

**CARGOJET**



2012 Annual Report



Cargojet is Canada's leading provider of time sensitive overnight air cargo service with a co-load network that constitutes approximately 50% of Canada's domestic overnight air cargo capacity. Cargojet's network consolidates cargo received from over 400 customers and carries over 750,000 pounds of cargo each business night across its North American network. Cargojet places importance on safety, reliability, customer service and strong financial performance by employing highly qualified and dedicated personnel. Cargojet maintains consistently reliable on time service levels within the overnight air cargo market. In 2012, Cargojet operated approximately 7,000 flights of which more than 98% arrived at destination within 15 minutes of scheduled arrival. Cargojet continues to maintain the highest levels of industry standards in overall performance by providing a first class service.





# Table of Contents



3	Financial Highlights
4	President's Message to the Shareholders
5	Corporate Governance
7	Management's Discussion and Analysis of Financial Results
33	Management's Report to the Shareholders
34	Auditors' Report to the Shareholders
36	Financial Statements
72	Directors and Officers of the Corporation

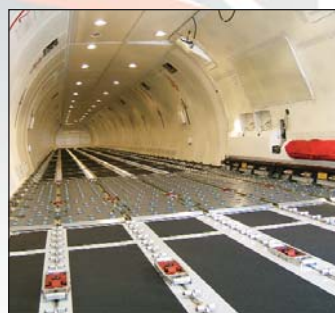


# Financial Highlights\*\*



Supplementary Financial Information (In thousands of dollars)	Year Ended	Three Month Period Ended				Year Ended
	December 31 2011	March 31 2012	June 30 2012	September 30 2012	December 31 2012	December 31 2012
Revenues	165,511	40,136	40,487	41,777	46,370	168,771
Direct Expenses	135,675	34,603	33,260	34,974	37,589	140,426
EBITDA	15,209	1,916	4,452	5,056	5,449	16,873
Dividends declared	4,245	1,135	1,135	1,135	1,192	4,597
Direct expense as percentage of revenue	82%	86%	82%	84%	81%	83%
EBITDA as percentage of revenue	9%	5%	11%	12%	12%	10%

\*\* Financial highlights for 2011 and 2012 are for continuing operations only.



# Message To Shareholders



**Message to Shareholders,**

## **STRONG FINISH AFTER A WEAK START**

The past year revealed a strong growth in core domestic overnight revenues and adhoc air cargo charter revenues, particularly in the last half of the year. The enhancement and expansion of our domestic network in Eastern Canada that began in July, has resulted in better than expected volume and revenue growth that continues into this year.

Cargojet continues to position itself as a dominant global air cargo charter operator and we experienced significant growth in this sector in 2012 by utilizing aircraft assets during traditional down-time in the day and on weekends. Cargojet is able to compete effectively in this market with our lower cost base.

The strong revenue finish to the year when combined with the continued aggressive cost management programs has resulted in improved overall financial performance for the year. Consistent operational performance and safety continue to be the priority and Cargojet achieved over 98% on-time arrival within fifteen minutes of scheduled arrival time on almost 7,000 flight legs operated during the year.

We will continue to manage our costs and seek out new revenue opportunities and our consistent cash flows will continue to provide value to shareholders through our consistent dividend policy. Excess cash will be primarily used to pay down debt, increase dividends when warranted and to strengthen our overall balance sheet.

## **FINANCIAL RESULTS**

A strong finish to the year resulted in total revenues of \$168.8 million, an increase of \$3.3 million over the previous year. Combined with lower operating costs resulted in EBITDA of \$16.9 million an increase of 11.2% over the previous year. Prudent cost management and operating efficiencies continue to contribute to improved operating yields and cash flows.

## **OUTLOOK**

Although we remain cautious and somewhat uncertain about the continued speed of economic recovery, we are optimistic about the opportunities for Cargojet in 2013.

We have positioned ourselves strategically to take advantage of new revenue growth opportunities when and where they occur. Cargojet continues to manage its capacity including aircraft fleet requirements in a prudent and cost-effective manner and will deploy the necessary assets as necessary.

## **CARGOJET TEAM**

Cargojet is committed to providing a safe and secure and highly reliable level of service to our Customers at all times. We cannot do this without the dedication, loyalty and commitment of every single member of the Cargojet team.

The Board of Directors of Cargojet Inc. determines dividend policy and any future dividend payments will be determined by the Board in accordance with the company's financial results and cash requirements.

In conclusion and on behalf of the Board of Directors, I would like to thank our Customers for their on-going loyalty and support; our Shareholders for their confidence in our business; and every member of the Cargojet Team for their dedication, hard work and support.

Dr. Ajay K. Virmani  
President & Chief Executive Officer

March 2013

# CHARTER OF THE CORPORATE GOVERNANCE COMMITTEE



## I. Purpose

The Corporate Governance Committee's mandate is to generally assume the responsibility for developing the approach of Cargojet Inc. (the "**Corporation**") to matters of corporate governance.

## II. Composition

The Corporate Governance Committee will be comprised of at least three directors of the Corporation, a majority of whom, subject to any exemptions set out in National Instrument 52-110 Audit Committees ("**NI 52-110**"), will be independent. An "independent" director is a director who has no direct or indirect material relationship with the Corporation. A "material relationship" is a relationship that could, in the view of the Board of Directors of the Corporation, be reasonably expected to interfere with the exercise of the director's independent judgement or a relationship deemed to be a material relationship pursuant to NI 52-110.

## III. Responsibilities

Responsibilities of the Corporate Governance Committee generally include, but are not limited to, the undertaking of the following tasks:

1. Annually reviewing the charters of the Board of Directors of the Corporation, Audit Committee, Corporate Governance Committee and the Compensation and Nominating Committee and after consulting with the Board of Directors of the Corporation and the members of each committee, recommending such amendments to those charters as the Corporate Governance Committee believes are necessary or desirable.
2. Annually reviewing the performance of management of the Corporation and its subsidiaries, the effectiveness of the Board of Directors, the effectiveness of the Board of Directors as a whole and the contribution of individual Directors.
3. Assisting the Independent Chairman of the Corporation in carrying out his responsibilities, including without limitation:
  - (a) ensuring that the responsibilities of the Board of Directors of the Corporation are well understood by the Board of Directors and management, and that the boundaries between board and management responsibilities are clearly understood and respected;
  - (b) ensuring that the Board of Directors of the Corporation works as a cohesive team and providing the leadership essential to achieve this;
  - (c) ensuring that the resources available to the Board of Directors of the Corporation (in particular timely and relevant information) are adequate to support its work; and
  - (d) adopting procedures to ensure that the Board of Directors of the Corporation can conduct its work effectively and efficiently, including committee structure and composition, scheduling, and management of meetings.
4. Supervising and evaluating the Corporation's securities compliance procedures and reporting to the Board of Directors of the Corporation on the necessary changes to such procedures and on the adoption of any additional procedures.
5. Considering and, if thought fit, approving requests from directors or committee members for the engagement of special advisors from time to time.



6. Preparing and recommending to the Board of Directors of the Corporation, annually, a “Statement of Corporate Governance Practices”. The Statement of Corporate Governance Practices will discuss the process used by the Board of Directors of the Corporation and Corporate Governance Committee to fulfill their functions as required.
7. Recommending procedures to permit the Board of Directors of the Corporation to meet on a regular basis without management being present.
8. Considering, and providing a recommendation to the Directors on any transaction involving the Corporation or any subsidiary or affiliate thereof before such transaction is approved by the Board of Directors.

#### **IV. Meetings**

The Corporate Governance Committee will meet regularly at times necessary to perform the duties described above in a timely manner, but not less than two times a year. Meetings may be held at any time deemed appropriate by the Corporate Governance Committee.

At the discretion of the Corporate Governance Committee, meetings may be held with representatives of appropriate members of management.

The Chairman of the Corporate Governance Committee will report periodically to the Board of Directors of the Corporation.





# CARGOJET INC.

Management's Discussion and Analysis  
Of Financial Condition and Results of Operations

For the Three and Twelve Month  
Periods Ended December 31, 2012





# CARGOJET 2012 Annual Report



The following is the Management's Discussion and Analysis ("MD&A") of the consolidated financial condition and results of operations of Cargojet Inc. (the "Company") for the three month and twelve month periods ended December 31, 2012. The following also includes a discussion of and comparative operating results for the three month and twelve month periods ended December 31, 2011.

Cargojet is publicly listed with shares and convertible debentures traded on the Toronto Stock Exchange ("TSX"). The Company is incorporated and domiciled in Canada and the registered office is located at 350 Britannia Road East, Units 5 and 6, Mississauga, Ontario.

The effective date of the MD&A is March 4, 2013. The consolidated financial statements have been prepared in accordance with International Financial Reporting Standard ("IFRS"). This MD&A should be read in conjunction with the consolidated financial statements of the Company for the years ended December 31, 2012 and 2011.

## EBITDA <sup>(A)</sup> AND ADJUSTED FREE CASH FLOW <sup>(B)</sup>

References to "EBITDA" are to earnings before interest, income taxes, depreciation, amortization, gain or loss on disposal of capital assets and after adjusting aircraft heavy maintenance amounts to actual net expenditures. Non-GAAP measures, EBITDA and Adjusted Free Cash Flow, are not earnings measures recognized by IFRS and do not have standardized meanings prescribed by IFRS. Therefore, EBITDA and Adjusted Free Cash Flow may not be comparable to similar measures presented by other issuers. Investors are cautioned that EBITDA and Adjusted Free Cash Flow should not be construed as an alternative to net income determined in accordance with IFRS as indicators of the Company's performance or to cash flows from operating, investing and financing activities as measures of liquidity and cash flows. The calculations of EBITDA and Adjusted Free Cash Flow are shown on page 10 of the MD&A.



# CARGOJET 2012 Annual Report



## KEY FACTORS AFFECTING THE BUSINESS

The results of operations, business prospects and financial condition of the Company are subject to a number of risks and uncertainties and are affected by a number of factors outside the control of the management of the Company. For a more complete discussion of the risks affecting the Company's business, reference should be made to the Annual Information Form ("AIF"), filed February 27, 2012 with the regulatory authorities.

## FORWARD LOOKING STATEMENTS

This discussion includes certain forward-looking statements that are based upon current expectations, which involve risks and uncertainties associated with our business and the environment in which the business operates. Any statements contained herein that are not statements of historical facts may be deemed to be forward-looking statements including those identified by the expressions "anticipate", "believe", "plan", "estimate", "expect", "intend" and similar expressions to the extent they relate to the Company or its management. The forward-looking statements are not historical facts, but reflect Cargojet's current expectations regarding future results or events. These forward-looking statements are subject to a number of risks and uncertainties that could cause actual results or events to differ materially from current expectations, as detailed in the Company's AIF, filed February 27, 2012 with the regulatory authorities.

<sup>(A)</sup> Please refer to End Note <sup>(A)</sup> included at the end of this MD&A.

<sup>(B)</sup> Please refer to End Note <sup>(B)</sup> included at the end of this MD&A.

## CORPORATE OVERVIEW

The Company is Canada's leading provider of time sensitive overnight air cargo services. Its main air cargo business is comprised of the following:

- Operating a domestic overnight air cargo co-load network between thirteen major Canadian cities
- Providing dedicated aircraft to customers on an Aircraft, Crew, Maintenance & Insurance ("ACMI") basis, operating between points in Canada and the USA
- Operating scheduled international routes for multiple cargo customers between the USA and Bermuda and between Canada and Poland.

The Company operates its business across North America transporting time sensitive air cargo each business night utilizing its fleet of all-cargo aircraft. The Company's domestic overnight air cargo co-load network consolidates cargo received from customers and transports such cargo to the appropriate destination in a timely and safe manner. The Company continually monitors key performance indicators and uses this information to reduce costs and improve the efficiency of its services.

The Company currently operates one leased 757-200ER ("B757") series aircraft, two leased 767-200ER ("B767") series aircraft and ten Boeing 727-200 ("B727") series aircraft, owned by the Company. The Company also periodically contracts other airlines on an ACMI or sub-charter basis to temporarily operate aircraft on the Company's behalf. This provides added capacity to its overall network to meet new business and/or peak period demands.

As at the date of this MD&A, the Company owns two regional aircraft. One regional aircraft is under a finance lease to a third party and accordingly the aircraft has been discontinued as an owned asset. The other regional aircraft is available for lease.

# CARGOJET 2012 Annual Report



## RECENT EVENTS

### PROPERTY, PLANT AND EQUIPMENT

In July 2012, the Company purchased a Boeing 727 aircraft for total consideration of \$1,224,925. The costs were segregated into three components consisting of engines totaling \$540,630, airframe totaling \$619,295 and deferred heavy maintenance totaling \$65,000.

In August 2012, the Company reviewed the carrying value of its used engine cores and estimated that the recoverable amount was less than the book value. The Company reduced the net book value of the used engine cores to fair value by \$567,395 and reported a loss on impairment of property, plant and equipment.

### ISSUANCE OF CONVERTIBLE DEBENTURES - 6.5%

In March 2012, \$28.8 million of unsecured subordinated convertible debentures were issued with a term of five years. These debentures bear a fixed interest rate of 6.5% per annum, payable semi-annually in arrears on April 30 and October 31 of each year, commencing April 30, 2012.

On or after April 30, 2015, but prior to April 30, 2016, the debentures are redeemable, in whole at any time or in part from time to time, at the option of the Company at a price equal to at least \$1,000 per debenture plus accrued and unpaid interest, provided that the current market price of the common shares of the Company on the date on which the notice of redemption is given is at least 125% of the conversion price of \$11.75 per common share. After April 30, 2016, but prior to the maturity date of April 30, 2017, the debentures are redeemable at a price equal to \$1,000 per debenture plus accrued and unpaid interest. On redemption or at maturity on April 30, 2017, the Company has the option to repay the debentures in either cash or freely tradable voting shares of the Company. The number of common shares to be issued will be determined by dividing the aggregate amount of the principal amount of the debentures by 95% of the current market price of the common shares.

Based on certain conditions, the debentures are convertible, at the holders' discretion, at \$11.75 per voting share at any time prior to the close of business on the earliest of the business day immediately preceding the maturity date; if called for redemption, on the business day immediately preceding the date specified by the Company for redemption of the debentures; or if called for repurchase pursuant to a change of control, on the business day immediately preceding the payment date. The Company also has the right at any time to purchase debentures in the market, by tender or by private contract subject to regulatory requirements, provided, however, that if an event of default has occurred and is continuing, the Company or any of its affiliates will not have the right to purchase the debentures by private contract. The conversion rate of \$11.75 per voting share is subject to adjustment in certain circumstances, including the payment of a cash dividend or distribution to holders of voting shares in excess of \$0.142 per quarter (\$0.568 per annum).

In the event of a change in control, as defined in the indenture, the Company will be required to make an offer to the holders of debentures to repurchase the debentures at a price equal to 100% of the principal amount plus accrued and unpaid interest. In addition, if a change in control occurs in which 10% or more of the consideration consists of cash, certain equity securities or other property not traded or intended to be traded immediately following such transaction on a recognized exchange, holders of the debentures will be entitled to convert their debentures and, subject to certain limitations, receive an additional amount of voting shares to those that they would otherwise be entitled at the normal conversion rate. The amount of such additional voting shares will depend on the effective date and the price paid per voting share in the transaction constituting the change in control.

# CARGOJET 2012 Annual Report



## RECENT EVENTS (CONTINUED)

### ISSUANCE OF CONVERTIBLE DEBENTURES - 6.5% (CONTINUED)

The principal amount of the debentures has been allocated between its debt component and the conversion option and has been classified separately on the balance sheet. The fair value of the debt component was determined using an estimated market rate for a similar liability without an equity component and the residual was allocated to the conversion option.

The debt component is measured at amortized cost. The balance of the debt component at December 31, 2012 consisted of the following:



	December 31, 2012
	\$
Principal balance	28,750,000
Less:	
Issuance costs	(1,312,192)
Conversion option at inception	(2,642,384)
Accretion	468,107
<b>Balance</b>	<b>25,263,531</b>

The conversion option, net of related issuance costs of \$132,808, has been recorded in shareholders' equity. Factoring in issuance costs, the effective interest rate on the debentures is 10.01%.

Interest expense on the debentures for the three and twelve month periods ended December 31, 2012 totaled \$624,545 and \$1,927,272, respectively.

### REDEMPTION OF CONVERTIBLE DEBENTURES - 7.5%

In May 2012, the Company redeemed \$24,655,000 principal amount of the convertible debentures (\$24,100,397 net of the related unamortized issuance cost and the portion allocated to the conversion option) at par or \$1,000 per convertible debenture. At redemption, the Company allocated \$24,655,000 to the liability component redeemed and the equity component of \$1,271,503 was reclassified from conversion option to reserve for surplus on debenture repurchases in shareholders' equity. The redemption of the convertible debenture resulted in a loss of \$554,603.

