QUÉBEC-TÉLÉPHONE

55th ANNUAL REPORT

1981

Our Signature

As a general rule, business today dictates that companies use symbolism to create instantaneous, overall and continuous awareness of their presence among clients, suppliers and employees. To that effect, Québec-Téléphone's signature has become a communications medium, in the true sense of the word.

The image projected by the Company in its correspondence, and on its vehicles and buildings, expresses solidity and continuity. In addition, it suggests availability and application of the most sophisticated technology currently being used in the telecommunications field.

An Identity

Since 1927, Québec-Téléphone has been providing telecommunications services throughout a vast territory covering 272,000 km², equal to 40% of the inhabited area of Québec. The half million people it serves reside on the outskirts of Québec City, and in the Lower St. Lawrence, Gaspé and North Shore regions.

The Company's 2,166 employees have expertise in various fields of activity: voice and data transmission, radio and television broadcasting, computer communications, word processing, mobile radio communications and paging systems.

The Company generates $130.9 million in annual revenues. It has 281,725 telephones in service and serves 136 exchanges. Its buildings, land and equipment are worth $428.5 million.

Québec-Téléphone is the leading telecommunications company under the jurisdiction of the *Régie des services publics* of Québec. Its two major common shareholders are *La Compagnie de Téléphone Anglo-Canadienne* (51.6%) and *Caisse de dépôt et placement du Québec* (16.1%).

Report in Brief

	1981	1980	1979
Financial (thousands of dollars)			
Operating revenues	**$130,884**	$112,000	$101,303
Operating expenses	**91,888**	77,378	69,082
Salaries and benefits	**50,702**	44,033	39,645
Net income applicable to Common shares	**12,205**	9,875	9,020
Common share dividends	**8,089**	6,444	5,875
Funds used for construction	**42,705**	41,601	35,840
Telecommunications property, at cost[1]	**428,517**	394,648	361,496
Shareholders items			
Earnings per Common share	**$ 3.02**	$ 2.82	$ 2.72
Dividends declared per Common share	**$ 2.00**	$ 1.84	$ 1.77
Common equity per Common share[1]	**$ 21.36**	$ 20.44	$ 19.16
Rate of return on average Common share equity	**14.5%**	14.5%	14.6%
Average number of Common shares	**4,044,266**	3,502,114	3,318,706
Number of Common shareholders[1]	**3,295**	2,815	1,876
Other statistics			
Telephone gain for the year	**4,855**	11,533	11,483
Telephones in service[1]	**281,725**	276,870	265,337
Toll messages (in thousands)	**30,002**	29,656	27,929
Number of employees[1]	**2,166**	2,195	2,209

1. Year-end

The Chairman's Letter

Raymond Sirois
President and Chief
Executive Officer

The search for renewed stability in the telecommunications field has been the dominant factor during 1981 - a transitional year. In fact, the last twelve months of analyses and planning have enabled management to measure the impact of the industry's shift towards more competitiveness on our own activities. Our major aim has been to meet this challenge with new, innovative strategies to take full advantage of every development opportunity.

Even if there are risks, transition towards revolutionary operating models appears to be quite beneficial as part of the overall restructuring of a society which is rapidly becoming computerized. Such a vast evolution must follow stringent guidelines to reach its objective. And the telephone network already appears as the most appropriate and economical medium for supporting the impending expansion of telematics, considering the scope of coverage it provides.

These opportunities that our existing resources allow us to contemplate rest on the rapid growth of digital technology. Powerful computers are significantly increasing the capacity and flexibility of network operation while permitting substantial savings in space and maintenance.

However, accelerated innovation has a negative effect on the useful life of equipment. To offset this, we are deploying considerable efforts to recover existing capital investments as quickly as possible by depreciating our plant over shorter periods than before. Furthermore, spiralling inflation has prompted the Company to rely more on internal funding to decrease the impact of costly external financing.

By preparing today development plans to meet the expectations of our subscribers tomorrow, our objective is to harmonize the growth of networks with the social, political, industrial and commercial priorities of the population we serve.

Only by remaining aware of our clients' needs will we be able to help them cope with technological changes which will gradually modify their way of life. Consequently, we firmly believe that the successful introduction of the most innovative services will depend on our ability to make them known, understood and accepted by our clientele.

Should terminal interconnection be extended to all our regions, Québec-Téléphone's subscribers will have to pay for maintenance of their privately-owned equipment. It will then be clear that the reliability of telephone service does not rest solely on the telephone instrument, but on the quality of every link in the switching chain.

Up to now, we have maintained high levels of efficient, reliable and accessible services which has contributed to the good reputation of this country. However, in a more competitive environment, we will need adequate legislation to allow us freedom of action compatible with our responsibilities towards the public.

The competence, dedication and continued efforts of the Company's approximately 2,200 employees have contributed in maintaining this stability of presence and action. We are proud to say that it is with such human resources that Québec-Téléphone intends to face the challenges of the future.

On behalf of the Board of Directors

Raymond Sirois

Raymond Sirois
Chairman of the Board
February 2, 1982

Report of Activities

Operations

Charles Mercier
Vice President - Marketing and Customer Service

During 1981, Québec-Téléphone maintained improved services to business and residential subscribers among its top priorities. The year's most important achievement has been the conversion of several switching centers serving the Saint-Flavien, Mont-Joli and Chandler areas to digital technology. In addition, the same concern for efficiency prompted the Company to initiate an automation program in the Québec Region for long-distance switching operations.

Services

In order to provide better customer services, the Company reorganized its operations in the Gaspé Peninsula. The Matane and New Carlisle districts have been assigned smaller, easier-to-serve territories. On the eastern side of the peninsula, a new district with a business office in Gaspé has been set up as a result of a recent growth trend in this area.

The introduction of new Extended Area Services between Neuville and the Québec Urban Community, and also between Port-Daniel and New Carlisle, has intensified communications between the communities involved. Subscribers also welcomed the rural upgrading program which was developed in 20 exchanges. In addition, 9 other exchanges have been equipped with Automatic Number Identification.

With the application of new rate schedules, users can make calls on Saturday mornings at lower weekend rates. Night and weekend discounts are now in effect from 11 p.m. Friday night to 8 a.m. Monday morning. Subscribers now also benefit from lower extension telephone rental rates.

