Consolidated Financial Statements of

# DISCOVERY AIR INC.

Years ended January 31, 2011 and 2010

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# INDEPENDENT AUDITORS' REPORT

To the Shareholders of Discovery Air Inc.

We have audited the accompanying consolidated financial statements of Discovery Air Inc., which comprise the consolidated balance sheets as at January 31, 2011 and January 31, 2010, the consolidated statements of net earnings (loss) and comprehensive income (loss), shareholders' equity and cash flows for the years then ended, and notes, comprising 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 Canadian generally accepted accounting principles, 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.

*Auditors' 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 an 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 our 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, we consider 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 opinions.

*Opinion*

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of Discovery Air Inc. as at January 31, 2011 and January 31, 2010 and its consolidated results of operations and its consolidated cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Chartered Accountants

April 21, 2011
Edmonton, Canada

# DISCOVERY AIR INC.

Consolidated Balance Sheets
January 31, 2011 and 2010

(thousands of dollars)

| | 2011 | 2010 |
|---|---|---|
| **Assets** | | |
| Current assets: | | |
| Cash | $ 9,693 | $ 9,237 |
| Restricted cash (note 14) | 834 | 1,330 |
| Accounts receivable | 16,685 | 9,501 |
| Inventory | 14,950 | 13,902 |
| Prepaid expenses and other | 2,170 | 2,935 |
| | 44,332 | 36,905 |
| Land, buildings and equipment (note 3) | 157,633 | 157,944 |
| Goodwill | 37,862 | 37,862 |
| Intangible assets (note 4) | 19,159 | 23,599 |
| | $ 258,986 | $ 256,310 |
| **Liabilities and Shareholders' Equity** | | |
| Current liabilities: | | |
| Accounts payable and accrued liabilities | $ 12,633 | $ 10,444 |
| Income taxes payable | 1,282 | 817 |
| Current portion of long-term debt (note 5) | 38,888 | 10,330 |
| | 52,803 | 21,591 |
| Long-term debt (notes 5 and 13) | 101,325 | 135,777 |
| Future income taxes (note 7) | 24,204 | 24,531 |
| Non-controlling interest | 2,884 | 2,136 |
| Shareholders' equity (note 8): | | |
| Share capital | 65,134 | 184,535 |
| Contributed surplus | 7,170 | 7,141 |
| Retained earnings (deficit) | 5,466 | (119,401) |
| | 77,770 | 72,275 |
| | $ 258,986 | $ 256,310 |

Commitments, restricted cash and contingencies (note 14)

Subsequent events (note 17)

See accompanying notes to consolidated financial statements.

On behalf of the Board:

***"Gilbert S. Bennett" (signed)***
Director

***"James L. Goodfellow" (signed)***
Director

# DISCOVERY AIR INC.

Consolidated Statements of Net Earnings (Loss) and Comprehensive Income (Loss)
Years ended January 31, 2011 and 2010

(thousands of dollars, except per share amounts)

| | 2011 | 2010 |
|---|---|---|
| Revenue | $ 152,418 | $ 123,173 |
| Operating expenses | 114,865 | 94,362 |
| Earnings before undernoted items | 37,553 | 28,811 |
| | | |
| Interest and financing charges | 15,298 | 15,410 |
| Amortization of buildings and equipment | 9,434 | 9,614 |
| Amortization of intangible assets | 4,440 | 4,464 |
| Corporate office relocation expenses (note 5) | 158 | 1,678 |
| | 29,330 | 31,166 |
| | | |
| Earnings (loss) before income taxes and non-controlling interest | 8,223 | (2,355) |
| | | |
| Income tax provision (recovery) (note 7) | | |
| Current | 2,765 | 1,145 |
| Future | (327) | (3,462) |
| | 2,438 | (2,317) |
| Earnings (loss) before non-controlling interest | 5,785 | (38) |
| | | |
| Non-controlling interest | 319 | 248 |
| | | |
| Net earnings (loss) and comprehensive income (loss) | $ 5,466 | $ (286) |
| | | |
| Basic and diluted earnings (loss) per share (note 9) | $ 0.04 | $ (0.00) |

See accompanying notes to consolidated financial statements.

# DISCOVERY AIR INC.

Consolidated Statements of Shareholders' Equity
Years ended January 31, 2011 and 2010

| (thousands of dollars) | 2011 | 2010 |
|---|---|---|
| Share capital (note 8): | | |
| Balance, beginning of year | $ 184,535 | $ 184,535 |
| Reclassification of opening deficit | (119,401) | – |
| Balance, end of year | $ 65,134 | $ 184,535 |
| Contributed surplus: | | |
| Balance, beginning of year | $ 7,141 | $ 7,012 |
| Stock-based compensation | 29 | 129 |
| Balance, end of year | $ 7,170 | $ 7,141 |
| Retained earnings (deficit) (note 8): | | |
| Balance, beginning of year | $ (119,401) | $ (119,115) |
| Reclassification of opening deficit | 119,401 | – |
| Net earnings (loss) and comprehensive income (loss) | 5,466 | (286) |
| Balance, end of year | $ 5,466 | $ (119,401) |

See accompanying notes to consolidated financial statements.

# DISCOVERY AIR INC.

Consolidated Statements of Cash Flows
Years ended January 31, 2011 and 2010

| (thousands of dollars) | 2011 | 2010 |
|---|---|---|
| Cash provided by (used in): | | |
| Operating activities: | | |
| Net earnings (loss) | $ 5,466 | $ (286) |
| Items not involving cash: | | |
| Future income tax recovery | (327) | (3,462) |
| Stock-based compensation (note 8) | 29 | 129 |
| Deferred share unit compensation (note 8) | 215 | 241 |
| Amortization of buildings and equipment and intangible assets | 13,874 | 14,078 |
| Amortization of rotable and overhauled components | 5,899 | 4,823 |
| Accretion of discount on long-term debt | 1,670 | 1,470 |
| Loss (gain) on disposal of equipment | (629) | 421 |
| Non-controlling interest | 319 | 248 |
| Change in non-cash operating working capital (note 10) | (4,532) | 3,776 |
| | $ 21,984 | $ 21,438 |
| Investing activities: | | |
| Purchases of land, buildings and equipment | $ (18,153) | $ (22,691) |
| Proceeds on disposal of equipment | 3,760 | 4,773 |
| | $ (14,393) | $ (17,918) |
| Financing activities: | | |
| Proceeds from long-term debt | $ 2,831 | $ 44,159 |
| Financing costs | (546) | (1,698) |
| Repayment of long-term debt | (9,849) | (43,550) |
| Distributions to non-controlling interest | (71) | (59) |
| Proceeds from non-controlling interest | 500 | – |
| | $ (7,135) | $ (1,148) |
| Increase in cash | 456 | 2,372 |
| Cash, beginning of year | 9,237 | 6,865 |
| Cash, end of year | $ 9,693 | $ 9,237 |
| Supplementary cash flow information: | | |
| Interest paid | $ 13,527 | $ 12,458 |
| Income taxes paid (recovered) | 2,300 | (470) |

See accompanying notes to consolidated financial statements.

Discovery Air Inc. (the "Corporation") was incorporated on November 12, 2004 under the *Ontario Business Corporations Act* and on March 27, 2006 was continued under the *Canada Business Corporations Act*. Its primary business activities are carried out by its wholly-owned subsidiaries Great Slave Helicopters Ltd. ("Great Slave"), Air Tindi Ltd. ("Air Tindi"), Top Aces Inc. ("Top Aces"), Hicks & Lawrence Limited ("Hicks"), Discovery Mining Services Ltd. ("Discovery Mining") and Discovery Air Technical Services Inc. ("Technical Services").

The Corporation's business is divided into two segments: the Northern Services segment, which consists of Great Slave, Air Tindi and Discovery Mining; and the Government Services segment, consisting of Top Aces, Hicks and Technical Services.

