



**Consolidated Financial Statements  
December 31, 2013 and 2012**

February 19, 2014

## Management's Report

The accompanying consolidated financial statements of **Chorus Aviation Inc. ("Chorus")** (the "financial statements") 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 generally accepted accounting principles in Canada ("GAAP") as set out in the Chartered Professional Accountants of Canada Handbook - Accounting - Part 1 ("CPA Canada Handbook") which incorporates International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") and include certain amounts and assumptions that are based on management's best estimates and have been derived with careful judgement.

Management is responsible for establishing and maintaining adequate internal control over financial reporting which includes those policies and procedures that provide reasonable assurance over the safeguarding of assets and over the completeness, fairness and accuracy of the consolidated financial statements and other financial information.

The Audit, Finance and Risk Committee, which is comprised entirely of independent directors, reviews Chorus' financial reporting and recommends approval to the Board of Directors; oversees management's responsibilities as to the adequacy of the supporting systems of internal controls; provides oversight of the independence, qualifications and appointment of the external auditor; and, pre-approves audit and audit-related fees and expenses. The Board of Directors approves Chorus' consolidated financial statements, management's discussion and analysis and annual report disclosures prior to their release. The Audit, Finance and Risk Committee meets with management, the internal auditors and external auditors at least four times each year to review and discuss financial reporting issues and disclosures, auditing and other matters.

The external auditors, PricewaterhouseCoopers LLP, conduct an independent audit of the consolidated financial statements in accordance with Canadian generally accepted auditing standards and express their opinion thereon. Those standards require that the audit is planned and performed to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. The external auditors have unlimited access to the Audit, Finance and Risk Committee and meet with the Committee on a regular basis.

(signed) "Joseph D. Randell"  
President and Chief Executive Officer

(signed) "Richard Flynn"  
Chief Financial Officer



February 19, 2014

## **Independent Auditor's Report**

### **To the Shareholders of Chorus Aviation Inc.**

We have audited the accompanying consolidated financial statements of Chorus Aviation Inc. and its subsidiaries, which comprise the consolidated statements of financial position as at December 31, 2013 and December 31, 2012 and the consolidated statements of changes in equity, income, comprehensive income and cash flows the years then ended, and the related notes, which comprise a summary of significant accounting policies and other explanatory information.

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

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

### **Auditor's responsibility**

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

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

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

### **Opinion**

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Chorus Aviation Inc. and its subsidiaries as at December 31, 2013 and December 31, 2012 and their financial performance and their cash flows for the years then ended in accordance with International Financial Reporting Standards.

(signed) "PricewaterhouseCoopers LLP"

### **Chartered Accountants**

*PricewaterhouseCoopers LLP  
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"PwC" refers to PricewaterhouseCoopers LLP, an Ontario limited liability partnership.

## Consolidated Statements of Financial Position

(expressed in thousands of Canadian dollars)

	<b>As at December 31,</b>	
	<b>2013</b>	<b>2012</b>
	<b>\$</b>	<b>\$</b>
<b>Assets</b>		
<b>Current assets</b>		
Cash and cash equivalents (note 5)	159,901	118,306
Restricted cash (note 5)	3,320	6,017
Accounts receivable – trade and other (note 23)	76,891	78,949
Inventories (note 23)	45,121	38,149
Prepaid expenses and deposits (note 23)	22,896	25,942
<b>Total current assets</b>	<b>308,129</b>	<b>267,363</b>
<b>Property and equipment (note 6)</b>	<b>594,650</b>	<b>499,872</b>
<b>Goodwill (note 7)</b>	<b>6,693</b>	<b>6,693</b>
<b>Deferred income tax (note 11)</b>	<b>—</b>	<b>2,099</b>
<b>Other assets (note 23)</b>	<b>67,453</b>	<b>36,280</b>
	<b>976,925</b>	<b>812,307</b>
<b>Liabilities</b>		
<b>Current liabilities</b>		
Accounts payable and accrued liabilities (note 23)	207,334	205,588
Current portion of obligations under finance leases (note 8)	3,356	2,875
Current portion of long-term debt (note 9)	31,354	20,281
Dividends payable (note 13)	13,786	18,602
Convertible debentures (note 10)	78,535	—
Income tax payable	1,737	513
<b>Total current liabilities</b>	<b>336,102</b>	<b>247,859</b>
<b>Obligations under finance leases (note 8)</b>	<b>3,073</b>	<b>6,014</b>
<b>Long-term debt (note 9)</b>	<b>371,445</b>	<b>257,165</b>
<b>Convertible debentures (note 10)</b>	<b>—</b>	<b>76,769</b>
<b>Deferred income tax (note 11)</b>	<b>35,790</b>	<b>—</b>
<b>Other long-term liabilities (note 23)</b>	<b>44,534</b>	<b>92,385</b>
	<b>790,944</b>	<b>680,192</b>
<b>Equity</b>	<b>185,981</b>	<b>132,115</b>
	<b>976,925</b>	<b>812,307</b>

**Economic dependence (note 19)**

**Commitments (note 15)**

**Contingencies (note 17)**

**Subsequent event (note 24)**

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

**Approved by the Board of Directors**

By: (signed) "Karen Cramm"  
Director

By: (signed) "Richard H. McCoy"  
Director

## Consolidated Statements of Changes in Equity

(expressed in thousands of Canadian dollars)

	Capital \$	Deficit \$	Contributed surplus \$	Equity component of convertible debentures \$	Total \$
<b>Balance - December 31, 2011</b>	1,572	(918,832)	1,050,907	9,497	143,144
Net income for the year (note 3)	—	100,223	—	—	100,223
Other comprehensive loss for the year (net of tax) (note 3)	—	(39,298)	—	—	(39,298)
Comprehensive income for the year	—	60,925	—	—	60,925
Dividends	—	(74,408)	—	—	(74,408)
Shares released from stock-based compensation plans	2,056	—	(2,056)	—	—
Expense related to the stock-based compensation plans	—	—	2,454	—	2,454
<b>Balance - December 31, 2012</b>	3,628	(932,315)	1,051,305	9,497	132,115
Net income for the year	—	61,866	—	—	61,866
Other comprehensive income for the year (net of tax)	—	45,593	—	—	45,593
Comprehensive income for the year	—	107,459	—	—	107,459
Dividends	—	(50,880)	—	—	(50,880)
Repurchase of shares under normal course issuer bid (note 14)	(78)	—	(3,928)	—	(4,006)
Share issuance for stock-based compensation plans (note 14)	1,566	—	(3,068)	—	(1,502)
Expense related to the stock-based compensation plans	—	—	2,795	—	2,795
<b>Balance - December 31, 2013</b>	5,116	(875,736)	1,047,104	9,497	185,981

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



Consolidated Statements of Income  
For the years ended December 31, 2013 and 2012

(expressed in thousands of Canadian dollars, except earnings per share)

	2013 \$	2012 \$
<b>Operating revenue</b> (note 19)		
Passenger	1,662,020	1,702,392
Other	10,040	8,294
	1,672,060	1,710,686
<b>Operating expenses</b> (note 19)		
Salaries, wages and benefits (note 3)	411,831	412,663
Aircraft fuel	378,996	396,413
Depreciation and amortization	62,602	56,745
Food, beverage and supplies	18,130	18,437
Aircraft maintenance materials, supplies and services	153,592	162,361
Airport and navigation fees	197,505	204,209
Aircraft rent	89,905	100,083
Terminal handling services	113,785	112,881
Other	121,452	119,508
	1,547,798	1,583,300
<b>Operating income</b>	124,262	127,386
<b>Non-operating income (expenses)</b>		
Interest revenue	1,333	1,337
Interest expense	(22,182)	(17,896)
Gain on disposal of property and equipment	1,521	1,232
Foreign exchange (loss) gain	(21,465)	5,909
Other	2,412	450
	(38,381)	(8,968)
<b>Income before income taxes</b>	85,881	118,418
<b>Income tax expense</b> (note 11)		
Current income tax	(3,264)	(513)
Deferred income tax (note 3)	(20,751)	(17,682)
	(24,015)	(18,195)
<b>Net income</b>	61,866	100,223
<b>Earnings per share, basic</b> (note 14)	0.50	0.81
<b>Earnings per share, diluted</b> (note 14)	0.50	0.77

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



Consolidated Statements of Comprehensive Income  
For the years ended December 31, 2013 and 2012

(expressed in thousands of Canadian dollars)

	2013	2012
	\$	\$
<b>Net income</b>	61,866	100,223
<b>Other comprehensive income (loss)</b>		
<i>Items that will not be subsequently reclassified to the statements of income</i>		
Actuarial gain (loss) on employee benefit liabilities, net of tax expense (recovery) of \$17,138 (2012 - (\$8,372)) (note 3)	45,593	(22,947)
Loss arising on revaluation of financial assets at fair value through other comprehensive loss (note 21)	—	(16,351)
<b>Comprehensive income</b>	107,459	60,925

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



Consolidated Statements of Cash Flows  
For the years ended December 31, 2013 and 2012

(expressed in thousands of Canadian dollars)

	2013	2012
	\$	\$
<b>Cash provided by (used in)</b>		
<b>Operating activities</b>		
Net income	61,866	100,223
Charges (credits) to operations not involving cash		
Depreciation and amortization	62,602	56,745
Amortization of prepaid aircraft rent and related fees	2,318	2,280
Gain on disposal of property and equipment	(1,521)	(602)
Stock-based compensation	2,795	2,454
Unrealized foreign exchange loss (gain) on long-term debt and finance leases	22,827	(5,614)
Deferred income tax expense	20,751	17,682
Accretion of debt component of convertible debentures	1,766	1,661
Other	6,220	484
	179,624	175,313
Net changes in non-cash balances related to operations (note 22)	(19,007)	(32,506)
	160,617	142,807
<b>Financing activities</b>		
Repayment of obligations under finance leases	(2,977)	(2,653)
Long-term borrowings	127,275	124,573
Repayment of long-term borrowings	(24,526)	(14,904)
Restricted cash related to aircraft financing	(5,930)	—
Repurchase of shares under normal course issuer bid	(4,006)	—
Dividends	(55,696)	(74,408)
	34,140	32,608
<b>Investing activities</b>		
Additions to property and equipment	(159,918)	(170,120)
Assets held for sale	—	(281)
Proceeds on disposal of property and equipment	4,059	602
Decrease in restricted cash related to letters of credit	2,697	4,622
	(153,162)	(165,177)
<b>Net change in cash and cash equivalents during the years</b>	41,595	10,238
<b>Cash and cash equivalents – Beginning of years</b>	118,306	108,068
<b>Cash and cash equivalents – End of years</b>	159,901	118,306
<b>Cash payments of interest</b>	19,995	20,032
<b>Cash receipts of interest</b>	1,382	1,220
<b>Cash payments of tax</b>	2,040	—

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



## Notes to the Consolidated Financial Statements For the years ended December 31, 2013 and 2012

(expressed in thousands of Canadian dollars, except shares and earnings per share)

### 1 General information

Chorus Aviation Inc. ("Chorus") was incorporated on September 27, 2010 under the laws of Canada. On November 18, 2010, Chorus incorporated Aviation General Partner Inc. to act as general partner for Jazz Aviation LP (the "Partnership"). On January 5, 2011, substantially all of the assets of Jazz Air LP were transferred to the Partnership and the airline business previously carried on by Jazz Air LP is now carried on by the Partnership. On February 28, 2011, Chorus incorporated Chorus Leasing I Inc., Chorus Leasing II Inc., and Chorus Leasing III Inc. (collectively, the "Initial LeaseCos"). The Initial LeaseCos were established for the sole purpose of acquiring Q400 NextGen turboprop aircraft ("Q400 aircraft") and related equipment to be financed by Export Development Canada ("EDC"). On December 31, 2012, the Initial LeaseCos were reorganized as follows: Chorus Leasing I Inc. and Chorus Leasing II Inc. amalgamated to form Chorus Leasing Amalco (2012) Inc. ("Amalco"), and Chorus Leasing III Inc. then acquired the assets and liabilities of Amalco. On November 28, 2013, Chorus incorporated Chorus Aviation Holdings Inc. ("CAHI") and CAHI incorporated Chorus Airport Services Inc. ("CASI"). CAHI was established to act as a holding company and CASI was established for the purpose of providing airport services.

On December 31, 2013, Chorus' subsidiaries were reorganized as follows: Chorus incorporated Jazz Aviation Holdings Inc. ("JAHI"), JAHI incorporated Jazz Aircraft Financing Inc. ("JAFI") as a wholly-owned subsidiary, and JAFI incorporated Jazz Leasing Inc. ("JLI"). Chorus Leasing III Inc. and 7503695 Canada Inc. ("7503695") amalgamated ("CL3 Amalco"). CL3 Amalco transferred the majority of its assets to JLI and JAFI assumed the EDC financing obligations from CL3 Amalco.

The registered office of Chorus is located at 100 King Street West, 1 First Canadian Place, Suite 6100, P.O. Box 50, Toronto, Ontario, M5X 1B8 and its country of domicile is Canada. Chorus was established to acquire and hold, directly or indirectly, investments in the Partnership and its general partner Aviation General Partner Inc. and other investments that it may acquire from time to time.

References to Chorus in the following notes to the consolidated financial statements refer to, as the context may require, Chorus, its current and former subsidiaries (including, but not limited to, the Partnership, Aviation General Partner Inc., 7503695, the Initial LeaseCos, Amalco, CAHI, CASI, JAHI, JAFI, JLI and CL3 Amalco) collectively, Chorus and one or more of its current and former subsidiaries, one or more of Chorus' current and former subsidiaries, or Chorus itself.

