

Consolidated Financial Statements of

# **CARGOJET INC.**

For the years ended December 31, 2017 and 2016

(expressed in millions of Canadian dollars)



March 12, 2018

## **Independent Auditor's Report**

### **To the Shareholders of Cargojet Inc.**

We have audited the accompanying consolidated financial statements of Cargojet Inc., which comprise the consolidated balance sheets as at December 31, 2017 and December 31, 2016 and the consolidated statements of earnings and comprehensive income, the consolidated statements of changes in equity and the consolidated statements of cash flows for the years then ended, and the related notes, which comprise a summary of significant accounting policies and other explanatory information.

#### **Management's responsibility for the consolidated financial statements**

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

#### **Auditor's responsibility**

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

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

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**Opinion**

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Cargojet Inc. as at December 31, 2017 and December 31, 2016 and its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards.

**(Signed) “PricewaterhouseCoopers LLP”**

**Chartered Professional Accountants, Licensed Professional Accountants**

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# CARGOJET INC.

## Consolidated Balance Sheets

As at December 31, 2017 and December 31, 2016

(in millions of Canadian dollars)

	Note	2017	2016
		\$	\$
<b>ASSETS</b>			
<b>CURRENT ASSETS</b>			
Cash		5.7	2.2
Trade and other receivables		40.1	25.7
Inventories	3	0.9	0.9
Prepaid expenses and deposits		5.8	2.7
Income taxes recoverable		0.1	0.1
Derivative financial instruments	25	1.8	6.8
		54.4	38.4
<b>NON-CURRENT ASSETS</b>			
Property, plant and equipment	4, 8	514.7	371.1
Goodwill	5	46.4	46.4
Intangible assets		2.0	2.0
Deposits		5.7	4.6
Deferred income taxes	12	4.5	1.3
		627.7	463.8
<b>LIABILITIES</b>			
<b>CURRENT LIABILITIES</b>			
Trade and other payables	7	38.1	30.4
Borrowings	8	-	35.7
Finance leases	9	62.1	12.7
Provisions	10	0.1	0.7
Dividends payable		2.6	1.9
Derivative financial instruments	25	1.6	-
		104.5	81.4
<b>NON-CURRENT LIABILITIES</b>			
Borrowings	8	124.5	0.2
Finance leases	9	99.1	117.6
Provisions	10	1.2	1.7
Convertible debentures	11	114.8	181.1
Deferred income taxes	12	18.5	6.5
Pension benefit liability	19	10.5	8.7
		473.1	397.2
<b>EQUITY</b>			
		154.6	66.6
		627.7	463.8

The accompanying notes are an integral component of these consolidated financial statements.

# CARGOJET INC.

## Consolidated Statements of Earnings and Comprehensive Income Years ended December 31, 2017 and 2016

(in millions of Canadian dollars except per share data)

	Note	2017	2016
		\$	\$
REVENUES		382.9	331.0
DIRECT EXPENSES	13	276.6	245.2
		106.3	85.8
General and administrative expenses	14	47.6	43.2
Sales and marketing expenses		1.7	2.3
Impairment of property, plant and equipment	4	-	3.9
Finance costs	15	25.2	30.8
Loss on extinguishment of debt	8	2.3	7.5
Other gain (net)	16	(4.1)	(4.9)
		72.7	82.8
EARNINGS BEFORE INCOME TAXES		33.6	3.0
PROVISION FOR INCOME TAXES	12		
Deferred		9.9	0.6
NET EARNINGS AND COMPREHENSIVE INCOME		23.7	2.4
EARNINGS PER SHARE	18		
- Basic		\$1.96	\$0.23
- Diluted		\$1.93	\$0.22

The accompanying notes are an integral component of these consolidated financial statements.

# CARGOJET INC.

## Consolidated Statements of Changes in Equity Years ended December 31, 2017 and 2016

(in millions of Canadian dollars)

	Note	Shareholders' capital	Contributed surplus	Conversion option	Surplus on debenture settlement	Deficit	Total shareholders' equity
		\$	\$	\$	\$	\$	\$
Balance, January 1, 2017		100.9	3.3	10.0	3.1	(50.7)	66.6
Net earnings and comprehensive income		-	-	-	-	23.7	23.7
Share-based compensation	20	-	3.1	-	-	-	3.1
Restricted shares, dividend shares and options vested and exercised	17,20	3.8	(3.8)	-	-	-	-
Deferred tax on conversion option		-	-	1.7	(1.7)	1.1	1.1
Convertible debenture-conversion	11,17	69.7	-	(6.6)	6.6	-	69.7
Dividends	17	-	-	-	-	(9.6)	(9.6)
<b>Balance, December 31, 2017</b>		<b>174.4</b>	<b>2.6</b>	<b>5.1</b>	<b>8.0</b>	<b>(35.5)</b>	<b>154.6</b>
Balance, January 1, 2016		91.3	2.0	5.1	2.8	(46.4)	54.8
Net earnings and comprehensive income		-	-	-	-	2.4	2.4
Treasury shares-net		0.2	(0.2)	-	-	-	-
Conversion option on debenture redemption		-	-	7.1	-	-	7.1
Private placement of shares		3.3	-	-	-	-	3.3
Restricted shares vested		1.6	(1.6)	-	-	-	-
Share-based compensation		-	3.1	-	-	-	3.1
Deferred tax on conversion option-net		-	-	(1.9)	-	0.1	(1.8)
Convertible debenture-conversion	11	4.5	-	(0.3)	0.3	-	4.5
Dividends	17	-	-	-	-	(6.8)	(6.8)
<b>Balance, December 31, 2016</b>		<b>100.9</b>	<b>3.3</b>	<b>10.0</b>	<b>3.1</b>	<b>(50.7)</b>	<b>66.6</b>

The accompanying notes are an integral component of these consolidated financial statements.

# CARGOJET INC.

## Consolidated Statements of Cash Flows

### Years ended December 31, 2017 and 2016

(in millions of Canadian dollars)

	Note	2017	2016
		\$	\$
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>			
Net earnings		23.7	2.4
Items not affecting cash			
Depreciation of property, plant and equipment	4	49.7	42.0
Share-based compensation	20	3.1	3.2
Finance costs	15	25.2	30.8
Gain on derecognition of provision for lease return conditions	10	(1.6)	-
Impairment of property, plant and equipment	4	-	3.9
Employee pension	19	1.8	8.7
Income tax provision	12	9.9	0.6
Other gains	16	(1.2)	(4.3)
		110.6	87.3
Items affecting cash			
Interest paid		(21.0)	(27.7)
		89.6	59.6
Changes in non-cash working capital items and deposits			
Trade and other receivables		(14.4)	(2.8)
Inventories		-	(0.1)
Prepaid expenses and deposits		(4.2)	1.9
Trade and other payables		7.7	3.4
<b>NET CASH GENERATED FROM OPERATING ACTIVITIES</b>		<b>78.7</b>	<b>62.0</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>			
Purchase of property, plant and equipment	4	(135.7)	(59.8)
Proceeds from total return swap & settlement of derivative financial instrument		5.7	-
Collection of notes receivable		-	0.2
<b>NET CASH USED IN INVESTING ACTIVITIES</b>		<b>(130.0)</b>	<b>(59.6)</b>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>			
Repayment of borrowings		(35.2)	(137.4)
Proceeds from borrowings		124.3	38.0
Repayment of obligations under finance leases		(24.2)	(22.4)
Proceeds from debenture issuance net of issuance costs		-	119.3
Proceeds from private placement		-	3.3
Dividends paid to shareholders		(8.9)	(6.4)
<b>NET CASH PROVIDED FROM (USED IN) FINANCING ACTIVITIES</b>		<b>56.0</b>	<b>(5.6)</b>
<b>EFFECT OF EXCHANGE RATE CHANGES</b>		<b>(1.2)</b>	<b>(0.6)</b>
<b>NET CHANGE IN CASH</b>		<b>3.5</b>	<b>(3.8)</b>
<b>CASH, BEGINNING OF YEAR</b>		<b>2.2</b>	<b>6.0</b>
<b>CASH, END OF YEAR</b>		<b>5.7</b>	<b>2.2</b>

The accompanying notes are an integral component of these consolidated financial statements.



# **CARGOJET INC.**

## **Notes to the Consolidated Financial Statements**

**December 31, 2017 and 2016**

**(in millions of Canadian dollars except where noted)**

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### **1. NATURE OF THE BUSINESS**

Cargojet Inc. (“Cargojet” or the “Company”) operates a domestic overnight air cargo co-load network between fourteen major Canadian cities. The Company also provides dedicated aircraft to customers on an Aircraft, Crew, Maintenance and Insurance (“ACMI”) basis, operating between points in Canada and the USA. As well, the Company operates scheduled international routes for multiple cargo customers between the USA and Bermuda and Canada and Germany and flights between Canada, Colombia, and Peru.

Cargojet is publicly listed with shares and convertible debentures traded on the Toronto Stock Exchange (“TSX”). The Company is incorporated in Ontario and domiciled in Canada and the registered office is located at 2281 North Sheridan Way, Mississauga, L5K 2S3, Ontario.

These consolidated financial statements (the “financial statements”) were approved and authorized for issuance by the Board of Directors on March 12, 2018.

### **2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

#### **Statement of Compliance**

These financial statements have been prepared in accordance with generally accepted accounting principles in Canada (“GAAP”), as set out in the Chartered Professional Accountants of Canada Handbook – Accounting (“CPA Handbook”), which incorporates International Financial Reporting Standards (“IFRS”) as issued by the International Accounting Standards Board (“IASB”).

#### **Basis of preparation**

These financial statements include the accounts of the Company and its wholly owned subsidiaries, Cargojet GP Inc. (“CGP”), Cargojet Holdings Limited Partnership (“CHLP”), and CHLP’s wholly owned subsidiaries, Cargojet Holdings Ltd. (“CJH”), CJH’s wholly owned subsidiary, 2422311 Ontario Inc., CJH’s wholly owned subsidiary, ACE Air Charter Inc. (“ACE”), ACE’s wholly owned subsidiaries, ACE Maintenance Ontario Inc. (“ACEM”), 2166361 Ontario Inc. (“ACEO”), and ACEO’s wholly owned subsidiary, Navigatair Inc. (“NAVIGATAIR”), CJH’s wholly owned subsidiary, Cargojet Airways Ltd. (“CJA”) Cargojet Partnership (“CJP”) and Aeroship Handling Ltd. (“AH”).

All intra-company balances and transactions are eliminated in full on consolidation. The company has also reclassified previous year figures in accordance with the change in presentation applicable in the current year.

#### **Cash**

Cash balance consists of cash on hand and demand deposits.

# **CARGOJET INC.**

## **Notes to the Consolidated Financial Statements**

**December 31, 2017 and 2016**

**(in millions of Canadian dollars except where noted)**

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### **Prepaid expenses and deposits**

Prepaid expenses are cash paid amounts that represent costs incurred from which a service or benefit is expected to be derived in the future. The future write-off period of the incurred cost will normally be determined by the period of benefit covered by the prepayment. Prepaid expense specific to a particular period will be expensed when the period arrives and the costs will be treated as a period cost for that period. Prepaid costs for an extended period of time are normally written off equally during the period in which the benefit will be derived.

Prepaid expenses are generally classified as current assets unless a portion of the prepayment covers a period longer than twelve months.

Deposits include vendor deposits and lease security deposits and are classified as loans and receivables and are measured at amortized cost using the effective interest rate method.

### **Revenue recognition**

Revenue is recognized when the transportation services are complete. Revenue from overnight cargo services is recorded based on actual volume of cargo at agreed upon rates when the cargo services have been provided. Minimum guaranteed contract revenue is recognized in the event that the actual volumes do not exceed the guaranteed minimum volumes. Amounts recognized include surcharges. Ad hoc revenue for non-contract customers is recorded at the time the cargo services have been provided.