Great Slave is a helicopter company that, directly and in partnership with northern Aboriginal groups, operates a fleet of 62 helicopters and provides services throughout northern Canada and in several Canadian provinces and select international locations. Services are provided to private sector companies and governments in areas such as resource and base mineral exploration and production, wildlife services, forest fire suppression, oil and gas exploration, power line construction and maintenance, aerial surveys, tourism and flight training. Great Slave's principal operations are carried out in Yellowknife, Northwest Territories and Calgary, Alberta. It has additional facilities in Fort Simpson, Fort Liard, Norman Wells and Inuvik in the Northwest Territories, Rankin Inlet in Nunavut, Churchill in Manitoba and Dryden in Ontario.

Air Tindi, based in Yellowknife, operates a diversified fleet of 22 fixed-wing aircraft offering scheduled and chartered passenger and cargo services, as well as air ambulance services, in northern Canada. Air Tindi, both directly and in partnership with northern Aboriginal groups, provides services to a diversified customer base that includes major diamond and mineral exploration and mining companies, as well as the Governments of Canada and the Northwest Territories.

Discovery Mining is a provider of remote exploration camps and expediting, logistics and staking services to diamond and mineral exploration companies. Based in Yellowknife, Discovery Mining conducts operations in the Northwest Territories, Nunavut, northern Alberta and northern Saskatchewan.

Top Aces is a Quebec-based approved supplier of airborne training and special mission services to the Department of National Defence ("DND"). Top Aces operates a fleet of 22 aircraft. Top Aces provides a variety of military training services ranging from simulated combat to target tow and ground support, operating throughout Canada as well as in parts of the United States.

Hicks is an Ontario-based aviation company that provides aerial fire management services to the Province of Ontario, employing 29 aircraft from operation and maintenance bases throughout northern Ontario. Hicks also provides air charter services, using 3 aircraft, to the provincial government and various other corporate entities which conduct business in northern Ontario.

Technical Services is a Quebec-based company that provides a range of aircraft maintenance, repair and overhaul, modification engineering and certification services.

## 1. Significant accounting policies:

These consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles. The significant accounting principles used in the preparation of these consolidated financial statements are summarized below:

(a) Investments in subsidiaries:

The consolidated financial statements include the accounts of the Corporation's wholly owned subsidiaries Great Slave, Air Tindi, Top Aces, Hicks, Discovery Mining, Technical Services and Great Slave's wholly-owned subsidiaries Superior Helicopters Canada Ltd. ("Superior") and Hudson Bay Helicopters Ltd. ("Hudson Bay"). All significant intercompany balances and transactions have been eliminated on consolidation.

(b) Use of estimates:

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the stated amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amounts of revenue and expenses during the reporting periods. Significant items subject to such estimates and assumptions include determining the useful lives of land, buildings and equipment and intangible assets with finite useful lives, the recoverability or impairment of long-lived assets, intangible assets and goodwill, valuation allowances for receivables, inventory, future income taxes, and contingent liabilities related to lawsuits. Actual results could differ from those estimates and assumptions.

(c) Variable interest entities:

The Corporation is the primary beneficiary of variable interest entities and consolidates these entities in its consolidated financial statements. Accounting Guideline 15, *Consolidation of Variable Interest Entities*, requires the primary beneficiary of a variable interest entity ("VIE") to consolidate the VIE. A VIE is an entity: (i) which does not have sufficient equity at risk to finance its activities without additional subordinated financial support; or (ii) in which the holders of the equity at risk lack the characteristics of a controlling financial interest. The primary beneficiary is the enterprise that will absorb or receive the majority of the VIE's expected losses or residual returns or both.

(d) Cash:

Cash includes cash on hand, balances with financial institutions and short-term investments with an initial term to maturity of three months or less.

(e) Inventory:

Inventory, consisting of aircraft parts and supplies, is stated at the lower of cost (on a first-in, first-out basis) and net realizable value (where replacement cost may be used as an indicator of value).

**1. Significant accounting policies (continued):**

(f) Land, buildings and equipment:

Land, buildings and equipment are stated at cost and amortized over their expected useful lives. Maintenance and repair expenditures which do not improve or extend productive life are expensed as incurred.

Amortization is provided using the following methods and annual rates:

| Assets | Methods | Annual Rates |
|---|---|---|
| Buildings | Straight-line | 5% |
| | Diminishing balance | 4% |
| Furniture and equipment | Diminishing balance | 10 - 30% |
| | Straight-line | 20 - 30% |
| Aircraft | Straight-line | 5% |
| Leasehold improvements | Straight-line | 20% |
| Vehicles | Diminishing balance | 30% |
| Rotable and overhauled components | Flight hours | hours flown |

(g) Aircraft overhaul and maintenance costs:

Aircraft airframes, engines and components are inspected, repaired and overhauled at pre-specified intervals. Overhaul and maintenance costs that extend the useful lives of the aircraft are capitalized as incurred and amortized over their useful lives based on hours flown. Other overhaul and maintenance costs are expensed as incurred.

(h) Goodwill:

Goodwill is the amount by which the purchase price of an acquired business (including liabilities assumed) exceeds the sum of the fair values of the other assets acquired. Goodwill is not amortized.

The Corporation tests goodwill for impairment annually at the end of its fourth quarter, and at any other time when circumstances or events have occurred that would more likely than not reduce the long-term fair value of a reporting unit below the carrying value of that reporting unit. The goodwill impairment test is a two-step process. In the first step, the Corporation compares the fair value of each reporting unit to that reporting unit's carrying value, which includes the goodwill allocated to that reporting unit. In determining the fair value of a reporting unit, the Corporation considers both the discounted cash flow method as well as valuations based on a market approach. If the carrying value of the reporting unit exceeds its fair value, then step two requires the fair value of that reporting unit to be allocated to its underlying assets and liabilities. The remaining fair value of the reporting unit (if any) is the fair value of the goodwill of that reporting unit.

When the carrying value of a reporting unit's goodwill exceeds the fair value of that goodwill, an impairment loss equal to the excess is recorded on the Consolidated Balance Sheet and recognized as a non-cash impairment charge in the Consolidated Statements of Net Earnings (Loss) and Comprehensive Income (Loss). The assessment of goodwill impairment is not a mechanical exercise and requires the use of considerable management judgment. Changes in expected financial results or other underlying assumptions may have a significant impact on either the fair value of a reporting unit or the amount of any goodwill impairment charged.

**1. Significant accounting policies (continued):**

(i) Intangible assets:

Intangible assets are assets acquired which lack physical substance and which meet specified criteria for recognition apart from goodwill. Intangible assets are comprised mainly of trade names and customer relationships. Customer relationships are amortized on a straight-line basis over eight years, while trade names have an indefinite life and, therefore, are not amortized.

Each intangible asset with an indefinite life is tested for impairment annually or more frequently if events or changes in circumstances indicate that the asset might be impaired. The impairment test consists of a comparison of the fair value of the intangible asset with its carrying amount. Any impairment loss in the carrying amount compared with the fair value is charged to income in the period in which the loss is incurred.

(j) Impairment of long-lived assets:

Each long-lived asset, including land, building and equipment, and an intangible subject to amortization, is reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of that asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset or group of assets to estimated undiscounted future cash flows expected to be generated by the asset or group of assets. If such an asset or group of assets is considered to be impaired, the impairment charge to be recognized is measured by the amount by which the carrying amount of the asset or group of assets exceeds the fair value of the asset or group of assets and is charged to income in the period in which the loss is incurred.

(k) Financing costs:

Financing costs related to the origination and renewal of long-term credit facilities are recorded as a reduction of the related debt. Financing costs are amortized using the effective interest rate method.

(l) Revenue recognition:

Revenue from providing aviation and aviation-related services is recorded based on the terms of customer contracts that generally provide for revenue on the basis of hours flown or services provided at contract rates or fixed monthly charges or a combination of both. Revenue is recorded if amounts are fixed or determinable and collection is reasonably assured.