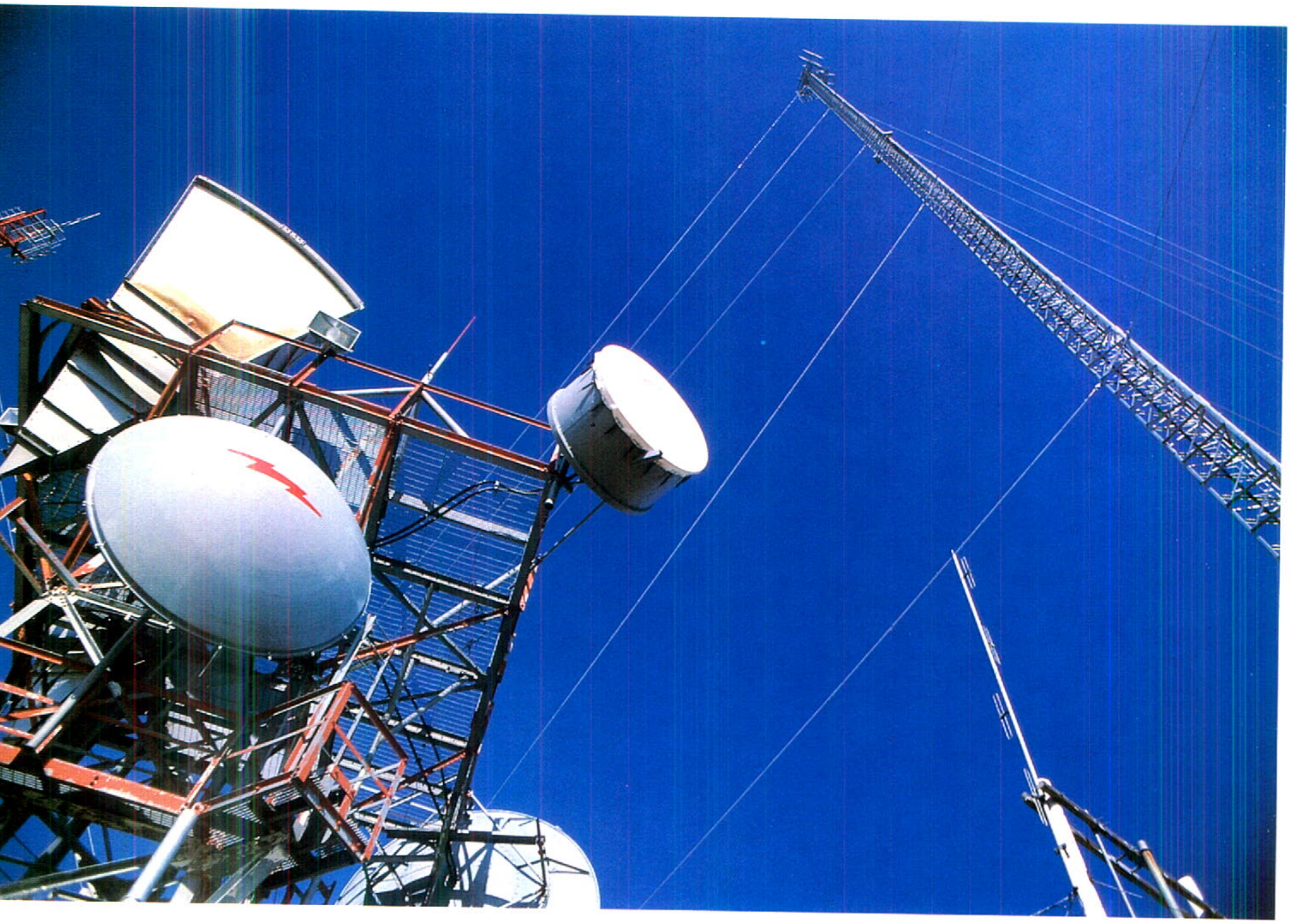
Marketing

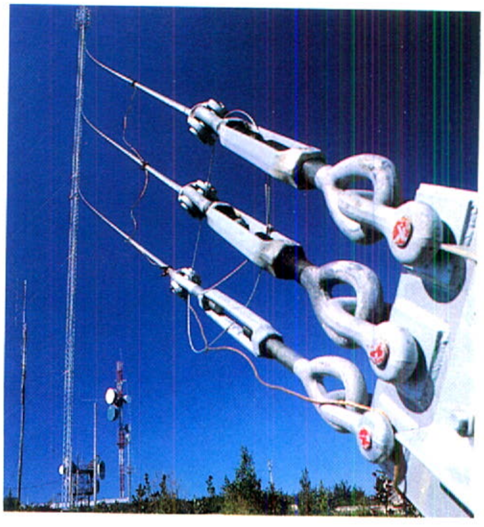
In 1981, the Marketing Department has accomplished a significant breakthrough on the new technology markets. Among the wider range of products offered by Québec-Téléphone, stand-alone word processing equipment including shared logic systems is now being marketed. Another major achievement during the past year has been the linking of the various health institutions in Eastern Québec to a computerized electrocardiogram management center located in Rimouski.

As part of Québec-Téléphone's involvement in broadcasting, the Company has expanded its signal transmission program provided to several private and public broadcasters serving the North Shore and Northern Gaspé regions. Rearrangement of the facilities located at Trouble Mountain, Sept-Îles, has led to operational diversity enabling this major transmission center to provide more efficient services to both shores of the St. Lawrence River.

Finally, among services providing greater client mobility, the significant growth of shared frequency mobile radio systems should be highlighted.

In 1981, Québec-Téléphone built a new 152-meter tower on Trouble Mountain, Sept-Îles. The tower, which supports an antenna for *Entreprises Télé-Capitale*, dominates the Gulf of St. Lawrence and provides the various localities of Northern Gaspé with access to the second French television network (TVA) programming.





Engineering

Robert Duchesne
Vice President -
Network Engineering and Construction

As a participant in the planning and development process on the national telecommunications network, Québec-Téléphone adjusts its objectives to those of its various partners while pursuing an approach that takes into consideration its own environmental reality.

In the same vein, recent integration of Rimouski into the major transcanadian Dataroute linkup stations now provides Company data transmission users with more economical and reliable digital technology equipment.

Application of the digital concept in various areas of the Company's territory effectively illustrates integration of the various network components. There are several technological advantages to this: grouping of switching equipment, maximum use of existing facilities, as well as assurance that uniform and continuous network management is applied.

To keep pace with the extensive computerization trend spreading to residential and business markets, Québec-Téléphone devoted considerable energy to the planning of its infrastructures. The Company is thus seeking to be in a better position to meet a wide range of emerging telecommunications needs. The intensive efforts dedicated to this end should guarantee a high level of stability in the efficient servicing of these markets.

Human Resources

Ghislain Bouchard
Vice President -
Human Resources and Legal Affairs, Secretary

As part of its manpower planning programs, Québec-Téléphone attempts to assess the impact of technology on job profiles in various departments. In addition, a new plan is being developed to define more precisely the number and types of functions required in the coming years. Mechanized processing of career plans, which was initiated in 1979, has provided employees with a wealth of information about jobs, enabling them to make clear and realistic choices specifically adapted to their personal development. Administrative and technical courses provided to employees represented over 50,000 hours of intensive training. More than 80% of these sessions were conducted in-house, as a less costly, better suited alternative to training than the use of external services.

In the labour relations sector, the Company renewed four collective agreements applying to operators, office employees and technicians, craft employees, and security and housekeeping personnel. On September 29, 1981, the Labour Commissioner rendered a decision recognizing the status of "employee" - pursuant to the Labour Code - to 9 of about 150 technical and professional employees whom Québec-Téléphone regarded as its representatives. This decision has been appealed against by both the Union and the Company.

In order to cope with a fluctuating economy and accelerated technological changes, the *Régie des services publics* of Québec proposes a new approach to the regulatory process based on the sharing of information and work in joint committees for analysis of major corporate activities. This should contribute to the acceleration of the examination, hearing and decision cycle on the Company's future applications.

Public Relations

Henri Dionne
Vice President - Public Relations

In an effort to provide all its subscribers, whatever their condition, with equal accessibility to communications, Québec-Téléphone developed a service program for clients with visual, hearing, speech and motor disabilities, which includes access ramps to key Company buildings, standard height pay telephones in public places and the promotion and supply of other related products and services.

As part of its community relations programs, Québec-Téléphone supported cultural activities by sponsoring summer recitals, popular concerts and art exhibitions. Various works of art reproduced on the covers of its telephone directories were exhibited publicly this year.

In order to improve communications with the communities it serves, the Company regionalized its public information practices in 1981, by involving our district managers in the production and distribution of communiqués to the media as well as to community groups and organizations. Since last September, this dialogue with our clients led to regular publication and distribution of 200,000 copies of a bulletin providing tips on efficient use of our equipment and services as well as answers to many of our subscribers' questions.

These various public relations programs are supported by Québec-Téléphone's desire to cooperate actively in fostering a better way of life.