Revenue from the lease of aircraft is billed on the basis of a contracted rate and recorded when the lease rental service is provided.

Interest revenue is recognized when earned.

### **Inventories**

Fuel inventories are stated at the lower of cost and net realizable value. Net realizable value represents the estimated selling price for inventories less costs necessary to make the sale.

### **Property, plant and equipment**

Property, plant and equipment are carried at cost, less accumulated depreciation and any recognized impairment losses. Cost includes expenditures that are directly attributable to the acquisition or construction of the asset. Purchased software that is integral to the functionality of related equipment is capitalized as part of that equipment.

Property, plant and equipment under development relates to the purchase, construction and/or modification of aircraft and other property, plant and equipment that is not yet available for use. These assets are carried at costs. Cost includes expenditures that are directly attributable to the purchase, or modification of the asset. Borrowing costs attributable to the purchase, construction or modification of qualifying assets are capitalized to the cost of the item until the asset is ready for use. Once the property, plant and equipment are ready for use, the respective cost of property, plant and equipment will be transferred to the qualifying class of assets.

When a significant part of an asset has a different useful life from the overall asset's useful life, it is identified as a separate component and depreciated accordingly.

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**Notes to the Consolidated Financial Statements**  
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(in millions of Canadian dollars except where noted)

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Spare parts are treated as property, plant and equipment and depreciated based on actual usage.

The Company recognizes airframe heavy maintenance expenditures for owned and certain leased aircraft using the deferral method. Under the deferral method, the actual cost of each overhaul is capitalized under property, plant and equipment and amortized on a straight-line basis over the period to the next overhaul or the end of the lease term whichever is earlier. Any remaining carrying amount of the cost of the previous overhaul is derecognized.

The Company capitalizes the cost of rotatable parts purchased as an asset and depreciates it over its useful life of up to 10 years. The cost of repairing the rotatable part is recognized in maintenance expense when incurred.

Depreciation is recognized so as to amortize the cost of assets less their residual values over their useful lives using the straight-line method. The Company reviews the depreciation methods, useful lives and residual values at each reporting date with the effect of any changes in estimate accounted for on a prospective basis.

Property, plant and equipment are derecognized upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on the disposal or retirement of an item of property, plant and equipment is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognized in consolidated statement of earnings and comprehensive income.

The estimated useful lives are as follows:

<b>Asset</b>	<b>Estimated useful life</b>
Aircraft hull	30 – 45 years from the date of manufacture
Engines	4 - 15 years
Rotable spares	Up to 10 years
Spare parts	Actual usage
Ground equipment	Up to 10 years
Hangar and cross-dock facility	Up to 30 years
Vehicles	Up to 8 years
Computer hardware and software	Up to 5 years
Furniture and fixtures	Up to 10 years
Leasehold improvements	Lesser of useful life and term of lease
Deferred heavy maintenance	Up to the date of the next scheduled heavy maintenance or end of lease term whichever is earlier

**Leases**

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

# **CARGOJET INC.**

## **Notes to the Consolidated Financial Statements**

### **December 31, 2017 and 2016**

**(in millions of Canadian dollars except where noted)**

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#### *Finance leases*

Assets held under finance leases are initially recognized at their fair value or, if lower, at amounts equal to the present value of the minimum lease payments, each determined at the inception of the lease. The corresponding liability is included in the balance sheet as a finance lease obligation.

Lease payments are apportioned between finance charges and reduction of the lease obligation so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly into consolidated statement of earnings and comprehensive income, unless they are directly attributable to qualifying assets, in which case they are capitalized in accordance with the policy on borrowing costs. Contingent rents are recognized as expenses in the periods in which they are incurred.

Finance leased assets are reported under the relevant asset categories, with recognition of a corresponding financial liability. They are depreciated on a straight-line basis over the shorter of their estimated useful life and the term of the agreement.

#### *Operating leases*

Payments made under operating leases are charged to consolidated statement of earnings and comprehensive income on a straight-line basis over the term of the lease agreement. Contingent rents arising under operating leases are recognized as an expense in the period in which they are incurred. Lease incentives from operating leases are recognized on a straight-line basis over the term of the lease.

Rental income from operating leases is recognized on a straight-line basis over the term of the lease.

#### **Intangible assets**

Definite life intangible assets are carried at cost less accumulated amortization and accumulated impairment losses. Amortization is recognized on a straight-line basis over their estimated useful lives. Indefinite life intangible assets, such as licenses, have no foreseeable limit to the period over which they are expected to generate net cash inflows and are carried at cost less accumulated impairment losses and are not amortized.

The estimated useful life and amortization method are reviewed at the end of each annual reporting period, with the effect of any changes in estimate being accounted for on a prospective basis.

#### **Impairment of tangible and intangible assets excluding goodwill**

At the end of each reporting period, the Company reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss. Where it is not possible to estimate the recoverable amount of an individual asset, the Company estimates the recoverable amount of the cash-generating unit ("CGU") to which the asset belongs. Where a reasonable and consistent basis of allocation can be identified, corporate assets are also allocated to an individual CGU, or otherwise they are allocated to the smallest group of CGU's for which a reasonable and consistent allocation basis can be identified.

Intangible assets with indefinite useful lives are tested for impairment at least annually, and whenever there is an indication that the asset may be impaired.

The recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.

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## **Notes to the Consolidated Financial Statements**

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If the recoverable amount of an asset or CGU is estimated to be less than its carrying amount, the carrying amount of the asset or CGU is reduced to its recoverable amount. An impairment loss is recognized immediately in consolidated statement of earnings and comprehensive income.

Where an impairment loss subsequently reverses, the carrying amount of the asset or CGU is increased to the revised estimate of its recoverable amount. However, the increased carrying amount cannot exceed the carrying amount that would have been determined had no impairment loss been recognized for the asset or CGU in prior years. A reversal of an impairment loss is recognized immediately in consolidated statement of earnings and comprehensive income.

### **Goodwill**

Goodwill arising in a business combination is recognized as an asset at the date that control is acquired, and carried at cost as established on the acquisition date of the business less accumulated impairment losses, if any. Goodwill is measured as the excess of the sum of the consideration transferred, the amount of any non-controlling interests in the acquiree, and the fair value of the Company's previously held equity interest in the acquiree, if any, over the net of the acquisition-date amounts of the identifiable assets acquired and the liabilities assumed.

Goodwill is not amortized but is reviewed for impairment annually on April 1. For the purpose of impairment testing, goodwill is allocated to each of the Company's cash-generating units expected to benefit from the synergies of the combination. Cash-generating units to which goodwill has been allocated are tested for impairment annually, or more frequently when there is an indication that the cash-generating unit may be impaired. If the recoverable amount of the cash-generating unit is less than its carrying amount, the impairment loss is allocated first to reduce the carrying amount of any goodwill allocated to the cash-generating unit and then to the other assets of the cash-generating unit pro-rata on the basis of the carrying amount of each asset in the cash-generating unit. An impairment loss recognized for goodwill is not reversed in a subsequent period.

### **Foreign currencies**

The functional currency of each subsidiary is Canadian dollars, which is the currency of the primary economic environment in which each subsidiary and the Company operates. The results and financial position of each subsidiary are expressed in Canadian dollars.

Transactions in currencies other than the entity's functional currency are recognized at the rates of exchange prevailing at the dates of the transactions. At the end of each reporting period, monetary items denominated in foreign currencies are retranslated at the exchange rates prevailing at that date. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

Exchange differences are recognized in consolidated statement of earnings and comprehensive income in the period in which they arise.

# **CARGOJET INC.**

## **Notes to the Consolidated Financial Statements**

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**(in millions of Canadian dollars except where noted)**

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### **Borrowing costs**

Borrowing costs specifically attributable to the acquisition, construction or production of qualifying assets, which are assets that necessarily take a substantial period of time to get ready for their intended use or sale, are added to the cost of those assets. Borrowing costs, for the funds that are borrowed generally and used for the purpose of obtaining a qualifying asset, are capitalized by applying a capitalization rate to the expenditures on that asset. The capitalization rate is the weighted average borrowing rate to the Company that are outstanding during the period, other than borrowings made specifically for the purpose of obtaining a qualifying asset.

All other borrowing costs are recognized in consolidated statement of earnings and comprehensive income in the period in which they are incurred.

### **Income taxes**

#### *Deferred taxes*

Deferred taxes are recognized on temporary differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable income or loss. Deferred tax liabilities are generally recognized for all taxable temporary differences. Deferred tax assets are generally recognized for all deductible temporary differences to the extent that it is probable that taxable income will be available against which those deductible temporary differences can be utilized. Such deferred tax assets and liabilities are not recognized if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable income nor the accounting income.

The carrying amount of deferred tax assets is reviewed at the end of each reporting period and reduced to the extent that it is no longer probable that sufficient taxable income will be available to allow all or part of the asset to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the period in which the liability is settled or the asset realized, based on tax rates that have been enacted or substantively enacted by the end of the reporting period. The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Company expects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and the Company intends to settle its current tax assets and liabilities on a net basis.

#### *Current and deferred taxes for the period*

Current and deferred taxes are recognized in consolidated statement of earnings and comprehensive income, except when they relate to items that are recognized outside income (such as in other comprehensive income or directly in equity), in which case the current and deferred tax is also recognized outside income, or where they arise from the initial accounting for a business combination. In the case of a business combination, the tax effect is included in the accounting for the business combination.

# **CARGOJET INC.**

## **Notes to the Consolidated Financial Statements**

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**(in millions of Canadian dollars except where noted)**

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### **Provisions**

Provisions are recognized when the Company has a present obligation (legal or constructive) as a result of a past event, it is probable that the Company will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation.

The amount recognized as a provision is the best estimate of the consideration required to settle the present obligation at the end of the reporting period, taking into account the risks and uncertainties surrounding the obligation. Where a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those estimated cash flows.

### **Share based payments**

#### Equity-settled share-based compensation plans

##### *Long-term incentive plan (the “Plan” or “LTIP”)*

Equity-settled share-based compensation plans are granted to eligible employees as disclosed in Note 20, which are measured at the market value of the Company's voting shares on the date of the grant based on the units granted to the employees. The Company's voting shares to be distributed to the employees are acquired from the open market and held in trust as treasury shares, and recorded as a reduction of share capital. The cost of the equity-settled share-based compensation plans is recognized as a compensation expense with a corresponding increase in equity over the related service period provided to the Company as vested. Upon the distribution of the Company's voting shares, the Company's voting shares previously held as treasury shares are recorded as an increase in share capital.

##### *Restricted share units (“RSU”)*

Restricted share units are granted to non-employee directors and certain key executives and are measured at the fair value of the Company's voting shares on the date of the grant based on the units granted to the non-employee directors and certain key executives. The cost of the restricted share units are recognized as a compensation expense with a corresponding increase in equity over the related vesting period as service is provided to the Company.

##### *Stock options (“Options”)*

Stock options are granted to non-employee directors and certain key executives and are measured at the fair value of the Company's voting shares on the date of the grant. The cost of the stock options are recognized as a compensation expense with a corresponding increase in equity over the related vesting period as service is provided to the Company.

##### *Cash-settled share-based compensation options*

The Company provides cash-settled share-based compensation options to an equipment finance and leasing company as an additional fee in respect of each lease contract as disclosed in Note 8 and Note 9, respectively. A liability is recognized for the service rendered and is initially measured at the fair value using an option pricing model, and a corresponding amount is capitalized as a part of the acquisition costs of the assets or the transaction costs of the related financial instruments.

The liability is re-measured at each reporting period with any further re-measurement of the liability due to the change in the fair value of the option is recognized as other gains or losses on the consolidated statement of earnings and comprehensive income during the period.