(m) Income taxes:

The Corporation uses the asset and liability method of accounting for income taxes. Under the asset and liability method, future tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Future tax assets and liabilities are measured using enacted or substantively enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on future tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the date of enactment or substantive enactment of the change in tax rates.

## 1. Significant accounting policies (continued):

(n) Foreign currency:

Monetary items denominated in foreign currency are translated to Canadian dollars at exchange rates in effect at the balance sheet date. Non-monetary items are translated at rates of exchange in effect when the assets were acquired or obligations incurred. Revenues and expenses are translated at rates in effect at the time of the transactions. Foreign exchange gains and losses are included in income.

(o) Stock-based compensation:

The Corporation has stock-based compensation plans which are described in note 8. The Corporation accounts for employee stock options using the fair value method. This method recognizes the fair value of the stock option over the applicable vesting period as an increase in compensation expense and contributed surplus. Any consideration paid by employees on exercise of these stock options is credited to common shares along with the amount previously recognized in contributed surplus.

The Corporation awards deferred share units ("DSUs") to the directors of the Corporation. These DSUs are recognized as compensation expense and liabilities are accrued as they are awarded. The issued DSUs are re-measured at the end of each reporting period using the closing market price of the Corporation's common shares at the end of that reporting period.

(p) Earnings per share:

Basic earnings per share is calculated by dividing net earnings (loss) by the weighted average number of shares outstanding during the year. For the purpose of calculating the average weighted number of shares outstanding, shares are determined to be outstanding from the date they are issued. Diluted earnings per share is calculated using the treasury stock method. The treasury stock method increases the diluted weighted average number of shares outstanding to include additional shares from the assumed exercise of stock options, if dilutive. The number of additional shares is calculated by assuming outstanding in-the-money stock options were exercised and the proceeds of such exercises, including any unamortized stock-based compensation cost, were used to acquire shares of common stock at the average market price during the year.

(q) Financial instruments:

Financial assets and financial liabilities, including derivative financial instruments, are initially measured at fair value. Subsequent to initial recognition, financial assets and financial liabilities are measured based on their classification: held-for-trading, loans and receivables or other financial liabilities.

The Corporation's financial assets and liabilities are classified into the following categories:

| | |
|---|---|
| Cash and restricted cash | Assets held-for-trading |
| Accounts receivable | Loans and receivables |
| Operating line of credit | Other financial liabilities |
| Accounts payable and accrued liabilities | Other financial liabilities |
| Long-term debt | Other financial liabilities |

**1. Significant accounting policies (continued):**

(q) Financial instruments (continued):

Assets held-for-trading are measured at fair value and the gains and losses arising from the remeasurement at the end of each reporting period are recorded in earnings. Loans and receivables are recorded at cost, which on initial recognition represents their fair value. Subsequent valuations are recorded at amortized cost using the effective interest rate method. For the Corporation, the measured amount generally corresponds to the cost. Other financial liabilities are initially measured at fair value. Subsequent valuations are recorded at amortized cost using the effective interest rate method. For the Corporation, the measured amount generally corresponds to the cost.

Transaction costs related to held-for-trading financial assets and liabilities are expensed as incurred. Transaction costs related to financial assets classified as loans and receivables or to financial liabilities classified as other financial liabilities are reflected in the carrying value of the financial asset or financial liability and are then amortized over the estimated useful life of the instrument using the effective interest rate method.

Management has determined that the only material embedded derivative in the Corporation's financial instruments that requires separate recognition and measurement is the conversion feature contained in its unsecured convertible debentures (see notes 5 and 8). At the date of issue, the fair value of the liability and equity components were measured separately, and to the extent necessary, were adjusted on a pro-rata basis so that the sum of the components equals the amount of the instrument as a whole. The liability component has been subsequently recognized on an amortized cost basis using the effective interest rate method until extinguished on conversion or at the instrument's maturity date. The equity component has been recognized and included in equity, and has not been subsequently re-measured.

**2. Recently issued standards:**

International Financial Reporting Standards ("IFRS"):

In February 2008, the CICA Accounting Standards Board announced that all Canadian publicly accountable enterprises will be required to adopt IFRS for fiscal years beginning on or after January 1, 2011. The Corporation's first annual IFRS consolidated financial statements will be for the fiscal year beginning February 1, 2011 and ending January 31, 2012 and will include the comparative period of fiscal 2011, which began on February 1, 2010. Starting in the first quarter of fiscal 2012, the Corporation will provide unaudited consolidated quarterly financial information in accordance with IFRS, including comparative figures for fiscal 2011.

### 3. Land, buildings and equipment:

(thousands of dollars)

| January 31, 2011 | Cost | Accumulated amortization | Net book value |
|---|---|---|---|
| Land | $ 654 | $ – | $ 654 |
| Buildings | 19,520 | 4,062 | 15,458 |
| Furniture and equipment | 10,694 | 4,800 | 5,894 |
| Aircraft | 143,074 | 29,026 | 114,048 |
| Rotable and overhauled components | 40,044 | 19,186 | 20,858 |
| Vehicles | 1,717 | 1,351 | 366 |
| Leasehold improvements | 1,167 | 812 | 355 |
| | $ 216,870 | $ 59,237 | $ 157,633 |

(thousands of dollars)

| January 31, 2010 | Cost | Accumulated amortization | Net book value |
|---|---|---|---|
| Land | $ 637 | $ – | $ 637 |
| Buildings | 17,960 | 3,293 | 14,667 |
| Furniture and equipment | 8,979 | 4,473 | 4,506 |
| Aircraft | 140,939 | 22,698 | 118,241 |
| Rotable and overhauled components | 32,694 | 13,767 | 18,927 |
| Vehicles | 1,827 | 1,287 | 540 |
| Leasehold improvements | 1,104 | 678 | 426 |
| | $ 204,140 | $ 46,196 | $ 157,944 |

During the year ended January 31, 2011, $5.9 million (2010 - $4.8 million) relating to the amortization of rotable and overhauled components was included in operating expenses in the Consolidated Statements of Net Earnings (Loss) and Comprehensive Income (Loss).

### 4. Intangible assets:

(thousands of dollars)

| January 31, 2011 | Cost | Accumulated amortization and impairment charge | Net book value |
|---|---|---|---|
| Customer relationships | $ 35,385 | $ 17,071 | $ 18,314 |
| Trade names | 845 | – | 845 |
| Other | 210 | 210 | – |
| | $ 36,440 | $ 17,281 | $ 19,159 |

(thousands of dollars)

| January 31, 2010 | Cost | Accumulated amortization and impairment charge | Net book value |
|---|---|---|---|
| Customer relationships | $ 35,385 | $ 12,649 | $ 22,736 |
| Trade names | 845 | – | 845 |
| Other | 210 | 192 | 18 |
| | $ 36,440 | $ 12,841 | $ 23,599 |

