixed and floating rate debt. The Company does not currently hold any derivative financial instruments to manage its interest rate risk.

Interest rate swaps

During the three months ended March 31, 2010 the Company amortized \$1.1 million of a deferred gain to Interest expense relating to an interest rate swap previously unwound.

Prior to the unwind, accounting for the associated debt at the floating interest rate decreased Interest expense by \$1.4 million for the three months ended March 31, 2009.

At March 31, 2010 and December 31, 2009, the Company had no outstanding interest rate swaps.

Treasury rate locks

At March 31, 2010, the Company had net unamortized losses related to interest rate locks settled in previous years totalling \$24.0 million (December 31, 2009 \$23.9 million), which are reflected in Accumulated other comprehensive loss. This amount is composed of various unamortized gains and losses related to specific debts. These unamortized gains and losses are amortized to Interest expense in the period that interest on the related debt is charged. The amortization of these gains and losses resulted in a decrease in Interest expense and Other comprehensive income of \$0.1 million for the three months ended March 31, 2010 (three months ended March 31, 2009 \$0.1 million).

CANADIAN PACIFIC RAILWAY LIMITED
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2010

(unaudited)

6 Financial instruments (continued)

Stock-based compensation expense management

The Company is exposed to stock-based compensation risk, which is the probability of increased compensation expense due to the increase in the Company's share price.

The Company's compensation expense is subject to volatility due to the movement of CP's share price and its impact on the value of certain management and director stock-based compensation programs. These programs include tandem share appreciation rights (TSARs), deferred share units (DSUs), restricted share units (RSUs), and performance share units (PSUs). As the share price appreciates, these instruments create increased compensation expense.

The Company entered into a Total Return Swap (TRS) to reduce the volatility to the Company over time on three types of stock-based compensation programs: TSARs, DSUs and RSUs. The TRS is a derivative that provides price appreciation and dividends, in return for a charge by the counterparty. The swaps were intended to minimize volatility to Compensation and benefits expense by providing a gain to offset increased compensation expense as the share price increased and a loss to offset reduced compensation expense when the share price falls. If stock-based compensation share units fall out of the money after entering the program, the loss associated with the swap would no longer be fully offset by compensation expense reductions, which would reduce the effectiveness of the swap. During 2009, the Company decided not to expand its TRS program.

Compensation and benefits expense included an unrealized gain on these swaps of \$0.8 million for the three months ended March 31, 2010. For the same period in 2009, the Company recorded a net loss of \$10.7 million for the quarter, which was inclusive of both realized losses and unrealized gains. During the three months ended March 31, 2009, in order to improve the effectiveness of the TRS in mitigating the volatility of stock-based compensation programs, CP unwound a portion of the program for a total cost of \$31.1 million. This cost had previously been recognized in

Compensation and benefits expense and was settled in the second quarter of 2009. At March 31, 2010, the unrealized loss on the TRS of \$17.4 million was included in Accounts payable and accrued liabilities (December 31, 2009 \$18.2 million).

Fuel price management

The Company is exposed to potential volatility in net income due to increases or decreases in the price of diesel. Volatility in diesel fuel prices can have a significant impact on the Company's income.

The impact of variable fuel expense is mitigated substantially through fuel cost recovery programs. While these programs provide effective and meaningful coverage, residual exposure remains as the fuel expense risk cannot be completely recovered from shippers due to timing and volatility in the market. The Company continually monitors residual exposure, and where appropriate, may enter into derivative instruments.

Derivative instruments used by the Company to manage fuel expense risk may include, but are not limited to, swaps and options for crude oil and diesel. In addition, the Company may combine FX forward contracts with fuel derivatives to effectively hedge the risk associated with FX variability on fuel purchases and commodity hedges.

At March 31, 2010, the Company had diesel futures contracts, which are accounted for as cash flow hedges, to purchase approximately 13.5 million US gallons during the period April 2010 to March 2011 at an average price of US\$2.05 per US gallon. This represents approximately 5% of estimated fuel purchases for this period. At March 31, 2010, the unrealized gain on these futures contracts was \$2.8 million (December 31, 2009 \$2.5 million) and was reflected in Other current assets with the offset, net of tax, reflected in Accumulated other comprehensive loss. At March 31, 2010 and December 31, 2009, the Company had no remaining crude futures and associated FX forward contracts.

During the three months ended March 31, 2010, the impact of settled commodity swaps benefited Fuel expense by \$0.9 million as a result of realized gains on diesel swaps. For the same period in 2009, the net impact of settled commodity swaps increased Fuel expense in the quarter by \$5.7 million as a result of realized losses on diesel swaps, offset in part by gains on West Texas Intermediate (WTI) swaps.

CANADIAN PACIFIC RAILWAY LIMITED
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6 Financial instruments (continued)

The following table summarizes information on the location and amounts of gains and losses, before tax, related to derivatives on the Consolidated Statement of Income and in comprehensive income for the three months ended March 31, 2010 and 2009:

	Location of gain (loss) recognized in income on derivatives	Amount of gain (loss) recognized in income on derivatives For the three months ended March 31		Amount of gain (loss) recognized in other comprehensive income on derivatives For the three months ended March 31	
		2010	2009	2010	2009
(in millions of Canadian dollars)					
Derivatives designated as hedging instruments					
<i>Effective portion</i>					
Crude oil swaps	Fuel expense	\$	\$ 0.2	\$	\$(0.6)
Diesel future contracts	Fuel expense	0.9	(5.9)	0.3	4.4
FX contracts on fuel	Fuel expense				0.2
Interest rate swap	Interest expense	1.1	1.4		
Treasury rate locks	Interest expense	0.1	0.1	(0.1)	(0.1)
Derivatives not designated as hedging instruments					
Total return swap	Compensation and benefits	0.8	(10.7)		
FX forward contracts	Other income and charges	(1.9)	14.1		
		\$ 1.0	\$ (0.8)	\$ 0.2	\$ 3.9

At March 31, 2010, the Company expected that, during the next 12 months, \$2.8 million of unrealized holding gains on diesel future contracts will be realized and recognized in the consolidated statement of income, reported in Fuel expense as a result of these derivatives being settled.