**CARGOJET INC.**  
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(in millions of Canadian dollars except where noted)

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**Financial instruments**

Financial assets are classified into the following specified categories: fair value through consolidated statement of earnings and comprehensive income (“FVTPL”), held to maturity investments, available for sale (“AFS”) financial assets and loans and receivables. The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition. All financial liabilities are classified as either FVTPL or other financial liabilities.

The Company’s financial assets and financial liabilities are classified and measured as follows:

<u>Asset/Liability</u>	<u>Classification</u>	<u>Measurement</u>
Cash, trade and other receivables, notes receivables, and deposits	Loans and receivables	Amortized cost
Trade and other payables, dividends payable, borrowings and convertible debentures	Other financial liabilities	Amortized cost
Derivative financial instruments	Fair value through consolidated statement of earnings and comprehensive income	Fair value

*Loans and receivables and other financial liabilities*

Cash, trade and other receivables, notes receivable, deposits, trade and other payables, dividends payable, convertible debentures and borrowings are initially recognized at fair value and subsequently at amortized cost using the effective interest method less any impairment. Interest is recognized by applying the effective interest rate.

*Derivative financial instruments*

Derivative financial instruments are utilized by the Company occasionally in the management of its foreign currency exposures. The Company’s policy is not to utilize derivative financial instruments for trading or speculative purposes. Derivatives embedded in non-derivative host contracts are treated as separate derivatives when they meet the definition of a derivative, their risks and characteristics are not closely related to those of the host contracts and the contracts are not measured at FVTPL. All derivative financial instruments are recorded at their fair values.

Derivatives are initially recognized at fair value at the date the derivative contract is entered into and are subsequently re-measured to their fair value at the end of each reporting period. The resulting gain or loss is recognized in consolidated statement of earnings and comprehensive income immediately.

A derivative with a positive fair value is recognized as a financial asset; a derivative with a negative fair value is recognized as a financial liability.

*Basis of fair values*

Assets and liabilities recorded at fair value on the balance sheet are classified using a fair value hierarchy that reflects the significance of the inputs used in making the measurements. The fair value hierarchy has the following levels:

Level 1 - valuation based on quoted prices (unadjusted) observed in active markets for identical assets or liabilities.



# **CARGOJET INC.**

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Level 2 - valuation techniques based on inputs that are quoted prices of similar instruments in active markets; inputs other than quoted prices used in a valuation model that are observable for that instrument; and inputs that are derived principally from or corroborated by observable market data by correlation or other means.

Level 3 - valuation techniques with significant unobservable market inputs.

There have been no significant transfers between levels in the year.

#### *Impairment of financial assets*

Financial assets, other than those at FVTPL, are assessed for indicators of impairment at the end of each reporting period. Financial assets are considered to be impaired when there is effective evidence that as a result of one or more events that occurred after the initial recognition of the financial assets, the estimated future cash flows of the assets have been affected.

For certain categories of financial assets, such as trade and other receivables, assets that are assessed not to be impaired individually are, in addition, assessed for impairment on a collective basis. Objective evidence of impairment could include the Company's past experience of collecting payments, an increase in the number of delayed payments past the average credit period, as well as observable changes in national or economic conditions that correlate with default on global receivables.

#### *De-recognition of financial assets and liabilities*

De-recognition is applied for all or part of a financial asset, when the contractual rights making up the asset expire, or the Company substantially transfers most of the significant risks and benefits associated with ownership of the asset. De-recognition is applied for all or part of a financial liability, when the liability is extinguished due to cancellation or expiry of the obligation. When a debt is renegotiated with a lender giving rise to substantially different terms, a new liability is recognized.

#### **Employee benefits**

The Company has adopted an unfunded defined benefit pension plan. A defined benefit plan is a post-employment benefit plan (pension plan) that is not a defined contribution plan. Defined benefit plans define an amount of pension benefit that an employee will receive on retirement, usually dependent on one or more factors such as age, years of service and compensation. The Company's net obligation in respect of the defined benefit pension plan is calculated by estimating the amount of future benefit that the employee has earned in return for his service in the current and prior periods; that benefit is discounted to determine its present value. The calculations are performed by qualified actuaries using the projected unit credit prorated on service method that incorporates the Company's best estimates of future salary levels, other cost escalations, retirement age of employee and other actuarial factors. Due to the long-term nature of these plans, such estimates and assumptions are subject to inherent risks and uncertainties. These assumptions are determined by management and are reviewed by actuaries at least annually. The benefits under the plan will be reassessed annually by the qualified actuaries and the actuarial gain or loss in the fair value of the defined benefit plan will be recognized in the consolidated statement of earnings and comprehensive income. Changes to any of the above assumptions may affect the amounts of benefits obligations, expenses and re-measurements recognized. Past service costs arising from the plan are recognized immediately in the statement of consolidated earnings and comprehensive income.

# **CARGOJET INC.**

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The Company has also adopted an Individual Pension Plan (the "IPP") as a defined contribution plan. A liability and an expense in the amount of the contribution payable to the IPP are recognized when an employee renders services. Contributions to the IPP are discounted when they are payable more than 12 months after the end of the annual reporting period in which an employee rendered the related services. The discount rate is determined by reference to market yields at the end of the reporting period on high-quality corporate bonds of the same currency and the term as the IPP. Effective December 31, 2016, up to and until the date as of the member's Termination or Actual Retirement Date, whichever is earlier, the Company shall make a yearly contributions to the IPP in an amount equal to the lesser of (i) the "Money Purchase Limit" for the year and (ii) 18% of the IPP member's compensation from the Company, as defined in for this purpose under the Income Tax Act, for the year. The IPP member shall not be required nor permitted to contribute to the IPP.

### **Convertible debentures**

The component parts of compound instruments issued by the Company are classified separately as financial liabilities and equity in accordance with the substance of the contractual arrangement. At the date of issue, the fair value of the liability is measured separately using an estimated market rate for a similar liability without an equity component and the residual is allocated to the conversion option. The liability component is subsequently recognized on an amortized cost basis using the effective interest method until extinguished upon conversion or at the instrument's maturity date. The equity component is recognized and included in equity, and is not subsequently re-measured. In addition, the conversion option classified as equity will remain in equity until the conversion option is exercised, in which case, the balance recognized in equity will be transferred to another equity account. Transaction costs are divided between the liability and equity components in proportion to their values.

On the early redemption or repurchase of convertible debentures, the Company allocates the consideration paid on extinguishment to the liability based on its fair value at the date of the transaction and the residual is allocated to the conversion option. Any resulting gain or loss relating to the liability element is credited or charged to consolidated statement of earnings and comprehensive income and the difference between the carrying amount and the amount considered to be settled relating to the holder option is treated as a capital transaction.

### **Critical accounting judgments and key sources of estimation uncertainty**

In preparing the financial statements, the Company's management is required to make judgments, estimates and assumptions that may affect the reported amount of the assets, liabilities, revenues and expenses. Although these estimates are based on management's best knowledge of the current events and actions that the Company may undertake in the future, actual results may differ from these estimates. Reported amounts which require management to make significant estimates and assumptions include property, plant and equipment, goodwill, deferred taxes, provision, pension obligation and financial instruments. These items are discussed below.

### **Critical judgments in applying accounting policies**

#### *Componentization of property, plant and equipment*

The componentization of the Company's property, plant and equipment is based on management's judgment of the cost of the component in relation to the total cost of an asset and whether these components have different useful lives for determination of depreciation.

# **CARGOJET INC.**

## **Notes to the Consolidated Financial Statements**

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### *Impairment of property, plant and equipment, goodwill and intangibles assets*

Assessment of impairment is based on management's judgment of whether there are sufficient internal and external factors that would indicate that an asset of a CGU is impaired. The determination of CGUs is also based on management's judgment and is an assessment of the smallest group of assets that generate cash inflows independently of other assets. Factors considered include whether an active market exists for the output produced by the asset or group of assets as well as how management monitors and makes decisions about operations.

### *Classification of leases*

Assessing whether a lease is a finance lease or an operating lease is based on management's judgment of whether or not the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee.

### **Key sources of estimation uncertainty**

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised if the revision affects only that period or in the period of the revision and future periods if the revision affects both current and future periods.

### *Impairment of property, plant and equipment, goodwill and intangibles assets*

At the end of each reporting period, the Company reviews the carrying amounts of its property, plant and equipment, intangibles and goodwill to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss. Where it is not possible to estimate the recoverable amount of an individual asset, the Company estimates the recoverable amount of the cash-generating unit to which the asset belongs.

Recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted. If the recoverable amount of an asset or cash-generating unit is estimated to be less than its carrying amount, the carrying amount of the asset or cash-generating unit is reduced to its recoverable amount. Determining whether goodwill is impaired requires the Company to determine the recoverable amount of the cash-generating unit. To determine the recoverable amount of the cash-generating unit, management is required to estimate its fair value by evaluating expected future cash flow using an appropriate growth rate, margins, and a suitable discount rate to calculate the value in use.

### *Cash settled share based payment arrangement*

The cost and related liability of the Company's cash settled share based payment arrangement under a Master Capital Lease Agreement ("MLA") and the credit facility agreement with an equipment finance and leasing company is recognized using a Black-Scholes option pricing model involving assumptions including discount rates and early exercise dates. Due to the long-term nature of these rights, such estimates are subject to significant uncertainty.

# **CARGOJET INC.**

## **Notes to the Consolidated Financial Statements**

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#### *Deferred taxes*

Deferred tax assets are only recognized to the extent that it is probable that there will be sufficient taxable profits against which to utilize the benefits of the temporary differences and they are expected to reverse in the foreseeable future. The Company reviews the carrying amount of deferred tax assets at the end of each reporting period and assesses recoverability using forecasts that are based on the actual operating results and the expected future performance based on management's estimates and assumptions of revenue growth and the development. The deferred tax assets are reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

#### *Provisions*

The Company has estimated that it will incur certain maintenance costs at the end of its aircraft lease terms and has recorded a maintenance provision liability for these costs. Such costs have been estimated based on contractual commitments, current and estimated future aircraft utilization rate, the Company's maintenance program, rates provided by current maintenance service providers and Company specific history. The Company reviews the provisions at each reporting period to determine the change in estimated liability. The Company believes that the assumptions used are reasonable based on the information currently available but the final payments may change materially due to a change in timing, cost of maintenance or discount rates.

#### *Financial instruments*

The issuance of compound instruments, such as convertible debentures, requires the Company to estimate the debt and equity components of the instruments issued or repurchased. The component parts of the convertible debentures are classified separately as financial liabilities and equity in accordance with the substance of the contractual arrangement. At the date of issue, the fair value of the liability is measured separately using an estimated market rate for a similar liability without an equity component and the residual is allocated to the conversion option.

#### *Employee future benefits*

The cost and related liabilities of the Company's pension, other post-retirement and post-employment benefit programs are determined using actuarial valuations. The actuarial valuations involve assumptions including discount rates, future salary increases, mortality rates and future benefit increases. Also, due to the long-term nature of these programs, such estimates are subject to significant uncertainty.

## **Accounting changes**

### **Accounting standards effective for 2017**

There were no changes to the accounting standards that impacted the Company's accounting policies in the current year.

### **Standards, amendments and interpretations issued and not yet adopted**

*Financial instruments:* In July 2014, the IASB issued IFRS 9 (2014), *Financial Instruments* ("IFRS 9"), which replaces IAS 39, *Financial Instruments: Recognition and Measurement* ("IAS 39") in its entirety.