## 5. Long-term debt:

| (thousands of dollars) | 2011 | 2010 |
|---|---|---|
| 8.75% unsecured convertible debentures, maturing December 31, 2011 (see note 5(a)) | $ 28,053 | $ 27,349 |
| Long-term secured debt bearing a floating interest rate of 90 day bankers acceptance yield (the "BA rate") plus 7.65%, maturing September 24, 2020 (see note 5(b)) | 46,186 | 48,027 |
| Long-term secured debt bearing a fixed rate of 10.00%, maturing February 1, 2013 (see note 5(c)) | 33,388 | 33,156 |
| Long-term secured debt incurred by a subsidiary, bearing an interest rate of floating base bank rate plus 4.50%, maturing January 15, 2015 (see note 5(d)) | 12,149 | 15,188 |
| Long-term debt secured by specific assets, incurred by subsidiary companies bearing fixed interest rates at a weighted average of 7.06%, maturing fiscal 2012 through fiscal 2014 | 1,045 | 1,359 |
| Long-term debt secured by specific assets, incurred by subsidiary companies bearing floating interest rates at a weighted average of 5.53%, maturing fiscal 2013 through fiscal 2022 | 1,897 | 1,244 |
| Secured subordinated notes payable to officers and directors of the Corporation and its subsidiaries bearing interest at prime plus 1.25%, maturing fiscal 2015 through fiscal 2016 (note 13 and 17) | 13,447 | 14,277 |
| Unsecured notes payable to officers and directors of the Corporation and its subsidiaries, bearing interest at prime, maturing fiscal 2010 (note 13) | – | 752 |
| Finance contracts with varying terms and maturities | 215 | 122 |
| Secured demand loan bearing an interest rate of 18.00% per annum, maturing June 9, 2011 (see note 5(e)) | 3,833 | 4,633 |
| Total long-term debt | 140,213 | 146,107 |
| Less current portion of long-term debt | 38,888 | 10,330 |
| | $ 101,325 | $ 135,777 |

a) The 8.75% convertible debentures are convertible at any time into common shares at $2.05 per share. The convertible debentures were not redeemable before December 31, 2009. Between December 31, 2009 and December 31, 2010, the convertible debentures were redeemable by the Corporation at the principal amount outstanding plus accrued and unpaid interest, provided that the weighted average trading price of the Class A Shares of the Corporation's shares was greater than 125% of the conversion price. On or after December 31, 2010, the convertible debentures are redeemable by the Corporation at their principal amount plus accrued interest. The debentures were issued in December, 2006 at which time the

**5. Long-term debt (continued):**

fair value of the Corporation's obligation to make future payments of principal and interest (the liability component) was $27.6 million and the fair value of the holders' conversion option (the equity component) was determined to be $1.1 million. Financing costs of $1.9 million related to the issue of the convertible debentures were netted against the carrying value of the liability component. As interest expense and financing costs are recognized, they increase the recorded carrying value of the liability component until such time as the liability component equals the debentures' face value of $28.75 million, calculated at an effective interest rate of 11.70%. As at January 31, 2011, the Corporation was in compliance with all financial covenants related to this debt.

Subsequent to January 31, 2011, the Corporation entered into an agreement to sell to a syndicate of underwriters $30.0 million principal amount of new convertible unsecured subordinated debentures at a price of $1,000 per debenture. The proceeds of this new offering will be used by the Corporation to fully repay the current convertible debentures and accrued interest payable thereon, and the balance, if any, will be used for working capital and general corporate purposes (see note 17(a)).

b) In January 2008, the Corporation entered into a 5-year revolving credit agreement to finance certain fleet assets. The facility borrowing base and interest rate were subject to annual review and the lender retained an option to convert the facility to an amortizing term facility at each annual review date. The lender exercised this option during the 2010 annual review, and effective September 24, 2010, negotiated (i) repayment of the facility over a 10-year term through monthly blended principal and interest payments; and (ii) a reduction in the facility interest rate to the 90 day BA rate plus 7.65%. Financing costs of $2.3 million are netted against the carrying value of the facility and are being expensed over the term of the facility on an effective interest basis, resulting in an effective interest rate of 9.29%. The Corporation can elect at future anniversary dates to retain the facility on a floating interest rate basis, or to amend the interest rate to a market-based fixed rate over various term options.

The facility is secured by: (i) a general security agreement providing a security interest in the Corporation's assets; (ii) guarantees from each of Great Slave, Superior, Hudson Bay, Air Tindi, Discovery Mining and Hicks, each of which is supported by a general security agreement over the assets of those subsidiaries; (iii) unsecured guarantees of the indebtedness by Top Aces and Technical Services; and (iv) mortgage interests in certain real estate owned by subsidiaries subject to prior charges in favour of other term lenders. The security structure provides a first charge over specific aircraft owned by the above-named subsidiaries and a secondary floating charge over all other assets, subordinated in specific instances to lenders by way of priority agreements. The credit documentation requires that the Corporation observe a variety of non-financial covenants, and make it subject to financial covenants that require it to remain below specified levels of balance sheet and cash flow leverage and to maintain minimum levels of fixed charge coverage and tangible net worth. As at January 31, 2011, the Corporation was in compliance with all financial covenants related to this facility.

Amounts outstanding under the facility may not exceed a borrowing base value calculated annually as an agreed maximum percentage of the U.S. dollar valuation of pledged aircraft assets. As at January 31, 2011, the Corporation was in compliance with the facility borrowing base requirement.

**5. Long-term debt (continued):**

c) In February 2009, the Corporation entered into a $34.0 million term loan agreement to refinance a maturing term loan. The 2009 term loan has an effective interest rate of 10.98% per annum and matures on February 1, 2013. The loan is secured by: (i) a general security agreement over the assets of the Corporation and a specific pledge of the shares of Top Aces; and (ii) guarantees from each of Great Slave, Superior, Hudson Bay, Air Tindi and Discovery Mining, each of which is supported by a general security agreement over the assets of those subsidiaries; and (iii) an unsecured guarantee of the indebtedness by Top Aces. The security structure provides a first charge over specific aircraft and a secondary floating charge over all other assets of the guarantors, including real estate assets, subordinated in specific instances to the interests of other lenders by way of priority agreements. The Corporation incurred $1.1 million in financing costs related to this term loan, which are netted against the carrying value of the debt and which are being expensed over the term of the loan on an effective interest basis. Under this term loan agreement, the Corporation was obligated to relocate its corporate office to Yellowknife, Northwest Territories from London, Ontario. As at January 31, 2011, the Corporation was in compliance with all financial covenants related to this debt.

d) In February 2008, the Corporation entered into a $21.5 million term loan agreement to refinance its existing term debt and to fund the purchase of additional aircraft, spare engines and aircraft parts. The principal amount of the loan is repayable in monthly instalments of $256,000, commencing in February 2008 and ending on January 15, 2015. The debt bears an interest rate equal to the lender's floating base rate plus 4.50% per annum and has an effective interest rate of 6.79% per annum. The loan is secured by a first charge on all the assets of Top Aces, subject to a priority interest over Top Aces' accounts receivable in favour of the Corporation's operating lender (see Note 6). As at January 31, 2011, $12.3 million was outstanding under this term facility. Related financing costs of $226,000 were netted against the carrying value of the loan and are being amortized over the term of the loan on an effective interest basis. The agreement requires that the Corporation observe a variety of non-financial covenants and make it subject to financial covenants which require that it remain below specified levels of cash flow leverage and that it maintain minimum levels of fixed charge coverage and tangible net worth. As at January 31, 2011, the Corporation was in compliance with all financial covenants related to this debt.

e) In December 2009, the Corporation entered into a $6.2 million demand loan agreement with its operating lender (see note 6) to finance the purchase of additional aircraft and support equipment for one of its subsidiaries. The principal amount of the loan is repayable in monthly instalments of $100,000 ending on June 9, 2011, at which time the principal balance is due in full. The loan bears an interest rate of 18.00% per annum payable monthly and is secured by a specific charge on the purchased aircraft and support equipment. As at January 31, 2011, $3.8 million was outstanding under this demand credit facility, with an additional $1.1 million available if required to finance the purchase of additional spare components and support equipment. This demand facility is provided by the lender in conjunction with the operating line of credit and shares the same general terms, including financial covenant requirements.

**5. Long-term debt (continued):**

Long-term debt principal repayments for each of the next five years and thereafter are as follows:

| (thousands of dollars) | |
|---|---|
| 2012 | $ 38,888 |
| 2013 | 7,707 |
| 2014 | 49,237 |
| 2015 | 10,108 |
| 2016 | 4,222 |
| Thereafter | 30,051 |

Interest on long-term debt for the year ended January 31, 2011 was $13.3 million (2010 - $12.2 million).