The following table summarizes information on the effective and ineffective portions, before tax, of the Company's net investment hedge on the Consolidated Statement of Income and in comprehensive income for the three months ended March 31, 2010 and 2009:

	Location of ineffective	Effective portion recognized in other comprehensive	
		Ineffective portion	

	portion recognized in income	recognized in income		income	
		For the three months ended March 31		For the three months ended March 31	
(in millions of Canadian dollars)		2010	2009	2010	2009
FX on LTD within net investment hedge	Other income and charges	\$2.0	\$(3.6)	\$50.2	\$(57.9)

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7 Stock-based compensation

At March 31, 2010, the Company had several stock-based compensation plans, including stock option plans, various cash settled liability plans and an employee stock savings plan. These plans resulted in an expense for the three months ended March 31, 2010 of \$17.9 million (three months ended March 31, 2009 recovery of \$4.0 million).

Regular options and TSARs

In the first three months of 2010, under CP's stock option plans, the Company issued 758,400 TSARs at the weighted average price of \$51.17 per share, based on the closing price on the grant date.

Pursuant to the employee plan, these TSARs may be exercised upon vesting, which is between 24 months and 36 months after the grant date, and will expire after 10 years.

Under the fair value method, the fair value of the TSARs at the grant date was \$10.6 million (2009 \$5.4 million). The weighted average fair value assumptions were approximately:

	For the three months ended March 31	
	2010	2009
Grant price	\$51.17	\$36.29
Expected life (years) ⁽¹⁾	6.25	5.00
Risk-free interest rate ⁽²⁾	2.72%	2.14%
Expected stock price volatility ⁽³⁾	30%	30%
Expected annual dividends per share ⁽⁴⁾	\$ 0.99	\$ 0.99
Weighted average fair value of TSARs granted during the period	\$14.02	\$ 7.24

(1) *Represents the period of time that awards are expected to be outstanding. Historical data on exercise behaviour was used to estimate the expected life of the option.*

(2) *Based on the implied yield available on zero-coupon government issues with an equivalent remaining term at the time of*

the grant.

- (3) *Based on the historical stock price volatility of the Company's stock over a period commensurate with the expected term of the option.*
- (4) *Determined by the current annual dividend divided by the current stock price. The Company does not employ different dividend yields throughout the year.*

Performance share unit (PSU) plan

In the first three months of 2010, the Company issued 314,820 PSUs with a grant date fair value of \$14.5 million. These units attract dividend equivalents in the form of additional units based on the dividends paid on the Company's Common Shares. PSUs vest and are settled in cash approximately three years after the grant date contingent upon CP's performance (performance factor). The fair value of PSUs are measured, both on the grant date and each subsequent quarter until settlement, using a Black-Scholes option-pricing model and a Monte Carlo simulation model. The model utilizes multiple input variables that determine the probability of satisfying the performance and market condition stipulated in the grant.

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8 Pensions and other benefits

At March 31, the elements of net periodic benefit cost for defined benefit pension plans and other benefits recognized in the quarter included the following components:

(in millions of Canadian dollars)	For the three months ended March 31			
	Pensions		Other benefits	
	2010	2009	2010	2009
Current service cost (benefits earned by employees in the period)	\$ 21.6	\$ 16.9	\$ 3.9	\$ 4.2
Interest cost on benefit obligation	116.1	120.7	7.0	7.9
Expected return on fund assets	(149.6)	(139.5)	(0.2)	(0.3)
Recognized net actuarial loss	17.8	1.9	1.3	0.9
Amortization of prior service costs	3.3	5.7	(0.4)	(0.4)
Net periodic benefit cost	\$ 9.2	\$ 5.7	\$11.6	\$12.3

9 Variable interest entities

The Company leases equipment from certain trusts, which have been determined to be variable interest entities financed by a combination of debt and equity provided by unrelated third parties. The lease agreements, which are classified as operating leases, have a fixed price purchase option which create the Company's variable interest and result in the trusts being considered variable interest entities. These fixed price purchase options are set at the estimated fair market value as determined at the inception of the lease and could provide the Company with potential gains. These options are considered variable interests, however, they are not expected to provide a significant benefit to the Company.

The Company is responsible for maintaining and operating the leased assets according to specific contractual obligations outlined in the terms of the lease agreements and industry standards. The rigor of the contractual terms of the lease agreements and industry standards are such that the Company has limited discretion over the maintenance activities associated with these assets. As such the Company concluded these terms do not provide the Company with the power to direct the activities of the variable interest entities in a way that has a significant impact on the entities economic performance.

The Company's financial exposure as a result of its involvement with the variable interest entities is equal to the fixed lease payments due to the trusts. In 2010 lease payments after tax will amount to \$9.3 million. Future minimum lease payments, before tax, of \$246 million will be payable over the next 20 years (Note 10). The Company does not guarantee the residual value of the assets to the lessor, however, it must deliver to the lessor the assets in good operating condition, subject to normal wear and tear, at the end of the lease term.