# **CARGOJET INC.**

## **Notes to the Consolidated Financial Statements**

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IFRS 9 introduces a single approach to determine whether a financial asset or liability is measured at amortized cost or fair value, a single, forward-looking “expected loss” impairment model and a substantially reformed approach to hedge accounting. Under IFRS 9, the criteria for classifying and measuring financial assets are principally based on how an entity manages such financial instruments in the context of its business model and whether the contractual cash flows of the financial assets give rise to payments on specified dates that are solely payments of principal and interest (“SPPI”). IFRS 9 also replaces the ‘incurred loss’ model in IAS 39 with a forward-looking expected credit loss (“ECL”) model that applies to all financial instruments, which will require more timely recognition of expected credit losses. It also includes changes in respect of own credit risk in measuring liabilities elected to be measured at fair value, so that gains caused by the deterioration of an entity’s own credit risk on such liabilities are no longer recognized in consolidated statement of earnings and comprehensive income. IFRS 9 is effective for annual periods beginning on or after January 1, 2018. The Company has made considerable progress in assessing its existing financial assets and financial liabilities. In assessing the cash flow characteristics of its existing financial assets, the Company has assessed its business model objectives and reviewed the underlying contractual terms to determine whether the SPPI criteria have been met. The Company anticipates that the majority of its existing receivables will be measured at amortized cost. For those receivables measured at amortized cost, the Company will assess whether an expected impairment loss exists by taking the practical expedient to measure lifetime expected credit losses for these instruments. Historically the credit losses have been minimal. The Company does not currently anticipate that there will be any material change in the measurement and classification of its existing financial assets and financial liabilities that are measured on a fair value basis. The Company plans to adopt the new standard on a retrospective basis.

*Revenue from Contracts with Customers:* IFRS 15, Revenue from Contracts with Customers (“IFRS 15”) which was issued by the IASB on May 28, 2014 outlines a single comprehensive model to account for revenue arising from contracts with customers and will replace the majority of existing IFRS requirements on revenue recognition including IAS 18, Revenue, IAS 11, Construction Contracts and related interpretations. The core principle of the standard is to recognize revenue to depict the transfer of goods and services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods and services. The standard has prescribed a five-step model to apply the principles. The standard also specifies how to account for the incremental costs of obtaining a contract and the costs directly related to fulfilling a contract as well as requiring more informative and relevant disclosures. IFRS 15 applies to nearly all contracts with customers, unless covered by another standard, such as leases, financial instruments and insurance contracts. In April 2016, the IASB issued amendments to IFRS 15, which provided additional guidance on the identification of performance obligations, on assessing principal versus agent considerations and on licensing revenue. The amendments also provide additional transition relief upon initial adoption of IFRS 15 and have the same effective date as IFRS 15. IFRS 15 is effective for annual periods beginning on or after January 1, 2018, with early adoption permitted. The Company expects no significant change in revenue recognition. The company expect to adopt the new standard on a retrospective basis.

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*Leases:* In January 2016, the IASB issued IFRS 16, *Leases*, which sets out the principles for the recognition, measurement, presentation and disclosure of leases for both parties to a contract, i.e., the customer ("lessee") and the supplier ("lessor"). IFRS 16 replaces the previous lease standard, IAS 17 *Leases*, and related interpretations. The most significant effect of the new requirements will be an increase in lease assets and financial liabilities as IFRS 16 eliminates the classification of leases as either operating leases or finance leases for a lessee. All leases are 'capitalized' by recognizing the present value of the lease payments and showing them either as lease assets (right-of-use assets) or together with property, plant and equipment. If lease payments are made over time, a company also recognizes a financial liability representing its obligation to make future lease payments. IFRS 16 is effective for annual periods beginning on or after January 1, 2019, with earlier adoption permitted. The Company is currently evaluating the impact of the adoption of this standard on its consolidated statement of earnings and comprehensive income.

*IFRS 2, Share-based payments ("IFRS 2")*, has been amended to address (i) certain issues related to the accounting for cash settled awards, and (ii) the accounting for equity settled awards that include a "net settlement" feature in respect of employee withholding taxes. The amendments are effective for annual periods beginning on or after January 1, 2018. For cash settled award in item (i) above IASB incorporated under IFRS 2 specify accounting for the cash-settled share based transactions which include a performance condition. The added guidance will introduce accounting requirements for cash-settled share-based payments to have similar approach as equity-settled share-based payments. For item (ii), an exception is introduced with respect to share-based payment where the entity settles the share-based payment arrangement net is classified as equity-settled in its entirety provided the share-based payment would have been classified as equity-settled had it not included the net settlement feature. Also, upon change from a cash settled share based payment arrangement to equity settled share based payment, IFRS 2 now specifies to derecognize the cash settle payment liability and replace with equity settle payment amount at the modification date value to the extent the services have been rendered. Any difference between the carrying amount of the liability as at the modification date and the amount recognized in equity at the same date would be recognized in consolidated statement of earnings and comprehensive income immediately.

*IFRS 7, Financial Instruments: Disclosure ("IFRS 7")* has been amended due to IFRS 9 to make a significant number of additional disclosures. IFRS 7 sets out disclosure requirements that are intended to enable users to evaluate the significance of financial instruments for an entity's financial position and performance, and to understand the nature and extent of risks arising from those financial instruments to which the entity is exposed. These risks include credit risk, liquidity risk and market risk. It is applicable to all entities that have financial instruments. The amendment is effective for annual periods beginning on or after January 1, 2018.

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IFRIC 22 Interpretation on Foreign Currency Transactions and Advance Consideration: On December 8, 2016, the IFRS Interpretations Committee of the International Accounting Standards Board (IASB) issued IFRS Interpretation, IFRIC 22, Foreign Currency Transactions and Advance Consideration which clarifies the date of the transaction for the purpose of determining the exchange rate to use on initial recognition of the related asset, expense or income, when an entity has received or paid advance consideration in foreign currency. As per IFRIC 22, the date of transaction for the purpose of determining the exchange rate to use on initial recognition of the related asset, expense or income (or part of it) is the date on which an entity initially recognises the non-monetary asset or non-monetary liability arising from the payment or receipt of advance consideration in accordance with IFRS standards. In case there are multiple payments or receipts in advance, the entity should determine a date of the transaction for each payment or receipt of advance consideration. IFRIC 22 applies to foreign currency transaction (or part of it), when an entity recognises a non-monetary asset or non-monetary liability arising from payment or receipt of advance consideration before the entity recognises the related asset, expense or income (or part of it). IFRIC 22 does not apply when an entity measures the related asset, expense or income on initial recognition at: a) fair value b) the fair value of the consideration paid or received at a date other than the date of the initial recognition of the non-monetary asset or non-monetary liability arising from advance consideration. Further IFRIC 22 does not apply to: a) insurance contracts that an entity issues or reinsurance contracts that it holds and b) income taxes. IFRIC 22 is applicable for annual periods on or after January 1, 2018. The Company does not anticipate any material change on the foreign currency transactions due to the adoption of IFRIC 22. The Company plans to adopt this interpretation on a retrospective basis.

### 3. INVENTORIES

	December 31, 2017	December 31, 2016
	\$	\$
Fuel Inventory	0.8	0.8
Glycol Inventory	0.1	0.1
Total Inventory	0.9	0.9

For the years ended December 31, 2017 and 2016, costs of fuel inventory of \$75.5 and \$59.2, respectively, and costs of glycol inventory of \$0.4 and \$0.2, respectively, were recognized in direct expenses.

# CARGOJET INC.

## Notes to the Consolidated Financial Statements

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### 4. PROPERTY, PLANT AND EQUIPMENT

<b>Cost</b>	Balance as at	Additions	Transfers	Adjustments	Balance as at
	January 1, 2017				December 31, 2017
	\$	\$	\$	\$	\$
Aircraft hull	230.3	56.1	11.7	(1.4)	296.7
Engines	114.4	41.4	17.8	-	173.6
Spare parts	3.3	0.7	-	-	4.0
Ground equipment	20.5	16.8	0.5	-	37.8
Rotable spares	28.1	3.4	3.9	-	35.4
Computer hardware and software	8.6	1.3	-	-	9.9
Furniture and fixtures	2.5	0.5	0.1	-	3.1
Leasehold improvements	11.6	0.4	8.8	-	20.8
Vehicles	3.0	0.1	-	-	3.1
Hangar and cross-dock facilities	23.8	0.3	-	-	24.1
Property, plant and equipment under development	16.3	60.7	(42.8)	(2.5)	31.7
Deferred heavy maintenance	39.1	11.6	-	-	50.7
	501.5	193.3	-	(3.9)	690.9

<b>Accumulated Depreciation &amp; Impairment</b>	Balance as at	Depreciation	Adjustments	Balance as at	Net Book Value
	January 1, 2017			December 31, 2017	December 31, 2017
	\$	\$	\$	\$	\$
Aircraft hull <sup>(1)</sup>	32.5	13.6	(0.2)	45.9	250.8
Engines	33.1	17.2	-	50.3	123.3
Spare parts	-	-	-	-	4.0
Ground equipment	9.9	2.8	-	12.7	25.1
Rotable spares	13.0	2.4	-	15.4	20.0
Computer hardware and software	5.6	1.1	-	6.7	3.2
Furniture and fixtures	1.3	0.3	-	1.6	1.5
Leasehold improvements <sup>(1)</sup>	8.7	1.2	(1.2)	8.7	12.1
Vehicles	1.2	0.3	-	1.5	1.6
Hangar and cross-dock facilities	6.2	0.9	-	7.1	17.0
Property, plant and equipment under development	2.5	-	(2.5)	-	31.7
Deferred heavy maintenance	16.4	9.9	-	26.3	24.4
	130.4	49.7	(3.9)	176.2	514.7

<sup>(1)</sup>Depreciation has been adjusted for the change in the terms of operating leases of three Boeing 757-200 aircraft (See Note - 9)



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## Notes to the Consolidated Financial Statements

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<b>Cost</b>	Balance as at January 1, 2016	Additions	Transfers	Fully Depreciated	Balance as at December 31, 2016
	\$	\$	\$		\$
Aircraft hull	200.1	22.4	7.8	-	230.3
Engines	100.6	10.6	3.2	-	114.4
Spare parts	2.6	0.7	-	-	3.3
Ground equipment	20.2	0.3	-	-	20.5
Rotable spares	23.7	4.4	-	-	28.1
Computer hardware and software	7.6	1.0	-	-	8.6
Furniture and fixtures	2.3	0.2	-	-	2.5
Leasehold improvements	10.9	0.4	0.3	-	11.6
Vehicles	2.7	0.3	-	-	3.0
Hangar and cross-dock facilities	23.8	-	-	-	23.8
Property, plant and equipment under development	17.1	11.1	(11.9)	-	16.3
Deferred heavy maintenance	35.2	8.4	0.6	(5.1)	39.1
	446.8	59.8	-	(5.1)	501.5

<b>Accumulated Depreciation &amp; Impairment</b>	Balance as at January 1, 2016	Depreciation	Disposals/ Transfers	Impairment	Balance as at December 31, 2016	Net Book Value December 31, 2016
	\$	\$	\$	\$	\$	\$
Aircraft hull	16.3	14.8	-	1.4	32.5	197.8
Engines	20.8	12.3	-	-	33.1	81.3
Spare parts	-	-	-	-	-	3.3
Ground equipment	7.8	2.1	-	-	9.9	10.6
Rotable spares	10.9	2.1	-	-	13.0	15.1
Computer hardware and Furniture and fixtures	4.7	0.9	-	-	5.6	3.0
Leasehold improvements	1.1	0.2	-	-	1.3	1.2
Vehicles	7.6	1.1	-	-	8.7	2.9
Hangar and cross-dock	1.0	0.2	-	-	1.2	1.8
Property, plant and equipment under development	5.3	0.9	-	-	6.2	17.6
Deferred heavy maintenance	-	-	-	2.5	2.5	13.8
	14.1	7.4	(5.1)	-	16.4	22.7
	89.6	42.0	(5.1)	3.9	130.4	371.1

Property, plant and equipment under development of \$31.7 (2016 - \$13.8 ) relates to the purchase and/or modification primarily of aircraft and aircraft engines that are not yet available for use.