Chorus provides a significant part of Air Canada's domestic and transborder network. Chorus is economically and commercially dependent upon Air Canada and certain of its subsidiaries, as, in addition to being Chorus' primary source of revenue, these entities currently provide significant services to Chorus. Chorus and Air Canada are parties to an amended and restated capacity purchase agreement, effective January 1, 2006, as amended by agreements (the "Rate Amending Agreements") dated July 6, 2009, August 6, 2012 and June 3, 2013 and amending agreements (the "CPA Amending Agreements") dated September 22, 2009, March 8, 2011 and June 6, 2013 (as amended, the "CPA"), under which Air Canada currently purchases the greater part of Chorus' fleet capacity on aircraft operated by Chorus (the "Covered Aircraft") at predetermined rates (the "Rates").

On April 13, 2012, Chorus announced that it had received notification from Thomas Cook of its intention to discontinue operating dedicated charter aircraft, branded as Thomas Cook Canada, due to market conditions. As a consequence, the remaining three years of the five-year Flight Services Agreement with Chorus were terminated effective April 30, 2012. Chorus had, prior to such termination, operated Boeing 757-200 aircraft on behalf of Thomas Cook to various sun destinations from Canadian gateways. Chorus and Thomas Cook reached a commercial settlement in respect of the termination of the Flight Services Agreement, the economic terms of which reflect the original and intended expiration of the agreement, and address the recovery of certain initial start-up costs and foregone revenues. In the second quarter of 2012, \$9,000 was recorded in the financial statements of Chorus as revenue in respect of this settlement.

## Notes to the Consolidated Financial Statements For the years ended December 31, 2013 and 2012

(expressed in thousands of Canadian dollars, except shares and earnings per share)

### 1 General information (continued)

Under the CPA, Chorus experiences greater demand for its services in the second and third quarters of the calendar year and lower demand in the first and fourth quarters of the calendar year. Chorus has substantial fixed costs that do not meaningfully fluctuate with passenger demand in the short-term. Chorus' revenues do not fluctuate significantly with passenger load factors.

### 2 Basis of presentation

Chorus prepares its consolidated financial statements in accordance with GAAP as set out in the CPA Canada Handbook which incorporates IFRS as issued by the IASB.

These consolidated financial statements include all adjustments considered necessary by management to fairly state Chorus' annual results of operations, financial position and cash flows.

These consolidated financial statements have been authorized for issuance by the Board of Directors on February 19, 2014.

### 3 Significant accounting policies

#### a) Basis of measurement

These consolidated financial statements have been prepared under a historical cost basis, except for certain financial assets and financial liabilities, that are measured at fair value.

#### b) Critical accounting estimates and judgements

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the period. Actual results could differ from those estimates.

Significant estimates made in the preparation of these financial statements include, but are not limited to, the following areas, with further information contained in the applicable accounting policy or note:

#### *Employee benefits*

The cost and related liabilities of Chorus' post-employment benefit programs are determined using actuarial valuations. The actuarial valuations involve assumptions including those in relation to discount rates, future salary increases, mortality rates and future benefit increases. Also, due to the long-term nature of these programs, such estimates are subject to significant uncertainty. The Canadian Institute of Actuaries ("CIA") issued a Draft Report on Canadian Pensioners' Mortality during the third quarter of 2013, which included draft standard tables based on experience in Canadian Registered Pension Plans and a draft standard projection scale based on experience in the Canada Pension Plan. The draft tables were incorporated at December 31, 2013 to reflect the appropriate standard table and projection scale. This resulted in an actuarial remeasurement of the accounting liabilities with the impact being recorded in other comprehensive income. The CIA issued its final report on Canadian Pensioners' Mortality on February 13, 2014, and no adjustment was required to the financial statements. A change in mortality rate assumptions would not impact the solvency valuation for funding purposes at January 1, 2014. Funding current service cost for 2014 will be affected when new mortality assumptions are adopted for the January 1, 2014 funding actuarial valuations. See note 3(g) for further details.

## Notes to the Consolidated Financial Statements For the years ended December 31, 2013 and 2012

(expressed in thousands of Canadian dollars, except shares and earnings per share)

### 3 Significant accounting policies (continued)

#### *Depreciation of long-lived assets*

Management makes estimates and judgements about the expected useful life and the expected residual value of long-lived assets. Depreciation methods for long-lived assets are based on management's judgement of the most appropriate method to reflect the pattern of an asset's future economic benefit. Useful life and residual values are based on estimates of future fair values and can vary significantly from actual. Management revises depreciation estimates and patterns regularly and makes any changes on a prospective basis. A 25% reduction to the residual values of aircraft would result in an increase of \$7,739 to annual depreciation expense.

During 2013, Chorus reviewed the residual value of its owned aircraft and the estimated useful economic lives of these aircraft. As a result, the expected residual values of the Dash 8-100 and Dash 8-300 aircraft have been revised upwards. The effect of these changes on depreciation expense and related CPA revenue (excluding mark-up) for the year ended December 31, 2013 was approximately \$5,200.

#### c) Principles of consolidation

These consolidated financial statements include the accounts of Chorus and its current and former subsidiaries, the Partnership, Aviation General Partner Inc., 7503695, the Initial LeaseCos, Amalco, CAHI, CASI, JAH, JAFI, JLI and CL3 Amalco. All inter-company and inter-entity balances and transactions are eliminated. Chorus has no non-controlling interests, therefore, all profits and comprehensive income are attributable to the shareholders of the Company.

#### d) Cash and cash equivalents

Cash and cash equivalents consist of current operating bank accounts, term deposits and fixed income securities with an original term to maturity of 90 days or less. Cash equivalents are readily convertible into a known amount of cash and are subject to an insignificant risk of changes in value.

#### e) Restricted cash

Chorus has recorded restricted cash under current assets related to funds on deposit with a financial institution as collateral for letters of credit. Restricted cash recorded under other assets relates to funds required to be held in a segregated account with a financial institution as security for the EDC financing related to the purchase of six Q400 aircraft in 2013.

#### f) Operating revenue

Under the CPA, Chorus is paid to provide services to Air Canada, as explained in note 1. The related fees payable by Air Canada are recognized in revenue as the capacity is provided and incentive payments and margin adjustments are recognized, respectively, as increases in and reductions of, passenger revenue based on management estimates during the year when the amount of revenue can be measured reliably, and it is probable that the economic benefit will flow to Chorus.

Revenue earned by Chorus under its flight services agreement with Thomas Cook in 2012 and its operation of charter flights is also included in passenger revenue and recognized when the service is provided. Maintenance, repair and overhaul ("MRO") operations and other sources of revenue, such as third party ground handling services, are included in other revenue and are recognized when the service is provided. Revenue earned under an inventory consignment agreement with a third party is recognized when the inventory is received by the end purchaser.

## Notes to the Consolidated Financial Statements For the years ended December 31, 2013 and 2012

(expressed in thousands of Canadian dollars, except shares and earnings per share)

### 3 Significant accounting policies (continued)

The CPA provides for a monthly payment for an amount per aircraft designed to reimburse Chorus for certain aircraft ownership costs. Chorus has concluded that a component of its revenue under the CPA is rental income since the CPA identifies the “right of use” of a specific type and number of aircraft over a stated period of time otherwise known as the Covered Aircraft. The amount deemed to be rental income is \$165,313 for the year ended December 31, 2013 (\$153,353 for the year ended December 31, 2012).

#### g) Employee benefits

Chorus' significant policies related to the defined benefit pension plan for its pilots, the supplemental executive retirement plan for Chorus executives, which is also a defined benefit pension plan (collectively referred to as “Pension Benefits”), and the Other Employee Benefits are as follows:

- The cost of pension benefits earned by employees is actuarially determined using the projected benefit method prorated on service, market interest rates, management's best estimate of salary escalation and retirement ages and life expectancy of employees. Obligations are attributed to the period beginning on the date the employee joins the plan and ending on the earlier of the date of termination, death or retirement. Actuarial gains and losses on the pension benefits are recognized in full in the period in which they occur in other comprehensive income and retained earnings without recycling to the statement of income in subsequent periods. Current service cost, the recognized element of any past service cost, the interest income on plan assets and the interest arising on the pension liability are included in salaries, wages and benefits in the statement of income.
- Other employee benefits consist of two categories of benefits:
  - Medical and dental benefits provided to employees while on long-term disability, and Worker's Compensation and Workers Safety Insurance Board benefits in respect of Ontario employees, are collectively referred to as other long-term benefits. The actuarial gains and losses for this component of other employee benefits are charged to operating expense in the year they occur.
  - Sick leave benefits are paid to certain employees upon or just prior to retirement. The actuarial gains and losses on this component of other employee benefits are charged to other comprehensive income in the year they occur.
- The cost of the other employee benefits is actuarially determined using the projected benefit method prorated on service (where applicable), market interest rates, and management's best estimate of retirement ages of employees, health care cost inflation, salary escalation and general inflation, as applicable to each of the categories of benefits.
- Past service costs arising from plan amendments of the defined benefit pension plan and the supplemental executive retirement plan and other employee benefit plans are recognized immediately in income.
- The registered pension plan is subject to certain minimum funding requirements. The liability, where applicable, in respect of the minimum funding requirement is determined using the projected minimum funding requirements based on actuarial forecasts. The liability in respect of the minimum funding requirement and any subsequent re-measurement of that liability is recognized in other comprehensive income without subsequent reclassification to income.

## Notes to the Consolidated Financial Statements For the years ended December 31, 2013 and 2012

(expressed in thousands of Canadian dollars, except shares and earnings per share)

### 3 Significant accounting policies (continued)

- The measurement date of each of the plans' assets and obligations is December 31. Pension obligations are attributed to the period beginning on the employee's date of joining the plan and ending on the earlier of the date of termination, death or retirement. The obligations relating to other employee benefits plans are attributed to the period beginning on the employee's date of joining the plan or disablement (whichever applicable) and ending on the earlier of retirement or end of disablement or age 65 (whichever applicable).
- Chorus also maintains several defined contribution pension plans. The cost of defined contribution pension plans is charged to expense as the contributions become payable.

#### h) Stock-based compensation

##### *Long-term incentive plan*

The Chorus long-term incentive plan (the "Chorus LTIP") is a restricted share unit ("RSU") plan under which participants receive an annual grant of RSUs that vest at the end of a three year period if certain performance goals and service conditions, established at the time of grant by the Board of Directors, are achieved. RSUs entitle the participant to receive common shares of Chorus on a one-for-one basis. Additional RSUs representing the value of quarterly dividends paid on corresponding common shares of Chorus accrue for the benefit of participants. Unvested RSUs held by participants are forfeited if performance goals or service conditions are not met. On vesting, Chorus has the option to issue the shares from treasury or purchase them on the secondary market.

The Jazz long-term incentive plan (the "Jazz LTIP") was also a "restricted share unit" plan similar to the Chorus LTIP which applied to awards granted prior to the implementation of the Chorus LTIP on December 31, 2010. As detailed in note 14(c), the remaining awards granted in the Jazz LTIP vested during 2012. The Jazz LTIP held all of the same attributes as the Chorus LTIP except that the shares of the Jazz LTIP were purchased in the secondary market at the time of the grant and held in a trust for the benefit of the participants until vesting occurred. Dividends paid by Chorus on common shares held by the trust were also used to invest in additional common shares and vested concurrently and proportionately with the restricted units. On forfeiture of any restricted units, the common shares and related dividends accrued to Chorus. The trust was a structured entity which was consolidated by Chorus. The shares of Chorus held by the trust were presented as a reduction of equity.

For the Chorus LTIP, the cost of the RSUs is measured at the fair value of the common shares of Chorus at the grant date and the number of RSUs expected to vest. Each vesting tranche of RSUs is considered a separate award with its own vesting period and estimated grant date fair value. Compensation expense is recognized over each tranche's vesting period by increasing contributed surplus based on the number of awards expected to vest. The number of awards expected to vest is reviewed at least annually with any impact being recognized immediately.

## Notes to the Consolidated Financial Statements For the years ended December 31, 2013 and 2012

(expressed in thousands of Canadian dollars, except shares and earnings per share)

### 3 Significant accounting policies (continued)

#### *Deferred share units*

Non-executive directors receive a portion of their remuneration in deferred share units ("DSUs") under a DSU Plan (the "DSU Plan") designed to promote the alignment of interests between individual non-executive directors and the shareholders of Chorus. DSUs have a value equivalent to the value of the Chorus shares. DSUs vest immediately and may only be redeemed for cash and will be paid out only subsequent to the time the director ceases to be a director, or in the case of a U.S. taxpayer, subsequent to the date such person incurs a "separation from service" under applicable U.S. law. Participating directors will receive, in respect of their DSUs, an amount equivalent to the amount of any dividends paid on the shares in the form of additional DSUs. Under the DSU Plan, participating directors may receive annual grants of DSUs. In addition, a participating director may elect to have his or her annual retainer and/or any additional retainer payable in the form of DSUs or a combination of DSUs and cash. DSUs are cash-settled share-based payments that are measured at fair value and recognized as a liability. The liability is remeasured at fair value each period and at the settlement date with changes in fair value recognized in the statement of income.

#### *Employee share ownership program*

Chorus' employee share ownership plan (the "ESOP") permits employees to buy common shares of Chorus through payroll deduction. Under this plan, contributions made by employees are matched to a specific percentage by Chorus. These contributions are expensed to salaries, wages and benefits expense over the one year vesting period. The amount expected to vest is reviewed at least annually, with any change in estimate recognized immediately in salaries, wages and benefits.