Interest expense on the debentures for the three and twelve month periods ended December 31, 2012 totaled \$nil and \$802,030, respectively (2011 - \$605,870 and \$2,403,728, respectively).

# CARGOJET 2012 Annual Report



## RECENT EVENTS (CONTINUED)

### PROVISIONS

The Company's aircraft operating lease agreements require leased aircraft to be returned to the lessor in a specified operating condition. As a result of changes in the Company's c-check intervals for certain aircraft from 18 months to 24 months, the Company has estimated that it will incur certain maintenance end of the lease terms and has recorded a maintenance provision liability for these costs. The change in the carrying amount of the provisions is as follows:



	\$
Balance, January 1, 2012	-
Recognition of provision for lease return conditions	1,476,973
Accretion	49,141
Effects of exchange rate changes on the provisions balance	17,670
<b>Balance, December 31, 2012</b>	<b>1,543,784</b>

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 Company specific history. Accretion expense of \$49,141 has been recorded in the period as part of finance costs in the consolidated statement of income. The provision has been added to the cost of deferred heavy maintenance included in property, plant and equipment and will be amortized over the remaining terms of the leases.

### LONG-TERM INCENTIVE PLAN

The Company's long-term incentive plan (the "Plan" or "LTIP") provides certain of its executive officers and senior management of the Company with compensation opportunities tied to the performance of the Company. Company incentive bonuses, in the form of shares, are provided to eligible employees on an annual basis where the earnings of the Company exceed a pre-determined base (the "Base Target"). The Base Target is set annually by the Compensation Committee of the Company's Board of Directors in accordance with the terms of the Plan.

If the Company's earnings exceed the Base Target, a percentage of the excess is contributed by the Company into a long-term incentive pool. Shares are then purchased on the open market by the Company and held by the Company until they vest. Vesting of the shares will occur on the basis of one-third of the total grant at the time of granting, and one-third on each of the first and second anniversary dates.

For the years ended December 31, 2012 and 2011 share-based compensation expense totaled \$402,932 and \$497,144, respectively, including withholding taxes of \$52,313 and \$99,675, respectively, paid on behalf of the eligible employees.

# CARGOJET 2012 Annual Report



## RECENT EVENTS (CONTINUED)

### 2012 Awards

In March 2012, pursuant to the Company's LTIP, an amount of \$348,750 was approved to the executive officers and senior management. Accordingly, the Company purchased 39,275 shares from the open market at an average price of \$7.55. As at December 31, 2012, 7,580 of these shares had vested and \$63,210 was transferred from share-based compensation reserve to shareholders' capital. The balance of LTIP award not vested as at December 31, 2012 was \$233,227.

In March 2011, in accordance with the Plan, the Company purchased 65,984 shares from the open market at an average price of \$8.55, plus commissions. As at December 31, 2011, 14,238 of these shares had vested, \$121,825 being transferred from share-based compensation reserve to shareholders' capital.

As at December 31, 2012, an additional 25,875 of the shares for the 2011 awards had vested and \$221,500 was transferred from share-based compensation reserve to shareholders' capital. The balance of LTIP award not vested as at December 31, 2012 was \$221,500.

The following table details the impact of the above transactions on shareholders' capital as at December 31, 2012 and on the consolidated statements of income for the years ended December 31, 2012 and 2011:

Shares purchased under the Plan	Number	\$
Balance, January 1, 2011	-	-
Shares acquired by Company for long-term incentive plan	65,984	564,825
Shares distributed by Company to long-term incentive plan participants	(14,238)	(121,825)
Balance, December 31, 2011	51,746	443,000
Shares acquired by Company for long-term incentive plan	39,275	296,437
Shares distributed by Company to long-term incentive plan participants	(33,455)	(284,710)
Balance, December 31, 2012	57,566	454,727

	December 31, 2012	December 31, 2011
<b>Share-based compensation expense</b>	\$	\$
Shares transferred to long-term incentive plan participants	107,507	121,825
Withholding tax paid for long-term incentive plan participants	52,313	99,675
Share-based compensation, not yet vested	243,112	275,643
Share-based remuneration	402,932	497,143

### RENEWAL OF CREDIT AGREEMENT

On October 12, 2012, the Company renewed its revolving credit facility with a Canadian chartered bank. The renewal changed the maturity date from December 31, 2013 to December 31, 2015. All other terms and conditions related to the credit facility remained the same.

# CARGOJET 2012 Annual Report



## REVENUE

The Company's revenues are primarily generated from its overnight air cargo service between thirteen major Canadian cities each business night. Customers pre-purchase a guaranteed space and weight allocation on the Company's network and a corresponding guaranteed daily revenue amount is paid to the Company for this space and weight allocation. Remaining capacity is sold on an *ad hoc* basis to contract and non-contract customers. The Company also generates revenue from a variety of other air cargo services:

- The Company provides domestic air cargo services for a number of international airlines between points in Canada that connect such airlines' gateways to Canada. This helps to support lower demand legs and provides a revenue opportunity with little or no incremental cost, as the flights are operating on regular schedules.
- To further enhance its revenues, the Company offers a specialty charter service, typically in the daytime and on weekends. The charter business targets livestock shipments, military equipment, emergency relief supplies and virtually any large shipment requiring immediate delivery across North America, to the Caribbean and to Europe.

- The Company operates an international route between Newark, New Jersey, USA and Hamilton, Bermuda. This provides a five-day per week air cargo service for multiple customers and is patterned after the domestic business that Cargojet has built in Canada. Customer contracts contain minimum daily revenue guarantees and the ability to pass through increases in fuel costs. The Company also operates scheduled international routes between Canada and Poland.

- The Company provides and operates dedicated aircraft on an ACMI basis. On these contracts, the customer is responsible for all commercial activities and the Company is paid a fixed amount to operate the routes.

## EXPENSES

Direct expenses consist of fixed and variable expenses including aircraft and ground support, aircraft maintenance, vehicle leases, fuel, ground handling services, aircraft de-icing, sub-charter, ground transportation costs, landing fees, navigation fees, insurance, salaries and benefits, office equipment costs and building leases.

Administrative expenses are primarily costs associated with executive and corporate management and the overhead of the Company's business that include functions such as load scheduling, flight operations coordination, client relations, administration, accounting, human resources and information systems.



# CARGOJET 2012 Annual Report



## CARGOJET INCOME FUND

### Management's Discussion and Analysis of Financial Condition and Results of Operations

For the Three Month and Twelve Month Periods Ended December 31, 2012

#### Expenses (continued)

#### Results of Operations and Supplementary Financial Information (in thousands)

	Three Month Period Ended December 31		Twelve Month Period Ended December 31	
	2012 (unaudited) \$	2011 (unaudited) \$	2012 (unaudited) \$	2011 (unaudited) \$
<b>Revenue</b>	<b>46,370</b>	42,914	<b>168,771</b>	165,511
<b>Direct expenses</b>	<b>37,589</b>	35,860	<b>140,426</b>	135,675
	<b>8,781</b>	7,054	<b>28,345</b>	29,836
General and administrative	<b>5,587</b>	5,215	<b>18,117</b>	18,956
Sales and marketing	<b>542</b>	189	<b>835</b>	587
(Gain) Loss on disposal of property, plant and equipment	<b>(82)</b>	533	<b>(87)</b>	1,765
Loss on impairment of property, plant and equipment	-	626	<b>567</b>	1,164
Finance costs	<b>831</b>	877	<b>3,504</b>	3,323
Finance income	<b>(59)</b>	(64)	<b>(210)</b>	(235)
(Gain) Loss on derivative contracts	<b>71</b>	-	<b>(2)</b>	(678)
Loss on debenture redemption	-	-	<b>555</b>	-
	<b>6,890</b>	7,376	<b>23,279</b>	24,882
<b>Earnings before income taxes</b>	<b>1,891</b>	(322)	<b>5,066</b>	4,954
<b>Provision for (recovery of) income taxes</b>				
Current	<b>529</b>	56	<b>528</b>	1,485
Deferred	<b>(166)</b>	(170)	<b>986</b>	(496)
	<b>363</b>	(114)	<b>1,514</b>	989
<b>Income from continuing operations</b>	<b>1,528</b>	(208)	<b>3,552</b>	3,965
<b>Loss from discontinued operations</b>	-	(33)	-	(168)
<b>Net Income</b>	<b>1,528</b>	(241)	<b>3,552</b>	3,797
<b>Earnings per share from continuing and discontinued operations</b>				
Basic	0.19	(0.03)	0.44	0.48
Diluted	0.19	(0.03)	0.44	0.48
<b>Earnings per share from continuing operations</b>				
Basic	0.19	(0.03)	0.44	0.50
Diluted	0.19	(0.03)	0.44	0.50
<b>Average number of shares - basic (in thousands of shares) <sup>(1)</sup></b>	<b>7,993</b>	<b>7,993</b>	<b>7,993</b>	<b>7,993</b>

<sup>1</sup>: Average number of shares includes treasury shares.



# CARGOJET 2012 Annual Report



## CARGOJET INCOME FUND Management Discussion and Analysis of Financial Condition and Results of Operations

For the Three Month and Twelve Month Periods Ended December 31, 2012

### Expenses (continued)

#### Summary of Most Recently Completed Consolidated Quarterly Results

	Three Month Periods Ended							
	December 31	September 30	June 30	March 31	December 31	September 30	June 30	March 31
	2012	2012	2012	2012	2011	2011	2011	2011
	(unaudited)	(unaudited)	(unaudited)	(unaudited)	(unaudited)	(unaudited)	(unaudited)	(unaudited)
Revenue (in thousands)	\$ 46,370	\$ 41,777	\$ 40,487	\$ 40,136	\$ 42,914	\$ 40,307	\$ 41,182	\$ 41,108
Net income (loss) from continuing operations (in thousands)	\$ 1,528	\$ 947	\$ 1,047	\$ 30	\$ (208)	\$ 1,482	\$ 1,407	\$ 1,283
Net loss from discontinued operations (in thousands)	\$ -	\$ -	\$ -	\$ -	\$ (33)	\$ (136)	\$ -	\$ -
<b>Earnings (loss) per Share</b>								
From continuing and discontinued operations								
- Basic	\$ 0.19	\$ 0.12	\$ 0.13	\$ -	\$ (0.03)	\$ 0.17	\$ 0.18	\$ 0.16
- Diluted	\$ 0.19	\$ 0.12	\$ 0.13	\$ -	\$ (0.03)	\$ 0.17	\$ 0.18	\$ 0.16
From continuing operations								
- Basic	\$ 0.19	\$ 0.12	\$ 0.13	\$ -	\$ (0.03)	\$ 0.19	\$ 0.18	\$ 0.16
- Diluted	\$ 0.19	\$ 0.12	\$ 0.13	\$ -	\$ (0.03)	\$ 0.19	\$ 0.18	\$ 0.16
Average number of shares - basic (in thousands of shares) <sup>(1)</sup>	7,993	7,993	7,993	7,993	7,993	7,993	7,993	7,993
Average number of shares - diluted (in thousands of shares) <sup>(1)</sup>	7,993	7,993	7,993	7,993	7,993	7,993	7,993	7,993

<sup>(1)</sup> Average number of shares includes treasury shares.

# CARGOJET 2012 Annual Report



## CARGOJET INCOME FUND

### Management's Discussion and Analysis of Financial Condition and Results of Operations

For the Three Month and Twelve Month Periods Ended December 31, 2012

#### Expenses (continued)

#### Calculation of EBITDA and Adjusted Free Cash Flow: (in thousands)

	Three Month Period Ended December 31		Twelve Month Period Ended December 31	
	2012	2011	2012	2011
	(unaudited) \$	(unaudited) \$	(unaudited) \$	(unaudited) \$
<b>Net income from continuing operations</b>	<b>1,528</b>	<b>(208)</b>	<b>3,552</b>	<b>3,965</b>
Add:				
Interest	771	813	3,294	3,088
(Recovery of) provision for current income taxes	529	56	528	1,485
Provision for (recovery of) deferred income taxes	(166)	(170)	986	(496)
(Gain) loss on disposal of property, plant and equipment	(81)	533	(87)	1,164
Impairment on property, plant & equipment	-	626	567	1,765
Change in fair value on non-hedge derivatives	72	-	(2)	(466)
Loss on debenture redemption	-	-	555	-
Amortized maintenance deposits	932	-	3,360	-
Depreciation of property, plant and equipment	1,754	2,167	6,258	9,068
Aircraft heavy maintenance expenditures	136	(69)	(1,381)	(3,423)
Heavy maintenance deposits <sup>(1)</sup>	(26)	(510)	(757)	(941)
<b>EBITDA from continuing operations</b>	<b>5,449</b>	<b>3,238</b>	<b>16,873</b>	<b>15,209</b>
EBITDA from discontinued operations	-	(45)	-	(234)
<b>Total EBITDA</b>	<b>5,449</b>	<b>3,193</b>	<b>16,873</b>	<b>14,975</b>
	\$	\$	\$	\$
<b>Cash inflow from operating activities</b>	<b>7,057</b>	<b>1,993</b>	<b>20,355</b>	<b>15,130</b>
Less: Additions to plant, property and equipment	(2,887)	(4,336)	(7,726)	(11,250)
Add: Proceeds from disposal of capital assets	237	-	289	959
<b>Standardized free cash flow</b>	<b>4,407</b>	<b>(2,343)</b>	<b>12,918</b>	<b>4,839</b>
Less: Changes in non-cash working capital items and deposits	(1,980)	1,131	(4,226)	(562)
Provision for current income taxes	(529)	(56)	(528)	(1,485)
Cash outflow from discontinued operations	-	-	-	234
<b>Adjusted free cash flow</b>	<b>1,898</b>	<b>(1,268)</b>	<b>8,164</b>	<b>3,026</b>

<sup>(1)</sup> Heavy maintenance deposits are paid to the aircraft lessors on a monthly basis. Cargojet is entitled to a refund of these payments when it incurs actual heavy maintenance expenditures.

# CARGOJET 2012 Annual Report



## HIGHLIGHTS FOR THE THREE MONTH PERIODS ENDED DECEMBER 31, 2012 AND 2011

- Total revenue for the three month period ended December 31, 2012 was \$46.4 million as compared to \$42.9 million for the same period in 2011, representing an increase of \$3.5 million or 8.2%.
- Average cargo revenue excluding fuel surcharges and other cost pass-through revenues for the three month period ended December 31, 2012 was \$0.75 million per operating day as compared to \$0.67 million for the same period in 2011, representing an increase of \$0.08 million or 11.9%.
- EBITDA from continuing operations for the three month period ended December 31, 2012 was \$5.4 million as compared to \$3.2 million for the same period in 2011, an increase of \$2.2 million or 68.8%.
- Adjusted free cash flow was an inflow of \$1.9 million for the three month period ended December 31, 2012 as compared to an outflow of \$1.3 million for the same period in 2011, an increase of \$3.2 million.

## REVENUE

Total revenue for the three month period ended December 31, 2012 was \$46.4 million, as compared to \$42.9 million for the same period in 2011, representing an increase of \$3.5 million or 8.2%. The increase in total revenue was due primarily to the increase in ad-hoc charter activity, an increase in core overnight revenues and the expansion of Cargojet's network in Eastern Canada.

Revenue related to the core overnight business excluding fuel surcharges and other cost pass-through revenues, for the three month period ended December 31, 2012 was \$30.3 million compared to \$28.1 million for the same period in 2011, an increase of \$2.2 million or 7.8%.

Revenue related to the ACMI cargo business for the three month period ended December 31, 2012 was \$1.8 million compared to \$2.3 million for the same period in 2011, a decrease of \$0.5 million or 21.7%. The decrease in revenues was due primarily to lower ad-hoc ACMI demand.

Revenue related to scheduled and ad-hoc charters for the three month period ended December 31, 2012 was \$3.9 million compared to \$2.5 million for the same period in 2011, an increase of \$1.4 million or 56.0%. The increase in the revenue was due primarily to the increase in ad-hoc charter activities during the quarter.

Fuel surcharges and other cost pass-through revenues were \$10.1 million for the three month period ended December 31, 2012 as compared to \$9.6 million for the same period in 2011, representing an increase of \$0.5 million or 5.2%. Fuel surcharges and other cost pass-through revenues include fuel sales to third parties of \$0.8 million for the three month period ended December 31, 2012 as compared to \$0.4 million for the same period in 2011, an increase of \$0.4 million or 100.0%.

Other revenues were \$0.3 million for the three month period ended December 31, 2012 as compared to \$0.4 million for the three month period ended December 31, 2011, a decrease of \$0.1 or 25.0%.



## DIRECT EXPENSES

Total direct expenses were \$37.6 million for the three month period ended December 31, 2012 as compared to \$35.9 million for the three month period ended December 31, 2011. As a percentage of revenue, direct expenses decreased from 83.7% in 2011 to 81.0% for the same period in 2012.