# **CARGOJET INC.**

## **Notes to the Consolidated Financial Statements**

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During the year ended December 31, 2017, the Company recognized three Boeing 757-200 aircraft as assets after changing the terms of the operating leases for these aircraft resulting in the leases being reclassified as finance leases. The Company also acquired one Boeing 767-300 aircraft under a lease arrangement which has been classified as a finance lease and disclosed in Note 9. The Company also completed the acquisition of an additional Boeing 757-200 aircraft and three Boeing 757-200 engines using the revolving syndicate credit facility and term loan, and also purchased ground service equipment to permit the Company to provide its own ground handling at certain locations instead of utilizing the services and equipment of third parties.

Depreciation expense on property, plant and equipment for the year ended totaled \$49.7 (2016 - \$42.0 ) out of which \$48.4 (2016 – \$41.0) was recorded in direct expenses and \$1.3 (2016 - \$1.0 ) was recorded in general and administrative expenses.

### **5. GOODWILL**

For purposes of testing goodwill impairment, the Company reports its results as a single cash-generating unit. Goodwill is tested for impairment annually on April 1, or more frequently when there is an indication of potential impairment. The recoverable amount is determined based on a value in use calculation which uses cash flow projections for a five-year period using a steady 3.5% per annum growth rate thereafter (2016 – 3.5%), which has been estimated based on long-term growth rates in the cash flow of the Company, and a pre-tax discount rate of approximately 16.6% per annum (2016 – 18.2%). Based on the Company's analysis the recoverable amount determined exceeded the carrying amount of cash generating unit. The Company believes that any reasonably possible change in key assumptions on which recoverable amounts are based would not cause the aggregate carrying amount to exceed the aggregate recoverable amount of the cash-generating unit.

### **6. INTANGIBLE ASSETS**

Intangible assets at December 31, 2017 and 2016 consist of licenses with indefinite lives carried at \$2.0 (2016 - \$2.0). The Company believes that licenses have indefinite useful lives as the licenses provide a renewal option, at Transport Canada's discretion, provided that licensing conditions are met and the Company complies with the licensing conditions specified in the existing laws, agreements, treaties and regulations.

# CARGOJET INC.

## Notes to the Consolidated Financial Statements

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7. TRADE AND OTHER PAYABLES	December 31, 2017	December 31, 2016
	\$	\$
Trade payables and accrued charges	29.5	25.9
Payroll and benefits	8.6	4.5
Trade and other payables	38.1	30.4

## 8. BORROWINGS

Borrowings consist of the following:

	December 31, 2017	December 31, 2016
	\$	\$
Revolving credit facility	124.3	-
Aircraft facility arrangement	-	35.7
Other borrowings	0.2	0.2
	124.5	35.9
Less: current portion	-	35.7
Long-term portion	124.5	0.2

### Revolving syndicate credit facility and term loan

Effective September 20, 2016, the Company amended its revolving operating credit facility (the "facility") availed through its subsidiary, Cargojet Airways Ltd., as borrower, with a syndicate of financial institutions (collectively, the "Lenders") by, amongst other things, increasing the maximum credit available from \$100 to \$175 and extending the maturity date by one year to expire on December 16, 2019. The facility bears interest payable monthly; at the lead Lender's prime lending rate / US base rate plus 150 basis points to 200 basis points, depending on the currency of the advance and certain financial ratios of the Company. No scheduled repayments of principal are required under the facility prior to maturity.

On April 7, 2017, the Company further amended the facility by, amongst other things, increasing the maximum revolving credit available from \$175 to \$200 and establishing a non-revolving \$75 delayed-draw term loan facility (the "DDTL Facility"). The maturity date of the facility was further extended to April 7, 2020 and the maturity date of the DDTL Facility is April 7, 2022. The Company can draw the amount under the DDTL Facility until April 6, 2018. Any undrawn amount under the DDLT Facility at the end of this period will expire and will reduce the amount available under the facility. The DDTL Facility can be used to purchase aircraft, refinance aircraft loans, and make termination payments of aircraft capital leases and other capital expenditures. As of the balance sheet date, the Company has an outstanding balance of \$69.7 under the DDTL facility. Any advance under the DDTL facility is repayable in equal monthly payments based on the amount of the advance and a straight line amortization from the borrowing date to the DDLT Facility maturity date.

Amounts drawn on the facility may be advanced to the Company and its subsidiaries by way of intercompany loans. The facility will be used primarily to finance the working capital requirements and capital expenditures of the Company and its subsidiaries.

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## **Notes to the Consolidated Financial Statements**

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The facility is secured by the following:

- general security agreement constituting a first ranking security interest over all personal property of Cargojet Airways Ltd., as borrower, subject to certain permitted encumbrances (including those of aircraft financing parties);
- guarantee and postponement of claim supported by a general security agreement constituting a first ranking security interest over all personal property of the Company and its other material subsidiaries subject to certain permitted encumbrances;
- charge over real property of the Company at Hamilton airport;
- security over aircraft owned by the Company which are otherwise unencumbered; and
- assignment of insurance proceeds.

Advances under the facility are repayable without any prepayment penalties and bear interest based on the prevailing prime rate, US base rate or at a banker's acceptance rate, as applicable, plus an applicable margin to those rates. The facility is subject to customary terms and conditions for borrowers of this nature, including limits on incurring additional indebtedness, granting liens or selling assets without the consent of the Lenders, and restrictions on the Company's ability to pay dividends in certain circumstances. The facility is also subject to the maintenance of a minimum fixed charge coverage ratio and a total adjusted leverage ratio.

The Company was in compliance with the terms of the lending agreements for current and prior facilities as at December 31, 2017 and 2016.

Included in the consolidated statement of earnings and comprehensive income for the year ended December 31, 2017 was interest expense on the revolving credit facility of \$4.7 (2016 -\$3.1).

### **Loan arrangement**

In March 2015, the Company executed an aircraft facility loan with a US based lender for USD \$27.5 and drew down on it to finance the acquisition of one Boeing 767-300 aircraft. This facility was expiring in April 2022 and was secured by the related aircraft and all its components and records. On February 1, 2017, the Company prepaid the entire outstanding amount of this loan facility including the prepayment fees using the revolving operating credit facility. The prepayment resulted in a pre-tax loss of \$2.3 including prepayment fees and unamortized costs, which were recorded as a loss on the extinguishment of debt. The prepayment also resulted in a pre-tax exchange loss of \$1.3. On February 14, 2017, the Company cancelled the \$6.6 letter of credit issued to the lender in respect of this facility following the prepayment of the loan.

# **CARGOJET INC.**

## **Notes to the Consolidated Financial Statements**

### **December 31, 2017 and 2016**

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Included in the consolidated statement of earnings and comprehensive income for the year ended December 31, 2017 was interest expense on the loan arrangement of \$0.3 (2016 - \$9.2).

## **9. FINANCE LEASES**

In 2014, the Company entered into a Master Capital Lease Agreement (“MLA”) with an equipment finance and leasing company. As at December 31, 2015, the Company had completed four finance leases to acquire four Boeing 767-300 aircraft under the MLA in the aggregate amount of \$120.0. The Company is required to purchase the aircraft financed under the MLA at the end of the term of each lease at a predetermined price. Accordingly, these leases are classified as finance leases and corresponding lease obligations are recognized in the financial statements. Each lease under the MLA is arranged in two tranches, A and B, each with its own schedule of principal and interest payments. The estimated weighted effective interest rate at December 31, 2017 was 7.23%. The leases under the MLA are guaranteed by the Company and its subsidiaries.

Under the terms of the MLA, the Company paid arrangement fees in an amount equal to 0.75% of the amounts advanced and was required to pay additional fees (the “share- based additional fees”) equal to the positive difference between the price of 233,332 Cargojet common voting shares on the TSX on the date of the MLA and the twenty day volume weighted average closing price for such shares as of the date preceding the date on which the lessor demands payment by a written notice, provided that such notice can only be given on a day after the first anniversary of the applicable agreement and before the fourth anniversary of such agreement. The Company had also paid success fees in an amount equal to 1.5% of the amount advanced under the MLA to an independent investment banking firm for its services towards completion of these transactions.

In September 2016, the Company received a written demand to pay the share- based additional fees and paid \$3.8 in full satisfaction thereof.

The MLA is subject to the maintenance of certain financial covenants. The Company was in compliance with all such covenants as at December 31, 2017 and 2016.

As at December 31, 2017, the total outstanding balance of the leases under the MLA is \$85.4 out of which \$15.7 is recognized as a current liability on the consolidated balance sheets.

The Company also has finance lease arrangements for two Boeing 767-300 aircraft that includes bargain purchase options. The estimated effective interest rates for these leases are 7.21% and 6.63% respectively. These leases are deemed to be maturing on the early exercisable date of the bargain purchase options in March 2018 and October 2020 respectively. As at December 31, 2017 the total outstanding balance of these finance lease arrangements is \$57.6 out of which \$28.2 is recognized as a current liability on the consolidated balance sheets.

During the year ended December 31, 2017, The Company renegotiated the terms of the operating leases of three of the Boeing 757-200 aircraft. Under the revised terms, the Company acquired the right to buy back the aircraft at the end of their lease terms in October 2017, December 2017 and January 2018 respectively. Accordingly the leases were classified as finance leases and on the date of conversion of leases an asset and liability of \$58.6 was recognized. On September 29, 2017 and October 26, 2017 respectively, the Company prepaid the entire outstanding amount of the finance leases ending in October 2017 and December 2017 respectively using the revolving operating credit facility. The balance of the liability of \$18.2 as at December 31, 2017 is recognized as a current liability on the consolidated balance sheets and was paid in its entirety on January 3, 2018 using the revolving credit facility (see Note 27).

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The following is a schedule of future minimum annual lease payments for aircraft under finance leases together with the balance of the obligation as at December 31, 2017.

	Minimum lease payments	Present value of minimum lease payments
	\$	\$
Not later than one year	70.2	62.1
Later than one year and not later than five years	113.2	99.1
	183.4	161.2
Less: interest	22.2	-
Total obligations under finance leases	161.2	161.2
Less: current portion	62.1	62.1
Non-current portion	99.1	99.1

Interest amounts on the finance leases for the year ended December 31, 2017 totaled \$9.2 (2016 - \$10.1).

**10. PROVISIONS**

The Company's aircraft operating lease agreements require leased aircraft to be returned to the lessor in a specified operating condition. The Company has estimated that it will incur certain maintenance costs at the end of the lease terms and has recorded a maintenance provision liability for these costs. A reconciliation of the carrying amount of the provision is as follows:

	December 31, 2017	December 31, 2016
	\$	\$
Balance, beginning of year	2.4	2.4
Recognition of provision for lease return conditions	0.6	-
Gain on derecognition of provision for lease return conditions	(1.6)	-
Accretion	0.1	0.1
Effects of exchange rate changes on the provision balance	(0.2)	(0.1)
Balance, end of year	1.3	2.4
Less: current portion	0.1	0.7
Non-current portion	1.2	1.7

The provision for lease return conditions represents the present value of management's best estimate of the future outflow of economic benefits that will be required to settle the obligation at the end of the leases. Such costs have been estimated based on contractual commitments and the Company's specific history. The provision has been reduced to the cost of deferred heavy maintenance included in property, plant and equipment and is being amortized over the remaining terms of the leases.

The change in carrying amount of the provision is related to the recognition of the maintenance obligation of one leased Boeing 757-200 aircraft, the lease period of which has been extended to February 2019 from June 2018, and the derecognition of the maintenance obligation of the three leased Boeing 757-200 aircraft that were acquired through conversion of operating leases to finance leases during the year ended December 31, 2017 (see Note 4).