#### i) Financial instruments

Chorus has early adopted IFRS 9, *Financial Instruments*. The standard requires financial assets to be classified into two measurement categories: amortized cost and fair value. Classification depends on the entity's business model for managing its financial instruments and the contractual cash flow characteristics of the instrument. For investments in equity instruments which are not subject to control, joint control, or significant influence, on initial recognition GAAP allows an entity to irrevocably elect classification at "fair value through profit or loss" or "fair value through other comprehensive income". For financial liabilities, changes in fair value attributable to an entity's own credit risk are recorded through other comprehensive income rather than through net income.

Management has designated that equity investments not held for trading that were previously classified as available for sale, be classified as fair value through other comprehensive income.

Financial instruments are classified as follows:

- Asset backed commercial paper ("ABCP") is classified as "Fair Value through Profit and Loss." These financial assets are measured at fair value, with changes in fair value recognized in the statement of income each reporting period.
- Cash and cash equivalents, restricted cash and accounts receivable are classified as "Financial Assets Measured at Amortized Cost" After their initial fair value measurement, they are measured at amortized cost using the effective interest method, less a provision for impairment, established on an account-by-account basis, based on, among other factors, prior experience and knowledge of the specific debtor and its assessment of the current economic environment.



Notes to the Consolidated Financial Statements  
For the years ended December 31, 2013 and 2012

(expressed in thousands of Canadian dollars, except shares and earnings per share)

**3 Significant accounting policies (continued)**

- Accounts payable, dividends payable, long-term debt and the debt component of convertible debentures are classified as “Other Financial Liabilities”. Other Financial Liabilities are initially recognized at fair value less transaction costs, except for the debt component of the convertible debentures. Subsequent to initial recognition, Other Financial Liabilities are measured at amortized cost using the effective interest method.

*Hedging*

The IASB made amendments during the year to IFRS 9, *Financial Instruments*, related to hedging. Chorus does not currently hedge, so there was no impact on the Chorus consolidated financial statements.

*Impairment of financial assets*

At each reporting date, Chorus assesses whether there is objective evidence that a financial asset carried at amortized cost is impaired. If such evidence exists, Chorus recognizes an impairment loss, as the difference between the carrying value of the instrument and the present value of the estimated future cash flows, discounted using the instrument's original effective interest rate or a discount rate based on the risk associated with the financial asset being tested. The carrying amount of the asset is reduced by this amount through a charge to the statement of income.

Impairment losses on financial assets carried at amortized cost are reversed in subsequent periods if the amount of the loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized.

j) Property and equipment

Property and equipment are stated at cost less accumulated depreciation and accumulated impairment losses. Cost includes expenditures that are directly attributable to the acquisition of the asset. Property and equipment are depreciated to estimated residual values based on the straight-line method over their useful lives. Aircraft and flight equipment are depreciated over 20 to 30 years, with 5% - 25% estimated average residual values.

Major maintenance overhaul expenditures (“heavy checks”), including labour, are capitalized and depreciated over the expected life of the maintenance cycle. Any remaining carrying value is derecognized when the major maintenance overhaul commences. All other costs associated with maintenance of fleet assets (including engine maintenance provided under “power-by-the-hour” arrangements) are charged to the statement of income as incurred.

Buildings are depreciated over their useful lives not exceeding 40 years on a straight-line basis. An exception to this is where the useful life of the building is greater than the term of the land lease. In these circumstances, the building is depreciated over the life of the lease.

Depreciation on other property and equipment is provided on a straight-line basis from the date assets are placed in service, to their estimated residual values, over the following estimated useful lives:

Leaseholds	Over the term of the related lease
Ground and other equipment	5 years

Property under finance leases and the related obligation for future lease payments are initially recorded at an amount equal to the lesser of fair value of the property or equipment and the present value of those lease payments. Property and equipment under finance leases are depreciated to estimated residual value over the useful life, unless there is no reasonable certainty that Chorus will obtain ownership at the end of the lease term, in which case the asset is depreciated over the shorter of the lease term and its useful life.

## Notes to the Consolidated Financial Statements For the years ended December 31, 2013 and 2012

(expressed in thousands of Canadian dollars, except shares and earnings per share)

### 3 Significant accounting policies (continued)

Depreciation methods, residual values and useful lives of the assets are reviewed at least annually and adjusted if appropriate.

#### k) Transaction costs

Transaction costs that are incremental and directly attributable to the acquisition or issue of a financial asset or financial liability are recorded as follows:

- Financial assets or financial liabilities at fair value through profit and loss - expensed to net income as incurred;
- Financial assets or liabilities recorded at amortized cost - included in the carrying value of the financial asset or financial liability and amortized over the expected life of the financial instrument using the effective interest method; and
- Equity instruments recorded at fair value through other comprehensive income - included in the initial cost of the underlying asset.

Transaction costs for operating and finance leases are capitalized and amortized over the life of the lease on a straight-line basis.

#### l) Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of Chorus' share of the net identifiable assets of the acquired business at the date of acquisition. Goodwill is tested annually for impairment, or at any time if an indication of impairment exists, and carried at cost less accumulated impairment losses. Impairment losses on goodwill are not reversed. For the purpose of impairment testing, goodwill is tested for impairment at the cash-generating unit or ("CGU") level.

#### m) Impairment of non-financial assets

Property and equipment, is tested for impairment when events or changes in circumstances indicate that the carrying amount may not be recoverable. Long-lived assets that are not amortized are subject to an annual impairment test. For the purpose of measuring recoverable amounts, assets are grouped at the lowest levels for which there are separately identifiable cash inflows (cash-generating units or "CGUs"). The recoverable amount is the higher of an asset's fair value less costs to sell and value in use (being the present value of the expected future cash flows of the relevant asset or CGU). An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount.

Chorus evaluates impairment losses for potential reversals when events or circumstances warrant such consideration.

#### n) Foreign currency translation

Items included in the financial statements of each of the consolidated entities are measured using the currency of the primary economic environment in which the entity operates (the "functional currency"). The functional currency of Chorus and its subsidiaries is the Canadian dollar.

Monetary assets and liabilities denominated in foreign currencies are translated into Canadian dollars at rates of exchange in effect at the date of the statement of financial position. Non-monetary assets, liabilities and other items recorded in income are translated at rates of exchange in effect at the date of the transaction.



## Notes to the Consolidated Financial Statements For the years ended December 31, 2013 and 2012

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(expressed in thousands of Canadian dollars, except shares and earnings per share)

### 3 Significant accounting policies (continued)

Foreign currency transactions are translated into Canadian dollars using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of foreign currency transactions and from the translation of monetary assets and liabilities denominated in currencies other than the Canadian dollar are recognized in the statement of income.

#### o) Provisions

Provisions are recognized in other liabilities when Chorus has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and the amount can be reliably estimated. Provisions are measured at management's best estimate of the expenditure required to settle the obligation at the end of the reporting period, and are discounted to present value where the effect is material. Chorus performs evaluations to identify onerous contracts and, where applicable, records provisions for such contracts.

#### p) Aircraft lease payments

Total aircraft rentals under operating leases and the related lease inducements received and fees paid over the lease term are amortized to operating expense on a straight-line basis. Prepaid aircraft rentals and related fees are the difference between the straight-line aircraft rent and the payments stipulated under the lease agreements and legal and related transaction fees associated with the leases. Current and non-current unamortized lease inducements are included in accounts payable and accrued liabilities and other long-term liabilities, respectively.

#### q) Inventories

Inventories are valued at the lower of cost and net realizable value. Cost is determined on a first-in, first-out basis, and net realizable value is the estimated selling price to a third party in the ordinary course of business, less estimated selling costs. Inventories consist of aircraft expendables and supplies, fuel and de-icing fluid and used aircraft expendables and rotables being held by a third party under a consignment agreement.

#### r) Income taxes

Chorus uses the asset and liability method for accounting for income taxes.

Current tax assets and liabilities for the current and prior periods are measured at the amounts expected to be paid or recovered, using tax rates and tax laws that have been enacted or substantively enacted by the end of the period.

Deferred tax assets and liabilities are recognized for all future tax consequences attributable to the differences between the financial statement carrying amounts of assets and liabilities and their respective tax bases, except for the initial recognition of goodwill and the initial recognition of an asset or liability, which at the time of the transaction, affects neither accounting profit nor taxable profit or loss. Deferred tax assets are also recognized for unused tax losses and unused tax credits. Deferred tax assets are recognized only to the extent that it is probable that future taxable profit will be available against which the deductible temporary differences, unused tax losses and unused tax credits can be utilized. Deferred tax assets and liabilities are measured using enacted or substantively enacted tax rates and tax laws expected to apply when the carrying amount of the assets or liabilities are recovered or settled or the unused losses are expected to be utilized.

## Notes to the Consolidated Financial Statements For the years ended December 31, 2013 and 2012

(expressed in thousands of Canadian dollars, except shares and earnings per share)

### 3 Significant accounting policies (continued)

Current and deferred income tax expense is recognized in the statement of income for the period, except to the extent that the income taxes related to a transaction or event which is recognized, in the same or different period, either in other comprehensive income or directly in equity.

#### s) Earnings per share

Earnings per share are calculated on a weighted average number of shares outstanding basis. Shares formerly held in trust under the Jazz LTIP reduced the weighted average number of outstanding shares from the date they were contributed to the plan.

Diluted earnings per share are presented for the effects of all dilutive potential common shares by adjusting the net income attributable to Chorus shareholders and the weighted average number of shares outstanding, for convertible debentures, by adding back to net income the after-tax effect of any interest expense or other changes recognized in the statement of income, and by adding to the weighted average number of common shares outstanding, the weighted average number of common shares that would be issued on the conversion of the convertible debentures at the later of the beginning of the period, or the date the convertible debentures were issued.

#### t) Dividends

Dividends payable by Chorus to its shareholders, which are determined at the discretion of the Directors, are recorded when declared.

#### u) Government assistance

Non-repayable government assistance is recorded in the period earned as non-operating income. During the year ended December 31, 2013, Chorus recorded \$2,000 (2012 - \$nil) of Human Resource Development Funding from the Province of Nova Scotia.

Where forgivable loans are provided by governments with forgiveness contingent on meeting certain criteria, the forgivable loan is recorded as non-operating income when Chorus has met the terms for forgiveness of the loan. As at December 31, 2013, Chorus has received a \$2,500 forgivable loan from the Province of Nova Scotia of which \$nil has been recognized as income. The entire \$2,500 has been recorded as a liability with \$500 in current liabilities expected to be earned in 2014.

### New accounting standards adopted during the year

#### *IFRS 10, Consolidated Financial Statements*

The IASB issued IFRS 10, "Consolidated Financial Statements" ("IFRS 10"), effective for annual periods beginning on or after January 1, 2013. IFRS 10 replaces portions of IAS 27, "Consolidated and Separate Financial Statements" ("IAS 27") that addresses consolidation, and supersedes Standing Interpretations Committee ("SIC") SIC-12 in its entirety. The objective of IFRS 10 is to define the principles of control and establish the basis of determining when and how an entity should be included within a set of consolidated financial statements. IAS 27 has been amended to reflect the issuance of IFRS 10 and retains guidance only for separate financial statements. Chorus assessed its consolidation conclusions on January 1, 2013 and determined that the adoption of IFRS 10 did not result in any change in the consolidation status of any of its subsidiaries.

## Notes to the Consolidated Financial Statements For the years ended December 31, 2013 and 2012

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(expressed in thousands of Canadian dollars, except shares and earnings per share)

### 3 Significant accounting policies (continued)

#### *IFRS 11, Joint Arrangements*

The IASB issued IFRS 11, "Joint Arrangements" ("IFRS 11"), effective for annual periods beginning on or after January 1, 2013. IFRS 11 supersedes IAS 31, "Interest in Joint Ventures" and SIC-13, "Jointly Controlled Entities - Non Monetary Contributions by Venturers". Through an assessment of the rights and obligations in an arrangement, IFRS 11 establishes principles to determine the type of joint arrangement and guidance for financial reporting activities required by the entities that have an interest in arrangements which are controlled jointly. As a result of the issuance of IFRS 10 and IFRS 11, IAS 28, "Investments in Associates and Joint Ventures" ("IAS 28") was amended to reflect the guidance provided in IFRS 10 and IFRS 11. Chorus currently has no interests in joint arrangements, therefore the adoption of this standard had no impact on the Chorus consolidated financial statements.

#### *IFRS 12, Disclosures of Interest in Other Entities*

The IASB issued IFRS 12, "Disclosures of interests in other entities" effective for annual periods beginning on or after January 1, 2013. The standard includes disclosure requirements for all forms of interests in other entities, including joint arrangements, associates, structured entities and other off balance sheet vehicles. The adoption of this standard did not result in any additional disclosures for Chorus.

#### *IFRS 13, Fair Value Measurement*

The IASB issued IFRS 13, "Fair Value Measurement" ("IFRS 13") effective for annual periods beginning on or after January 1, 2013. IFRS 13 defines fair value, provides guidance in a single framework for measuring fair value and identifies the required disclosures pertaining to fair value measurement. The adoption of IFRS 13 did not require any adjustments to the valuation techniques used by Chorus to measure fair value and did not result in any measurement adjustments as at January 1, 2013.

#### **Amendments to standards**

IAS 1, *Presentation of Financial Statements*, has been amended to require entities to separate items presented in other comprehensive income ("OCI") into two groups, based on whether or not items may be recycled in the future. Entities that choose to present OCI items before tax will be required to show the amount of tax related to the two groups separately. The amendment is effective for annual periods beginning on or after July 1, 2012 with earlier application permitted. These changes did not result in any adjustments to OCI or comprehensive income.