**6. Operating line of credit:**

The Corporation has a secured demand credit facility to finance its working capital requirements. The credit facility has a maximum borrowing limit of $15.0 million, with increased availability of up to $25.0 million during the Corporation's peak operating period of April through November annually. As at January 31, 2011, the Corporation had available an unused borrowing capacity of $9.6 million. The maximum borrowing limit availability is dependent upon a borrowing base which is calculated by reference to eligible accounts receivable and inventory, and is subject to an allowance for specific reserves. The credit facility bears an interest rate of 18.00% per annum on the amount drawn. On June 9, 2010, the Corporation renewed the operating line of credit for a further 12-month term, maturing on June 9, 2011. Conditions set under the renewal are substantially consistent with those previously applicable, except for an amendment to include a stand-by fee of 75 basis points per annum on amounts authorized but not drawn. The Corporation incurred $250,000 in financing fees related to the renewal of this credit facility. The credit facility is secured by a first charge over the accounts receivable of all the Corporation's operating entities and over inventories of all the Corporation's operating entities except Top Aces, as well as a second floating charge over all other assets of the Corporation and its subsidiaries, except real estate, subject to specific permitted encumbrances. As at January 31, 2011, the Corporation was in compliance with all financial covenants related to this debt.

**7. Income taxes:**

Income tax provision (recovery) differs from the amounts that would be computed by applying the federal and provincial statutory income tax rates of 30.00% (2010 – 31.00%) to income before income taxes and non-controlling interest. The reasons for the differences are as follows:

(thousands of dollars)

| | 2011 | 2010 |
|---|---|---|
| Computed tax provision (recovery) | $ 2,467 | $ (730) |
| increase (decrease) resulting from: | | |
| Change in expected future tax rates | (126) | (1,731) |
| Valuation allowance | - | (127) |
| Permanent differences arising from the write-down of goodwill | - | - |
| Other permanent differences | 97 | 271 |
| | $ 2,438 | $ (2,317) |

**7. Income taxes (continued):**

The tax effects of temporary differences that give rise to significant portions of the future tax assets and future tax liabilities are presented below:

| (thousands of dollars) | 2011 | 2010 |
|---|---|---|
| Future tax assets: | | |
| Loss carry-forwards | $ 5,410 | $ 4,747 |
| Tax basis recorded in subsidiary investment | 1,817 | 1,817 |
| Valuation allowance | (1,817) | (1,817) |
| | 5,410 | 4,747 |
| Future tax liabilities: | | |
| Land, buildings and equipment | (29,614) | (29,278) |
| | (29,614) | (29,278) |
| Net future income tax liability | $ (24,204) | $ (24,531) |

The Corporation has $19.9 million available to reduce future years' income for tax purposes, of which $6.1 million expires on January 31, 2029, $9.3 million expires on January 31, 2030 and the balance of which expires on January 31, 2031. The potential tax benefit of these non-capital losses has been recorded in the Corporation's accounts.

**8. Share capital and stock-based compensation:**

(a) Authorized:

The Corporation is authorized to issue an unlimited number of Class A common voting shares and an unlimited number of Class B common voting shares.

(b) Issued and outstanding:

| (thousands of dollars, except for shares) | 2011 | | 2010 | |
|---|---|---|---|---|
| | Shares | Amount | Shares | Amount |
| Class A common shares: | | | | |
| Outstanding, beginning of year | 134,461,555 | $ 182,244 | 134,461,555 | $ 182,244 |
| Reclassification of opening deficit | – | (119,401) | – | – |
| Outstanding, end of year | 134,461,555 | 62,843 | 134,461,555 | 182,244 |
| Class B common shares: | | | | |
| Outstanding, beginning of year | 742,604 | 1,175 | 742,604 | 1,175 |
| Class A common shares converted to Class B common shares | – | – | – | – |
| Outstanding, end of year | 742,604 | 1,175 | 742,604 | 1,175 |
| Warrants and other equity: | | | | |
| Conversion feature on convertible debt | – | 1,116 | | 1,116 |
| Total share capital end of year | 135,204,159 | $ 65,134 | 135,204,159 | $ 184,535 |

**8. Share capital and stock-based compensation (continued):**

(b) Issued and outstanding (continued):

At the Corporation's annual and special shareholders meeting held on June 3, 2010, the shareholders approved the reclassification of the Corporation's deficit of $119.4 million as at January 31, 2010 to share capital. The deficit arose primarily during the year ended January 31, 2009, when the Corporation recorded a goodwill and intangible assets impairment charge of approximately $133.6 million.

(c) Stock-based compensation:

Employee Stock Options

The Corporation has stock options outstanding that were granted to the directors, officers and employees of the Corporation under two different employee stock option plans.

The employee stock option plan created in January 2006 (the "January 2006 plan") was terminated in June 2008, eliminating any additional grants under the plan. All outstanding stock options granted under the January 2006 plan are fully vested.

In June 2010, a new employee stock option plan (the "June 2010 plan") was approved by the shareholders. In September 2010, 1,500,000 employee stock options were granted under the June 2010 plan. The stock options were granted at an exercise price set at the closing market price of the Corporation's common shares on the day preceding the date when the options were granted. Subject to vesting conditions, the stock options are exercisable for seven years from the date of grant. 300,000 of these stock options will vest on January 31, 2013 and the remaining 1,200,000 stock options will vest on January 31, 2015.

At January 31, 2011, 4,390,800 common shares have been reserved for stock options as follows:

| | Options outstanding | | | Options exercisable | |
|---|---|---|---|---|---|
| Range of exercise prices | Number Outstanding | Weighted average remaining contractual life (years) | Weighted average exercise price | Number Exercisable | Weighted average exercise price |
| $0.26 | 1,500,000 | 6.62 | $ 0.26 | - | $ - |
| $0.50 - $1.00 | 95,000 | 5.91 | 0.59 | 95,000 | 0.59 |
| $1.01 - $1.50 | 319,500 | 7.06 | 1.23 | 319,500 | 1.23 |
| $1.51 - $1.75 | 1,920,200 | 6.29 | 1.58 | 1,920,200 | 1.58 |
| $1.76 - $1.85 | 556,100 | 6.05 | 1.85 | 556,100 | 1.85 |
| | 4,390,800 | | | 2,890,800 | |

**8. Share capital and stock-based compensation (continued):**

(c) Stock-based compensation (continued):

Stock option transactions for the periods ended January 31, 2011 and 2010 are as follows:

| | 2011 | | 2010 | |
|---|---|---|---|---|
| | Number of options | Weighted average exercise price | Number of options | Weighted average exercise price |
| Outstanding, beginning of year | 3,129,900 | $ 1.57 | 7,447,450 | $ 1.21 |
| Granted | 1,500,000 | 0.26 | - | - |
| Exercised | - | - | - | - |
| Forfeited | - | - | (79,015) | 1.18 |
| Expired/cancelled | (239,100) | 1.60 | (4,238,535) | 0.95 |
| Outstanding, end of year | 4,390,800 | $ 1.12 | 3,129,900 | $ 1.57 |

The fair value of the 1,500,000 options granted under the June 2010 plan during the year ended January 31, 2011 was determined using the Black-Scholes option pricing model with the following weighted average assumptions:

| | |
|---|---|
| Exercise price per share | $0.26 |
| Risk-free interest rate | 2% |
| Dividend yield | 0% |
| Expected volatility | 126% |
| Expected option life | 4 years |
| Expected forfeiture rate | 0% |

During the year ended January 31, 2011, the Corporation recognized compensation expense of $29,000 (2010 - $129,000) relating to the estimated fair value of vesting stock options.

(d) Deferred share units:

At January 31, 2011, there were 2,089,065 (2010 – 1,308,779) DSUs held by the directors of the Corporation. Each DSU entitles a retiring director to a cash distribution equal to the closing market price of the Corporation's common shares on a date selected by the retiring director, which date may not be later than December 31 of the year following the year of the director's retirement. During the year ended January 31, 2011, the Corporation granted 780,286 (2010 – 1,061,124) DSUs. No payments (2010 - $Nil) were made to retire DSUs during the year ended January 31, 2011. The Corporation recognized $215,200 (2010 - $241,000) of compensation expense related to DSUs during the year ended January 31, 2011.