# CARGOJET INC.

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### 11. CONVERTIBLE DEBENTURES

The balances of convertible debentures as at December 31, 2017 and December 31, 2016 consist of the following :

	December 31, 2017	December 31, 2016
	\$	\$
Convertible debentures - 5.5%	-	68.4
Convertible debentures - 4.65%	114.8	112.7
Balance	114.8	181.1

#### Convertible debentures – 5.5% due June 30, 2019

In April 2014, \$74.0 of unsecured subordinated convertible debentures were issued with a term of five years. These debentures had a fixed interest rate of 5.5% per annum, payable semi-annually in arrears on June 30 and December 31 of each year, commencing December 31, 2014.

On May 15, 2017, the Company issued a redemption notice pursuant to the convertible debenture indenture dated April 29, 2014 (the "Indenture") to redeem all of the outstanding debentures issued under the Indenture (the "5.5% Debentures") on July 5, 2017. Pursuant to the Indenture, the Company elected to satisfy its obligation to pay the redemption price of the 5.5% Debentures due at redemption by issuing that number of voting shares of the Company obtained by dividing the outstanding principal amount of the 5.5% Debentures by 95% of the volume weighted average trading price of the common voting shares on the TSX for the 20 consecutive trading days ending five trading days before the redemption date and to pay accrued and unpaid interest thereon up to but excluding the redemption date in cash to the holders of the 5.5% Debentures. From December 31, 2016 to July 4, 2017, \$72.4 million of the outstanding 5.5% Debentures were converted to 2,518,911 common voting shares of the Company by the holders thereof pursuant to the Indenture. The remaining \$1.4 of the outstanding 5.5% Debentures were redeemed by issuing 30,788 common voting shares of the Company and paying accrued and unpaid interest in cash to the holders thereof.

The debt component is measured at amortized cost. The balance of the debt component as at December 31, 2017 and December 31, 2016 consists of the following:

	December 31, 2017	December 31, 2016
	\$	\$
Principal balance - beginning of period	73.8	74.0
Less:		
Issuance costs	(3.3)	(3.3)
Conversion option at inception	(6.6)	(6.6)
Accretion	5.8	4.5
Converted during the year	(69.7)	(0.2)
Balance	-	68.4

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Interest expense on the debentures for the year ended December 31, 2017 totaled \$3.1, (2016 - \$5.9).

**Convertible debentures – 4.65% due December 31, 2021**

In September 2016, \$125.0 of unsecured subordinated convertible debentures were issued at a price of 1,000 (dollars) per debenture with a term of five years. These debentures bear a fixed interest rate of 4.65% per annum, payable semi-annually in arrears on June 30 and December 31 of each year, commencing December 31, 2016. The intended use of the net proceeds of the debentures is to refinance three US dollar denominated aircraft finance loans.

The debt component is measured at amortized cost. The balance of the debt component as at December 31, 2017 and December 31, 2016 consists of the following:

	December 31, 2017	December 31, 2016
	\$	\$
Principal balance - beginning of year	125.0	125.0
Less:		
Issuance costs	(5.8)	(5.8)
Conversion option at inception	(7.1)	(7.1)
Accretion	2.7	0.6
<b>Balance</b>	<b>114.8</b>	<b>112.7</b>

Interest expense on the debentures for the year ended December 31, 2017 totaled \$8.0 (2016 - \$2.3).

**12. INCOME TAXES**

The reconciliation between the Company's statutory and effective tax rate is as follows:

	December 31, 2017	December 31, 2016
	\$	\$
Earnings before income taxes	33.6	3.0
Basic rate of 26.5% (2016 - 26.5%)	8.9	0.8
Exchange gains on capital loans	(0.1)	(1.3)
Share- based compensation	0.8	0.8
Meals and entertainment	0.2	0.2
Sundry items	0.1	0.1
<b>Provision for income taxes</b>	<b>9.9</b>	<b>0.6</b>



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The tax effect of significant temporary differences is as follows:

	December 31, 2016	Recognized in equity	Recognized in Profit & Loss	December 31, 2017
	\$	\$	\$	\$
Property, plant and equipment	10.1	-	10.4	20.5
Operating loss carryforward	(10.6)	-	0.8	(9.8)
Licenses	0.3	-	-	0.3
Intangible assets	(0.5)	-	0.1	(0.4)
Derivative contracts	0.4	-	(0.8)	(0.4)
Pension costs	(2.3)	-	(0.5)	(2.8)
Financing costs	(0.3)	-	(0.7)	(1.0)
Convertible debentures	2.7	(1.1)	(0.1)	1.5
Provision for lease retirement costs	(0.5)	-	0.3	(0.2)
Deferred heavy maintenance	5.9	-	0.4	6.3
Net deferred income tax liability	5.2	(1.1)	9.9	14.0

### 13. DIRECT EXPENSES

	December 31, 2017	December 31, 2016
	\$	\$
Fuel costs	75.5	59.2
Maintenance costs	25.6	21.5
Heavy maintenance amortization	10.0	7.4
Aircraft costs	19.6	25.7
Crew costs	24.3	22.0
Depreciation	38.4	33.6
Commercial and other costs	83.2	75.8
Direct expenses	276.6	245.2

### 14. GENERAL AND ADMINISTRATIVE EXPENSES

	December 31, 2017	December 31, 2016
	\$	\$
Salaries and benefits	21.4	18.9
Employee pension	1.8	8.7
Depreciation	1.3	1.0
Net realized foreign exchange losses (gain)	1.9	(4.3)
Bonuses and incentives	8.1	7.1
Audit, legal and consulting	2.0	1.5
IT network and communications	2.4	2.3
Other general and administrative expenses	8.7	8.0
General and administrative expenses	47.6	43.2

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## Notes to the Consolidated Financial Statements

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### 15. FINANCE COSTS

	December 31, 2017	December 31, 2016
	\$	\$
Interest on capital leases	9.2	10.1
Interest on loans	0.3	9.2
Interest on debentures	11.0	8.4
Other interest	4.7	3.1
Finance costs	25.2	30.8

### 16. OTHER GAINS & LOSSES

	December 31, 2017	December 31, 2016
Gain on derecognition of provision for lease return conditions	(1.6)	-
Net loss on forward foreign exchange contracts	2.2	3.4
Gain on cash settled share based payment arrangements and total return swap	(1.2)	(4.3)
Unrealized foreign exchange gain	(3.5)	(4.0)
Other gain (net)	(4.1)	(4.9)

### 17. SHAREHOLDERS' CAPITAL

#### a) Authorized

The Company is authorized to issue an unlimited number of no par value common voting shares, variable voting shares and preferred shares. The common voting shares are held only by shareholders who are "Canadian" as such term is defined in the Canada Transportation Act. The variable voting shares are held only by shareholders who are not Canadian. Under the articles of incorporation and bylaws of the Company, any common voting share that is sold to a non-Canadian is automatically converted to a variable voting share. Similarly, a variable voting share that is sold to a Canadian is automatically converted to a common voting share.

Variable voting shares carry one vote per share held, except where (i) the number of issued and outstanding variable voting shares exceeds 25% of the total number of all issued and outstanding common and variable voting shares, or (ii) the total number of votes cast by or on behalf of the holders of variable voting shares at any meeting on any matter on which a vote is to be taken exceeds 25% of the total number of votes that may be cast at such meeting.

If either of the above noted thresholds is surpassed at any time, the vote attached to each variable voting share will decrease automatically without further act or formality. Under the circumstances described in (i) above, the variable voting shares as a class cannot carry more than 25% of the total voting rights attached to the aggregate number of issued and outstanding common and variable voting shares. Under the circumstances described in (ii) above, the variable voting shares as a class cannot, for a given shareholders' meeting, carry more than 25% of the total number of votes that may be cast at the meeting.

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### b) Issued and outstanding

The following table shows the changes in shareholders' capital from December 31, 2016 to December 31, 2017:

	Number of shares	Amount \$
Variable voting shares	234,571	2.2
Common voting shares	10,408,794	98.7
Outstanding- December 31, 2016	10,643,365	100.9
Changes during the year		
Conversion of convertible debentures	2,549,867	69.7
Restricted share units settled	80,718	2.6
Exercise of options	108,679	1.2
	13,382,629	174.4
Consisting of:		
Variable voting shares	291,652	3.8
Common voting shares	13,090,977	170.6
Outstanding- December 31, 2017	13,382,629	174.4

### Dividends

Dividends to shareholders declared for year ended December 31, 2017 amounted to \$9.6 (\$0.77 per share) December 31 2016 - \$6.8 (\$0.65 per share).

As at December 31, 2017, the dividend amount of \$2.6 was payable to the shareholders (2016 - \$1.9).

### 18. EARNINGS PER SHARE

The following table shows the computation of basic earnings per share for the year ended December 31, 2017 and 2016:

	December 31, 2017	December 31, 2016
Basic earnings per share		
Net earnings	\$23.7	\$2.4
Weighted average number of shares	12.1	10.5
Dilutive impact of share- based awards	0.2	0.3
Diluted weighted average number of shares	12.3	10.8
Total basic earnings per share	\$1.96	\$0.23
Total diluted earnings per share	\$1.93	\$0.22

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The effect of the convertible debentures has been excluded from the calculation of diluted earnings per share for the year ended December 31, 2017 and 2016 as the impact would be anti-dilutive. Diluted earnings includes the potentially dilutive impact of share-based awards outstanding at year end, consisting of the incremental shares assumed to be issued on the exercise of stock options and the incremental shares assumed to be issued under restricted stock unit arrangements.

### 19. Employee benefits

In 2016, the Company established an unfunded defined benefit plan for one of its senior executives (for plan descriptions refer to policy Note 2 on employee benefits). The movement in the defined benefit pension cost during the year is as follows:

	December 31, 2017	December 31, 2016
	\$	\$
Balance as at January 1, 2017	8.7	-
Current service cost	0.6	
Interest expense	0.3	
Effect of experience adjustment	0.3	
Effect of changes in financial assumptions	0.6	
Present value of defined benefit obligations	-	8.7
Balance as at December 31, 2017	10.5	8.7

The significant actuarial assumptions used in the measurement of accrued benefit obligations for the unfunded defined benefit plan are as follows:

#### Assumptions for 2017

Discount rate:	3.5% per year
Increase in pensionable earnings:	2.0% per year
Inflation:	2.0% per year
Longevity post retirement:	CPM 2014 mortality table with generational mortality improvements using CPM-B improvement scale.
Retirement age:	65 years

#### Assumptions for 2016

Discount rate:	3.9% per year
Increase in pensionable earnings:	2.75% per year
Inflation:	2.0% per year
Longevity post retirement:	CPM 2014 mortality table with generational mortality improvements using CPM-B improvement scale.
Retirement age:	65 years

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## Notes to the Consolidated Financial Statements

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### Sensitivity Analysis

Certain assumptions were used in the actuarial valuation of the pension obligation as at December 31, 2017. Due to uncertainty inherent in a projection over a long period of time due to changing factors, the alternative outcomes and amounts cannot be determined. Accordingly, the Company performed a sensitivity analysis on the projections. Sensitivity analysis of pension expense is performed based on changing one assumption at a time while keeping all other assumptions constant. This may be an unlikely event to occur in practice where changes in some of the assumptions may be correlated. When calculating the sensitivity of the defined benefit obligation to variations in significant actuarial assumptions, the same method (present value of the defined benefit obligation calculated with the projected unit credit method at the end of the reporting period) has been applied as for calculating the liability recognized in the consolidated statement of financial position. Sensitivity analysis performed on pension expense relating to pension benefit liabilities, based on different actuarial assumptions is given below.