IAS 19, *Employee Benefits*, has been amended effective for annual periods beginning on or after January 1, 2013. The revised standard requires immediate recognition of actuarial gains and losses in other comprehensive income, eliminating the previous options that were available. A number of other amendments have been made to recognition, measurement, classification and disclosure. Chorus' accounting policy as at December 31, 2012 for recognition of actuarial gains and losses through other comprehensive income was consistent with the revisions contained in the standard. Chorus has retrospectively applied the amendments to IAS 19 and as a result has restated net income from the 2012 comparative period to be lower than originally reported under the historical standard. The decrease arose due to the projected rate of return on plan assets being higher than the discount rate, and results in the statement of income receiving an additional pre-tax charge of \$1,208, recorded to salaries, wages and benefits, and a reduction of income tax expense of \$324 for the year ended December 31, 2012 with an offsetting equivalent increase of \$884 (net of tax of \$324) to actuarial gain on employee benefits liabilities in other comprehensive income. The revised standard does not impact the balances of employee benefits in the statement of financial position or the total amount of comprehensive income for prior years.

Notes to the Consolidated Financial Statements  
For the years ended December 31, 2013 and 2012

(expressed in thousands of Canadian dollars, except shares and earnings per share)

**3 Significant accounting policies (continued)**

The IASB made several amendments to IAS 36, *Impairment of assets*, in conjunction with issuing IFRS 13. They later issued a limited scope amendment, effective January 1, 2014, introducing additional disclosures about fair value measurement where an impairment has been recorded or reversed. Chorus has early adopted the limited scope amendment with no material impact on Chorus' financial statements.

**4 Capital management**

Chorus' capital consists of cash and cash equivalents, restricted cash, finance leases, long-term debt, convertible debentures and equity.

Total capital as at December 31, 2013 and December 31, 2012 is calculated as follows:

	December 31,	
	2013	2012
	\$	\$
Cash and cash equivalents	(159,901)	(118,306)
Restricted cash	(3,320)	(6,017)
Restricted cash included in other assets	(6,208)	—
Finance leases (including current portion)	6,429	8,889
Long-term debt (including current portion)	402,799	277,446
Convertible debentures (excluding equity portion)	78,535	76,769
Equity	185,981	132,115
<b>Total capital</b>	<b>504,315</b>	<b>370,896</b>

Chorus' main objectives when managing capital are to provide a strong capital base to maintain shareholder, creditor and market confidence and to sustain future development of the business. Chorus manages its capital structure and makes adjustments to it in light of changes in economic conditions and Chorus' risk profile. The airline business is capital intensive and highly sensitive to uncertain external circumstances.

## Notes to the Consolidated Financial Statements For the years ended December 31, 2013 and 2012

(expressed in thousands of Canadian dollars, except shares and earnings per share)

### 4 Capital management (continued)

In order to maintain a strong financial position, Chorus may, from time to time, adjust the amount of dividends paid to shareholders, buy back shares for cancellation pursuant to normal course issuer bids or issue new shares. Chorus may also pay down debt or issue new debt.

In managing its capital structure, Chorus monitors performance throughout the year having regard to anticipated cash dividends, working capital requirements, maintenance and growth capital expenditures, available cash on deposit and, where applicable, long-term borrowings. Chorus also monitors performance having regard to financial metrics within the covenants associated with the Q400 aircraft and engine financing, and other financial metrics such as adjusted net debt. Adjusted net debt is calculated as the sum of long-term debt, finance leases, convertible debentures and capitalized operating leases less cash and cash equivalents.

The following table reflects Chorus' adjusted net debt balances as at December 31, 2013 and as at December 31, 2012:

	December 31,		
	2013	2012	Change
	\$	\$	\$
Total long-term debt and finance leases	374,518	263,179	111,339
Current portion of long-term debt and finance leases	34,710	23,156	11,554
Convertible debentures	78,535	76,769	1,766
Total long-term debt and finance leases (including current portion) and convertible debentures	487,763	363,104	124,659
Less: Cash and cash equivalents	(159,901)	(118,306)	(41,595)
Net debt	327,862	244,798	83,064
Capitalized operating leases	71,348	163,044	(91,696)
Adjusted net debt	399,210	407,842	(8,632)

Adjusted net debt is a non-GAAP financial measure used by Chorus and may not be comparable to measures presented by other public companies. Adjusted net debt is a key component of the capital management by Chorus and provides management with a measure of its net indebtedness. Chorus includes capitalized operating leases which is a measure commonly used in the airline industry to ascribe a value to obligations under operating leases. Common industry practice is to multiply annualized aircraft rent by 7.5. This definition of capitalized operating leases is used by Chorus and may not be comparable to similar measures presented by other public companies. Aircraft rent was \$89,905 for the year ended December 31, 2013 and \$100,083 for the year ended December 31, 2012. The majority of Chorus' aircraft under operating leases are subleased from Air Canada, or its subsidiary, who hold the head lease or own the aircraft. Aircraft rent related to these aircraft of \$80,393 for the year ended December 31, 2013 and \$78,344 for the year ended December 31, 2012 has been removed from the calculation due to Air Canada's offsetting liability under the CPA for rental payments and return condition obligations. If these Air Canada operating leases were included in the above definition, adjusted net debt would be \$1,002,150 and \$995,421, respectively.

## Notes to the Consolidated Financial Statements For the years ended December 31, 2013 and 2012

(expressed in thousands of Canadian dollars, except shares and earnings per share)

### 5 Cash and cash equivalents

	As at December 31,	
	2013	2012
	\$	\$
Cash <sup>(1)</sup>	119,938	83,338
Term deposits and fixed income securities	39,963	34,968
<b>Cash and cash equivalents</b>	<b>159,901</b>	<b>118,306</b>

(1) Cash encumbered in support of issued letters of credit has been classified as restricted cash and shown separately in the consolidated statement of financial position (2013 - \$3,320; 2012 - \$6,017). Chorus has also recorded restricted cash of \$6,208 (2012 - \$nil) in other assets related to a segregated account required as security for the EDC financing related to six Q400 aircraft in 2013 (see note 23).

The weighted average interest rate on investments as at December 31, 2013 is 1.10% (2012 - 1.09%).

### 6 Property and equipment

	Year ended December 31, 2012					Year ended December 31, 2013				
	Opening net book value \$	Additions \$	Disposals/ deposits applied \$	Depreciation for the period \$	Closing / opening net book value \$	Additions \$	Disposals/ deposits applied \$	Depreciation for the period \$	Closing net book value \$	
Flight equipment	337,969	123,777	—	(32,799)	428,947	142,641	—	(38,342)	533,246	
Major maintenance overhauls	14,545	11,267	—	(13,229)	12,583	17,523	—	(14,634)	15,472	
Facilities	11,676	6,270	—	(683)	17,263	6,830	(2,538)	(972)	20,583	
Equipment	10,219	4,181	—	(5,442)	8,958	6,196	—	(4,330)	10,824	
Leaseholds	12,211	322	—	(1,795)	10,738	123	—	(1,528)	9,333	
Flight equipment under finance leases	10,785	—	—	(2,797)	7,988	—	—	(2,796)	5,192	
Deposits on aircraft/ engines	11,635	13,634	(11,874)	—	13,395	263	(13,658)	—	—	
<b>Total</b>	<b>409,040</b>	<b>159,451</b>	<b>(11,874)</b>	<b>(56,745)</b>	<b>499,872</b>	<b>173,576</b>	<b>(16,196)</b>	<b>(62,602)</b>	<b>594,650</b>	

Notes to the Consolidated Financial Statements  
For the years ended December 31, 2013 and 2012

(expressed in thousands of Canadian dollars, except shares and earnings per share)

**6 Property and equipment (continued)**

	<u>At December 31, 2012</u>			<u>At December 31, 2013</u>		
	Cost \$	Accumulated depreciation \$	Net book value \$	Cost \$	Accumulated depreciation \$	Net book value \$
Flight equipment	537,041	(108,094)	428,947	673,052	(139,806)	533,246
Major maintenance overhauls	29,261	(16,678)	12,583	31,284	(15,812)	15,472
Facilities	22,378	(5,115)	17,263	25,466	(4,883)	20,583
Equipment	46,110	(37,152)	8,958	52,306	(41,482)	10,824
Leaseholds	26,847	(16,109)	10,738	26,970	(17,637)	9,333
Flight equipment under finance leases	22,951	(14,963)	7,988	22,951	(17,759)	5,192
Deposits on aircraft/engines	13,395	—	13,395	—	—	—
<b>Total</b>	<b>697,983</b>	<b>(198,111)</b>	<b>499,872</b>	<b>832,029</b>	<b>(237,379)</b>	<b>594,650</b>

**7 Goodwill**

Goodwill, representing less than one percent of Chorus' total assets, is allocated to the Jazz CGU (which approximates the entity as a whole). The recoverable amount of the Jazz CGU was determined using fair value less costs of disposal. In assessing the goodwill for impairment, Chorus compares the aggregate recoverable amount consisting of the sum of its quoted equity market capitalization and the fair value of its debt to the carrying value of its net assets excluding long term debt. An impairment charge is recognized to the extent that the carrying value exceeds the recoverable amount. No impairment of goodwill was recognized during 2013 or 2012.

Notes to the Consolidated Financial Statements  
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**8 Obligations under finance leases**

Chorus has entered into finance leases related to aircraft. The obligations are as follows:

	2013 \$	2012 \$
No later than one year	3,791	3,546
Later than one year and no later than five years	3,201	6,541
Total minimum lease payments	6,992	10,087
Less: Amount representing interest (at rates ranging from 8.755% to 9.450%)	563	1,198
Present value of net minimum finance lease payments	6,429	8,889
Less: Current portion	3,356	2,875
Obligations under finance leases	3,073	6,014

The present value of net minimum finance lease payments is as follows:

	2013 \$	2012 \$
No later than one year	3,356	2,875
Later than one year and no later than five years	3,073	6,014
	6,429	8,889

A significant portion of the minimum lease payments for aircraft are payable in US dollars and have been converted to Canadian currency at \$1.0636, which was the exchange rate in effect at the end of day closing on December 31, 2013 (2012 - \$0.9949). Interest of \$682 (2012 - \$907) relating to finance lease obligations has been included in aircraft rent. The majority of these lease agreements are renewable at the end of the lease period, at market rates.



Notes to the Consolidated Financial Statements  
For the years ended December 31, 2013 and 2012

(expressed in thousands of Canadian dollars, except shares and earnings per share)

**9 Long-term debt**

Long-term debt consists of the following:

	As at December 31,	
	2013	2012
	\$	\$
Term loans - purchased aircraft <sup>(1)</sup>	382,759	267,339
Term loans - purchased engines <sup>(2)</sup>	8,040	3,807
Term loan - Halifax facility <sup>(3)</sup>	12,000	6,300
	402,799	277,446
Less: Current portion	31,354	20,281
	371,445	257,165

- (1) 21 individual term loans, repayable in semi-annual instalments, ranging from \$883 to \$1,080, bearing fixed interest at a weighted average rate of 3.386%, maturing between May 2023 and March 2025, each secured primarily by one Q400 aircraft and two PW150A engines. At December 31, 2013, the total Q400 aircraft financing payable in US dollars was US\$359,871 (December 31, 2012 - US\$268,710), and the net book value of property and equipment pledged as collateral under Q400 aircraft financing was \$425,070 (December 31, 2012 - \$308,953).
- (2) Four individual term loans, repayable in quarterly instalments ranging from \$56 to \$59, including fixed interest at a weighted average rate of 4.867%, maturing between December 2024 and October 2025, each secured by one PW150A engine. At December 31, 2013, the total Q400 engine financing payable in US dollars was US\$7,560 (December 31, 2012 - US\$3,853) and the net book value of property and equipment pledged as collateral under Q400 engine financing was \$8,567 (December 31, 2012 - \$4,722).
- (3) Nova Scotia Jobs Fund loan, with a maximum contribution of \$12,000, bearing interest at a fixed rate of 3.33% annually. Principal repayments of \$1,000 are payable annually commencing on August 31, 2016. Maturing on August 31, 2027, the loan may be repaid in full or in part at any time without bonus or penalty and is secured by a first security interest in the land and office building located at 3 Spectacle Lake Drive, Dartmouth, Nova Scotia and the assignment of the building tenant leases. As of December 31, 2013, the amount drawn on the loan was \$12,000 (December 31, 2012 - \$6,300).

The majority of the following future repayments of long-term debt are payable in US dollars and have been converted to Canadian dollars at \$1.0636, which was the exchange rate in effect at the end of day closing December 31, 2013.

	\$
No later than one year	31,354
Later than one year and no later than five years	139,591
Later than five years	231,854
	<u>402,799</u>

Under its financing agreement with EDC (for both aircraft and engines), the "Jazz Group" (currently comprised of the Partnership, JAFI and JLI) is required to maintain a maximum adjusted leverage ratio of 2.25:1 and a minimum adjusted interest coverage ratio of 1.66:1. As at December 31, 2013, the Jazz Group was in compliance with these covenants. Failure by the Jazz Group to satisfy either such ratio at an applicable time would constitute an event of default under the financing agreement, which could have a material adverse effect on Chorus.

## Notes to the Consolidated Financial Statements For the years ended December 31, 2013 and 2012

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(expressed in thousands of Canadian dollars, except shares and earnings per share)

### 9 Long-term debt (continued)

The financing agreement with EDC also contains several covenants which are specific to the Partnership as the lessee of the Q400 aircraft and engines including:

- a tangible asset disposal covenant, and;
- a continuation of business under the CPA covenant.