Financial Review

Simon Soucy
Vice President - Finance and Treasurer

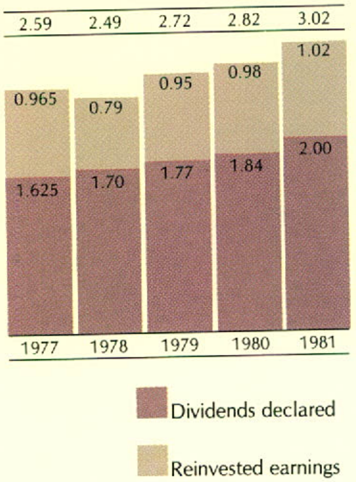
Earnings and Dividends

Despite difficult economic conditions, high inflation and unemployment rates throughout the year, Québec-Téléphone's earnings were higher in 1981 than in the previous year. Net income applicable to common shares was $12.2 million or $3.02 per common share compared with $9.9 million or $2.82 in 1980, with an increase of 15.5% in the average number of common shares outstanding. The increase in income is attributable to a general adjustment of rates, a greater use of our Wide Area Telephone Service, a moderate increase in demand for our other services and it is also due to a decrease in dividends paid to preferred shareholders as a result of the redemption of preferred shares for sinking fund purposes.

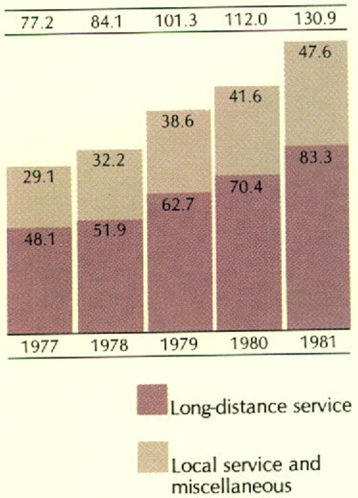
In 1981, the rate of return on average common share equity was 14.5%, as in 1980, but 0.5% lower than the level authorized by the *Régie des services publics* of Québec. The rate of return on average invested capital reached 11.6% in 1981 as compared with 11.0% in 1980 and 10.9% in 1979.

Quarterly dividends for 1981 were paid to all common, preferred and subordinate preferred shareholders. At the meeting of the Board of Directors held on February 3, 1981, the quarterly dividend per common share payable on April 1 was raised to $0.50 from $0.46. This increase brought the total dividends declared in 1981 to $2.00 per common share compared with $1.84 for 1980.

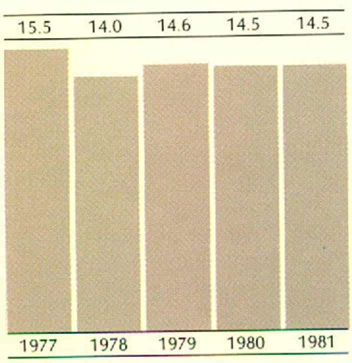
Earnings and dividends per common share
(Dollars)



Operating revenues
(Millions of dollars)



Rate of return on average common share equity *(%)*



Operating Revenues and Expenses

Growth in operating revenues was 16.9% bringing the total to $130.9 million compared with $112.0 million in 1980. Long-distance revenues, which represent 63.7% of the Company's operating revenues, increased by 18.3% to $83.3 million. This increase in long-distance revenues is mainly due to the rate adjustment of March 30, 1981 which raised the average toll message rate by 15.5%. Despite sluggish economic conditions, the number of long-distance calls handled during the year reached 30.0 million compared with 29.7 million in 1980, while revenues derived from Wide Area Telephone Service increased from $5.8 million in 1980 to $8.5 million in 1981, representing a 45.7% increase. For their part, local service revenues rose by 14.8% to attain $46.7 million. This increase is the combined result of the rate adjustment on basic telephone and other services effective July 1, 1981, a demand for new services and the increase in the number of telephones in service which reached 281,725 on December 31, 1981 compared with 276,870 at the same date last year.

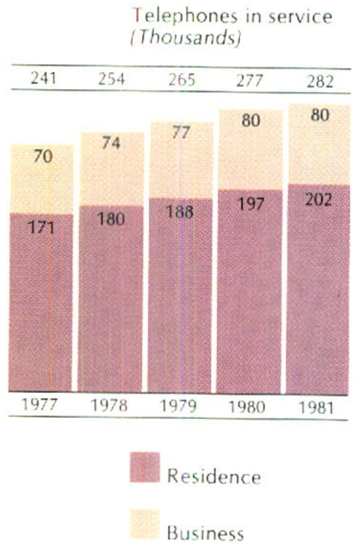
Operating expenses, excluding depreciation charges and general taxes, totalled $56.5 million, an 18.2% rise over the $47.8 million in 1980. With the approval of the *Régie des services publics* of Québec, additional costs previously capitalized and recovered through depreciation and amounting to approximately $1.1 million have been charged directly to operating expenses this year. The Company's on-going equipment automation and modernization programs and constant efforts to obtain maximum in-house efficiency were restrained by increases in labor costs and the high inflation rate that prevailed throughout the year. Following additions to telecommunications property and the application of new depreciation rates to certain classes of telephone plant, reflecting a reduction in the useful life of the equipment, depreciation charges reached $26.3 million in 1981, a rise of 17.1% over last year. General taxes rose to $9.1 million from $7.1 million in 1980, or 27.8%. This increase is mainly due to the application of new rates for employer's contribution to the Québec Health Insurance Plan and to the increase of the rate of capital tax. Interest charges for the year increased by 3.8% over 1980 to attain $13.1 million. This moderate increase is a result of an improvement of internal generated funds for capital expenditures which rose to 83.3% from 72.8% in 1980; however, the overall effect of this increase was partially offset by successive rises in interest rates paid on our short-term debts.

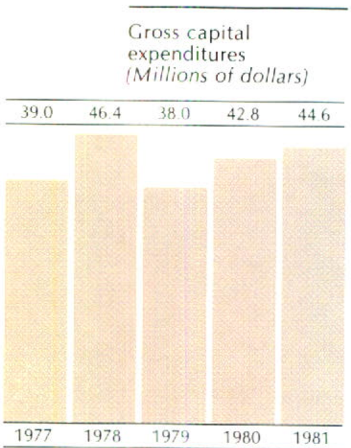
Capital Expenditures

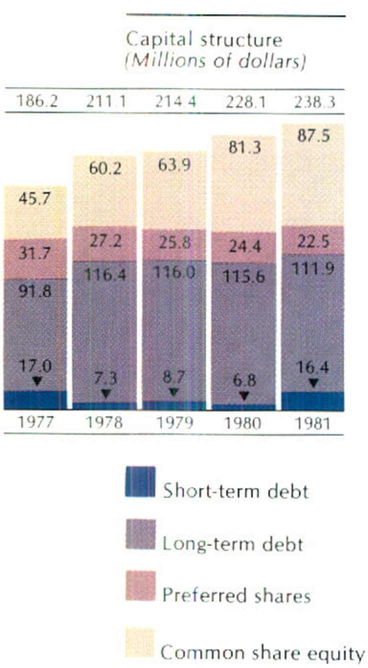
The Company's expansion and improvement programs during the year required $44.6 million in gross capital expenditures, or $6.3 million less than forecasted. This reduction was necessary to offset the effects of a particularly weak economy which resulted in a lower demand for new services.

A major part of these capital outlays ($18.0 million) were invested in the development of local and long-distance services to meet demands for new services in the coming years. Network and service improvements totalled $4.6 million of which $3.0 million were used to provide individual or two-party line service to rural customers.

An amount of $9.6 million was invested in the switching equipment modernization program, with a significant portion covering local digital systems at Amqui, Mont-Joli, Saint-Augustin, Sainte-Marie-de-Beauce, Percé, Val-Alain and Saint-Moïse. A toll digital system was also installed at Sainte-Marie-de-Beauce.







Purchases and connection of subscriber and special services equipment amounted to $10.7 million, with remaining investments being used for the addition and replacement of vehicles, tools and furnitures as well as building extensions. Funds generated from operations, after payment of dividends on common shares, permitted the Company to finance 83.3% of its construction program, the balance being made up of short-term borrowings.