As the Company's actions and decisions do not have the most significant effect on the variable interest entities performance, and the Company's fixed purchase price option is not considered to be potentially significant to the variable interest entities, the Company is not considered to be the primary beneficiary, and does not consolidate these variable interest entities. As the leases are considered to be operating leases, the Company does not recognize any balances in the Consolidated Balance Sheet in relation to the variable interest entities.

CANADIAN PACIFIC RAILWAY LIMITED
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March 31, 2010

(unaudited)

10 Commitments and contingencies

In the normal course of its operations, the Company becomes involved in various legal actions, including claims relating to injuries and damages to property. The Company maintains provisions it considers to be adequate for such actions. While the final outcome with respect to actions outstanding or pending at March 31, 2010, cannot be predicted with certainty, it is the opinion of management that their resolution will not have a material adverse effect on the Company's financial position or results of operations.

At March 31, 2010, the Company had committed to total future capital expenditures amounting to \$195.4 million and operating expenditures amounting to \$1,722.1 million for the years 2010-2028.

Operating lease commitments

At March 31, 2010, minimum payments under operating leases were estimated at \$881.3 million in aggregate, with annual payments in each of the next five years of: balance of 2010 \$105.4 million; 2011 \$127.8 million; 2012 \$117.3 million; 2013 \$103.3 million; 2014 \$77.2 million.

Environmental remediation accruals

Environmental remediation accruals cover site-specific remediation programs. Environmental remediation accruals are measured on an undiscounted basis and are recorded when the costs to remediate are probable and reasonably estimable. The estimate of the probable costs to be incurred in the remediation of properties contaminated by past railway use reflects the nature of contamination at individual sites according to typical activities and scale of operations conducted. CP has developed remediation strategies for each property based on the nature and extent of the contamination, as well as the location of the property and surrounding areas that may be adversely affected by the presence of contaminants, considering available technologies, treatment and disposal facilities and the acceptability of site-specific plans based on the local regulatory environment. Site-specific plans range from containment and risk management of the contaminants through to the removal and treatment of the contaminants and affected soils and ground water. The details of the estimates reflect the environmental liability at each property. Provisions for environmental remediation costs are recorded in *Other long-term liabilities*, except for the current portion which is recorded in *Accounts payable and accrued liabilities*. Payments are expected to be made over 10 years to 2020.

The accruals for environmental remediation represent CP's best estimate of its probable future obligation and includes both asserted and unasserted claims, without reduction for anticipated recoveries from third parties. Although the recorded accruals include CP's best estimate of all probable costs, CP's total environmental remediation costs cannot be predicted with certainty. Accruals for environmental remediation may change from time to time as new information about previously untested sites becomes known, environmental laws and regulations evolve and advances are made in environmental remediation technology. The accruals may also vary as the courts decide legal proceedings against outside parties responsible for contamination. These potential charges, which cannot be quantified at this time, are not expected to be material to CP's financial position, but may materially affect income in the particular period in which a charge is recognized. Costs related to existing, but as yet unknown, or future contamination will be accrued in the period in which they become probable and reasonably estimable. Changes to costs are reflected as changes to *Other long-term liabilities* or *Accounts payable and accrued liabilities* and to *Purchased services and other* within operating expenses. The amount charged to income in the three months ended March 31, 2010 was \$1.6 million (three months ended March 31, 2009 \$1.0 million).

Guarantees

At March 31, 2010, the Company had residual value guarantees on operating lease commitments of \$163.5 million. The maximum amount that could be payable under these and all of the Company's other guarantees cannot be reasonably estimated due to the nature of certain of the guarantees. All or a portion of amounts paid under certain guarantees could be recoverable from other parties or through

insurance. The Company has accrued for all guarantees that it expects to pay. At March 31, 2010, these accruals amounted to \$9.1 million.

CANADIAN PACIFIC RAILWAY LIMITED
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2010

(unaudited)

11 Reconciliation of U.S. GAAP to Canadian GAAP

The unaudited consolidated financial statements of the Company have been prepared in accordance with U.S. GAAP. The material differences between U.S. GAAP and Canadian generally accepted accounting principles (Canadian GAAP) as they relate to the Company are explained and quantified below, along with their effect on the Company's Consolidated Statement of Income and Consolidated Balance Sheet.