As at December 31, 2013, the Partnership was in compliance with both of these covenants.

As additional security under the financing agreements, the aircraft and engine leases between the Partnership and JLI have been assigned to EDC. Also, JLI has provided a full recourse guarantee to EDC and JAFI pledged the issued shares of JLI to EDC. In addition, restricted cash recorded under other long-term assets relates to funds required to be held in a segregated account with a financial institution as security for the EDC financing related to the purchase of six Q400 aircraft in 2013.

### 10 Convertible debentures

In November of 2009, Chorus entered into an agreement to sell to a group of underwriters \$86,250 principal amount of 9.50% convertible unsecured subordinated debentures (the "Debentures"). The net proceeds received by Chorus from the sale of Debentures were \$82,265 after deduction of the underwriters' fee and the expenses of the offering. On December 14, 2010, \$6,040 of the Debenture principal was converted, leaving \$80,210 outstanding.

The Debentures bear interest at a rate of 9.50% per annum, payable semi-annually in arrears on June 30 and December 31 in each year commencing on June 30, 2010, and will mature on December 31, 2014 (the "Maturity Date"). As such, as at December 31, 2013, the Debentures are shown as a current liability. The Debentures are convertible at each holder's option into shares of Chorus at any time prior to 5:00 pm (EST), on the earlier of the Maturity Date and the date fixed for redemption at a conversion price of \$5.25 per share (the "Conversion Price"). The Debentures were not redeemable on or before December 31, 2012, except on a change of control of Chorus or default under the terms of the Debentures. From December 31, 2012 to December 31, 2013, the Debentures were redeemable in whole or in part from time to time at Chorus' option at a price equal to their principal amount plus accrued interest, provided that the volume weighted average trading price for the shares is not less than 125% of the Conversion Price. Chorus did not exercise that option. On and after December 31, 2013 and prior to the Maturity Date, the Debentures may be redeemed in whole or in part from time to time at Chorus' option at a price equal to their principal amount plus accrued interest. See note 24 - Subsequent event for discussion on partial redemption. Subject to regulatory approval, Chorus may satisfy its obligation to repay the principal amount of the Debentures on redemption or at maturity, in whole or in part, by delivering that number of shares equal to the amount due divided by 95% of the market price for the shares at that time, plus accrued interest in cash. Upon issuance, the Debentures were separated into liability and conversion components for accounting purposes.

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**10 Convertible debentures (continued)**

The following table allocates the Debentures between debt and equity:

	Cost of borrowing %	Debt \$	Equity \$	Total \$
<b>As at December 31, 2011</b>	9.5	75,108	9,497	84,605
Accretion expense		1,661	—	1,661
<b>As at December 31, 2012</b>		76,769	9,497	86,266
Accretion expense		1,766	—	1,766
<b>As at December 31, 2013</b>		78,535	9,497	88,032

Transaction costs are capitalized and offset with the debt and equity portions of the debentures and amortized over the life of the debentures using the effective interest rate.

For the year ended December 31, 2013, the total interest expense on the convertible debentures was \$9,386 (2012 - \$9,281) which included interest accretion of \$1,766 (2012 - \$1,661).

**11 Income taxes**

The effective rate on Chorus' earnings before income tax differs from the expected amount that would arise using the combined Canadian Federal and Provincial statutory income tax rates. A reconciliation of the difference is as follows:

	2013 %	Year ended December 31, 2013 \$	2012 %	2012 \$
Income tax expense at the Canadian statutory tax rate	27.1	23,274	27.3	32,350
Recognition of previously unrecognized cumulative eligible capital related to:				
- current period	(12.3)	(10,583)	(9.2)	(11,026)
- prior period	—	—	(5.4)	(6,404)
Net impact of capital items <sup>(1)</sup>	8.1	6,998	(1.2)	(1,515)
Non-deductible expenses	2.8	2,386	2.0	2,376
Impact of tax rate changes and tax rate differential	2.3	1,940	2.0	2,414
Income tax expense	28.0	24,015	15.5	18,195

(1) The impact of capital items is mainly related to the foreign exchange fluctuations on the long-term debt associated with the purchase of the Q400 aircraft, of which the impact of the non-deductible (non-taxable) portion of any unrealized loss (gain) is considered in the calculation of income tax expense at the end of each period. To the extent that a capital loss is recorded for accounting purposes, the benefit of the deductible portion of the loss is recognized only to the extent that it is probable that the loss will be utilized. Chorus does not have a plan in place to utilize the deductible portion of the balance of the foreign exchange losses, accordingly no deferred tax asset has been recognized related to the foreign exchange losses. As at December 31, 2013, less than 1% of the impact of the foreign exchange fluctuations have been realized through principal repayments.

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**11 Income taxes (continued)**

In addition to the tax deductible amounts recognized as deferred tax assets in the financial statements, Chorus has other tax deductible amounts of approximately \$509,215, as at December 31, 2013, related to cumulative eligible capital. In accordance with the initial recognition exemption, as outlined in IAS 12, the benefit of these deductible expenditures cannot be recognized in the financial statements until such time that those benefits can be applied to reduce current tax expense. During the years ended December 31, 2013 and December 31, 2012, Chorus utilized a total of \$38,328 (\$10,583 tax effected) and \$63,841 (\$17,430 tax effected), respectively, of these previously unrecognized tax deductions to reduce its taxable income.

As at December 31, 2013, Chorus had \$20,363 (December 31, 2012 - \$9,594) of allowable capital losses that have not been recognized as a deferred tax asset, as Chorus has no current plan in place to utilize these losses.

**Deferred tax**

Components of the net deferred income tax asset are as follows:

	December 31, 2012 \$	Recognized in Net Income \$	Recognized in OCI \$	Charged Directly to Equity \$	December 31, 2013 \$
Deferred income tax liability					
– Deferred Partnership income	(16,540)	3,532	—	—	(13,008)
– Convertible debentures	(577)	266	—	—	(311)
– Property and equipment	(26,401)	(23,209)	—	—	(49,610)
– Pension and Other Future Employee Benefits	13,784	(6,034)	(17,138)	—	(9,388)
Deferred income tax asset					
– Loss carryforwards	21,842	3,945	—	—	25,787
– Deferred lease inducement	8,952	(1,047)	—	—	7,905
– Other long-term liabilities	1,039	1,796	—	—	2,835
<b>Net deferred income tax</b>	<b>2,099</b>	<b>(20,751)</b>	<b>(17,138)</b>	<b>—</b>	<b>(35,790)</b>

Notes to the Consolidated Financial Statements  
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**11 Income taxes (continued)**

The estimated recovery periods for the deferred tax balances are as follows:

	December 31,	
	2013	2012
	\$	\$
Deferred tax assets		
- Deferred tax assets to be recovered within 12 months	13,962	16,360
- Deferred tax assets to be recovered after more than 12 months	22,565	29,259
Deferred tax liabilities		
- Deferred tax assets to be recovered within 12 months	(6,381)	(7,801)
- Deferred tax assets to be recovered after more than 12 months	(65,936)	(35,719)
	(35,790)	2,099

**12 Pension and Other Future Employee Benefits**

Chorus maintains several registered defined contribution pension plans for eligible employees and a registered defined benefit plan for Pilots. Chorus is the plan sponsor for these plans under the Pension Benefits Standard Act, 1985 (Canada). In addition, Chorus maintains an unregistered supplemental executive retirement plan ("SERP") which is partially funded for certain employees. Contributions to the supplementary pension plan started in December 2007. The registered and supplementary defined benefit pension plans provide benefits upon retirement, termination or death based on the member's years of service and the final average earnings for a specified period.

Chorus also maintains Other (non-pension) Future Employee Benefits. The Other Future Employee Benefits include medical and dental benefits provided to the employees on long-term disability and Workplace Safety Insurance Board ("WSIB"). These benefits cease to be provided when the employee reaches age 65. The sick leave gratuity benefits represent the payout of sick leave accruals upon or just prior to retirement for eligible employees. The self-insured WSIB benefits are in respect of self-insured benefits provided to Ontario employees.

The total expense for Chorus' defined contribution plans including two pension plans sponsored by an employee group and a union respectively, for which Chorus is obligated to make defined contributions only, for the year ended December 31, 2013 is \$9,076, and for the year ended December 31, 2012 is \$9,117.

Expected contributions to the defined benefit pension plans for the year ending December 31, 2014 are \$28,600. Expected contributions to the defined contribution pension plans for the year ending December 31, 2014 are \$9,700. Expected benefit payments for Other Future Employee Benefits for the year ending December 31, 2014 are \$1,270.

The Company is the legal administrator of the plans and is responsible for its overall management of the plan. Responsibility for the governance of the plans, including investment decisions lies with the Company and the Board of Directors.

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**12 Pension and Other Future Employee Benefits (continued)**

The most recent actuarial valuations of the defined pension benefit plans for funding purposes were as of January 1, 2013 and the next funding valuation will be as of January 1, 2014.

Information about Chorus' defined benefit plans and Other Future Employee Benefits in aggregate, is as follows:

	Pension Benefits		Other Future Employee Benefits	
	2013 \$	2012 \$	2013 \$	2012 \$
<b>Change in benefit obligation</b>				
Benefit obligation, beginning of year	281,960	213,489	16,398	15,453
Current service cost	23,934	17,445	2,297	2,329
Interest cost	13,693	12,847	578	608
Plan participants' contributions	7,930	8,150	—	—
Benefits paid	(21,951)	(5,253)	(1,588)	(1,252)
(Gain)/loss from change in demographic assumptions	4,327	(36,793)	(120)	(1,131)
(Gain)/loss from change in financial assumptions	(38,045)	69,358	(760)	(264)
Experience (gains)/losses	(2,223)	2,717	(4,019)	655
<b>Benefit obligation, end of year</b>	<b>269,625</b>	<b>281,960</b>	<b>12,786</b>	<b>16,398</b>
<b>Change in plan assets</b>				
Fair market value of plan assets, beginning of year	246,232	194,670	—	—
Interest income	11,596	11,598	—	—
Employer contribution	36,514	34,542	1,588	1,252
Plan participants' contributions	7,930	8,150	—	—
Benefits paid	(21,951)	(5,253)	(1,588)	(1,252)
Administrative expenses	(400)	(300)	—	—
Return on plan assets (excluding interest income)	26,534	2,825	—	—
<b>Fair market value of plan assets, end of year</b>	<b>306,455</b>	<b>246,232</b>	<b>—</b>	<b>—</b>
<b>Funded status, end of year</b>	<b>36,830</b>	<b>(35,728)</b>	<b>(12,786)</b>	<b>(16,398)</b>
<b>Accrued contributions</b>	<b>549</b>	<b>605</b>	<b>—</b>	<b>—</b>
<b>Accrued benefit asset (liability)</b>	<b>37,379</b>	<b>(35,123)</b>	<b>(12,786)</b>	<b>(16,398)</b>

Notes to the Consolidated Financial Statements  
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**12 Pension and Other Future Employee Benefits (continued)**

The table below outlines where the defined benefit pension and Other Future Employee Benefits amounts are included in the statements of financial position.

	December 31,	
	2013	2012
<b>Assets</b>		
Defined benefit pension	37,379	7,509
<b>Liabilities</b>		
Defined benefit pension	—	42,632
Other Future Employee Benefits	12,786	16,398
	12,786	59,030

Plan assets are comprised as follows:

	December 31,	
	2013	2012
Canadian Equity	17%	32%
Universe Bonds	30%	43%
Long Bonds	7%	—%
International Equity	40%	20%
Short-term and Other	4%	4%
Real Estate	2%	1%
	100%	100%

The plan's assets are invested in Canadian bonds, equities and real estate and foreign equities. The balanced fund was unwound in 2012. These assets include no significant investment in Chorus at the measurement date.

Notes to the Consolidated Financial Statements  
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**12 Pension and Other Future Employee Benefits (continued)**

Weighted average assumptions used to determine the accrued benefit liability:

	Pension Benefits		Other Future Employee Benefits	
	2013	2012	2013	2012
Discount rate to determine accrued benefit obligations	5.0%	4.4%	4.4%	3.7%
Discount rate to determine the pension and benefit cost	4.4%	5.4%	3.7%	4.3%
Rate of compensation increase	4.5%	4.5%	2.3%	2.6%
Health care inflation - Select to determine accrued benefit obligation	n/a	n/a	6.3%	6.4%
Health care inflation - Select to determine pension and benefit cost	n/a	n/a	6.4%	6.1%

The health care inflation assumption was graded down in and after 2030 to 4.5% per annum

Assumptions regarding future mortality are set based on actuarial advice with statistics published by the Canadian Institute of Actuaries. The assumptions translate into an average life expectancy in years for a pensioner retiring at age 65 as follows:

	2013	2012
Retiring at the end of the reporting period		
Male	21.2	19.7
Female	23.4	22.1
Retiring 20 years after the end of the reporting period		
Male	22.3	21.2
Female	24.2	22.9



## Notes to the Consolidated Financial Statements For the years ended December 31, 2013 and 2012

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### 12 Pension and Other Future Employee Benefits (continued)

The defined benefit pension plan and Other Future Employee Benefits produce exposure to a number of risks, the most significant of which are detailed below:

#### **Asset Volatility**

For a defined benefit pension plan, fluctuations in the value of plan assets are assessed in the context of fluctuations in the plan liabilities. The plan liabilities are calculated using a discount rate set with reference to high quality corporate bond yields. As discount rates change, the value of the plan liabilities will fluctuate. If the growth of plan liabilities exceeds that of plan assets a deficit will result. The plan currently holds a significant proportion of equities, which are expected to outperform corporate bonds in the long-term but which provide volatility and risk in the short-term. The plan's investment time horizon is a key input in deciding on the proportion of equities held.