During the next five years, the Company plans to invest $260 million to continue to expand and modernize its installations and to meet the demand for telecommunications services. Forecasted external capital requirements for these programs will be approximately $52 million.

Shareholders' Plans

During its second year the Common Shareholders' Dividend Reinvestment and Share Purchase Plan was particularly successful; 86,848 common shares were issued in 1981, increasing equity by $1.6 million and bringing to 104,946 the total number of common shares issued since the institution of the Plan in 1980. As at January 2, 1982, 585 of the Company's common shareholders, representing 17.8% of the common shareholders holding 19.1% of the common shares outstanding, had participated in the Plan.

In November 1981, the Board of Directors approved a Stock Dividend and Share Purchase Plan, effective with the April 1, 1982 dividend, that will enable shareholders to take advantage of tax reductions on stock dividends, as opposed to cash dividends. The price of these shares will be 100% of the average market price, and like in the Common Shareholders' Dividend Reinvestment and Share Purchase Plan, participants will have no brokerage or administrative fees to pay under the Plan.

Statements of Income and Reinvested Earnings

for the years ended December 31

QUEBEC-TELEPHONE

	1981	1980
	Thousands of dollars	
Operating revenues		
Local service	$ 46,704	$ 40,687
Long-distance service	83,328	70,436
Miscellaneous	1,652	1,338
Less: uncollectible accounts	800	461
	130,884	112,000
Operating expenses (Note 4)		
Maintenance	23,211	19,584
Depreciation	26,318	22,470
Traffic	4,542	3,940
Customer services and marketing	8,072	6,589
Administrative and other expenses	18,099	15,695
Pension plan and other employee benefits (Note 5)	2,531	1,967
General taxes (Note 6)	9,115	7,133
	91,888	77,378
Operating income	38,996	34,622
Other income (Note 7)	1,768	1,177
Income before interest charges and income taxes	40,764	35,799
Interest charges		
Interest on long-term debt	11,278	11,266
Interest on short-term notes	1,671	1,206
Amortization of discount and expenses on long-term debt	170	170
	13,119	12,642
Income before income taxes	27,645	23,157
Income taxes (Note 11)	13,821	11,517
Net income	13,824	11,640
Preferred share and Subordinate Preferred share dividends	1,619	1,765
Net income applicable to Common shares	12,205	9,875
Reinvested earnings at beginning of year	30,712	27,486
	42,917	37,361
Common share dividends	8,089	6,444
Commission and expenses on sale of shares	15	205
	8,104	6,649
Reinvested earnings at end of year	$ 34,813	$ 30,712
Earnings per Common share	$ 3.02	$ 2.82
Dividends declared per Common share	$ 2.00	$ 1.84
Average number of Common shares	4,044,266	3,502,114

The accompanying notes are an integral part of these financial statements.

Balance Sheets
December 31

QUÉBEC-TÉLÉPHONE

ASSETS	1981	1980
	Thousands of dollars	
Telecommunications property, at cost (Note 9)		
Buildings, plant and equipment	**$408,214**	$377,072
Less: accumulated depreciation	**126,325**	107,888
	281,889	269,184
Land	**1,780**	1,614
Property under construction	**9,893**	7,421
Construction materials, at average cost	**8,630**	8,541
	302,192	286,760
Investment in Common shares of Télésat Canada, at cost	**600**	600
Current assets		
Cash	**75**	273
Accounts receivable	**14,999**	12,948
Prepaid expenses	**702**	689
	15,776	13,910
Deferred charges		
Unamortized discount and expenses on long-term debt	**1,338**	1,508
Other	**2,805**	1,008
	4,143	2,516
Total assets	**$322,711**	$303,786

On behalf of the Board of Directors, February 2, 1982:

Raymond Sirois

Raymond Sirois, Director

Hervé Belzile

Hervé Belzile, Director

CAPITALIZATION AND LIABILITIES	1981	1980
	Thousands of dollars	
Capitalization (per accompanying statement)		
Common share equity	**$ 87,461**	$ 81,316
Subordinate Preferred shares	**226**	242
Preferred shares	**22,323**	24,126
Long-term debt	**111,924**	115,641
	221,934	221,325
Current liabilities		
Short-term debt (Note 10)	**16,376**	6,792
Accounts payable:		
Affiliates	**179**	219
Other	**7,454**	7,086
Income taxes payable (Note 11)	**3,384**	1,313
Dividends payable	**2,439**	2,260
Accrued interest	**2,286**	2,294
Other accrued liabilities	**5,415**	4,042
Unearned revenues	**2,853**	2,058
	40,386	26,064
Deferred income taxes (Note 11)	**60,391**	56,397
Total capitalization and liabilities	**$322,711**	$303,786

Simon Soucy

Simon Soucy
Vice President - Finance and Treasurer

The accompanying notes are an integral part of these financial statements.

Statements of Capitalization (Note 2)

December 31

QUÉBEC-TÉLÉPHONE

		1981		1980	
		Thousands of dollars			
Common share equity					
Common shares without nominal or par value		**$ 52,648**		$ 50,604	
Authorized	5,000,000				
Outstanding (1980: 3,979,035)	4,093,829				
Reinvested earnings (see accompanying statement)		**34,813**		30,712	
		87,461	**39%**	81,316	37%
Subordinate Preferred shares of the par value of $15 each					
Authorized	1,000,000				
Outstanding (1980: 15,106)	14,135				
$1.68 Cumulative Redeemable Convertible, Series B		**212**		227	
Premium on Subordinate Preferred shares, Series B		**14**		15	
		226	**—%**	242	—%
Cumulative Redeemable Preferred shares of the par value of $20 each					
Authorized	1,682,898				
Outstanding (1980: 1,269,103)	1,179,420				
Series					
1955 5% (sinking fund)		**852**		885	
1956 5% (sinking fund)		**406**		432	
1965 $4\frac{3}{4}$%		**8,000**		8,000	
1973 $7\frac{3}{4}$% (purchase fund)		**4,430**		4,940	
1975 $9\frac{3}{4}$% (sinking fund)		**2,400**		3,000	
1977 7% (sinking fund)		**7,500**		8,125	
Less: sinking fund payments		**1,265**		1,256	
		22,323	**10%**	24,126	11%

					1981		1980	
					Thousands of dollars			
				Issued				
Long-term debt								
First Mortgage Bonds								
Series	Rate	Maturing						
F	$5^5/8$%	December 1,	1984	$ 3,000,000 (U.S.)	**$ 2,416**		$ 2,465	
G	$5^1/2$%	October 15,	1982	5,000,000	**3,405**		3,457	
H	$5^1/2$%	June 1,	1987	6,000,000	**4,289**		4,355	
I	6%	October 15,	1990	5,000,000	**4,550**		4,625	
J	7%	January 2,	1989	5,000,000	**5,000**		5,000	
L	$9^1/8$%	April 15,	1991	7,500,000	**389**		389	
M	$8^3/4$%	May 15,	1992	7,500,000	**7,500**		7,500	
N	$8^1/2$%	March 15,	1993	8,500,000	**8,500**		8,500	
O	$9^3/4$%	July 1,	1994	16,500,000 (U.S.)	**15,921**		15,921	
P	$11^7/8$%	October 15,	1995	15,000,000	**15,000**		15,000	
Q	$10^5/8$%	December 15,	1996	20,000,000	**20,000**		20,000	
R	$10^1/2$%	December 2,	1983	25,000,000	**25,000**		25,000	
Less: sinking fund payments and debt due within one year					**3,621**		221	
					108,349		111,991	
General Mortgage Bonds								
Series	Rate	Maturing						
D	$5^3/4$%	April 1,	1983	5,000,000	**3,590**		3,715	
Less: sinking fund payment					**15**		65	
					3,575		3,650	
					111,924	**51%**	115,641	52%
Total capitalization					**$221,934**	**100%**	$221,325	100%

The accompanying notes are an integral part of these financial statements.