**Change in discount rate:** A 0.50 percentage point decrease in discount rate would have increased the benefit obligation by 7%. A 0.50 percentage point increase in discount rate would have decreased the benefit obligation by 6%.

**Change in salary scale:** A 0.25 percentage point increase in salary scale would have increased the benefit obligation by 1%. A 0.25 percentage point decrease in salary scale would have decreased the benefit obligation by 1%.

**Change in mortality assumption:** A one year increase in life expectancy would have increased the benefit obligation by 2%. A one year decrease in life expectancy would have decreased the benefit obligation by 2%.

**Defined Contribution Pension Plans:** During the year ended on December 31, 2017, the Company contributed to the plan an amount equal to the Money Purchase Limit for the year.

## 20. SHARE-BASED COMPENSATION

### Restricted Share Units

The Company's restricted share unit plan (the "RSU Plan") and stock option plan (the "Stock Option Plan") provide the Company the ability to grant restricted share units ("RSUs") and options ("Options") to certain of its executive officers and senior management as part of its long term incentive plan. Each RSU granted entitles the holder to one common voting share or one variable voting share of the Company on the settlement thereof. Each Option granted entitles the holder to one common voting share or one variable voting share of the Company on due exercise thereof or if the holder duly elects a cash-less exercise of the Option, the holder will receive that number of common voting shares or variable voting shares, as the case may be, equal to the excess of the five day volume weighted average trading price of the shares (as determined in accordance with the rules of the TSX) ending on the trading day before the exercise date of the Option (the "Market Price") over the exercise price of the Option, multiplied by the number of shares in respect of which the Option is exercised, divided by the Market Price, less any amount to be deducted or withheld in respect of taxes or otherwise pursuant to law.

# CARGOJET INC.

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During the year ended December 31, 2017, in accordance with the RSU Plan, the Company granted 60,986 RSUs to certain key executives. Each RSU had an average value of \$47.32 calculated as the volume weighted average trading price of the common voting shares of the Company on the TSX for the five trading days prior to the grant date. 20,710 of \$1.0 RSUs vested and settled in August 2017. Of the remaining 40,276 RSUs granted, 20,138 will vest in each of the first quarters of 2018 and 2019 respectively.

During the year ended December 31, 2017, the Company also granted 2,103 RSUs to three non-employee directors. Each RSU had an average value of \$47.32 calculated as the volume weighted average trading price of the common voting shares of the Company on the TSX for the five trading days prior to the grant dates. All 2,103 of \$0.1 RSUs vested and were settled in August 2017.

On March 24, 2017, 56,466 RSUs granted to the Company's executives and senior management in prior years vested and were settled on the same date. Accordingly, an amount of \$1.5 was transferred to share capital from contributed surplus. Prior to vesting, and in accordance with the RSU Plan, the Company accrued notional dividends on the RSUs equivalent to 1,439 RSUs that were issued, vested and settled upon the satisfaction of the RSUs vesting conditions. An amount of \$0.1 was recognized on the notional dividends as share-based compensation with a corresponding increase in the share capital account.

There are 23,000 remaining RSUs which were granted in the prior years that will vest in the first quarter of 2018.

The RSU activity for the year ended December 31, 2017 and 2016 is summarized below:

	Number of RSUs	Fair value \$
Balance at January 1, 2016	108,662	1.5
Granted in the year	29,297	0.8
Share dividend	1,969	-
Share based compensation-Vested and settled	(60,462)	(0.7)
Share based compensation-Unvested and amortized	-	(1.1)
Balance at December 31, 2016	79,466	0.5
Granted in the year	63,089	3.0
Share dividend	1,439	0.1
Share based compensation-Vested and settled	(80,718)	(1.3)
Share based compensation-Unvested and amortized	-	(1.2)
Balance at December 31, 2017	63,276	1.1

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During the year ended December 31, 2017, the total share based compensation expense of \$2.5 related to settled and unvested RSUs was included in the consolidated statements of earnings and comprehensive income (for the year ended December 31, 2016 – \$1.8). Unrecognized share-based compensation expense as at December 31, 2017 related to these RSUs was \$1.1 (December 31, 2016 – \$0.5) and will be amortized on a pro-rated basis in the consolidated statements of earnings and comprehensive income over the vesting period.

### Options:

The Options activity during the year ended December 31, 2017 is summarized below:

<b>OPTIONS (in Canadian dollars)</b>	Number of Options	Weighted average exercise price in \$
Balance as at January 1, 2017	452,805	\$27.86
Exercised during the year	(232,358)	\$26.11
Balance as at December 31, 2017	220,447	\$29.71
Vested & exercisable at December 31, 2017	82,324	\$35.83
Unvested at December 31, 2017	138,123	\$26.07

As at December 31, 2017, there were a total of 82,324 vested Options outstanding and the weighted average contractual life remaining of the outstanding Options, both vested and non-vested, is 2.0 years.

During the year ending December 31, 2017, 87,700 Options granted on June 15, 2015 and 144,658 Options granted on March 28, 2016 were exercised by certain executives when the volume weighted average trading price per share was \$47.74. The number of shares issued was determined based on the market value of the shares in excess of the Options exercise price. Upon such exercise a total of 108,679 shares were issued to the executives and the amount of \$1.2 was transferred to the share capital account. The Company also recognized an expense for the year ended December 31, 2017 of \$0.6 (for the year ended December 31, 2016 – \$1.4) in respect of the amortization of the Options over the vesting period. The unrecognized value as at December 31, 2017 related to the Options was \$0.3 (December 31, 2016 – \$0.9) and will be amortized on a pro-rated basis in the consolidated statements of earnings and comprehensive income over the vesting period.

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### Weighted average assumptions

	November 17, 2016	March 28, 2016	June 15, 2015
	Series 3	Series 2	Series 1
Exercise price redemption	\$47.22	\$26.50	\$25.47
Expected volatility	32.96%	32.4%	22.6%
Option life in years	3	5	5
Dividend yield	1.41%	2.5%	2.4%
Risk free rate	1.75%	0.63%	0.94%
Vesting period	immediate	2016-2018	2016-2018
Options granted	38,440	241,966	172,399
Options outstanding	38,440	97,308	84,699
Fair value per option on grant date	\$10.41	\$5.43	\$4.98

There has been no alteration of the terms and conditions of the above share-based payment arrangements since the grant date.

## 21. COMMITMENTS AND CONTINGENCIES

### Commitments

The Company is committed to the following annual minimum lease payments under operating leases for its fleet of aircraft, office premises and certain equipment:

	\$
Not later than one year	6.5
Later than one year and not later than five years	9.0
Later than five years	12.6
<b>Total</b>	<b>28.1</b>

In the normal course of business, the Company has certain commitments for expenditures related to the continuation of operations and the maintenance and acquisition of property, plant and equipment.

### Contingencies

The Company has provided irrevocable standby letters of credit totaling \$18.7 to financial institutions as security for its loan, corporate credit cards and to several vendors as security for the Company's ongoing purchases. The letters of credit expire unless further renewed as follows:

	\$
December 31, 2017	18.7
<b>Total</b>	<b>18.7</b>



# CARGOJET INC.

## Notes to the Consolidated Financial Statements

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## 22. RELATED PARTY TRANSACTIONS

### New Head Office

In February 2017, the Company entered into a lease agreement with respect to a new 62,000 square feet head office and warehouse area. The lessor of the property is indirectly and beneficially owned by one of the Company's executive officers and directors (the "Interested Party"). The transaction is in the normal course of business and will be measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties. The lease was negotiated on behalf of the Company by an independent director of the Company after an independent appraisal and review by outside counsel to ensure the lease was on market terms and approved by the directors other than the Interested Party. Entering into the lease is not subject to minority shareholder approval nor valuation requirements of Multilateral Instrument 61-101 - *Protection of Minority Security Holders in Special Transactions* as neither the fair market value of the subject matter of, nor the fair market value of the consideration for, the lease, insofar as it involves the Interested Party, exceed 25 per cent of the Company's current market capitalization.

The lease term is for a period of 15 years. The annual rental payments will be approximately \$1.0 million plus taxes, maintenance and insurance costs. The basic rent is subject to revision every five years at a predetermined rate per the terms of the lease.

### Compensation of key management personnel

In 2017, the employee benefit expense was \$76.4 (2016 - \$72.4) of which \$44.4 (2016 - \$37.4) was recorded in direct expenses and \$32.0 (2016 - \$35.0) was recorded in general and administrative expenses. The general and administrative expenses include the remuneration of directors and other members of key management personnel for the years ended December 31, 2017 and 2016 as follows:

	December 31, 2017	December 31, 2016
	\$	\$
Short term benefits	6.3	6.5
Post-employment benefits	0.1	0.1
Share-based payments	3.1	3.2
Defined pension benefits	1.8	8.7
Total remuneration	11.3	18.5

## 23. ECONOMIC DEPENDENCE

In 2017, the Company had sales to three individual customers that represented 63.3% of the total revenues (2016 - 66.3%). These sales are provided under service agreements that expire over various periods to April 2025. All of these customers had sales in excess of 10% of total revenues in each of 2017 and 2016. The sales to individual customers represented 31.9%, 19.2% and 12.2% respectively of the total revenues (2016 - 33.1%, 21.7% and 11.5%).

# **CARGOJET INC.**

## **Notes to the Consolidated Financial Statements**

**December 31, 2017 and 2016**

**(in millions of Canadian dollars except where noted)**

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### **24. CAPITAL MANAGEMENT**

The Company's objectives when managing capital are: (i) to maintain flexibility when managing the short-term cash needs of the business and the funding of future growth; and (ii) to manage capital in a manner that balances the interests of the shareholders and debt holders.

The Company defines capital as the sum of total equity, borrowings, including the current portion, obligations under finance leases, convertible debentures, cash, and the present value of the future operating lease payments.

The Company manages its capital structure and will make adjustments to it in ways that support the broader corporate strategy or in light of changes in economic conditions. In order to maintain or adjust its capital structure, the Company may adjust the amount of dividends paid to shareholders, purchase shares for cancellation pursuant to normal course issuer bids, issue new shares, issue new debt, issue new debt to replace existing debt which may have different characteristics, repurchase debt instruments for cancellation pursuant to normal course issuer bids or reduce the amount of existing debt. There were no changes in the Company's approach to capital management during the year.

The Company is subject to financial covenants related to its credit facility, finance leases and aircraft facility arrangement (Note 8 and Note 9, respectively). As at December 31, 2017 and 2016, the Company was in compliance with all financial covenants.

### **25. FINANCIAL INSTRUMENTS**

#### **Derivative financial instruments**

Derivative financial instruments are utilized by the Company occasionally in the management of its foreign currency exposures, interest rate risks and share price. The Company's policy is not to utilize derivative financial instruments for trading or speculative purposes. All derivative financial instruments are recorded at their fair values.

Derivatives are initially recognized at fair value at the date the derivative contract is entered into and are subsequently remeasured to their fair value at the end of each reporting period. The resulting gain or loss is recognized in income immediately.

A derivative with a positive fair value is recognized as a financial asset; a derivative with a negative fair value is recognized as a financial liability.

# **CARGOJET INC.**

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### **Total return swap**

The Company had an obligation to pay share-based additional fees under the MLA and certain aircraft facility arrangements. In September 2015, the Company entered into a total return swap agreement with a financial institution to manage its exposure under these arrangements. Under the total return swap agreement, the Company pays interest to the financial institution based on Canadian LIBOR on the total value of the notional equity amount which is equal to the total cost of the underlying shares. At the settlement of the total return swap agreement, the Company will receive or remit the net difference between the total value of the notional equity amount and the total proceeds of sales of the underlying shares. The Company did not designate the total return swap agreement as a cash flow hedge for accounting purposes.