Given the long-term nature of the defined benefit pension plan, the current level of equity investment is an appropriate element of the long-term strategy to manage the defined benefit plan efficiently. Based on a comprehensive asset-liability study completed in late 2011, the plan's investment policy was revised in 2012 to:

- Reduce equity content
- Improve the equity portfolio's diversification
- Reduce interest rate risk over time
- Expand investments to include a diversified real estate allocation

#### **Interest rate risk**

The discount rate used to determine benefit obligations was determined by reference to the market interest rates on corporate bonds rated "AA" or higher, with cash flows that approximate the timing and amount of the expected benefit payments. A decrease in corporate bond yields will increase plan liabilities, although this will be partially offset by an increase in the value of the pension plans' bond holdings.

#### **Salary risk**

The present value of the benefit obligations is calculated by reference to the future salaries of plan participants, so salary increases of the plan participants greater than assumed will increase plan liabilities.

#### **Life expectancy**

The majority of the plans' obligations are to provide benefits for the life of the member, so increases in life expectancy will result in an increase in the plans' liabilities.

Each sensitivity analysis disclosed in this note is based on changing one assumption while holding all other assumptions constant. In practice, this is unlikely to occur, and changes in some of the assumptions may be correlated. When calculating the sensitivity of the defined benefit obligation to variations in significant actuarial assumptions, the same method (present value of the defined benefit obligation calculated with the projected unit credit method at the end of the reporting period) has been applied as for calculating the liability recognized in the statement of financial position.

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**12 Pension and Other Future Employee Benefits (continued)**

The sensitivity of the defined benefit obligation to changes in assumptions is on the pension plans as follows:

	Change in assumption	Impact on defined benefit obligation	
		Increase in assumption	Decrease in assumption
Discount rate	0.25%	Decrease by 3.2%	Increase by 3.5%
Compensation increase rate	0.25%	Increase by 1.1%	Decrease by 1.0%
Life expectancy	1 year	Increase by 1.9%	Decrease by 2.0%

The sensitivity of the defined benefit obligation to changes in assumptions on Other Future Employee Benefits is as follows:

	Change in assumption	Impact on defined benefit obligation	
		Increase in assumption	Decrease in assumption
Discount rate	0.25%	Decrease by 1.8%	Increase by 1.8%
Compensate increase rate	0.25%	Increase by 0.9%	Decrease by 0.9%
Health care cost trend rate	1.0%	Increase by 3.9%	Decrease by 3.6%

The weighted duration of the pension plans and Other Future Employee Benefits is 15 and 7.5 years, respectively.

Expected maturity analysis of undiscounted defined benefit pension and Other Future-Employment Benefit payments are as follows:

	Less than 1 year	2 - 3 years	3 - 5 years	Next 5 years	Total
Defined benefit pension	12,710	27,930	34,380	137,460	212,480
Other Future Employee Benefits	1,270	1,914	1,748	4,134	9,066
	13,980	29,844	36,128	141,594	221,546

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**12 Pension and Other Future Employee Benefits (continued)**

Chorus' net defined benefit pension plan and Other Future Employee Benefits expense recognized in the consolidated statements of income and consolidated statements of comprehensive income is as follows:

	Pension		Other Future Employee Benefits	
	2013 \$	2012 \$ (revised - note 3)	2013 \$	2012 \$
Components of cost under IAS 19				
Amounts recognized in profit or loss:				
Current service cost	23,934	17,445	2,297	2,329
Interest cost on benefit obligation	13,693	12,847	578	608
Administrative expenses	400	300	—	—
Interest income on plan assets	(11,596)	(11,600)	—	—
Costs arising in the period	26,431	18,992	2,875	2,937
Remeasurements recognized in the consolidated statements of income	—	—	(4,643)	397
	26,431	18,992	(1,768)	3,334
Remeasurements recognized in other comprehensive income				
Loss (gain) on demographic assumptions	4,327	(36,793)	12	(1,132)
(Gain) loss from financial assumptions	(38,045)	69,358	(268)	(6)
Experience (gains) losses	(2,223)	2,717	—	—
(Return) on plan assets (excluding interest income)	(26,534)	(2,825)	—	—
(Gain) loss recognized in the statement of other comprehensive income for the period <sup>(1)</sup>	(62,475)	32,457	(256)	(1,138)

(1) There is no impact on the minimum funding requirements for pensions in 2013 or 2012.

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**12 Pension and Other Future Employee Benefits (continued)**

The funding of employee benefit as compared to the expense recorded in the consolidated statements of income is summarized in the table below:

	Year ended December 31,	
	2013	2012
<b>Net defined benefit pension and Other Future Employee Benefits expense recorded in the consolidated statements of income</b>		
Wages, salaries and benefits	24,663	22,328
<b>Employee benefit funding by Chorus</b>		
Defined benefit pension	36,514	34,542
Other Future Employee Benefits	1,588	1,252
	38,102	35,794
<b>Employee benefit funding greater than expense</b>	(13,439)	(13,466)

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### 13 Dividends

On May 9, 2013, Chorus reduced its quarterly dividend from \$0.15 per share to \$0.075 per share. Chorus declared \$50,880 in dividends for the year ended December 31, 2013 (\$74,408 for the year ended December 31, 2012). Cash dividends paid for the year ended December 31, 2013 was \$55,696 (\$74,408 for the year ended December 31, 2012).

On December 10, 2013, Chorus increased its quarterly dividend from \$0.075 per share to \$0.1125 per share.

### 14 Capital stock

#### Capital stock

##### a) Authorized:

- An unlimited number of Class A Variable Voting Shares, no par value ("Variable Voting Shares"); and
- An unlimited number of Class B Voting Shares, no par value ("Voting Shares")

##### Issued and outstanding:

	Number of Shares <sup>(1)</sup>	\$
Shares reported in equity December 31, 2011	123,540,555	1,572
Shares released from the stock-based compensation plan <sup>(2)</sup>	474,916	2,056
Shares issued and outstanding December 31, 2012	124,015,471	3,628
Shares issued <sup>(3)</sup>	398,355	1,566
Shares repurchased <sup>(4)</sup>	(1,871,800)	(78)
Shares issued and outstanding December 31, 2013	122,542,026	5,116

- 1) References to "Shares" above are inclusive of Variable Voting Shares and Voting Shares. As at December 31, 2013, Chorus had 4,789,193 Variable Voting Shares (December 31, 2012 - 15,472,846) and 117,752,833 Voting Shares (December 31, 2012 - 108,542,625).
- 2) As Shares from the stock-based compensation plan vested, they were released from a trust into capital at the weighted average cost on date of grant.
- 3) On February 25, 2013 Chorus issued 398,355 Voting Shares to satisfy the vesting of the stock-based compensation plans. The shares were issued at market price at closing on the day of issuance, net of the amount Chorus paid in withholding taxes on behalf of the employees.
- 4) On March 14, 2013, Chorus announced that it had received approval from the Toronto Stock Exchange to make a normal course issuer bid to purchase up to 11,093,612 Shares during the period March 18, 2013 to no later than March 17, 2014. From April 1 to December 31, 2013, Chorus repurchased and cancelled 1,871,800 Shares under its normal course issuer bid at an aggregate cost of \$4,006. Share capital was reduced by \$78 and the remaining \$3,928 was accounted for as a reduction of contributed surplus.

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**14 Capital stock (continued)**

The common shares issuable by Chorus consist of an unlimited number of Variable Voting Shares and an unlimited number of Voting Shares. The two classes of common shares have equivalent rights as common shareholders except for voting rights. Holders of Variable Voting Shares are entitled to one vote per share unless (i) the number of Variable Voting Shares outstanding, as a percentage of the total number of voting shares of Chorus exceeds 25% or, (ii) the total number of votes cast by or on behalf of holders of Variable Voting Shares at any meeting exceeds 25% of the total number of votes that may be cast at such meeting. If either of the above noted thresholds would otherwise be surpassed at any time, the vote attached to each Variable Voting Share will decrease proportionately such that, (i) the Variable Voting Shares as a class do not carry more than 25% of the aggregate votes attached to all issued and outstanding voting shares of Chorus, and (ii) the total number of votes cast by or on behalf of holders of Variable Voting Shares at any meeting do not exceed 25% of the votes that may be cast at such meeting.

Variable Voting Shares are to be held, beneficially owned or controlled, directly or indirectly, by persons who are not Canadians within the meaning of the Canada Transportation Act. An issued and outstanding Variable Voting Share shall be converted into one Voting Share automatically and without any further act of Chorus or the holder, if such Variable Voting Share becomes held, beneficially owned and controlled, directly or indirectly, otherwise than by way of security only, by a Canadian, as defined in the Canada Transportation Act.

Voting Shares are to be held, beneficially owned and controlled, directly or indirectly, by Canadians. An issued and outstanding Voting Share shall be converted into one Variable Voting Share automatically and without any further act of Chorus or the holder, if such Voting Share becomes held, beneficially owned or controlled, directly or indirectly, otherwise than by way of security only, by a person who is not a Canadian.

b) Earnings per share

The following table provides a breakdown of the numerator and denominator used in the calculation of earnings per share and diluted earnings per share.

	2013 \$	2012 \$
<b>Numerator</b>		
Income	61,866	100,223
Interest expense on convertible debentures, net of tax	7,304	7,193
Diluted income	69,170	107,416
<b>Denominator</b>		
Weighted average number of shares	123,389,502	123,946,699
Weighted average convertible debenture dilutive shares	15,278,095	15,278,095
Weighted average number of diluted shares	138,667,597	139,224,794

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**14 Capital stock (continued)**

In 2012, the Jazz LTIP shares held in trust were anti-dilutive and excluded from diluted earnings per share.

c) Stock-based compensation

The details of shares held in trust under stock-based compensation plans discussed in note 3 are as follows:

	<b>December 31, 2012 Jazz LTIP</b>
Number of shares granted	995,892
Number of shares forfeited	(184,322)
	811,570
Number of shares vested	(811,570)
Number of shares outstanding, end of year	—
Weighted average remaining life (years)	—
Cost of shares purchased during the year <sup>(1)</sup>	\$nil
Weighted average fair value per share on date of grant	\$nil

(1) Commencing with the 2010 grant, shares were granted notionally, rather than purchased on the open market at time of grant.

During the year ended December 31, 2013, Chorus notionally granted 710,306 shares under the Chorus LTIP (2012 - 667,703 shares).

Total compensation expense related to stock-based compensation (including the Chorus LTIP, the DSU Plan and the ESOP) during 2013 was \$6,303 (2012 - \$5,712).

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**15 Commitments**

Chorus is committed to the following future minimum lease payments under operating leases for flight equipment and base facilities that have initial non-cancellable terms in excess of one year. The majority of these lease agreements are renewable at the end of the lease period, at market rates.

	<b>December 31, 2013</b>	
	<b>Other third parties</b>	<b>Air Canada and its subsidiary</b>
	<b>\$</b>	<b>\$</b>
No later than one year	13,024	84,352
Later than one year and no later than five years	23,021	284,880
Later than five years	15,339	277,345

A significant portion of the minimum lease payments for aircraft are payable in US dollars and have been converted to Canadian currency at \$1.0636, which was the exchange rate in effect at the end of day closing on December 31, 2013 (2012 - \$0.9949).

Certain of the aircraft lease agreements have been entered into by Air Canada Capital Ltd. or Air Canada with head lessors and subleased to Chorus. Future minimum lease payments that will arise under these leases are listed in the above table under the heading "Air Canada and its subsidiary".

In 2007 and 2010, Chorus entered into common terms agreements ("CTAs") with aircraft lessors which govern three of Chorus' aircraft leases and which will also apply to any future aircraft leases with the same lessors. As at December 31, 2013, Chorus was in compliance with the tangible asset disposal covenants contained in these CTAs.



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**16 Financial instruments and fair values**

Chorus' financial instruments consist of cash and cash equivalents, accounts receivable, long-term investment, ABCP, accounts payable and accrued liabilities, obligations under finance leases, long-term debt and convertible debentures.

**Measurement categories**

As explained in note 3 (i), financial assets and liabilities have been classified into categories that determine their basis of measurement and, for items measured at fair value, whether changes in fair value are recognized in the statement of income or comprehensive income. Those categories are: fair value through profit or loss; fair value through other comprehensive income; and amortized cost. The following table shows the carrying and fair values of assets and liabilities for each of these categories at December 31, 2013 and December 31, 2012.

	December 31, 2013		December 31, 2012	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
	\$	\$	\$	\$
<b>Financial assets</b>				
Financial assets measured at amortized cost				
Cash and cash equivalents	159,901	159,901	118,306	118,306
Restricted cash	3,320	3,320	6,017	6,017
Restricted cash included in other assets	6,208	6,208	—	—
Accounts receivable <sup>(1)</sup>	73,822	73,822	75,396	75,396
Fair value through profit and loss				
Asset backed commercial paper	1,231	1,231	1,003	1,003
<b>Financial liabilities</b>				
Other financial liabilities, carried at amortized cost				
Accounts payable and accrued liabilities <sup>(1)</sup>	192,704	192,704	190,898	190,898
Dividends payable	13,786	13,786	18,602	18,602
Long-term debt	402,799	392,172	277,446	286,656
Obligations under finance leases	6,429	6,429	8,889	8,889
Convertible debentures	78,535	79,132	76,769	79,034

(1) Assets and liabilities, such as commodity taxes, that are not contractual and that arise as a result of statutory requirements imposed by governments, do not meet the definition of financial assets or financial liabilities and are therefore excluded.