## 9. Per share amounts:

Basic earnings (loss) per share:

| (thousands of dollars, except per share amounts) | 2011 | 2010 |
|---|---|---|
| Earnings (loss) | $5,466 | $(286) |
| Weighted average number of common shares outstanding | 135,204 | 135,204 |
| Basic earnings (loss) per share | $0.04 | $(0.00) |

Diluted earnings (loss) per share:

| (thousands of dollars, except per share amounts) | 2011 | 2010 |
|---|---|---|
| Earnings (loss) | $5,466 | $(286) |
| Weighted average number of common shares outstanding | 135,204 | 135,204 |
| Dilutive adjustments | – | – |
| Weighted average number of common shares outstanding assuming dilution | 135,204 | 135,204 |
| Diluted earnings (loss) per share | $0.04 | $(0.00) |

As at January 31, 2011, all employee stock options and the conversion feature on the convertible debentures were anti-dilutive.

## 10. Change in non-cash operating working capital:

| (thousands of dollars) | 2011 | 2010 |
|---|---|---|
| Restricted cash | $ 496 | $ (1,330) |
| Accounts receivable | (7,184) | 4,932 |
| Inventory | (1,048) | (348) |
| Prepaid expenses and other | 765 | 632 |
| Accounts payable and accrued liabilities | 1,974 | (1,725) |
| Income taxes payable | 465 | 1,615 |
| | $ (4,532) | $ 3,776 |

## 11. Capital disclosures:

The Corporation's capital structure consists of long-term debt and shareholders' equity. The Corporation's objectives in managing its capital are to ensure that:

1. an appropriate balance is maintained between levels of debt and equity in the Corporation's capital structure;
2. sufficient, appropriately-structured and properly-priced credit facilities are in place to meet ongoing operational and capital investment requirements;
3. debt capital markets relationships are developed and managed in a way that supports continued access to capital; and
4. the Corporation is positioned to issue, when favourable to do so, additional equity to support execution of its business plan.

Capital is managed in accordance with policies and financial plans that are approved and regularly reviewed by senior management and the Board of Directors and take into account forecasted capital needs, actual performance and market conditions. The Board of Directors reviews and approves any material transactions outside the ordinary course of business. An improvement in capital market conditions over the past several quarters, combined with improved operating results, may leave the Corporation positioned to reassess and modify its capital structure to better support future operations and growth (see note 17).

Certain of the Corporation's debt agreements include affirmative and negative covenants which restrict the Corporation's ability to deal with its assets and operations in the normal course of business including, but not limited to: borrowing money or issuing guarantees; providing liens to secure indebtedness; undertaking investments or disposing of assets; paying dividends, redeeming capital stock, or making other restricted payments; and changing control or merging with another person or selling substantially all of its assets. Certain of the Corporation's debt agreements also require that the Corporation maintain specified financial ratios and satisfy specified financial tests. The Corporation monitors the covenants regularly and the Corporation's Board of Directors and its related lenders review the covenants on a quarterly basis. Other than the covenants under its credit facilities, the Corporation is not subject to any externally-imposed capital requirements.

## 12. Financial instruments - Disclosure and Presentation:

The Corporation is exposed to a variety of financial risks arising from normal business operations as well as from the Corporation's financial instruments, including its cash, trade accounts receivable, trade accounts payable and accrued liabilities, operating loan indebtedness and long-term debt. These risk factors include market, credit and liquidity risks. The Corporation's risk management process is designed to identify, manage and, where appropriate, mitigate business risk, which includes financial risk, among others. Management and the Board of Directors, both separately and together, discuss the principal business risks to which the Corporation is exposed. The Board of Directors sets policies for the implementation of systems to manage, monitor and mitigate identifiable risks. Risk management strategies, policies and limits are designed to provide reasonable assurance that the risk exposures are managed within the Corporation's business objectives and risk tolerance. The Corporation's risk

**12. Financial instruments - Disclosure and Presentation (continued):**

management objective is to optimize the balance between maximizing return for its shareholders and protecting and minimizing volatility in cash flow.

The risks associated with the Corporation's financial instruments, and the ways in which such risks are managed, are described below.

Market risk

Market risk is the risk of loss that could result from changes in market factors such as foreign currency exchange rates and interest rates. The level of market risk to which the Corporation is exposed at any time depends on market conditions, market rate movements and the composition of the Corporation's financial assets and liabilities. The Corporation's management and Board of Directors are responsible for determining the acceptable level of risk and may utilize hedging instruments to the extent they believe it is prudent to manage existing or anticipated risks, commitments or obligations based on past experiences and expectations for the future.

i) Foreign exchange risk:

The Corporation is exposed to foreign currency exchange risk arising from fluctuations in exchange rates on its U.S. dollar and Euro denominated revenues, its U.S dollar and Euro denominated purchases of aircraft inventory parts, and on its periodic purchases and financing of aircraft. As at January 31, 2011, the Corporation did not have any material net foreign exchange exposures.

Aircraft of the type operated by the Corporation are generally valued in U.S. dollars. The Corporation's revolving long-term secured debt facility (see note 5(b)) is denominated in Canadian dollars. Under the terms of this credit facility, a borrowing base governs the maximum borrowing limit and is recalculated in September of each year based on an updated appraisal of the aircraft pledged to secure the facility. The maximum borrowing limit is reset annually based on the lesser of: (1) $48.4 million; and (2) the borrowing base, which is determined by applying an agreed upon lending margin to the annual appraised value of the aircraft and converting the resulting value to Canadian dollars using an agreed exchange rate.

The borrowing base available to the Corporation is based on appraisals completed for the September 2010 reset. The borrowing base is $49.2 million, which exceeds the amount drawn under the facility by $2.1 million. The borrowing base was established in July 2010 based on an exchange rate of $1.05 Canadian dollars for each U.S. dollar. A 5.00% rise or fall in the Canadian dollar against the U.S. dollar, with all other variables unchanged, would result in a borrowing base decrease or increase of $2.5 million. Appraisals to determine the September 2011 reset will be undertaken during the Corporation's second quarter.

ii) Interest rate risk:

The Corporation's cash flow and net earnings are exposed to interest rate fluctuations due to the Corporation's variable interest rate long-term debt instruments. As at January 31, 2011, a 25 basis point increase or decrease in interest rates, with all other variables unchanged, would have resulted in a decrease or increase of $127,000 in the Corporation's earnings for the year ended January 31, 2011.

**12. Financial instruments - Disclosure and Presentation (continued):**

Credit risk

The Corporation is exposed to credit risk from a diverse range of charter customers, including mining, oil and gas companies, governments and the general public related to tourism activities. The Corporation performs on-going credit evaluations of new and existing customers and provisions are set up where potential exists for credit losses.

As at January 31, 2011, 49% (2010 – 48%) of the Corporation's total accounts receivable balance was due from government entities. The Corporation considers the credit risk from government entities to be extremely low. The remaining accounts receivable are distributed over a large base of customers. The diverse distribution of accounts receivable and management's diligence in monitoring the credit quality of its customers serve as mitigating factors for the credit risk that exists. As at January 31, 2011, accounts receivable outstanding for more than 90 days, net of allowances for doubtful accounts, represented 7% (2010 – 5%) of reported accounts receivable.

Liquidity risk

Liquidity risk is the risk that the Corporation will not be able to meet its financial obligations as they fall due or will not be in a position to refinance maturing obligations at a reasonable price or on reasonable terms. The Corporation's management is responsible for ensuring there is sufficient capital to meet short-term and medium-term business requirements, after taking into account expected cash flows from operations and the Corporation's cash position. The Corporation's liquidity is monitored regularly by management and the Board of Directors, factoring in the seasonal cycle of the Corporation's operations, by preparing short-term and long-term cash flow forecasts and also by matching the maturity profiles of financial assets and liabilities.