Fuel costs were \$16.7 million for the three month period ended December 31, 2012 as compared to \$16.0 million for the same period in 2011. The \$0.7 million or 4.4% increase in fuel costs were due to an increase in the block hours related to charter flights and the expansion of Cargojet's network in Eastern Canada. Any changes in fuel cost experienced by the Company due to changes in fuel prices are passed on to customers as an increase or decrease in their fuel surcharges.

Depreciation expense was \$2.3 million for the three month period ended December 31, 2012 as compared to \$1.2 million in 2011, representing an increase of \$1.1 million or 91.7%. The increase was due primarily to the acquisition of previously leased aircraft at the end of 2011, acquisition of one aircraft in 2012 and a change in the estimate of engine depreciation.

Aircraft costs were \$3.1 million for the three month period ended December 31, 2012 as compared to \$4.4 million in 2011, representing a decrease of \$1.3 million or 29.5%. The decrease was due primarily to the acquisition of previously leased aircraft and reduction in sub-charter cost due to Cargojet's network expansion in Eastern Canada. These amounts were partially offset by higher variable cost due to increased charter activities and expenses related to aircraft lease reserves.

Heavy maintenance amortization costs were \$0.8 million for the three month period ended December 31, 2012 and remain unchanged from \$0.8 million for the same period in 2011. Heavy maintenance of aircraft occurs at regular and predetermined intervals and costs related to these are deferred by the Company and amortized over a period of 24 months until the next scheduled heavy maintenance.

Maintenance costs were \$2.2 million for the three month period ended December 31, 2012 as compared to \$2.6 million for the same period in 2011. The decrease of \$0.4 million or 15.4% was primarily due to the decrease in line maintenance costs.

Total crew costs including salaries, training and positioning were \$2.4 million for the three month period ended December 31, 2012 and \$2.3 million for the same period in 2011, an increase of \$0.1 million or 4.3%. The increase was due primarily to the increase in cost related to ad-hoc charter activities.

Commercial and other direct operating costs were \$10.2 million for the three month period ended December 31, 2012 as compared to \$8.5 million for the same period in 2011. The increase of \$1.7 million or 20.0% was due primarily to the increase in ground handling, landing and navigation charges due to the higher number of ad-hoc charter flights and the expansion of Cargojet's network in Eastern Canada.

## SELLING, GENERAL AND ADMINISTRATIVE EXPENSES

Selling, general and administrative ("SG&A") expenses were \$6.1 million for the three month period ended December 31, 2012 compared to \$5.4 million for the same period in 2011, an increase of \$0.7 million or 13.0%. The increase was due primarily to the increase in employee and management's bonuses and the increase in sales and promotional expenses.

## EBITDA

EBITDA from continuing operations for the three month period ended December 31, 2012 was \$5.4 million or 11.6% of revenue, compared to \$3.2 million or 7.5% of revenue for the same period in 2011. The increase in EBITDA of \$2.2 million or 68.8% was due primarily to the following:

- The increase in core overnight revenues and the expansion of Cargojet's network in Eastern Canada.
- Increased ad-hoc charters.

## FINANCE COSTS

Finance costs were \$0.8 million for the three month period ended December 31, 2012, and December 31, 2011.

# CARGOJET 2012 Annual Report



## CURRENT INCOME TAXES

The provision for current income taxes for the three month period ended December 31, 2012 was a charge of \$0.5 million as compared to the charge of \$0.1 million for the same period in 2011. The Company is carrying forward taxable losses from prior years which are eligible to be set-off against the current year's taxable profits.

## DEFERRED INCOME TAXES

Provision for deferred income taxes for the three month period ended December 31, 2012 were a recovery of \$0.2 million and was the same for the corresponding period in 2011. Deferred taxes result from the change in temporary differences between the financial reporting and tax bases of certain balance sheet items for the period.

## ADJUSTED FREE CASH FLOW

Adjusted free cash flow was an inflow of \$1.9 million for the three month period ended December 31, 2012, compared to an outflow of \$1.3 million for the three month period ended December 31, 2011. The increase in adjusted free cash flow for the three month period ended December 31, 2012 was due primarily to the increase in EBITDA and changes in working capital.

# CARGOJET 2012 Annual Report



## DIVIDENDS

Total dividends declared for the three month period ended December 31, 2012 were \$1,191,818 or \$0.149 per share. In comparison, total dividends declared for the three month period ended December 31, 2011 were \$1,079,112 or \$0.135 per share.

Record Date	Date Dividends Paid/Payable	Declared	Number of Shares	Per Share	Paid
		\$		\$	\$
September 20, 2012	October 4, 2012	-	-	-	1,135,065
December 20, 2012	January	1,191,818	7,993,416	0.1491	
		1,191,818		0.1491	1,135,065

Record Date	Date Dividends Paid/Payable	Declared	Number of Shares	Per Share	Paid
		\$		\$	\$
September 20, 2011	October 5, 2011	-	-	-	1,079,111
December 20, 2011	January 15, 2012	1,079,112	7,993,416	0.1350	
		1,079,112		0.1350	1,079,111

The Company increased its dividend to \$0.149 per share from \$0.142 per share on a quarterly basis effective with the three month period ended December 31, 2012.

## LIQUIDITY AND CAPITAL RESOURCES

Cash provided by operating activities after net changes in non-cash working capital balances for the three month period ended December 31, 2012 was \$6.7 million as compared to \$2.0 million for the same period in 2011. The \$4.7 million increase in cash was due primarily to the increase in EBITDA and timing of collections of accounts receivable and settlement of accounts payable.

Cash used in financing activities during the three month period ended December 31, 2012 was \$0.4 million as compared to the inflow of \$2.5 million for the same period in 2011. The \$2.9 million decrease was due to the lower bank borrowings in 2012.

Cash used in investing activities during the three month period ended December 31, 2012 was \$6.6 million and was due primarily to net capital asset additions.

## CAPITAL EXPENDITURES

Net capital asset additions were \$6.9 million for the three month period ended December 31, 2012 as compared to \$4.3 million for the same period in 2011. The capital asset additions in the current period were comprised of the purchase of engines, the transfer of heavy maintenance deposits for leased aircraft to deferred heavy maintenance and the purchase of leasehold improvements and rotatable assets.



## **REVIEW OF OPERATIONS FOR THE TWELVE MONTH PERIODS ENDED DECEMBER 31, 2012 AND 2011**

### **HIGHLIGHTS FOR THE TWELVE MONTH PERIODS ENDED DECEMBER 31, 2012 AND 2011**

- Total revenue for the twelve month period ended December 31, 2012 was \$168.8 million as compared to \$165.5 million for the same period in 2011, representing an increase of \$3.3 million or 2.0%.
- Average daily cargo revenue excluding fuel surcharges and other cost pass-through revenues for the twelve month period ended December 31, 2012 was \$0.66 million per operating day, as compared to \$0.64 million per operating day for the same period in 2011, representing an increase of \$0.02 million or 3.1%.
- EBITDA from continuing operations for the twelve month period ended December 31, 2012 was \$16.9 million as compared to \$15.2 million for the same period in 2011 representing an increase of \$1.7 million or 11.2%.
- Adjusted free cash flow was an inflow of \$8.2 million for the twelve month period ended December 31, 2012 as compared to an inflow of \$3.0 million for the same period in 2011, an increase of \$5.2 million or 173.3%

## **REVENUE**

Total revenue for the twelve month period ended December 31, 2012 was \$168.8 million as compared to \$165.5 million for the same period in 2011, representing an increase of \$3.3 million or 2.0%. The increase in revenues was due primarily to higher ad-hoc charter revenues and the expansion of Cargojet's network in Eastern Canada.

Revenue related to the core overnight business excluding fuel surcharges and other cost pass-through revenues, for the twelve month period ended December 31, 2012 was \$109.4 million compared to \$110.3 million for the same period in 2011, a decrease of \$0.9 million or 0.8%.

Revenue related to the ACMI cargo business for the twelve month period ended December 31, 2012 was \$6.5 million compared to \$9.5 million for the same period in 2011, a decrease of \$3.0 million or 31.6%. The decrease in ACMI revenues was due primarily to the cancellation of an ACMI route in last quarter of 2011 by one of Cargojet's customers who exited the North American air cargo market.

Revenue related to scheduled and ad-hoc charters for the twelve month period ended December 31, 2012 was \$14.2 million compared to \$6.5 million for the same period in 2011, an increase of \$7.7 million or 118.5%. The increase in the revenue was due primarily to the increase in ad-hoc charter activities during the year.

Fuel surcharges and other cost pass-through revenues were \$37.2 million for the twelve month period ended December 31, 2012 as compared to \$37.7 million for the same period in 2011, representing a decrease of \$0.5 million or 1.3%. The decrease was due primarily to the reduction in ACMI surcharge revenue partially offset by an increase in third party fuel sales. Fuel surcharges and other cost pass-through revenues include fuel sales to third parties of \$3.3 million for the twelve month period ended December 31, 2012, as compared to \$2.1 million for the same period in 2011.

Other revenues were \$1.5 million for the twelve month period ended December 31, 2012 and remained unchanged from \$1.5 million for the same period in 2011.

## **DIRECT EXPENSES**

Total direct expenses were \$140.5 million for the twelve month period ended December 31, 2012 as compared to \$135.7 million for the same period in 2011, representing an increase of \$4.8 million or 3.5%. As a percentage of revenue, direct expenses increased from 82.0% in 2011 to 83.2% for the same period in 2012. The overall increase in direct expenses was due primarily to higher fuel costs, increased commercial and crew costs and increased depreciation expense partially offset by savings in maintenance and aircraft costs.

Fuel costs were \$62.4 million for the twelve month period ended December 31, 2012 as compared to \$56.8 million for the same period in 2011. The \$5.6 million or 9.9% increase in fuel costs were due to higher fuel prices and an increase in block hours flown related to ad-hoc charter flights and expansion of Cargojet's network in Eastern Canada. The cost incurred by the Company due to higher fuel prices was passed on to customers as an increase in their fuel surcharges.

Depreciation expense increased from \$4.8 million in 2011 to \$6.4 million in 2012, an increase of \$1.6 million or 33.3%. The increase was due primarily to the acquisition of previously leased aircraft in the last quarter of 2011 and a change in the estimate related to engine depreciation partially offset by the sale of regional aircraft.



## DIRECT EXPENSES (CONTINUED)

Aircraft costs were \$14.8 million for the twelve month period ended December 31, 2012 as compared to \$16.1 million for the same period in 2011. The \$1.3 million or 8.1% decrease in aircraft costs were due primarily to lower lease costs due to the acquisition of previously leased aircraft in the last quarter of 2011 and cancellation of regional sub-charter flights due to Cargojet's network expansion in Eastern Canada, partially offset by the lease of 767 engines due to unscheduled engine maintenance.

Heavy maintenance amortization costs were \$2.9 million for the twelve month period ended December 31, 2012 as compared to \$3.4 million for the same period in 2011, a decrease of \$0.5 million or 14.7%. Heavy maintenance of aircraft occurs at regular and predetermined intervals and costs related to these are deferred by the Company and amortized over a period of 18 to 24 months until the next scheduled heavy maintenance.

Maintenance costs were \$9.0 million for the twelve month period ended December 31, 2012 as compared to \$10.0 million for the same period in 2011. The decrease of \$1.0 million or 10.0% was primarily due to the decrease in maintenance staff and lower line maintenance costs.

Total crew costs including salaries, training and positioning were \$9.6 million for the twelve month period ended December 31, 2012 as compared to \$9.4 million for the same period in 2011, an increase of \$0.2 million or 2.1%. The increase was due primarily to the increase in crew positioning costs.

Commercial and other direct operating costs were \$35.3 million for the twelve month period ended December 31, 2012 as compared to \$34.9 million for the same period in 2011. The increase of \$0.4 million or 1.1% was due primarily to the increase in ground handling, landing and navigation charges due to the higher number of ad-hoc charter flights and due to the expansion of Cargojet's network in Eastern Canada.

## SELLING, GENERAL AND ADMINISTRATIVE EXPENSES

Selling, general and administrative ("SG&A") expenses were \$18.9 million for the twelve month period ended December 31, 2012 compared to \$19.6 million for the same period in 2011. The decrease of \$0.7 million in SG&A expenses was due primarily to staff reduction in 2012, foreign exchange losses and dissolution costs in 2011 related to Prince Edward Air Ltd. partially offset by higher employee and management bonuses in 2012.

## EBITDA

EBITDA from continuing operations for the twelve month period ended December 31, 2012 was \$16.9 million or 10.0% of revenue, compared to \$15.2 million or 9.2% of revenue for the same period in 2011. The increase of \$1.7 million in EBITDA was due primarily to the following:

- The increase in core overnight revenues due to the expansion of Cargojet's network in Eastern Canada.
- Increased ad-hoc charters during the year.
- Savings from headcount reductions.
- Reduced net heavy maintenance expenditures.

## FINANCE COSTS

Net finance costs were \$3.3 million for the twelve month period ended December 31, 2012, compared to \$3.1 million for the twelve month period ended December 31, 2011. The increase of \$0.2 million or 6.5% was due to the interest on debentures and the timing of the issuance of new debentures and the redemption of old debentures.

## CURRENT INCOME TAXES

The provision for current income taxes for the twelve month period ended December 31, 2012 was a charge of \$0.5 million as compared to the charge of \$1.5 million for the same period in 2011. The Company is carrying forward taxable losses from prior years that are eligible to be set-off against the current year's taxable profits.



# CARGOJET 2012 Annual Report



## DEFERRED INCOME TAXES

The deferred income tax provision of \$1.0 million for the twelve month period ended December 31, 2012 compared to the recovery of deferred income tax of \$0.5 million for the same period in 2011 represents the change in temporary differences between the financial reporting and tax bases of certain balance sheet items for the period and the reduction of deferred tax asset on operating losses proportionate to utilization during the current year to offset income.

## ADJUSTED FREE CASH FLOW

Adjusted free cash flow was an inflow of \$8.2 million for the twelve month period ended December 31, 2012, compared to an inflow of \$3.0 million for the twelve month period ended December 31, 2011. The improvement of \$5.2 million was due primarily to the increase in EBITDA and lower expenditures for property, plant and equipment.

## DIVIDENDS

Total dividends declared for the twelve month period ended December 31, 2012 were \$4,597,013 or \$0.575 per share. In comparison, total dividends declared for the twelve month period ended December 31, 2011 were \$4,244,504 or \$0.531 per share.



Record Date	Date Dividends Paid/Payable	Declared	Number of Shares	Per Share	Paid
		\$		\$	\$
December 20, 2011	January 5, 2012	-	-	-	1,079,112
March 20, 2012	April 5, 2012	1,135,065	7,993,416	0.1420	1,135,065
June 20, 2012	July 5, 2012	1,135,065	7,993,416	0.1420	1,135,065
September 20, 2012	October 5, 2012	1,135,065	7,993,416	0.1420	1,135,065
December 20, 2012	January 4, 2013	1,191,818	7,993,416	0.1491	-
		4,597,013		0.5751	4,484,307

Record Date	Date Dividends Paid/Payable	Declared	Number of Shares	Per Share	Paid
		\$		\$	\$
December 31, 2010	January 14, 2011	-	-	-	335,723
January 31, 2011	February 15, 2011	335,723	7,993,416	0.0420	335,723
February 28, 2011	March 15, 2011	335,724	7,993,416	0.0420	335,724
March 31, 2011	April 15, 2011	335,723	7,993,416	0.0420	335,723
June 20, 2011	July 5, 2011	1,079,111	7,993,416	0.1350	1,079,111
September 20, 2011	October 5, 2011	1,079,111	7,993,416	0.1350	1,079,111
December 20, 2011	January 5, 2012	1,079,112	7,993,416	0.1350	-
		4,244,504		0.5310	3,501,115

The Company began paying dividends on a quarterly basis effective with the three month period ended June 30, 2011.

The Company increased its dividend to \$0.149 per share from \$0.142 per share on a quarterly basis effective with the three month period ended December 31, 2012.

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## LIQUIDITY AND CAPITAL RESOURCES

Cash provided by operating activities from continuing operations after net changes in non-cash working capital balances for the twelve month period ended December 31, 2012 was \$20.4 million as compared to \$15.1 million for the same period in 2011. The increase of \$5.3 million in cash was due primarily to the increase in EBITDA, the transfer of heavy maintenance deposits that will not be refunded but will reduce the obligations related to leased returned conditions and the timing of collections of accounts receivable and settlement of accounts payable.

Cash used in financing activities during the twelve month period ended December 31, 2012 was \$9.8 million and was comprised of the net repayment of long-term debt of \$7.6 million, redemption of debentures of \$24.7 million, purchase of treasury shares of \$0.3 million and dividends paid to shareholders of \$4.5 million partially offset by the proceeds from the issuance of debentures of \$27.3 million.