## Notes to the Consolidated Financial Statements For the years ended December 31, 2013 and 2012

(expressed in thousands of Canadian dollars, except shares and earnings per share)

### 16 Financial instruments and fair values (continued)

#### Fair value of financial instruments

The carrying amounts reported in the statement of financial position for cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities, and dividends payable approximate fair values based on the immediate or short-term maturities of these financial instruments. The methods and assumptions used in estimating the fair value of other financial assets and liabilities are as follows:

- ABCP

The ABCP classified as level three is a financial security that currently has no active trading market. Valuation is done based on limited available market information, maturity dates and expected return of capital on a discounted basis. During the year ended December 31, 2013, a valuation gain of \$412 (2012 - \$450) was recorded.

- Long-term debt

At December 31, 2013, the fixed rate term loans had a fair value of \$392,172. The fair values were calculated by discounting the future cash flow of the respective long-term debt at the estimated yield to maturity of similar debt instruments.

- Finance leases

The repayment terms that Chorus is committed to make have been discounted at the relevant market interest rates applicable at year end. Interest rates used to calculate fair value are based on the change in the risk-free rate at December 31, 2013, compared to the risk-free rates at the inception of the leases.

- Convertible debentures

Chorus' convertible debentures are listed on the Toronto Stock Exchange and the fair value was determined using the closing price on the last trading day of the year.

#### Fair value hierarchy

Financial instruments 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 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; quoted prices for identical or similar instruments in markets that are not active; 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.

Notes to the Consolidated Financial Statements  
For the years ended December 31, 2013 and 2012

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**16 Financial instruments and fair values (continued)**

A financial instrument is classified to the lowest level of the hierarchy for which a significant input has been considered in measuring fair value.

The following table presents the financial instruments recorded at fair value in the consolidated balance sheet, classified using the fair value hierarchy described above:

	2013 \$	2012 \$
<b>Level 3</b>		
Asset backed commercial paper	1,231	1,003

The following table presents the changes in level 3 instruments by class of asset for the years ended December 31, 2013 and 2012.

	2013 \$	2012 \$
Start of year	1,003	17,091
Payments received	(184)	(187)
Loss recognized in other comprehensive income (note 21)	—	(16,351)
Gains recognized in profit or loss	412	450
	1,231	1,003

**Financial risk factors**

Chorus, through its financial assets and liabilities, has exposure to the following risks from its use of financial instruments: interest rate risk, credit risk, liquidity risk and currency risk. Senior management monitors risk levels and reviews risk management activities as they determine to be necessary.

*Interest rate risk*

Investments included in Chorus' cash and cash equivalents earn interest at prevailing and fluctuating market rates, as Chorus' objective is to maintain these balances in highly liquid investments. As at December 31, 2013, Chorus' investments consisted of bankers acceptances and bankers deposit notes issued by a Schedule 1 Bank.

The 25 term loans with EDC and the Nova Scotia Jobs Fund loan bear fixed interest rates. The debt is therefore not subject to interest rate volatility.

A 1% change in the interest rate would not have a significant impact on the net income of Chorus.

Notes to the Consolidated Financial Statements  
For the years ended December 31, 2013 and 2012

(expressed in thousands of Canadian dollars, except shares and earnings per share)

**16 Financial instruments and fair values (continued)**

*Credit risk*

Credit risk arises from cash and cash equivalents, restricted cash, deposits, as well as credit exposure to customers, including outstanding receivables. Chorus manages the credit risk on cash and cash equivalents by ensuring that the counter-parties are governments, banks and corporations with high credit-ratings assigned by international credit-rating agencies. In accordance with its investment policy, Chorus invests excess cash in Government of Canada treasury bills, short-term Canadian and provincial government debt, bankers' acceptance notes, term deposits of Schedule 1 Banks and Schedule 2 Banks rated R-1 high, and commercial paper rated R-1 high.

The maximum exposure to credit risk for cash and cash equivalents, restricted cash, deposits and trade and other receivables approximate the amount recorded on the statement of financial position.

With the exception of trade receivables, Chorus has no financial assets past due. As at December 31, 2013, the total amount of trade receivables was \$59,733 (2012 - \$61,883), net of allowance for bad debts, which has been estimated by management based on prior experience and its assessment of the current economic environment and the specific debtor. The amount of this allowance was \$nil (2012 - \$nil). At December 31, 2013, trade receivables of \$59,373 (2012 - \$59,786) were not past due or impaired; \$360 (2012 - \$2,097) were past due, but not impaired; and \$nil (2012 - \$nil) were impaired. The aging of the latter two categories is as follows:

	<b>2013</b>	<b>2012</b>
	<b>\$</b>	<b>\$</b>
Past due but not impaired		
60 - 90 days	153	343
Over 90 days	207	1,754
	<b>360</b>	<b>2,097</b>
Impaired		
60 - 90 days	—	—
Over 90 days	—	—
	<b>—</b>	<b>—</b>

Chorus continues to work with the entities from which it holds past due receivables to recover the full amount outstanding. Approximately \$58,682 (2012 - \$58,495) of the total receivables are with one company, Air Canada. Accordingly, Chorus is directly affected by the financial and operational strength of Air Canada. Chorus does not believe it is subject to any significant concentration of credit risk other than with Air Canada.

*Liquidity risk*

Cash flow forecasting is performed in respect of each operating entity of Chorus and then aggregated. Chorus monitors rolling forecasts of Chorus' liquidity requirements. Such forecasts take into consideration Chorus' operational cash flow requirement, debt financing plans and compliance with internal balance sheet ratio targets.

Notes to the Consolidated Financial Statements  
For the years ended December 31, 2013 and 2012

(expressed in thousands of Canadian dollars, except shares and earnings per share)

**16 Financial instruments and fair values (continued)**

Chorus' objective is to maintain sufficient liquidity to meet liabilities when due. Chorus monitors its cash balances and cash flows generated from operations to meet its liquidity requirements.

The tables below analyze Chorus' non-derivative financial liabilities into relevant maturity groupings based on the remaining period from the statement of financial position date to the contractual maturity date. The amounts disclosed in the table are the contractual undiscounted cash flows. The analysis is based on foreign exchange in effect at the consolidated statement of financial position date, and contractual interest rates, and includes both principal and interest cashflows for long-term debt, obligations under finance leases and convertible debentures.

	December 31, 2013			
	Less than 3 months \$	3 months to 1 year \$	2 - 5 years \$	Over 5 years \$
<b>Principal</b>				
Trade payables and accrued liabilities <sup>(1)</sup>	189,300	—	—	—
Finance leases	811	2,545	3,073	—
Long-term debt	7,319	24,035	139,591	231,854
Convertible debentures	60,000	20,210	—	—
	257,430	46,790	142,664	231,854
<b>Interest</b>				
Finance leases	136	299	128	—
Long-term debt	3,129	10,313	42,495	25,273
Convertible debentures	1,129	1,440	—	—
	4,394	12,052	42,623	25,273

	December 31, 2013			
	Less than 3 months \$	3 months to 1 year \$	2 - 5 years \$	Over 5 years \$
<b>Total principal and interest</b>				
Trade payables and accrued liabilities <sup>(1)</sup>	189,300	—	—	—
Finance leases	947	2,844	3,201	—
Long-term debt	10,448	34,348	182,086	257,127
Convertible debentures	61,129	21,650	—	—
	261,824	58,842	185,287	257,127

(1) Excludes commodity taxes and deferred lease inducements as they do not meet the definition of a financial liability. Debenture interest is included in convertible debentures within the table.

## Notes to the Consolidated Financial Statements For the years ended December 31, 2013 and 2012

(expressed in thousands of Canadian dollars, except shares and earnings per share)

### 16 Financial instruments and fair values (continued)

#### *Currency risk*

Chorus receives revenue and incurs expenses in US and Canadian currency, and as a result, is subject to fluctuations as foreign exchange rates fluctuate. Chorus manages its exposure to currency risk by billing for its services within the CPA in the underlying currency related to the expenditure. Accordingly, the primary exposure results from balance sheet fluctuations of US denominated cash, accounts receivable, accounts payable, and in particular, obligations under finance leases and long-term debt, which are long-term and so are subject to larger unrealized gains or losses. Chorus mitigates this currency risk by maintaining a balance of US dollars which is used to pay down US denominated liabilities and replenishes the balance through US denominated revenues. The amount of US dollar denominated assets was \$78,474 and US denominated liabilities was \$413,988 at December 31, 2013. A 1¢ change in the US exchange rate would result in a change in the unrealized gain or loss of approximately \$3,355.

### 17 Contingencies

The Canada Business Corporations Act, as amended (the "CBCA") provides that the Directors will act honestly and in good faith with a view to the best interest of Chorus and, in connection with that duty, will exercise the degree of care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances. The CBCA and bylaws of Chorus provide that each Director will be entitled to indemnification from Chorus in respect of the exercise of the Director's power and the discharge of the Director's duties, provided that the Director acted honestly and in good faith with a view to the best interests of all shareholders, or in the case of a criminal or administrative action proceeding that is enforced by a monetary penalty, where the Director had reasonable grounds for believing that his/her conduct was lawful. Chorus and its subsidiaries have agreed to indemnify their respective directors and officers against certain costs and damages incurred by the directors and officers as a result of lawsuits or any other judicial, administrative or investigative proceeding in which the directors and officers are sued as a result of their service. The directors and officers are covered by directors' and officers' liability insurance. No claims with respect to such occurrences have been made and, as such, no amount has been recorded in these financial statements with respect to these indemnifications.

Various other lawsuits and claims that have arisen in the normal course of business are pending by and against Chorus. The provisions that have been recorded are not material. It is the opinion of management that final determination of these claims will not have a material adverse effect on the financial position or the results of Chorus.

Chorus enters into various operating agreements and real estate licenses or leases, which in some cases permit Chorus to use certain premises and/or operate at certain airports, and which in other cases lease space in Chorus' facilities to its tenants. It is common in such commercial license or lease transactions for the licensee or tenant to agree to indemnify the landlord for tort liabilities that arise out of or relate to its use or occupancy of the licensed or leased premises. In certain cases, this indemnity extends to related liabilities arising from the negligence of the indemnified parties, but generally excludes any liabilities caused by their gross negligence or willful misconduct. In addition, the licensee or tenant, as the case may be, typically indemnifies the landlord for any environmental liability that arises out of or relates to its use or occupancy of the leased or licensed premises.

Notes to the Consolidated Financial Statements  
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(expressed in thousands of Canadian dollars, except shares and earnings per share)

**17 Contingencies (continued)**

In aircraft and engine financing or leasing agreements, Chorus typically indemnifies the financing parties, directors acting on their behalf and other related parties and/or lessors against liabilities that arise from the manufacture, design, ownership, financing, use, operation and maintenance of the aircraft and engines and for tort liability, whether or not these liabilities arise out of or relate to the negligence of these indemnified parties, but generally excludes any liabilities caused by their gross negligence or willful misconduct. In addition, in aircraft and engine financing or leasing transactions, including those structured as leveraged leases, Chorus typically provides indemnities in respect of certain tax consequences.

When Chorus, as a customer, enters into technical service agreements with service providers, primarily service providers who operate an airline as their main business, Chorus has from time to time agreed to indemnify the service provider against liabilities that arise from third party claims, whether or not these liabilities arise out of or relate to the negligence of the service provider, but generally excluding liabilities that arise from the service provider's gross negligence or willful misconduct.

**18 Related parties**

**Compensation of key management**

Key management includes Chorus' Directors, President and Chief Executive Officer, Chief Operating Officer, Chief Financial Officer and Chief Administrative Officer. Compensation awarded to key management is summarized as follows:

	Year ended December 31,	
	2013	2012
	\$	\$
Salaries and other benefits	4,273	3,309
Other post-employment benefits	110	2,299
Stock-based compensation	1,771	1,449
	6,154	7,057

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**19 Economic dependence**

The transactions between Air Canada and its subsidiary (Air Canada Capital Ltd.) and Chorus are summarized in the table below:

	2013 \$	2012 \$
<b>Operating revenue</b>		
Air Canada	1,649,581	1,646,402
<b>Operating expenses</b>		
Air Canada	72,369	79,617
Air Canada Capital Ltd.	80,226	78,094

The following balances with Air Canada and its subsidiary (Air Canada Capital Ltd.) are included in the financial statements:

	2013 \$	2012 \$
<b>Accounts receivable</b>		
Air Canada	58,682	58,495
<b>Accounts payable and accrued liabilities</b>		
Air Canada	60,403	65,816
Air Canada Capital Ltd.	7,768	7,336

**The CPA**

Chorus provides a significant part of Air Canada's domestic and transborder network. Chorus is economically and commercially dependent upon Air Canada and certain of its subsidiaries, as, in addition to being Chorus' primary source of revenue, these entities currently provide significant services to Chorus. Chorus and Air Canada are parties to the CPA, under which Air Canada currently purchases the greater part of Chorus' fleet capacity on aircraft operated by Chorus (the "Covered Aircraft") at predetermined rates (the "Rates").

The arrangements under the CPA are based upon a number of variable components based on certain different metrics, including Block Hours flown, flight hours, cycles (number of take-offs and landings), number of passengers and number of Covered Aircraft. The rates for these metrics are fixed for annual periods and vary by aircraft type. In addition, Air Canada is required to reimburse Chorus for certain pass-through costs, including fuel, deicing, navigation, landing and terminal fees, station provisioning costs, station termination costs, passenger liability insurance and certain employee relocation costs. Since these costs are required to operate the Covered Aircraft, the reimbursement of these costs is included in Chorus' revenue. Chorus also has the ability to earn certain performance incentive payments on a quarterly basis related to on-time performance, controllable flight completion, baggage handling performance and other customer satisfaction criteria.