- (a) **Accounting for derivative instruments and hedging:** The measurement and recognition rules for derivative instruments and hedging under Canadian GAAP, as described in Canadian Institute of Chartered Accountants (CICA) accounting standards Section 3855 Financial Instruments, Recognition and Measurement , Section 3862 Financial Instruments - Disclosures , Section 3865 Hedging , Section 1530 Comprehensive Income and Section 3251 Equity , are largely harmonized with U.S. GAAP. However, under Canadian GAAP, only the ineffective portion of a net investment hedge that represents an over hedge is recognized in income, whereas under U.S. GAAP, any ineffective portion is recognized in income immediately.
- (b) **Pensions and post-retirement benefits:** The Company is required to recognize the over or under funded status of defined benefit pension and other post-retirement benefit plans on the balance sheet under U.S. GAAP. The over or under funded status is measured as the difference between the fair value of the plan assets and the benefit obligation, being the projected benefit obligation for pension plans and the accumulated benefit obligation for other post-retirement benefit plans. In addition, any previously unrecognized actuarial gains and losses and prior service costs and credits that arise during the period will be recognized as a component of other comprehensive income (OCI), net of tax. Under Canadian GAAP the over or under funded status of defined benefit pension and post-retirement benefit plans is not recognized in the balance sheet. Canadian GAAP recognizes an asset for contributions made in excess of amounts recognized as expense in the Consolidated Statement of Income and a liability when contributions are less than amounts recognized as expense.
- Prior service costs are amortized under Canadian GAAP and U.S. GAAP. However, the period over which costs related to events before 2000 are amortized differs between Canadian GAAP and U.S. GAAP.
- (c) **Post-employment benefits:** Post-employment benefits are covered by the CICA Section 3461 Employee Future Benefits . Consistent with accounting for post-retirement benefits, the policy permits amortization of actuarial gains and losses only if they fall outside of the corridor. Under U.S. GAAP, such gains and losses on post-employment benefits that do not vest or accumulate are included immediately in income.
- (d) **Termination and severance benefits:** Termination and severance benefits are covered by the CICA Section 3461 Employee Future Benefits and the CICA Emerging Issues Committee Abstract 134 Accounting for Severance and Termination Benefits (EIC 134). Upon transition to the CICA Section 3461 effective January 1, 2000, a net transitional asset was created and was being amortized to income. During the first quarter of 2009 this transitional asset was fully amortized. Under U.S. GAAP, the expected benefits were not accrued and are expensed when paid.
- (e) **Stock-based compensation:** U.S. GAAP requires the use of an option-pricing model to fair value, at the grant date, share-based awards issued to employees, including stock options, TSARs, PSUs, RSUs, and DSUs. TSARs, PSUs, RSUs, and DSUs are subsequently re-measured at fair value each reporting period. Under Canadian GAAP, liability awards, such as TSARs, PSUs, RSUs and DSUs, are accounted for using the intrinsic method. U.S. GAAP also requires that CP accounts for forfeitures on an estimated basis. Under Canadian

GAAP, CP has elected to account for forfeitures on an actual basis as they occur.

Under U.S. GAAP compensation expense must be recorded if the intrinsic value of stock options is not exactly the same immediately before and after an equity restructuring. As a result of the Canadian Pacific Limited (CPL) corporate reorganization in 2001, CPL underwent an equity restructuring, which resulted in replacement options in CP stock having a different intrinsic value after the restructuring than prior to it. Canadian GAAP did not require the revaluation of these options. The Company adopted on a prospective basis effective January 2003 the CICA Section 3870 Stock-based Compensation and Other Stock-based Payments, which requires companies to account for stock options at their fair value. Concurrently, the Company elected to also account for stock options at their fair value under U.S. GAAP.

CANADIAN PACIFIC RAILWAY LIMITED
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2010

(unaudited)

11 Reconciliation of U.S. GAAP to Canadian GAAP (continued)

- (f) **Internal use software:** Under U.S. GAAP certain costs, including preliminary project phase costs, are expensed as incurred. These costs are capitalized and depreciated under Canadian GAAP.
- (g) **Capitalization of interest:** U.S. GAAP requires interest costs to be capitalized for all qualifying capital programs. Under Canadian GAAP capitalization of interest is a policy choice and the Company expenses interest related to capital projects undertaken during the year unless specific debt is attributed to a capital program. Differences in GAAP result in additional capitalization of interest under U.S. GAAP and subsequent related depreciation.
- (h) **Joint venture:** The CICA Section 3055 Interest in Joint Ventures requires the proportionate consolidation method to be applied to the recognition of interests in joint ventures in consolidated financial statements. Until April 1, 2009, the Company accounted for its joint-venture interest in the Detroit River Tunnel Partnership (DRTP) under Canadian GAAP using the proportionate consolidation method. During the second quarter of 2009, the Company completed a sale of a portion of its investment in the DRTP to its existing partner, reducing the Company's ownership from 50% to 16.5%. Effective April 1, 2009, the Company discontinued proportionate consolidation and accounts for its remaining investment in the DRTP under the equity method of accounting. U.S. GAAP requires the equity method of accounting to be applied to interests in joint ventures. This had no effect on net income as it represents a classification difference within the Consolidated Statement of Income and Consolidated Balance Sheet.
- (i) **Long-term debt:** Under Canadian GAAP, offsetting amounts with the same party and with a legal right to offset are netted against each other. U.S. GAAP does not allow netting of assets and liabilities among three parties. In 2003, the Company and one of its subsidiaries entered into a contract with a financial institution resulting in a receivable amount and long-term debt payable.

As well, transaction costs have been added to the fair value of the Long-term debt under Canadian GAAP whereas under U.S. GAAP such costs are recorded separately with Other assets .

- (j) **Capital leases:** Under U.S. GAAP, certain leases, which are recorded as capital leases under Canadian GAAP, do not meet the criteria for capital leases and are recorded as operating leases. These relate to equipment leases, previously recorded as operating leases under Canadian and U.S. GAAP, which were renewed within the last 25 percent of the equipment's useful life.
- (k) **Investment tax credits:** Under U.S. GAAP investment tax credits are credited against income tax expense whereas under Canadian GAAP these tax credits are offset against the related operating expense. There is no impact to net income as a result of this GAAP difference.
- (l) **Cash flows:** There are no material differences between cash flows under U.S. GAAP and Canadian GAAP.

CANADIAN PACIFIC RAILWAY LIMITED
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2010

(unaudited)

11 Reconciliation of U.S. GAAP to Canadian GAAP (continued)

Comparative income statement

Consolidated net income is reconciled from Canadian to U.S. GAAP in the following manner.