Changes in Financial Position
for the years ended December 31

	1981	1980
	Thousands of dollars	
Source of funds		
From operations		
Net income applicable to Common shares	**$ 12,205**	$ 9,875
Expenses not requiring a cash outlay:		
Depreciation	**26,318**	22,470
Deferred income taxes - this year (Note 11)	**3,760**	4,159
Other	**1,396**	1,033
	43,679	37,537
Net proceeds from financing		
Common shares	**2,013**	13,997
Change in short-term notes	**6,225**	(1,885)
	8,238	12,112
Total	**51,917**	49,649
Application of funds		
Funds used for construction		
Gross capital expenditures	**44,550**	42,641
Increase (decrease) in construction materials	**89**	145
Less: charges not requiring a cash outlay	**1,934**	1,185
	42,705	41,601
Other		
Common share dividends	**8,089**	6,444
Redemptions of Preferred shares and long-term debt	**2,161**	1,811
Increase (decrease) in working capital (Note 12)	**(2,872)**	(815)
Miscellaneous items	**1,834**	608
	9,212	8,048
Total	**$ 51,917**	$ 49,649

The accompanying notes are an integral part of these financial statements.

Notes to Financial Statements
for the years ended December 31, 1981 and 1980

QUEBEC-TELEPHONE

1.Summary of Significant Accounting Policies

The Company's financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles, and in conformity with prevailing practices in the Canadian telecommunications industry. The Company is subject to the regulations of the *Régie des services publics* of Québec.

Earnings per Common Share
Earnings per Common share are calculated using the quarterly weighted average number of outstanding Common shares eligible for quarterly dividend.

Principles of Consolidation
These financial statements are consolidated and include the accounts of *La Compagnie de Téléphone Bonaventure et Gaspé, Limitée*, an inactive wholly-owned subsidiary.

Accounting for Certain Disbursements
The Company, together with other telecommunications companies and with the concurrence of the *Régie des services publics* of Québec, has modified the accounting for certain disbursements. Certain costs capitalized in prior years and charged to income through depreciation, are now expensed, resulting in an increased charge to operating expenses of approximately $1,090,000 in 1981.

Telecommunications Property
Telecommunications property is recorded at original cost and includes certain costs related to pension, payroll taxes, funds used during construction and general overheads applicable to the construction activity. In conformity with the prevailing practice in the Canadian telecommunications industry, the Company charges to operating expenses the costs of maintenance of property and replacement and renewals of items that are not units of property. Additions, replacements and renewals of property considered to be units of property are charged to telecommunications property accounts. The original cost of telecommunications property retired is charged to accumulated depreciation or transferred to construction materials when such property can be re-used; therefore, no gain or loss on retirement is recognized in the statement of income.

Depreciation
Depreciation is computed on the straight-line method using rates based on the estimated useful lives of the assets. The composite depreciation rate was 6.49% in 1980 and 6.99% in 1981.

Investment
The investment in Common shares of Télésat Canada is recorded at original cost. Its estimated value under the equity method as at December 31, 1981 was $1,079,000.

Amortization of Discount and Expenses on Long-Term Debt
The discount and expenses on long-term debt are amortized over the life of each series of bonds and the amortization is included in interest charges.

Income Taxes
The Company uses the tax allocation method to account for temporary variations between taxable and booked income.

Long-Distance Service Revenues
The Company receives part of its long-distance service revenues pursuant to agreements with other telecommunications companies for services provided jointly. The Company's actual share of the joint business cannot be specifically determined before the completion of settlement studies. In management's opinion such revenues are reasonable estimates of the amounts ultimately accruing to the Company.

Translation of Foreign Currencies
Current and long-term debt transactions completed in foreign currencies are translated into Canadian dollars at the rate of exchange prevailing at the respective transaction date except for long-term debt issued before June 1, 1970 which has been translated at the rate of exchange prevailing before the Canadian dollar was floated.

Exchange gains or losses are reflected in the statement of income as they occur.

2.Capitalization

Capital Stock
During 1981, transactions related to the capital stock of the Company were as follows:

	Common	Subordinate, Series B	Preferred
Shares outstanding at December 31, 1980	3,979,035	15,106	1,269,103
Issued	113,823	—	—
Redeemed	—	—	(89,683)
Converted	971	(971)	—
Shares outstanding at December 31, 1981	**4,093,829**	**14,135**	**1,179,420**

Common Shares
During the year 1981, 113,823 Common shares amounting to $2,028,543 were issued under the Common Shareholders' Dividend Reinvestment and Share Purchase Plan and under the Employees' Stock Purchase Plan. Also 971 $1.68 Cumulative Redeemable Convertible Subordinate Preferred shares, Series B were converted into 971 Common shares.

As of December 31, 1981, 250,690 Common shares were reserved for conversion of the Convertible Subordinate Preferred shares and for issuance under the Common Shareholders' Dividend Reinvestment and Share Purchase Plan and under the Employees' Stock Purchase Plan.

Subordinate Preferred Shares
The $1.68 Cumulative Redeemable Convertible Subordinate Preferred shares, Series B are convertible at the option of the holders thereof at any time on or before June 30, 1986, into one Common share for each share so converted.

Since more than 85% of the original issue has now been converted into Common shares, the Company has the option at any time to redeem all or part of the outstanding Series B shares at the then current redemption price.

Preferred Shares
In order to meet the sinking fund requirements for the 1955 and 1956 Series, payments for the next five years will be as follows: $39,446 in 1982 and $50,000 for each of the years 1983, 1984, 1985 and 1986.

In addition, the Company must redeem each year 30,000 Preferred shares, Series 1975, at par value and make all reasonable efforts to redeem each year 9,000 Preferred shares, Series 1973, at a price not exceeding $20.

The Company must call for redemption and redeem 31,248 Preferred shares, Series 1977 on October 1, in each of the years 1982 to 1985 inclusive, and the remaining 250,016 Preferred shares, Series 1977 on October 1, 1986 at their par value.

Long-Term Debt
The Trust Deeds of the Company require the use of a sinking fund or the pledge of additional unmortgaged property for each of the series as follows:

a) Series F, H and I, First Mortgage and Series D, General Mortgage:
   Annual payment of $1^1/2$% of the principal amount of the bonds issued.
b) Series J, M, N, O, P, Q and R, First Mortgage:
   Annual payment of 1% or additional mortgage of $1^1/2$% of the principal amount of bonds issued. During the previous years, the Company used the latter alternative.
c) Series L, First Mortgage:
   Annual payment of $8,960 representing 2% of the aggregate principal amount of bonds issued and not prepaid on April 15, 1975.

To meet the sinking fund requirements and the debt retirements, the following payments will have to be made during the next five years:

Year ending December 31	Requirements: Sinking fund payments	Requirements: Debt retirements
	Thousands of dollars	
1982	$ 231	$ 3,405
1983	223	28,575
1984	174	2,319
1985	174	—
1986	174	—

As of December 31, 1981, the principal amount of the Series F and Series O which principal and interest are payable in United States funds amounted to $2,416,220 and $15,920,850 respectively. At the rate of exchange prevailing on December 31, 1981, the Series F would stand at $2,653,168 and the Series O at $19,587,150.

First Mortgage Bonds of all series are secured equally and rateably under a fixed and specific hypothec, mortgage, pledge, charge, cession and transfer of/and on all immovable property, such as buildings, equipment, telephone lines and apparatus, rights-of-way and similar rights and a floating charge on all other assets. The security provided for the General Mortgage Bonds is similar but subordinated to that provided for the First Mortgage Bonds.