Cash used in investing activities during the twelve month period ended December 31, 2012 was \$10.3 million and was primarily comprised of net additions to property, plant and equipment.

The Company renewed its revolving credit facility with a Canadian chartered bank in October 12, 2012. The credit facility is to a maximum of \$25.0 million, bears interest at bank prime plus 1.75% and is repayable on maturity, December 31, 2015. The credit facility is subject to customary terms and conditions for borrowers of this nature, including, for example, limits on incurring additional indebtedness and granting liens or selling assets without the consent of the lenders. The credit facility is subject to the maintenance of certain financial covenants. The Company was in compliance with all covenants as at December 31, 2012.

The credit facility is secured by the following:

- general security agreement over all assets of the Company;
- guarantee and postponement of claim to a maximum of \$35.0 million in favour of Cargojet Partnership (wholly-owned subsidiary of the Company) and certain other entities of the Company; and
- assignment of insurance proceeds, payable to the bank.

The Company also maintains fixed loans with another Canadian chartered bank through its subsidiary Cargojet Airways Ltd. ("CJA"). The fixed loans bear interest at rates ranging from 8.1% to 8.2%. They are secured by the regional aircraft owned by CJA and the Company's notes receivable. The loans are repayable in monthly installments plus interest and will mature by August 2014. The Company has also provided a standby letter of credit of \$780,000 to the bank which is held against the fixed loans.

Management anticipates that the funds available under the revolving credit facility and cash flow from operations will be adequate to fund anticipated capital expenditures, working capital and cash dividends. There are no provisions in debt, lease or other arrangements that could trigger an additional funding requirement or early payment based on current or expected results. There are no circumstances that management is aware of that would impair the Company's ability to undertake any transaction which is essential to the Company's operations.

## CAPITAL EXPENDITURES

Net additions to property, plant and equipment were \$11.5 million for the twelve month period ended December 31, 2012 as compared to \$10.3 million for the same period in 2011.

## FINANCIAL CONDITION

The following is a comparison of the financial position of the Company as at December 31, 2012 to the financial position of the Company as at December 31, 2011.

## ACCOUNTS RECEIVABLE

Accounts receivable as at December 31, 2012 amounted to \$11.2 million as compared to \$10.7 million as at December 31, 2011. The increase of \$0.5 million was due to the timing of cash collections from customers. The quality of the Company's net receivable balances and its current collections, in management's opinion, remains excellent.

# CARGOJET 2012 Annual Report



## PROPERTY, PLANT AND EQUIPMENT

As at December 31, 2012 property, plant and equipment were \$46.7 million as compared to \$44.0 million as at December 31, 2011. The \$2.7 million net increase in property, plant and equipment was due primarily to the property, plant and equipment additions of \$11.5 million, the recognition of \$1.5 million deferred heavy maintenance assets partially offset by the amortization of property, plant and equipment of \$9.8 million and asset impairment of \$0.5 million.

## TRADE AND OTHER PAYABLES

Trade and other payables as at December 31, 2012 were \$11.8 million as compared to \$10.6 million as at December 31, 2011. The increase of \$1.2 million was due primarily to the timing of supplier payments.

## WORKING CAPITAL POSITION

The Company had a working capital surplus as at December 31, 2012, representing the difference between total current assets and current liabilities, of \$1.3 million, compared to a working capital surplus of \$1.6 million as at December 31, 2011. The decrease of \$0.3 million is primarily due to the timing of collection of trade and other receivables and settlement of trade and other payables partially offset by a decrease in prepaid expenses and deposits.

## BORROWINGS

Total borrowings excluding the current portion were \$3.0 million as at December 31, 2012 as compared to \$10.6 million as at December 31, 2011. The long-term debt consists of revolving credit facility and fixed loans. The decrease of \$7.6 million is due to the reduced usage of the revolving credit facility and partial repayment of the fixed loans.

## PROVISIONS

Provisions as at December 31, 2012 were \$1.5 million as compared to \$nil as at December 31, 2011 and were comprised of maintenance liabilities for leased aircraft estimated to be incurred at the end of their lease terms.

## SUMMARY OF CONTRACTUAL OBLIGATIONS

As at December 31, 2012 (in thousands)	Payments due by period					
	Total	2013	2014	2015	2016	Thereafter
Fixed Loans	1,139	822	317	-	-	-
USD Forward Sale Contracts	1,000	1,000	-	-	-	-
Revolving credit facility	2,730	-	-	2,730	-	-
Operating Leases	33,112	10,514	10,377	9,079	1,989	1,153
	37,981	12,336	10,694	11,809	1,989	1,153



## OFF-BALANCE SHEET ARRANGEMENTS

The Company does not have any off-balance sheet arrangements other than those disclosed under “Summary of Contractual Obligations”.

## MAJOR CUSTOMERS

During the three and twelve month periods ended December 31, 2012, the Company had sales to three customers that represented 54% and 55%, of the total revenues, respectively (December 31, 2011 - 53% and 48% respectively). These sales are provided under service agreements that expire over various periods to September 2018.

## CONTINGENCIES

The Company has provided irrevocable standby letters of credit totaling approximately \$3.0 million to financial institutions as security for its loans, corporate credit cards, and to a number of vendors as security for the Company’s ongoing leases and purchases.

## OUTLOOK

Cargojet experienced strong demand for its charter services and customer demand on its core overnight network improved with stabilizing economic conditions. Cargojet continues to retain all of its major customers and expects that demand on its core overnight network will further improve with a stronger economy. The pro-active management of its fleet capacity, strong on-time performance and control over its cost structure will give added advantage to the Company in this competitive market. Management expects to achieve organic growth within its existing customer base and to obtain new customers for both its domestic and international routes as the Company is making efforts to build on its competitive market position. Continued efforts to expand business have created growth opportunities in Eastern Canada in its overnight network and in international market, in its charter activities that has resulted in enhancements to volumes and revenue. The Company expects long-term enhancements to overnight and charter volumes and revenue as a result of the new activities.

The Company also continues to recover fuel price increases through fuel surcharges. Any fuel cost increases due to higher fuel prices are passed on to customers as an increase in fuel surcharge and billed to customers on a cost recovery basis only. Similarly, any cost savings due to lower fuel prices are passed on to customers as a decrease in fuel surcharge. Management is confident that the Company will continue to fully recover any future increases in fuel costs.

Management’s principal objective is to maximize free cash flow available for dividends by continuing to provide quality air cargo services, increasing the range of these services, focusing on improving efficiencies and cost controls, and growing the business organically and through strategic and accretive acquisitions. Management continuously reviews and evaluates all of the foregoing initiatives especially those that can improve cash flow.

Future strategic initiatives may be financed from working capital, cash flow from operations, borrowing or the issuance of shares. Any decisions regarding the above, including further increases or decreases in dividends, will be considered and determined as appropriate by the Board of Directors of Cargojet Inc.

## CRITICAL ESTIMATES

The preparation of financial statements in conformity with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates. The significant items requiring the use of management estimates are the valuation of financial instruments, the impairment assessment of property, plant and equipment and goodwill, the accounting for deferred taxes, and the estimate of provisions. The table below discloses the methodology used by management in the assessment of these accounting estimates.

# CARGOJET 2012 Annual Report



## CRITICAL ESTIMATES (CONTINUED)



Critical Accounting Estimate	Methodology, Assumptions
Financial instruments	<p>The issuance or repurchase of a compound instrument, such as convertible debentures, requires the Company to estimate the debt and equity components of the instruments issued or repurchased. Estimates are also required for determining the fair values of financial instruments that are not publicly traded for disclosure purposes.</p>
Impairment of property, plant and equipment and goodwill	<p>At the end of each reporting period, the Company reviews the carrying amounts of its property, plant and equipment 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.</p> <p>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. An impairment loss is recognized immediately in profit or loss.</p>
Deferred taxes	<p>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 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</p>
Provisions	<p>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. Such costs have been estimated based on contractual commitments and Company specific history. The Company reviews the provisions at each reporting period to determine the change in estimated liability.</p>



## **ACCOUNTING CHANGES**

### **ACCOUNTING STANDARDS EFFECTIVE FOR 2012**

*IFRS 7, Financial Instruments: Disclosures and IAS 12, Income Taxes* were amended to address disclosures with respect to the transfer of financial assets and the recovery of revalued investment properties, respectively. These amendments, which were effective January 1, 2012, had no impact on the Company's financial statements.

A number of new standards, amendments to standards and interpretations have been issued but are not yet effective for the financial year ending December 31, 2012, and accordingly, have not been applied in preparing these financial statements:

#### *Presentation of Financial Statements*

The IASB amended IAS 1, Presentation of Financial Statements ("IAS 1"), providing guidance on items contained in other comprehensive income ("OCI") and their classification within OCI. The amendments to IAS 1 must be applied retrospectively for annual periods beginning on or after July 1, 2012. The Company does not expect the adoption of this standard to have a significant impact on the Company's disclosures.

#### *Annual Improvements to IFRSs: 2009 - 2011 Cycle*

The Annual Improvements to IFRSs: 2009 - 2011 Cycle include a number of amendments to various IFRSs that are effective for periods beginning on or after January 1, 2013.

Amendments to *IAS 1, Presentation of Financial Statements* clarify the requirements for providing comparative information in financial statements. Amendments reduce the amount of information from previous reporting periods which is required to be repeated in the event of a change in accounting policy, reclassification or restatement by limiting the requirement to present an additional statement of financial position to circumstances when the statement is materially affected and by clarifying that related notes to an additional statement of financial position are not required.

*IAS 16, Property, Plant and Equipment* was amended to clarify the classification requirement for servicing equipment. If spare parts and servicing equipment meet the definition of property, plant and equipment, they should be accounted for as such rather than a current asset.

*IAS 34, Interim Financial Reporting* was amended to clarify the requirements on segment information for total assets and liabilities for each reportable segment.

The Company does not expect the adoption of these amendments to have a significant impact on the Company's disclosures.

#### *Employee Benefits*

The primary amendment to *IAS 19, Employee Benefits*, is the elimination of the corridor approach, with a requirement that all changes to the defined benefit obligation and planned assets to be recognized when they occur. The standard also does not permit the use of an assumed expected rate of return which differs from the rate used to discount plan liabilities and changes the presentation for defined benefit plans.

This standard is applicable for periods commencing January 1, 2013. Retrospective application is required with certain exceptions. The Company does not expect the adoption of this standard to have a significant impact on its results of operations, financial position and disclosures.

#### *Fair Value Measurement*

*IFRS 13, Fair Value Measurement ("IFRS 13")* is a new standard that defines fair value, sets out in a single IFRS, a framework for measuring fair value and requires disclosures about fair value measurements. *IFRS 13* does not determine when an asset, a liability or an entity's own equity instrument is measured at fair value. Rather, the measurement and disclosure requirements of *IFRS 13* apply when another IFRS requires or permits the item to be measured at fair value (with limited exceptions). The standard is applicable commencing January 1, 2013.

#### *Consolidation, Joint Arrangements, Associates and Disclosures*

A package of five standards addressing consolidation, joint arrangements, associates and disclosures are effective for periods beginning on or after January 1, 2013.

# CARGOJET 2012 Annual Report



## **FINANCIAL CONDITION (CONTINUED)**

### **STANDARDS AND INTERPRETATIONS ISSUED NOT YET ADOPTED (CONTINUED)**

*IFRS 10, Consolidated Financial Statements ("IFRS 10")* builds on existing principles by identifying the concept of control as the determining factor in whether an entity should be included within the consolidated financial statements of the parent company. The standard provides additional guidance to assist in the determination of control where this is difficult to assess.

*IFRS 11, Joint Arrangements* establishes principles that are applicable to the accounting for all joint arrangements.

*IFRS 12, Disclosure of Interests in Other Entities* provides guidance on disclosure requirements for all forms of interests in other entities, including subsidiaries, joint arrangements, associates and unconsolidated structured entities.

The Company does not expect the implementation of these standards to have a significant impact on the Company's results of operations, financial position and disclosures.

#### *Offsetting Financial Assets and Financial Liabilities and Related Disclosures*

Amendments to *IFRS 7, Financial Instruments: Disclosures* and *IAS 32, Financial Instruments: Presentation*, applicable for periods commencing on or after January 1, 2013 and January 1, 2014, respectively, require entities to disclose information about rights of offset and related arrangements and clarify existing application issues relating to the offset of financial assets and financial liabilities requirements. The Company does not expect the adoption of these standards to have a significant impact on the Company's disclosures.

#### *Financial Instruments*

The IASB has issued *IFRS 9, Financial Instruments ("IFRS 9")*, which will ultimately replace *IAS 39, Financial Instruments: Recognition and Measurement ("IAS 39")*. IFRS 9 introduces new requirements for the classification and measurement of financial assets and liabilities and for de-recognition.

The replacement of IAS 39 is a multi-phase project with the objective of improving and simplifying the reporting for financial instruments and the issuance of IFRS 9 is part of the first phase. This standard becomes effective on January 1, 2015. The Company has yet to assess the impact of the new standard on its results of operations, financial position and disclosures.

## **OUTSTANDING SHARE DATA**

Cargojet listed its common shares for trading on January 6, 2011 under the symbol "CJT" on the TSX stock Exchange. The following table sets out the common shares outstanding and securities convertible into common shares as of the date of this MD&A:

<b>Capital</b>	<b>Authorized/Principal</b>	<b>Outstanding</b>	<b>Common Shares underlying Convertible securities</b>
Common Shares	Unlimited	7,993,416	-
Convertible Debentures - 6.5%	\$ 28,750,000	-	2,446,809



## INFORMATION DISCLOSURE CONTROLS AND PROCEDURES AND INTERNAL CONTROLS OVER FINANCIAL REPORTING

Disclosure controls and procedures within the Company are designed to provide reasonable assurance that appropriate and timely decisions are made regarding public disclosure. This is accomplished through the establishment of systems that identify and communicate relevant information to persons responsible for preparing public disclosure items, in accordance with the Disclosure Policy adopted jointly by the Directors of the Company.

Internal controls over financial reporting are designed to provide reasonable assurance regarding the reliability of the Company's financial reporting and its preparation of financial statements for external purposes in accordance with IFRS.

An evaluation of the effectiveness of the Company's disclosure controls and procedures and internal controls over financial reporting, as defined under the rules of the Canadian Securities Administrators, was conducted at December 31, 2012 by management. Based on this evaluation, the Chief Executive Officer and the Chief Financial Officer have concluded that the disclosure controls and procedures and internal controls over financial reporting of the Company are effective. This Management Discussion and Analysis was reviewed by the Disclosure Officers of the Company (individuals authorized to communicate with the public about information concerning the Company), the Audit Committee and the Board of Directors of the Company, all of whom approved it prior to its publication.

## END NOTES

<sup>(A)</sup> All references to "EBITDA" in the Management's Discussion and Analysis exclude some or all of the following: "depreciation, interest on long-term debt, future income tax recovery, provision for current income taxes, non-controlling interest, gain or loss on disposal of capital assets and amortization of aircraft heavy maintenance expenditures". EBITDA is a term used by the Company that does not have a standardized meaning prescribed by IFRS and is therefore unlikely to be comparable to similar measures used by other issuers. EBITDA is a measure of the Company's operating profitability and by definition, excludes certain items as detailed above. These items are viewed by management as non-cash (in the case of depreciation, gain or loss on disposal of capital assets, amortization of aircraft heavy maintenance

expenditures and future income tax recovery), or nonoperating (in the case of interest on long-term debt, provision for current income taxes and non-controlling interest). The underlying reasons for exclusion of each item are as follows:

**Depreciation** - as a non-cash item, depreciation has no impact on the determination of EBITDA.

**Interest on long-term debt** - interest on long-term debt is a function of the Company's treasury/financing activities and represents a different class of expense than those included in EBITDA.

**Deferred income tax** - the calculation of deferred income tax is a function of temporary differences between the financial reporting and the tax basis of balance sheet items for calculating tax expense and is separate from the daily operations of the Company.

**Provision for current income taxes** - the provision for current income taxes is a non-operating item and represents a different class of expense than those included in EBITDA.

**Gain or loss on disposal of property, plant & equipment** - the gain or loss arising from the disposal of property, plant & equipment is a non-cash item and has no impact on the determination of EBITDA.

**Gain or loss on disposal of intangible assets** - the gain or loss arising from the disposal of intangible assets is a non-cash item and has no impact on the determination of EBITDA.

**Gain or loss on repurchases of debentures** - the gain or loss arising from repurchase of debentures is a non-cash item and has no impact on the determination of EBITDA.

**Aircraft heavy maintenance depreciation** - aircraft heavy maintenance depreciation represents a non-cash item and is excluded from EBITDA.