(in millions of Canadian dollars, except per share data)	Three months ended March 31					
	2010			2009		
	Canadian	U.S.	U.S.	Canadian	U.S.	U.S.
	GAAP	GAAP	GAAP	GAAP	GAAP	GAAP
		adjustments	adjustments		adjustments	
(unaudited)	GAAP	adjustments	GAAP	GAAP	adjustments	GAAP
Revenues						
Freight (h)	\$ 1,138.2	\$	\$ 1,138.2	\$ 1,079.1	\$ (3.1)	\$ 1,076.0
Other (h)	28.6		28.6	30.0	3.6	33.6
	1,166.8		1,166.8	1,109.1	0.5	1,109.6
Operating expenses						
Compensation and benefits (b, c, d, e, f)	345.0	8.5	353.5	341.2	1.7	342.9
Fuel	181.7		181.7	171.0		171.0
Materials (f)	62.0	1.9	63.9	76.1	0.5	76.6
Equipment rents (j)	48.7	0.3	49.0	66.1	0.3	66.4
Depreciation and amortization (f, g, h, j, k)	124.3	0.7	125.0	121.5	(1.8)	119.7
Purchased services and other (c, f, h, k)	193.3	(4.6)	188.7	196.3	4.5	200.8
	955.0	6.8	961.8	972.2	5.2	977.4
Operating income	211.8	(6.8)	205.0	136.9	(4.7)	132.2
Less:						
Other income and charges (a)	(3.0)	(1.9)	(4.9)	7.7	0.8	8.5
Interest expense (g, j)	69.2	(2.5)	66.7	72.3	(0.7)	71.6
Income before income tax expense	145.6	(2.4)	143.2	56.9	(4.8)	52.1
Income tax expense (recovery) (k) ⁽²⁾	41.7	1.7	43.4	(3.2)	(2.0)	(5.2)
Net income	\$ 103.9	\$ (4.1)	\$ 99.8	\$ 60.1	\$ (2.8)	\$ 57.3
Basic earnings per share	\$ 0.62	\$(0.03)	\$ 0.59	\$ 0.37	\$(0.01)	\$ 0.36
Diluted earnings per share	\$ 0.61	\$(0.02)	\$ 0.59	\$ 0.37	\$(0.01)	\$ 0.36

⁽¹⁾ Restated for the Company's change in accounting policies in relation

to the accounting for locomotive overhauls and amortization of pension plan amendments for unionized employees, discussed in Note 2 to the Company's 2009 annual consolidated financial statements. In addition, certain revenue and operating expense items have been reclassified in order to be consistent with the U.S. GAAP presentation.

- (2) Adjustment for income tax expense (recovery) includes the tax effect of other U.S. to Canadian GAAP differences, in addition to the impact of difference (k) Investment tax credits.

CANADIAN PACIFIC RAILWAY LIMITED
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2010

(unaudited)

II Reconciliation of U.S. GAAP to Canadian GAAP (continued)

Consolidated balance sheet

The Consolidated Balance Sheet is reconciled from Canadian to U.S. GAAP in the following manner:

(in millions of Canadian dollars) (unaudited)	Canadian GAAP	March 31, 2010 U.S. GAAP adjustments	U.S. GAAP	Canadian GAAP	December 31, 2009 U.S. GAAP adjustments	U.S. GAAP
Assets						
Current assets						
Cash and cash equivalents	\$ 723.8	\$	\$ 723.8	\$ 679.1	\$	\$ 679.1
Accounts receivable, net (i)	488.6	217.2	705.8	441.0	214.1	655.1
Materials and supplies	122.7		122.7	132.7		132.7
Deferred income taxes	133.6		133.6	128.1		128.1
Other current assets	57.6		57.6	46.5		46.5
	1,526.3	217.2	1,743.5	1,427.4	214.1	1,641.5
Investments	160.5		160.5	156.7		156.7
Net properties (e, f, g, j)	11,803.7	98.9	11,902.6	11,967.8	99.7	12,067.5
Goodwill and intangible assets	195.1		195.1	202.3		202.3
Other assets (b, i)	1,866.5	(1,693.9)	172.6	1,777.2	(1,601.4)	175.8
Total assets	\$15,552.1	\$(1,377.8)	\$14,174.3	\$15,531.4	\$(1,287.6)	\$14,243.8
Liabilities and shareholders equity						
Current liabilities						
Accounts payable and accrued liabilities (e)	\$ 883.9	\$ 16.7	\$ 900.6	\$ 917.3	\$ 9.8	\$ 927.1
Income and other taxes payable	40.3		40.3	31.9		31.9
Dividends payable	41.7		41.7	41.7		41.7
Long-term debt maturing within one year (i, j)	395.6	216.3	611.9	392.1	213.2	605.3
	1,361.5	233.0	1,594.5	1,383.0	223.0	1,606.0
Pension and other benefit liabilities (b, c)		1,417.7	1,417.7		1,453.9	1,453.9
Other long-term liabilities (b, c, e)	786.5	(309.2)	477.3	790.2	(310.3)	479.9
Long-term debt (i, j)	4,074.2	(50.9)	4,023.3	4,102.7	35.5	4,138.2
Future / deferred income taxes (b, c, e, f, g, j)	2,566.6	(697.6)	1,869.0	2,549.5	(704.5)	1,845.0

Total liabilities	8,788.8	593.0	9,381.8	8,825.4	697.6	9,523.0
Shareholders equity						
Share capital (e)	1,750.1	25.8	1,775.9	1,746.4	24.7	1,771.1
Contributed surplus / Additional paid-in capital (e)	33.5	(4.0)	29.5	33.5	(2.7)	30.8
Accumulated other comprehensive income (loss) (a, b)	41.0	(1,777.2)	(1,736.2)	49.5	(1,795.8)	(1,746.3)
Retained income / earnings (a, b, c, e, f, g, j)	4,938.7	(215.4)	4,723.3	4,876.6	(211.4)	4,665.2
	6,763.3	(1,970.8)	4,792.5	6,706.0	(1,985.2)	4,720.8
Total liabilities and shareholders equity	\$15,552.1	\$(1,377.8)	\$14,174.3	\$15,531.4	\$(1,287.6)	\$14,243.8