3. Construction Program

The cost of the Company's program for improvements and construction of new plant and facilities in 1982, as now planned, is estimated at $45.0 million, including the cost of re-usable material and equipment; purchase commitments amounting to approximately $1.6 million have been made in connection therewith as of December 31, 1981.

4. Operating Expenses

Traffic expenses represent mainly operators' wages incurred in handling telephone calls; customer services and marketing expenses represent costs incurred in business relations with customers, advertising and directories; administrative and other expenses include principally accounting, data processing, budget, internal auditing, engineering costs incurred for planning and administrative purposes, stationery expenses and office services such as mail, house service and the administration of a purchase department.

5. Pension Plan

The Company maintains a funded pension plan for the benefit of its employees in conformity with the requirements of the Québec Supplemental Pension Plans Act. As a rule, an annual actuarial study is made for administration purposes.

The total unrecorded estimated liability for past services was $707,602 at the end of 1980 and, with interests thereon, was to be amortized by annual instalments of $77,260 to December 31, 1993.

Significant improvements to the benefits ensuing to the participants have been made to the pension plan, most particularly to the hourly employees covered by collective agreements signed on December 29, 1981; based on a preliminary actuarial study in progress at December 31, 1981, the total unrecorded estimated past service liability would be approximately $2,750,000 at December 31, 1981. This amount, plus interests thereon, would be amortized by annual instalments of approximately $360,000 to December 31, 1996.

The cost inherent to this pension plan charged to operating expenses was $1,514,000 for the year ended December 31, 1981 and $1,222,000 for 1980.

6.General Taxes

General taxes were as follows:

	1981	1980
	Thousands of dollars	
Tax on capital	**$ 1,117**	$ 573
Tax based on the Real Estate Assessment Act	**5,343**	4,834
Other real estate taxes	**421**	395
Payroll taxes	**2,550**	1,570
Other taxes	**88**	84
	9,519	7,456
Less: portion capitalized	**404**	323
	$ 9,115	$ 7,133

7.Other Income

This account includes an allowance for the cost of funds used during construction. For the year ended December 31, 1981, $826,999 ($505,482 in 1980) was applied to the telecommunications property at the rate of 11.03% (10.94% in 1980) and credited to other income. This rate reflects the Company's rate of return on total invested capital for the previous year.

8.Remuneration of Directors and Officers

The total direct remuneration of the directors and officers was $562,435 for the year ended December 31, 1981 and $549,248 for 1980.

9.Accumulated Depreciation

Changes in the accumulated depreciation account were as follows:

	1981	1980
	Thousands of dollars	
Balance at beginning of year	**$107,888**	$ 93,083
Depreciation charged to operations	**26,318**	22,470
Depreciation on motor vehicles, tools and others	**1,103**	929
Less: telecommunications property retired (net value)	**8,984**	8,594
Balance at end of year	**$126,325**	$107,888

10.Short-Term Debt

At December 31, short-term debt included:

	1981	1980
	Thousands of dollars	
Short-term notes		
Bank	**$ 9,475**	$ 5,250
La Compagnie de Téléphone Anglo-Canadienne	**2,000**	—
	11,475	5,250
Sinking fund payments on Cumulative Redeemable Preferred shares	**1,265**	1,256
Sinking fund payments on long-term debt	**231**	286
Retirement of First Mortgage Bonds, $5^1/_2$%, Series G	**3,405**	—
	$16,376	$ 6,792

The average interest rate on short-term notes was 19.86% in 1981 and 13.44% in 1980.

The Company's policy is to utilize short-term financing mainly to finance its construction program pending long-term financing. In computing the rate of return on average invested capital and interest as a percentage of average debt, short-term debt is included in total capitalization.

11.Income Taxes

The Company has been assessed by the Department of National Revenue and by the Department of Revenue of Québec up to and including December 31, 1980. Audits have also been made respectively by the Department of National Revenue from 1977 to 1979 inclusively and by the Department of Revenue of Québec from 1974 to 1978 inclusively. These audits have not yet been completed but management estimates that no important liability should ensue.

The effective income tax rate was 50.8% in 1981 and 50.6% in 1980.

Current and deferred income taxes for the years were as follows:

	1981	1980
	Thousands of dollars	
Current	**$10,061**	$ 7,358
Deferred	**3,760**	4,159
	$13,821	$11,517

The reconciliation of the income tax accounts shown in the balance sheets is presented below:

	Current income taxes		Deferred income taxes	
	1981	1980	**1981**	1980
	Thousands of dollars			
Balance at beginning of year	**$ 1,313**	$3,406	**$56,397**	$52,082
Payments	**(7,751)**	(9,082)	**—**	—
Provision	**10,061**	7,358	**3,760**	4,159
Prior years' adjustments	**(239)**	(369)	**234**	156
Balance at end of year	**$ 3,384**	$1,313	**$60,391**	$56,397

12. Change in Working Capital other than Short-Term Debt

The change in working capital is accounted for by:

	1981	1980
	Thousands of dollars	
Increase (decrease) in current assets		
Cash	**$ (198)**	$ (676)
Accounts receivable	**2,051**	762
Prepaid expenses	**13**	69
(Increase) decrease in current liabilities		
Accounts payable and other accrued liabilities	**(2,667)**	(3,063)
Income taxes payable	**(2,071)**	2,093
Increase (decrease) in working capital	**$(2,872)**	$ (815)

13. Related Party Transactions

GTE International Incorporated, GTE Service Corporation, *La Compagnie de Téléphone Anglo-Canadienne,* AEL Microtel Limited, GTE Sylvania Canada Limited and Dominion Directory Company Limited and their respective subsidiaries are direct or indirect affiliates of the Company.

The Company policy is to purchase high-quality goods and services at the best possible price. Consequently, no advantage is given to affiliates and transactions with these are made on a competitive basis, that is at the same or better conditions which would have prevailed if the parties had not been affiliated.

During 1981, the Company has paid in dividends, goods and services the sum of $74.5 million of which $10.3 million to affiliates. The Company has paid to *La Compagnie de Téléphone Anglo-Canadienne* interests on short-term notes amounting to $0.2 million, the rate of interest on these notes being the same as on promissory notes.

Management's Report

QUÉBEC-TELEPHONE

Management is responsible for the integrity and objectivity of data in the financial statements and complementary notes to the annual report.

Fully aware of this responsibility, Québec-Téléphone maintains elaborate systems of internal controls to ensure that the books and records supporting the financial statements present fairly all the transactions in accordance with generally accepted accounting principles and to ensure compliance with policies and administrative rules of conduct. The systems of internal controls are strengthened through periodic examinations conducted by the internal auditors and through the examination of financial statements by the external auditors, Arthur Andersen & Cie and Samson Bélair, Chartered Accountants.

The Board of Directors pursues its responsibility for these financial statements principally through its Audit Committee which meets periodically with management as well as with the internal and external auditors. The latter have full and free access to the Audit Committee, and meet with it, with and without management being present, to discuss auditing and financial reporting matters.

On behalf of management,

Simon Soucy

Simon Soucy
Vice President - Finance
and Treasurer

Raymond Sirois

Raymond Sirois
President and Chief
Executive Officer

Auditors' Report

To the Shareholders of Québec-Téléphone:

We have examined the consolidated balance sheets and consolidated statements of capitalization of Québec-Téléphone (a Québec company) and subsidiary as of December 31, 1981 and 1980, and the related consolidated statements of income and reinvested earnings and changes in financial position for the years then ended. Our examinations were made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, the accompanying consolidated financial statements present fairly the financial position of Québec-Téléphone and subsidiary as of December 31, 1981 and 1980, and the results of their operations and the changes in financial position for the years then ended, in accordance with generally accepted accounting principles applied on a consistent basis during the periods.