## Notes to the Consolidated Financial Statements For the years ended December 31, 2013 and 2012

(expressed in thousands of Canadian dollars, except shares and earnings per share)

### 19 Economic dependence (continued)

#### Benchmarking Process

The CPA provides that Controllable Mark-Up may be reduced as a result of benchmarking Chorus' Controllable Costs to those of a group of specified comparable operators (the "Comparable Operators") using publicly available information. Under the CPA, this benchmarking was effected in 2010 (based on information from Chorus' 2009 calendar year - the "2009 Benchmark") and is to be again in 2016 (using information from Chorus' 2015 calendar year - the "2015 Benchmark"). If the 2009 Benchmark revealed that the percentage difference between Chorus' Unit Costs and the median controllable unit costs, stage length adjusted, of the Comparable Operators had increased compared to the percentage difference of these costs for the twelve-month period beginning July 1, 2006 and ending June 30, 2007, the Controllable Mark-up was to be reduced accordingly with effect as of January 1, 2010 until December 31, 2020 (unless as a result of the 2015 Benchmark it is further reduced) to the lower of 12.50% or the percentage that is equal to 16.72% minus the change in Controllable Mark-up resulting from the 2009 Benchmark. If the 2015 Benchmark indicates that percentage difference between Chorus' Unit Costs and the median controllable unit costs, stage length adjusted, of the Comparable Operators has increased compared to the percentage difference determined during the 2009 Benchmark, the Controllable Mark-Up then in effect shall be reduced based on the results of the 2015 Benchmark, with effect as of January 1, 2016 until December 31, 2020. The comparison of Chorus' Unit Costs to the median controllable unit costs of the Comparable Operators, stage length adjusted, shall be subject to adjustments required to reflect the differences between Chorus and each Comparable Operator for matters such as fleet type and size, aircraft utilization, currency, geographical deployment and growth relative to Chorus. These adjustments are necessary to facilitate a reasonable and fair comparison of unit costs.

Chorus and Air Canada were unable to reach an agreement in 2010 on the results of the 2009 Benchmark and as a result, on February 3, 2011, Chorus and Air Canada agreed to proceed to binding arbitration (the "Arbitration"). The hearing of the Arbitration occurred in June 2012. Subsequent to the hearing, the parties exchanged written submissions and their reply submissions. On October 2 and 3, 2012, the Arbitration panel (the "Panel") released its initial award (the "Initial Award").

In the Initial Award, two of the three member Panel concluded that the component unit cost driver methodology put forward by Air Canada was the appropriate methodology to use in the 2009 Benchmark to compare Chorus' Unit Costs to the stage length adjusted median controllable unit costs of the Comparable Operators. However, the Panel also agreed with Chorus that a number of the additional normalizations and adjustments proposed by Chorus were also required to be made (the "Adjustments") but did not provide guidance on the calculation of the impact of such Adjustments on the Controllable Mark-Up. The Panel also agreed with Chorus that fleet age impacts the rate at which maintenance costs increase. The Panel directed Air Canada and Chorus to negotiate a further adjustment that would account for the impact of fleet age on the rate at which maintenance costs increase (the "Fleet Age Adjustment"), failing which the parties were to submit new proposals and analysis to the Panel on that issue.

The parties were unable to reach agreement on the calculation of certain of the Adjustments or on the Fleet Age Adjustment. As a result, the parties scheduled a further hearing with the Panel to occur in the last week of November 2012 to resolve the outstanding issues in dispute. That hearing was subsequently adjourned to the first week of April 2013 in order to provide the parties with additional time to put forward evidence on the issues which remained in dispute. The April 2013 hearing occurred, but the parties were unable to complete the evidence within the time available. As a result, further hearings were held in July 2013 and final written and oral arguments occurred in September 2013.

On November 25, 2013, Chorus received the Panel's final award (the "Final Award") confirming acceptance of Chorus' position on each of the remaining adjustments in dispute, including Chorus' position that differences in fleet type and size between it and the Comparable Operators required adjustments to the Comparable Operators' airframe and component (but not engine) maintenance costs. As a result of the Final Award, the 2009 Benchmark will not result in changes to the 12.5% Controllable Mark-Up.

## Notes to the Consolidated Financial Statements For the years ended December 31, 2013 and 2012

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(expressed in thousands of Canadian dollars, except shares and earnings per share)

### 19 Economic dependence (continued)

#### **Minimum Average Daily Utilization Guarantee ("MADUG")**

On June 21, 2012, Chorus and Air Canada agreed to amend the CPA to support the continued fleet renewal program with the acquisition of six additional Q400 aircraft and the removal of nine CRJ aircraft from the Chorus fleet. Pursuant to this agreement, the number of Covered Aircraft was reduced from 125 to 122. The June 6, 2013 CPA Amending Agreement finalized the details of the changes. Effective February 2013, the Annual Minimum Block Hours of 339,000 Block Hours was reduced to 331,106 Block Hours to reflect the reduced number of Covered Aircraft. The amendments did not change the Controllable Mark-Up or rates, but established certain new metrics. The Compensating Mark-Up will now be applied based on the range between the reduced Annual Delivered Block Hours of 367,106 and the revised Annual Minimum Block Hours of 331,106 Block Hours. These agreements also resolved one of the issues raised in the 2009 Benchmark Arbitration regarding the manner in which the Compensating Mark-Up formula would be applied.

The 331,106 Annual Minimum Block Hours is calculated based on the MADUG for each individual aircraft type within the fleet based on the number of Covered Aircraft for each scheduled period. There are currently two schedule periods: Winter (from approximately November 1 to March 31) and Summer (from approximately April 1 to October 31) (each a "Schedule Period").

At the end of each Schedule Period, a reconciliation from the previous Schedule Period is prepared by Chorus and is provided to Air Canada. In the event Air Canada goes below the MADUG on any aircraft type, Chorus is entitled to be paid by Air Canada for the shortfall for that period.

#### **Compensating Mark-Up**

In the event the Annual Delivered Block Hours fall below 367,106, the Compensating Mark-Up formula contained in the CPA will be applied and the Controllable Mark-Up will be increased to compensate Chorus for reduced operating margin resulting from the reduced Block Hours. The Compensating Mark-Up percentage applies to all fixed and variable rates billed to Air Canada during the affected calendar year. This incremental mark-up amount (above the Controllable Mark-Up) will be calculated and billed to Air Canada in the fourth quarter of each calendar year in which the Compensating Mark-Up is triggered.

#### **Margin adjustment**

The controllable target margin is 11.11%. With respect to each calendar year during the remaining term of the CPA, if the annual margin for flights provided under the CPA is greater than 11.11%, Chorus will pay Air Canada an amount equal to 50% of the dollar value of the margin exceeding 11.11%. Margin represents the total operating revenue from scheduled flights under the CPA less expenses incurred related to such flights, including employee profit sharing expenses; however, it excludes incentive and pass-through revenue.

#### **Master Services Agreement**

Under a master services agreement dated September 24, 2004, between Chorus and Air Canada, Air Canada provides certain services to Chorus for a fee. These services include information technology services, french language training, and insurance claims services.

The master services agreement will continue in effect until the termination or expiration of the CPA, but individual services can be amended or terminated earlier in accordance with the terms of the master services agreement.

## Notes to the Consolidated Financial Statements For the years ended December 31, 2013 and 2012

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(expressed in thousands of Canadian dollars, except shares and earnings per share)

### 19 Economic dependence (continued)

#### Other

Air Canada provides certain supplies from third parties, primarily fuel, to Chorus and subsequently collects payment from Chorus. As these transactions and balances merely represent a method of settlement for transactions in the normal course of business, they have not been separately disclosed. Air Canada also provides ground handling services.

Substantially all of the trade receivable from Air Canada relates to outstanding balances under the CPA.

The balances in accounts payable and accrued liabilities are payable on normal trade terms and have arisen from the services provided by the applicable party.

### 20 Assets held for sale

During 2012, Chorus completed a sale of Q400 spare parts to a third party for non-cash proceeds of \$13,237. These parts had previously been recorded as assets held for sale. The proceeds were received in the form of a credit note to be drawn down monthly against expenses with the same third party. The credit note has been classified into its current and long-term receivable portions and is expected to be fully realized by 2014. These non-cash transactions have been excluded from the statement of cash flows in 2012 and 2013.

### 21 Long-term investment

On April 30, 2010, Chorus purchased a 33% non-voting equity interest in Latin American Regional Aviation Holding Corporation ("LARAH"). LARAH held an indirect 75% equity interest in Pluna Líneas Aéreas Uruguayas S.A. ("Pluna"). The remaining 25% equity interest in Pluna was held, indirectly, by the Government of Uruguay. In the second quarter of 2012 it was announced that Pluna was in financial difficulty and that the Uruguayan government had taken control of the airline and ceased its operations. All of the shares in Pluna held indirectly by LARAH, including the portion indirectly owned by Chorus, were transferred to the Government of Uruguay. As a result, in the second quarter of 2012 Chorus recorded a write-down of \$16,351 to the fair value of the investment through other comprehensive loss.

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**22 Statement of cash flows - supplementary information**

Net changes in non-cash balances related to operations:

	<b>2013</b>	<b>2012</b>
	<b>\$</b>	<b>\$</b>
(Increase) decrease in accounts receivable – trade and other	(1,560)	22,283
Increase in inventories	(6,972)	(1,075)
Decrease in prepaid expenses	3,046	13,104
Decrease (increase) in other assets	32,605	(6,210)
Increase (decrease) in accounts payable and accrued liabilities	1,469	(27,845)
Decrease in unearned revenue	—	(21,495)
Decrease in other long-term liabilities	(47,595)	(11,268)
	<b>(19,007)</b>	<b>(32,506)</b>

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(expressed in thousands of Canadian dollars, except shares and earnings per share)

**23 Additional information**

**(a) Assets**

	<b>As at December 31,</b>	
	<b>2013</b>	<b>2012</b>
	<b>\$</b>	<b>\$</b>
<b>Accounts receivable</b>		
Trade receivables	1,051	3,388
Commodity taxes	3,069	3,553
Other receivables (note 20)	14,089	13,513
	18,209	20,454
Trade amounts due from Air Canada and its subsidiary (see note 19 - Economic Dependence)	58,682	58,495
	76,891	78,949
<b>Inventories <sup>(1)</sup></b>		
Aircraft expendables	31,588	30,091
Used aircraft expendables and rotables under consignment	5,738	—
Supplies	2,476	2,784
Fuel and de-icing fluid	5,319	5,274
	45,121	38,149

(1) For the year ended December 31, 2013, the cost of aircraft expendables and supplies and consignment inventory recognized as a maintenance expense was \$29,719 (2012 - \$32,245). For the year ended December 31, 2013 inventory write-downs to net realizable value of \$1,551 were recognized as a maintenance expense (2012 - \$1,752).

	<b>As at December 31,</b>	
	<b>2013</b>	<b>2012</b>
	<b>\$</b>	<b>\$</b>
<b>Prepaid expenses and deposits</b>		
Airport and navigation fees	9,572	11,557
Fuel	6,543	8,972
Aircraft rent and other	3,150	3,399
Other	3,631	2,014
	22,896	25,942
<b>Other assets</b>		
Prepaid aircraft rent and related fees, net of accumulated amortization	22,635	24,089
Accrued pension benefit asset ("SERP") (note 12)	10,617	7,509
Accrued defined pension benefit asset (note 12)	26,762	—
Other long-term receivables (note 20)	—	3,679
Asset backed commercial paper	1,231	1,003
Restricted cash (note 5)	6,208	—
	67,453	36,280

Notes to the Consolidated Financial Statements  
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(expressed in thousands of Canadian dollars, except shares and earnings per share)

**23 Additional information (continued)**

**(b) Liabilities**

	<b>As at December 31,</b>	
	<b>2013</b>	<b>2012</b>
	<b>\$</b>	<b>\$</b>
<b>Accounts payable and accrued liabilities</b>		
Trade payables and accrued liabilities	121,129	114,427
Commodity taxes	14,630	14,690
Current portion of deferred lease inducements	3,404	3,319
	139,163	132,436
Trade payables and accrued liabilities due to Air Canada and its subsidiary (see note 19 - Economic Dependence)	68,171	73,152
	207,334	205,588
<b>Other Long-term liabilities</b>		
Accrued defined pension benefit liability (note 12)	—	42,632
Accrued Other Future Employee Benefits liability (note 12)	12,786	16,398
Deferred operating lease inducements, non-current portion	28,070	32,319
Other	3,678	1,036
	44,534	92,385

**24 Subsequent event**

On February 10, 2014 (the "Early Redemption Date"), Chorus exercised its right to redeem \$60,000 of its \$80,210 aggregate principal amount of Debentures outstanding at December 31, 2013. The Debentures were redeemed on a pro rata basis. Chorus paid the holders of the redeemed Debentures the outstanding principal amount of the redeemed Debentures (the "Redemption Price"), together with all accrued and unpaid interest thereon up to but excluding the Early Redemption Date, for a total of approximately \$1,011 per \$1,000.00 principal amount of Debentures. The Debentures that were redeemed ceased to bear interest from and after the Early Redemption Date. Chorus used surplus cash to pay the Redemption Price, together with all accrued and unpaid interest thereon as described above. Following the redemption, \$20,210 of Debentures remain outstanding.