CANADIAN PACIFIC RAILWAY LIMITED
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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11 Reconciliation of U.S. GAAP to Canadian GAAP (continued)

Disclosures required by Canadian GAAP

Future accounting changes

U.S. GAAP / International Financial Reporting Standards (IFRS)

On February 13, 2008, the Canadian Accounting Standards Board (AcSB) confirmed that publicly accountable enterprises will be required to adopt IFRS in place of Canadian GAAP for interim and annual reporting purposes for fiscal years beginning on or after January 1, 2011, unless, as permitted by Canadian securities regulations, registrants were to adopt U.S. GAAP on or before this date. Commencing on January 1, 2010, CP adopted U.S. GAAP for its financial reporting, which is consistent with the reporting of other North American Class I railways. As a result, CP will not be adopting IFRS in 2011.

Business combinations, consolidated financial statements and non-controlling interests

In January 2009, the CICA issued three new standards:

Business Combinations, Section 1582

This section which replaces the former Section 1581 Business Combinations and provides the Canadian equivalent to IFRS 3 Business Combinations (January 2008). The new standard requires the acquiring entity in a business combination to recognize most of the assets acquired and liabilities assumed in the transaction at fair value including contingent assets and liabilities; and to recognize and measure the goodwill acquired in the business combination or a gain from a bargain purchase. Acquisition-related costs are also to be expensed.

Consolidated Financial Statements, Section 1601 and Non-controlling Interests, Section 1602

These two sections replace Section 1600 Consolidated Financial Statements . Section 1601 Consolidated Financial Statements carries forward guidance from Section 1600 Consolidated Financial Statements with the exception of non-controlling interests which are addressed in a separate section. Section 1602 Non-controlling Interests , requires the Company to report non-controlling interests within equity, separately from the equity of the owners of the parent, and transactions between an entity and non-controlling interests as equity transactions.

All three standards are effective January 1, 2011 and therefore will not impact the Company as it has adopted U.S. GAAP for financial reporting.

Capital disclosures

The Company s objectives when managing its capital are:

- o to maintain a flexible capital structure which optimizes the cost of capital at acceptable risk while providing an appropriate return to its shareholders;
- o to manage capital in a manner which balances the interests of equity and debt holders;
- o to manage capital in a manner that will maintain compliance with its financial covenants;
- o to manage its long-term financing structure to maintain its investment grade rating; and
- o to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business.

The Company defines its capital as follows:

- o shareholders equity;
- o long-term debt, including the current portion thereof; and

- o short-term borrowing.

The Company manages its capital structure and makes adjustments to it in accordance with the aforementioned objectives, as well as in light of changes in economic conditions and the risk characteristics of the underlying assets. In order to maintain or adjust its capital structure, the Company may, among other things, adjust the amount of dividends paid to shareholders, purchase shares for cancellation pursuant to normal course issuer bids, issue new shares, issue new debt, and/or issue new debt to replace existing debt with different characteristics.

CANADIAN PACIFIC RAILWAY LIMITED
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2010

(unaudited)

11 Reconciliation of U.S. GAAP to Canadian GAAP (continued)

The Company monitors capital using a number of key financial metrics, including:

o debt to total capitalization; and

o interest coverage ratio.

The calculations for the aforementioned key financial metrics are as follows:

Debt to total capitalization

Debt is the sum of long-term debt, long-term debt maturing within one year and short-term borrowing. This sum is divided by debt plus total shareholders' equity as presented on our Consolidated Balance Sheet.

Interest coverage ratio

Interest coverage ratio is measured, on a twelve month rolling basis, as adjusted EBIT divided by interest expense. Adjusted EBIT excludes changes in the estimated fair value of the Company's investment in long-term floating rate notes/ABCP, the gains on sales of partnership interest and significant properties and the loss on termination of a lease with a shortline railway as these are not in the normal course of business and foreign exchange gains and losses on long-term debt, which can be volatile and short term. The interest coverage ratio and adjusted EBIT are non-GAAP measures and do not have standardized meanings prescribed by GAAP and, therefore, are unlikely to be comparable to similar measures of other companies.

The following table illustrates the financial metrics and their corresponding guidelines currently in place:

(in millions of Canadian dollars, U.S. GAAP)	Guidelines	March 31, 2010	March 31, 2009
Long-term debt		\$4,023.3	\$ 5,024.4
Long-term debt maturing within one year		611.9	64.4
Short-term borrowing			132.0
Total debt		\$4,635.2	\$ 5,220.8
Shareholders' equity		\$4,792.5	\$ 4,847.2
Total debt		4,635.2	5,220.8
Total debt plus equity		\$9,427.7	\$10,068.0
Operating income		\$ 909.5	\$ 970.8
Less:			
Other income and charges		(1.0)	38.8
Plus:			
(Gain) loss in long-term floating rate notes/ABCP		(7.3)	28.1
Foreign exchange (gain) loss on long-term debt		(10.1)	(7.2)
Equity income in DM&E			39.9
Gain on sales of significant properties		(79.1)	
Loss on termination of lease with shortline railway		54.5	

Adjusted EBIT⁽¹⁾⁽²⁾		\$ 868.5	\$ 992.8
Total debt		\$4,635.2	\$ 5,220.8
Total debt plus equity		\$9,427.7	\$10,068.0
Total debt to total capitalization⁽¹⁾	No more than 50.0%	49.2%	51.9%
Adjusted EBIT ⁽¹⁾⁽²⁾		\$ 868.5	\$ 992.8
Interest expense ⁽²⁾		\$ 262.7	\$ 258.1
Interest coverage ratio⁽¹⁾⁽²⁾	No less than 4.0	3.3	3.8

(1) These earnings measures have no standardized meanings prescribed by GAAP and, therefore, are unlikely to be comparable to similar measures of other companies.