**Amortization of maintenance deposits** - amortization of non-refundable maintenance deposits paid to lessors that exceeds the estimated amounts recoverable represents a non-cash item and is excluded from EBITDA.





## END NOTES (CONTINUED)

<sup>(B)</sup> Adjusted Free Cash Flow is a term, which does not have a standardized meaning prescribed by IFRS and is therefore unlikely to be comparable to similar measures used by other Companies. The objective of presenting this non-IFRS measure is to calculate the amount, which is available for dividend distributions to shareholders. Adjusted Free Cash Flow is not necessarily indicative of cash available to fund cash needs and should not be considered an alternative to cash flow as a measure of liquidity. All references in the Management's Discussion and Analysis to "Adjusted Free Cash Flow" have the meaning set out in this note.

In November 2010, the Canadian Institute of Chartered Accountants ("CICA") issued a consultation guidance titled *Reporting Supplementary Financial Measures, General Principles (The Guidance)*. The Guidance approved the continuation of previously published guidance on EBITDA and free cash flow as they continue to be relevant in the post IFRS environment.

Standardized Free Cash Flow is defined as "Cash flows from operating activities as reported in the IFRS financial statements, including operating cash flows provided from or used in discontinued operations; total capital expenditures minus proceeds from the disposition of capital assets other than those of discontinued operations, as reported in the IFRS financial statements; and dividends, when stipulated, unless deducted in arriving at cash flows from operating activities."

The Company has adopted a measurement called Adjusted Free Cash Flow to supplement net earnings as a measure of operating performance. Adjusted Free Cash Flow is defined by the Company as Standardized Free Cash Flow as defined by the CICA, less operating cash flows provided from or used in discontinued operations, changes in working capital, plus provision or recovery of current income taxes.

*The underlying reasons for the inclusion and exclusion of each item are as follows:*

**Operating cash flows provided from or used in discontinued operations** - As the operating cash flows provided from or used in discontinued operations are not expected to recur in the future, it has been excluded from the calculation of Adjusted Free Cash Flow to enhance the predictive value of the measure.

**Changes in working capital** - Changes in non-cash working capital items and deposits represents timing differences in the Company's working capital from year to year. These items are expected to be recoverable or payable shortly from the balance sheet date. Since it only represents short-term timing differences, it should be excluded from standardized free cash flow to determine a more representative measure of cash that is available for dividend distributions.

**Provision for current income taxes** - The expected cash outflows from the provision of current income tax is deducted to determine cash that is available for dividend distributions as it has priority over distribution.





# Management's Report to the Shareholders



The consolidated financial statements of Cargojet Inc. and all information in this annual report are the responsibility of management and have been approved by the Board of Directors.

The financial statements have been prepared by management in accordance with International Financial Reporting Standards. They include some amounts that are based on management's best estimates and judgments. Financial information included elsewhere in the annual report is consistent with that in the financial statements.

The management of Cargojet has developed and maintains an internal accounting system and administrative controls in order to provide reasonable assurance that the financial transactions are properly recorded and carried out with the necessary approval, and that the consolidated financial statements are properly prepared and the assets properly safeguarded.

The Board of Directors carried out its responsibility for the financial statements in this annual report principally through its Audit Committee. The Audit Committee reviews the corporation's annual consolidated financial statements and recommends their approval by the Board of Directors.

These financial statements have been audited by the external auditors, Deloitte & Touche LLP, Chartered Accountants, Licensed Public Accountants, whose report follows.

Dr. Ajay K. Virmani

President and Chief Executive Officer  
March 2013



# Independent Auditor's Report

## Deloitte.

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, 2012 and December 31, 2011, and the consolidated statements of income, consolidated statements of comprehensive income, consolidated statements of changes in equity, and consolidated statements of cash flows for the years then ended, and a summary of significant accounting policies and other explanatory information.

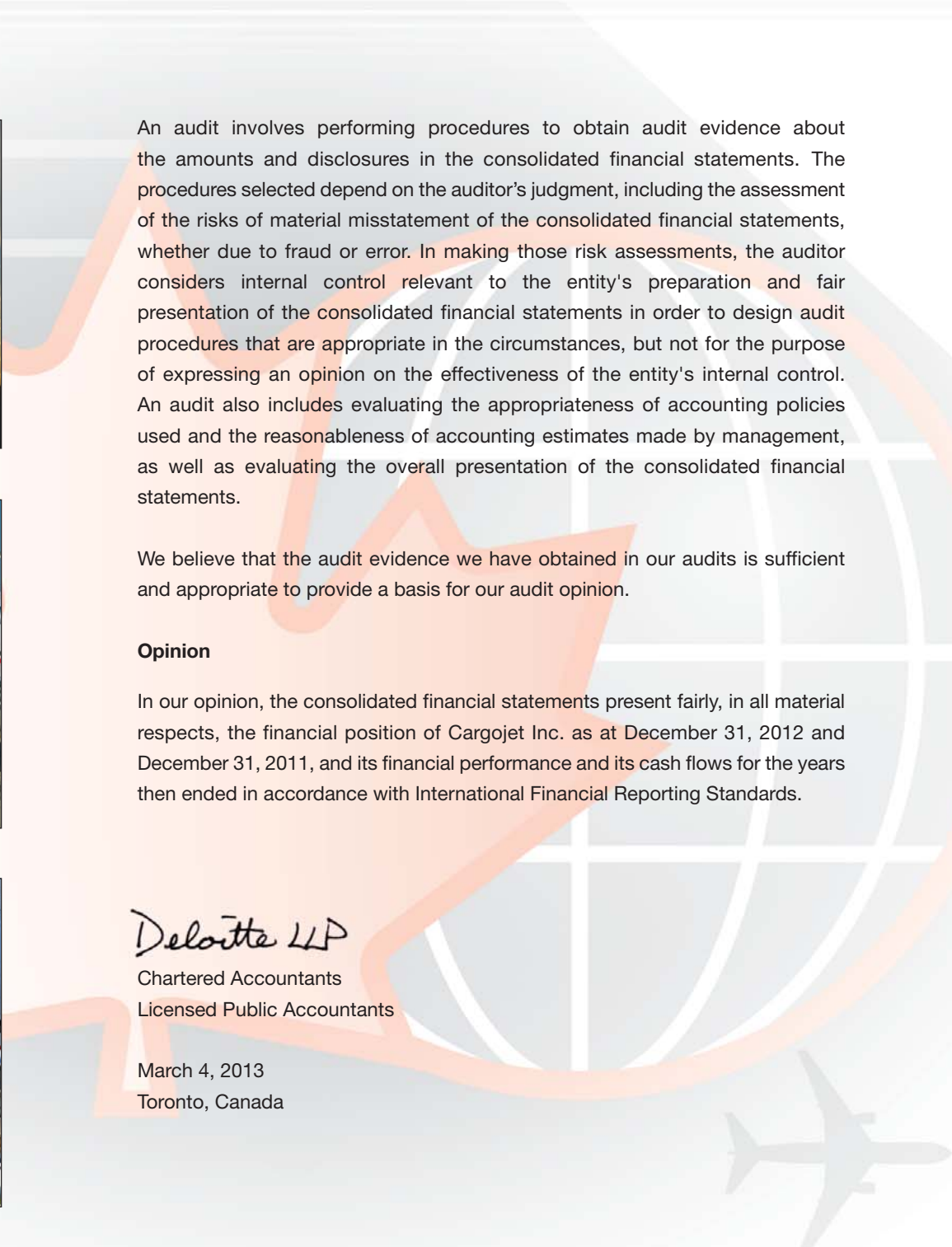
### Management's Responsibility for the Consolidated Financial Statements

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.

#### Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Cargojet Inc. as at December 31, 2012 and December 31, 2011, and its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards.

*Deloitte LLP*

Chartered Accountants  
Licensed Public Accountants

March 4, 2013  
Toronto, Canada





Consolidated Financial Statements of

# CARGOJET INC.

For the years ended  
December 31, 2012 and 2011



# CARGOJET 2012 Annual Report



## CARGOJET INC. Consolidated Balance Sheets

As at December 31, 2012 and 2011 (in Canadian dollars)

	Note	December 31, 2012 \$	December 31, 2011 \$
<b>ASSETS</b>			
<b>CURRENT ASSETS</b>			
Cash		149,976	-
Trade and other receivables		11,245,805	10,744,026
Inventories	3	720,756	700,626
Prepaid expenses and deposits		2,397,021	2,300,663
Current portion of notes receivable	4	821,102	821,102
Current portion of finance lease receivable	5	293,017	293,017
Assets held for sale	6	-	45,000
		15,627,677	14,904,434
<b>NON-CURRENT ASSETS</b>			
Property, plant and equipment	6	46,710,150	43,999,601
Notes receivable	4	1,719,188	2,418,568
Finance lease receivable	5	361,477	623,693
Goodwill	7	46,169,976	46,169,976
Intangible assets	8	1,000,000	1,000,000
Deposits		1,853,412	5,521,614
Deferred income taxes on assets held for sale	6	-	3,567
		113,441,880	114,641,453
<b>LIABILITIES</b>			
<b>CURRENT LIABILITIES</b>			
Overdraft		-	110,235
Trade and other payables	9	11,755,753	10,580,082
Income taxes payable		449,927	734,000
Dividends payable		1,191,819	1,079,112
Borrowings	10	885,780	757,677
Finance leases		-	35,135
		14,283,279	13,296,241
<b>NON-CURRENT LIABILITIES</b>			
Borrowings	10	2,983,470	10,562,566
Provisions	11	1,543,784	-
Convertible debentures	12	25,263,531	23,916,542
Deferred income taxes	13	4,897,545	3,249,721
		48,971,609	51,025,070
<b>EQUITY</b>			
		64,470,271	63,616,383
		113,441,880	114,641,453

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

John P. Webster  
Trustee

Dr. Ajay K. Virmani  
President and Chief Executive Officer

# CARGOJET 2012 Annual Report



## CARGOJET INC. Consolidated Statements of Income

Years ended December 31, 2012 and 2011 (in Canadian dollars)

	Note	2012 \$	2011 \$
REVENUES		168,770,688	165,510,674
DIRECT EXPENSES		140,425,837	135,674,982
		28,344,851	29,835,692
General and administrative expenses		18,117,073	18,956,206
Sales and marketing expenses		835,435	587,251
(Gain) loss on disposal of property, plant and equipment		(87,636)	1,164,270
Loss on impairment of property, plant and equipment	6	567,395	1,764,285
Finance costs		3,504,211	3,323,148
Finance income		(210,459)	(234,950)
Gain on derivative contracts		(1,831)	(678,149)
Loss on debenture redemption	12	554,603	-
		23,278,791	24,882,061
EARNINGS BEFORE INCOME TAXES AND DISCONTINUED OPERATIONS		5,066,060	4,953,631
PROVISION FOR (RECOVERY OF) INCOME TAXES	13		
Current		527,528	1,485,404
Deferred		986,353	(495,773)
		1,513,881	989,631
INCOME FROM CONTINUING OPERATIONS		3,552,179	3,964,000
LOSS FROM DISCONTINUED OPERATIONS		-	(168,256)
NET INCOME		3,552,179	3,795,744
EARNINGS PER SHARE	15		
From continuing and discontinued operations			
- Basic		0.44	0.48
- Diluted		0.44	0.48
From continuing operations			
- Basic		0.44	0.50
- Diluted		0.44	0.50

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

# CARGOJET 2012 Annual Report



## CARGOJET INC. Consolidated Statements of Comprehensive Income

Years ended December 31, 2012 and 2011 (in Canadian dollars)

	Note	2012 \$	2011 \$
<b>NET INCOME</b>		3,552,179	3,795,744
OTHER COMPREHENSIVE INCOME			
Transfer of losses on foreign exchange contracts to net income, net of income taxes of \$Nil (2011 - \$71,210)	21	-	144,274
<b>TOTAL COMPREHENSIVE INCOME</b>		3,552,179	3,940,018

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



# CARGOJET 2012 Annual Report



## CARGOJET INC. Consolidated Statements of Changes in Equity

Years ended December 31, 2012 and 2011 (in Canadian dollars)

	Shareholders' Note capital	Share-based compensation reserve	Conversion option	Reserve for surplus on debenture repurchases	Accumulated comprehensive other income	Total shareholders' Deficit	equity
	\$	\$	\$	\$	\$	\$	\$
Balance, December 31, 2011	67,341,167	275,643	1,271,503	-	-	(5,271,930)	63,616,383
Net income and comprehensive income	-	-	-	-	-	3,552,179	3,552,179
Treasury shares - net	14 (11,727)	-	-	-	-	-	(11,727)
Share-based compensation	16 -	65,911	-	-	-	-	65,911
Conversion option on debenture redemption	12 -	-	(1,271,503)	1,271,503	-	-	-
Conversion option on debenture issuance	12 -	-	2,509,576	-	-	-	2,509,576
Deferred tax on conversion option	13 -	-	(665,038)	-	-	-	(665,038)
Dividends	14 -	-	-	-	-	(4,597,013)	(4,597,013)
Balance, December 31, 2012	67,329,440	341,554	1,844,538	1,271,503	-	(6,316,764)	64,470,271
Balance, December 31, 2010	-	-	-	-	(144,274)	(4,823,170)	(4,967,444)
Net income	-	-	-	-	-	3,795,744	3,795,744
Other comprehensive income	-	-	-	-	144,274	-	144,274
Total comprehensive income	-	-	-	-	144,274	3,795,744	3,940,018
Income trust conversion	1 67,784,167	-	1,778,326	-	-	-	69,562,493
Conversion option	-	-	(506,823)	-	-	-	(506,823)
Treasury shares - net	14 (443,000)	-	-	-	-	-	(443,000)
Share-based compensation	16 -	275,643	-	-	-	-	275,643
Dividends	14 -	-	-	-	-	(4,244,504)	(4,244,504)
Balance, December 31, 2011	67,341,167	275,643	1,271,503	-	-	(5,271,930)	63,616,383

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

# CARGOJET 2012 Annual Report



## CARGOJET INC. Consolidated Statements of Cash Flows

Years ended December 31, 2012 and 2011 (in Canadian dollars)

	Note	2012 \$	2011 \$
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>			
Net income		3,552,179	3,964,000
Items not affecting cash			
Depreciation of property, plant and equipment	6	9,827,694	9,067,742
Share-based compensation	16	350,619	397,468
Finance costs		3,504,211	3,323,148
Interest paid		(2,642,023)	(2,768,546)
Loss on purchase of debentures	12	554,603	-
(Gain) loss on disposal of property, plant and equipment		(87,636)	1,164,270
Impairment on property, plant and equipment	6	567,395	1,764,285
Non-cash interest on notes receivable		(158,314)	(217,056)
Non-cash interest on finance lease receivable		(41,353)	(16,710)
Income tax provision		1,513,881	989,631
Income tax payments		(811,601)	(2,403,521)
Transfer of losses on derivatives from other comprehensive income		-	215,484
Change in fair value on non-hedge derivatives		-	(678,149)
		16,129,655	14,802,046
Changes in non-cash working capital items and deposits			
Trade and other receivables		(501,779)	546,691
Inventories		(20,130)	374,032
Prepaid expenses and deposits		3,571,844	147,215
Trade and other payables		1,175,671	(506,198)
Net inflow of cash from continuing operations		20,355,261	15,363,786
Net outflow of cash from discontinued operations		-	(233,688)
<b>NET CASH GENERATED BY OPERATING ACTIVITIES</b>		<b>20,355,261</b>	<b>15,130,098</b>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>			
Repayment of borrowings		(7,594,406)	(7,998,496)
Proceeds from borrowings		-	5,655,002
Repayment of finance leases payable		(35,135)	(155,550)
Proceeds from disposition of derivative contracts		-	212,450
Proceeds from debenture issuance	12	27,305,000	-
Repayment of debenture	12	(24,655,000)	-
Purchase of treasury shares		(296,437)	(564,825)
Dividends paid to shareholders		(4,484,306)	(3,501,115)
<b>NET CASH USED IN FINANCING ACTIVITIES</b>		<b>(9,760,284)</b>	<b>(6,352,534)</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>			
Payments for property, plant and equipment		(11,785,116)	(11,249,786)
Proceeds from disposal of property, plant and equipment		289,087	958,861
Collections of notes receivable		857,694	681,604
Collections of finance lease receivable		303,569	100,000
<b>NET CASH USED IN INVESTING ACTIVITIES</b>		<b>(10,334,766)</b>	<b>(9,509,321)</b>
<b>NET CHANGE IN CASH</b>		<b>260,211</b>	<b>(731,757)</b>
<b>CASH (OVERDRAFT), BEGINNING OF YEAR</b>		<b>(110,235)</b>	<b>621,522</b>
<b>CASH (OVERDRAFT), END OF YEAR</b>		<b>149,976</b>	<b>(110,235)</b>

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



## **CARGOJET INC.** **Notes to the Consolidated Financial Statements**

December 31, 2012 and 2011

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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 thirteen 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 between Canada and Poland.