The Corporation's credit agreements include financial covenants, compliance with which is tested on a quarterly and an annual basis. These covenants place minimum and maximum requirements, as applicable, on leverage, fixed charge coverage and tangible net worth. The credit agreements also include non-financial covenants that limit the Corporation's ability to deal with its assets and operations in the ordinary course of business, complete acquisitions or make distributions. As at January 31, 2011, the Corporation was in compliance with all of the covenants established by its lenders.

In order to ensure adequate financing is in place to meet its working capital requirements, the Corporation arranged a demand operating line of credit (note 6). The operating line of credit is an important aspect of ensuring an adequate level of liquidity exists, especially given the seasonal nature of the Corporation's business and seasonality's impact on cash flow available from operations. This line of credit and a non-revolving demand loan used to provide funding for aircraft purchases provided by the same lender mature on June 9, 2011. The failure to renew or refinance these credit facilities would have a material adverse impact on the Corporation's liquidity.

The Corporation's liquidity could be negatively impacted by the annual reset of the Corporation's 10-year term loan maximum borrowing base (see - note 5 (b)). There are two important variables that affect the calculation of the maximum borrowing base: (1) the Canadian dollar has strengthened against the U.S. dollar since the last reset; and (2) the appraised value of aircraft may have diminished as a result of

**12. Financial instruments - Disclosure and Presentation (continued):**

market conditions. The Corporation does not have the ability to influence these variables. Should the borrowing limit be reduced as a result of one or both of the above factors, the Corporation's liquidity could be adversely affected as a result of being required to fund a non-scheduled repayment of the principal outstanding in excess of the borrowing limit under the facility.

The Corporation is not aware of any current balance sheet conditions, income statement items or cash flow items, other than those previously disclosed, that could materially impact liquidity.

The expected repayment of financial liabilities is as follows:

| (thousands of dollars) | Due within 1 year | Due between 1 & 2 years | Due between 2 & 3 years | Due between 3 & 4 years | Due between 4 & 5 years | Due after 5 years | Total |
|---|---|---|---|---|---|---|---|
| Accounts payable and accrued liabilities | $ 12,633 | $ - | $ - | $ - | $ - | $ - | $ 12,633 |
| Long-term debt (note 5) | 38,888 | 7,707 | 49,237 | 10,108 | 4,222 | 30,051 | 140,213 |
| | $ 51,521 | $ 7,707 | $ 49,237 | $ 10,108 | $ 4,222 | $ 30,051 | $152,846 |

Fair value

Carrying values for financial assets and liabilities classified as held for trading, loans and receivables and other financial liabilities (excluding long-term debt) approximate their fair value, as such instruments are short-term in nature. The fair value of long-term debt as at January 31, 2011 was $139.6 million as compared to $140.2 million in carrying value.

The fair value of the Corporation's fixed rate long-term debt, excluding the convertible debentures, was estimated based on discounted future cash flows using current rates for similar financial instruments subject to similar risks and maturities. The fair value of the convertible debentures was based on the closing trade price on the Toronto Stock Exchange as at January 31, 2011. The fair value of the Corporation's variable rate long-term debt approximates its carrying value as it bears a floating market rate of interest.

Fair value hierarchy

Financial instruments recorded at fair value on the Corporation's Consolidated Balance Sheets are classified using a fair value hierarchy that reflects the significance of the inputs used in making the fair value 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

**12. Financial instruments - Disclosure and Presentation (continued):**

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.

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

Cash and restricted cash were recorded at fair value in the Corporation's Consolidated Balance Sheet as at January 31, 2011, using the Level 1 fair value criteria described above.

**13. Related party transactions:**

At January 31, 2011, the Corporation had long-term debt including accrued interest totalling $13.6 million (January 31, 2010 - $15.0 million) owing to current and former officers and directors of the Corporation or its subsidiaries who were former owners of the subsidiaries. Interest expense on this debt for the year ended January 31, 2011 was $0.5 million (January 31, 2010 - $0.5 million). Subsequent to January 31, 2011, the Corporation entered into an agreement to settle this debt through a cash payment of $3.2 million and the issuance of 10,352,000 Class A common shares (see note 17 - Subsequent events).

During the year ended January 31, 2009, the Corporation became aware of potential claims by the Corporation against former shareholders of one of the Corporation's subsidiaries. The Corporation believes the amount of these claims could exceed the $1.1 million owing to the former shareholders of the subsidiary. The Corporation is of the opinion that the original purchase agreement provides it with the right of set-off for these potential claims. The face value of the amount owing of $1.1 million has been fully offset by the potential claims as at January 31, 2011. Further disclosure is provided in note 14 – Commitments, restricted cash and contingencies, below.

**14. Commitments, restricted cash and contingencies:**

The Corporation has annual lease obligations for aircraft and premises. Minimum lease payments under these leases for each of the five succeeding years and thereafter are as follows:

| (thousands of dollars) | |
|---|---|
| 2012 | $3,899 |
| 2013 | 1,612 |
| 2014 | 848 |
| 2015 | 377 |
| 2016 | 267 |
| Thereafter | 8,430 |

As at January 31, 2011, the Corporation had $0.8 million in restricted cash (January 31, 2010 - $1.3 million) which is required to collateralize contingent exposures. The requirement to cash collateralize

**14. Commitments, restricted cash and contingencies (continued):**

contingent exposures has arisen as the Corporation's operating lender is in a position to provide only direct loan advances. $0.6 million (January 31, 2010 - $0.5 million) of this restricted cash is used as collateral for letters of credit the Corporation has obtained through other lenders and $0.2 million (January 31, 2010 - $0.8 million) relates to other contingent exposures. The letters of credit serve as collateral for customer contracts and certain contractual obligations of the Corporation's subsidiaries.

As an alternative to letters of credit, the Corporation may place deposits with its customers to secure contractual obligations and at January 31, 2011, these deposits totalled $0.3 million (January 31, 2010 - $0.3 million).

The Corporation is subject to legal proceedings that arise in the ordinary course of business. While the outcome with respect to actions outstanding or pending as at January 31, 2011 cannot be predicted with certainty, it is management's opinion that their resolution will not have a material adverse effect on the consolidated financial position, results of operations or cash flows of the Corporation. Legal costs are expensed as incurred on these matters.

During the quarter ended April 30, 2010, the Corporation was served with a Statement of Claim by two former officers of one of the Corporation's subsidiaries whose employment was terminated in February 2009. The Statement of Claim alleges wrongful dismissal and claims damages totalling $1.8 million plus costs and pre-judgment interest. Additionally, the claim alleges that the $1.1 million balance outstanding on the notes payable by the Corporation's subsidiary to the claimants is due in its entirety. The face value of these notes as at January 31, 2011 was $1.1 million. Although it is not possible as at the date of these financial statements to determine with a reasonable degree of certainty the outcome of this legal proceeding, management believes the claims are without merit and has filed a Statement of Defence.

During the quarter ended January 31, 2011, the Corporation committed to purchase two aircraft for approximately US $2.2 million in the third quarter of this fiscal year. The Corporation provided non-refundable deposits totalling US $100,000, which will be applied to the final purchase price of the aircraft.

The Corporation enters into short-term (less than one year) aircraft operating lease arrangements in the first quarter of each year. The arrangements allow the Corporation to manage its fleet in a more cash-efficient manner. Subsequent to year-end, the Corporation has committed to minimum lease payments of $6.2 million related to these arrangements.

The Corporation is currently in the process of negotiating a $2.7 million long-term lease agreement with the landlord of the Corporation's hangar facility in the city and province of Quebec. The arrangement is expected to be finalized in the first quarter of fiscal 2012.

The Corporation has $0.8 million available to draw upon for future equipment purchases at its Quebec City hangar facility. Any amounts drawn on this term loan facility will have a maturity date of September 1, 2021 and will bear interest at the lender's floating base bank rate plus 4%. There was no amount drawn at year end.