(2) The amount is calculated on a twelve month rolling basis.

CANADIAN PACIFIC RAILWAY LIMITED
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2010

(unaudited)

11 Reconciliation of U.S. GAAP to Canadian GAAP (continued)

The Company's financial objectives and strategy as described above have remained substantially unchanged over the last two fiscal years. The objectives are reviewed on an annual basis and financial metrics and their management targets are monitored on a quarterly basis. The interest coverage ratio has decreased during the twelve-month period ended March 31, 2010 due to a reduction in year-over-year earnings. The interest coverage ratio for the period is below the management target provided in the above table, due to lower volumes as a result of the global recession that occurred during the period.

The Company is subject to a financial covenant of funded debt to total capitalization in the revolver loan agreement. Performance to this financial covenant is well within permitted limits.

Summary of Rail Data
(Reconciliation of GAAP earnings to non-GAAP earnings on page 2)

<u>Financial (millions, except per share data)</u>	2010	First Quarter 2009	Fav/(Unfav)	%
<u>Revenues</u>				
Freight revenue	\$1,138.2	\$1,076.0	\$ 62.2	5.8
Other revenue	28.6	33.6	(5.0)	(14.9)
	1,166.8	1,109.6	57.2	5.2
<u>Operating expenses</u>				
Compensation and benefits	353.5	342.9	(10.6)	(3.1)
Fuel	181.7	171.0	(10.7)	(6.3)
Materials	63.9	76.6	12.7	16.6
Equipment rents	49.0	66.4	17.4	26.2
Depreciation and amortization	125.0	119.7	(5.3)	(4.4)
Purchased services and other	188.7	200.8	12.1	6.0
	961.8	977.4	15.6	1.6
Operating income	205.0	132.2	72.8	55.1
Less:				
Other income and charges	(4.9)	8.5	13.4	157.6
Interest expense	66.7	71.6	4.9	6.8
Income before income tax expense	143.2	52.1	91.1	174.9
Income tax expense (recovery)	43.4	(5.2)	(48.6)	
Net income	\$ 99.8	\$ 57.3	\$ 42.5	74.2
Basic earnings per share	\$ 0.59	\$ 0.36	\$ 0.23	63.9
Diluted earnings per share	\$ 0.59	\$ 0.36	\$ 0.23	63.9

Summary of Rail Data (Page 2)
(Reconciliation of GAAP earnings to non-GAAP earnings)

<u>Financial (millions)</u>	2010	2009	First Quarter Fav/(Unfav)	%
Net income	\$ 99.8	\$ 57.3	\$ 42.5	74.2
Exclude:				
<u>Foreign exchange (gain) loss on long-term debt (FX on LTD)</u>				
FX on LTD	(4.1)	2.4	6.5	
Income tax expense (recovery) on FX on LTD ⁽¹⁾	7.2	(8.9)	(16.1)	
FX on LTD (net of tax)	3.1	(6.5)	(9.6)	
<u>Other specified items</u>				
Gain in fair value of long-term floating rate notes	(1.0)		1.0	
Income tax expense	0.1		(0.1)	
Gain in fair value of long-term floating rate notes (net of tax)	(0.9)		0.9	
Income before FX on LTD and other specified items ⁽²⁾	\$102.0	\$ 50.8	\$ 51.2	100.8
<u>Earnings per share (EPS)</u>				
Diluted EPS	\$ 0.59	\$ 0.36	\$ 0.23	63.9
Exclude (gain) loss:				
Diluted EPS, related to FX on LTD, net of tax ⁽²⁾	0.02	(0.04)	(0.06)	
Diluted EPS, related to other specified items, net of tax ⁽²⁾	(0.01)		0.01	
Diluted EPS, before FX on LTD and other specified items ⁽²⁾	\$ 0.60	\$ 0.32	\$ 0.28	87.5
Operating ratio (%) ⁽³⁾	82.4	88.1	5.7	
<u>Shares Outstanding</u>				
Weighted average number of shares outstanding (millions)	168.5	160.9	7.6	4.7
Weighted average number of diluted shares outstanding (millions)	169.1	161.2	7.9	4.9
<u>Foreign Exchange</u>				

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Average foreign exchange rate (US\$/Canadian\$)	0.96	0.81	(0.15)	(18.5)
Average foreign exchange rate (Canadian\$/US\$)	1.04	1.24	(0.20)	(16.1)

(1) Income tax on
FX on LTD is
discussed in the
MD&A in the
Other Income
Statement Items
section Income
Taxes .

(2) These earnings
measures have
no standardized
meanings
prescribed by
GAAP and may
not be
comparable to
similar
measures of
other
companies. See
note on
non-GAAP
earnings
measures
attached to
commentary.

(3) Operating ratio
is the
percentage
derived by
dividing
operating
expenses by
total revenues.