Cargojet is publicly listed with shares and convertible debentures traded on the Toronto Stock Exchange (“TSX”). The Company is incorporated and domiciled in Canada and the registered office is located at 350 Britannia Road East, Units 5 and 6, Mississauga, Ontario.

Prior to January 1, 2011, the operations of the Company were carried out by Cargojet Income Fund (“the Fund”). Effective January 1, 2011, the Fund was converted from an income trust to a corporate structure whereby all unitholders of the Fund had their trust units automatically converted into common shares of the Company on a one-for-one basis. The trust units and convertible debentures of the Fund were delisted from the TSX and the common voting shares and variable voting shares of the Company began trading on the TSX under the symbols “CJT” and “CJT.A”, respectively, on January 6, 2011. Convertible debentures of the Fund were converted into convertible debentures of the Company with no changes in their rights or terms.

The conversion has been accounted for using the continuity of interest basis, recognizing the Company as the successor in interest to the Fund. Accordingly, all assets and liabilities of the Company have been recorded in Cargojet at their previous carrying amounts at the date of conversion in the Fund. On conversion, the carrying values of the Trust Units of the Fund were transferred to the common shares of the Company. As the interest in the puttable Trust Units of the Fund were converted into common shares of the Company, the common shares, including the conversion option attached to the convertible debentures, have been classified as equity.

These consolidated financial statements (the “financial statements”) were approved and authorized for issuance by the Board of Directors on March 4, 2013.

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

#### ***Statement of compliance***

These financial statements have been prepared under International Financial Reporting Standards (“IFRS”), as issued by the International Accounting Standards Board (“IASB”) and the Canadian Accounting Standards Board for publicly-accountable enterprises.

#### ***Basis of preparation***

The financial statements are presented in Canadian dollars and have been prepared on the historical cost basis except for financial instruments measured at fair value through profit or loss. Historical cost is generally based on the fair value of the consideration given in exchange for assets.

These financial statements include the accounts of the Company and its wholly-owned subsidiaries Cargojet CP Inc. and, Cargojet Holdings Limited Partnership (“CHLP”), and CHLP’s wholly-owned subsidiaries, Cargojet Holdings Ltd. (“CJH”), Cargojet Airways Ltd. (“CJA”) and Cargojet Partnership (“CJP”).



## **CARGOJET INC.** **Notes to the Consolidated Financial Statements**

December 31, 2012 and 2011

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### **2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

#### ***Basis of preparation (continued)***

For the year ended December 31, 2011, the financial statements include the wholly-owned subsidiary Prince Edward Air Ltd. ("PEAL") up to the date of dissolution of PEAL on December 22, 2011. Upon dissolution of PEAL, the assets and liabilities were rolled over to CJA, its sole shareholding company, without any effect on the financial statements of the Company.

All intra-company balances and transactions are eliminated in full upon consolidation.

#### ***Cash***

Cash balance consists of cash on hand and demand deposits.

#### ***Goodwill***

Goodwill arising in a business combination is recognized as an asset at the date that control is acquired (the acquisition date). 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.

On disposal of a subsidiary, the attributable amount of goodwill is included in the determination of the gain or loss on disposal.

#### ***Assets held for sale***

Assets and disposal groups are classified as held for sale if their carrying amount will be recovered principally through a sale transaction rather than through continuing use. This condition is regarded as met only when the sale is highly probable and the asset (or disposal group) is available for immediate sale in its present condition. Management must be committed to the sale, which should be expected to qualify for recognition as a completed sale within one year from the date of classification.

When the Company is committed to a sale plan involving loss of control of a subsidiary, all of the assets and liabilities of that subsidiary are classified as held for sale when the criteria described above are met, regardless of whether the Company will retain a non-controlling interest in its former subsidiary after the sale.

Assets and disposal groups classified as held for sale are measured at the lower of their previous carrying amount and fair value less costs to sell.



## **CARGOJET INC.** **Notes to the Consolidated Financial Statements**

December 31, 2012 and 2011

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### **2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

#### ***Revenue recognition***

Revenue is recognized when delivery occurs and 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 billed in the event that the actual volumes do not exceed the guaranteed minimum volumes. Amounts billed include surcharges. Ad hoc revenue for non-contract customers is recorded at the time the cargo services have been provided. Revenue from ACMI cargo services is recorded when the cargo aircraft has been provided exclusively to a customer at a fixed daily rate operating on a specific route that may include cost of fuel and other commercial activities.

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

Revenue from fuelling services is billed on the basis of prevailing rates at the time of sale and recorded when the sale is completed.

Interest revenue is recognized when it is probable that the economic benefits will flow to the Company and the amount of revenue can be measured reliably. Interest revenue is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount on initial recognition.

#### ***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 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. Borrowing costs related to the acquisition, construction or production of qualifying assets is capitalized to the cost of the item until the asset is ready for use.

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.

Spare parts are treated as property, plant and equipment and depreciated 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 to the next overhaul.



## CARGOJET INC. Notes to the Consolidated Financial Statements

December 31, 2012 and 2011

### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

#### *Property, plant and equipment (continued)*

The cost of replacing a part of an item of property, plant and equipment is recognized in the carrying amount of the item if it is probable that the future economic benefits will flow to the Company and can be reliably measured. The carrying amount of the replaced part is derecognized. Gains and losses on the disposal of an item of property, plant and equipment are determined by comparing the proceeds on disposal to the carrying amount of the property, plant and equipment and are recognized in income. The cost of day-to-day servicing of the property, plant and equipment is expensed as incurred in income.

Depreciation is recognized so as to write off 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.

The estimated useful lives are as follows:

Asset	Estimated useful life
Aircraft hull	40 – 45 years from the date of manufacture
Engines	Up to 8 years from the date of purchase
Rotable spares	10 years
Spare parts	Actual usage
Ground equipment	10 years
Hangar facility	30 years
Vehicles	8 years
Computer hardware and software	5 years
Furniture and fixtures	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

#### **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.

#### *Finance leases*

Assets held under finance leases are initially recognised 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 against income, unless they are directly attributable to qualifying assets, in which case they are capitalized in accordance with the policy on borrowing costs. Contingent rentals are recognized as expenses in the periods in which they are incurred.



## CARGOJET INC. Notes to the Consolidated Financial Statements

December 31, 2012 and 2011

### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

#### *Leases (continued)*

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.

Amounts due from lessees under finance leases are recognized as receivables at the amount of the net investment in the lease. Finance lease income is recognized so as to reflect a constant periodic rate of return on the net investment outstanding in respect of the leases.

#### *Operating leases*

Payments made under operating leases are charged to income on a straight-line basis over the term of the related lease agreement. Contingent rentals arising under operating leases are recognized as an expense in the period in which they are incurred.

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

#### *Arrangements containing a lease*

In compliance with *IFRIC 4, Determining if an Arrangement Contains a Lease*, ("IFRIC 4") the Company identifies agreements that convey the right to use an asset or group of specific assets to the purchaser although they do not have the legal form of a lease contract, as the purchaser in the arrangement benefits from a substantial share of the asset's production and payment is not dependent on production or market price. Such arrangements are treated as leases, and analyzed with reference to *IAS 17, Leases* ("IAS 17") for classification as either finance or operating leases.

#### *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 to which the asset belongs. Where a reasonable and consistent basis of allocation can be identified, corporate assets are also allocated to individual cash-generating units, or otherwise they are allocated to the smallest group of cash-generating units 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.



## **CARGOJET INC.** **Notes to the Consolidated Financial Statements**

December 31, 2012 and 2011

### **2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

#### ***Impairment of tangible and intangible assets excluding goodwill (continued)***

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.

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. An impairment loss is recognized immediately in income.

Where an impairment loss subsequently reverses, the carrying amount of the asset or cash-generating unit 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 cash-generating unit in prior years. A reversal of an impairment loss is recognized immediately in income.

#### ***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 income in the period in which they arise.

#### ***Borrowing costs***

Borrowing costs directly 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, until such time as the assets are substantially ready for their intended use or sale. All other borrowing costs are recognized in income in the period in which they are incurred.

#### ***Income taxes***

##### ***Current taxes***

The tax currently payable is based on taxable income for the year. Taxable income differs from income as reported in the statement of income because of items of income or expense that are taxable or deductible in other years and items that are never taxable or deductible. The Company's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the end of the reporting period.





## CARGOJET INC. Notes to the Consolidated Financial Statements

December 31, 2012 and 2011

### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

#### *Income taxes (continued)*

##### *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. 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 set off 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 as an expense or income, except when they relate to items that are recognized outside income (whether in other comprehensive income or directly in equity), in which case the 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.

##### *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 cash flows.

When some or all of the economic benefits required to settle a provision are expected to be recovered from a third party, a receivable is recognized as an asset if it is virtually certain that reimbursement will be received and the amount of the receivable can be measured reliably.



## CARGOJET INC. Notes to the Consolidated Financial Statements

December 31, 2012 and 2011

### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

#### *Financial instruments*

Financial assets are classified into the following specified categories: fair value through profit or loss ("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, finance lease receivable, notes receivables, and deposits	Loans and receivables	Amortized cost
Overdraft, trade and other payables, dividends payable, convertible debentures and borrowings	Other financial liabilities	Amortized cost
Foreign exchange forward contracts	Fair value through profit or loss	Fair value

#### *Loans and receivables and other financial liabilities*

Cash, trade and other receivables, finance lease receivable, notes receivable, deposits, overdraft, 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 in the management of its foreign currency exposures. 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 re-measured 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. Notes to the Consolidated Financial Statements

December 31, 2012 and 2011

### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

#### *Financial instruments (continued)*

##### *Impairment of financial assets*

Financial assets, other than 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.

The Company periodically enters into foreign exchange forward contracts to manage its exposure to fluctuations in the Canadian/U.S. exchange rate on its purchase transactions denominated in U.S. dollars. These contracts require the exchange of currencies on maturity of the contracts.

#### **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. 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 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.



## **CARGOJET INC.** **Notes to the Consolidated Financial Statements**

December 31, 2012 and 2011

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### **2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

#### ***Accounting judgments and use of estimates***

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, provisions and financial instruments. These items are discussed below.

The 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 and goodwill***

Impairment tests on property, plant and equipment and goodwill are sensitive to the macro-economic and other assumptions used, and long-term financial forecasts. The Company therefore revises the underlying estimates and assumptions based on regularly updated information.

#### ***Deferred taxes***

Deferred tax assets are only recognized to the extent that it is probable that there will be sufficient taxable income 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 which is 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 the lease terms and has recorded a maintenance provision liability for these costs. Such costs have been estimated based on contractual commitments and Company specific history. The Company reviews the provisions at each reporting period to determine the change in estimated liability.

#### ***Financial instruments***

The issuance or repurchase of a compound instrument, such as convertible debentures, requires the Company to estimate the debt and equity components of the instruments issued or repurchased. Estimates are also required for determining the fair values of financial instruments that are not publicly traded for disclosure purposes.

#### ***Accounting changes***

##### ***Accounting standards effective for 2012***

*IFRS 7, Financial Instruments: Disclosures* and *IAS 12, Income Taxes* were amended to address disclosures with respect to the transfer of financial assets and the recovery of revalued investment properties, respectively. These amendments, which were effective January 1, 2012, had no impact on the Company's financial statements.



## CARGOJET INC. Notes to the Consolidated Financial Statements

December 31, 2012 and 2011

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

A number of new standards, amendments to standards and interpretations have been issued but are not yet effective for the financial year ending December 31, 2012, and accordingly, have not been applied in preparing these financial statements:

#### *Presentation of Financial Statements*

The IASB amended *IAS 1, Presentation of Financial Statements ("IAS 1")*, providing guidance on items contained in other comprehensive income ("OCI") and their classification within OCI. The amendments to IAS 1 must be applied retrospectively for annual periods beginning on or after July 1, 2012. The Company does not expect the adoption of this standard to have a significant impact on the Company's disclosures.

#### *Annual Improvements to IFRSs: 2009 – 2011 Cycle*

The Annual Improvements to IFRSs: 2009 – 2011 Cycle include a number of amendments to various IFRSs that are effective for periods beginning on or after January 1, 2013.

Amendments to *IAS 1, Presentation of Financial Statements* clarify the requirements for providing comparative information in financial statements. Amendments reduce the amount of information from previous reporting periods which is required to be repeated in the event of a change in accounting policy, reclassification or restatement by limiting the requirement to present an additional statement of financial position to circumstances when the statement is materially affected and by clarifying that related notes to an additional statement of financial position are not required.

*IAS 16, Property, Plant and Equipment* was amended to clarify the classification requirement for servicing equipment. If spare parts and servicing equipment meet the definition of property, plant and equipment, they should be accounted for as such rather than a current asset.

*IAS 34, Interim Financial Reporting* was amended to clarify the requirements on segment information for total assets and liabilities for each reportable segment.

The Company does not expect the adoption of these amendments to have a significant impact on the Company's disclosures.

#### *Employee Benefits*

The primary amendment to *IAS 19, Employee Benefits*, is the elimination of the corridor approach, with a requirement that all changes to the defined benefit obligation and planned assets to be recognized when they occur. The standard also does not permit the use of an assumed expected rate of return which differs from the rate used to discount plan liabilities and changes the presentation for defined benefit plans.

This standard is applicable for periods commencing January 1, 2013. Retrospective application is required with certain exceptions. The Company does not expect the adoption of this standard to have a significant impact on its results of operations, financial position and disclosures.

#### *Fair Value Measurement*

*IFRS 13, Fair Value Measurement ("IFRS 13")* is a new standard that defines fair value, sets out in a single IFRS a framework for measuring fair value and requires disclosures about fair value measurements. IFRS 13 does not determine when an asset, a liability or an entity's own equity instrument is measured at fair value. Rather, the measurement and disclosure requirements of IFRS 13 apply when another IFRS requires or permits the item to be measured at fair value (with limited exceptions). The standard is applicable commencing January 1, 2013.



## CARGOJET INC. Notes to the Consolidated Financial Statements

December 31, 2012 and 2011

### *Consolidation, Joint Arrangements, Associates and Disclosures*

A package of five standards addressing consolidation, joint arrangements, associates and disclosures are effective for periods beginning on or after January 1, 2013.

*IFRS 10, Consolidated Financial Statements ("IFRS 10")* builds on existing principles by identifying the concept of control as the determining factor in whether an entity should be included within the consolidated financial statements of the parent company. The standard provides additional guidance to assist in the determination of control where this is difficult to assess.

*IFRS 11, Joint Arrangements* establishes principles that are applicable to the accounting for all joint arrangements.

*IFRS 12, Disclosure of Interests in Other Entities* provides guidance on disclosure requirements for all forms of interests in other entities, including subsidiaries, joint arrangements, associates and unconsolidated structured entities.

The Company does not expect the implementation of these standards to have a significant impact on the Company's results of operations, financial position and disclosures.

### *Offsetting Financial Assets and Financial Liabilities and Related Disclosures*

Amendments to *IFRS 7, Financial Instruments: Disclosures* and *IAS 32, Financial Instruments: Presentation*, applicable for periods commencing on or after January 1, 2013 and January 1, 2014, respectively, require entities to disclose information about rights of offset and related arrangements and clarify existing application issues relating to the offset of financial assets and financial liabilities requirements. The Company does not expect the adoption of these standards to have a significant impact on the Company's disclosures.

### *Financial Instruments*

The IASB has issued *IFRS 9, Financial Instruments ("IFRS 9")*, which will ultimately replace *IAS 39, Financial Instruments: Recognition and Measurement ("IAS 39")*. IFRS 9 introduces new requirements for the classification and measurement of financial assets and liabilities and for de-recognition.

The replacement of IAS 39 is a multi-phase project with the objective of improving and simplifying the reporting for financial instruments and the issuance of IFRS 9 is part of the first phase. This standard becomes effective on January 1, 2015. The Company has yet to assess the impact of the new standard on its results of operations, financial position and disclosures.

### 3. INVENTORIES

	December 31, 2012	December 31, 2011
	\$	\$
Fuel inventory	720,756	700,626

For the years ended December 31, 2012 and 2011, costs of inventory of \$62,436,152 and \$56,896,328, respectively, were recognized in direct expenses.



## CARGOJET INC. Notes to the Consolidated Financial Statements

December 31, 2012 and 2011

### 4. NOTES RECEIVABLE

On July 14, 2010, the Company entered into an agreement with Skylink Express to sell its 55% interest in Cargojet Regional Partnership (the "Partnership"). The Partnership operated the Company's regional air cargo business segment that provided service to thirty-three smaller cities in Ontario, Quebec and the Maritime provinces. Skylink Express held the other 45% interest in the Partnership. Proceeds for the sale included a \$3.2 million non-interest bearing note receivable ("First Note Receivable") over five years, that was reduced by approximately \$0.7 million to account for the difference between the amounts due to Cargojet and Skylink Express from the Partnership, net of the total cash losses of the Partnership since its inception relative to the proportionate ownership of the Company and Skylink Express.