## 15. Segmented information:

The Corporation has two reportable business segments: Northern Services and Government Services. These segments are differentiated by the markets in which the Corporation's aviation and related services operate. The Northern Services segment is comprised of Great Slave, Air Tindi and Discovery Mining and the Government Services segment is comprised of Top Aces, Hicks and Technical Services.

The Northern Services segment's primary market is northern Canada. The segment has a wide customer base, servicing companies and government entities in the business of mineral, base and precious metal exploration and production, wildlife services, forest fire suppression, oil and gas exploration, power line construction and maintenance, aerial surveys, seismic, air ambulance, scheduled charters and tourism.

The Government Services segment provides specialty services primarily aimed at government entities.

All other operating activities that are not allocated to these two business segments are reported under Corporate Support.

(thousands of dollars)

| 2011 | Northern Services | Government Services | Corporate Support | Total |
|---|---|---|---|---|
| Revenue | $ 90,383 | $ 62,029 | $ 6 | $ 152,418 |
| Operating expenses | 71,514 | 36,859 | 6,492 | 114,865 |
| Income (loss) from operations before undernoted items | 18,869 | 25,170 | (6,486) | 37,553 |
| Amortization | 8,555 | 5,278 | 41 | 13,874 |
| Relocation of corporate office | – | – | 158 | 158 |
| Income (loss) before undernoted items | $ 10,314 | $ 19,892 | $ (6,685) | $ 23,521 |
| Interest and financing charges | | | | 15,298 |
| Income taxes provision | | | | 2,438 |
| Non-controlling interest | | | | 319 |
| Net income | | | | $ 5,466 |
| Total assets | $ 134,989 | $ 117,616 | $ 6,381 | $ 258,986 |
| Goodwill | $ – | $ 37,862 | $ – | $ 37,862 |
| Intangible assets | $ 7,929 | $ 11,230 | $ – | $ 19,159 |
| Capital expenditures | $ 10,087 | $ 8,013 | $ 53 | $ 18,153 |

**15. Segmented information (continued):**

(thousands of dollars)

| 2010 | Northern Services | Government Services | Corporate Support | Total |
|---|---|---|---|---|
| Revenue | $ 70,761 | $ 52,378 | $ 34 | $ 123,173 |
| Operating expenses | 57,980 | 30,896 | 5,486 | 94,362 |
| Income (loss) from operations before undernoted items | 12,781 | 21,482 | (5,452) | 28,811 |
| Amortization | 9,281 | 4,743 | 54 | 14,078 |
| Relocation of corporate office | – | – | 1,678 | 1,678 |
| Income (loss) before undernoted items | $ 3,500 | $ 16,739 | $ (7,184) | $ 13,055 |
| Interest and financing charges | | | | 15,410 |
| Income taxes recovery | | | | (2,317) |
| Non-controlling interest | | | | 248 |
| Net loss | | | | $ (286) |

(thousands of dollars)

| 2010 | Northern Services | Government Services | Corporate Support | Total |
|---|---|---|---|---|
| Total assets | $ 135,272 | $ 113,401 | $ 7,637 | $ 256,310 |
| Goodwill | $ – | $ 37,862 | $ – | $ 37,862 |
| Intangible assets | $ 10,077 | $ 13,522 | $ – | $ 23,599 |
| Capital expenditures | $ 10,019 | $ 12,644 | $ 28 | $ 22,691 |

The Government Services segment includes business entities that are economically reliant upon a single customer.

Top Aces' revenue is primarily derived from Standing Offer Agreements to provide airborne training services to DND. These Standing Offer Agreements were extended in January 2011 for a further 16-month period, with an option in favour of DND to extend for an additional twelve months thereafter. DND is not obligated to call up any Top Aces services under these Standing Offer Agreements and may cancel them at its convenience. Top Aces is currently the only supplier with approved airworthiness clearances under these Standing Offer Agreements, and given this fact, together with the essential nature of the services provided by Top Aces, management does not believe it likely that these Standing Offer Agreements will be terminated prior to their expiry, or that there will be any substantial reduction in service required by DND. Top Aces submitted a proposal for a Public Works Government Services Canada (PWGSC) Request for Proposal ("RFP") for a 10 year contracted airborne training services contract with an option for two 5 year extensions in October 2010. This solicitation was cancelled in early fiscal 2012, with PWGSC indicating their intention to retender a new RFP for the long term Contracted Airborne Training Services program.

**15. Segmented information (continued):**

Hicks' revenue from aerial fire management services is derived from three 5-year contracts with the Government of Ontario. The continuation of each contract for each new fiscal year is conditional upon a sufficient appropriation of funds by the Government of Ontario. Given the nature of the services being provided, management believes that it is unlikely that the Government of Ontario will discontinue the appropriation of funds for these contracts. Either contract may be terminated by the Government of Ontario (i) upon occurrence of certain events of default, including Hicks' insolvency or its breach of specified material terms or conditions of the contract, and (ii) without cause by giving 30 days prior written notice to Hicks.

**16. Comparative figures:**

Certain comparative figures have been reclassified to conform with the current year's financial statement presentation.

**17. Subsequent events:**

(a) On April 21, 2011, the Corporation entered into an agreement to sell to a syndicate of underwriters $30.0 million principal amount of new convertible unsecured subordinated debentures (the "New Debentures") at a price of $1,000 per debenture. The Corporation also granted the underwriting syndicate an over-allotment option to purchase up to an additional $4.5 million aggregate principal amount of New Debentures for a period of up to 30 days following closing to cover over-allotments at closing and for market stabilization purposes. The net proceeds of the offering will be used by the Corporation to fully repay the Corporation's existing 8.75% Convertible Unsecured Subordinated Debentures due December 31, 2011 and accrued interest payable thereon, and the balance, if any, will be used for working capital and general corporate purposes.

The New Debentures will mature on June 30, 2016 and will accrue interest at the rate of 8.375% per annum payable semi-annually. At the holders' option, the New Debentures may be converted into the Corporation's Class A common voting or Class B variable voting shares at any time prior to the maturity date at a conversion price of $0.73 for each common share, subject to standard anti-dilution provisions.

The New Debentures will not be redeemable before June 30, 2014. From June 30, 2014 to the maturity date, the Corporation may, at its option and subject to notice period requirements, redeem the New Debentures, in whole or in part, at par plus accrued and unpaid interest, provided that the weighted average trading price of the common shares on the Toronto Stock Exchange during a specified period prior to redemption is not less than 125% of the conversion price.

Subject to specified conditions, the Corporation will have the right to repay the outstanding principal amount of the New Debentures on maturity or redemption, by delivering common shares of the Corporation. The Corporation also has the option to pay interest in cash and/or through the issue and sale of additional common shares of the Corporation. Additionally, the Corporation has the option,

**17. Subsequent events (continued):**

subject to prior agreement of the holders, to settle its obligations on conversion by way of a cash payment of equal value.

The issue of New Debentures is scheduled to close on or about May 12, 2011 and is subject to certain conditions including, but not limited to, the receipt of all necessary approvals including the approval of the Toronto Stock Exchange.

(b) Subsequent to January 31, 2011, the Corporation entered into an agreement to repay related party debts aggregating $13.2 million (see note 5 and note 13) through a cash payment of $3.2 million and the issuance of 10,352,000 Class A common shares. Based on the market value of the Class A common shares at the date of settlement ($0.43 per share), the Corporation expects to record a gain on the extinguishment of the related party debts of approximately $5.5 million. The closing date of this transaction is expected to be late in the first quarter or the beginning of the second quarter of fiscal 2012.

(c) During the first quarter of fiscal 2012, the Corporation committed to purchasing two aircraft. One aircraft will be acquired directly by the Corporation for approximately $1.8 million. The second aircraft will be acquired through an Aboriginal partnership for $1.2 million, of which the Corporation will contribute 49% of the total purchase price, consistent with its ownership interest in the Aboriginal partnership. These transactions are expected to be completed at the end of the first quarter or the beginning of the second quarter of fiscal 2012.