Summary of Rail Data (Page 3)

	2010	2009	First Quarter Fav/(Unfav)	%
<u>Financial (millions, except per share data)</u>				
Operating income	\$205.0	\$132.2	\$ 72.8	55.1
Other income and charges, before FX on LTD and other specified items ⁽¹⁾	0.2	6.1	5.9	96.7
Interest expense	66.7	71.6	4.9	6.8
Income tax expense, before income tax on FX on LTD and other specified items ⁽¹⁾	36.1	3.7	(32.4)	
Income before FX on LTD and other specified items ⁽¹⁾	\$102.0	\$ 50.8	\$ 51.2	100.8
Operating ratio (%) ⁽²⁾	82.4	88.1	5.7	
Diluted EPS, before FX on LTD and other specified items ⁽¹⁾	\$ 0.60	\$ 0.32	\$ 0.28	87.5

(1) These earnings measures have no standardized meanings prescribed by GAAP and may not be comparable to similar measures of other companies. See note on non-GAAP earnings measures attached to commentary.

(2) Operating ratio is the percentage derived by dividing

operating
expenses by
total revenues.

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Summary of Rail Data (Page 4)

	2010	2009	First Quarter Fav/(Unfav)	%
<u>Commodity Data</u>				
Freight Revenues (millions)				
- Grain	\$ 271.3	\$ 287.7	\$ (16.4)	(5.7)
- Coal	110.5	116.5	(6.0)	(5.2)
- Sulphur and fertilizers	117.8	76.2	41.6	54.6
- Forest products	43.2	45.4	(2.2)	(4.8)
- Industrial and consumer products	205.5	205.8	(0.3)	(0.1)
- Automotive	77.6	51.9	25.7	49.5
- Intermodal	312.3	292.5	19.8	6.8
Total Freight Revenues	\$1,138.2	\$1,076.0	\$ 62.2	5.8
Millions of Revenue Ton-Miles (RTM)				
- Grain	8,636	8,528	108	1.3
- Coal	4,308	3,832	476	12.4
- Sulphur and fertilizers	4,392	2,180	2,212	101.5
- Forest products	1,378	1,064	314	29.5
- Industrial and consumer products	4,887	4,350	537	12.3
- Automotive	545	363	182	50.1
- Intermodal	6,057	5,608	449	8.0
Total RTMs	30,203	25,925	4,278	16.5
Freight Revenue per RTM (cents)				
- Grain	3.14	3.37	(0.23)	(6.8)
- Coal	2.56	3.04	(0.48)	(15.8)
- Sulphur and fertilizers	2.68	3.50	(0.82)	(23.4)
- Forest products	3.13	4.27	(1.14)	(26.7)
- Industrial and consumer products	4.21	4.73	(0.52)	(11.0)
- Automotive	14.24	14.30	(0.06)	(0.4)
- Intermodal	5.16	5.22	(0.06)	(1.1)
Total Freight Revenue per RTM	3.77	4.15	(0.38)	(9.2)
Carloads (thousands)				
- Grain	113.2	111.5	1.7	1.5
- Coal	76.0	70.8	5.2	7.3
- Sulphur and fertilizers	44.3	24.9	19.4	77.9
- Forest products	17.6	17.5	0.1	0.6
- Industrial and consumer products	91.8	86.6	5.2	6.0
- Automotive	33.5	21.0	12.5	59.5
- Intermodal	248.6	244.0	4.6	1.9

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Total Carloads	625.0	576.3	48.7	8.5
Freight Revenue per Carload				
- Grain	\$ 2,397	\$ 2,580	\$ (183)	(7.1)
- Coal	1,454	1,645	(191)	(11.6)
- Sulphur and fertilizers	2,659	3,060	(401)	(13.1)
- Forest products	2,455	2,594	(139)	(5.4)
- Industrial and consumer products	2,239	2,376	(137)	(5.8)
- Automotive	2,316	2,471	(155)	(6.3)
- Intermodal	1,256	1,199	57	4.8
Total Freight Revenue per Carload	\$ 1,821	\$ 1,867	\$ (46)	(2.5)

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Summary of Rail Data (Page 5)

	2010	2009 ⁽¹⁾	First Quarter Fav/(Unfav)	%
<u>Operations Performance</u>				
Total operating expenses per GTM (cents)	1.64	1.92	0.28	14.6
Freight gross ton-miles (GTM) (millions)	58,524	50,933	7,591	14.9
Train miles (000)	9,557	8,907	650	7.3
Average number of active employees Total	14,431	15,051	620	4.1
Average number of active employees Expense	13,824	14,384	560	3.9
Number of employees at end of the period Total	14,530	14,970	440	2.9
Number of employees at end of the period Expense	13,840	14,125	285	2.0
U.S. gallons of locomotive fuel consumed per 1,000 GTMs -freight & yard	1.23	1.34	0.11	8.2
U.S. gallons of locomotive fuel consumed total (millions) ⁽²⁾	71.5	67.7	(3.8)	(5.6)
Average fuel price (U.S. dollars per U.S. gallon)	2.44	2.04	(0.40)	(19.6)
<u>Fluidity Data (excluding DM&E)</u>				
Average terminal dwell AAR definition (hours)	24.1	23.2	(0.9)	(3.9)
Average train speed AAR definition (mph)	24.2	25.0	(0.8)	(3.2)
Car miles per car day	144.2	140.0	4.2	3.0
Average daily active cars on-line (000)	52.5	48.7	(3.8)	(7.8)
Average daily active road locomotives on-line	860	833	(27)	(3.2)
<u>Safety</u>				
FRA personal injuries per 200,000 employee-hours	2.07	1.80	(0.27)	(15.0)
FRA train accidents per million train-miles	1.36	1.97	0.61	31.0

(1) Certain prior period figures have been revised to conform with current presentation or have been updated to reflect new

information.

- (2) Includes gallons of fuel consumed from freight, yard and commuter service but excludes fuel used in capital projects and other non-freight activities.