The sale agreement also included the sale of the Company's aircraft spare parts and other operating assets that were required by Skylink Express in the operation of the Partnership, which were sold to Skylink Express on December 20, 2010 in exchange for a separate non-interest bearing note ("Second Note Receivable") of \$1.8 million receivable over five years.

Both notes receivable due from Skylink Express are secured by a first charge on aircraft owned by Skylink Express. They are discounted at an annual rate of 6%.

The discounted balance of the notes receivable is comprised of the following as at December 31, 2012:

	December 31, 2012	December 31, 2011
	\$	\$
Notes receivable	2,540,290	3,239,670
Less: notes receivable - current portion	821,102	821,102
<b>Notes receivable - long-term portion</b>	<b>1,719,188</b>	<b>2,418,568</b>

Interest revenue of \$158,314 was recognized for the year ended December 31, 2012 (2011 – \$217,056).

### 5. FINANCE LEASE RECEIVABLE

In 2011, the Company entered into a lease agreement which transfers the title of one of its regional aircraft to the lessee at nominal value at the end of the lease. Accordingly, the lease has been classified as a finance lease.

The finance lease receivable as at December 31, 2012 and December 31, 2011 is as follows:

	December 31, 2012	December 31, 2011
Minimum lease payments	\$	\$
Not later than one year	300,000	300,000
Later than one year and not later than five years	396,431	700,000
Finance lease receivable	696,431	1,000,000
Less: unearned finance income	(41,937)	(83,290)
Present value of minimum lease payments	654,494	916,710
Current portion	293,017	293,017
Long-term portion	361,477	623,693

The estimated average effective interest rate is 5.17% and \$41,353 (2011 - \$16,710) of finance income was recognized in the year.

The finance lease receivable is secured by the leased aircraft.

# CARGOJET 2012 Annual Report



## CARGOJET INC. Notes to the Consolidated Financial Statements

December 31, 2012 and 2011

### 6. PROPERTY, PLANT AND EQUIPMENT

The changes in property, plant and equipment for the year ended December 31, 2012 are as follows:

	Balance as at January 1, 2012	Additions / Transfers	Disposals / Transfers	Impairment	Balance as at December 31, 2012
<b>Cost</b>					
	\$	\$	\$	\$	\$
Aircraft hull	11,691,346	1,222,908	-	-	12,914,254
Engines	12,270,371	1,617,199	(156,760)	( 567,395)	13,163,415
Spare parts	1,405,468	167,169	-	-	1,572,637
Ground equipment	7,436,634	922,729	-	-	8,359,363
Rotable spares	12,198,047	1,154,123	-	-	13,352,170
Computer hardware and software	3,739,004	570,219	-	-	4,309,223
Furniture and fixtures	1,051,833	173,344	-	-	1,225,177
Leasehold improvements	4,379,545	111,750	220,577	-	4,711,872
Vehicles	607,288	158,673	(2,621)	-	763,340
Hangar facility	14,950,992	-	-	-	14,950,992
Deferred heavy maintenance	12,758,453	7,164,597	(247,462)	-	19,675,588
	82,488,981	13,262,711	(186,266)	(567,395)	94,998,031

	Balance as at January 1, 2012	Depreciation	Disposals / Transfers	Balance as at December 31, 2012	Net Book Value, December 31, 2012
<b>Accumulated Depreciation</b>					
	\$	\$	\$	\$	\$
Aircraft hull	4,418,680	871,377	-	5,290,057	7,624,197
Engines	5,899,055	1,700,945	-	7,600,000	5,563,415
Spare parts	-	-	-	-	1,572,637
Ground equipment	3,910,170	628,626	-	4,538,796	3,820,567
Rotable spares	4,061,863	1,767,665	-	5,829,528	7,522,642
Computer hardware and software	2,718,586	416,544	-	3,135,130	1,174,093
Furniture and fixtures	596,435	95,042	-	691,477	533,700
Leasehold improvements	3,221,008	306,712	80,210	3,607,930	1,103,942
Vehicles	443,843	42,240	(2,308)	483,775	279,565
Hangar facility	3,655,193	429,315	-	4,084,508	10,866,484
Deferred heavy maintenance	9,564,547	3,569,228	(107,095)	13,026,680	6,648,908
	38,489,380	9,827,694	(29,193)	48,287,881	46,710,150



# CARGOJET 2012 Annual Report



## CARGOJET INC. Notes to the Consolidated Financial Statements

December 31, 2012 and 2011

### 6. PROPERTY, PLANT AND EQUIPMENT (continued)

The changes in property, plant and equipment for the year ended December 31, 2011 are as follows:

	Balance as at January 1, 2011	Additions / Transfers	Disposals / Transfers	Impairment	Balance as at December 31, 2011
<b>Cost</b>					
	\$	\$	\$	\$	\$
Aircraft hull	15,442,051	825,010	(3,279,042)	(1,296,673)	11,691,346
Engines	11,307,866	2,940,068	(1,509,951)	(467,612)	12,270,371
Spare parts	1,138,350	267,118	-	-	1,405,468
Ground equipment	7,254,333	484,368	(302,067)	-	7,436,634
Rotable spares	9,563,624	2,634,423	-	-	12,198,047
Computer hardware and software	3,503,488	235,516	-	-	3,739,004
Furniture and fixtures	938,970	112,863	-	-	1,051,833
Leasehold improvements	4,325,319	54,226	-	-	4,379,545
Vehicles	583,803	23,485	-	-	607,288
Hangar facility	14,880,402	70,590	-	-	14,950,992
Deferred heavy maintenance	10,234,558	4,402,117	(1,878,222)	-	12,758,453
	79,172,764	12,049,784	(6,969,282)	(1,764,285)	82,488,981

	Balance as at January 1, 2011	Depreciation	Disposals / Transfers	Balance as at December 31, 2011	Net Book Value, December 31, 2011
<b>Accumulated Depreciation</b>					
	\$	\$	\$	\$	\$
Aircraft hull	4,852,834	1,091,455	(1,525,609)	4,418,680	7,272,666
Engines	5,630,714	899,732	(631,391)	5,899,055	6,371,316
Spare parts	-	-	-	-	1,405,468
Ground equipment	3,418,846	612,173	(120,849)	3,910,170	3,526,464
Rotable spares	2,554,051	1,507,812	-	4,061,863	8,136,184
Computer hardware and software	2,092,168	626,418	-	2,718,586	1,020,418
Furniture and fixtures	484,188	112,247	-	596,435	455,398
Leasehold improvements	2,909,465	311,543	-	3,221,008	1,158,537
Vehicles	394,877	48,966	-	443,843	163,445
Hangar facility	3,226,907	428,286	-	3,655,193	11,295,799
Deferred heavy maintenance	7,604,229	3,429,110	(1,468,792)	9,564,547	3,193,906
	33,168,279	9,067,742	(3,746,641)	38,489,380	43,999,601

In July 2012, the Company purchased a Boeing 727 aircraft for total consideration of \$1,224,925. The costs were segregated into three components consisting of engines totaling \$540,630, airframe totaling \$619,295 and deferred heavy maintenance totaling \$65,000.

In 2011, the Company purchased three Boeing 727 aircraft that were previously leased for total consideration of \$3,062,400. The costs were segregated into three components consisting of engines totaling \$1,487,953, airframe totaling \$757,807, and deferred heavy maintenance totaling \$816,640.



## **CARGOJET INC.** **Notes to the Consolidated Financial Statements**

December 31, 2012 and 2011

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### **6. PROPERTY, PLANT AND EQUIPMENT (continued)**

In August 2012, the Company reviewed the carrying value of its used engine cores and estimated that the recoverable amount was less than the book value. The Company reduced the net book value of the used engine cores to fair value by \$567,395 and reported a loss on impairment of property, plant and equipment.

In 2011, the Company sold most of its regional fleet, including the aircraft that were returned upon the termination of the related leases. The Company reviewed the carrying value of the remaining regional aircraft and estimated that the recoverable amount was less than the book value of the aircraft. The recoverable amount was determined on a fair value less costs to sell basis, fair value being the market value for similar aircraft. The Company reduced the net book value of the aircraft hull and engines to fair value by \$783,698 and reported a loss on impairment of property, plant and equipment. The related deferred heavy maintenance expenditure of \$409,430 was written off and recorded in loss on disposal of property, plant and equipment.

Also in 2011, the Company permanently removed one of its cargo aircraft from service. The Company used the aircraft as a source for spare parts to maintain its existing fleet of aircraft. Accordingly, the Company reviewed the carrying value of this aircraft at December 31, 2011 and estimated that the recoverable value of the aircraft was less than the book value. The recoverable amount was determined on a fair value less costs to sell basis, fair value being the market value for similar spare parts. The Company reduced the net book value of this aircraft to fair value by \$980,587 at December 31, 2011 and reported a loss on impairment of property, plant and equipment.

Depreciation expense on property, plant and equipment for the years ended December 31, 2012 and 2011 totaled \$9,827,694, and \$9,067,742, respectively.

#### **Assets held for sale**

In 2011, an aircraft was approved for disposal and was presented as held for sale at an estimated fair value of \$45,000 with the related deferred tax asset of \$3,567.

### **7. 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 based on historical results and using a steady 2.0% per annum growth rate (2011 - 1.5%), which has been estimated based on long-term growth rates in cash flow of the Company, and a pre-tax discount rate of approximately 16.1% per annum (2011 - 16.5%). 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.



## CARGOJET INC. Notes to the Consolidated Financial Statements

December 31, 2012 and 2011

### 8. INTANGIBLE ASSETS

#### Financial instruments (continued)

Intangible assets at December 31, 2012 and 2011 consist of licenses with indefinite lives carried at \$1,000,000. 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. As a result, the Company believes that the licenses have indefinite lives as the Company complies, and will continue to comply, with the licensing conditions specified in the existing laws, agreements, treaties and regulations.

### 9. TRADE AND OTHER PAYABLES

	December 31, 2012	December 31, 2011
	\$	\$
Trade payables and accrued charges	11,311,796	10,279,042
Payroll and benefits	443,957	301,040
Trade and other payables	11,755,753	10,580,082

### 10. BORROWINGS

Borrowings consist of the following:

	December 31, 2012	December 31, 2011
	\$	\$
Revolving credit facility	2,729,592	9,123,300
Fixed loans - Cargojet Airways Ltd.	1,139,658	2,196,943
	3,869,250	11,320,243
Less current portion	885,780	757,677
Long-term portion	2,983,470	10,562,566

The Company has a revolving credit facility with a Canadian chartered bank. The credit facility is to a maximum of \$25.0 million and bears interest at bank prime plus 1.75% and is repayable on maturity, December 31, 2015. The credit facility is subject to customary terms and conditions for borrowers of this nature, including, for example, limits on incurring additional indebtedness and granting liens or selling assets without the consent of the lenders. The credit facility is subject to the maintenance of certain financial covenants. The Company was in compliance with all covenants as at December 31, 2012.

The credit facility is secured by the following:

- general security agreement over all assets of the Company;
- guarantee and postponement of claim to a maximum of \$35.0 million in favour of Cargojet Partnership (a wholly-owned subsidiary of the Company) and certain other entities of the Company; and
- assignment of insurance proceeds, payable to the bank.

The Company also maintains fixed loans with another Canadian chartered bank through its subsidiary Cargojet Airways Ltd. ("CJA"). The fixed loans bear interest at rates ranging from 8.1% to 8.2%. They are secured by the regional aircraft owned by CJA and the Company's notes receivable. The loans are repayable in monthly installments plus interest and will mature by August 2014. The Company also has provided a standby letter of credit of \$780,000 to the bank which is held against the fixed loans.



## CARGOJET INC. Notes to the Consolidated Financial Statements

December 31, 2012 and 2011

### 10. BORROWINGS (continued)

The following is the future minimum repayment schedule for the fixed loans related to CJA:

	\$
2013	885,780
2014	253,878
	1,139,658
Less current portion	885,780
Long-term portion	253,878

Interest expense on the borrowings for the years ended December 31, 2012 and 2011 totaled \$800,551 and \$864,742, respectively.

### 11. PROVISIONS

The Company's aircraft operating lease agreements require leased aircraft to be returned to the lessor in a specified operating condition. As a result of changes in the Company's c-check intervals for certain aircraft from 18 months to 24 months, 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. The change in the carrying amount of the provisions is as follows:

	\$
Balance, January 1, 2012	-
Recognition of provision for lease return conditions	1,476,973
Accretion	49,141
Effects of exchange rate changes on the provisions balance	17,670
Balance, December 31, 2012	1,543,784

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 Company specific history. Accretion expense of \$49,141 has been recorded in the period as part of finance costs in the consolidated statement of income. The provision has been added to the cost of deferred heavy maintenance included in property, plant and equipment and will be amortized over the remaining terms of the leases.

### 12. CONVERTIBLE DEBENTURES

#### Convertible Debentures – 6.5% due April 30, 2017

In March 2012, \$28,750,000 of unsecured subordinated convertible debentures were issued with a term of five years. These debentures bear a fixed interest rate of 6.5% per annum, payable semi-annually in arrears on April 30 and October 31 of each year, commencing April 30, 2012.

On or after April 30, 2015, but prior to April 30, 2016, the debentures are redeemable, in whole at any time or in part from time to time, at the option of the Company at a price equal to at least \$1,000 per debenture plus accrued and unpaid interest, provided that the current market price of the common shares of the Company on the date on which the notice of redemption is given is at least 125% of the conversion price of \$11.75 per common share. After April 30, 2016, but prior to the maturity date of April 30, 2017, the debentures are redeemable at a price equal to \$1,000 per debenture plus accrued and unpaid interest. On redemption or at maturity on April 30, 2017, the Company has the option to repay the debentures in either cash or freely tradable voting shares of the Company. The number of common shares to be issued will be determined by dividing the aggregate amount of the principal amount of the debentures by 95% of the current market price of the common shares.



## CARGOJET INC. Notes to the Consolidated Financial Statements

December 31, 2012 and 2011

### 12. CONVERTIBLE DEBENTURES (continued)

#### Convertible Debentures – 6.5% due April 30, 2017 (continued)

Based on certain conditions, the debentures are convertible, at the holders' discretion, at \$11.75 per voting share at any time prior to the close of business on the earliest of the business day immediately preceding the maturity date; if called for redemption, on the business day immediately preceding the date specified by the Company for redemption of the debentures; or if called for repurchase pursuant to a change of control, on the business day immediately preceding the payment date. The Company also has the right at any time to purchase debentures in the market, by tender or by private contract subject to regulatory requirements, provided, however, that if an event of default has occurred and is continuing, the Company or any of its affiliates will not have the right to purchase the debentures by private contract. The conversion rate of \$11.75 per voting share is subject to adjustment in certain circumstances, including the payment of a cash dividend or distribution to holders of voting shares in excess of \$0.142 per quarter (\$0.568 per annum).

In the event of a change in control, as defined in the indenture, the Company will be required to make an offer to the holders of debentures to repurchase the debentures at a price equal to 100% of the principal amount plus accrued and unpaid interest. In addition, if a change in control occurs in which 10% or more of the consideration consists of cash, certain equity securities or other property not traded or intended to be traded immediately following such transaction on a recognized exchange, holders of the debentures will be entitled to convert their debentures and, subject to certain limitations, receive an additional amount of voting shares to those that they would otherwise be entitled at the normal conversion rate. The amount of such additional voting shares will depend on the effective date and the price paid per voting share in the transaction constituting the change in control.

The principal amount of the debentures has been allocated between its debt component and the conversion option and has been classified separately on the balance sheet. The fair value of the debt component was determined using an estimated market rate for a similar liability without an equity component and the residual was allocated to the conversion option.

The debt component is measured at amortized cost. The balance of the debt component at December 31, 2012 consisted of the following:

	December 31, 2012
Principal balance	\$ 28,750,000
Less:	
Issuance costs	(1,312,192)
Conversion option at inception	(2,642,384)
Accretion	468,107
<b>Balance</b>	<b>25,263,531</b>



## CARGOJET INC. Notes to the Consolidated Financial Statements

December 31, 2012 and 2011

### 12. CONVERTIBLE DEBENTURES (continued)

#### Convertible Debentures – 6.5% due April 30, 2017 (continued)

The conversion option, net of related issuance costs of \$132,808, has been recorded in shareholders' equity. Factoring in issuance costs, the effective interest rate on the debentures is 10.01%. Interest expense on the debentures for the year ended December 31, 2012 totaled \$1,927,272.