During the year ended December 31, 2017, \$4.7 of the total return swap was settled. The fair market value of the swap was \$1.8 in favour of the Company (December 31, 2016 - \$5.3) and is included under derivative financial instruments on the balance sheet. The change in the fair market value during the year ended December 31, 2017 was of \$1.2 (for the year ended December 31, 2016 - \$4.3) and is included as other gains in the consolidated statements of earnings and comprehensive income.

The fair value of the total return swap is classified as level 3 under the fair value hierarchy and is determined by using the Black Scholes model. This model uses the following inputs: market price of the underlying asset, strike price of the underlying asset, risk free rate, dividend yield and expected volatility. An increase or decrease of 10% in the market price of the underlying asset will result in a gain or loss of \$0.3 respectively. A 10% increase or decrease in other inputs will result in an immaterial amount of gain or loss respectively.

The Company's Controller performs the valuations of non-property items required for financial reporting purposes, including level 3 fair values. The Controller reports directly to the Company's Chief Financial Officer ("CFO") who in turn reports to the Company's Audit Committee ("AC"). Discussions of valuation processes and results are held between the CFO, AC and Controller at least once every three months, in line with the Company's quarterly reporting period.

### **Fair Values**

The fair value of the 4.65% convertible debentures as at December 31, 2017 was approximately \$122.4 (December 31, 2016-\$125.0). The fair value of the debentures was determined using the discounted cash flow method using the discount rate of 7.0%. The discount rate is determined by using the government of Canada's benchmark bond rate adjusted for the Company's specific credit risk. The fair value of the long-term debt as disclosed in Note 8 was approximately equal to its carrying value. The debentures are categorized as Level 3 under the fair value hierarchy. An increase or decrease of 10% in discount rate used for valuation of the debentures will decrease or increase the fair value by \$2.7 respectively.

The fair values of all other financial assets and liabilities approximate their carrying values given the short-term nature of these items. The fair values of the interest rate swap and the forward contracts are the estimated amounts the issuer would receive or pay to terminate the agreement at the reporting date. Unrealized gains on derivatives are recorded as derivative instrument assets and unrealized losses are recorded as derivative instrument liabilities in the consolidated balance sheets.

# **CARGOJET INC.**

## **Notes to the Consolidated Financial Statements**

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**(in millions of Canadian dollars except where noted)**

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#### **Forward Foreign Exchange Contracts**

As at December 31, 2017, the Company had foreign exchange forward contracts outstanding to buy US \$38.0 at a weighted average contracted rate of CAD \$1.2993 per US dollar (December 31, 2016 – US\$ 59.9 at a weighted average contracted rate of CAD \$1.3045 per US dollar). The estimated value of the foreign exchange forward contracts as at December 31, 2017 is a payable of \$1.6 (December 31, 2016 – receivable of \$1.5) and is included under derivative financial instruments on the balance sheet. Foreign exchange contracts of \$30.7 were settled during the year ended December 31, 2017 resulting in a gain of \$1.0.

The fair values of the forward contracts are the estimated amounts the issuer would receive or pay to terminate the agreement at the reporting date. The forward contracts are categorized as Level 2 under the fair value hierarchy. The fair value of the forward contracts is determined using the observable foreign exchange rate at the balance sheet date. Unrealized gains on derivatives are recorded as derivative instrument assets and unrealized losses are recorded as derivative instrument liabilities in the consolidated financial statements.

There are no other assets or liabilities recorded at fair value as at December 31, 2017 and December 31, 2016.

#### **Credit risk**

The Company's principal financial assets that expose it to credit risk are accounts receivable and notes receivable.

The Company is subject to risk of non-payment of accounts receivable and notes receivable. The amounts disclosed in the balance sheet represent the maximum credit risk and are net of allowances for bad debts, based on management estimates taking into account the Company's prior experience and its assessment of the current economic environment. The Company's receivables are concentrated among several of its largest customers with approximately 76.2% (December 31, 2016 – 59.1%) of total receivables on account of the Company's ten largest customers. However, the Company believes that the credit risk associated with these receivables is limited for the following reasons:

- (a) Only a small portion (0.5%) of trade receivables is outstanding for more than 60 days and is considered past due. The Company considers all of these amounts to be fully collectible. Trade receivables that are not past due are also considered by the Company to be fully collectible. Consistent with its past collection history, the Company has not recognized any significant provisions for bad debts.
- (b) The Company mitigates credit risk by monitoring the creditworthiness of its customers.
- (c) A majority of the Company's major customers are large public corporations with positive credit ratings and history.

# CARGOJET INC.

## Notes to the Consolidated Financial Statements

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### Liquidity risk

The Company monitors and manages its liquidity risk to ensure it has access to sufficient funds to meet operational and investing requirements. Management of the Company believes that future cash flows from operations, the availability of credit under existing bank arrangements, and current debt market financing is adequate to support the Company's financial liquidity needs. Available sources of liquidity include a revolving credit facility with a Canadian chartered bank. The available facility is to a maximum of \$200 million. The Company was in compliance with all covenants as at December 31, 2017 and 2016.

The Company has financial liabilities with varying contractual maturity dates. Total financial liabilities at December 31, 2017 based on contractual undiscounted payments are as follows:

	Less than 1 year	Between 1 and 2 years	Between 2 and 5 years	Over 5 Years	Total
	\$	\$	\$	\$	\$
Borrowings and convertible debentures	-	-	249.5	-	249.5
Finance leases	62.1	14.7	84.4	-	161.2
Interest on finance leases	8.1	6.4	7.7	-	22.2
Trade and other payables	38.1	-	-	-	38.1
Provisions	0.1	1.2	-	-	1.3
Pension benefit liability	-	-	-	10.5	10.5
Dividends payable	2.6	-	-	-	2.6
Total	111.0	22.3	341.6	10.5	485.4

Total financial liabilities at December 31, 2016 based on contractual undiscounted payments are as follows:

	Less than 1 year	Between 1 and 2 years	Between 2 and 5 years	Over 5 Years	Total
	\$	\$	\$	\$	\$
Borrowings and convertible debentures	35.7	-	198.8	-	234.5
Finance leases	12.7	46.8	60.3	10.5	130.3
Interest on borrowings (at current rates)	0.4	-	-	-	0.4
Interest on finance leases	9.0	6.3	11.0	-	26.3
Trade and other payables	31.1	-	1.7	8.7	41.5
Dividends payable	1.9	-	-	-	1.9
Total	90.8	53.1	271.8	19.2	434.9

### Market risk

In the normal course of business, the financial position of the Company is routinely subject to a variety of risks. The Company regularly assesses these risks and has established policies and business practices to protect against the adverse effects of these and other potential exposures. As a result, the Company does not anticipate any material losses from these risks.

# **CARGOJET INC.**

## **Notes to the Consolidated Financial Statements**

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The Company performs a sensitivity analysis to determine the effects that market risk exposures may have on the fair value of the Company's debt and other financial instruments. The financial instruments that are included in the sensitivity analysis comprise all of the Company's cash, borrowings, convertible debentures and all derivative financial instruments. To perform the sensitivity analysis, the Company assesses the risk of loss in fair values from the effect of hypothetical changes in interest rates and foreign currency exchange rates on market-sensitive instruments.

Interest rate risk is the risk that the fair value or future cash flows of a financial liability will fluctuate because of changes in market interest rates. The Company enters into both fixed and floating rate debt and also leases certain assets with fixed rates. The Company risk management objective is to minimize the potential for changes in interest rates to cause adverse changes in cash flows to the Company. The ratio of fixed to floating rate obligations outstanding is designed to maintain flexibility in the Company's capital structure and is based upon a long term objective of minimum 70% fixed and maximum 30% floating but allows flexibility in the short-term to adjust to prevailing market conditions. These practices aim to minimize the net interest cost volatility. The ratio at December 31, 2017 is 100% fixed after repayment of the floating rate loans in September 2016.

At December 31, 2017, the Company had no interest rate risk due to fixed interest rates of all existing financing arrangements.

The Company earns revenue and undertakes purchase transactions in foreign currencies, and therefore is subject to gains and losses due to fluctuations in the foreign currencies. The company also enters into contracts attributed to asset purchases including aircraft and aircraft parts and pays debt in foreign currency. The Company manages its exposure to changes in the Canadian/U.S. exchange rate on anticipated purchases and debt payments by buying forward U.S. dollars at fixed rates in future periods. As at December 31, 2017, the Company held 13 foreign exchange forward purchase agreements maturing on a monthly basis to April 2022 for a total of USD \$38 (2016 - \$59.9). These agreements fix the amount of Canadian dollars that the Company will pay to buy USD to offset its purchases in USD.

Total unrealized foreign exchange gains during the year ended December 31, 2017 on foreign exchange transactions were \$3.5 (2016 – gain of \$4.0). The unrealized loss on forward contracts during the year ended December 31, 2017 were \$2.2 (December 31, 2016 – loss of \$3.4)

At December 31, 2017, a weakening of the Canadian dollar that results in a 10 percent decrease in the exchange rate for the purchase of US dollars would increase the value of the Company's other net financial assets and liabilities denominated in US dollars by approximately \$2.9 (2016 - \$0.6). An increase in the exchange rate for the purchase of US dollars of 10 percent would decrease the value of these net financial assets and liabilities by the same amount (2016 - \$0.6).

At December 31, 2017, a weakening of the Canadian dollar that results in a 10 percent decrease in the exchange rate for the purchase of EURO would increase the value of the Company's other net financial assets and liabilities denominated in EURO by approximately \$0.3 (2016 - \$0.1). An increase in the exchange rate for the purchase of EURO of 10 percent would decrease the value of these net financial assets and liabilities by the same amount (2016 - \$0.1).

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**26. GUARANTEES**

In the normal course of business, the Company enters into agreements that meet the definition of a guarantee. The Company's primary guarantees are as follows:

(a) The Company has provided indemnities under lease agreements for the use of various operating facilities and leased aircrafts. Under the terms of these agreements, the Company agrees to indemnify the counterparties for various items including, but not limited to, all liabilities, loss, suits and damages arising during, on or after the term of the agreement. The maximum amount of any potential future payment cannot be reasonably estimated.

(b) In the normal course of business, the Company has entered into agreements that include indemnities in favor of third parties, such as purchase and sale agreements, confidentiality agreements, engagement letters with advisors and consultants, outsourcing agreements, leasing contracts, information technology agreements and service agreements. These indemnification agreements may require the Company to compensate counterparties for losses incurred by the counterparties as a result of breaches in representation and regulations or as a result of litigation claims or statutory sanctions that may be suffered by the counterparty as a consequence of the transaction. The terms of these indemnities are not explicitly defined and the maximum amount of any potential reimbursement cannot be reasonably estimated.

(c) The Company participates in Fuel Facility Corporations ("FFC") along with other airlines that contract for fuel services at various major airports in Canada. Each FFC operate on a cost recovery basis. The purpose of the FFC is to own and finance the system that distributes fuel to the contracting airlines, including leasing the required land rights. The aggregate debt of these FFC and any liabilities of environmental remediation costs are not considered as part of the Financial Statements of the Company. The Company views this loss potential as remote. The airlines that participate in the FFC guarantee on a pro-rata basis the share of the debt based on system usage.

The nature of these indemnification agreements prevents the Company from making a reasonable estimate of the maximum exposure due to the difficulties in assessing the amount of liability which stems from the unpredictability of future events and the unlimited coverage offered to counterparties.

Historically, the Company has not made any payments under such or similar indemnification agreements and therefore no amount has been accrued in the balance sheet with respect to these agreements.

**27. SUBSEQUENT EVENTS**

On January 3, 2018 the Company paid the entire outstanding amount of the finance lease of \$18.2 ending in January 2018 using the revolving credit facility.