Samson Bélair

Samson Bélair
Chartered Accountants

Arthur Andersen & Cie

Arthur Andersen & Cie
Chartered Accountants

January 27, 1982

Five Years of Progress

QUÉBEC-TÉLÉPHONE

	1981	1980	1979	1978	1977
Selected results and reinvested earnings items (thousands of dollars)					
Operating revenues	**$ 130,884**	$ 112,000	$ 101,303	$ 84,136	$ 77,191
Operating expenses (excluding depreciation and general taxes)	**56,455**	47,775	42,040	34,137	31,156
Depreciation of telecommunications property	**26,318**	22,470	20,839	18,514	16,240
General taxes	**9,115**	7,133	6,203	4,110	3,405
Total operating expenses	**91,888**	77,378	69,082	56,761	50,801
Interest charges	**13,119**	12,642	12,347	10,936	10,846
Income taxes	**13,821**	11,517	10,015	8,718	8,045
Net income	**13,824**	11,640	10,902	9,590	8,643
Dividends on Preferred shares and Subordinate Preferred shares	**1,619**	1,765	1,882	2,094	2,332
Net income applicable to Common shares	**12,205**	9,875	9,020	7,496	6,311
Common share dividends	**8,089**	6,444	5,875	5,119	3,957
Reinvested net income	**4,116**	3,431	3,145	2,224	2,306
Selected balance sheet items (thousands of dollars)					
Telecommunications property, at cost	**$ 428,517**	$ 394,648	$ 361,496	$ 341,954	$ 301,140
Accumulated depreciation	**126,325**	107,888	93,083	83,826	69,811
Capitalization	**221,934**	221,325	205,673	203,842	169,107
Common share equity	**87,461**	81,316	63,864	60,225	45,668
Preferred shares and Subordinate Preferred shares	**22,549**	24,368	25,790	27,225	31,682
Long-term debt	**111,924**	115,641	116,019	116,392	91,757
Short-term debt	**16,376**	6,792	8,711	7,316	17,019
Financial statistics					
Average number of Common shares	**4,044,266**	3,502,114	3,318,706	3,010,975	2,431,980
Earnings per Common share	**$ 3.02**	$ 2.82	$ 2.72	$ 2.49	$ 2.59
Dividends declared per Common share	**$ 2.00**	$ 1.84	$ 1.77	$ 1.70	$ 1.625
Percent net income applicable to Common shares paid in dividends	**66.3%**	65.3%	65.1%	68.3%	62.7%
Value of Common shares issued					
Equity per Common share[1]	**$ 21.36**	$ 20.44	$ 19.16	$ 18.21	$ 17.32
Market value (high-low)[2]	**$ 20 7/8-16 1/2**	$ 23-18	$ 26-21 1/2	$ 24 1/2-20 1/2	$ 21-16 1/2
Rate of return					
On average Common share equity	**14.5%**	14.5%	14.6%	14.0%	15.5%
On average invested capital[3]	**11.6%**	11.0%	10.9%	10.3%	10.7%
Interest in percentage of average debt[3]	**10.6%**	10.1%	10.0%	9.5%	9.9%
Percent long-term debt to total capitalization	**51%**	52%	56%	57%	54%
Times interest earned before taxes	**3.45**	3.06	2.85	3.06	2.93
Number of Common shareholders	**3,295**	2,815	1,876	1,878	1,877
Other statistics					
Number of employees[1]	**2,166**	2,195	2,209	2,199	2,081
Salaries and benefits (thousands of dollars)	**$ 50,702**	$ 44,033	$ 39,645	$ 33,422	$ 30,398
Funds used for construction (thousands of dollars)	**$ 42,705**	$ 41,601	$ 35,840	$ 45,991	$ 37,255
Telecommunications property per telephone[1]	**$ 1,521**	$ 1,425	$ 1,362	$ 1,347	$ 1,250
Telephones in service[1]	**281,725**	276,870	265,337	253,854	240,982
Percent Automatic Number Identification	**72.8%**	66.2%	66.5%	64.8%	62.4%
Toll messages (thousands)	**30,002**	29,656	27,929	26,015	24,265

1. Year-end.
2. Valuation day value (December 22, 1971) : $13.75 per share.
3. See Note 10 to the accompanying financial statements.

Board of Directors

Hervé Belzile †
Chairman and Chief Executive Officer
Alliance compagnie mutuelle d'assurance-vie

Roger Charbonneau †
President
Laboratoires Anglo-French Limitée

Roger DeSerres *
President
Omer DeSerres Ltée

James L. Johnson
President - Telephone Operating Group
GTE Service Corporation

Charles Mercier *
Vice President - Marketing and Customer Service
Québec-Téléphone

M. Brian Mulroney *
President
Compagnie minière I O C

Bernard Panet-Raymond *†
President
O.R.C. Canada Inc.

Claude Pratte, Q.C. *
Advocate

William C. Rowland
Executive Vice President - Telephone Operating Group
General Telephone & Electronics Corporation
(retired on September 10, 1981)

Raymond Sirois **
President and Chairman of the Board
Québec-Téléphone

Antoine Turmel
Chairman and Chief Executive Officer
Provigo Inc.

** president of executive committee
* member of executive committee
† member of audit committee

Officers

Raymond Sirois
President and Chief Executive Officer

Charles Mercier
Vice President - Marketing and Customer Service

Ghislain Bouchard
Vice President - Human Resources and Legal Affairs, Secretary

Robert Duchesne
Vice President - Network Engineering and Construction

Simon Soucy
Vice President - Finance and Treasurer

Henri Dionne
Vice President - Public Relations

Gilles Laroche
Vice President - Business Development

Andrée Bélanger
Assistant Secretary

Director, Officer Changes

Mr. Henri Dionne, Vice President-Public Relations, retired after 42 years of service with the Company. At the end of this lengthy career, Québec-Téléphone is indebted to Mr. Dionne for his invaluable support and dedicated service in various functions with the Company.

Mr. Jean-Marc Tremblay, named Judge with the Provincial Court, was subsequently appointed Vice President of the *Régie des services publics* of Québec. On February 3, 1981, Mr. Ghislain Bouchard replaced Mr. Tremblay as Vice President-Human Resources and Legal Affairs, Secretary. At the same date, Mrs. Andrée Bélanger was appointed Assistant Secretary.

Mr. Robert Duchesne became Vice President-Network Engineering and Construction on April 14, 1981, replacing Mr. Denis Mercier who left the Company.

Mr. William C. Rowland, Executive Vice President-Telephone Operating Group, General Telephone & Electronics Corporation, retired on September 10, 1981 and resigned as a member of the Board of Directors of Québec-Téléphone on the same date.

Mr. Gilles Laroche was appointed Vice President-Business Development on November 3, 1981, with authority over the Revenue Requirements Planning, Strategic Planning and Public Relations Departments.

On behalf of the Board of Directors

Raymond Sirois
Chairman of the Board

General Information

Québec-Téléphone is incorporated under the laws of Québec by Letters Patent dated June 7, 1927 and is subject to the regulatory authority of the *Régie des services publics* of Québec.

Major Shareholder
As at December 31, 1981, *La Compagnie de Téléphone Anglo-Canadienne,* 8750, chemin de la Côte-de-Liesse, Saint-Laurent, Québec, owned 2,113,940 Common shares of Québec-Téléphone, or 51.6% of outstanding Common shares.

Listing of Shares
Common shares, 4 3/4% Preferred shares, 1965 Series, 7 3/4% Preferred shares, 1973 Series and $1.68 Cumulative Redeemable Convertible Subordinate Preferred shares, Series B are listed on the Montréal and Toronto stock exchanges. The 5% Preferred shares, 1955 and 1956 Series, are listed on the Montréal stock exchange.