#### Convertible Debentures – 7.5%

In May 2012, the Company redeemed the outstanding \$24,655,000 principal amount of the convertible debentures issued in 2008 (\$24,100,397 net of the related unamortized issuance costs and the portion allocated to the conversion option) at par or \$1,000 per convertible debenture. At redemption, the Company allocated the full \$24,655,000 purchase price to the liability component redeemed and the equity component of \$1,271,503 was reclassified from conversion option to reserve for surplus on debenture repurchases in shareholders' equity. The redemption of the convertible debentures resulted in a loss of \$554,603.

Interest expense on the debentures for the years ended December 31, 2012 and 2011 totaled \$802,030 and \$2,403,728, respectively.

### 13. INCOME TAXES

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

	Year ended December 31,	
	2012	2011
	\$	\$
Earnings before income taxes and discontinued operations	5,066,060	4,953,631
Income tax provision at the combined basic rate of 26.5% (2011 - 26.5%)	1,342,506	1,312,712
Effect of changes in tax rates	262,440	-
Permanent and other differences	(91,065)	(323,081)
Income tax expense	1,513,881	989,631

The tax effect of significant temporary differences and loss carry forwards is as follows:

	December 31, December 31,	
	2012	2011
	\$	\$
Property, plant and equipment	3,019,272	2,945,589
Intangible assets	(607,359)	(586,604)
Operating loss carryforward	-	(1,478,268)
Notes receivable	(55,349)	(91,795)
Financing costs	(344,828)	(6,444)
Convertible debentures	901,598	196,390
Provision for lease retirement costs	79,796	-
Finance lease receivable	173,441	229,178
Long term incentive plan	(90,511)	-
Deferred heavy maintenance	1,821,485	2,041,675
Net deferred income tax liability	4,897,545	3,249,721



## CARGOJET INC. Notes to the Consolidated Financial Statements

December 31, 2012 and 2011

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### 13. INCOME TAXES (continued)

A deferred tax liability of \$665,038 was recorded in shareholders' equity relating to the value of the conversion option recorded on the issuance of the convertible debentures in March 2012.

### 14. SHAREHOLDERS' CAPITAL

#### a) Authorized

The Company is authorized to issue an unlimited number of common voting shares, variable voting shares and preferred shares. The common voting shares are held only by shareholders who are Canadian residents. The variable voting shares are held only by shareholders who are non-Canadian residents. Under the articles of incorporation and bylaws of the Company, any common voting share that is sold to a non-Canadian resident is automatically converted to a variable voting share. Similarly, a variable voting share that is sold to a Canadian resident 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.

#### b) Issued and outstanding

On January 1, 2011, the Company was converted from an income trust to a corporation. All unitholders of the Fund had their trust units automatically converted into shares in the new corporate entity on a one-for-one basis.

The outstanding 6,437,109 trust units and 1,556,307 exchangeable LP units as at January 1, 2011 were converted into 7,755,271 common voting shares and 238,145 variable voting shares. No preferred shares are issued and outstanding.



## CARGOJET INC. Notes to the Consolidated Financial Statements December 31, 2012 and 2011

### 14. SHAREHOLDERS' CAPITAL (continued)

#### b) Issued and outstanding (continued)

The following table shows shareholders' capital as at December 31, 2012 and 2011:

	Number	Amount
		\$
Variable voting shares	238,145	2,019,470
Common voting shares	7,755,271	65,764,697
Outstanding, January 1, 2011	7,993,416	67,784,167
Treasury stock purchase	(65,984)	(564,825)
Distributed share-based compensation	14,238	121,825
Outstanding, December 31, 2011	7,941,670	67,341,167
Consisting of:		
Variable voting shares	225,445	1,911,655
Common voting shares	7,716,225	65,429,512
Changes during the period		
Treasury stock purchase	(39,275)	(296,437)
Distributed in connection with share-based compensation	33,455	284,710
Outstanding, December 31, 2012	7,935,850	67,329,440
Consisting of:		
Variable voting shares	706,745	4,298,548
Common voting shares	7,229,105	63,030,892

#### Dividends

Dividends to shareholders declared for the years ended December 31, 2012 and 2011 amounted to \$4,597,013 (\$0.575 per share) and \$4,244,504 (\$0.531 per share), respectively.

### 15. EARNINGS PER SHARE

The following table shows the computation of basic earnings per share for the years ended December 31, 2012 and 2011:

Basic earnings per share	2012	2011
Net income from continuing operations	\$ 3,552,179	\$ 3,964,000
Loss from discontinued operations	-	(168,256)
Net income	\$ 3,552,179	\$ 3,795,744
Weighted average number of shares	7,993,416	7,993,416
Total basic earnings per share	\$ 0.44	\$ 0.48
Basic earnings per share - continuing operations	\$ 0.44	\$ 0.50
Basic earnings per share - discontinued operations	-	\$ (0.02)

The shares held under the long-term incentive plan have been included in the calculation of basic earnings per share for the years ended December 31, 2012 and 2011 as they participate in dividend distributions. The effect of the convertible debentures has been excluded from the calculation of diluted earnings per share for the years ended December 31, 2012 and 2011 as the impact would be anti-dilutive.





## **CARGOJET INC.** **Notes to the Consolidated Financial Statements**

December 31, 2012 and 2011

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### **16. LONG-TERM INCENTIVE PLAN**

The Company's long-term incentive plan (the "Plan" or "LTIP") provides certain of its executive officers and senior management of the Company with compensation opportunities tied to the performance of the Company. Company incentive bonuses, in the form of shares, are provided to eligible employees on an annual basis where the earnings of the Company exceed a pre-determined base (the "Base Target"). The Base Target is set annually by the Compensation Committee of the Company's Board of Directors in accordance with the terms of the Plan.

If the Company's earnings exceed the Base Target, a percentage of the excess is contributed by the Company into a long-term incentive pool. Shares are then purchased on the open market by the Company and held by the Company until they vest. Vesting of the shares will occur on the basis of one-third of the total grant at the time of granting, and one-third on each of the first and second anniversary dates.

For the years ended December 31, 2012 and 2011 share-based compensation expense totaled \$402,932 and \$497,144, respectively, including withholding taxes of \$52,313 and \$99,675, respectively, paid on behalf of the eligible employees.

#### **2012 Awards**

In March 2012, pursuant to the Company's LTIP, an amount of \$348,750 was approved to the executive officers and senior management. Accordingly, the Company purchased 39,275 shares from the open market at an average price of \$7.55. As at December 31, 2012, 7,580 of these shares had vested and \$63,210 was transferred from share-based compensation reserve to shareholders' capital. The balance of LTIP award not vested as at December 31, 2012 was \$233,227.

#### **2011 Awards**

In March 2011, in accordance with the Plan, the Company purchased 65,984 shares from the open market at an average price of \$8.55, plus commissions. As at December 31, 2011, 14,238 of these shares had vested, \$121,825 being transferred from share-based compensation reserve to shareholders' capital.

As at December 31, 2012, an additional 25,875 of the shares for the 2011 awards had vested and \$221,500 was transferred from share-based compensation reserve to shareholders' capital. The balance of LTIP award not vested as at December 31, 2012 was \$221,500.



## CARGOJET INC. Notes to the Consolidated Financial Statements

December 31, 2012 and 2011

### 16. LONG-TERM INCENTIVE PLAN (continued)

The following table details the impact of the above transactions on shareholders' capital as at December 31, 2012 and on the statements of income for the years ended December 31, 2012 and 2011:

Shares purchased under the Plan	Number	\$
Balance, January 1, 2011	-	-
Shares acquired by Company for long-term incentive plan	65,984	564,825
Shares distributed by Company to long-term incentive plan participants	(14,238)	(121,825)
Balance, December 31, 2011	51,746	443,000
Shares acquired by Company for long-term incentive plan	39,275	296,437
Shares distributed by Company to long-term incentive plan participants	(33,455)	(284,710)
Balance, December 31, 2012	57,566	454,727

	December 31, 2012	December 31, 2011
<b>Share-based compensation expense</b>	<b>\$</b>	<b>\$</b>
Shares transferred to long-term incentive plan participants	107,507	121,825
Withholding tax paid for long-term incentive plan participants	52,313	99,675
Share-based compensation, not yet vested	243,112	275,643
Share-based remuneration	402,932	497,143

### 17. 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	\$ 10,513,747
Later than one year and not later than five years	21,851,945
Later than five years	746,749
<b>Total</b>	<b>33,112,441</b>



## CARGOJET INC. Notes to the Consolidated Financial Statements

December 31, 2012 and 2011

### 17. COMMITMENTS AND CONTINGENCIES (continued)

#### Contingencies

The Company has provided irrevocable standby letters of credit totaling \$2,968,000 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 as follows:

	\$
March 3, 2013	780,000
March 20, 2013	20,000
June 15, 2013	350,000
July 6, 2013	122,000
July 28, 2013	352,000
December 31, 2013	200,000
December 31, 2013	448,000
December 31, 2013	223,000
December 31, 2013	223,000
January 13, 2014	250,000
<b>Total</b>	<b>2,968,000</b>

### 18. RELATED PARTY TRANSACTIONS

#### Contingencies

In 2012 and 2011, the Company entered into transactions with a related party, First Take Entertainment Ltd., a company controlled by one of the Company's executive officers.

These transactions were in the normal course of business and measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties. The amount of \$150,000 (2011 - \$150,000) included in sales and marketing costs was paid on account of advertising and promotional expenses.

#### Compensation of key management personnel

In 2012, the employee benefit expense was \$28,278,986 (2011 - \$27,706,793) of which \$15,428,713 (2011 - \$16,625,766) was recorded in direct expenses and \$12,850,273 (2011 - \$11,081,027) 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, 2012 and 2011 as follows:

	Year Ended	
	December 31, 2012	December 31, 2011
	\$	\$
Short-term benefits	2,983,241	2,351,873
Post-employment benefits	19,500	10,384
Share-based payments	402,932	497,143
<b>Total remuneration</b>	<b>3,405,673</b>	<b>2,859,400</b>

### 19. ECONOMIC DEPENDENCE

In 2012, the Company had sales to three customers that represented 54.5% of the total revenues (2011 - 48.0%). These sales are provided under service agreements that expire over various periods to September 2018.



## **CARGOJET INC.** **Notes to the Consolidated Financial Statements**

December 31, 2012 and 2011

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### **20. 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 (with 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 (Note 10). As at December 31, 2012 and 2011, the Company was in compliance with all financial covenants.

### **21. FINANCIAL INSTRUMENTS**

#### **Risk management policies**

Through its financial assets and liabilities, the Company is exposed to various risks. The following analysis provides an overview of these risks as well as a measurement of these risks as at December 31, 2012.

#### **Fair values**

The fair value of the convertible debentures, based on quoted market prices as at December 31, 2012, was approximately \$29,612,500 (December 31, 2011 – \$24,901,550). The fair value of the long-term debt based on an estimate of market interest rates as at December 31, 2012 and 2011, was approximately equal to its carrying value. The fair values of the notes receivables and finance lease receivable as at December 31, 2012 and 2011 were approximately equal to their carrying values. The fair values of all other financial assets and liabilities approximate their carrying values given the short-term nature of these items.

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.

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.



## CARGOJET INC. Notes to the Consolidated Financial Statements

December 31, 2012 and 2011

### 21. FINANCIAL INSTRUMENTS (continued)

#### Fair values (continued)

The Company does not have any Level 3 fair value measurements and thus no continuity schedule has been presented. In addition, there have been no significant transfers between levels.

There are no assets and liabilities recorded at fair value as at December 31, 2012. Total assets and liabilities recorded at fair value as at December 31, 2011 are as follows:

	Level 1	Level 2	Level 3	Total
	\$	\$	\$	\$
Assets				
Assets held for sale	-	45,000	-	45,000

#### Credit risk

The Company's principal financial assets that expose it to credit risk are accounts receivable, notes receivable, finance lease receivable and foreign exchange derivative contracts.

The Company is subject to risk of non-payment of accounts receivable, finance lease 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 52% (December 31, 2011 – 69%) 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 sixty 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.

The notes receivable due from Skylink Express are secured by a first charge on Skylink Express aircraft.

The finance lease receivable is secured by the leased aircraft.

#### 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 \$25.0 million.



## CARGOJET INC. Notes to the Consolidated Financial Statements

December 31, 2012 and 2011

### 21. FINANCIAL INSTRUMENTS (continued)

#### Liquidity risk (continued)

The Company has financial liabilities with varying contractual maturity dates. Total financial liabilities at December 31, 2012 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	885,780	253,878	28,750,000	-	29,889,658
Interest on borrowings (at current rates)	1,933,021	1,878,493	4,357,003	-	8,168,517
Trade and other payables	11,755,753	-	-	-	11,755,753
Dividends payable	1,191,819	-	-	-	1,191,819
<b>Total</b>	<b>15,766,373</b>	<b>2,132,371</b>	<b>33,107,003</b>	<b>-</b>	<b>51,005,747</b>

Total financial liabilities at December 31, 2011 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	905,133	34,687,470	609,291	-	36,201,894
Interest on borrowings (at current rates)	2,023,849	697,677	26,099	-	2,747,625
Trade and other payables	10,580,082	-	-	-	10,580,082
Dividends payable	1,079,112	-	-	-	1,079,112
<b>Total</b>	<b>14,588,176</b>	<b>35,385,147</b>	<b>635,390</b>	<b>-</b>	<b>50,608,713</b>

#### Foreign exchange risk

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 sometimes manages its exposure to changes in the Canadian/U.S. exchange rate on anticipated purchases by buying forward U.S. dollars at fixed rates in future periods.

As at December 31, 2012, the Company entered into U.S. dollar forward sale contracts maturing on January 31, 2013 for USD \$1,000,000. As at December 31, 2012, these contracts had a positive fair value of \$1,831 which was recorded as an asset in trade and other receivables.

On January 1, 2010, the Company discontinued hedge accounting and recognized the deferred loss on the outstanding foreign exchange contracts as at January 1, 2010 over the period to October 2011 in the same periods in which the hedged anticipated transactions would affect net income. During the year ended December 31, 2012, \$nil and for the year ended December 31, 2011, a loss of \$144,274 (net of taxes of \$71,210) was recognized and transferred from other comprehensive income to net income.

In August and October of 2010, the Company entered into a series of U.S. dollar forward purchase contracts maturing on a monthly basis from September 2010 to December 2011 for an aggregate total of USD \$23.5 million. In 2011, the Company sold all of its outstanding U.S. dollars forward purchase contracts. A pre-tax gain of \$212,450 was realized from the sale of these contracts.



## **CARGOJET INC.** **Notes to the Consolidated Financial Statements**

December 31, 2012 and 2011

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### **21. FINANCIAL INSTRUMENTS (continued)**

#### **Foreign exchange risk (continued)**

Total other foreign exchange gains during the year ended December 31, 2012 were \$121,262 (2011 – loss of \$594,197).

#### **Commodity risk**

The Company is exposed to commodity risk for fluctuations in fuel costs to the extent that it cannot pass price increase on to its customers. The Company does not use derivative instruments to mitigate this risk.

#### **Market risk**

In the normal course of business, the financial position of the Company is routinely subject to a variety of risks. In addition to the market risk associated with interest rate and currency movements on outstanding debt and non-Canadian dollar denominated assets and liabilities, other examples of risk include collectability of accounts receivable.

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.

To meet disclosure requirements, 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.

At December 31, 2012 and 2011, movements in interest rates would not have any significant impact on the fair value of the Company's financial assets and liabilities.

At December 31, 2012, 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 \$0.1 million (2011 - \$0.1 million). 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 (2011 - \$0.1 million).

At December 31, 2012, 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 \$0.1 million (2011 - \$nil). 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 (2011 - \$nil).



## **CARGOJET INC.** **Notes to the Consolidated Financial Statements**

December 31, 2012 and 2011

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### **22. 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 aircraft. 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) Indemnity has been provided to all directors and officers of the Company for various items including, but not limited to, all costs to settle suits or actions due to association with the Company, subject to certain restrictions. The Company has purchased directors' and officers' liability insurance to mitigate the cost of any potential future suits or actions. The term of the indemnification is not explicitly defined, but is limited to the period over which the indemnified party served as a director or officer of the Company. The maximum amount of any potential future payment cannot be reasonably estimated.

(c) 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.

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.



# Directors and Officers of Cargojet



Dr. Ajay K. Virmani, MBA  
President,  
Chief Executive Officer  
Chairman of the Board



Jamie Porteous  
Executive Vice-President



# Directors and Officers of Cargojet



John P. Webster  
Lead Director



Paul V. Godfrey  
Director



Terence M. Francis  
Director



# Officers of Cargojet



John Kim, CA  
Chief Financial Officer  
Corporate Secretary



George Sugar  
Senior Vice President,  
Flight Operations



# CARGOJET 2012 Annual Report



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