Stock Transfer Offices
Trust Général du Canada, 1100, rue University, Montréal, Québec, is the Registrar and Transfer Agent for all classes of shares of the Company. *Compagnie Trust Royal* is the Co-Transfer Agent and Registrar for the 4 3/4% Preferred shares, 1965 Series, at its offices in Toronto and Winnipeg, and is the Co-Transfer Agent and Registrar for the 7 3/4% Preferred shares,1973 Series, for the $1.68 Cumulative Redeemable Convertible Subordinate Preferred shares, Series B and for the Company's Common shares at its offices in Saint John, N.B., Toronto, Winnipeg, Regina, Calgary and Vancouver.

Trustee for Bonds
Trust Général du Canada
1100, rue University
Montréal, Québec

Bankers
Banque Nationale du Canada
Banque de Montréal

Subsidiary
La Compagnie de Téléphone Bonaventure et Gaspé, Limitée
New Carlisle, Québec

Annual Meeting
Your Directors appreciate the interest shown by shareholders who attend the Annual General Meetings and who participate in the discussion of the Company's affairs. This year the meeting will be held on April 13, 1982, in Rimouski, Québec. All shareholders who find it possible to attend are urged to do so.

Territorial Map

This impressive picture of the Province is an actual retransmission from LANDSAT satellites launched and controlled by NASA. The composite is the result of 200 photographs taken at an altitude of 500 kilometers, and assembled by computer. The unusual colours are produced by the satellite's special camera eye which does not capture blue light, but picks up infrared rays. (Map issued by the *Ministère de l'Énergie et des Ressources* of Québec, Cartography Department.)

Reliability of our Services
(Typical Examples)

The installation by Québec-Téléphone of an electrocardiogram management system has helped the Rimouski Hospital to better affirm its regional vocation. Some 12 health care institutions in the Lower St. Lawrence and Gaspé regions are now routing an average volume of 50,000 electrocardiograms per year to the central computer located in Rimouski. Producing a diagnosis within two minutes, the system can handle 99% of all cases submitted. The breakthrough of Québec-Téléphone into this market is a first in the Canadian telecommunications industry.

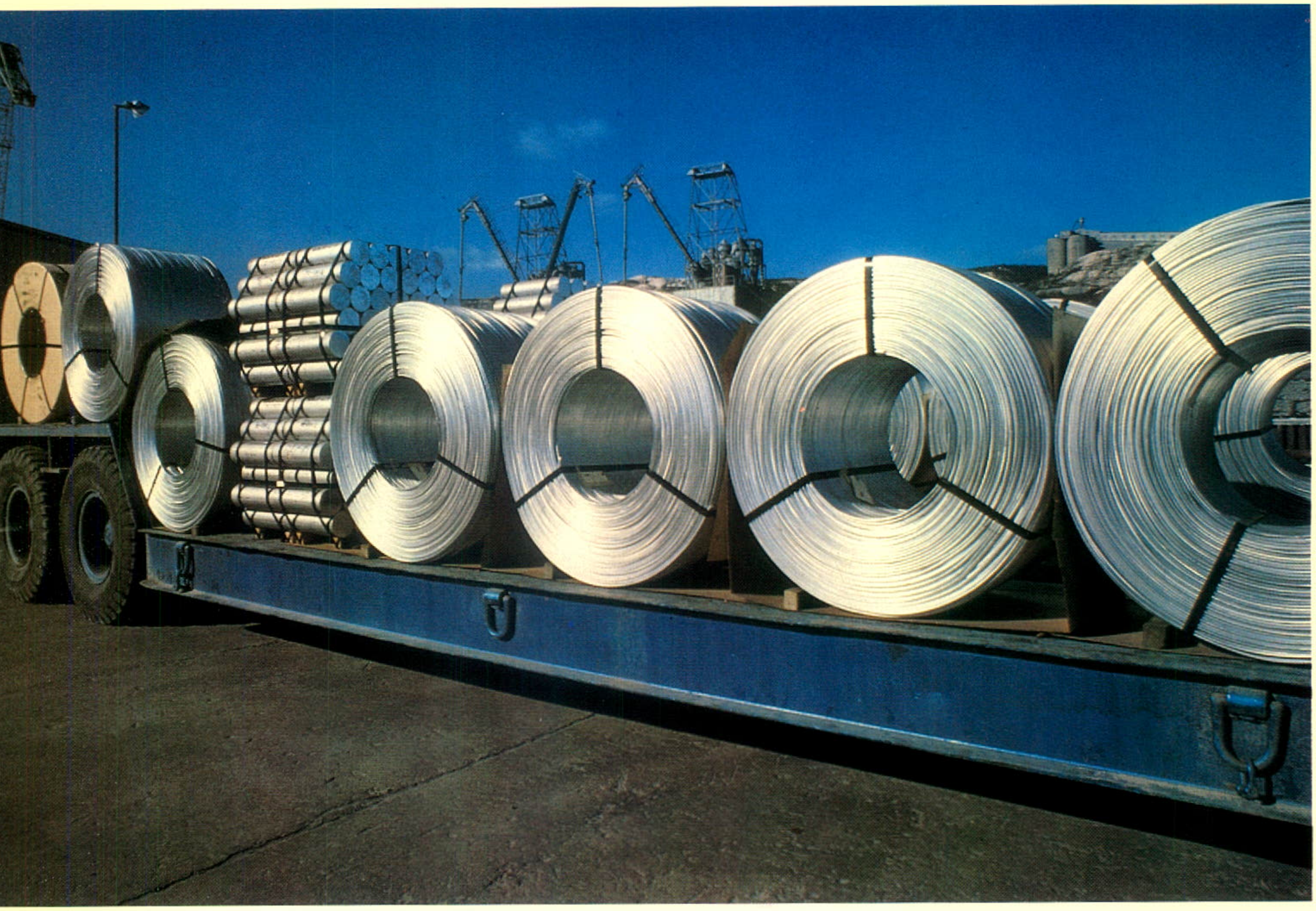
The second largest bus manufacturer in North America, *Prévost Car*, of Sainte-Claire, Dorchester County, will soon expand its operation to a new high technology field - the manufacturing of mechanical robots.

Like any prosperous, dynamic company, *Prévost Car* has always emphasized communications in its development planning. The Company, which uses an ultramodern private electronic switchboard, also takes advantage of a wide range of optional services for long-distance communications.

The *Sûreté du Québec* operates in Québec-Téléphone's entire territory. Coordination and effectiveness of police operations depend largely on extensive use of telecommunications resources. Mobile radio units and other modern data transmission systems are an integral part of the network.

One of the main contributors to the economic development of the North Shore, the *Société Canadienne de Métaux Reynolds Limitée*, in Baie-Comeau, produces 175,000 tons of primary aluminum castings per year. The Company, with its 356 pots, casts four basic shapes: blocks, billets, rods and ingots.

Equipped with a high-capacity private electronic switchboard, it also uses two-way telecopiers, Wide Area Telephone Service and teleprinters.



Founded in 1928 at Bic, near Rimouski, the *Coopérative Agricole du Bas-St-Laurent* is the second largest agricultural co-op in Québec. The modern agro-food enterprise has 1,850 members. It operates several subsidiaries in Québec and has obtained major export contracts to Africa and South America. The Co-op regularly uses Québec-Téléphone's specialized telecommunications services.

On peut obtenir des exemplaires français de ce rapport à l'adresse suivante:
Le secrétaire
Québec-Téléphone
6, rue Saint-Jean, Dép. 4
Rimouski (Québec)
G5L 7E4
Tél. : (418) 723-2271
TWX : 610-592-5921
Télex : 051-8-6338

QUÉBEC-TÉLÉPHONE

Head Office: 6, rue Saint-Jean, Rimouski (Québec) G5L 7E4